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Fitch Upgrades Realkredit to 'A+'; Outlook Stable

Fitch Ratings - Warsaw - 15 Sep 2023: Fitch Ratings has upgraded Realkredit Danmark A/S's (Realkredit) Long-Term Issuer Default Rating (IDR) to 'A+' from 'A'. The Outlook is Stable. Fitch has also affirmed the Viability Rating (VR) at 'a'. A full list of rating actions is below.

The upgrade of the IDR is driven by the upgrade of Realkredit's Shareholder Support Rating (SSR) to 'a+' from 'a', which reflects the upgrade of Danske Bank A/S's (Realkredit's 100% shareholder) Long-Term IDR to 'A+' from 'A'.

Key Rating Drivers

Support-Driven IDRs: The IDRs and SSR of Realkredit reflect Fitch's view of a very high probability of support from Danske, if ever required. Realkredit's 'F1' Short-Term IDR is the lower of two options mapping to an 'A+' Long-Term IDR on Fitch's rating scale and is in line with its parent's. The Stable Outlook on Realkredit's Long-Term IDR reflects that on the parent.

Shareholder Support: In Fitch's view, Danske has a very high propensity to support Realkredit, given the latter's role as the group's domestic mortgage provider (about 40% of the group's total loans). Mortgage lending is an integral part of Danske's domestic business and as a result a potential default of Realkredit would constitute huge reputational risk for Danske and would materially hurt its domestic franchise.

We also take into consideration the high level of management and operational integration and capital and funding fungibility between Danske and Realkredit. We believe any potentially required support could be material, albeit manageable relative to Danske's ability to provide it. Realkredit is not included in Danske's single-point-of-entry resolution strategy, but it must observe its own bail-in-able debt buffer requirement, which comprises equity and bonds issued to the parent.

Strong Intrinsic Creditworthiness: Realkredit's VR reflects its low risk appetite and strong asset-quality metrics, which balance its monoline business model and undiversified, but stable, earnings. They also reflect Realkredit's entrenched mortgage lending franchise in Denmark, strong capitalisation and manageable reliance on wholesale funding.

Low Risk Profile: Credit risk exposure solely comprises mortgage lending with tight underwriting standards underpinned by conservative Danish covered bond and mortgage lending legislation. Its loan book is geographically concentrated in Denmark and strongly linked to the performance of the Danish economy and real estate market.

Strong Asset Quality: Realkredit's asset quality is a rating strength, underpinned by low arrears and

defaults, prudent collateralisation and underwriting standards, contained growth and low levels of loan impairment charges (LICs) through the cycle. We expect Realkredit's impaired loan ratio to modestly increase to 1.6% by end-2024 while LICs should remain contained around 2bp in 2023 and 6bp in 2024.

Undiversified but Stable Earnings: Realkredit's profitability is weaker than that of similarly rated peers as its income almost solely relies on lending. However, the lack of revenue diversification is offset by limited credit losses and robust cost efficiency. In 2023, we expect Realkredit's operating profit to rise to 3.2% of risk-weighted assets (RWAs) due to higher net interest income from its securities portfolio while LICs should remain contained.

Strong Capitalisation: Realkredit's capitalisation is underpinned by its low-risk business model and solid capital surplus over regulatory minimums, giving the bank a sufficient cushion to absorb potential LICs and RWAs inflation. We also consider Realkredit's high product concentration and potential ordinary capital support from the parent. Capital fungibility across the Danske group is constrained by Realkredit's standalone prudent capital requirements.

Solely Wholesale-Funded: Realkredit relies extensively on wholesale funding because mortgage lending is, by law, entirely funded by covered bonds in Denmark. We believe the risk of Realkredit not being able to access the covered bond market is low due to strong demand for these bonds from Danish financial institutions, insurance companies and pension funds. Refinancing risk is also mitigated by the bank's good liquidity buffer and potential ordinary support from Danske, if needed.

Rating Sensitivities

Factors that Could, Individually or Collectively, Lead to Negative Rating Action/Downgrade

Realkredit's IDR and SSR would be downgraded if Danske's IDR were downgraded as Realkredit's ratings are driven by institutional support. Realkredit's IDR and SSR are also sensitive to a weakening of Danske's propensity to support the subsidiary, for example, if Realkredit became a less strategic entity for the group or if the entity became significantly less integrated within the group, which we do not expect.

We would downgrade Realkredit's VR if we expected its impaired loans ratio to increase durably above 2.5% and its common equity Tier (CET1) ratio to shrink durably below 14%. This could be due to a more severe and prolonged economic downturn than we currently expect.

An adverse change in investor sentiment requiring extraordinary support from the parent, due to a material weakening of Realkredit's ability to access competitively priced covered-bond funding, would be negative for the bank's VR. An increased reliance on international debt investors, who could prove less stable during periods of financial stress, would also put negative pressure on the ratings.

Factors that Could, Individually or Collectively, Lead to Positive Rating Action/Upgrade

Realkredit's IDR and SSR could be upgraded if Danske's IDRs were upgraded, assuming Realkredit retains its important role within the group.

Realkredit's VR is constrained by its limited product range. In the longer term, an upgrade would be contingent on the bank broadening its product offering, providing it with significantly more diversified revenue streams.

VR ADJUSTMENTS

The business profile score of 'a-' is above the 'bbb' category implied score due to the following adjustment reason: market position (positive).

The capitalisation and leverage score of 'a+' is below the 'aa' category implied score due to the following adjustment reasons: risk profile and business model (negative).

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

Public Ratings with Credit Linkage to other ratings

The ratings of Realkredit are linked to the ratings of its parent, Danske.

ESG Considerations

The highest level of ESG credit relevance is a score of '3', unless otherwise disclosed in this section. A score of '3' means ESG issues are credit-neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. Fitch's ESG Relevance Scores are not inputs in the rating process; they are an observation on the relevance and materiality of ESG factors in the rating decision. For more information on Fitch's ESG Relevance Scores, visit <https://www.fitchratings.com/topics/esg/products#esg-relevance-scores>.

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Rating Actions

ENTITY/DEBT	RATING		RECOVERY	PRIOR
Realkredit Danmark A/S	LT IDR	A+ 	Upgrade	A 
	ST IDR	F1	Affirmed	F1
	Viability	a	Affirmed	a
	Shareholder Support	a+	Upgrade	a

RATINGS KEY OUTLOOK WATCH

POSITIVE



NEGATIVE



EVOLVING



STABLE



Applicable Criteria

[Bank Rating Criteria \(pub.01 Sep 2023\) \(including rating assumption sensitivity\)](#)

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