S&P Global
Ratings

Research

Presale:

Newtek Small Business Loan Trust 2023-1

May 30, 2023

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Preliminary Ratings

Class	Preliminary rating	Preliminary amount (mil. $)	Initial credit enhancement (%)(i)	SDR (%)	Min. BDR (%)(ii)	Min. BDR cushion (%)
A	A- (sf)	84.27	36.18	46.43	50.21	3.78
B	BBB- (sf)	19.59	21.00	37.28	41.53	4.25

This presale report is based on information as of May 30, 2023. The ratings shown are preliminary. This report does not constitute a recommendation to buy, hold, or sell securities. Subsequent information may result in the assignment of final ratings that differ from the preliminary ratings. (i)Includes the reserve account, overcollateralization, and subordination for the class A notes. (ii)Excludes the bottom 10% of all the BDR runs, assuming the base-case prepayment scenarios. SDR--Scenario default rate. BDR--Break-even default rate.

Transaction Profile

Expected closing date	June 8, 2023.
Stated maturity date	July 2050.
Collateral	An amortizing pool of unguaranteed interests in small business loans issued under the U.S. Small Business Administration's Section 7(a) loan program.
Note payment frequency	The 25th day of each month.
Initial purchasers	Deutsche Bank Securities Inc. and Capital One Securities Inc.
Seller, servicer, and originator	Newtek Small Business Finance LLC.
Depositor	Newtek Asset Backed Securities LLC.
Indenture trustee and administrator	U.S. Bank Trust Co. N.A.
Custodian and backup servicer	U.S. Bank N.A.
Owner trustee	Wilmington Trust N.A.

Rationale

S&P Global Ratings assigned its preliminary ratings to Newtek Small Business Loan Trust 2023-1's class A and B notes. The preliminary ratings reflect our assessment of:

- The credit enhancement in the form of overcollateralization, subordination (for the class A notes), a funded reserve account, and excess spread.

- The transaction's legal structure, which is intended to be bankruptcy remote.
- The diversified collateral portfolio, which consists of unguaranteed term loans issued under the U.S. Small Business Administration's (SBA) Section 7(a) loan program.
- Our expectation of timely interest payments on the non-written down balance of the notes, ultimate payment of interest on the written down note balance (if any), and ultimate principal payments on the notes, based on our Cash Flow Evaluator-Engine and assumptions commensurate with the ratings assigned under various interest rate scenarios.
- Newtek Small Business Finance LLC's (Newtek. the seller) servicing capability as a commercial finance business-based primary and special servicer, which is ranked as AVERAGE by S&P Global Ratings.

The notes are secured by unguaranteed interests in SBA 7(a) loans following the conveyance of the loans owned by the seller, Newtek, to the issuer.

Environmental, Social, And Governance (ESG) Factors

Our rating analysis considered the transaction's potential exposure to ESG credit factors. For Newtek, we view the exposure to environmental, social, and governance credit factors as neutral:

- Environmental credit factors. Physical climate risks such as floods, storms, earthquakes, or wildfires could severely damage properties and reduce their value, impacting recoveries if borrowers default and/or insurance is not adequate. SBA program and specific lender requirements mandate that borrowers have valid and existing insurance policies for any loan secured by a mortgaged property, with the servicer bearing responsibility for monitoring maintenance of insurance. Significant obligor, industry, and geographic diversification also mitigate environmental risk factors.
- Social credit factors. The SBA 7(a) loan program is mandated to provide capital to small business concerns that are not able to obtain financing through conventional lending channels, at reasonable terms. Each borrower must satisfy certain eligibility criteria, which include demonstrating an ability to repay the loan in a timely manner from the business' projected operating cash flow. The program promotes various initiatives for minority-, underserved-, veteran-, and women-owned business concerns.
- Governance credit factors. The collateral pools are typically managed by the originator or servicer. The roles and responsibilities of each transaction party and the allocation of cash flows are well defined, and the transaction is structured to achieve isolation of the assets from the originator or seller. There is also an additional layer of oversight from the SBA regarding the underwriting and servicing of the loans in the SBA 7(a) loan program.

Rating Considerations

We considered the following transaction strengths, weaknesses, and mitigating factors in our analysis.

Strengths

- Newtek has a long operating history, originating and servicing loans since 1994.
- U.S. Bank N.A. will act as the backup servicer in the event the current servicer resigns or is terminated.
- Newtek's seasoned and well-tenured senior and middle management team.
- Approximately 17% of the collateral securing the series 2023-1 notes was originally securitized in two Newtek Small Business Loan Trust transactions previously issued in 2016 and 2017, thus providing seasoning to the collateral securing the series 2023-1 notes.

Weaknesses

- The portion of the SBA 7(a) loans securing the series 2023-1 notes are not guaranteed by the SBA or any governmental agency, and any defaults or realized losses could impact the cash flows servicing the notes.
- The notes are sensitive to prepayment rates and liquidations of the collateral, with higher prepayments reducing the future cash flows available to service the notes.
- Inclusion of loans originated under the SBA's "SBA Express Loans" program. These loans are unsecured and underwritten according to a process that is relatively abbreviated when compared with standard 7(a) program loans. However, SBA Express Loans account for only 3.1% of the collateral.

Mitigating factors

- Credit enhancement in the form of overcollateralization, subordination (for the class A notes), excess spread, and a reserve account, which provide limited protection from realized losses, increased debt servicing costs, and prepayments.
- The servicer's proven track record in originating and servicing loans, with performance history spanning multiple economic downturns.
- Our cash flow analysis incorporated various interest rate, realized loss, and prepayment scenarios to ensure future cash flows were sufficient to service the notes under various economic conditions.
- SBA Express Loans were stressed in our modeling by increasing the probability of default and assigning no recovery credit.

Pool And Structural Characteristics

The collateral pool consists of the unguaranteed interest in 1,064 SBA 7(a) loans, with an aggregate current loan balance of approximately $129 million. Approximately 17% of the collateral consists of loans from two securitizations that were recently called by Newtek: series 2017-1 (183 loans; 16.9% of the total collateral pool) and series 2016-1 (five loans; less than 0.1%). This results in a higher seasoning for the series 2023-1 pool when compared to series 2022-1.

Table 1 shows the series 2023-1 pool characteristics as of March 31, 2023. We view this pool as generally comparable to the series 2016-1 through 2022-1 pools, even though it contains a small portion of SBA Express Loans, which are unsecured and are underwritten in a relatively abbreviated process when compared with standard 7(a) loans. The series 2023-1 collateral pool has both a lower weighted average current loan-to-value (LTV) ratio and a lower average principal balance compared with the series 2022-1 pool. The initial weighted average FICO score for series 2023-1 is higher than those for the prior series. No industry concentration is above 10%.

Table 1

Pool characteristics

	Series(i)						
	2023-1	2022-1	2021-1	2019-1	2018-1	2017-1	2016-1
Agg. loan principal balance ($ mil.)	129.02	121.44	101.66	107.35	105.02	76.19	56.07
No. of loans	1,064	724	677	623	547	375	321
WA loan rate (%)	10.44	6.24	6.00	8.24	7.74	7.00	6.23
WA spread over prime (%)	2.97	2.75	2.75	2.72	2.75	2.75	2.73
Avg. current principal balance ($000)(ii)	121.26	167.73	150.17	172.32	192.01	203.17	174.68
WA original term to maturity (mos.)	175	186	187	213	210	213	215
WA remaining term to maturity (mos.)	160	172	175	192	192	207	210
WA current LTV ratio (%)	86.08	95.75	90.39	86.40	90.09	93.95	93.22
WA borrower FICO score	734	725	730	716	712	705	708
Loan purpose (%)							
Refinance debt	32.13	36.34	42.78	48.24	56.37	53.86	48.13
Working capital	34.41	26.24	25.07	11.70	10.76	17.21	21.18
Real estate acquisition	19.30	18.02	13.99	22.47	18.00	18.96	15.30
Purchase business	5.45	9.34	9.67	7.23	5.46	2.76	9.03
Machinery and equipment	3.08	5.84	4.78	6.73	6.45	2.34	3.17
Leasehold improvements	3.15	2.43	1.73	1.61	1.69	1.47	1.75
Inventory purchase	1.10	1.19	0.38	0.96	0.24	0.01	0.16
Construction	1.28	0.52	1.55	1.05	0.97	1.74	1.28
Other	0.10	0.08	0.06	0.00	0.06	1.65	0.00
Top industry sectors (%)							
Food services and drinking places	7.92	9.85	5.36	9.63	8.40	11.11	9.54
Specialty trade contractors	9.59	9.43	5.77	4.09	4.58	2.70	3.37
Professional, scientific, and technical services	9.38	8.79	8.59	4.21	5.48	8.49	3.18
Administrative and support services	3.91	6.41	6.23	--	--	--	3.23
Ambulatory health care services	6.74	5.89	5.75	6.74	4.97	3.46	11.88
Merchant wholesalers, durable goods	4.93	5.74	6.31	4.00	3.01	--	--
Support activities for mining	--	3.25	--	--	--	--	--
Repair and maintenance	3.74	3.20	--	3.31	5.13	--	4.66
Merchant wholesalers, nondurable goods	3.88	2.65	3.94	--	--	--	--
Construction of buildings	--	2.49	3.79	--	--	--	--

Table 1

Pool characteristics (cont.)

	Series(i)						
	2023-1	2022-1	2021-1	2019-1	2018-1	2017-1	2016-1
Transportation equipment manufacturing	--	--	3.37	--	--	--	--
Miscellaneous manufacturing	--	--	2.93	--	--	--	--
Nonstore retailers	--	--	--	4.12	--	--	--
Truck transportation	--	--	--	6.99	8.66	8.47	--
Motor vehicle and parts dealers	--	--	--	3.32	--	--	--
Amusement, gambling, and recreation industries	4.49	--	--	5.31	5.26	6.70	8.82
Sporting goods, hobby, musical instrument, book, and miscellaneous retailers	3.73	--	--	--	--	--	--
Accommodation	--	--	--	--	2.98	--	--
Fabricated metal product manufacturing	--	--	--	--	4.78	4.31	--
Building material and garden equipment and supplies dealers	--	--	--	--	--	2.57	--
Personal and laundry services	--	--	--	--	--	3.81	--
Transit and ground passenger transportation	--	--	--	--	--	3.06	--
Nonmetallic mineral product manufacturing	--	--	--	--	--	--	3.22
Food and beverage stores	--	--	--	--	--	--	3.23
Clothing and clothing accessories stores	--	--	--	--	--	--	3.63
Other	41.70	42.30	47.97	48.29	46.74	45.32	45.22
Collateral type (%)							
Commercial real estate	32.01	38.39	43.35	51.70	51.36	54.84	54.49
Residential real estate	28.78	27.29	14.57	9.62	9.47	12.71	13.41
Machinery and equipment	10.17	16.87	19.22	20.32	19.34	12.69	17.61
Accounts receivable and inventory	21.54	13.95	17.65	10.48	9.81	4.04	6.22
Other	3.04	2.26	4.00	3.88	8.98	12.88	6.72
Unsecured	4.08	0.57	0.47	3.04	0.54	0.55	1.14
Furniture and fixtures	0.29	0.54	0.67	0.48	0.49	1.92	0.36
Liquid assets	0.09	0.13	0.06	0.47	0.01	0.36	0.05
Top state concentrations (%)							
	FL:14.11	CA:13.50	FL:11.22	CA:11.49	NY:9.81	NY:13.64	FL:20.03
	CA:13.81	FL:11.23	TX:10.90	FL:7.26	TX:9.47	CA:6.83	NY:10.16
	TX:9.24	TX:11.12	CA:10.69	NY:5.94	FL:9.31	FL:6.62	CA:9.82
	NY:4.67	NY:8.00	NY:7.60	TX:5.41	CA:9.03	IL:6.22	CT:6.62

Table 1

Pool characteristics (cont.)

	Series(i)						
	2023-1	2022-1	2021-1	2019-1	2018-1	2017-1	2016-1
	GA:4.02	NJ:4.78	MI:3.97	IL:5.03	CT:8.00	MA:6.06	TX:6.39
	IL:4.01	GA:5.08	NC:3.23	NC:4.52	NJ:5.35	VA:5.24	NJ:5.78
	NJ:3.46	PA:4.15	PA:3.22	CT:4.23	AK:4.62	OH:4.96	GA:5.07
	PA:3.43	OH:3.30	OH:3.05	VA:4.03	IL:4.20	CT:4.68	NC:4.86
	NV:2.62	CO:3.17	WA:3.04	GA:3.81	GA:3.71	NC:4.30	KS:3.94
	AZ:2.57	CT:3.13	CO:3.01	NJ:3.36	PA:3.33	RI:3.38	OH:3.48
	VA:2.49	NC:3.10	GA:2.86	DE:3.25	LA:2.97	NJ:3.25	MN:2.26
	NC:2.48	MO:2.27	CT:2.85	PA:3.00	OH:2.41	AZ:3.25	IL:2.18
	LA:2.44	MI:2.19	NV:2.64	RI:2.83	NC:2.41	MO:2.82	PA:2.15
	SC:2.37	IL:2.07	NJ:2.60	NV:2.61	AZ:2.20	PA:2.64	TN:1.98
	CT:2.34	VA:1.63	RH:2.44	LA:2.39	IA:2.12	TX:2.32	VA:1.91

(i)As of the cut-off date. (ii)Balance of unguaranteed interests. LTV--Loan to value. WA--Weighted avg.

Portfolio Analysis

The series 2023-1 collateral portfolio consists of unguaranteed loans under the SBA 7(a) loan program, which will total $129.02 million as of the closing date.

The results from the Small Business Portfolio Evaluator model, the Cash Flow Evaluator-Engine model, and sensitivity analyses take into account the actual collateral and the portfolio information that the transaction's arrangers provided, as well as additional assumptions or stresses that form the basis for the assigned preliminary ratings.

The SBA is a U.S. government agency that supports entrepreneurs and small businesses with loans made through partner banks, credit unions, and other lenders. Newtek, a direct SBA nonbank lender, is the seller and servicer for the series 2023-1's collateral. The SBA 7(a) loan program provides financial help for businesses with special requirements. Pursuant to SBA 7(a), the SBA is authorized to guarantee loans made to small business concerns for the purposes of plant acquisition, construction, conversion, or expansion, including the acquisition of land, materials, supplies, equipment, and working capital, when those small business concerns are not able to obtain financing through conventional lending channels.

Newtek Underwriting And Servicing

Newtek is a wholly owned subsidiary of NewtekOne Inc., which acquired National Bank of New York City in January 2023 and became a bank holding company. Newtek lends to small business borrowers for business acquisition, expansion, or opening; working capital; equipment purchase; commercial real estate; and refinancing. The company's underwriting guidelines include requirements for site visits by Newtek or a representative of Newtek. When deciding to lend to small business borrowers, Newtek considers certain factors, among others:

- The collateral, equipment, and/or other assets to be purchased with the loan proceeds;

- Borrower quality (i.e., tax returns);
- The balance sheet, including current debt;
- The accounts receivable and accounts payable aging summaries; and
- The down payment.

Newtek also considers a borrower's credit report when making lending decisions, with an emphasis on individual credit histories. Per the company, all loans are approved by the Newtek credit committee, assembled, packaged, and closed by Newtek employees, and funded by Newtek. Loans must meet Newtek underwriting guidelines as well as SBA rules and regulations. This process includes verification of all business income tax returns with the IRS and the request that financial statements be submitted on an annual basis after the loan closes. The company has stated that none of the receivables in series 2023-1 pool were originated as exceptions to either Newtek's or the SBA's underwriting guidelines.

Servicing

S&P Global Ratings' rankings on Newtek are AVERAGE as both a commercial finance business-based real estate servicer and a special servicer. Our outlook for both rankings is stable (see "Newtek Small Business Finance LLC Business-Based Real Estate Servicer Rankings Affirmed; Outlooks Revised To Stable," published June 10, 2021).

Structural Overview

Newtek Small Business Loan Trust 2023-1 is a special-purpose entity that was formed as a Delaware statutory trust. The issuer's only purposes are to acquire the collateral portfolio, issue the rated notes and equity, enter into the transaction documents, and engage in certain related transactions. We expect the issuer's special-purpose entity provisions to be consistent with S&P Global Ratings' bankruptcy-remoteness criteria.

Payment Priority

On each payment date, the trustee will distribute the funds available in the note account in the specified order of priority shown in table 2. The available funds exclude the 1.0% annual servicing fee on the balance of each SBA loan and the 0.6% premium protection fee on the guaranteed portion of the SBA loan where applicable.

Table 2

Payment priority

Priority	Payment
1	Reimbursable advances to the class OC-1 certificates.
2	To the owner trustee, indenture trustee/administrator, custodian, and backup servicer, the related indenture trustee/administrator, custodian, owner trustee, and backup servicing fees; unreimbursed out-of-pocket expenses (subject to a $75,000 annual expense cap in aggregate per year) in all cases as unpaid or unreimbursed for current and prior periods; and, solely from funds from the servicer transition account, any unpaid servicer transition costs of no more than $100,000.
3	Current and any carryforward class A note interest.
4	Current and any carry-forward class B note interest.

Table 2

Payment priority (cont.)

Priority	Payment
5	If no trigger event has ever occurred, an amount up to the required reserve account balance (1.5% of closing collateral balance) to the reserve account.
6	During a non-trigger event period, to the class A and B notes, pari passu and pro rata (based on a percentage interest determined at closing), until each class is reduced to zero. During a trigger event period, pay down the class A and then class B notes.
7	To the class A notes, any unpaid unapplied loss amount plus interest due to prior write-downs; and then any unpaid applied loss amount plus interest due to prior write-downs to the class B notes.
8	Indenture trustee/administrator, backup servicer, owner trustee, and custodian expenses not paid in item 2 above.
9	Any remainder to the certificateholders.

Credit Support

The notes receive credit support in the form of overcollateralization, subordination (for class A notes), excess spread, and a reserve account. The transaction structure also has a performance trigger in which the principal payment sequence will switch to sequential from pro rata between the class A and B notes if a trigger event occurs on any payment date.

At closing, the issuer will deposit approximately $1,935,285 into the reserve account; and, before a trigger event occurs, the reserve account will be replenished each period after interest payments on the notes. The trustee may withdraw from the reserve account to pay note interest or principal due to shortfalls in available funds, according to the payment priority waterfall outlined in table 2. Note that the reserve account will only be replenished during the initial non-trigger event period, which is the period before the first occurrence of a trigger event. During a trigger event period, the reserve account will not be replenished but will instead be used to cover any shortfalls in interest and principal payments. Also, to the extent that the reserve account is reduced during a trigger event period, there will be no replenishment even after the trigger event is cured and a non-trigger event period is reestablished.

The available excess spread amount will be determined by gross defaults, prepayments, recoveries, and the interest rates on both the notes and the loans. We apply rating level-specific assumptions that incorporate these factors in our cash flow stress tests.

A trigger event will occur if:

- The total default level as of the last day of any collection period exceeds the specified percentage and continues until the total default level is less than the corresponding percentage for three consecutive periods (see table 3);
- The cumulative realized loss level as of the last day of any collection period exceeds the specified percentage (see table 4); or
- An event of default under the indenture occurs and is continuing.

The total default level is not a cumulative default trigger but rather reflects the loans that are in default and not yet realized as a loss divided by the pool balance as of the closing date (see tables 3 and 4).

Table 3

Total default level

Collection period	Total default level (%)
1-3	2.500
4-6	4.375
7-9	6.250
10-12	8.750
13-15	12.500
16-18	16.250
19-21	20.000
22-24	23.750
25-27	27.500
28-30	31.250
31-33	35.000
34-36	38.125
37-39	40.000
40-42	41.875
43-45	43.750
46-48	45.000
49-51	46.250
52-54	47.500
55 and after	48.750

Table 4

Cumulative realized losses

Collection period	Cumulative realized loss level (%)
1-12	3.25
13-24	6.25
25-36	9.25
37-48	12.25
49 and after	15.25

Write-downs

The class A and B notes will have a payment priority over the ownership certificates, and the class A notes will also have a payment priority over the class B notes during any trigger event period. Losses on the collateral will be covered by overcollateralization and then the reserve account--to the extent that the portfolio balance exceeds the outstanding class A and B combined note balance. If the portfolio balance falls below the outstanding note balance on any payment date, the applied loss amounts may result in a write-down of the notes' principal amount. The applied loss amounts will be applied to first reduce the class B note principal balance to zero and then to the class A notes.

Any subsequent recoveries will be applied to increase the note principal balance to reimburse the previous write-downs. The reimbursement will be applied first to the class A notes and then to the class B notes. However, no interest on the write-down portion will be due for the periods when the note principal balance was written down. The amount will be deferred and due at the note interest rate by the legal final payment date.

Credit Analysis

Historically, we analyzed pools of small business loans using an actuarial approach based on the seller's historical lending data. We began using our Small Business Portfolio Evaluator in 2005 to incorporate an SBA data-driven analysis. This model uses Monte Carlo simulations to determine a specific default distribution for small business loan pools (see "Small Business Portfolio Evaluator," published July 27, 2022). To give credit to the series 2023-1 loan pool's diversification, we ran the entire portfolio through the model.

We introduced our revised methodology for U.S. small business loan-backed securitizations in March 2014, and in it we applied a targeted output approach and a scoring framework to derive an asset probability of default (PD) scaling factor. The scoring framework incorporates multiple factors for the performance history score (80% weighting to overall score), including the originator's default rate relative to the SBA data, the number of years of historical origination and default data, and whether the performance history incorporates a period of moderate economic stress. For the underwriting quality score (20% weighting), we consider factors such as the LTV ratio, the percentage of the pool with personal guarantees, the average debt service coverage ratio, the frequency of changes to underwriting criteria, and any regular outside audits of underwriting practices.

We assessed Newtek's performance history score as 4.0 and its underwriting quality score as 2.2. Given the 80/20 weighting of these two assessments, the overall scoring framework is 3.64, which would correspond to a 119% asset PD scaling factor (of a possible 75%-125% scaling factor range for an SBA loan pool) and a "weak" ranking. However, since we view the series 2023-1 pool as stronger than the series 2022-1 pool, we used a scaling factor of 108.33%, which is consistent with series 2016-1 through 2022-1.

To determine the appropriate recovery level for the series 2023-1 pool, we looked at the LTV ratio for loans secured by commercial real estate and equipment. We apply a haircut to the recovery rate if the LTV ratio is above 90%. For loans secured by a first lien on commercial real estate or equipment, we applied a 55% and 28% recovery, respectively, at the 'A-' level, and a 65% and 33% recovery at the 'BBB-' level. The pool's overall recovery level is the weighted average of individual loan-level recovery rates.

Interest Rate Mechanics

The underlying loans pay interest based on prime plus a margin, as stated in each loan agreement. The interest rates on the class A and B notes are based on the lesser of the 30-day average compounded secured overnight financing rate (SOFR) and prime, each with a spread. Newtek's transactions prior to series 2022-1 featured coupons based on the lesser of one-month LIBOR and prime, each plus or minus a spread.

In our analysis, we assumed the lesser of the 30-day average compounded SOFR and prime, each with a spread, using our standard interest rate curves.

Stress Scenarios

In reviewing the transaction's credit enhancement and subordination levels, our cash flow modeling assumptions included stressed loan defaults and recoveries after considering industry diversity within the pool, the pool's geographic concentration, the obligor concentration, and assumed recoveries on certain collateral types in the pool. The transaction's ability to pass the cash flow stress scenarios relied on the assumption that the servicer and the trustee (as backup servicer) will perform as required under the transaction documents. We also varied prepayment assumptions to include slow- and fast-pay scenarios in addition to base prepayment scenarios, and assumed the transaction uses all available proceeds, including prepayments, to pay down the notes.

Under the various stresses described above, commensurate with the assigned preliminary ratings, the transaction's cash flows indicate the timely payment of interest and principal on the class A and B notes.

Related Criteria

- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings , Oct. 10, 2021
- Criteria | Structured Finance | General: Global Framework For Payment Structure And Cash Flow Analysis Of Structured Finance Securities , Dec. 22, 2020
- Criteria | Structured Finance | Legal: U.S. Structured Finance Asset Isolation And Special-Purpose Entity Criteria , May 15, 2019
- Criteria | Structured Finance | General: Counterparty Risk Framework: Methodology And Assumptions , March 8, 2019
- Criteria | Structured Finance | General: Global Framework For Assessing Operational Risk In Structured Finance Transactions , Oct. 9, 2014
- Criteria | Structured Finance | General: Methodology And Assumptions For U.S. Small Business Loan-Backed Securitizations , March 28, 2014
- General Criteria: Global Investment Criteria For Temporary Investments In Transaction Accounts , May 31, 2012
- General Criteria: Principles Of Credit Ratings , Feb. 16, 2011

Related Research

- Economic Outlook U.S. Q2 2023: Still Resilient, Downside Risks Rise, March 27, 2023
- Newtek Small Business Finance LLC Business-Based Real Estate Servicer Rankings Affirmed; Outlooks Revised To Stable, June 10, 2021
- Global Structured Finance Scenario And Sensitivity Analysis 2016: The Effects Of The Top Five Macroeconomic Factors, Dec. 16, 2016

Appendix

Small Business Portfolio Evaluator and cash flow results

The Small Business Portfolio Evaluator is an integral part of S&P Global Ratings' methodology for rating and monitoring small business securitization transactions. The Small Business Portfolio

Evaluator is a one-period portfolio default model, which stochastically simulates default events for each small business (or obligor) using a Gaussian copula framework, which is a formula for determining correlation. The model aggregates the notional amount of the defaulted assets for each simulation trial, producing a probability distribution of portfolio default rates. This probability distribution of default rates describes the likelihood of any particular portfolio's default rate occurring. After calculating the probability distribution, the model derives a set of scenario default rates (SDRs). The model uses these SDRs as a factor in determining, for each credit rating, the assumed gross level of asset defaults. We generally would expect that a tranche with that rating should be able to withstand that relevant assumed gross level of asset defaults consistent with our rating criteria.

Interest rate scenarios

S&P Global Ratings' cash flow analysis uses different interest rate stress scenarios to test the impact different interest rate environments have on the transaction structure's ability to pay timely interest and ultimate principal on the rated notes. S&P Global Ratings' interest rate assumptions are based on historical interest rate levels and changes in those rates. Specifically, S&P Global Ratings subjected the transaction's cash flows to interest rate paths that increased over time, declined over time, declined and then increased, increased and declined, and followed the forward curve (see "Global Methodology And Assumptions For CLOs And Corporate CDOs," published June 21, 2019).

Cash flow results

S&P Global Ratings used its proprietary cash flow model to calculate a break-even default rate (BDR) for each tranche based on the portfolio's projected composition. The BDR represents the maximum cumulative portfolio default rate that a tranche can withstand while subjected to the interest rate scenarios described in the Interest Rate Scenarios section above and the default stresses shown in the table below, and still pay timely interest and ultimate principal by the notes' stated maturity date. The BDRs may change over the transaction's life if the assets' weighted average recovery rate, coupon, or spread changes. The BDRs will also change as the par amount and the portfolio's weighted average life change.

Annual defaults (% of cumulative defaults)

Default pattern	Year 1	Year 2	Year 3	Year 4	Year 5
I	15	30	30	15	10
II	40	20	20	10	10
III	20	20	20	20	20

For a tranche to be eligible for an S&P Global Ratings' credit rating, the BDR for each tranche must be higher than the portfolio's SDR for the specific rating, indicating that the portfolio can withstand a higher percentage of defaults than what is required for that rating level. Based on the portfolio's composition, the Small Business Portfolio Evaluator calculates the SDRs and S&P Global Ratings' proprietary cash flow model produces the BDRs.

Other defined terms

BDR: S&P Global Ratings uses its proprietary cash flow model to calculate a BDR for each tranche based on the portfolio's projected composition. The BDR represents the maximum cumulative portfolio default rate that a tranche can withstand while subjected to the interest rate and default stresses described in the Interest Rate Scenarios section above and the default stresses shown in the table above, and still pay timely interest and ultimate principal by the notes' stated maturity date. The BDRs may change over the transaction's life if the assets' weighted average recovery rate, coupon, or spread changes. The BDRs will also change as the par amount and portfolio's weighted average life change.

BDR cushion: The BDR cushion is the excess of the BDR above SDR at the assigned rating for a given class of rated notes.

S&P Global Ratings' credit rating: Our credit rating is the public rating, which is typically the issuer credit rating.

SDR: The SDR is the minimum level of portfolio defaults that each tranche must withstand to support the specific rating level using the Small Business Portfolio Evaluator.

Subordination: Subordination is calculated as the notes' total face amount (including the subordinated notes) that have payment priorities subordinate to the assessed class of notes divided by the notes' total face amount (including the subordinated notes).

Target portfolio: The target portfolio consists of collateral that has already been purchased and/or collateral for which a commitment to purchase has been initiated, as well as hypothetical portfolio information that the arrangers present to S&P Global Ratings for its rating analysis.