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Transaction Update: BNP Paribas Fortis SA/NV (Mortgage Covered Bonds)

€10 Billion Belgian Pandbrieven Covered Bond Program

Primary Credit Analyst:
Tristan Gueranger, London (44) 20-7176-3628; tristan.gueranger@spglobal.com

Secondary Contact:
Alejandro Marcilla, Madrid +34 91 389 69 44; alejandro.marcilla@spglobal.com

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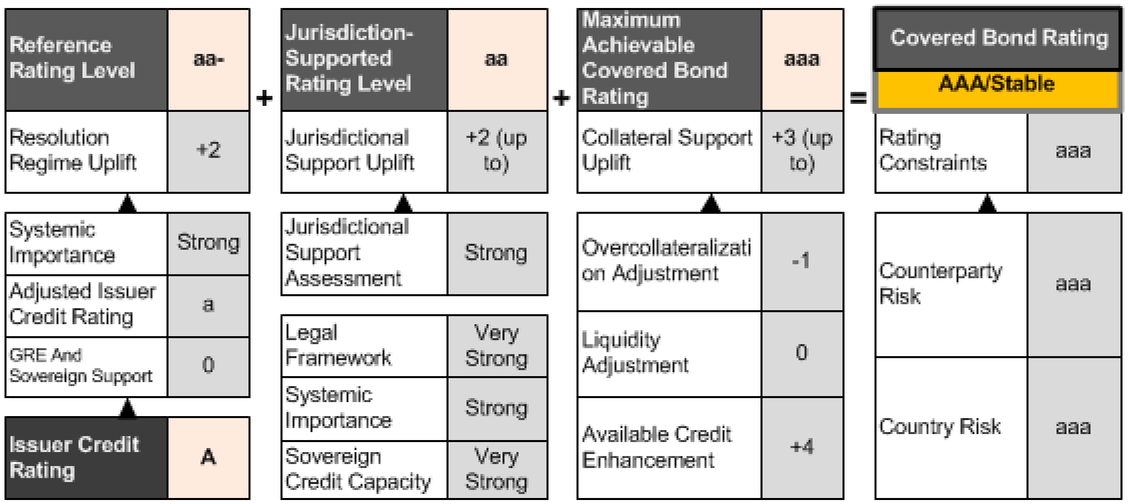
Ratings Detail



Major Rating Factors

Strengths

- The cover pool comprises prime Belgian residential mortgage loans.
- Available credit enhancement exceeds the credit enhancement required for the current rating level.
- Following the issuance of the series 2 covered bonds and the addition of new loans to the cover pool, credit and cash flow results show a generally positive trend.
- There is one unused notch of uplift incorporated in our jurisdiction-supported rating level (JRL) and another resulting from our analysis of the collateral-based uplift.

Weaknesses

- There is no commitment to maintain the current overcollateralization level beyond the legal requirement.
- Since we view commingling risk as not mitigated in our analysis, we incorporate it into our cash flow results.

Outlook: Stable

S&P Global Ratings' stable outlook on its 'AAA' credit ratings on the covered bonds (mortgage pandbrieven) issued by Belgium-based BNP Paribas Fortis SA/NV (BNPP Fortis) reflects our view that adverse developments relating to the issuer, cover pool, or other factors would not automatically lead to a rating action on the covered bonds.

The main reason for this is the two unused notches of uplift for the ratings, one for the JRL and another resulting from our analysis of the collateral-based uplift (see "Covered Bonds Criteria," published on Dec. 9, 2014). These provide a buffer if we were to lower our long-term issuer credit rating (ICR) on BNPP Fortis (A/Stable/A-1). Such downgrade would not automatically affect our ratings on the covered bonds.

Rationale

This transaction update follows our periodic review of BNPP Fortis' mortgage covered bond program. On March 24, 2017, following a second issuance out of the program, we affirmed our 'AAA' ratings on the program and related issuances (see "BNP Paribas Fortis Mortgage Covered Bonds 'AAA' Ratings Affirmed Following New Criteria Application; Outlook Stable").

Our covered bond ratings process follows the methodology and assumptions outlined in our covered bonds criteria and our "Covered Bond Ratings Framework: Methodology And Assumptions," published on June 30, 2015.

We consider that the provisions in the transaction documents, together with the Belgian legal and regulatory framework to effectively isolate the cover pool assets for the benefit of the covered bondholders. This asset isolation allows us to assign a higher rating to the covered bonds than our long-term ICR on the issuer.

BNPP Fortis is based in Belgium, a jurisdiction which applies the EU's Bank Recovery and Resolution Directive (BRRD). In addition, we consider that mortgage covered bonds have a strong systemic importance in Belgium.

These factors increase the likelihood that BNPP Fortis 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 reference rating level (RRL) as 'aa-', two notches above the adjusted ICR of 'a' on the issuer.

We also consider the likelihood for the provision of jurisdictional support. Based on a strong jurisdictional support assessment for mortgage programs in Belgium, we assign up to two notches of uplift from the RRL, capped at the level of the sovereign rating on Belgium (AA/Stable/A-1+, unsolicited). Therefore, we assess the JRL as 'aa'.

Based on our cash flow analysis as of March 11, 2017, the available credit enhancement of 33.1% exceeds both the 13.5% target credit enhancement and the 12.9% required for a 'AAA' rating.

There are no rating constraints to the 'AAA' ratings relating to legal, administrative, operational, country, or counterparty risks.

We have based our analysis on the criteria articles referenced in the "Related Criteria" section.

Program Description

BNPP Fortis is the largest bank in Belgium as measured by deposits. It offers a full range of financial services to private and corporate clients, wealthy individuals, companies, public, and financial institutions. French-based BNP Paribas owns 99.93% of BNPP Fortis, which we consider to be a "core" subsidiary. BNPP Fortis' ratings and outlook (A/Stable/A-1) are aligned with those of its parent.

The pool of residential mortgage loans securing the covered bonds was originated by BNP Fortis or its predecessor.

Mortgage pandbrieven are Belgian legislation-enabled covered bonds monitored by an independent trustee, the covered bond monitor. They constitute unsubordinated senior unsecured obligations and rank pari passu among themselves. BNPP Fortis was authorized in February 2016 by the domestic regulator, National Bank of Belgium (NBB), to issue covered bonds out of its program.

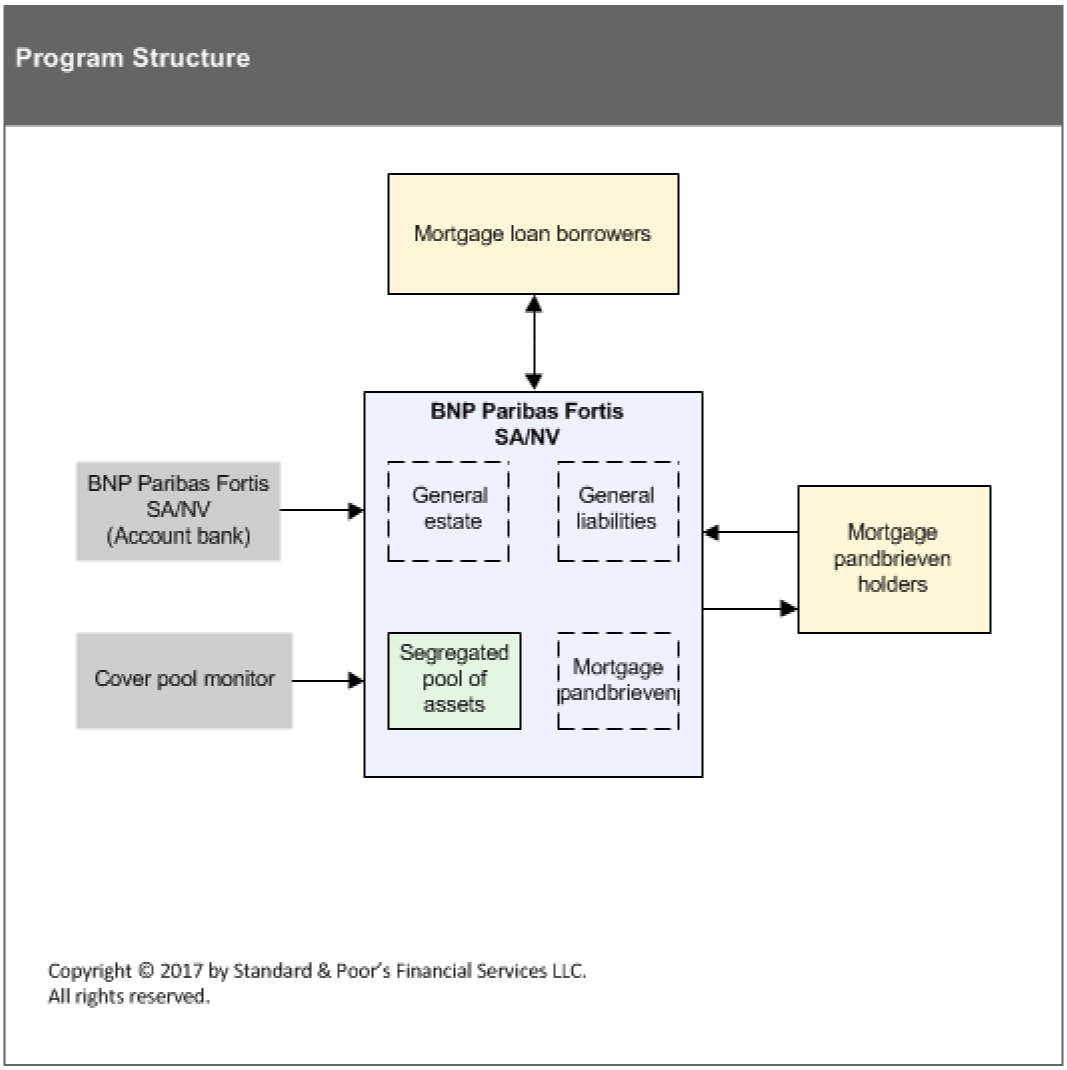


Table 1

Program Overview*	
Jurisdiction	Belgium
Year of first issuance	2016
Covered bond type	Legislation-enabled
Outstanding covered bonds (bil. €)	1

Table 1

Program Overview* (cont.)	
Redemption profile	Soft-bullet
Underlying assets	Residential mortgages
Assigned jurisdictional support uplift (notches)	1
Unused notches for jurisdictional support	1
Target credit enhancement (%)	13.51
Credit enhancement commensurate with rating (%)§	12.86
Available credit enhancement (%)	33.07
Collateral support uplift	3
Unused notch for collateral support	1
Total unused notches	2

*Based on data as of March 11, 2017. §Level of credit enhancement corresponding to 'AAA' credit risk and 75% of refinancing costs.

Table 2

Program Participants

Role	Name	Rating	Rating dependency
Issuer	BNP Paribas Fortis SA/NV	A/Stable/A-1	Yes
Arranger	BNP Paribas Fortis SA/NV	A/Stable/A-1	No
Arranger	BNP Paribas	A/Stable/A-1	No
Originator	BNP Paribas Fortis SA/NV	A/Stable/A-1	No
Servicer	BNP Paribas Fortis SA/NV	A/Stable/A-1	No
Bank account provider	BNP Paribas Fortis SA/NV	A/Stable/A-1	No

Rating Analysis

Legal and regulatory risks

The regulatory regime governing Belgian covered bonds was adopted by Parliament on Aug. 3, 2012 and was completed by Royal Decrees published on Oct. 11, 2012 and various subsequent regulations. Covered bond issuers are regulated by the NBB and programs are subject to the supervision of a cover pool monitor appointed by the issuer and approved by the NBB.

Similar to German Pfandbriefe, covered bonds in Belgium typically remain on the balance sheet of the issuer. Under Belgian legislation, the pandbrieven holders benefit from a ringfenced estate called the special estate. Issuing credit institutions must maintain a "register of cover assets" recording all cover pool assets backing the covered bonds. The special estate comprises those cover pool assets, any collateral posting received from swap counterparties, guarantees or privileges granted in connection with the cover pool assets, and cash held by the issuing bank for the special estate.

The cover pool assets in the special estate are available to meet the obligations under the covered bonds and are excluded from the issuer's bankruptcy estate. If the issuer becomes insolvent, pandbrieven holders have dual recourse to cover pool assets constituting the segregated estate and to the issuer's general estate (in respect of which they are treated as the issuer's unsecured creditors).

Other key features of the Belgian covered bond framework are a minimum overcollateralization level of 5%, the requirement to maintain a level of assets generating sufficient liquidity over a period of six months, and an encumbrance level resulting from the cover pool assets that does not exceed 8% of the bank's assets.

In our view, Belgium's legal framework for covered bonds sufficiently addresses the legal aspects outlined in our covered bonds criteria, enabling us to rate the covered bonds higher than the issuer.

We base our analysis of legal risk on our criteria "Europe Asset Isolation And Special-Purpose Entity Criteria--Structured Finance," published on Sept. 13, 2013, and other criteria articles listed in our covered bonds rating framework.

Resolution regime analysis

The program has no structural features to fully mitigate asset-liability mismatch. The ratings on the covered bonds are therefore linked to the issuer's RRL, under our covered bonds criteria.

The BRRD was transposed into Belgian law by a Royal Decree published on March 3, 2015. We assess the systemic importance for mortgage programs in Belgium as strong (see "Assessments For Jurisdictional Support According To Our Covered Bonds Criteria," published on July 20, 2016). Under our covered bonds criteria, this means that the RRL can be two notches above the adjusted long-term ICR (which adjusts the ICR by removing the uplift allocated to reflect extraordinary government support to the issuer). This uplift recognizes 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 in the event of bank resolution. We consider this as an internal form of support, because the bail-in of certain creditors of the issuer does not require direct support from the government.

The long-term ICR of 'A' on BNPP Fortis does not incorporate any notch of uplift for government support. Applying our covered bonds criteria, the adjusted ICR of 'a' is the same as the long-term ICR. The RRL is 'aa-', which reflects the two-notch uplift above the adjusted 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.

Our assessment of the expected jurisdictional support for Belgian mortgage programs is strong. Under our covered bonds criteria, this means that the program can receive up to two notches of jurisdictional uplift over the RRL, capped at the rating on the Belgian sovereign (unsolicited, AA/Stable/A-1+). Therefore, the JRL for the program is 'aa'.

Collateral Support Analysis

Key assumptions and results

In assessing the cover pool's credit quality, we apply our new criteria "Methodology And Assumptions: Assessing Pools Of European Residential Loans," published on Dec. 23, 2016.

We base our analysis on loan-by-loan data as of Feb. 10, 2017.

The cover pool comprises loans secured by first-lien mortgages inscriptions over residential properties in Belgium and/or mortgage mandates to create mortgages, as well as a small proportion of Belgian government bonds for liquidity purposes. Approximately 15% of the cover pool is secured by buy-to-let properties or second homes. In addition, approximately 1% of loans in the cover pool are to BNPP Fortis' employees. We consider that if the issuer becomes insolvent, these borrowers would offset their mortgage loan against any amounts due to them by their employer and have assumed a full set-off of these loans.

Both the weighted-average foreclosure frequency (WAFF) and weighted-average loss severity (WALS) have reduced significantly since our previous analysis (see table 3). The WAFF benefits from better seasoning and debt-to-income ratios. In addition, under our European residential loans criteria, we no longer assume any geographic concentration for this program and we apply a favorable originator adjustment, described in our covered bonds criteria, reflecting the overall strength of the program.

The lower WALS is attributable to lower loan-to-value ratios, as well as the assumptions in our European residential loans criteria: in particular, the higher thresholds for jumbo valuations, and the benefit given to 50% of the value of mortgage mandates (against 0% previously) in applying our market-value decline analysis.

Mortgage mandates

In Belgium, when taking out a mortgage, the borrower must pay a registration fee based on a percentage of the mortgage loan. To reduce this fee, and in line with market practice, a lender may grant a mortgage loan partly secured by a mortgage inscription on the property and by a mortgage mandate. The registration fee is only payable on the mortgage inscription because a mandate is not collateral for the loan. A mortgage mandate is solely an irrevocable option given to the lender (or a third-party assignee) to unilaterally create a mortgage. Only when the mortgage mandate has been converted into a mortgage is the portion of the original loan represented by the mortgage mandate supported by a security interest in the relevant property.

There is a risk that another creditor would also benefit from the mortgage mandate over the property. In this instance, the creditor who first registers the mortgage (i.e., convert its mortgage mandate into an inscription) has priority over the security. Consequently, we have factored into our credit analysis the greater loss severity associated with mortgage mandates by giving credit to half the value of mortgage mandates in our recovery analysis.

Tables 3 to 8 summarize the cover pool's composition and key characteristics.

Table 3

Key Credit Metrics

	As Of Feb, 10, 2017	**As Of June 30, 2016**
Average loan size (€)	85,184	95,840
Weighted-average OLTV (%)*	68.99	N/A
Weighted-average loan seasoning (months)§	21.08	17.3
Balance of loans in arrears (%)	0.05	0.07
Buy-to-let loans (approx. %)	10	10
Second homes loans (approx. %)	5	10
Credit analysis results		
Weighted-average foreclosure frequency (WAFF; %)	17.88	22.3

Table 3

Key Credit Metrics (cont.)		
	As Of Feb, 10, 2017	**As Of June 30, 2016**
Weighted-average loss severity (WALS; %)	32.26	36.0
Asset default risk (%)	10.9	9.14

*In our credit analysis, we cap the recoveries from the property sale at the mortgage inscription value. §Seasoning refers to the elapsed loan term. LTV--Loan-to-value. N/A--Not applicable.

Table 4

Loan Seasoning Distribution		
Seasoning (%)*	**As Of Feb. 10, 2017**	**As Of June 30, 2016**
Less than 18 months	38.33	72.3
18-24	44.61	17.4
24-36	13.23	4.2
36-48	1.35	1.9
48-60	0.2	0.4
More than 60 months	2.28	3.8
Weighted-average loan seasoning (months)	21.08	17.3

*Seasoning refers to the elapsed loan term.

Table 5

DTI Distribution		
(%)	**As Of Feb. 10, 2017**	**As Of June 30, 2016**
0-30	30.2	25.8
30-40	32.9	35.3
40-50	20.0	20.9
50-60	9.0	8.9
60-70	3.7	4.2
70-80	1.9	2.5
>80	2.3	2.4

DTI--Debt service to income.

Table 6

Collateral Uplift Metrics		
	As Of March 11, 2017	**As Of June 30, 2016**
Asset WAL (years)	8.49	10
Liability WAL (years) at extended maturity date	8	8
Available credit enhancement (%)	33.07	54.15
Required credit enhancement for coverage of 'AAA' credit risk (%)	10.9	9.14
Required credit enhancement for first notch of collateral uplift (%)	10.9	9.14
Required credit enhancement for second notch of collateral uplift (%)	12.21	11.81
Required credit enhancement for third notch of collateral uplift (%)	12.86	13.14
Target credit enhancement (%)	13.51	14.48
Potential collateral-based uplift (notches)	4	4
Adjustment for liquidity (Y/N)	N	N

Table 6

Collateral Uplift Metrics (cont.)

	As Of March 11, 2017	As Of June 30, 2016
Adjustment for committed overcollateralization (Y/N)	Y	Y
Collateral support uplift (notches)	3	3

N/A--Not applicable. WAL--Weighted-average life.

Table 7

Geographical Distribution By Province

	As Of Feb. 10, 2017	As Of June 30, 2016
Antwerp	17.6%	18.4%
East Flanders	14.7%	14.4%
Flemish Brabant	14.0%	14.3%
Brussels	12.9%	12.2%
West Flanders	10.9%	10.0%
Liège	7.5%	6.9%
Limburg	6.3%	6.7%
Hainaut	5.8%	6.3%
Walloon Brabant	5.0%	5.0%
Namur	3.0%	3.6%
Luxembourg	2.2%	2.2%

Table 8

Original Loan-to-Value

Range	As Of Feb. 10, 2017*
0% - 60%	43.60%
60% - 70%	11.10%
70%-80%	12.50%
80%-90%	10.00%
90%-100%	17.00%
>100%	5.80%

*This is the first time we calculate the original loan-to-value under our new European residential loans criteria.

We analyze cash-flow risk according to our European residential loans criteria.

Our analysis of the pandbrieven's payment structure shows that cash flows from the cover pool assets would be sufficient, at the current rating level, to make timely payment of interest and principal to the covered bondholders. The program is exposed to refinancing risk because the mismatches in its asset-liability profile are not addressed by structural features.

Under our cash flow criteria, we model a program's cash flows under five different interest rate paths, with both high and low prepayment rates, to determine likely outcomes under different stress scenarios. We analyze the program's cash flows under 'AAA' credit stresses, as well as liquidity, interest rate and spread compression stresses; we also run different default timing and prepayment patterns. To assess market-value risk we apply a target asset spread of 425 basis points in our cash flow analysis, as outlined in "Assessments For Target Asset Spreads According To Our Covered Bonds Criteria," published on Aug. 15, 2016.

Because there is an active secondary market for Belgian mortgages such as the ones in the cover pool, the program can potentially benefit from up to four notches of collateral-based uplift, according to our covered bonds criteria.

Under these criteria, we decrease the collateral-based uplift by one notch as the issuer did not make any commitment to maintain the level of overcollateralization that is commensurate with the current ratings.

There is no notch of adjustment for liquidity risk as we consider this risk to be covered through the legal requirement to maintain 180 days of liquidity and because the ratings that we have assigned are higher than the long-term foreign currency rating on the Belgian sovereign, which is a eurozone member state.

Based on information as of March 11, 2017, our analysis shows that the available credit enhancement of 33.1% exceeds the credit enhancement of 10.9% required for the covered bonds to achieve a 'AAA' rating, as well as the target credit enhancement of 13.5%, which is down from 14.5% in our previous analysis. This reduction in the target credit enhancement reflects the better credit results (see table 3) as well the lower maturity mismatch on assets and liabilities (see table 6). As they are based on only two outstanding series, the cash flow results remain sensitive, in particular to the WAL of the liabilities we model and could significantly vary in future depending on the maturity of any new issuances.

With a JRL of 'aa' and a one-notch downward adjustment for uncommitted overcollateralization, the program needs to mitigate credit risk at the 'AAA' level and 75% refinancing risk in order to achieve a 'AAA' rating, equivalent to three notches of collateral-based uplift.

Additional Factors

Counterparty risk

We analyze counterparty risk using our criteria "Counterparty Risk Framework Methodology And Assumptions," published on June 25, 2013, and "Counterparty Risk Analysis In Covered Bonds," published on Dec. 21, 2015.

Liquidity risk

At closing, the cover pool includes a small proportion (approximately €40 million) of Belgian government bonds and other liquid assets to ensure liquidity for the payment of interest due on the covered bonds over the next six months.

The bonds are eligible for refinancing with the European Central Bank (ECB).

Commingling risk

In the program documentation, there is no clause relating to the downgrade of a bank where some of the assets in the segregated estate are deposited. However, the covered bond legislation contains provisions that aim to limit commingling risk between the issuer's two separate estates.

The revindication mechanism ensures that, if the issuer becomes insolvent, if any cash that belongs to the segregated estate cannot be identified in the general estate, then the special estate has a priority claim on unencumbered assets in the general estate. Under a provision defined in the prospectus, the special estate will receive the best available assets, ranging from ECB-eligible credit quality step 1 bonds, to any assets selected by the cover pool administrator. There is therefore no certainty as to the quality of assets that would be transferred to the special estate to address commingling risk. Accordingly, we have not given credit to this mechanism in our analysis.

Based on borrowers' monthly payments and our understanding of how much cash could accumulate, we have assumed two months of commingling risk, corresponding to the period immediately preceding the bank's insolvency. We believe that cash received post insolvency would be available in a timely fashion for the benefit of covered bondholders. Commingling risk is reflected in our target credit enhancement measure.

Country risk

We base our analysis of country risk on "Ratings Above The Sovereign - Structured Finance: Methodology And Assumptions," published on Aug. 8, 2016. Under these criteria, we classify the sensitivity of assets to country risk as moderate. Combined with Belgium's unsolicited long-term 'AA' rating and the lack of 12-month liquidity coverage, this allows the covered bonds to be rated three notches above the sovereign. Therefore, our ratings on the covered bonds are not constrained by country risk.

Related Criteria And Research

Related Criteria

- Criteria - Structured Finance - General: Methodology And Assumptions: Assessing Pools Of European Residential Loans, Dec. 23, 2016
- Criteria - Structured Finance - General: Ratings Above The Sovereign - Structured Finance: Methodology And Assumptions, Aug. 08, 2016
- Criteria - Structured Finance - Covered Bonds: Counterparty Risk Analysis In Covered Bonds, Dec. 21, 2015
- Criteria - Structured Finance - Covered Bonds: Covered Bond Ratings Framework: Methodology And Assumptions, June 30, 2015
- Criteria - Structured Finance - Covered Bonds: Covered Bonds Criteria, Dec. 09, 2014
- Europe Asset Isolation And Special-Purpose Entity Criteria--Structured Finance, Sept. 13, 2013
- Criteria - Structured Finance - General: Counterparty Risk Framework Methodology And Assumptions, June 25, 2013
- Criteria - Structured Finance - General: Global Derivative Agreement Criteria, June 24, 2013
- General Criteria: Global Investment Criteria For Temporary Investments In Transaction Accounts, May 31, 2012
- General Criteria: Methodology: Credit Stability Criteria, May 03, 2010
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009

Related Research

- BNP Paribas Fortis Mortgage Covered Bonds 'AAA' Ratings Affirmed Following New Criteria Application; Outlook Stable, March 24, 2017
- Europe's Housing Markets Continue To Recover Amid Extended QE, Feb 15, 2017
- Request For Comment: Methodology For Incorporating The Effect Of Resolution Regimes Into Covered Bond Ratings, Jan. 31, 2017
- Request for Comment: Methodology For Assigning Financial Institution Resolution Counterparty Ratings, Jan. 31, 2017

- Global Covered Bond Characteristics And Rating Summary Q4 2016, Jan. 13, 2017
- Outlook Assumptions For The Belgian Residential Mortgage Market, Nov. 18, 2016
- Assessments For Target Asset Spreads According To Our Covered Bonds Criteria, Aug. 15, 2016
- BNP Paribas, July 30, 2016
- Assessments For Jurisdictional Support According To Our Covered Bonds Criteria, July 20, 2016
- Belgium's Covered Bond Framework Allows Rating Above The Issuer, May 22, 2013