



NEWS RELEASE

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R&I Eligibility Criteria of Swap Counterparties for Securitized Products (Minimization of Swap Counterparty Credit Risk)

Rating and Investment Information, Inc. (R&I) has summarized its ratings approach for products that minimize swap counterparty credit risk (de-linked structured finance vehicles). R&I intends to apply the approach described in this report to the swap counterparties of swap agreements entered into for the purpose of hedging the mismatch between the cash flow generated by underlying assets and the cash flow of Securitized Products (including ABS, CLO, ABCP, RMBS and CMBS).

Issuers sometimes utilize hedge transactions to adjust the cash flows on Securitized Products. For Securitized Products, the major credit risk depends on the quality of the underlying assets that are securitized, while swap counterparty credit risk arising from the hedging transaction is regarded as a secondary credit risk. Therefore a Securitized Product generally is structured to ensure swap counterparty default does not constitute an early redemption event for the issue. Among the substitution measures described in this report for rating triggers for such Securitized Products, R&I will evaluate a Securitized Product by considering "the selection of a swap counterparty to serve as a substitute to succeed to all the swap agreements" to be the main scenario for the swap counterparty credit enhancement measures. Provided an appropriate rating trigger has been set, R&I may assign a rating to the Securitized Product that is higher than that of the swap counterparty. This report summarizes only the most typical de-link measures. Reflecting the diversity of Securitized Products' structures, there are such types of scheme in which the swap counterparty risk is minimized by measures other than the de-link measures described in this report (such as a cash reserve) .

For the de-link measures for Credit-Linked Products (synthetic CDO, first-to-default products, single-name credit-linked products, repackaged products, etc.), please refer to the report "R&I Eligibility Criteria of Counterparties for Credit-Linked Products" released on July 31, 2008.

Rating and Investment Information, Inc. Nihonbashi 1-chome Bldg., 1-4-1, Nihonbashi, Chuo-ku, Tokyo 103-0027, Japan
Structured Finance Rating Division TEL. 03-3276-3406-3428 FAX. 03-3276-3429 EMAIL sfdept@r-i.co.jp Homepage <http://www.r-i.co.jp>

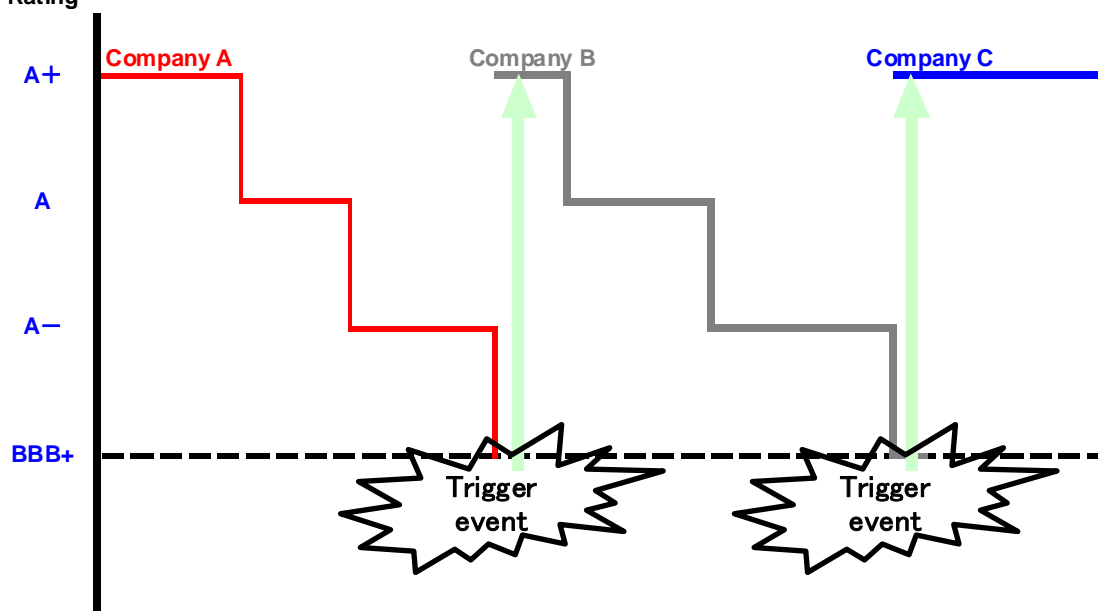
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1. R&I's Assumptions

The effect of swap counterparty credit risk on a Securitized Product will be minimized if the creditworthiness of the swap counterparty incorporated into the Securitized Product can be maintained above a certain level at all times. The de-link measure to achieve this result is the rating trigger. If a rating trigger functions effectively, the creditworthiness of the swap counterparty will not fall below a certain level. The scenario R&I assumes here is "replacement by a new swap counterparty."

■ Figure 1 Counterparty replacement
Rating



R&I continually monitors the creditworthiness of swap counterparties for Securitized Products to which de-link measures have been applied. Nevertheless, the possibility a swap counterparty with a high rating might default within a short timeframe cannot be eliminated entirely. Consequently the rating trigger will not function if this risk is actualized. In that sense, de-link measures can be called measures to minimize swap counterparty risk. R&I monitors the creditworthiness of swap counterparties with an eye to preventing actualization of this risk.

2. Swap agreement substitutability

Because of the cash flow generated by the underlying assets, the contents of swap transactions incorporated into Securitized Products are assumed to be more complex than plain swap transactions available in the market. For a new swap counterparty to succeed to a swap agreement with the same conditions as the prior and existing agreement, the original swap counterparty must bear the cost of restructuring the swap agreement for the new swap counterparty. R&I therefore evaluates the practicability of the main scenario from two points of view.

The first looks at whether a market for the relevant type of swap transaction has been formed with a certain consensus based on mark-to-market methodology. To estimate the replacement cost of the swap transaction born by the original swap counterparty, the swap transaction must be marked to market. Should there be a significant difference in the recognition of the current market value of the swap between the new swap counterparty and the original swap counterparty, there is a possibility the time required to replace the counterparty will lengthen and the likelihood of realizing the replacement with the new swap counterparty will fall. Therefore it is desirable that the swap transaction can be easily marked to market based on a certain consensus concerning the mark-to-market methodology.

The second point is the swap counterparty's short-term debt performance capacity. During the period until the original swap counterparty pays the additional cost to the new swap counterparty and succession to the swap agreement is completed, there is a risk the original swap counterparty will default. R&I therefore applies a Short-term Rating as a criterion for judging the eligibility of the swap counterparty. If the swap counterparty does not have a Short-term Rating, however, R&I will sometimes substitute the Issuer Rating based on Figure 2.

■ Figure 2: Alternative reading of the Short-term Rating from the Issuer Rating

Issuer Rating	AAA to AA-	A+ to A-
Short-term Rating	a-1+	a-1

3. Rating Trigger

The level of the rating trigger is set mainly based on two factors: the Securitized Product target rating, and the substitutability of the swap transaction. The criterion for the substitutability of the swap counterparty is established to respond to the issue of substitutability described in Section 2. Furthermore, even though the swap counterparty credit risk is a secondary risk for Securitized Products as stated previously, R&I establishes a criterion for the Securitized Product target rating because it has judged that a structure with a higher degree of safety should be prepared when the target rating of the Securitized Product is high.

3.1. When substitutability is comparatively high

The rating trigger details for substitution measures for a target rating of AA- or higher are described below as an example. R&I basically considers the substitutability of swap agreements used for Securitized Products to be high.

If its short-term rating falls below a-1, the original swap counterparty promptly implements one of the following measures, and bears the related cost.

- (1) Selects the substitute swap counterparty and has it succeed to all swap agreements.
- (2) Adds a swap agreement guarantee from a financial institution rated a-1+ or higher.
- (3) Deposit cash or other highly liquid assets as additional collateral to cover the amount deemed to be necessary by R&I and in a form acceptable to R&I.
- (4) Takes other credit enhancement measures deemed to be suitable by R&I.

In the situation described above, in principle, the new swap counterparty will be substituted in all of the swap agreements when the Short-term rating of the swap counterparty falls below a-1 (substitution measure (1)). The other substitution measures ((2) to (4)) can also be provided as rating triggers. By increasing the number of alternative de-link measures, the likelihood of supplement the swap counterparty credit risk can be improved.

3.2. When substitutability is comparatively low

When the swap agreement incorporated into a Securitized Product highly varies and R&I judges the substitutability is low from the viewpoint described above in "2. Swap agreement substitutability," R&I sets the rating trigger at more conservative levels as shown in Figure 3 to reflect the original swap counterparty's ability to pay the cost of restructuring the swap agreement and other amounts.

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■ Figure 3: Swap counterparty trigger level

		Swap counterparty trigger level	
		Comparatively high substitutability	Comparatively low substitutability
Securitized Product target rating	AAA to AA-	a-1	a-1+
	A+ to A-	a-2	a-1

The de-link measures described in this report are typical de-link measures for Securitized Products. Because Securitized Products have various structures as stated above, R&I will continue to study de-link measures corresponding to the characteristics of Securitized Products.