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Transaction Update: AIB Mortgage Bank (Mortgage Covered Bonds)

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Ratings Detail

Reference Rating Level	a-
Resolution Regime Uplift	+2
Systemic Importance	Very Strong
Adjusted Issuer Credit Rating	bbb
GRE And Sovereign Support	0
Issuer Credit Rating	**BBB***

+

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

+

Maximum Achievable Covered Bond Rating	aaa
Potential Collateral Support Uplift	+4
Overcollateralization Adjustment	0
Liquidity Adjustment	0
PotentialCredit Enhancement	+4

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Covered Bond Rating	
AAA/Stable	
Rating Constraints	aaa
Counterparty Risk	aaa
Country Risk	aaa

*We use the long-term rating on Allied Irish Banks PLC, to which the issuer is deemed a core entity.

Major Rating Factors

Strengths

- The available credit enhancement exceeds the target credit enhancement for the maximum potential collateral-based uplift.
- The issuer has made a public statement that it intends to maintain overcollateralization at a level that supports the covered bond ratings.

Weakness

- The rating on the program uses all notches of the collateral-based uplift, and is therefore sensitive to the long-term sovereign rating on Ireland.

Outlook: Stable

S&P Global Ratings' stable outlook on its ratings on AIB Mortgage Bank's (AIBMB) mortgage covered bonds reflects our outlook on Ireland. If we were to lower our long-term sovereign rating on Ireland, all other things being equal, we would lower the ratings on the covered bonds.

Rationale

We are publishing this transaction update as part of our review of AIBMB's mortgage covered bond program (see "Ratings Affirmed On AIB Mortgage Bank's Mortgage Covered Bonds Following Review; Outlook Stable," published on July 31, 2018).

Our covered bond ratings process follows the methodology and assumptions outlined in our "Covered Bonds Criteria," published on Dec. 9, 2014. From our analysis of the covered bond program, we have concluded that the assets in the cover pool are isolated from the risk of the issuer's insolvency. This asset isolation allows us to potentially assign a higher rating to the covered bond program than our long-term issuer credit rating (ICR) on the issuer.

In accordance with our covered bonds criteria, we uplift the ratings on the covered bonds from the adjusted ICR, taking into account that the issuer is based in a country subject to the EU's Bank Recovery And Resolution Directive (BRRD), and considering the potential jurisdictional support and the portfolio of assets backing the bonds. Here we use the ICR on Allied Irish Banks PLC (AIB), to which the issuer is deemed core under our group rating methodology (see "Group Rating Methodology," published on Nov. 19, 2013). Based on the long-term ICR on AIB and our assessments of systemic importance of mortgage covered bonds in the Republic of Ireland, we assess the reference rating level (RRL) at 'a-'. Though we may assign up to three notches of uplift from the RRL based on a very strong jurisdictional support assessment for mortgage programs in Ireland, the jurisdictional support uplift is limited by our long-term rating on Ireland. Therefore, we assess the jurisdiction-supported rating level (JRL) as 'a+'. The program can benefit from up to four notches of collateral-based uplift.

As of March 31, 2018, the assets backing the program comprised Irish residential mortgages totaling €13.8 billion. Our measure of the portfolio's weighted-average foreclosure frequency (WAFF; the level of defaults) is 25.58% and the weighted-average loss severity (WALS; estimated losses given default) is 31.97%, based on a 'AAA' stress level, calculated according to our European residential loans criteria (see "Methodology And Assumptions: Assessing Pools Of European Residential Loans," published on Aug. 4, 2017). The available credit enhancement, 84.75%, is above the 21.23% target enhancement needed for the maximum collateral-based uplift, and we deduct no notches for liquidity issues or lack of overcollateralization commitment. The potential collateral-based uplift is four notches above the JRL of 'a+'. The program can therefore reach a 'AAA' rating under our covered bonds criteria.

There are currently no rating constraints to the current rating relating to country, counterparty, legal, or administrative and operational risks.

We consider the assets to have moderate sensitivity to country risk. Therefore, we can assign an uplift to the covered bonds of up to four notches above the sovereign rating on Ireland if liquidity risk is mitigated for 12 months. The bonds' maturities are one-year extendible, which structurally mitigates liquidity risk on 99.13% of the bonds. While two covered bonds maturing in 2019 have no extendible features, in our view liquidity risk is mitigated by the cover pool's scheduled cash collection. We understand that the issuer has no intention to issue further notes without extendible features and our revised cash flow analysis shows that collections from the cover pool can repay the principal outstanding on such notes without exposing the issuer to a material liquidity risk. Thus, we can assign ratings up to four notches above our 'A+' foreign currency long-term sovereign rating on Ireland.

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

Program Description

Table 1

Program Overview*	
Jurisdiction	Ireland
Year of first issuance	2006
Covered bond type	Legislation-enabled
Outstanding covered bonds (bil. €)	7.5
Redemption profile	Soft bullet§
Underlying assets	Residential mortgages
Jurisdictional support uplift	2
Unused notches for jurisdictional support	1
Target credit enhancement (%)	21.23
Available credit enhancement (%)	84.75
Collateral support uplift	4
Unused notches for collateral support	0
Total unused notches	1

*Based on cover pool data as of March 31, 2018. §Two issuances, which represent less than 1% of the liability are hard-bullet covered bonds.

AIBMB's mortgage covered securities program is a €20 billion covered bond program backed by residential mortgage assets all located in the Republic of Ireland. The first issuance was in 2006.

The issuer is AIBMB. AIBMB was incorporated in Ireland as a public limited company in 2005, subsequently re-registered as a public unlimited company. It obtained an Irish banking license and was registered as a designated mortgage credit institution in 2006.

AIBMB is a wholly owned subsidiary of AIB, one of the two main Irish banks, with a high and resilient market share. It operates principally in Ireland with a limited, but focused overseas, presence, which includes the U.K.

The issuer's main purpose is to finance loans secured on residential property, in particular through the issuance of mortgage covered securities in accordance with the Irish Asset Covered Securities (ACS) Acts. The issuer may either grant these loans directly or purchase them from AIB and other members of the group or third parties.

Chart 1

AIB Mortgage Bank Covered Bond Program Structure

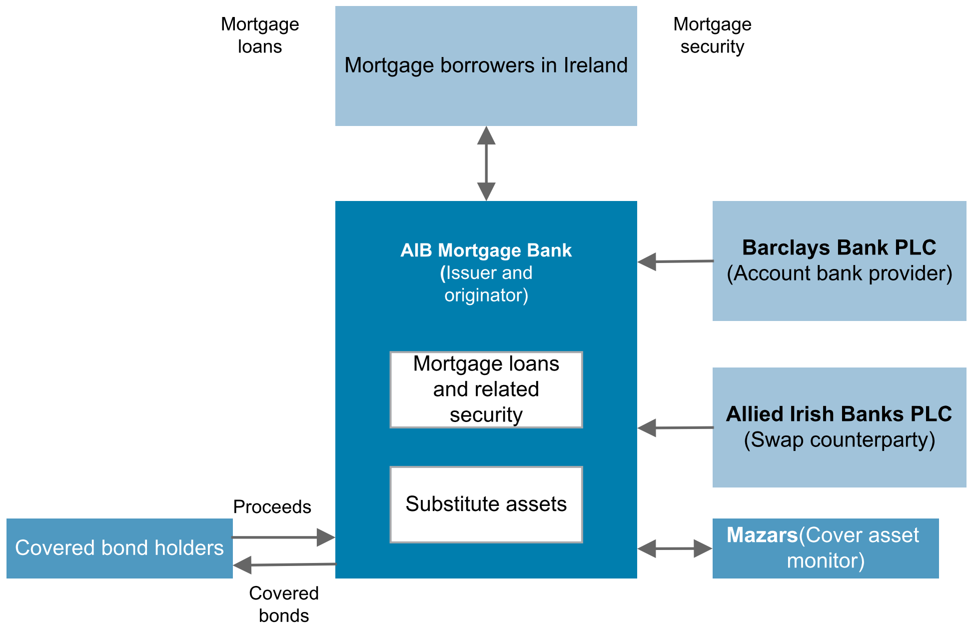

Table 2

Program Participants

Role	Name	Rating	Rating dependency
Issuer	AIB Mortgage Bank	NR	Yes
Originator	AIB Mortgage Bank	NR	No
Seller	Allied Irish Banks PLC	BBB/Positive/A-2	No
Servicer/cash manager/interest rate swap provider/covered bond swap provider	Allied Irish Banks PLC	BBB/Positive/A-2	No
Account provider	Barclays Bank PLC	A/Stable/A-1	Yes
Cover asset monitor	Mazars	NR	No

NR--Not rated.

Rating Analysis

Legal and regulatory risks

We base our legal analysis on our "Asset Isolation And Special-Purpose Entity Methodology," published on March 29, 2017 and our covered bonds criteria.

AIBMB's mortgage covered bonds benefit from the protection of specialist covered bond legislation under the Irish ACS Acts.

As an ACS issuer, AIBMB holds its cover pool assets on its balance sheet. Under the ACS Acts, the cover pool assets are ringfenced from the ACS issuer's other assets for the benefit of ACS holders. The cover pool assets along with any hedge contracts are registered in a cover register. The cover register may only be amended with the consent of the cover asset monitor.

ACS holders also benefit from a statutory preference created by the ACS Acts. ACS holders have recourse to cover pool assets ahead of all other non-preferred creditors. The ACS Acts further protect ACS holders by restricting the ACS issuer's business activities, in particular, by limiting the scope of non-core ACS activities. Hence, the ACS issuer cannot hold more than 15% of substitution assets (as opposed to mortgage assets and hedge contracts) in the cover pool.

Furthermore, if the ACS issuer becomes insolvent, all ACS issued remain outstanding and hedge contracts are not affected. We believe the Irish covered bond legal framework addresses legal risks outlined in our criteria. This enables us to assign ratings to the covered bonds that are above the long-term ICR on AIB. We have concluded that legal and regulatory risks do not constrain the covered bond ratings.

Our analysis incorporates the impact of the European Union's BRRD, applicable in the Republic of Ireland, in our determination of the RRL.

Operational and administrative risks

Our analysis of operational and administrative risks follows the guidelines in our covered bond ratings framework.

Based on information provided to us by the issuer, we believe the issuer's underwriting and servicing standards are prudent and aligned with the market standards. We therefore do not apply any analytical adjustments to account for operational and administrative risks.

Resolution regime analysis

The program has no structural features to fully mitigate asset-liability mismatch; the covered bonds ratings are therefore linked to the issuing bank's RRL, under our covered bonds criteria.

We assess the systemic importance for mortgage programs in the Republic of Ireland as very strong (see "Assessments For Jurisdictional Support According To Our Covered Bond Criteria," published on Nov. 3, 2017). Under our covered bonds criteria, this means the RRL can be two notches above the adjusted long-term ICR (adjusted by removing the uplift allocated to reflect extraordinary government support to the issuer, if any). This uplift recognizes that 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 in the event of a bank resolution. We consider this as an internal form of support, because the bail-in of certain creditors of the issuer does not required direct support from the government.

Under our group rating methodology, we consider the issuer to be a core entity of AIB. The long-term ICR on AIB incorporates no notches of sovereign support. We therefore assess the adjusted ICR as equal to the ICR at 'bbb' and derive the RRL at '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 mortgage programs in the Republic of Ireland is very strong. Under our covered bonds criteria, this means that the program can receive up to three notches of jurisdictional uplift over the RRL. However, the JRL cannot exceed the rating on the sovereign providing the support to the covered bond. Since the sovereign rating is that on the Republic of Ireland (A+/Stable/A-1), the JRL is therefore capped at 'a+'.

Collateral support analysis

We base our analysis on loan-by-loan data as of a cut-off date of March 31, 2018.

The pool comprises loans for Irish residential properties (see table 3).

Table 3

Cover Pool Composition

	As of March 31, 2018		As of March 31, 2017	
Asset type	**Value (mil. €)**	**Percentage of cover pool**	**Value (mil. €)**	**Percentage of cover pool**
Irish residential Mortgages	13,802	99.75	13,994	99.74
Cash	35	0.25	35	0.25
Total	13,837	100.00	14,030	100.00

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 WAFF, and our loss-estimate measure, the WALS. We base our loan level analysis of the AIB cover pool on our European residential loans criteria.

As of the cut-off date, the WAFF is 25.58% and the WALS is 31.97%, based on a 'AAA' stress level. Both the WAFF and the WALS have remained very stable since our previous analysis. The portfolio is well seasoned, has no excessive geographical concentration according to our criteria (see table 8), and has a very low level of arrears (see table 4).

Table 4

Key Credit Metrics

	As of March 31, 2018	As of March 31, 2017
Weighted-average LTV ratio (S&P stresses; %)	63.99	72.17
Weighted-average LTV ratio (investor report; %)	57.2	65.1
Weighted-average loan seasoning (months)*	94.18	92.48
Balance of loans in arrears (%)	0.09	0.11
Buy-to-let loans (%)	11.22	12.41
Credit analysis results:		
Weighted-average foreclosure frequency (WAFF; %)	25.58	26.93
Weighted-average loss severity (WALS; %)	31.97	32.2
AAA credit risk (%)	5.69	6.29

*Seasoning refers to the elapsed loan term. LTV--Loan to value.

Table 5

Loan Seasoning Distribution*

	As of March 31, 2018	As of March 31, 2017
Less than 18 months	12.66	10.69
18-24	3.71	3.20
24-36	6.02	5.13
36-48	4.78	3.89
48-60	3.62	4.24
60-72	3.89	2.80
72-84	2.54	5.14
84-96	4.74	9.16
96-108	8.35	11.89
108-120	10.86	11.89
More than 120	38.82	31.97
Weighted-average loan seasoning (months)	94.18	92.48

*Seasoning refers to the elapsed loan term.

Table 6

Original LTV Ratios

	As of March 31, 2018	As of March 31, 2017
(%)	Percentage of cover pool	
0-40	9.33	9.46
40-50	8.71	8.64
50-60	9.07	9.17
60-70	10.68	10.46
70-80	15.49	14.99
80-90	20.57	19.30
90-100	17.22	18.36
Above 100	8.93	9.62
Weighted-average OLTV ratios	79.09	79.59

LTV--Loan to value

Table 7

Indexed LTV Ratios (Percentage Of Cover Pool)

	As of March 31, 2018	As of March 31, 2017
0-60	44.9	35.5
60-70	14.4	13.1
70-80	13.9	13.0
80-90	11.0	12.7
90-100	7.91	9.4
Above 100	7.89	16.3
Weighted-average LTV ratios	63.99	72.2

LTV--Loan to value

Table 8

Geographic Distribution Of Loan Assets

	As of March 31, 2018	As of March 31, 2017
Top five concentrations	**Percentage of cover pool**	
Dublin	38.5	38.4
Cork	13.7	13.8
Galway	5.6	5.7
Kildare	5.3	5.2
Limerick	3.6	3.6
Total	66.7	66.8
Dublin	38.5	38.4
Outside Dublin	61.5	61.6

We apply our covered bonds criteria and our European residential loans criteria to analyze the cash flows in the transaction.

Our analysis of the covered bonds' payment structure determines that cash flows from the cover pool assets would be sufficient, at the current rating level, to make timely payment of interest and ultimate payment of principal to the covered bondholders.

As there is an active secondary market for Irish residential mortgages such as those found in the cover pool, the program can benefit from up to four notches of collateral-based uplift, according to our covered bonds criteria.

The bonds' maturities are extendible, which structurally mitigates liquidity risk on 99.13% of the bonds. While two covered bonds maturing in 2019 have no extendible features, in our view liquidity risk is mitigated by the cover pool's scheduled cash collection. The issuer has a public overcollateralization commitment of 22% in line with the current rating. As a result, we do not deduct notches from the potential collateral-based uplift for liquidity risk nor uncommitted overcollateralization.

We analyze the cash flows applying our credit stresses as determined in the credit section, as well as liquidity and interest rate stresses. We also run different default timing and prepayment patterns. For assessing market value risk, we apply a target asset spread in our cash flow analysis. We apply a spread of 1,000 basis points (bps) which reflects the Irish mortgage assets in the portfolio, as outlined in "Assessments For Target Asset Spreads According To Our Covered Bonds Criteria," published on Nov. 3, 2017.

The program benefits from swaps with AIB both on the assets and on the liabilities side. However, these do not reflect our current counterparty criteria. As our covered bond ratings are above the long-term ICR on the swap counterparty, we consider that the latter could default and leave the covered bond program unhedged from closing. Conversely, we also look at the case where the swap counterparty performs and look at the cash flows including the swaps. We then retain the most conservative output, which is the result of the scenario without the benefit of the swaps.

As of March 2018, the credit enhancement needed for coverage of 'AAA' credit risk is 5.69%. The target credit enhancement that is commensurate with the four notches of maximum collateral-based uplift is 21.23%. As of that date, the program's available credit enhancement is 84.75%, which exceeds the target credit enhancement, allowing the program to achieve four notches of collateral-based uplift, and therefore to reach a 'AAA' rating under our covered bonds criteria (see table 9). The target credit enhancement has remained stable compared with our previous review.

Table 9

Collateral Uplift Metrics

	As of March 31, 2018	As of July 13, 2017
Asset WAM (years)	10.71	10.76
Liability WAM (years)	5.72	5.78
Available credit enhancement	84.75	60.53
Required credit enhancement for first notch of collateral uplift (%)	9.58	10.03
Required credit enhancement for second notch of collateral uplift (%)	13.46	13.77
Required credit enhancement for third notch of collateral uplift (%)	17.35	17.51
Target credit enhancement for maximum uplift (%)	21.23	21.25
Potential collateral-based uplift (notches)	4	4
Adjustment for liquidity (Y/N)	N	N
Adjustment for committed overcollateralization (Y/N)	N	N
Collateral support uplift (notches)	4	4

WAM--Weighted-average maturity.

Counterparty risk

There are no counterparty risks in the program to constrain the program rating, in our opinion.

Liquidity risk on the bonds' interest payments arising from potential commingling risk is mitigated by amounts held with Barclays Bank PLC (A/Stable/A-1). This bank account has downgrade language that is in line with our current counterparty criteria. Therefore, commingling risk is effectively structurally mitigated at a level that is commensurate with the current ratings on the bonds.

AIB is the interest rate and covered bond swap counterparty, providing a hedge against mismatches between the interest rates on the assets and covered bonds. Based on our counterparty criteria, we do not believe a counterparty rated at the long-term rating level that we have assigned to AIB can mitigate counterparty risk in a structured finance transaction. Therefore, we model the transaction on an unhedged basis. As a result, we have accounted for interest rate mismatch risk in our total target credit enhancement for the maximum achievable rating on the covered bonds.

There are no foreign currency mismatches between the assets and liabilities in the program.

We analyze counterparty risk using our criteria "Counterparty Risk Analysis in Covered Bonds," published on Dec. 21, 2015 and "Counterparty Risk Framework Methodology And Assumptions," published on June 25, 2013.

Country risk

We assess country risk based on our criteria "Criteria - Structured Finance - General: Ratings Above The Sovereign - Structured Finance: Methodology And Assumptions," published on Aug. 8, 2016. Under these criteria, we consider that the assets in the pool, residential mortgages, have a moderate sensitivity to country risk. Of the bonds, 99.13% have a 12-month maturity extension feature and two private placements do not. In our view, the pool's scheduled cash collections mitigate the limited liquidity risk. We can therefore assign a jurisdictional-based uplift on the covered bonds' rating of up to four notches above the sovereign rating on Ireland (A+/Stable/A-1). Based on the current sovereign rating, the covered bonds can achieve a rating of up to 'AAA'.

Potential Effects Of Proposed Criteria Changes

Our ratings are based on our applicable criteria, including our "Covered Bonds Criteria," published on Dec. 9, 2014. However, the resolution regime analysis section of these criteria is under review (see "Request For Comment: Methodology For Incorporating The Effect Of Resolution Regimes Into Covered Bond Ratings," published on Jan. 31, 2017). As a result of this review, we may amend certain paragraphs of our covered bonds criteria. This change may affect the ratings on the outstanding covered bonds issued under this covered bond program. Until then, we will continue to rate and surveil these covered bonds using our existing criteria (see "Related Criteria").

Related Criteria

- Criteria - Structured Finance - General: Methodology And Assumptions: Assessing Pools Of European Residential Loans, Aug. 4, 2017
- Legal Criteria: Structured Finance: Asset Isolation And Special-Purpose Entity Methodology, March 29, 2017
- Criteria - Structured Finance - General: Ratings Above The Sovereign - Structured Finance: Methodology And Assumptions, Aug. 8, 2016
- Criteria - Structured Finance - Covered Bonds: Counterparty Risk Analysis In Covered Bonds, Dec. 21, 2015
- Criteria - Structured Finance - Covered Bonds: Covered Bond Ratings Framework: Methodology And Assumptions, June 30, 2015
- Criteria - Structured Finance - Covered Bonds: Covered Bonds Criteria, Dec. 9, 2014
- Criteria - Structured Finance - General: Counterparty Risk Framework Methodology And Assumptions, June 25, 2013
- Criteria - Structured Finance - General: Global Derivative Agreement Criteria, June 24, 2013
- General Criteria: Methodology: Credit Stability Criteria, May 3, 2010
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009

Related Research

- Ratings Affirmed On AIB Mortgage Bank's Mortgage Covered Bonds Following Review; Outlook Stable, July 31, 2018
- Allied Irish Banks PLC Upgraded To 'BBB/A-2' On Growing ALAC Buffer; Holding Company Ratings Affirmed; Outlook Positive, July 10, 2018
- Global Covered Bond Characteristics And Rating Summary Q2 2018, June 13, 2018
- Ireland 'A+/A-1' Ratings Affirmed; Outlook Remains Stable, June 1, 2018

- Covered Bonds Criteria Guidance, May 2, 2018
- Glossary Of Covered Bond Terms, April 27, 2018
- Assessments For Target Asset Spreads According To Our Covered Bond Criteria, Nov. 3, 2017
- Assessments For Jurisdictional Support According To Our Covered Bonds Criteria, Nov. 3, 2017
- Request For Comment: Methodology For Incorporating The Effect Of Resolution Regimes Into Covered Bond Ratings, Jan. 31, 2017