ARC Ratings, S.A. places the public, final 'AAA(sf)' to 'BB+(sf)' ratings accorded to the A-D tranches of the Credit Protection Deed provided by York 2019-1 CLO DAC, on Negative Outlook

London, 1 June 2020 - ARC Ratings, S.A. (ARC) has placed the final, long-term public ratings of 'AAA(sf)' to 'BB+(sf)' accorded to the A-D tranches of the Credit Protection Deed provided by York 2019-1 CLO DAC to Santander UK PLC (Santander), on Negative Outlook due to the high exposure of the portfolio to the economic fallout from Covid- 19.

The above ratings relate to the credit risk the protection seller is exposed to on the reference portfolio.

ORIGINATOR	CLASS / TRANCHE	ATTACHMENT POINT	RATING CLASS	RATING	OUTLOOK	NEXT REVIEW DATE
Santander UK PLC	Tranche A	26.62%	Synthetic CLO	AAA(sf)	Negative	31 August 2020
Santander UK PLC	Tranche B	18.52%	Synthetic CLO	A(sf)	Negative	31 August 2020
Santander UK PLC	Tranche C	15.66%	Synthetic CLO	BBB+(sf)	Negative	31 August 2020
Santander UK PLC	Tranche D	10.21%	Synthetic CLO	BB+(sf)	Negative	31 August 2020

TRANSACTION OVERVIEW

The portfolio Reference Obligation Notional Amount is GBP 2.28bn as at 13 March 2020 with a Scheduled Redemption Date of 20 March 2029 and a Final Redemption Date of 20 March 2029.

The portfolio is comprised of loans to SMEs, with the majority (66.08%) secured against Commercial Real Estate (CRE) and 13.46% is unsecured; the largest sectors are Accomodation & Food Services (18.74%), Care Homes (14.36%), Professional Services & Other Services (10.70%), and Retail (7.37%). This portfolio's industry exposure is the primary driver of the rating action as, in ARC's opinion, the Covid-19 economic fallout represents a significant risk to the credit quality of the underlying obligors and the value of the colleteral. This exacerbated by Retail and Offices experiencing a deterioriation prior to Covid-19, which will be discussed in more detail below. Therefore, the Negative Outlooks reflects the significant uncertainty that is prevalent in the highlighted sectors which is compounded by them being located in the UK where a deep recession is predicted after experiencing a 5.8% reduction in GDP in March 2020, the largest decline on record.

ARC expects to receive an updated Reference Registry reflecting the forbearance measures requested by the underlying Obligors and granted by Santander prior to its next review. ARC has revised the review date to 31 August 2020, thus enabling the inclusion of the forbearance measures within the analysis.

RATING RATIONALE

The rating action is premised on the deteriorating state of the CRE market and that of the post Brexit UK economy, worsened by the outbreak of Covid-19. As a result of the factors considered below, ARC will determine the extent, if any, to which a future downgrade is necessary upon the provision of additional information. Key rating drivers include:

Key rating drivers include:

- Commercial Real Estate Sector: The largest collateral type, CRE account for 66.08% of which offices and retail form a notable proportion. This is a concern to ARC given that both sectors were already under strain due to shifting trends prior to Covid-19; thus, the outbreak has only exacerbated this. In ARC's opinion, the virus is anticipated to accelerate the decline of High Street retail and shopping centres, given the structural shift to online shopping as well as forced shutdown of shops selling non-essential goods. Prior to the aforementioned Covid related deterioration, office investment in London contracted in 2019 with GBP 12.6bn traded in 2019 compared with GBP 18.0bn in 2018, this due primarily to the uncertainty caused by Brexit. Nevertheless, the pandemic has resulted in more people working from home leaving office spaces unoccupied due to lockdown measures and, due to working from home's success, future office space demand is likely to fall. Consequently, owing to the uncertainty in the medium and long-term for both collateral types, there may be a shortfall in rent collections; a survey conducted by Remit Consulting in March 2020 analysed 80,000 leases from 6 of the leading property management companies and discovered that only 48% of tenants paid their rent on time and in full (however ARC notes the present portfolio does not consist of investment income producing real estate). This creates a concern to ARC as the value of the collateral provided as security is likely to decrease due to the deterioriating market conditions.
- UK Economy: The portfolio is concentrated in the UK as aforementioned, which is a concern for the transaction primarily due to the poor economic outlook of the country which is further exacerbated by Covid-19. UK household spending fell 1.7% in the first quarter of 2020 which has already been on a downward spiral due to the relocation of business units as a result of the uncertainty arising from Brexit and the depreciation of sterling, leading to knock-on effects on job creation, inflation rates and the value of savings. In addition, the virus has had a significant impact on the UK labour market with the total number of people claiming unemployment-related benefits totaling 2.1m as at 9 April 2020, which is 69% higher than in the previous month and the first time the claimant count has exceeded 2m since 1996. Accordingly, the number of vacancies posted by employers dropped 50% between March and April 2020. The combination of all of these factors leads to reduced discretionary spending power, severely impacting sectors such as retail and is an indicator of the reduced office space requirement. This despite the UK Government's introduction of various fiscal and monetary stimulus measures, including the Job Retention Scheme which has accepted approximately 8m workers, as at 19 April 2020, on the furlough wage subsidy programme.
- Forbearance Measures: At the direction of the Prudential Regulation Authority and other regulators, NatWest will not class obligors who request forbearance, such as interest or capital deferrals, as being in arrears or defaulted. In ARC's opinion, the impact of such measures in the short-term are credit neutral for the ratings of the Financial Guarantee as loans cannot default if they are granted forbearance. However, more significantly, in the medium to long-term ARC views this as credit negative as either there will be an increase in the quantum of

future repayments, placing greater financial pressure on the obligor, or extending of the maturity, which in turn will increase the loss horizon; both of which increase the probability of future claims being made against the financial guarantee.

- <u>Internal Ratings/Santander Rating Revisions:</u> Santander's internal ratings, to which ARC maps it's ratings, are designed to 'look through the cycle' and are based on historical data which encompasses the 2008/9 recession. Therefore, whilst the internal ratings are designed to incoporate the typical cycle, they do not reflect the impact of Covid-19 due to a combination of the pandemic being an unprecedented event (i.e. a freeze in the economy is not included within the historical data) and Santander having inadequate information currently due to a time lag between the outbreak occurring and the effects from it being realised and reported by their clients. Furthermore, Santander's ratings are adjusted manually and each client is assigned a risk analyst whom undertakes reviews as applicable although, due to the aforementioned implementation of forbearance measures and moratoria at the direction of the PRA, the underlying obligors have not been marked as being in arrears or defaulted. This inhibits ARC's ability to accurately assess the current credit quality of of the portfolio, as the negative prospects of the CRE market and UK economy are not being reflected in the internal ratings. As a result, ARC has brought forward its review date to 31 August 2020 to enable the inclusion of forbearance measures within its analysis.

SENSITIVITY ANALYSIS

ARC has run sensitivity tests to determine how the portfolio would be impacted if ARC's internal Covid rating adjustment matrix were to be applied to this portfolio; with industries and jurisdictions organised into those which ARC views as low, medium or high risk with a corresponding downgrade to the obligors mapped rating given the level of perceived risk. In ARC's opinion.

	Current Rating	Adjusted Rating (Rating Only)	Adjusted Rating (Rating & Collateral Values)
Tranche A	AAA(sf)	AA(sf)	A+(sf)
Tranche B	A(sf)	A(sf)	BBB(sf)
Tranche C	BBB+(sf)	BBB+(sf)	BB+(sf)
Tranche D	BB+(sf)	BB+(sf)	BB(sf)

Note: If ARC receives insufficient data prior to the review date to form an updated opinion on each of the underlying obligors, the above referenced adjustments will be applied.

KEY TIPPING POINTS	
Positive Turning Points • Given the current market circumstances, ARC does not consider there to be any upward movement in the medium term.	Negative Turning Points • Increase in the portfolio's probability of default, caused by a decrease in the internal ratings. • Sustained deterioration of the market, thus reducing collateral values and thus potential recoveries.

RELATED CRITERIA AND RESEARCH

Methodology

ARC Ratings' Global Structured Finance Methodology (September 2019)

ARC Ratings' Global Collateralised Loan Obligation (CLO) Rating Criteria (February 2020)

THIS DISCLOSURE IS FOR INFORMATION PURPOSES ONLY

ARC Ratings, S.A.

11 Hollingworth Court
Turkey Mill, Ashford Road
Maidstone, Kent ME14 5PP
UNITED KINGDOM

Phone: +44 (0)1622 397350
E-mail: arcratings@arcratings.com
Site: www.arcratings.com

Key Contacts:

Ashley Thomas	Jake Shoer	Mark Vrdoljak	Philip Walsh
Senior Structured Finance Analyst	Structured Finance Analyst	Head of Structured Finance	Chief Ratings Officer &
Lead Analyst	Back-up Analyst		Panel Chairperson
ashley.thomas@arcratings.com	jake.shoer@arcratings.com	mark.vrdoljak@arcratings.com	philip.walsh@arcratings.com

ARC Ratings, S.A. is registered as a Credit Rating Agency (CRA) by the European Securities and Markets Authority (ESMA), within the scope of the REGULATION (EC) N° 1060/2009 OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL, of 16 September, and recognised as External Credit Assessment Institution (ECAI).

This Review Report should be read together with initial Rating Report and with the subsequent Review reports.

Ratings assigned by ARC Ratings represent opinions on the capacity and willingness of an entity to make all required payments on a given obligation in a timely manner. The meaning of each rating category is explained in www.arcratings.com.

The rating(s) assigned by ARC Ratings in this report was / were sought by the entity whose financial commitments are being rated.

ARC Ratings provides to the entity whose financial commitments are being rated the documents that substantiate the rating to be attributed. This entity is thus given the opportunity to clarify or correct factual details, thus allowing the rating assigned to be as accurate as possible. ARC Ratings also grants the issuer the possibility of appealing a rating accorded by ARC Ratings as long as this appeal is supported on additional information that hasn't been taken into account in the original rating accordance.

ARC Ratings, S.A. historical default rates are published in the European Securities and Markets Authority Central Repository (CEREP) which can be accessed on the website cerep.esma.europa.eu/cerep-web/. ARC Ratings default rate is the probability of lack of full and timely payment of capital or interest or of the occurrence of any event that explicitly indicates that the future full and timely payment of those commitments will not occur (e.g., in case of insolvency).

Ratings do not constitute a recommendation to buy or sell, but only one of the factors to be weighted by investors.

Throughout the entire period during which ratings are valid, ARC Ratings monitors the issuer's performance on a constant basis, and may even bring forward the date of the review unless stated as point in time. Hence, prior to an investor using a rating, ARC Ratings recommends that it be confirmed, namely by consulting the list of public ratings available on the website www.arcratings.com.

ARC Ratings' ratings are assigned based on information, which may include confidential information, collected from a wide group of sources, which may include the entity whose financial commitments are subject to rating. ARC Ratings uses and treats this information with due care and attention. Although all due care was taken in the collection, cross-checking and processing of the information for the purposes of the rating analysis, ARC Ratings cannot be held liable for its accuracy. ARC Ratings must make sure that the information has a minimum level of quality prior to assigning a rating based on such information.

In the rating process, ARC Ratings adopts procedures and methodologies aimed at ensuring transparency, credibility and independence, and also that rating classifications are not influenced by situations of conflict of interests. Any exceptions to these principles are disclosed by ARC Ratings together with the rating of the financial commitment in question.