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

Saerligt Daekkede Obligationer

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Ratings Detail

Reference Rating Level	**aa**
Resolution Regime Uplift	+2
Systemic Importance	Very Strong
Resolution Counterparty Rating	AA-
Issuer Credit Rating	**A+**

+

Jurisdiction-Supported Rating Level	**aaa**
Assigned Jurisdictional Support Uplift	+2
Jurisdictional Support Assessment	Very Strong
Legal Framework	Very Strong
Systemic Importance	Very Strong
Sovereign Credit Capacity	Very Strong

+

Maximum Achievable Covered Bond Rating	**aaa**
Collateral Support Uplift	0
Overcollateralization Adjustment	-1
Liquidity Adjustment	0
Potential Collateral Based Uplift	+2

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Covered Bond Rating	**AAA**
Rating Constraints	aaa
Counterparty Risk	aaa
SovereignRisk	aaa

Major Rating Factors

Strengths

- The issuer credit rating (ICR) allows for a 'AAA' rating to be reached with the jurisdictional support and the coverage of 'AAA' credit risk.
- The program benefits one notch of unused jurisdiction-supported rating level (JRL) uplift, which would protect the rating if we lower our rating on the issuer.
- Due to the covered bonds' soft bullet maturities, we consider 180 days liquidity covered.

Weaknesses

- The cover pool's assets comprise commercial real estate loans, which we consider to be riskier than residential real estate loans.
- The Norwegian assets have some concentration in the region of Trondelag.
- Since our previous review, excess spread has decreased while the asset liability mismatch has increased (see "Related Research").

- The available overcollateralization is provided on a voluntary basis, reducing the amount of collateral-based uplift by one notch.

Outlook: Stable

S&P Global Ratings' stable outlook on the ratings on Danske Bank A/S' cover pool C 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 a single notch.

Rationale

This transaction update follows our periodic review of Danske Bank's cover pool C 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.

Danske bank issues according to the Danish covered bond act, which implements the EU's Covered Bonds Directive. Bonds issued before the update of the Danish legislation are grandfathered, and treated as bonds issued after the implementation of the amended covered bond act. All covered bonds carry the "European covered bonds (Premium)" designation.

We consider that the Danish legal and regulatory framework isolates the cover pool assets from the issuer's insolvency estate for the benefit of the covered bondholders. Based on our review of the issuer's processes and procedures, we believe that the ratings on the covered bonds are not constrained by operational risk.

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

Danske Bank is domiciled in Denmark, which is subject to the EU's Bank Recovery and Resolution Directive (BRRD). We consider mortgage covered bonds to have very strong systemic importance to Denmark. These factors increase the likelihood that the issuer would continue servicing its covered bonds without accessing the cover pool or receiving jurisdictional support, even following a bail-in of its senior unsecured obligations. Therefore, under our covered bonds criteria, we assess the RRL as 'aa', two notches above its ICR.

Our jurisdictional support analysis determined the JRL of the covered bonds as 'aaa'. We considered the likelihood of jurisdictional support for mortgage covered bonds in Denmark, which we assess as very strong, resulting in a jurisdictional support uplift from the RRL of up to three notches. Danske Bank's covered bonds use two notches of uplift to achieve a JRL of 'aaa'.

The ratings on the program and related issuances are not constrained by counterparty or sovereign risks.

Program Description

Danske Bank is a leading Danish financial services group. It operates primarily in Denmark, Finland, Sweden, and Norway. Danske Bank has a leading position as a deposit-taker in Denmark and plays a significant role in the well-functioning Danish mortgage market through Realkredit Denmark A/S.

We currently rate the category C, D, and I covered bonds issued under the €30.0 billion global covered bond program.

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

Danske Bank adheres to the general balance principle (in contrast to the specific balance 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.

The covered bonds rank pari passu with other covered bonds and derivatives from the same cover pool. If the issuer were to become bankrupt, Danske Bank's cover pools would be separated and managed independent of each other.

Table 1

Program description*	
Jurisdiction	Denmark
Covered bond type	Legislation-enabled
Underlying assets	Commercial mortgage loans
Outstanding covered bonds (bil. SEK)	51.89
Year of first issuance	2010
Rating at closing	AAA
Extendible maturities	Yes
Target credit enhancement (%)	38.95
Available credit enhancement (%)	21.91

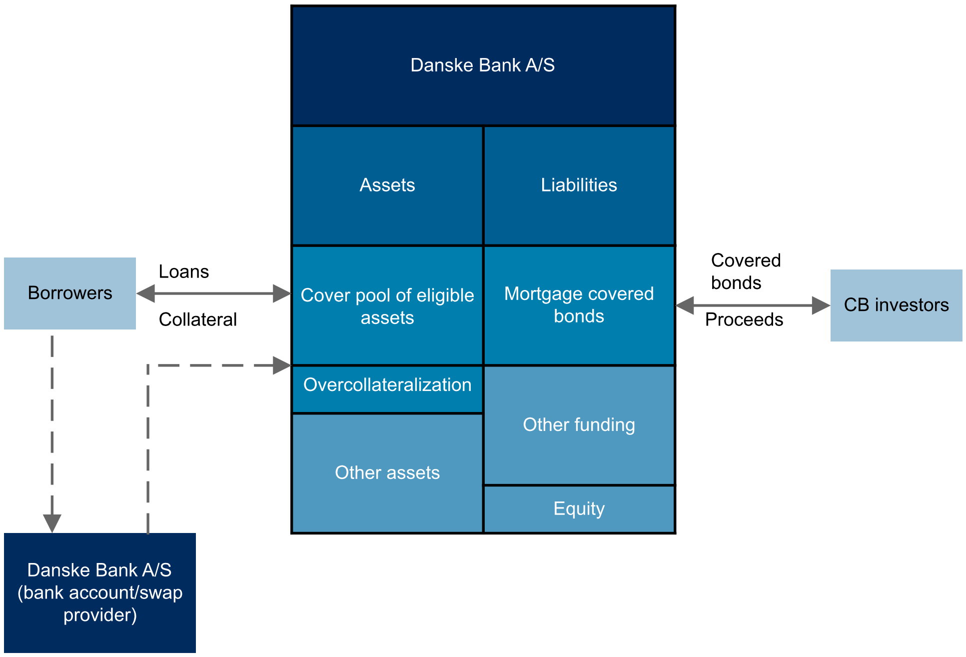
*Based on data as of Dec. 31, 2023. SEK--Swedish krona.

Table 2

Program 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
Interest rate hedge provider	Danske Bank A/S	A+/Stable/A-1	Y
Bank account provider	Danske Bank A/S	A+/Stable/A-1	N

Program structure



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 legislation to transpose the EU Covered Bond Directive into the Danish legal framework was passed in May 2021 and became effective on July 8, 2022. The amendments introduced a nominal statutory overcollateralization requirement of 2%. This does not include the cost of managing a cover pool that is winding down. It also introduced a formal requirement for coverage of 180 days of liquidity, which does not recognize previous maturity extension features. For Danish covered bonds without a maturity match (as is the case in Danske Bank C's cover pool), the administrator may extend the covered bonds' maturity.

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 issuer must maintain an overcollateralization of at least 2% of covered bonds outstanding on a nominal basis The issuer must cover 180 days liquidity for bonds issued before the introduction of the law.

If Danske Bank becomes insolvent, the covered bond holders have a preferential claim on the proceeds generated by the pool. Danish covered bonds do not automatically accelerate if the issuer becomes insolvent. 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, to repay the maturing covered bonds' principal.

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.

The amendments to the legal framework are relatively limited, in our view, and as the Danish legislation was already well aligned to the requirements of the directive, the new legislation does not affect our analysis of the Danish legal framework.

Operational and administrative risks

We analyze operational and administrative risk by applying our covered bonds framework, and consider Danske Bank's origination, underwriting, collection, and default management procedures for the cover pool assets. We also consider the cover pool management and administration.

Since our previous review, Danske Bank has sold its Norwegian retail and private banking operations, but it will maintain its commercial client operations. We understand Danske Bank remains committed to the remaining Norwegian business and do not expect any risks to arise from the sale.

Danske Bank actively manages the cover pool and underwriting and loan management policies are maintained centrally. We have not identified any operational or administrative risks that would affect our assessment of the program.

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

Resolution regime analysis

Denmark is part of the EU and has implemented the EU's BRRD.

Therefore, we consider the program's RRL is equal to 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.

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

Jurisdictional support analysis

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. We have assessed jurisdictional support for Danish mortgage covered bonds as very strong, under our covered bonds criteria, which 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 C mortgage covered bonds.

Collateral support analysis

Table 3

Cover pool composition*

	As of Sept. 30, 2023		As of Sept. 30, 2022	
Asset type	**Value (mil. SEK)**	**Percentage of cover pool (%)**	**Value (mil. SEK)**	**Percentage of cover pool (%)**
Residential	-	0	-	0
Commercial	62,620	100	63,188	100
Substitute assets	-	0	-	0
Other asset type	-	0	-	0
Total	62,620	100	63,188	100

*This is based on S&P Global Ratings' classification and therefore does not necessarily equal publicly available information (e.g., we classify multifamily homes as commercial).

Table 4a

Key credit metrics

	As of Sept. 30, 2023	As of Sept. 30, 2022
Weighted-average foreclosure frequency (%)	25.19	24.13
Weighted-average loss severity (%)	40.4	42.61

Table 4b

Key credit metrics: Norwegian assets

	As of Sept. 30, 2023	As of Sept. 30, 2022
Weighted-average loan-to-value ratio (%)	44.31	43.48
Balance of loans in arrears (%)	0	0
Credit analysis results		
Weighted-average foreclosure frequency (%)	25.83	25.06
Weighted-average loss severity (%)	41.41	41.01

Table 4c

Key credit metrics: Swedish assets

	As of Sept. 30, 2023	As of Sept. 30, 2022
Weighted-average loan-to-value ratio (%)	43.97	47.17
Balance of loans in arrears (%)	0	0
Credit analysis results		
Weighted-average foreclosure frequency (%)	24.79	23.99
Weighted-average loss severity (%)	39.76	42.84

Table 5a

Loan-to-value ratios: Norway

	Percentage of cover pool (%)	
(%)	As of Sept. 30, 2023	As of Sept. 30, 2022
0 to 60	92.03	93.41
60 to 70	6.16	4.65
70 to 80	0.52	0.08
80 to 90	0.01	1.86
90 to 100	1.28	0
More than 100	0	0
Weighted-average loan-to-value ratios	44.31	43.38

Table 5b

Loan-to-value ratios: Sweden

	Percentage of cover pool (%)	
(%)	As of Sept. 30, 2023	As of Sept. 30, 2022
0 to 60	87.29	76.82
60 to 70	11.55	17.82
70 to 80	1.16	3.86
80 to 90	0	0.92
90 to 100	0	0.27
Above 100	0	0.31
Weighted-average loan-to-value ratios	43.97	47.17

Table 6a

Geographic distribution of loan assets: Norway

	Percentage of cover pool (%)	
	As of Sept. 30, 2023	As of Sept. 30, 2022
East	57.69	54.78
West	17.53	17.23
Trondelag	18.47	19.96
North	6.19	7.26
South	0.12	0.77
Total	100	100

Table 6b

Geographic distribution of loan assets: Sweden

	Percentage of cover pool (%)	
	As of Sept. 30, 2023	As of Sept. 30, 2022
West Sweden	24.19	23.05
Stockholm	20.62	23.09
East Middle Sweden	23.06	22.49
South Sweden	13.37	12.47
Smaland and the islands	10.98	10.55
North Middle Sweden	5.62	5.84
Middle Norrland	1.39	1.43
Upper Norrland	0.77	1.08
Total	100	100

Table 7

Collateral uplift metrics

	As of Sept. 30, 2023	As of Sept. 30, 2022
Asset WAM (years)	2.17	1.84
Liability WAM (years)	4.95	3.01
Maturity gap (years)	(2.78)	(1.17)
Available credit enhancement	21.91	16.37
'AAA' credit risk	14.66	12.26
Credit enhancement for first notch of collateral uplift (%)	20.75	14.21
Credit enhancement for second notch of collateral uplift (%)	26.84	16.17
Credit enhancement for third notch of collateral uplift (%)	32.92	18.12
Target credit enhancement for maximum uplift (%)	39.01	20.07
Potential collateral-based uplift (notches)	0	1
Adjustment for liquidity (Y/N)	N	N
Adjustment for committed overcollateralization (Y/N)	Y	Y
Collateral support uplift (notches)	0	1

WAM--Weighted-average maturity.

We base our credit analysis on the loan-level data provided by the issuer as of Sept. 30, 2023. The cover pool comprises only commercial mortgage loans backed by Swedish (61.06%) and Norwegian (38.94%) assets. The percentage of Norwegian assets has increase since our previous review when such assets made up 12.7%. We analyze these pools under our commercial real estate criteria (see "Methodology And Assumptions: Analyzing European Commercial Real Estate Collateral In European Covered Bonds," published on March 31, 2015).

The pool's weighted-average foreclosure frequency (WAFF) is 25.19% (24.13% as of the September 2022 analysis). The pool's weighted-average loss severity (WALS) is 40.40% (42.61% as of the September 2022 analysis).

The WAFF has increased due to higher whole-loan (including loan parts outside the cover pool) loan-to-value (LTV) ratios above 80%. The WALS has decreased due to a lower weighted-average cover pool LTV ratio, and lower percentage of operational properties, which we consider to have comparably worse liquidity in the event of foreclosure.

We have performed the cash flow analysis as of December 2023, and calculated the target credit enhancement (TCE), which would allow the program to receive four notches of collateral-based uplift. The TCE is 38.95%, which exceeds the 20.07% TCE figure from our September 2022 analysis, due to lower excess spread and higher asset-liability mismatch.

Given the JRL of 'aaa' under our covered bonds criteria, coverage of the 'AAA' credit risk, at 14.66%, maintains the current 'AAA' rating. The available credit enhancement, which is 21.91% after applying a haircut to account for setoff risk.

We adjust the maximum collateral-based uplift depending on whether the issuer covers six months of liquidity and overcollateralization is committed. Due to the covered bonds' soft bullet maturities, we consider liquidity to be covered. The available credit enhancement is provided on a voluntary basis, which reduces the amount of collateral-based uplift by one notch.

Under our commercial real estate criteria, we apply the largest obligor test to address portfolio concentration risk. Our largest obligor test, currently at 6.08%, is lower than the aforementioned 'AAA' credit risk, meaning that it does not floor the overcollateralization requirements.

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. Borrowers make their payments via direct debit or bank transfer into the accounts held with the account bank provider. Danske Bank uses these accounts in its normal course of business. Cash collections are accessible at any time. There is no documented replacement mechanism in place, which would protect the covered bondholders from the bank account providers' credit deterioration. Therefore, in our cash flow analysis, we considered the risk that cover pool collections may be lost if they have not been reinvested in cover assets or used to pay the covered bonds.

We have stressed this risk in our analysis considering the issuer's quarterly overcollateralization reporting and assuming

that a weeks' worth of collections are lost.

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, and we consider the collateral posting framework as adequate.

The swap agreements contain a replacement trigger set at a RRL of 'a', which refers to the 'BBB+' ICR on the issuer. As the counterparty is related to the issuer, the counterparty criteria consider the trigger at the corresponding RRL. This translates to a replacement trigger of 'a', which combined with an adequate collateral framework, is supportive of a 'AAA' rating on the program.

Setoff risk. There is a risk that borrowers of certain loans included in the cover pool retain a residual right under the relevant local legislation to set off claims against the outstanding amount of their loans. To mitigate this risk, the issuer will include additional assets in the cover pool, up to a value that is equal to the setoff risk as calculated quarterly. We reduce the available overcollateralization due to setoff risk accordingly to 21.91%.

Sovereign risk

We assess country risk by applying our structured finance sovereign risk criteria (see "Incorporating Sovereign Risk In Rating Structured Finance Securities: Methodology And Assumptions," published on Jan. 30, 2019).

The assets are domiciled in Norway and Sweden (unsolicited), which are both rated 'AAA/Stable'. The issuer is domiciled in Denmark, which is also rated 'AAA/Stable' (unsolicited). Therefore, our rating on the program is not limited by the application of these criteria.

Environmental, social, and governance

Danske Bank's cover pool C's exposure to environmental and social considerations is in line with other Danish issuers we rate. Danske Bank's cover pool C issues SDOs backed by mainly commercial real estate in Norway and Sweden. SDO programs must ensure continuous LTV ratio compliance on an individual loan basis and not just at origination. If collateral values drop during the loan maturity, the issuer must pledge additional assets to the cover pool. Governance factors are a negative consideration in our ratings analysis of Danske Bank. Moreover, the issuer does not commit to maintain a minimum level of overcollateralization in the program that is commensurate with a 'AAA' rating, which reduces by one - unused notch of uplift. We consider liquidity coverage to be covered as all outstanding issues are soft-bullet bonds with a one-year maturity extension.

Related Criteria

- Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- Global Framework For Payment Structure And Cash Flow Analysis Of Structured Finance Securities, Dec. 22, 2020
- 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: Analyzing European Commercial Real Estate Collateral In European Covered Bonds, March 31, 2015
- Covered Bonds Criteria, Dec. 9, 2014
- Principles Of Credit Ratings, Feb. 16, 2011

Related Research

- Global Covered Bond Insights Q1 2024, Dec. 15, 2023

- Covered Bonds Outlook 2024: Stability Amid Turbulence, Dec. 11, 2023
- Danish Covered Bond Market Insights 2023, Nov. 30, 2023
- Danske Bank A/S, Aug. 2, 2023
- S&P Global Ratings Definitions, June 9, 2023
- Denmark, Feb. 13, 2023
- European Covered Bonds Reach Harmonization Milestone As The Journey Continues, July 12, 2022
- Glossary Of Covered Bond Terms, April 27, 2018