



## Fitch Affirms 5 Danish Covered Bonds on New Criteria

**Link to Fitch Ratings' Report:** Danish Covered Bond Programmes – Rating Action Report (<https://www.fitchratings.com/site/re/890549>)

Fitch Ratings-London-14 November 2016: Fitch Ratings has affirmed the ratings of five Danish covered bond programmes, following the implementation of the agency's revised Covered Bonds Rating Criteria published on 26 October 2016.

The rating actions are as follows:

- Realkredit Danmark's (Realkredit) Capital Centre S mortgage covered bonds affirmed at 'AAA'/Stable Outlook
- Realkredit's Capital Centre T mortgage covered bonds affirmed at 'AA+'; Outlook revised to Stable from Positive.
- Danske Bank's (Danske) combined mortgage covered bonds affirmed at 'AAA'/Stable Outlook
- Danske's domestic mortgage covered bonds affirmed at 'AAA'/Stable Outlook
- Danske's international mortgage covered bonds affirmed at 'AAA'/Stable Outlook

### Issuer Default Rating (IDR) Uplift

The covered bonds issued by Danish commercial banks are eligible for a maximum IDR uplift of two notches given their exemption from bail-in in a resolution scenario, Fitch's assessment that resolution of the issuer will not result in the direct enforcement of recourse against the cover pool and the low risk of undercollateralisation at the point of resolution (see Fitch's Jurisdictional Analysis of the Risk of Undercollateralisation of Covered Bonds - Excel file).

The three programmes of Danske (combined, domestic and international) have been assigned a two-notch IDR uplift, as this bank's Long-Term IDR is driven by Viability Rating,

Realkredit Capital Centre S and T programmes have been assigned a zero-notch IDR uplift, as Realkredit is a specialised mortgage lender not operationally integrated into a parent bank and the bail-in tool is not applicable

to specialised mortgage banks in Denmark.

#### Payment Continuity Uplift (PCU)

Fitch has assigned a PCU of five, instead of six, notches to Danske's programmes for the mortgage covered bonds' 12-month principal maturity extension and three-month protection for interest payment. This is due to the lack of formal provisions to find a refinancing solution without delay in the event of a maturity extension.

Realkredit Capital Centre S's mortgage covered bonds have been assigned a PCU of six notches based on the programme's liquidity provision, which Fitch has assessed as equivalent to at least 12-month principal protection. Ninety-four per cent of the bonds have a pass-through amortisation profile while the remaining 6% are hard-bullet, whose redemptions are covered by substitute liquid assets for at least 12 months. The six notches also reflect the government bonds (Danish and French bonds rated respectively AAA and AA) held for overcollateralisation (OC) to cover at least three months of interest payment.

Realkredit Capital Centre T's covered bonds have been assigned a PCU of three notches based on the programme's liquidity provision, which Fitch has assessed as equivalent to a six months protection. Sixty-four per cent of the outstanding bonds were issued after March 2014 and thus have an extendible maturity feature that mitigates refinancing risk. As the remaining hard bullet bonds (36%) mature over time, the programme's refinancing risk decreases. The cover pool includes liquid assets that are external to the issuer group and are adequate to provide protection against principal payment interruption risk for six months.

#### Recovery Uplift

Danske's mortgage covered bonds have been assigned a one-notch recovery uplift, down from two notches previously for domestic and international programmes, and unchanged for Danske combined programme, due to the programmes' material exposure to recoveries denominated in a different currency than the covered bonds.

For Danske's domestic programme, the cover assets are denominated in DKK while the covered bonds are issued in DKK (56%), in EUR (33%), in CHF (6%) and in NOK (5%). For Danske's combined programme, the cover assets are denominated in SEK and NOK while the covered bonds are issued in EUR (67%), in SEK (17%) and in DKK (16%). For Danske's international programme, the cover assets are denominated in SEK and NOK while the

covered bonds have are issued in EUR (82%), in NOK (11%), in CHF (4%) and in GBP (3%).

For all three Danske programmes, the covered bonds are swapped into the currencies of the assets up to their extended maturity date; however, cash flows from longer-dated assets are not hedged in a recovery given default scenario.

Realkredit Capital Centres S's and T's mortgage covered bonds have been assigned a one-notch recovery uplift, reflecting good recovery prospects from the cover pool in the event of a covered bond default. However, the OC Fitch relies upon in its analysis is not sufficient to offset the stressed credit loss in the covered bond rating scenario to achieve the previous two-notch recovery uplift.

#### Breakeven OC for Ratings

The breakeven OC for the ratings of Danske's combined and domestic programmes have remained stable. For the combined programme, the updated breakeven OC is related to the same tested rating on a probability of default (PD) basis of 'AA+' as at the last rating action. For Danske's domestic programme, Fitch-tested rating on a PD basis has changed to 'AA+' from 'AA' but the impact on the breakeven OC was offset by a reduction of the cushion applied on the modelled asset margin.

The breakeven OC for the rating of Danske's international programme has increased to 10.5% from 10.0% due to the recovery uplift reduction to one from two notches, and a subsequent change in the tested rating on a PD basis to 'AA+' from 'AA' .

The breakeven OC for the rating of Realkredit Capital Centre T's programme has increased to 9.0% from 8.0% due to the recovery uplift reduction to one from two notches, and a subsequent change to the tested rating on a PD basis to 'AA' from 'AA-'.

The breakeven OC for the rating of Realkredit Capital Centre S's programme has decreased to 6.5% from 7.5% as maturity mismatches have narrowed. The impact on Capital Centre S is more positive than on Capital Centre T as the tested rating on a PD basis (AA+) has not changed for Capital Centre S.

A summary of rating steps for the programmes mentioned in this commentary can be found in the excel file "Danish Covered Bond Programmes - Rating Action Report" dated 14 November 2016 which can be accessed in the link

above.

### KEY RATING DRIVERS

#### Realkredit Capital Centre S Covered Bonds

The mortgage covered bonds of Realkredit (A/Stable/F1) Capital Centre S are rated 'AAA'/Stable, five notches above the bank's Long-Term IDR. This is based on a newly assigned IDR uplift of zero notches, a newly assigned PCU of six notches and a recovery uplift of one notch.

The OC of 8.4% which Fitch relies upon in its analysis provides more protection than the breakeven OC of 6.5% for a 'AAA' rating. The breakeven OC corresponds to a 'AA+' tested rating on a PD basis and a one-notch recovery uplift. The Stable Outlook on the covered bonds' reflects that on Realkredit's Long-Term IDR and the significant buffer against a downgrade due to different uplift factors above the bank's IDR.

#### Realkredit Capital Centre T Covered Bonds

The mortgage covered bonds of Realkredit (A/Stable/F1) Capital Centre T are rated 'AA+'/Stable, four notches above the bank's Long-Term IDR. This is based on a newly assigned IDR uplift of zero notches, a newly assigned PCU of three notches and a recovery uplift of one notch.

The OC of 8.3% which Fitch relies upon in its analysis provides less protection than the breakeven OC of 9.0% for a 'AA+' rating. However, Realkredit committed to increase the nominal OC in Capital Centre T to at least 9.0% within a month. The breakeven OC corresponds to a 'AA' tested rating on a PD basis and a one-notch recovery uplift. The Stable Outlook on the covered bonds' reflects that on Realkredit's Long-Term IDR. The outlook on the rating was revised to Stable from Positive given that the rating is currently constrained by the relied-upon OC.

#### Danske Banks's Combined Covered Bonds

The combined mortgage covered bonds of Danske (A/Stable/F1) are rated 'AAA'/Stable, five notches above the bank's Long-Term IDR. This is based on a newly assigned IDR uplift of two notches, a newly assigned PCU of five notches and a recovery uplift of one notch.

The OC of 25.9% which Fitch relies upon in its analysis provides more protection than the breakeven OC of 23.5% for a 'AAA' rating. The breakeven OC corresponds to a 'AA+' tested rating on a PD basis and a one-notch recovery uplift. The Stable Outlook on the covered bonds' reflects that on Danske's Long-Term IDR and the significant buffer against a downgrade due

to different uplift factors above the bank's IDR.

#### Danske Banks's Domestic Covered Bonds

The domestic mortgage covered bonds of Danske are rated 'AAA'/Stable, five notches above the bank's Long-Term IDR. This is based on a newly assigned IDR uplift of two notches, a newly assigned PCU of five notches and a recovery uplift of one notch.

The OC of 12.9% which Fitch relies upon in its analysis provides more protection than the breakeven OC of 10.0% for a 'AAA' rating. The breakeven OC corresponds to a 'AA+' tested rating on a PD basis and a one-notch recovery uplift. The Stable Outlook on the covered bonds' reflects that on Danske's Long-Term IDR and the significant buffer against a downgrade due to different uplift factors above the bank's IDR.

#### Danske Banks's International Covered Bonds

The international mortgage covered bonds of Danske are rated 'AAA'/Stable, five notches above the bank's Long-Term IDR. This is based on a newly assigned IDR uplift of two notches, a newly assigned PCU of five notches and a recovery uplift of one notch.

The OC of 12.5% which Fitch relies upon in its analysis provides more protection than the breakeven OC of 10.5% for a 'AAA' rating. The breakeven OC corresponds to a 'AA+' tested rating on a PD basis and a one-notch recovery uplift. The Stable Outlook on the covered bonds' reflects that on Danske's Long-Term IDR and the significant buffer against a downgrade due to different uplift factors above the bank's IDR.

### RATING SENSITIVITIES

#### Realkredit Danmark Capital Centre S Mortgage Covered Bonds

The 'AAA' rating of Realkredit Capital Centre S's mortgage covered bonds is vulnerable to a downgrade if any of the following occurs: (i) the bank's Long-Term Issuer Default Rating (IDR) is downgraded by three notches to 'BBB' or below; (ii) the relied upon overcollateralisation (OC), which is the lowest level of OC over the last 12 months, decreases below Fitch's 'AAA' breakeven OC of 6.5%. Should the OC decrease to the legal minimum, the covered bonds would be downgraded to 'A+'.

#### Realkredit Danmark Capital Centre T Mortgage Covered Bonds

The 'AA+' rating of Realkredit Capital Centre T's mortgage covered bonds is vulnerable to a downgrade if the bank's Long-Term IDR is downgraded by one

notch to 'A-' or below, or if the relied upon OC decreases below Fitch's 'AA+' breakeven OC of 9.0%. Should the OC decrease to the legal minimum, the covered bonds would be downgraded to 'A+'.

The programme could be upgraded to 'AAA' if the hard bullet bonds decrease significantly, so that eligible liquid assets would cover refinancing risk on a nine-months rolling basis, or if the OC relied upon by Fitch increases.

#### Danske Bank Combined Mortgage Covered Bonds

The 'AAA' rating of Danske's combined mortgage covered bonds is vulnerable to a downgrade if the bank's Long-Term IDR is downgraded by four notches to 'BBB-' or below, or if the relied upon OC, which is the lowest level of OC over the last 12 months, decreases below Fitch's 'AA+' breakeven OC of 23.5%. Should the OC decrease to the legal minimum, the covered bonds would be downgraded to 'AA'.

#### Danske Bank Domestic Mortgage Covered Bonds

The 'AAA' rating of Danske's domestic mortgage covered bonds is vulnerable to a downgrade if the bank's Long-Term IDR is downgraded by four notches to 'BBB-' or below, or if the relied upon OC, which is the lowest level of OC over the last 12 months, decreases below Fitch's 'AA+' breakeven OC of 10.0%. Should the OC decrease to the legal minimum, the covered bonds would be downgraded to 'AA'.

#### Danske Bank International Mortgage Covered Bonds

The 'AAA' rating of Danske's international mortgage covered bonds is vulnerable to a downgrade if the bank's Long-Term IDR is downgraded by four notches to 'BBB-' or below, or if the relied upon OC, which is the lowest level of OC over the last 12 months, decreases below Fitch's 'AA+' breakeven OC of 10.5%. Should the OC decrease to the legal minimum, the covered bonds would be downgraded to 'AA'.

Fitch's breakeven OC for a given covered bond rating will be affected by, among other factors, the profile of the cover assets relative to outstanding covered bonds, which can change over time even in the absence of new issuance. Therefore, breakeven OC for the covered bond rating cannot be assumed to remain stable over time.

Contact:

Primary Analyst  
Anne-France Chane

**Analyst**

+44 20 3530 1491

Fitch Ratings Limited

30 North Colonnade

London E14 5GN

**Secondary Analyst**

Andrea Gallina

Analyst

+44 20 3530 1251

**Committee Chairperson**

Helene Heberlein

Managing Director

+33 1 44 29 9140

Media Relations: Christian Giesen, Frankfurt am Main, Tel: +49 69 768076  
232, Email: christian.giesen@fitchratings.com.

Additional information is available on [www.fitchratings.com](http://www.fitchratings.com)

**Applicable Criteria**

Counterparty Criteria for Structured Finance and Covered Bonds (pub. 01 Sep 2016) (<https://www.fitchratings.com/site/re/886006>)

Counterparty Criteria for Structured Finance and Covered Bonds: Derivative Addendum (pub. 18 Jul 2016) (<https://www.fitchratings.com/site/re/884964>)

Covered Bonds Rating Criteria (pub. 26 Oct 2016) (<https://www.fitchratings.com/site/re/888874>)

Criteria Addendum: Denmark - Residential Mortgage Assumptions (pub. 11 Dec 2015) (<https://www.fitchratings.com/site/re/875209>)

Criteria Addendum: Norway - Residential Mortgage Assumptions (pub. 31 Mar 2016) (<https://www.fitchratings.com/site/re/879693>)

Criteria for Interest Rate Stresses in Structured Finance Transactions and Covered Bonds (pub. 26 Oct 2016) (<https://www.fitchratings.com/site/re/888492>)

Criteria for Rating Granular Corporate Balance-Sheet Securitizations (SME CLOs) (pub. 10 Oct 2016) (<https://www.fitchratings.com/site/re/888325>)

Criteria for the Analysis of Commercial Real Estate Loans Securing Covered Bonds (pub. 10 Dec 2015) (<https://www.fitchratings.com/site/re/874686>)

EMEA RMBS Rating Criteria (pub. 18 May 2016) (<https://www.fitchratings.com/site/re/881836>)

Fitch's Cover Asset Refinancing Spread Level (RSL) Assumptions - Excel File

(pub. 26 Oct 2016) (<https://www.fitchratings.com/site/re/888877>)  
Fitch's Interest Rate Stress Assumptions for Structured Finance and Covered Bonds - Excel File (pub. 17 May 2016)  
(<https://www.fitchratings.com/site/re/880522>)  
Global Bank Rating Criteria (pub. 15 Jul 2016)  
(<https://www.fitchratings.com/site/re/884135>)

**Additional Disclosures**

Dodd-Frank Rating Information Disclosure Form  
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