Markit

Rolling Procedures CMBX Indices

Overview: Rolling into the New Series of CMBX Indices

CDS IndexCo and Markit will be introducing a new series of the CMBX indices on October 25th, 2006. This document will provide important information on "rolling" from first series index trades into second series indices. The roll concept was originally introduced in the corporate index market as a way for investors to retain exposure to the most liquid series of indices. With a large overlap in reference entities from series to series in CDX and iTraxx, liquidity tends to be concentrated in the most recent, "on-the-run" series. CMBX is constructed to function differently, with each series providing a unique vintage profile. In anticipation that there may be interest from investors in rolling into CMBX Series 2, CDS IndexCo and Markit have prepared this brief overview.

Rolling from CMBX 1 into CMBX 2 changes the nature of risk referenced in a trade as the new series will consist of a unique set of deals (and underlying loans). In this way, CMBX differs fundamentally from corporate indices as CMBX was developed to provide participants with vintage exposure:

- CMBX Series 1 represents Commercial Mortgages underwritten in Q4 of 2005 and Q1 of 2006
- CMBX Series 2 represents Commercial Mortgages underwritten in Q2 and Q3 of 2006

In contrast, each series of CDX and iTraxx indices is constructed to reflect the most liquid names in the corporate market at that point in time. For example, rolling from one series of CDX.IG to the next has historically changed one's exposure by only 3-5%.

Considerations for Rolling into CMBX 2

- It is possible that the "on-the-run" indices will maintain the most liquidity, but dealers will continue mark the most recent "off-the-run" series to retain transparency in the first series Indices as well.
- As coupons may vary between the two versions of CMBX, upfront payments may be significant

Quoting Conventions

When asked to quote a roll for a counterparty, dealers can bid or offer the roll. In this instance there would be two quotes, one consisting of a quote on the CMBX 1 index and another quote on the CMBX 2 index:

<u>Roll a client's standing CMBX 1 Position Into a CMBX 2 Position</u>

- "Dealer Offers Roll" –
    - Dealer Bids $[size]mm client from CMBX 1 & Offers client into $[size]mm CMBX 2
- "Dealer Bids Roll" –
    - Dealer Offers $[size]mm client from CMBX 1 & Bids client into $[size]mm CMBX 2

Operational Procedures

<u>Roll Into CMBX 2 with Original Counterparty</u>

This consists of two transactions, first a tear-up of the original trade and entering into new position on CMBX 2.

The tear-up and the new trade will include a market value exchange based upon the market quoted as well as an accrued component.

<u>Roll Into CMBX 2 with New Counterparty</u>

Investors are under no obligation to roll into a CMBX Series 2 index with their original counterparty on a trade. An investor will novate (or assign) their leg of a trade to the new counterparty. An investor will then enter a trade on the CMBX 2 series with the new counterparty.

In this case, the assignment and the new trade will include a market value exchange based upon the market quoted as well as an accrued component.

It is also important to note that the market for CDS of ABS and CMBS also observes the ISDA Protocol on assignments. Importantly, this requires that all parties to an assignment consent to the trade. Generally, investors should be confident that consent will be granted by their original dealer counterparty.