
S&P Global Ratings

Mexican ABS Transactions - Stress Test of Administrators **Strengths in transactions that contribute to credit risk separation**

Date: July 5, 2022

Key Strengths

- Transactions have maintained sufficient credit protection to withstand deterioration in securitized assets.
- A replacement manager and substitution mechanism are agreed from the outset of the transaction.
- The legal structures of the transactions have proven effective in isolating securitized assets from the manager's credit risk.
- Collections are deposited directly into trust accounts, mitigating the risk of asset commingling.

Key Risk Factors

- A manager's default generally leads to deterioration in the performance of securitized assets.
- Such defaults increase the operational risk of the instrument relative to that of the manager.

Overview

Over the past decade, we have observed that administrators of certain asset-backed securities (ABS) in Mexico—who are often also the originators—have defaulted on their debt obligations or even filed for bankruptcy (*concurso mercantil*).

Despite these events, ABS transactions have continued to meet their payment obligations to investors on time. Since the mortgage-backed transactions impacted by the 2008–2009 crisis, we have seen increasing sophistication in structures placed in the market, designed to mitigate potential risks stemming from an administrator default. In our view, these enhancements have been favorable and have contributed significantly to the successful repayment of affected issues.

It is important to highlight that the incidence of such events has been low: fewer than 4% of total ABS transactions issued in Mexico from 2012 to date have experienced administrator defaults. We believe these cases merit analysis, as they underscore the strength of structured finance mechanisms that effectively separate the credit risk of the instrument from that of the administrator.

Strengths Observed in Transactions

Adequate Levels of Credit Protection

Credit protection levels in ABS transactions have proven sufficient to absorb portfolio deterioration while maintaining liquidity for payment obligations. Most transactions include cash reserves to cover expenses and interest, as well as accelerated amortization triggers tied to administrator default events.

Additionally, many transactions feature straightforward payment waterfalls, combining principal and interest collections to cover expenses, interest, and principal repayment when applicable. Others incorporate “full-turbo” amortization schemes, where remaining cash flows—after covering expenses and interest—are fully applied to principal amortization. These features have enabled transactions to deleverage rapidly in response to manager defaults.

For example, in July 2021, Alpha Holding S.A. de C.V. (unrated) defaulted on its debt obligations and, along with its subsidiaries, filed for bankruptcy. At the time, Alpha Credit Capital, S.A. de C.V., SOFOM, E.N.R. (Alpha Credit; unrated), held outstanding ALPHACB 18 certificates. Since the revolving period ended in July 2020, overcollateralization increased due to the full-turbo amortization feature, enabling the certificates to be fully amortized by June 2022—a full year before legal maturity.

Replacement Manager Designation and Substitution Mechanism

Recent transactions more consistently include a designated master servicer. This role typically covers reporting, monitoring of primary servicer activities, reconciliation, eligibility checks, and periodic audits of securitized portfolios.

Frequently, the master servicer is also named as the substitute servicer. In our opinion, this greatly reduces the uncertainty seen in earlier cases where substitution processes were less clearly defined. Moreover, recent transactions feature well-documented substitution mechanisms ensuring orderly transitions if replacement is required.

In the ALPHACB 18 case, following Alpha Holding’s bankruptcy, Alpha Credit was replaced as transaction servicer by Administradora de Activos Terracota, S.A. de C.V. (unrated), which had already been serving as master servicer. This arrangement significantly reduced uncertainty regarding securitized cash flows during the transition.

Legal Transfer to Trust Structures

The legal transfer of securitized assets to trusts continues to be effective in isolating them from originators’ credit risk, constituting what we consider a “true sale.” These structures typically rely on trust agreements alongside factoring or assignment contracts to perfect the transfer.

Trusts holding securitized assets are generally considered bankruptcy-remote, based on characteristics outlined in legal documentation. For instance, in the ALPHACB 18 transaction, securitized cash flows temporarily deteriorated due to a judicial precautionary measure. Once revoked, flows were released back to the trust, further demonstrating the effectiveness of the true sale mechanism.

Mitigation of Asset Commingling Risk

In most cases, collections are deposited directly into trust accounts or centralized master collection accounts. This structure mitigates the risk of asset commingling. Some legal frameworks establish eligibility criteria or early amortization triggers linked to the percentage of collections transferred into trust accounts. Where managers still initially collect funds, documentation limits the time allowed before transfer to the trust. These mechanisms have proven effective in safeguarding securitized assets from manager accounts.

Risks Arising from Manager Default

While ABS structures are designed to isolate securitized assets from manager credit risk, manager defaults can still temporarily affect portfolio performance. Impacts may include rising non-performing loan levels, reduced collections, and activation of servicer replacement mechanisms.

Although most transactions outline substitution procedures, such events remain disruptive, increasing operational risk. Temporary liquidity pressures may also arise, especially in transactions still within revolving periods.

Key risks in the event of manager default:

- Deterioration in securitized portfolio performance
- Increased operational risk
- Heightened liquidity risk

An illustrative case is Leasing Operations de México, S. de R.L. de C.V. (LOM; unrated), which defaulted in March 2014 while managing a securitization of equipment lease contracts (LOMCB 12). The issuance lacked a designated substitute servicer, delaying replacement by six months and disrupting portfolio flows. Arrendadora Actinver, S.A. de C.V., acting as trustee advisor, eventually assumed collections, recovering some defaulted assets. The transaction was nonetheless fully repaid at legal maturity in May 2016.

Conclusion

Over the last decade, several Mexican ABS transactions rated by S&P Global Ratings have ultimately repaid investors in full despite administrator defaults. While these events have at times undermined credit quality—prompting rating actions due to higher loss assumptions or greater operational risk—they also demonstrate the resilience of ABS structures. In our opinion, these mechanisms have been effective in insulating securitized assets from administrator credit risk while ensuring the continuation of investor payments.