FitchRatings

Fitch Upgrades Caja Rural de Granada's Mortgage Covered Bonds

06 MAY 2022 2:52 PM

Fitch Ratings - Madrid - [publication date will be automatically inserted]
Fitch Ratings has upgraded Caja Rural de Granada S.C.C.'s (CRG) mortgage covered bonds (Cédulas Hipotecarias, CH) to 'A+' from ‘A’ with a Stable Outlook. The issuer is a rural cooperative bank established in the Spanish region of Andalusia.

CRG's single outstanding CH issuance is an EUR600 million fixed-rate covered bond, with a remaining maturity of around six years and hard-bullet amortisation profile.

KEY RATING DRIVERS

Mirroring Bank Rating Action: As the CH programme uses all notches of uplift from the issuer rating, the upgrade of the CH rating mirrors that on CRG’s Long-Term Issuer Default Rating (IDR), which Fitch monitors privately. The Stable Outlook on the CH rating mirrors the Outlook on CRG's IDR.

Uplifts: The CH rating is driven by the first-ranking rights of CH holders against the entire unencumbered mortgage book of the issuer, the CH exemption from bail-in in a resolution scenario, and the outstanding recovery prospects in the event of a CH default due to the large over-collateralisation (OC) provided by the cover pool.

The resolution uplift reflects Spain's implementation of the EU Bank Recovery and Resolution Directive, which foresees the bail-in of senior bank’s liabilities and explicitly exempts fully collateralised covered bonds from bail-in. It also considers that a resolution of CRG, should it happen, is not likely to result in the direct enforcement of the recourse against the cover pool.

Fitch's payment continuity uplift is derived from the lack of liquidity protection for CH upon a default of their issuer. The CH have a hard bullet maturity whereas the cover pool has an amortising redemption profile. Therefore, collections from the cover pool may not allow for timely payment of CH once the source of interest and principal payments shifts from the issuer to the cover pool.

Fitch has granted a recovery uplift to the programme as the agency did not identify any material downside risk to recovery expectations. Assets and liabilities are both euro-denominated.

OC Protection

In its analysis, Fitch relies on an OC of 193% as of December 2021, equal to the minimum OC of the past 12 months minus a haircut. The relied-upon OC significantly exceeds Fitch's 'A+' break-even OC of 16.5%, which corresponds to the credit loss for CRG's CH rounded to the nearest 0.5%. In a 'A+' stress scenario, Fitch calculated a lifetime default and recovery rate on the cover pool of 28.2% and 49.8%, respectively.

ESG Risks - Governance

The CH have an Environmental, Social and Governance (ESG) Relevance Score of '5' for Transaction and Collateral Structure, due to the absence of liquidity protection. This results in a narrower uplift of the CH rating than if a dedicated liquidity mechanism was in place for the timely payment of interest and principal. The liquidity mechanism is important to ensure a smooth transition to interest and principal payments arising from the cover pool rather than the issuer. Fitch therefore rates the CH programme on a recovery basis approach and does not test for timely payment on the CH.

RATING SENSITIVITIES

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

- An upgrade of the bank's IDR would lead to an equivalent upgrade of the CH due to a direct link between the CH rating and the issuing bank Long-Term IDR, subject to OC sufficiency.

- The implementation by 8 July 2022 of the law transposing the EU Covered Bonds Directive into Spanish legislation, which introduces dedicated liquidity protection in the form of mandatory liquid assets covering the net cumulative outflow over a 180-day period, and optional soft bullet principal redemption. However, any rating uplift will depend on the final terms of the law and OC being sufficient to support the stresses of higher rating scenarios

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

- A downgrade of the bank's IDR would lead to an equivalent downgrade of the CH.

- The CH would be downgraded if the lifetime projected credit loss on the cover pool is not fully compensated by the OC Fitch relies upon. We view this scenario as highly remote, although we note that the EU Directive implementation in Spain is likely to lead to lower relied upon OC for the programme.

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

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.

PUBLIC RATINGS WITH CREDIT LINKAGE TO OTHER RATINGS

The CH rating is driven by the credit risk of the issuer as measured by CRG's Long-Term IDR.

ESG CONSIDERATIONS

CRG CH has an ESG Relevance Score of '5' for Transaction & Collateral Structure.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

RATING ACTIONS

ENTITY	RATING		
Caja Rural de Granada, Sociedad Cooperativa de Credito			
senior secured, Mortgage Covered Bonds, Cedulas Hipotecarias	LT	A+ ⦿	Upgrade

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Applicable Criteria
Bank Rating Criteria (pub.12-Nov-2021)(includes rating assumption sensitivity)
Covered Bonds Rating Criteria (pub.02-Jun-2021)(includes rating assumption sensitivity)
Multi-Issuer Cedulas Hipotecarias Rating Criteria (pub.19-Oct-2021)(includes rating assumption sensitivity)
Structured Finance and Covered Bonds Country Risk Rating Criteria (pub.28-Oct-2021)
Structured Finance and Covered Bonds Interest Rate Stresses Rating Criteria (pub.20-Sep-2021)

Applicable Models
MICH Model, v4.37.0 (1 (https://www.fitchratings.com/site/re/1003369))

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