S&P Global Ratings

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Transaction Update: Bankia S.A. (Mortgage Covered Bonds)

Primary Credit Analyst:
Marta Escutia, Madrid + 34 91 788 7225; marta.escutia@spglobal.com

Research Contributor:
Nidhi Nair, CRISIL Global Analytical Center, an S&P affiliate, Mumbai

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Ratings Detail

Reference Rating Level	a-
Resolution Regime Uplift	+2
Systemic Importance	Very Strong
Resolution Counterparty Rating	BBB+
Issuer Credit Rating	BBB

+

Jurisdiction-Supported Rating Level	a
Assigned Jurisdictional Support Uplift	1
Jurisdictional Support Assessment	Very Strong
Legal Framework	Very Strong
Systemic Importance	Very Strong
Sovereign Credit Capacity	Very Strong

+

Maximum Achievable Covered Bond Rating	aa
Collateral Support Uplift	+3
Overcollateralization Adjustment	-1
Liquidity Adjustment	0
Potential Collateral Based Uplift	+4

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Covered Bond Rating	
AA/Negative	
Rating Constraints	aa+
Counterparty Risk	aaa
Country Risk	aa+

Major Rating Factors

Strengths

- Available credit enhancement that is well above the target credit enhancement required to achieve a 'AA' rating.
- Prudent underwriting and servicing standards since the restructuring process began.
- The program benefits from two unused notches of uplift above the issuer credit rating.

Weaknesses

- Although decreasing, there is still a relatively high percentage of restructured loans, which we consider to have a higher probability of default.
- The balance of defaulted loans in the non-residential pool is still high, albeit reducing.
- The Spanish real estate market shows signs of overvaluation, in our view.

Outlook

S&P Global Ratings' negative outlook on its credit ratings on the mortgage covered bonds ("cédulas hipotecarias" or CHs) issued by Spain-based Bankia S.A. (BBB/Watch Pos/A-2; Bankia) reflects the negative outlook on the long-term sovereign credit ratings on Spain (unsolicited; A/Negative/A-1). This means that, all else being equal, a one-notch rating action on the sovereign would result in a similar rating action on the covered bonds.

Rationale

We are publishing this transaction update as part of our periodic review of Bankia's mortgage covered bond program.

In our analysis, we assume the issuer's insolvency and look to the resolution regime, the jurisdictional support, and the cover pool to repay the covered bonds. Our ratings reflect the likelihood of the covered bonds being repaid in a timely manner on their legal final maturity.

From our analysis of the legal and regulatory framework for covered bonds in Spain, we have concluded that the assets in Bankia's cover pool are isolated from the risk of a bankruptcy or insolvency of the issuer. This asset isolation allows us to assign a higher rating to the covered bond program than the long-term issuer credit rating (ICR) on Bankia.

Bankia is domiciled in Spain, which is subject to the EU's Bank Recovery and Resolution Directive (BRRD). We assess the systemic importance of covered bonds in Spain as very strong, under our "Assessments For Jurisdictional Support According To Our Covered Bonds Criteria," published on Nov. 27, 2020. These factors increase the likelihood that Bankia 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 rating reference level (RRL) as 'a-'.

We then consider the likelihood for the provision of jurisdictional support, which we assess as very strong for mortgage covered bonds in Spain. This could result in a potential uplift from the RRL of up to three notches under our covered bonds criteria. The support is capped at the long-term rating on the sovereign. Given that the RRL is 'a-' and the unsolicited long-term sovereign rating on Spain is 'A', the covered bonds benefit from one notch of jurisdictional-support uplift. Therefore, we assess a jurisdiction-supported rating level (JRL) at 'a', one notch above the RRL.

We have reviewed the stratified data asset information provided as of June 30, 2020 and the liabilities as of Sept. 30, 2020. The available credit enhancement in the program continues to support the four potential notches of collateral-based uplift above the JRL. However, we have deducted one notch from the potential uplift because there is no public commitment from the issuer to maintain a level of collateral that is commensurate with the current ratings on the covered bonds. As a result, the maximum potential rating on the program is 'aa' according to our covered bonds criteria.

There are currently no rating constraints for the covered bonds that relate to counterparty, legal, administrative, and operational risks.

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

Program Description

Table 1

Program Overview*	
Jurisdiction	Spain
Year of first issuance	2011
Covered bond type	Legislation-enabled
Outstanding covered bonds (bil. €)	23.5
Redemption profile	Hard bullet
Underlying assets	Residential and commercial mortgages
Jurisdictional support uplift	1
Unused notches for jurisdictional support	2
Target credit enhancement (%)	39.64
Available credit enhancement (%)	179.13
Collateral support uplift	3
Unused notches for collateral support	0
Total unused notches	2

*Based on portfolio data as of June 30, 2020 as reported by the issuer, and liabilities as of Sept. 30, 2020.

Bankia is one of the major Spanish banks resulting from the merger of seven Spanish savings banks in May 2011. In December 2012 it transferred certain problematic assets to SAREB, the Spanish bad bank.

Bankia established its mortgage covered bond program in 1999 (as Caja Madrid at that time), and we first rated it in 2011 as Bankia and since 2008 as Caja Madrid.

The covered bonds are regulated by Spanish law, which requires, among other things, minimum overcollateralization of 25% over the eligible mortgage book. Moreover, if the issuer becomes insolvent, covered bond holders have preferential rights to the entire pool of mortgage assets assigned to the covered bonds as collateral.

Table 2

Program Participants

Role	Name	Rating	Rating dependency
Issuer	Bankia S.A.	BBB/Watch Pos/A-2	Yes
Arranger, bank account provider, loan originator, servicer, and paying agent	Bankia S.A.	BBB/Watch Pos/A-2	No

Rating Analysis

Legal and regulatory risks

In our view, the Spanish covered bond framework sufficiently addresses the relevant legal aspects of our covered bonds criteria. This enables us to assign ratings to Spanish mortgage covered bonds (CHs) that exceed the long-term ICR on the issuer.

Spain's legal framework for covered bonds comprises seven main laws. Law 2/1981 (The Mortgage Market Law) and its development into Law 716/2009 (Mortgage Market Regulation) restrict covered bond issuance to regulated financial institutions such as commercial and savings banks. There are five laws regarding issuer insolvency: Law 26/1988 (Discipline And Intervention of Credit Institutions), Law 22/2003 (Spanish Insolvency Act), Law 6/2005 (Reorganization And Winding-Up of Credit Institutions), Law 9/2012 (the Restructuring And Resolution of Credit Institutions Act), and Law 11/2015 (Recovery And Resolution Of Credit Institutions And Investment Firms).

CHs provide investors with primary recourse to the issuer, which is responsible for full and timely payments as long as it is not in default. If the issuer were to default, the CH holders would be privileged creditors with a claim on all non-securitized or unencumbered mortgage loans on the issuer's balance sheet.

Under Spanish law, the issuer must maintain overcollateralization of at least 25%, and only loans meeting certain requirements can be included in the overcollateralization calculation. Eligible loans must be, among other things, loans guaranteed by a first-ranking mortgage and have a loan-to-value (LTV) ratio of below 80% for residential mortgages (or 60% for commercial mortgages). In addition, under the law, an official appraiser must have valued the mortgaged property.

Our legal analysis is based on "Structured Finance: Asset Isolation And Special-Purpose Entity Methodology," published on March 29, 2017, and "Covered Bond Ratings Framework: Methodology And Assumptions," published on June 30, 2015.

Operational and administrative risks

Bankia is a listed Spanish financial institution. With €209.5 billion in assets as of March 2020, it is the fourth-largest financial institution in Spain by total domestic assets, with nationwide market shares of about 12% in loans and 11% in deposits. Its main business segments are retail banking, business banking, and the corporate center.

Bankia's risk management has been completely revamped since its bailout in 2012, and its credit risk culture has strengthened throughout the organization.

In September 2020, CaixaBank S.A. and Bankia S.A.'s boards agreed an all-share merger that they expect will close in the first quarter of 2021. Upon completion, Bankia will be absorbed by CaixaBank and all of its assets and liabilities will be transferred to the acquiring entity. As a result, we placed our long-term rating on Bankia on CreditWatch with positive implications (see "Spain-Based CaixaBank Affirmed As Merger With Bankia Announced; Bankia Placed On CreditWatch Positive," published on Sept. 24, 2020).

We view Bankia's current underwriting criteria as prudent, although it may not have been so in the past, as shown by the high level of delinquencies and restructurings in Bankia's balance sheet during the crises.

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

Under the covered bonds law, if the bank becomes insolvent, an administrator will be appointed to manage the mortgage book. This administrator will be required to actively manage the cover pool assets and to ensure the timely payment of the covered bonds. We believe the issuer will find an administrator, given that the type of assets to be managed is common in Spanish financial institutions.

Our analysis of operational and administrative risks follows the principles laid out in our covered bond ratings framework criteria.

Resolution regime analysis

Bankia is domiciled in Spain, which is subject to the EU's BRRD. We assess the systemic importance for Spanish mortgage covered bonds as very strong (see "Assessments For Jurisdictional Support According To Our Covered Bonds Criteria," published on Nov. 27, 2020). Under our covered bonds criteria, this means the RRL will be the greater of (i) the ICR on the issuing bank, plus two notches; and (ii) the resolution counterparty rating (RCR) on the issuing bank, where applicable. As the ICR on Bankia is 'BBB' and the RCR is 'BBB+', the resulting RRL is 'a-', two notches above the ICR.

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. This is 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. This increases the likelihood that Bankia would continue servicing its covered bonds without accessing the cover pool or receiving jurisdictional support, even if it were to face insolvency.

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. Under our assessments for jurisdictional support under our criteria, the expected jurisdictional support for Spanish covered bonds is very strong. Under our covered bonds criteria, this means that the program can receive up to three notches of jurisdictional uplift above the RRL. However, the jurisdictional support is capped at the long-term rating on the sovereign. As Bankia's RRL is 'a-' and the unsolicited long-term sovereign rating on Spain is 'A', the covered bonds benefit from one notch of jurisdictional-support uplift. Therefore, we assess a jurisdiction-supported rating level (JRL) at 'a', one notch above the RRL.

Collateral support analysis

We base our analysis on stratified mortgage book data as of June 30, 2020.

We analyze the portfolio's credit quality by applying our European residential loans criteria, applying the specific assumptions for Spain, and our criteria for analyzing European commercial real estate collateral in covered bonds (see "Methodology And Assumptions: Assessing Pools Of European Residential Loans," published on Aug. 4, 2017, and "Analyzing European Commercial Real Estate Collateral In European Covered Bonds," published on March 31, 2015).

For our analysis, we have excluded defaulted loans (more than one year past due), due to uncertainty regarding their future performance. We have also excluded mortgage loans backed by land, due to uncertainty regarding their valuation. In addition, we took loans granted to Bankia employees into account when adjusting the cover pool, due to the risk of these loans being set off if the issuer were to become insolvent. We also deduct a small volume of loans granted outside Spain as we do not have detailed information to perform our credit analysis on these loans. We therefore also reduced the corresponding collateral in our cash flow model, but included expected recoveries on defaulted assets.

We have analyzed aggregate data from the issuer and applied stresses that are commensurate with a 'AAA' rating scenario to estimate the level of defaults. In doing so, we use the following measures: our risk measure, the weighted-average foreclosure frequency (WAFF), and our loss estimate measure, the weighted-average loss severity (WALS).

The cover pool comprises residential (88.40%) and nonresidential or commercial mortgage loans (11.60%) after adjustments. The portfolio composition has remained stable since 2019, with relatively high seasoned loans and decreasing ratios of restructured mortgages.

The portfolio WAFF has decreased to 25.65% from 28.26% mainly due to the decrease in the WAFF of commercial assets due to the improvement in our BICRA economic risk assessment for Spain and the overall decrease in the share of restructured loans. The WALS has decreased to 35.48% from 39.49% mainly due to the cover pool now being concentrated in lower current LTV buckets.

Tables 3 to 7 summarize the cover pool's composition, and table 8 summarizes the results of our cash flow analysis.

Table 3

Cover Pool Composition

	--As of June 30, 2020--		--As of June 30, 2019--	
Asset type	Value (mil. €)	Percentage of cover pool (%)	Value (mil. €)	Percentage of cover pool (%)
As reported by the issuer				
Residential	57,279	87.37	61,094	87.56
Non-residential	8,282	12.63	8,682	12.44
Total	65,561	100.00	69,776	100.00
After our adjustments*				
Residential	55,230	88.40	57,817	88.57
Non-residential	7,244	11.60	7,464	11.43
Total	62,474	100.00	65,281	100.00

*Balance net of defaults, land, employee loans, and loans granted outside Spain.

Table 4

Key Credit Metrics

	--As of June 30, 2020--			--As of June 30, 2019--		
	Residential	**Non-residential**	**Total**	**Residential**	**Non-residential**	**Total**
Weighted-average original LTV ratio (%)	70.23	N/A	N/A	70.19	N/A	N/A
Weighted-average LTV ratio (%) reported	55.22	62.00	56.01	57.47	61.83	57.97
Weighted-average LTV ratio (%)*	56.47	54.52	56.24	59.10	55.20	58.65
Weighted-average loan seasoning (months)	117.01	77.21	112.39	116.30	76.77	111.78
Loans in arrears over 30 days to 90 days (%)§	1.35	1.24	1.34	1.23	1.30	1.24
Loans in arrears over 90 days to 360 days (%)§	0.82	1.24	0.87	0.84	0.95	0.85

Table 4

Key Credit Metrics (cont.)

	--As of June 30, 2020--			--As of June 30, 2019--		
	Residential	**Non-residential**	**Total**	**Residential**	**Non-residential**	**Total**
Defaults (%)	1.85	9.56	2.74	3.67	10.88	4.49
Restructured (%)	5.98	24.57	8.14	8.63	26.75	8.37
Second or higher-ranking mortgage (%)	1.91	N/A	1.69	2.20	N/A	1.95
Second homes (%)	6.72	N/A	5.94	6.69	N/A	5.93
Buy-to-let (%)	8.91	N/A	7.88	9.52	N/A	8.43
Self employed (%)	14.98	N/A	13.24	15.39	N/A	13.63
Non-Spanish citizens (%)	2.01	N/A	1.78	2.04	N/A	1.81
Credit analysis results:						
WAFF (%)	22.21	51.91	25.65	24.15	60.10	28.26
WALS (%)	32.46	45.32	35.48	38.68	45.77	39.49

*LTV ratios are calculated after adjusting valuations for fluctuations in house prices. §Arrears % calculated net of defaults. LTV--Loan-to-value. N/A--Not applicable or not available. WAFF--Weighted-average foreclosure frequency. WALS--Weighted-average loss severity.

Table 5

Original Loan-To-Value Ratios

	--As of June 30, 2020--	--As of June 30, 2019--
(%)	**Residential (%)**	
0-60	24.74	24.82
60-70	15.55	15.32
70-80	29.99	29.41
80-90	17.24	17.66
Above 90	12.48	12.79
Weighted-average loan-to-value ratio	70.23	70.19

Table 6

Loan Seasoning Distribution*

	--As of June. 30, 2020--			--As of June. 30, 2019--		
	Residential (%)	**Non-residential (%)**	**Total (%)**	**Residential (%)**	**Non-residential (%)**	**Total (%)**
Less than 24 months	11.23	21.47	12.42	10.65	20.52	11.78
24-36	4.12	9.88	4.78	3.15	10.48	3.99
36-48	3.15	9.79	3.92	3.35	8.56	3.95
48-60	3.31	7.27	3.77	3.42	8.04	3.95
60-72	3.27	7.05	3.71	3.79	6.85	4.14
72-84	3.62	5.86	3.88	4.41	5.41	4.52
84-96	4.12	4.53	4.17	3.66	3.82	3.68

Table 6

Loan Seasoning Distribution* (cont.)

	--As of June. 30, 2020--			--As of June. 30, 2019--		
	Residential (%)	**Non-residential (%)**	**Total (%)**	**Residential (%)**	**Non-residential (%)**	**Total (%)**
96-108	3.48	3.35	3.47	5.12	4.37	5.03
108-120	4.92	3.75	8.28	6.19	8.04	
More than 120						

*Seasoning refers to the elapsed loan term. Loans in arrears do not receive seasoning credit in our analysis, and are assumed to be in the 0-24 months bucket.

Geographic Distribution Of Loan Assets

Table 7

	--As of June 30, 2020--			--As of June 30, 2019--		
Top five concentrations	**Residential (%)**	**Non-residential (%)**	**Total (%)**	**Residential (%)**	**Non-residential (%)**	**Total (%)**
Madrid	28.07	22.07	27.37	27.49	21.05	26.75
Valencia	15.66	15.27	15.61	15.88	15.85	15.88
Catalonia	12.24	12.54	12.27	12.54	12.60	12.55
Andalucia	13.56	15.86	13.83	13.70	14.58	13.80
Balearic Islands	6.13	9.87	6.56	5.97	10.12	6.44
Others	24.34	24.39	24.35	24.42	25.80	24.58
Total	100.00	100.00	100.00	100.00	100.00	100.00

Table 8

Collateral Uplift Metrics

	September 2020 Analysis	**September 2019 Analysis**
Asset WAM (years)	19.84	19.70
Liability WAM (years)	5.28	5.68
Available credit enhancement (%)*	168.91	155.3
'AAA' credit risk (%)	26.34	31.55
Required credit enhancement for first notch of collateral uplift (%)	26.34	31.55
Required credit enhancement for second notch of collateral uplift (%)	32.99	36.57
Required credit enhancement for third notch of collateral uplift (%)	36.32	39.08
Target credit enhancement for maximum uplift (%)	39.64	41.59
Potential collateral-based uplift (notches)	4	4
Adjustment for liquidity (Y/N)	N	N
Adjustment for committed overcollateralization (Y/N)	Y	Y
Collateral support uplift (notches)	3	3

WAM--Weighted-average maturity. *After our adjustments.

Our analysis of the covered bond program's payment structure shows that cash flows from the cover pool assets would be sufficient, at the given rating, to pay the covered bond holders interest and principal.

The covered bonds are exposed to refinancing risk because asset and liability mismatches are not addressed by structural features, such as pass-through liabilities or committed liquidity arrangements. For assessing market value risk, we applied a target asset spread in our cash flow analysis. We applied a spread of 735 basis points, which reflects the mix of residential and nonresidential loans in the mortgage book, as outlined in "Assessments For Target Asset Spreads According To Our Covered Bonds Criteria," published on Nov. 27, 2020.

By applying our credit and cash flow stresses, we calculate a target credit enhancement of 39.64% (based on asset information provided as of June 30, 2020 and liabilities as of September 2020). This is lower than in our 2019 analysis (41.59%) mainly due to the lower expected losses on the cover pool and the decrease in the average coupon on the covered bonds. The target credit enhancement is below the available credit enhancement of 168.91% (after we made our adjustments).

As a result, and because there is an active secondary market for Spanish mortgages such as the ones in the cover pool, the program can potentially benefit from up to four notches of collateral-based uplift from the JRL under our covered bonds criteria.

We have lowered the potential collateral-based uplift to three notches due to the issuer's lack of commitment to maintain overcollateralization at a level that supports the ratings on the covered bonds.

However, we have not adjusted to account for liquidity not being covered for the next six months because we have already adjusted for refinancing risk not being fully covered by limiting the maximum number of notches of uplift above the unsolicited long-term sovereign rating on Spain.

As a result, the target credit enhancement is also the level commensurate with the three notches of collateral-based uplift above the JRL of 'a'. As the available credit enhancement is higher than the target credit enhancement, the maximum achievable rating for these covered bonds is under our covered bonds criteria is 'aa'.

Counterparty risk

We analyze counterparty risk by applying our current counterparty criteria (see "Counterparty Risk Framework: Methodology And Assumptions," published on March 8, 2019).

The program's only counterparty is Bankia, in its role as bank account provider.

In our view, the Spanish legal framework mitigates bank account risk and commingling risk in covered bond transactions when the issuer is the bank account provider. As such, counterparty risk does not constrain our ratings on Bankia's mortgage covered bonds.

Sovereign risk

Under our structured finance ratings above the sovereign criteria, covered bonds issued in a jurisdiction that is within a monetary union that do not include structural coverage of refinancing need over a 12-month period to exhibit moderate sensitivity to country risk (see "Incorporating Sovereign Risk In Rating Structured Finance Securities: Methodology And Assumptions," published on Jan. 30, 2019). As a result, we can rate these covered bonds up to four notches above the sovereign rating. This is provided that the covered bonds have sufficient overcollateralization to withstand a sovereign default.

Bankia's mortgage covered bonds' available overcollateralization is sufficient to cover our sovereign default stress scenario. Therefore, considering our unsolicited current long-term sovereign foreign currency rating on Spain, the covered bonds can achieve a rating of up to 'AA+' under our structured finance sovereign risk criteria.

Potential Effects Of COVID-19

S&P Global Ratings believes there remains a high degree of uncertainty about the evolution of the coronavirus pandemic. Reports that at least one experimental vaccine is highly effective and might gain initial approval by the end of the year are promising, but this is merely the first step toward a return to social and economic normality; equally critical is the widespread availability of effective immunization, which could come by the middle of next year. We use this assumption in assessing the economic and credit implications associated with the pandemic (see our research here: www.spglobal.com/ratings). As the situation evolves, we will update our assumptions and estimates accordingly.

Potential Effects Of Proposed Criteria Changes

Our ratings are based on our applicable criteria, including our "Methodology And Assumptions: Assessing Pools Of European Residential Loans," published on Aug. 4, 2017. However, these criteria are under review (see "Global Methodology And Assumptions: Assessing Pools Of Residential Loans (Spain, Portugal, Italy, And Greece)," published on Oct. 30, 2020. As a result of these reviews, we may amend our analysis of a portfolio's credit quality if the program is domiciled in one of the above jurisdictions. These changes may affect the ratings on the outstanding covered bonds issued under this covered bond program. Until this time, we will continue to rate and surveil these covered bonds using our existing criteria (see "Related Criteria").

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
- Covered Bond Ratings Framework: Methodology And Assumptions, June 30, 2015
- Analyzing European Commercial Real Estate Collateral In European Covered Bonds, March 31, 2015
- Covered Bonds Criteria, Dec. 9, 2014
- Credit Stability Criteria, May 3, 2010
- Use Of CreditWatch And Outlooks, Sept. 14, 2009

Related Research

- Assessments For Jurisdictional Support According To Our Covered Bonds Criteria, Nov. 27, 2020
- Assessments For Target Asset Spreads According To Our Covered Bonds Criteria, Nov. 27, 2020

- Covered Bonds 2021 Outlook: Policy Intervention Is Reshaping The Role Of Covered Bonds, Nov. 26, 2020
- Comments Requested On Proposed Expansion Of The Global RMBS Criteria To Include Spain, Portugal, Italy, And Greece, Oct. 31, 2020
- Spain-Based CaixaBank Affirmed As Merger With Bankia Announced; Bankia Placed On CreditWatch Positive, Sept. 24, 2020
- Spain Outlook Revised To Negative From Stable On Mounting Fiscal and Structural Challenges; Affirmed At 'A/A-1', Sept. 19, 2020
- Global Covered Bond Characteristics And Rating Summary Q3 2020, Sept. 17, 2020
- Global Covered Bond Insights Q3 2020, Sept. 17, 2020
- Banking Industry Country Risk Assessment: Spain, June 18, 2020
- Spanish Covered Bond Market Insights 2020, Jan. 29, 2020
- S&P Global Ratings' Covered Bonds Primer, June 20, 2019
- Glossary Of Covered Bond Terms, April 27, 2018