



## Fitch Affirms Realkredit Danmark's Capital Centres S & T Covered Bonds at 'AAA'/'AA+'

Fitch Ratings-London-30 March 2017: Fitch Ratings has affirmed Realkredit Danmark A/S's (Realkredit, A/Stable/F1/a) mortgage covered bonds issued out of Capital Centre (CC) S at 'AAA', and out of CC T at 'AA+'. The Outlook is Stable.

The rating actions follow an annual review of the programmes. As of 31 December 2016, CC S had DKK240 billion and CC T DKK458 billion 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 payment continuity uplift (PCU) of six notches, a one notch recovery uplift and the 7.3% overcollateralisation (OC) that Fitch takes into account in its analysis, which provides more protection than the revised 6.0% 'AAA' breakeven OC. The Stable Outlook is driven by the Stable Outlook on Realkredit's IDR and the three-notch cushion against an IDR downgrade.

CC T covered bonds' rating is based on Realkredit's Long-Term IDR of 'A', an increased PCU to four notches from three, a one notch recovery uplift and the 9.4% OC that Fitch takes into account in its analysis, which provides more protection than the revised 8.0% 'AA+' breakeven OC. The Stable Outlook is driven by the Stable Outlook on Realkredit's IDR, the two-notch cushion against an IDR downgrade and the fact that the rating is currently constrained by the relied-upon OC.

The six-notch PCU for CC S reflects the liquidity protection in place for at least 12 months. 95% of the outstanding bonds have a pass-through amortisation profile while the remaining 5% are hard-bullet, whose redemptions are covered by liquid assets for at least 12 months. The six notches also reflect the interest payment protection for at least three months in the form of government bonds (Danish and French bonds rated AAA and AA, respectively).

We have increased the PCU for CC T to four notches to reflect the lower liquidity risk since last year. This is based on the programme's liquidity provision, which Fitch has assessed as equivalent to nine months protection. 72% 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 (28%) mature over time, the programme's refinancing risk decreases. The cover pool includes liquid assets that are external to the issuer group and provide protection against principal payment interruption risk for six months, which will extend to nine months once upcoming hard-bullet bonds mature this year. The four notches also reflect the government bonds held for OC purposes that cover at least three months of interest payment.

CC S 'AAA' breakeven OC has decreased to 6.0% from 6.5% and CC T 'AA+' breakeven OC has reduced to 8.0% from 9.0%. The OC as of 4Q16 is 7.3% for CC S and 9.4% for CC T and is mostly invested in highly rated securities external to the group.

CC S and CC T cover assets contain 66% and 54% of residential mortgage loans to private individuals, respectively, with the remainder commercial mortgage loans. 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', dated 20 December 2016). To ensure idiosyncratic risks are adequately protected against, we have floored the 'AAA' expected loss for residential mortgages in CC S at 4% in line with Fitch's EMEA RMBS Rating Criteria dated 29 November 2016.

Fitch has analysed the commercial sub-portfolios using its Criteria for the Analysis of Commercial Real Estate Loans Securing Covered Bonds. These loans are subject to significantly higher loss rates than the residential loans in Fitch's stress scenarios, albeit lower than last year as we gave more credit to the very good performance of the social and cooperative housing segments. In its analysis, Fitch applied a benchmark one-year PD of 0.5% for these loans (with no PD floor), compared with 1.75% for the other segments (with a floor at 0.5%). Fitch assumed a 50% cure rate in a 'B' scenario. The 'AAA' market value decline assumptions are 75% for industrial properties, 53% for social and cooperative housing and 65% for the other properties. Fitch also applied stressed prepayment rates of 0% and 15%-25% depending on the rating scenario and a three-year recovery timing assumption for these loans.

The breakeven OC for both covered bond programmes remains driven by the credit risk of the pools (5.9% on 'AA+' PD basis for CC S and 8.5% on 'AA' for CCT) as Fitch does not model a sale of assets in its cash flow analysis, but considers the possibility of bond refinancing post insolvency or models the maturity extension of bonds with this feature. The level of the credit loss component has reduced for both CCs due to lower default assumptions for social and cooperative housing loans in the commercial pools. The breakeven OC is also driven by the cash-flow valuation components that reflect the excess spread available in both CCs.

Fitch currently does not assign an IDR uplift to the covered bonds issued by Realkredit, as the issuer 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.

#### RATING SENSITIVITIES

##### Realkredit Capital Centre (CC) S Covered Bonds

The rating would be vulnerable to a downgrade if any of the following occurs: (i) Realkredit's Long-Term IDR was downgraded by four notches to 'BBB-' or below; (ii) the PCU was lowered by four notches to two notches; or (iii) the relied upon OC decreased to below Fitch's 'AAA' breakeven OC of 6.0%. Should the OC decrease to the legal minimum, the covered bonds would be downgraded to 'A+'.

##### Realkredit CC T Covered Bonds

The rating could be upgraded to 'AAA' should the relied upon OC increase to 10%. The rating would be vulnerable to a downgrade if any of the following occurs: (i) Realkredit's Long-Term IDR was downgraded by three notches to 'BBB' or below; (ii) the PCU was lowered by three notches to one notch; or (iii) the relied upon OC decreased to below Fitch's 'AA+' breakeven OC of 8.0%. Should the OC decrease to the legal minimum, the covered bonds would be downgraded to 'A+'.

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.

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#### Applicable Criteria

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

Criteria Addendum: Denmark (pub. 20 Dec 2016) (<https://www.fitchratings.com/site/re/891791>)

Criteria for Country Risk in Global Structured Finance and Covered Bonds (pub. 26 Sep 2016)

(<https://www.fitchratings.com/site/re/881269>)

Criteria for the Analysis of Commercial Real Estate Loans Securing Covered Bonds (pub. 17 Nov 2016)

(<https://www.fitchratings.com/site/re/890302>)

EMEA RMBS Rating Criteria (pub. 29 Nov 2016) (<https://www.fitchratings.com/site/re/891276>)

Fitch's Cover Assets Refinancing Spread Level (RSL) Assumptions - Excel file (pub. 20 Jan 2017)

(<https://www.fitchratings.com/site/re/893377>)

Fitch's Interest Rate Stress Assumptions for Structured Finance and Covered Bonds - Excel File (pub. 17 Feb 2017)

(<https://www.fitchratings.com/site/re/894478>)

Fitch's Foreign-Currency Stress Assumptions for Residual Foreign-Exchange Exposures in Covered Bonds and Structured Finance – Excel File (pub. 26 Oct 2016) (<https://www.fitchratings.com/site/re/888865>)

Global Bank Rating Criteria (pub. 25 Nov 2016) (<https://www.fitchratings.com/site/re/891051>)

Global Rating Criteria for CLOs and Corporate CDOs (pub. 09 Sep 2016) (<https://www.fitchratings.com/site/re/887497>)

SME Balance Sheet Securitisation Rating Criteria (pub. 03 Mar 2017) (<https://www.fitchratings.com/site/re/894773>)

Structured Finance and Covered Bonds Counterparty Rating Criteria (pub. 20 Mar 2017)

(<https://www.fitchratings.com/site/re/894432>)

Structured Finance and Covered Bonds Counterparty Rating Criteria: Derivative Addendum (pub. 20 Mar 2017)

(<https://www.fitchratings.com/site/re/894433>)

Structured Finance and Covered Bonds Interest Rate Stresses Rating Criteria (pub. 17 Feb 2017)

(<https://www.fitchratings.com/site/re/893890>)

#### Additional Disclosures

Dodd-Frank Rating Information Disclosure Form

([https://www.fitchratings.com/creditdesk/press\\_releases/content/ridf\\_frame.cfm?pr\\_id=1021383&cf=eyJ0eXAiOiJKV1QiLCJhbGciOiJIUzI1NiJ9.eyJzZXNzaW9uS2V5IjoiaW50bWV1dIMUJWFBZSEJBWVQwSjUwOEIDRFRKOVVTS0NCV1A2TTIHQyIsImV4cCI6MTQ5MTQ3MTU1NCwidXNlcklkIjoyNTcwNTE3fQ.YWr-5UBPFhi9hfTo7jZmKNMIYX4PL44Rvfab3weVqH8](https://www.fitchratings.com/creditdesk/press_releases/content/ridf_frame.cfm?pr_id=1021383&cf=eyJ0eXAiOiJKV1QiLCJhbGciOiJIUzI1NiJ9.eyJzZXNzaW9uS2V5IjoiaW50bWV1dIMUJWFBZSEJBWVQwSjUwOEIDRFRKOVVTS0NCV1A2TTIHQyIsImV4cCI6MTQ5MTQ3MTU1NCwidXNlcklkIjoyNTcwNTE3fQ.YWr-5UBPFhi9hfTo7jZmKNMIYX4PL44Rvfab3weVqH8))

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