

Transaction Update: Danske Bank A/S (Cover Pool I Mortgage Covered Bonds)

Saerligt Daekkede Obligationer

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Ratings Detail

Reference Rating Level	aa-	+	Jurisdiction-Supported Rating Level	aaa	+	Maximum Achievable Covered Bond Rating	aaa	=	Covered Bond Rating	
Resolution Regime Uplift	+2		Assigned Jurisdictional Support	+3		Collateral Support Uplift	+1		AAA	
Systemic Importance	Very Strong		Jurisdictional Support Assessment	Very Strong		Overcollateralization Adjustment	-1		Rating Constraints	aaa
Resolution Counterparty Rating	A+		Legal Framework	Very Strong		Liquidity Adjustment	0		Counterparty Risk	aaa
Issuer Credit Rating	A		Systemic Importance	Very Strong		Potential Collateral Based Uplift	+2		Country Risk	aaa
			Sovereign Credit Capacity	Very Strong						

Major Rating Factors

Strengths

- The long-term issuer credit rating (ICR) on the issuer is such that the program needs to cover 'AAA' credit risk in order to achieve a 'AAA' rating.
- The program benefits from one unused notch of collateral uplift, which would protect the rating if we downgraded the issuer.
- Due to the covered bonds' soft-bullet maturities, six months liquidity coverage is ensured.

Weaknesses

- The available overcollateralization is provided on a voluntary basis, meaning that we deduct one notch from the collateral-based uplift.

Outlook: Stable

S&P Global Ratings' stable outlook on the ratings on Danske Bank A/S' cover pool I mortgage covered bonds ("saerligt daekkede obligationer"; SDOs) reflects our view that we would not automatically lower the ratings on the covered bonds if we were to lower our long-term ICR on Danske Bank by one notch.

Rationale

This transaction update follows our periodic review of Danske Bank's cover pool I mortgage covered bonds. Our rating analysis for the covered bonds follows the framework set out in our criteria article "Covered Bond Ratings Framework: Methodology And Assumptions," published on June 30, 2015.

The 'AAA' ratings reflect our reference rating level (RRL) of 'aa-' and our jurisdiction-supported rating level (JRL) of 'aaa', as well as the overcollateralization coverage of the 'AAA' credit risk.

The ratings on the program and related issuances are not constrained by legal, operational, counterparty risks, or country risks.

Program Description

Danske Bank is a leading Danish financial services group. It operates primarily in Denmark, Finland, Sweden, and Norway.

We currently rate the category C, D, and I covered bonds issued under the €30,000,000,000 global covered bond program.

Cover pool I contains mortgage loans denominated in Norwegian krone (NOK) and Swedish krona (SEK), secured on Norwegian and Swedish residential properties. The covered bonds are issued in euros, Norwegian krone and Swiss francs. The transaction features interest rate swaps and cross-currency swaps on both assets and liabilities.

In 2017, through its Swedish subsidiary, Danske Hypotek, Danske Bank launched a covered bond program entirely backed by Swedish residential mortgages. Ever since, the share of Swedish assets in Cover Pool I has decreased, as loans that refinance get transferred to the Swedish program and loans that mature are not replaced by new origination.

The bonds are senior-secured obligations. They rank pari passu with other obligations backed by the same cover pool. If the issuer were to become bankrupt, the pools would be managed separately.

Table 1

Program Description*	
Jurisdiction	Denmark
Covered bond type	Legislation-enabled
Underlying assets	Residential mortgage loans
Outstanding covered bonds (Bil. NOK)	123.7 Bn

Table 1

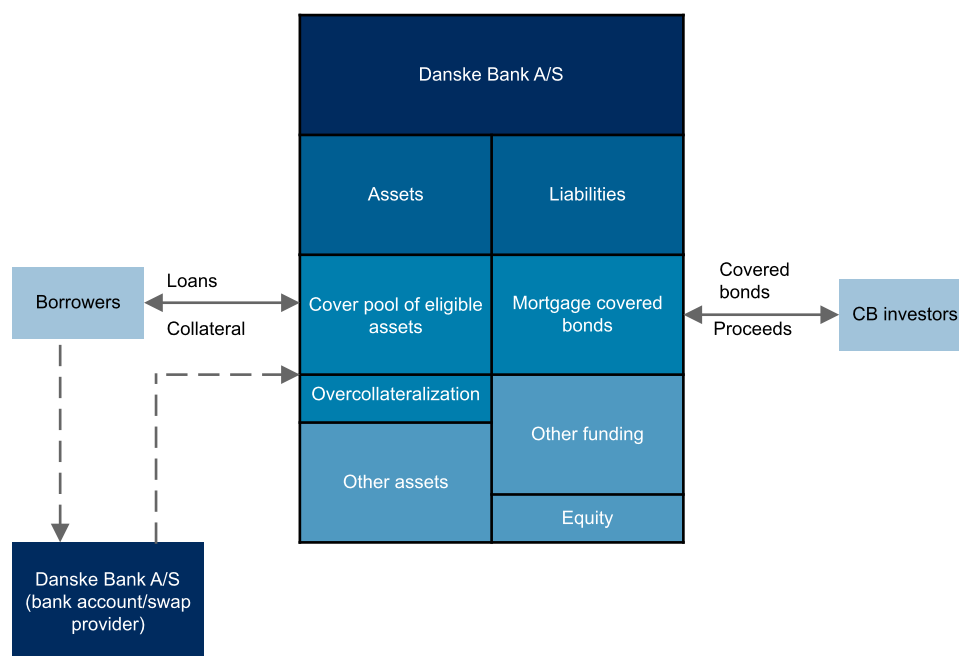
Program Description* (cont.)	
Rating at closing	'AAA'
Extendible maturities	Yes
Target credit enhancement (%)	22.21
Available credit enhancement (%)	16.86

*Based on data as of Sept. 30, 2019. NOK--Norwegian krona.

Table 2

Participants			
Role	Name	Rating	Rating dependency
Issuer	Danske Bank A/S	A/Stable/A-1	Y
Swap provider	Danske Bank A/S	A/Stable/A-1	Y
Bank account provider	Danske Bank A/S	A/Stable/A-1	N
Originator	Danske Bank A/S	A/Stable/A-1	N

Program Structure



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Rating Analysis

Legal and regulatory risks

In our view, the Danish covered bond framework sufficiently addresses the relevant legal aspects of our covered bonds criteria and our legal criteria (see "Asset Isolation And Special-Purpose Entity Methodology," published on March 29, 2017). This enables us to assign ratings to the covered bonds that exceed the long-term ICR on the issuer.

The Danish Covered Bond Act provides the legal framework for the issuance of the Danish covered bonds. It also outlines eligibility criteria for the inclusion of assets in the cover pool. The issuer needs to obtain a general covered bond issuing license from the Danish Financial Supervisory Authority.

Under certain restrictions, an SDO cover pool can include mortgage credit assets secured on residential and commercial properties within the European Economic Area (EEA), the Organization for Economic Cooperation and Development (OECD), as well as loans granted to public bodies in the EEA and OECD. It may also include supplementary assets, such as securities from eligible financial institutions in the EEA or the OECD.

Under the law:

- The cover pool must register all derivatives used for hedging mismatches. The derivatives rank pari passu with the bonds.
- The cover pool's value must always exceed that of the covered bonds.
- The law requires the prudent market valuation of the mortgage credit assets according to recognized principles, and collateral valuation is performed annually.

If Danske Bank becomes insolvent, the covered bondholders have a preferential claim on the proceeds generated by the pool. Danish covered bonds do not automatically accelerate if the issuer becomes insolvent. In such a scenario, the cover pool is managed by a bankruptcy administrator, who is obliged to ensure timely payment. To this end, the administrator is entitled to take appropriate measures aimed at raising liquidity by selling or borrowing against unmatched assets, in order to repay the maturing covered bonds' principal. The cover pool bears costs, which rank senior to the covered bondholders' claims.

Danske Bank adheres to the general balancing principle (in contrast to the specific balancing principle) in order to manage market risk exposure. The issuer has the flexibility to issue covered bonds that are delinked from the mortgage assets, and the mortgage collateral acts as overcollateralization.

Under Danish law, collateral added to a cover pool less than three months before the bankruptcy of the issuer may be "clawed back" or challenged by other creditors if the covered bondholders received preferential treatment at the expense of the issuer's ordinary creditors. If such a challenge were to succeed, fewer assets would be available for covered bondholders from the relevant cover pool. We continuously monitor the transfer of collateral and consider the credit rating on the issuer in determining the size of a potential clawback. As Danske Bank has shown a pattern of providing sufficient overcollateralization to maintain a 'AAA' rating, any increase in the asset pool to maintain this rating would likely be considered ordinary, and therefore not subject to clawback.

Operational and administrative risks

In June 2019, we conducted a review of Danske Bank's origination, underwriting, collection, and default management procedures for the cover pool assets. We also reviewed the cover pool management and administration. We consider that Danske Bank actively manages the cover pool and has strict underwriting and loan management policies. We have not identified any operational or administrative risks that would affect our assessment of the program.

We believe that a replacement servicer can be found should the issuer become insolvent. We consider Denmark to be an established covered bond market and the assets in the cover pool to be standard, hence not limiting the range of available cover pool managers or servicers.

Resolution regime analysis

As part of our covered bonds criteria, our analysis considers the presence of resolution regimes when determining the RRL. Denmark is a member of the EU and implemented the EU's Bank Recovery and Resolution Directive (BRRD), therefore this analysis considers the support provided by the adoption of the regime.

The program's RRL is equal to the greater of (i) the ICR on the issuing bank, plus up to two notches for programs in jurisdictions with effective resolution regimes that exempt covered bond from bail-in, and (ii) the resolution counterparty rating (RCR) on the issuing bank, where applicable.

Given Danske Bank's 'A+' RCR, and our very strong systemic importance assessment for covered bonds in Denmark, the RRL is 'aa-', two notches above the ICR.

Jurisdictional support analysis

Our analysis of jurisdictional support in our covered bonds criteria determines a JRL of 'aaa', which is our assessment of the creditworthiness of a covered bond program once we have considered the level of jurisdictional support, but before giving credit to the amount of collateral.

In our jurisdictional support analysis, we assess the likelihood that a covered bond program facing stress would receive support from a government-sponsored initiative, instead of from the liquidation of collateral assets in the open market. Our assessment of the expected jurisdictional support for Danish mortgage covered bond programs is very strong (see ""Assessments For Jurisdictional Support According To Our Covered Bonds Criteria" ," published on Mar. 3, 2020). It this means that the program can receive up to three notches of jurisdictional uplift from the RRL. This leads to a JRL of 'aaa' for Danske Bank's cover pool I mortgage covered bonds.

Collateral support analysis

Table 3

Cover Pool Composition				
Asset type	As of Sept. 30, 2019		As of Dec. 31, 2018	
	Value (Mil. NOK)	Percentage of cover pool (%)	Value (Mil. NOK)	Percentage of cover pool (%)
Residential	144,611.5	100.0	141,550.8	100.0
Commercial	0.0	0.0	0.0	0.0
Substitute assets	0.0	0.0	0.0	0.0
Other asset type	0.0	0.0	0.0	0.0
Total	144,611.5	100.0	141,550.8	100.0

NOK--Norwegian krone.

Table 4a

Key Credit Metrics: Norwegian Assets		
	As of Sept. 30, 2019	As of Dec. 31, 2018
Weighted-average loan-to-value ratio (%)	58.9	58.3
Balance of loans in arrears (%)	1.0	1.0
Credit analysis results		
Weighted-average foreclosure frequency (%)	14.3	15.9
Weighted-average loss severity (%)	41.1	42.0

Table 4b

Key Credit Metrics: Swedish Assets		
	As of Sept. 30, 2019	As of Dec. 31, 2018
Weighted-average loan-to-value ratio (%)	58.7	60.4
Balance of loans in arrears (%)	0.1	0.2
Credit analysis results		
Weighted-average foreclosure frequency (%)	11.9	12.5
Weighted-average loss severity (%)	57.5	59.6

Table 4c

Key Credit Metrics		
	As of Sept. 30, 2019	As of Dec. 31, 2018
Weighted-average foreclosure frequency (%)	13.9	15.6
Weighted-average loss severity (%)	44.5	45.4

Table 5a

Loan-To-Value Ratios: Norway		
	As of Sept. 30, 2019	As of Dec. 31, 2018
(%)	Percentage of cover pool (%)	
0 to 60	47.9	52.4
60 to 70	17.6	19.2
70 to 80	16.5	17.0
80 to 90	12.0	7.7
90 to 100	3.1	2.1
More than 100	2.8	1.5
Weighted-average loan-to-value ratios	58.9	58.3

Table 5b

Loan-To-Value Ratios: Sweden		
	As of Sept. 30, 2019	As of Dec. 31, 2018
(%)	Percentage of cover pool (%)	
0 to 60	56.0	48.2
60 to 70	15.1	16.8
70 to 80	13.5	16.3
80 to 90	9.2	10.6

Table 5b

Loan-To-Value Ratios: Sweden (cont.)		
	As of Sept. 30, 2019	As of Dec. 31, 2018
90 to 100	3.7	4.9
Above 100	2.6	3.1
Weighted-average loan-to-value ratios	58.7	60.4

Table 6a

Loan Seasoning Distribution: Norway		
	As of Sept. 30, 2019	As of Dec. 31, 2018
Percentage of cover pool (%)		
Less than 5 years	76.2	75.3
5-6	4.0	3.3
6-7	2.5	3.8
7-8	3.4	3.7
8-9	2.4	2.6
9-10	1.9	2.2
More than 10 years	9.1	9.3
Weighted-average loan seasoning (years)	4.0	4.0

*Seasoning refers to the elapsed loan term.

Table 6b

Loan Seasoning Distribution: Sweden		
	As of Sept. 30, 2019	As of Dec. 31, 2018
Percentage of cover pool (%)		
Less than 5 years	59.3	61.5
5-6	3.7	3.7
6-7	4.2	5.7
7-8	4.2	3.9
8-9	4.5	6.0
9-10	5.6	4.9
More than 10 years	18.5	14.4
Weighted-average loan seasoning (years)	5.5	4.9

*Seasoning refers to the elapsed loan term.

Table 7a

Geographic Distribution Of Loan Assets: Norway		
Percentage of cover pool (%)		
	As of Sept. 30, 2019	As of Dec. 31, 2018
East	84.3	83.9
West	4.3	4.7
Trondelag	11.4	11.5
North	0.0	0.0
South	0.0	0.0
Total	100.0	100.0

Table 7b

Geographic Distribution Of Loan Assets: Sweden		
	Percentage of cover pool (%)	
	As of Sept. 30, 2019	As of Dec. 31, 2018
Smaland and the islands	42.4	41.6
South Sweden	57.3	58.0
Upper Norrland	0.4	0.4
Total	100.0	100.0

Table 8

Collateral Uplift Metrics		
	As of Sept. 30, 2019	As of Dec. 31, 2018
Asset WAM (years)	11.94	11.91
Liability WAM (years)	3.88	4.35
Maturity gap (years)	8.06	7.56
Available credit enhancement	16.86	19.43
AAA' credit risk	8.64	9.72
Credit enhancement for first notch of collateral uplift (%)	12.03	12.83
Credit enhancement for second notch of collateral uplift (%)	15.43	15.93
Credit enhancement for third notch of collateral uplift (%)	18.82	19.04
Credit enhancement for maximum uplift (%)	22.21	22.14
Potential collateral-based uplift (notches)	2	3
Adjustment for liquidity (Y/N)	N	N
Adjustment for committed overcollateralization (Y/N)	Y	Y
Collateral support uplift (notches)	1	2

WAM--Weighted-average maturity.

We base our credit analysis on the loan-level data provided by the issuer as of Sept. 30, 2019. The cover pool comprises only residential mortgage loans backed by Norwegian (83.4%) and Swedish (16.6%) assets. We analyze these pools under our European residential loans criteria (see "Methodology And Assumptions: Assessing Pools Of European Residential Loans," published on Aug. 4, 2017).

The pool's current weighted-average foreclosure frequency (WAFF) is 13.88%, down from the 15.61% that resulted from our December 2018 analysis.

In the Norwegian sub-pool the WAFF decreases to 14.28% from 15.93%, due to a lower weighted-average original LTV and to a lower amount of second lien loans. In the Swedish sub-pool the figure decreases to 11.90% from 12.49%, due to a higher seasoning, a lower amount of tenant-owner rights and, here too, to a decrease in the weighted-average original LTV.

The pool's weighted-average loss severity (WALS) is 44.49%, lower than the December 2018 figure, 45.37%.

In the Norwegian sub-pool the WALS goes down to 41.13%, from 41.99%, in light of a slightly lower assumed overvaluation. In the Swedish sub-pool the figure drops to 57.54% from 59.62%, thanks to a lower weighted-average

current LTV and lower amount of jumbo valuations and tenant-owner rights.

According to our covered bonds criteria, the maximum potential collateral-based uplift on a covered bond program above the JRL is four notches. We then look to make adjustments to the maximum collateral-based uplift by reviewing the six-month liquidity coverage and the level of committed overcollateralization. Due to the covered bonds' soft-bullet maturities, liquidity coverage is being met, according to our criteria. The available credit enhancement is provided voluntarily, which means that we reduce the amount of collateral-based uplift by one notch.

By applying our credit and cash flow stresses, we calculate a target credit enhancement (TCE), which would allow the program to receive four notches of collateral-based uplift. The TCE calculated on September 2019 data is 22.21%. This is marginally higher than the 22.14% resulting from the December 2018 analysis, due to a higher asset-liability mismatch, only partially offset by the lower credit figures.

However, given the JRL of 'aaa', under our covered bonds criteria, only coverage of the 'AAA' credit risk, at 8.64%, is required to maintain the current 'AAA' rating, based solely on jurisdictional support. The available credit enhancement, which is 16.86% after applying a haircut to account for set-off risk, is sufficient to cover this requirement.

Counterparty risk

We analyze counterparty risk by applying our counterparty criteria (see "Counterparty Risk Framework: Methodology And Assumptions," published on March 8, 2019).

Commingling risk. Pre-insolvency, principal proceeds are either reinvested or immediately used to repay the bondholders. Post-insolvency, proceeds from the borrowers are identified and promptly segregated for the benefit of the bondholders. We size a small amount to account for the potential disruption that might affect payments in a post-insolvency scenario.

Swaps. Danske Bank is the sole swap counterparty for this program. Hedging addresses interest rate and currency mismatches between the pool's mortgage loans and the payments due to covered bondholders. Termination costs are not subordinated.

Given that the counterparty is related to the issuer, the applicable counterparty rating is the RRL, according to our criteria. We deem the commitment made by the counterparty to replace itself upon downgrade to be satisfactory, and the collateral framework to be moderate.

The swap agreements contain a replacement trigger set at 'A-', which we map to its corresponding RRL, of 'A'.

Given the issuer's RRL, the collateral framework and the replacement trigger, the swap we see in this program is supportive of a 'AAA' rating.

Set-off risk. There is a risk that borrowers of certain loans contained in the cover pool retain a residual right under the relevant local legislation to set-off claims against the outstanding amount of their loans. In order to mitigate this risk the issuer will include additional assets in the cover pool, up to a value that is equal to the set-off risk as calculated quarterly. We deduct this amount from the cover pool balance when calculating the transaction's available overcollateralization. As of September 2019 the amount at risk is equal to roughly DKK1 billion.

Sovereign risk

We consider country risk in line with our criteria (see "Incorporating Sovereign Risk In Rating Structured Finance Securities: Methodology And Assumptions," published on Jan. 30, 2019).

The assets are located in Norway and Sweden and we consider this to be a multijurisdictional pool under our criteria. To determine the maximum differential above the sovereign rating, we look at the issuer's domicile. As Denmark is currently rated 'AAA' (unsolicited), sovereign risk does not constrain the rating on the program.

Potential effects of COVID-19

While there continues to be a high degree of uncertainty about the rate of spread and timing of the peak of the coronavirus outbreak--some government authorities are estimating late second-quarter 2020 to mid-third-quarter, which we've used in assessing economic and credit implications. In any case, the COVID-19 pandemic has likely pushed the global economy into recession, which could also negatively affect employment levels or housing markets (see "COVID-19 Macroeconomic Update: The Global Recession Is Here And Now," and "COVID-19 Credit Update: The Sudden Economic Stop Will Bring Intense Credit Pressure," both published on March 17, 2020). As the situation evolves, we will update our assumptions and estimates accordingly.

Related Criteria

- Counterparty Risk Framework: Methodology And Assumptions, March 8, 2019
- Incorporating Sovereign Risk In Rating Structured Finance Securities: Methodology And Assumptions, Jan. 30, 2019
- Asset Isolation And Special-Purpose Entity Methodology, March 29, 2017
- Covered Bond Ratings Framework: Methodology And Assumptions, June 30, 2015
- Methodology And Assumptions: Assessing Pools Of European Residential Loans, Aug. 4, 2017
- Covered Bonds Criteria, Dec. 9, 2014
- Credit Stability Criteria, May 3, 2010
- Use Of CreditWatch And Outlooks, Sept. 14, 2009

Related Research

- COVID-19 Macroeconomic Update: The Global Recession Is Here And Now, March 17, 2020
- COVID-19 Credit Update: The Sudden Economic Stop Will Bring Intense Credit Pressure, March 17, 2020
- Global Covered Bond Characteristics And Rating Summary Q4 2019, Dec. 12, 2019
- Global Covered Bond Insights Q4 2019, Dec. 12, 2019
- Various Rating Actions Taken On Five Danish Banks As Denmark's Banking Market Offers Mixed Blessings, Oct. 23, 2019
- S&P Global Ratings Definitions, Sept. 18, 2019

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- Denmark Ratings Affirmed At 'AAA/A-1+'; Outlook Stable, March 8, 2019
- Assessments For Target Asset Spreads According To Our Covered Bonds Criteria, March 3, 2020
- Assessments For Jurisdictional Support According To Our Covered Bonds Criteria, March 3, 2020
- Credit FAQ: The Danish Covered Bond Market Explained, July 15, 2014

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