

16 Apr 2020 | Affirmation

## Fitch Affirms Danske Bank AS's Mortgage Cover Pool C Covered Bonds at 'AAA'

---

**Link to Fitch Ratings' Report(s):** [Danske Bank AS, Mortgage SDO \(Cover Pool C\) ESG Navigator](#)

Fitch Ratings-Frankfurt am Main-16 April 2020:

Fitch Ratings has affirmed Danske Bank AS's (Danske, A/Rating Watch Negative (RWN)/F1) mortgage covered bonds secured by the bank's cover pool C at 'AAA' with a Stable Outlook.

### KEY RATING DRIVERS

The covered bonds' rating is based on Danske's Long-Term Issuer Default Rating (IDR) of 'A', the various uplifts above the IDR granted to the programme and also considers the overcollateralisation (OC) protection for covered bond holders.

The covered bonds are rated five notches above the bank's IDR. This is out of a maximum achievable uplift of nine notches, consisting of an IDR uplift of two notches, a payment continuity uplift (PCU) of five notches and a recovery uplift of two notches.

Fitch relies on the lowest level of OC of the last 12 months of 21%, which provides more protection than Fitch's reduced 'AAA' breakeven OC of 17%.

The Stable Outlook on Danske's covered bonds reflects the four-notch buffer against a downgrade of the bank's IDR, which is on RWN.

### 'AAA' Breakeven OC

The 17% Fitch 'AAA' breakeven OC supports timely payments in a 'AA+' stress scenario and a one-notch recovery uplift to 'AAA'. The credit loss of currently 15.6% remains the largest component of the breakeven OC. In its asset analysis, Fitch applied a benchmark one-year probability of default (PD) of 1.85% for loans secured by Swedish commercial real estate (67%), with a PD floor of 0.5%, and a benchmark one-year PD 2.35% for loans secured by Norwegian commercial real estate (with a floor at 0.5%). The benchmark one-year PDs, based on extensive data on observed default rates (ODR) and expected PDs provided by Danske, was increased by 0.35% for both countries compared to last year. This additional stress reflects the potential impact

of the COVID-19 pandemic, where we currently expect a temporary, sharp economic deterioration similar or worse compared with the financial crisis of 2008-09.

The lower credit loss component is driven by the smaller proportion of large obligors (reduced to 16% from 19.56%). For these obligors, Fitch applies a minimum one-year PD of at least 1.0%, a correlation uplift of 50% and a recovery rate multiplier of 0.5, in line with criteria. In assessing the cover pool's PD, Fitch has assumed a three-year longer maturity for the interest-only loans (26%) to reflect the longer effective term as those borrowers are expected to seek to refinance their loans at maturity. Fitch also assumed a 40% cure rate in a 'B' scenario.

Fitch applied market value decline (MVD) assumptions according to its SME Balance Sheet Securitisation Rating Criteria, where multi-family properties were treated as residential property, and residential MVDs for Swedish and Norwegian properties defined in the Originator-Specific Residential Mortgage Analysis Rating Criteria were applied. The remaining property types were treated as commercial properties, for which we applied the fall-back MVDs under the SME criteria.

The ALM loss decreased to 1.2%, from previously 1.3%. As the weighted-average life (WAL) of the assets is shorter than the WAL of the bonds, the driving high prepayment scenario puts strain on the negative cost of carry of holding cash before repaying the maturing bonds. In the cash flow modelling, the low and high stressed prepayment rate is 5% and 25%, respectively, and a foreclosure timing assumption of 36 months.

#### Uplifts

The programme's two-notch IDR uplift reflects that covered bonds issued by retail banks in Denmark are exempt from bail-in, Fitch's assessment that the risk of under-collateralisation at the point of resolution is sufficiently low, and that a resolution of Danske, should it happen, would not result in the direct enforcement of the recourse against the cover pool.

Fitch's PCU for Danske's C programme is five notches, rather than the standard six for mortgage covered bonds with a 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.

The recovery uplift for the programme was increased to two notches from previously one, as Fitch deems that the foreign exchange risk in a recovery given default scenario is mitigated by the shorter weighted average life of the assets compared with the liabilities. The relied-upon OC now also offsets the credit loss in a 'AAA' stress scenario and no other material downside risk to recoveries has been identified.

## RATING SENSITIVITIES

Factors that could, individually or collectively, lead to positive rating action/upgrade:

The covered bonds' rating is 'AAA', which is the highest level on Fitch's scale. The rating cannot be upgraded.

Factors that could, individually or collectively, lead to negative rating action/downgrade:

(i) Danske's Long-Term IDR is downgraded by five notches to 'BB+' or below; or (ii) the payment continuity uplift is reduced to zero; or (iii) the level of OC Fitch gives credit to in its analysis fell below the 'AAA' breakeven OC for the programme of 17.0 %.

If the actual OC is reduced to the legal minimum of 0%, the covered bonds would be downgraded to 'AA', three notches above the bank's IDR.

Fitch expects the coronavirus containment measures to negatively affect the performance of Norwegian and Swedish commercial real estate loans. However, the covered bonds' rating benefits from a cushion between the OC that Fitch relies upon in its analysis and Fitch's 'AAA' breakeven OC (21% versus 17%). Danske also has eligible mortgage loans on its balance sheet, allowing it to replenish the cover pool with performing loans. In addition, the rating is well protected by the four-notch buffer against a downgrade of Danske's IDR. Nevertheless, the agency expects the OC cushion and the buffer against an issuer downgrade to reduce as a consequence of the coronavirus crisis.

When Fitch performed downside sensitivity scenario stresses to the programme by increasing the cover pool's PD assumption, decreasing recovery rates on the mortgage loans, increasing the obligor concentration, as well as increasing the stressed cost to refinance the cover pool, the current OC still provided sufficient protection for the 'AAA' rating of the programme.

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

### Best/Worst Case Rating Scenario

International scale credit ratings of Financial Institutions issuers have a best-case rating upgrade scenario (defined as the 99th percentile of rating transitions, measured in a positive direction) of

three notches over a three-year rating horizon; and a worst-case rating downgrade scenario (defined as the 99th percentile of rating transitions, measured in a negative direction) of four notches over three years. The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Best- and worst-case scenario credit ratings are based on historical performance. For more information about the methodology used to determine sector-specific best- and worst-case scenario credit ratings, visit <https://www.fitchratings.com/site/re/10111579>.

#### REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

#### PUBLIC RATINGS WITH CREDIT LINKAGE TO OTHER RATINGS

The covered bonds' ratings are driven by the credit risk of Danske Bank as measured by its Long-Term IDR.

#### ESG Considerations

The highest level of ESG credit relevance is a score of '3'. This means ESG issues are credit neutral or have only a minimal credit impact on Danske's covered bonds, either due to their nature or to the way in which they are being managed by the programme. For more information on Fitch's ESG Relevance Scores, visit [www.fitchratings.com/esg](http://www.fitchratings.com/esg).

#### Danske Bank A/S

---senior secured, Mortgage Covered Bonds, Combined; Long Term Rating; Affirmed; AAA; RO:Sta

#### Contacts:

Primary Rating Analyst

Matthew Aitken,

Associate Director

+49 69 768076 165

Fitch Deutschland GmbH

Neue Mainzer Strasse 46 - 50

Frankfurt am Main D-60311

Secondary Rating Analyst

Geir Brust,

Director

+44 20 3530 1638

Committee Chairperson

Vessela Krmnicek, CFA

Senior Director

+49 69 768076 298

Media Relations: Athos Larkou, London, Tel: +44 20 3530 1549, Email:

athos.larkou@thefitchgroup.com

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

### **Applicable Criteria**

[Bank Rating Criteria \(pub. 28 Feb 2020\) \(including rating assumption sensitivity\)](#)

[Covered Bonds Rating Criteria \(pub. 24 Jul 2019\) \(including rating assumption sensitivity\)](#)

[EMEA CMBS and CRE Loan Rating Criteria \(pub. 31 May 2019\) \(including rating assumption sensitivity\)](#)

[Fitch Ratings Interest Rate Stress Assumptions for Structured Finance and Covered Bonds \(Excel\) \(pub. 06 Dec 2019\)](#)

[Originator-Specific Residential Mortgage Analysis Rating Criteria \(pub. 21 Feb 2020\) \(including rating assumption sensitivity\)](#)

[SME Balance Sheet Securitisation Rating Criteria \(pub. 07 Feb 2020\) \(including rating assumption sensitivity\)](#)

[Structured Finance and Covered Bonds Counterparty Rating Criteria \(pub. 29 Jan 2020\)](#)

[Structured Finance and Covered Bonds Counterparty Rating Criteria: Derivative Addendum \(pub. 29 Jan 2020\)](#)

[Structured Finance and Covered Bonds Country Risk Rating Criteria \(pub. 06 Feb 2020\)](#)

[Structured Finance and Covered Bonds Interest Rate Stresses Rating Criteria \(pub. 06 Dec 2019\)](#)

### **Applicable Model**

Numbers in parentheses accompanying applicable model(s) contain hyperlinks to criteria providing description of model(s).

Covered Bonds Cash Flow Model, v1.27.0 (1)

Portfolio Credit Model, v2.8.1 (1)

## **Additional Disclosures**

[Dodd-Frank Rating Information Disclosure Form](#)

[Solicitation Status](#)

[Endorsement Status](#)

[Endorsement Policy](#)

ALL FITCH CREDIT RATINGS ARE SUBJECT TO CERTAIN LIMITATIONS AND DISCLAIMERS. PLEASE READ THESE LIMITATIONS AND DISCLAIMERS BY FOLLOWING THIS LINK:

[HTTPS://WWW.FITCHRATINGS.COM/UNDERSTANDINGCREDITRATINGS](https://www.fitchratings.com/understandingcreditratings). IN ADDITION, THE FOLLOWING [HTTPS://WWW.FITCHRATINGS.COM/RATING-DEFINITIONS-DOCUMENT](https://www.fitchratings.com/rating-definitions-document) DETAILS FITCH'S RATING DEFINITIONS FOR EACH RATING SCALE AND RATING CATEGORIES, INCLUDING DEFINITIONS RELATING TO DEFAULT. PUBLISHED RATINGS, CRITERIA, AND METHODOLOGIES ARE AVAILABLE FROM THIS SITE AT ALL TIMES. FITCH'S CODE OF CONDUCT, CONFIDENTIALITY, CONFLICTS OF INTEREST, AFFILIATE FIREWALL, COMPLIANCE, AND OTHER RELEVANT POLICIES AND PROCEDURES ARE ALSO AVAILABLE FROM THE CODE OF CONDUCT SECTION OF THIS SITE. DIRECTORS AND SHAREHOLDERS RELEVANT INTERESTS ARE AVAILABLE AT [HTTPS://WWW.FITCHRATINGS.COM/SITE/REGULATORY](https://www.fitchratings.com/site/regulatory). FITCH MAY HAVE PROVIDED ANOTHER PERMISSIBLE SERVICE TO THE RATED ENTITY OR ITS RELATED THIRD PARTIES. DETAILS OF THIS SERVICE FOR RATINGS FOR WHICH THE LEAD ANALYST IS BASED IN AN EU-REGISTERED ENTITY CAN BE FOUND ON THE ENTITY SUMMARY PAGE FOR THIS ISSUER ON THE FITCH WEBSITE.

Copyright © 2020 by Fitch Ratings, Inc., Fitch Ratings Ltd. and its subsidiaries. 33 Whitehall Street, NY, NY 10004. Telephone: 1-800-753-4824, (212) 908-0500. Fax: (212) 480-4435. Reproduction or retransmission in whole or in part is prohibited except by permission. All rights reserved. In issuing and maintaining its ratings and in making other reports (including forecast information), Fitch relies on factual information it receives from issuers and underwriters and from other sources Fitch believes to be credible. Fitch conducts a reasonable investigation of the factual information relied upon by it in accordance with its ratings methodology, and obtains reasonable verification of that information from independent sources, to the extent such sources are available for a given security or in a given jurisdiction. The manner of Fitch's factual investigation and the scope of the third-party verification it obtains will vary depending on the nature of the rated security and its issuer, the requirements and practices in the jurisdiction in which the rated security is offered and sold and/or the issuer is located, the availability and nature of relevant public information, access to the management of the issuer and its advisers, the availability of pre-existing third-party verifications such as audit reports, agreed-upon procedures letters, appraisals, actuarial reports, engineering reports, legal opinions and other reports provided by third parties, the availability of independent and competent third-party verification sources with respect to the particular security

or in the particular jurisdiction of the issuer, and a variety of other factors. Users of Fitch's ratings and reports should understand that neither an enhanced factual investigation nor any third-party verification can ensure that all of the information Fitch relies on in connection with a rating or a report will be accurate and complete. Ultimately, the issuer and its advisers are responsible for the accuracy of the information they provide to Fitch and to the market in offering documents and other reports. In issuing its ratings and its reports, Fitch must rely on the work of experts, including independent auditors with respect to financial statements and attorneys with respect to legal and tax matters. Further, ratings and forecasts of financial and other information are inherently forward-looking and embody assumptions and predictions about future events that by their nature cannot be verified as facts. As a result, despite any verification of current facts, ratings and forecasts can be affected by future events or conditions that were not anticipated at the time a rating or forecast was issued or affirmed.

The information in this report is provided "as is" without any representation or warranty of any kind, and Fitch does not represent or warrant that the report or any of its contents will meet any of the requirements of a recipient of the report. A Fitch rating is an opinion as to the creditworthiness of a security. This opinion and reports made by Fitch are based on established criteria and methodologies that Fitch is continuously evaluating and updating. Therefore, ratings and reports are the collective work product of Fitch and no individual, or group of individuals, is solely responsible for a rating or a report. The rating does not address the risk of loss due to risks other than credit risk, unless such risk is specifically mentioned. Fitch is not engaged in the offer or sale of any security. All Fitch reports have shared authorship. Individuals identified in a Fitch report were involved in, but are not solely responsible for, the opinions stated therein. The individuals are named for contact purposes only. A report providing a Fitch rating is neither a prospectus nor a substitute for the information assembled, verified and presented to investors by the issuer and its agents in connection with the sale of the securities. Ratings may be changed or withdrawn at any time for any reason in the sole discretion of Fitch. Fitch does not provide investment advice of any sort. Ratings are not a recommendation to buy, sell, or hold any security. Ratings do not comment on the adequacy of market price, the suitability of any security for a particular investor, or the tax-exempt nature or taxability of payments made in respect to any security. Fitch receives fees from issuers, insurers, guarantors, other obligors, and underwriters for rating securities. Such fees generally vary from US\$1,000 to US\$750,000 (or the applicable currency equivalent) per issue. In certain cases, Fitch will rate all or a number of issues issued by a particular issuer, or insured or guaranteed by a particular insurer or guarantor, for a single annual fee. Such fees are expected to vary from US\$10,000 to US\$1,500,000 (or the applicable currency equivalent). The assignment, publication, or dissemination of a rating by Fitch shall not constitute a consent by Fitch to use its name as an expert in connection with any registration statement filed under the United States securities laws, the Financial Services and Markets Act of 2000 of the United Kingdom, or the securities laws of any particular jurisdiction. Due to the relative efficiency of electronic publishing

and distribution, Fitch research may be available to electronic subscribers up to three days earlier than to print subscribers.

For Australia, New Zealand, Taiwan and South Korea only: Fitch Australia Pty Ltd holds an Australian financial services license (AFS license no. 337123) which authorizes it to provide credit ratings to wholesale clients only. Credit ratings information published by Fitch is not intended to be used by persons who are retail clients within the meaning of the Corporations Act 2001. Fitch Ratings, Inc. is registered with the U.S. Securities and Exchange Commission as a Nationally Recognized Statistical Rating Organization (the "NRSRO"). While certain of the NRSRO's credit rating subsidiaries are listed on Item 3 of Form NRSRO and as such are authorized to issue credit ratings on behalf of the NRSRO (see <https://www.fitchratings.com/site/regulatory>), other credit rating subsidiaries are not listed on Form NRSRO (the "non-NRSROs") and therefore credit ratings issued by those subsidiaries are not issued on behalf of the NRSRO. However, non-NRSRO personnel may participate in determining credit ratings issued by or on behalf of the NRSRO.

---

**ENDORSEMENT POLICY** - Fitch's approach to ratings endorsement so that ratings produced outside the EU may be used by regulated entities within the EU for regulatory purposes, pursuant to the terms of the EU Regulation with respect to credit rating agencies, can be found on the [EU Regulatory Disclosures](#) page. The endorsement status of all International ratings is provided within the entity summary page for each rated entity and in the transaction detail pages for all structured finance transactions on the Fitch website. These disclosures are updated on a daily basis.