S&P Global Ratings

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Presale:

VCL Multi-Compartment S.A., Compartment VCL 37

October 10, 2022

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Preliminary Ratings

Class	Prelim. rating*	Prelim. amount (mil. €)	Overcollateralization and subordination (%)	Cash reserve (%)	Available credit enhancement (%)§	Interest (%)†	Legal final maturity
A	AAA (sf)	708.80	5.49	1.10	6.59	1ME + a margin	September 2028
B	AA- (sf)	15.10	3.48	1.10	4.58	1ME + a margin	September 2028
Subordinated loan	NR	19.30	N/A	N/A	N/A	N/A	N/A

Note: This presale report is based on information as of Oct. 10, 2022. The ratings shown are preliminary. Subsequent information may result in the assignment of final ratings that differ from the preliminary ratings. Accordingly, the preliminary ratings should not be construed as evidence of final ratings. This report does not constitute a recommendation to buy, hold, or sell securities. *Our preliminary ratings address timely payment of interest and ultimate principal. §Includes subordination, overcollateralization (€6.8 million or 0.91% of the discounted pool balance), and a cash reserve (initial amount of €8.25 million or 1.10% of the discounted pool balance). †Subject to a floor of zero. 1ME--One-month Euro Interbank Offered Rate. NR--Not rated. N/A--Not applicable.

Transaction Summary

- S&P Global Ratings has assigned its preliminary credit ratings to VCL Multi-Compartment S.A., Compartment VCL 37's (VCL 37) class A and B notes. At closing, VCL 37 will also be granted an unrated subordinated loan.
- Our preliminary ratings address timely payment of interest and ultimate payment of principal on the class A and B notes.
- VCL 37's notes will securitize a portfolio of German auto lease receivables, which Volkswagen Leasing GmbH (VW Leasing) originated to its mostly retail and commercial customer base in the ordinary course of its business. The lease receivables arise from fixed-term, level payment lease contracts, with payments due monthly. The residual values of the leased vehicles corresponding to the lease receivables will not be sold to VCL 37, so no direct residual value risk is present in this transaction.
- The transaction is static (i.e., it has no replenishment period), and the notes will start to amortize immediately after closing. Amortization will begin sequentially, but will switch to pro rata after further overcollateralization has built up, assuming no performance triggers are breached.

- A combination of subordination, overcollateralization, and a cash reserve will provide credit enhancement to the rated notes. The transaction will only benefit from excess spread if VW Leasing becomes insolvent or the cumulative net loss ratio exceeds 1.6%. There is no principal deficiency ledger mechanism in place.
- A fixed-to-floating interest rate swap agreement with a suitable counterparty, in line with our counterparty criteria, will mitigate the risk of potential interest rate mismatches between the fixed-rate assets and floating-rate liabilities.
- All of the receivables to be securitized have previously been refinanced through the existing warehousing facility, VCL Master S.A. Compartment 1.
- The transaction's capital structure is slightly different compared to that of VCL Multi-Compartment S.A., Compartment VCL 35 (VCL 35), which we rated in March 2022. The cash reserve in VCL 37 will be equal to the lower of (i) 1.1% of the initial outstanding discounted asset balance, and (ii) the class A and B notes' aggregate outstanding principal amount as of the relevant payment date. VCL 35's cash reserve amortized at 1.2% of the outstanding discounted asset balance, subject to a floor of 1.0% of the initial discounted pool balance.
- Similar to VCL 35, seller-related risks (German trade tax risks, and value-added tax [VAT] risks) are mitigated by a nonamortizing seller risk reserve (1.10% of the initial discounted pool balance), which VW Leasing will fund at closing. In our view, the seller risk reserve only partially mitigates the potential German trade tax and VAT risks. Therefore, we have considered the uncovered portion (0.60% of the initial discounted pool balance) as a loss in our cash flow analysis.
- Similar to other recent VCL transactions we rated, the servicer will advance collections to cover potential commingling risk if our ratings on its parent company, Volkswagen Financial Services AG, fall below 'BBB'/'A-2' (or 'BBB+' in the absence of a short-term rating) or if we consider that the servicer is no longer deemed eligible under our counterparty criteria (see "Counterparty Risk Framework: Methodology And Assumptions," published on March 8, 2019). We deem that commingling risk is fully mitigated by this servicer advance mechanism.
- Given the sovereign rating on Germany (unsolicited; AAA/Stable/A-1+), our preliminary ratings in this transaction are not constrained by our structured finance sovereign risk criteria (see "Incorporating Sovereign Risk In Rating Structured Finance Securities: Methodology And Assumptions," published on Jan. 30, 2019).
- We expect the final documentation and the presented remedy provisions at closing to adequately mitigate counterparty risk in line with our counterparty criteria. We also expect that the final documentation will adequately address any operational risk in line with our operational risk criteria.

The Credit Story

Strengths, Concerns, And Mitigating Factors

Strengths	Concerns and mitigating factors
In our view, VW Leasing has a strong market position as one of the largest leasing companies in Europe, with more than 50 years' business experience.	Although historical net loss data provided by VW Leasing cover the period between 2011 to June 2022, it does not include any gross default or recoveries information. We have factored this into our analysis when deriving our credit and stress assumptions.
The preliminary pool is granular and diversified. As of Aug. 31, 2022, it comprised 79,660 lease contracts for a total of 65,226 lessees. The largest single lessee concentration is 0.24% and the top 20 lessees comprise just 1.34% of the pool's discounted principal balance.	The transaction's payment structure will not be fully sequential. Once certain target overcollateralization levels have been reached (and as long as certain performance triggers are met), the issuer will pay pro rata principal on the class A and B notes. We have stress-tested appropriate cash flows for each rating level, which included modeling the potential effect of the pro rata payment structure with a back-loaded loss curve.
As of the pool cut-off date, the pool did not contain any contracts with overdue payments.	The transaction will be exposed to commingling risk (as the pool collections are paid to the servicer's accounts before being transferred to the issuer), VAT risk (in accordance with section 13c of the German VAT Act), and German trade tax risk. A specific advance mechanism fully mitigates commingling risk, in our view. To mitigate the VAT and trade tax risks, the seller will fund at closing a nonamortizing seller risk reserve representing 1.10% of the initial discounted pool balance. In our view, the seller's risk reserve only partially mitigates these potential tax risks. Therefore, we stressed the uncovered portion (0.60% of the initial discounted pool balance) as an additional loss in our cash flows.
The portfolio will not revolve, so a shift in pool quality due to substitution cannot occur.	
The structure will benefit from a liquidity reserve, sized at 1.1% of the initial discounted pool balance, which will be fully funded at closing. The liquidity reserve will serve primarily as liquidity support to mitigate any cash strains. Ultimately, it is available to repay the notes at the end of the transaction's life.	

Changes From The Predecessor Transaction

- The buffer release mechanism has changed compared to that in VCL 35 and earlier rated transactions (see "Transaction Structure" below). Excess spread will now remain in the transaction if cumulative net losses exceed 1.6% or if the servicer becomes insolvent. Previously, the only potential trigger that would keep excess spread in the transaction was the servicer's insolvency. Given that the buffer rate release is linked to performance triggers, this is now modelled within the cash flows.
- VCL 37's cash reserve will be equal to the lower of (i) 1.1% of the initial outstanding discounted asset balance, and (ii) the class A and B notes' aggregate outstanding principal amount as of the relevant payment date. VCL 35's cash reserve amortized at 1.2% of the outstanding discounted asset balance, subject to a floor of 1.0% of the initial discounted pool balance.
- Under our updated global auto ABS criteria, we introduced a recovery framework that has an originator- and market-specific expected-case recovery rate and increasingly stressful

recovery rate haircuts at higher ratings (tiered recoveries). We apply a haircut of 36.5% and 32.0% on our base case recovery rate assumption of 60% on the 'AAA' and 'AA-' scenarios, respectively, to obtain stressed recovery rates of 38.1% and 40.8%. This compares to the stressed recovery rate of 38% that we applied at all rating levels in previously rated VCL transactions.

Environmental, Social, And Governance (ESG)

Our rating analysis considers a transaction's potential exposure to ESG credit factors. For the auto ABS sector, we view the exposure to environmental credit factors as above average, social credit factors as average, and governance credit factors as below average (see "ESG Industry Report Card: Auto Asset-Backed Securities," March 31, 2021). In our view, the exposure to ESG credit factors in this transaction is in line with our sector benchmark.

Environmental credit factors are generally viewed as above average given that the collateral pool primarily comprises vehicles with internal combustion engines (ICE), which create emissions of pollutants including greenhouse gases. While the adoption of electric vehicles and future regulation could in time lower ICE vehicle values, we believe that our current approach to evaluating recovery and residual values adequately accounts for vehicle values over the relatively short expected life of the transaction. As a result, we have not separately identified this as a material ESG credit factor in our analysis.

Asset Description

As of the cut-off date, the preliminary collateral pool backing the notes comprised 79,660 lease contracts for a total of 65,226 lessees with a total discounted principal balance of €750 million.

Table 1

Collateral Key Features*

Compartment of VCL Multi-Compartment S.A.	VCL Multi-Compartment S.A., Compartment VCL 37	VCL Multi-Compartment S.A., Compartment VCL 35	VCL Multi-Compartment S.A., Compartment VCL 32	VCL Multi-Compartment S.A., Compartment VCL 31	VCL Multi-Compartment S.A., Compartment VCL 30	VCL Multi-Compartment S.A., Compartment VCL 29
Originator	Volkswagen Leasing GmbH	Volkswagen Leasing GmbH	Volkswagen Leasing GmbH	Volkswagen Leasing GmbH	Volkswagen Leasing GmbH	Volkswagen Leasing GmbH
Country	Germany	Germany	Germany	Germany	Germany	Germany
Type of assets	Auto leases	Auto leases	Auto leases	Auto leases	Auto leases	Auto leases
Pool cut-off (date)	Aug. 31, 2022	Feb. 28, 2022	Feb. 28, 2021	Oct. 31, 2020	Feb. 28, 2020	Oct. 31, 2019
Closing date	Nov. 25, 2022	March 25, 2022	March 25, 2021	Nov. 25, 2020	March 25, 2020	Nov. 25, 2019
Pool volume (mil. €)	750	1,000	1,000	1,064	1,000	1,000
Number of receivables	79,660	118,391	123,724	130,378	109,798	107,487
Discount rate or weighted-average yield (%)	5.70	5.70	5.70	5.70	5.70	5.70
Buffer rate (%)	TBD	4.06	4.49	4.49	4.50	4.45

Table 1

Collateral Key Features* (cont.)

Compartment of VCL Multi-Compartment S.A.	VCL Multi-Compartment S.A., Compartment VCL 37	VCL Multi-Compartment S.A., Compartment VCL 35	VCL Multi-Compartment S.A., Compartment VCL 32	VCL Multi-Compartment S.A., Compartment VCL 31	VCL Multi-Compartment S.A., Compartment VCL 30	VCL Multi-Compartment S.A., Compartment VCL 29
Discount rate minus buffer release rate (%)	TBD	1.64	1.21	1.21	1.19	1.25
Weighted-average original term (months)	39.5	39.8	39.8	39.9	39.8	39.8
Weighted-average remaining term (months)	33.4	31.6	30.3	29.9	31.8	32.0
Weighted-average seasoning (months)	6.1	8.2	9.5	10.0	8.0	7.9
Contract type (%)						
Amortizing	100	100	100	100	100	100
Balloon	0	0	0	0	0	0
Vehicle status (%)						
New	93.6	90.9	91.9	90.8	92.7	94.6
Used and demonstration	6.4	9.1	8.9	9.2	7.3	5.4
Vehicle type (%)						
Car	100	100	100	100	100	100
Customer type (%)						
Private	23.1	23.3	21.1	19.8	13.1	11.5
Commercial	76.9	76.7	78.9	80.2	86.9	88.5
Engine type (%)						
Gasoline	32.2	28.7	31.8	34.7	31.8	30.1
Diesel	40.6	41.5	57.3	61.4	66.4	68.4
Electric	13.1	12.5	3.0	2.0	1.1	1.0
Hybrid	13.9	17.1	7.5	1.4	0.3	0.1
Other	0.1	0.2	0.4	0.4	0.4	0.4
Vehicle brand (%)						
Audi	28.2	30.0	33.1	31.8	31.7	32.4
Volkswagen	35.6	34.2	32.3	33.3	34.4	32.7
Volkswagen LCV (%)	10.2	10.4	11.9	12.6	12.9	14.3
Skoda (%)	14.4	15.9	14.9	14.3	13.8	13.3
Seat (%)	11.2	9.1	7.5	7.7	6.7	6.9
Geographic concentration (%)						
Top 1	22.2	22.9	22.6	22.6	22.3	22.5

Table 1

Collateral Key Features* (cont.)

Compartment of VCL Multi-Compartment S.A.	VCL Multi-Compartment S.A., Compartment VCL 37	VCL Multi-Compartment S.A., Compartment VCL 35	VCL Multi-Compartment S.A., Compartment VCL 32	VCL Multi-Compartment S.A., Compartment VCL 31	VCL Multi-Compartment S.A., Compartment VCL 30	VCL Multi-Compartment S.A., Compartment VCL 29
Top 2	17.9	17.2	17.0	17.2	17.6	17.5
Top 3	15.4	15.0	15.2	14.9	15.1	15.7

*Percentages are expressed as a percentage of the outstanding discounted principal balance. TBD--To be determined. N.A.--Not available. LCV--Light commercial vehicle.

Chart 1

Geographic Distribution

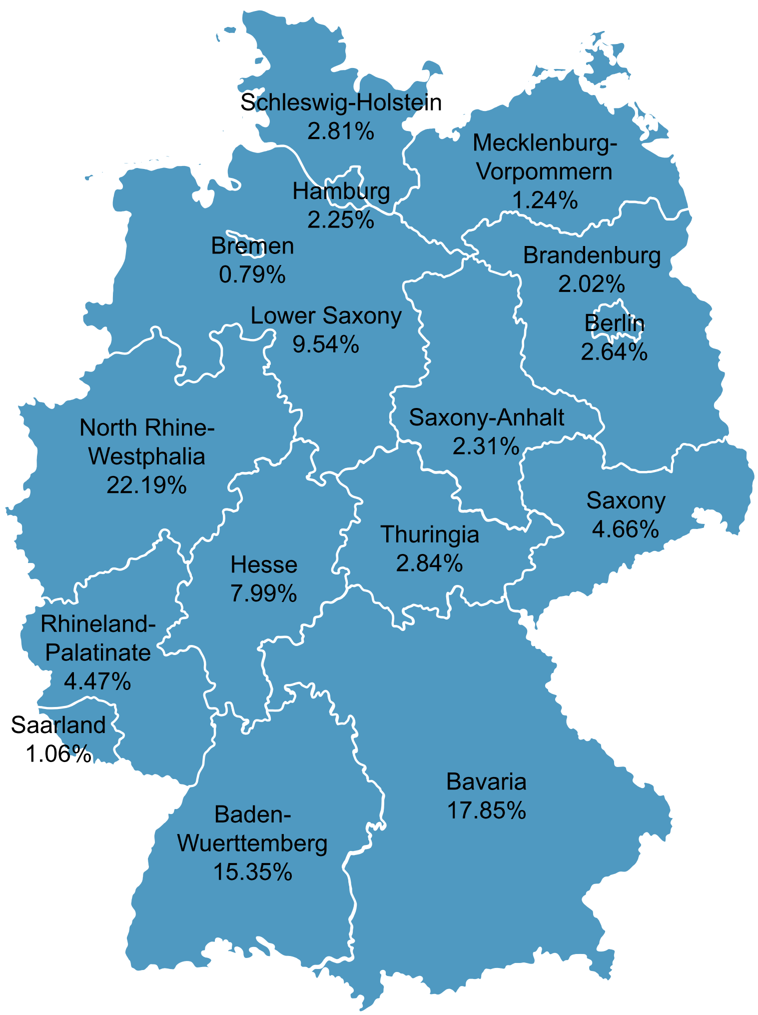
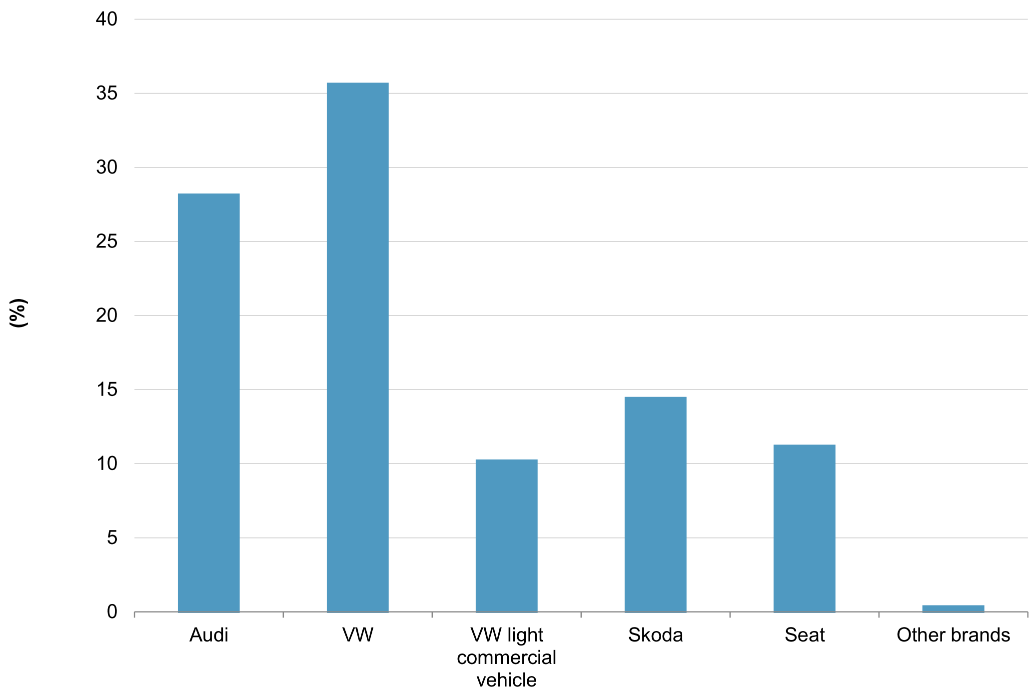


Chart 2

Pool Distribution By Brand



Eligibility Criteria

The transaction documents set out the eligibility criteria for receivables in the pool. Simplified, these state that:

- Contracts are legally valid and binding agreements and their enforceability is not impaired.
- Receivables are denominated and payable in euro.
- The leased vehicles are in Germany.
- The seller may freely dispose of the receivables.
- Receivables are free of defenses and from the rights of third parties. Lessees have no set-off claim.
- No receivable was overdue at the cut-off date.
- None of the lessees is an affiliate of Volkswagen AG, Family Porsche Stuttgart, or Family Piech Salzburg Group.
- Contracts are governed by the laws of Germany.
- Lessees have their registered office/place of residence in Germany.
- At least two lease instalments have been paid.
- Lease contracts require monthly payments to be made within 12 to 60 months after origination.

- The total amount of purchased lease receivables due from one and the same lessee does not exceed 0.50% of the initial aggregate discounted pool balance.
- Acquisition of the leased vehicles by VW Leasing is financed in compliance with the requirements of section 108 (I) sentence 2 of the German Insolvency Code ("Insolvenzordnung").
- The share of the discounted pool corresponding to non-VW group vehicle does not exceed 5%.
- None of the lessees has exercised their right of revocation, if any.

Nature of the leases

A lease contract comprises two elements. The first, typically the regular lease instalments, relates to the payments from the lessee covering the vehicle's value depreciation over the contract's duration. The second relates to the vehicle's residual value when the lease contract expires. VCL 37 will only purchase the regular lease instalments, and not the residual value. Furthermore, it will also purchase rights associated with the premature termination of a lease receivable or with the transfer of the lease receivable, plus rights to payments from the realization of vehicles. It will not buy rights to insurance premiums, any VAT payments, and the residual value element.

Commercial retail lessees typically have no contractual right to prepay the lease contract. If VW Leasing allows prepayment, it will pay the outstanding net present value of the future lease payments due to VCL 37, discounted at the rate at which the issuer initially purchased the receivables.

VCL 37 will purchase the lease receivables in this transaction from the VCL Master Compartment 1 securitization, where they have been warehoused. Furthermore, all of the corresponding residual values can be refinanced via the VCL Master Residual Value S.A. Compartment 2 securitization. The legal title over the leased vehicles is held by the trustee of VCL 37.

Originator/Seller

VW Leasing is a limited liability company and has underwritten auto leasing contracts in Germany since 1966. It is wholly owned by Volkswagen Financial Services AG, which in turn is a 100% subsidiary of Volkswagen AG. In the overall car financing market, VW Leasing is the leading captive car leasing provider in Germany. Its objectives are to lease motor vehicles and other movable assets from brands such as Volkswagen, Audi, SEAT, Skoda, and Volkswagen Nutzfahrzeuge vehicles, service-leasing to commercial and non-commercial customers, and leasing of used vehicles of all makes, including demonstration vehicles as used vehicles.

In our view, the company's track record of stable, strong quality asset origination is among the best of all European auto ABS issuers.

Servicing

We conducted a review of VW Leasing's origination, underwriting, collections, and risk management practices. We consider these to be in line with general market practice and our criteria for assessing operational risk (see "Related Criteria"). In our operational risk analysis, we look at the risk that cash flows may be disrupted following an operational failure of the servicer. Our preliminary 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 fulfil its role as servicer under the transaction documents. Our operational risk analysis do not impose any cap on the maximum achievable rating.

The transaction will not have a back-up servicer at closing. We rely on the general availability of servicing in the German market to mitigate the risk of servicing disruption and have applied a stressed servicing fee in our cash flow analysis, in line with market standards.

Credit Analysis and Assumptions

We analyzed the transaction's credit risk under various stress scenarios by applying our global auto ABS criteria (see "Related Criteria").

Economic outlook

In our base-case scenario for Germany, we forecast GDP growth of 1.5%, -0.3%, and 1.2%, in 2022, 2023, and 2024, respectively. Our baseline forecast was informed by our economic outlook for the Eurozone published on Sept. 26, 2022 (see "Related Research"). An unprecedented deterioration in the terms of trade has pushed inflation to record highs and confidence to record lows. Although, supporting the economy are still accommodative monetary policy, increasing fiscal support in response to the energy crisis, easing supply chain bottlenecks with large remaining production backlogs, and a growing population. What's more, the labor market, with employment at an all-time high, is unusually strong.

We expect inflation to be 8.4%, 7.0%, and 2.2% in 2022, 2023, and 2024, respectively. We set our credit assumptions to reflect our economic outlook for Germany.

Defaults

A written-off purchased lease receivable is one that has been reduced by recoveries and that VW Leasing has finally written off in its capacity as servicer in accordance with its customary accounting practice. The net loss definition used in the performance data is in line with the net loss definition used in the transaction documents.

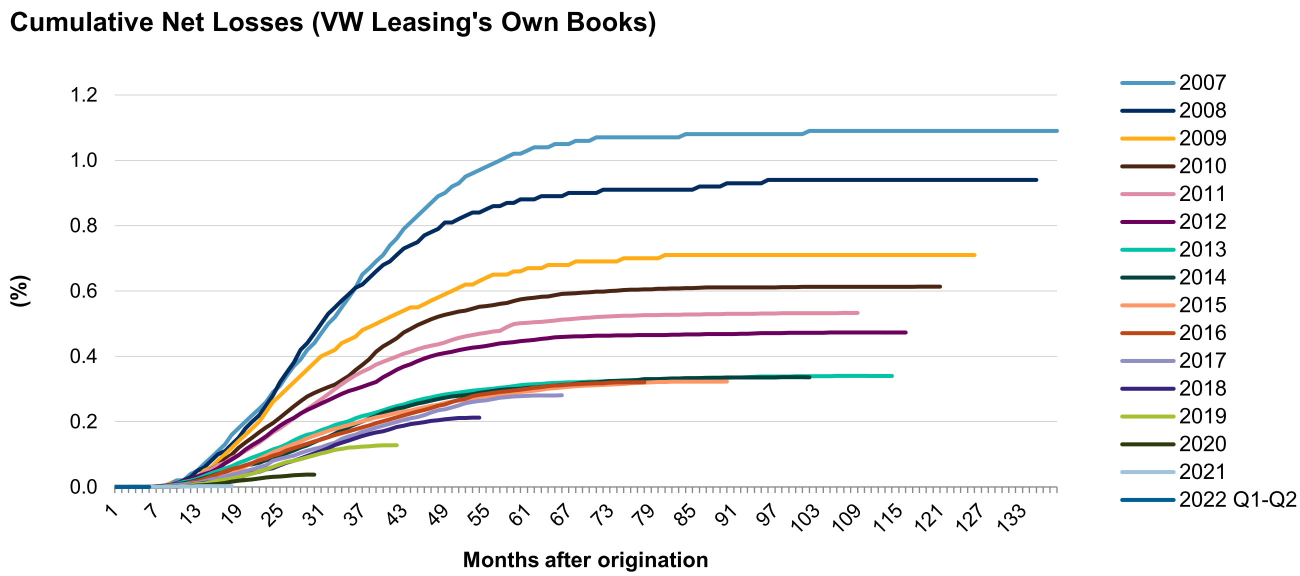
Cumulative net losses (VW Leasing's own books)

We received monthly static net loss data, showing cumulative net losses (i.e., actual write-offs after recoveries) as a percentage of VW Leasing's origination volume in its entire lease book. We received data from September 2011 to June 2022. The originator did not provide us with separate recovery or prepayment data. To arrive at a gross loss proxy, we "gross up" the net loss data, using a recovery rate assumption of 60%, which we derived from the historical recoveries of other VCL transactions.

We have also used the performance information available from the predecessor transactions (from January 2009). The quality of data provided is in line with our standards in relation to quality, timeliness, and reliability.

Performance in the originators' books has significantly improved between 2007 and 2017 and has stabilized at very low levels since then (see chart 3).

Chart 3



Based on the historical performance of receivables originated by VW Leasing and of the outstanding VCL transactions, we sized an average net loss of 0.80% for the pool. We then derived a gross loss assumption of 2.00% by assuming a 60% recovery rate. Although the book's and predecessor transactions' performance are very good, we did not decrease the base-case gross loss assumption as we expect German inflation to reach 8.4% in 2022 under our baseline forecast. Although elevated inflation is overall credit-negative for all borrowers, inevitably some borrowers will be more negatively affected than others. To the extent inflationary pressures materialize more quickly or more severely than we currently expect, risks may emerge.

Lessees in this transaction are paying a fixed rate. As a result, in the short to medium term borrowers are protected from rate rises but will face cost-of-living pressures. We consider the borrowers in the transaction to be prime and as such will generally have resilience to inflationary pressures.

At the same time, we maintained our base-case multiples of 4.3x and 3.0x for defaults at the 'AAA' and 'AA-' ratings, respectively, resulting in unchanged gross losses in these stress scenarios compared to VCL 35.

Recoveries and recovery timing

Under our global auto ABS criteria, we establish recovery rate assumptions based primarily on an analysis of historical recovery rates for the issuer and the market, the volatility of past performance, and credit, operational, or other factors that might affect the timing, amount, and sustainability of recovery rates. After considering all this information we set the base-case recovery rate at 60%.

For VCL 37, we sized stressed recoveries of 38.1% and 40.8% for the 'AAA' and 'AA-' ratings, respectively, based on recovery data provided for previous VCL transactions and a peer comparison with other German auto leasing transactions. VCL 37 comprises about 27% electric vehicles and hybrids, including about 13% of pure electric vehicles. Our recovery rate assumption incorporates the risk of lower vehicle realization values for these latter engine types. This is in line with VCL 35.

Table 2 summarizes our credit assumptions.

Table 2

Credit Assumption Summary

Rating level	Net loss base case (%)	Recovery rate (for gross up) (%)	Gross loss base case (%)	Multiple	Stressed cumulative default rate (%)	Recovery rate haircut	Stressed recovery rate (%)*	Stressed cumulative net losses (%)
AAA (sf)	0.80	60	2.00	4.30	8.60	36.5	38.1	5.32
AA- (sf)	0.80	60	2.00	2.97	5.93	32.0	40.8	3.51

*We assume that 100% of recoveries are realized nine months after default in our cash flow model.

Residual value risk

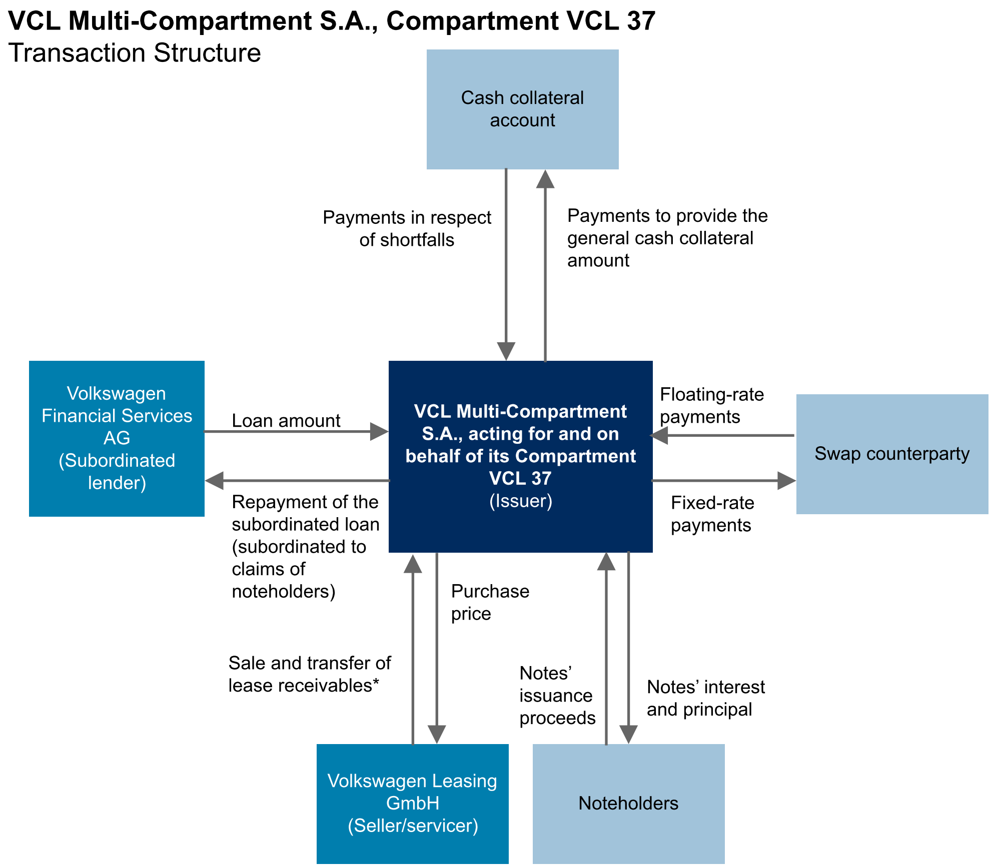
VCL 37 is not directly exposed to residual value risk as it has not purchased this type of receivables.

Transaction Structure

At closing, the issuer will buy a pool of auto lease receivables with a net present value of €750 million. The lease receivables will be discounted at a fixed rate of 5.7016%. However, the effective interest available to the issuer will be reduced in a way to leave no excess spread in the transaction, unless VW Leasing becomes insolvent or the cumulative net loss ratio exceeds 1.6% at any time. Therefore, interest receipts will be equal, in practice, to the sum of:

- Administrative expenses and a servicing fee;
- The weighted-average interest due to the swap counterparty under the terms of the swaps on the class A and B notes; and
- The interest due under the subordinated loan considering a hypothetical hedging of the latter.

Chart 4



*Currently held by VCL Master S.A. acting for and on behalf of its Compartment 1 pursuant to the receivables purchase agreement / distribution of collections.

The issuer is a Luxembourg special-purpose entity, which we consider to be bankruptcy remote under our legal criteria (see "Related Criteria"). We anticipate that the transaction legal opinion at closing will confirm that the sale of the assets would survive the seller's insolvency.

Cash Flow Mechanics

Priority of payments

The class A and B notes will pay interest in arrears on a designated date each month, at the Euro interbank offered rate (EURIBOR) plus a respective margin. The first interest payment date (IPD) will be on Dec. 21, 2022, and the legal final maturity of the notes will be in September 2028.

On each monthly IPD, the issuer will apply to the priority of payments any asset collections (less the buffer release amount), net swap receipts, and amounts drawn from the cash reserve from the previous month, in the order outlined in table 3.

Table 3

Priority Of Payments (Simplified)

1	Taxes and payments to the trustee.
2	Senior fees, including payments to the corporate services provider, data protection trustee, and servicer.
3	Payments to the account bank. Payments to the swap counterparty (except termination payments if the swap counterparty is the defaulting party).
4	Interest on the class A notes.
5	Interest on the class B notes.
6	Top-up cash reserve (only if drawn upon previously).
7	Class A notes' principal (sequential or pro rata).
8	Class B notes' principal (sequential or pro rata).
9	Payments to the swap counterparty not paid above.
10	Interest on the subordinated loan.
11	Principal on the subordinated loan.
12	Final success fee to VW Leasing.

Repayment of the notes

From closing, the issuer will redeem the notes sequentially until it reaches the target overcollateralization levels for the class A and B notes. Once the target overcollateralization levels have been reached, the transaction will switch to pro rata pay-down. Moreover, the transaction will switch back to sequential pay-down if there is a credit enhancement increase condition level 1 or level 2, or if the servicer becomes insolvent (see table 4).

The target overcollateralization levels would increase if one of the following performance triggers is breached:

- Trigger level 1: The cumulative net loss ratio exceeds 0.50% before or during February 2024 or 1.15% between February 2024 (exclusive) and November 2024; or
- Trigger level 2: The cumulative net loss ratio exceeds 1.6% at any time.

Table 4

Overcollateralization Levels

	Actual overcollateralization (%)	Target overcollateralization levels (%)		
	At closing	No trigger breach	Trigger level 1 breached	Trigger level 2 breached
Class A	5.49	12.25	14.00	100.00
Class B	3.48	7.50	8.25	100.00

Event of default

If interest on the most senior notes outstanding is not paid timely or principal is not fully paid by the legal maturity, the noteholders or the trustee can call an event of default. This could lead to multiple events, such as the swap terminating (with the issuer needing to make termination payments), and the post-enforcement priority of payments being applied. However, we consider these events as ratings remote, and as such, we do not model the post-enforcement priority of payments in our analysis. If the trustee were to call an event of default, it could affect the transaction's cash flows.

Cash reserve

The issuer will deposit 1.1% of the initial discounted asset balance as a general cash reserve at closing. Amounts deposited in the general cash reserve account will be available to bridge any liquidity shortfalls in the payment of senior costs and expenses, and interest on the class A and B notes. On the scheduled maturity date, the issuer can also use the cash reserve to redeem the class A and B notes.

Funds in this account can only be invested in cash. After all the lease receivables and notes have been repaid, VW Leasing is entitled to any outstanding balance in the cash collateral account.

Excess spread

There is initially no excess spread in the transaction. All receivables are discounted using a rate equal to 5.7016%. VW Leasing calculated this number for VCL Master Compartment 1 in order to cover swap, interest and costs, and a buffer in case of increased interest cost for the warehouse facility prior to the subsequent sale to VCL 37. The difference between the 5.7016% discount rate and total interest (i.e., swap payments) and senior costs for this transaction is taken out of the available distribution amount prior to applying the waterfall sequence. Following the servicer insolvency or if the cumulative net loss ratio exceeds 1.6% at any time, the buffer component will not be released, and it will be considered as cash available to the issuer.

Fixed-to-floating interest rate swaps

At closing the issuer will also enter into fixed-to-floating interest rate swap agreements with a swap counterparty to hedge the risk between the assets' fixed-rate interest and the notes' floating-rate interest for the class A and B notes. Under the swap agreements the issuer pays a fixed rate on the class A and B notes' agreements. The swap counterparty pays one-month EURIBOR plus a class-specific margin. The notional in both contracts is the class A and B outstanding note balance, respectively.

Mitigation Of Seller Risks

Commingling risk

An advance mechanism will be applied to address the servicer commingling risk if our issuer credit rating on Volkswagen Financial Services falls below 'BBB'/'A-2' (or 'BBB+' if no short-term rating is available) or if we consider that the servicer is no longer deemed eligible under our counterparty criteria. We deem that commingling risk is fully mitigated by this servicer advance mechanism.

Setoff risk

The transaction's eligibility criteria for the pool exclude leases granted to VW employees, thereby mitigating employee setoff risk. We also do not believe any setoff would arise from lessee deposits, insurance, or maintenance/servicing agreements. Lastly, we are not currently aware of any setoff claims that have arisen due to vehicle defects. As part of our ongoing surveillance of the transaction, we will monitor any potential setoff that could arise because of vehicle recalls, and consider the mitigating factors available at that time to determine any potential ratings impact.

Tax risks

Similar to VCL 35, seller-related risks (German trade tax risks, and VAT risks) are mitigated by a nonamortizing seller risk reserve (1.10% of the initial discounted pool balance), which VW Leasing will fund at closing. In our view, the seller risk reserve only partially mitigates the potential German trade tax risk and VAT risks. Therefore, we have considered the uncovered portion (0.60% of the initial discounted pool balance) as a loss in our cash flow analysis.

Cash Flow Assumptions

In our cash flow modeling of this transaction, we applied stressed losses equally over the asset portfolio's weighted-average life (17 months). We also ran a back-loaded loss curve to test the impact of the pro rata pay-down mechanism on the available credit enhancement. We stressed the prepayment rates and ran different interest rate scenarios (stressed interest rate curve [up, down, up/down, down/up]). The model incorporates the notes' potential pro rata amortization, and the cash reserve's amortizing features. We did not model commingling losses because we consider that the advance mechanism will fully mitigate these losses. We also modeled tax losses amounting to 0.60% of the portfolio's initial discounted value because we consider that the seller risk reserve only partially mitigates the related risks. In addition, we modeled the cash credit enhancement's erosion due to negative interest rate scenarios.

Table 5

Cash Flow Assumptions

Recession start	At closing
Length of recession	WAL (17 months)
Cumulative gross loss curve 1	Evenly distributed over WAL
Cumulative gross loss curve 2	Back loaded
Recovery lag	9 months
Delinquency	Two-thirds of credit losses recovered six months later
Stressed servicing fees (%)	1.03
Fixed fees (£)	100,000
Replacement bank cost	80,000
Prepayments (high/low)(%)	16.0/0.5
Interest rate	Stressed interest rate curve (up, down, up/down, down/up)
Initial WAC (%)	TBD
Relative WAC compression (%)	N/A as purchased at discount

Table 5

Cash Flow Assumptions (cont.)

Commingling stress	None, mitigated through servicer advances subject to rating triggers.

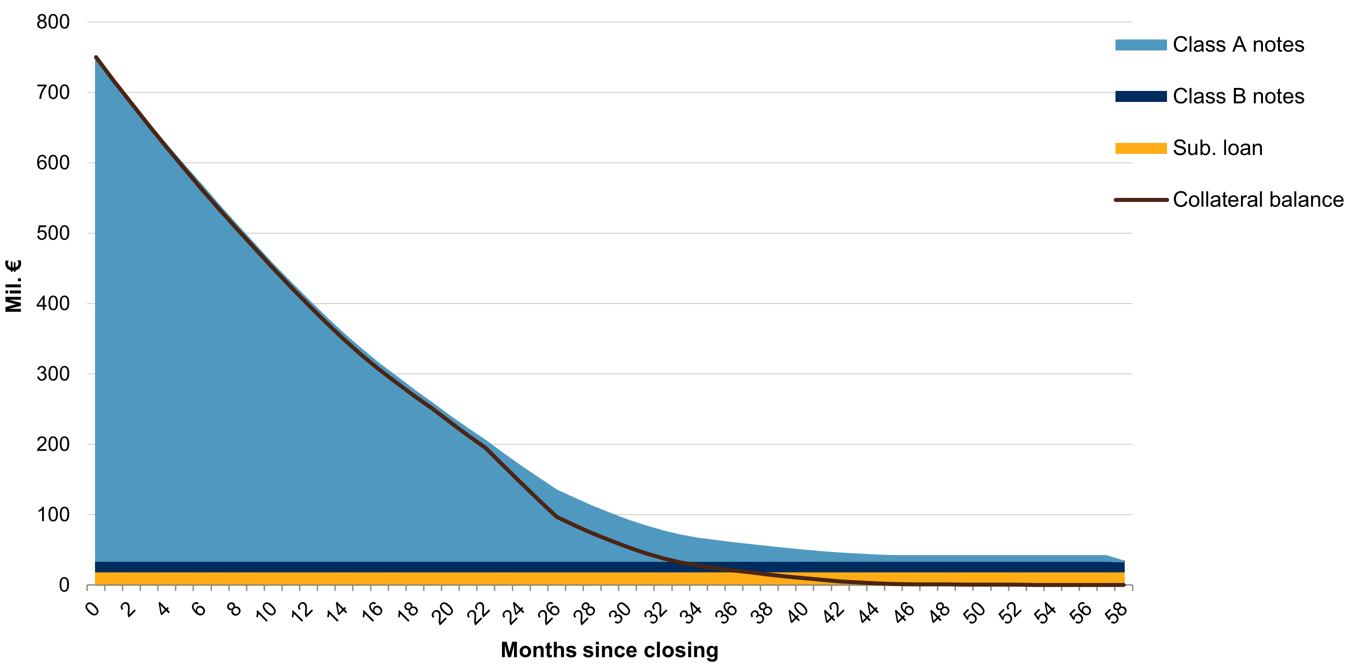
WAL--Weighted average life. WAC--Weighted average coupon. TBD--To be determined. N/A--Not applicable.

The ratings scenarios address not only the availability of funds for full payment of interest and principal, but also the timeliness of these payments in accordance with the terms of the rated securities.

Chart 5 below shows the collateral and the note amortization profile under our most stressful scenario.

Chart 5

Collateral And Note Balances (End Of Period) In A 'AAA' Rating Scenario



Counterparty Risk

Our preliminary ratings also reflect that the replacement mechanisms to be implemented in the transaction documents will adequately mitigate the counterparty risks to which the transaction is exposed. We expect the final documentation and the presented remedy provisions at closing to adequately mitigate counterparty risk in line with our counterparty criteria.

Table 6

Supporting Ratings

Institution/role	Ratings	Replacement trigger	Collateral posting trigger
The Bank of New York Mellon, Frankfurt Branch as the transaction accounts provider*	ICR: AA-/Stable/A-1+	A/A-1 (or 'A+' if no short-term rating available)	N/A
Interest rate swap counterparty	TBD	TBD	TBD

*After application of our bank branch criteria and considering the ratings on the parent company. ICR--Issuer credit rating. N/A--Not applicable. TBD--To be determined.

Sovereign Risk

Our long-term unsolicited sovereign rating on Germany is 'AAA'. Therefore, our preliminary ratings in this transaction are not constrained by our structured finance sovereign risk criteria.

Scenario Analysis

We analyzed the effect of a moderate stress on the credit variables (recovery rates and prepayment rates) and its ultimate effect on our ratings on the notes. We ran two scenarios to test the rating's stability, and the results are in line with our credit stability criteria (see tables 7 and 8).

Table 7

Scenario Stresses

12-month stress horizon			
Rating variable	Base case	Scenario 1	Scenario 2
Gross loss rate (%)	2.00	2.00	2.00
Stressed recovery rate ('AAA'; %)	38.10	30.24	21.60
Stressed recovery rate ('AA-'; %)	40.80	35.04	25.02
Constant prepayment rate (%)	8.00	6.40	5.30

Table 8

Scenario Stress Analysis: Rating Transition Results

Scenario stress	Class	Initial rating	Scenario stress rating
Scenario 1	A	AAA (sf)	AA+ (sf)
	B	AA- (sf)	A+ (sf)
Scenario 2	A	AAA (sf)	AA- (sf)
	B	AA- (sf)	A- (sf)

As part of our analysis we also conducted additional sensitivity analysis to assess the impact of, all else being equal, an increased gross default base case and a haircut to the recovery rate base case, on our ratings on the notes. For this purpose, we ran eight sensitivity runs by either increasing stressed defaults and/or reducing expected recoveries as shown in the tables below.

The results of the above sensitivity analysis indicate a deterioration of no more than two notches on the notes (see table 9).

Table 9

Sensitivity Analysis

	Recovery rate base case (%)		
Gross default rate base case (%)	**0%**	**(10%)**	**(25%)**
0%	Base run	3	4
10%	1	5	7
25%	2	6	8

Table 10

Sensitivity Analysis Results

	Standard run	1	2	3	4	5	6	7	8
Gross loss base case (%)	2.0	2.2	2.5	2.0	2.0	2.2	2.5	2.2	2.5
Recovery rate base case (%)	60.0	60.0	60.0	54.0	45.0	54.0	54.0	45.0	45.0
A	AAA	AA+	AA	AA+	AA+	AA+	AA	AA	AA-
B	AA-	A+	A	A+	A	A	A	A	A-

Monitoring And Surveillance

As part of our ongoing surveillance of this transaction, we will regularly assess:

- The performance of the underlying pool, including defaults, delinquencies, and prepayments;
- The supporting ratings in the transaction; and
- The servicer's operations and its ability to maintain minimum servicing standards.

Appendix

Transaction Participants

Seller and servicer	Volkswagen Leasing GmbH
Arranger	Skandinaviska Enskilda Banken AB
Lead managers	Skandinaviska Enskilda Banken AB, MUFG Securities (Europe)N.V., and Société Générale
Security trustee	Intertrust Trustees GmbH
Expectancy rights trustee	Wilmington Trust (London) Ltd.
Corporate services provider	Circumference FS (Luxembourg) S.A.
Bank account provider and cash administrator	The Bank of New York Mellon, Frankfurt Branch
Principal paying agent, calculation agent, and interest determination agent	The Bank of New York Mellon, London Branch

Transaction Participants (cont.)

Data protection trustee	Data Custody Agent Services B.V.
Registrar	The Bank of New York Mellon SA/NV, Luxembourg Branch
Swap counterparties	To be determined

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: Principles Of Credit Ratings, Feb. 16, 2011
- Criteria | Structured Finance | General: Methodology For Servicer Risk Assessment, May 28, 2009

Related Research

- Economic Outlook Eurozone Q4 2022: Crunch Time, Sept. 26, 2022
- European Auto ABS Index Report Q2 2022, Aug. 2, 2022
- Credit Conditions Europe Q3 2022: Pain On The Horizon, June 28, 2022
- Germany 'AAA/A-1+' Ratings Affirmed; Outlook Stable, March 25, 2022
- S&P Global Ratings Definitions, Nov. 10, 2021
- ESG Industry Report Card: Auto Asset-Backed Securities, March 31, 2021
- How Much Is Enough? Information Quality Standards For The EMEA RMBS And ABS Rating

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- 2017 EMEA ABS Scenario And Sensitivity Analysis, July 6, 2017
- Global Structured Finance Scenario And Sensitivity Analysis 2016: The Effects Of The Top Five Macroeconomic Factors, Dec. 16, 2016
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- Scenario Analysis: Gross Default Rates And Excess Spread Hold The Answer To Future European Auto ABS Performance, May 12, 2009