



Fitch Affirms Realkredit Danmark's S & T Covered Bonds

Fitch Ratings-London-31 March 2016: Fitch Ratings has affirmed Realkredit Danmark A/S's (Realkredit, A/Stable/F1, Viability Rating: a) mortgage covered bonds issued out of Capital Centre (CC) S at 'AAA', and CC T at 'AA+'. The Outlook is Stable for CC S and has been revised to Positive from Stable for CC T. The rating actions follow an annual review of the programmes. At 31 December 2015, CC S had DKK226bn and CC T DKK452bn of covered bonds outstanding

KEY RATING DRIVERS

CC S covered bonds' rating is based on Realkredit's Long-term Issuer Default Rating (IDR) of 'A', a Discontinuity Cap (D-Cap) of 4 notches (moderate risk), increased from 3 (moderate high risk) and the 8.8% overcollateralisation (OC) which provides more protection than the 7.5% 'AAA' breakeven OC. The Stable Outlook on the CC S covered bonds' ratings is driven by the Stable Outlook on Realkredit's IDR and the one notch cushion against an IDR downgrade.

CC T covered bonds' rating is based on Realkredit's Long-term IDR of 'A', an unchanged D-Cap of 2 notches (high risk) and the 8.7% OC, which provides more protection than the 8.0% 'AA+' breakeven OC. The positive outlook is driven by the continued reduction in refinancing risk in CC T, which could lead to a higher D-Cap and an upgrade to 'AAA' should the OC that Fitch relies upon support 'AAA' stresses.

The D-Cap has been increased to 4 notches for CC S to reflect the lower liquidity risk for this capital centre since last year. 92% of the bonds have a pass-through feature and the liquid assets in CC S that are external to the issuer group provide liquidity protection for the next 12 months. The liquidity gap risk is also falling in CC T as the hard-bullet bonds (50% of the total) mature over time and because all bonds issued after March 2014 have an extendible maturity feature that mitigates refinancing risk. The D-Cap for CC T is likely to be revised up when the liquid assets external to the group provide liquidity protection for the upcoming hard-bullet maturities. This would increase the maximum achievable rating to the covered bonds issued out of CC T to 'AAA'.

CC S 'AAA' breakeven OC has decreased at 7.5% from 8% and CC T 'AA+' breakeven OC has remained unchanged at 8.0%. The OC as of Q116 is 8.8% for CC S and 8.7% for CC T and is mostly invested in highly rated securities external to the group.

CC S and CC T cover assets contain respectively 66% and 54% of residential mortgage loans to private individuals, the remainder being commercial mortgages. The residential mortgage loans in CC S are mostly 30-year fixed-rate mortgages for which Fitch applies lower default assumptions than for floating rate or interest reset mortgages that are predominant in CC T (see Criteria Addendum - Denmark Residential Mortgage Assumptions', 11 December 2015). To ensure idiosyncratic risks are adequately protected against, the 'AAA' expected loss for residential mortgages in CC S has been floored at 4% in line with Fitch's EMEA RMBS Rating Criteria dated 16 December 2015. The commercial sub-portfolios have been analysed using Fitch's SME CLO criteria and are subject to significantly higher loss rates than the residential loans in Fitch's stress scenarios.

The breakeven OC for both covered bond programmes remains driven by the credit risk of the pools (9.6% at 'AAA' for CC S and 14.4% at 'AA+' for CCT) as Fitch does not model a fire sale of the assets in its cash flow analysis. Instead we consider the possibility of bond refinancing post insolvency. In the recovery rate analysis, Fitch assumes that the cover pool would be sold below its par value. The breakeven OCs for the ratings are below the credit loss components because of the excess spread available in both CCs and because Fitch gives credit to recoveries for one notch above the tested rating on a PD basis for CC S and two notches for CC T.

Fitch assigns no IDR uplift to the covered bonds issued by Realkredit. This is because specialised mortgage institutions that do not take deposits are not subject to the Minimum Requirement of own funds and Eligible Liabilities (MREL) and can be wound-up through specific insolvency procedures in which covered bonds could bear losses. Fitch IDR uplift applies to regulated covered bonds issued in jurisdictions with an advanced bank resolution regime that includes a bail-in tool for senior liabilities, from which covered bonds are exempt, and where resolution will not result in the enforcement of the recourse against the cover pool. The Danish legislation specifies that the bail-in tool is not applicable to specialised mortgage institutions and introduced a 2% debt buffer requirement, which can be met by senior unsecured debt with write down language, among others, but such debt has not been issued so far.

RATING SENSITIVITIES

The covered bonds' ratings would be vulnerable to a downgrade if any of the following occurred: (i) Realkredit's IDR was downgraded by two notches or more for CC S and one notch or more for CC T; or (ii) the D-Cap fell by two categories or more for CC S and one category or more for CC T; or (iii) the OC that Fitch takes into account in its analysis fell below 7.5% for CC S and 8% for CC T.

CC T covered bonds could be upgraded when more than 90% of the bonds have the new mandatory maturity extension feature as it will improve the liquidity risk.

The Fitch breakeven OC for the covered bond ratings will be affected, among others, by the profile of the cover assets relative to outstanding covered bonds, which can change, even in the absence of new issuance. Therefore the breakeven OC for the ratings cannot be assumed to remain stable.

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Additional information is available on www.fitchratings.com

Applicable Criteria

Covered Bonds Rating Criteria (pub. 11 Mar 2016)

(https://www.fitchratings.com/creditedesk/reports/report_frame.cfm?rpt_id=878761&cft=eyJ0eXAiOiJKV1QiLCJhbGciOiJIUzI1NiJ9.eyJleHAiOiJlNDEzOTc3InNlc3NpY25LZXkiOiJNR0M3WTNQTUZJWUJPUjFTR1FSSklzUDhDV1ZKWIIPMFJITUtYSIZYIn0.hdiXfNgVhHfN4mVbE-OBUPnHtJHKcQsX_a-5-esxHek)

Fitch's Foreign Currency Stress Assumptions for Residual Foreign Exchange Exposures in Covered Bonds - Excel file (pub. 11 Mar 2016)

([https://www.fitchratings.com/creditdesk/reports/report_frame.cfm?](https://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=878760&cft=eyJ0eXAiOiJKV1QiLCJhbGciOiJIUzI1NiJ9.eyJleHAiOiJlE0NTk1NDEzOTcsInNlc3Npb25LZXkiOiJNR0M3WTNQTUZZWUJPUjFTR1FSSklzUDhDV1ZKWIIPMFJITUyYSIZYIn0.hdiXfNgVhHfN4mVbE-OBUPnHtJHKcQsX_a-5-esxHek)

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Global Structured Finance Rating Criteria (pub. 06 Jul 2015)

([https://www.fitchratings.com/creditdesk/reports/report_frame.cfm?](https://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=867952&cft=eyJ0eXAiOiJKV1QiLCJhbGciOiJIUzI1NiJ9.eyJleHAiOiJlE0NTk1NDEzOTcsInNlc3Npb25LZXkiOiJNR0M3WTNQTUZZWUJPUjFTR1FSSklzUDhDV1ZKWIIPMFJITUyYSIZYIn0.hdiXfNgVhHfN4mVbE-OBUPnHtJHKcQsX_a-5-esxHek)

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