Fitch Affirms Desio’s OBG Programme; Outlook Stable

Fitch Ratings - Milan - 21 Dec 2022: Fitch Ratings has affirmed the Italian mortgage covered bonds (Obbligazioni Bancarie Garantite, OBG) issued by Banco di Desio e della Brianza S.p.A. (Desio, BB+/Stable/B) at 'AA' with Stable Outlooks.

The rating action follows a periodic review of the OBG programme.

KEY RATING DRIVERS

The covered bonds' rating is based on the bank's Long-Term Issuer Default Rating (IDR) and the various uplifts above the IDR granted to the programme. It also considers the over-collateralisation (OC) protection provided through the programme' asset percentage (AP).

The OBG programme is rated at its maximum achievable rating in line with Italy's Country Ceiling of 'AA', which acts as a rating cap for the programme. The Stable Outlook on the OBG rating mirrors that on Italy's IDR.

The highest achievable rating uplift is 10 notches, consisting of a resolution uplift of two notches, a payment continuity uplift (PCU) of six notches and a recovery uplift of two notches. The AP that Fitch relies upon in its analysis (80% for Desio) is in line with the 80% (from 83%) for Desio's OBG

Fitch considers in its analysis the levels of AP the issuers publicly disclosed in the latest programmes' investor reports.

OC Protection

The revision of the 'AA' break-even AP factors in the increased net present value difference between the covered bonds and the cover assets in a rising interest rate scenario, due to a larger proportion of fixed-rate assets as well as the reduction of the excess spread available over the life of the programme. The change in the cover pools’ composition is the result of transfer of newly originated assets to the underlying portfolio in 2022.

The 'AA' break-even AP has been adjusted to factor in the additional OC that the issuers put aside in the programme test to account for set-off exposures. Fitch believes that the set-off risk is a secondary risk driver for the programme and remedial actions (including sizing of the loss via deductions in the programme tests) will trigger upon the loss of 'BB-' deposit rating, while the issuer has deposit rating higher than 'BB-'.

The covered bonds have soft-bullet amortisation profile, so the break-even AP for the rating is driven by the ALM (assets/liabilities mismatch) loss component, which is 22.3%. This is followed by the credit loss component for the OBG rating of 2.5%, driven by the portfolio loss floor. The cover pool comprises prime residential mortgage loans originated in Italy.

Uplifts

The resolution uplift for the programme reflects exemption from bail-in of fully collateralised OBG, the low risk of under-collateralisation at the point of resolution and our view that a bank resolution will not result in enforcement against the cover pool. The two-notch resolution uplift also considers that the bank's Long-Term IDR is driven by the bank's Viability Rating.

The PCU of six notches reflects the OBG' 12 months' protection for principal payments and the available protection for interest payments of at least three months.

The programme is eligible for Fitch's maximum recovery uplift of two notches as no limitations to recovery expectations apply.

RATING SENSITIVITIES

Factors that could, individually or collectively, lead to positive rating action/upgrade:

The rating of the OBG could be upgraded if Italy's Country Ceiling is upgraded by at least one notch. This is provided that the AP that Fitch relies upon is sufficient to withstand stresses associated with the higher rating.

Factors that could, individually or collectively, lead to negative rating action/downgrade:

The rating of the OBG would be downgraded if any of these events occurs (i) Italy's 'AA' Country Ceiling is downgraded by at least one notch; (ii) the AP that Fitch relies upon in its analysis increases above the respective Fitch 'AA' break-even AP.

Furthermore, the rating of the covered bonds would be downgraded if the bank's Long-Term IDR is downgraded to 'B+' or below.

Fitch's break-even AP for the covered bond rating will be affected, among other factors, 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 break-even AP to maintain the covered bonds' ratings cannot be assumed to remain stable over time.

The continued neutral sector outlook for global covered bonds, despite the deteriorating asset performance outlook for many jurisdictions, reflects the instrument's dual-recourse nature, liquidity protection mechanisms, ample overcollateralisation (OC) cushion, and limits, such as cover assets eligibility criteria and contractual tests, which mitigate asset performance deterioration (see “Global Covered Bonds Outlook 2023”).

BEST/WORST CASE RATING SCENARIO

International scale credit ratings of Financial Institutions and Covered Bond issuers have a best-case rating upgrade scenario (defined as the 99th percentile of rating transitions, measured in a positive direction) of three notches over a three-year rating horizon; and a worst-case rating downgrade scenario (defined as the 99th percentile of rating transitions, measured in a negative direction) of four notches over three years. The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Best- and worst-case scenario credit ratings are based on historical performance. For more information about the methodology used to determine sector-specific best- and worst-case scenario credit ratings, visit https://www.fitchratings.com/site/re/10111579

CRITERIA VARIATION

Fitch's analysis of Desio's cover pool varied from the agency's Covered Bonds Rating Criteria. Fitch has modelled the cover pool enforcement up to six quarters after the pool cut-off date, although there is no principal redemption in the six quarters after the pool cut-off date and the issuer is non-investment grade. This variation is based on Fitch’s forwardlooking view on the redemption profile of the covered bonds and on the cover pool composition.The application of this variation has an upward one-notch impact on the OBG rating.

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

ESG CONSIDERATIONS

Unless otherwise disclosed in this section, the highest level of ESG credit relevance is a score of '3'. This means ESG issues are credit-neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg