



# Structured Finance

## *Russian Mortgage Backed Securities 2006-1 S.A.*

### HIGHLIGHTS

- First residential mortgage-backed securitization from Russia
- US\$88.3mn issue backed by residential mortgages originated by JSC Vneshtorgbank
- Credit enhancement provided by IFC in the form of a purchase of US\$10.6mn Class B mezzanine notes
- First use of IFC's guarantee of an offshore liquidity facility (GOLF) product to mitigate certain currency risks

### THE COMPANY

JSC Vneshtorgbank (VTB) is Russia's second largest bank in terms of assets, capital, retail deposits, and lending. It is also a leading originator of mortgage loans in the Russian Federation. VTB commenced its residential mortgage lending operations relatively recently (2003) but by end-2005 had built the second largest mortgage loan portfolio (totalling US\$200mn) among Russian mortgage originators. VTB provides mortgage loans to borrowers in order to fund the purchase of apartments on the secondary market, properties under construction, stand-alone houses, and plots of land. Mortgage loans are provided in fixed rate US dollars for a term of up to 25 years. Its mortgage portfolio—with loans for the purchase of apartments dominating—is concentrated geographically in Moscow and St. Petersburg due to the relatively high levels of wealth and financial sophistication among the populations of these two areas.

### FINANCING OBJECTIVES

A key goal for VTB was to free-up capital in order to expand the bank's mortgage origination business. By selling the mortgage loans, VTB was able to recycle the capital released from the asset sale into the origination of new mortgage assets. The securitization also allowed VTB to manage more effectively its asset-liability maturity gap and to transfer the prepayment risk of the mortgage portfolio to investors. This is a key advantage as mortgage loan tenors continue to increase in Russia. Moreover, the

success of this inaugural offering of mortgage-backed securities has given VTB an additional sustainable funding option to support the rapid growth of its mortgage origination business.

### THE STRUCTURE

VTB's first RMBS transaction involved the securitization of approximately US\$88mn worth of fixed rate US dollar-denominated loans. The transaction was divided into three tranches consisting of US\$74.2mn (84%) in senior Class A notes, US\$10.6mn (12%) in mezzanine Class B notes, and US\$3.5mn (4%) in junior Class C notes. The Class A notes achieved ratings of A1/BBB+ from Moody's/Fitch, with the Class B and Class C notes rated Baa2/BBB and B2/BB-, respectively. The senior notes benefit from several forms of credit enhancement, including excess spread, subordination of the Class B and Class C notes in the payment waterfall, and a non-amortizing cash reserve account equal to 2.5% of the initial total balance of all three note classes. The senior notes (as well as the Class B mezzanine notes) also benefit from IFC's provision of its GOLF product to mitigate currency transfer and convertibility risk. The IFC GOLF product enabled the senior notes to achieve credit ratings (A1/BBB+) one notch higher than each agency's then-current Russia country ceiling and higher than VTB's own foreign currency ratings (Baa2/BBB).

## OUTCOME

The transaction placement was a notable success, with the Class A notes oversubscribed 3 times. The VTB transaction marked the first use of securitization as a long-term funding option for a Russian mortgage originator and is expected to be replicated by other lenders in Russia. The active role of IFC as an investor, structurer, and credit enhancement provider assisted VTB in its goal to access long-term, cost-effective US dollar financing and to establish its name with European and US asset-backed investors. Borrowers in Russia will also benefit as VTB recycles the proceeds of the issuance into additional lending to aspiring home purchasers.

Finally, the transaction also serves the important developmental goal of furthering the adoption of capital market standards in the Russian economy. The increasing use of credit ratings, credit scoring, and market-standard securitization structuring techniques by Russian originators will help improve the efficiency of financial intermediation in Russia. In addition, the dissemination of these standards and “best practice” financing techniques should assist in the development of the local ruble capital market. These factors taken together should over time expand the provision of housing finance to a broader cross-section of the Russian population.

## TERMS AND CONDITIONS

<b>Amount</b>	US\$88.3mn
<b>Currency</b>	US Dollar
<b>Issue Date</b>	July 18, 2006
<b>Legal Maturity</b>	July 19, 2034
<b>Series</b>	Class A: US\$74.2mn Class B: US\$10.6mn Class C: US\$3.5mn
<b>Interest Payment</b>	Class A: 1-month LIBOR + 1.0%, payable monthly Class B: 1-month LIBOR + 2.0%, payable monthly Class C: 1-month LIBOR + 5.0%, payable monthly
<b>Principal Payment</b>	Pass-through
<b>Initial Rating</b>	Class A: A1 by Moody's, BBB+ by Fitch Class B: Baa2 by Moody's, BBB by Fitch Class C: B2 by Moody's, BB- by Fitch
<b>Enhancement</b>	IFC purchase of US\$10.6mn subordinated Class B notes and provision of GOLF product, excess spread, Class C notes subordination, and cash reserve account

