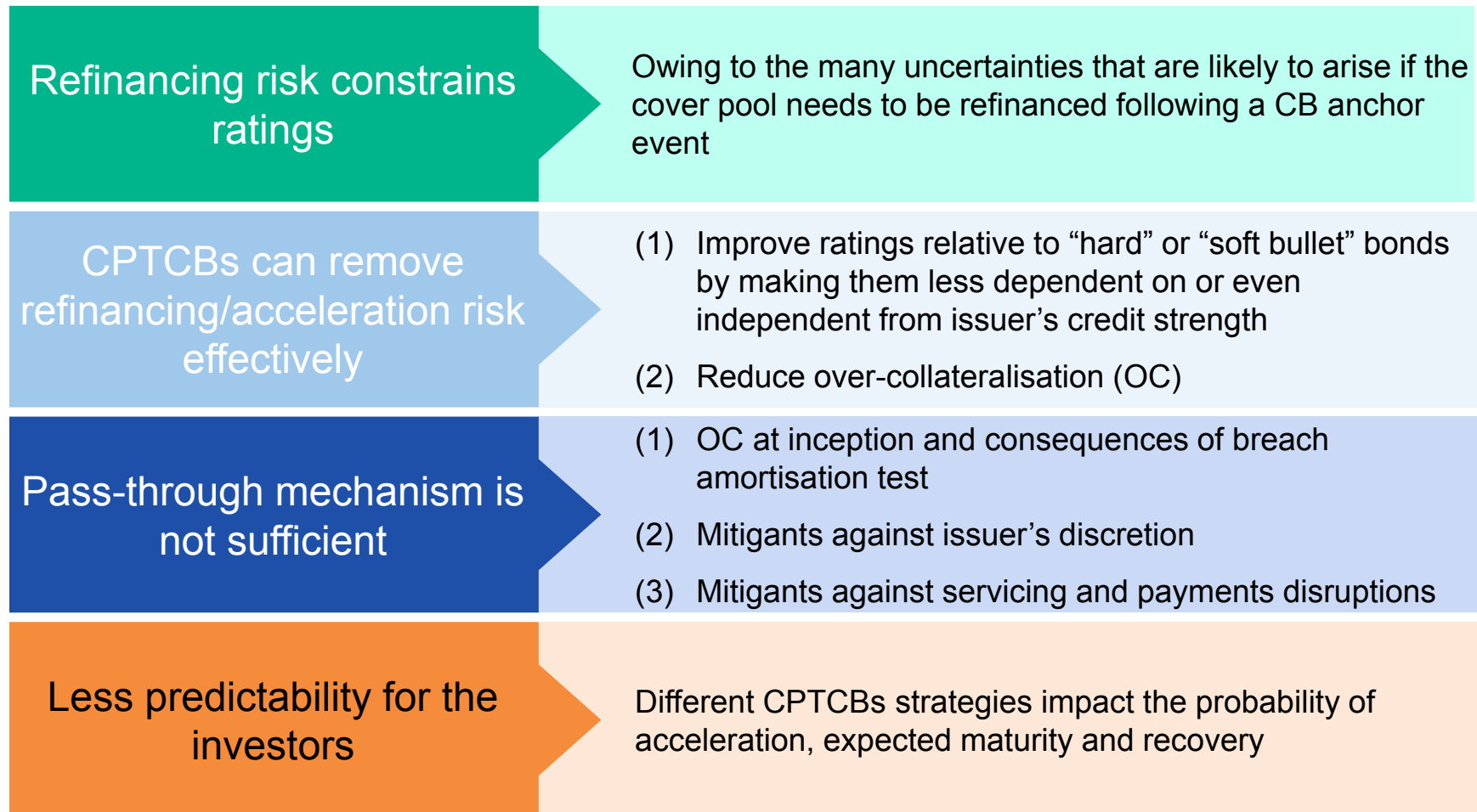




Conditional Pass-Through Covered Bonds

A Ratings View

Conditional Pass-through CBs (CPTCBs) can get Full De-linkage from Issuer's Rating

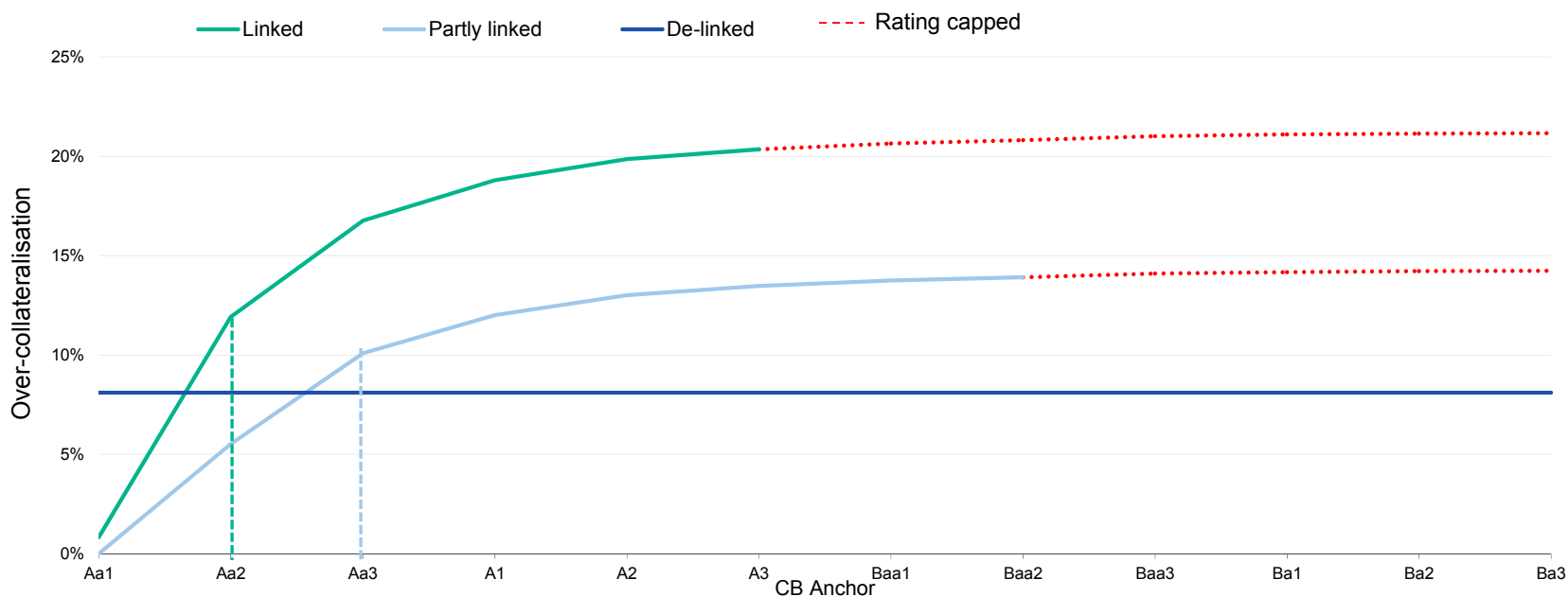


CPTCBs can Reduce OC and Improve Ratings

» Expected Loss = PD x LGD ↓ → ↓ OC required to achieve the same rating as with traditional CBs since market risk reduces

Collateral Risk ↓
Market Risk ↓

» Simplified example → Target rating: Aaa, collateral risk 7.5%, market risk 10%,
 Linked (TPI= "Probable"/ CP losses: 17.5%), Partly linked (TPI= "Very High"/ CP losses: 12.5%), De-linked (CP losses: 7.5%)

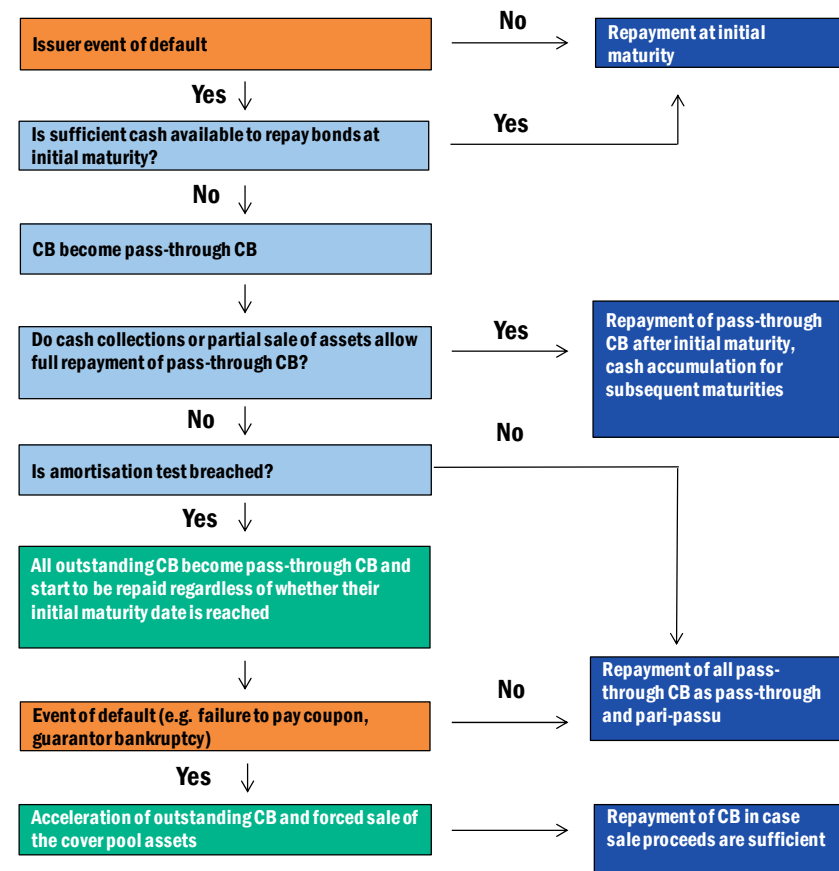


Source: Moody's Investors Service

Different Structures Impact Refinancing Risk Mitigation and Time Subordination

- » **Level of OC at deal inception:** is cover pool under-collateralised if losses crystallise?
- » **Consequences of breaching the minimum OC level (amortisation test):**
 - the breach of certain tests may lead to an event of default under the notes, thus fire-sale. Against → shorter extension.
 - the breach of the amortisation test could lead to all series becoming pass-through. Against → longer extension
- » **Issuer's discretion:** change in pool composition or liabilities' structure. Mitigants, e.g.:
 - Tight eligibility criteria
 - Rating confirmation on issuance of new series
- » **Servicing and cashflow disruption and counterparty risks:**
 - Liquidity reserve
 - Back-up servicing provisions by law or contract

Example payment-mechanism scheme: breach of amortisation test leads to all series becoming CPTCBs

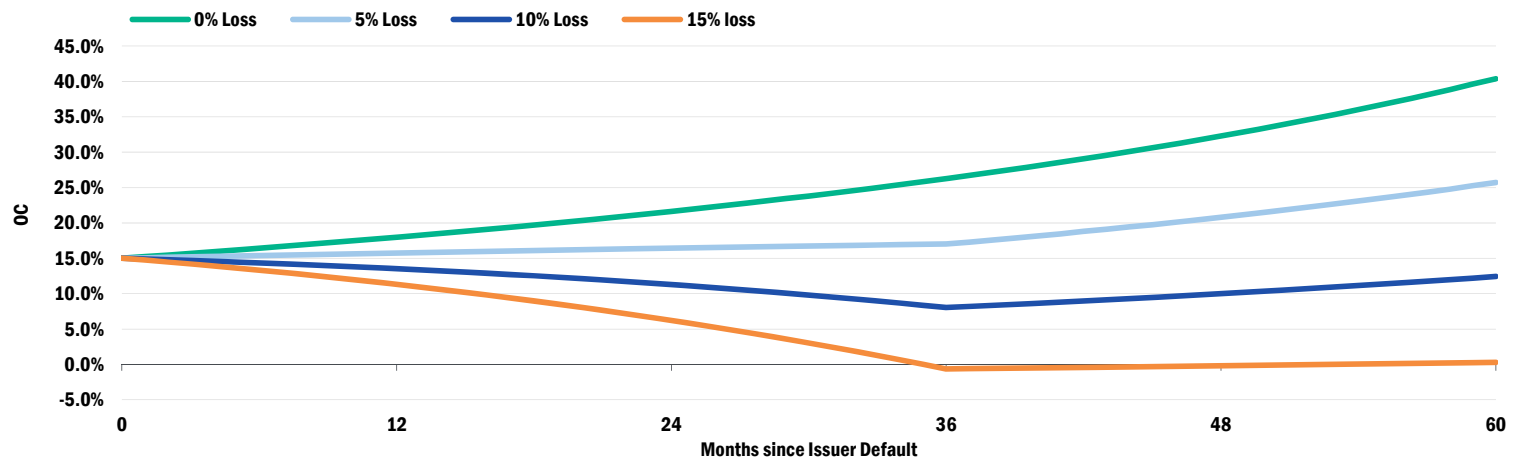


Source: Moody's Investors Service

Less Predictability of Redemption Timing vs. Lower Acceleration and Higher Recovery

- » Different CPTCBs strategies impact the probability of acceleration and recovery expectations.

Example: OC evolution on CPTCBs diverges under different loss-rate scenarios



Example of outcomes of different CPTCBs strategies relative to hard and soft-bullet bonds

	Hard-bullet	Soft-bullet (12 months)	CPTCBs: Amortisation test OC levels		
			10%	5%	0%
Probability of acceleration	100%	100%	9.7%	3.4%	1.4%
Recovery Rate	75.2%	81.2%	98.2%	99.3%	99.7%
Notes expected average life (yrs.) upon issuer event of default	0	1	4.9	5.2	5.2

Source: Moody's Investors Service

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