Request For Comment
Methodology For Rating Covered Bonds

Antonio Farina: Managing
Director, Covered Bonds

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S&P Global
Ratings

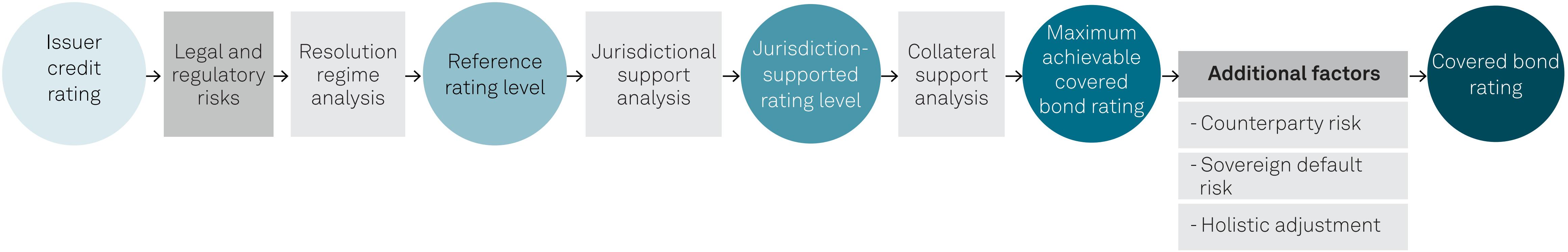
Highlights | Proposed Update To Methodology For Rating Covered Bonds

- S&P Global Ratings is requesting comments on proposed changes to its methodology for rating covered bonds. If adopted, this methodology would supersede “Covered Bonds Criteria” and “Covered Bond Ratings Framework: Methodology And Assumptions.” It would also partly supersede “Counterparty Risk Framework: Methodology And Assumptions,” in so far as it relates to the analysis of counterparty risk in covered bonds. The current criteria remain in effect until we finalize these proposed criteria.
- S&P Global Ratings is seeking feedback on the proposed criteria by May 23, 2025. We encourage interested market participants to submit their written comments to https://disclosure.spglobal.com/ratings/en/regulatory/ratings-criteria. Comments may also be sent to CriteriaComments@spglobal.com should participants encounter technical difficulties.

Highlights | Proposed Update To Methodology For Rating Covered Bonds

Our overall framework and building blocks for analyzing covered bonds remain the same, but we are proposing changes to the jurisdictional support analysis, to the collateral support analysis, and to some of the additional credit factors.

The main steps in analyzing covered bonds



Highlights | Why This Update To The Covered Bond Criteria?

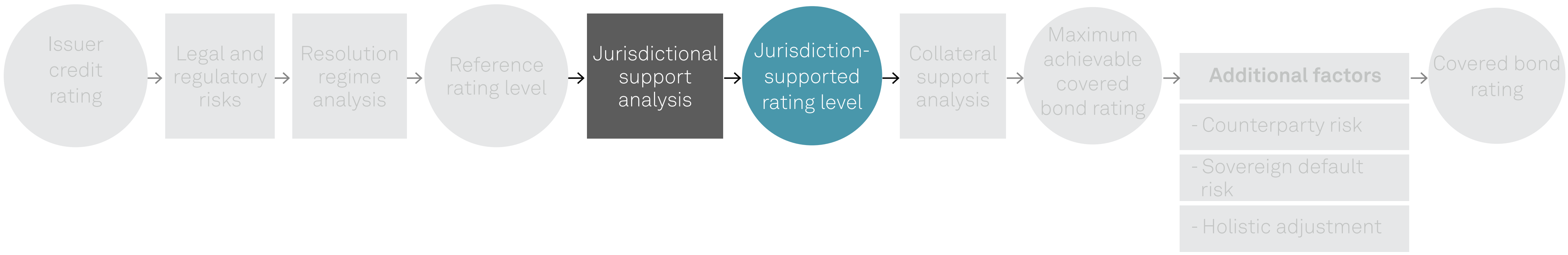
- Incorporate relevant information in connection with the market's evolution.
- Update the collateral analysis and enhance its stability over time.
- Simplify the counterparty analysis and differentiate it from standalone structured finance issues.

Highlights | Impact On Outstanding Ratings

- Approximately 100 covered bond program ratings outstanding.
- Expected ratings impact of one covered bond rating upgrade by one notch.
- Expected impact on overcollateralization levels commensurate with current rating levels is a reduction by 5 percentage points (37% in relative terms) for around 70 programs.

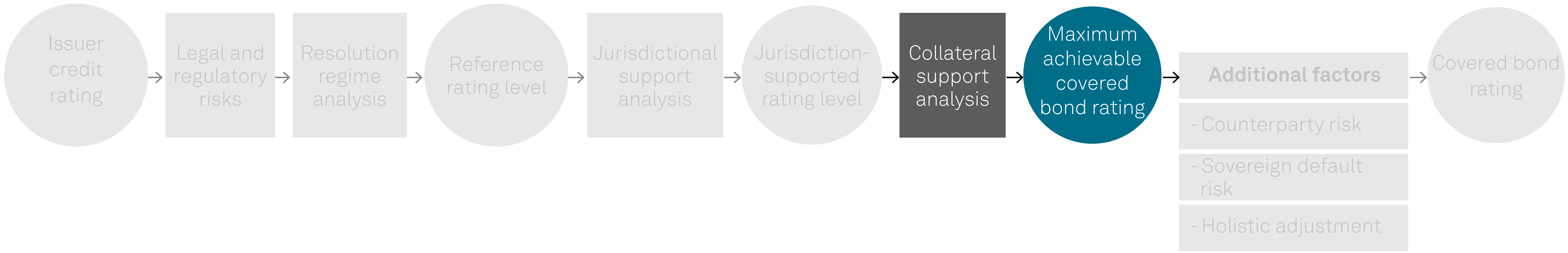
Key Changes | Jurisdictional Support Analysis

- When rating a covered bond program on the sole merit of jurisdictional support, we generally expect to do so on the basis of the provisions of the local covered bond legislation, without considering any additional overcollateralization (OC) beyond the applicable regulatory OC levels. Exceptions would be when we identify specific risk factors in the cover pool or in the minimum regulatory OC level. In such cases, we would expect coverage of the pool's credit risk to a 'aaa' level of stress to assign a 'AAA' rating.
- For covered bonds issued in countries that are members of a monetary union, uplift based on jurisdictional support may include up to one notch above the rating on the sovereign.



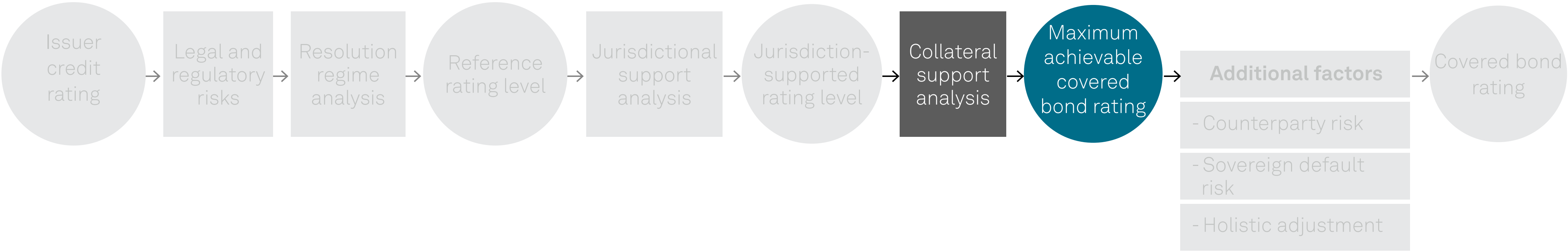
Key Changes | Collateral Support Analysis – Credit Risk

- We allow up to two notches of collateral-based uplift based on credit risk coverage, without refinancing costs.
- We may in certain cases simplify our credit risk analysis compared to structured finance issues for these dual recourse instruments, where certain elements have limited impact on credit enhancement levels.



Key Changes | Collateral Support Analysis – Refinancing Costs

- We adjust down the assumed target asset spread levels used when modelling refinancing costs, moving away from the historical peaks observed in certain countries for the asset type in the cover pool. This is to reflect a moderate stress scenario in our spread assumptions, acknowledging that some of the peak spread levels were observed in countries that experienced higher degrees of stress.
- In addition, to inform our spread assumptions, we account for historical covered bond spread data, rather than structured finance spreads, when we expect covered bonds to be the most likely secured funding tool for the asset type in the pool. Over the past decade, although we observed the effect of central bank intervention on market liquidity in times of stress, we recognize that the extent and timing of such market support in the future remains uncertain.



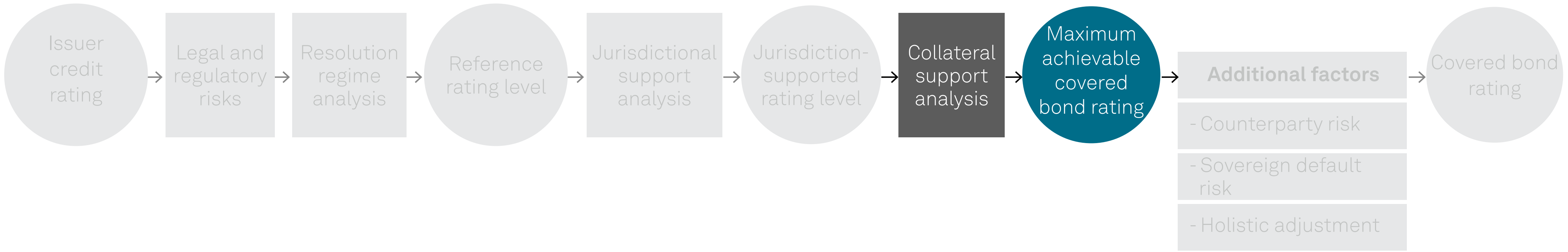
Key Changes | Collateral Support Analysis – Refinancing Costs

Asset buckets	Prime residential mortgages--target asset spreads (bps)	Prime residential mortgages-- base-case asset spreads (bps)
Bucket 1	200	50
Australia		
Austria		
Belgium		
Canada		
Denmark		
Finland		
France		
Germany		
Ireland		
Netherlands		
Norway		
Sweden		
U.K.		

Asset buckets	Prime residential mortgages--target asset spreads (bps)	Prime residential mortgages-- base-case asset spreads (bps)
Bucket 2	250	50
South Korea		
Singapore		
Bucket 3	400	100
Iceland		
Italy		
Spain		

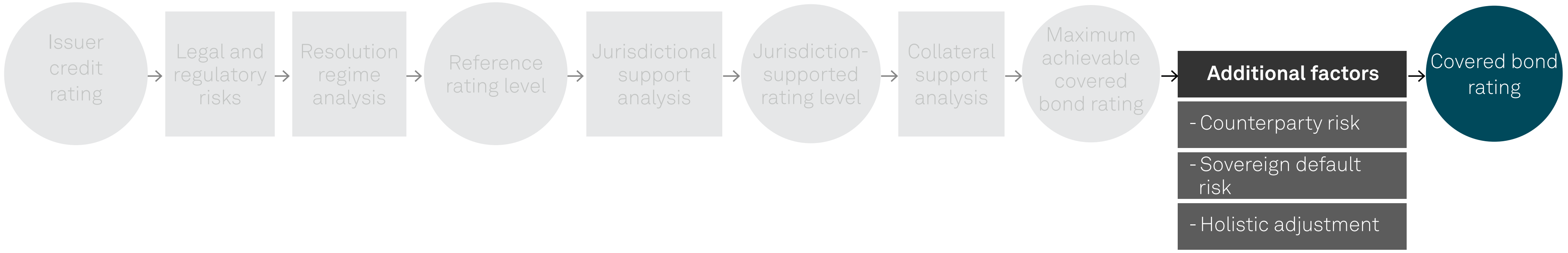
Key Changes | Collateral Support Analysis – Refinancing Costs

- We apply these target assets spreads to model refinancing costs for covered bonds maturing over the first three years in our cash flow simulation. For covered bonds maturing later, we assume base-case spreads, which are informed by historical observations during periods of lesser stress and our forward-looking view.
- We expand the forward-looking analysis of the covered bond program management to include our expectation of the issuer's near- to medium-term covered bond issuance plans, as well as expected variations in our target credit enhancement levels, to enhance the stability of our credit enhancement levels, commensurate with each degree of uplift.



Key Changes | Counterparty Risk Analysis

- We update our analysis of counterparty risks when our rating analysis is linked to the issuer, to reflect the dual recourse nature of covered bonds and our consideration of the issuer's management the covered bond program.
- We simplify our approach by focusing on a smaller number of key risk factors
- If counterparties are investment grade and we believe there is a high likelihood that they will be replaced upon a downgrade, we consider the risk to the covered bonds' overall creditworthiness to be minimal.
- When lower-rated counterparties result in enhanced counterparty risk, we may adjust ratings downward.
- We use analytical judgement to assess unusual situations and/or the benefit that regulatory frameworks may have on a program's counterparty risk profile



Key Changes | Counterparty Risk Analysis

Derivative exposures

- If there is an effective replacement framework and an investment grade counterparty (ies), we do not constrain the covered bonds' rating on account of counterparty risk.
- If downgraded counterparties aren't replaced as expected, we may adjust the rating down considering the creditworthiness of the issuer, the seniority of termination payments, the rating on the counterparty, and whether they are related or unrelated to the issuer.

Non-derivative exposures

- We rely on an investment grade issuer's ability to manage bank account risk. For lower rated issuers, we expect downgrade language to be documented, unchanged from currently.
- Commingling risk resulting from the issuer's failure to reinvest cash payments into new assets would be addressed as part of our forward-looking analysis of available collateral levels.

Note also the release of a separate Request For Comment on counterparty risk analysis in structured finance (see Related Publications slide).

Related Publications

Publications:

- Request For Comment: Methodology For Rating Covered Bonds
- Financial Institutions Rating Methodology
- Counterparty Risk Framework: Methodology And Assumptions
- Request For Comment: Counterparty Risk Methodology

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