A report by the Spanish Mortgage Association

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Analysing the Spanish mortgage pool Q3 2018

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1. Preliminary comments

This report presents an update of the data and analysis published by the Spanish Mortgage Association (AHE) in July 2018 (which contained data up to March 2018). The aim of this report is to provide stakeholders with an outlook of the composition and of the main features of Spanish credit institutions' total mortgage pool.

The figures analysed comprise data from 14 credit institutions[1] that issue covered bonds (*cédulas hipotecarias*) with a Covered Bond Label[2] by the European Covered Bond Council (ECBC).

The data were gathered from the information published by each institution on their corporate websites relating to the cover pool backing their covered bond issues. As a member of the ECBC, the Spanish Mortgage Association manages part of the publication process of this information as well as the definition of different concepts. Thus, all the variables presented in this analysis are subject to a homogeneous definition.

This short assessment offers interesting information on the Spanish mortgage pool profile, which can be useful for further analysis and decision making. Its content may be quoted and reproduced with specific reference to the Spanish Mortgage Association.

[1] *Banco Sabadell, Bankia, Caixabank, Banco Santander, Kutxabank, Unicaja Banco, Banco Popular, BBVA, Bankinter, Ibercaja Banco, Eurocaja Rural-Caja Rural Castilla-La Mancha, Caja Rural de Navarra, Abanca and Cajamar.*

[2] *https://coveredbondlabel.com/*

2. Fundamental data of the cover pool

As of September 2018, the mortgage pool under analysis[3], which represents more than 93% of the total national outstanding mortgage lending[4] -not including on-balance and off-balance residential mortgage backed securities RMBS-, has increased by 3.5%, from EUR 468.79 bn in March 2018 to **EUR 485.22 bn** in September 2018. This increase can be explained by both the growing importance of the ECBC Label, with the incorporation of new entities, and also by the mergers and acquisitions (M&As) carried out over the last quarter, which generate larger-sized balance sheets.

In accordance to this, the cover asset pool includes **5,670,693 loans** in September 2018, compared to 5,382,811 loans reported in July 2018 (an increase near to 5.4%).

In general, the average loan size of the aggregate pool maintained a downward trend over the last quarters, setting its value at **EUR 87,696** in September 2018.

Since the last analysis published in July 2018 the weighted average LTV ratio (non indexed) remained constant, at 57.6%.

Table 1

General information	
Outstanding lending (EUR million)(*) (**)	520.319
HTT portfolio (EUR million)	485.216
Size of portfolio	93,3%
Residential	79,0%
commercial	21,0%
number of loans	5.670.693
Average amount (EUR)	87.696
Average residential (EUR)	75.894
Average commercial (EUR)	210.888
Weighted average life (in years)	15,0
Average weighted LTV	57,6%

(*) Not including RMBs

(**) Last available data corresponds to March 2017

Source: Spanish Mortgage Association

[3] *The data analysed is dated to September 2018 except for 4 institutions (which represent 34,2 % of the cover pool) with data as of June 2018.*

[4] *The outstanding value is dated to March 2017 since it is the latest available.*

3. Property type information

According to the type of collateral, around 79.0% of the analysed pool -taking into account the size of each entity- is made up of residential properties[5], while the remaining 21.0% is secured by commercial lending [6].

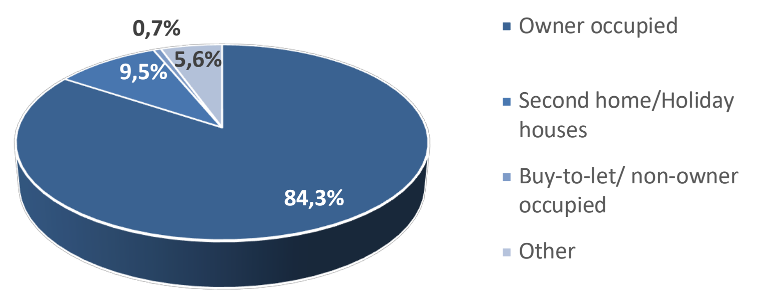
Table 2

Property type	
Residential	79,0%
Maximum in pool	87,8%
Minimum in pool	63,0%
Comercial	21,0%
Maximum in pool	37,0%
Minimum in pool	12,2%

Source: Spanish Mortgage Association

Within the residential segment, 84.3% of residential loans were guaranteed by primary residence; 9.5% by second or vacation homes, 0.7% by buy-to-let houses and the remaining 5.6% by other residential properties of a different nature.

Chart 1: Residential property composition



Source: Spanish Mortgage Association

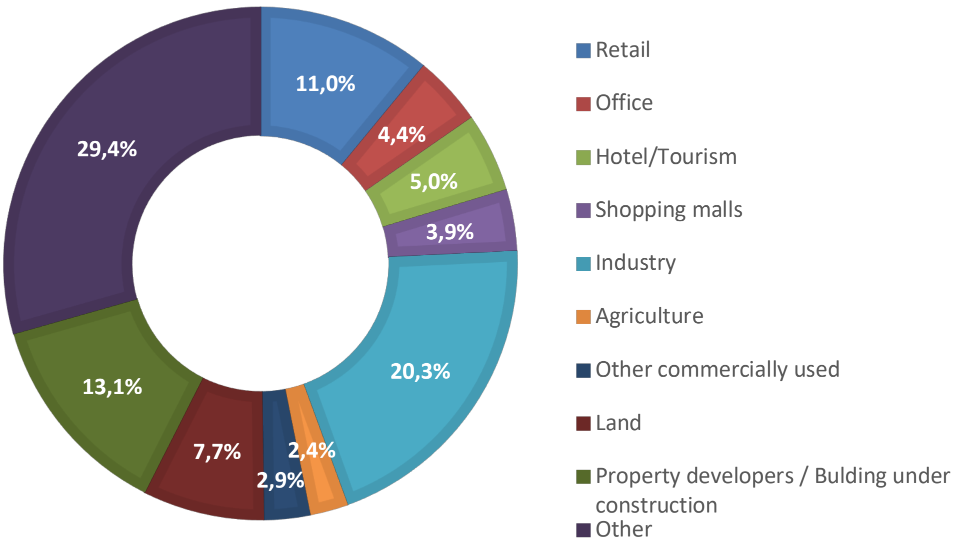
[5] *Residential loans meet the following criteria: loans that are full recourse to the individual taking out the loan; and either (a) loans secured against a residential property in which the borrower resides or b) where the borrower rents out less than four properties.*
[6] *Commercial loans are loans backed by a mortgage and which have recourse to a borrower excluding individuals and public-sector entities.*

With respect to lender rights in the event of a borrower default, near to 97.2% of residential lending were first-lien mortgages whilst 2.8% corresponded to any other second ranking mortgages.

Moving to the commercial exposure, in general, the portfolio was very diversified, remaining roughly unchanged since the latest [report published in July 2018](). The industry and real estate sector accounted for 20.3% and 13.1%, respectively. As we can see, real estate sector continued to show a downward trend in the mortgage market thanks to the important measures taken by the Spanish banks to address Non-Performing Loans (NPLs) and foreclosed Assets (FAs).

Continuing with the composition of the commercial segment, the pool was also made up of retail and shopping malls (14.9%), lending for land purposes (7.7%), hotel and tourism sector (5.0%), offices (4.4%), agriculture (2.4%) and other purposes (32.3%).

Chart 2: Commercial property composition



Source: Spanish Mortgage Association

4. Loan to Value Ratio (LTV)

Based on the available data of 13 institutions -which account for approximately 86% of the sample- the weighted distribution of pool's LTV in terms of unindexed LTV buckets showed that 86.9% of outstanding lending was up to 80%, while the remaining 13.1% corresponded to mortgage loans with an LTV above 80%. Since the latest [report published in July 2018](), a contraction of 40 bps can be observed among the 80%-90% LTV bucket.

Table 3

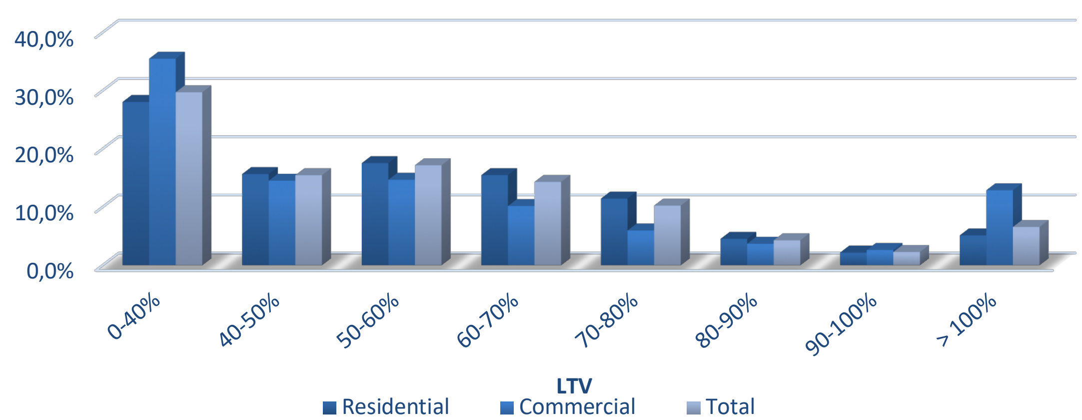
LTV ratio distribution			
LTV	**Total**	**Residential**	**Commercial**
0-40%	29,7%	28,0%	35,5%
40-50%	15,5%	15,7%	14,5%
50-60%	17,2%	17,5%	14,7%
60-70%	14,3%	15,5%	10,2%
70-80%	10,2%	11,4%	6,0%
80-90%	4,3%	4,5%	3,7%
90-100%	2,3%	2,2%	2,6%
> 100%	6,6%	5,1%	12,9%

Source: Spanish Mortgage Association

The breakdown within the residential pool is similar due to the significant weight of the activity in the total pool. Loans with an LTV under 80% accounted for 88.2% outstanding residential lending, which is notably more than the 80.8% from the commercial segment. Compared to the latest report published in July 2018, the proportion of loans originated with an LTV above 80% has decreased. Assuming that early repayment kept steady, these dynamics would be explained by either a tightening of credit conditions or by the increase of the collateral values.

The weighted average LTV for residential lending, considering the size of each entity of the sample, stood at 56.3%, ranging from 50.5% to 64.3% among 12 entities of the sample. A different picture is seen in the commercial pool, where this ratio was 63.7%, ranging the maximum and minimum of the sample from 82.5% to 45.3%.

Chart 3: LTV residential and commercial distribution



Source: Spanish Mortgage Association

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5. Loan size

In this section, it is depicted the pool's breakdown in terms of the outstanding loan amount for a sample of around 97% of the pool under analysis.

When considering the outstanding amounts in the aggregate pool, 37.4% of the outstanding loans corresponded to loans whose principal reached up to EUR 100,000 and 31.0% corresponded to those between EUR 100,000 and EUR 200,000. For its part, 12,8% of the outstanding portfolio were loans with a principal over 1 million euros.

Table 4

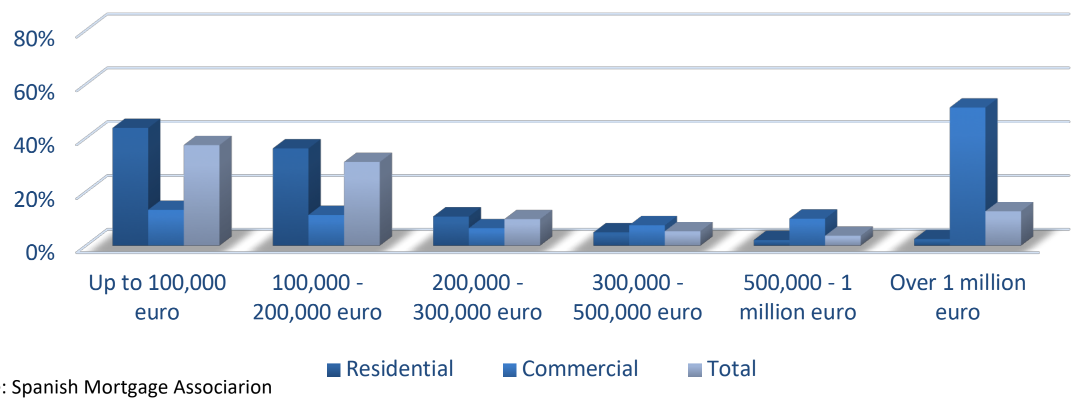
Loan size (outstanding lending loans)			
Interval	**Total**	**Residential**	**Commercial**
Up to 100,000 euro	37,4%	43,7%	13,3%
100,000 - 200,000 euro	31,0%	36,1%	11,4%
200,000 - 300,000 euro	9,8%	10,8%	6,5%
300,000 - 500,000 euro	5,4%	4,9%	7,5%
500,000 - 1 million euro	3,7%	2,1%	10,0%
Over 1 million euro	12,8%	2,4%	51,3%

Source: Spanish Mortgage Association

In the residential pool, on a weighted average basis, 43.7% of outstanding residential lending did not exceed EUR 100,000 and 36.1% did not surpassed EUR 200,000. A residual 2.4% corresponded to loans over 1 million.

Moving to the commercial portfolio, loans which amounted up to EUR 100,000 accounted for 13.3% and those within the EUR 100,000-200,000 bucket, accounted for 11.4%. Regarding loans over one million euro, 51.3% corresponds to outstanding commercial lending.

Chart 4: Loan amount distribution (oustanting lending)



Source: Spanish Mortgage Associarion

In order to provide a better representativeness of the sample, averages for each of the tranches in terms of the number of loans instead of their sizes have been considered.

Table 5

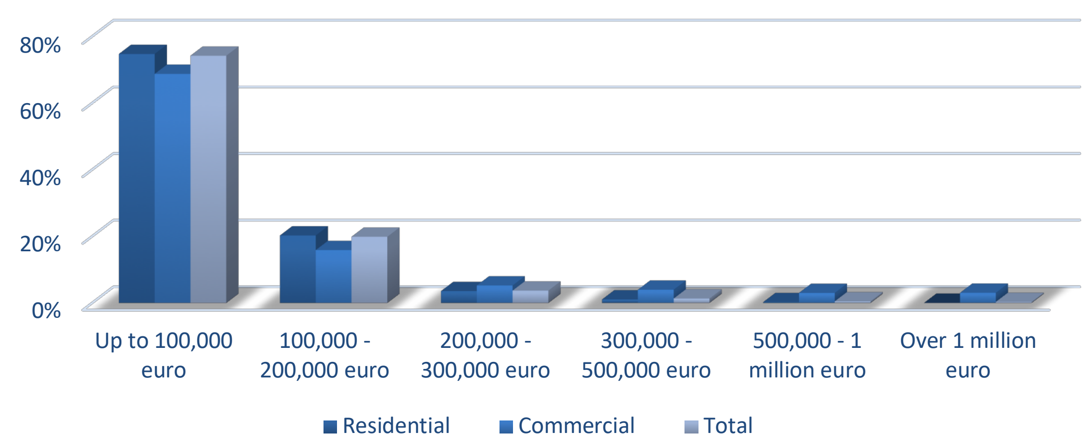
Loan size (number of loans)			
Interval	**Total**	**Residential**	**Commercial**
Up to 100,000 euro	74,2%	74,8%	68,8%
100,000 - 200,000 euro	19,9%	20,3%	15,9%
200,000 - 300,000 euro	3,7%	3,6%	5,3%
300,000 - 500,000 euro	1,3%	1,1%	4,0%
500,000 - 1 million euro	0,5%	0,3%	3,0%
Over 1 million euro	0,3%	0,1%	3,1%

Source: Spanish Mortgage Association

Under this new approach, it was observed that in the residential mortgage pool the number of loans with outstanding amounts under EUR 100,000, represented around 74.8% and the number of loans with outstanding amounts between EUR 100,000-200,000 accounted for 20.3%. Continuing with the commercial activity, the aforementioned buckets showed lower market shares than those in the residential one, amounting to 68.8% and 15.9%, respectively.

From this perspective -as outstanding amounts were not consider- a notably decrease on the proportions can be seen in the interval over one million compared to table 4 (above). Thus, 0.1% corresponded to the residential pool and 3.1% to the commercial one.

Chart 5: Loan amount distribution (mortgage units)



Source: Spanish Mortgage Associarion

On the other hand, on an aggregate basis, the top 10 exposures represented 1.9% of the total outstanding. This results from weighing the value of the residential pool -where this proportion was 0.5%-, and the value of the commercial pool -where the same rate was 8.5%.

6. Loan Seasoning

In this section it is analysed the distribution of the outstanding mortgage portfolio based on the loan seasoning. Compared to the latest report published in July 2018, data showed slight divergences in terms of seasoning over 5 years, accounting for 67.7% of the aggregate pool (69.6% in Q1 2018).

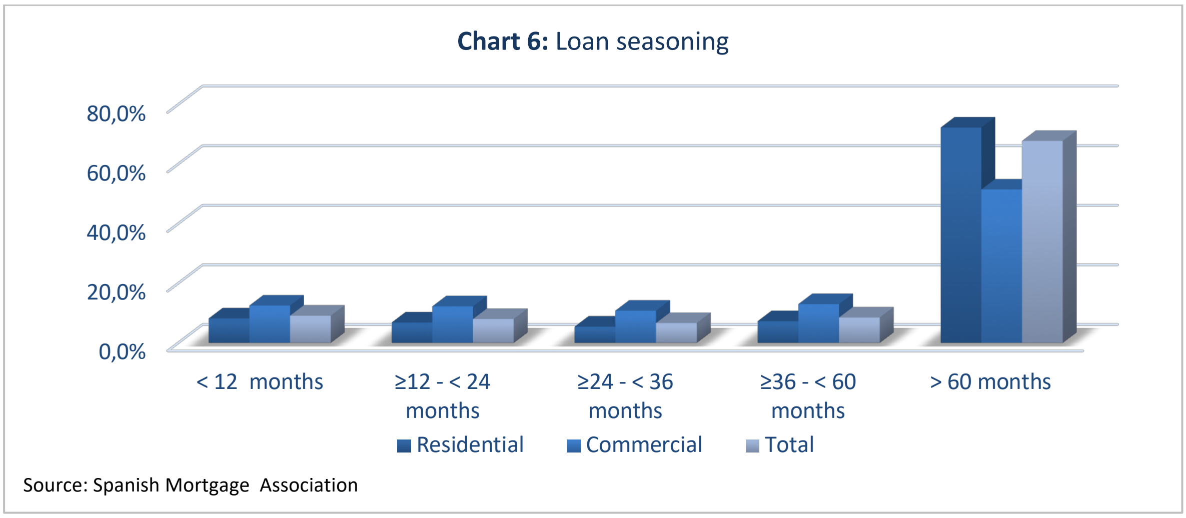
Table 6

Loan seasoning			
Antigüedad	**Total**	**Residential**	**Commercial**
< 12 months	9,1%	8,2%	12,5%
≥12 - < 24 months	8,0%	6,8%	12,3%
≥24 - < 36 months	6,6%	5,5%	10,8%
≥36 - < 60 months	8,5%	7,3%	13,0%
> 60 months	67,7%	72,2%	51,5%

Source: Spanish Mortgage Association

Regarding the residential segment, 72.2% depicted a seasoning above 5 years, while this proportion dropped down to 51.5% in the commercial segment. The differences noticed between the two portfolios can be explained by the credit conditions, especially for first time buyers (FTBs), where the term of the loan can sometimes be over 40 years.

Likewise, with regards to the analysis published in July 2018, it can be observed that new lending continued to pick up speed while loans with a seasoning equal to or greater than 5 years slowed down.



7. Amortisation profile

The average amortisation period compared to the latest report published in July 2018 (Q1 2018) showed a slight increase, standing at 15.05 years. This would show -if the same structure portfolio had been maintained- that longer terms on the new lending have been granted.

Table 7

Amortisation profile	
0 - 1 years	3,8%
1 - 2 years	2,4%
2 - 3 years	2,6%
3 - 4 years	2,8%
4 - 5 years	3,0%
5 - 10 years	17,4%
10+ years	67,8%
Average maturity (years)	15,05

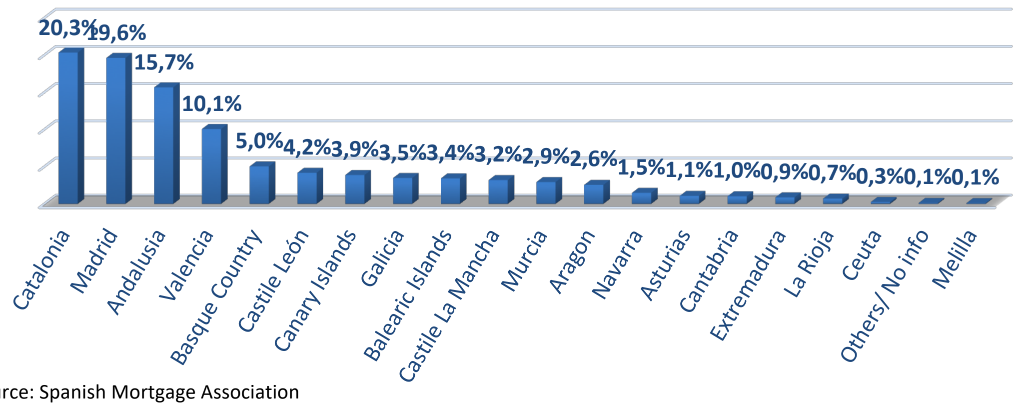
Source: Spanish Mortgage Association

In aggregate terms, the percentage breakdown for the different maturity periods has not practically changed from the report published in July 2018 (Q1 2018). Namely, 14.7% of the outstanding lending pool is expected to be amortised within the next 5 years, another 17.4% would be amortised in a medium term (5 to 10 years), leaving 67.8% of the portfolio with maturity dates exceeding 10 years.

8. Geographic distribution

According to the location of the underlying assets in the national territory, the core regions with leading market shares were Catalonia with 20.3%, followed by Madrid (19.6%), Andalusia (15,7%), Valencia (10,1%) and, to a lesser extent, the Basque Country (5,0%). The remaining pool is constituted by the rest of regions, being Ceuta and Melilla by far, the ones with the lowest exposure (0.1% each one).

Chart 7: Cover pool interest rate distribution



Source: Spanish Mortgage Association

By type of portfolio, also Catalonia, Madrid, Andalusia, Valencia and the Basque Country have the largest concentration, with a market share of 70.6% in the residential segment and 71.1% in the commercial one.

According to credit risk assessment, it is worth stressing that a vast majority (99.8%) of the total portfolio is guaranteed by properties located in Spain, leaving 0.2% to international exposure (especially properties located within the EU).

9. Interest rates

Here below, it is analysed the breakdown of the mortgage pool in terms of the loans' interest rates. Assuming that variable loans had not been amortised at a faster pace than fixed ones and that the joining of a new Spanish entity to the ECBC Label did not meaningfully modify the interest rate composition, it can be noticed the increasing role played by fixed-term in gross lending compared to the last report.

Table 8

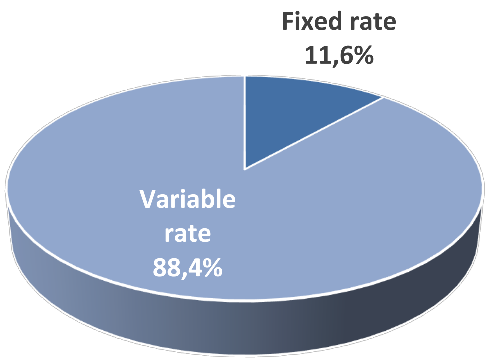
Interest rate market share		
	Residential	**Commercial**
Fixed rate	10,9%	14,5%
Variable rate	89,1%	85,5%

Source: Spanish Mortgage Association

Within the residential portfolio, 10.9% of the outstanding lending is linked to a fixed rate[7] contract compared to the report published in July 2018 (Q1 2018), with 8.5% of market share. Structure variations can also be spotted in the commercial portfolio, where fixed rates showed an increase from 12.7% in Q1 2018 to 14.5% in Q3 2018.

Paradoxically, the ECB's expansive monetary policy, as well as its normalization, is having effects on borrower's profile, who are adopting a more risk adverse behaviour. On the one hand, the ongoing low interest rate scenario has convicted borrowers to opt for loan-fixed rate given the attractiveness of prices (despite fixed rates are usually higher than floating ones[8]) and, on the other hand, the expected changes in market conditions for the upcoming years in terms of future interest rate hikes, has also discouraged consumers' risk appetite.

Chart 8: Cover pool interest rate distribution



Source: Spanish Mortgage Association

10. Other data

[7] *Loans with an interest rate over 1 year of initial rate fixation.*

[8] *Loans with an interest rate up to 1 year of initial rate fixation.*

The cleaning up of banks' balance sheets has continued during Q3 2018. The weighted ratio of Non-performing loans (NPLs)[9] in the residential segment showed a modest decrease, from 4.2% seen in the report published in July 2018 (Q1 2018) to 4.1% in Q3 2018. In the commercial segment, although there are still large problematic assets in banks' balance sheets, most financial entities have reduced substantially these toxic assets. Thus, as of the report published in July 2018 (Q1 2018) NPLs rate have decreased from 13.8% to 12.0%.

Finally, regarding the amortisation method, in the residential pool, a vast majority (99.1%) of the total mortgage pool used the French system (principal plus interest payments), 0.4% is amortised by bullet or interest-only systems and 0.6% followed any other different system. By contrast, in the commercial portfolio, 87.9% used the French amortisation system, 7.3% followed a bullet system and the remaining 4.8% used other.

[9] *Past due installments over 90 days, considering the total loan amount.*