CDO/CDS Update 07/31/06

I. Commentary

Surprisingly, Friday's lower-than-expected second quarter GDP figure of 2.5%, compared to expectations of 3.1%, helped the equity and credit markets rally as the perceived likelihood of an interest rate hike at the August 8 FOMC meeting decreased. While the focus in the corporate sector continues to revolve around earnings season, HCA Inc. announced the largest leveraged buyout ever last week. The $32.5 billion bid, which includes the assumption of debt, from Bain Capital, KKR and Merrill Lynch moved HCA 5-year CDS spreads to 426 bps after starting the month at around 150 bps. However, on Friday, a group of shareholders filed a lawsuit against the company claiming that it failed to receive a high enough price. In addition, according to *The Wall Street Journal*, Blackstone Group is considering entering a higher bid for the healthcare company. Despite heightened event risk in the market, credit index spreads managed to tighten slightly for the week.

In North America, the CDX investment grade series 6 index tightened just under 1 bp to close at 40.7 bps. The crossover and high yield indices performed well with tightening of about 6 bps each, to finish the week at 195 and 347 bps, respectively. The high volatility index was tighter by 2.3 bps to 79.3 bps. In Europe credit spreads were also tighter across the board. The iTraxx Europe crossover index was tighter by 9.1 bps, ending the week at 269.4 bps. The iTraxx Europe series 5 and high volatility indices were both tighter by about 1 bp to close at 30.6 and 56.9 bps, respectively. The biggest mover on the week was the CDX emerging markets index, which tightened 21.8 bps to a 3-month low of 142.9 bps.

In just its second week of trading, the ABX.HE 06-2 index curve witnessed flattening. The ABX BBB- tranche finished the week 16.7 bps tighter to 225.6 bps, while the AA and AAA tranches traded slightly wider. The A and BBB tranches were tighter by 0.6 and 2.2 bps. Spreads for the CMBX were tighter throughout the index, as the BBB tranche saw spread tightening of 4.3 bps to 65 bps.

FAS 140 meeting update. On July 26 FASB decided to reconsider various issues related to Statement 140-Transfers of Financial Assets. Specifically, the Board decided to address the issue of a qualifying special purpose entity's (QSPE) ability to hold derivative instruments. The Board also agreed to combine the issues of servicer discretion and the rollover of beneficial interests for QSPEs in order to improve efficiency. Ultimately, the Board's decision will likely produce delays in settling the open issues that continue to plague FAS 140. Certain market participants may benefit from the delays because the ultimate resolution of the open issues may make it harder to achieve off-balance sheet accounting. FASB is expected to meet again in September to re-deliberate these topics.

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Fitch's SF CDO 2006 update. Fitch released its US structured finance (SF) CDO performance update for 2006 last week.[1] The report notes that upgrades for new SF CDOs are primarily the result of amortization through prepayments or structural features that allocate excess spread to mezzanine tranches. In SF CDOs rated from 2003 through 2005, 48 tranches were upgraded while only one tranche was downgraded. The positive rating performance is attributed to higher concentrations of MBS and home equity ABS[2] in those vintages and the collateral's stable performance.

Compared to Fitch's previous SF CDO performance update in 2003, there is a much higher concentration of MBS and home equity ABS exposure in new SF CDOs. When comparing 2000 and 2005 vintages, the average exposure to sub-prime mortgage ABS has increased from 25.7% to 58.6%. Mean exposure to MBS (*i.e.*, backed by prime-quality mortgage loans) has also increased from just 4.5% of the 2000 vintage to 23% of the 2005 vintage. Manufactured housing has witnessed a significant decline with 2005 vintage exposure of less than 0.5%, down from 18% in 2000. ABS and CMBS average exposure is also down to just 2.5% and 6.7% in 2005 from 20% and 22.1%, respectively, in the 2000 vintage. Although recent SF CDOs have performed relatively well, the high concentration of RMBS collateral make the sector vulnerable to losses in the event of a long-term downturn in the housing market.

II. Recent Pricing & Pipeline

Issue	Date	Size (mm)	Collateral Manager	Assets	Lead	Class	Rating (*M/S/F*)	WAL	Spread
Seawall 2006-4*	7/28	$300.00	(static)	CMBS	DB				
		165.00				Super Snr	Aaa/AAA/-	-	Not Offered
		79.50				A	Aaa/AAA/-	-	+40/1ML
		19.50				B	Aa3/AA-/-	-	+55/1ML
		9.00				C	A3/A-/-	-	Not Offered
		9.00				D1	Baa2/BBB/-	-	Not Offered
		3.00				D2	Baa3/BBB-/-	-	Not Offered
		15.00				E	-/-/-	-	Not Offered
Stone Tower CLO-V	7/28	$800.00	Stone Tower Debt Advisors	Loans	CS				
		60.00				A1	Aaa/AAA/-	-	+24/3ML
		487.00				A2a	Aaa/AAA/-	-	+23/3ML
		54.50				A2b	Aa1/AAA/-	-	+33/3ML
		43.00				A3	Aa2/AA/-	-	+43/3ML
		36.00				B	Baa2/BBB/-	-	+75/3ML
		29.00				C1	Baa2/BBB/-	-	+160/3ML
		2.50				C2	Baa2/BBB/-	-	FX 7.173%
		24.00				D	Ba2/BB/--	-	+375/3ML
		64.00				Sub Notes	-/-/-	-	-
Mayflower 2006-1**	7/28	$1,000.00	Vanderbilt Capital Advisors	MZ ABS	BS				
		20.00				X	Aaa/AAA/-	3.18	-
		609.00				A1LA	Aaa/AAA/-	-	-
		157.00				A1LB	Aaa/AAA/-	6.48	+45/3ML
		75.00				A2L	Aa2/AA/-	6.48	+50/3ML
		46.00				A3L	A2/A/-	6.48	+140/3ML
		50.00				B1L	Baa2/BBB/-	6.48	+325/3ML
		50.00				Inc. Notes	-/-/-	-	-

[1] Kendra, K, A. Pak and B. Vorderbrueggen, *U.S. Structured Finance CDO Performance: 2006 Update*, Fitch credit products special report (24 July 2006).

[2] The term "home equity ABS" refers primarily to ABS backed by sub-prime mortgage loans.

Issue	Date	Size (mm)	Collateral Manager	Assets	Lead	Class	Rating (M/S/F)	WAL	Spread
Resource RE Funding CDO 2006-1	7/27	$345.00	Resource Real Estate	CRE	DBS				
		129.37				A1	Aaa/AAA/AAA	7.51	+32/1ML
		17.42				A2-FI	-/AAA/AAA	7.64	+35/1ML
		5.00				A2-Fx	-/AAA/AAA	7.64	+35/Sw
		6.90				B	Aa2/AA/AA	8.04	+40/1ML
		20.70				C	A1/A+/A+	8.04	+62/1ML
		15.52				D	A3/A-/A-	8.04	+80/1ML
		20.70				E	Baa1/BBB+/BBB+	8.04	+130/1ML
		19.83				F	Baa2/BBB/BBB	8.04	+160/1ML
		17.25				G	Baa3/BBB-/BBB-	8.04	+190/1ML
		12.93				H	-/-/BBB-	8.04	-
Tropic Trust Pref CDO V	7/27	$800.00	-	TruPs	BS				
		220.00				A-1L1	Aaa/AAA/AAA		Not Offered
		220.00				A-1L2	Aaa/AAA/AAA		Not Offered
		94.00				A-1LB	Aaa/AAA/AAA		+40/3ML
		51.00				A-2L	Aa2/AA-/AA		+60/3ML
		62.00				A-3L	A3/-/A		+128/3ML
		45.00				A-3F	A3/-/A		+128/5ySw
		50.00				B-1L	Baa3/-/BBB		+290/3ML
		8.00				B-2L	Ba2/-/BB		+475/3ML
		59.00				P/S	-/-/-		-
Guggenheim Structured RE 2006-3	7/26	$400.00	GSREA	CRE	CS				
		181.50				A-1	Aaa/-/AAA	5.9	+28/1ML
		22.80				A-2	Aaa/-/AAA	6.4	+32/1ML
		42.10				B	Aa2/-/AA	6.6	+40/1ML
		42.10				C	A2/-/A	6.8	+55/1ML
		24.00				D	Baa1/-/BBB+	7.0	+110/1ML
		28.00				E	Baa3/-/BBB-	7.3	+165/1ML
		18.00				F	-/-/-		Retained
		22.00				G	-/-/-		Retained
		20.00				PS	-/-/-		Retained
		5.00				S	Aaa/-/AAA	2.5	+30/Sw
Stillwater ABS CDO 2006-1	7/26	$650.00	Long Lake Partners	HG ABS (static)	WS				
		520.00				A1	Aaa/AAA/-	4.8	-
		72.48				A2	Aaa/AAA/-	5.0	+37/3ML
		26.00				A3	Aaa/AAA/-	5.0	+42/3ML
		11.05				B	Aa2/AA/-	5.0	+50/3ML
		8.13				C	A3/A-/-	5.0	+140/3ML
		4.55				D	Baa2/BBB/-	5.0	+310/3ML
		7.80				PS	-/-/-	-	Retained
Sextant CLO	7/26	$400.00	Gulf Stream Asset Mgmt	Loans	LB				
		200.00				A1A	Aaa.AAA/-	8.8	+23/3ML
		25.00				A1R	Aaa.AAA/-	8.8	-
		56.25				A1B	Aaa.AAA/-	9.3	+34/3ML
		26.75				A2	Aaa.AAA/-	8.9	+25/3ML
		12.00				B	Aa2/AA/-	9.3	+40/3ML
		24.00				C	A2/A/-	9.3	+70/3ML
		28.00				D	Baa2/BBB/-	9.3	+160/3ML
Gemstone CDO VI	7/26	$700.00	HBK	RMBS/ABS	LB				
		446.25				A1	Aaa/AAA/-	2.8	+23/3ML
		78.75				A2	Aaa/AAA/-	5.1	+40/3ML
		66.50				B	Aa2/AA/-	5.9	+50/3ML
		26.00				C	A2/A/-	6.0	+130/3ML
		35.25				D	Baa2/BBB/-	5.5	+315/3ML
		10.50				E	Ba2/BB/-	6.0	-

Issue	Date	Size (mm)	Collateral Manager	Assets	Lead	Class	Rating (*M/S/F*)	WAL	Spread
Longstreet CDO I	7/25	$500.00	JPMorgan Asset Mgmt	Mezz SF	ML				
		350.00				A1	Aaa/AAA/-	5.8	+30/3ML
		55.00				A2	Aaa/AAA/-	6.2	+42/3ML
		27.00				B	Aa2/AA/-	6.2	+50/3ML
		5.00				C	Aa3/AA-/-	6.2	+60/3ML
		20.00				D	A2/A/-	6.2	+130/3ML
		10.00				E	Baa2/BBB/-	6.2	+300/3ML
		10.00				F	Baa3/BBB-/-	5.5	+385/3ML
		8.00				G	Ba1/BB+/-	5.5	+600/3ML
		15.00				Pref	-/-/-	-	-
Bering CDO I	7/24	$400.00	Terwin Money Mgmt	RMBS	UBS				
		175.00				A1S1	-/AAA/AAA	6.5	+26/1ML
		93.00				A1S2	-/AAA/AAA	6.5	+38/1ML
		42.00				A1J	-/AAA/AAA	6.5	+44/1ML
		40.00				A2	-/AA/AA	6.5	+54/1ML
		14.00				A3	-/A/A	6.5	+150/1ML
		16.00				B	-/BBB/BBB	5.9	+325/1ML
		4.00				C	-/BB/BB	6.5	+650/1ML
		16.00				PS	-/-/-	-	-
START 2006-B*	7/24	$1,000.00	n/a (static)	RMBS	DB				
		500.00				A1A	Aaa/AAA/-	3.6	Not Offered
		15.00				A1B	Aaa/AAA/-	4.3	+43/3ML
		110.00				A2	Aaa/AAA/-	4.5	+47/3ML
		80.00				B1	Aa1/AA+/-	4.5	+57/3ML
		35.00				B2	Aa3/AA-/-	4.5	+67/3ML
		40.00				C	A3/A/-	4.5	Not Offered
		40.00				D	Baa3/BBB/-	4.5	+450/3ML
		50.00				E	-	-	-

New Pipeline	Size (mm)	Collateral Man.	Assets	Lead
Dillon Read CMBS CDO 2006-1**	$1,000.00	Dillon Read Capital Mgmt	CMBS	UBS
Springdale 2006-1*	$611.30	Princeton Advisory	MZ ABS	CS
Hamilton Gardens CDO**	$500.00	Rabobank	RMBS	DBS
Carlyle IX	$425.00	Carlyle Investment Mgmt	Loans	LB
MKP CBO VI	$300.00	MKP Capital Mgmt		CS
Jackson 2006-1	$1,000.00	(static)	MZ ABS	CITG
Wadsworth CDO	$1,200.00	Hartford Investment Mgmt	HG ABS	MS

* denotes synthetic; ** denotes hybrid deals.
Source: MCM, IFR, Bloomberg

III. CDS Spreads

Index Constituent	28-Jul	Week Ago	Moody's Rating	S&P's Rating
Fannie Mae	7	7	Aaa	AAA
Boeing	14	15	A2	A
IBM	19	17	A1	A+
Deere & Co	21	21	A3	A-
GE Capital	15	15	Aaa	AAA
AIG	14	14	Aa2	AA
Dow Chemical	21	20	A3	A-
Alcoa	21	21	A2	A-
CIT Group	28	29	A2	A
Duke Energy	27	28	A3	BBB
McDonalds	15	14	A2	A
Walt Disney	19	17	A3	A-
Viacom	61	54	Baa3	BBB
Time Warner	49	49	Baa2	BBB+
Computer Associates	139	150	Ba1 /*-	BB /*-
Altria Group	36	35	Baa2 /*+	BBB
Tyson Foods	110	87	Ba1	BBB
Ford Motor Credit	428	479	B2	B+
GMAC	215	229	Ba1 /*-	BB /*
Carrefour	17	17	A2	A
AXA	18	18	A2	A
AKZO Nobel N V	22	23	A3	A-
Suez	19	18	A2 /*+	A- /*+
GUS PLC	46	50	Baa1 /*-	BBB+ /*-
Cadbury Schweppes PLC	35	31	Baa2	BBB
Renault	43	42	Baa1	BBB+
Brit Telecom PLC	51	48	Baa1	BBB+
Lafarge	45	46	Baa2	BBB
Deutsche Telekom AG	42	43	A3	A-
METRO AG	37	36	Baa2	BBB
France Telecom	36	36	A3	A-
Telecom Italia SpA	56	56	Baa2	BBB+
Volkswagen AG	28	29	A3	A-
DaimlerChrysler AG	57	59	A3	BBB
VNU	505	419	Caa1	CCC+
Koninklijke Ahold N V	142	151	Ba1	BB

5Y CDS Index	28-Jul	Week Ago	Change
CDX.NA.IG 6	40.67	41.53	-0.86
CDX.NA.IG 6 HVOL	79.33	81.55	-2.22
CDX.NA.IG XOVER	195.33	201.67	-6.34
CDX.NA.HY 6	346.80	352.54	-5.74
CDX.EM 5	142.87	164.67	-21.80
iTraxx Europe 5	30.59	31.93	-1.34
iTraxx Europe HVOL	56.91	57.75	-0.84
iTraxx Europe X-over	269.38	278.47	-9.09
iTraxx CJ Japan 5	28.08	28.39	-0.31
iTraxx Asia ex-Japan	58.25	62.00	-3.75
iTraxx Australia	28.34	28.34	+0.00
iTraxx SDI-75 2	38.75	42.25	-3.50

CDX Widest	28-Jul
SUPERVALU INC	206
Jones Apparel Gp Inc	156
Wendys Intl Inc	128
RadioShack Corp	127
Tribune Co	120

CDX Tightest	28-Jul
Fed Natl Mtg Assn	7
Wells Fargo & Co	10
Wal Mart Stores Inc	10
Target Corp	12
Bristol Myers Squibb Co	13

iTraxx Widest	28-Jul
Portugal Telecom Intl Fin B	176
Degussa AG	117
ITV Plc	116
Glencore Intl AG	107
Koninklijke KPN N V	73

iTraxx Tightest	28-Jul
Nestle S A	6
ABN AMRO Bk N V	7
Royal Bk Scotland plc	8
Barclays Bk plc	9
SAN PAOLO IMI S p A	10

Single-name CDS spreads are on a "XR" basis (without restructuring) for North America.
Source: Markit and Bloomberg

ABX.HE Index (as of July 28, 2006)				
	Price	Weekly change (bps)	Spread* (bps)	Coupon (bps)
ABX.HE.AAA.06-2	100.09	0.04	8.90	11
ABX.HE.AA.06-2	100.10	0.25	14.59	17
ABX.HE.A.06-2	99.88	- 0.57	46.92	44
ABX.HE.BBB.06-2	99.97	- 2.15	131.77	133
ABX.HE.BBB-.06-2	99.99	- 16.69	225.62	242
CMBX.NA Index (as of July 28, 2006)				
	Spread	Weekly change (bps)	Coupon (bps)	
CMBX.NA.AAA.06-1	6.50	0.00	10	
CMBX.NA.AA.06-1	17.86	- 0.50	25	
CMBX.NA.A.06-1	28.21	- 0.79	35	
CMBX.NA.BBB.06-1	65.00	- 4.29	76	
CMBX.NA.BBB-.06-1	112.86	- 2.71	134	

Source: Markit * assuming 35% CPR.

IV. CDS Index Tranche Indicative Spreads & Base Correlation

iTraxx Europe Series 5 (5 years)						
	28-Jul		14-Jul		Change	
Overall index spread	30.5 bps		33.3 bps		- 2.8 bps	
	Spread	Correlation	Spread	Correlation	Spread	Correlation
0%-3%	20%	11.7%	23%	10.3%	- 2.9%	+ 1.4%
3%-6%	79 bps	20.2%	83 bps	19.0%	- 4.5 bps	+ 1.2%
6%-9%	23 bps	26.4%	23 bps	25.5%	+ 0.0 bps	+ .9%
9%-12%	11 bps	31.4%	11 bps	30.8%	+ 0.0 bps	+ .6%
12%-22%	4 bps	46.1%	4 bps	45.8%	- .3 bps	+ .2%
CDX.NA.IG Series 6 (5 years)						
	28-Jul		14-Jul		Change	
Overall index spread	41.0 bps		43.0 bps		- 2.0 bps	
	Spread	Correlation	Spread	Correlation	Spread	Correlation
0%-3%	30%	10.5%	31%	9.9%	- 1.3%	+ .6%
3%-7%	97 bps	24.2%	105 bps	23.0%	- 8.5 bps	+ 1.3%
7%-10%	25 bps	31.7%	25 bps	30.4%	+ 0.0 bps	+ 1.3%
10%-15%	11 bps	42.2%	11 bps	40.8%	+ 0.0 bps	+ 1.4%
15%-30%	5 bps	64.3%	5 bps	63.9%	+ .8 bps	+ .5%
iTraxx Europe Series 5 (7 years)						
	28-Jul		14-Jul		Change	
Overall index spread	40.3 bps		43.4 bps		- 3.1 bps	
	Spread	Correlation	Spread	Correlation	Spread	Correlation
0%-3%	37%	9.9%	41%	8.1%	- 3.6%	+ 1.8%
3%-6%	189 bps	19.0%	195 bps	17.8%	- 6.0 bps	+ 1.2%
6%-9%	58 bps	25.9%	60 bps	24.9%	- 2.0 bps	+ 1.0%
9%-12%	26 bps	32.1%	30 bps	30.8%	- 3.5 bps	+ 1.2%
12%-22%	8 bps	50.3%	8 bps	49.7%	+ .5 bps	+ .6%
CDX.NA.IG Series 6 (7 years)						
	28-Jul		14-Jul		Change	
Overall index spread	51.0 bps		53.3 bps		- 2.3 bps	
	Spread	Correlation	Spread	Correlation	Spread	Correlation
0%-3%	47%	7.0%	48%	6.9%	- .6%	+ .1%
3%-7%	242 bps	18.2%	248 bps	18.5%	- 6.0 bps	- .3%
7%-10%	53 bps	25.6%	55 bps	26.1%	- 2.0 bps	- .6%
10%-15%	22 bps	36.1%	23 bps	36.9%	- 1.0 bps	- .8%
15%-30%	8 bps	60.9%	7 bps	63.5%	+ 1.0 bps	- 2.6%
iTraxx Europe Series 5 (10 years)						
	28-Jul		14-Jul		Change	
Overall index spread	51.8 bps		54.5 bps		- 2.8 bps	
	Spread	Correlation	Spread	Correlation	Spread	Correlation
0%-3%	49%	10.3%	51%	9.3%	- 2.4%	+ .9%
3%-6%	476 bps	13.6%	535 bps	12.1%	- 59.0 bps	+ 1.6%
6%-9%	124 bps	21.0%	135 bps	19.6%	- 11.0 bps	+ 1.4%
9%-12%	57 bps	27.4%	64 bps	25.9%	- 6.5 bps	+ 1.5%
12%-22%	20 bps	46.4%	22 bps	44.7%	- 2.0 bps	+ 1.7%
CDX.NA.IG Series 6 (10 years)						
	28-Jul		14-Jul		Change	
Overall index spread	63.8 bps		65.8 bps		- 2.0 bps	
	Spread	Correlation	Spread	Correlation	Spread	Correlation
0%-3%	55%	7.4%	55%	7.3%	- .1%	+ .1%
3%-7%	551 bps	13.0%	560 bps	13.1%	- 9.0 bps	- .1%
7%-10%	125 bps	20.8%	126 bps	21.3%	- 1.0 bps	- .5%
10%-15%	60 bps	30.8%	63 bps	31.4%	- 3.5 bps	- .5%
15%-30%	16 bps	58.0%	14 bps	60.5%	+ 1.5 bps	- 2.5%

Source: Nomura Securities International

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