

# **CORRECT: FITCH AFFIRMS AAREAL BANK AG'S MORTGAGE PFANDBRIEFE AT 'AAA' ON WI'S PFANDBRIEFE TRANSFER**

Fitch Ratings-Frankfurt/London-30 January 2018: This announcement corrects the version published on 4 January 2018 to include additional applicable criteria.

Fitch Ratings has affirmed Aareal Bank AG's (BBB+/Stable) mortgage Pfandbriefe rating at 'AAA' with a Stable Outlook.

The affirmation follows Fitch's assessment of Aareal's mortgage Pfandbriefe programme after the transfer of Westdeutsche Immobilienbank's (WI) cover assets and outstanding mortgage Pfandbriefe to Aareal. The legal completion of the integration of WI's Pfandbriefe programme, which took place on 30 June 2017, led to an immediate merger of Aareal's and WI's mortgage Pfandbriefe programmes. As a result, WI's and Aareal's outstanding Pfandbriefe now rank *pari passu* and are secured jointly by one cover pool.

## **KEY RATING DRIVERS**

The 'AAA' rating of the covered bonds is based on Aareal's Long-Term Issuer Default Rating (IDR) of 'BBB+', an IDR uplift of two, a payment continuity uplift (PCU) of four notches, a one-notch recovery uplift and the overcollateralisation (OC) Fitch relies upon of 28.5%, which provides more protection than the 'AAA' breakeven OC of 27.5%.

The breakeven OC of 27.5% (down from 28.5%) continues to be driven by a decreased credit loss component of 21.1% (24.5% previously). This improvement mainly reflects the improved credit quality of the US and Canadian commercial real estate portfolio, roughly 20% of the cover pool. The inclusion of 5% highly seasoned residential assets with a weighted average (WA) loan-to-value of only 36% further contributed to lower loss expectations.

The reduction of the breakeven OC has been partially offset by an increased cash flow valuation component, which has become the second largest driver of the breakeven OC, up to 5.2% from 1.4%. It mainly mirrors compressed excess spread following the Pfandbrief programme merger. WI's Pfandbriefe carry a higher WA coupon than Aareal's. Fitch expects this effect to diminish over the next 12 months as the majority of WI's Pfandbriefe will mature by the end of 2018.

The low asset disposal loss component of 1.1% reflects the well-matched asset and liability profile. The programme is vulnerable towards high prepayment scenarios, which limits the need to model asset sales but at the same time also reduces available excess spread.

## **VARIATION**

Fitch has applied a variation to its "Covered Bonds Rating Criteria" published 1 December 2017. Substitute assets that may vary in quantity and in nature are generally not included when calculating the refinancing spread levels for a specific programme. As Aareal commits to holding at least EUR700 million of these assets at any time, we have included an amount up to this level in the calculation of the refinancing spread levels. The application of this variation has not affected the programme's rating.

## **RATING SENSITIVITIES**

Aareal Bank AG's mortgage Pfandbriefe 'AAA' rating would be vulnerable to downgrade if any of the following occurs: (i) the IDR is downgraded by one notch or more to 'BBB' or lower; or (ii) the combined number of notches represented by the IDR uplift and the PCU is reduced from six to five

or lower; or (iii) the OC that Fitch considers in its analysis drops below Fitch's 'AAA' breakeven level of 27.5%.

If the OC that Fitch considers in its analysis drops to the legal minimum requirement of 2% on a net present value basis, the programme could only achieve a one-notch recovery uplift. As a result, the covered bond rating would likely be downgraded to 'A+'.

The Fitch breakeven OC for the covered bond rating will be affected, among others, 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 the breakeven OC to maintain the covered bond rating cannot be assumed to remain stable over time.

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Applicable Criteria

Commercial Real Estate Loans Securing Covered Bonds Rating Criteria (pub. 21 Nov 2017)

<https://www.fitchratings.com/site/re/906003>

Covered Bonds Rating Criteria (pub. 01 Dec 2017)

<https://www.fitchratings.com/site/re/906615>

Covered Bonds and CDOs Public Entities' Asset Analysis Rating Criteria (pub. 21 Dec 2017)

<https://www.fitchratings.com/site/re/911872>

Fitch's Cover Assets Refinancing Spread Level (RSL) Assumptions - Excel File (pub. 30 Oct 2017)

<https://www.fitchratings.com/site/re/10008155>

Fitch's Interest Rate Stress Assumptions for Structured Finance and Covered Bonds - Excel File (pub. 17 Feb 2017)

<https://www.fitchratings.com/site/re/894478>

Fitch's Foreign-Currency Stress Assumptions for Residual Foreign-Exchange Exposures in Covered Bonds and Structured Finance – Excel File (pub. 30 Oct 2017)

<https://www.fitchratings.com/site/re/10008156>

Global Bank Rating Criteria (pub. 25 Nov 2016)

<https://www.fitchratings.com/site/re/891051>  
SME Balance Sheet Securitisation Rating Criteria (pub. 03 Mar 2017)  
<https://www.fitchratings.com/site/re/894773>  
Structured Finance and Covered Bonds Counterparty Rating Criteria (pub. 23 May 2017)  
<https://www.fitchratings.com/site/re/898537>  
Structured Finance and Covered Bonds Counterparty Rating Criteria: Derivative Addendum (pub. 23 May 2017)  
<https://www.fitchratings.com/site/re/898538>  
Structured Finance and Covered Bonds Country Risk Rating Criteria (pub. 18 Sep 2017)  
<https://www.fitchratings.com/site/re/903496>  
Structured Finance and Covered Bonds Interest Rate Stresses Rating Criteria (pub. 17 Feb 2017)  
<https://www.fitchratings.com/site/re/893890>  
U.S. and Canadian Multiborrower CMBS Rating Criteria: Effective 5/24/2017 to 1/5/2018 (pub. 24 May 2017)  
<https://www.fitchratings.com/site/re/897950>

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