SOVEREIGN
AFRICA RATINGS

# Servicer Rating Methodology

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# 1. Introduction

This methodology outlines SAR's fundamentals and analytical approach to assigning servicer ratings in several sectors and for different types of underlying servicers and assets. These ratings give lenders, investors, and other market players information about the competence of the servicers handling their portfolios. They are also a helpful tool for servicers, helping them to find possibilities for performance improvement, operational strengths and weaknesses, and benchmarking against relevant peers and industry standards.

The general process includes the servicer providing information to SAR relating to its servicing platform and operational environment, as well as an onsite inspection of the servicer where SAR's analysts would engage the relevant staff members and concomitant parties of the servicer. The initial assessment incorporates a review of the servicer type to determine whether the reviewed party is a (i) primary servicer – loan administration for performing loans with direct borrower contact, (ii) special servicer – focused on managing non-performing assets (defaults, covenant breaches, and repossessions) or a primary servicer for residential borrowers with below-average credit scores, or a (iii) master servicer – monitoring of loans serviced by other servicers and ensuring accurate investor reporting and compliance with servicing agreements and industry standards. It is worth noting that the functions of servicers may overlap, including one being a backup servicer on standby to assume the duties of a primary servicer where the primary servicer's performance becomes inadequate in relation to its servicing agreements with the originator. The weights below are indicative and may have slight differences depending on the servicer type under review. For example, Default Management and Loss Mitigation will be weighted higher for special servicers.

# 2. Methodology Overview

| Pillar | Weight | Attribute | Weight |
|---|---|---|---|
| Management and Organisational Structure | 25% | Experience | 7.5% |
| | | Business Strategy | 7.5% |
| | | Structure | 10% |
| Loan/Asset Administration | 35% | Loan/Asset Boarding and Document Tracking | 10% |
| | | Payment Processes | 10% |
| | | Insurance Management | 7.5% |
| | | Reporting | 7.5% |
| Customer Service, Delinquency and Default Management | 35% | Customer Service and Contact | 15% |
| | | Default Management and Loss Mitigation | 20% |
| Comparative Analysis | 5% | Peer Analysis | 5% |
| | 100% | | 100% |

## 2.1. Pillar 1: Management and Organisational Structure

### Attributes 1 and 2: Experience and Business Strategy

In determining the experience score, SAR will review the number of years the servicer has been in existence and its tenure in servicing the various asset type classifications. Staff competency will be evaluated based on average performance relating to customer service and overall company performance incorporating loss mitigation track record, reporting efficiency, and average time for resolving delinquencies (elaborated upon in the sections below). The staff turnover rate, staff size for adequacy, skills base and training standards are also reviewed to assess the staff's efficiency.

The servicer's business strategy is assessed by reviewing management's quality and level of oversight of the entity's activities. In this assessment, management's responses to changing market dynamics, planning for expansions (or contractions), mergers and acquisitions, and portfolio volume statistics will be evaluated to determine any disruptions to the servicer's lines of business due to management decisions.

### Attribute 3: Structure

SAR will review the servicer's internal reporting lines and segmentation of duties, portfolio complexity, as well as the robustness of the compliance, information technology, human resource, and legal functions. Segmentation of duties will receive granular attention in the core of the business, payment processing, where SAR will review whether the design of operations ensures separation of duties and strong controls for the movement of funds.

## 2.2. Pillar 2: Loan/Asset Administration

### Attribute 1: Loan/Asset Boarding and Document Tracking

**New Loan/Asset Boarding:** SAR assesses the servicer's policies and procedures for new loan and asset boarding, as well as its compliance with these policies and procedures. The accuracy and timeliness of adding loans and assets to the servicing system are also reviewed, as well as the level of automation.

**Document Tracking:** SAR reviews the completeness of information (loan file tracking versus document tracking) and storage procedures, assesses document tracking methods and the measures put in place to ensure lien perfection, and evaluates the efficacy of the system used to monitor and pursue omitted documents.

### Attribute 2: Payment Processes

**Payment Processing:** SAR assesses the operational design to ensure there are suitable controls over the movement of funds and separation of duties. It establishes whether funds are appropriately reconciled and assesses any issues with aged open reconciling items. The assessment also takes into account the degree of process automation.

### Attribute 3: Insurance Management

**Loan/Asset Insurance:** SAR reviews the servicer's procedures for monitoring loan and property insurance policies, including coverage levels. It also assesses the servicer's processes for the involvement of external parties in the insurance process.

### Attribute 4: Reporting

**Investor/Client Reporting:** SAR expects reporting to be conducted by appropriate staff (separate from funds transfer and reconciliation staff) and for the reporting to be reflective of the servicer's performance relative to its servicing agreements.

## 2.3. Pillar 3: Customer Service, Delinquency and Default Management

### Attribute 1: Customer Service and Contact

**Customer Service:** SAR will evaluate the adequacy of policies and procedures that are in place for addressing resolutions and the servicer's maintenance of timely responses to meet customer needs while adhering to compliance measures. SAR also assesses the types of communication channels employed for effectiveness and frequency. SAR therefore assesses the appropriateness of technology that is utilised for communication with borrowers, including interactive response systems for managing peak traffic periods and handling incoming calls, call routing software, and borrower self-service capabilities on websites, portals, and mobile applications.

**Asset/Borrower Review:** SAR reviews the practices for monitoring portfolio performance. The following activities may be included in SAR's review, which is primarily related to the servicing of commercial mortgage loans: financial statement and tenant analysis; property insurance monitoring; loan and transaction covenant compliance; upkeep of the servicer "watchlist"; and management of surety and reserve accounts. SAR also examines the management of any external vendors providing these services, as well as the inspection and valuation procedures.

### Attribute 2: Default Management and Loss Mitigation

**Delinquencies:** In addition to reviewing the delinquent statistics, SAR evaluates the servicer's policies and practices for sending out late notices and getting in touch with borrowers in the early phases of delinquency.

**Default Management:** SAR assesses the servicer's processes for loans and accounts that go unresolved during the early stages of delinquencies (30 – 90 days) and reviews the defaulted and delinquent portfolio's performance. Loan servicing for defaulting borrowers might be done by primary servicers or special servicers. In certain jurisdictions, defaulted loans are managed by the primary servicer until a specific trigger occurs, at which point the loan transfers to the special servicer for final resolution. The method could be less explicit when there is no differentiation between the primary and special servicer. Loans that have fallen behind should be promptly transferred to the special servicer once this procedure is set up. The legal and economic subtleties in the jurisdiction(s) where its assets are being managed are required to be clearly understood and appreciated by special servicers (and primary servicers when assigned these responsibilities).

**Loss Mitigation:** For the management of foreclosure, loan recovery, and general loss mitigation, SAR assesses the servicer's procedures for decision-making and approval processes, the timeliness of resolutions relative to the servicer's agreements and internal controls, as well as the track record of the servicer's resolution activities. SAR assesses the servicer's range of strategies and the experience of its asset managers and loss mitigation staff in loss mitigation activities. SAR will also assess the proceeds achieved from foreclosed and repossessed assets relative to peers. Policies and procedures relating to the management of third-party involvement in liquidation proceedings are also assessed.

## 2.4. Pillar 4: Comparative Analysis

### Attribute 1: Peer Analysis

SAR performs peer comparisons considering Pillar 3: Customer Service, Delinquency and Default Management. This approach ensures consistent outputs using a weighted average approach in scoring each factor under the pillar to establish the associated ranking order. SAR may drag or lift the servicer's rating by up to two notches depending on its relative performance metrics.

# 3. Servicer Ratings

**Servicer Ratings**

Servicer ratings are assigned on a scale of one to five, where one represents the highest rating. SAR also utilises pluses (+) and minuses (-) to further distinguish between different ratings. Outlooks are also assigned to indicate the likely direction of the ratings in the short to medium term, including a positive outlook indicating a high likelihood for an upgrade, a negative outlook indicating a high likelihood for a downgrade, and a stable outlook indicating a high likelihood for maintaining the current ratings. The purpose of the rating scale is to give investors and other market participants a way to quantify servicer quality and pinpoint best practices in the sector. Each report issued will denote the type of servicer being rated, whether a primary servicer, special servicer, or master servicer.

| Rating | Description |
|---|---|
| **1**<br>(-) | The best rating indicative of a track record of strong and stable management, performance that meets industry averages and servicer agreement standards, exceptional information technology, and exceptional internal controls, policies, and procedures, as well as the highest ability, efficiency, and competence in managing large and frequently diverse asset portfolios. |
| **2**<br>(+)<br>(-) | A good rating is indicative of high efficiency and competence in overseeing medium- to large-sized portfolios; additionally, a strong management background, a respectable servicing track record, strong internal policies and procedures, and a managed portfolio performance history that is on par with or better than industry averages. |
| **3**<br>(+)<br>(-) | A moderate rating is indicative of a reasonable servicing track record, internal procedures and guidelines that adhere to industry or servicer agreement requirements, and a managed portfolio performance history that is comparable to industry averages. |
| **4**<br>(+)<br>(-) | A below-average rating is indicative of inadequate capacity and effectiveness or competency, a below-average servicing track record, or subpar internal controls. |
| **5**<br>(+)<br>(-) | A weak rating is indicative of persistent losses and a severe lack of internal controls, both of which point to a bad servicing history. |

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