FitchRatings

The Netherlands

F. Van Lanschot Bankiers N.V.

Conditional Pass-Through Mortgage Covered Bonds

Presale

Ratings/Outlook

Conditional Pass-Through Mortgage Covered Bonds	'AAA'(EXP)/S table

Rating Rationale

IDR/outlook	'A-'/Negative
IDR uplift	1
D-cap	8 (Minimal discontinuity risk)
Tested rating on a PD basis	'AA'
Recovery given default uplift (notches)	2
Covered bonds rating	'AAA'
AP Fitch considers in analysis (%)	90.0
AAA breakeven AP (%)	90.0

Discontinuity Risk (D-Cap of 8)

Overall assessment	Minimal discontinuit y
Asset segregation	Moderate
Liquidity gap and systemic risk	Minimal discontinuit y
Systemic alternative management	Low
Cover pool-specific management	Moderate
Privileged derivatives	Very Low

Key Data

	Dec 2014
Asset type	Residential mortgages
Cover assets (EURbn)	0.66
Covered bonds (EURbn)	0.50
Nominal OC (%)	31.9
WAL of assets (years)	18.8
WAL of liabilities (years) – expected	5.0

Related Research

Covered Bonds Surveillance Snapshot (January 2015)

F. Van Lanschot Bankiers N.V. Full Rating Report (December 2014)

Global Housing and Mortgage Outlook - 2015 (January 2015)

Covered Bonds with Extendible Maturities (October 2014)

'B' Portfolio Loss Rates for Covered Bonds (October 2014)

Breaking Down Breakeven Overcollateralisation (July 2014)

Dutch Covered Bonds Framework - Discontinuity Analysis of Principles-Focused Legislation Strengthened by Contracts (March 2015)

Analysts

Roger Bickert
+44 20 3530 1667
roger.bickert@fitchratings.com

Stephen Kemmy
+44 20 3530 1474
stephen.kemmy@fitchratings.com

Key Rating Drivers

'A-' Rated Issuer: The 'AAA' rating of the conditional pass-through (CPT) mortgage covered bonds is based on F. Van Lanschot Bankiers N.V.'s (FvL) Long-Term (LT) Issuer Default Rating (IDR) of 'A-', an IDR uplift of '1' (applicable since the registration of the programme with the Dutch central bank (DNB)), a Discontinuity Cap (D-Cap) of 8 (minimal discontinuity) and the issuer asset percentage (AP) commitment of 90%, which is equal to the breakeven AP for the 'AAA' rating.

Minimal Discontinuity Risk: The D-Cap of 8 is driven by the minimal discontinuity risk assessment for the liquidity gap and systemic risk component. The D-Cap reflects the CPT maturity profile, which includes a 32-year extension period, and the reserve fund that covers three-months of interest due on the covered bonds plus a buffer for senior expenses. The CPT nature eliminates any refinancing risk should the source of payments switch to the cover pool.

Credit Loss Drives AP: The 10.3% credit loss at 'AAA' is the greatest contributor to the 90% breakeven AP for the programme (equivalent to an overcollateralisation (OC) of 11.1%). This high expected loss compared to peers reflects stresses applied to the high portion of interest-only loans in the pool (70.3%) and a conservative assumed debt-to-income (DTI) ratio of 35% for all borrowers. Higher stresses are also applied to high value properties (for 63% of loans).

Five Notches Cushion: With a D-Cap of 8, IDR uplift of 1 and 2 notches credit for recoveries, the maximum achievable rating on the covered bonds is 'AAA' as long as the issuer is rated 'BB' or above. This high level of cushion relative to FvL's 'A-' IDR drives the Stable Outlook on the covered bonds despite the Negative Outlook on the IDR.

Programme Highlights

Conditional Pass-Through Feature: A failure by the issuer to meet timely principal payments on the covered bonds triggers the 32 years maturity extension for the bonds. The guarantor will undertake its best efforts to sell parts of the portfolio during the extension period to fully redeem the extended series and to accumulate proceeds to repay the next maturing one.

Unhedged Interest Rate Mismatches: The programme is exposed to interest rate risk on the fixed rate loans (79.4%) when they revert in a low interest rate environment to another fixed or floating rate at their reset date. Fitch does not give credit to FvL's minimum mortgage rate commitment of 1.5% and modelled the loans to revert to a lower fixed or floating rate at an assumed margin above three-month Euribor. The documents provide FvL with the option to enter into a portfolio or interest rate swap agreement whenever they deem necessary.

Highly Seasoned Portfolio: The pool is well seasoned, with a weighted average (WA) seasoning of 120 months. The cover pool consists of 3,279 loans granted to prime Dutch borrowers, with an aggregate outstanding balance of EUR660m. A majority of these assets were previously securitised in FvL's RMBS transactions. Any deterioration of credit quality over time or adverse selection will negatively affect the 'AAA' breakeven AP.

Commingling Risk: Because the cover pool collections are paid into an account held with FvL which Fitch does not consider to be an eligible counterparty to support a 'AAA' rating according to its counterparty criteria, the rating agency sizes in the breakeven AP for the maximum monthly exposure that could be subject to commingling risk.

Figure 1
Selected Peers for Comparison

Issuer/ Programme	IDR/ outlook	CVB rating
NIBC Bank N.V.	'BBB-'/ Stable	'AAA'/ Stable
Achmea Bank N.V.	'A-'/Stable	'AAA'/ Stable
ABN Amro Bank N.V.	'A'+/ Neg	'AAA'/ Stable
ING Bank N.V.	'A+'/ Neg	'AAA'/ Stable
SNS Bank N.V.	'BBB+'/ Neg	'AA+'/ Stable

Source: Fitch

Peer Comparison

Some key rating drivers compare favourably for FvL (A-/Negative/F2, Viability Rating: a-) (see Figure 2) versus a selection of peers, which are the five other Dutch covered bond programmes that Fitch rates. The lower asset disposal loss is due to the conditional pass-through nature of the bonds issued under the programme. The selected peers are listed in Figure 1.

Please see the Covered Bond Surveillance Snapshot and related excel file (January 2015), for a detailed comparison of rating drivers across Fitch-rated covered bond programmes.

Figure 2
Peer Comparison: Key Rating Drivers

	FvL	Selected Peer Average	Selected Peer Range
IDR/Outlook	'A-'/Negative	'A-'/Negative	'BBB-'/ Stable – 'A+'/Negative
IDR uplift	1.0	1.8	0 – 2
D-cap	8	4.8	4–8
'B' Portfolio Loss Rate (%)	1.7	1.1	0.7 – 1.3
'AAA' breakeven OC (%)	11.1	25.6	9.9 – 33.3
Breakeven OC components (%)			
Credit loss (%)	10.3	6.5	4.6 – 7.4
Cash flow valuation (%)	-0.5	-0.3	-3.9 – 5.1
Asset disposal loss (%)	4.2	22.4	3.2 – 34.5

Source: Fitch

Sovereign Impact

The covered bonds rating does not include any adjustments due to the Dutch sovereign rating of 'AAA'/Stable. For countries rated above 'A+' Fitch applies its standard liquidity gap analysis, which forms part of the D-Cap, focussing on asset liquidity following an idiosyncratic stress of an issuer, while the banking sector as a whole is expected to remain stable and not suffer from a systemic crisis. Therefore, Fitch's view on liquidity and systemic risk is unlikely to change unless the Dutch sovereign was downgraded four notches to 'A+' or below.

The Netherlands has a country ceiling of 'AAA' and all cover assets are located in the Netherlands. Therefore, Fitch does not adjust the calculated rating default and recovery rates, which are applied in its covered bond analysis.

Sensitivity Analysis

There is limited downward pressure on the 'AAA' rating for FvL's mortgage covered bonds. FvL's LT IDR of 'A-' is in line with its Viability Rating (VR), which reflects standalone strength, of 'a-'. With the current IDR uplift of 1 and D-Cap of 8 in place, FvL's covered bond rating would likely remain unchanged (due to IDR impact) unless the IDR fell by six notches to 'BB-'.

If FvL's IDR remains at 'A-', the covered bond rating would likely remain unchanged (due to IDR uplift and D-Cap impact) unless the combination of the IDR uplift of 1 and D-Cap of 8 (equivalent to a total of 9 notches currently) fell to three notches. This would involve the D-Cap moving to 2 or worse, which correspond to a high discontinuity risk or below, which are unlikely assessments for liquidity protection in the form of a switch to conditional pass-through for a standard residential mortgage cover pool in a country with a 'AAA' sovereign rating.

There is no cushion between the 90% breakeven AP and the level of AP that Fitch gives credit to in its analysis, which will be published quarterly within the asset cover test. However, there is substantial cushion relative to the nominal OC of 31.9%.

Related Criteria

Covered Bonds Rating Criteria (August 2014)

Counterparty Criteria for Structure Finance and Covered Bonds (May 2014)

Counterparty Criteria for Structured Finance and Covered Bonds: Derivative Addendum (May 2014)

EMEA RMBS Master Rating Criteria (March 2015)

EMEA Residential Mortgage Loss Criteria (March 2015)

Criteria Addendum: Netherlands - Residential Mortgage Loss and Cash Flow Assumptions (June 2014)

Covered Bonds Rating Criteria - Mortgage Liquidity & Refinancing Stress Addendum (February 2015)

Criteria for Interest Rate Stresses in Structured Finance Transactions and Covered Bonds (December 2014)

Abbreviations
AP: Asset percentage
D-Cap: Discontinuity Cap
IDR: Issuer Default Rating
OC: Overcollateralisation
PD: Probability of default
WAL: Weighted average life
WAFF: Weighted average frequency of foreclosure
WARR: Weighted average recovery rate

The Issuer and CBC

Headquartered in s'Hertogenbosch, FvL (A-/Negative/F2) is the oldest independent bank in the Netherlands. The bank presents itself as a wealth manager and has a relatively simple organisational structure through a network of 25 branches located across the Netherlands, and five branches in the North of Belgium..The bank's main focus is on mid-size family businesses, affluent customers and services to institutional clients. In September 2004, FvL acquired C&E Bankiers, a niche business providing financial services to high net worth individuals and family business in the healthcare sector.

The bank's rating is driven by its strong intrinsic creditworthiness as reflected in its VR of 'a-', supported by strong capitalisation, sound liquidity management and a robust and balanced funding profile. The Negative Outlook is driven by its prolonged weaknesses in asset quality and profitability, despite improving trends in the latter.

Half of the bank's lending consists of solid domestic residential mortgage loans. However, in common with other Dutch banks, loans-to-value are high and the majority of the book consists of interest-only lending. The bank's SME and CRE loan books are of weaker quality, but in line with similar portfolios of Dutch peers. The bank announced in May 2013 a strategic refocus on wealth management and a target of strengthening its balance sheet mainly through reduction of its corporate and CRE lending.

The covered bond holders benefit from a dual recourse against Van Lanschot Covered Bond Company (CBC), which is secured by the cover assets, and an unsecured, unsubordinated recourse against FvL (see Appendix 1 for a programme summary).

IDR Uplift of 1

In bank resolution frameworks where covered bonds are favourably treated, such as under the Bank Recovery and Resolution Directive (BRRD) for EU countries, Fitch's analysis starts with an uplift over the IDR of up to two notches for programmes of issuers rated in the 'BB' category and above. A two-notch uplift is granted if at least two of the following three factors are present in Fitch's view or one notch if one of the factors is present.

Fitch assigned FvL an IDR uplift of 1 in line with the description presented in Figure 3 below.

Figure 3
IDR Uplift of 1 for FvL's Covered Bonds

IDR uplift driver	Fitch assessment
Relative ease/ motivation for alternative resolution methods to liquidation	No. FvL is not a global or domestic systemically important bank that would be more likely to be supported by resolution tools other than liquidation if insolvent.
Covered bond intensive country	No
Sufficient protection through senior unsecured debt	Yes. FvL's level of senior unsecured debt is higher than the 5% threshold (relative to the total balance sheet, adjusted for insurance assets and derivatives) that Fitch considers.

Source: Fitch

The IDR uplift of 1 was also applied to one of the selected peer programmes: NIBC CPT. No IDR uplift is applicable for Achmea's covered bonds programme because it is not registered with the DNB and not UCITS or CRD compliant. The other four Dutch covered bonds programmes have an IDR uplift of 2 due to their issuers' status as domestic systemically important banks and a level of senior unsecured debt higher than 5%.

D-Cap of 8

The potential risk that a covered bond could default if recourse shifts to the cover pool from an issuer is captured via Fitch's D-Caps, which determine the maximum uplift from the IDR (adjusted by any IDR uplift) to the tested rating on a probability of default (PD) basis. It reflects the highest risk assessment of the five components ranging from '8' for minimal discontinuity to '0' for full discontinuity.

Fitch has assigned this programme a D-Cap of 8 (minimal discontinuity), which is in line with Fitch's criteria for pass-through programmes with three months' coverage of interest and expenses as long as the assessment of the other components does not raise any particular concerns. This is because there should be no need to liquidate cover assets, which removes most payment interruption risk for the covered bonds once recourse against the cover pool is enforced.

Figure 4

Summary of FvL's Covered Bonds Discontinuity Risk Assessment

Overall assessment	**8 (minimal discontinuity)**
Asset segregation	Moderate
Liquidity gap and systemic risk	Minimal discontinuity
Systemic alternative management	Low
Cover pool-specific alternative management	Moderate
Privileged derivatives	Very low

Source: Fitch

Details on the assessment for each D-Cap component can be found in Appendix 2. The assessments for FvL's programme are standard for pass-through programmes.

Cover Pool

Figure 5

FvL's Cover Pool

Characteristics as of December 2014 (%s of current loan balance)

General		**Borrower type (%)**	
Current principal balance (EURbn)	0.66	Prime	100.0
Average current loan per borrower (EUR)	406,306	Employed	n/d
Number of loans	3,279	Self-employed	n/d
WA seasoning (years)	10.0	Unemployed	n/d
WA DTI (%) – assumption	35.0	Retired and other	n/d
		Multiple properties owner	4.2
Loan-to-value (LTV) (%)			
WA original LTV	85.4	**Loan type (%)**	
WA indexed current LTV	84.3	First–ranking	100.0
		NHG	0.0
		Construction deposit (>EUR2,500)	0.7
Property type (%)		Fixed rate	79.4
Houses	86.8	Floating rate	20.6
Flats	12.1	Annuity	1.3
Other	1.1	Linear	2.1
		Savings	2.8
		Life	13.1
		Investment	10.5
Valuation type		Interest Only	70.2
Full	100		
Desktop	0	**Geographic distribution (%)**	
Automated Valuation Model (AVM)	0	Noord-Holland	29.6
		Zuid-Holland	22.5
Current arrears (%)		Noord-Brabant	14.8
3m+ arrears	0.0	Utrecht	13.0
Less than 3m arrears	0.7	Gelderland	10.7

Source: Fitch/FvL

Cover Pool Credit Analysis

Fitch analysed the portfolio using its Dutch mortgage loss criteria (for further details see "*EMEA Residential Mortgage Loss Criteria*", published 28 May 2014 and its Dutch addendum under *Related Criteria* on page 2). Fitch applied its standard default probability adjustments under the criteria.

Lender adjustment

Fitch's base default probabilities assume that origination, underwriting and servicing practices and procedures are in line with those of a standard traditional Dutch lender, with market expertise and relevant management experience.

As part of the analysis, the agency performs an operational review of the originator to assess the origination, underwriting and servicing capabilities of the seller. As a result of this review, if Fitch believes that origination, underwriting and servicing procedures have significant weaknesses, an adjustment to the base default probabilities of the whole portfolio may be warranted.

As positives in FvL's practices Fitch has identified that FvL performs a case-by-case affordability analysis, has a private banking business with a wealthy client base and close client relations and uses a centralised mortgage approval centre that has a strong quality control framework in place.

Weaknesses Fitch has identified are that FvL's underwriting relies on the assessment of several income sources (basis salary, variable income, assets pledged as collateral), that the servicing is decentralised to branches until payments on the loans are three months overdue and that a larger amount of loans is underwritten on an 'explain' basis compared to a standard Dutch lender.

Based on these weaknesses, Fitch applied a lender adjustment of 1.05x.

In addition, Fitch has also reviewed an agreed-upon-procedures (AUP) report conducted by an international accounting firm. A sample of 450 loans was drawn from the population and verified against a 99% confidence level. The amount of findings is substantially higher compared to other Dutch originators and mainly relates to property valuation, valuation date, and a borrower's income. Although the majority of findings relates to missing loan documentation and older loans, given that the bank handles an internal document retention policy of seven years, Fitch has applied an upward adjustment of 1.05x due to the large number of findings in the AUP report and the uncertainty associated with unverifiable information.

Combined with a small adjustment for borrowers owning multiple properties, for whom Fitch considers the default risk comparable to borrowers owning a buy-to-let property, the total lender adjustment applied is 1.11x.

Asset Analysis

The cover pool consists of 3,279 loans granted to borrowers in The Netherlands, with an aggregate outstanding amount of EUR660m. The pool has a weighted average seasoning of 10.0 years and all loans are secured by a first-ranking mortgage. Of the loans, 0.7% are in arrears of up to three months and no loans are in arrears over three months. Fitch calculated a WA original LTV of 85.4% and a WA indexed current LTV of 84.3% for the pool.

The majority of assets were previously securitised in "Citadel 2011-1" with the remainder coming from new originations and savings loans which were previously present on the back-book.

Figure 8

Default Model Output (%)

Rating level	WAFF	WARR	WA MVD	Loss rate
AAA	19.3	51.4	43.8	9.4
B	5.3	68.1	29.8	1.7

Source: Fitch

Affordability

FvL did not provide Fitch with data regarding the borrowers' incomes. This is due to the fact that FvL takes into account a borrower's income as well as wealth position. As this is not reported jointly into one system FvL are not able to deliver this information. Fitch assumed a conservative debt-to-income (DTI) ratio of 35% for all borrowers.

Mortgage Type

The residential mortgage portfolio consists of linear, annuity, interest-only, investment, life and savings products (see Figure 7). Fitch increases the default probability for non-amortising loans to reflect the higher risk of borrowers facing a payment shock at maturity. Similarly, for life and investment mortgages, the probability of default is increased to capture the risk that the capital available at maturity may not be sufficient, depending on the performance of the underlying investment, with no certain return guaranteed.

Interest Rate Type

Of the portfolio, 79.4% is subject to a fixed interest rate. The remaining 20.6% pays a floating rate. The agency has increased the probability of default for floating-rate mortgages because a rising interest rate environment could put pressure on the ability of the borrowers to meet their mortgage payments.

The loans do not remain at a fixed rate for life; about 32% have an interest reset date before 2016. Most borrowers have the option to switch to a floating rate or another fixed rate for another period; however, it is common for borrowers in the Dutch market to enter into another fixed-rate agreement at the reset date. Borrowers who took a savings mortgage have to enter into another fixed-rate mortgage at the reset date.

Borrowers' Employment and Income Status

FvL does case-by-case budgeting, including income that stems from wealth positions rather than salaries. Total income information is not available in one system and FvL was not able to provide Fitch with the borrowers' employment information. However, all loans were originated to borrowers with verified income information. Fitch assumed a conservative split of 40% self-employed and 60% employed.

In Fitch's asset analysis both employment type and income verification status have an impact on the loans' foreclosure frequency. The frequency of foreclosure for a standard Dutch borrower assumes full-time employment, no adverse credit history and evidence of income. Where cases deviate from this standard, Fitch adjusts the probability of default to address the increasing risk of a borrower default on mortgage payments.

Geographical Distribution and Property Type

The geographical distribution of the properties is well diversified over the Netherlands and follows the distribution of the population. The province of Noord-Holland has the highest concentration of 29.6%, followed by Zuid-Holland 22.5%, Noord-Brabant 14.8% and Utrecht 13.0%.

All properties in the portfolio are owner occupied. There are no investment or second-home properties in the pool. Houses account for 86.7% of properties, apartments for 12.1%. A minimal proportion is partially for commercial use.

Illiquid Properties

Fitch has determined 63.2% of the portfolio to be secured by particularly high-value properties (higher than EUR600,000) and 0.1% to be secured by low-value properties (lower than EUR130,000). These loans are at risk of greater market value declines (MVDs) owing to the relatively poor liquidity at either end of the market. The agency has increased the MVDs for these loans.

Construction Loans

Construction loans form 0.7% of the pool. An element of the loan principal of these loans is to be disbursed to the borrower at a certain point, depending on the fulfilment of certain conditions. The granting of these loans is common practice in the Netherlands. Fitch views such loans as riskier if the construction works on the property still to be paid for are significant and final bills may be above the expected costs, leading to the provisioned construction deposit being insufficient to provide coverage for these extra expenses.

FvL posts any undrawn construction deposit amounts as cash in a separate account held by the CBC. Fitch believes that this sufficiently mitigates set-off risk regarding construction loans.

Dynamic Pool

As the pool is dynamic any deterioration of the pool's credit quality over time resulting from a pool top-up (adding additional mortgage loans) or after unfavourable substitution of the assets will negatively affect the 'AAA' breakeven AP.

The Fitch breakeven AP for the covered bonds' rating will also be affected, among other things, by the profile of the cover assets relative to outstanding covered bonds, which can change over time, even in the absence of new issuance. Therefore it cannot be assumed that it will remain stable over time.

Default Model Output

Fitch has analysed the portfolio using its Dutch mortgage loss criteria (for further details see *EMEA Residential Mortgage Loss Criteria and Criteria Addendum: Netherlands* under *Related Criteria* on page 2). Fitch derived a stressed cumulative default rate and recovery rate for the cover pool based on a loan-by-loan analysis of the cover assets. The WA frequency of foreclosure (WAFF) and WA recovery rate (WARR) in a 'AAA' scenario were calculated as 19.3% and 51.4%, respectively. Expected loss was 9.4% in the 'AAA' scenario. The composition and credit quality of the cover pool may change over time because of the dynamic nature of the programme.

Cash Flow Analysis

Fitch's cash flow model simulates the asset cash flows to reflect prepayment, servicing costs, delinquencies, defaults and recoveries in multiple stress scenarios under various issuer default timings.

The model tests whether the cover pool, managed by a third party, is able to service the interest and principal payments on the covered bonds in a timely manner. As there are no privileged derivatives in place, the agency made some assumptions on the evolution of the interest rate on the pool, in particular the change of interest rate at the interest reset date, and the margin on the floating-rate assets (see *Interest Rate Risk* below). The cash flows expected from the assets were also modified to reflect prepayments, delinquencies, default and recovery assumptions in a 'AAA' scenario, while hypothesising the issuer's default at different dates. In addition, the cost of replacing FvL as servicer/manager of the cover pool was modelled.

Asset Cover Test (ACT)

The ACT is designed to ensure a minimum level of credit enhancement to protect bondholders against specific risks; it is calculated monthly before an issuer event of default. If breached, failure to satisfy the ACT on or before the next succeeding calendar month will not constitute an issuer event of default. However, it will prevent FvL from issuing any further bond series until remedied. If not remedied on the next succeeding calculation date, the security trustee will be entitled to serve a notice of breach. After the service of a breach of the asset cover test, the CBC is not allowed to make any payments to FvL. FvL will continue to have a "best efforts" obligation to procure sufficient eligible assets. If a breach of the ACT is remedied, FvL can issue new series.

The ACT ensures that the value of the assets, multiplied by the AP, and adjusted for different risks (including insurance and deposit set-off), is higher than the nominal value of the covered bonds.

The ACT also tests that all the mortgage receivables, substitution assets and amounts standing to the balance of the CBC, excluding swap collateral and construction balances, will be at least equal to 115% of the principal amount of outstanding covered bonds. This minimum 115% is currently equivalent to a maximum AP of 87%. The relationship between OC and AP may change over time, notably because the AP applies to an adjusted asset balance, where an LTV cut-off percentage of 80% is used for all mortgages in the pool.

If an unremedied breach occurs post issuer default and a notice to pay is made by the security trustee on the CBC, this would trigger the amortisation test to be run to check there is at least 15% OC between the performing assets and the bonds (see *Amortisation Test* below).

Amortisation Test

The amortisation test is run following the service of a notice to pay on the CBC, to check that the stressed collateralisation level calculated under the test is at least 115%. If breached, the covered bonds will become due by their extended maturity date and will be paid pro rata subject to the availability of funds. Fixed-rate covered bonds will continue to bear interest at a fixed rate until their extended due for payment.

When covered bonds become pass-through after a breach of the amortisation test has been served, there is a risk that principal repayments could be made before the bond's expected maturity date and therefore earlier than expected.

Fitch's cash flows model tests that, even after a breach of the amortisation test, the modelled recoveries on the bonds would be more than 91% under 'AAA' stresses.

After an issuer event of default occurs, the CBC will undertake its best efforts to sell assets every six months, provided this does not lead to a breach of the amortisation test.

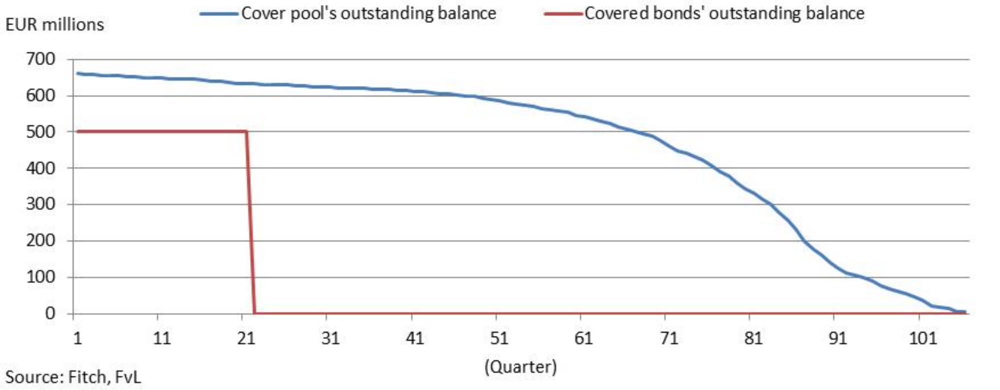
Maturity Profile

The cover assets are amortising, with a weighted average maturity of 18.8 years, while the covered bonds are expected to have a maturity of five years. FvL has the obligation to meet the payments on the bonds at their maturity date. After an issuer event of default resulting from FvL failing to meet these payments, or in case of a breach of the amortisation test, the bonds will become due by their extended due for payment date 32 years later, making the bonds effectively pass-through. This prevents any maturity mismatches between the cover assets and the covered bonds.

In its cash flow analysis Fitch modelled a hypothetical issuance of a EUR500m bond with a five-year term and a fixed coupon of 1.75% per annum.

Figure 7

Amortisation Profile



Source: Fitch, FvL

More generally, an issuer event of default will also be triggered when: FvL fails to make payments on any of its financial or material obligations; the issuer is wound up or goes bankrupt; or a liquidator is assigned. After an issuer event of default, the CBC will pay the interest due on the bonds and will accumulate principal proceeds from the assets until the maturity date of the bonds, at which point they will be distributed on a pass-through basis. It is only upon a breach of the amortisation test that all bonds will be paid pro rata.

Interest Rate Risk

There is no swap between the assets, mostly at a fixed rate until their next interest reset date, and the bonds, which are issued at a fixed rate. As a result, there is some natural hedging between the proportion of fixed (79.4% of the portfolio is subject to a fixed interest rate) and floating mortgage assets and the fixed rate bonds, with the interest rate risk initially stemming from the floating rate assets. However, the interest rate risk could increase significantly, due to the flexibility given to borrowers to reset their mortgages at a future date. This could lead to a migration of the WA interest rate on the mortgage receivables. In addition, any new issuance of covered bonds at a higher rate than the initial issuance will reduce the excess interest rate between the assets and the bonds, which could affect the breakeven AP for a given rating.

Decreasing interest rates should have a negative impact on the excess margin and should be the most stressful for FvL's first covered bond series. The first public issuance is a fixed-rate bond up to the final maturity date, with the extension period also at a fixed rate until the extended maturity date. The most stressful scenario for the bond would be when fixed-rate mortgages reset at lower fixed or floating rates, potentially causing a large interest rate mismatch between the cover pool and the bonds outstanding.

Under the programme documents, FvL will only transfer mortgages to the CBC that have a minimum interest rate of 1.5% a year. Fitch does not give credit to minimum mortgage rate commitments. Notably, the agency's tests assumed that FvL has defaulted and following that event the CBC cannot guarantee that the mortgage rates can be kept above the minimum level at the time of a reset. Therefore, Fitch has modelled the risk that mortgages at their reset date will switch to a rate below the minimum mortgage rate.

As no credit is given to a minimum mortgage rate commitment, Fitch modelled a conservative low fixed interest rate at the reset date for fixed rate loans and a conservative margin above three-month Euribor for floating rate loans. At the reset dates Fitch assumed that 30% of fixed-rate loans will revert to floating and that the floating-rate loans will remain floating. This compares to data provided by FvL from 2008 onwards, in which on average 1.6% of borrowers switched from fixed to a floating rate and 1.9% of borrowers switched from floating to a fixed rate.

Figure 8

The breakeven AP for a rating will be affected, among other things, by the profile of the assets relative to the outstanding covered bonds, which can change over time, even in the absence of new issuance, and should not be assumed to remain constant.

The interest and maturity of any future bond issuance could increase interest rate mismatches, causing the breakeven AP for the rating to be more volatile than in a fully hedged programme.

In order to mitigate certain mismatches between the interests received on the assets and those payable under the covered bonds the transaction documents include the option for FvL to enter into portfolio or interest swap agreements.

Commingling Risk

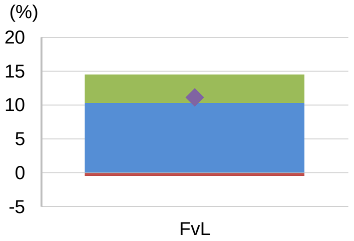
As long as the borrowers have not been notified to direct their mortgage payments to the CBC or to a new account bank, they will keep paying the servicers so that in an insolvency event funds belonging to the cover pool may be commingled with the bankruptcy estate of the issuer. Cover pool collections are paid into an account held with FvL and transferred on a monthly basis to an account held in the name of the CBC. Since FvL is rated 'A-'/'F2' Fitch does not consider it to be an eligible counterparty according to the agency's counterparty criteria and therefore does do not see commingling risk to be sufficiently mitigated. As such, the agency sizes for the potential amount at risk, equal to the maximum monthly exposure that could be subject to commingling risk. FvL has provided Fitch with data on monthly collections. Fitch has sized for commingling risk equal to one month of collections on the cover pool which has been deducted from the 'AAA' breakeven AP.

Insurance Set-Off

FvL has EUR86.8m mortgages in the pool that are potentially exposed to insurance set-off. These are all life mortgage loans and equate to 13.1% of the cover pool. All insurance companies for loans in the pool are external to FvL's banking group. As borrowers keep paying the insurance provider, the exposures with the insurer provider will continue to grow until the loan matures. If an insurance provider defaults and the borrower invokes a right of set-off on his loan for the accumulated amounts paid to the insurance company, the CBC could incur a loss on these loans. This depends on the likelihood that set-off rights will be recognised for the borrowers. This is more likely to be the case if the loan and the insurance contract have been sold as one product.

Fitch calculated the likelihood of default of the insurance companies in a 'AAA' scenario and combined it with the probability that borrowers would exercise set-off, and the increase of exposure to the insurance companies as borrowers pay their premium over time. The agency determined the maximum set-off risk over time to be 25% of the insurance loans. As insurance set-off risk in relation to life mortgage loans is not sized for in the ACT, Fitch has made an adjustment to the breakeven AP to account for the maximum set-off exposure. This was sized at 0.5% of the pool.

Breakeven OC Components



Source: Fitch

Breakeven AP for the Rating

FvL first issued a privately placed EUR1m covered bond maturing in April 2016 and bearing a fixed coupon rate. This issuance was made in order to seek registration for the programme with the Dutch central bank under regulatory requirements.

The 'AAA' breakeven AP is based on an second issuance assumed to be up to EUR500m with a five-year term. When determining the 'AAA' breakeven AP for this programme, Fitch has modelled a fixed coupon of 1.75% for the bond. Under these assumptions, Fitch calculated a 'AAA' breakeven AP of 90.0%, which relates to a 'AA' tested rating on a PD basis and recoveries given default in excess of 91% at 'AAA', which supports a two notch uplift to the 'AAA' covered bond rating.

The equivalent 'AAA' breakeven OC of 11.1% is mainly driven by the credit loss component (10.3%) and to a lesser extent the asset disposal loss (4.2%) and cash flow valuation (-0.5%) components (see Figure 8).

The credit loss reflects the impact of the WA default rate of 19.3% and the WA recovery rate of 51.4% in a 'AAA' scenario. The credit loss component is high for FvL's programme relative to its peers, because FvL mainly targets wealthy borrowers and therefore a large share of the portfolio (63.2%) is secured by particularly high-value properties (higher than EUR600,000) which leads to a larger illiquid property adjustment in Fitch's cover pool analysis and subsequently a lower recovery rate for those loans.

The asset disposal loss component is driven by the modelled high prepayment rate of 25% in line with Fitch's assumptions for The Netherlands (see *Related Criteria* on page 2) which increases early collection of cash that yield a lower rate than the interest on the bonds. Fitch gives no credit to the current interest earned on the cash held by the CBC at EONIA minus 5bp and assumed that cash is invested at Euribor minus a conservative margin.

The cash flow valuation component leads to a 0.7% lower 'AAA' breakeven OC for the programme. This is due to a small excess margin in the worst case scenario of high prepayment, leading to the stressed PV of the assets being higher than the PV of the liabilities. This component is unfavourable for FvL's programme relative to its peers, because of (i) a modelled worst case scenario of a low interest environment leading to a large interest rate mismatch between the cover assets (79.4% fixed rate) compared with the interest on the covered bonds (100% fixed rate); and (ii) the conservative margin assumed on the bond (1.75%) which reduces the excess spread.

Figure 9

Drivers of Cash Flow Valuation Component for FvL's Breakeven OC

Driver	Assets	Covered Bonds
Fixed-rate (%)	79.4	100
WA margin (from current interest rates) (%)	1.78	1.75
Worst case prepayment assumption (%)	25	
WAL (years) under scheduled amortisation	18.8	5.0
WAL (years) including worst case prepayments	3.5	

Source: Fitch

For this rating that considers both an uplift on a probability of default basis and for recoveries given default, the asset disposal loss component is in line with the 'AA' tested rating on a PD basis, while the other breakeven OC components represent 'AAA' stresses. This, plus Fitch's testing for at least 91% recoveries rather than 100% to assign two notches credit for recoveries given default, is why the sum of the breakeven OC drivers is higher than the 'AAA' breakeven OC. See *Breaking Down Breakeven Overcollateralisation* (July 2014) for Fitch's approach on determining breakeven OC components.

In the future, the breakeven AP for the rating will be affected, among other things, by the credit quality of the cover pool and the profile of the cover assets relative to the outstanding covered bonds, which can change over time.

AP Fitch Relies On

Fitch bases its analysis on the AP of 90.0% which is part of the programme's ACT calculation. It will be published in the programme's investor report on a quarterly basis.

Ongoing Programme Review

Fitch will periodically review the credit quality of the cover pool and perform a cash flow analysis to assess whether the AP taken into account by the agency provides protection against identified risks commensurate with the rating of the covered bonds issued by FvL under this programme. Cover pool and covered bonds information will be updated regularly and displayed on Fitch's covered bond surveillance tool (available at www.fitchratings.com) and in the quarterly Covered Bonds Surveillance Snapshot (January 2015).

Appendix 1: Programme Summary

Under this programme, FvL can issue from time to time covered bonds up to EUR5bn secured by a dynamic pool of residential mortgages located in The Netherlands and up to 20% eligible liquid assets, the latter being the maximum allowed under the Dutch covered bond legislation. The covered bonds rank pari passu among themselves and represent direct, unsecured and unconditional obligations of FvL and are guaranteed by the CBC which is the owner of the cover assets. The programme is regulated by the DNB under the Dutch covered bonds legislation.

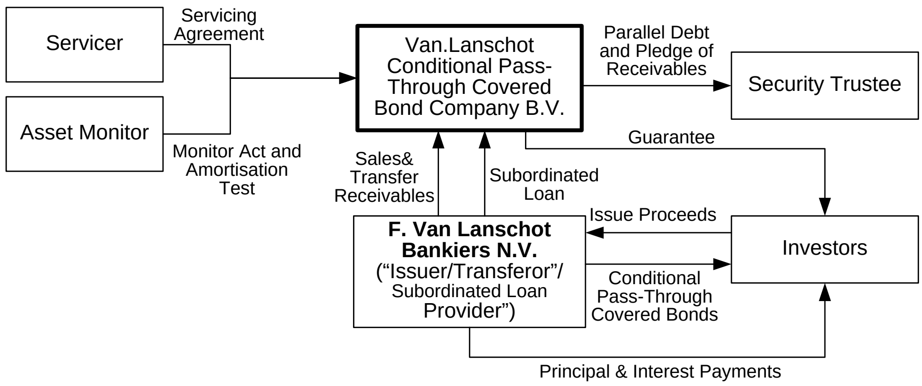
The scope of the activities of the CBC includes periodically acquiring mortgage loans, and guaranteeing payments of interest and principal under the covered bonds. The CBC was incorporated to act solely for FvL's covered bond programme.

Figure 10
Main Parties

F. van Lanschot Bankiers N.V.	Issuer Seller/originator Servicer
Van Lanschot Conditional Pass-Through Covered Bond Company B.V.	Guarantor
Citibank, N.A., London Branch	Principal paying agent
Stichting Security Trustee Van Lanschot Conditional Pass-Through Covered Bond Company	Security trustee
PricewaterhouseCoopers Accountants N.V.	Asset monitor
Intertrust Administrative Services B.V.	Administrator
Société Générale S.A., Amsterdam Branch	Account bank/GIC provider

Source: Programme documents

Figure 11
Structure Diagram



Source: Programme documents, Transaction documents

Figure 12

Summary of Certain Contractual Features

Contractual Features	Summary
ACT	The ACT is designed to ensure a minimum level of OC on the covered bonds to protect bondholders against specific credit and market risks; it is calculated monthly (unless an issuer event of default occurs). A breach of the ACT will not constitute an issuer event of default. However, until remedied it will prevent the issuer from issuing any further covered bonds and the CBC will not be allowed to make any payment to the issuer and the subordinated loan provider.
Amortisation Test	After an issuer event of default and the service of a notice to pay on the CBC, an amortisation test verifies whether the value of the cover pool, including any cash held in the deposit account and any substitution assets, adjusted to account for delinquencies and collateral value, is higher than the notional amount of outstanding covered bonds. Failure to pass the amortisation test allows the trustee to serve a breach of amortisation test notice on the issuer and the CBC upon which all outstanding covered bonds become pass-through. The CBC will undertake its best efforts to sell the loans and the proceeds from such a sale will be used to repay, pro rata, the outstanding covered bonds, provided that they are sufficient to redeem the relevant bonds in full. If the proceeds are insufficient the sale fails and will be repeated every six months until the proceeds are sufficient. The amortisation test mitigates time subordination of covered bonds within the programme.

Source: Programme documents

Appendix 2: D-Cap Assessment for FvL's Covered Bonds

Asset Segregation: Moderate Risk

Fitch expects that ring-fencing of the cover pool will be effective when applying any D-Cap assessment other than full discontinuity, given the 'all or nothing' nature of this risk. The differentiation between the D-Cap categories is based on whether any portion of the cash flow or assets might still be lost (and if so, to what extent), which would lower the cover pool amount available for bondholders.

A moderate risk assessment is applied to most Dutch programmes, because Fitch is of the view that there is some residual commingling and various set-off risks in these programmes.

Figure 13

Asset Segregation: Moderate risk

Component driver	Fitch assessment
Segregation of cover pool from other creditors of issuer	Effectively done via silent title assignment (stille cessie) from the Issuer to the CBC in line with other Dutch covered bonds and RMBS programmes.
Excess OC immune from claims from other creditors	The transfer of the assets under a true sale ensures effective segregation of the assets from the issuer's bankruptcy estate. Once the transfer has taken place, other creditors have a secondary claim on the cover pool.
Asset and liability claw back risk	The assets are transferred by means of a true sale to the CBC. In addition, the CBC is set up as a limited recourse bankruptcy remote entity which only enters into agreements with the transaction parties (which sign up to the limited recourse language). Claw-back risk on monies paid to bondholders just before an insolvency event of the issuer is also unlikely since the parties and potential creditors acknowledge that entering into a covered bond transaction does not harm their interests.
Commingling risk	Cover pool collections are paid into an account held with FvL and transferred on a monthly basis to an account held in the name of the CBC. Since FvL is rated 'A-'/'F2' Fitch does not consider it to be an eligible counterparty according to the agency's counterparty criteria for 'AAA' rated bonds and therefore does do not see commingling risk to be sufficiently mitigated. Fitch sizes for the amount at risk in the 'AAA' breakeven AP calculation.
Set-off risk for deposits, construction deposits and insurance products	Deposit set-off risk is mitigated by a deduction in the ACT for all deposits exceeding the amount guaranteed by the Dutch deposit guarantee scheme. FvL mitigates construction set-off risk through posting any undrawn amount as cash with the CBC. The following insurance mortgage products can be included in the pool: Investment mortgage loans, insurance savings mortgage loans, life mortgages loans or any combination of the above. Life insurance mortgages are subject to potential set-off risk which is not sized for in the ACT. Fitch has made an adjustment to the breakeven AP to account for the insurance set-off exposure. Fitch considers any set-off risk related to investment mortgage loans to be very limited, as policy providers usually hold the investment accounts with bankruptcy-remote special-purpose vehicles. Set-off exposure related to savings mortgage loans is mitigated through sub-participation agreements FvL entered into.

Source: Fitch

Liquidity Gap and Systemic Risk: Minimal Discontinuity

The analysis of the liquidity gap and systemic risk component considers liquidity risks, principal payment risk and systemic risks. In most countries with established mortgage markets, a moderate risk liquidity gap and systemic risk assessment will usually apply for non-pass-through programmes if the liquidation protection period is at least a year; although a higher risk assessment might apply if the liquidity mechanism is considered weak. A minimal discontinuity assessment applies when there are no liquidity gaps within a programme, such as for pass-through programmes with coverage for interest payments and expenses for the next three months on a rolling basis.

Figure 14

Liquidity Gap and Systemic Risk: Minimal discontinuity

Component driver	Fitch assessment
Principal protection	Sufficient. Conditional pass-through structure with a 32 month extendible maturity avoids a stressed sale of assets.
Limitations of principal protection mechanism	None highlighted.
Liquidity protection	Sufficient. Reserve fund covers three month's interest due and annual buffer for senior expenses. Held by the CBC in the GIC account at an institution rated at least 'A'/'F1' (currently Société Générale)
Senior/pari passu termination or intra-group loan payments	Should there be a swap agreement in place, termination payments would be subordinated to covered bonds principal & interest payments
Systemic risks	No additional stress applied. Because the Netherlands (AAA/Stable) is rated above 'A+', Fitch focuses on asset liquidity following an idiosyncratic stress of an issuer while the banking sector as a whole is expected to be stable

Source: Fitch

The minimal discontinuity assessment for the liquidity gap and systemic risk of FvL's programme is in line with all conditional pass-through programmes with three months interest reserve (plus senior costs) fund in place.

Alternative Management

Systemic Alternative Management: Low Risk

Fitch takes into consideration the framework or contractual clauses governing the appointment of a substitute manager — together with the length of time required to appoint one — any potential conflict of interest (in cases where a single administrator in a bankruptcy takes care of covered bonds and other creditors), the manager's responsibilities in the servicing and liquidation of the cover assets to meet payments due on the covered bonds and any further protection due to oversight or potential support for regulated covered bonds

A low risk assessment is applied to all Dutch covered bond programmes which are registered with the DNB. The DNB regularly monitors, among others, the programme's asset/liabilities ratio in light of the balance sheet encumbrance to ensure a healthy ratio is maintained. FvL has on-going reporting obligations towards the DNB and needs to keep fulfilling the programme's registration requirements.

Figure 15

Systemic Alternative Management: Low risk

Component driver	Fitch assessment
Administrator takes exclusive care of covered bondholders? When are they appointed?	Intertrust Management B.V. will act as administrator from day one. Intertrust will take on the management / administration / cash management role of the CBC and any other reporting activities.
Importance of timeliness of payments in the legal provisions	High. Protection is in place provided by a 3-month dynamic reserve fund (interest and senior costs). With regards to principal, the extended due for payment date is 32 years which is later than the maturity date of the mortgage loans (maximum 30yrs).
Substitute manager able to sell cover assets or borrow to make timely payments	Should a liquidation of the cover pool be contemplated, Intertrust will assign a reputable corporate finance firm to manage a sale and look for a potential buyer. The conditions of the sale would be subject to the security trustee's consent.
Regulatory oversight	Fitch considers DNB's active oversight positive. Under the Dutch legislative framework, the covered bond issuers have ongoing reporting duties to demonstrate that the covered bond programmes fulfil the regulatory requirements for registration. Fitch gives credit to the registered status of Dutch covered bonds by applying a low systemic alternative management risk assessment to Dutch regulated covered bonds programmes.

Source: Fitch

Cover Pool-Specific Alternative Management: Moderate Risk

Fitch focuses on the likely ease of the transferability of relevant data and IT systems to an alternative manager and buyer, with such quality and ease also judged on the quality and quantity of data provided to Fitch. Fitch expects a moderate risk assessment, such as that applied for FvL and most Dutch programmes, for most mortgage programmes with issuers deemed to have IT systems that are very capable of managing cover pools, covered bonds and data delivery. Fitch considers the following factors when judging this capability.

Figure 16

Cover Pool Alternative Management for FvL's Covered Bonds

Component drivers	Fitch assessment
Cover assets, debtors' accounts and privileged swaps clearly identified within IT systems	Strong systems and processes are in place, which are comparable with other Dutch programmes
Standardised or custom-made IT systems used.	FvL uses the PRoMMiSe system which is developed by Hypoport and widely used among Dutch CVB and RMBS issuers.
Automation and speed of cover pool reporting	Reporting is to a large extent automated through PRoMMiSe. Investor reports will be generated on a monthly basis.
Adequate filing of loan documentation, evidence of security	FvL files the loan documentation adequately in their systems which are backed up automatically. Disaster recovery procedures are in place.

Source: Fitch

Privileged Derivatives: Very Low Risk

Fitch considers programmes encompassing privileged hedging agreements to be more vulnerable to a potential insolvency of the issuer.

A very low risk, which applies to FvL's programme, is for programmes without any privileged derivatives.

The programme is unhedged. However, the documents provide FvL with the option to enter into a portfolio or interest rate swap whenever they deem necessary and market circumstances require entering into a hedge. Certain mismatches between the cover pool and covered bonds can be potentially hedged by a portfolio swap, whereby the proceeds of the pool will be hedged for a fixed or floating interest rate on one or more series of covered bonds. In addition to the portfolio swap, the CBC may enter into hedging arrangements whereby a certain fixed/floating rate will be exchanged for a specific rate on one or more covered bonds series.

Appendix 3: Originator and Servicer Operational Review

Origination

Mortgage loans are originated at branch offices of FvL. As of 2009, FvL discontinued the use of intermediaries but are currently reviewing the work with selected intermediaries again, with the goal of increasing their mortgage book. Mortgage applications are received by the underwriter at the branch level and checked against the applicable underwriting criteria. The ASK workflow system is used to support the underwriting process. Once a borrower has made an application, the ASK system will browse the BKR (Bureau Krediet Registratie) database and will conduct various fraud checks including Stichting Fraudebestrijding Hypotheken (SFH), which specialises in mortgage fraud; Verificatie Informatie Systeem (VIS), which provides an inventory of invalid ID documents; Externe Verwijzings Applicatie (EVA), a more general fraud database, and specific fraud checks against employer certificates regarding proof of employment.

No automatic approval can be issued by the ASK system. All applications are manually reviewed by the underwriters. The mortgage advisors have authority to approve loan applications up to EUR1,000,000 but only for borrowers with an indefinite employment contract and for mortgages which are fully compliant with the Dutch Mortgage Code of Conduct. All other applications require an approval by FvL's credit risk department. Applications up to EUR3m can be approved by one or two of these officers, depending on the case. Loan amounts above EUR3m require approval by a specific credit committee, composed of board members.

A quality control team assess the work done by underwriters on a monthly basis and any findings are corrected to ensure repeat errors do not occur.

Underwriting

FvL's underwriting criteria are in line with the Dutch Mortgage Code of Conduct. FvL analyses a borrower's overall financial position based on the amount of income and the borrower's wealth which will determine the limits of the mortgage offer. Underwriters carry out an affordability assessment based on DTI whereby the National Institute for Family Finance Information (NIBUD) benchmark is used to determine the borrower's minimum expenses. The borrower's net income is then simulated by removing relevant expense items from the gross income, such as other debts (as recorded in the BKR database), maintenance costs of the property, car expenses, taxes, alimonies, pension contributions and insurance premiums. The remainder, available for consumption and leisure, must be at least equal to a certain acceptable threshold, defined in accordance with the applicant's gross income. If the income criteria are not met, the application will be rejected. In that case a borrower can supplement their income by the combination of additional collateral, such as liquid capital assets, in which case the application can be accepted and will be classified as a special condition.

Self-employed borrowers are requested to provide audited accounts for the past three years. In case of a start-up, the borrower will only be considered if future income can be determined with a high degree of certainty.

As of January 2015 Fvl's underwriting criteria permits a maximum loan-to-market value (LTMV) of 103% with regard to mortgage loans up and to including EUR 2 million. For mortgage loans above that level, a pledge of securities of 25% (50% for loans above EUR 3 million) of the part of the loan above 75% of the market value of the residence is required.

A full valuation must be carried out by certified appraisers belonging to recognised associations and must not be older than six months. An exception to this rule is newly-built properties, to the extent they belong to greater real estate projects which can be valued at the purchase price. In such cases, the purchase price is taken as the market value. Local tax assessments (WOZ) can also be considered when the loan amount applied for is less than 50% of the tax estimate.

Servicing

All borrowers are required to open an account with FvL at origination of the loan and all payments must be made via direct debit. Loans in the early stages of delinquency are managed by the branches, until three months overdue. When a borrower has missed their mortgage payment, their current account with FvL will automatically be debited for those delinquent amounts, even if this will exceed the predefined current account limit. If an overdraft exceeds EUR250, a reminder letter is sent to the customer.

For Private Banking clients, once the overdraft has become material the first letter is sent after 30 days and the second letter after 45 days. In respect of Personal Banking clients it is 7 and 30 days, respectively. Each month, branches produce a list of delinquent loans that are more than three months in arrears, for the attention of the recovery division of the credit risk department.

Loans which are more than three months overdue are handled by the Recovery Division which is based in s'-Hertogensbosch. A check of the client's banking position will be performed, including their asset position. If the division considers the situation to be curable, a tailor-made recovery plan will be set up. Each borrower's situation will be assessed individually looking at their payment problems and spending behaviour, including the potential for asset sales. Temporary forbearance options such as reduced or suspended loan amortisations as well as reduced level of interest rates can be considered.

If the situation is not deemed curable, the recovery department will initiate the foreclosure process. Most properties are sold via a private sale. If the client does not agree to a voluntary sale, the sale will be forced via auction. FvL attends the auctions and in some cases acquires the properties for its book to ensure a minimum sale price. If the property is sold and there is no other collateral, but there still is a remaining debt, the client is handed over to a debt collection agency for further collection.

Appendix 4: Outstanding Liabilities

Figure 17

List of Outstanding Covered Bonds

Series	Currency	Interest rate type	(Size/bn)	Coupon rate	Payment frequency	Maturity	ISIN
1	EUR	Fixed	0.001	0.25%	Annually	2 Apr 16	XS1197830208

Source: FvL

The ratings above were solicited by, or on behalf of, the issuer, and therefore, Fitch has been compensated for the provision of the ratings.