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Ratings

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New Issue: Mortimer BTL 2020-1 PLC

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Table Of Contents

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Ratings Detail

Ratings List

Class	Rating*	Amount (mil. £)	Initial credit enhancement (%)	Coupon	Coupon after step-up date	Step-up date	Legal final maturity
A	AAA (sf)	242.249	15.0	Compounded daily SONIA plus 107 bps	Compounded daily SONIA plus 207 bps	June 2023	June 2052
B-Dfrd	AA (sf)	15.674	9.5	Compounded daily SONIA plus 165 bps	Compounded daily SONIA plus 265 bps	June 2023	June 2052
C-Dfrd	A+ (sf)	11.399	5.5	Compounded daily SONIA plus 215 bps	Compounded daily SONIA plus 315 bps	June 2023	June 2052
D-Dfrd	BBB+ (sf)	9.974	2.0	Compounded daily SONIA plus 265 bps	Compounded daily SONIA plus 365 bps	June 2023	June 2052
E-Dfrd	BB (sf)	5.699	0.0	Compounded daily SONIA plus 315 bps	Compounded daily SONIA plus 415 bps	June 2023	June 2052
X-Dfrd	B- (sf)	9.974	0.0	Compounded daily SONIA plus 340 bps	Compounded daily SONIA plus 340 bps	N/A	June 2052
Z	NR	4.385	N/A	Compounded daily SONIA plus 500 bps	Compounded daily SONIA plus 500 bps	N/A	June 2052
Certificates	NR	N/A	N/A	N/A	N/A	N/A	June 2052

*Our ratings address timely receipt of interest and ultimate repayment of principal for the class A notes, and the ultimate payment of interest and principal on the other rated notes. N/A--Not applicable. NR--Not rated. SONIA--Sterling Overnight Index Average. Bps--Basis points.

Transaction Summary

- S&P Global Ratings has assigned credit ratings to Mortimer BTL 2020-1 PLC's (Mortimer 2020-1) class A notes and class B-Dfrd to X-Dfrd interest deferrable notes. Mortimer 2020-1 is a static RMBS transaction that securitizes a portfolio of buy-to-let (BTL) mortgage loans secured on properties in the U.K. LendInvest originated the loans in the pool between January 2018 and February 2020.
- At closing, the issuer used the issuance proceeds to purchase the full beneficial interest in the mortgage loans from the seller. The issuer granted security over all of its assets in favor of the security trustee.
- Credit enhancement for the rated notes consists of subordination from the closing date and overcollateralization following the step-up date, which will result from the release of the excess amount from the revenue priority of payments to the principal priority of payments.
- The transaction features a liquidity reserve fund to provide liquidity in the transaction.
- There are no rating constraints in the transaction under our counterparty, operational risk, or structured finance sovereign risk criteria. We consider the issuer to be bankruptcy remote.

The Credit Story

Strengths	Concerns and mitigating factors
Top-slicing/personal income is not considered in the affordability stresses, ensuring that servicing the mortgage debt relies solely on rental income.	LendInvest is a specialist lender with less than three years of track record in BTL origination, operating until now in a benign macro environment and not regulated by the Prudential Regulatory Authority (PRA). In addition, the rental income used to calculate the debt to service coverage ratio (DSCR) disregards ongoing costs (service charge, insurance, repairs, ground rent, etc.). In our view, this approach is less conservative than what the PRA's buy-to-let underwriting standards recommend.As such, we assigned a base originator multiple above the neutral point (in the range of 1.00x to 1.15x), which affects the weighted-average foreclosure frequency (WAFF) at all rating levels.
As of the Feb. 11, 2020 cut-off date, the pool does not have any arrears. Additionally, 98% of the borrowers in the pool are classified by the originator as Tier One, which means, among other things, that a borrower could not have had a county court judgement (CCJ) or an unsecured default in the last 60 months. Tier Two assets decreased to 2% from 5%, compared to LendInvest's previous transaction, Mortimer BTL 2019-1 PLC.	The pool is newly originated with low seasoning. Borrowers are predominantly portfolio landlords and have to demonstrate experience in running a BTL business, which in our view is a mitigant.
All valuations are full inspections using a Royal Institution of Chartered Surveyors (RICS)-qualified surveyor. LendInvest's underwriters also used third-party automated valuation models as a further control to establish the market value.	The weighted-average original loan-to-value (OLTV) ratio is 72.8%. However, 64.5% of the loans in the pool have an OLTV between 75.0% and 80.8% (as product fees can be added), which is at the high end of LendInvest's lending criteria. For the loans with an OLTV above 75%, the average DSCR is relatively high, which mitigates risk layering (high LTV loans combined with low DSCR).
There are no non-standard properties within the pool. Further advances or product switches are not allowed.	There is no back-up servicer, but if LendInvest were to cease its activities, there are contractual mitigants in place to guarantee that Pepper (UK) Ltd. would service the portfolio until a back-up servicer is appointed.
The transaction structure is a static pool with no revolving or prefunding features.	In the portfolio, around half of the loans are classified as cash-out remortgages in order to withdraw equity. We consider loans for this purpose, rather than to purchase a property, to be riskier. This is reflected in our analysis.
The weighted-average fixed rate on day 1 is 3.52% while the weighted-average post-reversion margin on the loans is close to 4.3%, which generates a considerable level of excess spread to the transaction.	All loans in the pool are fixed and will revert to higher reversionary rates. Therefore, borrowers who are not able to refinance might be exposed to a payment shock. We have reflected this in our analysis by applying a 1.2x adjustment to the foreclosure frequency.
The notes' principal amortization is fully sequential. Credit enhancement can therefore build-up over time, enabling the capital structure to withstand performance shocks. Additionally, on or after the step-up date, certain revenue funds will be diverted to the principal waterfall benefitting noteholders of the rated classes.	The transaction contains a number of loans advanced to limited liability companies. However, all of these loans benefit from personal guarantees and a first-ranking charge on the property as security.
A fully-funded liquidity reserve fund provides support to class A and B-Dfrd notes. Principal can also be used to cure interest shortfalls if the relevant class of notes is the most senior outstanding.	

Originator

LendInvest is a London-based specialist U.K. mortgage lender. It operates through its property lending and investing platform and is registered with the Financial Conduct Authority (FCA).

LendInvest started operating in late 2008 under the name Montello Bridging Finance. It originally provided short-term financing through bridging and development finance products. In November 2017 it started lending in the U.K. BTL space.

As of December 2019, LendInvest's cumulative originations in all products reached £2.6 billion in 12 years of operating, of which £1.2 billion comprises their current book. Most of their BTL book was securitized in either

Mortimer 2019-1 or is securitized in the Mortimer 2020-1 transaction.

Overall, we consider the origination process to be appropriate, with significant and relevant experience of individuals at key stages of the process.

Key factors of the BTL origination process include:

- The loans' applications in BTL business are made via brokers, but LendInvest makes all of the underwriting decisions.
- Full property valuations are conducted for every case using a RICS-qualified surveyor. Full red book valuation is used for large houses in multiple occupation (HMOs) and multi-unit freehold block (MUFBs).
- The decision mandate in the underwriting process depends on the experience and an appropriate seniority status in the company. Fraud checks are done using external databases.
- There is limited tolerance to adverse credit such as CCJs and bankruptcies, and all borrowers must meet income thresholds.
- The affordability assessment for five-year fixed-rate loans is done either at a stressed rate of 5.0% or at the pay rate as compared to a stressed rate of 5.5%, which is used for short-term fixed-rate loans. The minimum DSCR is related to the borrower's tax bracket and is set at a minimum of 125%. Top-slicing is not permitted.
- In LendInvest's current BTL book (as of January 2020) exceptions are marginal. All underwriting exceptions need to be well documented and double-checked by another underwriter.
- There is no lending to non-standard construction properties.

The use of "Open banking" (after customer consent is obtained) is still in an early stage but LendInvest has provided examples showing how it has incorporated the system in its underwriting process. We expect the use of this type of technology to gradually increase over the years, strengthening the origination and underwriting quality.

Servicing

LendInvest is the servicer in the transaction. Pepper acts as the delegated servicer and undertakes primary servicing and special servicing activities (subject to LendInvest oversight at all times) on all loans.

Pepper is responsible for all primary servicing activities:

- New loan processing;
- "Know Your Customer" reviews;
- Direct debit and payment management;
- Statement production;
- Buildings insurance management;
- Covenant monitoring;
- Special servicing and enforcement;
- General loan administration; and

- Redemptions and closure.

LendInvest retains an oversight of the arrears management and collections and recoveries, specifically:

- Approval of the strategy when a loan is in arrears;
- Removal of receivers;
- Possession: price set, price reduction, and offers;
- Death of borrower; and
- Borrower living at security address.

LendInvest maintain weekly checks on all arrears cases with continuous discussion with Pepper on a case by case basis.

We reviewed Pepper's and LendInvest's servicing and default management processes, and determined that they're both capable of performing their functions in this transaction as key transaction parties. We do not cap the maximum achievable rating on the transaction under our operational risk framework (see "Related Criteria").

Asset description

Table 1

Collateral Key Features*

	Mortimer BTL 2020-1 PLC	**Canada Square Funding 2019-1 PLC**	**Precise 2020-1B PLC**
Pool cut-off date	February 2020	September 2019	October 2019
Originator	LendInvest (non-bank)	Fleet Mortgages (non-bank)	Charter Court Financial Services (bank)
Jurisdiction	U.K.	U.K.	U.K.
Principal outstanding of the pool (mil. £)	£285.0	£427.1	£400.7
Number of properties	1,484	1,925	2,424
Average loan balance (£)	£192,048	£221,838	£165,330
Weighted-average interest rate (%)	3.5	3.6	3.5
Weighted-average indexed current LTV ratio (%)	73.0	69.8	72.6
Weighted-average original LTV ratio (%)	72.8	69.5	71.5
Weighted-average effective LTV ratio (%)	72.9	69.5	71.7
Weighted-average seasoning (months)	5	13	10
Interest only (%)	100	95	90
Buy-to-let (%)	100	100	100
CCJ's >= one (%)	0.1	0.1	0.0
Bankruptcy (%)	0.0	0.0	0.0
Loan purpose – purchase (%)	36	26	44
Jumbo valuations (%)	4.4	6.9	3.3
'AAA' RMVD (%)	67.2	70.7	65.3
Arrears >= one month (%)	0.0	0.0	0.0
'AAA' WAFF (%)	25.82	21.88	23.01

Table 1

Collateral Key Features* (cont.)

	Mortimer BTL 2020-1 PLC	Canada Square Funding 2019-1 PLC	Precise 2020-1B PLC
'AAA' WALS (%)	57.75	59.72	54.83

*Calculations are according to S&P Global Ratings' methodology. Information at closing. LTV--Loan to value. CCJs--County court judgments. RMVD--Repossession market value declines. WAFF--Weighted-average foreclosure frequency. WALS--Weighted-average loss severity.

The transaction comprises a U.K. pool of residential mortgage loans (100% first-ranking and BTL). We benchmarked the transaction against the recently closed Canada Square Funding 2019-1 and Precise 2020-1B, which are also 100% BTL.

We received loan-level data as of Feb. 11, 2020, and the quality of the data provided is in line with S&P Global Ratings' standards. All proceeds received for the pool during and after the pool cut-off date (Feb. 11, 2020) until closing (March 19, 2020) were transferred to the issuer transaction account on the closing date.

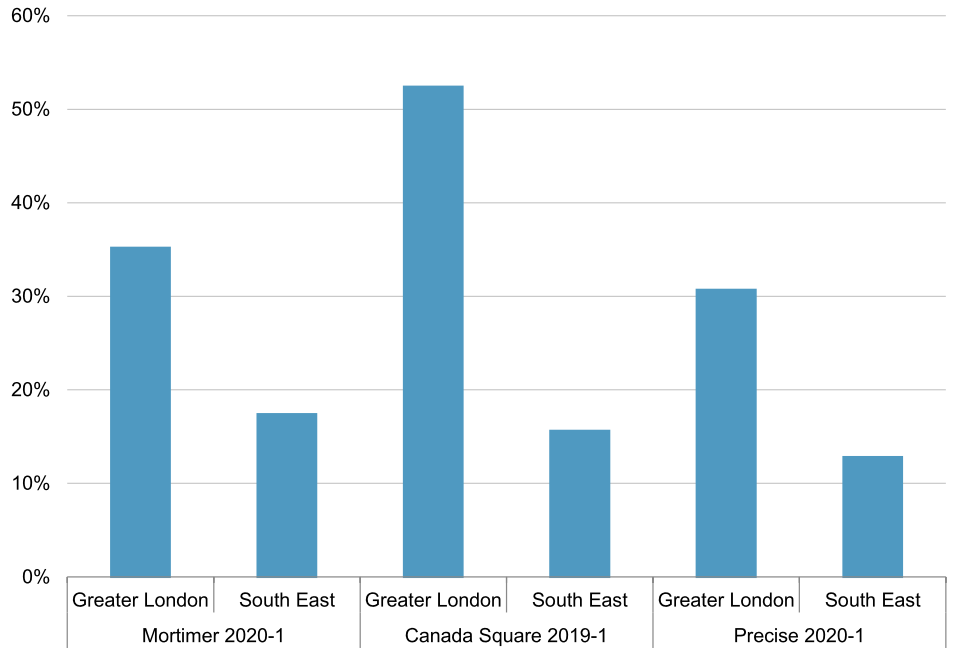
We also received pool audit and re-underwriting reports and did not apply any adjustment to our weighted-average foreclosure frequency (WAFF) given there were no material errors or findings in these reports.

All the loans in the portfolio are interest-only mortgage loans. Given that interest-only is a standard product in the U.K. BTL market, we do not consider this to pose additional credit risk. As part of our surveillance process we will monitor the success ratio of bullet payments at maturity.

The assets are primarily concentrated in Greater London (35.2%) and the South East (17.4%). Pools from peer originators shown similar propensity towards these two regions, which is a common feature in UK BTL transactions. However, given that the concentration in Greater London exceeds the threshold defined in our criteria (26.0%), we applied an adjustment to the excess (9.2%) in our WAFF calculation.

Chart 1

Exposure To Greater London And The South East In BTL Transactions
As a percentage of the pool



BTL--Buy to let.

We applied an adjustment for those cases where the borrower increased the size of the loan when remortgaging or there was no previous loan data. The additional leverage might increase the risk of default when compared to a refinance where no further funds are drawn. In our view, in a professional BTL context remortgages are normally used as a means to fund the purchase of additional properties. Even if LendInvest has affordability criteria on the overall exposure, including to other lenders, we cannot assume that the same underwriting criteria applies to third-party lenders.

The pool is newly originated with low seasoning and the majority of the loans are to professional portfolio BTL landlords. Of the final pool, 63.4% of the loans have been granted to U.K. limited companies and U.K. limited liability partnerships, reflecting the recent trend of lending to corporate borrowers in the BTL space. These loans benefit from personal guarantees provided by the directors (those with at least 25% of the equity in the company) and a first-ranking charge on the property. In addition, corporate borrowers must have a minimum verifiable income of £30,000 from all directors/shareholders.

The exposure to new builds is limited to 8.7% of the current pool balance, which we do not deem excessive. New build or converted properties must benefit from a third-party warranty or equivalent and have all planning consents at the time of application. New builds with an OLTV above 75% are limited to a handful of cases and the weighted-average

OLTV of all new builds in the pool is 74%.

Virtually all fixed-rate loans revert to higher reversionary rates. Therefore, borrowers who are not able to refinance might be exposed to a payment shock. We have reflected this in our analysis by applying a 1.2x adjustment to the foreclosure frequency. In addition, a high proportion of fixed-rate loans will revert to floating in 2024 (see table 2). Therefore, the prepayment rates might increase significantly, causing a reduction in excess spread. We have reflected this in our cash flow analysis by applying different prepayment assumptions (see "Cash Flow Modeling And Analysis").

Table 2

Fixed Rate

Reset year	% of the pool
2020	0.2
2021	15.2
2022	4.7
2023	0.2
2024	61.9
2025	17.9

The rental income used to calculate the DSCR disregards ongoing costs. In our view, this approach is less conservative than what is recommended by the PRA's BTL underwriting standards and we have taken it into account when sizing the originator adjustment. Moreover, the rental income is determined by the property valuer, which, at times, can be higher than the actual rental income. Having said that, the data provided show that the pool's DSCR is comparable to what is observed in peer transactions in the U.K. BTL space (see table 3).

Table 3

Average Yield For Non-HMO Properties

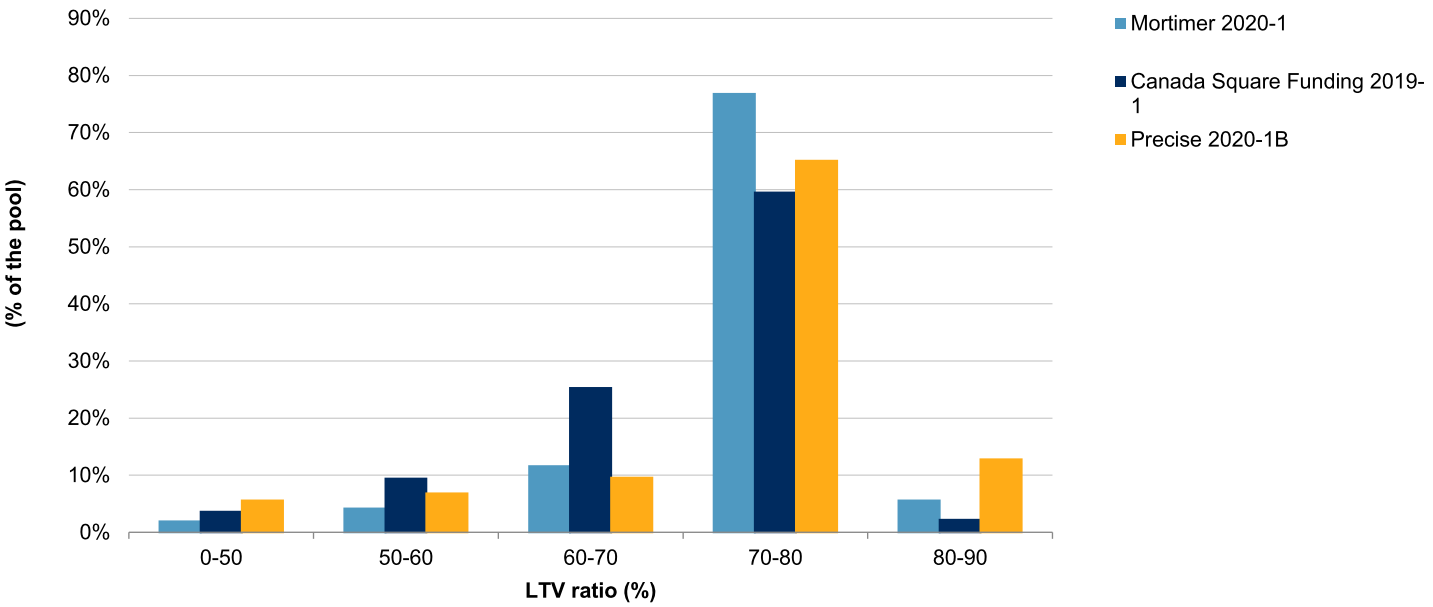
Region	Mortimer BTL 2020-1
East Anglia	5.0%
East Midlands	5.7%
London	4.6%
North	6.9%
North West	6.3%
South East	4.8%
South West	4.8%
West Midlands	5.4%
Yorks and Humber	6.0%

HMO--Houses in multiple occupation.

The pool's weighted-average OLTV is 72.8%. However, 64.5% of the loans in the pool have an OLTV between 75.0% and 80.8% (after product fees are added to the loan balance), which is at the higher end of LendInvest's lending criteria.

Chart 2

Original LTV Ratio Distribution



LTV--Loan to value.

Chart 3

Geographic Distribution Of The Pool

Historical performance data

As a starting point for the rating analysis of RMBS transactions, we typically seek historical performance data (defaults, delinquencies, prepayment, and recovery/loss severity, among others) spanning a minimum of three years, ideally covering a period of economic stress that demonstrates performance consistent with our expectations of similar assets in the relevant asset class. Historical performance data for Mortimer 2020-1 is limited given the fact that LendInvest started lending to BTL mortgages in the fourth-quarter of 2017. We have therefore followed alternative analytical considerations and conducted several tests to mitigate this fact (see "How Much Is Enough? Information Quality

Standards For The EMEA RMBS And ABS Rating Process," published on Jan. 8, 2019). Based on the results of our analysis, we have not applied a ratings cap in this transaction. However, we have applied an originator adjustment above the neutral point (in the range of 1.00x to 1.15x).

LendInvest's BTL book size has increased substantially albeit from a small base. To date, only one property has entered into arrears, and it was eventually sold with no principal loss. Unscheduled amortizations in the BTL products have been marginal as most of the loans are still in their fixed rate periods.

Credit Analysis And Assumptions

We applied our global residential loans criteria to the pool in order to derive the WAFF and the weighted-average loss severity (WALS) at each rating level (see table 4).

The WAFF and WALS assumptions increase at each rating level because notes with a higher rating should be able to withstand a higher level of mortgage defaults and loss severity. Our credit analysis reflects the characteristics of loans, properties, and borrowers relative to the U.K. archetypal pool.

Table 4

Portfolio WAFF And WALS

Rating level	WAFF (%)	WALS (%)	Credit coverage (%)
AAA	25.82	57.74	14.91
AA	17.21	50.58	8.71
A	12.91	37.91	4.89
BBB	8.61	29.70	2.56
BB	4.30	23.46	1.01
B	3.23	17.56	0.57

WAFF--Weighted average foreclosure frequency. WALS--Weighted average loss severity.

Macroeconomic And Sector Outlook

There continues to be a high degree of uncertainty about the rate of spread and timing of the peak of the coronavirus outbreak--some government authorities are estimating late second-quarter 2020 to mid-third-quarter, which we've used in assessing economic and credit implications. In any case, the COVID-19 pandemic has likely pushed the global economy into recession, which could also negatively affect employment levels or housing markets (see "COVID-19 Macroeconomic Update: The Global Recession Is Here And Now," and "COVID-19 Credit Update: The Sudden Economic Stop Will Bring Intense Credit Pressure," both published on March 17, 2020). As the situation evolves, we will update our assumptions and estimates accordingly.

The overall collateral performance of transactions in our U.K. BTL RMBS index has proven stable in the fourth quarter of 2019 compared to the previous quarter.

As with the owner-occupied market, competition in the BTL mortgage sector remains intense. We consider it likely that non-PRA lenders may increasingly look for ways to operate outside regulatory guidelines for competitive

advantage (see "European RMBS Outlook 2020," published on Jan. 27, 2020). The growing prevalence of five-year fixed rates in BTL could lead to lower refinancing activity, although an increase in new lenders gaining scale and reaching the market is likely to boost overall transaction volumes.

Transaction Summary

The issuer is an English special-purpose entity (SPE), which we consider to be bankruptcy remote. We analyzed its corporate structure in line with our legal criteria.

Interest will be paid quarterly, beginning in June 2020. The rated notes pay interest equal to compounded daily Sterling Over Night Index Average (SONIA) plus a class-specific margin, with a step-up in margin following the first optional call date in June 2023. The legal final maturity date of the notes is in June 2052.

Further lending to borrowers would not trigger a mandatory repurchase of those exposures by the seller. Instead, an agreement is in place to ensure that any foreclosure proceeds realized after the sale of a given Mortimer 2020-1 mortgage asset will be first applied toward payment of interest and principal of the relevant mortgage loan. We received legal comfort that upon insolvency of the seller or other lenders governed by English insolvency law, this agreement would still be effective. We consider the risk that there could be a situation in which an acceding party is not governed by English law to be remote, and we will monitor it as part of our surveillance process.

Deferral of interest

Under the transaction documents, interest payments on the class B-Dfrd, C-Dfrd, D-Dfrd, E-Dfrd, and X-Dfrd notes can be deferred until the legal final maturity date and non-payment of interest on an interest payment date would not constitute an event of default until the legal final maturity date. Unpaid interest will accrue at the same rate as the note-specific coupon.

Our ratings address the timely payment of interest and the ultimate payment of principal on the class A notes and the ultimate payment of interest and principal on the other classes of rated notes. Our analysis reflects our view that, at the assigned ratings, the senior fees and senior swap outflows, if any, will be paid on time.

Liquidity reserve fund

The transaction features a liquidity reserve fund that will be available to cover shortfalls on the senior fees, senior swap outflows, and the interest payment on the class A and B-Dfrd notes, provided that the class B-Dfrd notes' principal deficiency ledger (PDL) balance is less than 10% of its original balance. This condition falls away when the class B-Dfrd notes become the most-senior class outstanding.

The liquidity reserve fund was fully funded at closing. The required amount at closing and before the step-up date is 1.7% of the outstanding balance of the class A and B-Dfrd notes, floored at 1.3% of the closing balance of these notes. After the step-up date, the liquidity reserve fund target will stand at the higher of (i) 1.7% of the class A and B-Dfrd notes' outstanding balance, and (ii) 1.3% of the class A to E-Dfrd notes' outstanding balance. Prior to the step-up date, any excess funds will flow down the revenue waterfall. After the step-up date, excess funds will be released to the principal waterfall.

Principal to pay interest

In high-delinquency scenarios, there may be liquidity stresses where the issuer would not have sufficient revenue funds to pay senior fees, swap payments, or interest on the outstanding classes of notes. To mitigate this risk, the issuer can use any existing principal receipts to pay shortfalls in senior fees, swap payments and interest on the class A notes. The issuer can also use principal receipts to pay interest on the class B-Dfrd to E-Dfrd notes once they become the most-senior class outstanding. The use of principal to pay interest will be recorded in the PDL and may reduce the credit enhancement available to the notes. Principal will be used, if applicable, only if revenue funds and the liquidity reserve fund have been exhausted.

Principal deficiency ledgers

The PDL comprises five sub-ledgers, one for each of the mortgage-backed classes of notes (the class X-Dfrd notes does not have a PDL as it is not asset-backed).

Amounts will be recorded on the PDL if the portfolio suffers any losses or if the transaction uses principal as available revenue receipts. This is the market-standard in U.K. RMBS transactions.

Payment priority

Table 5

Priority of Payments

Revenue priority of payments	Principal priority of payments
Senior fees (including servicing fees)	To pay shortfalls on senior fees, the swap outflows, class A notes' interest at all times, and the class B-Dfrd to E-Dfrd notes' interest when they are the most-senior (see "principal to pay interest")
Swap payments	Class A notes' principal
Class A notes' interest	Class B-Dfrd notes' principal
Class A notes' PDL	Class C-Dfrd notes' principal
Class B-Dfrd notes' interest	Class D-Dfrd notes' principal
Top-up liquidity reserve to target	Class E-Dfrd notes' principal
Class B-Dfrd notes' PDL	Excess amounts to the revenue waterfall
Class C-Dfrd notes' interest	
Class C-Dfrd notes' PDL	
Class D-Dfrd notes' interest	
Class D-Dfrd notes' PDL	
Class E-Dfrd notes' interest	
Class E-Dfrd notes' PDL	
Class X-Dfrd notes' interest	
Class X-Dfrd notes' principal	
Junior servicing fees (above cap)	
On or after the step-up date, funds flow to principal waterfall	
Class Z-Dfrd notes' interest	
Class Z-Dfrd notes' principal (only after classes A to F-Dfrd have been fully repaid)	
Swap subordinated amounts	
Excess to certificates	

PDL--Principal deficiency ledger.

Interest rate risk

The pool pays interest based on a fixed rate on day 1 with the majority of the loans on a 5-year fixed rate (see table 6).

Table 6

Distribution Of The Fix-Term In The Pool

	% of the pool
2-year fixed	20.0%
5-year fixed	80.0%

To address the interest mismatch between the mortgage loans and the rated notes, the transaction features a fixed-to-floating interest rate swap, where the issuer pays a fixed rate and receives SONIA to mirror the index paid on the notes. The balance of the swap is a fixed amortization schedule, assuming 0.0% prepayments on the fixed-rate loans. As a result, if any prepayments and/or defaults take place, the deal will be over-hedged. If SONIA is below the fixed rate paid by the SPV, being over-hedged is negative for the transaction, as the notional would be higher than the actual size of the collateral.

Post-reversion interest rates on the mortgage loans are based on three-month LIBOR, whereas the notes are linked to SONIA. To account for this risk, we applied basis risk stresses in our cash flow analysis.

Excess spread

Excess spread results from the difference between:

- The interest income received from the assets; and
- The interest on the rated notes plus any senior fees, servicing fees, and swap expenses.

Excess spread is available to cure any principal deficiencies that arise as a result of losses on defaulted assets. Based on the final pool, we estimate the excess spread to be about 1.3% of the pool balance at closing based on the portfolio's weighted-average yield of 3.52% and assuming a stressed servicing fee of 0.35%.

Cash Flow Modeling And Analysis

In order to assess the payment structure and cash flow mechanics, we model inflows of cash to the issuer, in accordance with the transaction's payment waterfall under a variety of scenarios. Our stress assumptions are primarily asset-specific and generally encompass our analysis of historical credit performance, our forward-looking view, and the economic scenarios. The higher the rating, the more stressful the economic scenario the bond must survive without defaulting on principal or missing a promised interest payment.

In our analysis, the class A notes address rating on timely payment of interest and ultimate repayment of principal. The class B-Dfrd to X-Dfrd notes address the ultimate payment of principal and interest.

Class D-Dfrd and E-Dfrd notes

Our global RMBS criteria establish rating-specific minimum credit enhancement (CE) levels applicable for assigning ratings at issuance of a new transaction. For the class D-Dfrd and E-Dfrd notes, the level of hard credit enhancement is

below the minimum required CE; however, in our analysis, we have concluded that the level of soft enhancement in the transaction (excess spread) is sufficient to support the assigned ratings.

Class X-Dfrd notes

Payment of interest and principal on the class X-Dfrd notes is reliant upon excess spread, with excess spread levels being dependent on prepayment rates in the transaction. In our cash flow analysis, the class X-Dfrd notes do not pass all our cash flow scenarios at the 'B' rating level, with principal shortfalls in the high prepayment rate (30%), declining interest rate curve, and back-loaded defaults scenario. However, we believe this scenario should not materialize at very low rating levels.

Given this and based on our overall view of the U.K. BTL sector, payment of interest and principal on the class X-Dfrd notes is not dependent upon favorable business, financial, and economic conditions (see "Criteria For Assigning 'CCC+', 'CCC', 'CCC-', And 'CC' Ratings," published on Oct. 1, 2012). We have therefore assigned our 'B- (sf)' rating to this class of notes.

Commingling

Borrowers pay into a collection account held with Barclays Bank PLC in the seller's name. The downgrade language on the collection account provider is in line with our counterparty criteria.

If the seller were to become insolvent, the mortgage collection amounts in the collection account may become part of the seller bankruptcy estate. In order to mitigate this risk, at closing the seller signed a declaration of trust in the issuer's favor over the collection account funds. In addition, collections are transferred daily (to the extent £30,000 is accumulated) into the issuer's bank account. Approximately 97% of the borrowers pay on the same day, therefore, funds are swept accordingly.

Although we believe that the above mechanisms (downgrade language and declaration of trust) mitigate against loss of collections, the transfer of funds could be delayed in the event of an insolvency. Therefore, we have applied a liquidity stress equal to one month of collections in our analysis.

Spread compression

The asset yield on the pool can decrease if higher-paying assets default or prepay (product switches are not allowed). Our cash flow analysis accounts for this by assuming that the weighted-average yield on the portfolio is haircut by 0.08% at the 'AAA' level before the step-up date and 0.11% after.

After the step-up date, the pool's weighted-average rate goes from 3.5% (fixed) to 3-months British pound sterling LIBOR plus 4.3% (floating; see table 7).

Table 7

Post-Switch Margin

Margin (%)	Percentage of pool (%)
3.80	38.8
4.59	56.6
4.69	4.6

In addition, we have run a scenario applying 0.30% spread compression at all rating levels, post-switch date. It is based

on the assumption that 50% of the pool prepay close to the switch date as we expect that a large proportion of professional landlords will refinance in order to maximize their investment. The risk is common to all fixed-to-float interest rate products in the U.K.

Servicing fees

The contractual servicing fee are 0.20% per year, as a percentage of the current pool balance. The issuer will also pay a fee of £55 per loan in arrears, per month. The senior servicing fee is capped at 0.25%. Amounts above this cap would be paid junior in the revenue waterfall reducing the available excess spread that is diverted to the principal waterfall, post step-up date.

In line with our global residential loans criteria, we applied a stressed servicing fee to account for the potential increase in costs and need to attract a replacement servicer. We consider 0.35% to be sufficient to attract a replacement servicer given how liquid and developed the U.K. BTL market is.

We have not given credit to the servicing fee cap as we believe in a stressed economic environment this could be waived. Because we have stressed servicing fees above this cap, we have not modelled any junior servicing fee.

Set-off

Since LendInvest is not a deposit-taking institution and loans to their own employees are excluded from the pool, there is no deposit or employee set-off risk in the transaction.

Default and recovery timings

We used the WAFF and WALS derived in our credit analysis as inputs in our cash flow analysis (see table 8). At each rating level, the WAFF specifies the total balance of the mortgage loans that we assume will default over the transaction's life. Defaults are applied on the outstanding balance of the assets as of the closing date. We time defaults following two paths, namely, front-loaded and back-loaded, over a six-year period. During the recessionary period within each scenario, we assume that 25% of the expected WAFF is applied annually for three years.

Table 8

Default Timings For Front-Loaded And Back-Loaded Default Curves

Year after closing	Front-loaded defaults (% of WAFF per year)	Back-loaded defaults (% of WAFF per year)
1	25.0	5.0
2	25.0	10.0
3	25.0	10.0
4	10.0	25.0
5	10.0	25.0
6	5.0	25.0

WAFF--Weighted-average foreclosure frequency.

We assume recoveries on the defaulted assets will be received 12 months after default for BTL properties in England and Wales and 18 months in Northern Ireland and Scotland. The majority of the assets in the pool are located in England and Wales (99.1%).

We estimate foreclosure to cost £5,000 in fixed expenses and an additional 3% of the repossession value in variable

costs. This is based on our observations of the U.K. market.

Our loss severities are based on loan principal and do not give any credit to the recovery of interest accrued on the loan during the foreclosure process.

Delinquencies

To simulate the effect of delinquencies on liquidity, we model a proportion of scheduled collections equal to one-third of the WAFF (in addition to assumed foreclosures reflected in the WAFF) to be delayed. We apply this in each of the first 18 months of the recession and assume a full recovery of these delinquencies will occur 36 months after they arise.

Prepayments

To assess the impact on excess spread and the absolute level of defaults in a transaction, we model both high and low prepayment scenarios at all rating levels (see table 9). There is a high proportion of loans fixed for five years (80%). Therefore, the prepayment rates might increase significantly causing a reduction in excess spread. We have reflected this in our cash flow analysis by performing a sensitivity run in which we increased the prepayments to 50% after four years.

Table 9

Prepayment Assumptions

	High	Low
Pre-recession	30.0	4.0
During recession	3.0	3.0
Post-recession	30.0	4.0

Interest rates

We modeled two interest rate scenarios in our analysis: up and down.

We derived the stressed interest rate curves for the compounded SONIA by subtracting a spread of 0.25% from the LIBOR curves we model. There has been a close relationship between the backward-looking compounded SONIA and the forward-looking LIBOR determined for the same period. However, since SONIA does not include the various risk premiums reflected in LIBOR, the former has generally been lower. The spread adjustment applied to the interest rate reflects the lower SONIA rates historically observed.

Summary

In combination, the default timings, recession timings, interest rates, and prepayment rates described above give rise to eight different scenarios at each rating level (see table 10).

Table 10

RMBS Stress Scenarios

Total number of scenarios	Prepayment rate	Interest rate	Default timing
8	High and low	Up and down	Front-loaded and back-loaded

Counterparty Risk

The issuer is exposed to Elavon Financial Services DAC, UK Branch as the swap collateral account provider, Barclays Bank PLC as the collection account provider, Citigroup N.A., London Branch as the transaction account provider, and Citigroup Global Markets Ltd. as swap counterparty (see table 11). The documented replacement mechanisms adequately mitigate the transaction's exposure to counterparty risk in line with our current counterparty criteria.

Table 11

Supported Ratings

Institution/role	Current Counterparty rating	Minimum eligible counterparty rating	Remedy period	Maximum Supported Rating
Barclays Bank PLC as collection account provider	A/Stable/A-1	BBB/A-2	30 calendar days	AAA

Table 11

Supported Ratings (cont.)				
Institution/role	**Current Counterparty rating**	**Minimum eligible counterparty rating**	**Remedy period**	**Maximum Supported Rating**
Citibank, N.A., London Branch*	A+/Stable/A-1	A/A-1	60 calendar days	AAA
Elavon Financial Services DAC, (U.K. Branch) as swap collateral account provider*	AA-/Stable/A-1+	A	60 calendar days	AAA
Citigroup Global Markets Ltd.§	A+/--/A-1	BBB+	10 business days to post collateral and 90 calendar days to replace.	AAA

*Rating derived from the rating on the parent entity. §Resolution counterparty rating.

Sovereign Risk

Our long-term unsolicited sovereign credit rating on the U.K. is 'AA'. Therefore, our ratings in this transaction are not constrained by our structured finance sovereign risk criteria.

Surveillance And Scenario Analysis

We will maintain surveillance on the transaction until the notes mature or are otherwise retired. To do this, we will analyze regular servicer/investor reports detailing the performance of the underlying collateral, monitor supporting ratings, and make regular contact with the servicer to ensure that it maintains minimum servicing standards and that any material changes in the servicer's operations are communicated and assessed.

Various factors could lead us to lower our ratings on the notes, such as increasing foreclosure rates in the underlying pool and changes in the pool composition. We have analyzed the effect of increased defaults by testing the sensitivity of the ratings to two different levels of movements.

Under our scenario analysis, the ratings on the notes in both scenarios would not suffer a rating transition outside of that considered under our credit stability criteria.

Appendix

Transaction participants

The main transaction parties (excluding those providing supporting ratings) are listed below.

Transaction Participants	
Originator, servicer, and seller	LendInvest BTL Ltd.
Arranger	Citigroup Global Markets Ltd.
Joint lead managers	Citigroup Global Markets Ltd., J.P. Morgan Securities PLC, and National Australia Bank Ltd.
Cash manager and principal paying agent	Citibank, N.A., London Branch
Trustee	Citicorp Trustee Company Ltd.
Delegated servicer	Pepper (UK) Ltd.

Transaction Participants (cont.)	
Servicer facilitator and corporate services provider	Law Debenture Corporate Services Ltd.

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