MOODY'S
INVESTORS SERVICE

Announcement: Moody's: Increased uplift for Swiss covered bond programmes increases their rating robustness

13 Sep 2021

London, 13 September 2021 -- Moody's Investors Service ("Moody's") has published an updated methodology for rating covered bonds (CB). In the update, Moody's introduced criteria for applying a new notching uplift to the issuer's Counterparty Risk (CR) Assessment when determining the CB Anchor for covered bonds. The CR Assessment reflects an issuer's ability to avoid defaulting on certain senior bank operating obligations and contractual commitments.

We may apply the new uplift, which typically ranges from one to three notches, when the issuer's CR Assessment does not fully reflect the reduced probability of default on covered bonds due to a potential bail-in of junior deposits. These criteria are relevant to Swiss covered bonds because we determine CR Assessments for Swiss banks on the assumption that junior deposits rank above all obligations covered by CR Assessments.

Applying the new criteria, we have identified three covered bond programmes that benefit from the new notching uplift to account for the bail-in of junior deposits. These programmes are:

- Valiant Bank AG -- Mortgage Covered Bonds ("Valiant")

- Pfandbriefbank Schweizer Hypothekarinstitute -- Mortgage Covered Bonds ("PBH")

- Pfandbriefzentrale der schweizerischen Kantonalbanken -- Mortgage Covered Bonds ("PBZ")

At this time, the update has no rating impact as the affected covered bonds are all rated Aaa. However, the new notching uplift increases the CB Anchor, which is a key determinant of a covered bond programme's rating robustness. The higher CB Anchor reduces the overcollateralization required to be consistent with the Aaa covered bond ratings and increases the TPI Leeway of the programmes. The TPI Leeway indicates the covered bond programme's rating robustness as it measures the number of notches by which Moody's might lower the CB Anchor before the rating agency downgrades the covered bonds because of TPI framework constraints.

The methodology implements the approach proposed in a Request for Comment (RFC) called "Moody's Approach to Rating Covered Bonds: Proposed Methodology Update" dated June 9, 2021, which can be accessed via this link: https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBS_1284762 .

INCREASED CB ANCHOR

The CB Anchor for Valiant's programme increases to Aa3. We derive the CB Anchor for this programme by applying an uplift of three notches to the CR Assessment of A3(cr). The uplift was zero notches prior to the methodology update. This new uplift is attributable to the potential benefit to covered bondholders resulting from a bail-in of junior deposits to recapitalize Valiant, which is not reflected in Valiant's CR Assessment.

The CB Anchors for both Swiss Pfandbrief programmes are not disclosed as the issuer's CR Assessments are not disclosed. We derive the CB anchor for these programmes by applying an uplift of two notches (prior to the methodology update: one notch) to the issuers' CR Assessments. One notch of this uplift is attributable to the potential benefit to covered bondholders resulting from a bail-in of junior deposits at the member bank level. We continue to apply an additional notch of uplift as the Pfandbrief setup is structured to ensure continuity of payments with authorities likely to take measures specifically aimed at supporting Pfandbriefe in the event of a member bank resolution.

REDUCED OVER-COLLATERALISATION (OC) REQUIREMENT

For Valiant, the OC consistent with the Aaa ratings reduces to 3.0% from 11.5%. Moody's does not give value to 'uncommitted' OC in its analysis. Valiant commits to an OC level of 3.0% (see the programme's credit opinion for further details on the OC modalities).

For the Swiss Pfandbriefe, the OC consistent with the Aaa ratings is unchanged at 0%. Moody's does give value to 'uncommitted' OC in its analysis. At a member bank level, PBH commits 8.0% and PBZ commits 15.0% OC for its Pfandbriefe.

INCREASED TPI LEEWAY

Moody's assigns a "timely payment indicator" (TPI), which is our assessment of the likelihood of timely payment of interest and principal to covered bondholders following a CB Anchor event. TPIs are assessed as Very High, High, Probable-High, Probable, Improbable or Very Improbable. The TPI framework limits the covered bond rating to a certain number of notches above the CB Anchor.

The TPI for Valiant's programme and the Swiss Pfandbriefe is Probable. The TPI Leeway for Valiant's programme is three notches, which means that Moody's might downgrade the covered bonds of Valiant because of a TPI cap if it lowers the CB Anchor by at least four notches. Prior to the methodology update, the TPI Leeway for Valiant was zero notches. The TPI Leeway for the Swiss Pfandbrief programmes is not disclosed.

TWO PROGARMMES WITH UNCHANGED CB ANCHORS

For the following two Swiss covered bond programmes, applying the new criteria has not resulted in changes to the CB Anchor because the benefit of bail-in in bank resolution scenarios has already been incorporated sufficiently in the issuers' CR-Assessments:

UBS AG - Mortgage Covered Bonds, rated Aaa, four-notch TPI Leeway (unchanged)

Credit Suisse AG - Mortgage Covered Bonds, rated Aaa, two-notch TPI Leeway (unchanged)

For further details, please refer to the Performance Overview reports of these programmes.

This press release is not intended to provide a summary of the methodology. For a full explanation of the methodology, please consult the updated report called "Moody's Approach to Rating Covered Bonds," now available on www.moodys.com and accessible at:
http://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBS_1284753 .

This publication does not announce a credit rating action. For any credit ratings referenced in this publication, please see the ratings tab on the issuer/entity page on www.moodys.com for the most updated credit rating action information and rating history.

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