

# FITCH AFFIRMS SANTANDER'S MORTGAGE COVERED BONDS AT 'AA'

Fitch Ratings-Madrid-28 September 2018: Fitch Ratings has affirmed Banco Santander S.A.'s (Santander, A-/Stable/F2) mortgage covered bonds (Cedulas Hipotecarias or CH) at 'AA' with Stable Outlook upon the completion of the merger through absorption of Banco Popular Espanol, S.A.U. and Banco Pastor, S.A.U. (together Grupo Popular) on 28 September 2018. The 'AA' rating of Santander's CH has been assigned to the CH being transferred from Grupo Popular.

The Stable Outlook on Santander's CH reflects that on the bank's Long-Term Issuer Default Rating (IDR).

## KEY RATING DRIVERS

### Merger by Absorption

As a consequence of the merger all assets and liabilities of Grupo Popular have been absorbed by Santander. The merger leads to a consolidated mortgage cover pool of approximately EUR84.9 billion providing security to outstanding CHs of EUR35.8 billion as of 28 September 2018. These post-merger figures are supported by separate cover pool data files for Banco Santander and Grupo Popular and express a total over-collateralisation (OC) ratio of 135.3% as of end-June 2018.

The merged cover pool comprises approximately 65.3% residential mortgages, 26.4% commercial mortgages to SME borrowers and 8.3% to real estate developers. The weighted average seasoning of the cover pool is 7.3 years and its remaining term to maturity 15.5 years. The post-merger official cover pool data tape will be delivered by Santander during the next few months, and therefore the above cover pool statistics are preliminary and subject to change.

### IDR and Recovery Uplift

The 'AA' rating of Santander's CH inclusive of those transferred from Grupo Popular is based on Santander's 'A-' Long-Term IDR, an IDR uplift of two notches and a recovery uplift of two notches. Spanish covered bonds are eligible for a maximum IDR uplift of two notches given their bail-in exemption in a resolution scenario, Fitch's assessment that resolution of the issuer will not result in the direct enforcement of recourse against the cover pool and a low risk of under-collateralisation at the point of resolution.

The level of OC of 122% relied upon by Fitch, provides more protection than the agency's unchanged 'AA' breakeven OC of 36%. The agency will review Santander's CH's breakeven OC once official post-merger cover pool tape is available. Fitch expects this ratio to remain broadly stable, given the cover pool composition and granularity.

### Relied-Upon OC

Given the merger, and in accordance with Fitch Covered Bonds Rating Criteria, the 12-month look-back period to establish the level of OC that can be relied upon starts in June 2018. The relied-upon OC is derived after applying a 10% OC haircut to the total OC ratio as per the agency's criteria for Spanish issuers with a 'F2' Short-Term IDR.

### Payment Continuity Uplift (PCU)

The unchanged PCU of zero notches reflects the lack of liquidity protection mechanisms to bridge payments to CHs in the event of recourse to the cover pool. This is common for all CHs rated by Fitch as they have hard bullet maturities while the cover assets gradually amortise.

## RATING SENSITIVITIES

The 'AA' rating of Santander's CH is vulnerable to a downgrade if the bank's Long-Term IDR is downgraded by one or more notches, or if the OC that Fitch considers in its analysis decreases below Fitch's 'AA' breakeven level of 36%. If the OC declines to the 25% legal minimum, the CH rating would be downgraded by one notch to 'AA-'.

Contact:

Primary Analyst

Beatriz Gomez

Associate Director

+34 91 702 57 75

Fitch Ratings Espana S.A.U.

Plaza de Colon 2, Torre II, planta 5

Madrid, 28046

Secondary Analyst

Ricardo Garcia

Associate Director

+34 91 702 57 72

Committee Chairperson

Juan David Garcia

Senior Director

+34 91 702 57 74

Media Relations: Athos Larkou, London, Tel: +44 20 3530 1549, Email:  
athos.larkou@fitchratings.com.

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

Applicable Criteria

CLOs and Corporate CDOs Rating Criteria (pub. 19 Jul 2018)

<https://www.fitchratings.com/site/re/10038306>

Covered Bonds Rating Criteria - Effective from 13 August 2018 to 8 October 2018 (pub. 13 Aug 2018)

<https://www.fitchratings.com/site/re/10040601>

European RMBS Rating Criteria - Effective from 11 May 2018 to 5 October 2018 (pub. 11 May 2018)

<https://www.fitchratings.com/site/re/10030134>

Multi-Issuer Cedulas Hipotecarias Rating Criteria (pub. 13 Mar 2018)

<https://www.fitchratings.com/site/re/10022868>

SME Balance Sheet Securitisation Rating Criteria (pub. 23 Feb 2018)

<https://www.fitchratings.com/site/re/10020825>

Structured Finance and Covered Bonds Counterparty Rating Criteria (pub. 01 Aug 2018)

<https://www.fitchratings.com/site/re/10039504>

Structured Finance and Covered Bonds Country Risk Rating Criteria (pub. 18 Sep 2017)

<https://www.fitchratings.com/site/re/903496>

Structured Finance and Covered Bonds Interest Rate Stresses Rating Criteria (pub. 02 Feb 2018)

<https://www.fitchratings.com/site/re/10018549>

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