FitchRatings

Structured Finance
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Sprint Spectrum Securitization Bespoke Rating Criteria

Bespoke Criteria

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This report updates and replaces the *Sprint Spectrum Securitization Bespoke Rating Criteria*, dated May 18, 2020.

Related Criteria

Global Structured Finance Rating Criteria (March 2023)

Future Flow Securitization Rating Criteria (April 2022)

Structured Finance and Covered Bonds Counterparty Rating Criteria (July 2022)

Aircraft Enhanced Equipment Trust Certificates Rating Criteria (August 2021)

Corporates Recovery Ratings and Instrument Ratings Criteria (April 2021)

Digital Infrastructure Securitization Rating Criteria (September 2022)

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Scope

This bespoke criteria report is applicable to the rating assignment and surveillance analysis of notes issued by Sprint Spectrum Issuer LLC in the U.S. Fitch's rating reflects a relative vulnerability to default and addresses recovery prospects following a default. Fitch does not assign a 'sf' modifier to the Spectrum securitization transaction.

Elements Requiring Bespoke Criteria

Fitch Ratings adopts a hybrid rating approach, which incorporates elements of Structured Finance and Corporates' rating methodologies. The rating approach used is very similar to Fitch's "Future Flow Securitization Rating Criteria" and to its "Aircraft Enhanced Equipment Trust Certificates Rating Criteria" (EETC) rating approach for the subordinated tranches, which, in turn, incorporates elements of both Fitch's Corporates group and Structured Finance methodologies. The approach is based on the underlying credit quality of the lessee, and our assessment of its willingness to meet its lease obligations through a distressed period including bankruptcy.

Key Rating Drivers

The key rating drivers are listed below in order of importance.

Credit Quality of Lessee: The Issuer Default Rating (IDR) of the company acting as the lessee will be determined by Fitch's Corporates group and is used as the starting point for the analysis. Hence, the Corporate IDR functions as a floor for the Spectrum securitization transactions.

Performance Risk and GCA Score: Timely payment on the bonds may depend on the ongoing performance of the lessee. The going concern assessment (GCA), also to be determined by Fitch's Corporates group, will determine the maximum number of notches for the differential between the IDR and the issuance's probability of default (PD) assessment. The GCA score is derived from Fitch's "Future Flow Securitization Rating Criteria" and assigned by Fitch's Corporate group.

Strategic Nature of Assets: The affirmation factor, i.e., the likelihood of affirmation of a particular lease during reorganization, is a function of the strategic importance of the specific asset. Thus, weaker attributes related to the strategic importance of the asset would prevent the transaction from obtaining the maximum notching differential considered by the GCA score. The affirmation factor limits the achievable uplift on the PD assessment to four notches.

Asset Isolation and Legal Structure: Fitch assesses the legal protections present in bankruptcy codes and structural features incorporated into the transaction, which increase the lessee's willingness to pay the monthly lease payments and enhance recovery potential.

Recovery Analysis: The Fitch-adjusted valuation range of the collateral is determined to incorporate a recovery component into the transaction rating. The benefit for transactions will vary between zero and three notches depending on the PD assessment of the underlying transaction. The uplift for investment grade PD assessments will be limited to a maximum of one notch for Triple-B PD assessments and no recovery uplift for Single-A PD assessments. To obtain the maximum recovery benefit, transactions would need to achieve Outstanding recovery (RR1 — recovery of 91% and above).

Transactions with PD assessments below investment grade would achieve the maximum recovery uplift of two notches for Double-B and three notches for Single-B PD assessments, if they have Outstanding recovery. If recoveries are expected to be less than Outstanding, Fitch will limit the recovery uplift potential.

Liquidity Facility in Place: For the transaction to obtain an investment grade rating, Fitch assesses whether there is sufficient liquidity to cover timely payment of interest while the asset is repossessed and then liquidated in an orderly manner. A liquidity facility of 18 months is considered sufficient for this.

Maximum Uplift for Investment Grade Lessees: Overall, aggregate uplift from PD assessments and recovery analysis is limited to two notches for lessees with an investment grade IDR starting point.

Ratings Approach and Assumptions

Issuances rated under these bespoke criteria can be rated above the lessee's IDR to reflect the likelihood that the lessee will meet its lease obligations through a distressed period including bankruptcy and can obtain an additional benefit for recovery. However, the maximum aggregate uplift would be limited to two notches for lessees with an investment grade IDR.

Fitch will start its analysis by determining the PD of the transaction, called the PD assessment, by notching up from the lessee's IDR. The rating outlook of the transaction is typically derived from the lessee's IDR; however, Fitch will assess the impact of a one-notch movement (positive or negative) on the transaction rating where appropriate to assess whether the same outlook as the lessee can be assigned.

Fitch's assessment of the company's going concern, which gauges the likelihood that the company will stay in operation through the transaction's life, will act as a cap for the transaction's PD, but the assessment of the affirmation factor may constrain the rating on the transaction below the GCA score rating equivalent.

A review of the strategic nature of the asset being leased to the company's operations will determine the likelihood of lease affirmation by the lessee in a bankruptcy scenario (the affirmation factor). Weaker attributes related to the strategic importance of the asset would prevent the transaction from obtaining the maximum notching differential considered by the GCA.

The maximum notching uplift provided by the affirmation factor will be applied to transactions with originators that are rated at the lower end of the rating scale ('B+' and lower). These entities are more susceptible to near-term defaults, and Fitch has more visibility related to the potential outcome of any default/bankruptcy scenario. For more highly rated originators, Fitch will temper the notching uplift provided by the affirmation factor as the potential for bankruptcy is far removed and the predictability of the outcome is more uncertain, while the maximum uplift for investment-grade entities is not more than two notches.

Affirmation Factor Uplift[a]

	Fitch Estimate of Affirmation Likelihood		
Lessee Rating Range	Low	Medium	High
B+ and Lower	0–2	2–3	3–4
BB Category	0–2	2–3	3
BBB– and Higher	0–1	0–2	2

[a]Table considers a one-notch benefit for 18 months liquidity.
Source: Fitch Ratings; actual outcome within the range to be determined by credit committee.

Fitch will then determine recovery expectations given default by evaluating collateral coverage using a Fitch-adjusted valuation range. The potential recovery uplift over the PD assessment is dependent upon Fitch's recovery estimate as well as the PD assessment of the underlying obligation. For example, the recovery uplift for a transaction with an Outstanding recovery estimate greater than 91% (RR1) will range between zero and three notches depending on the PD assessments. The Single-B assessment may be assigned up to a 3-notch recovery uplift, the

Double-B may be assigned up to a 2-notch recovery uplift, and the Triple-B may be assigned up to a 1-notch recovery uplift. There is no recovery uplift assigned for PD assessments in the 'A' category. If recovery is deemed to be less than Outstanding, this would limit the recovery uplift applied. For more details related to Fitch's approach to recovery ratings, see Fitch's criteria "Corporates Recovery Ratings and Instrument Ratings Criteria."

Finally, for the transaction to be able to obtain a rating at the investment grade level, Fitch assesses whether there is sufficient liquidity to cover timely payment of interest while the asset is repossessed and then liquidated in an orderly manner. A liquidity facility of 18 months is considered sufficient for this.

Going Concern Assessment

The GCA score of the company will be determined by Fitch's Corporates group. Its assessment of the company's going concern, which gauges the likelihood that the company will stay in operation throughout the transaction's life, will act as a cap for the transaction's PD, but the assessment of the affirmation factor may constrain the transaction rating below the GCA score rating equivalent.

Affirmation/Rejection of the Lease

Under a Chapter 11 bankruptcy proceeding, a debtor must determine whether to assume or reject a lease of personal property within 60 days, under Section 365(d)(5). In assessing the likelihood of affirmation of a particular lease (affirmation factor), Fitch considers the strategic importance of the specific asset in conjunction with its Corporates group.

Additionally, the analysis incorporates legal protections present in bankruptcy codes and structural features incorporated into the transaction, which typically increase the lessee's willingness to pay. The Fitch Estimate of Affirmation Likelihood can be deemed as low, medium or high, in line with its EETC criteria inclusive of the liquidity facility benefit.

Asset Isolation

The transaction is structured with the intention to isolate, or de-link, an underlying pool of assets from the corporate credit risk of the original owner.

Sales Process/Liquidity

The approximate time frame of a sale of Spectrum between announcement and closing, which includes full Federal Communications Commission (FCC) approval, has been less than 14 months and, given a rejection would happen in 60 days, the total process is approximately 16 months. A liquidity facility of 18 months is considered sufficient to achieve a rating at the investment grade level given the timing of the process and the fact that the structure already owns and controls the assets in this transaction.

Recovery

The recovery analysis assumes that the lease is rejected by the company and that the assets are resold by the creditors that compose the controlling party. Given the amortizing structure of the transaction and the nature of the collateral (non-depreciating asset), the recovery rate is expected to increase year over year.

The Fitch-adjusted valuation range can be obtained using independent valuations as a reference as, historically, they have proved accurate. Historical third-party valuations of Spectrum have been in line with or below subsequent traded values.

Existence of Secondary Market for the Collateral

Potential Spectrum buyers include other wireless providers, telecom companies, technology companies, cable providers and other technology providers. Unlike the airlines (EETC potential buyers), some of these companies are rated in the 'A' rating category.

Product Specific Risks

- Non-payment of a hell or high-water operational lease from Sprint Communication Inc. (SCI). Such risk is addressed by the fact that the PD assessment of the notes is linked to the IDR of the lessee. A missed lease payment triggers a collateral disposition event. In these cases, the proceeds from the sale of the collateral will be used to pay back investors.

- Since interest has to be paid on a timely basis, liquidity is an important factor to cover debt service until the collateral is sold.
- For transactions with a PD assessment of 'BBB' and below, Fitch will apply an additional rating uplift depending on the recovery prospects.
- Fitch will limit the overall uplift from PD assessments and recovery analysis to two notches for lessees with an investment grade IDR starting point.

Rating Assumption Sensitivity

The transaction's rating is linked to the IDR of the corporate entity acting as the lessee. Therefore, a change in the IDR of the company can lead to a change on the rating of the notes. Additionally, the rating of the notes is strongly influenced by the GCA score and affirmation factor. A reassessment of the affirmation factor from high to medium can lead to a change in the ratings of the notes.

In addition, a change in Fitch's adjusted valuation of the collateral that would result in a reduction of the recovery prospect estimations may lead to a rating downgrade.

Surveillance

The ongoing performance analysis of a transaction forms an essential part of Fitch's rating process. Comprehensive, clear and timely reporting on every transaction is key to assessing current performance and forming an accurate credit view. The Fitch surveillance process is split into two parts: an ongoing review of quarterly information; and a full review at committee at least annually.

Should actual performance be inconsistent with Fitch's original expectations, the agency may review the transaction in committee prior to the annual review. Ratings may be affirmed, upgraded or downgraded as a result of such committee.

Criteria Disclosure

Fitch expects to disclose, as part of its rating action commentaries or presale reports, the GCA score, the affirmation factor and recovery rating assumptions. In addition, Fitch will disclose any variation to criteria (as mentioned in the Variations from Criteria section). In many cases, Fitch uses the assumptions that it derived in its initial analysis in its surveillance review. To focus on Fitch's rating action commentaries on the most important changes to the rating, Fitch will not disclose these assumptions in subsequent rating action commentaries unless there is any change to the assumption.

Criteria Variations

Fitch's criteria are designed to be used in conjunction with experienced analytical judgment exercised through a committee process. The combination of transparent criteria, analytical judgment applied on a transaction-by-transaction or issuer-by-issuer basis, and full disclosure via rating commentary strengthens Fitch's rating process while assisting market participants in understanding the analysis behind our ratings.

A rating committee may adjust the application of these criteria to reflect the risks of a specific transaction or entity. Such adjustments are called variations. All variations will be disclosed in the respective rating action commentaries, including their impact on the rating where appropriate.

A variation can be approved by a ratings committee where the risk, feature, or other factor relevant to the assignment of a rating and the methodology applied to it, are both included within the scope of the criteria, but where the analysis described in the criteria requires modification to address factors specific to the particular transaction or entity.

Limitations

Ratings, including Rating Watches and Outlooks assigned by Fitch are subject to the limitations specified in Fitch's Ratings Definitions and are available at www.fitchratings.com/definitions.

Data Sources

- Independent third-party consultants.
- Internal valuation, provided by Fitch's Corporates group.
- Sponsor/arranger valuation provided by Aetha Consulting.