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Transaction Update: Van Lanschot N.V. Conditional Pass-Through Mortgage Covered Bond Program

Conditional Pass-Through Covered Bonds

Primary Credit Analyst:
Judit O Woelk, Frankfurt (49) 69-33-999-319; judit.woelk@spglobal.com

Secondary Contacts:
Andreas M Hofmann, Frankfurt +49 69 33999 314; andreas.hofmann@spglobal.com
Ana Galdo, Madrid (34) 91-389-6947; ana.galdo@spglobal.com

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Ratings Detail

Reference Rating Level	**a**
Resolution Regime Uplift	+2
Systemic Importance	Strong
Resolution Counterparty Rating	N/A
Issuer Credit Rating	**BBB+**

N/A--Not applicable.

+

Jurisdiction-Supported Rating Level	**aa-**
Assigned Jurisdictional Support Uplift	+2
Jurisdictional Support Assessment	Strong
Legal Framework	Very Strong
Systemic Importance	Strong
Sovereign Credit Capacity	Very Strong

+

Maximum Achievable Covered Bond Rating	**aaa**
Collateral Support Uplift	Up to aaa
Overcollateralization Adjustment	0
Liquidity Adjustment	0
Potential Collateral Based Uplift	Up to aaa

=

Covered Bond Rating	**AAA**
Rating Constraints	aaa
Counterparty Risk	aaa
Country Risk	aaa

Major Rating Factors

Strengths

- Potential mismatches between the assets and liabilities are structurally mitigated, allowing us to delink the covered bond ratings from the long-term issuer credit rating (ICR).
- Contractual credit enhancement provides a substantial buffer over the credit enhancement level commensurate with the 'AAA' rating.
- Cover pool credit quality has remained stable over time.

Weaknesses

- The structure does not benefit from an interest rate swap.
- Cash belonging to the special-purpose entity (SPE) is mixed with cash belonging to the issuer and could be lost if Van Lanschot becomes insolvent.

Rationale

This transaction update follows our periodic review of Van Lanschot N.V.'s (Van Lanschot) conditional pass-through covered bond program.

Our covered bond ratings process follows the methodology and assumptions outlined in our "Covered Bonds Criteria," published on Dec. 9, 2014, and "Covered Bond Ratings Framework: Methodology And Assumptions," published on June 30, 2015. In addition, our analysis is based on our criteria for assessing pools of Dutch residential loans (see "Methodology And Assumptions: Assessing Pools Of European Residential Loans," published on Aug. 4, 2017).

We consider that the transaction documents, together with the Dutch legal and regulatory framework, 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.

Van Lanschot is domiciled in The Netherlands, which is subject to the EU's Bank Recovery and Resolution Directive (BRRD). We consider that mortgage covered bonds have a strong systemic importance to The Netherlands. These factors increase the likelihood that Van Lanschot 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 'a'.

We considered the likelihood for the provision of jurisdictional support. Based on a strong jurisdictional support assessment for mortgage programs in The Netherlands, we assigned two notches of uplift from the RRL. Therefore, we assess the jurisdiction-supported rating level (JRL) as 'aa-'.

The program can switch the bullet payment obligation into a pass-through payment, allowing us to delink the ratings on the covered bonds from the JRL. The JRL constitutes a floor to our ratings, but the potential uplift granted by our analysis of the collateral support could exceed the four notches that we would grant to programs that are exposed to asset-liability mismatch risk.

Based on our cash flow analysis as of Dec. 31, 2018, the available credit enhancement, after our adjustment for set-off of 14.52%, exceeds the 4.21% commensurate with a 'AAA' rating.

There are currently no rating constraints to the 'AAA' ratings relating to counterparty or country risks. We do not assign outlooks for ratings on programs whose creditworthiness we believe does not depend on that of the issuing bank.

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

Program Description

Table 1

Program Overview*	
Jurisdiction	The Netherlands

Table 1

Program Overview* (cont.)	
Year of first issuance	2015
Covered bond type	Structured§
Outstanding covered bonds (mil. €)	1,500
Redemption profile	Conditional pass-through
Underlying assets	Residential mortgages
Jurisdictional support uplift (notches)	2
Unused notches for jurisdictional support	0
Target credit enhancement (%)	4.21
Available credit enhancement (%)	14.52
Collateral support uplift (notches)	up to 'AAA'
Unused notches for collateral support	Not relevant
Total unused notches	Not relevant

*Based on data as of Dec. 31, 2018. §A covered bond law in The Netherlands governs the program, together with the program's documentation.

Set up in 2015, the program is backed by Dutch residential mortgage loans.

The issuer, Van Lanschot N.V., is a midsize bank within the Dutch banking system and the second-largest private bank in this market.

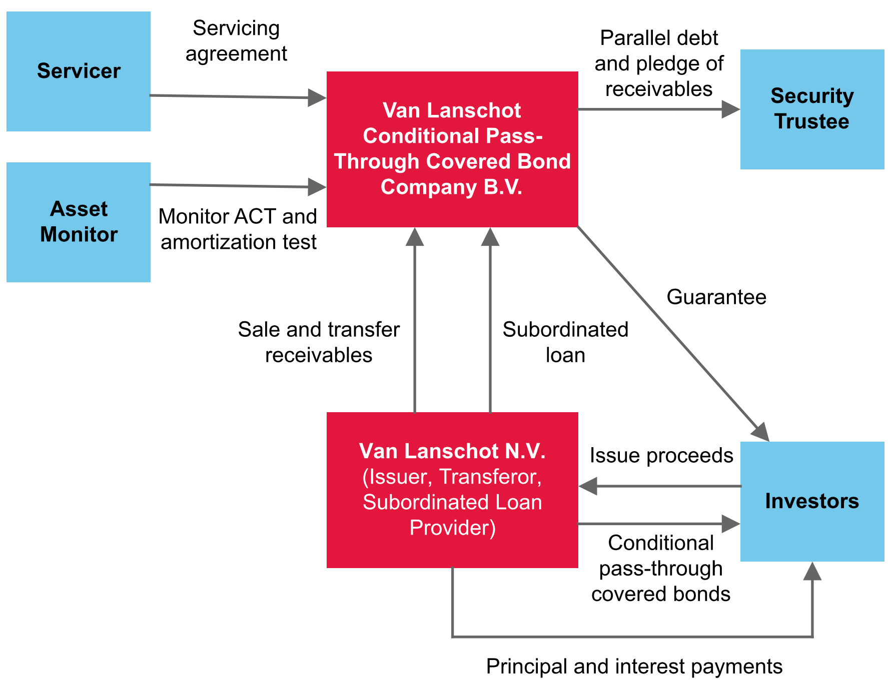
The mortgage covered bonds issued by Van Lanschot's conditional pass-through covered bond program constitute senior unsecured unsubordinated obligations of Van Lanschot.

If Van Lanschot is unable to pay the outstanding covered bonds, the Van Lanschot Conditional Pass-Through Covered Bond Co. B.V. (CBC) will guarantee payments on the bonds.

The CBC is a bankruptcy remote SPE with the mandate to manage the mortgage receivables in the cover pool and to guarantee payment of the covered bonds to the noteholders. In order to enable the CBC to guarantee payments on the covered bonds, Van Lanschot sold the cover pool assets to the SPE at closing and further sales may take place regularly.

Chart 1

Program Structure



Source:

Van Lanschot will pay interest and principal on each series of covered bonds on the respective scheduled payment dates. The program is structured such that, following an issuer bankruptcy and upon certain trigger events materializing, the redemption of the notes will switch to pass-through, and the scheduled maturity date of the covered bond will become extended to the legal final maturity date. In "pass-through mode" the covered bond will continue to pay timely interest, and the legal final maturity date is 32 years after the scheduled maturity date.

The possibility to extend the scheduled maturity date, as well as to switch the bullet payment obligation into a pass-through payment, allows us to delink the ratings on the covered bonds from the JRL.

This means that the JRL constitutes a floor to our rating, but the potential uplift granted by analysis of the collateral support could exceed the four notches that we would grant to programs that are exposed to asset-liability mismatch risk.

Two tests control that the overcollateralization does not decrease below a minimum predetermined level. Prior to issuer insolvency, the monthly asset cover test (ACT) monitors the level of credit enhancement. If this falls below the minimum commitment, the issuer will undertake its best efforts to transfer collateral to the CBC to ensure that the ACT is met by the next monthly evaluation. As long as the breach of the ACT is not cured, the issuer cannot issue new covered bonds, and the CBC cannot transfer funds back to the issuer.

After issuer bankruptcy the monthly amortization test determines if there is at least 15% overcollateralization available to the program. If the amortization test is breached, all covered bonds will become pass-through covered bonds, and the CBC will be required to use all funds available to redeem all covered bonds pro rata.

Table 2

Program Participants

Role	Name	Rating	Rating dependency
Issuer	Van Lanschot N.V.	BBB+/Stable/A-2	No
Originator	Van Lanschot N.V.	BBB+/Stable/A-2	No
Guarantor	Van Lanschot Conditional Pass-Through Covered Bond Company B.V.	NR	No
Arranger	Van Lanschot N.V.	BBB+/Stable/A-2	No
Co-arranger	Rabobank Nederland, based on the rating on the parent bank.	A+/Positive/A-1	No
CBC account bank	Société Générale S.A., Amsterdam Branch, based on the rating on the parent bank.	A/Positive/A-1	Yes
Trustee	Stichting Security Trustee Van Lanschot Conditional Pass-Through Covered Bond Company	NR	No
Servicer	Van Lanschot N.V.	BBB+/Stable/A-2	No
Administrator	Intertrust Administrative Services B.V.	NR	No
Principal paying agent and registrar	Citibank N.A., London Branch, based on the rating on the parent bank.	A+/Stable/A-1	No

NR--Not rated.

Rating Analysis

Legal and regulatory risks

We base our legal analysis on our "Structured Finance: Asset Isolation And Special-Purpose Entity Methodology," criteria, published on March 29, 2017 (SPE criteria), "Guarantee Criteria," published on Oct. 21, 2016, and our covered bond ratings framework.

The covered bonds are governed by the Dutch covered bond framework. The Dutch general framework is principle-based and was introduced as secondary legislation in the Dutch Financial Supervision Act ("Wet op het financieel toezicht"). It comprises the Decree on Prudential Rules Regulation ("Besluit prudentieel toezicht Wft") and the Implementing Regulation ("Uitvoeringsregeling Wft"). In January 2015, a revised legislative framework came into force. The new legislation is incorporated into the Dutch Financial Supervision Act and introduces, among other provisions, mandatory ACTs, including a 5% minimum overcollateralization, mandatory liquidity buffer, and mandatory audits.

As is typical for structured covered bonds, the detailed provisions applicable to Van Lanschot's conditional pass-through covered bonds are established via contractual obligations.

From our analysis we have concluded that the cover pool assets are effectively isolated for the benefit of covered bondholders. This asset isolation allows us to assign a higher rating to the covered bond program than the long-term ICR on Van Lanschot.

In order to grant a security interest over its assets, the CBC and the security trustee entered into a parallel debt agreement for the benefit of the secured parties. Under this agreement, the guarantor undertakes, through parallel debt, to pay the security trustee the amounts due by it to the secured parties. It thereby creates a claim of the security trustee, which can be validly secured by the rights of pledge created by the pledge agreements.

We have examined whether we can rely on the cover pool cash flows to serve the covered bonds if the issuer becomes insolvent. In our view, this implies that two key preconditions are satisfied: First, that we can reasonably expect that the CBC would not go bankrupt; and, second, that we can be comfortable that the CBC would serve the guarantee if the issuer becomes insolvent.

We have analyzed the CBC within the framework of our SPE criteria. S&P Global Ratings generally regards an entity that satisfies these criteria as sufficiently protected against both voluntary and involuntary insolvency risks. We have concluded the CBC establishment follows our SPE criteria and that we can therefore treat the CBC as a bankruptcy remote entity in our analysis.

We have also analyzed the CBC guarantee based on our guarantee criteria. The guarantee criteria are intended to minimize the risk that a guarantor may be excused from making a payment necessary for paying the holders of rated debt. Therefore, we would normally expect these criteria to be satisfied before giving credit to the guarantee. We have concluded that the CBC guarantee is in line with our guarantee criteria, and therefore we give benefit to the guarantee agreement in the program.

Operational and administrative risks

In our opinion, there is no new operational risk from the cover pool's management and loan origination that would constrain the covered bond ratings to the same level as the long-term ICR.

We believe that it is highly likely that a replacement cover pool manager could be appointed if the issuer were to become insolvent. We consider The Netherlands to be an established covered bond market and we believe that the mortgage assets in Van Lanschot's cover pool do not comprise product features that would materially limit the range of available replacement cover pool managers or servicers.

We view the bank's underwriting criteria as prudent. Our view is also supported by the low level of delinquencies on Van Lanschot's mortgages.

Our analysis of operational risk follows the principles laid out in our covered bond ratings framework and "Global Framework For Assessing Operational Risk In Structured Finance Transactions," published on Oct. 9, 2014.

Resolution regime analysis

As part of our covered bonds criteria, our analysis considers any resolution regime in place in the Netherlands to determine the RRL. The RRL on Van Lanschot, which is the starting point for any further uplift in our analysis, is 'a'. We consider the following factors:

- Van Lanschot is domiciled in the Netherlands, which is subject to the EU's BRRD. 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 risk if there is a 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 government support.
- Further, we consider covered bonds to have strong systemic importance to the Netherlands. Based on these two facts, we add two notches of resolution support uplift to the ICR. (see "Assessments For Jurisdictional Support According To Our Covered Bonds Criteria," published on Oct. 16, 2018).
- There is no resolution counterparty rating (RCR) on Van Lanschot N.V.

The resulting RRL is the higher of ICR plus two notches and RCR, which results in an RRL of 'a'.

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 Dutch 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. As the rating on the Netherlands is 'AAA', the program can receive the full two notches of jurisdictional support. The JRL is therefore 'aa-'.

Collateral support analysis

The cover pool comprises solely Dutch owner-occupied residential mortgage loans originated by Van Lanschot (see table 3). We base our analysis on loan-by-loan data provided by the issuer as of Dec. 31, 2018.

We have analyzed the portfolio and applied stresses commensurate with a 'AAA' rating scenario to estimate the level of defaults, as shown by our risk measure, the weighted-average foreclosure frequency (WAFF); and our loss estimate measure, the weighted-average loss severity (WALS). We base our loan-level analysis of Van Lanschot's cover pool on our assumptions for Dutch residential loans in our European residential loans criteria (see "Methodology and Assumptions: Assessing Pools Of European Residential Loans," published on Aug. 4, 2017).

The cover pool decreased by about 9% to €1.73 billion in December 2018 from €1.91 billion in January 2017, but continues to remain fairly granular.

The below tables provide an overview on the key characteristics of the cover pool. All loans are backed by owner-occupied residential properties. The weighted-average loan-to-value ratios have decreased, which resulted in lower 'AAA' WAFF and WALS for the cover pool, compared to the previous analysis. Arrears remain at a very low level and the predominant share of the loans pay fixed interest rate.

Table 3

Cover Pool Composition

	As of Dec. 31, 2018		As of Jan. 31, 2017	
Asset type	**Value (mil. €)**	**Percentage of cover pool (%)**	**Value (mil. €)**	**Percentage of cover pool (%)**
Residential*	1,717.9	100	1,890.1	100
Commercial	0	0	0	0
Substitute assets	0	0	0	0
Other asset type	0	0	0	0
Total	1,717.9	100	1,890.1	100

*Net of saving deposits.

Table 4

Key Credit Metrics

	As of Dec. 31, 2018	**As of Jan. 31, 2017**
Average loan size (€)	433,289	421,470
Original weighted-average LTV ratio (%)	84.19	92.89
Current weighted-average LTV*	67.89	80.16
Weighted-average loan seasoning (months)§	118.77	122.85
Balance of loans in arrears (%)	0.07	0.41
Owner occupied properties (%)	100	100
Interest rate type (%)	97.7 fixed-rate loans	91.9 fixed-rate loans
Weighted-average interest rate (%)	2.66	2.99
Interest-only	96.2	96.36
Credit analysis results:		
WAFF (%)	16.47	20.44
WALS (%)	39.42	41.4

*Loan-to-foreclosure value adjusted for developments in the house-price index. §Seasoning refers to the elapsed loan term. LTV--Loan-to-value.

Table 5

Original Loan-To-Value Ratios

	As of Dec. 31, 2018	**As of Jan. 31, 2017**
(%)	Percentage of cover pool (%)	Percentage of cover pool (%)
Below 50	9.74	8.26
50-60	7.00	6.10
60-70	9.19	7.06
70-80	12.33	9.50
80-90	15.13	10.32
90-100	15.93	14.2
Above 100	30.67	44.55
Weighted-average loan-to-value ratios	84.19	92.89

Table 6

Current Indexed Loan-To-Value Ratios

	As of Dec. 31, 2018	As of Jan. 31, 2017
(%)	Current loan-to-indexed value	Current loan-to-indexed value
Below 50	25.33	8.26
50-60	11.71	6.1
60-70	16.12	7.06
70-80	14.68	9.5
80-90	11.61	10.32
90-100	9.57	14.2
Above 100	10.98	44.55
Weighted-average loan-to-value ratios	67.89	92.89

Our analysis of the covered bonds' payment structure shows that cash flows from the cover pool assets would be sufficient, at the 'AAA' rating level, to make timely payment of interest and ultimate payment of principal to the covered bond program on its legal final maturity.

Total available credit enhancement in the program was 15.23% as of Dec. 31, 2018. Following our adjustment to account for set-off risk, we calculated an adjusted available credit enhancement of 14.52% for end 2018. We believe the target credit enhancement level sufficient to achieve the 'AAA' rating is 4.21%. This is a decrease from 5.72% as of Jan. 2017, mainly due to the improved credit results.

Table 7

Loan Seasoning Distribution*

	As of Dec. 31, 2018	As of Jan. 31, 2017
	Percentage of portfolio (%)	Percentage of portfolio (%)
Less than 18 months	14.68	10.15
18-24	2.49	3.87
24-36	6.35	3.22
36-48	8.24	1.40
48-60	2.29	0.65
60-72	0.93	0.94
72-84	0.59	2.61
84-96	0.81	5.86
96-108	2.32	6.49
108-120	4.92	7.53
Above 120	56.39	57.28

*Seasoning refers to the elapsed loan term.

Table 8

Geographic Distribution Of Loan Assets

	As of Dec. 31, 2018	As of Jan. 31, 2017
Top five concentrations	Percentage of cover pool	Percentage of cover pool
Noord Holland	31.44	29.30

Table 8

Geographic Distribution Of Loan Assets (cont.)

	As of Dec. 31, 2018	As of Jan. 31, 2017
Zuid Holland	19.86	21.26
Noord Brabant	15.74	16.25
Gelderland	9.33	9.61
Utrecht	13.79	13.36
Other	9.84	10.22
Total	100.00	100.00

Table 9

Collateral Uplift Metrics

	As of Dec. 31, 2018	As of Feb 28, 2017
Asset WAM (years)	18.74	19.13
Liability WAM (years)	5.3 (extendible by up to 32)	7.2 (extendible by up to 32)
Available credit enhancement	14.52	26.00
Required credit enhancement for first notch of collateral uplift (%)	N/A	N/A
Required credit enhancement for second notch of collateral uplift (%)	N/A	N/A
Required credit enhancement for third notch of collateral uplift (%)	N/A	N/A
Target credit enhancement for maximum uplift (%)	4.21	5.72
Potential collateral-based uplift (notches)	Unlimited	Unlimited
Adjustment for liquidity	N	N
Adjustment for committed overcollateralization	N	N
Collateral support uplift (notches)	Unlimited	Unlimited

WAM--Weighted-average maturity. N/A--Not applicable.

Counterparty risk

We have identified several counterparty risks to which the covered bonds are exposed. However, these are either structurally addressed in line with our current counterparty criteria or taken into account in our cash flow modeling. Therefore, we believe that they do not constrain the rating from a counterparty risk perspective (see "Counterparty Risk Framework: Methodology And Assumptions" published on March 8, 2019).

Borrowers in the cover pool will make mortgage payments by direct debit into Van Lanschot collection accounts. This would expose the program to commingling risk. We have stressed this risk in our cash flow model by assuming that two months of collections are lost.

The collections are transferred on the 14th day of each month into the CBC account held with Société Générale S.A., Amsterdam Branch. The CBC account bank has committed to replace itself if it were to lose its 'A' long-term rating.

In addition, there are various forms of set-off risk relating to deposit accounts, other claims, and savings deposits. The ACT addresses these risks by limiting the maximum amount of covered bonds that can be issued under the program.

There are no derivatives registered in the cover pool, and we have taken interest rate risk into account in our cash flow modelling.

Country risk

We analyze country risk according to our structured finance ratings above the sovereign criteria (see "Incorporating Sovereign Risk In Rating Structured Finance Securities: Methodology And Assumptions," published on Jan. 30, 2019). Given our 'AAA' long-term unsolicited rating on The Netherlands, country risk does not constrain our rating on the covered bonds.

Related Criteria And Research

Related Criteria

- Counterparty Risk Framework: Methodology And Assumptions, March 8, 2019
- Incorporating Sovereign Risk In Rating Structured Finance Securities: Methodology And Assumptions, Jan. 30, 2019
- Methodology And Assumptions: Assessing Pools Of European Residential Loans, Aug. 4, 2017
- Structured Finance: Asset Isolation And Special-Purpose Entity Methodology, March 29, 2017
- Guarantee Criteria, Oct. 21, 2016
- Covered Bond Ratings Framework: Methodology And Assumptions, June 30, 2015
- Covered Bonds Criteria, Dec. 9, 2014
- Global Framework For Assessing Operational Risk In Structured Finance Transactions, Oct. 9, 2014
- Credit Stability Criteria, May 3, 2010
- Understanding S&P Global Ratings' Rating Definitions, June 3, 2009

Related Research

- Global Covered Bond Characteristics And Rating Summary Q1 2019, April 11, 2019
- Global Covered Bond Insights Q1 2019, April 11, 2019
- Criteria Guidance: Counterparty Risk Framework: Methodology And Assumptions, March 8, 2019
- Dutch RMBS Index Report Q4 2018, Feb. 19, 2019
- Criteria Guidance: Incorporating Sovereign Risk In Rating Structured Finance Securities: Methodology And Assumptions, Jan. 30, 2019
- The Netherlands Ratings Affirmed At 'AAA/A-1+'; Outlook Stable, Nov. 16, 2018
- Assessments For Target Asset Spreads According To Our Covered Bonds Criteria, Oct. 16, 2018
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- Van Lanschot N.V., July 19, 2018
- Criteria Guidance: Covered Bonds Criteria, May 2, 2018
- Glossary Of Covered Bond Terms, April 27, 2018
- Outlook Assumptions For The Dutch Residential Mortgage Market, April 17, 2018