Auto ABS Index – Australia: The Dinkum ABS Index 2Q20

Pandemic Pressures ABS Performance

Record High Delinquency: Both 30+ and 60+ day quarter-end arrears reached record highs of 2.7% and 1.7%, respectively, by end-2Q20. The increase in delinquencies reflects the impact of the coronavirus pandemic on individual borrower and business income; payment assistance provided by lenders has been mitigating some of the impact on borrowers. Higher arrears are also partly attributable to the reduced size of the index, as ABS issuance ceased at the start of the pandemic.

Spikes in 30+ day arrears are a result of a small number of lenders who reported COVID-19-affected loans as arrears. This provides some insight into future performance, although Fitch Ratings expects the full effect of the pandemic to be delayed past 1Q21, following the cessation of payment assistance and government support that offset some of the near-term performance deterioration.

At end-July 2020, about 7.7% of the outstanding auto portfolio was granted assistance for pandemic-related hardship. Assistance varied, with the majority of lenders providing full payment deferrals for three to six months and a smaller portion offering reduced repayments.

Loss Performance to Worsen: Annualised net losses increased to 0.6% in 2Q20, but remained in line with historically observed figures, down 2bp from the same time last year. Even so, Fitch expects arrears, defaults and recovery performance to weaken in the near term, as the extended lockdown in Victoria, ongoing restrictions and border closures continue to hurt the economy. Transactions with a higher proportion of corporate, SME or self-employed exposure are more likely to be affected, as businesses have been shut temporarily or have limited capacity to operate.

Strong Recoveries: Recoveries reached 44.2% by end-2Q20, above the five-year average of 39.0%. The rebound in recoveries indicates a strengthening in the used-car market as new-vehicle sales continued to contract. The used-car market is also partially boosted by pandemic-related factors affecting demand, including the government's instant asset write-off policy and a shift in customer preference toward second-hand vehicles as an alternative to public transport due to social-distancing measures and the potential risk of infection.

Related Research

Auto ABS Index - Australia: The Dinkum ABS Index 2Q20 (Excel file)

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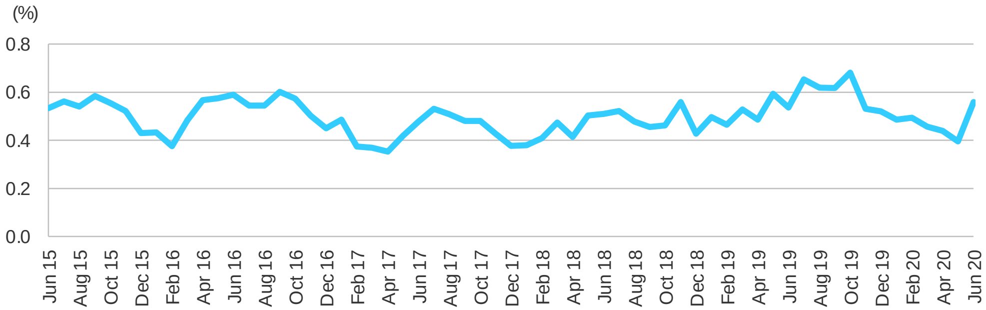
At a Glance

	2Q20	Δ	1Q20	2Q19
Auto ABS Index				
Number of transactions	25	↓	26	25
Collateral (AUDbn)	12.6	↓	13.0	13.7
30+ days (%)	2.74	↑	2.29	2.01
60+ days (%)	1.74	↑	1.11	1.02
Annualised net loss (%)	0.56	↑	0.46	0.54
Recovery rate (%)	44.22	↑	36.51	35.92
Absolute payment rate (%)	28.22	↑	26.73	30.75

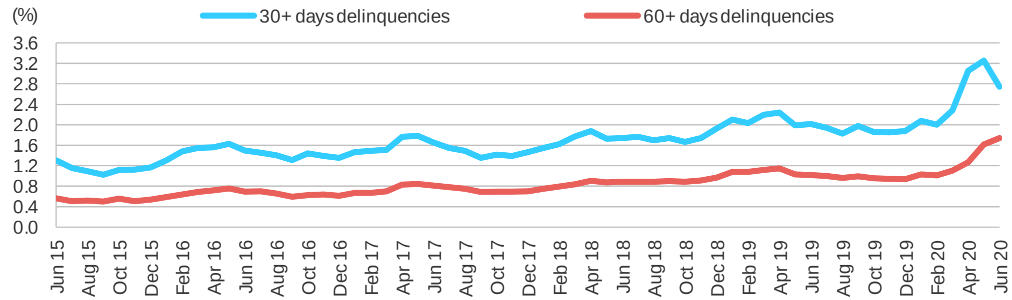
Source: Fitch Ratings

Fitch Dinkum ABS - Annualised Net Loss Index



Source: Fitch Ratings

Fitch Dinkum ABS - 30+ Days and 60+ Days Delinquency Indices



Source: Fitch Ratings

Prime Auto ABS Performance

Performance Overview

Cumulative gross and net losses at 36 months after closing remained in line with the previous seven quarters at 1.5% and 0.9%, respectively. The charts show lower gross and net losses for the final months of 2016, 2017 and 2018 vintages. This is due to fewer transactions having seasoned past 32, 23 and 10 months, respectively, meaning only a few issues drive the data. There were no new transactions added to the index in 2Q20. We expect the collateral underlying the index to decline and become more seasoned in the short term, as there have been no new public issues since January 2020. These compositional changes may place further pressure on portfolio performance metrics.

Index recovery rates increased to 44.2% in 2Q20, comparable with the three-year-high of 44.4% experienced in 4Q19 and above the five-year average of 39.1%. Stronger recoveries are partly attributable to a strengthening in the used car market that typically follows weaker economic activity; in this case, as a result of the pandemic. We expect the pandemic-related effects on borrower income, unemployment and underemployment to weigh on consumer appetite for spending on 'big-ticket' items, such as new vehicles over the coming months, further supporting the rebound in the used vehicle market.

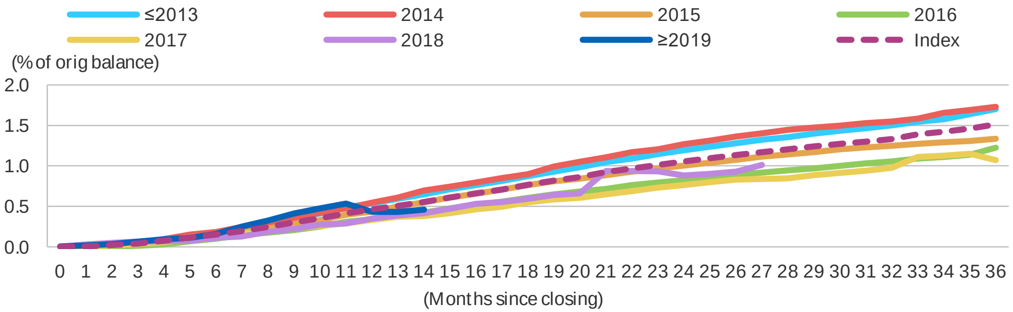
Recovery rate data were volatile in the quarter, declining to below zero in April and May. This reflects net losses which exceeded gross losses for the same period. This is due to timing mismatches, meaning recoveries recorded do not match the defaults for the same period. Lockdown restrictions in March and April contributed to temporary cessation of repossession activity, resulting in lower gross losses. On the other hand, restrictions on resale activity by lenders contributed to higher net losses for the same period.

Performance Expectations

Index performance is well within Fitch's expectations despite some deterioration in delinquencies. However, the steep decline in macroeconomic conditions globally means the agency is revising the base-case scenarios to reflect the potential effect on borrower performance in auto-loan portfolios. We expect higher delinquencies and subsequent defaults in the near term as a short but severe global recession hit major economies in 2020, underpinned by high Australian unemployment and GDP shrinking by 3.6%. Australia's economic forecast was revised at the end of August amid disrupted economic activity as a result of the imposition of a strict lockdown in the Melbourne metropolitan area in July-August.

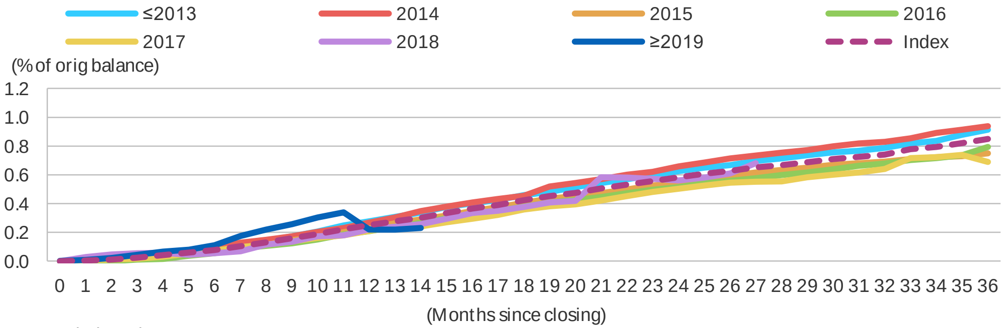
Fitch uses multiples of its base loss at each rating scenario to ensure ratings can withstand different stress scenarios. See our Consumer ABS Rating Criteria, dated June 2020, for more information. Existing ABS transactions are exhibiting strong levels of excess spread and rapid build-up of credit enhancement, which should provide some buffer against performance deterioration.

Auto ABS Cumulative Gross Losses (CGL) Since Closing



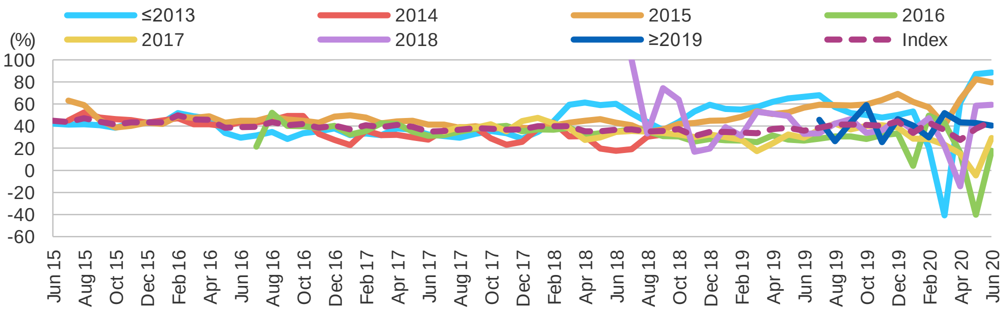
Source: Fitch Ratings

Auto ABS Cumulative Net Losses (CNL) Since Closing



Source: Fitch Ratings

Auto ABS Average Recovery Rates



Source: Fitch Ratings

Payment Deferrals

The Australian government has instructed lenders to provide flexibility to consumers and SMEs during the pandemic. All the lenders in our portfolio announced assistance measures, commonly in the form of hardship assistance programmes that offer partial or full payment deferrals for up to six months. Auto loans typically do not feature optional interest-only periods, as such, auto loan servicers have not offered interest-only periods to borrowers applying for hardship. They more often opt to capitalise arrears and increase repayments to fit within the original term, lower repayments or extend the loan term. Lenders assess borrowers on a case-by-case basis when offering payment holidays and other loan modifications.

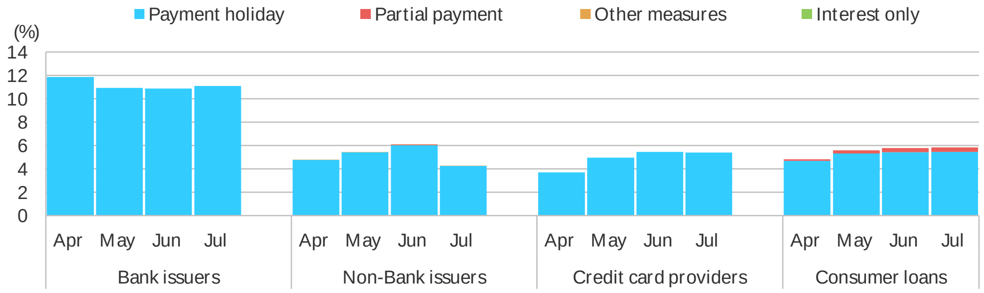
Fitch surveyed the lenders in its portfolio and on average 7.7% (of the total outstanding balance of loans) of auto portfolios as of end-July had been granted some form of assistance for pandemic-related hardship. An average of 5.6% of credit card and unsecured consumer portfolios were on payment assistance as of end July.

Reporting of loans on payment holiday varies between lenders; the general guideline for banks is that the reporting of these loans does not form part of stated arrears figures. However, reporting is varied as one major lender classifies loans as being in arrears until the payment deferral has been approved, while another has opted to classify loans in arrears throughout the assistance period. The take-up of payment holidays has been low for the majority of lenders with greater take-up in portfolios underpinned by SMEs .

Payment holidays can affect the liquidity of ABS transactions, but we do not expect our rated ABS transactions to experience liquidity shock, as most have multiple months of liquidity available to cover payment obligations, using the current low rates.

See The Dinkum ABS Index and Methodology for information.

COVID-19 Payment Assistance



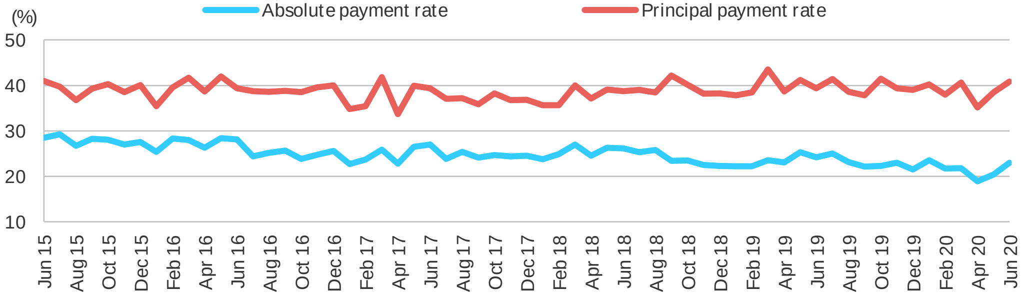
Source: Fitch Ratings

Auto ABS Payment Rates Slow

The absolute payment rate (APR) across Fitch-rated transactions was 23.0% at end-2Q20, a decrease of 1.2% from the same period in the previous year and up 1.2% from the previous quarter. The principal payment rate (PPR) remained roughly unchanged from the same time last year, at 40.9% at end-2Q20, compared to 39.3% last year. The rise in both payment measures during the quarter can be partly attributed to one transaction being called in May, with larger clean-up call payments flowing through as well as a decreasing outstanding portfolio balance with no new issues since January 2020. Increases in payment rates are partly offset by the full or partial payment deferral assistance offered by lenders during the pandemic.

Fitch expects the APR to remain subdued as a result of lenders implementing payment deferral programmes and weakened borrower serviceability due to reduced income for consumers and SMEs. Still, low interest rates continue to indirectly support borrowers' ability to service debt.

Fitch Australian Auto ABS Payment Rate



Source: Fitch Ratings

Key Drivers: Unemployment and Disposable Income

High Unemployment

Unemployment spiked to 7.4% in June 2020, passing a two-decade high. Fitch believes unemployment and disposal income are major determinants of portfolio delinquencies, and the agency expects the restrictions on economic activity and reduced business productivity, particularly in recreational services and retail sectors, to continue to have an adverse effect on borrower defaults. Household consumption decreased by 1.1% in the March quarter and 0.2% through the year. Declines of this severity were last observed during the GFC. The virus has prompted consumers and businesses to focus on essential spending with 84% of those receiving the JobKeeper payment from their employer using it to pay household bills.

The CPI fell by 1.9% qoq in 2Q20, representing the largest quarterly fall in the 72-year history of the measure according to the Australian Bureau of Statistics. The June quarter fall was driven by a significant decline in the price of automotive fuel and a free childcare scheme introduced by the government in April.

Furthermore, wages growth slumped to the lowest rate in 23 years, rising just 0.2% in the June quarter and 1.8% for the year. The three months to the end of June was the first full quarter that captured pandemic-related social and business restrictions in the wage price index, and excluded the government's JobKeeper subsidy. Prolonged low wage growth could affect auto-loan performance unless borrowers adjust their spending behaviour.

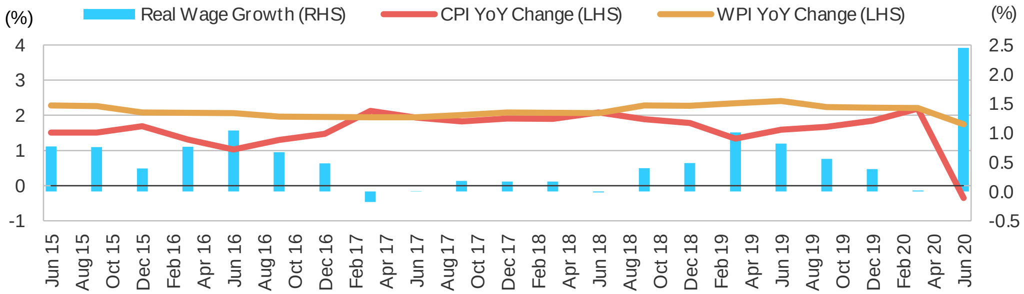
The policy response from the government and the Reserve Bank of Australia, coupled with payment relief from lenders, has contributed to easing some pressure on serviceability for some borrowers, limiting or delaying defaults and therefore forced sales, and partially mitigating a significant downward shock to recoveries. However, the economy faces uncertainty despite the policy stimulus, as risks of a resurgence of the virus could prompt nationwide lockdowns again and further contribute to reduced consumer and business confidence.

CPI, Wage Price Index and Unemployment Rate

Quarter	CPI index	Wage price index	Unemployment rate (%)
June 2020	114.4	134.1	7.4
March 2020	116.6	134.1	5.2
December 2019	116.2	133.5	5.1
September 2019	115.4	132.9	5.2
June 2019	114.8	131.8	5.3

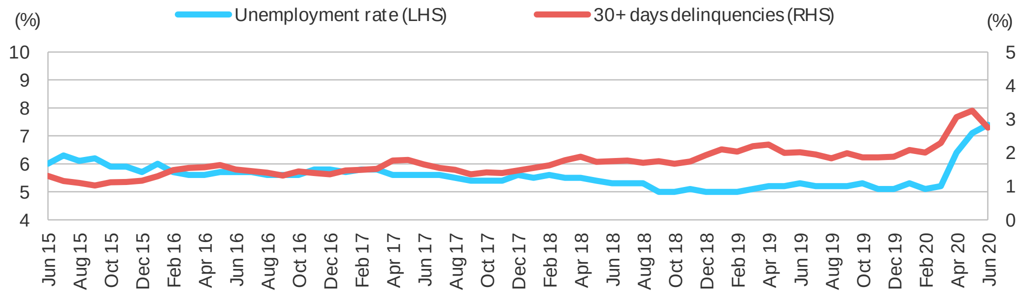
Source: Fitch Ratings, Australian Bureau of Statistics

Real Wage Growth (Comparison of Changes to CPI and WPI)



Source: Fitch Ratings, Australian Bureau of Statistics

Unemployment Rate



Source: Fitch Ratings, Australian Bureau of Statistics

Confidence at Five-Year-Low

The Westpac-Melbourne Institute Consumer Sentiment Index plunged to 75.6 in March – its lowest level since the recession in the early 1990s – before rebounding close to pre-pandemic levels at the end of the June quarter, at 88.1. Similarly, the sub-index "time to buy a major household item" fell by 8.0% to 106.3, when compared with June 2020.

Business confidence also weakened in the quarter, falling below GFC lows in April by 11 points to -3 index points, according to the survey by National Australia Bank Limited, and rebounded during May and June. However, Australian business appetite for spending in areas such as fleet renewal will be highly limited over the coming months, as the domestic economy slows dramatically.

Fitch expects consumer and business confidence to continue to remain subdued due to the pandemic and associated economic deterioration. Some government initiatives have been extended past the initial timeframe and continue to support borrower serviceability, but social-distancing measures and border closures continue to place pressure on economic activity. Consumer sentiment is expected to continue to be tempered by uncertainty around when all businesses can return to regular trading.

Developing Trends

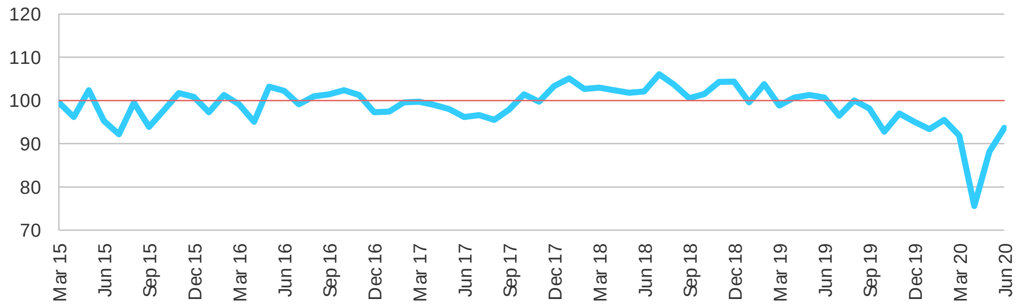
We expect the pandemic containment measures to contribute to historically high unemployment levels across various industries, particularly retail, hospitality and tourism due to restricted cross-border movement – domestically and internationally. The recovery is likely to be protracted should restrictions continue for a prolonged period or there is a return to stricter containment measures. We expect Australia to remain vulnerable to risks arising from high household debt and further international and bilateral trade tensions with China. A gradual economic recovery should begin in the second half of 2020, in Fitch's view, as goods exports to China which are already surging, continue, despite political tensions between the Australian and the Chinese governments. However, we do not expect the appeal of lower domestic interest rates to fully offset the economic insecurity being felt by local consumers in the current climate.

Consumer Sentiment

Quarter	Sentiment index
June 2020	93.7
March 2020	91.9
December 2019	95.1
September 2019	98.2
June 2019	100.7

Source: Westpac – Melbourne Institute

Consumer Sentiment Index



Source: Westpac - Melbourne Institute

Australian Prime Auto ABS Market

Other Pandemic-Related Effects

There were no new Australian auto-ABS transactions issued in 2Q20 or added to the index. Lower market activity continues to reflect the uncertain market conditions amid the pandemic and either a lesser need for funding or the use of alternative funding, for some issuers.

The Australian automotive sector is in a three-year contraction. June sales resulted in a 6.4% decline compared with the same time last year, although increased sales of trucks and heavy commercial vehicles softened the decline. We expect new cars sales to remain low as consumer sentiment stays subdued against a backdrop of high levels of uncertainty stemming from the pandemic, high levels of personal indebtedness and the fact that Australian consumers and businesses are continuing to recover from a series of recent natural disasters (bushfires, followed by flooding), which all place further downward pressure on demand.

From an operational perspective, servicing and collections continue to be being carried out remotely in most states, in line with the social-distancing measures to limit the spread of the virus. Some servicers use re-allocated staff from originations in their collection teams to manage the hardship applications anticipated from a greater number of delinquencies and hardship requests. Repossession activity has varied across the market, with some lenders temporarily placing litigation and asset sales on hold, while others operate with restrictions in place in accordance with the social-distancing guidelines. Servicers have generally preferred to defer or stagger vehicle sales until market demand increases. This helps support re-sale values and therefore recoveries.

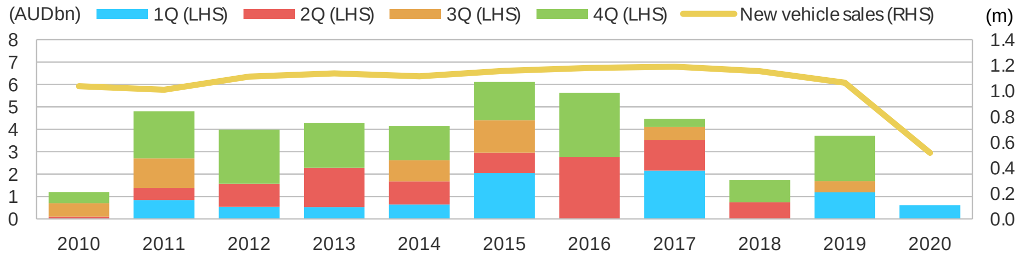
Expected Long-Term Trends

Fitch expects the collateral underlying the index to decline in the short term, further pressuring portfolio performance. In general, arrears ratios are likely to rise and become more volatile as transactions pay down because arrears balances are compared against declining pool balances, magnifying the effect that an individual delinquent loan has on the ratio. We expect the extended lockdown measures in Victoria to place further pressure on arrears and potentially increase payment deferrals.

Issuance may see a small boost as a result of a government-funded commitment facility of AUD15 billion, under which the Australian Office of Financial Management is directed to support primary market securitisations, warehouse financing and invest in public term issuance. The charts on the right only show issuance data and trends relating to public transactions. They do not encompass warehouses or privately placed transactions. Lower asset growth for lenders could lead to the relaxation of underwriting standards in an attempt to stimulate growth. However, we have been closely monitoring asset quality and have not observed such a shift to date.

Australian Auto ABS Issuance vs. New Vehicle Sales

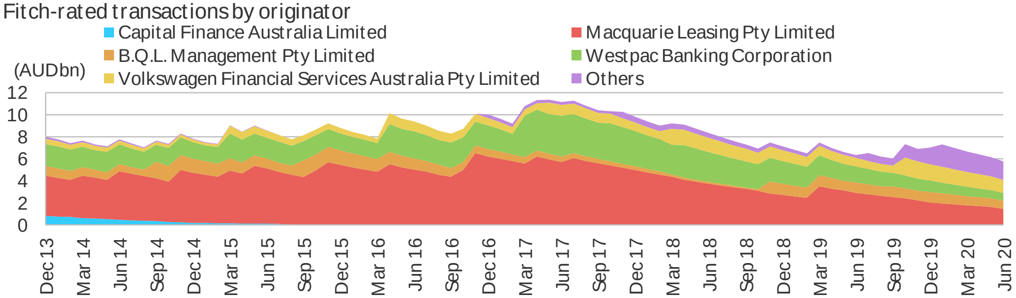
Fitch-rated transactions by quarter of issuance



Note: Warehouses and privately placed transactions not shown
Source: Fitch Ratings, Federal Chamber of Automotive Industries

Australian Auto ABS Outstanding Volumes

Fitch-rated transactions by originator



Note: Warehouses and privately placed transactions not shown
Source: Fitch Ratings

Fitch-Rated ABS Transactions at a Glance

	(AUD)		(% current balance)		(AUD)		(% original balance)		
Prime Auto ABS[a]	Original balance	Current balance	30+days	60+days	Gross losses	Net losses	Gross losses	Net losses	COVID-19 arrears classification
Crusade ABS Series 2016-1 Trust	1,300,000,000	116,847,367	9.68	7.85	22,006,261	14,861,976	1.69	1.14	Delinquent until approved for hardship
Crusade ABS Series 2017-1 Trust	2,150,000,000	570,027,462	7.14	5.62	30,586,049	19,749,082	1.42	0.92	Delinquent until approved for hardship
Driver Australia five Trust	742,698,295	265,320,327	3.47	2.14	7,609,735	5,079,922	1.02	0.68	Not delinquent
Driver Australia four Trust	495,018,686	99,922,171	3.18	2.34	4,656,912	3,189,457	0.94	0.64	Not delinquent
Driver Australia six Trust	1,000,006,169	772,192,180	1.83	1.02	1,262,717	917,961	0.13	0.09	Not delinquent
Eclipx Turbo Series 2017-1 Trust	351,500,000	79,819,121	0.58	0.28	383,323	169,234	0.11	0.05	Not delinquent
FP Turbo Series 2019-1 Trust	450,000,000	370,342,423	1.30	0.28	-	-	0.00	-	Not delinquent
Pepper SPARKZ Trust No. 1	511,600,000	300,497,898	1.34	0.63	4,187,502	3,284,844	0.82	0.64	Not delinquent
Pepper SPARKZ Trust No.2	616,700,000	500,986,566	0.75	0.35	903,786	799,837	0.15	0.13	Not delinquent
Series 2018-1 REDS EHP Trust	1,000,000,000	753,609,494	1.52	1.33	6,204,911	4,103,251	0.62	0.41	Not delinquent
Silver Arrow Australia 2019-1	580,100,000	413,272,509	1.01	0.47	3,398,785	2,539,600	0.59	0.44	Not delinquent
SMART ABS Series 2016-2US Trust	758,087,169	98,455,052	3.11	2.59	12,064,769	7,185,722	1.59	0.95	Not delinquent
SMART ABS Series 2016-3 Trust	1,764,800,000	267,067,032	3.14	2.25	30,754,590	20,294,358	1.74	1.15	Not delinquent
SMART ABS Series 2017-1 Trust	882,400,000	190,711,288	2.59	1.67	12,729,103	8,127,545	1.44	0.92	Not delinquent
SMART ABS Series 2017-2 Trust	588,250,000	153,556,765	2.03	1.41	9,716,816.83	6,272,812	1.65	1.07	Not delinquent
SMART ABS Series 2019-1 Trust	1,176,500,000	752,835,396	1.51	0.96	5,334,272	2,692,334	0.45	0.23	Not delinquent
Other asset types									
Flexi ABS Trust 2018-1	300,000,000	300,000,000	1.88	0.98	n.a	8,327,622	n.a	2.78	Not delinquent
Flexi ABS Trust 2019-1	300,000,000	300,000,000	2.67	1.42	n.a	7,856,746	n.a	2.62	Not delinquent
Flexi ABS Trust 2019-2	265,000,000	265,000,000	2.41	1.43	n.a	3,173,929	n.a	1.20	Not delinquent
Latitude Australia Personal Loans Series 2017-1	651,000,000	238,511,783	2.99	1.33	n.a	63,792,080	n.a	9.80	Not delinquent

n.a. = Information not publicly available
[a] Warehouses and privately placed transactions not shown
Source: Fitch Ratings

The Dinkum ABS Index and Methodology

Coverage: Fitch rates close to 100% of outstanding Australian securitised prime auto ABS.

Collateral: Transactions are included in the indices when prime auto loans and leases make up more than half of the collateral, with some containing a portion of equipment loans. Public warehouses and private transactions backed by prime auto loans and leases are also included in the indices.

Seasoning: Transactions are added to the arrears indices two months after issue to allow some seasoning to occur. Transactions are removed once fully redeemed.

Delinquent Receivables: The Dinkum ABS indices are calculated as a weighted average of the monthly delinquencies on the outstanding collateral balance. The Dinkum ABS indices are a good indicator of performance, especially when the total auto ABS outstanding volumes remain constant over time.

Annualised Net Loss Index: Delinquencies might show an upward trend when repayments are strong and are not accompanied by new issuance, as arrears increase as a percentage because the delinquent loans are not cleared as fast as repayments. For this reason, Fitch closely monitors the level of losses through the Annualised Net Loss Index (ANL), calculated as the weighted average of the monthly net losses divided by the total monthly outstanding collateral balance, and annualised linearly. ANL gives an indication of the level of losses that are expected each year.

Cumulative Loss Indices: Fitch also tracks defaults and losses since closing and compares levels through the life of the transaction to original expectations. For this reason, Fitch reports the level of defaults and losses in comparison with the original issue size, and expresses them in months since closing, rather than at a specific point in time, using the Cumulative Gross Loss Index (CGL) and the Cumulative Net Loss Index (CNL).

Losses: The losses (or defaults) are reported as the loan/lease amount at the time of default according to the servicer's reports. Net (or realised) losses are reported according to the servicer's methodology and when the losses have occurred in the trust. Net losses are reported before excess spread, but net of eventual sales proceeds.

Recoveries: These are reported as the difference between the monthly defaulted amount and monthly net losses, and expressed as a percentage of the monthly defaulted amount. Future recoveries from eventual future payments of delinquent borrowers – or from sales of non-performing loans to external parties – are usually excluded from the index.

Repayment Rates: Fitch monitors the Principal Payment Rate (PPR) and the Absolute Payment Rate (APR) to predict the amortisation profile of Australian securitised transactions. The difference between the two payment rates is that the PPR is calculated as monthly principal collections on the outstanding collateral balance, expressed in terms of a single monthly mortality rate. The APR is instead calculated as a monthly payment on the original collateral balance and is annualised linearly. Fitch has normalised its calculations to better take into account principal payments.

Fast Pay Down: The amortisation slope of a pool of auto loans/leases tends to be much more linear than in an RMBS due to the fast paydown of Australian auto ABS and the presence of balloon payments. For this reason, PPRs can increase significantly over the life of the transaction, while the APR is more constant and becomes a better predictor of future amortisation: for example, an APR of 30% would indicate that a transaction is expected to reach a 10% clean-up call option (or to have amortised by 90%) in three years.