

Rankings Raised To STRONG On Zenith Service As Master Servicer In Italy; Outlook Stable

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OVERVIEW

- We have raised to STRONG our overall rankings on Zenith Service SpA as a master servicer of residential mortgages, commercial loans, and unsecured credits in Italy.
- Our outlook on the rankings is stable.
- Established in 1999 and registered under Article 106 of the Italian Banking Act, we have ranked Zenith as a master servicer since 2004.

LONDON (S&P Global Ratings) April 10, 2017--S&P Global Ratings has today raised to STRONG its overall rankings on Zenith Service SpA as a master servicer of residential mortgages, commercial loans, and unsecured credits in Italy. At the same time, we revised our outlook on the rankings to stable.

Zenith was established as an independent company in November 1999. Registered under Article 106 of the Italian Banking Act, it is subject to the Bank of Italy (BOI) surveillance activity. It has a head office in Milan and a second office in Rome. From these, it manages and oversees securitized and non-securitized loan portfolios as a servicer. It also performs different roles, such as corporate and calculation agent, back-up servicer, and representative of noteholders. We have ranked Zenith on its activity as a master servicer since 2004.

In December 2016, Arrow Global Group--which is listed on the London Stock Exchange and is active in Europe as a debt purchaser and manager--announced its intention to acquire control of Zenith and enter the Italian servicing market. We expect the sale to be finalized during the first half of this year, following BOI's approval. According to Arrow's announcement, Arrow will retain Zenith's management team and existing service offering but, as part of its wider Italian strategy, plans to pursue a broader client offering.

In 2016, Zenith's master servicing portfolio almost doubled, expanding to €14.8 billion at year end from €8.7 billion at year end 2015. Most of the growth took place in non-real-estate-related business, an asset class which grew to €13.5 billion from €7.6 billion during 2016. Zenith's client base increased to 113 from 87 and it also grew in other areas. At year-end 2016, it performed a corporate servicer role for 135 transactions, up from 114 at year end 2015, and it was the calculation agent in 73 transactions, up from 55, for example. Although other business lines are outside the scope of our review, we do assess how they affect the company's master servicing activity.

In line with its business growth, Zenith hired 33 new staff in 2016, including five in the master servicing team (now composed of 16 members). It had 82 employees at the end of 2016, up from 57 at the beginning of the same year.

Our STRONG rankings reflect our assessment of the company's operations as a master servicer of residential mortgages, commercial loans, and unsecured credits in Italy, based on the major ranking factors in our criteria (see "Related Criteria").

MAJOR RANKING FACTORS

- Zenith succeeded in raising its visibility in the market by proactively proposing its offer to international investors and national counterparties. As a result, the company has registered a steady growth in its overall and master servicing activity over the past five years. Although a period of such intense growth could represent a risk, Zenith is well-positioned to smoothly absorb rising activity, in our view. The company has been planning and investing for expansion, by updating its information technology (IT) platform, expanding its management team, and enhancing its processes.
- Zenith's executive management team is well-established. The organization has strengthened its leadership team over the past 12 months by recruiting further senior resources that have relevant experience in similar roles. Finally, according to Arrow's announcement, Zenith's new ownership should be supportive of governance and operations' continuity and guarantee the stability of staff and processes.
- In our opinion, the company has structured the people management function in line with its current size. In early 2017, Zenith appointed as head of human resources an external consultant who had worked with the company for the past decade. In 2016, Zenith redesigned its benefits scheme to include the full workforce and provide better incentives to each

employee. Although it does not set a threshold for mandatory training, it provided almost 55 relevant training courses in 2016, excluding English courses or similar. Over the past two years, the company has run an extensive training program dedicated to senior and middle management. Finally, Zenith plans to run a morale survey right after the sale.

- Two resources manage internal controls, both independent from the operative management team and reporting to the board. Since our last review, the risk officer has fulfilled the compliance officer role, which was formerly a part of the auditor's responsibility. This separation better reflects the principles of the "three lines of defense" model that Zenith applies. Under this model, risk and compliance are identified as part of the same level of controls.
- The company relies on sound workflows supported by an automated IT system that is continuously improved through annual IT investment of about 10% of revenues. The servicer reviewed its processes and procedures in full in 2016 and introduced an innovative ranking methodology for subservicers. Although Zenith does not specify a minimum frequency for subservicers' onsite meetings, in practice it visits subservicers annually.

OUTLOOK

We have revised our outlook on the rankings to stable. The company has worked to train staff, update the system, and improve the processes to board and manage increasing number of portfolios. Although the transfer of ownership is a major change, according to Arrow's announcement the new controlling shareholder should offer further support to Zenith's growth, in continuity with the historical evolution of the business.

MANAGEMENT AND ORGANIZATION

We have raised to STRONG our subranking on Zenith for management and organization as a master servicer of residential mortgages, commercial loans, and unsecured credits in Italy. The servicer relies on an experienced leadership team, which has successfully managed to attract new business. The company offers incentives and recruitment schemes beyond what a company of its size would typically offer and this guarantees motivation and commitment to the company's long-term vision. Finally, the company has good internal controls and an IT system capable of handling larger volumes of business, which minimizes risks.

LOAN ADMINISTRATION

We have raised to STRONG our subrankings on Zenith for loan administration as a master servicer of residential mortgages, commercial loans, and unsecured credits. The company continuously improves its operational model and servicing platform to keep up with best practices in the market. Zenith has also introduced an element of innovation, such as better data visualization tools.

FINANCIAL POSITION

We consider Zenith's financial position to be SUFFICIENT, based on our assessment of its latest financial statements.

RELATED CRITERIA

- Criteria - Structured Finance - Servicer Evaluations: Revised Criteria For Including RMBS, CMBS, And ABS Servicers On Standard & Poor's Select Servicer List, April 16, 2009
- Criteria - Structured Finance - Servicer Evaluations: Servicer Evaluation Ranking Criteria: U.S., Sept. 21, 2004

RELATED RESEARCH

- Rankings Affirmed As ABOVE AVERAGE On Zenith Service As Master Servicer In Italy; Outlook Revised To Positive, July 23, 2015
- Servicer Evaluation: Zenith Service SpA, Sept. 8, 2015
- Select Servicer List, published monthly

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