S&P Global Ratings

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

Saerligt Daekkede Obligationer

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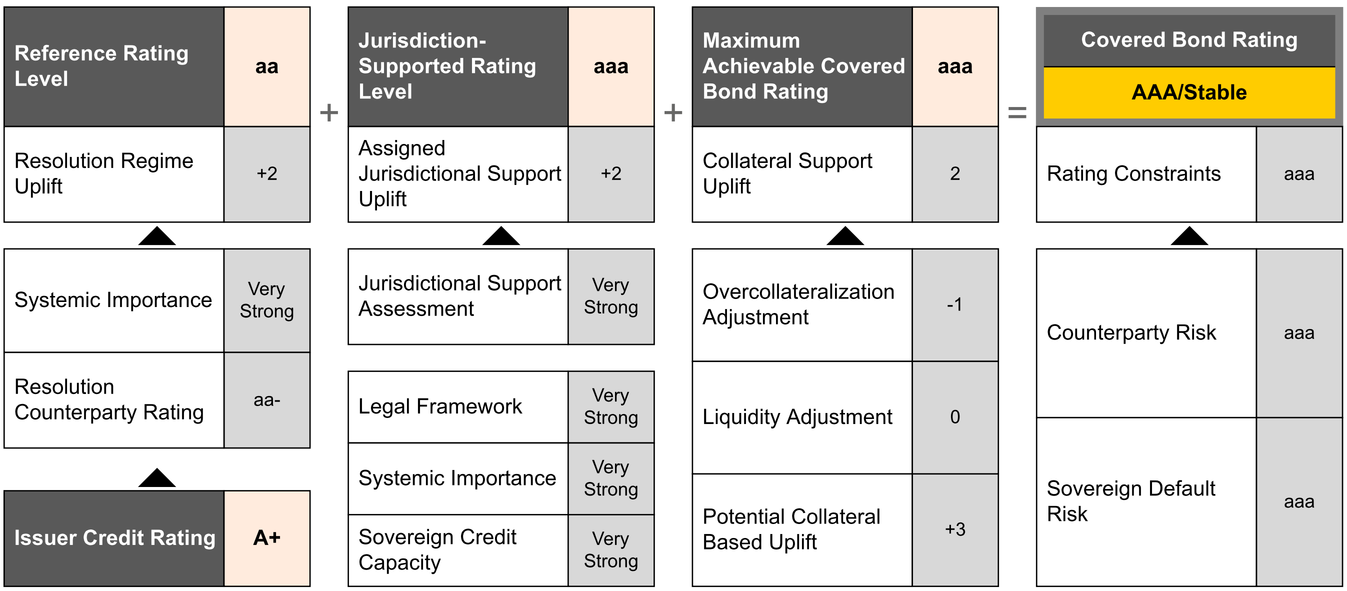
Ratings Detail



Major Rating Factors

Strengths

- The long-term issuer credit rating (ICR) allows for a 'AAA' rating to be reached with the jurisdictional support and the coverage of 'AAA' credit risk.
- Due to the covered bonds' soft-bullet maturities, we consider six months of liquidity covered.
- The program benefits from three unused notches of uplift, which would protect the rating if we lowered the ICR on Danske Bank A/S.

Weaknesses

- The available overcollateralization is voluntarily provided, reducing the number of potential collateral-based uplift by one notch.
- The cover pool includes about 21.1% of second-lien loans, which we consider have a higher risk than first-lien loans.

Outlook

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 if we were to lower our long-term ICR on Danske Bank by three notches. We would lower our ratings on the covered bonds if the credit enhancement needed to maintain the ratings were to exceed the available credit enhancement, all else being equal.

Rationale

We are publishing this transaction update following our review of Danske Bank's cover pool I's mortgage covered bond program and related issuances following the developments arising from the sale of Danske Bank's Norwegian personal banking portfolio to Nordea Bank Abp. As a result, the previous Norwegian pool was transferred to Nordea Bank Abp and replaced with Danish residential loans and a small percentage of substitute assets. Additionally, most of the outstanding Norwegian (NOK)-denominated covered bonds were transferred to Nordea Bank.

We have affirmed the 'AAA' ratings on the Danske Bank's cover pool I mortgage covered bond program and all related issuances (see "Danske Bank A/S Cover Pool I Mortgage Covered Bond ‘AAA’ Ratings Affirmed; Outlook Stable" published on Feb. 13, 2025).

Our covered bond ratings process follows the methodology and assumptions outlined in our "Covered Bonds Criteria," published on Dec. 9, 2014, and "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, or sovereign default risks.

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 a 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 the higher of (i) two notches above the long-term ICR; and (ii) the resolution counterparty rating (RCR). Given Danske Bank's RCR is 'AA-', the RRL is '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 to achieve a JRL of 'aaa'.

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 billion global covered bond program.

In July 2023, Danske Bank entered into an agreement with Nordea Bank to sell its Norwegian personal customer business and relocate resources for the expansion of its business customers, large corporate, and institutions segments in Norway. In November 2024, the transaction was completed, thereby affecting the cover pool I mortgage covered bond program.

Following the sale, all Norwegian mortgage loans, together with most of the outstanding NOK-denominated covered bonds, were transferred to Nordea Bank. The issuer transferred Danish mortgage loans to cover pool I to back the outstanding NOK- and euro-denominated covered bonds. The transaction features interest rate swaps and cross-currency swaps on both assets and liabilities.

The mortgage covered bonds are senior-secured unsubordinated obligations and rank pari passu with other obligations in the same cover pool register. 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	Residential mortgage loans
Outstanding covered bonds (Bil. DKK)	12.57
Rating at closing	'AAA'
Extendible maturities	Yes
Assigned jurisdictional support uplift	2
Unused notches for jurisdictional support	1
Target credit enhancement (%)	14.77
Available credit enhancement (%)	12.77
Collateral support uplift	2
Unused notches for collateral support	2

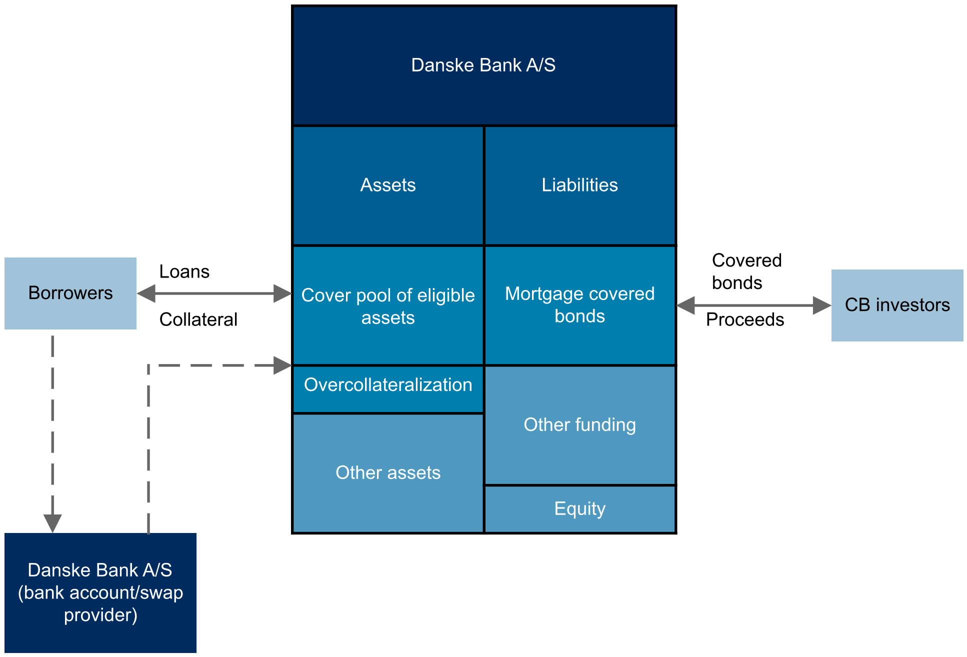
*Based on data as of Nov. 28, 2024. DKK--Danish krone.

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



Rating Analysis

Legal and regulatory risks

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 (DFSA, or "Finanstilsynet").

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.

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

Danske Bank's cover pool I covered bond investors have a primary secured claim against all assets in the cover pool.

The ratings on the covered bonds issued from cover pool I rely on the issuer's active management of the overcollateralization to support the current ratings.

To become eligible as collateral, mortgage loans must be entered in the Danish land register. The registration is legally binding and will form the basis of any bankruptcy proceedings. If bankruptcy proceedings have been initiated, a trustee appointed by the bankruptcy court will administer the cover pool assets. The trustee is ordered by law to meet all payment obligations as they fall due.

The issuer must maintain an overcollateralization of at least 2% of covered bonds outstanding on a nominal basis. Banking supervision is carried out by the DFSA. The DFSA has the authority to issue an order with which the issuer must comply. In case of severe or multiple breaches, the DFSA may revoke the license.

All Danish covered bonds that match the maturity of the mortgage may be extended in the instance of a failed refinancing. The issuer or administrator must attempt to refinance the extended bonds yearly. For covered bonds without a maturity match (as is the case in Danske Bank's cover pool I), the administrator may extend the maturities of the covered bonds.

The legislation to transpose the EU Covered Bond Directive in the Danish legal framework was passed in May 2021 and became effective on July 8, 2022. The amendments were essentially refinements and given that the Danish legislation was already well aligned to the requirements of the directive, the updated legislation did not affect our analysis of the Danish legal framework.

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 claw back. 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 claw back, in our view.

Operational and administrative risks

In June 2024, we reviewed Danske Bank's origination, underwriting, collection, and default management procedures for the cover pool assets, along with 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 cover pool manager would be available if the issuer were to become insolvent. We consider Denmark to be an established covered bond market and believe that the mortgage assets in the cover pool do not comprise product features that would materially limit the range of available replacement cover pool managers.

Resolution regime analysis

As part of our covered bonds criteria, our analysis considers the resolution regime in place in Denmark to determine the RRL. The RRL on the issuer, which is the starting point for any further uplift in our analysis, is 'aa' (two notches above the 'A+' ICR on Danske Bank). We consider the following factors:

- The issuer is domiciled in Denmark, which is subject to the EU's BRRD.
- Our very strong assessment of the systemic importance of Danish mortgage covered bonds, which allows for two notches of uplift from the ICR on Danske.

These factors recognize that resolution regimes like the BRRD increase the probability that an issuer could service its covered bonds even following a default on its senior unsecured obligations, because the law exempts covered bonds from bail-in. We consider this as an internal form of support because the bail-in of certain creditors does not require direct government support.

Jurisdictional support analysis

The JRL on Danske Bank's covered bonds is 'aaa'. Under our analysis of jurisdictional support in our covered bonds criteria, we determine a JRL--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 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. Under our covered bonds criteria, this means that the program can receive up to three notches of jurisdictional uplift from the RRL. Two notches are used to achieve a 'AAA' rating, resulting in one unused notch for jurisdictional support.

Collateral support analysis

We base our analysis on the loan-level data and asset and liability cash flow projections provided by the issuer as of Nov. 28, 2024. Following the transfer in November 2024, the cover pool comprises Danish residential mortgage loans and a small share of substitute assets (see table 3).

Table 3

Cover pool composition

	--As of Nov. 28, 2024--		--As of June 30, 2023--	
Asset type	**Value (Mil. DKK)**	**Percentage of cover pool**	**Value (Mil. NOK)**	**Percentage of cover pool**
Residential	13,904.3	98.1	145,001.4	99.1
Commercial	0.0	0.0	0.0	0.0
Substitute assets	265.0	1.9	1,256.9	0.9
Other asset type	0.0	0.0	0.0	0.0
Total	14,169.3	100.0	146,258.3	100.0

DKK--Danish Krone. NOK--Norwegian krone.

Table 4

Key credit metrics

	Danish assets as of Nov. 28, 2024	**Norwegian assets as of June 30, 2023**
Weighted-average effective LTV (%)*	60.7	63.6
Weighted-average current loan-to-value ratio (%)	60.7	56.6
Weighted-average seasoning (years)§	1.65	4.7
Second lien loans	21.13	21.96
Balance of loans in arrears (%)	0.0	0.1

Table 4

Key credit metrics (cont.)

	Danish assets as of Nov. 28, 2024	Norwegian assets as of June 30, 2023
Credit analysis results		
Weighted-average foreclosure frequency (%)	8.4	12.1
Weighted-average loss severity (%)	25.3	31.0

*The effective LTV ratio is the result of the application of our global RMBS criteria, which weight 100% of current indexed whole loan LTV ratio for the WAFF calculation. § Seasoning refers to the elapsed loan term.

Table 5

Loan-to-value ratios

	As of Nov. 28, 2024	As of June 30, 2023
(%)	Percentage of cover pool	Percentage of cover pool
0 to 60	49.6	56.0
60 to 70	16.83	18.5
70 to 80	26.98	14.64
80 to 90	3.97	7.9
90 to 100	1.41	1.51
More than 100	1.25	1.42
Weighted-average loan-to-value ratios	60.7	56.6

Table 6

Loan seasoning distribution*

	As of Nov. 28, 2024	As of June 30, 2023
	Percentage of cover pool	Percentage of cover pool
Less than 5 years	94.2	68.1
5-6	3.7	6.1
6-7	2.1	5.5
7-8	0.0	4.7
8-9	0.0	4.2
9-10	0.0	1.4
More than 10 years	0.0	10.0
Weighted-average loan seasoning (years)	1.7	4.7

*Seasoning refers to the elapsed loan term.

Table 7a

Geographic distribution of Danish assets

	Percentage of cover pool
	As of Nov. 28, 2024
Capital Region of Denmark	56.1
Central Denmark Region	14.7
North Denmark Region	5.4
Region Zealand	12.3
Region of Southern Denmark	11.5

Table 7a

Geographic distribution of Danish assets (cont.)	
	Percentage of cover pool
	As of Nov. 28, 2024
Total	100.0

Table 7b

Geographic distribution of Norwegian assets	
	Percentage of cover pool
	As of June 30, 2023
East	61.5
West	9.3
Trondelag	14
North	4.9
South	10.4
Total	100

Table 8

Collateral uplift metrics		
	As of Nov. 28, 2024	As of June 30, 2023
Asset WAM (years)	15.58	12.69
Liability WAM (years)	4.63	3.59
Maturity gap (years)	10.95	9.10
Available credit enhancement	12.77	10.51
AAA' credit risk	2.50	5.94
Credit enhancement for first notch of collateral uplift (%)	5.01	10.03
Credit enhancement for second notch of collateral uplift (%)	8.26	14.13
Credit enhancement for third notch of collateral uplift (%)	11.52	18.22
Credit enhancement for maximum uplift (%)	14.77	22.31
Potential collateral-based uplift (notches)	3	1
Adjustment for liquidity (Y/N)	N	N
Adjustment for committed overcollateralization (Y/N)	Y	Y
Collateral support uplift (notches)	2	0

WAM--Weighted-average maturity.

The residential mortgage assets contain about 7,909 Danish residential mortgage loans, with an average cover pool current loan-to-vale (LTV) ratio of 60.72% after house price indexation. The weighted-average seasoning is approximately 1.65 years. Most of the loans are on owner-occupied properties, with about 5% being for second homes.

For the residential mortgage loans in the pool, our analysis for each loan estimated the foreclosure frequency and the loss severity. The product of foreclosure frequency and loss severity calculates the potential loss associated with each loan. We have applied stresses that are commensurate with a 'AAA' rating scenario to estimate the level of defaults, expressed as the weighted-average foreclosure frequency (WAFF), and our loss estimate measure, the weighted-average loss severity (WALS). By multiplying these, we calculate the potential loss associated with the cover pool and the required loss protection, assuming all other factors remain unchanged.

Since our previous review, the collateral has changed completely from a Norwegian residential pool to a Danish residential pool.

WAFF decreased to 8.4% from 12.1% previously, mainly due to lower whole-loan current LTV ratios. This is driven by our updated house price overvaluation assessment in Denmark. We currently consider that residential house prices in Denmark are not overvalued, while Norwegian house prices were considered to be overvalued in our previous review (see "House Price Overvaluation Moderates For Europe's RMBS And Covered Bond Markets", Jan. 20, 2025). This positive factor is partially offset by the pool's lower seasoning and the higher share of interest-only loans.

WALS improved to 25.3% from 31.0%, mainly due to the lower repossession market value decline assumption driven by our updated house price overvaluation assessment in Denmark. Another driver for lower WALS is the lower share of loans with jumbo valuations. These positive factors are marginally offset by higher current LTV ratios.

Our credit analysis of the substitute assets (also referred to as the "reserve fund") includes an asset-by-asset review of underlying securities to estimate each individual exposure's credit risk. To determine the default and loss on the reserve fund, we apply our "Methodology And Assumptions For Assessing Portfolios Of International Public Sector And Other Debt Obligations Backing Covered Bonds And Structured Finance Securities," published on Dec. 9, 2014.

By applying our credit and cash flow stresses, we calculate a target credit enhancement (TCE), which would allow the program to receive potentially four notches of collateral-based uplift. The TCE calculated on November 2024 data is 14.77%, lower than the 22.31% previously. This is mainly due to a higher excess spread, a lower credit coverage, and our higher prepayment assumption on Danish residential loans compared with Norwegian residential loans previously, which is partially offset by an increase in asset-liability maturity mismatch.

Our global RMBS criteria identifies basis risk in relation to standard variable rate (SVR) mortgage loans, given that the lender may change the SVR at any time and for various reasons (for example, changes in the cost of funding or to retain borrowers). As the current SVR rates in Danske Bank's cover pool I reflect a competitive environment, we have not applied a haircut to these SVR rates in our analysis, as we do not expect margins to compress. However, we may apply a stress in the future if the SVR dynamics were to change.

Given the JRL of 'aaa', under our covered bonds criteria, only coverage of the 'AAA' credit risk at 2.50% (compared to 5.94% previously), is required to maintain the current 'AAA' rating. The available credit enhancement, which is 12.77%, is sufficient to cover this requirement. As the available credit enhancement exceeds the third notch of collateral-based uplift, the potential collateral-based uplift above the JRL is three notches. We reduce this by one notch because there is no commitment to maintain overcollateralization at the current rating level. Given that the covered bonds are soft-bullet with a one-year extension period, we do not lower the potential uplift to reflect liquidity risk. As the program only requires to cover 'AAA' credit risk to achieve a 'AAA' rating, this results in two unused notches of collateral-based uplift, which would protect the ratings on the covered bonds if we were to lower the ICR on Danske Bank A/S.

Counterparty risk

We have identified several counterparty risks to which the covered bonds are exposed. However, these are either structurally addressed in line with our current counterparty criteria or considered in our cash flow modeling (see "Counterparty Risk Framework: Methodology And Assumptions," published on March 8, 2019). Therefore, we believe that they do not constrain the ratings from a counterparty risk perspective.

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. No documented replacement mechanism exists to 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 just before issuer insolvency if they have not been reinvested in cover assets or used to pay the covered bonds. Post–insolvency, proceeds from the borrowers are identified and promptly segregated for the benefit of the bondholder.

We have stressed this risk in our analysis by sizing a small amount considering the issuer's weekly overcollateralization reporting.

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. To derive the maximum potential rating on the covered bonds under our counterparty criteria, we consider various factors, including whether the counterparties are related to the issuer, the seniority of termination payments, the replacement commitment, and the collateral posting framework.

Danske Bank is a related swap counterparty, derivative termination costs are not subordinated to payments due to covered bondholders. Because Danske Bank is a related counterparty, we consider the RRL ('aa') as the applicable counterparty rating when assessing counterparty risk. According to the swap documentation, Danske Bank has committed to post collateral and to replace itself within 90 calendar days if its RRL falls below 'a'. We categorize the current collateral-posting framework in the derivative contracts as adequate.

The collateral framework assessment, combined with the current 'aa' RRL on the issuer and the replacement trigger, supports a maximum potential rating of 'AAA' under our counterparty risk assessment.

Derivative risk does not limit the current three unused notches of uplift.

Setoff 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 setoff claims against the outstanding amount of their loans. We understand from the issuer that all borrowers have contractually agreed that they have no right to set off against the relevant loans.

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). Given Denmark's 'AAA' rating (unsolicited), sovereign risk does not constrain the ratings on the covered bonds.

Environmental, Social, And Governance

We view Danske Bank's cover pool I's exposure to environmental and social factors in line with other Danish issuers, while we view governance considerations as moderately negative in our credit rating analysis. In its cover pool I, Danske Bank issues the covered bonds under the Danish SDO framework backed solely by Danish residential properties. SDO programs must ensure continuous LTV compliance on an individual loan basis and not just at origination, meaning that if collateral values drop the issuer must pledge additional assets to the cover pool. Governance factors are now a neutral consideration in our ICR analysis of Danske Bank. However, 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 the unused notches of uplift.

We consider liquidity coverage to be addressed as all outstanding issues are soft-bullet bonds with a one-year maturity extension.

Related Criteria

- Global Methodology And Assumptions: Assessing Pools Of Residential Loans--Europe Supplement, April 4, 2024
- 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
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Related Research

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- Global Covered Bond Insights Q1 2025, Dec. 18, 2024
- Danish Covered Bond Market Insights 2024, Dec. 18, 2024
- Update: Danske Bank A/S, Oct. 10, 2024
- Denmark, Aug. 12, 2024

- The Danish Covered Bond Legal Framework: A Closer Look, June 5, 2024
- Covered Bonds Outlook Midyear 2023: Rising Interest Rates Will Test Asset Performance, July 19, 2023
- S&P Global Ratings Definitions, June 9, 2023
- European Covered Bonds Reach Harmonization Milestone As The Journey Continues, July 12, 2022
- Glossary Of Covered Bond Terms, April 27, 2018
- Credit FAQ: The Danish Covered Bond Market Explained, July 15, 2014