

The Auto Loan Market

A Week in Review: 17 – 24 Octobre 2007

This week saw Northern Rock's chairman, Matt Ridley, resign from his position. This decision was anticipated by the market and had a positive impact on both CDS and shares linked to Northern Rock. The troubled UK bank's role within Granite will raise an important question in the coming weeks when numerous consortia - such as Virgin, JC Flowers and Cerberus - are said to be mulling a takeover. As mentioned in last week's report, Northern Rock's key role within the master trust could be perceived to be a weakness by the rating agencies if a private equity owner were to take control of the bank.

Meanwhile, the Council of Mortgage Lenders released figures showing a 12% fall in gross mortgage lending in September compared with August. These figures will be well received by investors who, following this summer's credit crisis, are keen to see lenders becoming more stringent in their assessment of borrowers, particularly sub prime and first time buyers.

RBS's announcement that they had started talks with Cheyne Finance with a view to acquiring its SIV would indicate that bank sponsorship of a SIV is expected to improve the vehicle's funding proposition. It certainly shows that banks are acting to ease funding pressures on SIVs, illustrated by the joint venture fund launched by Band of America, Citi and JPMorgan.

Separately, despite enormous pressure on the Spanish ABS market this summer and fears of a much slower prepayment rate, Bankinter announced a 78% year-on-year increase in profit. Group Banco Pastor announced a revenue increase from €123 million to €154 million in the first three quarters of 2007.

Looking at this week's top five movers, European ABS spreads are finally tightening:

ABS Deteriorators							
Short Name	Name	Isin	Spread	Change	Rating	Sector	Avg Life
ABEST 1 A EUR	Asset Backed European Secn Transaction Srl	XS0193710182	26.939	3.35	AAA	Auto Loan	0.948
SANEMP2 2 A2 EUR	Fondo Titul Activos Santander Empresas 2	ES0338058011	58.402	2.67	AAA	Small Business Loan	2.858
PILL41 2004-1 B GBP	Pillar Fdg Ser 2004 1 PLC	XS0191545481	111.399	2.58	A	Credit Card	1.665
PERMAN7 3 C EUR	Perm Fing NO 7 PLC	XS0215351254	167.221	1.46	BBB	PRMBS	2.674
LOCATV2 1 A EUR	Locat Secn Veh 2 Srl	IT0003733083	42.82	0.83	AAA	Equip Lease	3.509
ABS Improvers							
Short Name	Name	Isin	Spread	Change	Rating	Sector	Avg Life
BPMSL 1 A2 EUR	BP Mtgs Srl	IT0004215320	38.007	-6.22	AAA	RMBS	6.397
LOMBFIN4 1 A EUR	Lombarda Lease Fin 4 Srl	IT0003856256	37.19	-5.46	AAA	Equip Lease	2.315
HOLMF10 3 C1 EUR	Holmes Fing No 10 PLC	XS0262872277	156.808	-5.38	BBB	PRMBS	1.752
CAFUND05-1 2005-1 A EUR	Cars Alliance Fdg PLC 2005 1	XS0210128822	30.265	-4.61	AAA	Auto Loan	2.272
GRANMAST06-3 2006-3 C3 EUR	Granite Master Issuer plc 2006 3	XS0268039699	261.474	-3.16	BBB	PRMBS	5.019

The presence of a number of auto loans/lease securities gives us the opportunity to look at the sector.

Auto loan securitisation has developed over the last ten years in response to the massive downgrades by the rating agencies of US car makers such as GM and Ford. Due to their junk ratings, these manufacturers found that raising funds through traditional bond issuance was expensive relative to the securitisation of receivables from car buyers/lesers.

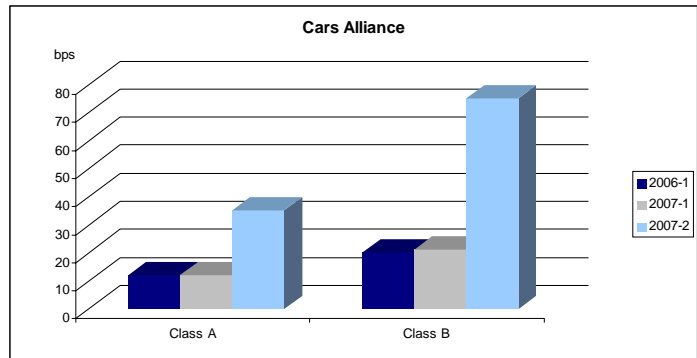
Securitisation thus became increasingly popular in Europe among companies such as Renault, Peugeot-Citroën, Volkswagen and Porsche.

The process is similar to RMBS since a SPV is created to manage these transactions. Because of the large amounts being securitised, these banks are generally ranked within the top 15 national banks. They tend to pay their investors the one month intra-bank rate and are structured with a senior and a junior note.

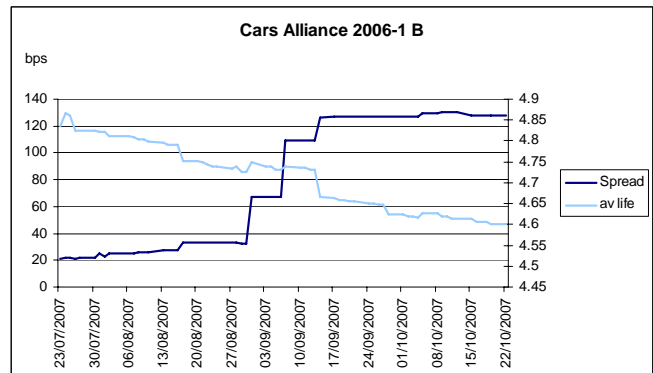
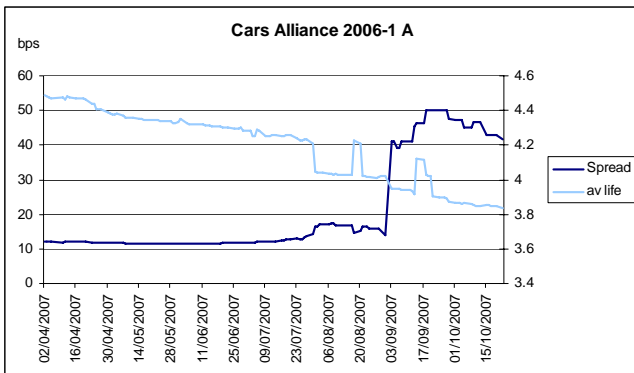
From the consumer's perspective, two types of financing are provided by these banks: loan or lease. Loans along with their prepayment options can be compared to mortgages. Leases, however, are different. At the end of a lease, two options are offered to consumers: They can either buy the vehicle or give it back to the manufacturer who will sell it on the secondary market. Both options could be equated to a prepayment option although the latter creates a residual value which is generally unknown and could impact either positively or negatively on the repayment.

In Europe, the most recent transaction to be priced was Cars Alliance Auto Loans Germany which was originated by RCI, Renault's bank. The credit turmoil has affected the auto sector and the new deal was priced at a new record for the sector. The three most recent Cars Alliance deals to be priced are as follows:

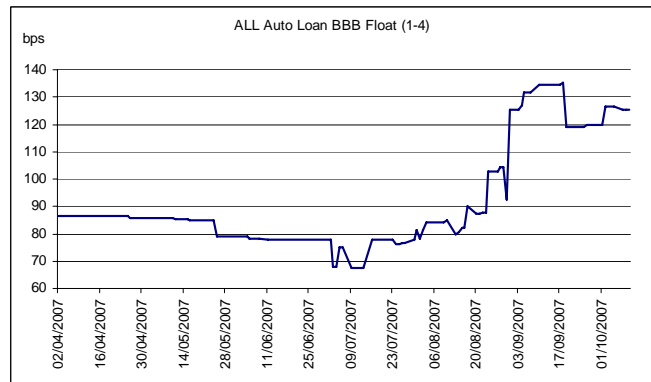
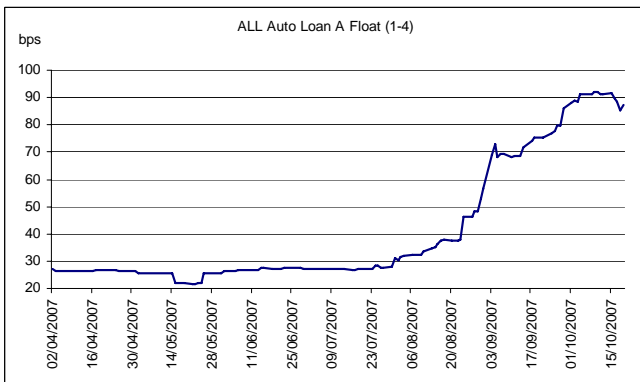
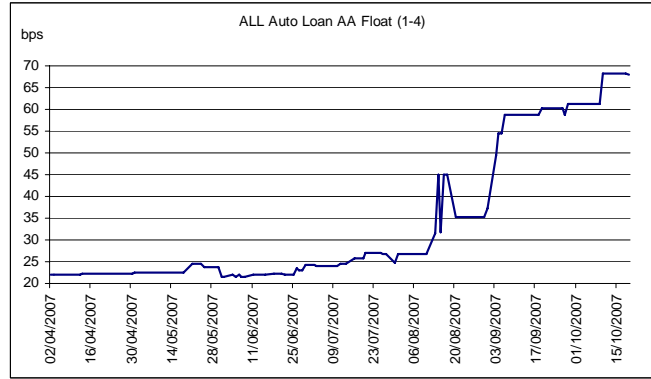
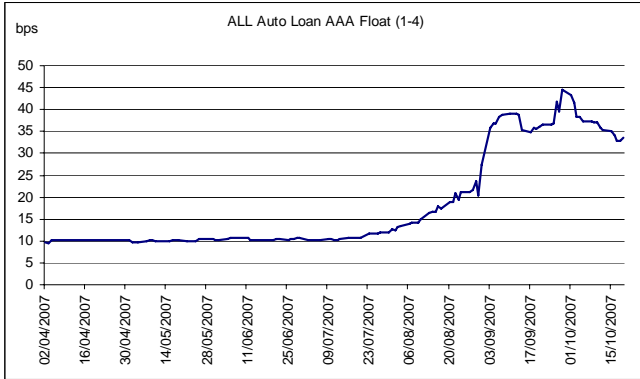
	2006-1	2007-1	2007-2
Class A	12	12	35
Class B	20	21	75
Credit Enhancement	5.5	4.1	6.8
Portfolio's Country	France	Italy	Germany
Number of Contracts	344,315	219,139	N/A
New	65%	93%	N/A
Used	35%	7%	N/A



The trend for the 2006-1 A and B are in line with the rest of the ABS market with the senior spread tightening and the junior stabilising:



The trends above are confirmed by our sector analysis:



Since the majority of European car manufacturers are rated BBB or below, financing through securitisation is an efficient and cheap option. Thanks to the presence of back up servicers in many auto securitisations, the default and delays are limited and well managed. In the case of default, repossession and sale on the secondary market is easier. However, the residual value of a car, contrary to a house, decreases with time and the traditional 40% recovery rate in the event of default can be lower in this sector.

From a corporate perspective, the auto industry is healthy with consistent sales and successful restructuring strategies. Goldman Sachs recently upgraded the sector from neutral to attractive, and Standard & Poor's are confident about growth revenues for the rest of the year.

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