

Commonwealth Bank of Australia

Mortgage Covered Bonds

Update

Ratings/Outlook

Mortgage Covered Bonds	AAA/Stable
------------------------	------------

Rating Rationale

Bank IDR/Outlook	AA-/Negative
IDR uplift	0 notches
PCU	6 notches
Tested Rating on probability of default basis	AA+
Recovery uplift	1 notch
Covered Bond Rating	AAA/Stable
AP Fitch considers in analysis (%)	92.5
AAA breakeven AP (%)	93.5

Key Data

	End-Sep 18
Asset type	Residential mortgages
Maturity profile of bonds	Soft/hard bullet
Cover assets (AUDbn) ^a	32.1
Covered Bonds (AUDbn equivalent) ^{a b}	28.0
Nominal AP (%) ^{a b}	87.2
WA life of assets (years)	15.0
WA life of liabilities (years)	5.1

^a Includes cash in GIC account

^b Includes Series 72 issued on 4 October 2018

Source: Fitch Ratings, Fitch Solutions

PCU Reduction

Asset segregation	No
Alternative manager	No

Rating Constraint

None

Related Research

[Commonwealth Bank of Australia \(March 2018\)](#)

[Commonwealth Bank of Australia – Ratings Navigator \(May 2018\)](#)

[APAC Covered Bonds Quarterly - 3Q18 \(November 2018\)](#)

[Covered Bonds Surveillance Snapshot \(October 2018\)](#)

['B' Portfolio Loss Rates for Covered Bonds \(September 2018\)](#)

Analysts

Jimmy Tanzil
+61 2 8256 0305
jimmy.tanzil@fitchratings.com

Sambit Agasti
+61 2 8256 0337
sambit.agasti@fitchratings.com

Key Rating Drivers

Four-Notch Downgrade Buffer: The 'AAA' covered bond rating is based on Commonwealth Bank of Australia's (CBA) Long-Term Issuer Default Rating (IDR) of 'AA-', an IDR uplift of zero notches, a payment continuity uplift (PCU) of six notches, a recovery uplift of one notch and an asset percentage (AP) of 92.5% that Fitch Ratings relies upon in its analysis and provides more protection than the agency's 'AAA' breakeven AP of 93.5%. The Stable Outlook on the rating reflects the four-notch buffer against a downgrade of CBA's IDR.

Zero IDR Uplift: The IDR uplift remains at zero notches. Australia does not have a specific advanced resolution regime, but the regulator has the ability to resolve a bank under its regulatory powers. Covered bonds are not explicitly exempt from bail-in should a bank be resolved, which may result in the direct enforcement of recourse against the cover pool for the payment of the outstanding covered bonds. Therefore, CBA's Long-Term IDR remains the floor for its covered bond rating.

Soft-Bullets Back Uplift: The PCU of six notches reflects the strong liquidity protection in the form of a 12-month extension period on the soft-bullet bonds, which make up 94.2% of issuance. The remaining hard-bullet bonds have a 12-month pre-maturity test with a cure period of six months. While these bonds have less liquidity protection due to the six-month cure period, Fitch considers the risk of cross default to be low. The PCU also reflects three months of interest protection in the form of a reserve should CBA lose its Short-Term IDR of 'F1+'.

Currency Risk Caps Recoveries: The recovery uplift is capped at one notch as the programme is significantly exposed to foreign-exchange risk that could affect recoveries given a default of the covered bonds. Fitch expects that the swaps in place on the liabilities may terminate upon a covered bond default, which would mean longer-dated Australian dollar asset cash flow would need to provide recoveries for foreign-currency denominated covered bonds.

ALM Loss Drives AP: The 'AAA' breakeven AP of 93.5% equates to a breakeven overcollateralisation of 7.0%. The ALM loss component of 3.5% reflects modelled asset and liability mismatches and corresponds to the sum of the cash flow valuation and asset disposal loss, the two components replaced by Fitch's ALM loss under its Covered Bonds Rating Criteria published in August 2018. The credit loss component of 3.1% reflects the credit quality of the underlying cover pool and is in line with that of local peers.

Programme Highlights

Low Credit Risk Pool: The cover pool consisted of 128,638 loans secured by first-ranking mortgages of Australian residential properties, totalling AUD28.7 billion at end-September 2018. The pool's weighted-average (WA) consolidated loan/value ratio was 58.7% and WA seasoning was 53.1 months. Interest-only loans formed 19.5% of the pool and approximately 23.9% of loans in the pool were secured by investment properties.

Fitch calculated that, in a 'AAA' scenario, there would be a cumulative WA foreclosure frequency of 7.5% and a WA recovery rate of 52.1% for the cover pool. The results are driven by the 'AAA' minimum loss floor of 4.0%, as outlined in criteria.

Minimal Hard-Bullet Bonds: The hard-bullet bonds represent a diminishing portion, currently 5.8% of the outstanding bonds. These bonds are AUD183 million or less in size and their maturities are well distributed. Fitch expects CBA to only issue soft-bullet bonds in the future.

Cover Pool Mortgage Characteristics: September 2018

Current balance (AUDbn)	28.7
Number of loans	128,638
WA consolidated current loan/value ratio (%)	58.7
WA seasoning (months)	53.1
WA interest rate (%)	4.4
WA remaining term to maturity (years)	24.4
Investment properties (%)	23.9

Substitute assets (AUDbn)

Cash in GIC account	3.4
---------------------	-----

Loan type (%)

Fixed	16.5
Variable	83.5

Repayment type (%)

Principle and interest	80.5
Interest only	19.5

Loan arrears (%)

>30 and <= 60 days	0.19
>60 and <=90 days	0.08
>90 days	0.00

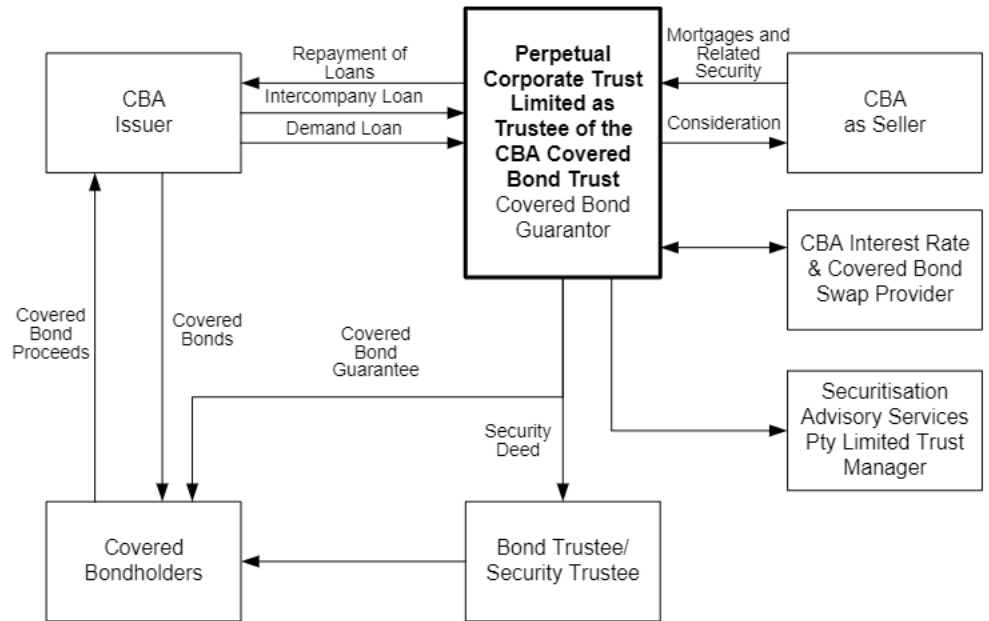
Geographic distribution (%)

New South Wales	37.0
Australian Capital Territory	0.5
Victoria	28.4
Queensland	15.8
Western Australia	10.9
South Australia	4.9
Tasmania	1.7
Northern Territory	1.0

Source: Fitch Ratings, CBA

Structure Diagram

Structure Diagram



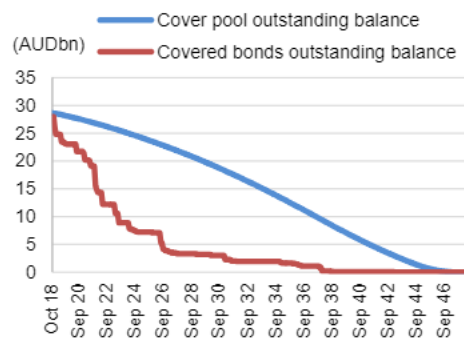
Source: Programme documents

Fitch Default Model Output (%)

Rating level	AAA	AA+	AA
WA foreclosure frequency	7.5	6.9	6.2
WA recovery rate	52.1	56.1	60.1

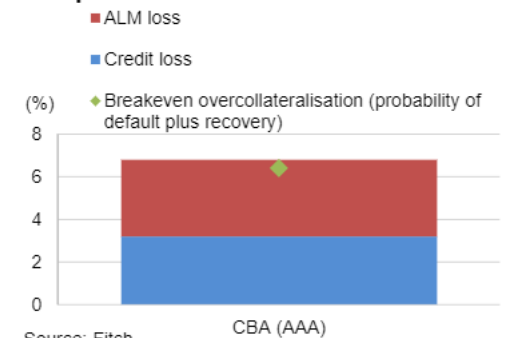
Source: Fitch Ratings

Amortisation Schedule



Source: Fitch, CBA

Breakeven Overcollateralisation Components



Source: Fitch

Related Criteria

- Covered Bonds Rating Criteria (October 2018)
- Bank Rating Criteria (October 2018)
- Structured Finance and Covered Bonds Counterparty Rating Criteria (August 2018)
- Structured Finance and Covered Bonds Counterparty Rating Criteria: Derivative Addendum (August 2018)
- APAC Residential Mortgage Rating Criteria (October 2018)
- RMBS Lenders' Mortgage Insurance Rating Criteria (April 2018)

Outstanding Mortgage Covered Bonds Volume

Currency	Amount outstanding	Hedged AUD equivalent amount	Number of issues	% of total issue	WA life (years)
AUD	2,584,000,000	2,584,000,000	6	9.2	3.8
CHF	450,000,000	462,363,814	2	1.7	1.6
EUR	10,479,500,000	15,148,020,348	42	54.1	6.8
GBP	1,137,000,000	1,799,442,719	3	6.4	6.2
HKD	6,100,000,000	1,002,745,221	1	3.6	2.8
NOK	4,125,000,000	673,615,918	2	2.4	3.4
NZD	314,000,000	291,957,229	1	1.0	2.3
USD	5,000,000,000	6,020,210,992	4	21.5	2.0

Data as at end-September 2018; includes Series 72 bond that was issued on 4 October 2018
Source: Fitch Ratings, CBA

The ratings above were solicited and assigned or maintained at the request of the rated entity/issuer or a related third party. Any exceptions follow below.

ALL FITCH CREDIT RATINGS ARE SUBJECT TO CERTAIN LIMITATIONS AND DISCLAIMERS. PLEASE READ THESE LIMITATIONS AND DISCLAIMERS BY FOLLOWING THIS LINK: [HTTPS://FITCHRATINGS.COM/UNDERSTANDINGCREDITRATINGS](https://fitchratings.com/understandingcreditratings). IN ADDITION, RATING DEFINITIONS AND THE TERMS OF USE OF SUCH RATINGS ARE AVAILABLE ON THE AGENCY'S PUBLIC WEB SITE AT WWW.FITCHRATINGS.COM. PUBLISHED RATINGS, CRITERIA, AND METHODOLOGIES ARE AVAILABLE FROM THIS SITE AT ALL TIMES. FITCH'S CODE OF CONDUCT, CONFIDENTIALITY, CONFLICTS OF INTEREST, AFFILIATE FIREWALL, COMPLIANCE, AND OTHER RELEVANT POLICIES AND PROCEDURES ARE ALSO AVAILABLE FROM THE CODE OF CONDUCT SECTION OF THIS SITE. FITCH MAY HAVE PROVIDED ANOTHER PERMISSIBLE SERVICE TO THE RATED ENTITY OR ITS RELATED THIRD PARTIES. DETAILS OF THIS SERVICE FOR RATINGS FOR WHICH THE LEAD ANALYST IS BASED IN AN EU-REGISTERED ENTITY CAN BE FOUND ON THE ENTITY SUMMARY PAGE FOR THIS ISSUER ON THE FITCH WEBSITE.

Copyright © 2018 by Fitch Ratings, Inc., Fitch Ratings Ltd. and its subsidiaries. 33 Whitehall Street, NY, NY 10004. Telephone: 1-800-753-4824, (212) 908-0500. Fax: (212) 480-4435. Reproduction or retransmission in whole or in part is prohibited except by permission. All rights reserved. In issuing and maintaining its ratings and in making other reports (including forecast information), Fitch relies on factual information it receives from issuers and underwriters and from other sources Fitch believes to be credible. Fitch conducts a reasonable investigation of the factual information relied upon by it in accordance with its ratings methodology, and obtains reasonable verification of that information from independent sources, to the extent such sources are available for a given security or in a given jurisdiction. The manner of Fitch's factual investigation and the scope of the third-party verification it obtains will vary depending on the nature of the rated security and its issuer, the requirements and practices in the jurisdiction in which the rated security is offered and sold and/or the issuer is located, the availability and nature of relevant public information, access to the management of the issuer and its advisers, the availability of pre-existing third-party verifications such as audit reports, agreed-upon procedures letters, appraisals, actuarial reports, engineering reports, legal opinions and other reports provided by third parties, the availability of independent and competent third-party verification sources with respect to the particular security or in the particular jurisdiction of the issuer, and a variety of other factors. Users of Fitch's ratings and reports should understand that neither an enhanced factual investigation nor any third-party verification can ensure that all of the information Fitch relies on in connection with a rating or a report will be accurate and complete. Ultimately, the issuer and its advisers are responsible for the accuracy of the information they provide to Fitch and to the market in offering documents and other reports. In issuing its ratings and its reports, Fitch must rely on the work of experts, including independent auditors with respect to financial statements and attorneys with respect to legal and tax matters. Further, ratings and forecasts of financial and other information are inherently forward-looking and embody assumptions and predictions about future events that by their nature cannot be verified as facts. As a result, despite any verification of current facts, ratings and forecasts can be affected by future events or conditions that were not anticipated at the time a rating or forecast was issued or affirmed.

The information in this report is provided "as is" without any representation or warranty of any kind, and Fitch does not represent or warrant that the report or any of its contents will meet any of the requirements of a recipient of the report. A Fitch rating is an opinion as to the creditworthiness of a security. This opinion and reports made by Fitch are based on established criteria and methodologies that Fitch is continuously evaluating and updating. Therefore, ratings and reports are the collective work product of Fitch and no individual, or group of individuals, is solely responsible for a rating or a report. The rating does not address the risk of loss due to risks other than credit risk, unless such risk is specifically mentioned. Fitch is not engaged in the offer or sale of any security. All Fitch reports have shared authorship. Individuals identified in a Fitch report were involved in, but are not solely responsible for, the opinions stated therein. The individuals are named for contact purposes only. A report providing a Fitch rating is neither a prospectus nor a substitute for the information assembled, verified and presented to investors by the issuer and its agents in connection with the sale of the securities. Ratings may be changed or withdrawn at any time for any reason in the sole discretion of Fitch. Fitch does not provide investment advice of any sort. Ratings are not a recommendation to buy, sell, or hold any security. Ratings do not comment on the adequacy of market price, the suitability of any security for a particular investor, or the tax-exempt nature or taxability of payments made in respect to any security. Fitch receives fees from issuers, insurers, guarantors, other obligors, and underwriters for rating securities. Such fees generally vary from US\$1,000 to US\$750,000 (or the applicable currency equivalent) per issue. In certain cases, Fitch will rate all or a number of issues issued by a particular issuer, or insured or guaranteed by a particular insurer or guarantor, for a single annual fee. Such fees are expected to vary from US\$10,000 to US\$1,500,000 (or the applicable currency equivalent). The assignment, publication, or dissemination of a rating by Fitch shall not constitute a consent by Fitch to use its name as an expert in connection with any registration statement filed under the United States securities laws, the Financial Services and Markets Act of 2000 of the United Kingdom, or the securities laws of any particular jurisdiction. Due to the relative efficiency of electronic publishing and distribution, Fitch research may be available to electronic subscribers up to three days earlier than to print subscribers.

For Australia, New Zealand, Taiwan and South Korea only: Fitch Australia Pty Ltd holds an Australian financial services license (AFS license no. 337123) which authorizes it to provide credit ratings to wholesale clients only. Credit ratings information published by Fitch is not intended to be used by persons who are retail clients within the meaning of the Corporations Act 2001.