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Analysing the Spanish Mortgage Pool

First half of 2020

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September 2020

1. Preliminary Comments

This report presents an update of the data and analysis published by the Spanish Mortgage Association (AHE) in March 2020 (which contained data up to December 2019). The aim of this report is to provide stakeholders with an outlook of the composition and the main features of the Spanish credit institutions' total mortgage pool.

The analysis comprises data from 13 credit institutions[1] that issue covered bonds (*cédulas hipotecarias*) with a Covered Bond Label[2] by the European Covered Bond Council (ECBC).

The data are gathered from the information on the cover pool backing covered bond issuances that is available on the corporate websites of each credit institution. As a member of the ECBC, the Spanish Mortgage Association coordinates 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 homogeneous definitions.

This short assessment offers 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.

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

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

2. Fundamental Data of the Cover Pool

The analysed mortgage pool[3], which represents approximately 85% of the national outstanding mortgage lending[4], experienced a slight contraction of 1% compared to the last half of 2019 (December 2019) and a decrease of almost 4% in year on year terms. This should be viewed in the current context. On the one hand, the ability to generate income from the various economic operators has been diminished as a result of the worldwide economic and health shock. On the other hand, supervisory bodies and competent authorities have articulated a series of monetary and fiscal policies with a high degree of expansive bias in order to preserve the economic situation of countries and their borrowing capacity.

In parallel, the number of outstanding loans in the portfolio has decreased from 5,645,002 in the second half of 2019 to 5,592,297 loans in the period under analysis. This is a decrease similar to that experienced by the outstanding balance of the portfolio (1%).

However, the average amount of the portfolio stood at EUR 82,543, being slightly lower in the residential portfolio – amounting to EUR 71,810 – and clearly higher in the case of the portfolio backed by a non-residential property, reaching EUR 205,171.

Table 1

Mortgage Portfolio Basic Data	
National mortgage outstanding loans (*) (**) (million €)	545,143
ECBC Label Mortgage Portfolio (million €)	461,603
Mortgage portfolio/outstanding balance	84.7%
Number of loans in the portfolio	5,592,297
Average loan amount (€)	82,543
Average residential amount (€)	71,810
Average commercial amount (€)	205,171
Average loan life (years)	11.15
Average LTV	58.4%
Residential collateral	80.0%
Commercial collateral	20.0

(*) Not including MBSs

(**) Latest available data December 2019

Source: own elaboration from ECBC Label data

[3] *Dated to June 2020 for the sample as a whole.*

[4] *The outstanding value is dated to December 2019 since it is the latest available.*
On-balance and off-balance residential mortgage backed securities (RMBS) are not considered.

3. Property Type Information

As for the nature of the loan, there was a deleveraging of the exposures linked to a commercial guarantee[5] – representing about 20% of the outstanding balance of the portfolio–. This was more intense than in residential backed transactions, with a much greater presence[6] (80%). Overall, the residential portfolio has always had major presence in the mortgage pool, although these differences seem to widen in recent years, as only a year ago the residential portfolio barely accounted for 79% and three years ago it did not reach 77%.

This same index, calculated by the number of outstanding mortgages, shows even greater differences, as it accounted for 92% for residential and 8% for the commercial portfolio.

As mentioned above, the competent authorities have redoubled their efforts and credit facilities, channelling much of these efforts through the financial sector and especially to the sectors most affected by the current crisis. Nonetheless, the truth is that these stimuli have not been translated into more weight of the commercial portfolio, since these credit lines have been mainly aimed at meeting the circulating capital needs of companies and leaving, to a large extent, mortgage loans aside.

Table 2

Property Type Information	
Residential	**80.0%**
Maximum in portfolio	90.4%
Minimum in Portfolio	68.0%
Commercial	**20.0%**
Maximum in portfolio	32.0%
Minimum in Portfolio	9.6%

Source: own elaboration from ECBC Label data

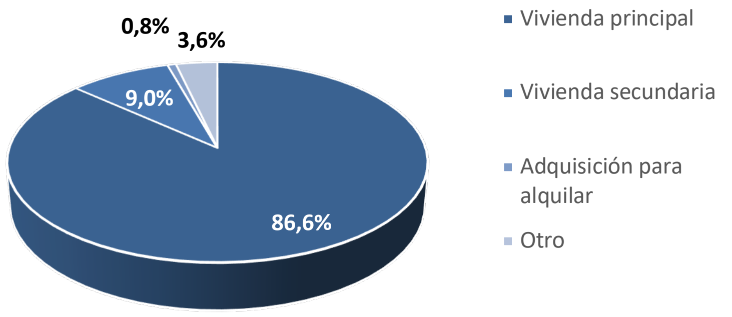
At a more detail level in terms of the purpose and type of loans in the analysed sample, within the <u>residential portfolio</u>, lending for purchase of a main residence remained reasonably stable, representing 86.6% of the share, while lending for second home purchase accounted for 9.0% of the outstanding residential portfolio. In addition, there is another 0.8% of the balance that corresponded to residential

[5] *Commercial loans are loans backed by a mortgage and which have recourse to a borrower, excluding individuals and public-sector entities.*

[6] *Residential loans meet the following criteria: loans with 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.*

mortgages granted for buy-to-let purposes, normally granted to a medium-high profile borrower, with lower financial needs to buy a property.

Chart 1: Type of collateral



Source: own elaboration from ECBC Label data

By type of guarantee in the residential portfolio, it is made a distinction between first mortgage and others, representing the former 98% of the transactions. Thus, in credit risk terms, there was a positive relationship between risk and the policies applied by credit institutions.

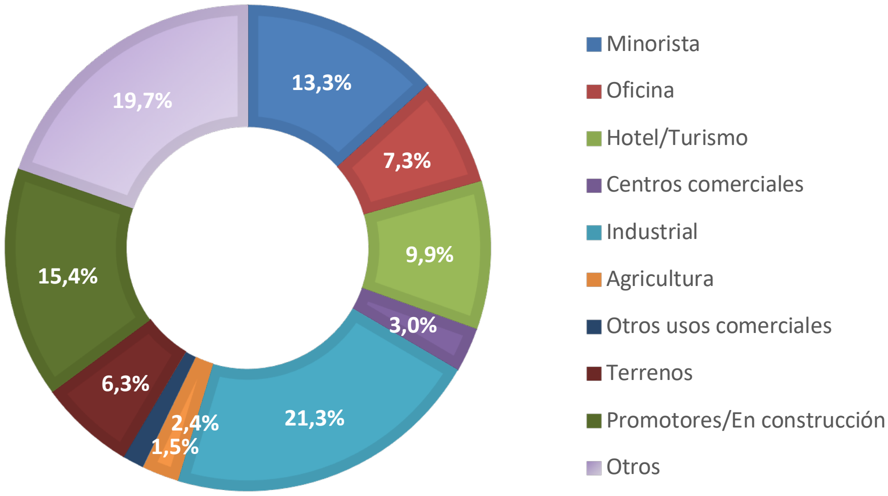
Table 3

Residential Collateral by ranking	
First lien	97.8%
Second mortgage	2.2%
Other	0.0%

Source: own elaboration from ECBC Label data

The industrial sector headed the commercial portfolio by volume recorded on the balance sheets, accounting for 21.3% of the commercial lending, followed by loans registered for a purpose other than those defined in the template or for which this information is unknown, which bring together 19.7% of the portfolio. With some distance, but also with high representativeness, stood exposures linked to the construction and property development activity, which concentrated 15.4% of the balance, followed by lending for the retail activity, accounting for 13.3%. All other activities had a market share below 10%. There were slight variations compared to previous analyses. These are due to small changes in the method of calculation and not to structural changes in the funding of institutions. While the detail for each lending purpose was previously given according to the total weight of the institutions that make up the aggregate sample (both residential and commercial), now it is established according to their weight only on the commercial portfolio, in the consideration that this analysis offers a clearer picture of the portfolio under analysis (in this case, the commercial portfolio). Therefore, the latter criterion will be met from now on.

Chart 2: Commercial Collateral Breakdown



Source: own elaboration from ECBC Label data

4. Loan-to-Value Ratio (LTV)

As for the weighted distribution of the unindexed LTV mortgage loan pool – available for 12 credit institutions which represent around 87% of the total sample – the volume of loans with an LTV ratio below 80% is maintained with slight upward variations: during the first half of 2020 the share accounted for 87.8% of the portfolio, compared to 87.3% in the previous half of the year or 86.7% in the same period of the previous year.

It can certainly be seen that the bulk of the loans were within the LTV ratio equal to or below 80% of the appraisal value, where 46.9% of the outstanding portfolio corresponded to loans with LTV under 50%, and 40.9% to loans with LTV between 50% and 80%. For its part, the share of the most sensitive tranche in terms of its risk-guarantee ratio, i.e. those with a collateral that does not back *per se* the credit (loans exceeding 100% LTV), was 6.5% of the total volume of outstanding loans.

Table 4

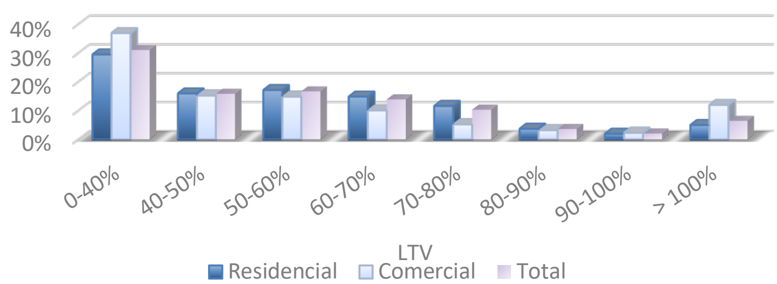
LTV ratio distribution			
LTV	**Total**	**Residential**	**Commercial**
0-40%	31.1%	29.5%	37.0%
40-50%	15.9%	16.0%	15.3%
50-60%	16.7%	17.2%	14.9%
60-70%	13.9%	14.9%	10.1%
70-80%	10.3%	11.6%	5.3%
80-90%	3.6%	3.7%	3.2%
90-100%	2.1%	2.0%	2.3%
> 100%	6.5%	5.0%	12.0%

Source: own elaboration from ECBC Label data

When analysing LTV coverage tranches according to the type of collateral, it is observed that within the residential segment the percentage of loans not exceeding 80% of the value of the collateral is significantly higher than in the commercial portfolio. In particular, in the first case 89.2% of residential volume corresponded to loans with an LTV ratio below 80%, in contrast to the commercial portfolio, where this ratio amounted to 82.4% of the portfolio.

In general, loans with an outstanding principal above 80% of the collateral value have undergone a down variation, helping to gauge risks and to improve the quality of the mortgage portfolio at a crucial moment due to uncertainty generated by potential deterioration in the credit outlook. In this regard, it also should be considered the regulatory relevance of risk exposures within this 80% threshold. Since as they are deemed to have a lower risk, they compute at a significantly lower risk-weighted in terms of calculating Risk-weighted Assets (RWA) in accordance with the required regulatory levels of capital. In addition, it is also noteworthy the positive effect of these loans[7] on the eligible pool constituted in favour of Covered Bonds (*cédulas hipotecarias*), as they serve to maximize the issuance capacity of institutions, always provided that the loan meets other criteria (first-rank mortgage, the volume of lending for buildings under construction cannot exceed 20% of the eligible portfolio, etc.)

Chart 3: Residential and commercial LTV distribution



Source: own elaboration from ECBC Label data

[7] *The maximum LTV ratio of eligible residential loans is 80%, while in eligible commercial loans the LTV limit is set at 60%.*

Regarding the average LTV ratio, the average resulting from weighing each institution's LTV according to its weight in the pool shows an average LTV of 56.3% in the residential portfolio and 66.5%[8] in the commercial portfolio. In aggregate terms, the average LTV of the pool is 58.4%.

5. Distribution of Loans by Size

Considering the composition of the pool according to the tranches of outstanding capital, the distribution remains virtually unchanged compared to the latest analyses.

Thus, it is observed that approximately 69% of the outstanding balance would fall under the tranche of loans with principal under EUR 200,000, 19% of which would correspond to loans ranging from EUR 200,000 to one million and the remaining 13% corresponding to mortgage operations amounting to more than one million.

Table 5

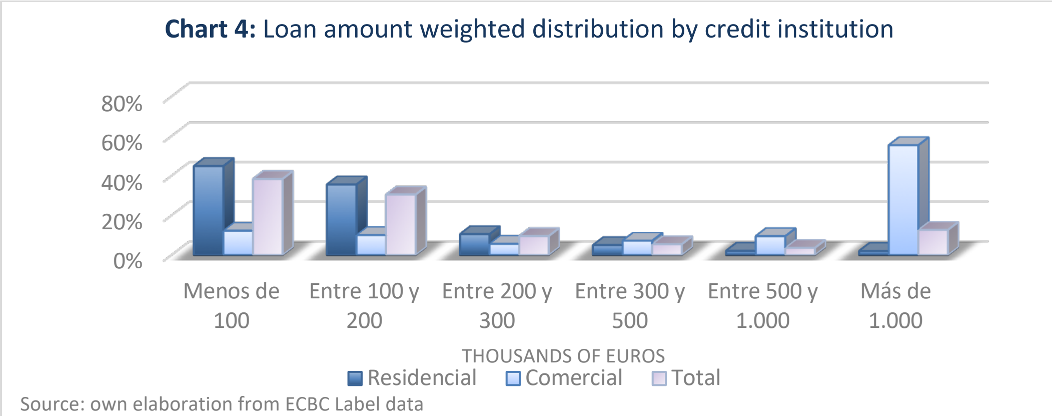
Weighted average distribution by credit institution (loan amount vs. outstanding balance)

Buckets	Total	Residential	Commercial
Up to 100,000 euros	38.4%	44.9%	12.3%
Between 100,000 and 200,000 euros	30.5%	35.6%	10.0%
Between 200,000 and 300,000 euros	9.5%	10.5%	5.6%
Between 300,000 and 500,000 euros	5.4%	5.0%	7.2%
Between 500,000 and 1,000,000 euros	3.6%	2.1%	9.5%
More than 1,000,000 euros	12.7%	2.0%	55.4%

Source: own elaboration from ECBC Label data

Depending on the underlying collateral of the portfolio, it can be observed that approximately 80% of the residential outstanding balance corresponded to operations not exceeding EUR 200,000, being considerably lower the weight in the commercial portfolio, where it barely exceeded 22% of the total balance. For the tranche of loans ranging from EUR 200,000 to one million euros, the dispersion between the two segments was smaller, with the residential portfolio accounting for 18% and 22% for the commercial portfolio. Lastly, there are loans with a principal exceeding one million euros – stressing the differences depending on the type of collateral provided – which represented 2% of the outstanding balance in the case of the residential portfolio and 55% in the case of the commercial portfolio.

[8]*While in aggregate and residential terms the available sample reaches about 86% of the pool in volume, in both cases, for the commercial portfolio, despite there are no data available for 2 institutions out of the 13 that make up the sample (one more compared to the aggregate and residential portfolio), the weight of the remaining 11 institutions accounted for almost 89%.*



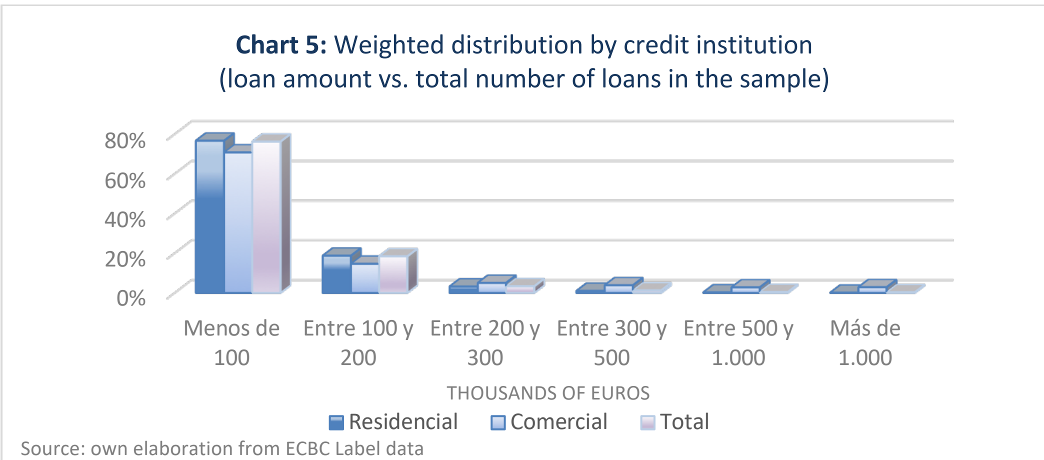
As in previous reports, to contribute to the analysis and interpretation of the data, we have also worked with weighted averages without considering the nominal value of the loan allocated to each tranche, instead it has been computed considering each loan as a unit.

Table 6

Weighted average distribution by credit institution (loan amount vs. mortgage units)			
Buckets	**Total**	**Residential**	**Commercial**
Up to 100,000 euros	76.2%	76.7%	70.8%
Between 100,000 and 200,000 euros	18.4%	18.7%	14.7%
Between 200,000 and 300,000 euros	3.3%	3.2%	5.0%
Between 300,000 and 500,000 euros	1.2%	1.0%	3.8%
Between 500,000 and 1,000,000 euros	0.5%	0.3%	2.8%
More than 1,000,000 euros	0.3%	0.1%	2.9%

Source: own elaboration from ECBC Label data

So, under this approach, the distribution by tranches according to the portfolio under analysis showed less pronounced differences: in the residential mortgage portfolio, the bulk of the portfolio was still in the tranche comprising up to EUR 200,000, but with a largest share, close to 95%, while in the commercial mortgage portfolio it reached 84% of the commercial loans.



Again, in relation to the outstanding balance, the composition of the pool showed significant differences, so that in the residential portfolio the 10 largest exposures (grouped by holder) represented around 0.4% of the outstanding balance, while in the case of the commercial portfolio this same coefficient stood at 6.9%.

6. Loan seasoning

In general, over the first half of 2020, there was a shift in the structure of the portfolio: from loans with a seasoning up to 12 months (1 year), to those with a seasoning of more than 12 months (1 year), especially those in the tranches between 12 months and 60 months (5 years). In particular, the latter had gone from 25.5% as of June 2019 or 27.3% as of December 2019 to near 29.2% as of June 2020; while loans with a seasoning up to one year recorded a fall: from 10.3% as of June 2019 or 9.9% in December 2019, down to 8.4% this year. This development would reflect the less dynamic behaviour that gross lending has maintained in recent months due to the economic implications and restrictions on mobility and air traffic caused by the pandemic.

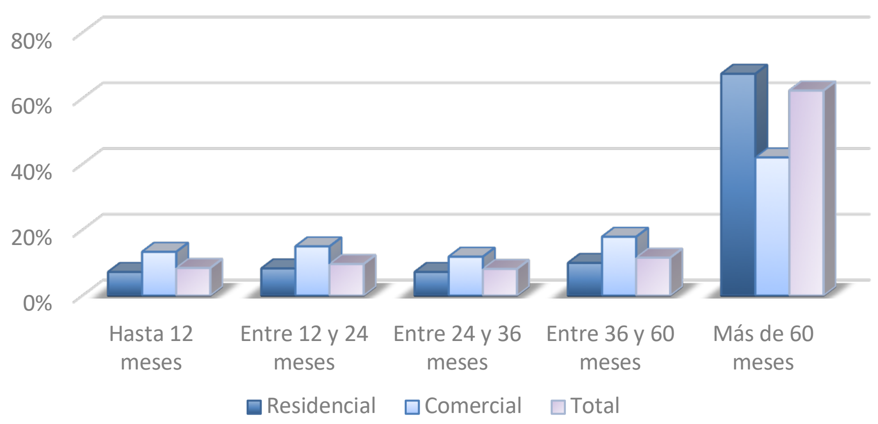
Table 7

Loan seasoning			
Buckets	**Total**	**Residential**	**Commercial**
Up to 12 months	8.4%	7.2%	13.3%
Between 12 and 24 months	9.6%	8.3%	15.0%
Between 24 and 36 months	8.1%	7.2%	11.8%
Between 36 and 60 months	11.5%	9.9%	17.9%
More than 60 months	62.4%	67.5%	42.0%

Source: own elaboration from ECBC Label data

When disaggregated by segments, it is observed that in the residential segment around 7.2% of the balance falls within the credit granted in the last 12 months, compared to the rate of 9.0% recorded a year ago. In the commercial segment this same magnitude barely exceeds 13.3% at the moment, compared to 15.6% last year. By contrast, loans with a seasoning between 12 and 60 months increased in the residential portfolio from 22.0% of the outstanding balance as of June 2019 to 25.4% as of June 2020. For its part, this share in the commercial portfolio grew from 39.2% as of June 2019 to 44.7% as of June 2020. Meanwhile, mortgages granted more than 60 months ago run out of steam throughout this period under analysis, despite maintaining a high weight in the portfolio, accounting for 67.5% for the residential portfolio and 42.0% for the commercial.

Chart 6: Loan seasoning



Source: own elaboration from ECBC Label data

Without considering 3 of the 13 entities in the sample, which represented about 28% of the pool, on average, the age of the aggregate portfolio stood at around 8 years and 8 months.

7. Amortisation Profile

According to the amortisation profile of the pool – weighing the maturity according to the contractually established repayment schedule – near to 4.0% of outstanding balance is expected to be repaid before one year, without prejudice to the early repayment of any loan. For its part, the remaining 96.0% will do so after one year from the reference period (first half of 2020). Of this, 30.1% of the balance is expected to be repaid within the next 10 years.

Table 8

Amortisation profile	
0-1 years	4.0%
1-2 years	2.7%
2-3 years	2.8%
3-4 years	3.1%
4-5 years	3.5%
5-10 years	18.0%
+10 years	65.9%
average term (years)	11.15

Source: own elaboration from ECBC Label data

However, the weighted average life[9] is 11 years and 1 month as of June 2020, with a weighted average maturity[10] of 20 years.

In total, for an available sample of approximately 72% of the total number of credit institutions participating in the study, the average age of loans was 28 years and 8 months, including not only the operations with a residential property collateral but also those with a non-residential real estate collateral.

From the liability side of the balance sheet, the average repayment period of the main funding source in the mortgage pool *(cédulas hipotecarias)* barely reached 4 years and 5 months, compared to 11 years and 1 month of its cover pool.

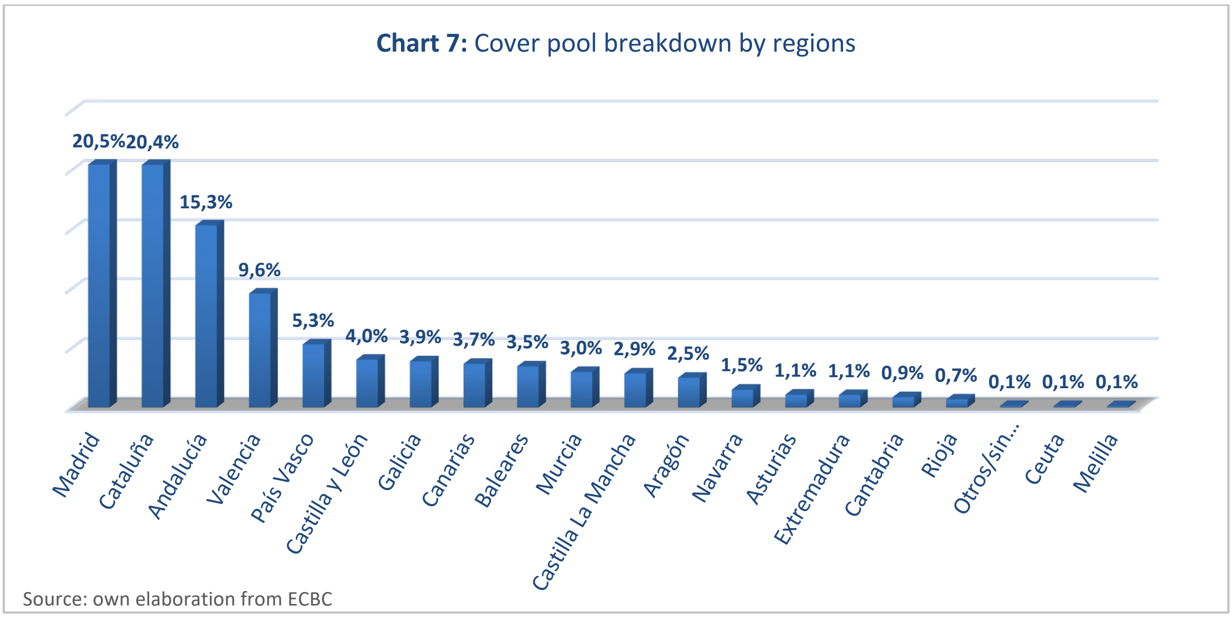
8. Geographical Distribution of the Pool

The geographical profiles of the pool under analysis draws a similar scenario compared to previous reports. Thus, more than 70% was concentrated in some of the autonomous communities with greater economic and tourist influence. In particular, Catalonia headed the ranking, with 20.4% share, only surpassed by the Community of Madrid that was at the forefront in volume of operations, with a market share of 20.5% in the first half of 2020. It is followed by Andalusia, which lost some weight, as it represented 15.3% of the activity compared to 15.4% in the two previous six-month periods. Within a reasonable distance, the Valencian Community has also experienced a slight decrease over this period, with a volume accounting for 9.6% of the portfolio. Above 5%, there was also the Basque Country, with a share of 5.3%. The rest of the regions make up the remaining 30% of the pool, all below 5%, highlighting Castilla y León (4,0%), Galicia (3,9%), the Canary Islands (3.7%), the Balearic Islands (3.5%) and Murcia (3,0%) by volume of operations.

[9] *The weighting of the loan life according to the repayment schedule accrued by the loan is considered. This is especially significant for loans under the French repayment system, where the principal is progressively amortised as the instalments are paid. Thus, in the case of a new loan, as the years gradually go by, a higher proportion of the instalment will be devoted to amortise capital.*

[10] *It is exclusively considered the residual term of the loan from the time of reference (the year under analysis) until maturity, without considering the planned repayment schedule.*

This data has been calculated on 10 of the 13 entities that make up the sample, which account for about 72% of the mortgage portfolio under analysis, since the details of the 3 excluded entities are not available.



In general, when the information is offered by market segments, the picture is very close to the scenario of the aggregate pool: communities such as Madrid, Catalonia, Andalusia, Valencia or the Basque Country represented the bulk of the portfolio, both in the residential portfolio, with a share of 70.8%, and in the commercial portfolio, reaching 72.3% of the commercial balance.

Outside the Spanish borders, we find only 0.5% of international exposure, with the vast majority of properties based within the European Union. These transactions occur mainly between institutions that, although operating in Spain, border other countries such as Portugal or France, expanding their network beyond the Spanish frontiers.

Table 9

International geographical exposure of the portfolio	
European Union	99.9%
Spain	99.5%

Source: own elaboration from ECBC Label data

9. Interest Rates

As for the modality of the subscribed interest rate, the fixed-rate option[11] consolidated as an alternative to variable interest rates[12], even though loans referenced to an external index continued to

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

dominate clearly in the portfolio, weighing close to 83%. However, when comparing the latter data with those of a year ago (85%) or four years ago (94%), the conclusions seem somewhat clearer.

This proliferation of fixed-rate mortgages in recent years must be understood within the European context of low inflation that has led the ECB to take a very expansive direction in its monetary policy, so that this low interest rate environment has fostered a framework with highly competitive offers in this field.

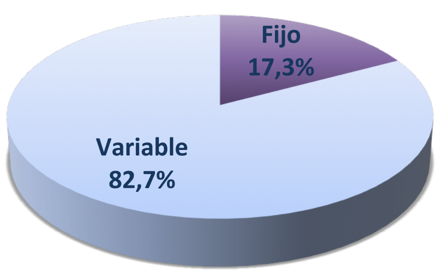
Table 10

Interest rate per segment			
	Total	**Residential**	**Commercial**
Fixed	17.3%	16.2%	21.7%
Variable	82.7%	83.8%	78.3%

Source: own elaboration from ECBC Label data

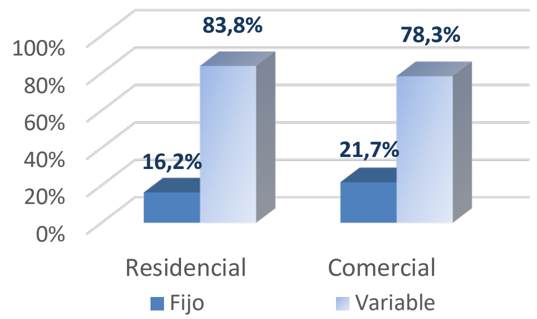
By segment, there is also a growing trend in the procurement of fixed-rate loans. Thus, for the residential segment, the percentage of loans linked to fixed interest rates compared to the total outstanding lending amounted to 16.2%, almost 2.5 points more than a year ago. Similarly, fixed-rate contracts also grew in the commercial portfolio, representing 21.7% of the total balance granted for non-residential activities, compared to 19.4% in the previous year.

Chart 8: Interest rate of the aggregate pool



Source: own elaboration from ECBC Label data

Chart 9: Interest rates by segment



Source: own elaboration from ECBC Label data

10.NPLs Portfolio

The balance sheet of the institutions that make up the pool showed some deterioration in the quality of collateral assets in the first half of 2020, after several years of significant improvements in a row. This development stems basically in the measures adopted to alleviate the spread of the COVID-19 at national level. These had a major impact during the months of confinement, causing a significant drop in the economic activity and, therefore, a deterioration of the employment in the market. This was partly tackled by temporary Layoff arrangements (known in Spain as ERTEs) and the application of moratoriums. However, the NPL's weighted ratio[13] (Non-Perfoming Loans) stood at 4.2% in the first half of 2020, after earning two tenths in the latter half of the year.

In parallel, residential loans, which in the second half of 2019 stood at an NPL rate of 3.2%, recorded a slight increase this half of the year, up to 3.3% of the residential balance. The commercial portfolio has also not been unaffected by these circumstances. Precisely, some of its sectors had been particularly hard-hit by the current crisis, and therefore the NPL ratio has gone from 7.3% in the second half of 2019 to the current 7.5%.

11. Amortisation Systems in the Pool

Finally, when analysing the composition of the pool according to the repayment system followed by the mortgage loan, the French repayment system stands out as the most used. Under this system, instalments are comprised by decreasing interest amounts and increasing principal amounts. In this sense, only 4.2% of outstanding mortgage loans would be amortised on the basis of any other method, be it a *bullet interest-only* system (with a capital grace period such as those currently followed by loans that have taken out a banking sector moratorium[14]), a system of increasing instalment, etc.

In the residential portfolio the volume of loans that have adopted a French repayment system (with constant instalments) amounted to 98.9% of the total balance represented by residential loans. In the case of the commercial portfolio, this system constitutes a smaller albeit significant share, accounting for 83.5% of the portfolio.

Table 11

Amortisation profile	Total	Residential	Commercial
French	95.8%	98.9%	83.5%
Bullet- only interest	2.2%	0.4%	9.2%
Other	2.0%	0.7%	7.2%

Source: own elaboration from ECBC Label data

[13] *Loans with defaults longer than 90 days considering the total amount of the loan, not just the unpaid amount.*
[14] *In order to address the economic and social impact of this pandemic crisis, several support measures have been put into place for households and enterprises. Apart from the moratoriums launched by the Spanish Government (legislative moratoriums), the Spanish banking sector has established another moratorium, which extends the range of persons eligible for debt deferrals and allows the extension of the payment holiday beyond the term set by the legislative moratoria.*