Marzio Finance S.r.l. – Series 4-2018

Italian Consumer CQS ABS

Ratings

Series	Rating	Notional (EUR m)	Notional (% assets)	CE[1] (% assets)	Coupon	Final maturity
Class A	AAA_{SF}	305.9	79.0	21.0	1mE + 0.65%	August 2043
Class B	$A+_{SF}$	54.2	14.0	7.0	1.0%	August 2043
Class J	NR	27.1[2]	7.0	0.0	Variable	August 2043
Rated notes		387.2				

Scope's analysis is based on the portfolio dated 30 September 2018 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 website for the SF Rating Definitions.

Transaction details

Purpose	Liquidity/funding
Issuer	Marzio Finance S.r.l.
Originator/sub-servicer	IBL – Istituto Bancario del Lavoro S.p.A. (IBL Banca or IBL)
Servicer	IBL Servicing S.p.A. (IBL Servicing)
Back-up servicer	Zenith Service S.p.A.
Account bank	Citibank N.A., Milan Branch
Swap counterparty	Credit Agricole Corporate and Investment Bank
Closing date	21 November 2018
Payment frequency	Monthly, 28th day of each month

The transaction (Series 4-2018) is IBL Banca's fourth 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 376.7m portfolio of CQS loans comprised of 'cessione del quinto' (82.3%) and 'delegazione di pagamento' (17.7%) loans extended to public administration (36.6%), central state administration (12.8%) and private sector employees (13.7%) as well as pensioners (36.9%). The portfolio is highly granular and around 98.7% of the loans were originated in 2018. All the underlying loans are insured against life and employment events. Regional concentration is as follows: north (30.2%), centre (28.4%) and south (41.4%).

Rating rationale (summary)

The ratings reflect: 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 (through its subsidiary IBL Servicing S.p.A.), 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. (Citibank) as transaction bank and paying agent, and to Credit Agricole Corporate and Investment Bank as swap counterparty.

The ratings are mainly driven by the securitised portfolio's characteristics and its expected performance, and by the relatively diversified pool of insurance companies covering life or employment events. The ratings also incorporate our positive assessment of the servicer's abilities and incentives. We considered Italian sovereign risk by

[1] Including a EUR 3.6m liquidity reserve and a EUR 5.6m additional reserve.
[2] Class J funds a portion of the portfolio (EUR 17.9m) 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.

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Related Research

General Structured Finance Rating Methodology

Consumer ABS Rating Methodology

Methodology for Counterparty Risk in Structured Finance

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assessing the impact on the ratings of a distress scenario affecting the government of Italy and the associated loss severity for the securitised assets.

Series 4-2018 class A and class B are supported by 21% and 7% of credit enhancement, respectively. Class A notes benefit from the structural protection provided by sequential principal amortisation and from credit protection via a fully funded cash reserve. A dedicated reserve provides liquidity protection to the class A and B notes. However, if cumulative net defaults exceed 3%, class B interest will be subordinated to the full repayment of the class A notes. As a result, the rating of the class B notes reflects strong credit quality in terms of expected loss, but is constrained by the default risk of the tranche.

IBL Banca performs several key roles, including that of originator, servicer (through its subsidiary IBL Servicing S.p.A.), 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 an above-average loans book performance track record.

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.

Diverse insurance coverage: The portfolio benefits from a well-diversified pool of over 10 insurance companies covering individual borrowers against life events and unemployment.

Liquidity and credit protection: A fully funded liquidity reserve will provide liquidity protection to the class A and B notes (for the latter only as long as the cumulative net default ratio does not exceed 3%) during the life of the transaction. An additional reserve will provide liquidity protection to the rated notes and ongoing credit protection to the class A notes. Both reserves will be available to repay the notes at maturity.

Interest rate swap: The class A notes pay one-month Euribor plus a margin, while the portfolio pays a fixed rate. To hedge interest rate risk, the issuer has entered into a fix-floating interest rate swap with Credit Agricole Corporate and Investment Bank.

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

Negative rating drivers and mitigants

Exposure to public entities: A large portion of the portfolio is exposed to the public entities that pay salaries or pensions to borrowers (86.3%). 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.

Loan up-front commissions set-off risk: Borrowers can claim back a portion of the fees and commissions paid up front if they prepay their loan. A dedicated reserve, equal to 25% of the total exposure, mitigates set-off risk. In addition, exposure at closing is relatively small, equal to EUR 20,710 of the total portfolio.

Commingling risk: Commingling risk is mitigated by: i) a daily sweep of collections to the issuer's account held at IBL, and subsequently to the issuer's account held at Citibank, two business days before each monthly payment date; and ii) instructions to borrowers to redirect payments to the issuer's account in the event of 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

Better-than-expected performance of the pool may positively impact the ratings.

A rating upgrade of Italy or a reduction of the insurance companies' default risk could also lead to an upgrade.

Downside rating-change drivers

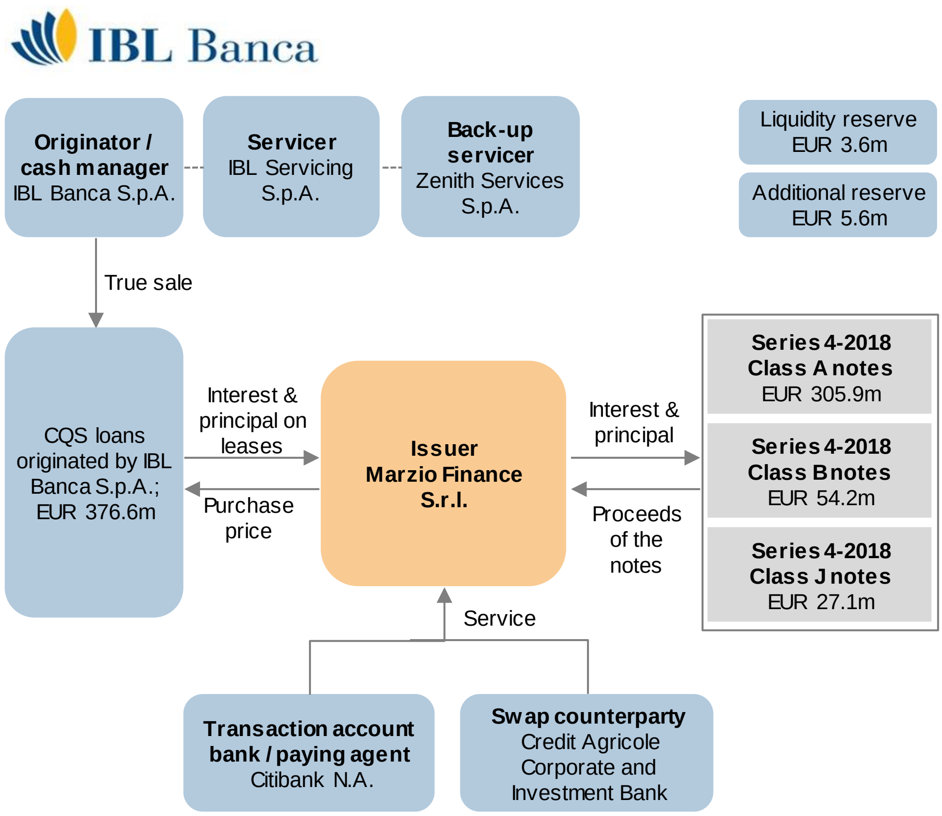
A significant deterioration in the credit profile of the insurance companies leading to lower rating-conditional recovery rate assumptions could negatively impact the ratings.

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 ratings.

Table of contents

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 4-2018 is IBL Banca's fourth 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 4-2018) is the fourth true-sale securitisation under the programme. It is backed by a EUR 376.7m 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-2017, 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 saving and insurance products, and payment cards.

IBL's distribution model comprises 50 branches, plus further branches via distribution agreements with nine banking partners. The bank also has a broker network of 81 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 firepower to transition to a more balance sheet-intensive model, reaching an asset size of around EUR 4.2m at end-2017.

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 receipt of insurance coverage and acceptance of the payment delegation by the employer or pension provider.

2.2. Servicing and recovery

IBL Servicing, a 100% owned subsidiary of IBL Banca, is servicer for the transaction, with IBL Banca acting as sub-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 payed 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 the borrower and the employer within 90 days via phone and email to solicit the payment. 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 other 90 days. After 180 days, a written notice is sent to the borrower and to 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 either in the public or the 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

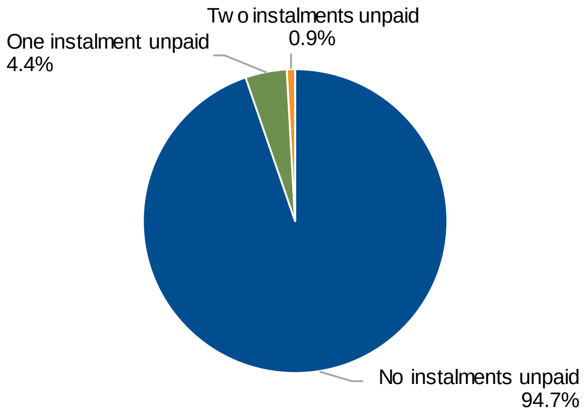
DP loans are typically granted to borrowers that already have an outstanding CDQ loan. The addition of a DP loan can mean a total monthly instalment of up to 50% of the borrower's net income. DP loans are subordinated to CDQ loans, but this risk is partly mitigated by the originator's familiarity with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

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

3.2. Securitised assets

The EUR 376.7m portfolio as of 30 September 2018 is comprised of CDQ (82.3%) and DP (17.7%) loans extended to public administration (36.6%), central state administration (12.8%), and private sector employees (13.7%) as well as pensioners (36.9%). Compared with IBL Banca's total loan book, the portfolio benefits from a 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



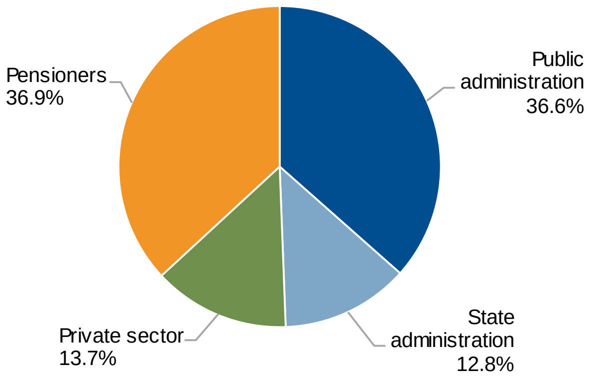
Source: IBL Banca, Scope

Portfolio seasoning is low

The current loan portfolio has around four months of weighted average seasoning and a weighted average remaining term to maturity of 8.9 years. The loans in the portfolio were originated between 2009 and 2018, with 98.7% originated in 2018. Loans transferred to the portfolio have at least one instalment paid and 99.5% of the portfolio matures around 10 years after the transaction closes. The extension of the maturity date is possible 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.

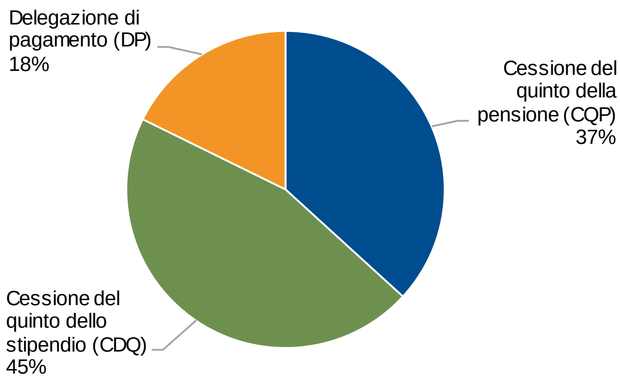
All the loans in the pool are amortising and pay monthly instalments at a weighted average fixed interest rate of 6.2%. Eligibility criteria exclude loans that have an interest rate below 3.5%.

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



Source: IBL Banca, Scope

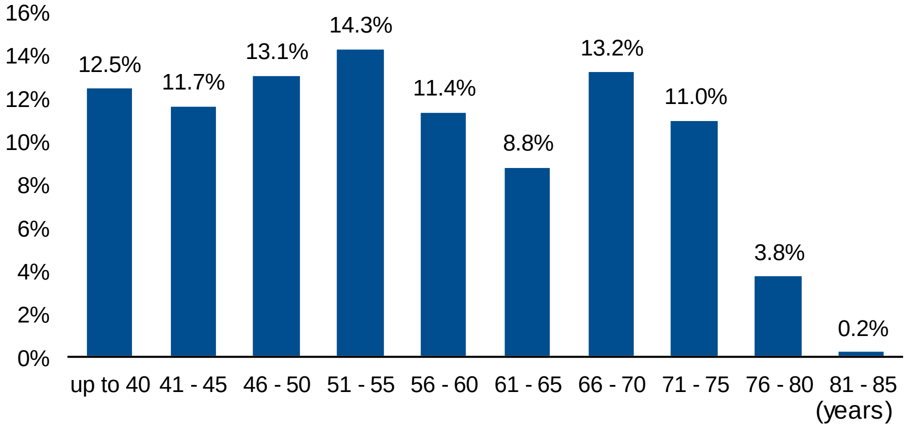
Figure 4: Distribution by loan type, % of outstanding balance



Source: IBL Banca, Scope

The pool is highly granular with top 1 and top 10 borrowers accounting for 0.03% and 0.23%, respectively. Borrowers receiving state salaries or pensions comprise 86.3% 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 35.8% and 15.3%, respectively. Our analysis accounts for this link to the state and the associated risk by incorporating a sovereign stress event. With respect to the private sector only, the top 1 and top 10 employers account for 1.0% and 7.1% of total private sector exposure, respectively.

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



Source: IBL Banca, Scope

3.2.1. Insurance coverage

Well diversified pool of insurance companies

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 is well diversified, with an inverse-Herfindahl score of 6.0. Aviva Life S.p.A. is the insurer with the largest exposure covering against life events (27.0%), while Generali Italia S.p.A. is the insurer with the largest exposure covering against employment events (16.5%). We analysed the effect of a deterioration in the insurance companies' credit quality and take comfort in the credit quality and diversity of the insurers.

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

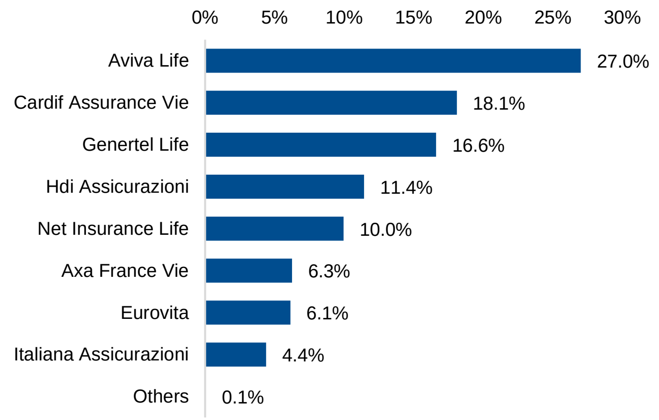
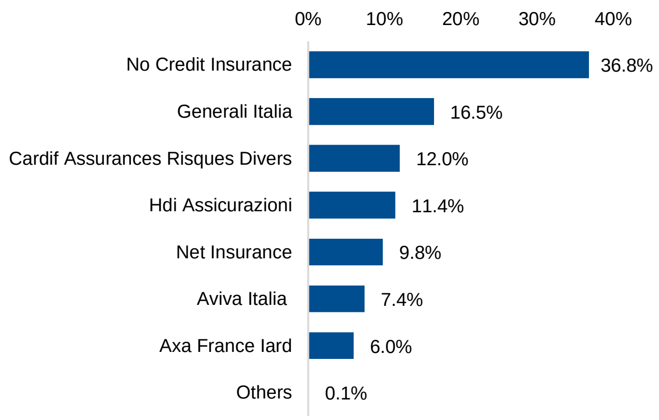


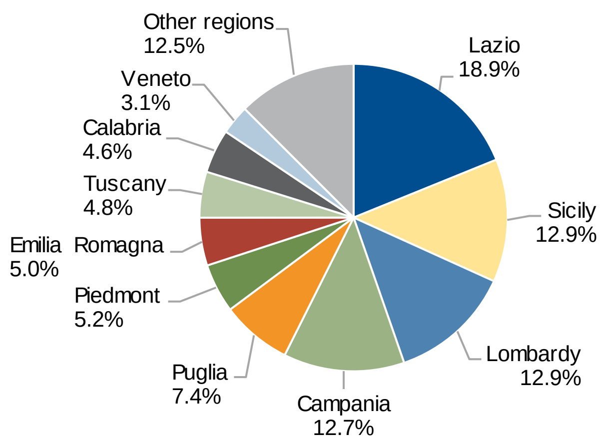
Figure 7: Distribution of insurance companies covering employment events, % of the outstanding balance



Source: IBL Banca, Scope

The portfolio is mainly concentrated in southern (41.4%) and central (30.2%) 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



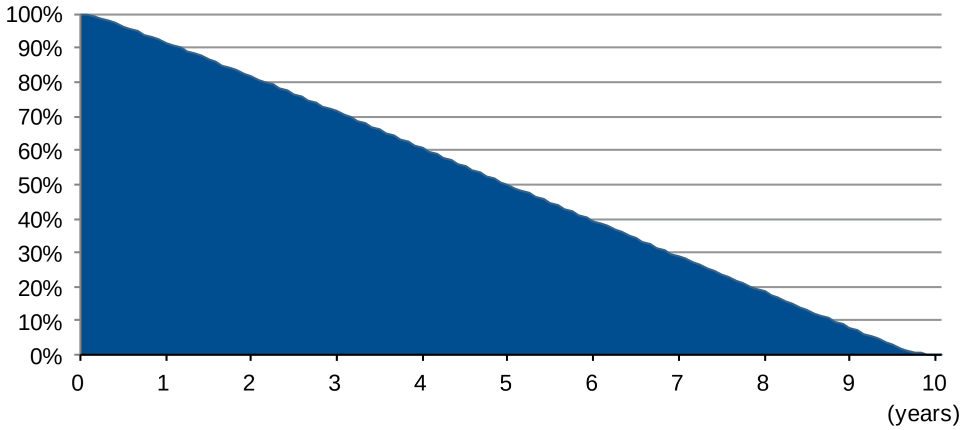
Source: IBL Banca, Scope

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 2008-2018 vintage data for IBL Banca's loan book, representative of the securitised portfolio, 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 a period of severe recession in Italy, from 2008-2009 and 2012-2014. Therefore, no long-term adjustment was applied to the mean default rate or 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

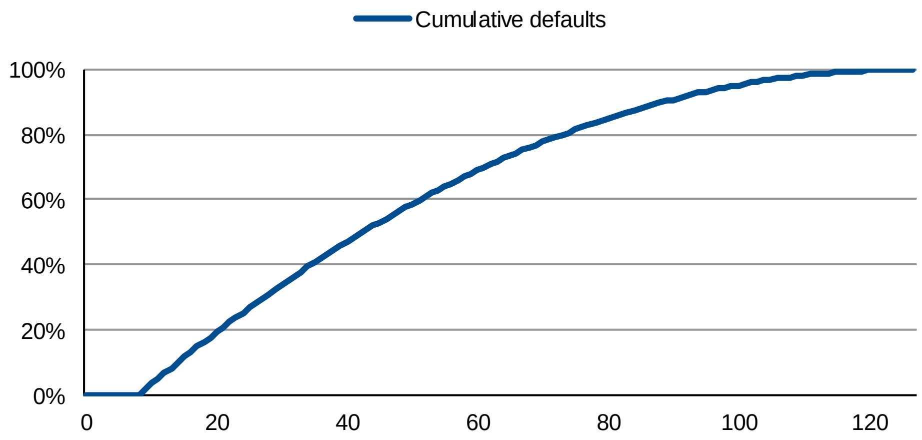
	Portfolio
Mean default rate	7.5%
Coefficient of variation	40.0%
Base case recovery rate	72.0%
AAA rating-conditional recovery rate	52.8%
Recovery timing	50% after 1 year, 20% after 2 years, 20% after 3 years and 10% after 4 years
CPR low	0.0%
CPR high	5.0%, for the first 3 years 10.0%, thereafter
Portfolio WA yield	5.3%

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 7.5% 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 simplified default definition of eight months in arrears and a front-loaded default term structure. The cumulative default-timing assumptions are shown in Figure 11 and represent the assumed default timing for the pool.

Figure 11: Cumulative default-timing assumption



Source: Scope

3.4.2. Loan recovery rate analysis

We calculated rating-conditional recovery rate assumptions as the weighted average of two levels of recovery rates. We assumed an 80% recovery rate in a scenario where the insurance does not default (RR1) and a 20% recovery rate in the event of insurance default (RR2). The weights applied to RR1 and RR2 reflect the default probability of the pool of insurance companies, assuming a 20% asset correlation between insurers. In addition, we applied rating-conditional haircuts to RR2 of 40% and 24% for the class A and class B notes, respectively.

Figure 12: Rating-conditional recovery rate assumptions

B	BB	BBB	A	AA	AAA
72.0%	71.8%	70.0%	59.2%	56.0%	52.8%

Source: Scope

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

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

Recoveries come 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 the 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 tested two CPR scenarios. A CPR assumption of 0% and a CPR assumption of 5% for the first three years and 10% thereafter, to test the structure's reliance on excess spread.

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 5.3%, 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 0.90% on the 6.2% original weighted average interest rate of the receivables.

The transaction benefits from a 3.4% estimated excess spread

Excess spread is estimated to be equal to 3.4%, 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 and class B 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. The post-enforcement priority of payments differs from the pre-enforcement priority of payments in the payment of class B interest, which is always subordinated to class A principal payment.

If, on any payment date, the cumulative portfolio net default ratio exceeds 3% of the initial outstanding balance, the interest amounts due on the class B notes will be subordinated to the full repayment of the principal of class A notes and the cash-trapping mechanism will be activated. The latter traps remaining funds at item 10 in the simplified pre-enforcement priority of payments below. Those funds would then be available in the next payment period to cover any shortfall on items 1-9.

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)	Prior to the occurrence of a class B interest subordination event, class B interest
4)	Replenish the liquidity reserve to the required balance
5)	Class A principal up to the target redemption amount
6)	Replenish the additional reserve to the required balance
7)	Upon occurrence of class B interest subordination event, class B interest
8)	Class B principal up to the target redemption amount
9)	Adjustment of purchase price and indemnity due and payable to the originator
10)	Cash trapping (if the cash trapping condition is satisfied)
11)	Remuneration on class J
12)	Class J principal (if class A and class B are redeemed in full) up to the target redemption amount
13)	Additional remuneration on class J

Source: Transaction documents and Scope

4.3. Liquidity reserve and additional reserve

Fully funded reserves provide 2.6% 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 is equal to 1% of the initial balance of the rated notes (EUR 3.6m).

During the life of the transaction, it will amortise up to the higher of 2% of the principal outstanding for the rated notes or 0.5% of the initial principal outstanding for the rated notes.

The liquidity reserve will provide liquidity protection to the class A notes and the class B notes (as long as the cumulative net default ratio does not exceed 3%) during the life of the transaction. It will also be available to repay the notes' principal at maturity.

4.3.2. Additional reserve

At closing, the additional reserve is equal to 1.6% of the initial balance of the rated notes (EUR 5.6m).

During the life of the transaction, it will amortise up to the higher of 1.5% of the principal outstanding of the rated notes or 0.75% of the portfolio purchase price.

The reserve will provide liquidity protection to the class A and B notes, and credit protection to class A notes during the life of the transaction. It will also be available to repay the notes' principal at maturity.

The aggregate amounts of the liquidity reserve and the additional reserve can cover costs and interests on the class A and class B notes for more than 15 monthly payment dates.

4.4. Management fee reserve

Limited exposure to management fees set-off

A management fee reserve covers a portion of the fees paid up front by the borrower. In the case of prepayment, management fees can be set off by the borrower, resulting in a reduction of outstanding instalments. A dedicated reserve, the management fee reserve, was funded at closing, to cover this set-off risk. In addition, if the reserve is not enough to cover the amounts which borrowers set off, the originator will cover the shortfall.

At each payment date, the target management fee reserve will be equal to 25% of the outstanding management fees exposure (EUR 5,178 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.

4.5. Amortisation and provisioning

The strict sequential amortisation effectively protects senior noteholders in times of stress. The amortisation of class A will be accelerated during stressed periods, due to the triggering of the class B interest subordination event and the cash-trapping mechanism.

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 10 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.

4.6. Matched interest rates

Hedging of interest rate risk

Class A notes pay one-month Euribor plus a margin, while the portfolio pays a fixed rate. To hedge interest rate risk, the issuer has entered into a fix-floating interest rate swap with Credit Agricole Corporate and Investment Bank (Paris branch). Under the terms of the swap, the issuer will pay a fixed rate of 0.67%, while the swap counterparty will pay a coupon of one-month Euribor plus 0.65% (floored at zero). The notional of the swap will be the minimum between the class A outstanding balance and the outstanding balance of the asset portfolio.

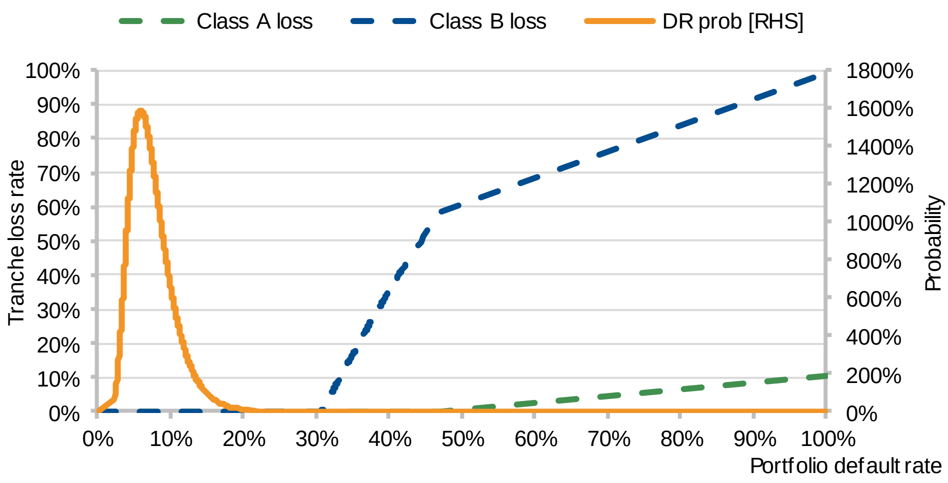
5. Quantitative analysis

We used a bespoke cash flow analysis

We performed a cash flow analysis, considering 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 11 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 11 consider a 0.80% reduction to the portfolio balance to account for commingling risk.

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

The rating of the class B notes reflects strong credit quality when measured in expected loss terms, but is constrained by the default risk of the tranche. This is due to the impact of the class B interest deferral trigger, which is hit if cumulative net defaults exceed 3%, subordinating class B interest payments to the full repayment of the class A notes.

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 each rated instrument 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:

Class A notes, rated AAASF: sensitivity to probability of default, zero notches; sensitivity to recovery rates, zero notches.

Class B notes, rated A+SF: sensitivity to probability of default, zero notches; sensitivity to recovery rates, zero 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 86% 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.

We considered the following risks in our analysis (referred to as a 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 in this instance the loan's maturity is extended – 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 a period of 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.

The public-sector headcount and salary/pension payments generally decrease after a sovereign default. Complete non-payment is significantly less likely because of the severe social, political and economic consequences this would have. We therefore assumed for the transaction that a sovereign CQS stress event is less likely than a sovereign default on public debt, commensurate with an A probability of default over the portfolio's weighted average life. Scope's current rating on the Republic of Italy is BBB+. For more insight into Scope's fundamental analysis of the Italian economy, refer to our press release on the Republic of Italy, dated 7 December 2018.

8. Counterparty risk

The transaction is exposed to counterparty risk from: i) IBL Banca, as originator, cash manager and calculation agent; ii) IBL Servicing, as servicer; iii) Zenith, as back-up servicer and back-up calculation agent; iv) Citibank N.A., Milan branch, as transaction account bank and paying agent; and v) Credit Agricole Corporate and Investment Bank, Paris branch, as swap counterparty.

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, IBL Servicing, is well mitigated in this transaction. Zenith, back-up servicer since closing, has undertaken to become operative within 30 days in the event of a termination event for IBL Servicing (or for IBL Banca as sub-servicer).

8.2. Commingling risk from account bank

The issuer has a collection account held at IBL Banca that receives all asset proceeds and 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 the occurrence of a servicer disruption event. However, employers may not immediately implement the new payment instructions. We have assumed a consequent loss of up to four months of collections. We sized a 0.8% loss based on the probability of a commingling event over the expected life of the

[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.

transaction. However, given the rating on IBL (BBB), we take comfort from the low probability of a servicer insolvency event happening.

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 to occur.

9.3. Use of legal and tax opinions

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.

Tax efficient set-up; bankruptcy remote SPV

The tax opinion produced for the issuer indicate that the transaction is tax-neutral, i.e. no taxes apply, except for VAT in the context of contracted services, which remain the cost of the issuer.

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 General Structured Finance Rating Methodology, Consumer 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 2018 and is generally very granular. The recovery data also covers a period from 2008 to 2018, 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 4-2018	Marzio Finance 3-2018	Marzio Finance 2-2018	Marzio Finance 1-2017	Dyret
Country	Italy	Italy	Italy	Italy	Italy
Closing date (dd/mm/yyyy)	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.	Dynamica Retail S.p.A.
Servicer	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 SpA	Zenith Service SpA	Zenith Service SpA	Zenith Service SpA	Zenith Service S.p.A.
Back-up servicer facilitator	-	-	-	-	Zenith Service S.p.A.
Portfolio characteristics					
Number of loans	19,397	22,952	13,145	19,884	8,392
Number of borrowers	18,687				8,392
Original portfolio balance (€)	389,163,840	487,141,290	334,298,977	429,475,538	194,603,643
Outstanding portfolio balance (€)	376,770,538	437,201,060	157,872,473	361,374,376	160,348,393
Average original loan balance (€)	20,063	21,224	25,432	21,599	23,189
Average outstanding loan balance (€)	19,424	19,048	12,010	18,174	19,107
Lenth of contracts					
WA original term (years)	9.2	9.3	9.7	9.4	9.6
WA seasoning (years)	0.3	1.0	4.4	1.6	1.8
WA remaining term (years)	8.9	8.3	5.3	7.8	7.8
Contract type					
CDQ - Cessione del quinto (%)	82.3%	83.4%	77.7%	83.3%	81.4%
DP - Delegazione di pagamento (%)	17.7%	16.6%	22.3%	16.7%	18.6%
Portfolio yield					
WA portfolio yield (%)	6.2%	6.0%	6.4%	5.9%	4.0%
Type of debtors					
Public sector employees (%)	36.6%	41.2%	39.1%	38.8%	54.8%
State employees (%)	12.8%	13.5%	16.7%	15.3%	-
Private sector employees (%)	13.7%	8.7%	2.8%	6.8%	9.9%
Pensioneers (%)	36.9%	36.6%	41.4%	39.1%	35.3%
Borrower concentration					
Top 1 (%)	0.03%	0.02%	0.04%	0.03%	-
Top 10 (%)	0.23%	0.19%	0.30%	0.21%	-
Employer concentration					
Top 1 (%)	1.4%*	2.0%*	2.0%*	2.0%*	34.3%
Top 10 (%)	4.7%*	10.9%*	7.2%*	6.5%*	54.7%
Public sector exposure (%)	86.3%	91.3%	97.2%	93.2%	90.1%
Employer regional concentration					
North	30.2%	29.1%	27.9%	25.7%	16.4%
Centre	28.4%	28.9%	31.3%	31.0%	21.8%
South	41.4%	42.0%	40.8%	43.3%	61.8%
Top region	Lazio - 18.9%	Lazio - 19.4%	Lazio - 21.5%	Lazio - 20.4%	Campania - 27.3%
Insurance company exposure					
Top 1 life insurance	27.0%	24.8%	25.2%	21.8%	21.8%
Top 2 life insurance	45.1%	43.6%	47.2%	43.1%	42.0%
Top 3 life insurance	61.7%	58.9%	66.2%	59.4%	58.6%
Top 1 unemployment insurance	16.5%	18.4%	25.2%	20.5%	21.8%
Top 2 unemployment insurance	28.5%	33.6%	44.6%	36.8%	42.0%
Top 3 unemployment insurance	39.9%	46.4%	54.0%	48.1%	58.6%
Assumptions summary					
Default definition	8 months	8 months	8 months	8 months	9 months
Mean default	7.5%	7.0%	5.0%	6.0%	10.5%
CoV	40%	40%	45%	45%	35.0%
Recovery rate (insurance coverage)	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%
AAA scenario recovery rate	52.8%	54.4%	30.2%	55.6%	42.9%
Recovery timing	4 yrs - (50% + 20% + 20% + 10%)	4 yrs - (50% + 20% + 20% + 10%)	4 yrs - (50% + 20% + 20% + 10%)	4 yrs - (50% + 20% + 20% + 10%)	4 yrs - (50% + 20% + 20% + 10%)
Prepayment rate	5.0%	5.0%	5.0%	5.0%	5.0%
Portfolio yield	5.3%	5.2%	5.8%	5.1%	3.8%
Insurers Inverse-herfindahl metric	6.0	5.7	4.3	5.1	5.9
Insurers correlation	20%	20%	20%	20%	20.0%
Public sector exposure (%)	86.3%	91.3%	97.2%	93.2%	85.0%
Private sector exposure (%)	13.7%	8.7%	2.8%	6.8%	15.0%
Structural features					
Tranching					
Class A	AAA	AAA	AAA	AAA	NR
CE Class A	21.0%	14.0%	18.0%	9.0%	20.5%
Class B	A+	N/A	N/A	N/A	BBB+
CE Class B	7.0%	N/A	N/A	N/A	10.3%
Class C	N/A	N/A	N/A	N/A	BB
CE Class C	N/A	N/A	N/A	N/A	4.7%
Class J	NR	NR	NR	NR	NR
CE Class J	0.0%	0.0%	0.0%	0.0%	0.0%
Cash reserve (% of rated notes)	2.6%	2.9%	3.3%	1.8%	2.0%
Revolving period (years)	0	0	0	0	0.75
Commingling risk (yes/no)	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
Set-off risk (yes/no)	Yes	Yes	Yes	Yes	Yes
Set-off risk mitigants (e.g., prepayment reserve)	Prepayment reserve	Prepayment reserve	Prepayment reserve	Prepayment reserve	Prepay reserve - 1.3% of balance of each loan
Type of swap	Fix-to-Floating IRS	Fix-to-Floating IRS	N/A	N/A	N/A
Swap co. rating trigger	A-	A-	N/A	N/A	N/A

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

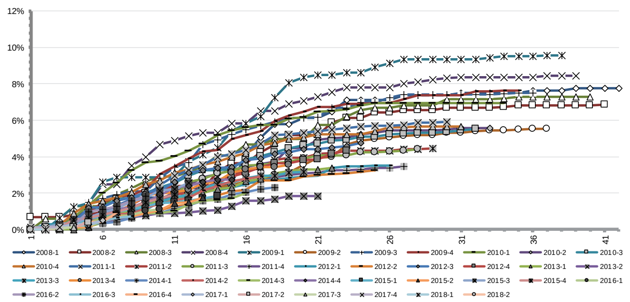
II. Vintage data provided by originator

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 for the portfolio

Figure 16: Public administration – default and recovery data

Defaults



Recoveries

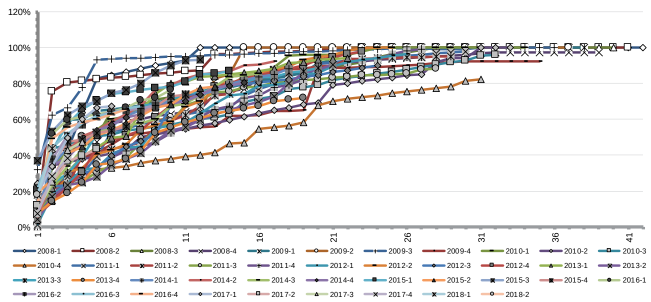
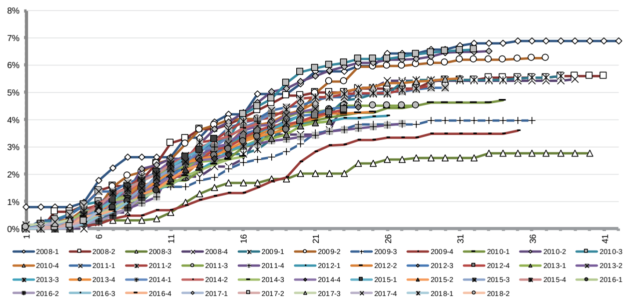


Figure 17: State administration – default and recovery data

Defaults



Recoveries

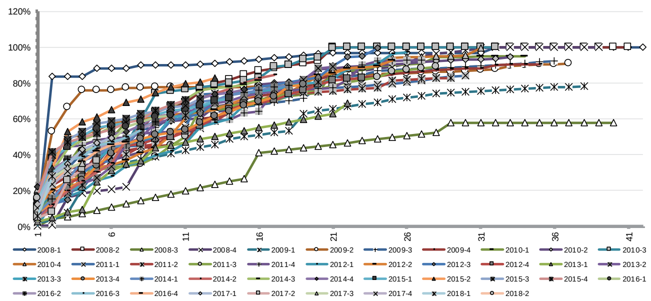
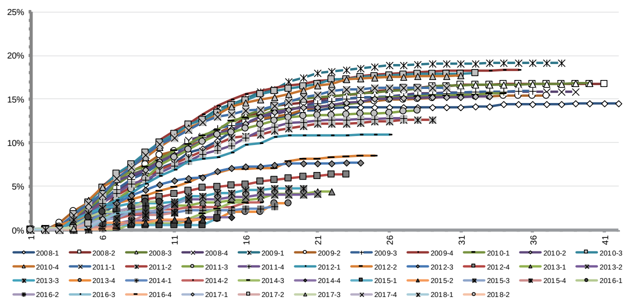


Figure 18: Private sector – default and recovery data

Defaults



Recoveries

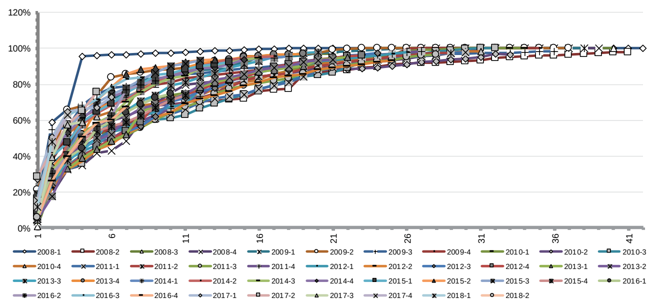
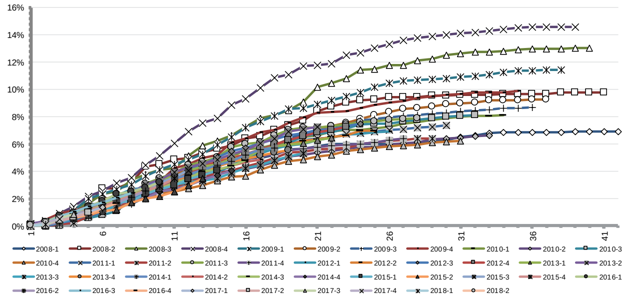
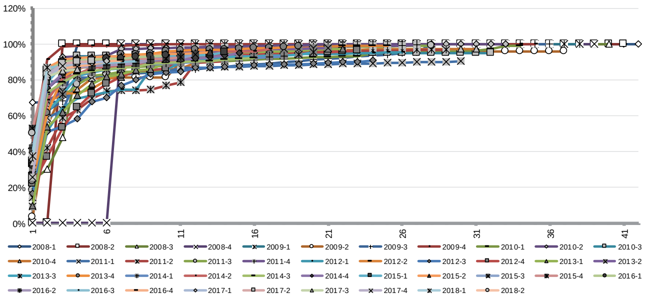


Figure 19: Pensioners – default and recovery data

Defaults



Recoveries



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