RFC Process Summary:

Global Equipment ABS Methodology And Assumptions

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On March 12, 2019, S&P Global Ratings published a request for comment (RFC) article on its proposed revisions to its criteria for rating global equipment asset backed securities (ABS), titled "Request For Comment: Global Equipment ABS Methodology And Assumptions."

Following feedback from the market, we finalized our criteria and published them on May 31, 2019, in an article titled "Global Equipment ABS Methodology And Assumptions." On the same day, we also published the related guidance article "Guidance: Global Equipment ABS Methodology And Assumptions," to provide further details on how we apply these criteria.

We would like to thank the market participants who provided feedback. This RFC process summary provides an overview of the changes between the RFC and the final criteria as well as the rationale behind those changes. In addition, this document outlines feedback from various market participants that was considered but didn't result in any changes to the final criteria. We made other changes that are purely stylistic and intended to clarify our methodology.

I) Summary Of Changes And Clarifications

Minimum credit enhancement

Feedback: One market participant asked if minimum credit enhancement as outlined in Table 5 of the RFC could be interpolated for each rating level (that is, including the +/- modifiers).

Response: We have updated the final criteria to allow for interpolation for minimum credit enhancement at each rating level (which includes the +/- modifiers).

Criteria scope

Feedback: One market participant asked for clarification on whether the equipment ABS criteria would be applicable to mixed automotive-backed pools of 'commercial' and 'consumer' contracts.
Response: We have further clarified the scope to indicate that the global equipment ABS criteria is applicable to (i) mixed asset pools that may include a combination of vehicles and equipment, if the pool is exposed to concentration risk or (ii) pools that are predominantly composed of vehicle fleets. Please refer to the final criteria for the description of the full scope.

For example, we'll determine whether a pool consisting of financing arrangements for self-employed borrowers or small and medium-sized enterprises (SMEs) falls within the scope of the global equipment ABS criteria by considering the collateral type and the obligor concentrations. If, for example, the underlying collateral for such a pool is predominantly vehicles (but not vehicle fleets) and the pool doesn't have significant obligor concentrations, it would not fall within the scope of the global equipment ABS criteria and may continue to be analyzed using other relevant criteria.

Alternatively, if that same pool's obligor concentrations are significant, then the pool would fall within the scope of global equipment ABS criteria.

Residual stress

Feedback: One market participant asked to clarify the last bullet point in Paragraph 55 of the RFC, specifically what is meant by "obligor default, to avoid application to both credit stress and residual stress on the same asset."

Response: In the final criteria, we have clarified that if residuals are included in the pool balance, we will apply our residual stress to the portion of the pool representing residuals of non-defaulted obligors, to avoid application of both credit stress and residual stress on the same asset.

II) Summary Of Other Market Feedback

Minimum credit enhancement

Feedback: One market participant asked whether credit could be given to fast-growing hard credit enhancement that accumulates after closing in relation to minimum credit enhancement (Table 5 of the RFC) at the time of transaction closing.

Response: The minimum hard credit enhancement has to be available at the time of transaction closing, and we would not consider fast-growing hard enhancement that accumulates after closing as part of the minimum because the growth is dependent on future performance.

Considerations related to down-payments and lessee guarantees

Feedback: One market participant commented that there seems to be no mention of certain features typical in equipment finance, such as down-payments and lessee guarantees. Is this covered somewhere, the commenter asked, or could it perhaps be specified in the section on performance risks?

Response: Down-payments and lessee guarantees are qualitative considerations in our assessment of defaults and recoveries.

Obligor concentration

Feedback: One market participant asked if the typical number of largest obligors assumed to default applies only when an obligor's exposure accounts for over 1.5% of the pool, and does it explicitly take into account the obligor creditworthiness? They also asked how the 1.5% typical threshold was determined given individual obligor concentration risk for Australian equipment ABS has historically been deemed relevant at exposure levels closer to 2.0% of the pool.

Response: The largest obligor default test is generally applicable when an obligor concentration is higher than approximately 1.5%. Please note that Paragraph 36 of the RFC also outlines additional considerations.

Furthermore, the large obligor default assumption does explicitly account for the obligor creditworthiness as outlined in the RFC by including only those obligors with a creditworthiness lower than the liability rating level and with a concentration of higher than approximately 1.5%.

We have not seen any largest obligor concentrations exceeding 1% in Australian equipment transactions we've rated over the past 10 years. We consider the threshold of approximately 1.5% to be appropriate globally.

Balloon loans

Feedback: One market participant asked whether providing quantitative guidance could be considered on what constitutes a significant portion of the total pool that may result in additional risk from balloon loans (in reference to Paragraph 23 of the RFC).

Response: This is not intended to be prescriptive; rather, it's determined based on the specific characteristics of the originator, the underwriting and historical performance data, and the composition of the pool. We may also take into account regional differences.

Supplemental test

Feedback: One market participant asked to clarify whether the liability ratings in Table 3 refer to issue ratings on the global scale. They also asked if a certain credit quality would be assumed depending on the product and/or collateral type backing the loan or lease.

Response: The liability ratings in Table 3 are on a global scale. Paragraph 40 of the RFC states that for each unrated obligor, we typically assume that the obligor's creditworthiness falls within the 'B+' to 'CCC-' buckets unless we have an assessment of its creditworthiness (based on, for example, a credit estimate or a guarantee that qualifies for ratings substitution, if applicable).

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