Marzio Finance S.r.l. – Series 6-2019
Italian Consumer CQS ABS

Ratings

Series	Rating	Notional (EUR m)	Notional (% assets)	CE[1] (% assets)	Coupon	Final maturity
Class A	AA+$_{SF}$	571.6	92.0	8.0	0.30%	September 2041
Class J	NR	49.6[2]	8.0	0.0	Variable	September 2041
Rated notes		621.2				

Scope's analysis is based on the portfolio dated 30 June 2019 provided by the originator. Scope's Structured Finance Ratings constitute an opinion about relative credit risks and reflect the expected loss associated with the payments contractually promised by an instrument on a particular payment date or by its legal maturity. See Scope's website for the SF Rating Definitions.

Transaction details

Purpose	Liquidity/funding
Issuer	Marzio Finance S.r.l.
Originator/servicer	IBL – Istituto Bancario del Lavoro S.p.A. (IBL Banca or IBL)
Seller	IBL Finance S.r.l.
Master servicer	IBL Servicing S.p.A. (IBL Servicing)
Back-up servicer	Zenith Service S.p.A. (Zenith)
Account bank	Citibank N.A., Milan Branch (Citibank)
Closing date	31 July 2019
Payment frequency	Monthly, 28th day of each month

The transaction (Series 6-2019) is IBL Banca's sixth true-sale static securitisation of Italian payroll-deductible loans ('cessione del quinto dello stipendio' or CQS[3]), under the Marzio Finance S.r.l. programme. The notes are backed by a EUR 604.4m portfolio of CQS loans comprised of 'cessione del quinto' (83.8%) and 'delegazione di pagamento' (16.2%) loans extended to employees working for the public administration (39.2%), the central state administration (13.8%) and the private sector (4.6%) as well as pensioners (42.3%). The portfolio is highly granular and has a weighted average seasoning of 3.8 years. All the underlying loans are insured against life and employment events. Regional concentration is as follows: north (28.4%), centre (32.1%) and south (39.5%).

Rating rationale (summary)

The rating reflects: i) the legal and financial structure of the transaction; ii) the quality of the underlying collateral; iii) the insurance protection against life and employment events; iv) the ability of IBL Banca (rated BBB by Scope) as originator, servicer, calculation agent, and collection account bank; v) the ability of Zenith Service S.p.A. (Zenith) in its role as back-up servicer and back-up calculation agent; and vi) the counterparty exposure to Citibank N.A., Milan Branch (Citibank) as transaction bank and paying agent.

The rating is mainly driven by the securitised portfolio's characteristics and its expected performance, and by the pool of insurance companies covering life or employment events. The rating also incorporates our positive assessment of the servicer's abilities and incentives. We considered Italian sovereign risk by assessing the impact on the rating of a distress scenario affecting the government of Italy and the associated loss severity for the securitised assets.

[1] Including a EUR 5.7m liquidity reserve and a EUR 9.1m additional reserve.
[2] Class J funds a portion of the portfolio (EUR 34.8m) as of the closing date, but also the liquidity reserve and the additional reserve, which is included in this figure.
[3] In Italy, CQS is used as an abbreviation for 'cessione del quinto dello stipendio'. In the context of this transaction, we use this term to refer to 'cessione del quinto' (CDQ) loans, extended to employees or pensioners, and to 'delegazione di pagamento' (DP) loans.

Analytical Team

Leonardo Scavo
+39 02 9475 9859
l.scavo@scoperatings.com

Paula Lichtensztein
+49 30 27891 0
p.lichtensztein@scoperatings.com

David Bergman
+39 02 3031 5838
d.bergman@scoperatings.com

Related Research

Consumer and Auto ABS Rating Methodology

Methodology for Counterparty Risk in Structured Finance

Scope Ratings GmbH
Lennéstraße 5
10785 Berlin
Tel. +49 30 27891 0
Fax +49 30 27891 100
info@scoperatings.com
www.scoperatings.com
Bloomberg: SCOP

Class A is supported by 8.0% of credit enhancement and benefits from the structural protection provided by sequential principal amortisation. A liquidity reserve and an additional reserve provide both liquidity and credit protection to the class A notes.

IBL Banca performs several key roles, including that of originator, servicer, calculation agent, and collection account bank. Operational risk is mitigated by the appointment of Zenith as back-up servicer and back-up calculation agent.

Rating drivers and mitigants

Positive rating drivers

Experienced originator. IBL Banca is one of the most experienced CQS loan originators in Italy, with a track record of above-average performance for its loan book.

Underlying asset type with low historical losses. CQS loans incur lower losses than standard unsecured consumer loans, primarily because the loans are fully insured, and instalments are withheld by the borrower's employer and paid directly to the lender.

Liquidity and credit protection. A fully funded liquidity reserve (EUR 5.7m at closing) will provide liquidity protection to the class A during the life of the transaction. An additional reserve (EUR 9.1m at closing) will also protect the liquidity of the rated notes and provide ongoing credit protection to the class A. Both reserves will be available to repay the notes at maturity.

Static portfolio. The portfolio will start amortising immediately after closing, reducing the risk of performance volatility compared to revolving transactions.

Excess spread. We expect that a high level of excess spread will remain available (3.1%) after stressing the weighted average portfolio yield and deducting fees and interests on liabilities.

No interest rate risk. There is no interest rate mismatch since both the notes and the portfolio pay a fixed rate.

Negative rating drivers and mitigants

Exposure to public entities. A large portion of the portfolio is exposed to public entities that pay salaries or pensions to borrowers (95.4%). These borrowers normally have lower default rates than those in the private sector. However, such a high concentration can increase vulnerability to a sovereign default. Our analysis has considered this by incorporating a sovereign stress event.

Set-off risk via upfront loan commissions. Borrowers can claim back a portion of the fees and commissions paid upfront if they prepay their loan. A dedicated management fee reserve, equal to 25% of the total exposure, mitigates the set-off risk. As of 30 June 2019, management fees amounted to EUR 6.4m.

High prepayment risk. The portfolio has a weighted average seasoning of 3.8 years. Historical data show a spike on prepayment rates after 4 years from origination, as borrowers are allowed to refinance their loan once they have reimbursed 40% of the initial loan balance. We have considered this risk by assuming that 25% of the highest yielding loans will prepay in the first year of the transaction's life.

Commingling risk. Commingling risk is mitigated by: i) a daily sweep of collections to the issuer's account; and ii) instructions to borrowers to redirect payments to the issuer's account in the event of a servicer disruption. However, as most employers pay by bank transfer, the redirection of payments may take longer than for a standard unsecured loan portfolio.

Upside rating-change drivers

A rating upgrade of Italy, a reduction of the insurance companies' default risk or better-than expected pool performance would contribute to an upgrade of the rating.

Downside rating-change drivers

A significant deterioration in the credit profile of the insurance companies leading to lower rating-conditional recovery rate assumptions could negatively impact the rating.

A decline in the pool's overall performance versus our expectations or a significant rating downgrade of Italy could also have a negative effect on the rating.

Marzio Finance S.r.l. – Series 6-2019

Italian Consumer CQS ABS

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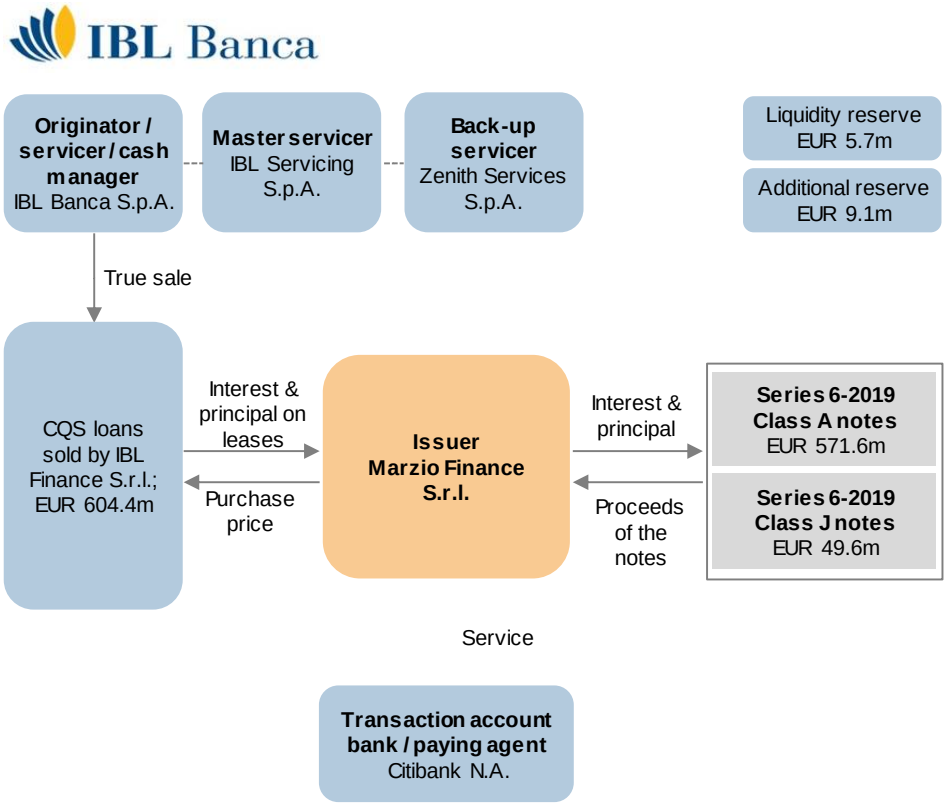
1. Transaction summary

Figure 1: Simplified transaction diagram



Source: Transaction documents and Scope

Marzio Finance S.r.l. has established a EUR 10bn securitisation programme of notes backed by CQS loans extended to borrowers in Italy and originated by IBL Banca. CQS loans are collateralised by the debtor's salary or pension and, in most cases, by any accrued severance amount (e.g. 'trattamento di fine rapporto' or TFR).

Series 6-2019 is IBL Banca's sixth issuance under the Marzio Finance programme

Under the programme, several series of notes may be issued. Each series is structured as an independent transaction, with no cross-collateralisation, for the purpose of financing the purchase of a static portfolio of receivables originated by IBL Banca. The capital structure, cash reserve level and notes' interest rates may differ among the different series.

The transaction (Series 6-2019) is the sixth true-sale securitisation under the programme. It is backed by a EUR 604.4m static portfolio of CQS loans.

2. Originator and seller

IBL Banca: market leader in Italy for CQS with a 15.2% market share

IBL Banca is the parent company of the IBL banking group, whose fully owned subsidiaries manage the services, real estate and the distribution of insurance for the entire group. IBL is a specialised lender that offers personal finance loans to individuals, particularly Italian CQS loans. As of end-2018, the group was a market leader in Italy for CQS, with a solid 15.2% market share and about 170,000 loans under management. IBL also offers savings and insurance products, and payment cards.

IBL's distribution model comprises 53 branches, plus further branches via distribution agreements with nine banking partners. The bank also has a broker network of 90 agents, promoters and intermediaries, as well as an online channel.

Historically, IBL has operated an originate-to-distribute model, largely due to limited financial resources. After obtaining a banking licence in 2004 and acquiring 30 Citifinancial branches, IBL started to raise funding through deposits. This gave the bank the financial ability to transition to a more balance sheet-intensive model, reaching an asset size of around EUR 6.02m at end-2018.

2.1. Sanctioning and underwriting

The originator employs a credit scoring system, which uses both internal and external information. All credit approval and underwriting activities are handled in-house, despite around half of new loans being originated by the broker network.

The underwriting process is mainly focused on the employer of the borrower, given the nature of payroll-deductible loans. The loan applicant must also satisfy all quantitative and qualitative requirements. Among other things, the credit department ascertains whether the employer meets certain size, legal, capital and performance requirements, using internal databases and external credit bureaus as its main sources of information. The loan applicant's credit is assessed with the support of a specialised outsourcer, focusing on the risk of fraud, creditworthiness and on the existence of any outstanding default exposures.

Loans are ultimately disbursed upon the receipt of insurance coverage and acceptance of the payment delegation by the employer or pension provider.

2.2. Servicing and recovery

IBL Banca is servicer for the transaction, with IBL Servicing acting as master servicer. IBL's management of collections and non-performing loans is adequate in our view, involving a reasonably proactive and diligent approach.

The management of collections is fully based in Rome, with a dedicated team of 13 employees. Most of the collections are paid via bank transfer and portfolio performance is monitored daily to check for any delinquent payments.

When a loan becomes delinquent, the credit monitoring department contacts both the borrower and the employer within 90 days via phone and email to solicit the payments. If the contract is still delinquent after 90 days and an insurance claim has not been opened, it is sent to an external supplier for another 90 days. After 180 days, a written notice is sent to both the borrower and the employer. IBL then starts legal proceedings within 30 days unless the borrower or the employer has cured its position.

In the case of life and employment events, the credit monitoring department classifies the loans as 'subject to claim' as soon as it receives the death certificate (for life events) or verifies the nature of unemployment (for employment events). For the latter, IBL sends a request to the employer, asking them to cover the residual debt (partially or in full) with the borrower's accrued severance indemnity. The remaining claim is then settled by the insurance company upon receipt of the relevant documentation.

3. Asset analysis

The securitised portfolio is a granular pool of CQS loans granted to individuals in Italy who work in the public or private sector, or are pensioners. A sub-pool of the portfolio is comprised of 'delegazione di pagamento' (DP) loans, which are also payroll-deductible but have slightly different characteristics to 'cessione del quinto' (CDQ) loans, as explained below.

3.1. Payroll-deductible loans: CDQ and DP loans

Payroll-deductible loans offer additional protection and are distinguishable from standard consumer loans in two key respects: i) monthly instalments are paid directly to the lender

by the employer or pension provider after being deducted from the obligor's monthly salary or pension; and ii) every loan is insured for job-loss and life-event risks. CQS portfolios are exposed directly to employers, pension providers and insurance companies. We have considered these risks in our analysis.

3.1.1. CDQ loans

Loan instalments cannot exceed 20% of the borrower's total net salary or pension and are deducted directly from the salary or pension by the employer or pension provider. For employees, the loans are also generally collateralised by a pledge on the debtor's accrued TFR. CDQ loans typically have an original term of 10 years, pay a fixed rate and cannot be refinanced until two-fifths of the loan has been repaid.

3.1.2. DP loans

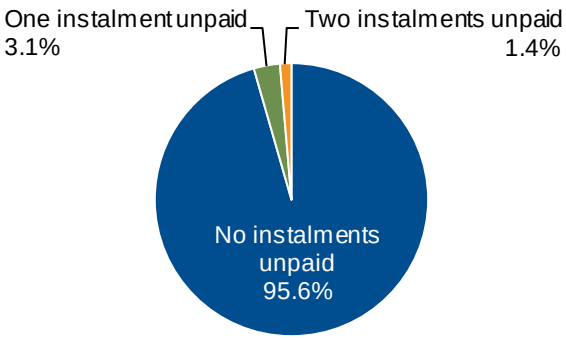
DP loans are typically granted to borrowers that already have an outstanding CDQ loan. The addition of a DP loan can mean a total monthly instalment of up to 50% of the borrower's net income. DP loans are subordinated to CDQ loans, but this risk is partly mitigated by the originator's familiarity with the existing borrower before a loan is authorised.

For more detail on CQS loans, download our Consumer and Auto ABS Rating Methodology.

3.2. Securitised assets

The EUR 604.4m portfolio as of 30 June 2019 is comprised of CDQ (83.8%) and DP (16.2%) loans extended to employees working for the public administration (39.2%), the central state administration (13.8%) and the private sector (4.6%), or to pensioners (42.3%). Compared with IBL Banca's total loan book, the portfolio benefits from positive selection, as eligibility criteria exclude, among other things, exposures that have more than two instalments due and unpaid.

Figure 2: Distribution by delinquency status in terms of unpaid instalments, % of the outstanding balance



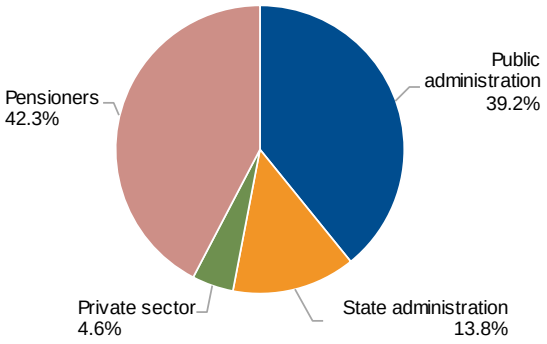
Source: IBL Banca, Scope

High-seasoned portfolio

The current loan portfolio has 3.8 years of weighted average seasoning and a weighted average remaining term to maturity of 6.0 years. Most of the loans were originated between 2015 (35.7%) and 2016 (51.7%). Loans transferred to the portfolio have at least one instalment paid and 78.7% of the portfolio matures around 6 years after the transaction closes. The maturity date could be extended if payments are suspended due to salary or pension reductions, or due to temporary leave (e.g. maternity leave). Suspended payments will then be moved to the end of the original amortisation plan.

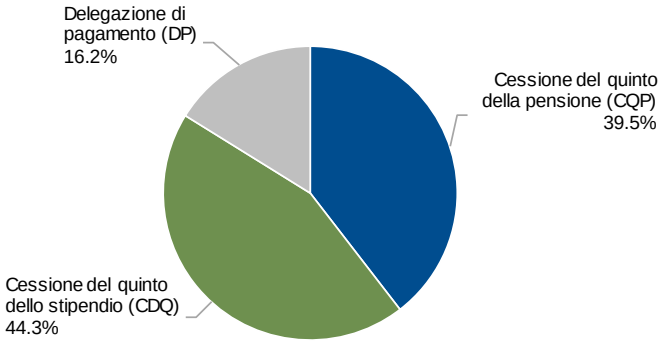
All loans in the pool are amortising and pay monthly instalments at a weighted average fixed interest rate of 5.8%. Eligibility criteria exclude loans that have an interest rate below 4.0%.

Figure 3: Distribution by employer type, % of outstanding balance



Source: IBL Banca, Scope

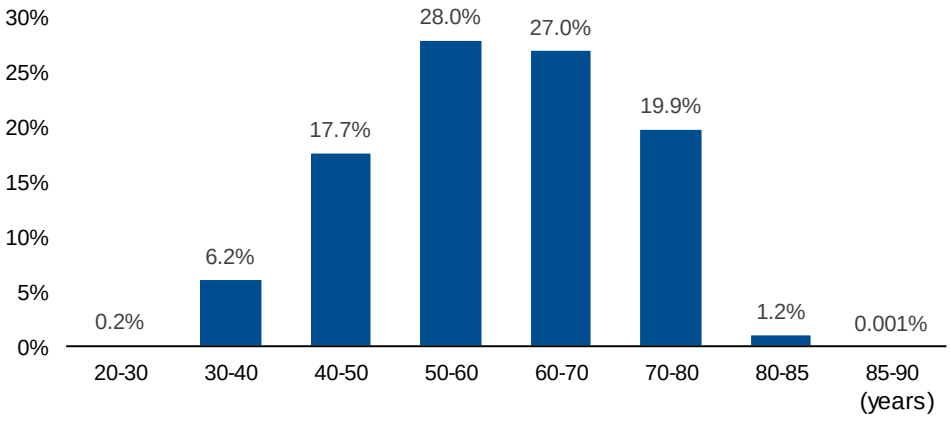
Figure 4: Distribution by loan type, % of outstanding balance



Source: IBL Banca, Scope

The pool is highly granular with the top one and top 10 borrowers accounting for 0.01% and 0.12%, respectively. Borrowers receiving state salaries or pensions comprise 95.4% of the initial portfolio. The two largest paying entities are the Istituto Nazionale della Previdenza Sociale (the national social welfare institution) and the Ragioneria Territoriale Stato (the ministry of finance), with exposures of 41.5% and 17.8%, respectively. Our analysis accounts for this link to the state and the associated risk by incorporating a sovereign stress event.

Figure 5: Distribution by borrower age, % of the outstanding balance



Source: IBL Banca, Scope

3.2.1. Insurance coverage

All underlying loans extended to public and private sector employees are insured against life and employment events, while the loans extended to pensioners are insured only against life events. Insurance coverage on the pool presents an inverse-Herfindahl score of 5.7. Cardif Assurance Vie S.A. is the insurer with the largest exposure covering life events (27.8%), while Hdi Assicurazioni S.p.A. is the insurer with the largest exposure covering employment events (19.1%). We analysed the effect of a deterioration in the insurance companies' credit quality and take comfort in the credit quality of the insurers.

Figure 6: Distribution of insurance companies covering life events, % of the outstanding balance

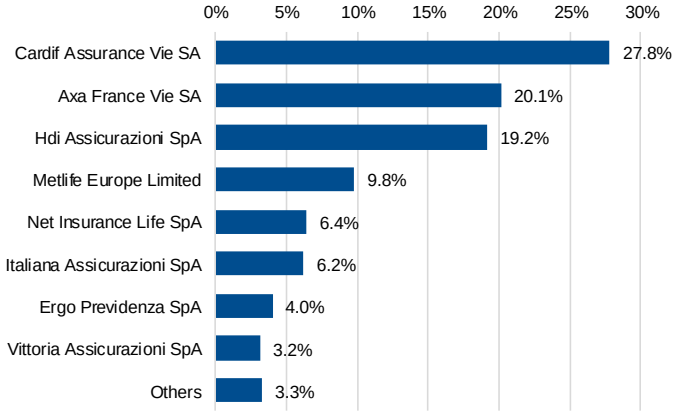
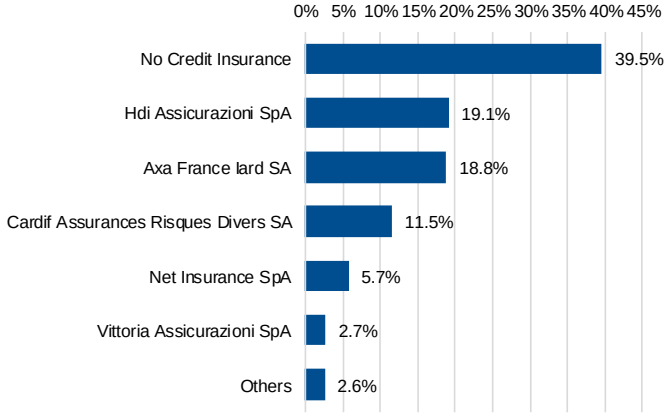


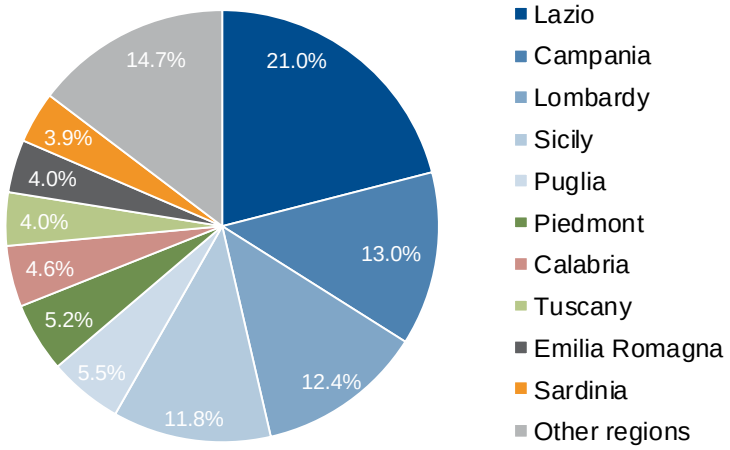
Figure 7: Distribution of insurance companies covering employment events, % of the outstanding balance



Source: IBL Banca, Scope

The portfolio is mainly concentrated in southern (39.5%) and central (32.1%) Italy, which is a common feature for Italian CQS portfolios. Borrowers in northern regions account for 28.4% of the outstanding portfolio.

Figure 8: Distribution by region, % of the outstanding balance



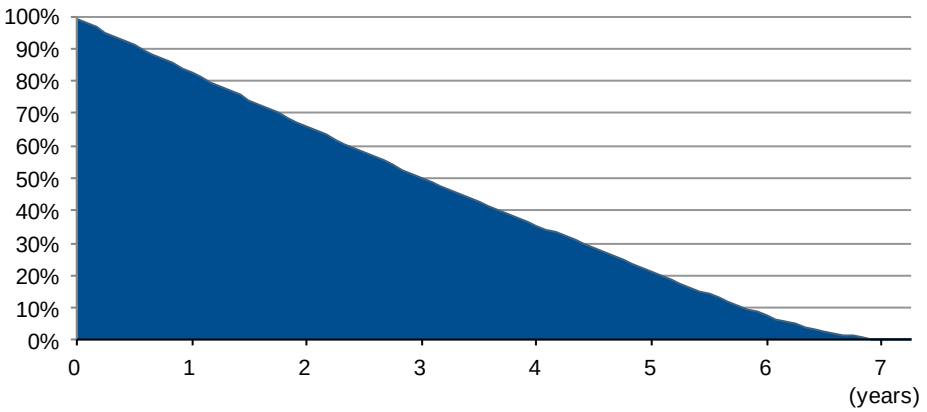
Source: IBL Banca, Scope

3.3. Amortisation profile

Amortisation profile may be extended if payments are suspended

The projected amortisation profile reflects the amortisation scheme of the underlying assets. Figure 9 shows the amortisation of the pool considered in our analysis, assuming a 0% prepayment and default rate.

Figure 9: Projected portfolio amortisation profile



Source: IBL Banca, Scope

3.4. Portfolio assumptions

We derived default rate and recovery rate assumptions based on 2008-19 vintage data for IBL Banca's loan book, representative of the securitised portfolio and segmented by type of default (delinquency, life event, employment event) and employer type (public administration, state administration, private sector and pensioners). These details are shown in Appendix II.

IBL Banca vintage data covers a period of severe recession in Italy

Vintage data includes periods of severe recession in Italy, in 2008-2009 and 2012-2014. Therefore, we did not apply a long-term adjustment to the mean default rate nor to the coefficient of variation derived from the vintage analysis.

Historical data does not reflect sovereign crisis scenarios, which, while rare, could prove highly severe. We incorporated sovereign risk as explained below in section 7.

Figure 10: Portfolio assumptions

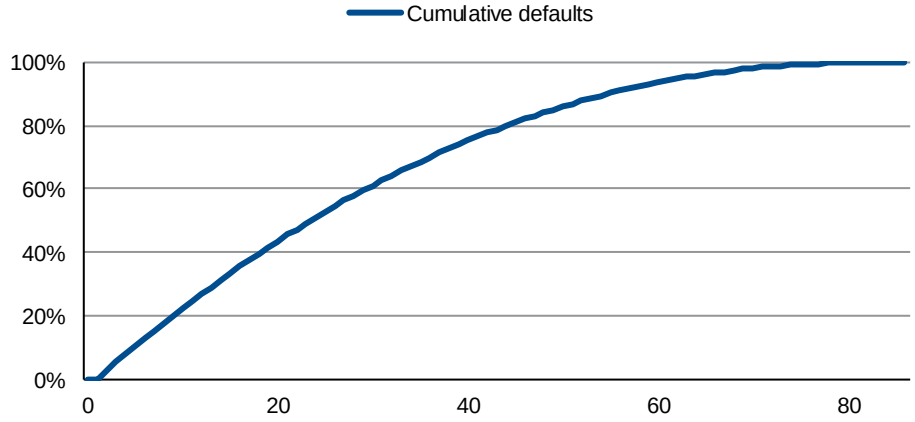
	Portfolio
Mean default rate	5.5%
Coefficient of variation	40.0%
Base case recovery rate	80.0%
AA rating-conditional recovery rate	61.6%
Recovery timing	50% after one year, 20% after two years, 20% after three years and 10% after four years
Low constant prepayment rate	0.0%
High constant prepayment rate	25.0%, for the first year 10.0%, thereafter
Portfolio weighted-average yield	4.4%

3.4.1. Portfolio defaults

We assumed a front-loaded default term structure

We assumed an inverse Gaussian default distribution, with a mean default rate of 5.5% and a coefficient of variation of 40%. In the transaction, a default occurs if either: i) a loan is eight months delinquent; ii) a loan is declared defaulted by the servicer ('in sofferenza'); iii) a life event occurs; or iv) an employment event occurs. In our analysis, we assumed a front-loaded default term structure, with loans starting to default after 1 month. The cumulative default-timing assumptions are shown in Figure 11 and represent the assumed default timing for the pool. Mean default rate and default-timing assumptions also reflect the current seasoning and amortisation of the pool.

Figure 11: Cumulative default-timing assumption



Source: Scope

3.4.2. Loan recovery rate analysis

We calculated rating-conditional recovery rate assumptions by taking the weighted average of two levels of recovery rates: i) 80% recovery rate in a scenario where the insurance company does not default (RR1); and ii) 13.6% recovery rate in the event of insurance default (RR2), after applying a rating-conditional haircut of 32%. The weights applied to RR1 and RR2 reflect the default probability of the pool of insurance companies, assuming a 20% asset correlation between insurers. For the class A notes specifically, we have assumed that the pool of insurance companies will default with a probability of 27.7%.

Figure 12: Rating-conditional recovery rate assumptions

B	BB	BBB	A	AA	AAA
80.0%	76.1%	73.4%	71.2%	61.6%	56.7%

Source: Scope

Further details on how we calculate rating-conditional recovery rates in CQS transactions can be found in the Consumer and Auto ABS Rating Methodology.

We give credit to recoveries from insurance pay-outs and other sources of recoveries

Recoveries stem from a combination of three sources: insurance pay-outs, the pledged TFR amount, and borrower collections. Figure 13 below shows the proportion of IBL Banca's historical recoveries on defaulted loans from these three sources. The 80% RR1 calculation is derived from vintage data, which incorporates all three recovery sources, while the 20% RR2 calculation represents expected recoveries in the absence of insurers and ultimately reflects the borrower's credit quality.

Figure 13: Sources of CQS recoveries (last five years, average)

Insurance	TFR	Borrower
67.0%	7.4%	25.6%

Source: IBL Banca, Scope

Additionally, the recovery vintage data shows that most recoveries are received in the first four years after default. Therefore, the portfolio recovery timing, derived from the corresponding recovery vintage data, was estimated as follows: 50% after one year, 20% after two years, 20% after three years and the remaining 10% after four years.

3.4.3. Constant prepayment rate (CPR)

We expect a spike of the prepayment rate in the first year

We used two CPR scenarios to test the structure's reliance on excess spread: a CPR assumption of 0%, and a CPR assumption of 25% for the first year and 10% thereafter. Given the weighted average seasoning of the portfolio (3.8 years), we expect a sharp increase of the prepayment rate in the first year of the transaction. Historical data show a spike on prepayment rates after 4 years from origination, as borrowers are allowed to refinance their loan once they have reimbursed at least 40% of the initial loan balance.

3.4.4. Excess spread

Excess spread will be available to cure undercollateralisation arising from portfolio defaults. Excess spread will also be trapped under certain trigger conditions (see Figure 14).

Available excess spread will depend on several factors, such as senior fees, the default rate, and the prepayment rate. In our analysis, we assumed a stressed portfolio weighted average yield of 4.4%, calculated assuming that 25% of the loans with the highest yield will either default or prepay first. This resulted in a portfolio yield compression of 1.4% on the 5.8% original weighted average interest rate of the receivables.

Transaction benefits from a 3.1% estimated excess spread

Excess spread is estimated at 3.1% after deducting liability costs and stressed annual fees of 1.0%.

4. Financial structure

4.1. Capital structure

The proceeds from the issuance of the class A notes, together with part of the proceeds from the class J notes, were used to purchase the portfolio of receivables. Class J notes fund a portion of the assets as well as the liquidity reserve and the additional reserve. The structure is fully sequential.

4.2. Priority of payments

Combined priority of payments is the main protection against payment interruption

The structure features a single priority of payments under which principal collections from the assets can be used to cover any interest shortfall on the notes, mitigating the risk of a missed interest payment. Figure 14 below details the transaction's pre-enforcement priority of payments.

If, on any payment date, the cumulative portfolio net default ratio exceeds 3% of the initial outstanding balance, remaining cash will be trapped at item 7 in the simplified pre-enforcement priority of payments (see Figure 14 below). Those funds would then be available in the next payment period to cover any shortfall on items 1-6.

Figure 14: Simplified priority of payments and available funds

Pre-enforcement priority of payments
Available funds Collections and recoveries from receivables, the management fee prepayment amount, the liquidity reserve and the additional reserve
1) Taxes and expenses (ordinary and extraordinary, including servicer fee, even if this has been replaced) 2) Class A interest 3) Replenish the liquidity reserve to the required balance 4) Class A principal up to the target redemption amount 5) Replenish the additional reserve to the required balance 6) Adjustment of purchase price and indemnity due and payable to the originator 7) Cash trapping (if the cash trapping condition is satisfied) 8) Remuneration on class J 9) Class J principal (if class A is redeemed in full) up to the target redemption amount 10) Additional remuneration on class J

Source: Transaction documents and Scope

4.3. Liquidity reserve and additional reserve

Fully funded reserves provide 2.3% of credit enhancement

The liquidity reserve and additional reserve were fully funded at closing with part of the proceeds from the issuance of the class J notes.

4.3.1. Liquidity reserve

At closing, the liquidity reserve was equal to 1% of the initial balance of the class A (EUR 5.7m).

During the life of the transaction, if class A is above 50% of the initial balance, the reserve will be equal to 1% of the class A initial balance, otherwise it will be the higher between 2% of the principal outstanding of the class A and 0.5% of the initial balance of the class A.

The liquidity reserve will provide liquidity protection to the class A notes during the life of the transaction and can be used to repay the notes' principal at maturity.

4.3.2. Additional reserve

At closing, the additional reserve is equal to 1.5% of the initial pool balance (EUR 9.1m).

During the life of the transaction, it will amortise up to the higher of 1.5% of the current pool balance or 0.75% of the initial pool balance. The additional reserve will provide liquidity and credit protection to the class A notes.

The aggregate amounts of the liquidity reserve and the additional reserve can cover costs and interest on the class A notes for around 23 monthly payment dates.

4.4. Management fee reserve

In the case of a loan prepayment, the borrower can set off management fees paid upfront but not yet due, resulting in a reduction of outstanding instalments.

Limited exposure to management fee set-off

A dedicated reserve, the management fee reserve, was funded at closing, to cover this set-off risk. At each payment date, the target management fee reserve will be equal to 25% of the outstanding management fees exposure (EUR 1.6m at closing). The repayment to the originator of the amortised portion of the management fee reserve will be made at each payment date, outside the priority of payments.

In addition, if the reserve is not enough to cover the amounts which borrowers set off, the originator will cover the shortfall.

4.5. Amortisation and provisioning

The strict sequential amortisation effectively protects senior noteholders in times of stress. The cash-trapping mechanism accelerates class A amortisation during stressed periods.

The transaction structure benefits from an implicit principal-deficiency ledger mechanism, since the notes amortise up to a target redemption amount. The target redemption amount is defined, on each payment date, as the difference between the notes' outstanding amount and the outstanding performing collateral portfolio (reduced by the amounts of the liquidity and additional reserves). As a consequence, the excess spread will be used to cover defaults rather than being distributed as additional remuneration to junior noteholders.

We believe that the cash-trapping mechanism (item 7 in the simplified pre-enforcement waterfall above) provides limited support in high-default scenarios, as excess cash will already have been used up by higher-ranking items in the priority of payments.

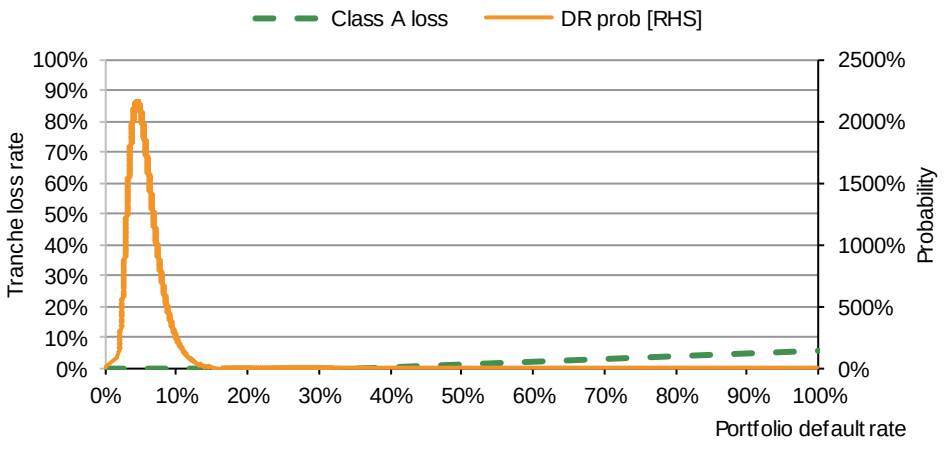
5. Quantitative analysis

We used a bespoke cash flow analysis

Our cash flow analysis considered the portfolio's characteristics and the transaction's main structural features. We applied our large homogenous portfolio approximation approach when analysing the granular collateral pool and projecting cash flows over its amortisation period. The cash flow analysis considers an inverse Gaussian default distribution to calculate the expected loss and the expected weighted average life of each rated tranche.

Figure 15 shows the losses of the rated notes at all portfolio default rates. The chart shows how credit enhancement, recovery proceeds, and excess spread protect the notes in the event of default. The results in Figure 15 consider a 0.75% reduction in the portfolio balance to account for commingling risk.

Figure 15: Cash flow results for base case mean default rate, coefficient of variation and rating-conditional recovery rate



Source: Scope
Note: The probabilities displayed on the right-hand side axis must be considered in the context of the calculation of the probability density

6. Rating sensitivity

We tested the resilience of the rating against deviations in the main input parameters: the portfolio mean default rate and the portfolio recovery rate. This analysis has the sole purpose of illustrating the sensitivity of the rating to input assumptions and is not indicative of expected or likely scenarios.

The following shows how the results for the rated instrument (class A notes, rated AA+$_{SF}$) change compared to the assigned rating when the portfolio's expected mean default rate is increased by 50% or the portfolio's expected recovery rate is reduced by 50%, respectively: sensitivity to default rate, zero notches; sensitivity to recovery rate, three notches.

7. Sovereign risk

Sovereign risk does not limit the transaction's ratings

CQS obligors are less likely to meet loan instalments if their salary or pensions are not paid. The obligor employer's credit quality is therefore a major source of credit risk. Around 95.4% of the portfolio relates to the public sector, exposing the transaction to sovereign risk as these borrowers' salaries or pensions may be affected should the sovereign default. A sovereign default could also trigger a significant restructuring of the public administration. Rather than mechanistically limiting the maximum ratings on the notes, we assess the potential rating impact of a distressed scenario affecting the Italian government.

Given the relevance of the exposure to public employees and pensioners, Scope's analysis quantified the impact of Italian sovereign risk by assessing the likelihood and severity of a distress scenario (CQS stress scenario) affecting the government of Italy. A CQS stress scenario would entail a significant increase in portfolio defaults and delinquencies compared to the agency's base case assumption. This approach allows us to reflect the benefits of each transaction's liability structure and discriminate between them, rather than applying a mechanistic cap to the assigned ratings based on Italy's sovereign rating.

Our analysis assumed the likelihood of a CQS stress scenario event to be equivalent to an A risk, i.e. two notches higher than Scope's current rating on Italy. This scenario captures the potential effect on the transaction of a government default on its public debt. The probability assigned to this scenario reflects our view that a sovereign default would not necessarily trigger the permanent suspension of payments to the entire population of civil servants or pensioners in Italy, or a general dismissal of civil servants, because the state needs to maintain a minimum level of key operations. For more insight into our fundamental analysis of the Italian economy, refer to our press release on the Republic of Italy, dated 17 June 2019.

We considered the following risks under the sovereign CQS stress:

1. **Liquidity risk.** A suspension or reduction of salary and pension payments may create a spike in arrears and thus a liquidity shortfall for the transaction. However, additional losses are generally not incurred because the loan's maturity is extended in this instance – unpaid instalments become due and payable as of the original loan's maturity date until the debt is fully extinguished[4]. When analysing the transaction, we assumed that 50% of the public sector portfolio was fully suspended (i.e. no interest or principal was paid on these loans) for two years.
2. **Credit risk**. A restructuring of the public administration may lead to job losses and, therefore, asset defaults for the securitisation. However, only some parts of the public administration may be affected, as vital functions such as tax collection and law enforcement would not be completely abolished. When analysing the transaction, we assumed that 25% of the public sector portfolio would default as a consequence of job losses.

[4] If the maturity of the loans is extended beyond the final maturity of the notes, suspensions or reductions of salary and pension payments will effectively generate a loss for the transaction. The final legal maturity date is set 15 years after the loan with the longest maturity date in order to mitigate this risk.

8. Counterparty risk

The transaction is exposed to counterparty risk from: i) IBL Banca, as originator, servicer, cash manager and calculation agent; ii) Zenith, as back-up servicer and back-up calculation agent; and iii) Citibank N.A., Milan Branch, as transaction account bank and paying agent.

Counterparty risk for the transaction supports the highest ratings. We do not consider any of the counterparty exposures to be excessive, i.e. if counterparty risk crystallises, a downgrade is still limited to six notches.

8.1. Operational risk from servicer

Back-up servicer appointed since closing

Operational risk from the servicer is well mitigated in this transaction. Zenith, back-up servicer since closing, has undertaken to become operational within 30 days in the event of a termination event for IBL Banca.

8.2. Commingling risk from account bank

The issuer has a collection account held at IBL Banca that receives all asset proceeds as well as a payment account held by Citibank N.A., Milan Branch. Two business days before each monthly payment date, the amounts in the collection account are transferred to Citibank.

Commingling risk driven by employers' responsiveness to new payment instructions

Commingling risk is mitigated by: i) daily sweeps to the issuer's collection account held with the servicer and monthly sweeps to the issuer's payment account held with Citibank N.A., Milan Branch; and ii) instructions to debtors to pay directly into the issuer's account at the transaction account bank upon a servicer disruption event. However, employers may not immediately implement the new payment instructions, and we have therefore assumed a loss of up to four months of collections. We sized a 0.75% loss based on the probability of a commingling event over the expected life of the transaction. However, the BBB rating on IBL implies that the servicer's insolvency is unlikely.

8.3. Set-off risk from originator

We believe set-off risk from the originator is well mitigated

Set-off risk is well mitigated in this transaction. The originator is a deposit-taking financial institution, but it has represented that, as of closing, none of the borrowers has a deposit account with IBL Banca.

9. Legal structure

9.1. Legal framework

This securitisation is governed by Italian law and represents the true sale of assets to a bankruptcy-remote vehicle, which is essentially governed by the terms in the transaction documentation.

9.2. Clawback

Clawback risk is mitigated

The originator has provided: i) a 'good standing' certificate from the Chamber of Commerce; ii) a solvency certificate signed by a representative duly authorised; and iii) a certificate from the bankruptcy court (tribunale civile – sezione fallimentare) confirming that the originator is not subject to any insolvency or similar proceedings.

This mitigates claw-back risk, as the issuer can prove it was unaware of the issuer's insolvency as of the transfer date.

Assignments of receivables made under the Italian Securitisation Law are subject to claw-back in the following events:

i) pursuant to article 67, paragraph 1, of the Italian Bankruptcy Law, if the bankruptcy declaration of the relevant originator is made within six months from the purchase of the relevant portfolio of receivables, provided the receivables' sale price exceeds their value

by more than 25% and the issuer cannot demonstrate it was unaware of the originator's insolvency, or

ii) pursuant to article 67, paragraph 2, of the Italian Bankruptcy Law, if the adjudication of bankruptcy of the relevant originator is made within three months from the purchase of the relevant portfolio of receivables, provided the receivables' sale price does not exceed their value by more than 25% and the originator's insolvency receiver can demonstrate that the issuer was aware of the originator's insolvency.

Clawback risk related to repurchased receivables is mitigated by a maximum amount of 5% of the portfolio on a cumulative basis. Upon the repurchase of single loans, the originator is also required to provide a solvency certificate to the issuer. However, in our view an insolvency of IBL (rated BBB) is unlikely.

9.3. Use of legal opinion

We reviewed the legal opinions produced for the issuer. These provide comfort on the issuer's legal structure and supports our general legal analytical assumptions.

10. Monitoring

We will monitor this transaction on the basis of the performance reports from the servicer and the calculation agent, as well as other available information. The ratings will be monitored on an ongoing basis.

Scope analysts are available to discuss all the details surrounding the rating analysis

Scope analysts are available to discuss all the details surrounding the rating analysis, the risks to which this transaction is exposed and the ongoing monitoring of the transaction.

11. Applied methodology and data adequacy

For the analysis of this transaction we applied Scope's Consumer and Auto ABS Rating Methodology and Methodology for Counterparty Risk in Structured Finance, all available on our website, www.scoperatings.com.

IBL Banca provided Scope with default and recovery data, segmented by quarterly vintage of origination, by type of default (delinquency, life event, employment event) and employer type (public administration, state administration, private sector and pensioners). The default rate data covers a period from 2008 to 2019 and is generally very granular. The recovery data also covers a period from 2008 to 2019, referring to all recoveries during that period. We also received data regarding the proportion of recoveries from different sources: insurance payments, recoveries from borrowers and recoveries from the pledged TFR.

I. Deal comparison

Transaction	Marzio Finance 6-2019	Marzio Finance 5-2019	Marzio Finance 4-2018	Marzio Finance 3-2018	Marzio Finance 2-2018	Marzio Finance 1-2017	Dyret
Country	Italy	Italy	Italy	Italy	Italy	Italy	Italy
Closing date (dd/mm/yyyy)	31/07/2019	05/04/2019	21/11/2018	28/05/2018	29/01/2018	28/09/2017	09/03/2018
Originator	IBL Banca S.p.A.	IBL Banca S.p.A.	IBL Banca S.p.A.	IBL Banca S.p.A.	IBL Banca S.p.A.	IBL Banca S.p.A.	Dynamica Retail S.p.A.
Servicer	IBL Banca S.p.A.	IBL Banca S.p.A.	IBL Servicing S.p.A.	IBL Banca S.p.A.	IBL Banca S.p.A.	IBL Banca S.p.A.	Dynamica Retail S.p.A
Back-up servicer	Zenith Service S.p.A.	Zenith Service S.p.A.	Zenith Service S.p.A.	Zenith Service S.p.A.	Zenith Service S.p.A.	Zenith Service S.p.A.	Zenith Service S.p.A.
Back-up servicer facilitator	-	-	-	-	-	-	Zenith Service S.p.A.
Portfolio characteristics							
Number of loans	44,960	14,268	19,397	22,952	13,145	19,884	8,392
Number of borrowers	42,492	13,842	18,687				8,392
Original portfolio balance (€)	982,255,231	287,877,728	389,163,840	487,141,290	334,298,977	429,475,538	194,603,643
Outstanding portfolio balance (€)	604,353,726	280,470,224	376,770,538	437,201,060	157,872,473	361,374,376	160,348,393
Average original loan balance (€)	21,847	20,176	20,063	21,224	25,432	21,599	23,189
Average outstanding loan balance (€)	13,452	19,657	19,424	19,048	12,010	18,174	19,107
Length of contracts							
WA original term (years)	9.8	9.3	9.2	9.3	9.7	9.4	9.6
WA seasoning (years)	3.8	0.2	0.3	1.0	4.4	1.6	1.8
WA remaining term (years)	6.0	9.1	8.9	8.3	5.3	7.8	7.8
Contract type							
CDQ - Cessione del quinto (%)	83.8%	82.7%	82.3%	83.4%	77.7%	83.3%	81.4%
DP - Delegazione di pagamento (%)	16.2%	17.3%	17.7%	16.6%	22.3%	16.7%	18.6%
Portfolio yield							
WA portfolio yield (%)	5.8%	5.9%	6.2%	6.0%	6.4%	5.9%	4.0%
Type of debtors							
Public sector employees (%)	39.2%	37.62%	36.6%	41.2%	39.1%	38.8%	54.8%
State employees (%)	13.8%	12.00%	12.8%	13.5%	16.7%	15.3%	-
Private sector employees (%)	4.6%	15.84%	13.7%	8.7%	2.8%	6.8%	9.9%
Pensioners (%)	42.3%	34.54%	36.9%	36.6%	41.4%	39.1%	35.3%
Borrower concentration							
Top 1 (%)	0.01%	0.04%	0.03%	0.02%	0.04%	0.03%	-
Top 10 (%)	0.12%	0.35%	0.23%	0.19%	0.30%	0.21%	-
Employer concentration							
Top 1 (%)	3.1%*	2.4%*	1.4%*	2.0%*	2.0%*	2.0%*	34.3%
Top 10 (%)	8.8%*	6.7%*	4.7%*	10.9%*	7.2%*	6.5%*	54.7%
Public sector exposure (%)	95.4%	84.2%	86.3%	91.3%	97.2%	93.2%	90.1%
Employer regional concentration							
North	28.4%	29.4%	30.2%	29.1%	27.9%	25.7%	16.4%
Centre	32.1%	30.6%	28.4%	28.9%	31.3%	31.0%	21.8%
South	39.5%	40.1%	41.4%	42.0%	40.8%	43.3%	61.8%
Top region	Lazio - 21.0%	Lazio - 21.2%	Lazio - 18.9%	Lazio - 19.4%	Lazio - 21.5%	Lazio - 20.4%	Campania - 27.3%
Insurance company exposure							
Top 1 life insurance	27.8%	28.5%	27.0%	24.8%	25.2%	21.8%	21.8%
Top 2 life insurance	47.9%	46.7%	45.1%	43.6%	47.2%	43.1%	42.0%
Top 3 life insurance	67.1%	61.6%	61.7%	58.9%	66.2%	59.4%	58.6%
Top 1 unemployment insurance	19.1%	14.5%	16.5%	18.4%	25.2%	20.5%	21.8%
Top 2 unemployment insurance	37.9%	28.7%	28.5%	33.6%	44.6%	36.8%	42.0%
Top 3 unemployment insurance	49.4%	40.8%	39.9%	46.4%	54.0%	48.1%	58.6%
Assumptions summary							
Default definition	1 month	8 months	8 months	8 months	8 months	8 months	9 months
Mean default	5.5%	7.5%	7.5%	7.0%	5.0%	6.0%	10.5%
Coefficient of variation	40%	40%	40%	40%	45%	45%	35.0%
Recovery rate (insurance coverage)	80.0%	80.0%	80.0%	80.0%	80.0%	80.0%	80.0%
Recovery rate (no insurance coverage)	20.0%	20.0%	20.0%	20.0%	20.0%	20.0%	20.0%
AAA scenario recovery rate	56.7%	48.7%	52.8%	54.4%	30.2%	55.6%	42.9%
Recovery timing	4 years - (50% + 20% + 20% + 10%)	4 years - (50% + 20% + 20% + 10%)	4 years - (50% + 20% + 20% + 10%)	4 years - (50% + 20% + 20% + 10%)	4 years - (50% + 20% + 20% + 10%)	4 years - (50% + 20% + 20% + 10%)	4 years - (50% + 20% + 20% + 10%)
Prepayment rate	25% in year 1 10% thereafter	5% from year 1 to year 3 10% thereafter	5% from year 1 to year 3 10% thereafter	5% from year 1 to year 3 10% thereafter	5% from year 1 to year 3 10% thereafter	5% from year 1 to year 3 10% thereafter	5% from year 1 to year 3 10% thereafter
Portfolio yield	4.4%	5.1%	5.3%	5.2%	5.8%	5.1%	3.8%
Insurers' inverse-Herfindahl metric	5.7	5.8	6.0	5.7	4.3	5.1	5.9
Insurers' correlation	20%	20%	20%	20%	20%	20%	20.0%
Public sector exposure (%)	95.4%	84.2%	86.3%	91.3%	97.2%	93.2%	85.0%
Private sector exposure (%)	4.6%	15.8%	13.7%	8.7%	2.8%	6.8%	15.0%
Structural features							
Tranching							
Class A	AA+	AAA	AAA	AAA	AAA	AAA	NR
CE Class A	8.0%	11.5%	21.0%	14.0%	18.0%	9.0%	20.5%
Class B	N/A	N/A	A+	N/A	N/A	N/A	BBB+
CE Class B	N/A	N/A	7.0%	N/A	N/A	N/A	10.3%
Class C	N/A	N/A	N/A	N/A	N/A	N/A	BB
CE Class C	N/A	N/A	N/A	N/A	N/A	N/A	4.7%
Class J	NR	NR	NR	NR	NR	NR	NR
CE Class J	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Cash reserve (% of rated notes)	2.6%	2.7%	2.6%	2.9%	3.3%	1.8%	2.0%
Revolving period (years)	0	0	0	0	0	0	0.75
Commingling risk (yes/no)	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Commingling risk mitigants	- Daily sweeps - Notification to borrowers to redirect payments into the issuer account upon servicer disruption	- Daily sweeps - Notification to borrowers to redirect payments into the issuer account upon servicer disruption	- Daily sweeps - Notification to borrowers to redirect payments into the issuer account upon servicer disruption	- Daily sweeps - Notification to borrowers to redirect payments into the issuer account upon servicer disruption	- Daily sweeps - Notification to borrowers to redirect payments into the issuer account upon servicer disruption	- Daily sweeps - Notification to borrowers to redirect payments into the issuer account upon servicer disruption	Daily sweeps
Set-off risk (yes/no)	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Set-off risk mitigants (e.g., prepayment reserve)	Prepayment reserve	Prepayment reserve	Prepayment reserve	Prepayment reserve	Prepayment reserve	Prepayment reserve	Prepayment reserve - 1.3% of balance of each loan
Type of swap	N/A	N/A	Fixed-to-floating IRS	Fixed-to-floating IRS	N/A	N/A	N/A
Swap co. rating trigger	N/A	N/A	A-	A-	N/A	N/A	N/A

*INPS (Istituto Nazionale della Previdenza) and Italian Ministry of Finance are excluded from this figure.

II. Vintage data provided by originator

IBL Banca provided default and recovery performance data for the pool. We used this information in our analysis as a foundation for the calibration of point-in-time default rates, the coefficient of variation and base case recovery rates.

Vintage data is granular and representative of the portfolio.

Figure 16: Public administration – default and recovery data

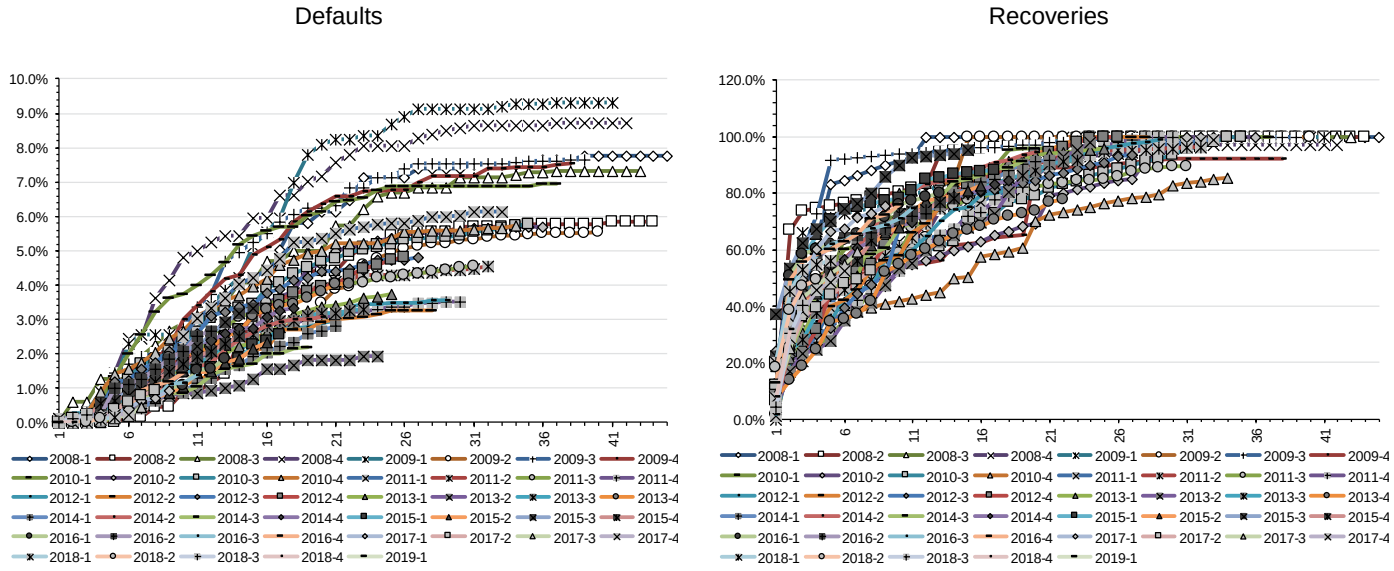


Figure 17: State administration – default and recovery data

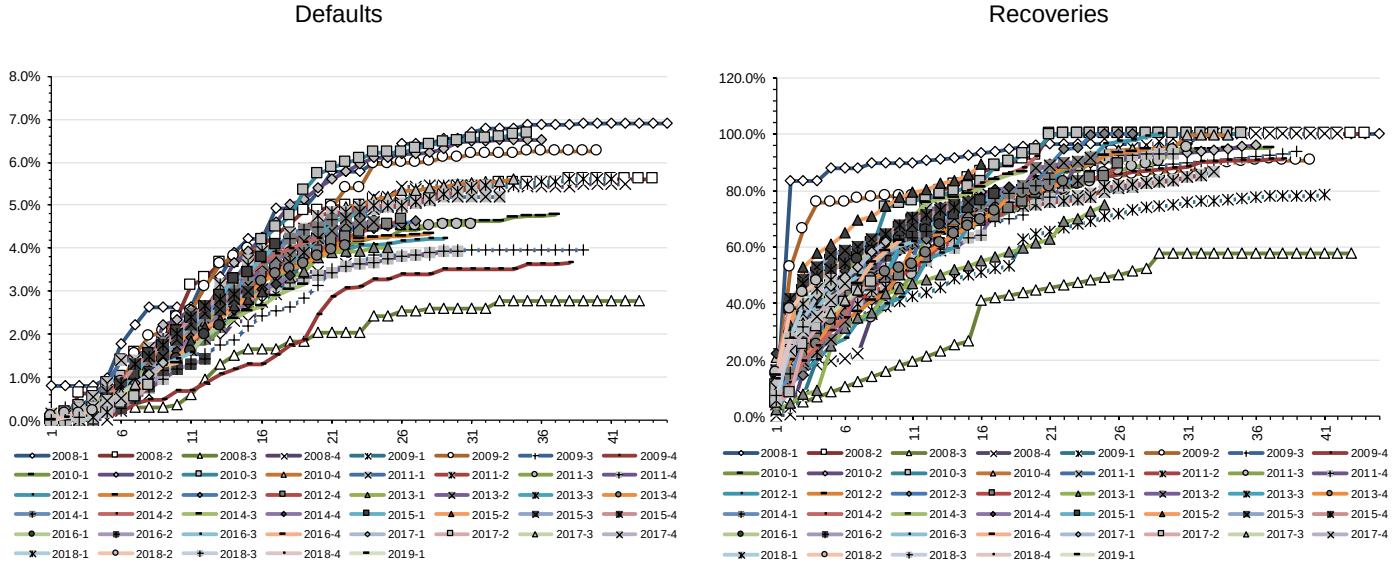
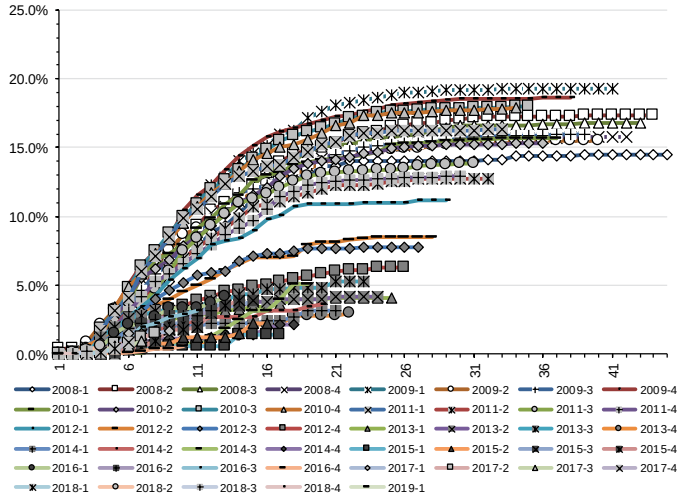


Figure 18: Private sector – default and recovery data

Defaults



Recoveries

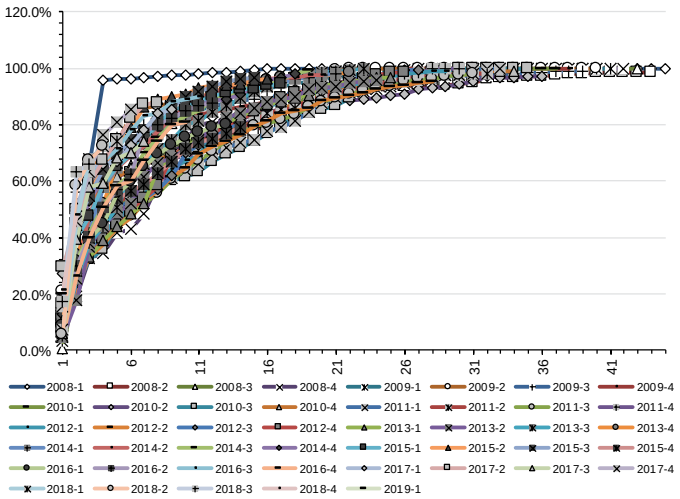
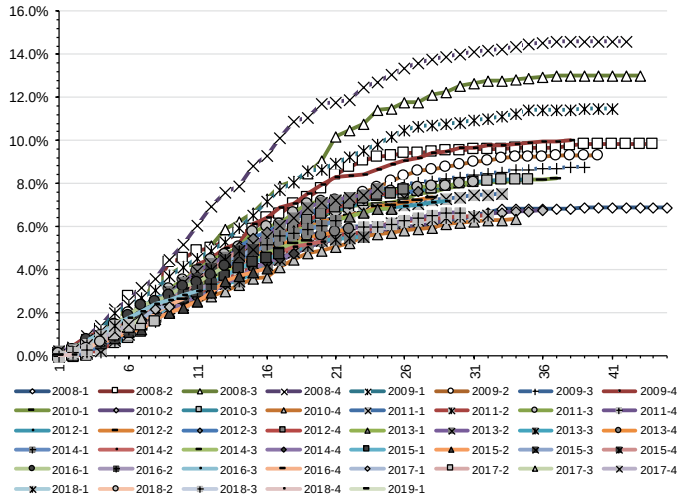
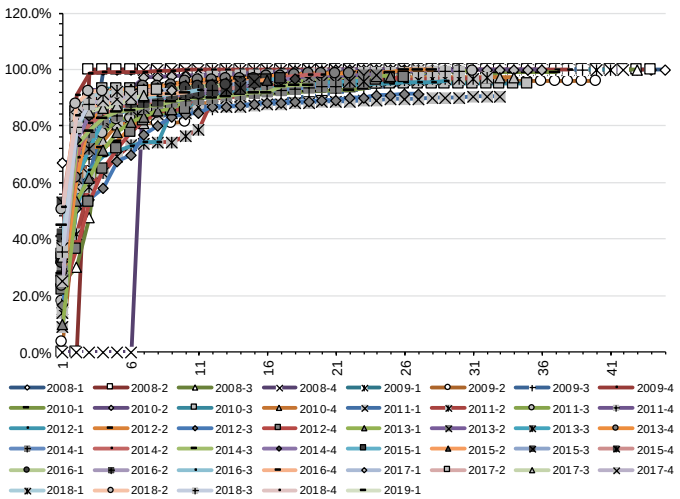


Figure 19: Pensioners – default and recovery data

Defaults



Recoveries



Scope Ratings GmbH

Headquarters Berlin
Lennéstraße 5
D-10785 Berlin

Phone +49 30 27891 0

Frankfurt am Main
Neue Mainzer Straße 66-68
D-60311 Frankfurt am Main

Phone +49 69 66 77 389-0

Paris
1 Cour du Havre
F-75008 Paris

Phone +33 1 8288 5557

London
Suite 301
2 Angel Square
UK-London EC1V 1NY

Phone +44 20 3457 0444

Madrid
Paseo de la Castellana 95
Edificio Torre Europa
E-28046 Madrid

Phone +34 914 186 973

Milan
Via Paleocapa 7
IT-20121 Milan

Phone +39 02 30315 814

Oslo
Haakon VII's gate 6
N-0161 Oslo

Phone +47 21 62 31 42

info@scoperatings.com
www.scoperatings.com

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