

Realkredit Danmark A/S

Danish Covered Bonds – Performance Update Capital Centre S and Capital Centre T



The AAA/Stable ratings on the Danish mortgage-covered bonds (*særligt dækkede realkreditobligationer*, or *SDROs*) issued out of Capital Centres S and T by Realkredit Danmark A/S (Realkredit) are based on the issuer's rating of A+ enhanced by six notches of governance support.

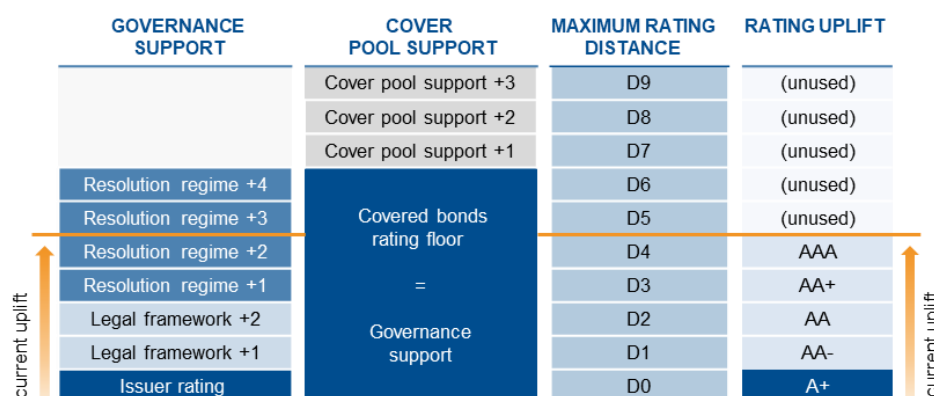
Cut-off date	CC ¹	Cover pool	Cover asset type	Covered bonds ²	Rating/Outlook
31 Mar 2023	S	DKK 294.4bn	Residential and commercial mortgage loans	DKK 276.2bn	AAA/Stable
31 Mar 2023	T	DKK 475.6bn		DKK 446.9bn	AAA/Stable

¹Capital Centres S & T; ²*særligt dækkede realkreditobligationer* – Danish mortgage-covered bonds issued under the strict balance principle of the Danish Mortgage Act.

Governance support is the primary rating driver for both capital centres, providing six notches of uplift above the issuer rating. Only four notches are needed to raise the covered bond ratings to the highest achievable level.

We classified the interplay between complexity and transparency with a cover pool complexity category of 'low', allowing the maximum additional uplift from cover pool support of three notches on top of the governance support uplift. The programme benefits from a five-notch buffer against an issuer downgrade. The cover pool rating buffer also benefits from the strong credit characteristics of both capital centres and the balance principle under which market risk is almost eliminated, particularly asset-liability mismatches.

Figure 1: Rating construct



Stable Outlook

The Stable Outlook on the covered bonds reflects the Stable Outlook on the issuer rating and the rating buffer provided by our governance and cover pool support analyses, which shield the covered bond ratings from a multi-notch issuer rating deterioration.

Changes since the last performance update

Since our last analysis one year ago, the Danish property price rally has continued to cool off, without harming the cover pool's credit quality. In fact, loan-to-value (LTV) is now lower, especially for Capital Centre S, driven by debt reductions from the rebuying or refinancing of fixed debt below par (a feature specific to the Danish market).

Realkredit's SDROs continue to benefit from strong credit enhancement supported by low LTVs and healthy credit metrics thanks to the predominant exposure to local commercial and residential mortgage borrowers.

Ratings & Outlook

Issuer rating	A+
Outlook	Stable
Last rating action	Affirmation
Last rating action	9 Nov 2022
Covered bond	AAA
Outlook	Stable
Rating action	Affirmation
Last rating action	30 June 2022

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Related Research

Scope completes a monitoring review for covered bonds issued out of Realkredit's CCS and CCT June 2023

Scope Affirms Realkredit Danmark's A+ issuer rating, revises Outlook to Stable November 2022

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Bloomberg: RESP SCOP

Realkredit, a core subsidiary of the Danske banking group

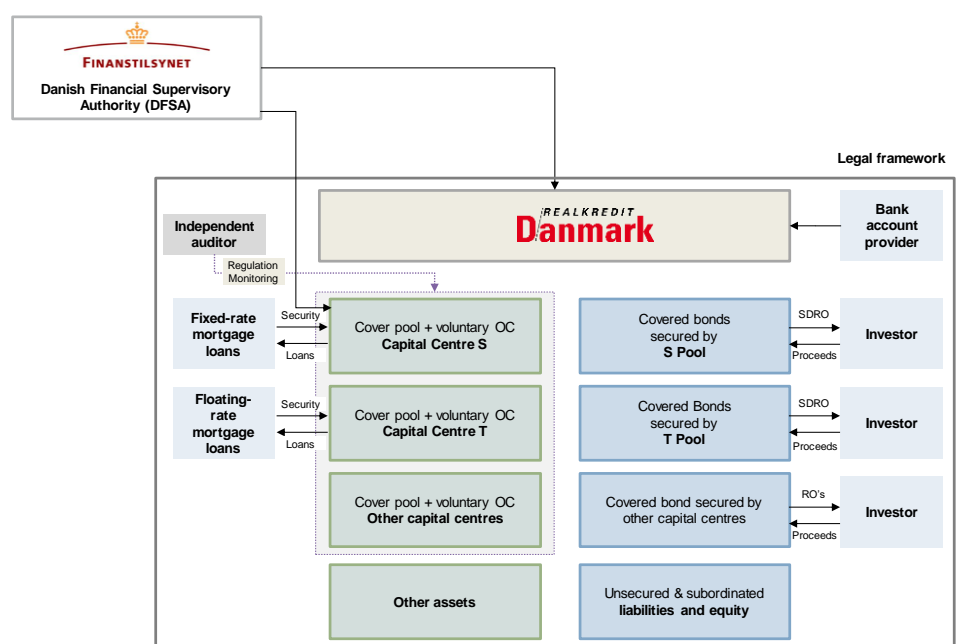
The issuer

We rate Realkredit, the issuer of the SDROs, at A+/Stable.

As a core subsidiary of Danske Bank A/S, Realkredit is closely integrated into the Danske group, sharing its strategy and risk management principles. Realkredit's standalone financial profile is supported by strong asset quality, high capitalisation and its position as a major covered bond issuer in Denmark. The Stable Outlook reflects our view that the downside risks for the group from ongoing regulatory investigations have significantly decreased. For further details on the bank's credit analysis see www.scooperatings.com.

Programme structure

Figure 2: On-balance sheet issuance structure



RO: Realkreditobligationer

OC: overcollateralisation

Source: Scope, Realkredit Danmark

Realkredit is a specialised mortgage bank. It originates the majority of its domestic mortgage loans within Danske Group. The loans are refinanced using SDROs, with issuances governed by the Danish Mortgage Act and supervised by Denmark's financial supervisor, Finanstilsynet.

Governance support analysis

Ratings for the SDROs issued out of Capital Centres S and T are primarily supported by the legal and resolution framework for Danish covered bonds, which enhances the rating to the highest achievable level (AAA). Cover pool support is therefore not needed.

Two notches of credit differentiation result from our legal framework analysis. This is driven by the benefits afforded by Denmark's covered bond framework, which we consider one of Europe's strongest, particularly due to the strict 'balance principle' applicable to SDROs. Changes to the Danish framework to apply the European covered bond directive were credit neutral to the SDROs issued.

Our resolution regime analysis provides an additional four-notch uplift. It reflects the programmes' preferential status and exemption from bail-in, our view on the resolvability and likely maintenance of Realkredit in the hypothetical scenario of regulatory intervention in the bank, and the very high importance of covered bonds in Denmark,

Full governance support of six notches

Two notches of legal framework uplift...

... plus up to four notches of resolution regime uplift.

where a strong stakeholder group maintains confidence in the bonds' high credit quality. For more information see our [related research](#).

Pool characteristics

Capital centre	S	T
Balance (DKK bn)	294.4	475.6
Residential (%)	75.2	65.4
Commercial (%)	18.6	28.5
Substitute (%)	6.2	6.0

General information

Capital centre	S	T
No. of exposures	158,530	196,517
Avg expos. ('000s)	1,742	2,274
Top 10 (%)	1.0	2.0
Remaining life (years)	22	21
LTV (%)	41.6	47.9

Interest rate type (%)

Capital centre	S	T
Floating	0.5	99.9
Fixed	99.5	0.1

Repayment type (%)

Capital Centre	S	T
Bullet	33.1	67.6
Amortising	66.9	32.4

Cover pool analysis

The programmes' governance credit support of up to six notches already provides for the highest possible rating. It is the key rating driver and, as such, cover pool support is not needed. We also determine whether cover pool support could further stabilise the ratings, in part by examining the interplay between complexity and transparency. This analysis translates into a cover pool complexity category of 'low', which allows for a maximum three-notch cover pool-related uplift on top of the governance-related uplift.

Our cover pool analysis stabilises the rating at AAA, even if the bank were downgraded to BBB-, provided at least the current overcollateralisation is maintained.

Cover pool composition

Both capital centres are predominantly secured by Danish commercial and residential mortgage loans denominated in Danish kroner. As of March 2023, only 0.4bp of mortgage loans in Capital Centre S were denominated in euros. For Capital Centre T, 2.7% are denominated in Swedish kronor, 0.8% in euros, and 1.2% in Norwegian kroner.

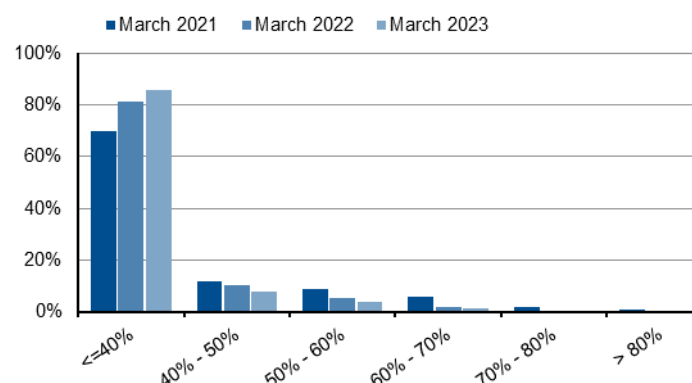
Both pools are highly granular with around 160,000 mortgage loans for Capital Centre S and around 200,000 for Capital Centre T as of March 2023. The top 10 exposures account for 1.0% in Capital Centre S and 2.0% in Capital Centre T.

The main and most important difference between the two capital centres concerns their interest rates: mortgage loans in Capital Centre S have fixed rate for life; the loans in Capital Centre T are floating-rate and reset loans (adjustable-rate mortgages), most of which have reset periods of under five years.

The split between residential and commercial loans has remained relatively stable in both capital centres. By total assets, residential mortgage loans account for 75% for Capital Centre S and 65.0% for Capital Centre T.

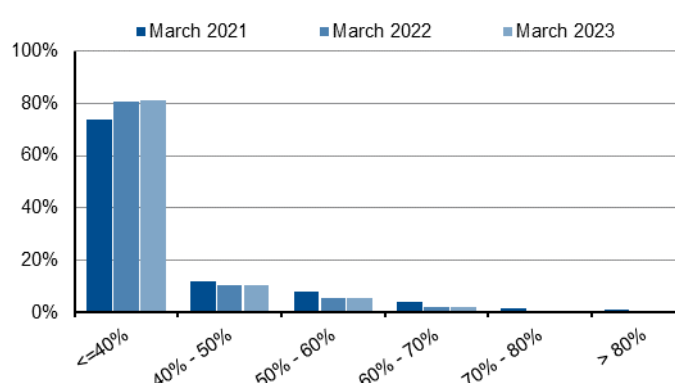
Since our last analysis from 30 March 2023, assets in Capital Centre S have decreased by around DKK 40bn, while Capital Centre T's have increased by around DKK 30 bn. Some key metrics on the mortgage loans have changed dramatically since our last review: overall LTV has dropped by around 7pp to 41.6% for Capital Centre S.

Figure 3: LTV distribution (Capital Centre S)



Source: Scope Ratings, Realkredit Danmark

Figure 4: LTV distribution (Capital Centre T)



Source: Scope Ratings, Realkredit Danmark

This material drop in LTVs is driven by continued loan amortisation from around two-thirds of loans for Capital Centre S and the ability to buy into mortgages below par under current interest rate conditions in Denmark, particularly among borrowers locked into a low-rate

fixed loan. Refinancing such loans at current conditions enables a significant reduction in debt balance.

Asset risk analysis

The credit quality of the two granular capital centres is strong. We have kept our lifetime mean default rate stable at 2.3% for Capital Centre S and 2.4% for Capital Centre T, supported by the strong performance in recent years.

Our projection of default on mortgage loans uses an inverse Gaussian distribution, based on available credit performance data provided by the bank (in particular, 'over 90 days past due' vintage data) and benchmarking.

We continue to assume a volatility of default (weighted average coefficient of variation) of 48% for Capital Centre S and 75% for Capital Centre T. Assumptions for capital centre T incorporate a potential increase in borrower defaults if margins increased by up to 500bp due to a failure to refinance covered bonds. Capital Centre S is not exposed to refinancing risk because the loans have a fixed rate for life.

We estimated an increased weighted average recovery rate ranging from 78.6% (from 74.3%) for Capital Centre S to 80.8% (from 79.6%) for Capital Centre T, under the most stressful scenarios.

Cash flow risk analysis

The overcollateralisation supporting the AAA ratings is 2% for both pools and is based on governance support. Consequently, cover pool support is not a rating driver.

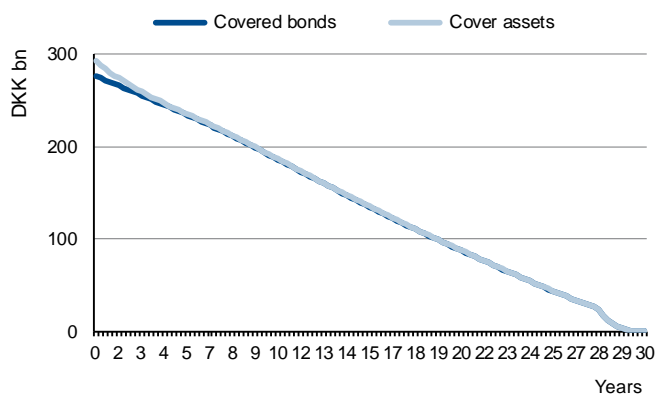
To test the stability of the ratings, we established the overcollateralisation levels needed to support the current rating uplift if the programme had to rely on cover pool support. We performed a full analysis supported by detailed data provided by Realkredit. Our analysis showed that cover pool support can maintain the current AAA ratings up to a five-notch issuer downgrade.

Credit risk is most pronounced for the cover pools, but remains low, reflecting their strong credit quality. Aided by the balance principle, market risks mainly result from minimum, regulatory and voluntary overcollateralisation, but are negligible in terms of the total balance and remaining term.

Strong credit quality reflected in low default expectation...

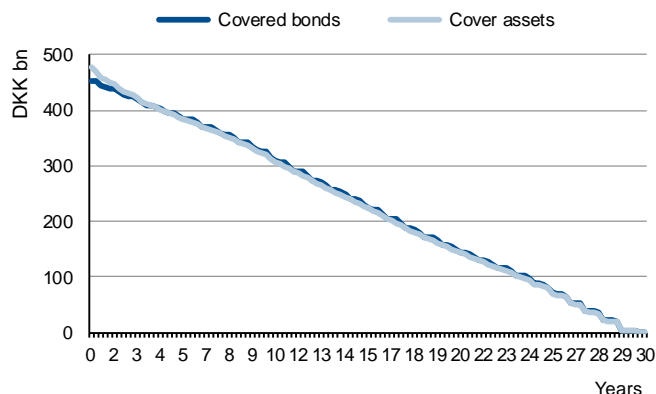
...and high recoveries, even under stressed scenarios

Figure 5: Amortisation profile (Capital Centre S)



Source: Scope Ratings, Realkredit Danmark

Figure 6: Amortisation profile (Capital Centre T)

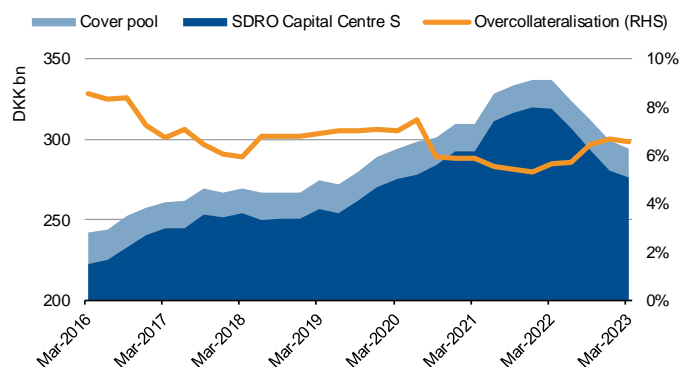


Source: Scope Ratings, Realkredit Danmark

Availability of overcollateralisation

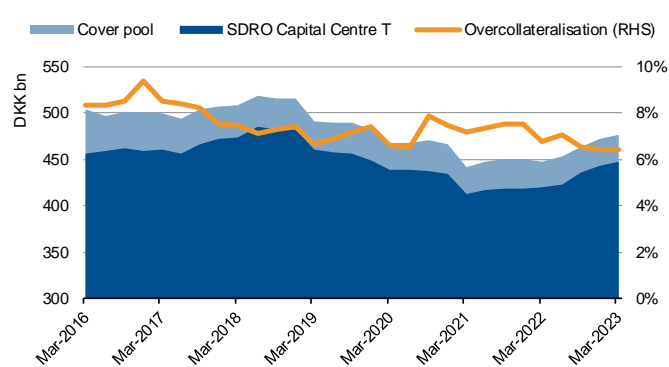
Realkredit's covered bond ratings are wholly supported by governance factors and therefore do not rely on the issuer's ability and willingness to provide overcollateralisation above the legal minimum. However, the current ratings allow us to fully account for the provided overcollateralisation.

Figure 7: Overcollateralisation (Capital Centre S)



Source: Scope Ratings, Realkredit Danmark

Figure 8: Overcollateralisation (Capital Centre T)



Source: Scope Ratings, Realkredit Danmark

Main counterparty exposure relates to Realkredit

Other risk considerations

The rated covered bonds have counterparty exposures to the issuer, as well as to the issuer's parent as loan originator, servicer, bank account provider and paying agent. No documented replacement mechanisms would automatically shield the covered bonds from a credit deterioration of counterparties providing bank accounts. However, we believe that the strong alignment of interests between the bank and covered bond holders would prevent a negative impact from such risks before regulatory intervention became necessary. The bank's risk management process regularly monitors accounts to ensure that remedial action can be taken early on.

Country risk does not affect the ratings

Sovereign risk does not limit the ratings of Realkredit's SDROs. We believe the risks of an institutional framework meltdown, legal insecurity and currency-convertibility problems are currently remote.

No direct impact from ESG

The ratings do not directly include ESG aspects because there is insufficient information on the collateral's energy efficiency or differences in recovery proceeds.

Challenging environment for benchmark ESG covered bonds

However, we acknowledge that the bank's green bond framework opens up the investor base and improves the appeal and liquidity of covered bonds issued by Realkredit.

On the other hand, the Danish match funding principle complicates an effective selection of eligible assets. This is because Danish mortgage banks have to ensure that covered bonds match the loans' maturity and interest profile, limiting the supply of eligible cover loans.



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Appendix: Summary of covered bond characteristics

Reporting date	30 March 2022	30 March 2023	30 March 2022	30 March 2023
Issuer name	Realkredit Danmark A/S			
Capital centre	S		T	
Country	Denmark			
Covered bond name	særligt dækkede realkreditobligationer (SDROs)			
	Danish mortgage covered bonds issued under the Danish mortgage act			
	(Specific balance principle)			
Covered bond legal framework	Danish legal covered bond framework			
Cover pool type	Mortgage loans			
Composition	Residential = 76.8%	Residential = 75.2%	Residential = 65.0%	Residential = 65.4%
	Commercial = 17.8%	Commercial = 18.6%	Commercial = 28.7%	Commercial = 28.5%
	Substitute = 5.4%	Substitute = 6.2%	Substitute = 6.3%	Substitute = 6.0%
Issuer rating	A+/Negative	A+/Stable	A+/ Negative	A+/Stable
Current covered bond rating	AAA/Stable	AAA/Stable	AAA/Stable	AAA/Stable
Covered bond maturity type ¹	Hard bullet	Hard bullet	Soft bullet	Soft bullet
Cover pool currencies	DKK (100%)	DKK (100%)	DKK (95.2%)	DKK (95.8%)
	EUR (0.0%)	EUR (0.0%)	EUR (0.8%)	EUR (0.6%)
			SEK (2.7%)	SEK (2.5%)
Covered bond currencies			NOK (1.2%)	NOK (1.1%)
	DKK (100%)	DKK (100%)	DKK (95.0%)	DKK (96.6%)
	EUR (0.0%)	EUR (0.0%)	EUR (0.8%)	EUR (0.5%)
			SEK (2.9%)	SEK (2.0%)
			NOK (1.3%)	NOK (0.9%)
Governance cover pool support	6	6	6	6
Maximum additional uplift from cover pool complexity category	3	3	3	3
Maximum achievable covered bond uplift	9	9	9	9
Potential covered bond rating buffer	5	5	5	5
Cover pool (DKK m)	337,266	294,381	447,564	475,613
Thereof substitute assets (DKK m)	18,109	18,168	28,399	28,671
Covered bonds (DKK m)	319,157	276,213	419,165	446,941
Current overcollateralisation/ legal minimum overcollateralisation	5.7% / 8% ²	6.6% / 2%	6.8% / 8% ²	6.4% / 2%
Overcollateralisation to support current rating	not applicable	not applicable	not applicable	not applicable
Overcollateralisation upon a one-notch issuer downgrade	not applicable	not applicable	not applicable	not applicable
Cover pool supporting overcollateralisation to support current rating	0.0%	0.0%	0.0%	0.0%
Cover pool overcollateralisation upon a one-notch issuer downgrade	0.0%	0.0%	0.0%	0.0%
Weighted average life of assets	25 years	24 years	22 years	22 years
Weighted average life of liabilities ³	27 years	26 years	3 years	2 years
Number of loans	173,579	158,530	197,032	196,517
Average loan size (in DKK ‘000s)	1,839	1,742	2,127	2,274
Top 10 residential	0.8%	0.9%	1.5%	1.4%
Top 10 commercial	4.3%	5.0%	6.7%	6.7%
Interest rate type – assets	Floating 0.5%	Floating 0.5%	Floating 100.0%	Floating 99.9%
	Fixed 99.5%	Fixed 99.5%	Fixed 0.0%	Fixed 0.1%
Interest rate type – liabilities (fixed/floating)				
	Floating 0.3%	Floating 0.3%	Floating 22.8%	Floating 21.8%
	Fixed 99.5%	Fixed 99.5%	Fixed 77.2%	Fixed 78.2%
Weighted average LTV (indexed)	Other 0.2%	Other 0.1%		
	48.4%	41.6%	48.1%	47.9%
Geographic split (top 3)	Denmark 100%	Denmark 100%	Denmark 95.9%	Denmark 96.3%
			Norway 1.2%	Norway 1.0%
			Sweden 2.9%	Sweden 2.7%
Domestic region split (top 3)	Hovedstaden 47.7%	Hovedstaden 48.1%	Hovedstaden 50.1%	Hovedstaden 51.0%
	Midtjylland 16.9%	Midtjylland 16.4%	Midtjylland 16.5%	Midtjylland 16.1%
	Syddanmark 16.1%	Syddanmark 16.2%	Syddanmark 16.1%	Syddanmark 15.5%
Default measure	Inverse Gaussian	Inverse Gaussian	Inverse Gaussian	Inverse Gaussian
Weighted average default rate (mortgage)	2.3%	2.3%	2.4%	2.4%
Weighted average coefficient of variation (mortgage)	48%	48%	75%	75%
Weighted average recovery assumption (D0/D9) ⁴	96.5% / 74.3%	94.1% / 78.6%	95.1% / 79.6%	96.6% / 80.8%

¹ Covered bonds issued after 2014 can be extended if refinancing fails.

² 8% of legal overcollateralisation was calculated based on risk-weighted assets and effectively results in a lower overcollateralisation as long as the risk-weighted assets are below 100% of the assets' nominal outstanding balance.

³ Fixed-rate bonds in Capital Centre T are refinanced regularly, reflecting the reset cycles of the mortgage loans.

⁴ D0 or D9 denote the stresses commensurate with the rating distance between the issuer rating and the covered bond ratings.



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