VCL Master Residual Value S.A. , Compartment 2 Series 2023 Auto ABS Notes Assigned Ratings; Other Ratings Affirmed

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Ratings list

Class	Rating*	Maximum commitment amount (mil. €)§	Minimum available credit enhancement (%)†	Interest‡	Legal final maturity
Ratings assigned					
A 2023-1	AAA (sf)	500.0	46.5	One-month EURIBOR plus 0.80%	Sept. 25, 2030
A 2023-2	AAA (sf)	100.0	46.5	One-month EURIBOR plus 0.80%	Sept. 25, 2030
B 2023-1	A+ (sf)	150.0	33.0	One-month EURIBOR plus 1.50%	Sept. 25, 2030
Ratings affirmed					
A 2015-1	AAA (sf)	464.1	46.5	One-month EURIBOR plus 0.80%	Sept. 25, 2030
A 2015-2	AAA (sf)	523.7	46.5	One-month EURIBOR plus 0.80%	Sept. 25, 2030
A 2015-3	AAA (sf)	930.0	46.5	One-month EURIBOR plus 0.80%	Sept. 25, 2030
A 2015-4	AAA (sf)	780.0	46.5	One-month EURIBOR plus 0.80%	Sept. 25, 2030
A 2015-5	AAA (sf)	755.0	46.5	One-month EURIBOR plus 0.80%	Sept. 25, 2030
A 2015-6	AAA (sf)	300.0	46.5	One-month EURIBOR plus 0.80%	Sept. 25, 2030
A 2016-1	AAA (sf)	476.5	46.5	One-month EURIBOR plus 0.80%	Sept. 25, 2030
A 2016-2	AAA (sf)	50.0	46.5	One-month EURIBOR plus 0.80%	Sept. 25, 2030
A 2016-4	AAA (sf)	578.6	46.5	One-month EURIBOR plus 0.80%	Sept. 25, 2030
A 2018-2	AAA (sf)	349.2	46.5	One-month EURIBOR plus 0.80%	Sept. 25, 2030

Ratings list (cont.)

Class	Rating*	Maximum commitment amount (mil. €)§	Minimum available credit enhancement (%)†	Interest‡	Legal final maturity
A 2018-4	AAA (sf)	265.0	46.5	One-month EURIBOR plus 0.80%	Sept. 25, 2030
A 2018-5	AAA (sf)	361.5	46.5	One-month EURIBOR plus 0.80%	Sept. 25, 2030
A 2021-2	AAA (sf)	500.0	46.5	One-month EURIBOR plus 0.80%	Sept. 25, 2030
A 2022-1	AAA (sf)	358.4	46.5	One-month EURIBOR plus 0.80%	Sept. 25, 2030
B 2015-1	A+ (sf)	110.9	33.0	One-month EURIBOR plus 1.50%	Sept. 25, 2030
B 2015-3	A+ (sf)	300.0	33.0	One-month EURIBOR plus 1.50%	Sept. 25, 2030
B 2016-3	A+ (sf)	443.1	33.0	One-month EURIBOR plus 1.50%	Sept. 25, 2030
B 2018-2	A+ (sf)	68.3	33.0	One-month EURIBOR plus 1.50%	Sept. 25, 2030
B 2020-1	A+ (sf)	80.0	33.0	One-month EURIBOR plus 1.50%	Sept. 25, 2030

*Our ratings address timely payment of interest and ultimate principal. §The current issuance amount may be less than the maximum commitment for each class. †Reflects the documented minimum figures and includes subordination, overcollateralization, and a cash reserve. ‡Subject to a floor of zero. EURIBOR--Euro interbank offered rate. NR--Not rated.

Overview

- We assigned our 'AAA (sf)' ratings to VCL Master Residual Value S.A., Compartment 2's series A 2023-1 notes and A 2023-2 notes, and our 'A+ (sf)' rating to the series B 2023-1 notes.
- At the same time, we affirmed our ratings on the outstanding class A and B notes.
- The transaction is a securitization of a portfolio of German auto lease residual values, which Volkswagen Leasing GmbH (VW Leasing) originated.

FRANKFURT (S&P Global Ratings) Sept. 25, 2023--S&P Global Ratings today assigned its 'AAA (sf)' credit ratings to VCL Master Residual Value S.A., Compartment 2's series A 2023-1 and A 2023-2 asset-backed floating-rate notes, and our 'A+ (sf)' rating to the series B 2023-1 notes. At the same time, we affirmed our 'AAA (sf)' and 'A+ (sf)' ratings on the issuer's outstanding series of A and B notes.

VCL Master Residual Value, Compartment 2 is a securitization of a portfolio of German auto lease residual values, which Volkswagen Leasing GmbH (VW Leasing) originated. VW Leasing is the initial servicer, and no back-up servicer was appointed at closing.

On any payment date during the revolving period, the issuer can issue new series of notes, subject to maintaining the initial required credit enhancement for both the class A and B notes. The most recent renewal was on Sept. 26, 2022, when the revolving period was extended by 12 months until September 2023 (see "VCL Master Residual Value S.A., Compartment 2 Series A 2022-1 Auto ABS

Rating Assigned; Other Ratings Affirmed," published on Sept. 26, 2022).

Together with the issuance of the series 2023 class A and B notes, the revolving phase was extended by one-year until September 2024. Also, the existing class A and B notes have been repriced and the issuer entered into new swap agreements.

The initial required credit enhancement or target overcollateralization amounts for both the class A and B notes have changed since our previous review. In September 2023, the required credit enhancement for the class A notes increased to 46.50% from 43.80%. It also increased for the class B notes to 33.00% from 30.90%. A combination of subordination, initial and additional overcollateralization, and a cash reserve provide credit enhancement to the rated notes.

In addition to the abovementioned ones, several additional changes were introduced under the September 2023 renewal. We have included in our analysis the following list of amendments to the transaction documents:

- The eligibility criteria have been modified so that the maximum share of used cars allowed in the pool is now 8% (up from 6%). Also, the criterium that limited the share of lease contracts in the pool younger than 12 months to 40% has been removed.
- During the revolving period, the cash reserve is now floored at 3% of the class A and B notes outstanding. A breach of this floor on any single payment date would trigger a CEIC. During the amortization phase, the reserve is funded at the minimum of 3% of the class A and B notes (outstanding as of the last payment date during the replenishment phase) and the class A and B notes outstanding.
- A new mechanism to support the transaction in case of negative excess spread has also been introduced. After applying available collections as per the priority of payments and if no reserve rating trigger has been breached, the seller will provide ongoing support to cover any liquidity shortfalls for the payments of senior costs, swap costs, and interest on the notes. If, however, our issuer credit rating on Volkswagen Financial Services AG falls below 'BBB'/'A-2' (or 'BBB+' in the absence of a short-term rating), the seller will post within 10 business days a buffer release reserve. The reserve will cover senior costs and interest on the notes for approximately two payment dates. In our driving run, we have not modelled this reserve.
- The issuer now grants to the seller the option to modify the discount rate for receivables already purchased and those to be purchased during the replenishment phase. This option can be exercised in conjunction with the extension of the revolving phase, and it is subject to a confirmation from S&P Global Ratings that the ratings on the notes will not be adversely affected.

The class A notes rank senior to the class B notes, and each class of notes ranks pari passu among themselves. Under the transaction documents, amortization is sequential, but switches to pro rata once the class-specific overcollateralization target levels are reached, assuming no specific triggers have been breached. The notes may switch to sequential payment again, once certain credit enhancement increase conditions have been met. If the servicer were to become insolvent at any point in the transaction's life, the notes would permanently switch to sequential amortization.

Rating Rationale

Operational risk

VW Leasing has underwritten auto leasing contracts in Germany since 1966. In our view, the company's track record of stable, strong quality asset origination is among the best of all European auto ABS issuers. Our ratings on the class A and B notes reflect our assessment of the company's origination policies, as well as our evaluation of VW Leasing's ability to fulfill its role as servicer under the transaction documents. There is no back-up servicer. For our analysis, we rely on the general availability of servicing in the German market and have also incorporated assumptions in our cash flow analysis, to analyze any potential impact from servicer disruption risk.

The collateral in this pool comprises expectancy rights related to prime auto leases. Under our operational risk criteria, we therefore consider the severity risk to be moderate and portability risk as low. We assess the disruption risk of servicer as low. Therefore, the criteria do not impose any cap on the maximum achievable rating due to operational risks (see "Related Criteria").

Credit risk

Following the good performance of the collateral over the past years, we have reviewed our credit assumptions. We reduced our base-case gross loss assumptions to 2.42% from 2.63% in our previous review. This reduction stems from a reduction in the net loss base case to 0.80% from 1.05%. At the same time, we have increased our recovery rate base case to 67% from 60%. We have also reduced the multiple to 4.3x at 'AAA' from 4.4x.

Table 1

Credit assumptions

Rating level	Net loss base-case	Recovery rate base-case	Gross loss base-case	Multiple	Recovery haircut	Stressed recovery rate	Applied net loss
AAA	0.8%	67%	2.4%	4.3x	45%	36.9%	6.6%
A+	0.8%	67%	2.4%	2.8x	35%	43.6%	3.8%

The portfolio consists of residual values, which are subject to market value decline risk. We reviewed our market value decline assumptions, in view of the current dampened auto market, and the consequent impact on used car values. We consider our market value decline assumptions for rating stresses of 'BBB' and above as already including the stress levels we expect to see in used car markets. Therefore, our stress residual value loss assumptions remained at 42.30% at 'AAA' and 29.90% at 'A+'.

We have analyzed credit risk and residual value risk under our global auto ABS criteria, using historical loss data for VW Leasing's book and performance data from previous VCL leasing transactions (see "Related Criteria").

Cash flow analysis

We have assessed the transaction's documented payment structure, and assumed the notes will have the minimum required credit enhancement in our cash flow analysis. The issuer can extend the transaction's revolving period several times. Once the revolving period ends, the transaction amortizes sequentially until certain overcollateralization targets for the class A and B notes are reached. However, the amortization between the class A and B notes and the subordinated loan switches to pro rata amortization from sequential if certain conditions (for instance, the CEIC not being in effect) are fulfilled, or when class-specific target overcollateralization levels are reached. Our analysis indicates that the minimum available credit enhancement for the class A and B notes is sufficient to withstand the credit and cash flow stresses that we apply at the respective rating levels.

Our cash flow analysis indicates the available credit enhancement for the junior notes is commensurate with a higher rating than that currently assigned. However, we have assigned a 'A+ (sf)' rating on the junior notes on account of the transaction's revolving nature, the ongoing frequent issuance of new series, and the current macroeconomic outlook for Germany.

Counterparty risk

Our ratings on the class A and B notes also consider that the replacement mechanisms implemented in the transaction documents adequately mitigate the counterparty risks to which the transaction is exposed. We have analyzed these counterparty risks by applying our counterparty criteria (see "Related Criteria"). Our ratings on the notes reflect that the swap agreements are in line with our counterparty criteria.

Legal risk

We consider the issuer to be bankruptcy remote, in line with our legal criteria (see "Related Criteria"). We have received a transaction legal opinion on the September 2023 renewal, which provides assurance that the structure achieves a valid and effective sale of assets, and we believe that the sale of the assets would survive the seller's insolvency.

We consider that the transaction may be exposed to trade tax risk. We have sized the unmitigated exposure as an additional loss.

Sovereign risk

Under our structured finance sovereign risk criteria, the maximum differential between the rating on the security and the rating on the sovereign depends on the asset sensitivity to country risk and the sovereign rating. We view the asset sensitivity to the country risk as low, and our long-term unsolicited sovereign rating on Germany is 'AAA'. Consequently, our sovereign risk criteria do not cap our ratings on the rated notes.

Forward-Looking View

In our analysis, we considered the following economic data and their baseline effect on collateral credit quality in determining our credit assumptions (see "Related Research").

Table 2

Economic factors

	2022	2023f	2024f	2025f
Real GDP (y/y growth, %)	1.9	(0.1)	0.8	1.6
Unemployment rate (annual average, %)	3.1	3.1	3.2	3.2
CPI inflation (%)	8.7	6.5	2.9	2.0

Sources: National Statistics offices, Eurostat, S&P Global Ratings.

We consider the transaction's resilience to additional stresses to some key variables, in particular defaults and recoveries, to determine our forward-looking view.

In our view, borrowers' ability to repay their auto loans will be highly correlated to macroeconomic conditions, particularly the unemployment rate and, to a lesser extent, consumer price inflation and interest rates. Given the loans are fixed-rate, we believe rising interest rates will have a lower effect on these borrowers in the near term, while longer term, they will likely further stretch household finances. As of today, our forecast on unemployment rates for Germany is 3.1% in 2023, and 3.2% for 2024 and 2025. Our forecast for inflation in Germany is 6.5% in 2023, and we expect this to decline to 2.9% in 2024 and 2.0% in 2025.

Furthermore, a decline in second-hand car values typically lowers realized recoveries. Although used car prices may decline moderately in Germany in 2023, we do not expect them to fall significantly.

Given our current macroeconomic forecast and forward-looking view of Germany's auto market, our sensitivity scenarios consider, all else being equal, the hypothetical effect on our credit ratings of:

- An increased gross default base case of up to 30%; and
- A maximum haircut of 30% to the recovery rate base case.

We therefore ran eight scenarios with increased gross defaults and/or reduced expected recoveries, as shown in the table below.

Sensitivity analysis and results

Class (%)	Base case	1	2	3	4	5	6	7	8
Default rate base case increase	-	10	30	-	-	10	30	10	30
Recovery rate base case decrease	-	-	-	10	30	10	10	30	30
Gross default rate	2.4	2.7	3.1	2.4	2.4	2.7	3.1	2.7	3.1
Recovery rate	67	67	67	60	47	60	60	47	47

Downgrade notches

No change	One	Two

Class of notes	Initial rating	1	2	3	4	5	6	7	8
A	AAA	AAA	AA+	AA+	AA	AA+	AA+	AA	AA
B	A+	A+	A+	A+	A	A+	A	A	A-

Source: S&P Global Ratings.

The results of the above sensitivity analysis indicate a deterioration of no more than two notches on the notes, which is in line with the credit stability considerations in our rating definitions. Transaction features such as initial subordination levels and a liquidity reserve enhance the stability of the ratings under each scenario.

Related Criteria

- Criteria | Structured Finance | ABS: Global Auto ABS Methodology And Assumptions, March 31, 2022
- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- Criteria | Structured Finance | General: Global Framework For Payment Structure And Cash Flow Analysis Of Structured Finance Securities, Dec. 22, 2020
- Criteria | Structured Finance | General: Methodology To Derive Stressed Interest Rates In Structured Finance, Oct. 18, 2019
- Criteria | Structured Finance | General: Counterparty Risk Framework: Methodology And Assumptions, March 8, 2019
- Criteria | Structured Finance | General: Incorporating Sovereign Risk In Rating Structured Finance Securities: Methodology And Assumptions, Jan. 30, 2019
- Legal Criteria: Structured Finance: Asset Isolation And Special-Purpose Entity Methodology, March 29, 2017
- Criteria | Structured Finance | General: Global Framework For Assessing Operational Risk In Structured Finance Transactions, Oct. 9, 2014
- General Criteria: Methodology Applied To Bank Branch-Supported Transactions, Oct. 14, 2013
- Criteria | Structured Finance | General: Global Derivative Agreement Criteria, June 24, 2013

- General Criteria: Global Investment Criteria For Temporary Investments In Transaction Accounts, May 31, 2012
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011
- Criteria | Structured Finance | General: Methodology For Servicer Risk Assessment, May 28, 2009

Related Research

- S&P Global Ratings Definitions, June 9, 2023
- European Auto ABS Index Report Q4 2022, Feb. 10, 2023
- Global Credit Conditions Downside Scenario: Inflation, Geopolitics Are Twin Threats To Our Base case, Dec. 8, 2022
- Economic Outlook U.K. Q1 2023: A Moderate Yet Painful Recession, Nov. 29, 2022
- United Kingdom, Oct. 24, 2022
- VCL Master Residual Value S.A., Compartment 2 Series A 2022-1 Auto ABS Rating Assigned; Other Ratings Affirmed, Sept. 26, 2022
- 2020 Annual European Structured Finance Default And Rating Transition Study, Sept. 21, 2021
- ESG Industry Report Card: Auto Asset-Backed Securities, March 31, 2021
- 2017 EMEA ABS Scenario And Sensitivity Analysis, July 6, 2017
- European Structured Finance Scenario And Sensitivity Analysis 2016: The Effects Of The Top Five Macroeconomic Factors, Dec. 16, 2016
- Global Structured Finance Scenario And Sensitivity Analysis 2016: The Effects Of The Top Five Macroeconomic Factors, Dec. 16, 2016