

# Covered Bonds

Introduction to the Programme

August 2020

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# Covered Bond Programme



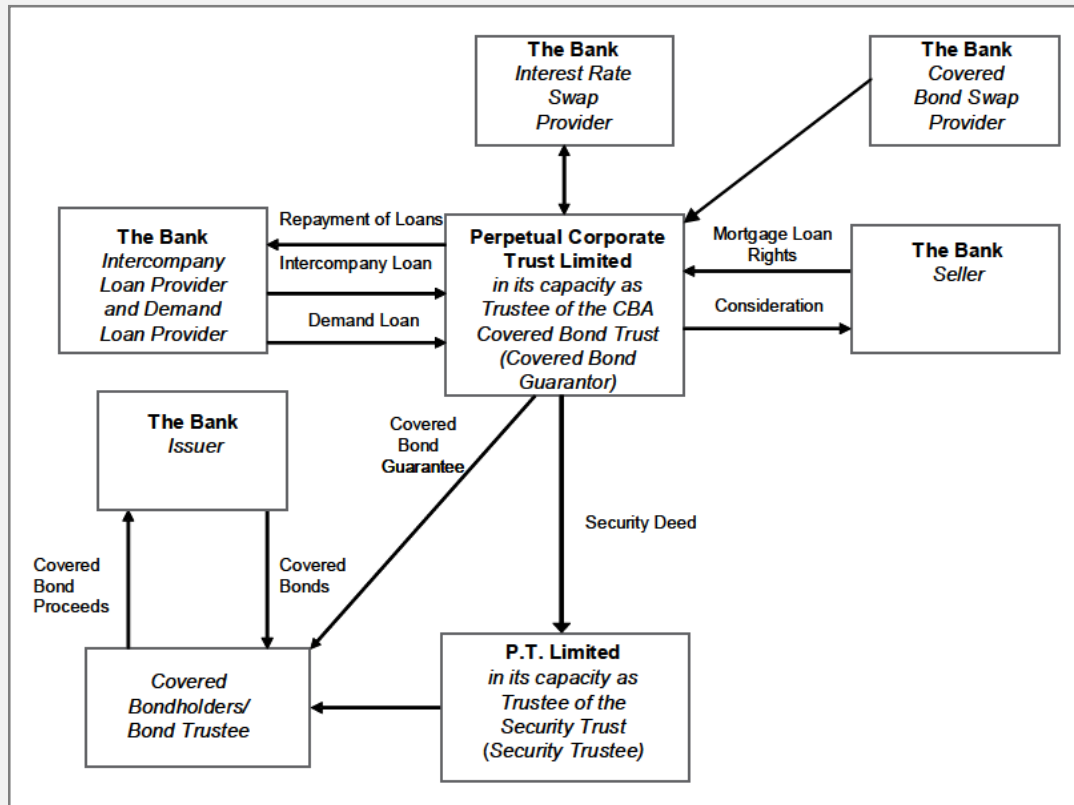
# Australian Covered Bond Legislation

- The Australian parliament passed the Banking Amendment (Covered Bonds) Bill in October 2011
- Issuance only allowed under the legislative framework
- The ADI (e.g. CBA) must be the covered bond issuer
- Segregation of cover assets achieved via a special purpose vehicle
- Legislation provides legal certainty for the segregation of the cover pool in bankruptcy
- Maximum cover pool assets of 8% of ADI assets in Australia
- Minimum 3% over-collateralisation
- Limitation on eligible cover pool assets
- Independent cover pool monitor
- APRA has established a Prudential Standard APS121 and has certain other powers with regards covered bond issuance

# CBA Covered Bond Programme



## CBA Covered Bonds Structure



- CBA cover pool assets include:
  - Mortgage Loans<sup>1</sup>
  - Cash
  - Government Bonds, Semi Government Bonds and Bank Bills (15% in total)
- Derivatives relating to the covered bond issuance such as currency and interest rate swaps
- Prime Australian residential mortgages (max LVR of 80% in the ACT)
- Maximum covered pool is 8% of assets in Australia

1. For more detail on the Covered Bond Pool, please refer to the Investor Reports on <https://www.commbank.com.au/about-us/investors/covered-bonds.html>

2. Where applicable, capitalised terms have meanings given to them in the Covered bond prospectus

# Programme Summary – US\$30bn Reg S / 144a / A\$



<b>Issuer</b>	<ul style="list-style-type: none"> <li>Commonwealth Bank of Australia</li> </ul>
<b>Covered Bond Guarantor</b>	<ul style="list-style-type: none"> <li>Perpetual Corporate Trust Limited in its capacity as Trustee of the CBA Covered Bonds Trust</li> </ul>
<b>Trust Manager</b>	<ul style="list-style-type: none"> <li>Securitisation Advisory Services Pty Limited (wholly owned subsidiary of Commonwealth Bank of Australia)</li> </ul>
<b>Programme limit</b>	<ul style="list-style-type: none"> <li>US\$30bn (Reg S / 144A / A\$)</li> </ul>
<b>Expected Ratings<sup>1</sup></b>	<ul style="list-style-type: none"> <li>AAA (Fitch) / Aaa (Moody's)</li> </ul>
<b>CBA Credit Rating (LT/ST)<sup>1</sup></b>	<ul style="list-style-type: none"> <li>A+ / F1 (Fitch) / Aa3 / P-1 (Moody's)</li> </ul>
<b>Maximum Asset Percentage</b>	<ul style="list-style-type: none"> <li>95%</li> </ul>
<b>Collateral</b>	<ul style="list-style-type: none"> <li>Prime Australian residential mortgages, Substitution Assets and Authorised Investments</li> </ul>
<b>Mortgage LVR Cap</b>	<ul style="list-style-type: none"> <li>80% of latest valuation</li> </ul>
<b>Indexation</b>	<ul style="list-style-type: none"> <li>Included using the ABS House Price Index (see Slide 8)</li> </ul>
<b>Cover Pool Monitor</b>	<ul style="list-style-type: none"> <li>PricewaterhouseCoopers</li> </ul>
<b>Security Trustee</b>	<ul style="list-style-type: none"> <li>P.T. Limited in its capacity as Trustee of the Security Trust</li> </ul>
<b>Bond Trustee</b>	<ul style="list-style-type: none"> <li>Deutsche Trustee Company Limited</li> </ul>
<b>Governing Law</b>	<ul style="list-style-type: none"> <li>English / State of New South Wales</li> </ul>

1. As at 31 May 2020.



# Structural Enhancements

<b>Asset Coverage Test</b>	<ul style="list-style-type: none"><li>The Asset Coverage Test (ACT) is performed monthly by the Trust Manager to test the Adjusted Aggregate Mortgage Loan Amount is at least equal to the A\$ equivalent of all outstanding covered bonds</li></ul>
<b>Amortisation Test</b>	<ul style="list-style-type: none"><li>The Amortisation Test is performed monthly by the Trust Manager following the service of a Notice to Pay to test that the Amortisation Test Aggregate Mortgage Loan Amount is at least equal to the A\$ equivalent of all outstanding covered bonds</li></ul>
<b>Pre-maturity Test</b>	<ul style="list-style-type: none"><li>The Pre-maturity Test is performed daily by the Trust Manager for twelve months prior to a hard bullet covered bond maturity to test that such maturity can be met. Issuer Event of Default will occur where the rating of CBA falls to Moody's short term rating P-2 or Fitch short term rating F1 and the hard bullet covered bond maturity has not been pre-funded for 6 months</li></ul>
<b>Reserve Fund</b>	<ul style="list-style-type: none"><li>While CBA is rated below F1+, CBA has established a Reserve Fund to credit the income accrued on each covered bond within the next three months and fees due and payable to servicer, cover pool monitor and trustee</li></ul>
<b>Interest Rate Swap</b>	<ul style="list-style-type: none"><li>The Interest Rate Swap will convert mortgage loan receipts (and other asset cash flows) to a floating rate of interest based on Bank Bill Swap Rate. CBA is the initial Interest Rate Swap provider and will be required to post collateral and/or be replaced subject to ratings triggers</li></ul>
<b>Covered Bond Swap(s)</b>	<ul style="list-style-type: none"><li>The Covered Bond Swap will, where necessary, convert payments from the Interest Rate Swap into the required currency and interest rate cash flows to match payment on the covered bonds. CBA is the Covered Bond Swap provider and will be required to post collateral and/or be replaced subject to ratings triggers</li></ul>
<b>Servicer Downgrade</b>	<ul style="list-style-type: none"><li>CBA will be the servicer of loans in the cover pool. If CBA's rating falls below P-1/F1 (Moody's/Fitch) the servicer role will be transferred to a suitably rated institution</li></ul>
<b>Indexation</b>	<ul style="list-style-type: none"><li>House price indexation is included in the ACT. There is no benefit from upward house price indexation given the structure of the ACT. The index is the quarterly Australian Bureau of Statistics (ABS) Price Index for Established Houses for the Weighted Average of the Eight Capital Cities</li></ul>

# House Price Indexation

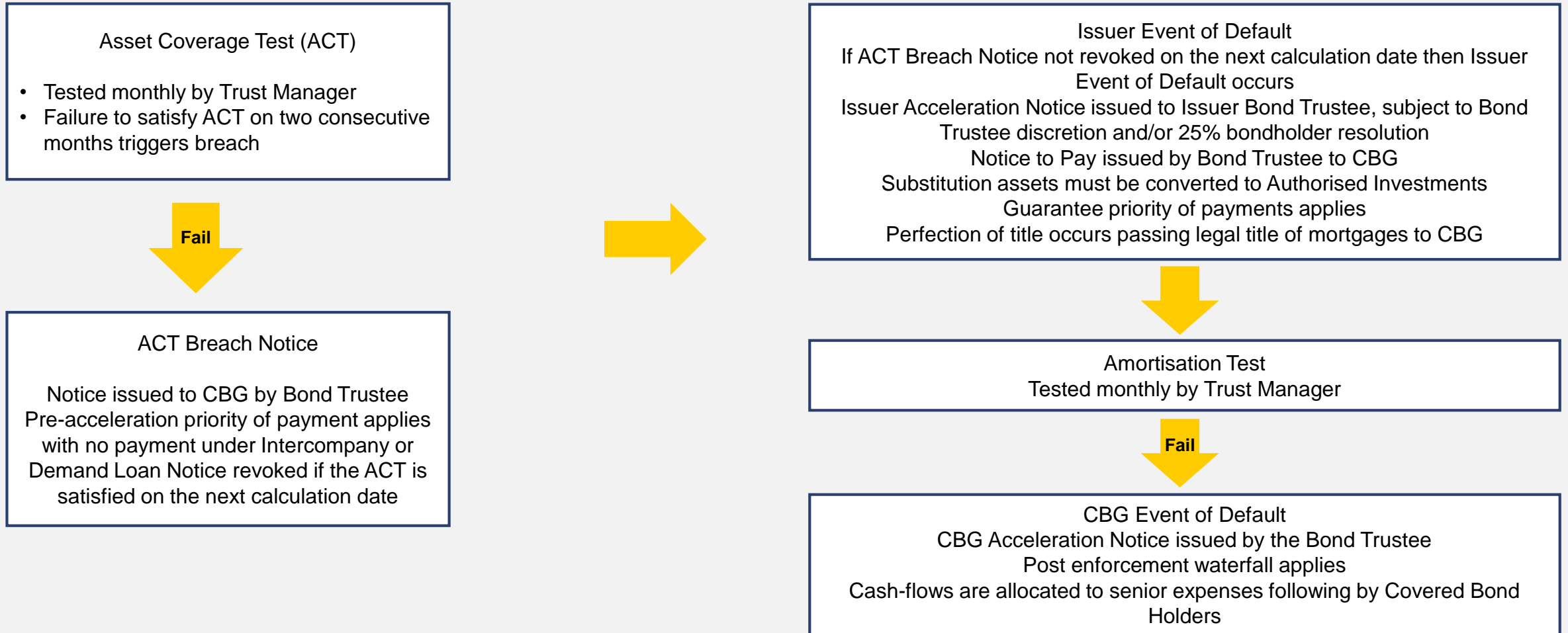


*“The **House Price Index (HPI)** is designed to provide a measure of the inflation or deflation in the price of the stock of established houses over time. Separate indexes are produced for each capital city in Australia, and these indexes are combined to produce a weighted average index of the eight capital cities. The HPI is published quarterly, approximately five weeks after the end of the reference quarter. The figures published for the two most recent quarters are regarded as preliminary and are revised in subsequent publications as more data is collected.” ABS*

- Indexation is used in the Asset Coverage Test and the Amortisation Test to protect investors from a downward move in property prices
- Indexation is applied to the LVR Adjusted Mortgage Loan Balance
- Indexation will be calculated using the Australian Bureau of Statistics (ABS) Weighted Average of Eight Capital Cities Residential Property Price Index<sup>1</sup>
- Applied 85% for upward revision of ABS Index and 100% for downward revision



# Issuer or Guarantor Default and Acceleration



# Asset Coverage Test (ACT)<sup>1</sup>



Adjusted Aggregate Mortgage Loan Amount



Covered Bonds

Adjusted Aggregate Mortgage Loan Amount



**LVR Adjusted Mortgage Loan Balance<sup>2</sup>**  
*is the lesser of*  
 Outstanding Current Principal Balance  
*and*  
 80% of the Indexed Valuation

**Asset Percentage Adjusted Mortgage Balance<sup>2</sup>**  
*is the lesser of*  
 Outstanding Current Principal Balance  
*and*  
 100% of the Latest Valuation  
*multiplied by the*  
 Asset Percentage<sup>3</sup>

*The lesser of*

LVR Adjusted Mortgage Loan Balance

*and*

Asset Percentage Adjusted Mortgage Balance

+

Term Advances and/or Demand Loan Advances unallocated

+

Substitution Assets and Authorised Investments less amounts allocated

+

Principal received in the GIC account

-

Adjustment for negative carry

1. This is only a summary of the Asset Coverage Test. Please see the Offer Document for a complete description. 2. No value is given to mortgages which are more than 90 days in arrears. 3. Asset Percentage is lower of: 95%, percentage notified by Fitch and/or Moody's, or percentage determined by Trust Manager

# Amortisation Test<sup>1</sup>



Amortisation Test Aggregate  
Mortgage Loan Amount



Covered Bonds

Amortisation Aggregate  
Mortgage Loan Amount



Amortisation Test Current Principal Balance

**Amortisation Test Current Principal Balance<sup>2</sup>**

*is the lesser of*  
Outstanding Current Principal Balance  
*and*  
80% of the *Indexed Valuation*



Substitution Assets



Principal received in the GIC account



Adjustment for negative carry

1. This is only a summary of the Amortisation Test. Please see the Offer Document for a complete description. 2. No value is given to mortgages which are more than 90 days in arrears.

# Covered Bond Ratings



## Moody's<sup>1</sup>

- Bonds Issued by Programme rating of Aaa
- Collateral Score 4.0%
- Required minimum over-collateralisation of 0.1%
- Timely Payment Indicator of “Probable”
- TPI Leeway of 4 notches from current Long Term Counterparty Risk Assessment of Aa2(cr)

Estimated OC to maintain current rating in following scenarios:

- Scenario 1: Issuer is downgraded by 1 notch: 2.9%

## Fitch<sup>2</sup>

- Bonds Issued by Programme rating of AAA
- Current Asset Percentage (AP) is 93% equating to over-collateralisation of 7.5%
- Payment continuity uplift of 6 notches
- AAA expected to be maintained down to BBB+ Issuer Rating - three notches below current A+ (stable)
- WA Frequency of Foreclosure 7.5%
- WA Recovery Rate 50.7%



# Rating Triggers

<b>Pre-maturity Test</b>	Moody's: below P-1 Fitch: below F1+	<ul style="list-style-type: none"> <li>The Pre-maturity Test is performed daily by the Trust Manager for twelve months prior to a hard bullet covered bond maturity to test that such maturity can be met. Issuer Event of Default will occur where the rating of CBA falls to Moody's short term rating P-2 or Fitch short term rating F1 and the hard bullet covered bond maturity has not been pre-funded for 6 months</li> </ul>
<b>Reserve Fund</b>	Moody's: below P-1 Fitch: below F1+	<ul style="list-style-type: none"> <li>CBA has established a Reserve Fund to credit the income accrued on each covered bond within the next three months and fees due and payable to servicer, cover pool monitor and trustee</li> </ul>
<b>Interest Rate Swap and Covered Bond Swap(s)</b>	Moody's: below P-1 and A2 or A1 Fitch: below F1 or A	<ul style="list-style-type: none"> <li>CBA is required to post collateral pursuant to a one way CSA to the Covered Bond Guarantor</li> </ul>
	Moody's: below P-2 and A3, as soon as reasonably practicable Fitch: below F3 or BBB-, within 30 days	<ul style="list-style-type: none"> <li>CBA is to use commercially reasonable efforts to, procure either a guarantee in respect of all present and future obligations or transfer the Interest Rate Swap or Covered Bond Swap</li> </ul>
<b>Transfer Trust Bank Account</b>	Moody's: below P-1 Fitch: below F1	<ul style="list-style-type: none"> <li>The Covered Bond Guarantor bank account must be transferred from CBA to a third party</li> </ul>
<b>Servicer Downgrade</b>	Moody's: below P-1 Fitch: below F1	<ul style="list-style-type: none"> <li>CBA will be the servicer of loans in the cover pool. If CBA's rating falls below P-1/F-1 (Moody's/Fitch) the servicer role will be transferred to a suitably rated institution</li> </ul>
<b>Perfection of Title</b>	Issuer EOD Moody's: below Baa3 Fitch: below BBB-	<ul style="list-style-type: none"> <li>Mortgage loans will be sold to the Covered Bond Guarantor by way of statutory assignment</li> </ul>

# Australian Mortgages Overview



## Australian Mortgage Product

- Principal and interest amortising 25/30 year loan
- Variable interest rate set at bank's discretion
- Limited pre-payment penalty
- Full recourse to borrower
- No tax deduction for owner occupied housing
- Higher risk loans are subject to Lenders Mortgage Insurance (LMI)
- Minimal "low documentation" (i.e. self-certified) market with tighter lending criteria
- Consumer credit regulations
- Major banks account for majority of new originations and "originate-to-hold"
- Lending criteria tightened further by regulator in 2015
- Interest only – assessed on P&I basis



# Appendix



# Income priority of payments (pre-EOD)

1. A\$1 to the Income Unitholder
2. Payment of Accrued Interest Adjustment to CBA if mortgages have been transferred to the Covered Bond Guarantor
3. Payment of expenses to Bond Trustee, Security Trustee and taxes
4. Payment to Servicer, Trust Manager, Account Bank, Cover Pool Monitor
5. If CBA is not the IRS provider, payments due on IRS
6. *Pari passu*: If CBA is IRS and covered bond swap provider, payments on IRS, Covered Bond Swap payments, Intercompany loan payments
7. If Pre-Maturity Test has been breached in respect of any Hard Bullet Covered Bond, credit to Pre-Maturity Ledger
8. Deposit into the Reserve Ledger income accrued on each covered bond within the next three months and fees due and payable to servicer, cover pool monitor, trustee
9. If a Servicer Default has occurred , the remaining Available Income Amount it to be deposited into a GIC account for the benefit of the Security Trustee
10. Payments to satisfy subordinated swap termination payments
11. Indemnity payments (if any) to Cover Pool Monitor
12. Interest on Demand Loan payable to Demand Loan Provider
13. Residual payments to Income Unitholder





# Principal priority of payments (pre-EOD)

1. Reimburse CBA for funding Further Advances (if any)
2. If Pre-Maturity Test has been breached in respect of any Hard Bullet Covered Bond, credit to Pre-Maturity Ledger
3. Acquire additional mortgages to satisfy Asset Coverage Test
4. Deposit remaining Principal Amount to GIC account to satisfy Asset Coverage Test
5. Repayment of senior portion of the Demand Loan (voluntary OC repayment)
6. Principal payments on covered bond swaps and Intercompany Loans
7. Acquire additional mortgage loans
8. Repayment of subordinate portion of the Demand Loan
9. Residual payments to Income Unitholder and Capital Unitholder



# Guarantee priority of payments (post-EOD)

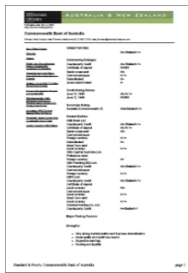
1. A\$1 to the Income Unitholder
2. Payment of Accrued Interest Adjustment to CBA if mortgages have been transferred to the Covered Bond Guarantor
3. Reimburse CBA for funding Further Advances (if any)
4. Payment of expenses to Bond Trustee, Security Trustee and taxes
5. Payments to Agents and third parties
6. Payment to Servicer, Trust Manager, Account Bank, Cover Pool Monitor
7. Repayment of senior portion of Demand Loan subject to ACT test being satisfied on the date of such repayment
8. If CBA is not the IRS provider, payments due on IRS
9. *Pari passu*: If CBA is IRS and covered bond swap provider, payments on IRS, Covered Bond Swap payments, scheduled interest due for payment under the Covered Bond Guarantee
10. Principal payable on the covered bond swap and
11. Final redemption amount of Covered Bonds if not paid by Issuer on the applicable Extension Determination Date
12. Deposit any remaining proceeds to GIC account if prior Covered Bonds have not been repaid
13. Excluded Swap Termination Payments
14. Any amounts due and payable on the Intercompany Loan
15. Indemnity Payments and other expenses to Cover Pool Monitor
16. Subordinated payments under the Demand Loan
17. Residual payments to Income Unitholder and Capital Unitholder

# Contact us



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## Programme Documentation

- ▶ Securitisation – Medallion
- ▶ Euro Medium Term Notes
- ▶ US Medium Term Notes
- ▶ Commercial Paper
- ▶ Covered Bonds

▶ Ratings reports/documentation: [www.commbank.com.au/about-us/investors.html](http://www.commbank.com.au/about-us/investors.html)