# Estate UK-3

## CMBS / UK

*This pre-sale report addresses the structure and characteristics of the proposed transaction based on the information provided to Moody's as of [23rd August 2006]. Investors should be aware that certain issues concerning this transaction have yet to be finalised. Upon conclusive review of all documents and legal information as well as any subsequent changes in information, Moody's will endeavour to assign definitive ratings to this transaction. The **definitive** ratings may differ from the **provisional** ratings set forth in this report. Moody's will disseminate the assignment of definitive ratings through its Client Service Desk. This report does not constitute an offer to sell or a solicitation of an offer to buy any securities, and it may not be used or circulated in connection with any such offer or solicitation.*

**Estimated Closing Date**

[· February 2007]

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## PROVISIONAL (P) RATINGS

| Class | Rating | Amount (million) | % of Notes | Scheduled Maturity | Legal Final Maturity |
|---|---|---|---|---|---|
| A1+(CDS) | (P)**Aaa** | £[482.45] | 80.93 | [Mar.20] | Mar.22 |
| A1+ | (P)**Aaa** | £[0.4] | 0.07 | [Mar.20] | Mar.22 |
| A2 | (P)**Aa1** | £[29.80] | 5.00 | [Mar.20] | Mar.22 |
| B | (P)**Aa2** | £[35.76] | 6.00 | [Mar.20] | Mar.22 |
| C | (P)**A1** | £[24.56] | 4.12 | [Mar.20] | Mar.22 |
| D | (P)**A3** | £[8.24] | 1.38 | [Mar.20] | Mar.22 |
| E | (P)**Baa3** | £[14.92] | 2.5 | [Mar.20] | Mar.22 |

*The ratings address the expected loss posed to investors by the legal final maturity. In Moody's opinion the structure allows for timely payment of interest and ultimate payment of principal at par on or before the rated final legal maturity date. Moody's ratings address only the credit risks associated with the transaction. Other non-credit risks have not been addressed, but may have a significant effect on yield to investors.*

## OPINION

### Strengths of the Transaction

- Property and tenant diversity; the portfolio benefits from a mix of retail, office and car dealership properties which receive income from a high number of commercial tenants (appx 221 tenants) hence reducing cashflow volatility.
- Credit strength of the tenants: Approximately 60% of the total income is contributed by investment grade or implied investment grade tenants.
- Geographic diversity – the thirteen reference claims are secured by a portfolio of 110 properties located throughout the United Kingdom.
- The good quality of the underlying properties: The properties in the pool have a weighted average property grade of 2.2 on a scale of 1 to 5; 1 being the best.
- Diversity of Loan size: The pool has a score of 7.0, indicating that this is relatively less concentrated than other recent European CMBS conduit transactions.
- Fully sequential priority of payments and scheduled principal payments.

### Weaknesses and Mitigants

- The pool is concentrated in respect of the loan size with the largest loan being 29.5% of the pool and the five largest loans totaling to 70.5% of the pool. This is mitigated by (i) the submarket diversification of the assets and the tenant diversification within the loans and (ii) the above average quality of the underlying properties. Loan Herf of 7.0 is a bit higher than recent comparable deals.
- A/B Loan structure: Five loans amounting to 28.4% of the pool comprise the senior or portions of the senior position of an A/B note structure. Moody's has given credit for the subordination of the B-Note in its severity of loss analysis. However, it should be noted that B note holder's enforcement right limitations are not satisfactory to Moody's (asset cover test not satisfactory). Therefore no benefit has been given for the subordination of the B note in our default probability analysis.

- Interest Rate Risk: One loan and portions of 3 others loans are not fully hedged. This is mitigated by the fact that Moody's has assumed higher interest rates for the unhedged portions, resulting in lower coverage ratios.
- As it is the case for all partially funded synthetic CMBS transactions, the ratings of the Class A1+, A2, B, C, D and E Notes are linked to the ratings of the respective Pfandbrief Collateral provided. For the Notes, the Pfandbrief Collateral consists of **Aa1**-rated Public Sector Pfandbrief issued by Hypo International. Any change in the rating of the Pfandbrief Collateral may affect the ratings of the respective Notes. However, this risk is partially mitigated by Hypo International's intent to substitute or supplement the Pfandbrief Collateral in the event of a downgrade of its Public Sector Pfandbrief below **Aa1**.

## STRUCTURE SUMMARY

| | |
|---|---|
| Issuer: | Hypo Real Estate Bank International AG (**A2**,**P-1**) |
| Credit Protection Buyer: | Hypo Real Estate Bank International AG (**A2**,**P-1**) |
| Structure Type: | Partially funded synthetic CMBS using Credit Linked Notes and a Credit Default Swap |
| Originator: | Hypo Real Estate Bank International AG (**A2**,**P-1**) |
| Servicer: | Hypo Real Estate Bank International AG (**A2**,**P-1**) |
| Interest Payments: | Quarterly sequential (20th March, 20th June, 20th September, 20th December) |
| Principal Payments: | Fully Sequential |
| Security Interest: | Class A1+ Notes and Class A2 Notes are collateralised by a combination of **Aa1**-rated Public Sector Pfandbriefe and a Cash Deposit. Class B, C, D and E Notes are collateralised by **Aa1**-rated Public Sector Pfandbriefe. |
| Pfandbrief Collateral: | **Aa1**-rated Public Sector Pfandbriefe issued by Hypo Real Estate Bank International AG (**A2**, **P-1**). |
| Credit Enhancement/Reserves: | Credit enhancement through subordinated tranches |
| Principal Paying Agent: | Hypo Real Estate Bank International AG (**A2**, **P-1**). |
| Trustee: | Deloitte & Touche GmbH, Wirtschaftspüfungsgesellschaft |
| Arranger: | Hypo Real Estate Bank International AG (**A2**, **P-1**) |

## COLLATERAL SUMMARY

| | |
|---|---|
| Assets: | [13] Loans with a total securitised principal balance of approximately [£596.12] million (the "Loans") |
| Number of Properties: | 110 properties |
| Type of Loan: | Mixture of fixed and floating |
| Property Type Distribution[1]: | [36.07%] Retail, [31.73%] Office, [20.31%] Car Show Rooms, [11.34%] Mixed, [0.55%] Other |
| Geographic Distribution[1] | 100% United Kingdom; [51.08%]London and the South East, [16.23%] Yorks & Humberside, [12.82%] Midlands, [8.81%] Wales, [3.73%] South West England, [3.51%] Scotland, [3.39%] North West England, [0.44%] North East England |
| Average Moody's LTV: [2] | [63.4] A Note only; [80.1] Whole Loan |
| Average U/W LTV: | [59.28%] |
| Average Moody's DSCR: [2] | [1.63x] A Note only; [1.24x] Whole Loan |
| Average U/W DSCR: | [1.66x] |
| Remaining Term: [2] | [7.85] years |

## NOTES

| Class | Subordination |
|---|---|
| A1+ | Classes A2, B,C,D,E |
| A2 | Classes B,C,D,E |
| B | Classes C,D,E, |
| C | Classes D,E |
| D | Classes E |
| E | None |

1 by market value

2 Weighted average figures are based on Moody's calculations and analysis of the pool and may differ from the figures presented in the offering circular.

## TRANSACTION SUMMARY

***Hypo International's Seventh Synthetic CMBS Transaction.***

Moody's has assigned provisional long-term ratings of (P)**Aaa** ratings to the Class A1+ (CDS) Notes, (P)**Aaa** ratings to the Class A1+ Notes, (P)**Aa1** ratings to the Class A2 Notes, (P)**Aa2** ratings to the Class B Notes, (P)**A1** ratings to the Class C Notes, (P)**A3** ratings to the Class D Notes and (P)**Baa3** ratings to the Class E Notes of the CMBS issuance ESTATE UK-3.

The transaction represents the synthetic securitisation of thirteen commercial mortgage loans or portions of loans (the "Reference Claims") originated by Hypo Real Estate Bank International ("Hypo International") secured by 110 commercial properties located throughout the United Kingdom. The purpose of the transaction is to transfer the credit risks associated with the reference pool and to achieve capital relief associated with the reference claims that remain on Hypo International's balance sheet.

***The Notes will be collateralised by Aa1-Public Sector Pfandbriefe (Class B, C, D & E) or a combination of both Cash and Aa1-Public Sector Pfandbriefe (Class A1+ and A2).***

This transaction adopts a partially funded structure with a Senior credit default swap ("CDS") and the issuance of credit-linked notes ("CLN" or "Notes").

***Ratings of the Class A1+, A2, B, C, D and E Notes are sensitive to the rating of the Pfandbrief Collateral.***

The Class A1+ Notes and the Class A2 Notes will be collateralised with a combination of 100 per cent **Aa1**-Public Sector Pfandbrief issued by Hypo International and a Cash Deposit, equal to 4% of the respective Notes. The Class B, C, D and E Notes will be collateralised with 100 per cent **Aa1**-Public Sector Pfandbrief issued by Hypo International. The ratings of the Class A1+, A2, B, C, D and E Notes have some sensitivity to the credit rating of the respective Pfandbrief Collateral.

***Moody's final review will be undertaken prior to the closing date.***

The provisional rating of the Notes is based upon an analysis of the characteristics of the Reference Claims backing the Notes, the protection the Notes receive from credit enhancement against defaults and arrears in the Reference Pool, and the legal and structural integrity of the transaction.

**Moody's issues provisional ratings in advance of the final sale of securities and these ratings only represent Moody's preliminary opinion. Upon a conclusive review of the transaction and associated documentation, Moody's will endeavour to assign a definitive rating to the notes. The final rating may differ from the provisional rating. The following is a brief description of other key elements of the transaction structure based on Moody's review to date.**

## STRUCTURAL AND LEGAL ASPECTS

***The Issuer will use the Note proceeds to provide the Pfandbrief Collateral and to make Cash Deposits.***

At the closing date, the Issuer will use the proceeds from the issuance of the Notes to provide the Pfandbrief Collateral. The Pfandbrief Collateral will have the same rate of interest, the same interest payment dates as the respective classes of Notes, but has a fixed final maturity date on the Legal Maturity Date. The Issuer will transfer the Pfandbrief Collateral and the Cash Deposits to the Trustee to secure its obligations under the respective Notes.

The Notes and the CDS are credit-linked to a pool of thirteen commercial mortgage loans or portions of loans originated and serviced by Hypo International, who will administer, collect payments on and enforce the loans in the Reference Pool. The Class A1+ Notes and the Senior CDS will rank senior to all other classes of Notes and will rank pari passu to each other. Realised losses will be applied in reverse sequential order and redemptions will be paid sequentially. Accordingly, the Class E Notes, then the Class D Notes, then the Class C Notes, then the Class B Notes and then the Class A2 Notes provide a first loss protection with respect to the Reference Pool.

***Compared to a true sale transaction, the structure exposes the noteholders to an additional risk associated with the Pfandbrief Collateral.***

This transaction exposes the noteholders to an additional source of risk compared to a true sale commercial mortgage backed transaction. In addition to the credit risk associated with the underlying Reference Pool, there is also credit risk associated with the Pfandbrief Collateral. Moody's has factored this risk into its analysis. In the event of a downgrade of the respective Pfandbrief Collateral, the Issuer will intend to either seek confirmation of the ratings, provide additional Pfandbrief Collateral or substitute Pfandbrief Collateral sufficient to maintain the then existing ratings of the Notes.

***Early redemption option for the Issuer.***

As common for synthetic CMBS transactions of German originators/issuers, the issuer has the right to terminate the Notes and the CDS early in the event of (i) a Regulatory Event occurred or (ii) the Aggregate Principal Balance of the Reference Pool has been reduced to less than 10 per cent of the Initial Aggregate Principal Balance of the Reference Pool as at the Cut-off Date or (iii) the 5th anniversary of the issue date has occurred.

## Pfandbrief Collateral and Cash Deposits

***The Notes will be collateralised by Aa1-rated Public Sector Pfandbriefe and Cash deposits.***

Class A1+ and A2 Notes will be collateralised by a Cash Deposit equal to 4% the principal amount outstanding and 100 per cent Pfandbrief Collateral.

The Pfandbriefe Collateral will consist of **Aa1-**Public Sector Pfandbriefe issued by Hypo International. The Class B, C, D and E Notes will be collateralised by 100 per cent **Aa1**-rated Public Sector Pfandbriefe issued by Hypo International. Future rating changes of the Pfandbrief Collateral may directly impact the ratings assigned to the Notes.

In the event that at any time the Pfandbrief Collateral is rated **Aaa** by Moody's, the Issuer shall have the option to request the Trustee for the funds standing to the credit on the Cash Deposit Account an amount equal to the sum of the Class A1+ Cash Deposit and the Class A2 Cash Deposit.

## Credit Events and Realised Losses

A Reference Claim is considered to be in default if a Credit Event has occurred and a Credit Event Notice has been given. A Credit Event with respect to a Reference Claim is defined as either:

a) Bankruptcy of the borrower,

b) Failure to pay the lower of either an amount of not less than GBP 15,000 or if lower, then not less than 50 per cent of the outstanding amount of such Reference Claim within 90 days of its due date,

c) Restructuring Event.

***Realised Losses consist of unpaid principal as well as accrued interest and related Enforcement Costs.***

A Realised Loss occurs if the total amount recovered after the entire enforcement and recovery efforts is less than the outstanding principal amount of the Reference Claim. The definition of a Realised Loss includes unpaid principal amount, accrued interest and the related Enforcement Costs in respect of such Reference Claim. A Realised Loss calculation must be confirmed by the Trustee prior to allocation and the Issuer must not be in breach of any of its obligations under the trust agreement that could detrimentally affect the Noteholders.

***The Trustee has to verify the calculation of any Realised Losses.***

To the extent that a Reference Claim did not meet specific eligibility criteria as of cut-off date or servicing standards have been breached, the affected loan ("Reference Claim") will not qualify for a Realised Loss and will be removed from the pool. However, if the Issuer can demonstrate to the satisfaction of the Trustee that either the type of breach did not contribute to the Realised Loss or such breach has been remedied to the satisfaction of the Trustee, the Reference Claim will be eligible for loss allocation and will remain in the pool. A Reference Claim will only qualify for loss allocation if all amounts expected to be recovered have been received by Issuer. On each Payment Date, the Realised Losses will be applied to the Notes and Credit Default Swaps, in reverse sequential order. The Pfandbrief Collateral will be redeemed on each payment date by an amount equal to the principal payments allocated to the respective class of Notes.

## Replenishment

Replenishment is allowed in the transaction on the last Business Day of each calendar month (each, a "**Replenishment Date**") during the replenishment period which ends in February 2012, provided the following conditions being met as of the relevant Replenishment Date:

i) the aggregate principal balance does not exceed the relevant maximum aggregate principal balance for the relevant replenishment date,

ii) the sum of the Outstanding Nominal Amounts of all Reference Claims added to the Reference Pool on or prior to such Replenishment Date may not exceed GBP [370,000,000],

iii) the Eligibility Criteria have been met,

iv) as of such Replenishment Date, Realised Losses do not exceed GBP [2,000,000],

v) the Outstanding Nominal Amount of any new Reference Claim shall not exceed [30%] of the Aggregate Principal Balance,

vi) in respect of each such new Reference Claim, Rating Agency Confirmation has been sought that the Replenishment does not adversely affect the existing rating of the Notes,

vii) the average Outstanding Nominal Amount of the Reference Claims shall not exceed the amount of GBP [60,000,000],

viii) the weighted average Loan-to-Value of the Reference Pool shall not be higher than [70%],

ix) such new Reference Claim may not arise from a development loan,

x) no more than [10%] of the aggregate principal balance of the Reference Pool may arise from loans or allocated loan amount secured by Speciality Assets (Hotels, Conference Centres, Restaurants, Bars, Pubs, Nursing Homes).

***Rating agency confirmation expected to mitigate the risk of pool deterioration during the Replenishment Period.***

Moody's assessment does not include any migration of credit quality due to the Replenishment. Moody's expects the requirement for Rating Agency Confirmation to mitigate the risk of pool deterioration during the Replenishment Period.

### Credit Enhancement

***Notes subordination will provide credit enhancement to each rated class of Notes.***

Class A1+ Note holders are protected from losses to the extent that credit enhancement is provided by any class A2, B, C, D and E Notes outstanding. All other classes of Notes are protected from losses to the extent of outstanding subordinated Notes.

## COLLATERAL (REFERENCE POOL)

***13 Reference Obligations with an aggregate principal balance of £596.12 million.***

As at the cut-off date, the underlying collateral consists of 13 commercial mortgage loans (each a "Reference Claim") with an aggregate outstanding securitised principal balance of £ 596,127,557 secured by 110 commercial properties located in the United Kingdom. Key characteristics of the pool are outlined below.

– ***Balance sheet loans*** not originated for securitisation purposes. The loans were originated for balance sheet lending purposes and often do not include many of the standard protections available to lenders including release price mechanism for property disposals and substitution criteria. Key mitigant: lender's consent typically a requirement.

***Largest Reference Obligation represents 29.5% of the Reference Pool.***

– ***Loan Concentration:*** The largest Reference Claim is £175.67 million or 29.5% of the Reference Pool principal balance, and the second largest Reference Claim is £68.3 million or 11.5% the Reference Pool. The average loan balance is £45.9 million

– ***A/B Note structures***: Five loans amounting to 28.4% of the pool comprise the senior or portions of the senior position of a A/B note structure. The junior portion of the Loan is subject to similar terms of Servicing and Intercreditor Agreements but they have limited enforcement rights. Following the occurrence of a material default, the Junior lenders maybe serve a notice on the agent and the senior lenders to serve an acceleration notice and commence enforcement proceedings. If within a certain period of serving this notice, no action has been taken by either the Senior lenders and the Agent and the asset cover test value exceeds zero, the junior lender may instruct the agent to serve an acceleration notice and to commence enforcement proceedings and at this stage the agent shall act in accordance with the instructions of the majority junior lenders. While Moody's provided benefit with regards to the severity of loss, but no benefit has been given in the default probability analysis.

– ***Diversity of Loan Size***: Moody's uses the Herfindahl Index to measure diversity of loan size. A score of 100 has a credit neutral diversity. This pool has a score of 7.0, indicating that this is relatively less concentrated than other recent European CMBS conduit transactions.

***All of the properties are located in the United Kingdom.***

– **Geographic Distribution:** Chart 1A shows the geographic distribution based on the U/W market value, the properties are distributed as follows: [51.08%]London and the South East, [16.23%] Yorks & Humberside, [12.82%] Midlands, [8.81%] Wales, [3.73%] South West England, [3.51%] Scotland, [3.39%] North West England, [0.44%] North East England

*36.07 % of the pool are retail properties*

– **Property Type Composition:** Chart 1B shows the property type distribution. In terms of property type, the properties are distributed as follows; [36.07%] Retail, [31.73%] Office, [20.31%] Car Show Rooms, [11.34%] Mixed, [0.55%] Other

Chart 1A:

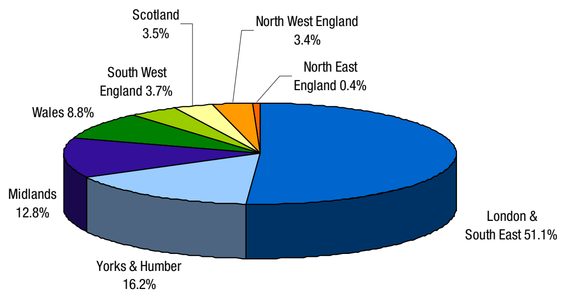
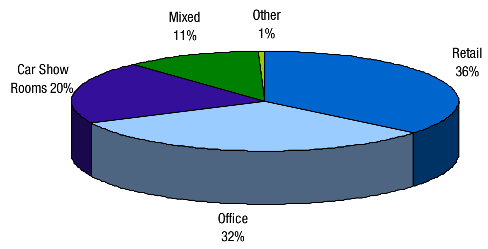



Chart 1B:




– ***Form of Collateral*:** The collateral consists of first charge positions on freehold and leasehold interests. In most instances, the security package for the Loans includes, among others 1) first ranking mortgages, 2) pledge of the relevant rent accounts, 3) pledges of shares of the borrowers and 4) assignments of rents, hedging agreements and insurance policies.

*Good weighted average property grade of 2.2*

– ***Quality Grade:*** The Moody's weighted average quality grade, by property value, is 2.2 on a scale of 1 to 5 (best to worst). Moody's quality grades reflect our assessment of the property relative to the national market taking into account construction quality, location, competition.

– ***Debt Service Ratio*:** The pool's weighted average DSCR is 1.26x (on whole loan basis) based on Moody's cash flows, actual Loan interest rates and scheduled amortisation.

– ***Moody's LTV*:** Based on Moody's initial model value, the LTV is [63.4] % on the A note and [80.1] % on the whole Loan.

## DESCRIPTION FIVE LARGEST REFERENCE CLAIMS

### Reference Claim 1

***Current Balance on the Whole Loan: £175,665,000 – 29.5% of total pool***

"Above average quality" in this pool from an expected loss perspective

| Maturity | Term | WA Property Grade | U/W Day 1 LTV | U/W exit LTV | MDY LTV | Day 1 U/W ICR | Day 1 MDY ICR |
|---|---|---|---|---|---|---|---|
| Apr-13 | 7yrs | 2.25 | 75% | 75% | 75% | 1.22x | 1.14x |

*The largest Reference Claims in the pool is secured by two Shopping Centres in the UK.*

LOAN: Reference Claim 1 is the largest loan in the pool which represents 29.5% of the principal pool balance, with £175.67 million outstanding Day 1. The loan is secured by 2 shopping centres located the United Kingdom. The purpose of the 7 year loan was the acquisition of the underlying properties. There is a cash sweep mechanism depending on the ratio of net income to finance costs. The loan is 85% hedged at a fixed rate at the borrower level. The Release Premiums due to disposals are 120% and 110% respectively for the two properties. The loan is secured by first ranking mortgages and assignment of rental income as part of a standard security package. The loan features an ICR Event of Default covenant at 1.10x and an LTV Event of Default covenant of 80%.

*Diversified tenant base*

PROPERTIES: The properties comprise of two enclosed purpose-built covered shopping centres are held on a mix of freehold and leasehold basis and have been constructed in 1983 and 1990 (and has since been refurbished) respectively. Both properties are well diversified in terms of tenant base with approximately 140 distinct tenants. The top 5 tenants represent 19% of the total gross income. The current blended vacancy rate is less than 3%. Appx 40.1% of the leases are subject to lease expiry or break within the next 5 yrs.

Moody's assessment of the term risk is linked to the diversified tenant structure and the respective estimated tenant quality. The refinancing risk of the Loan is also impacted by the diversified tenant structure and on the default probability of the Whole Loan.

## Reference Claim 2

### *Current Balance on the Whole Loan: £ 85,625,000*

A-Note current Balance: £68,300,000 - 11.5% of total pool

"Above average quality" in this pool from an expected loss perspective

| Maturity | Term | WA Property Grade | U/W Day 1 LTV A Loan | U/W exit LTV A Loan | MDY LTV | Day 1 U/W DSCR A Loan | Day 1 MDY DSCR A Loan |
|---|---|---|---|---|---|---|---|
| Jan-19 | 12yrs | 1.5 | 57.9% | 45.8% | 57.9% | 1.2x | 1.3x |

***The second largest Reference Claim in the pool is secured by a mixed-use property located in a prime location in the UK.***

Loan: The loan is a A/B loan with 80%/20% split and was originated in December 2005. Hypo International is the Senior lender. Reference Claim 2 is the second largest loan in the pool which represents 11.5% of the principal pool balance. The loan is a A/B loan with a whole loan balance of £85.6 million and the A note balance being £68.3 million. The loan is secured by mixed-use property containing 81% retail and 16% office located in a prime location in the United Kingdom. The purpose of the 12 year loan was the refinancing of the underlying properties. The loan is a fixed rate loan. The loan is secured by first ranking mortgages and assignment of rental income as part of a standard security package. The loan features an ICR Event of Default covenant at 1.10x, DSCR covenant of 1.0x and an LTV Event of Default covenant of 75%.

***Diversified tenant base***

PROPERTIES: The property is a mixed-use containing 81% retail and 16% office and is located in a prime location in the United Kingdom. The property is let to 23 distinct tenants and anchored by well known UK retailers. 38% of the current income comes from a single tenant on the retail side of which half will expire in 2018. The office space is let on long leases with 98% expiring after loan maturity. The current vacancy rate is less than 6%.

Moody's assessment of the term risk is linked to the diversified tenant structure and the respective estimated tenant quality based on the whole loan. The refinancing risk of the Loan is also impacted by the diversified tenant structure, location and on the default probability of the Whole Loan.

## Reference Claim 3

### *Current Balance on the Whole Loan: £ 146,452,912*

Hypo International Syndicate Portion Current Balance: £125,834,090

Hypo International Syndicate Portion Balance Securitised: £62,917,045 – 10.6% of total pool

"Above average quality" in this pool from an expected loss perspective

| Maturity | Term | WA Property Grade | U/W Day 1 LTV Loan | U/W exit LTV Loan | MDY LTV | Day 1 U/W DSCR Loan | Day 1 MDY DSCR Loan |
|---|---|---|---|---|---|---|---|
| Dec-19 | 13yrs | 2.5 | 49.8% | 31.3% | 59.6% | 1.77x | 1.7x |

***The third largest Reference Claim in the pool is secured by 85 car show rooms located throughout the UK.***

Loan: Hypo International is one of the two syndicate members with a share of 86% of the total senior loan. Hypo International is securitising 50% of its share. All portions of the senior loan within or outside the securitisation rank pari-passu to each other. Moreover the borrower has additional debt of a total amount of £98.6 million which is subordinated to the senior loan. Reference Claim 3 is the third largest loan in the pool which represents 10.6% of the principal pool balance. The loan is secured by 85 car show rooms let to a leading European Car manufacturer with a rated parent. The purpose of the 13 year loan was to refinance the senior loan. The loan is a fully hedged fixed rate loan. The loan is secured by first ranking mortgages and assignment of rental income as part of a standard security package. Substitutions are allowed but limited to 6.6% of Day 1 UW MV. The loan features an ICR Event of Default covenant at 1.87x, rising to 2.12x from Dec-2007 to Nov-2010, 2.45x from Dec 2010 to Nov-2013 and 2.89x from Dec-2013 to Nov-2016 and 3.50x thereafter. There is also an LTV covenant according to which until Dec-2014, the LTV must not exceed 70% and thereafter not to exceed 65%.

***Properties are fully let on a long lease which expires 9 years after loan maturity.***

***Fixed rental uplifts***

PROPERTIES: The properties are 85 car show rooms fully let to a leading European car manufacturer with a guarantee on a long lease expiring in October 2028. The properties are well distributed geographically within the UK. The tenant has a right to renew all the leases, not individually only, for 10, 15 or 20yrs. The rent is based on annual uplifts to RPI subject to a floor of 1.5% and a cap of 5% and is currently swapped into 2.6% uplifts every year.

Moody's assessment of the term risk is linked to the credit strength of the tenant and the diversified geographic property locations. The refinancing risk of the Loan is also impacted by the tenant strength, diversified geographic property distribution as well the long lease remaining at refinancing date.

## Reference Claim 4

### *Current Balance on the Whole Loan: £ 171,159,717*

Hypo International Syndicate Portion Current Balance: £ 85,579,859

Hypo International Syndicate Portion Balance Securitised: £ 57,053,239 - 9.6% of total pool

“Above average quality” in this pool from an expected loss perspective

| Maturity | Term | WA Property Grade | U/W Day 1 LTV Loan | U/W exit LTV Loan | MDY LTV | Day 1 U/W DSCR Loan | Day 1 MDY DSCR Loan |
|---|---|---|---|---|---|---|---|
| Dec-2010 | 4yrs | 1.5 | 81.9% | 79.5% | 87.6% | 1.02x | 1.02x |

***The fourth largest Reference Claim in the pool is secured by a prime office building located in a prime location in the UK.***

Loan: Reference Claim 4 is the fourth largest loan representing 9.6% of the total pool. Hypo International is one of the two syndicate members with a share of 50 per cent of the total loan. Hypo International is securitising 67% of their share. The loan is secured by a office building located in a prime location in the United Kingdom. The purpose of the 4 year loan was to finance purchase of the office building. The loan is a fully hedged fixed rate loan. The loan is secured by first ranking mortgages and assignment of rental income as part of a standard security package. The loan features an ICR Event of Default covenant at 1.063x, increasing to 1.15x until maturity. The LTV trigger is set at LTV not to exceed 82.06% until maturity.

***Property is 100% let to a reputable UK entity.***

***Fixed rental uplifts***

PROPERTY: The property comprises of a self contained 15 storey office building with 34 car spaces. The property is held on long leasehold for 999 yrs form July 2005. The head rent is fixed at GBP 1,000 until 2016 afterwards there are 10-yr rent reviews to RPI index. The property is 100% let to a well reputed UK entity for a term of 20 yrs from November 1998. There are fixed rental uplifts until Nov-2007 there after to annual change in RPI subject to a minimum increase of 2.5% and a maximum increase of 5% per annum. From 2008, there will be an RPI swap in place for fixed rental uplifts to 2.76% per annum.

Moody's assessment of the term risk is linked to the credit strength of the tenant. The refinancing risk of the Loan is also impacted by the credit strength of the tenant and the remaining lease term at refinancing date and on the default probability of the Whole Loan.

## Reference Claim 5

### *Current Balance on the Whole Loan: £ 66,200,000*

Securitised Balance: £56,200,000 - 9.4% of total pool

“Above average quality” in this pool from an expected loss perspective

| Maturity | Term | WA Property Grade | U/W Day 1 LTV Loan | U/W exit LTV Loan | MDY LTV | Day 1 U/W DSCR Loan | Day 1 MDY DSCR Loan |
|---|---|---|---|---|---|---|---|
| Nov-2015 | 9yrs | 2.5 | 28.02% | 28.02% | 35.4% | 2.86x | 2.30x |

***The fifth largest Reference Claim in the pool is secured three retails parks located in the UK.***

***The loan is currently not hedged.***

LOAN: Reference Claim 5 is the fifth largest loan representing 9.4% of the total pool. The loan is of a total of £66.2 million split into a term loan of £56.2 million and a revolving facility of £10.0 million. The term facility is fully drawn while the revolving facility has got an undrawn amount of £8.2 million. The term facility will be part of the securitisation while the revolving facility ranking equal but outside the securitisation. The loan is an interest only loan. The loan is secured by 3 retail parks located in the United Kingdom. The purpose of the 9 year loan was to refinance purchase of the properties. The loan is a floating rate loan and there are not hedging arrangements in place. Moody’s has applied a stressed interest rate in its analysis. The loan is secured by first ranking mortgages and assignment of rental income as part of a standard security package. The loan features an ICR Event of Default covenant at 1.50x and an LTV covenant not to exceed 50% until December 2010 and thereafter not to exceed 40%.

***Properties are fully let on long leases.***

Properties: The properties comprises of a portfolio of 3 retail parks located in the United Kingdom. The retail parks provide a total of 543,280 sq ft. All three parks are fully let to well know national as well as regional tenants on long leases. Rent reviews are upwards only on a 5 yearly basis. There are a total of 29 tenants.

Moody's assessment of the term risk is based on the diversified tenant structure and the respective estimated tenant quality. The refinancing risk of the Loan is also impacted by the diversified tenant structure and on the default probability of the Whole Loan.

Table 1:
**Information on the Remaining Loans**

| Loan Name | % of Pool balance | Maturity | WA Property Grade | U/W LTV | U/W exit LTV | MDY LTV | Day 1 U/W DSCR | MDY DSCR | Moody's Assessment |
|---|---|---|---|---|---|---|---|---|---|
| Reference Claim 6 | 7.2% | Jan-2013 | 2.5 | 46.83% | 45.94% | 59.36% | 2.05x | 2.1x | Above Average |
| Reference Claim 7 | 5.0% | Jan-2013 | 2.5 | 36.88% | 34.87% | 36.88% | 3.04x | 1.6x | Above Average |
| Reference Claim 8 | 4.9% | Oct-2010 | 2.6 | 55.75% | 51.52% | 55.75% | 1.41x | 1.4x | Above Average |
| Reference Claim 9 | 3.5% | Jul-2010 | 3.0 | 75.20% | 69.44% | 75.20% | 1.11x | 1.1x | Average |
| Reference Claim 10 | 3.3% | Jul-2014 | 1.5 | 26.80% | 23.44% | 39.55% | 3.61x | 3.6x | Above Average |
| Reference Claim 11 | 2.1% | Jul-2012 | 3.0 | 73.21% | 73.21% | 73.21% | 1.36x | 1.2x | Average |
| Reference Claim 12 | 2.1% | Jun-2011 | 2.5 | 60.69% | 49.72% | 75.86% | 1.04x | 1.04x | Average |
| Reference Claim 13 | 1.4% | Oct-2017 | 2.0 | 38.16% | 28.13% | 54.46% | 2.34x | 2.3x | Above Average |

## ORIGINATOR, SERVICER AND OPERATIONS REVIEW

### The Originator

Hypo Real Estate Bank International AG (**A2**, **P-1**). Hypo International originates its UK commercial mortgage loans partly by its representative office in London together with the respective origination department in its head office in Stuttgart, partly from Hypo International's London branch. Both are part of Hypo International's business line which provides necessary documentation, prepares the credit application for the credit decision process and does the underwriting. The credit application is checked by a member of Credit Risk Management (CRM) which is independent from the business line. Decision making is performed by persons with appropriate credit approval authority as members of a central credit committee.

Hypo International's underwriting criteria for UK commercial loans are based on cash flow analysis and the quality of the collateral in addition to the borrower's creditworthiness. Overall, the underwriting approach can be characterised as prudent with a clear focus on the cash flow generating ability of the properties. Loan terms usually include LTV and ICR covenants. HI usually requires a first ranking mortgage over the properties it lends on.

### The Servicer

Hypo Real Estate Bank International AG (**A2**, **P-1**) will act as servicer for all the loans in the transaction. Hypo International will be responsible for the day to day management of the loans it has serviced since origination, such as the monitoring of loan covenant compliance and portfolio surveillance. Loan servicing and administration is based in London and in Stuttgart under the same standards.

Subject to certain restrictions, Hypo International as servicer will be authorised to make adjustments to loans including payment rescheduling, debt restructuring, rate adjustments, and substitution of properties and replacement of borrowers. Any alterations must not materially adversely affect the interests of the Noteholders or the Swap Counterparties.

## MOODY'S ANALYSIS

For each property in the portfolio, Moody's received an external valuation including an outline of the building, quality, location, operating costs and rental levels. In addition, Moody's analysed the information provided in the external valuations, for example: market rents, void periods and yields data. For the A/B split, Moody's reviewed the inter-creditor Agreement's term sheet and assessed the relative merits of these agreements against other CMBS loan agreements. Moody's received its data input request with a significant amount of data on the loan and the properties.

### Sizing of Credit Enhancement

***Moody's assesses the default probability of a loan, both during term and at refinancing.***

Moody's assesses the default probability of the Loan; both during the term of the Loan on an annual basis (term shadow rating) and at the maturity date (refinance shadow rating). The following inputs, among others, were also incorporated in the analysis of the shadow ratings:

– Terms of the Loans;
– A/B Note structures, including using whole Loan assessment at Loan maturity;
– Moody's model values;
– Moody's property quality grades;
– Diversification of the properties;
– Cash flows available from tenants;
– Diversification of the tenants by industry group;

***Moody's uses Monte Carlo simulation to assign ratings to the Notes.***

Moody's then used a Monte Carlo simulation to derive a loss distribution of the reference loan (MoRE Portfolio). Hereby, a loss distribution is defined as a function that applies to each portfolio loss level a probability of such a loss level occurring. There are several key variables that drive the simulation: the term and refinancing default probability of the loans, and the loans' severity upon default. The latter is derived by simulating the value of the property that secures the defaulted loan in order to determine the recovery value, hereby taking into account accrued interest over the foreclosure time and costs related to foreclosure. Given the nature of the simulation, the recovery rate for each property is assumed to vary over time, reflecting the uncertainties related to property values when a default occurs and also the location and quality of the properties. Within the pool, the value of properties in the same region and/or of the same property type is assumed to be correlated. Having obtained the loss distribution under consideration, a cash flow model is used to assess the impact of structural features of the transaction (MoRE Cashflow). In general the sum of the loss experience per note class weighted by the probability of such loss scenario will then determine the expected loss on each tranche and hence the rating, consistent with Moody's target losses for each rating category.

The provisional ratings are based on an analysis of:

– The characteristics of the current pool backing the notes and the prepayment structure;
– The roles and creditworthiness of the transaction counterparties;
– The legal and structural characteristics of the Issue.

For more information regarding the collateral and loan analysis please refer to the Collateral section.

***Key outputs are then mapped to a rating for each class of Notes.***

The expected loss, probability of default and the weighted average life of the Notes, generated from the Monte Carlo simulation, are then mapped to a rating for each class of Notes

## Enhancement of Pfandbrief Collateral for Class A1+ and A2 Notes

The Pfandbrief Collateral for the **Aaa**-rated Class A1+ and the **Aa1**-rated Class A2 Notes is enhanced by a Cash Deposit, equal to 4% of the respective Notes.

### *Background*

Moody's currently rates the Public Sector Pfandbriefe issued by Hypo International **Aa1**. Public Sector Pfandbriefe are viewed as less risky than Mortgage Pfandbriefe for several reasons as outlined in the Moody's special comments[3]. The high quality of these covered bonds permits their use in this structure as collateral. They are being enhanced in order to collateralize the **Aaa**-rated credit linked Class A1+ Notes and the **Aa1**-rated credit linked Class A2 Notes.

One key element for the rating of the Pfandbriefe and for the determination of the enhancement is that in an insolvency of Hypo International, the cover pool for the Pfandbriefe is not part of the insolvency estate of the bank but is considered a separate estate (Sondervermögen). Hence, separate insolvency proceedings would have to be opened for the cover pool, if it were deemed to be insolvent. The cover pool could be sold more easily to third parties if *deemed* appropriate and in the interest of Pfandbriefe creditors than Moody's would expect to be the case for the cover pool of mortgage Pfandbriefe.

### *Enhancement*

The concept described below of sizing enhancement only applies to Public Sector Pfandbriefe and it would be very unlikely[4] that similar levels of enhancement could be achieved with Mortgage Pfandbriefe, even if the rating of such Mortgage Pfandbriefe were **Aa1**.

In this transaction, the enhancement for the Class A1+ and A2 Notes is in form of a combination of cash deposits and Pfandbrief Collateral. The cash deposit will be held with a **Prime-1** rated Deposit Bank at closing of the transaction. The cash deposit has been sized to address two separate risks of the Pfandbrief Collateral. These risks are not associated with the Reference Pool and are therefore not available to provide protection for Realised Losses occurring under the Reference Loans.

Firstly, the Cash Deposits will provide liquidity in the event that (a) Hypo International goes into insolvency and/or (b) insolvency proceedings are opened over the cover pool for the Public Sector Pfandbriefe. Moody's has determined that, due to the insolvency proceedings, it may be that interest payments under the Pfandbriefe Collateral are not received by the Trustee and hence result in an interest shortfall under the Notes. To protect the holders of the **Aaa**-rated Class A1+ Notes and the **Aa1**-rated Class A2 Notes from such risk, Moody's has sized a cash reserve to put aside enough funds to permit continued timely payment of interest under the respective Notes.

Secondly, the cash deposit is established to achieve protection for losses resulting in the cover pool backing the **Aa1**-rated Public Sector Pfandbriefe. As a starting point for the determination of the necessary cash collateral amount, Moody's has assumed a stressed economic environment under which losses could hit the cover pool. The expected loss of the cover pool in such scenario takes into account high recovery rates. High recovery rates are deemed realistic because of the quality and nature of the underlying public sector loans.

In a next step, the cover pool is enhanced to be in line with the rating necessary to achieve an **Aaa** equivalent expected loss under a two-party pay structure. The enhancement was also sized to cover the weighted average exposure period that the holders of the **Aaa**-rated Class A1+ Notes and the **Aa1**-rated Class A2 Notes have to the Pfandbrief Collateral.

3 For more detail, please see, among others, "Moody's Rating Methodology for German Pfandbriefe" July 2003.

4 The very low likelihood is mainly due to a different assumption of asset correlation and assumed recovery rates.

The concept of "two-party pay" reflects the fact that there are, on the one side, the obligations of Hypo International and, on the other, the security provided by the cover pool. The legal status of the cover pool allows a certain de-linkage between the default of Hypo International and a default under the Pfandbriefe.

In the event that at any time the Pfandbrief Collateral is rated **Aaa** by Moody's, the Issuer shall have the option to request the Trustee for the funds standing to the credit on the Cash Deposit Account an amount equal to the sum of the Class A1+ Cash Deposit and the Class A2 Cash Deposit.

### *Additional Cash Deposit for Class A1+, A2, B, C and D Notes*

In the event that the short-term unsecured debt of Hypo International as Issuer is rated below **P-1** by Moody's, the Issuer shall not later than 30 business days after it has become aware of this downgrade pay **an additional cash deposit for the Class A1+, A2, B, C and D Notes** into the Cash Deposit Account ("**Additional Cash Deposit**"). The amount of the Additional Cash Deposit shall be equal to the aggregate amount of interest payment to be made under each Class of Notes then outstanding, other than the Class E Notes, on the next two immediately following Payment Dates, assuming for that purpose that no Realised Losses, Late Recoveries or amounts of Unjustified Loss Allocation will be allocated to any Notes and no payment of principal will be made with respect to any Notes in each case on such two Payment Dates.

The Additional Cash Deposit shall secure the obligation of the Issuer to make payments of principal and interest under all Classes of Notes, except for the Class E Notes.

In the event that at any time the short-term unsecured debt of the Issuer is rated **P-1** by Moody's, the Issuer shall have the option to request the Trustee for the funds standing to the credit on the Cash Deposit Account an amount equal to the Additional Cash Deposit.

## RATING SENSITIVITIES AND MONITORING

***Moody's will monitor the transaction on an ongoing basis***

Moody's will monitor the transaction on an ongoing basis to ensure that this transaction continues to perform in the manner expected, including checking all supporting ratings and reviewing periodic servicing reports. Any subsequent changes in the rating will be publicly announced and disseminated through Moody's Client Service Desk.

## RELATED RESEARCH

***Moody's approach to CMBS transactions***

For a more detailed explanation of Moody's approach to this type of transaction as well as similar transactions please refer to the following reports:

**Rating Methodologies**

- Moody's Real Estate Analysis for CMBS in EMEA: Portfolio Analysis (MoRE Portfolio), April 2006 (SF71831)
- Update on Moody's Real Estate Analysis for CMBS Transactions in EMEA, June 2005 (SF57645)
- Moody's Approach to Rating European CMBS, June 2001 (SF10481)

**Special Report**

- Non-Sequential Payment Structures in European CMBS Transactions, February 2006 (SF69217)
- Moody's European Country Tiering for CMBS Recovery Rate Assumptions: Focus on Key Jurisdictions, January 2005 (SF45047)
- Swaps in European Term Securitisations, May 2002 (SF13204)
- Liquidity Facilities in European Term Securitisations, August 2002 (SF15810)

*To access any of these reports, click on the entry above. Note that these references are current as of the date of publication of this report and that more recent reports may be available. All research may not be available to all clients.*

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