Presale:

Silver Arrow China 2019-1 Retail Auto Loan Asset Backed Notes Trust

April 16, 2019

Preliminary Ratings As Of April 16, 2019

<table>
<thead>
<tr>
<th>Class</th>
<th>Preliminary rating</th>
<th>Preliminary amount (mil. RMB)</th>
<th>Minimum credit support (%)*</th>
<th>Credit support provided by subordination and overcollateralization (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>A</td>
<td>AAA (sf)</td>
<td>8,500.0</td>
<td>5.7</td>
<td>12.80</td>
</tr>
<tr>
<td>Subordinated</td>
<td>NR</td>
<td>447.4</td>
<td>N/A</td>
<td>N/A</td>
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</table>

Note: This presale report is based on information as of April 16, 2019. 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. *Minimum credit support only reflects estimated losses arising from borrower default and does not reflect the results of cash-flow analyses, which may consider factors such as potential commingling losses and negative carry. N/A—Not applicable. NR—Not rated.

Profile

Expected closing date | April 2019
Expected final maturity date | June 26, 2024
Collateral | Renminbi-denominated, fully amortizing loans to prime-quality borrowers, secured by first registered mortgages over vehicles
Structure type | Prime auto loan-backed securities with sequential repayment mechanism
Issuer | China Foreign Economy And Trade Trust Co. Ltd. as trustee of Silver Arrow China 2019-1 Retail Auto Loan Asset Backed Notes Trust
Servicer | Mercedes-Benz Auto Finance Ltd.
Primary credit enhancement | Note subordination, overcollateralization, and potential support from yield supplement overcollateralization.

Supporting Ratings

Bank account provider | Industrial And Commercial Bank Of China Ltd.

www.spglobal.com/ratingsdirect
Loan Pool Statistics As Of Jan. 31, 2019

<table>
<thead>
<tr>
<th>Description</th>
<th>Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total number of loans</td>
<td>72,269</td>
</tr>
<tr>
<td>Total receivable balance of contracts (RMB)</td>
<td>9,938,576,121</td>
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<tr>
<td>Maximum receivables balance of contracts (RMB)</td>
<td>1,648,356</td>
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<tr>
<td>Average receivables balance of contracts (RMB)</td>
<td>137,522</td>
</tr>
<tr>
<td>Weighted average down-payment (%)</td>
<td>41.17</td>
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<tr>
<td>Weighted average interest rate (%)</td>
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<tr>
<td>Total balloon payments as a percentage of total pool balance (%)</td>
<td>0.00</td>
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<tr>
<td>Weighted-average contract seasoning (months)</td>
<td>11.08</td>
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<tr>
<td>Weighted-average remaining term to maturity (months)</td>
<td>22.52</td>
</tr>
</tbody>
</table>

Rationale

This is an auto loan securitization transaction originated by Mercedes-Benz Auto Finance Ltd. (MBAFC). We assigned our 'AAA (sf)' preliminary rating to the class A notes to be issued by China Foreign Economy And Trade Trust Co. Ltd. as trustee of Silver Arrow China 2019-1 Retail Auto Loan Asset Backed Notes Trust (the issuer). The rating reflects the following factors:

- The credit risk associated with the underlying collateral portfolio and the credit support provided for the class A notes in the form of subordination and overcollateralization are commensurate with our view of credit risk under ‘AAA’ rating stresses. Our assessment of credit risk takes into account originator MBAFC’s underwriting standards and centralized approval process, which are largely consistent with Daimler AG’s financing business practice and risk-management approach, with some local adaptation. Daimler AG is MBAFC’s parent company.

- The transaction’s cash flows can meet the timely payment of interest and ultimate payment of principal to the rated notes under stresses commensurate with the ratings assigned. All rating stresses are assessed on the basis that the issuer does not call the notes on or beyond the call-option date, and that the notes must be fully redeemed via the mechanisms under the transaction documents.

- The timely payment of senior expenses and rated note coupon is supported by the use of interest and principal collections from the underlying pool of loans and a liquidity reserve equal to Chinese renminbi (RMB) 98 million. The liquidity reserve will not amortize and will be topped up through the priority of payments on each payment date.

- A proportion of the collateral portfolio comprises contracts that have an interest rate lower than that required to cover the trust’s senior expenses and class A note interest. However, the transaction's cash flows are further supported via the provision of additional overcollateralization in the form of yield supplement overcollateralization (YSOC).

- The legal structure of the trust, established as a special-purpose trust (SPT) under China's Trust Law, and the transaction structure and terms, are consistent with the governance of China Banking and Insurance Regulatory Commission (CBIRC) and The People's Bank of China (PBOC)'s credit assets securitization (CAS) scheme. The legal structure of the SPT reflects our criteria for insolvency remoteness.

- The transaction has counterparty exposure to Industrial And Commercial Bank Of China Ltd.
a bank account provider. The rating on the bank account provider, coupled with the replacement trigger of the bank account provider if this rating falls below a certain level, is consistent with our counterparty criteria to support an 'AAA' transaction.

- The preliminary ratings on the notes are higher than our sovereign rating on China. We applied our "Incorporating Sovereign Risk In Rating Structured Finance Securities: Methodology And Assumptions" criteria published on Jan. 30, 2019, and determined that the highest rating that can be considered for this transaction is 'AAA'.

Strengths And Weaknesses

Strengths

In our opinion, the strengths of the transaction observed in the rating analysis are:

- The sound quality of the loan portfolio at close. All underlying loans have a full-recourse feature, and are backed by new passenger vehicles for personal use. The initial portfolio is well diversified, with a single borrower concentration of around 0.02%, and it is seasoned by more than 11 months in weighted-average terms. Our observations in other markets suggest these features tend to support consistent and stronger performance.

- The limited exposure period. Loans with remaining terms no longer than 36 months account for almost 100% of the initial pool balance. The underlying pool at cut-off date has a weighted-average remaining term of around 23 months. This, coupled with the static nature of the portfolio, means that the risk exposure period of the pool—or weighted-average life of the notes—is likely to be short. We expect China's economic growth to remain relatively stable in the near term, with a slowdown being managed by the government.

- The repayment structure of the transaction. The transaction adopts a sequential payment waterfall, which means no principal may be passed through to the subordinated notes until the class A notes have been fully amortized.

- High global consistency between MBAFC and Daimler AG’s financing business on underwriting process, risk management and technology platform. Daimler AG is heavily involved in the development of MBAFC’s operation, underwriting, and risk management processes. MBAFC also has over than a decade of operating experience in China for local adaptation. A comprehensive technology system is deployed to store data, facilitate loan origination, and support auto loan securitization in a global standard. MBAFC has committed to ongoing system improvements to meet the needs of business growth.

Weaknesses

In our opinion, the weaknesses of the transaction and the corresponding mitigants observed in the rating analysis are:

- The short operating history of China's auto finance sector, which grown rapidly only in the past decade. As a result, the sector has limited historical performance data available for analysis. Unlike in the U.S., the auto finance sector in China has not experienced true periods of economic stress. We have factored this potential weakness into our credit risk analysis of the transaction. We also note that China's regulators have set forth stringent requirements on auto loan origination, and have adopted continued supervision and administrative guidelines on loan
quality control. In our view, such regulatory oversight, along with MBAFC’s underwriting capability and risk management, will prevent a lowering of the origination standards in auto finance.

- Lack of experience in servicing transition in China’s securitization market. Despite the rapid development of Chinese securitization during the past couple of years, only a few transactions to date have experienced the critical stress of a failure of important counterparties such as the servicer, and the resulting negative effect on the transaction’s cash flow. In this transaction, the risk of servicer transition and cash-flow continuity are partly mitigated by the payment arrangements. All loan payments in this transaction will be collected through the direct debit of borrowers’ cash accounts in major national banks rather than by other more demanding collection processes. This will reduce the process complexity and make it easier to find a replacement servicer. We also have considered in our analysis a potential increase in servicer fees if a replacement servicer requires a higher return. Moreover, the transaction sets up a liquidity reserve upfront that could cover two-three months of transaction expenses and note interest if asset collections are temporarily unavailable to meet the transaction obligations. In our view, this will allow the transaction sufficient time to find a new servicer and resume the asset collections.

**Notable Features**

The interest and principal collections from the YSOC portion, which is an indistinguishable part of the securitized loans, constitute additional support to the transaction. But the additional support is primarily for covering the expected shortfall of loan yields against transaction payments for tax, senior fees/expenses and note coupons. The YSOC will initially be approximately 1.68% of the total pool balance at transaction close. The YSOC is sized so that the effective asset yield on the collateral portfolio would be sufficient to generate excess spread. Sizing is determined on the cut-off date by assuming zero prepayments and zero defaults of the additional loan portion. As the collateral portfolio and the class A notes amortize and the expected difference between asset yields and note interest decreases, the YSOC will amortize through payment to junior waterfall items accordingly.

Under the transaction’s payment priority, after addressing negative carry, any collections from the YSOC portion will also be available to cover credit losses or commingling losses, by paying down the class A notes if the asset pool is under-collateralized. In other words, it could provide another source of credit enhancement under some scenarios. In a severe negative carry environment, the collections from the YSOC should be used to cover negative carry first, so the likelihood of the YSOC collections being available to cover credit losses and commingling losses would decrease. After covering negative carry, credit losses and commingling losses, the collections from the YSOC can be used to cover indemnity expenses or be released to the originator.

The transaction has a single—rather than separate “income” and “principal”—cash-flow priority of payments, and there is no concept of a principal deficiency ledger. There are no note charge-off arrangements or note invested/stated amount differentiation in the transaction.

**Transaction Structure**

The transaction is based on China’s CAS scheme set up by CBIRC and PBOC.

MBAFC sells a pool of auto loans receivables to an SPT, which is set up by China Foreign Economy And Trade Trust Co. Ltd., the trustee, for the purpose of securitization. To fund such receivables
purchase, the trustee will issue (on behalf of the SPT) two classes of trust certificates. The class A notes will be placed with the investors, while the subordinated notes will be held by the originator. Only class A notes will be rated by S&P Global Ratings. Such transfer will be deemed a true sale that segregates the assets from the originator, and the SPT is deemed bankruptcy remote under China’s Trust Law.

The collateralized assets are loans extended to retail borrowers, used to finance the purchase of new cars manufactured by Daimler AG, including those made by local joint ventures, under the Mercedes-Benz and smart brands. These loans have original terms spanning up to 60 months. The weighted-average remaining term is around 23 months. Initial loan-to-value (LTV) ratios of most loans (97%) ranged from 40% to 80%, and the weighted average initial LTV was 59%. Vehicles purchased through these loans are mortgaged for the benefit of the originator.

The asset pool will be static, meaning no asset substitution or reinvestment is allowed. In the pre-enforcement waterfall, collections (inclusive of interest, principal, penalties, and any other payments) from the assets will be used to pay SPT taxes, senior fees and expenses, interests on the rated notes, and replenish liquidity reserve if required. The remaining proceeds will be used to pay down the principal of the rated notes in accordance with the principal distributable amount.

A liquidity reserve equal to 0.98% of the initial asset pool balance, and equivalent to 1% of the initial adjusted pool balance (aggregate outstanding pool balance minus YSOC), will be funded upon transaction closing. The liquidity reserve provides liquidity support to the transaction’s expenses and interest on the rated notes, if needed.

The structure of the transaction is shown in chart 1.
Asset Segregation And Issuer's Bankruptcy Remoteness Under The CAS Scheme

The CAS pilot program shares the typical features of international securitization transactions, such as asset sale and issuer bankruptcy remoteness. The program is primarily for bank and nonbank financial institution originators under the management of CBIRC. It started in 2005 and has since undergone multiple reviews and amendments. The related guidelines under the CAS pilot program specify asset eligibility and protection of transferred assets and issuers.

We believe the asset true sale and issuer’s bankruptcy remoteness in this transaction reflect our special-purpose entity criteria. The primary reason for this is that the securitization transaction adopts an SPT structure by referring to China’s Trust Law, in line with the regulations in the CAS pilot program. With the 2001 Trust Law in place and the general acceptance of trusts' legal position, we believe there is a remote risk of issuer bankruptcy due to reasons unrelated to collateral performance or reconsolidation of the assets with the seller's bankruptcy estate if the seller becomes insolvent.

The 2001 Trust Law indicates:
The trust assets are segregated from the originator’s other assets, and are not part of the
bankruptcy estate;
- There is proper separation between the trust assets and the trustee’s own assets;
- The enforcement of trust assets can only be done under very limited situations;
- Limitation on trustee’s set-off rights; and
- The trust will continue to survive under the insolvency of the entruster (the originator) and the
trustees and will terminate only under limited conditions.

A trust set-up perfection process in accordance with the Trust Law will be followed before
transaction closing, through public announcements of the loans to be entrusted, and the trust
set-up based on the entrusted loans. In addition, one of the precedent conditions for trust set up
is the payment of the asset purchase price by the trustee to the originator (the asset seller). Given
this, we believe there is a remote risk that the entrusted assets would be considered as assets of
the seller in the event that an external administrator is appointed in respect of the seller.

The assets that may be securitized through SPT structures are stipulated in the related guidelines
under the CAS pilot program. We believe the securitized assets are eligible to be transferred
through the trust structure pursuant to the CAS guidelines because the transaction needs to be
registered with the CBIRC and PBOC. This assurance, coupled with the linkage of CAS program to
the Trust Law, supports our view that the SPT will be protected by the Trust Law, and the
entrusted assets will be segregated from the originator’s.

Having recognized the regulators’ support for securitization in China, we note that there is no
official securitization legislation in China for asset segregation and issuer bankruptcy remoteness.
The CAS program guidelines provided by CBIRC and PBOC are administrative measures, not
legislation. As such, there is a residual risk that the measures may be subject to court challenges
to the extent that they conflict with laws or other regulations.

**Collateral Assignment**

Typical car loan contracts in China have clauses addressing the transferrable and assignable
nature of the receivables, meaning that the originators can sell/transfer the contracts to third
parties without the borrowers’ consent, pursuant to China’s Contract Law. The asset eligibility
criteria stipulated in this transaction confirms that the purchased loan receivables are assignable.

Legally, the issuer will have the title of the loans and the associated rights, including the
mortgage, after the asset sale. Practically, however, the transfer will not be effective against the
borrowers if the originator does not notify the borrowers of the transfer. Without such notification,
although the receivables have been legally acquired by the issuer, the borrowers’ payments will
continue to be made to the originator or the initial servicer. This issue could be more complicated
if the originator becomes insolvent, making it unable to issue a notice to borrowers that a trust has
been created over the related loan and that borrowers should redirect their payments to the new
lender.

The transaction addresses this concern by introducing a rights-perfection event upon the
termination of the initial servicer. The occurrence of a rights-perfection event will cause the title
and rights transfer to be perfected through the originator’s notification to each borrower, each
guarantor, if any, and the vehicle’s insurance company. Such notification will state a trust has
been created over the related loan and all payments on the loans should be made from then on to
the issuer’s account or the replacement servicer’s account.
Through an executed power of attorney upon transaction closing, the originator has empowered the trustee to issue the transfer notices to individual obligors directly if the servicer does not do so, and to redirect the loan payments to the replacement servicer’s account or the issuer’s account.

**Note Terms And Conditions**

**Interest payments structure**

The rated notes are fixed-rate notes. Interest payments on the class A notes rank in priority to interest payments on the subordinated notes.

The transaction does not have a principal deficiency ledger mechanism. Consequently, the concepts of charge offs, note invested amounts, and note stated amounts are not applicable in this transaction. Interest paid on each class of notes will be calculated based on the outstanding principal, which is the initial principal as reduced by cumulative principal repayments on previous payment dates.

**Principal payment structure**

Principal repayment to the class A and subordinated notes will be sequential. The subordinated notes will receive payments only after class A notes’ principal is fully repaid. On each payment date, the class A notes will be paid down based on the formula of “principal distributable amount,” which essentially is the amount of assets’ principal collections, netting of the collections from the YSOC that are not used to cover negative carry or credit losses.

**Clean-up call**

The originator has a "clean-up call" option to purchase the auto loans from the trust if the pool balance at the end of any month is reduced to less than 10% of the initial note balance. The originator may exercise its clean-up call option only if the clean-up call price for the loans, together with amounts in the collection account, general reserve account, and commingling reserve account if any, will be sufficient to repay in full the rated notes and all fees and expenses of the trust. Upon the originator’s exercise of its clean-up call option, the notes will be redeemed and repaid in full and the trust will be liquidated.

**Priority Of Payments**

The transaction has a combined interest and principal cash-flow priority of payments. The pre-enforcement priority of payments is summarized in table 1.

<table>
<thead>
<tr>
<th>Priority Of Payments</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
</tr>
<tr>
<td>2</td>
</tr>
<tr>
<td>3</td>
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<tr>
<td>4</td>
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Table 1

Priority Of Payments (cont.)

<table>
<thead>
<tr>
<th></th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>5</td>
<td>Top up the liquidity reserve up to its required level</td>
</tr>
<tr>
<td>6</td>
<td>Class A notes principal to target level in accordance with principal distributable amount</td>
</tr>
<tr>
<td>7</td>
<td>Interest on subordinated notes (stated coupon is zero)</td>
</tr>
<tr>
<td>8</td>
<td>Subordinated notes principal if class A notes are paid in full</td>
</tr>
<tr>
<td>9</td>
<td>Indemnity payments</td>
</tr>
<tr>
<td>10</td>
<td>To originator (subordinated noteholder)</td>
</tr>
</tbody>
</table>

If at any time an enforcement event occurs, then all available funds, including all amounts deposited in the liquidity reserve account and all proceeds from asset liquidation, if any, will be used to make payments per post-enforcement priority of payments. An enforcement event relates to: (1) the insolvency event of the trust; (2) issuer's failure to pay the senior most class of notes' timely interest or principal amount on the legal maturity date; (3) its failure to perform or observe its obligations such that the failure can't be remedied; or (4) its illegality to perform or comply with its obligations, such that the noteholders declare the occurrence of an enforcement event.

Originator/Servicer Overview

Company background

MBAFC is a CBIRC-regulated auto finance company incorporated in Beijing, China in September 2005. The company initially was wholly-owned by Daimler AG, a leading global automotive manufacturer of premium cars and commercial vehicles based in Germany. Since May 2015, Daimler AG and Daimler Greater China Ltd. (a wholly-owned subsidiary of Daimler AG) own 52.2% and 47.8% of MBAFC, respectively.

MBAFC offers both passenger and commercial vehicle financing products across China for the purchase of Mercedes-Benz' passenger cars, vans, and trucks, Auman trucks, and smart vehicles. Its target customers are retail customers, small businesses, corporates, and dealerships. A small portion of loan products are offered to the borrowers with balloon payments. These loans accounted for less than 0.1% of the total outstanding loan balance as of Dec. 31, 2018.

The loan products securitized in this transaction include MBAFC's retail auto loan contracts secured by Mercedes-Benz passenger cars and smart vehicles extended to retail customers only. No loans with balloon payments are included.

The company manages sales through its four regional offices and a nation-wide dealer network of nearly 630 dealers in China as of Dec. 31, 2018. Growth of loan origination has been stable in the past five years. As of Dec. 31, 2018, the company’s outstanding loan assets has reached RMB84 billion. The number of employees stayed stable at around 700 for the past two years due to the company’s strategy to manage growth and improve efficiency with digitalization and outsourcing initiatives.

Risk management

MBAFC's risk-management practice leverages the experience and capability of its parent
company and is highly compliant with Daimler AG’s risk management standard applied to the financing business globally. The risk management framework covers the whole lifecycle of a loan and incorporates various policy rules to flag risk at different stages. The policy rules are China customized and reflect timely regulatory or market updates.

The risk management team follows a forward-looking approach to identify possible risk trends that are likely to adversely affect the company's portfolio. It then forms risk monitoring measures and action plans to ensure effective portfolio management.

A strict fraud prevention practice is implemented for credit assessment. The company flags applications with potential fraud signals such as inconsistent information or previous bank fraud record, and a fraud detection specialist will call or visit the applicants to investigate. Case studies on fraud are provided within MBAFC regularly to enhance risk management at the underwriting stage.

We also see well-established staff training and strong coaching support provided to credit analysts to control risks at the front end. Credit analysts are trained based on their specialized customer segments, and must pass certain exams before they can assume their roles.

**Loan origination and underwriting**

Dealerships recommend MBAFC products to the end customer and refer the customer to an onsite financial and insurance consultant as the first-contact point at MBAFC for the borrowers. The consultants perform initial checks on each borrower’s identity, collect supplementary documents, and enter the loan application data in MBAFC's system for credit review.

The regional credit department carries out the credit review. There are four regional credit teams and each is allocated with credit analysts based on the volume processed. A centralized credit governance team is responsible for the policies, procedures, and credit underwriting quality in retail and wholesale credit operations, which include headquarters coordination, credit policies and procedures maintenance, and quality assurance in credit processes.

MBAFC uses both a credit-scoring system and manual assessment to conduct credit review. Upon receiving the loan documents, MBAFC first verifies customer information via external sources such as NCIIC and SAIC data and checks credit history from the PBOC credit system before passing the application to the scoring system for credit assessment.

The credit-scoring system reviews the application and suggests that it go for automatic approval or refers it for a manual assessment. According to MBAFC, nearly 40% of loan applications received recommendation of automatic approval from the scoring system. All auto-approved cases will then be checked manually again for the completeness and quality of the documents. Applications that are not automatically approved will all go to manual review conducted by the credit analysts for further investigation and a more comprehensive analysis. Credit analysts can only approve a loan that falls within their credit approval limit.

The credit scoring system was developed in 2014 by the risk instrument team at the headquarters. It borrows the framework from Daimler AG’s global practices, but has different parameters to reflect China-specific features. The scoring system calculates a composite score for each applicant based on the application information and data from PBOC credit system. The scores range from 1 to 1000 and are categorized into four classes from A to D, to represent borrowers of different risk levels and default probabilities. Separate scorecards are applied for retail borrowers and small business borrowers at MBAFC to address the different risk factors of the various customer segments. Scorecards are monitored on a quarterly basis in model performance, variables distribution, and stability performance.
In addition to the scorecard, business policy rules are a supplementary tool used to form credit opinions and to reflect MBAFC’s policy appetite. Some of the rules are to reject borrowers to reflect restrictions by law and CBIRC regulation, or to flag a high risk factor such as a delinquency record or unemployment status. Each business policy rule is monitored and reviewed on quarterly basis jointly by the headquarters and the local risk teams.

MBAFC adopts a strict process for contract activation and disbursement after loan approval. For an approved application, MBAFC will notify the dealer to sign the contract with the borrower and submit it back to MBAFC along with additional documents such as insurance and direct-debit mandate. MBAFC’s retail operation team then verifies the documents to activate the loan and checks vehicle registration for disbursement.

**Loan servicing**

MBAFC will be responsible for servicing the receivables in the collateral pool. Its customer service and collection departments track and manage loan repayments. Part of the late collection process is outsourced, but supervised by MBAFC.

Borrowers repay their loans mainly through direct-debit repayments into MBAFC's account. To make direct-debit repayment, borrowers need to maintain a bank account at one of the nine cooperating banks, and deposit sufficient money for periodic loan repayments. Each of these banks has a nationwide network in China for such service.

MBAFC has defined processes and timelines to manage contracts in arrears based on the delinquency lifecycle. For loans that are at early collection stage (1 to 60 days past due), MBAFC sends a text message and makes a phone call to the borrowers using a call center vendor, and conducts an outsourced home visit. If the delinquency cannot be remedied within 60 days after missing the first payment, it will be passed to the late stage collection officers and outsourced agents to follow up. Contracts that are over 90 days past due may trigger contract termination and vehicle repossession. At this stage, MBAFC may arrange obligors' repayment, and voluntary or involuntary vehicle sales for borrowers to repay the loans. For any remaining amount owed to MBAFC after vehicle sale, including costs and expenses incurred during the collection process, MBAFC has the right to continue pursuing the borrowers, due to the full-recourse nature of the loans. If a loan is more than 180 days overdue, MBAFC generally charges off the contract. All outsourced activities and vendors are supervised by MBAFC's agent management team to ensure collection quality and consistency.

**Stringent regulatory oversight and characteristics of prime loans**

MBAFC's loan underwriting policies reflect the regulatory control on auto loan risks in China. The amended “Auto Loans Management Guideline” promulgated by the PBOC and CBIRC in 2018 constitutes certain basic loan underwriting requirements that all auto finance companies and commercial banks must follow in their auto loan business. These requirements are:

- The borrowers need to have good credit history, with evidence of stable income or other property to support the down payment and continued debt servicing.
- The term of the loan financing a new vehicle should not be longer than five years, and the loan tenor for preowned vehicles should not be longer than three years.
- The highest LTV ratio on retail loans is 80% for new vehicles, except defined new energy cars, and 70% for preowned vehicles.
- The value of the vehicles for the calculation of LTV ratio should be the lower of the manufacturers’ suggested vehicle price and the amount actually paid by the buyer (for new vehicles).

Borrowers with good credit quality and debt serviceability are no longer required to mortgage the vehicles financed by such loans or other collateral to the lenders after the guideline amendment. However, all loans in the securitized pool as of the initial cut-off date have a vehicle mortgage as confirmed by the originator. Although mortgage registration is not explicitly required in the asset eligibility criteria, MBAFC’s best practices require mortgage registration to be completed by the dealer within a limited time frame per the company’s underwriting policy.

In January 2008, CBIRC (the former CBRC) announced an administrative guideline in relation to auto loan risks, and asked financial institutions to enhance their fraud-prevention measures, validation of documents, use of credit check systems, and collection management. Since then, the CBIRC and PBOC have carried out ongoing surveillance on industry development and loan quality trends, and they could intervene by issuing growth targets or loan-origination guidelines to the industry.

We believe the strict regulatory oversight and continued surveillance explains the generally sound performance of auto loans in China since 2009. Even though auto loan penetration in China has been growing in the past few years, it remains in relatively low at 40%-50%. Therefore, industry competition is not as fierce as in other markets. We have observed that auto financiers do not try to use looser underwriting practices or higher risk products as leverage to grow their business. This also partly explains the stable loan performance in China’s auto loans industry.

The stringent regulations that apply to loan underwriting and the industry’s aversion to riskier borrowers and products support prudent underwriting. We believe the characteristics of MBAFC’s auto loan borrowers are consistent with those we typically observe for prime borrowers in other markets. Our view is supported by MBAFC’s internal policy rules, information check and document verification processes, centralized and independent loan-review process, stringent underwriting policy for higher risk customers, and the low default and loss rate in its historical arrears performance data in recent years.

Collateral

The pool contains 72,269 consumer loan contracts, secured by vehicles manufactured by Daimler AG and its China affiliates. In terms of the repayment method, all of the receivables require equal installments. The aggregate outstanding principal balance is about RMB9.9 billion.

The following summarizes some distinct features of the collateral pool:

- The collateral pool is a static auto loan pool that will amortize each month, with no reinvestment or substitution of receivables.
- The entire portfolio comprises receivables that are backed by new passenger vehicles. Historical data in other markets show that losses when the motor vehicle financed was new are typically lower than those when the motor vehicle was pre-owned.
- There are no balloon or bullet loans in the asset pool; all loans are fully amortized with equal instalments.
- The transaction has a diversified pool of 72,269 loans, with the largest single loan accounting for around 0.02% of the initial loan balance. Borrower concentrations therefore do not present an additional risk for this transaction.
The collateral pool is somewhat seasoned, with a weighted-average contract seasoning as of the cut-off date of 11.08 months.

The loans in the collateral pool have a weighted-average interest rate 4.75%. The loans with interest rates higher than 6% account for 16.88% of the pool, while those with interest rates less than or equal to 3% represent 22.88%.

All contract payments, including interest, principal, expenses, and prepayment penalty, are full-recourse obligations of the borrowers.

The trust is not exposed to any market-value risk associated with the sale of the motor vehicles (on performing receivables), which is a risk that could be associated with products such as operating leases.

The receivables pool for Silver Arrow China 2019-1 Retail Auto Loan Asset Backed Notes Trust as of Jan. 31, 2019 is summarized in table 2.

Table 2

<table>
<thead>
<tr>
<th>Loan Pool Characteristics (% pool by outstanding principal balance)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Customer type</strong></td>
</tr>
<tr>
<td>Retail business owner                                      60.35</td>
</tr>
<tr>
<td>Retail private individual                                   39.65</td>
</tr>
<tr>
<td><strong>New and used (financed vehicle)</strong></td>
</tr>
<tr>
<td>New                                                         100.00</td>
</tr>
<tr>
<td>Used                                                        0.00</td>
</tr>
<tr>
<td><strong>Loan payment method</strong></td>
</tr>
<tr>
<td>Direct debit                                                100.00</td>
</tr>
<tr>
<td><strong>Seasoning (months)</strong></td>
</tr>
<tr>
<td>Less than or equal to 6                                     33.11</td>
</tr>
<tr>
<td>Greater than 6 and less than or equal to 12                 30.22</td>
</tr>
<tr>
<td>Greater than 12 and less than or equal to 18                 21.08</td>
</tr>
<tr>
<td>Greater than 18 and less than or equal to 24                 10.95</td>
</tr>
<tr>
<td>Greater than 24 and less than or equal to 30                 4.01</td>
</tr>
<tr>
<td>Greater than 30 and less than or equal to 36                 0.62</td>
</tr>
<tr>
<td>Greater than 36 and less than or equal to 42                 0.02</td>
</tr>
<tr>
<td>Greater than 42 and less than or equal to 48                 0.01</td>
</tr>
<tr>
<td><strong>Remaining term to maturity (months)</strong></td>
</tr>
<tr>
<td>Less than or equal to 6                                     1.27</td>
</tr>
<tr>
<td>Greater than 6 and less than or equal to 12                  10.15</td>
</tr>
<tr>
<td>Greater than 12 and less than or equal to 18                  19.10</td>
</tr>
<tr>
<td>Greater than 18 and less than or equal to 24                  28.43</td>
</tr>
<tr>
<td>Greater than 24 and less than or equal to 30                  22.08</td>
</tr>
<tr>
<td>Greater than 30 and less than or equal to 36                  18.94</td>
</tr>
<tr>
<td>Greater than 36 and less than or equal to 42                  0.03</td>
</tr>
</tbody>
</table>
### Table 2

**Loan Pool Characteristics (% pool by outstanding principal balance) (cont.)**

<table>
<thead>
<tr>
<th>Value of loans (%)</th>
<th>Effective interest rate (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Greater than 42 and less than or equal to 48</td>
<td>0.00</td>
</tr>
<tr>
<td>Greater than 42 and less than or equal to 48</td>
<td>1.51</td>
</tr>
<tr>
<td>Effective interest rate (%)</td>
<td>Greater than 0 and less than or equal to 3</td>
</tr>
<tr>
<td>Greater than 0 and less than or equal to 3</td>
<td>21.28</td>
</tr>
<tr>
<td>Greater than 3 and less than or equal to 6</td>
<td>60.32</td>
</tr>
<tr>
<td>Greater than 6 and less than or equal to 9</td>
<td>16.43</td>
</tr>
<tr>
<td>Greater than 9 and less than or equal to 12</td>
<td>0.45</td>
</tr>
<tr>
<td>Receivables balance (RMB)</td>
<td>Less than or equal to 50,000</td>
</tr>
<tr>
<td>Less than or equal to 50,000</td>
<td>2.80</td>
</tr>
<tr>
<td>Greater than 50,000 and less than or equal to 100,000</td>
<td>14.81</td>
</tr>
<tr>
<td>Greater than 100,000 and less than or equal to 150,000</td>
<td>24.51</td>
</tr>
<tr>
<td>Greater than 150,000 and less than or equal to 200,000</td>
<td>22.76</td>
</tr>
<tr>
<td>Greater than 200,000 and less than or equal to 250,000</td>
<td>12.92</td>
</tr>
<tr>
<td>Greater than 250,000 and less than or equal to 300,000</td>
<td>7.91</td>
</tr>
<tr>
<td>Greater than 300,000 and less than or equal to 350,000</td>
<td>3.45</td>
</tr>
<tr>
<td>Greater than 350,000 and less than or equal to 400,000</td>
<td>2.56</td>
</tr>
<tr>
<td>Greater than 400,000</td>
<td>8.28</td>
</tr>
<tr>
<td>Car brand</td>
<td>Mercedes-Benz</td>
</tr>
<tr>
<td>Mercedes-Benz</td>
<td>98.50</td>
</tr>
<tr>
<td>Smart</td>
<td>1.50</td>
</tr>
</tbody>
</table>

The obligor concentrations for the collateral pool are set out in table 3.

### Table 3

**Obligor Concentrations (% Of Pool By Outstanding Receivables Balance)**

| The largest obligor | 0.02 |
| The largest 10 obligors | 0.14 |
| The largest 20 obligors | 0.25 |
Eligibility Criteria

MBAFC will represent and warrant with respect to the receivables that:

- Each loan receivable has been originated by the originator pursuant to a loan agreement governed by China’s laws;
- Each loan receivable has been originated in China for the sale of a financed vehicle in the ordinary course of the originator’s business in compliance with the credit and collection policy;
- Each obligor to which such loan receivable relates is a resident of China;
- Each loan receivable is secured by a mortgage over the relevant financed vehicle with MBAFC being the first priority mortgagee; the vehicle registration certificate of each vehicle to which such loan receivable relates is held by the originator;
- Each loan receivable may be segregated and identified at any time for the purpose of ownership and at any time be identified as a loan receivable;
- Each loan receivable can be, as of the issue date will have been, validly transferred to the issuer by way of sale and assignment according to the relevant loan agreement, such transfer is not subject to any legal restriction which prevents the valid transfer thereof to the issuer;
Each loan receivable is free of third party rights, including any set-off rights, any defense, retention or revocation rights of the relevant obligor;

- Each loan receivable constitutes the legal, valid and binding obligations of the obligor(s), enforceable against the obligor(s) in accordance with its terms;

- The receivables are denominated in RMB;

- The financed vehicles are classified as Mercedes-Benz or smart passenger cars or vans by MBAFC;

- Each loan receivable gives rise to monthly instalment payments;

- The interest rate applicable to each loan receivable is fixed;

- Each loan receivable has a seasoning above one month and shall mature in less than 59 months;

- According to MBAFC’s records, the obligor is not insolvent;

- Each loan receivable is classified as "normal" according to the 5-grade CBIRC classification;

- At origination, the relevant obligor is not an employee of MBAFC;

- At origination, each loan receivable has a loan-to-value of equal or lower than the then current maximum level permitted by regulations in China;

- Each loan receivable requires the obligor to maintain insurance on the financed vehicle;

- As of the cut-off date, no loan receivable is overdue and no loan receivable has been delinquent for more than thirty (30) days in a row; and

- Each loan agreement has specific repayment plans.

Commingling Risk

S&P Global Ratings' counterparty criteria consider a transaction’s commingling risk through the rating on the servicer, the amount of funds likely to be held in a servicer account at any given time, and the potential impact of a delay in receipt of those funds on the supported securities. In our opinion, there is potential commingling risk in this transaction if the servicer defaults, because MBAFC, acting as the servicer in this transaction, can hold the collections for a period of one month before remittance to the SPT account.

A commingling reserve account will be established for this transaction with the account bank upon closing. The servicer will arrange for the originator to deposit an amount that equals to the amount of scheduled installment to be received by the servicer during next monthly collection period (defined as "required commingling reserve amount") into the commingling reserve account if the rating on the servicer is lowered to certain levels under local ratings agencies' scales. Before each payment date, the trustee will transfer an amount equal to "the excess of commingling reserve account balance over the actual collections in the month" from the commingling reserve account to the originator. MBAFC will top up the commingling reserve account to ensure the account’s balance is at least equal to the required commingling reserve amount.

The mitigating mechanism is in line with transactions we rate in other markets. However, the rating triggers that require the originator to top up the commingling reserve account do not include S&P Global Ratings' ratings. Without the ratings triggers on MBAFC, we believe the current transaction arrangement does not sufficiently mitigate commingling risk in accordance with our
counterparty criteria, given that the collection holding period could be up to one month, the commingling reserve does not have a balance up front, and the asset collections are not made directly to SPT accounts or to a specific lock box after transaction closing. For this reason we have assumed that one full month of collections may be lost before collections could be redirected to the SPT accounts or the accounts of the replacement servicer, when the original servicer becomes insolvent. This one-month collection loss has been considered in our cash-flow analysis of the transaction and is mitigated by the liquidity reserve.

Set-Off Risk

We believe there is low set-off risk for cash deposits in this transaction because MBAFC is not an authorized deposit-taking institution in China. In addition, the representations and warranties provided by MBAFC in respect of the collateral pool include that the borrowers in particular have no set-off claim thereto or thereunder the loans, or the status and enforceability of the purchased loan receivables is not impaired by set-off rights.

Counterparty Risk With Respect To The Bank Account Provider

Issuer accounts for this transaction, including the collection account, the liquidity reserve account, and the commingling reserve account, will be held with Industrial And Commercial Bank Of China Ltd., pursuant to the bank account agreement. The agreement requires minimum ratings for the account provider, as per the ratings scales of ratings agencies in China. Moreover, the bank will be replaced if the ratings on it are lower than ‘A/A-1’, within 30 calendar days of the downgrade. This arrangement meets our counterparty criteria to support an ‘AAA’ rated transaction, considering the transaction's cash-flow arrangement.

Counterparty Risk With Respect To The Servicer

MBAFC cannot resign from its role as the initial servicer, but can be removed if a servicer termination event occurs. Such an event might happen if MBAFC: (1) becomes insolvent; (2) fails to remit collections to the issuer when due; (3) can’t remedy its failure to perform material obligations under the servicing agreement; (4) can’t remedy a case of false or incorrect representation or warranty in the servicing agreement or false or incorrect servicer report; (5) is placed under business sanctions; or (6) is dissolved. The transaction does not have a back-up servicer upon transaction closing. MBAFC as the servicer will be replaced following the occurrence of a servicer termination event, and a noteholders’ meeting will appoint a back-up servicer based on the minimum rating scales required by local rating agencies.

Prime auto transactions in other markets do not typically include back-up servicers upon transaction closing, however, because of the high credit quality and homogeneous nature of the receivables, combined with the availability of institutions experienced in servicing them. Unlike other markets, where the trustees of transactions may become the successor servicer in situations when no other substitute has been appointed, we consider that trustees in China would not take this role due to their trust company nature and the sheer volume of loan accounts and their geographic dispersion. We believe that in China the most likely servicer replacement would be other auto finance companies or commercial banks that have a nationwide network for loan collections.

All loan payments in this transaction will be collected through the direct debit of borrowers’ cash accounts in major national banks rather than by other more demanding collection process. This
will reduce the workload of the servicer and make it easier to find a replacement. We have also factored into our analysis a potential increase in servicer fees should a replacement servicer require a higher return. Finally, the transaction includes a liquidity reserve that is funded up front and could cover two to three months of transaction expenses and note interest should asset collections be temporarily unavailable to meet the transaction obligations. In our view, this will allow the transaction sufficient time to find a new servicer and resume asset collections.

**Liquidity Support**

Timely payment of senior expenses and rated note interest is supported by the use of principal collections through the combined waterfall, and a liquidity reserve funded at closing by MBAFC, at around RMB98 million or around 0.98% of the initial receivables balance.

The liquidity reserve is held in the general reserve account. It does not amortize and will be topped up to around RMB98 million through remaining proceeds available on each payment date. On each payment date, the trustee may draw funds in the general reserve account if asset collections are insufficient to cover the tax, if any, senior fees/expenses, and interest due to the rated notes. Upon the full repayment of the class A notes, any balance remaining in the liquidity reserve will be distributed to the subordinated notes.

In our cash-flow adequacy analysis of the transaction, we assume that one month of collateral collections will be lost due to the potential servicer commingling risk. In such a scenario, the liquidity reserve would provide liquidity support for the transaction.

**Interest Rate Risk**

The collateralized loans carry fixed interest rates, and the interest rate is fixed on the class A notes. As a result, there is no interest rate mismatch risk in this transaction.

In cash flow modeling we assume loan defaults and prepayment will first happen in the highest-yield loans, for the expectation of higher-credit-risk and higher-payment-burden feature of these loans. This will cause the weighted average asset yield to drop quickly over time.

**Credit And Cash-Flow Analysis**

We consider a significant performance deterioration of the underlying receivables to be the principal factor affecting rating transition in this transaction. We have applied our "Global Methodology And Assumptions For Assessing The Credit Quality Of Securitized Consumer Receivables" criteria, published Oct. 9, 2014, to the credit risk analyses in this transaction.

**Historical performance data**

We received the following historical performance data for auto loan pools originated by MBAFC:

- Static pool data grouped by origination month, including detailed origination amounts, repayments every month, and delinquency track every month. The data included vintage performance data from January 2014 to December 2018.

- Dynamic pool data: aggregate loans amounts, repayments, and delinquency statistics for each month from January 2014 to December 2018.
The pay-out ratio for each vintage is depicted in chart 3.

Chart 3

MBAFC's Loan Vintages
Payout ratio

MBAFC generally sets 90-plus and 180-plus days delinquencies for the recognition of loan defaults and loan losses, respectively.

In our credit-risk analysis, we assumed all loans delinquent for more than 90 days and loans that have been restructured would default, and used this classification to determine the base-case default frequency for the securitized pool. This assumption reflects the low but stable cure rates—returning from delinquency to current—of loans overdue for more than 90 days, and the practical collection operations MBAFC adopts. MBAFC typically start court processes and conduct vehicle repossession after loans become delinquent for 180 days. Our assessment also takes into account the comparison with the loans performance in major peers in the China auto finance industry and MBAFC's customer and product features.

We assume that loans overdue for more than 180 days or charged off would be deemed as a loss. We use this as a benchmark to estimate the recovery after defaults for the collateral pool.

MBAFC may agree to restructure loans in early delinquency, most likely within 60 days, if it believes the likelihood of continued repayment on the loans could increase after the restructuring. In our view, restructured loans typically have a much higher likelihood to default eventually than non-restructured loans do. As a result, we include the then-outstanding amounts of loans upon restructuring into the calculation of defaults. We however exclude the then-outstanding amounts of these restructured loans from the default calculation if we believe such loans have been
captured in the more-than-90-day-delinquent amounts. Charts 4 and 5 illustrate the cumulative default and cumulative loss experience of MBAFC's total auto loan portfolio, based on our assumptions of deemed default and deemed loss. The cumulative default and cumulative loss figures in Charts 4 and 5 might be higher than MBAFC's actual loan performance due to such assumptions.

Chart 4

**Historical Performance**

Cumulative default rate

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MBAFC attributes the decreasing delinquency after 2014 in part to the tightened companywide risk control, enhancement of credit policies and processes, and improved effectiveness of collection processes.

Data limitations

There was a limit to the data we received in respect of the credit risk analysis for this transaction.

Relatively short operating history of China auto captive finance companies limits the availability of historical performance data under economic stress

There are five years of performance data available for our credit risk analysis in this transaction. However, China has not experienced true macroeconomic stress during this period. This makes default and loss projections purely based on the historical performance data more difficult.

S&P Global Ratings in this case has considered different default extrapolation techniques to gauge the full-life loan default behavior. We took into account the worse-performing vintages and focused on the recent performance trend when determining base-case default rates, and applied a higher stress multiple to reflect higher expected losses under stress conditions.
Base-case assumptions and stressed default and loss

Our base-case default assumption for the collateral pool is 1.0%, based on the historical performance observed in the static pool and dynamic pool data. We applied a stress multiple to the base-case default percentage in the 'AAA' rating category. The magnitude of the stress multiple that we applied reflects the notes’ respective rating levels, as well as our consideration of the relatively short development history of auto loan securitization in China. We have not observed any real macroeconomic stress because the economic environment has been benign in the past decade. We therefore applied a higher stress multiple.

We have taken into account the remaining terms of the loans that are mostly 36 months or less, making the risk exposure period of the pool, or weighted-average life of the notes, relatively short. Moreover, despite the moderating economic growth in China, we expect the economy to remain relatively strong in the near term.

We gave limited credit to recoveries. Our base-case recovery assumption for the collateral pool is 10.0%, which we derived from the migration analyses of the "deemed default" and "deemed loss" loans. We gave 50% credit to the 10% base-case expected recoveries to arrive at a loss severity assumption of 95% for both rating stresses.

Table 4 shows a summary of the credit assessment.

Table 4
Credit Assessment Summary

<table>
<thead>
<tr>
<th></th>
<th>AAA</th>
</tr>
</thead>
<tbody>
<tr>
<td>Base-case default frequency (%)</td>
<td>1.0</td>
</tr>
<tr>
<td>Stress multiple used (x)</td>
<td>6.0</td>
</tr>
<tr>
<td>Default frequency (%)</td>
<td>6.0</td>
</tr>
<tr>
<td>Loss severity (%)</td>
<td>95.0</td>
</tr>
<tr>
<td>Minimum credit support after credit to recovery (%)</td>
<td>5.7</td>
</tr>
</tbody>
</table>

Cash-flow analysis

We analyzed the capacity of the transaction's cash flows to support the rated notes—i.e., timely interest payments and repayment of principal by the legal maturity date—by running several different scenarios correlated with a 'AAA' rating level for the rated notes. Our cash-flow analysis included various scenarios that reflect different combinations of the following factors:

- Level of defaults and recoveries commensurate with the rating level.
- Various default amount and default timing distribution.
- Recovery period (assumed to be nine months).
- Stressed fees and expenses upon servicer transition and unexpected expenses increase.
- The loss of one month of collections due to the potential commingling risk.
- Different prepayment rates.
- Compression in asset yield as a result of default and prepayment in the higher-yielding loans.
To evaluate the effect on cash flow of various pool default amount and default timing distributions, we modeled three different default curves: a front-loaded, back-loaded, and normal default curve. The curves we employed primarily reflected the default timing that we observed in MBAFC’s static default curves.

For the prepayment rates, we modeled three different prepayment curves. The prepayment stresses assumed include voluntary and involuntary (default) prepayments (table 5). In addition to the normal constant prepayment rate (CPR) test that mimics MBAFC’s historical prepayment behavior, we used a high CPR test—increasing to 15% annualized CPR under high CPR stress and a low CPR scenario (constant at 1%).

Table 5

Assumed Constant Prepayment Rates (CPR)

<table>
<thead>
<tr>
<th>Transaction seasoning</th>
<th>Normal CPR (% per year)</th>
<th>High CPR (% per year)</th>
<th>Low CPR (% per year)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>4.0</td>
<td>4.0</td>
<td>1.0</td>
</tr>
<tr>
<td>2</td>
<td>5.0</td>
<td>6.0</td>
<td>1.0</td>
</tr>
<tr>
<td>3</td>
<td>5.0</td>
<td>8.0</td>
<td>1.0</td>
</tr>
<tr>
<td>4</td>
<td>5.0</td>
<td>10.0</td>
<td>1.0</td>
</tr>
<tr>
<td>5</td>
<td>5.0</td>
<td>12.0</td>
<td>1.0</td>
</tr>
<tr>
<td>6</td>
<td>5.0</td>
<td>14.0</td>
<td>1.0</td>
</tr>
<tr>
<td>7+</td>
<td>5.0</td>
<td>15.0</td>
<td>1.0</td>
</tr>
</tbody>
</table>

Note: Total CPR shown is inclusive of voluntary and involuntary (defaults) prepayments.

Our preliminary ratings 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.

The transaction can pass all of the scenarios that we analyzed in our cash-flow adequacy tests. Some of the noteworthy features of the transaction cash flows are as follows:

- Credit support for the class A notes is provided by the subordination of the subordinated notes, overcollateralization, and a portion of the YSOC. The subordinated notes will never be paid down before the class A notes are paid in full. So the credit support from the subordinated notes for the class A notes will remain at a fixed amount and increase in percentage of outstanding pool balance when the class A notes are being paid down. That is unless the credit losses or commingling losses cause the transaction to become under-collateralized. Overcollateralization also will remain at the same amount at transaction closing and will increase in percentage of outstanding pool unless the credit losses or commingling losses cause the transaction to become under-collateralized. However, the amount of YSOC will amortize according to the schedule, and collections from YSOC will be treated as excess spread and used to cover negative carry and then pay down the class A notes only if the asset pool becomes under-collateralized due to commingling losses or credit losses. Otherwise, principal collections from YSOC assets will be used to cover indemnity expenses or released to the originator.

- Should credit losses or commingling losses occur at a later stage of the transaction’s life when the majority of the YSOC has been released or used to cover negative carry, the adequacy of the YSOC to cover commingling losses and credit losses would decrease. However, the risk of such
potentially leakage of principal collections from the YSOC is mitigated by sufficient credit support from the subordinated notes and the overcollateralization.

- Our cash-flow analysis indicates that scenarios in which the majority of loan defaults occur early in the transaction’s life—the front-loaded and normal default pattern—and a normal loan prepayment speed, will reduce the expected asset yield in this transaction, reducing the yield available to cover credit or commingling losses. Our cash-flow analysis shows that under these scenarios, the cash flow buffer will decrease significantly.

We analyzed the effect of an immediate moderate macroeconomic stress on the transaction to determine whether the maximum expected rating transition of the notes under such a scenario would be in line with those set out in our "Credit Stability Criteria," published May 3, 2010. The results of our analysis suggest that under a moderate rating stress scenario, the maximum expected rating transition on the class A notes would still fall within the bounds of those outlined in the criteria.

**Sensitivity Analysis**

We cash-flow modeled two additional scenarios to determine how vulnerable the notes would be to a downgrade under each scenario:

- Scenario 1: Base-case default frequency is 25% higher than our expected level of 1.0%.
- Scenario 2: Base recoveries are only 75% of our expected base recovery rate of 10%.

The minimum credit support under each scenario is set out in table 6.

**Table 6**

**Minimum Credit Support After Credit To Recovery (%)**

<table>
<thead>
<tr>
<th>Scenario</th>
<th>AAA</th>
</tr>
</thead>
<tbody>
<tr>
<td>Expected</td>
<td>5.7</td>
</tr>
<tr>
<td>Scenario 1</td>
<td>7.1</td>
</tr>
<tr>
<td>Scenario 2</td>
<td>5.8</td>
</tr>
</tbody>
</table>

Table 7 sets out what the rating level of each class of notes would be at transaction close under each scenario.

**Table 7**

**Rating Transition**

<table>
<thead>
<tr>
<th>Scenario</th>
<th>Class A notes</th>
</tr>
</thead>
<tbody>
<tr>
<td>Expected</td>
<td>AAA (sf)</td>
</tr>
<tr>
<td>Scenario 1</td>
<td>AAA (sf)</td>
</tr>
<tr>
<td>Scenario 2</td>
<td>AAA (sf)</td>
</tr>
</tbody>
</table>
Related Criteria

- Criteria | Structured Finance | General: Counterparty Risk Framework: Methodology And Assumptions, March 8, 2019
- Legal Criteria: Structured Finance: Asset Isolation And Special-Purpose Entity Methodology, March 29, 2017
- Criteria | Structured Finance | ABS: Global Methodology And Assumptions For Assessing The Credit Quality Of Securitized Consumer Receivables, Oct. 9, 2014
- General Criteria: Methodology: Timeliness Of Payments: Grace Periods, Guarantees, And Use Of 'D' And 'SD' Ratings, Oct. 24, 2013
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- General Criteria: Methodology: Credit Stability Criteria, May 3, 2010
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009
- General Criteria: Understanding S&P Global Ratings' Rating Definitions, June 3, 2009

Related Research

- An Overview Of China's Auto Finance Market And Auto Loan Securitization, March 12, 2019
- Macro And Industry Pressure Won't Be A Significant Threat To China Securitization In 2019, Jan. 24, 2019
- Rising Finance Penetration Hasn't Hindered Auto Loan ABS Performance In China Yet, Dec. 20, 2018
Presale: Silver Arrow China 2019-1 Retail Auto Loan Asset Backed Notes Trust

- How Does The Rising APAC Auto Loan ABS Market Compare With More Developed Ones?, March 9, 2018
- Securitization Performance Watch – China, published quarterly

The issuer has not informed S&P Global Ratings Hong Kong Limited whether the issuer is publically disclosing all relevant information about the structured finance instruments that are subject to this rating report or whether relevant information remains non-public.