MOODY'S
INVESTORS SERVICE

Rating Action: Moody's downgrades ratings in Elrond NPL 2017 S.r.l.

25 Mar 2020

Madrid, March 25, 2020 -- Moody's Investors Service ("Moody's") has today downgraded the ratings of Class A and B Notes in Elrond NPL 2017 S.r.l. The rating action reflects slower than anticipated cash-flows generated from the recovery process on the non-performing loans (NPLs) and simulation of cashflows from remaining collateral resulting in lower future recoveries than previously considered for the assigned ratings, in all scenarios.

....EUR 464.0M Class A Notes, Downgraded to Ba3 (sf); previously on Jul 14, 2017 Assigned Baa3 (sf)

....EUR 42.5M Class B Notes, Downgraded to Caa1 (sf); previously on Jul 14, 2017 Assigned B1 (sf)

RATINGS RATIONALE

The rating action is prompted by slower than anticipated cash-flows generated from the recovery process on the NPLs and simulation of cashflows from remaining collateral resulting in lower future recoveries than previously considered for the assigned ratings, in all scenarios.

Slower than anticipated cash-flows generated from the recovery process on the NPLs:

Cumulative Collection Ratio as of the latest reporting date stood at 72.7%, which means collections are significantly slower than anticipated in the original Business Plan projections. NPV Cumulative Profitability Ratio stood at 136.9%, above our expectations, however it only refers to closed positions while the key consideration will be the time to process open positions and the future collections on those.

Simulation of cashflows from remaining collateral resulting in lower future recoveries than previously considered for the assigned ratings, in all scenarios:

Moody's makes its own simulations of cashflows generated from the recoveries of the defaulted loans, their timing and their volatility depending on future property values.

Reported GBV stood at EUR 1,122.23 million as of December 2019 down from EUR 1,405.25 at closing. Split was EUR 1,032.9 million secured and EUR 372.4 unsecured as of November 2016, compared to EUR 799 million secured and EUR 323 unsecured as of December 2019 reporting date. Moody's has not received information on prior lien loans and therefore treated loans with a second and lower lien as unsecured. Same approach was taken for loans for which no reference to a backing collateral was found in the loan by loan information. Borrowers are mainly corporates (around 86%) and the pool is mostly concentrated in the North (about 58%) versus 23% in South and Islands.

Simulation of cashflows from the remaining pool in light of pool characteristics, for instance the share of secured loans and the backing collateral, results in lower recoveries expected in all scenarios and commensurate with lower ratings. In addition to this, temporary disruptions related to the coronavirus outbreak will create an additional backlog of legal proceedings, which will delay gross recoveries.

Our analysis has considered the increased uncertainty relating to the effect of the outbreak on the Italian economy as well as the effects that the announced government measures, put in place to contain the virus, will have on the performance of NPL transactions. We regard the coronavirus outbreak as a social risk under our ESG framework, given the substantial implications for public health and safety. It is a global health shock, which makes it extremely difficult to provide an economic assessment. The degree of uncertainty around our forecasts is unusually high.

Moody's has taken into account the potential cost of the GACS Guarantee within its cash flow modelling, while any potential benefit from the guarantee for the senior noteholders has not been considered in its analysis.

The principal methodology used in these ratings was "Non-Performing and Re-Performing Loan Securitizations Methodology" published in January 2020. 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 or circumstances that could lead to an upgrade of the ratings include: (1) the recovery process of the non-performing loans producing significantly higher cash-flows in a shorter time frame than expected; (2) improvements in the credit quality of the transaction counterparties; and (3) a decrease in sovereign risk.

Factors or circumstances that could lead to a downgrade of the ratings include: (1) significantly lower or slower cash-flows generated from the recovery process on the non-performing loans due to either a longer time for the courts to process the foreclosures and bankruptcies, a change in economic conditions from our central scenario forecast or idiosyncratic performance factors. For instance, should economic conditions be worse than forecasted and the sale of the properties generate less cash-flows for the issuer or take a longer time to sell the properties, all these factors could result in a downgrade of the ratings; (2) deterioration in the credit quality of the transaction counterparties; and (3) increase in sovereign risk.

REGULATORY DISCLOSURES

For further specification of Moody's key rating assumptions and sensitivity analysis, see the sections Methodology Assumptions and Sensitivity to Assumptions of the disclosure form.

The analysis relies on a Monte Carlo simulation that generates a large number of collateral loss or cash flow scenarios, which on average meet key metrics Moody's determines based on its assessment of the collateral characteristics. Moody's then evaluates each simulated scenario using model that replicates the relevant structural features and payment allocation rules of the transaction, to derive losses or payments for each rated instrument. The average loss a rated instrument incurs in all of the simulated collateral loss or cash flow scenarios, which Moody's weights based on its assumptions about the likelihood of events in such scenarios actually 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.

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

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.

Please see the ratings tab on the issuer/entity page on www.moodys.com for additional regulatory disclosures for each credit rating.

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