U.S. Subprime Rating Surveillance Update

Glenn Costello
Managing Director

July 2007
Agenda

Rating Actions And The July 2007 ‘Under Analysis’ List

Risk Factors Affecting Performance and Ratings

Going Forward
## Agenda

<table>
<thead>
<tr>
<th>Rating Actions And The July 2007 ‘Under Analysis’ List</th>
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<tbody>
<tr>
<td>Risk Factors Affecting Performance and Ratings</td>
</tr>
<tr>
<td>Going Forward</td>
</tr>
</tbody>
</table>
Fitch Downgrade Actions Accelerated In 2007

# Tranches Downgraded each Month

Source: Fitch
Understanding Fitch SMARTView

> Each month, monitoring criteria determines deals that are selected for review

> The ‘Under Analysis’ deals are posted on the website and a press release is issued. All other deals are marked as not being selected for review that month

> ‘Under Analysis’ is not the same as ‘Rating Watch’. Whole deals are placed under analysis, and only after analysis is completed are individual tranches upgraded/downgraded/put on ‘Watch’, or affirmed

> Separate lists are posted for subprime and Alt-A/prime

> Fitch’s goal is to process all deals under review within 30 days
The July 2007 Subprime ‘Under Analysis’ List

170 Transactions


> Ratings Distribution by # Tranches (2005 and 2006 Deals):
  – AAA: 611
  – AA/A: 812
  – BBB: 339
  – BB/B: 126

> We anticipate most action will be around ‘BBB’ which represent about 1.7% of our portfolio by balance.
Enhanced Selection Criteria For SMARTView

> Deals from 2H 2005 and 2006
> Loss expectation of 8% or greater; Estimated ‘BBB’ Loss Coverage estimate less than 1.25
> Revised loss forecasting assumptions:
  - Increased default rate expectation for performing loans (~16%) to reflect early performance
  - Loss severity based on deal history, approximately 40% but ranging from 30% to 65%
> Default expectations for delinquent loans remain at 40% for loans in the 30-59 day bucket, 60% for loans in the 60-89 day bucket, 70% for loans over 90 days, 80% for loans in foreclosure and 100% for loans in REO
Next Steps On ‘Under Analysis’ List

> Additional Assumption Changes:
  – Higher default rates post ARM reset, as much as 150% higher
  – Slower voluntary prepay speeds; sensitivity analysis

> Generate cash flows and loss coverage levels on each deal

> Rating Committees

> Rating action announcements with detailed assumptions and expected losses, along with key risk factors
Agenda

Rating Actions And The July 2007 ‘Under Analysis’ List

Risk Factors Affecting Performance and Ratings

Going Forward
Review of Risk Factors

> Collateral Attributes
> Home Prices
> ARM Resets
> Prepayment Rates
Loans Became Riskier as Rates Rose
Collateral Attributes by Vintage

Combined-Loan-to-Value Ratio

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<tr>
<th>Year</th>
<th>2000</th>
<th>2001</th>
<th>2002</th>
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<th>2004</th>
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Debt-to-Income Ratio

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<tr>
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Source: LoanPerformance, Fitch
Loans Became Riskier as Rates Rose (cont.)
Collateral Attributes by Vintage

Limited Borrower Documentation

“Piggy-Back” 2nd Liens

Source: LoanPerformance, Fitch
# Affordability Product Features Driving Early Default

## Collateral Attributes by Vintage

<table>
<thead>
<tr>
<th>Vintage</th>
<th>Avg. mtge bal.</th>
<th>FICO</th>
<th>LTV (%)</th>
<th>CLTV (%)</th>
<th>Low/no doc (%)</th>
<th>Purchase (%)</th>
<th>DTI (%)</th>
<th>Calif. WAC</th>
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<td><strong>Mortgages that defaulted by month 12 (90+ days delinquent)</strong></td>
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<td>2006</td>
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<td><strong>Mortgages that performed through month 12 (never 90+ days delinquent)</strong></td>
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<td>40</td>
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Source: Fitch, LoanPerformance
Home Price Growth Turned Down Sharply…

California Home Price Inflation by Origination Quarter

Source: Fitch, CSW
...And Continued Home Price Weakness Is Expected

UFA Regional Risk Multiplier Implied Growth vs. Actual – Calif.

Source: Fitch, OFHEO
## ARM Resets Without Home Price Growth will Increase Defaults

<table>
<thead>
<tr>
<th>Reset date</th>
<th>Jul 07</th>
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<th>Oct 07</th>
<th>Nov 07</th>
<th>Dec 07</th>
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<tr>
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<td>26.2</td>
<td>34.2</td>
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<td>7.1</td>
<td>7.2</td>
<td>7.2</td>
<td>7.3</td>
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<tr>
<td>Adjusted coupon</td>
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<td>9.6</td>
<td>9.4</td>
<td>9.5</td>
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<tr>
<td>FICO</td>
<td>623</td>
<td>628</td>
<td>623</td>
<td>628</td>
<td>626</td>
<td>623</td>
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<tr>
<td>LTV</td>
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<tr>
<td>Combined LTV</td>
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<td>88.0</td>
<td>86.9</td>
<td>86.2</td>
<td>87.3</td>
<td>87.3</td>
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<tr>
<td>Full doc %</td>
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<tr>
<td>HPI (1Q07)</td>
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<td>2.8</td>
<td>4.5</td>
<td>2.4</td>
<td>1.8</td>
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<tr>
<td>CPR</td>
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<tr>
<td>60+DQ</td>
<td>12.2</td>
<td>12.5</td>
<td>11.9</td>
<td>12.3</td>
<td>12.8</td>
<td>12.5</td>
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Source: Fitch, LoanPerformance
ARM Resets Without Home Price Growth Will Increase Defaults (cont.)

<table>
<thead>
<tr>
<th>Reset date</th>
<th>Jan 08</th>
<th>Feb 08</th>
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<tr>
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<td>Coupon</td>
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<td>10.3</td>
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<tr>
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<td>618</td>
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<tr>
<td>LTV</td>
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<tr>
<td>Combined LTV</td>
<td>87.0</td>
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<tr>
<td>Full doc %</td>
<td>52.5</td>
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<tr>
<td>HPI (1Q07)</td>
<td>1.2</td>
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<td>2.1</td>
<td>0.5</td>
<td>0.4</td>
<td>0.6</td>
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<tr>
<td>CPR</td>
<td>28.2</td>
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<td>28.5</td>
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<td>60+DQ</td>
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<td>13.7</td>
<td>15.3</td>
<td>14.9</td>
<td>14.7</td>
</tr>
</tbody>
</table>

Source: Fitch, LoanPerformance
Slower Prepayments and Failed Triggers Will Mitigate Bond Default Risk

CPR by Annual HPI% 

Historical scenario\(^a\)  BreakLoss (%) 

<5% HPI  10.97 
5-10% HPI  7.95 
>10% HPI  5.32 

\(^a\) Assumes CPR and delinquency exhibited by States with the indicated annual HPI since 2001 

Performance by State, Grouped by Annual Home Price Appreciation Since 2001 
Source: LoanPerformance/Case Schiller Weiss
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Risk Factors Affecting Performance and Ratings

Going Forward
Going Forward

> SmartView list will show additional deals ‘Under Analysis’ each month. The current ‘Under Analysis’ list represents about 40% of Fitch-rated subprime deals from 2006 and 2H 2005.

> We will provide detailed discussion of our actions

> We will report on the effectiveness of our assumptions as conditions develop, and take additional actions as warranted.
Structure Finance CDO
Rating Actions and Methodology Update

July 18, 2007

Kevin Kendra
Managing Director
Derivative Fitch
U.S. Structured Credit
Role of RMBS Ratings in SF CDOs

> Measure portfolio credit quality
  – Use asset ratings as measure of default probability in CDO analytics
  – Use weighted average rating factor as parameter in portfolio reinvestment guidelines
  – Use asset rating changes to discount the value of lower rated assets “haircut” in overcollateralization (OC) and interest coverage (IC) tests

> Derivative Fitch uses ratings from all three agencies
  – Derivative Fitch first defers to their Fitch RMBS group for credit quality
  – If not rated by Fitch, Derivative Fitch uses the lower of Moody’s and S&P public ratings
2007 RMBS Rating Actions

> Analysis of Rating Actions by Rating Agency
> Analysis of Downgrades by RMBS Vintage
> Analysis of 2006 Vintage RMBS Downgrades
RMBS Rating Actions through June 2007

Source: Intex, Fitch, S&P, Moody’s

www.derivativefitch.com
RMBS Rating Actions through July 16, 2007

Source: Intex, Fitch, S&P, Moody's
Cumulative Number of Downgrades by Month

Source: Intex, Fitch, S&P, Moody's
1H 2007 RMBS Downgrades by Agency and Vintage

Source: Intex, Fitch, S&P, Moody’s
YTD 2007 RMBS Downgrades by Agency and Vintage

Source: Intex, Fitch, S&P, Moody's
2005 and 2006 Vintage RMBS Downgrades by Type through 1H 2007

Source: Intex, Fitch, S&P, Moody's
2005 and 2006 Vintage RMBS Downgrades by Type through July 16, 2007

Source: Intex, Fitch, S&P, Moody’s
Number of 2006 Subprime CES Downgrades by Original Rating Category (through 1H 2007)
Magnitude of 2006 Subprime CES Downgrades by Original Rating Category (through 1H 2007)

<table>
<thead>
<tr>
<th>Original Rating</th>
<th>Fitch</th>
<th>S&amp;P</th>
<th>Moody's</th>
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<tr>
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<td>-</td>
<td>-</td>
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<td>-</td>
<td>3.0</td>
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<td>AA-</td>
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Structured Finance (SF) CDO Exposure to Subprime RMBS

> Overview of Fitch-rated SF CDOs
> Overview of Rating Watch Process
> SF CDO Rating Methodology Changes
> Outlook for SF CDOs in 2H 2007
Overview of Fitch-rated SF CDOs

> Fitch rates 160 mezzanine SF CDOs totaling approximately $54.4 billion
> Fitch rates 41 high-grade SF CDOs totaling approximately $39.6 billion
SF CDO Rating Watch Process

> Fitch placed 8 classes from 4 SF CDOs on Rating Watch Negative (RWN) on June 22, 2007.

> Fitch placed 33 classes from 19 SF CDOs on RWN on July 12, 2007.

> Derivative Fitch’s Rating Watch Process

  - Screen portfolios for portfolio credit migration
  - Screen portfolios for assets on RWN or ‘Under Analysis’
  - Screen portfolios for 2006 vintage subprime CES RMBS exposure
  - Qualitatively assess impact on CDO structural features to various notes
  - CDO tranches placed on RWN as a result of credit committee process

> The 23 SF CDOs with tranches placed on RWN will go through Fitch’s full CDO rating review process
SF CDO Review Process

> Discussion with the CDO asset manager
  – Asset performance
  – Distressed asset expectations
  – Portfolio management strategy

> Analysis and default modeling of the underlying portfolio
  – Stress default modeling for different prepayment assumptions

> Analysis of CDO cash flows under stress scenarios
  – Vary default timing, interest rate and prepayment assumptions
  – Apply different stresses for different rating categories

> Credit Committee
SF CDO Rating Methodology Changes

> 2005 and 2006 vintage subprime RMBS bonds are showing unprecedented rating performance as evidenced by the sharp increase in downgrade activity with less than 2 years of seasoning.

> Derivative Fitch modified its CDO modeling assumptions by increasing default probability by 25% for all 2005 and 2006 vintage subprime RMBS bonds.
   - A new version of VECTOR incorporating these changes is under development
SF CDO Outlook for Remainder of 2007

> RMBS downgrades will continue to increase each month through 3Q 2007 and beyond
> Future RMBS downgrades will have a direct impact on SF CDO ratings
> Mezzanine SF CDOs
  > Tranches originally rated ‘BBB’ and lower to face continued downgrade pressure from downward portfolio credit migration
    > CDO issued from 2002 from 2004 may be impacted sooner as they typically have exposure to both 2003-04 and 2005-06 subprime RMBS
    > 2005 and 2006 CDO vintages at risk of further RMBS downgrades from bonds issued in the second half of 2006
> High-grade SF CDOs
  > CDOs with larger exposures to 2006 vintage subprime CES are most at risk given the scope and relative magnitude of rating actions seen in this sub-sector
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