Request for Comment: Approach to Determining the Issuer Anchor Point for Covered Bond Ratings

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RFC and Background

- On 19 September, Moody's published a Request for Comment on "***approach for determining the issuer anchor point for Covered Bonds***"
- **Background**:
  - EU Council/ECOFIN announcement and draft Directive, 27 June 2013.
  - Covered bonds clearly excluded from bail-in
  - Strong expectation that bail-in tool will be used in conjunction with bank resolution under the Directive

= Sufficient certainty to propose an initial methodology adjustment

The RFC Proposal

- The probability of *issuer default* is the starting point (*anchor point*) for all our covered bond ratings.
- **Current anchor point**: the issuer's/supporting entity's senior unsecured debt/deposit rating (SUR)
- The revised anchor point is relevant to both our Expected Loss (EL Model) and TPI Framework:
  - Under our Expected Loss modelling => *EL (covered bonds)* = *PD (issuer)* x *cover pool losses.*
  - Under our TPI Framework => CB rating typically capped at the level indicated by our TPI table, depending on (1) issuer rating and (2) TPI assigned to programme.

- The **new anchor point** for covered bond ratings would be the higher of:

  (a) the issuer's adjusted BCA + 0-2 notches; or

  (b) the issuer's SUR + 1 notch

  with the number of notches depending on the level of unsecured debt / total liabilities.

  Exception: SUR+0 where very material government support already incorporated.

Scope and Impact of the RFC

» Final methodology will be based on RFC, after review of comments received.

» RFC is an initial, interim step – there remain many uncertainties around implementation of bank resolution.

» Initial impact on ratings would affect CB rated

(a) below Aaa and

(b) below country ceiling.

In addition, OC levels will be affected.