PCR Verum Ratifies Ratings Awarded To Navistar Financial as 'AAA/M' and '1+/M'; Stable Perspective'

Monterrey, Nuevo Leon (September 13, 2022): PCR Verum ratified the long-term and short-term, corporate ratings of Navistar Financial, S.A. de C.V., Sociedad Financiera de Objeto Múltiple, E.R. (NF) as 'AAA/M' with Stable Perspective and '1+/M', respectively.

The NF's ratings are based on the strong operation and commercial support and synergies existing with TRATON SE (Volkswagen AG), which, in PCR Verum's opinion, has the highest credit quality at national level. Such support is manifested as equity support, technical support, risk control, acquired bank resources (including a committed line of credit) among others; we also evaluate the strategic importance of its local operation as high.

NF has shown a favorable and sound evolution in its financial performance following an orderly growth, demonstrating a good equity basis, which has been strengthened in recent periods. It also has sufficient funding sources for future operations, which are diversified in the type of financial institution. Yet there is a higher deterioration in its delinquency levels, and its high credit concentrations are maintained; furthermore, there may be changes in the macroeconomic environment which might eventually reduce the rate of the loan placements of the SOFOM and might continue to put pressure on the payment capacity of some of its clients.

PCR Verum considers that the profitability level of NF shows significant recovery in respect of its historical performance. The net profit as of June 2022 was MX$ 411 million, resulting in indicators of asset profitability and average equity of 5.9% and 15.6%, respectively (2021: 3.7% and 11.1%); which, in comparison, are better than those of other non-banking financial institutions. This occurred mainly due to lower credit costs (direct impact on shareholder's equity) and a relative containment of operation expenses.

Since the recovery in the transport industry during this year 2022 will be gradual, the NF's strategy consists in the consolidation of its portfolio, expecting to increase its current portfolio levels (NF's forecasting: +15%). The company, being a captive financial institution (brand International), intends to maintain its credit products and does not expect any significant change in its business mix; however, because of the improvement observed in its funding costs, the access to larger clients is more feasible, and now it will look for large fleet loans and corporate clients. The net financial margin (considering the net lease income) with respect to its average asset was a well-suited 8.4% (2021: 7.4%) as of the close of 6M22.

Additionally, it is expected that the sale volumes within the segment of new trucks and tractors in the Mexican market for the next two years experience a slight improvement, with the brand International keeping a share between 20% and 25% in such market. Moreover, we consider that NF will continue to fund around 40% of the total sales.

The equity of Navistar Financial has been kept at high levels despite the estimates in portfolio directly affecting equity calculated during the first semester of 2022 (~MX$300 million: 5.7% of its shareholder's equity). Hence, its equity/total assets ratio was estimated at 38.7% as of 2Q22 (2021: 37.2%). Furthermore, the use of bank funding and commercial paper has been moderate in respect of its asset quality, reflecting a favorable leverage ratio (total liability/shareholder's equity), which was 1.6x on the same date (average 2018 – 2021: 2.4x). We believe that, despite the decrease in the company's profit and the potential future effects on the loan portfolio, NF will be capable of maintaining its asset quality at a favorable level.

Due to the effects of the recent economic crisis, the company's asset quality shows impairment. As of the close of 2Q22, the gross non-performing portfolio (Stage 3) represents 7.9% of the total portfolio, amounting to MX$932 million (-0.1% net of allowances). While NF showed an appropriate capacity to keep health its portfolio, a significant increase in its troubled portfolio indicator was observed since the last quarter of 2020.

The credit risk hedge covers an appropriate 1.0x of the total non-performing amount. We expect the company continues to set aside an allowance of at least 100% for its non-performing portfolio, based on the implementation of a conservative preventive policy in its loan allowances, as the company has been doing since its beginnings.

NF has taken actions to improve its non-performing portfolio. Currently, as a preventive measure, the financial institution is seeking to grant loans with a larger down payment, which will help to lessen the severity of the loss, as well as additional guarantees to increase the hedge. For the current cases in the non-performing portfolio, the administration implements a special approach to clients in Stage 3 and constituted a special collection committee to follow up relevant accounts.

Historically, the financial institution has shown significant concentrations in its loan portfolio. As of the close of 2Q22, the 20 major common-risk debtors concentrate 36.0% of its portfolio, which is equal to 0.8 times (x) its equity (2021: 29.8% and 0.6x, respectively).

NF funds its operation through short-term and long-term loans hired to development and commercial bank, representing 72.9% of its total cost-bearing liabilities; as well as through issues of unsecured short-term debt (27.1%). We believe that the SOFOM has an outstanding diversification of its funding sources, since it has lines of credit with nine financial institutions, amounting to MX$13,000 million (~MX$7,700 million available) in aggregate approximately as of 2Q22. Furthermore, it is important to note that NF has a committed line of credit, fully available, in the amount of US$50 million in aggregate, which provides an important backup to fulfill the company's financial obligations. So far, there has been no need to use such lines of credit.

The issuer has a “Stable” outlook. The rating is at the highest level awarded by PCR Verum. Potential effects will depend on the financial situation of the parent company since it might have a direct impact on the operations of its Mexican subsidiary.

Navistar Financial was incorporated in 1997 as a SOFOL (regulated entity), and it changed its business denomination to SOFOM in 2007. NF is subordinated to Navistar International Corporation (NIC), which helps NF to maintain a sound participation in the funding of the sales of the brand International in Mexico. The company's main business activity is the granting of funding to both distributors (wholesale loans) and individuals or entities (retail loans and financial lease, mainly) for the acquisition of trucks, tractor-trucks, buses, and spare parts of the brand “International,” by means of the company's distributors and sale points, which are located in every state of the Mexican Republic.

The following methodology has been employed to determine these ratings:

- Methodology for rating Banks and Other Financial Institutions (April 2020, approved in October 2020).

Contact Information:

Daniel Martinez Flores
Assistant General Manager of Analysis
M daniel.martinez@verum.mx

Jesus Hernandez de la Fuente
Associate Manager
M jesus.hernandez@verum.mx

Jonathan Felix Gaxiola
Director
M jonathan.felix@verum.mx

Mexico City Office
Amores #707 P.H. 1 Col. del Valle
Del. Benito Juarez, CDMX
C.P. 03100
T (52 55) 6276 2026

Monterrey Office
Arq. Pedro Ramírez Vázquez #200-12 Piso 5
Col. Valle Oriente
San Pedro Garza Garcia, N.L., C.P. 66278
T (52 81) 1936 6692

Regulatory Information:

The latest revision of the NF's ratings was carried out on July 12, 2021. The financial information used to analyze and determine the corresponding ratings covers a period from January 1, 2017, to June 30, 2022.

The meaning of the ratings, the explanation about the manner in which the ratings are determined; the periodicity of the rating follow-up; the rating specificities, characteristics and limitations; the rating methodologies; the committee's voting structure and process to determine the rating; as well as the criteria to withdraw or suspend a rating can be consulted on our web site http://www.pcrverum.mx.The models or criteria implemented to obtain the ratings granted above are not different from those used in the initial ratings.

According to the rating methodology aforementioned and under the provisions in Article 7, Section III, of the *General provisions applicable to securities issuer and other participants in the stock market*, it is worth mentioning that the corresponding rating may be subject to update from time to time. The ratings awarded are an opinion about the financial solvency, financial strength or asset management capacity, or respect of the duties performed in order to comply with the issuer's business purpose; all this in connection with the relevant issuer or issue. Consequently, the ratings do not constitute recommendations to buy, sell or maintain any instrument, or to carry out any business, transaction, or investment.

The ratings stated above are based on the information provided by the issuer and/or obtained from sources deemed accurate and reliable, including audited financial statements, operational information, corporate presentations, sector analyses, and regulatory analyses. Such information was reviewed by Verum, Calificadora de Valores, S.A.P.I. de C.V. to the necessary extent exclusively, and only in connection with the awarding of the relevant ratings, according to the methodology mentioned above. Under no circumstances, it will be understood that Verum, Calificadora de Valores, S.A.P.I. de C.V. has authenticated, guaranteed, or certified the accuracy, correctness, or completeness of such information; therefore, Verum, Calificadora de Valores, S.A.P.I. de C.V. undertakes no liability for any error or omission or the results obtained from the analysis of such information.

The goodness of the instrument or solvency of the issuer and the opinion on the capacity of the issuer concerning the asset management and business purpose accomplishment may be modified, as applicable, upgrading or downgrading the relevant ratings, without liability to Verum, Calificadora de Valores, S.A.P.I. de C.V. The corresponding ratings take into account an analysis of the issuer's credit quality or financial strength; it does not necessarily reflect a statistical probability of payment default. Verum, Calificadora de Valores, S.A.P.I. de C.V. awards the corresponding rating following the healthy practices in the market, as per the applicable regulations, and according to Verum's Conduct Code, which may be consulted at http://www.pcrverum.mx

The ratings described above were requested by the issuer (or on behalf thereof); therefore, Verum, Calificadora de Valores, S.A.P.I. de C.V. has received its corresponding compensation for the rating services provided. However, it is worth mentioning that Verum, Calificadora de Valores, S.A.P.I. de C.V has not received any payment from the issuer for concepts other than those related to the study, analysis, opinion, assessment and judgment on the issuer's credit quality and the provision of rating services.