AEGON Bank N.V.

Conditional Pass-Through Mortgage Covered Bonds

Presale

Ratings/Outlook

Conditional Pass-Through Mortgage Covered Bonds	AAA(EXP)/ Stable

Rating Rationale

IDR/outlook	A−/Stable
IDR uplift	0
D-cap (notches)	8 (Minimal discontinuity risk)
Tested Rating on a PD basis	'AA'
Recovery given default uplift (notches)	2
Covered Bonds Rating	AAA(EXP)
AP Fitch considers in analysis (%)	91.0
AAA breakeven AP (%)	95.0

Discontinuity Risk (D-Cap of 8)

Overall assessment	Minimal discontinuity
Asset segregation	Moderate
Liquidity gap and systemic risk	Minimal discontinuity
Systemic alternative management	Low
Cover pool-specific management	Moderate
Privileged derivatives	Very Low

Key Data

	Jun 15
Asset type	Residential mortgages
Cover assets (EURbn)	0.90
Covered bonds (EURbn)	0.50[a]
Nominal OC (%)	80.8
WAL of assets (years)	22.0
WAL of liabilities (years)	7.0[a]

[a] Assumed, minimum benchmark size

Related Research

Covered Bonds Surveillance Snapshot (October 2015)
AEGON Bank N.V. (November 2015)
2015 Outlook: Major Benelux Banks (December 2014)
Global Housing and Mortgage Outlook - 2015 (January 2015)
Covered Bonds with Extendible Maturities (October 2014)
'B' Portfolio Loss Rates for Covered Bonds (September 2015)
Breaking Down Breakeven Overcollateralisation (July 2014)
Dutch Covered Bonds Framework - Discontinuity Analysis of Principles-Focused Legislation Strengthened by Contracts (March 2015)

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Key Rating Drivers

'A−' Rated Issuer: The 'AAA(EXP)' rating of the conditional pass-through (CPT) mortgage covered bonds is based on AEGON Bank N.V.'s (Aegon Bank) Long-Term Issuer Default Rating (IDR) of 'A−', a Discontinuity Cap (D-Cap) of 8 notches (minimal discontinuity) and the 10% committed minimum overcollateralisation (OC) – translating into an asset percentage (AP) of 91% – which gives more protection than the Fitch breakeven AP of 95% for the 'AAA' rating.

The programme is registered with the Dutch central bank (DNB). The Stable Outlook on the covered bonds reflects that on the bank's IDR.

No IDR Uplift: The IDR uplift is 0 notches, which reflects Fitch's view that liquidation is the most likely resolution method for Aegon Bank. This is because Aegon Bank is not considered a systematically important bank for its domestic market, and senior unsecured debt accounts for less than 5% of its adjusted balance sheet.

Minimal Discontinuity Risk: The D-Cap of eight notches is driven by the minimal discontinuity risk assessment for the liquidity gap and systemic risk component. This reflects the CPT feature, which includes a 32-year extension period, and the legal requirement of a reserve fund that covers six months of interest due on the covered bonds plus a buffer for senior expenses.

Legal Minimum Drives AP: The Dutch covered bond legislation stipulates a minimum OC of 5% of the nominal value of outstanding covered bonds. Although a lower level of OC supports 'AAA' stresses in Fitch's cash-flows model, the agency sets the breakeven OC floor at the legal minimum. The 95% 'AAA' breakeven AP corresponds to the 5% legal minimum OC. High excess spread and low credit losses drive the cash-flows model output.

Low Credit Loss: The 2.2% 'AAA' credit loss is the lowest among peers due to a low weighted average (WA) foreclosure frequency, driven by a comparatively low share of interest-only (IO) loans and a low WA debt-to-income ratio, and a high WA recovery rate, due to a large portion of NHG loans (69%) and the small share of loans secured by illiquid properties.

Four-Notch Cushion: With a D-Cap of 8 notches, IDR uplift of 0 notches and 2 notches credit for recoveries, the maximum achievable rating on the covered bonds is 'AAA' as long as the issuer is rated 'BB+' or above.

Programme Highlights

Long-Term Interest-Only Loans: The pool contains long-term IO loans, which may mature after the legal final maturity of the covered bonds. This may lead to the need to liquidate cover assets and introduces refinancing risk, which would not normally be present in CPT programmes. However, due to the high excess spread, Fitch views the risk that a shortfall of funds may occur at the legal final maturity of the bonds to be sufficiently remote. The risk is also reduced by the 10% limit in the ACT for these loans.

Unhedged Interest Rate Mismatches: The programme is exposed to interest rate risk on the fixed-rate loans (82.6%) when they revert due to low interest rates to another fixed or floating rate at their reset date. This is mitigated by the long reset dates of the fixed rate loans (WA of 15 years) and the fixed rate on the bonds. Fitch conducted a sensitivity analysis if the loans reverted to a lower fixed or floating rate at an assumed margin above three-month Euribor.

Figure 1

Selected Peers for Comparison

Issuer/ Programme	IDR/ Outlook	CVB Rating
NIBC Bank N.V.[a]	BBB−/ Stable	AAA/ Stable
ABN Amro Bank N.V.	A/Stable	AAA/ Stable
ING Bank N.V.	A/Stable	AAA/ Stable
SNS Bank N.V.	BBB/ Stable	AAA/ Stable
F. Van Lanschot Bankiers N.V.[a]	BBB+/ Stable	AAA/ Stable

[a] CPT programme
Source: Fitch

Peer Comparison

Some of Aegon Bank's key rating drivers are better than those of the six other Dutch registered covered bond programmes that Fitch rates. Its credit loss is the lowest among peers, primarily due to the high proportion of NHG loans (69%). The peers are listed in Figure 1.

Figure 2

Peer Comparison: Key Rating Drivers

	Aegon Bank	CPT average	Hard and Soft Bullet average	Peer range
IDR/Outlook	'A-'/Stable	'BBB'/Stable	'A-'/Stable	
IDR uplift	0	1	2	1 – 2
D-cap	8	8	4	4 – 8
'B' Portfolio Loss Rate (%)	0.2	1.4	1.2	0.8 – 1.7
'AAA' breakeven AP (%)	95.0	93.8	78.3	76.5 – 95.0
Breakeven OC components (%)				
Credit loss (%)	2.2	8.8	7.3	5.6 – 10.3
Cash flow valuation (%)	-3.3	-5.5	-2.8	-6.9 – -1.2
Asset disposal loss (%)	7.2	6.0	26.2	4.8 – 30.0

Source: Fitch

See the July 2015 *Covered Bond Surveillance Snapshot* and related Excel file for a detailed comparison of rating drivers across Fitch-rated covered bond programmes.

Sovereign Impact

The covered bonds rating does not include any adjustments due to the Dutch sovereign rating of 'AAA'/Stable. For countries rated above 'A+', Fitch applies its standard liquidity gap analysis, which forms part of the D-Cap, focussing on asset liquidity following an idiosyncratic stress of an issuer, while the banking sector as a whole is expected to remain stable and not suffer a systemic crisis. Therefore, Fitch's view on liquidity and systemic risk is unlikely to change unless the Dutch sovereign was downgraded four notches to 'A+' or below.

The Netherlands has a Country Ceiling of 'AAA' and all cover assets are located in the country. Therefore, Fitch does not adjust the calculated rating default and recovery rates applied in its covered bond analysis.

Sensitivity Analysis

There is limited downward pressure on the 'AAA' rating for Aegon Bank's mortgage covered bonds. With the D-Cap of 8 notches, Aegon Bank's covered bond rating would be likely to remain unchanged (due to IDR impact) unless the IDR fell by five notches to 'BB'.

If Aegon Bank's IDR remains at 'A−', the covered bond rating would be likely to remain unchanged (due to IDR uplift and D-Cap impact) unless the D-Cap of 8 notches fell by five or more notches to 3 notches or worse, corresponding to a moderate high risk assessment or below, which is unlikely for the liquidity protection in the form of the conditional pass-through regime for a standard residential mortgage cover pool in a country with a 'AAA' sovereign rating.

There is a cushion between the 95.0% breakeven AP and the 91.0% AP that Fitch gives credit to in its analysis, the latter corresponding to the 10% nominal OC which Aegon Bank commits to within the ACT. There is also a substantial cushion relative to the nominal OC of 80.8% as of October 2015.

Related Criteria

Covered Bonds Rating Criteria (July 2015)
Counterparty Criteria for Structured Finance and Covered Bonds (May 2014)
Counterparty Criteria for Structured Finance and Covered Bonds: Derivative Addendum (May 2014)
EMEA RMBS Rating Criteria (August 2015)
Criteria Addendum: Netherlands - Residential Mortgage Assumptions (August 2015)
Covered Bonds Rating Criteria – Mortgage Liquidity and Refinancing Stress Addendum (September 2015)
Fitch' Mortgage Covered Bond Refinancing Stresses – Excel File (September 2015)
Criteria for Interest Rate Stresses in Structured Finance Transactions and Covered Bonds (December 2014)
Fitch's Interest Rate Stress Assumptions for Structured Finance and Covered Bonds – Excel File (December 2014)

Abbreviations
AP: Asset Percentage
D-Cap: Discontinuity Cap
IDR: Issuer Default Rating
OC: Overcollateralisation
PD: Probability of Default
WAL: Weighted Average Life
WAFF: Weighted Average Frequency of Foreclosure
WARR: Weighted Average Recovery Rate

The Issuer and CBC

Aegon Bank's ultimate 100% owner is Aegon N.V. (Aegon; A/Stable/F1), one of the largest life insurance and pension companies in the Netherlands.

At end-3Q15, Aegon's portfolio of residential mortgage loans was EUR30.6bn. Aegon is the fourth-largest lender in the Dutch mortgage market, with around 11% market share (new mortgage lending in September 2015).

Aegon Bank's IDRs and Support Rating are driven by potential support from its parent, in case of need. Fitch views Aegon Bank as a strategically important subsidiary due to the strong synergies between the bank and insurance activities in the Netherlands, a core market for the group. Through Aegon Bank the group can offer banking products to increase cross-selling and strengthen customer loyalty. We view the subsidiary as "strategically important" but not "core" to Aegon. This is reflected in Aegon Bank's Long-Term IDR being notched down once from Aegon's.

The covered bond company (CBC) was incorporated to act solely for Aegon Bank's CPT programme, guaranteeing payments on the covered bonds. The guarantee provided by the CBC plays a crucial role in Fitch's assessment of the default probability of the covered bonds, combined with the issuer's likelihood of default, to define if payments on the covered bonds can be continued without interruption despite the insolvency of the issuer, allowing Fitch to assign a rating above the issuer's.

No IDR Uplift

In bank resolution frameworks where covered bonds are favourably treated, such as under the Bank Recovery and Resolution Directive (BRRD) for EU countries, Fitch's analysis starts with an uplift over the IDR of up to two notches for programmes of issuers rated in the 'BB' category and above. A two-notch uplift is granted if at least two of the three factors in Figure 3 are present in Fitch's view, or one notch if one of the factors is present.

Figure 3
No IDR Uplift for Aegon Bank's Covered Bonds

IDR uplift driver	Fitch assessment
Relative ease/motivation for alternative resolution methods to liquidation	No. Aegon Bank is not a global or domestic systemically important bank that would be more likely to be supported by resolution tools other than liquidation if insolvent.
Covered bond-intensive country	No.
Sufficient protection through senior unsecured debt	No. Aegon Bank's level of senior unsecured debt is lower than the 5% threshold (relative to the total balance sheet, adjusted for insurance assets and derivatives) that Fitch considers.

Source: Fitch

Aegon Bank is the only covered bond programme registered with the DNB that does not benefit from any IDR uplift. NIBC CPT and Van Lanschot CPT benefit from an IDR uplift of 1 notch due to a level of senior unsecured debt higher than 5%. The other four Dutch registered covered bond programmes have an IDR uplift of 2 notches due to their issuers' status as domestic systemically important banks, and sufficient senior unsecured debt. No IDR uplift applies to Achmea's covered bond programme because it is not registered with the DNB and therefore is not UCITS compliant.

D-Cap of 8 Notches

The potential risk that a covered bond could default if recourse shifts from the issuer to the cover pool is captured via Fitch's D-Caps, which determine the maximum notch uplift from the IDR (adjusted by any IDR uplift) to the tested rating on a probability of default (PD) basis. It reflects the highest risk assessment of five components, ranging from 8 notches for minimal discontinuity to 0 notches for full discontinuity.

Fitch has assigned this programme a D-Cap of 8 notches (minimal discontinuity), in line with its criteria for CPT programmes with three months' coverage of interest and expenses, as long as the assessment of the other components does not raise any particular concerns.

Fitch considers there should not be a need to liquidate cover assets to pay the interest and principal on the bonds when due, and most payment interruption risk is removed for the covered bonds once recourse against the cover pool is enforced, despite the inclusion of long-term IO mortgage loans in the pool, which may not fully amortise before the final legal maturity of the longest outstanding covered bond. Long-term IO loans exceeding 10% of the current balance of the mortgage loans are not given any credit in the ACT.

Aegon Bank is bound by the legislative amendments to the Dutch covered bond framework effective January 2015. These require the reserve fund to cover interest obligations and other senior costs due in the next six months.

Figure 4

Summary of Aegon Bank's Covered Bonds Discontinuity Risk Assessment

Overall assessment	8 (minimal discontinuity)
Asset segregation	Moderate
Liquidity gap and systemic risk	Minimal discontinuity
Systemic alternative management	Low
Cover pool-specific alternative management	Moderate
Privileged derivatives	Very low

Source: Fitch

Details on the assessment for each D-Cap component can be found in Appendix 2. The assessments for Aegon Bank's programme are standard for CPT programmes.

Cover Pool

Figure 5

Aegon Bank's Cover Pool

Characteristics as of October 2015 (% of current loan balance)

General		**Borrower type (%)**	
Current principal balance (EURbn)	0.90	Prime	100.0
Average current loan per borrower (EUR)	185,948	Employed	96.7
Number of loans	9,863	Self-employed	0.0
WA seasoning (years)	2.4	Unemployed	1.0
WA DTI (%)	23.9	Retired and other	2.3
Loan-to-value (LTV%)		**Loan type (%)**	
WA original LTV	88.3	First–ranking	100.0
WA indexed current LTV	84.4	NHG	69.0
		Construction deposit (>EUR2,500)	6.8
		Fixed rate	82.6
Property type (%)		Floating rate	17.4
Houses	87.7	Annuity	39.6
Flats	12.3	Linear	4.9
Other	0.0	Savings	11.2
		Bank savings	7.9
		Universal life	2.2
Valuation type		Traditional life	1.2
Full	92.9	Investment	1.0
Construction	7.1	Interest only	31.9
		Geographic concentration (%)	
		Zuid-Holland	21.3
Current arrears (%)		Noord-Brabant	14.3
3m+ arrears	0.0	Noord-Holland	13.5
Less than 3m arrears	0.0	Gelderland	12.1

Source: Fitch/Aegon Bank

Cover Pool Credit Analysis

Fitch analysed the portfolio using its Dutch mortgage loss criteria (for further details see *EMEA Residential Mortgage Loss Criteria*, published 31 May 2015, and its Dutch addendum, under *Related Criteria*). Fitch applied its standard default probability adjustments under the criteria.

Lender Adjustment

Fitch's base default probabilities assume that origination, underwriting and servicing practices and procedures are in line with those of a standard traditional Dutch mortgage lender, with market expertise and relevant management experience.

As part of the analysis, the agency performed an operational review of the originator to assess the issuer's origination, underwriting and servicing capabilities. If as a result of this review Fitch believes that origination, underwriting and servicing procedures have significant weaknesses, an adjustment to the base default probabilities of the whole portfolio may be warranted.

Figure 6

Default Model Output (%)

Rating level	WAFF	WARR	WA MVD	Loss rate
AAA	11.1	80.4	44.0	2.2
B	3.0	92.6	30.0	0.2

Source: Fitch

Fitch considers Aegon's robust IT system allowing paperless underwriting and administration of loans, a comprehensive origination process across the Netherlands via intermediaries assisted by processing systems, and underwriting criteria in line with major lenders positive for its practices.

The customer contact for arrears is somewhat slower than at peers, with a first letter sent 15 days after the payment is missed. In addition, the determination of self-employed income is based on an average of the last three years' income, compared to peers who use the average or the lowest income of the last three years.

Aegon Bank's underwriting criteria are based on the Dutch Code of Conduct, so the underwriting standard is very similar to that of its peers. However, due to the default data showing weaker performance of the total loan book than some of the other lenders in the Dutch market Fitch has applied a lender adjustment, in line with originators whose default data shows comparable performance.

Fitch has also reviewed an agreed-upon-procedures report conducted by an international accounting firm to assess the accuracy of certain data relating to the loans in Aegon Bank's system compared to the corresponding mortgage loan files. A sample of 444 loans was drawn from the population and verified against a 99% confidence level. The number of findings is substantially lower than for other Dutch originators and mainly relates to the property type. No further lender adjustment was applied by Fitch.

The total lender adjustment applied is 1.05x.

Asset Analysis

The initial cover pool consists of 9,863 loans granted to borrowers in the Netherlands, with an aggregate outstanding amount of EUR904m. The pool has a WA seasoning of 2.4 years and all loans are secured by a first-ranking mortgage. None of the loans are in arrears. Fitch calculated a WA original LTV of 88.3% and a WA indexed current LTV of 84.4% for the pool.

Affordability

Aegon Bank provided detailed data regarding the borrowers' incomes and Fitch calculated the borrowers' debt-to-income (DTI) ratios. The majority (61%) have a DTI equivalent to Class 2 (20%-29%), 25% have a DTI equivalent to Class 1 (below 20%) and 14% have a DTI equivalent to Class 3 (30%-39%). Only 0.6% of the borrowers have a DTI above Class 3 (40% and above). The WA DTI of the pool is 23.9%.

Mortgage Type

The residential mortgage portfolio consists of linear, annuity, IO, universal life, investment, life and savings products (see Figure 5). Fitch increases the default probability for non-amortising

loans to reflect the higher risk of borrowers facing a payment shock at maturity. Similarly, for life and investment mortgages, the probability of default is increased to capture the risk that the capital available at maturity may not be sufficient, depending on the performance of the underlying investment, with no certain return guaranteed. Universal life mortgage loans are subject to set-off risk, which is accounted for in Fitch's cash flow analysis.

Interest Rate Type

Of the portfolio, 82.6% is subject to a fixed interest rate for a period between 1 and 30 years. The remaining 17.4% pays a floating rate. Fitch has increased the probability of default for floating-rate mortgages because rising interest rates could put pressure on the ability of the borrowers to meet mortgage payments.

The loans do not remain at a fixed rate for life; about 19% have an interest reset date within the next two years but 59.5% have at least 10 years or more until their interest reset date. Most borrowers have the option to switch to a floating rate or another fixed rate for another period; however, it is common for borrowers in the Dutch market to enter into another fixed-rate agreement at the reset date.

Borrowers' Employment and Income Status

Of the loans, 96.7% were made to employed borrowers, 1.0% are unemployed and 2.3% pensioners.

In Fitch's asset analysis both employment type and income verification status have an impact on the loans' foreclosure frequency. The frequency of foreclosure for a standard Dutch borrower assumes full-time employment, no adverse credit history and evidence of income. Where cases deviate from this standard, Fitch adjusts the probability of default to address the increased risk of a borrower default on mortgage payments.

Geographical Distribution and Property Type

The geographical distribution of the properties is well diversified over The Netherlands and follows the distribution of the population. The province of Zuid-Holland has the highest concentration, of 21.3%, followed by Noord-Brabant 14.3%, Noord-Holland 13.5% and Gelderland 12.1%.

All properties in the portfolio are owner occupied. There are no investment or second-home properties in the pool. Houses account for 87.7% of properties, apartments for 12.3%.

Illiquid Properties

Fitch has determined 4.1% of the portfolio to be secured by particularly high-value properties (higher than EUR500,000) and 2.2% to be secured by low-value properties (lower than EUR110,000). These loans are at risk of greater market value declines (MVDs) owing to the relatively poor liquidity at either end of the market. The agency has increased the MVDs for these loans.

Construction Loans

Mortgage loans containing construction deposits greater than EUR2,500 form 6.8% of the pool. An element of the principal of these loans is to be disbursed to the borrower at a certain point, depending on the fulfilment of certain conditions. The granting of these loans is common practice in The Netherlands. Fitch views such loans as riskier if the construction works on the property still to be paid for are significant as final bills may be above the expected costs, leading to the provisioned construction deposit being insufficient to provide coverage for these extra expenses.

Any undrawn construction deposit amounts are deducted in the calculation of the ACT. Fitch believes that this sufficiently mitigates set-off risk regarding construction loans.

Sub-Participation Agreements

Under an investment mortgage loan, insurance savings mortgage loan or bank savings mortgage loan a borrower pays a premium or deposit with the aim of accumulating enough funds to repay the principal balance of the mortgage at maturity. If the insurance policy provider or savings account provider defaulted the borrower could set off the accumulated premium or deposit plus accrued yield. Aegon Bank mitigates this through sub-participation agreements.

Under these agreements the participant (bank or insurance company) forwards the monies received (savings or premiums) to the CBC and in return acquires participations in the mortgage receivables equal to the corresponding instalments. Should the participant default and the borrowers invoke set-off or the participant fails to forward monies, the participations reduce accordingly. In addition, the participations are deducted in the ACT from the current balance of the corresponding loans.

NHG Guarantee Cover

A significant proportion of mortgage loans in the Netherlands are backed by an NHG guarantee. The guarantee is provided by Stichting Waarborgfonds Eigen Woningen (WEW), which is backed by the Dutch state. The NHG covers losses mortgage lenders incur on a loan after the sale or foreclosure of the house, but for mortgages originated since 1 January 2014 only 90% of the loan amount are covered by the guarantee and the rest has to be borne by the originator. This coverage extends to outstanding principal, unpaid accrued interest and repossession costs, and some other costs. However, the NHG guarantee is provided on the basis of a 30-year annuity mortgage irrespective of the actual mortgage type, and as a result the amount covered by the guarantee reduces over time. This is taken into account in the agency's default model.

Of loans in the pool, 69.0% benefit from an NHG guarantee. Fitch received static default data by vintage, split between standard loans and loans backed by the NHG. This data showed that for older vintages the NHG loans outperformed non-NHG loans, but for more recent originations the performance of NHG loans was worse. As the portfolio mainly consists of loans originated in recent years Fitch did not apply a downward adjustment to the base default probabilities of NHG loans. Fitch gives credit in its recovery analysis to the guarantee based on the compliance ratio for Aegon Bank supplied by WEW. The 90% pay-out rate for claims that Aegon Bank made to WEW between 2006 and 2014 is higher than the market average.

Dynamic Pool

As the pool is dynamic any deterioration of its credit quality over time resulting from a pool top-up (adding mortgage loans) or after unfavourable substitution of the assets will negatively affect the 'AAA' breakeven AP.

The Fitch breakeven AP for the covered bonds' rating will also be affected by, among other things, the profile of the cover assets relative to outstanding covered bonds, which can change over time, even in the absence of new issuance. Therefore it cannot be assumed that it will remain stable over time.

Default Model Output

Fitch has analysed the portfolio using its Dutch mortgage loss criteria (for further details see *EMEA Residential Mortgage Loss Criteria* and *Criteria Addendum: Netherlands* under *Related Criteria*). Fitch derived a stressed cumulative default rate and recovery rate for the cover pool based on a loan-by-loan analysis of the cover assets. The WA frequency of foreclosure and WA recovery rate in a 'AAA' scenario were calculated as 11.1% and 80.4%, respectively, resulting in an expected loss (EL) of 2.2% in the 'AAA' scenario. The WA recovery rate includes recovery benefit for NHG loans given by Fitch. Theoretically disregarding this recovery benefit would lead to an EL above the minimum 4% threshold in Fitch's criteria (see *EMEA Residential Mortgage Loss Criteria*). The composition and credit quality of the cover pool may change over

time because of the dynamic nature of the programme.

Cash Flow Analysis

Fitch's cash flow model simulates the asset cash flows to reflect prepayment, servicing costs, delinquencies, defaults and recoveries in multiple stress scenarios under various issuer default timings. The model takes into account the terms and conditions on the covered bonds issued at a fixed rate and switching to pass-through amortisation after the expected maturity, while bearing the same fixed rate of interest. If there is a switch to pass-through before the expected maturity of the bonds (triggered by a breach of the amortisation test, see below), the interest due on the bonds is the fixed rate applied to the outstanding amount at that time.

The model tests whether the cover pool is able to service the interest payments on the covered bonds in a timely manner. As there are no privileged derivatives, the agency made some assumptions on the evolution of the interest rate on the pool, in particular the change of interest rate at the interest reset date, and the margin over Euribor on the floating-rate assets (see *Interest Rate Risk* below). The cash flows expected from the assets were also modified to reflect prepayments, delinquencies, default and recovery assumptions in a 'AAA' scenario, while hypothesising the issuer's default at different dates. Fitch also modelled the cost of replacing Aegon Bank as servicer/manager of the cover pool.

Asset Cover Test

The ACT is designed to ensure a minimum level of credit enhancement to protect bondholders against specific risks; it is calculated monthly before an issuer event of default. If breached, failure to satisfy the ACT on or before the end of the next succeeding calendar month will not constitute an issuer event of default. However, it will prevent Aegon Bank from issuing any further bond series until remedied. If not remedied on the next succeeding calculation date, the security trustee will be entitled to serve a notice of breach. After service of an ACT breach notice, the CBC is not allowed to make any payments to Aegon Bank. Aegon Bank will continue to have a "best efforts" obligation to procure sufficient eligible assets. If a breach of the ACT is remedied, Aegon Bank can issue new series.

The ACT ensures that the value of the assets, multiplied by the AP, and adjusted for different risks (including insurance and deposit set-off), is higher than the nominal value of the bonds. In addition, since 1 January 2015 the Dutch covered bonds legislation has stipulated that the value of the cover assets must be at least 105% of the nominal value of the outstanding covered bonds.

The ACT also tests that all the mortgage receivables, substitution assets and amounts standing to the balance of the CBC, excluding swap collateral and construction balances, will be at least equal to 110% of the principal amount of outstanding covered bonds. This minimum 110% translates into an AP of 91%. The AP that will be published in the ACT section of the programme's monthly investor report is 93%. The relationship between OC and AP may change over time, particularly due to the evolution of the other components of the ACT (mainly cash and substitution assets).

If an unremedied breach occurs after issuer default and a notice to pay is made by the security trustee on the CBC, the amortisation test would be run to check there is at least 10% OC between the performing assets and the bonds (see *Amortisation Test* below).

Amortisation Test

The amortisation test is run following the service of a notice to pay on the CBC, to check that the collateralisation level calculated under the test is at least 110%. If breached, all covered bonds will become pass-through and will be paid pro rata subject to the availability of funds. Fixed-rate covered bonds will continue to bear interest at a fixed rate until their extended due for payment date.

When covered bonds become pass-through after a breach of the amortisation test has been served, there is a risk that principal repayments could be made before the bond's expected maturity date and therefore earlier than expected. If investors are unable to reinvest the received payments at a similar interest rate or higher, they will be faced with lower yields than expected on their initial investment. However, this would not constitute a default and investors would not be able to claim the difference from the issuer, as they would have received interest payments in line with the bond terms and conditions after a breach of the amortisation test.
Fitch's cash flow model tests that, even after a breach of the amortisation test, the modelled recoveries on the bonds would be at least 91% under 'AAA' stresses, corresponding to two notches' uplift for recovery under the agency's covered bonds rating criteria (see *Related Criteria* above).

After an issuer event of default occurs, the CBC will make best efforts to sell assets every six months to redeem all covered bonds that have become pass-through (due to not having been repaid in full on their maturity date or due to a breach of amortisation test), if applicable, provided this does not negatively affect the amortisation test. This is not taken into account in Fitch's analysis, as the agency models a worst-case scenario where no buyer could be found for the pool.

Maturity Profile

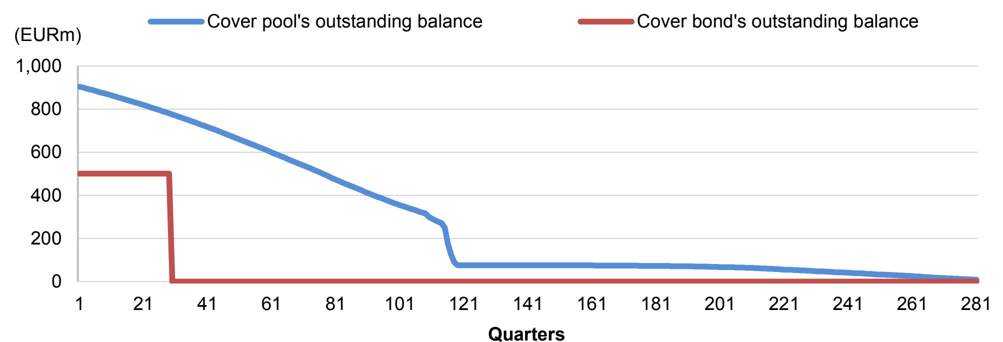
The cover assets have a WA maturity of 26.5 years, while the covered bonds have an expected maturity of 7 years. Aegon Bank has the obligation to meet the payments on the bonds at their maturity date. After an issuer event of default resulting from Aegon Bank failing to meet these payments, or in case of a breach of the amortisation test, the bonds will become due by their final legal maturity date 32 years later, making the bonds effectively pass-through.

Aegon Bank's cover pool contains long-term IO mortgage loans, which may not fully amortise before the final maturity date, giving rise to liquidity risk. However, the high excess spread in the programme means that even under severe stresses in Fitch's cash flow model there would be no need to sell any assets as the cash flows should be high enough to repay the covered bonds on time.

In its cash flow analysis Fitch modelled a minimum benchmark size EUR500m bond with a 7-year term and a fixed coupon of 1.0% a year. The agency modelled a higher coupon than expected for the actual issuance to reduce the volatility of the breakeven AP for future issuances from the programme.

Figure 7

Amortisation Profile



Source: Fitch, Aegon.

More generally, an issuer event of default will also be triggered when: Aegon Bank fails to make payments on any of its financial or material obligations; the issuer is wound up or goes bankrupt; or a liquidator is assigned. After an issuer event of default, the CBC will pay the interest due on the bonds and will accumulate the proceeds from the assets until the maturity

date of the bonds, at which point they will be used to repay the bonds. It is only upon a breach of the amortisation test that all bonds will be paid pro rata.

A failure by the issuer to meet principal payments at the bonds' expected maturity triggers the 32-year maturity extension for the bonds. The guarantor will make efforts to sell parts of the portfolio during the extension period to fully redeem the extended series. In addition, upon a breach of the amortisation test, all bonds will switch to pass-through amortisation (see *Amortisation Test* above). This may lead to investors receiving proceeds earlier than the expected maturity on the bonds.

Interest Rate Risk

There is no swap between the assets, which are mostly at a fixed rate, until their next interest reset date (on average at 14 years), and the bonds, which are issued at a fixed rate. There is some natural hedging between the proportion of fixed mortgage assets (82.6%) and the fixed-rate bonds, with the interest rate risk initially stemming from the floating-rate assets. However, the interest rate risk could increase significantly, due to the flexibility given to borrowers to reset their mortgages at a future date. This could lead to a downward migration of the WA interest rate on the mortgage receivables. In addition, any new issuance of covered bonds at a higher rate than the initial issuance will reduce the excess interest rate between the assets and the bonds, which could affect the breakeven AP for a given rating.

The first public issuance is expected to be a fixed-rate bond up to the maturity date, with the extension period also at a fixed rate until the extended maturity date. The most stressful scenario for the bond would be when fixed-rate mortgages reset at lower fixed or floating rates, potentially causing a large interest rate mismatch between the cover pool and the bonds outstanding.

Fitch modelled a conservative low fixed interest rate at the reset date for fixed-rate loans and a conservative margin above three-month Euribor for floating-rate loans. At the reset dates Fitch assumed that 30% of fixed-rate loans will revert to floating and that the floating-rate loans will remain floating. Aegon Bank's data from 2005 onwards shows that on average 10.0% of borrowers switched from fixed to floating rate and 5.2% of borrowers switched from floating to a fixed rate. However, the long interest reset date on the fixed-rate mortgages means even a migration to an interest rate as low as 1% on the loans has little impact on the 'AAA' breakeven AP, as significant excess interest from the high fixed-rate loans remains until the reset date.

The breakeven AP for a rating will be affected, among other things, by the profile of the assets relative to the outstanding covered bonds, which can change over time, even in the absence of new issuance, and should not be assumed to remain constant.

The interest and maturity of any future bond issuance could increase interest rate mismatches, causing the breakeven AP for the rating to be more volatile than in a fully hedged programme.

To mitigate certain mismatches between the interests received on the assets and those payable under the covered bonds, the transaction documents include the option for Aegon Bank to enter into portfolio or interest swap agreements.

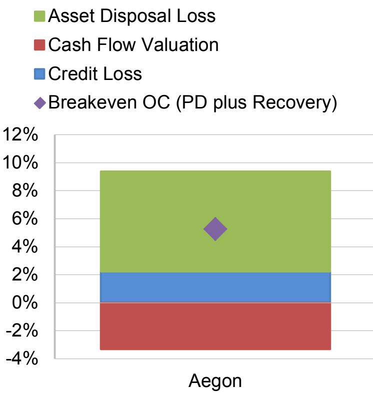
Commingling Risk

As long as the borrowers have not been notified to direct their mortgage payments to the CBC or to a new account bank, they will keep paying the servicers, so that in an insolvency event cover pool funds may be commingled with the bankruptcy estate of the issuer.

Cover pool collections are paid into an account held with ABN AMRO, in the name of Aegon Nederland (unrated). After the occurrence of certain events, such as an assignment notification event or a breach of ACT notice, Aegon Nederland will forward any moneys collected to the

Figure 8

Breakeven OC Components



Source: Fitch

CBC account on a monthly basis.

As Aegon Nederland as the collection account holder is not rated at least ‘A’/’F1’ Fitch does not consider it an eligible counterparty under its counterparty criteria and therefore does not regard commingling risk to be sufficiently mitigated for a ‘AAA’ covered bonds rating. The agency therefore sizes for the potential amount at risk, equal to the maximum monthly exposure that could be subject to commingling risk. Fitch has sized for commingling risk equal to one month of collections on the cover pool in its cash flow analysis.

Insurance Set-Off

Aegon Bank has EUR30.2m of mortgages in the pool that are potentially exposed to insurance set-off. These are traditional life and universal life mortgage loans, accounting for 1.2% and 2.2% of the cover pool, respectively. As borrowers keep paying the insurance provider, the exposures with the insurer provider will continue to grow until the loan matures. If an insurance provider defaults and the borrower invokes a right of set-off on his loan for the accumulated amounts paid to the insurance company, the CBC could incur a loss on these loans. This depends on the likelihood that set-off rights will be recognised for the borrowers. This is more likely to be the case if the loan and the insurance contract have been sold as one product.

Fitch calculated the likelihood of default of the insurance company, Aegon Leven, in a ‘AAA’ scenario and combined it with the probability that borrowers would exercise set-off, and the increase of exposure to the insurance companies as borrowers pay their premium over time. The agency determined the risk of borrower’s set-off claims being legally valid to be 100% which is the probability assumed for internal insurance providers. When estimating the capital accumulation Fitch considers prepayment rates, default rates, the rate of return on the policies and the capital cost. As insurance set-off risk in relation to life mortgage loans is not sized for in the ACT, Fitch has made an adjustment to the breakeven AP to account for the maximum set-off exposure. This was sized at 0.1% of the pool.

Breakeven AP for the Rating

The ‘AAA’ breakeven AP is based on the expected EUR500m benchmark issuance with a 7-year term. When determining the ‘AAA’ breakeven AP for this programme, Fitch has modelled a fixed coupon of 1.0% for the bond. Under these assumptions, Fitch calculated a ‘AAA’ breakeven AP of 95%, which relates to a ‘AA’ tested rating on a PD basis and recoveries given default of at least 91% at ‘AAA’, supporting a two-notch uplift to the ‘AAA’ covered bond rating.

The equivalent ‘AAA’ breakeven OC of 5% is mainly driven by the credit loss component (2.2%) and the cash flow valuation (-3.3%), reflecting the excess spread in the programme. The asset disposal loss component (7.2%) reflects (i) the negative carry in a scenario where cash proceeds are reinvested at a sub-Euribor rate, and (ii) the cushion between the model output and the legal minimum overcollateralisation level of 5% (see Figure 8).

Fitch’s cash flow analysis identifies the worst-case scenario by comparing high and low prepayment scenarios combined with stressed default timing and interest-rate assumptions according to general or country-specific Fitch criteria for covered bonds. Generally, the low prepayment scenario is likely to be the worst case for covered bonds that do not feature a conditional pass-through regime. This is due to the need to sell assets to make the redemption payment on a covered bond when due, and as a result the asset disposal loss component is typically the driver of the breakeven OC.

For Aegon Bank the high prepayment is the worst-case scenario, due to the negative carry from investing cash proceeds at a lower rate than the fixed interest on the bonds up to their maturity. Instead, the low prepayment scenario leads to lower losses owing to the high excess spread associated with the long interest reset period of the cover pool assets, which largely compensate for the credit risk on the assets. However, the possibility that the low prepayment scenario becomes the driving one in the future – through adding assets with a lower margin or

issuing covered bonds at a higher coupon – cannot be ruled out. In addition, Fitch will account for any potential risk from the long-term IO loans in the determination of the breakeven AP as explained below.

High Prepayment Scenario

The asset disposal loss component is driven by the modelled high prepayment rate of up to 25% in line with Fitch's assumptions for The Netherlands (see *Related Criteria*), leading to a high cash build-up from early collection which is modelled to be re-invested at Euribor minus a conservative margin yielding a lower rate than the interest on the bonds. The adjustment of the 'AAA' breakeven AP to the legal minimum OC is added to the asset disposal loss component.

The cash flow valuation component leads to a lower 'AAA' breakeven OC due to the excess spread over the lifetime of the assets, resulting in a stressed present value of the assets being higher than the present value of the liabilities.

The credit loss of 2.2% reflects the impact of the WA default rate of 11.1% and the WA recovery rate of 80.4% in a 'AAA' scenario. The credit loss component is the lowest for Aegon Bank's programme relative to its peers, because of the low share of IO loans in the portfolio (31.9%) and a low average DTI ratio (24%). The high portion of NHG loans (69.0%) and small share of loans secured by illiquid properties (6.3%) drive the high WA recovery rate.

The long-term IO mortgage loans would not need to be liquidated in the high prepayment scenario as in that scenario they would be repaid before the extended maturity date of the covered bonds.

Low Prepayment Scenario

In a low prepayment scenario there is a risk that some of the long-term mortgage loans in the cover pool may still be outstanding at the final extended maturity date of the longest outstanding covered bond, giving rise to the need to sell assets for timely payment. To ensure that no liquidity risk would occur in that scenario, Fitch will make a deduction corresponding to the amount at risk in the breakeven AP should the low prepayment scenario become the driving one in future.

Figure 9

Drivers of Cash Flow Valuation Component for Aegon Bank's Breakeven OC

Driver	Assets	Covered bonds
Fixed rate (%)	82.6	100
WA current margin (%)	3.3[a]	1.5
Worst case prepayment assumption (%)	25	
WAL (years) under scheduled amortisation	22.0	7.0
WAL (years) including worst case prepayments	4.1	

[a] Incorporates Fitch assumed compressed margins
Source: Fitch

In the future, the breakeven AP for the rating will be affected, among other things, by the credit quality of the cover pool and the profile of the cover assets relative to the outstanding covered bonds, which can change over time.

AP Fitch Relies On

Fitch bases its analysis on the 10% committed OC, translating into an AP of 91%, which is part of the programme's ACT calculation and is more conservative than the AP of 93% that will be published in the programme's monthly investor report. The contractually committed AP may change. However, the OC in the programme must at least be equal to the legal minimum OC of 5%.

Ongoing Programme Review

Fitch will periodically review the credit quality of the cover pool and perform a cash flow analysis to assess whether the AP it takes into account provides protection against identified risks commensurate with the rating of the covered bonds issued by Aegon Bank under this programme. Cover pool and covered bonds information will be updated regularly and displayed on Fitch's covered bond surveillance tool (available at www.fitchratings.com) and in the quarterly *Covered Bonds Surveillance Snapshot* (October 2015).

Appendix 1: Programme Summary

Under this programme, from time to time Aegon Bank can issue covered bonds up to EUR5bn secured by a dynamic pool of residential mortgage loans located in the Netherlands and up to 20% eligible liquid assets, the latter being the maximum allowed under the Dutch covered bond legislation. The covered bonds rank pari passu among themselves. They represent direct, unsecured and unconditional obligations of Aegon Bank and are guaranteed by the CBC, which is the owner of the cover assets. The CBC was incorporated to act solely for Aegon Bank's covered bond programme. The programme is regulated by the DNB under the Dutch covered bonds legislation.

Figure 10

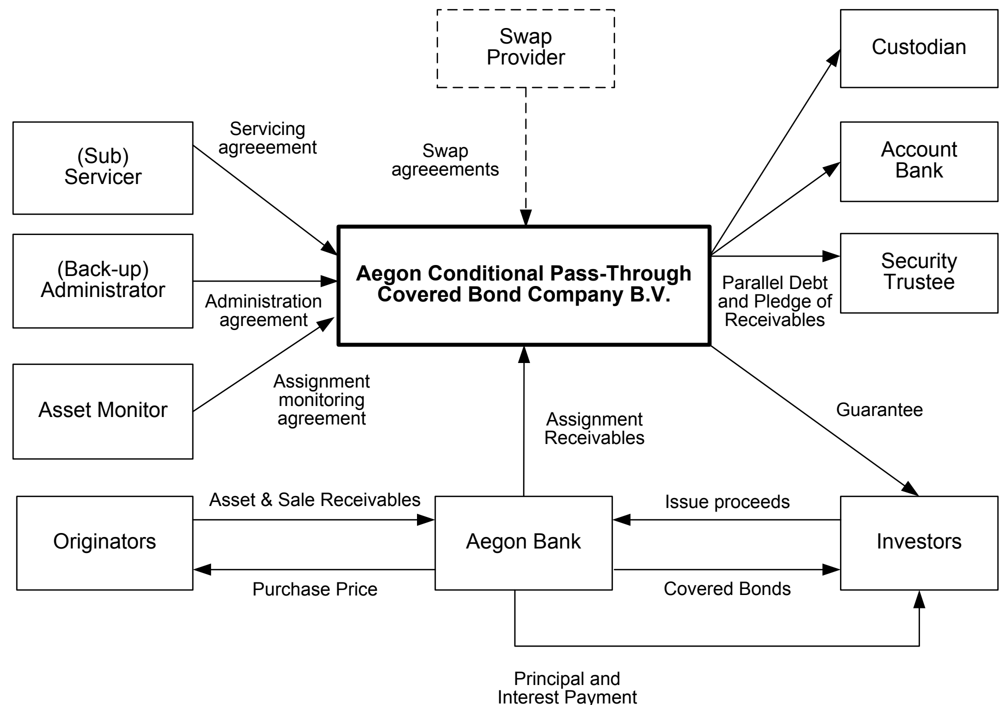
Main Parties

Aegon Bank N.V.	Issuer Seller/originator Servicer Administrator
Aegon Leven and Aegon Hypotheken	Originators, Servicers
Aegon Conditional Pass-Through Covered Bond Company B.V.	Guarantor
Citibank, N.A., London Branch	Principal paying agent
Stichting Security Trustee Aegon Conditional Pass-Through Covered Bond Company	Security trustee
PricewaterhouseCoopers Accountants N.V.	Asset monitor
Intertrust Administrative Services B.V.	Back-up Administrator
N.V. Bank Nederlandse Gemeenten	Account bank/GIC provider
Coöperatieve Centrale Raiffeisen-Boerenleenbank B.A.	Custodian

Source: Programme documents

Figure 11

Structure Diagram



Source: Programme documents

Figure 12

Summary of Certain Contractual Features

Contractual features	Summary
ACT	The ACT is designed to ensure a minimum level of OC on the covered bonds to protect bondholders against specific credit and market risks; it is calculated monthly (unless an issuer event of default occurs). The minimum OC stipulated in the Dutch covered bond law is the higher of i) 5% nominal OC; and ii) 0% OC when taking into account only the share of loans up to 80% of the property value. A breach of the ACT will not constitute an issuer event of default. However, until remedied it will prevent the issuer from issuing any further covered bonds and the CBC will not be allowed to make any payment to the issuer and the subordinated loan provider.
Amortisation test	After an issuer event of default and the service of a notice to pay on the CBC, an amortisation test verifies whether the value of the cover pool, including any cash held in the deposit account and any substitution assets, adjusted to account for delinquencies and collateral value, is at least 10% higher than the notional amount of outstanding covered bonds, and at least as high when taking into account only the share of loans up to 80% of the property value. Failure to pass the amortisation test allows the trustee to serve a breach of amortisation test notice on the issuer and the CBC, upon which all outstanding covered bonds become pass-through. The CBC will undertake its best efforts to sell the loans and the proceeds from such a sale will be used to repay, pro rata, the outstanding covered bonds, provided they are sufficient to redeem the relevant bonds. If the proceeds are insufficient the sale will not go through and will be repeated every six months until the proceeds are sufficient. However, six months before the first extended due for payment date of any outstanding series, the CBC will offer the loans for sale on a monthly basis up to and including the extended due for payment date, at the best terms it can achieve, subject to approval from the trustee Such proceeds may be lower than needed to repay the covered bond in full. The amortisation test mitigates time subordination of covered bonds within the programme.

Source: Programme documents

Appendix 2: D-Cap Assessment for Aegon Bank's Covered Bonds

Asset Segregation: Moderate Risk

Fitch expects ring-fencing of the cover pool to be effective when applying any D-Cap assessment other than full discontinuity, due to the "all or nothing" nature of this risk. The differentiation between the D-Cap categories is based on whether any portion of the cash flow or assets might still be lost (and if so, to what extent), which would lower the cover pool amount available to bondholders.

A moderate risk assessment is applied to most Dutch programmes, because Fitch is of the view that there is some residual commingling and various set-off risks in these programmes.

Figure 13

Asset Segregation: Moderate Risk

Component driver	Fitch assessment
Segregation of cover pool from other creditors of issuer	Effectively done via silent title assignment ("stille cessie") from the issuer to the CBC in line with other Dutch covered bonds and RMBS programmes. Under the terms of the silent assignment law, the legal ownership of the receivables can be transferred by registering a deed of assignment with the relevant tax authorities, without having to notify the borrowers of the assignment. In addition, the mortgages and other rights of the issuer are pledged to the security trustee via pledge agreements. The borrowers will be notified of the transfer of the loans to the CBC upon an assignment notification event that occurs, among other things, if: the issuer fails to make a payment or to fulfil or comply with any of its other obligations and this failure is not remedied within 10 business days of receiving notice thereof from the CBC or trustee; action is taken by or against the issuer for its dissolution, liquidation, demerger or bankruptcy, or its entering into emergency regulations; or an issuer or CBC event of default occurs.
Excess OC immune from claims from other creditors	The transfer of the assets under a true sale ensures effective segregation of the assets from the issuer's bankruptcy estate.
Asset and liability clawback risk	The assets are transferred by means of a true sale to the CBC. In addition, the CBC is set up as a limited-recourse, bankruptcy-remote entity that only enters into agreements with the transaction parties (which sign up to the limited recourse language). Claw-back risk on monies paid to bondholders just before an insolvency event of the issuer is also unlikely because the parties and potential creditors acknowledge that entering into a covered bond transaction does not harm their interests.
Commingling risk	Cover pool collections are paid into an account held with ABN AMRO in the name of Aegon Nederland (unrated). As Aegon Nederland as collection account holder is not rated at least 'A'/'F1' Fitch does not consider it an eligible counterparty according to the agency's counterparty criteria for 'AAA' rated bonds. It therefore does not consider commingling risk to be sufficiently mitigated. Fitch sizes for the amount at risk in the 'AAA' breakeven AP calculation at one month of collections from the pool.
Set-off risk for deposits, construction deposits and insurance products	Deposit set-off risk is mitigated by a deduction in the ACT of all deposits exceeding the amount guaranteed by the Dutch deposit guarantee scheme (EUR100,000 per borrower) if Aegon Bank's long-term or short-term ratings fall below 'A' or 'F1' respectively. Aegon Bank mitigates construction set-off risk through deducting any undrawn amount in the ACT. The following insurance mortgage products can be included in the pool: investment mortgage loans, insurance savings mortgage loans, bank savings mortgage loans, life mortgage loans, universal life mortgage loans or any combination of the above. Life insurance mortgages are subject to potential set-off risk, which is not sized for in the ACT. Fitch has made an adjustment to the breakeven AP to account for the insurance set-off exposure. Fitch considers any set-off risk related to investment mortgage loans to be very limited, as policy providers usually hold the investment accounts with bankruptcy-remote special-purpose vehicles. Set-off exposure related to insurance and bank savings mortgage loans is mitigated through sub-participation agreements Aegon Bank entered into, and is also accounted for in the ACT.

Source: Fitch

Liquidity Gap and Systemic Risk: Minimal Discontinuity

The analysis of the liquidity gap and systemic risk component considers short-term liquidity risks, principal payment risk and systemic risks. In most countries with established mortgage markets, a moderate risk liquidity gap and systemic risk assessment will usually apply for non-pass-through programmes if the liquidation protection period is at least a year, although a higher risk assessment might apply if the liquidity mechanism is considered weak. A minimal discontinuity assessment applies when there are no liquidity gaps within a programme, such as for pass-through programmes with coverage for interest payments and expenses for the next three months on a rolling basis.

Figure 14
Liquidity Gap and Systemic Risk: Minimal Discontinuity

Component driver	Fitch assessment
Principal protection	Conditional pass-through structure with a 32 years' extendible maturity avoids a stressed sale of assets due to the current cover pool characteristics. The potential amount at risk of stressed asset sales in the low prepayment scenario arising from the long-term mortgage loans in the cover pool will be deducted from the breakeven AP should the worst-case scenario switch from high to low prepayment. Therefore, no asset sale would be needed to repay the bonds by their legal final maturity.
Limitations of principal protection mechanism	None highlighted.
Liquidity protection	The reserve fund covers six months' interest due and other senior expenses. It is held by the CBC in the GIC account at an institution rated at least 'A'/'F1' (currently Bank Nederlandse Gemeenten).
Senior/pari passu termination or intra-group loan payments	Should there be a swap agreement, termination payments (payable upon swap termination due to swap counterparty default) would be subordinated to the covered bonds' principal and interest payments.
Systemic risks	No additional stress is applied due to the pass-through nature, which avoids the need to sell assets.

Source: Fitch

There should be no need to liquidate assets in pass-through programmes as this is naturally achieved by full amortisation before the covered bonds' legal final maturity date. Aegon Bank's cover pool may contain long-term IO mortgage loans, which may not be repaid before this date, giving rise to residual liquidity risk. But the high excess spread means that even under severe stresses there is no need to sell any assets as the cash flows are high enough to repay the covered bonds on a timely basis.

The minimal discontinuity assessment for the liquidity gap and systemic risk of Aegon Bank's programme is in line with all conditional pass-through programmes with three-month interest reserve (plus senior costs) fund.

The 2015 legislative amendments to the Dutch covered bonds framework requires a reserve fund to cover interest obligations and other senior costs due in the next six months. This amendment becomes effective in January 2016 for existing DNB registered programmes and is already effective January 2015 for new applicants and therefore is binding for Aegon Bank.

Alternative Management

Systemic Alternative Management: Low Risk

Fitch takes into consideration the framework or contractual clauses governing the appointment of a substitute manager — together with the length of time required to appoint one — any potential conflict of interest (where a single administrator in a bankruptcy takes care of covered bonds and other creditors), the manager's responsibilities in the servicing and liquidation of the cover assets to meet payments due on the covered bonds and any further protection due to oversight or potential support for regulated covered bonds.

A low risk assessment is applied to all Dutch covered bond programmes registered with the DNB. The DNB regularly monitors, among other things, the programme's asset/liabilities ratio in light of the balance-sheet encumbrance to ensure a healthy ratio is maintained. Aegon Bank has ongoing reporting obligations towards the DNB and needs to keep fulfilling the programme's registration requirements.

Figure 15

Systemic Alternative Management: Low Risk

Component driver	Fitch assessment
Does administrator take exclusive care of covered bondholders? When are they appointed?	Aegon Bank is taking on the role as administrator. Intertrust Management B.V. is appointed as back-up administrator and will take on the management/administration/cash management role of the CBC and any other reporting activities should Aegon Bank default.
Importance of timeliness of payments in the legal provisions	High. Protection is provided by a six-month dynamic reserve fund (interest and senior costs). The principal extended due for payment date is 32 years. The cover pool contains long-term IO mortgage loans but the high excess spread on the assets mitigates the risk of forced asset sales. In addition, long-term IO loans exceeding 10% of the current balance of the mortgage loans are not given any credit in the ACT.
Substitute manager able to sell cover assets or borrow to make timely payments	Should a liquidation of the cover pool be contemplated, Intertrust will assign a reputable corporate finance firm to manage a sale and look for a potential buyer. The conditions of the sale would be subject to the security trustee's consent.
Regulatory oversight	Fitch considers DNB's active oversight positive for bondholders. Under the Dutch legislative framework, the covered bond issuers have ongoing reporting duties to demonstrate that the covered bond programmes fulfil the regulatory requirements for registration. Fitch gives credit to the registered status of Dutch covered bonds by applying a low systemic alternative management risk assessment to Dutch regulated covered bonds programmes.

Source: Fitch

Cover Pool-Specific Alternative Management: Moderate Risk

Fitch focuses on the likely ease of the transferability of relevant data and IT systems to an alternative manager and buyer, and also considers the quality and quantity of data provided. Fitch expects a moderate risk assessment, such as that applied for Aegon Bank and most Dutch programmes, for most mortgage programmes with issuers with IT systems that are very capable of managing cover pools, covered bonds and data delivery. Fitch considers factors in Figure 16 when judging this ability.

Figure 16

Cover Pool Alternative Management for Aegon Bank's Covered Bonds

Component drivers	Fitch assessment
Cover assets, debtors' accounts and privileged swaps clearly identified within IT systems	Strong systems and processes, comparable with other Dutch programmes.
Standardised or custom-made IT systems used	Aegon Bank uses the PRoMMiSe system developed by Hypoport and widely used among Dutch covered bond and RMBS issuers.
Automation and speed of cover pool reporting	Reporting is largely automated through PRoMMiSe. Investor reports will be generated monthly.
Adequate filing of loan documentation, evidence of security	Aegon Bank files the loan documentation adequately in its systems, which are backed up automatically. Disaster recovery procedures are in place.

Source: Fitch

Privileged Derivatives: Very Low Risk

Fitch considers programmes encompassing privileged hedging agreements to be more vulnerable to a potential insolvency of the issuer.

A very low risk assessment, which applies to Aegon Bank's programme, is for programmes without any privileged derivatives.

The programme is unhedged. However, the documents give Aegon Bank the option to enter into a portfolio or interest rate swap whenever it considers it necessary and market circumstances require entry into a hedge. Certain mismatches between the cover pool and covered bonds could be hedged by a portfolio swap, where the proceeds of the pool will be hedged for a fixed or floating interest rate on one or more series of covered bonds. In addition to the portfolio swap, the CBC may enter into hedging arrangements under which a certain fixed/floating rate will be exchanged for a specific rate on one or more covered bonds series.

Appendix 3: Originator and Servicer Operational Review

Origination

Aegon historically originated mortgages under its Aegon Levensverzekering N.V. (Aegon Leven) brand name. However, since April 2011, new mortgage loans have been originated by Aegon Hypotheken B.V., a 100% subsidiary of Aegon Nederland N.V. All underwriting and servicing activities remain with Aegon Leven.

At end-3Q15, Aegon's portfolio of residential mortgage loans was EUR30.6bn. Aegon is the fourth-largest lender in the Dutch mortgage market, with around 11% market share based on new sales.

Aegon Bank sources all its mortgages through intermediaries. It does not accept mortgage applications via the internet or through a branch network.

Aegon NL consists of two main functions – the Sales Organisation and Servicer Centres. The sales function is responsible for maintaining relationships with intermediaries, while the service centres process new mortgage applications (including credit assessment and underwriting), and complete loan administration and collection duties. The service centres employ 140 staff (121 full-time equivalent) at an office in Leeuwarden.

All mortgage loan-related processes are periodically reviewed and are regularly audited.

Underwriting

Applications are transmitted in electronic form to the underwriting team of 47 full time staff. Credit searches are completed with the Credit Registration Office (BKR, Bureau Kredietregistratie), and the fraud registers Stichting Fraudebestrijding Hypotheken and Externe Verwijzings Applicatie, while underwriting criteria are based on the Dutch Code of Conduct. Aegon Bank states that about 20% of applications are declined immediately following completion of BKR checks and an initial underwriting assessment – typically due to negative BKR results or loans not being affordable. The average acceptance rate is about 75%.

Any approval to lend outside the automatically accepted lending criteria is granted loan by loan subject to senior underwriter approval. These "explain" cases are very rarely approved and represent less than 2% of Aegon Bank's total mortgage book.

Intermediaries analyse and advise on potential borrowers' data, adhering to Aegon's underwriting criteria. All underwriting decisions are centralised in Aegon's Leeuwarden office.

Key Lending Criteria

Aegon Bank's lending criteria are consistent with the Code of Conduct, the Act on Financial Supervision and, for mortgage loans benefiting from an NHG guarantee, the criteria set by WEW.

Highlights of Aegon Bank's defined lending criteria are:

- loan to market value maximum of 103% since 2015 (decreased steadily from 109% in 2009 and continuing to decrease to 100% by 2018);
- standard income multiples at 4.5x gross salary ("explain" cases maximum 6.5x);
- lending only against owner occupied residential property and always with first lien;
- life insurance coverage of the loan part exceeding 80% LTMV;
- no self-certification of income;
- three years' evidence of income required from self-employed borrowers;
- IO portion of loan capped at 50% of the market value, since August 2011.

Lending Authority

Underwriting mandates are as set out in Figure 17.

Figure 17

Lending Authority Schedule

	No. FTE	Lending authority
Underwriter	35	Up to EUR400,000
Senior underwriter	12	Up to EUR700,000
Underwriting co-ordinator and managers	4	Up to EUR2,200,000
Management team	2	Above EUR2,200,000

Source: Aegon Bank

Property Valuation

Aegon always requires a satisfactory full valuation completed by an approved valuer. The valuation must have been completed within the last six months, while a tax assessment is accepted for applications less than 90% loan to foreclosure value). For mortgages originated after 1 January 2014 the threshold is 67%. For new-build houses, Aegon accepts a building and purchase agreement.

Servicing

Servicing activities, including arrears management and the foreclosure process, are carried out by Aegon Leven staff.

Aegon's timeline for arrears management is fairly typical of the Dutch prime mortgage market. Key stages of the process are highlighted below:

- automated letter sent at day 15 after first missed payment;
- telephone contact attempted at day 30
- formal demand for payment sent at day 45;
- loan transferred to arrears department and put on "telephone collections" list at day 60;
- loan placed on an "urgent arrears" list at day 90, which leads to more vigorous contact attempts;
- loan declared immediately due at day 120; Aegon Bank will make a final attempt for voluntary payment, and after allowing time for the drafting of legal document will begin the foreclosure process;
- possession of the property typically obtained about six months after the first missed payment.

Appendix 4: Outstanding Liabilities

Figure 18
List of Outstanding Covered Bonds

Series	Currency	Interest rate type	(Size/bn)	Coupon rate	Payment frequency	Maturity	ISIN

Source: Aegon Bank

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