MOODY'S
INVESTORS SERVICE

# Rating Action: Moody's assigns Aaa (sf) to new notes in Driver UK Master S.A., Compartment 2 Auto ABS

25 Nov 2020

**GBP 150 million ABS Notes newly rated, relating to a portfolio of UK auto leases**

London, 25 November 2020 -- Moody's Investors Service ("Moody's") has assigned the following definitive rating to Notes issued by Driver UK Master S.A., acting for its Compartment 2:

....GBP 150.0M Class A Series 2020-1 Floating Rate Asset Backed Notes due November 2028, Assigned Aaa (sf)

Moody's has not assigned a rating to the GBP 275.9M Class A Series 2020-2 Floating Rate Asset Backed Notes due November 2028.

Moody's also affirms the existing ratings of Class A Notes issued by Driver UK Master S.A., Compartment 2:

....GBP 405.0M Class A Series 2013-2 Notes, Affirmed Aaa (sf); previously on May 28, 2019 Affirmed Aaa (sf)

....GBP 200.0M Class A Series 2013-4 Notes, Affirmed Aaa (sf); previously on May 28, 2019 Affirmed Aaa (sf)

....GBP 225.0M Class A Series 2013-8 Notes, Affirmed Aaa (sf); previously on May 28, 2019 Affirmed Aaa (sf)

....GBP 100.0M Class A Series 2014-1 Notes, Affirmed Aaa (sf); previously on May 28, 2019 Affirmed Aaa (sf)

....GBP 200.0M Class A Series 2014-2 Notes, Affirmed Aaa (sf); previously on May 28, 2019 Affirmed Aaa (sf)

....GBP 389.7M Class A Series 2014-3 Notes, Affirmed Aaa (sf); previously on May 28, 2019 Affirmed Aaa (sf)

....GBP 444.5M Class A Series 2015-1 Notes, Affirmed Aaa (sf); previously on May 28, 2019 Affirmed Aaa (sf)

....GBP 375.0M Class A Series 2016-2 Notes, Affirmed Aaa (sf); previously on May 28, 2019 Affirmed Aaa (sf)

....GBP 222.3M Class A Series 2018-1 Notes, Affirmed Aaa (sf); previously on May 28, 2019 Affirmed Aaa (sf)

....GBP 171.6M Class A Series 2018-2 Notes, Affirmed Aaa (sf); previously on May 28, 2019 Affirmed Aaa (sf)

....GBP 63.5M Class A Series 2018-3 Notes, Affirmed Aaa (sf); previously on May 28, 2019 Affirmed Aaa (sf)

....GBP 250.0M Class A Series 2019-1 Notes, Affirmed Aaa (sf); previously on May 28, 2019 Assigned Aaa (sf)

....GBP 200.0M Class A Series 2019-2 Notes, Affirmed Aaa (sf); previously on May 28, 2019 Assigned Aaa (sf)

Moody's has also affirmed the existing ratings of Class B Notes issued by Driver UK Master S.A., Compartment 2:

....GBP 140.6M Class B Series 2013-3 Notes, Affirmed Aa3 (sf); previously on May 28, 2019 Upgraded to Aa3 (sf)

....GBP 180.5M Class B Series 2015-1 Notes, Affirmed Aa3 (sf); previously on May 28, 2019 Upgraded to Aa3 (sf)

....GBP 48.5M Class B Series 2016-2 Notes, Affirmed Aa3 (sf); previously on May 28, 2019 Upgraded to Aa3 (sf)

....GBP 27.7M Class B Series 2018-1 Notes, Affirmed Aa3 (sf); previously on May 28, 2019 Upgraded to Aa3 (sf)

....GBP 88.4M Class B Series 2018-2 Notes, Affirmed Aa3 (sf); previously on May 28, 2019 Upgraded to Aa3

(sf)

....GBP 20.0M Class B Series 2018-3 Notes, Affirmed Aa3 (sf); previously on May 28, 2019 Upgraded to Aa3 (sf)

RATINGS RATIONALE

The transaction is a revolving cash securitisation of hire purchase receivables and PCP receivables with related residual value cash flows extended by Volkswagen Financial Services (UK) Limited ("VWFS UK") (not rated) (fully owned by Volkswagen Financial Services AG (A3/P-2) to obligors located in the UK. The revolving period ends in November 2021.

The portfolio of underlying assets consists of auto financing agreements distributed through auto dealers in the UK and will have a total amount of approximately GBP 5,923M.

As of October 2020, the pool cut shows 384,936 contracts with a weighted average seasoning of 18.9 months. The portfolio is collateralised by approximately 62% new cars and 38% used cars, and the vast majority of the financed vehicles are VW brands. Personal contract purchase ("PCP") agreements constitute approximately 94.2% and hire purchase agreements approximately 5.8% of the portfolio.

The ratings are primarily based on the credit quality of the portfolio, the structural features of the transaction and its legal integrity.

According to Moody's, the transaction benefits from credit strengths such as (i) the granularity of the portfolio; (ii) financial strength and securitisation experience of the originator; and (iii) high credit enhancement levels. However, Moody's notes that the transaction features some credit challenges such as residual value risk, a high degree of linkage to VWFS UK and commingling risk.

The revolving master structure allows for flexibility which could change the credit enhancement levels. This flexibility includes (i) the increase of the Notes' balances of existing series to the maximum issuance amounts; (ii) the issuance of additional series of Notes; and (iii) the take-out of assets in order to securitize them in the form of a term transaction ("term take-out").

Various mitigants have been put in place in the transaction structure, such as early amortization triggers, performance related triggers to switch to sequential amortization, eligibility criteria and provisions to ensure that the transaction is not negatively affected by the execution of the flexibility outlined above. Furthermore, rating triggers will provide additional reserves in case of a trigger breach. Collections are commingled at the collection account during monthly collection periods. The resulting commingling risk is partially mitigated by (i) the current rating of the servicer's ultimate parent Volkswagen Financial Services AG; (ii) cash advances upon a downgrade of Volkswagen Financial Services AG; and (iii) borrower notification to pay into the issuer account upon servicer insolvency.

Moody's analysis focused, amongst other factors, on (i) an evaluation of the underlying portfolio of receivables; (ii) historical performance on defaults and recoveries from Q3 2002 to Q2 2020; (iii) the credit enhancement provided by subordination and cash reserve; (iv) the liquidity support available in the transaction by way of the cash fund, principal to pay interest, and excess spread; and (v) the legal and structural aspects of the transaction.

PCP Handbacks: PCP agreements include a final balloon payment and permit obligors to return their vehicle at the end of the contract in lieu of final payment ("PCP Handbacks"). Therefore, portfolio cash flows result from fixed periodic instalment cash flows (approx. 40%) and residual value cash flows at the end of the PCP agreement (approx. 60%). There is no guarantee that actual RV cash flows will match the expectation, since such cash flows are by their nature subject to market value fluctuations. However, the transaction includes a commitment from the originator to repurchase receivables which have been subject to PCP Handback. This should substantially cover losses arising from lower residual values as long as VWFS UK continues to be solvent and able to execute these repurchases (see "Residual value risk credit enhancement ("RV CE") ").

Voluntary Terminations: Both HP and PCP agreements may be subject to voluntary termination ("VT") pursuant to the Consumer Credit Act. The lessee may, pursuant to section 99 of the CCA, terminate the relevant underlying contract and return the vehicle to the originator if the obligor has made payments equal to at least one half of the total amount which is payable for the good (including any deposit). VTs leave the lessor with the residual value (RV) risk of the vehicle.

The risk of losses from VTs is partially reduced in this transaction through a repurchase commitment by VWFS UK, which will repurchase receivables subject to voluntary terminations at their outstanding principal balance (together with any arrears outstanding). This feature should mitigate losses in a base case scenario where VWFS UK continues to be solvent and able to execute these repurchases. We have given credit to this feature in our expected net loss rate assumption (See "MAIN MODEL ASSUMPTIONS").

Moody's determined the portfolio lifetime mean loss rate ("expected loss") of 1.25% and Aaa portfolio credit enhancement ("PCE") of 8.5% related to borrower receivables. The mean loss rate captures our expectations of performance considering the current economic outlook, while the PCE captures the loss we expect the portfolio to suffer in the event of a severe recession scenario. Mean loss and PCE are parameters used by Moody's to calibrate its lognormal portfolio loss distribution curve and to associate a probability with each potential future loss scenario in its ABSROM cash flow model to rate Auto ABS.

The expected loss of 1.25% is lower than the EMEA Auto ABS average and is based on Moody's assessment of the lifetime expectation for the pool taking into account (i) historic performance of the book of the originator, (ii) benchmark transactions, and (iii) other qualitative considerations, such as the high balloon component of the portfolio.

The PCE of 8.5% is lower than the EMEA Auto ABS average and is based on Moody's assessment of the pool which is mainly driven by: (i) the exposure to balloon payments despite considering the strength of the originator, (ii) the relative ranking to originator peers in the EMEA market.

RESIDUAL VALUE RISK CREDIT ENHANCEMENT ("RV CE")

Moody's determined the Aaa RV CE of 17.6% and the Aa3 RV CE of 13.5% to account for the residual value market risk. RV CE captures additional portfolio losses which would arise on the securitised RV cash flows following a decline in the market prices of used cars in a severe recession environment. The pool contains lease agreements which permit the lessee to return their vehicle at the end of the lease in lieu of the final payment, which is not a default and thus is not captured in the loss assumptions for the lease receivables described in the previous section. The sum of the RV CE and PCE, as described above, determines the total credit enhancement that is needed to be consistent with the rating for each Class of notes.

In deriving the RV CE Moody's assumes a haircut on the securitised RV receivables of 34% for the Aaa (sf) rated Notes and 26% for the Aa3 (sf) rated Notes taking into account (i) robustness of RV setting; (ii) good track record of car sales; and (iii) comparatively low diversification of brands in the RV portfolio.

In accordance with the methodology Appendix 8, step 5, the Class B Notes benefit from a reduction in RV CE as a result of a repurchase agreement from the originator, whereby VWFS UK will repurchase receivables that have been subject to PCP Handbacks. The benefit attributed to this feature results in a 10% reduction to the Aa3 RV CE and no reduction in Aaa RV CE (see Exhibit 8-5 of the methodology).

CURRENT ECONOMIC UNCERTAINTY

The coronavirus outbreak, the government measures put in place to contain it, and the weak global economic outlook continue to disrupt economies and credit markets across sectors and regions. Our analysis has considered the effect on the performance of consumer assets from the current weak UK economic activity and a gradual recovery for the coming months. Although an economic recovery is underway, it is tenuous and its continuation will be closely tied to containment of the virus. As a result, the degree of uncertainty around our forecasts is unusually high.

We regard the coronavirus outbreak as a social risk under our ESG framework, given the substantial implications for public health and safety.

The principal methodology used in these ratings was 'Moody's Global Approach to Rating Auto Loan- and Lease-Backed ABS' published in July 2020 and available at https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBS_1236186 . Alternatively, please see the Rating Methodologies page on www.moodys.com for a copy of this methodology.

FACTORS THAT WOULD LEAD TO AN UPGRADE OR DOWNGRADE OF THE RATINGS:

Factors that may cause an upgrade of the ratings of the Class B Notes include significantly better than expected performance of the pool together with an increase in credit enhancement of Notes.

Factors that may cause a downgrade of the ratings of the notes include a worsening in the overall performance of the pool, or a meaningful deterioration of the credit profile of the servicers or sponsor.

REGULATORY DISCLOSURES

For further specification of Moody's key rating assumptions and sensitivity analysis, see the sections Methodology Assumptions and Sensitivity to Assumptions in the disclosure form. Moody's Rating Symbols and Definitions can be found at: https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_79004.

The analysis relies on an assessment of collateral characteristics to determine the collateral loss distribution, that is, the function that correlates to an assumption about the likelihood of occurrence to each level of possible losses in the collateral. As a second step, Moody's evaluates each possible collateral loss scenario using a model that replicates the relevant structural features to derive payments and therefore the ultimate potential losses for each rated instrument. The loss a rated instrument incurs in each collateral loss scenario, weighted by assumptions about the likelihood of events in that scenario occurring, results in the expected loss of the rated instrument.

Moody's quantitative analysis entails an evaluation of scenarios that stress factors contributing to sensitivity of ratings and take into account the likelihood of severe collateral losses or impaired cash flows. Moody's weights the impact on the rated instruments based on its assumptions of the likelihood of the events in such scenarios occurring.

For ratings issued on a program, series, category/class of debt or security this announcement provides certain regulatory disclosures in relation to each rating of a subsequently issued bond or note of the same series, category/class of debt, security or pursuant to a program for which the ratings are derived exclusively from existing ratings in accordance with Moody's rating practices. For ratings issued on a support provider, this announcement provides certain regulatory disclosures in relation to the credit rating action on the support provider and in relation to each particular credit rating action for securities that derive their credit ratings from the support provider's credit rating. For provisional ratings, this announcement provides certain regulatory disclosures in relation to the provisional rating assigned, and in relation to a definitive rating that may be assigned subsequent to the final issuance of the debt, in each case where the transaction structure and terms have not changed prior to the assignment of the definitive rating in a manner that would have affected the rating. For further information please see the ratings tab on the issuer/entity page for the respective issuer on www.moodys.com.

For any affected securities or rated entities receiving direct credit support from the primary entity(ies) of this credit rating action, and whose ratings may change as a result of this credit rating action, the associated regulatory disclosures will be those of the guarantor entity. Exceptions to this approach exist for the following disclosures, if applicable to jurisdiction: Ancillary Services, Disclosure to rated entity, Disclosure from rated entity.

The ratings have been disclosed to the rated entity or its designated agent(s) and issued with no amendment resulting from that disclosure.

These ratings are solicited. Please refer to Moody's Policy for Designating and Assigning Unsolicited Credit Ratings available on its website www.moodys.com.

Regulatory disclosures contained in this press release apply to the credit rating and, if applicable, the related rating outlook or rating review.

Moody's general principles for assessing environmental, social and governance (ESG) risks in our credit analysis can be found at https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_1133569 .

At least one ESG consideration was material to the credit rating action(s) announced and described above.

Please see www.moodys.com for any updates on changes to the lead rating analyst and to the Moody's legal entity that has issued the rating.

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