Santander Consumer Bank AG

Mortgage Pfandbriefe

Presale Report

Ratings/Outlook

Mortgage Pfandbriefe	AAA(EXP)

Rating Rationale

Bank IDR/Outlook	A-/Stable
IDR uplift	2
Payment continuity uplift (PCU)	4
Tested rating on a PD basis	AA
Recovery uplift	2
Covered bond rating	AAA(EXP)
OC Fitch considers in analysis (%)	19.5
AAA(EXP) breakeven OC (%)	19.5

Key Data	Oct 17
Asset type	Residential mortgages
Maturity profile of bonds	Hard Bullet
Cover assets (EURm)	322.8
Covered bonds (EURm)	250.0
Nominal OC (%)	29.1
WAL of assets (years)	10.7
WAL of liabilities – expected (years)	7.0

PCU Reduction

Asset segregation	No
Alternative manager	No

Rating Constraint

None

Related Research

Fitch Rates Santander Consumer Bank's Mortgage Pfandbriefe 'AAA(EXP)' (November 2017)

Fitch Affirms Santander Consumer Bank AG at 'A-'; Outlook Stable (July 2016)

Covered Bonds Surveillance Snapshot (October 2017)

'B' Portfolio Loss Rates for Covered Bonds (September 2017)

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Key Rating Drivers

OC Supports Rating: Fitch Ratings has assigned Santander Consumer Bank AG's (SCB AG; A-/Stable/F2) EUR250 million mortgage Pfandbrief with a seven-year maturity a 'AAA(EXP)' rating. The rating is based on the issuer's Long-Term Issuer Default Rating (IDR) of 'A-', an IDR uplift of two notches, a payment continuity uplift (PCU) of four notches, a recovery uplift of two notches and the 'AAA(EXP)' breakeven over-collateralisation (OC) of 19.5%, which is the minimum SCB AG intends to maintain. The Outlook is Stable.

Maturity Mismatch Likely to Decline: The high breakeven OC relative to peers is driven by a cash flow valuation component of 5.3% and an asset disposal loss of 11.8%, reflecting the maturity mismatches of this newly set-up programme. Residential mortgage loans with high remaining terms are tested to repay a bond issuance with a significantly shorter maturity. Both aspects are likely to vanish over time when the asset liability profile becomes more balanced.

Low-Risk Cover Pool: The credit loss component of only 2.7% reflects the high quality of SCB AG's cover assets. At end-October 2017, ordinary cover assets entirely consisted of German residential housing loans. The programme's credit loss is a secondary rating driver, driven by limited expected defaults together with the maximum low loan-to-value (LTV) anchored in the German Pfandbrief Act.

Two-Notch IDR Uplift: An IDR uplift of two notches has been assigned to SCB AG's mortgage programme as the issuer's Long-Term IDR is based on its own Viability Rating (VR), Pfandbriefe are exempt from bail-in in a resolution scenario, Fitch does not expect resolution of the issuer to result in the direct enforcement of recourse against the cover pool and the risk of undercollateralisation at the point of resolution is assessed as low.

PCU of Four Notches: The PCU of four notches reflects the mandatory inclusion of liquid assets in the cover pool matching the maximum negative accumulated balance of cash flows for the next 180 days, which provides effective protection for interest and principal payments for standard German mortgage Pfandbriefe.

Two-Notch Recovery Uplift: SCB AG's programme benefits from a two-notch recovery uplift, as the OC Fitch relies upon compensates for credit losses modelled in a stress scenario corresponding to the level of the assigned covered bond rating.

Programme Highlights

Granular Residential Mortgage Portfolio: The cover pool comprised 3,305 German residential mortgage loans with an average loan size of EUR93,746. The LTV ratio for the total cover pool amounts to 45.3% allowing for a large buffer to real-estate price declines before losses materialise. Assets and liabilities are exclusively denominated in euros.

Any references in this report to how relevant legislation works, or the impact of relevant legislation, represent Fitch's interpretation. Investors and others should form their own views.

Peer Comparison

The table below compares the key rating drivers for SCB AG with those of the three other German Pfandbrief programmes with predominantly residential mortgage collateral issued by investment-grade financial institutions.

Fitch assigns an IDR uplift of up to two notches to mortgage covered bond programmes in Germany as the agency understands that Germany has adopted an advanced bank resolution regime from which fully collateralised covered bonds and secured debt are exempt.

All German mortgage covered bond programmes receive a PCU of four notches given the mandatory inclusion of liquid assets in the cover pools matching the maximum negative accumulated balance of cash flows for the next 180 days laid down in the Pfandbrief Act.

The comparably high 'AAA' breakeven OC for SCB AG and Deutsche Postbank AG (DPB) is driven by significant asset-liability maturity mismatches reflected in the programmes' asset disposal loss and cash flow valuation components. Credit loss is less important as both cover pools consist entirely of German residential mortgage assets.

This contrasts to Sparkasse Pforzheim Calw's (SkPfCw) and Sparkasse Hannover's (SkH) credit loss components of 9.6% and 15.2%, respectively, reflecting the higher share of commercial assets, which are associated with higher loss expectations. The savings banks' high IDR of 'A+' together with an IDR uplift of two notches enables both programmes to reach the 'AAA' rating on a recovery basis without testing for timely payments.

See the *Covered Bond Surveillance Snapshot (October 2017)* and related *Excel file*, for a detailed comparison of rating drivers across Fitch-rated covered bond programmes.

Peer Comparison: Key Rating Drivers

	SCB AG	DPB	SkH	SpkPfCw
Covered bond rating	AAA(EXP)/Stable	AAA/Stable	AAA/Stable	AAA/Stable
IDR/Outlook	A-/Stable	BBB+/Stable	A+/Stable	A+/Stable
IDR uplift	2	2	2	2
PCU	4	4	4	4
Residential cover assets (%)	100	100	56	83
Commercial cover assets (%)	0	0	44	17
'B' portfolio loss rate (%)	0.2	0.0	0.0	0.0
'AAA' breakeven OC (%)	19.5	16.5	15.0	9.5
Breakeven OC components				
Credit loss (%)	2.7	2.1	15.2	9.6
Cash flow valuation (%)	5.3	6.3	-	-
Asset disposal loss (%)	11.8	8.1	-	-

Source: Fitch; data as at October 17

Country Risk Impact

There is no country risk impact on this programme as SCB AG's mortgage covered bond rating of 'AAA(EXP)' does not exceed Germany's Long-Term Local-Currency IDR of 'AAA'. Please see Criteria for Country Risk in Global Structured Finance and Covered Bonds.

Sensitivity Analysis

There is limited downward pressure following on the 'AAA(EXP)' rating for SCB AG's mortgage Pfandbriefe resulting from issuer rating downgrade. The IDR uplift of two notches, the PCU of four notches and the recovery uplift of two notches mean that the covered bond rating is likely to remain unchanged unless SCB AG's IDR fell by three or more notches to 'BBB-' or below.

There is a moderate cushion between Fitch's breakeven OC of 19.5% and the (expected) nominal OC of 29.1%. Furthermore, the programme could only achieve a one-notch recovery uplift if the OC that Fitch considers in its analysis drops to the legal minimum requirement of

Related Criteria

Covered Bonds Rating Criteria (October 2017)

Global Bank Rating Criteria (November 2016)

Structured Finance and Covered Bonds Counterparty Rating Criteria (May 2017)

Structured Finance and Covered Bonds Counterparty Rating Criteria: Derivative Addendum (May 2017)

EMEA RMBS Rating Criteria (October 2017)

Germany Residential Mortgage Rating Criteria Addendum (May 2017)

Structured Finance and Covered Bonds Interest Rate Stresses Rating Criteria (February 2017)

Fitch's Interest Rate Stress Assumptions for Structured Finance and Covered Bonds – Excel File (February 2017)

Fitch's Cover Assets Refinancing Spread Level (RSL) Assumptions - Excel File (October 2017)

2% on a net present value (NPV) basis. As a result, the covered bond rating would likely be downgraded to ‘AA-’, one notch above SCB AG’s IDR as adjusted by the IDR uplift.

Abbreviations

PCU: Payment Continuity Uplift
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
PPI: Purchasing Power Index

The Issuer

Santander Consumer Bank AG (SCB AG), headquartered in Moenchengladbach, Germany, is one of the leading financial institutions in the area of car and consumer goods financing.

SCB AG (A-/F2/a-) is deeply integrated within the operations of its intermediate parent Santander Consumer Finance, S.A. (A-/F2/bbb+), which has a leading consumer finance franchise in Europe and is in the top three in its core operating markets. SCF is 100% owned by and deeply integrated into Banco Santander, S.A. (A-/F2/a-). Banco Santander uses a decentralised business model with legally autonomous subsidiaries, which limits possible contagion risk. At the same time, many middle- and back-office operations are centralised at the group headquarters in Spain.

At end-2016, SCB AG’s loan book totalled EUR31 billion, of which 47% related to car financing. Its mortgage business (14%) is comparably small, although we expect it to gradually increase in line with its corporate lending businesses, which should improve the bank’s revenue diversification. The bank holds a Pfandbrief licence for the issuance of mortgage Pfandbriefe since September 2016. It issued its first Pfandbrief, a EUR10 million bond in June 2017. The issuer intends to call this bond shortly and plans to issue a EUR250 million bond in December.

Fitch’s most recent report on SCB AG’s bank ratings is the *Ratings Navigator* (August 2017).

IDR Uplift: Two Notches

The IDR uplift of two notches reflects that collateralised covered bonds in Germany are exempt from bail-in in a resolution scenario, Fitch deems the risk of under-collateralisation to be sufficiently low. Resolution of SCB AG, should this occur, is not expected to lead to a direct enforcement of recourse to the cover pool. SCB AG’s IDR of ‘A-’ is based on its own VR.

PCU: Four Notches

Fitch has assigned this programme a PCU of four notches due to the principal and interest payment protection mechanism, notably the inclusion of highly liquid assets covering potential cash shortfalls in the next 180 days. Fitch does not consider that other PCU components, “Asset Segregation” and “Alternative Risk Management”, present a high risk to payment continuity. Details on the assessment for the asset segregation and alternative risk management component can be found in Appendix 3.

Recovery Uplift: Two Notches

SCB AG’s Pfandbriefe are eligible for a recovery uplift of two notches as we expect the programme to benefit from outstanding recoveries. This is because the OC Fitch relies upon in its analysis offsets the stressed credit loss in the ‘AAA’ rating scenario and we did not identify any material risks to these recovery expectations.

Cover Pool

As of 19 October 2017, the cover pool contained EUR309.8 million of residential mortgage loans to private individuals and EUR13.0 million substitute assets.

SCB AG's Cover Pool

Characteristics as of 19 October 2017

General		**Geographical breakdown (%)**	
Current principal balance (EURm)	309.8	North Rhine-Westphalia	35.0
Number of loans	3,305	Hesse	11.8
Number of borrowers	3,153	Lower Saxony	10.8
Average loan per borrower (EUR)	93,746	Baden-Wuerttemberg	8.9
WA seasoning (months)	53	Bavaria	5.2
WA remaining term to maturity (years)	20	Berlin	5.0
WA original LTV (%)	66.9	Brandenburg	4.3
WA current LTV (%)	45.3	Other	18.9
Property purpose (%)		**Property type (%)**	
Owner occupied	79.6	Flat	25.4
Investment property	13.4	Single family house	60.4
Mixed	7.1	Multifamily house	14.2
Loan type (%)		**Amortisation type (%)**	
Fixed	100.0	Annuity	97.3
Variable	0.0	Bullet	2.7
Borrower type (%)		**Borrower location**	
Employee	77.2	PPI Group A	8.6
Self-employed	11.2	PPI Group B	41.7
Civil servant	6.7	PPI Group C	45.9
Retiree	4.8	PPI Group D	3.8

Source: SCB AG/Fitch

Cover Pool Credit Analysis

Fitch analysed the collateral portfolio using its applicable mortgage loss criteria for Germany in its Germany Residential Mortgage Rating Criteria Addendum. SCB AG's quality of origination, servicing procedures and staff qualifications are in line with other German prime lenders. The composition and credit quality of the cover pool may change over time because of the dynamic nature of the programme.

The cover pool comprised 3,305 residential mortgage loans to private individuals, with an aggregate outstanding amount of EUR309.8 million as of 19 October 2017. The WA LTV ratio was 45.3%, and the WA seasoning of the mortgage loans was 53 months. Interest-only loans formed only 2.7% of the pool. 13.4% of the pool was investment loans. Despite the relative small size of the current balance, the cover pool was geographically diversified across Germany (see Cover Pool table).

SCB AG has provided Fitch with a comprehensive set of loan-by-loan data, which include the majority of data fields used in the agency's analysis of German residential mortgages. Information on other loan parts, such as external financing with favourable conditions sponsored by Kreditanstalt für Wiederaufbau for energy-efficient constructions, was not provided on a line-by-line basis. Accordingly, when calculating the original LTV, Fitch manually increased the original loan balance of the cover pool by about 9% based on data regarding SCB AG's total mortgage book.

According to Fitch's methodology, the two key components of the default probability on the residential loans are the willingness and ability of a borrower to make payments on the loan. Willingness to pay is usually measured by the original LTV: higher default probability is assigned to high LTV loans. The ability to pay is measured by the ratio of the borrower's income to the mortgage payments: the debt/income (DTI) ratio. In absence of DTI data on a line-by-line basis, the agency applies a standard 40% assumption for all loans in the portfolio.

This is supported by SCB AG's underwriting practices, which we consider to be in line with market standards, and the relatively low average DTI for the issuer's total loan book. Fitch further adjusts the default probabilities to account for borrower- and asset-specific characteristics.

The recovery rates are mainly driven by market value decline (MVD) assumptions and the cover pool LTV. The German Pfandbrief Act allows loans to be included into the cover pool up to 60% of its mortgage lending value. The current WA LTV of 45.3% allows for a large buffer to real-estate price declines before losses would materialise. The 'AAA' MVD of 57.7% reflects the property type and location as outlined in the Germany Residential Mortgage Rating Criteria Addendum.

Fitch Default Model Output (%)

Rating level	AAA	AA+	AA
WAFF	14.4	13.1	11.8
WARR	72.2	75.2	78.1
Loss rate	4.0	3.3	2.6

Source: Fitch

Fitch derived a stressed cumulative default rate and recovery rate for the cover pool based on the loan-by-loan analysis of the cover assets, and taking into account the features of the mortgages. In a 'AAA' rating scenario, the WA foreclosure frequency (WAFF) equated to 14.4% and the WA recovery rate (WARR) 72.2%, which is equivalent to an expected loss rate of 4.0%.

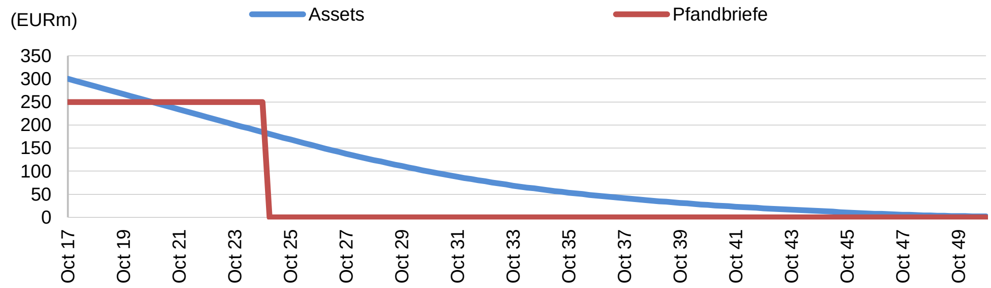
Cash Flow Analysis

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 tests whether the cover pool can service principal and interest payments on the covered bonds in a timely manner, while testing different points at which recourse against the cover pool is enforced up to the first large principal redemption. Based on this analysis, Fitch finds that the combination of a late issuer default and low prepayments within a high-interest-rate environment is most stressful for SCB AG's covered bond programme. In such scenario an OC of 19.5% is sufficient to withstand the agency's 'AA' tested rating on a PD basis under the covered bonds cash flow model.

The below graph shows the amortisation profile of the assets assuming no prepayments until final legal maturity and the amortisation of the outstanding covered bonds. In its analysis Fitch modelled a bond issuance of EUR250 million and a seven-year maturity as indicated by SCB AG.

Amortisation Profile

(As of October 2017)



Source: Fitch/SCB AG

Maturity Mismatches

The cover assets are amortising, with an initial average remaining maturity of 10.7 years, while the covered bond has a modelled residual maturity of 7.0 years. As a result, temporary liquidity shortfalls may arise, putting strain on available resources.

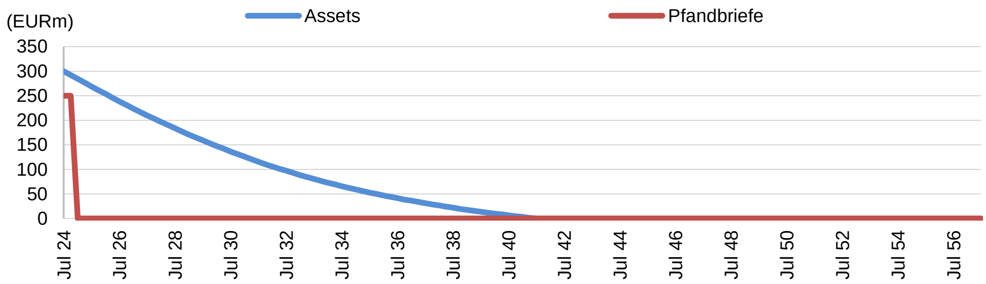
Criteria Variation

The agency usually assumes that the cover pool is replenished with assets of a similar amortisation. However, when testing a switch of the recourse against the cover pool shortly ahead of the modelled bond redemption, Fitch assumed that any replenishment would be made from the existing stock of loans, leading to a shorter cover assets' residual life. This keeps maturity mismatches between the cover pool and the covered bonds constant. This constitutes a variation to Fitch's criteria Covered Bonds Rating Criteria. The variation has no rating impact.

The below graph shows the amortisation profile of assets and covered bonds in Fitch's stress scenario. After the recourse against the cover pool is enforced, Fitch applies prepayment assumptions of 2% for the whole term of the mortgage loans.

Stressed Amortisation Profile

(As of October 2017)



Source: Fitch/SCB AG

Refinancing Spread Levels

Fitch assumes that if there is a liquidity shortfall, an alternative manager would be able to sell part of the mortgage portfolio within the timeframe provided by the mandatory liquidity provision. The ability to find a buyer will depend on several factors, including buyer appetite in light of the economic environment and the proportion of the portfolio required to be liquidated.

The cost of sales are driven by the amount of cash needed to bridge the liquidity gaps and the haircut an alternative manager has to accept when selling assets in a stressed environment. To determine the stressed price at which such asset sales would occur, Fitch has assumed refinancing costs (shown below) for any potential buyer. However, in light of the lack of a precedent in Germany, there is no guarantee that a portfolio can be realised in any prevailing economic environment.

Refinancing Spread Levels

(bp)	AAA	AA	A	BBB	BB	B
German mortgage loans	200	174	152	132	115	100

Source: Fitch

The programme is most vulnerable to an issuer default just before the maturity of the covered bond. Under this scenario, the cover pool is unable to accumulate cash through amortisation before the redemption of the covered bond. Accordingly, the amount of asset sales needed to bridge the liquidity gap is comparably high, which ultimately drives the asset disposal loss of 11.8%.

The cash flow valuation component of 5.3% expresses the difference in the NPV of both the assets and liabilities. The combination of a high-interest-rate scenario and the long remaining term of the fixed-rate cover assets leads to a high discount, thus constituting the most stressful scenario for this programme. This is partly offset by Fitch's assumption that after the loan interest-rate reset date, interest is paid according to its interest-rate stresses.

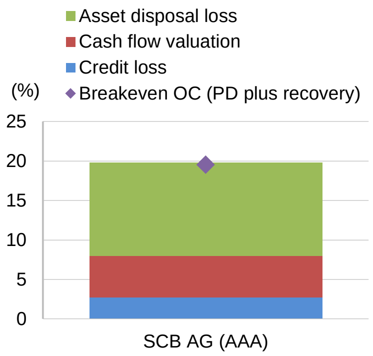
Breakeven OC for the Rating

Fitch calculated a 'AAA(EXP)' breakeven OC of 19.5%. The breakeven OC relates to a 'AA' tested rating on a PD basis and a two-notch recovery uplift. The breakeven OC is dependent on multiple factors that could be affected by significant movements in the WA interest rate on the bonds or a change to the WA remaining term. Fitch will regularly reassess the breakeven OC in line with the covered bond ratings and upon new issuances or cover pool changes.

The breakeven OC is driven by a cash flow valuation component of 5.3% and an asset disposal loss of 11.8%. These two components reflect the maturity mismatches of this newly set-up programme. Residential mortgage loans with a low seasoning and long remaining terms are tested to repay a bond issuance with a significantly shorter stressed maturity. Both aspects are likely to vanish over time when the asset liability profile becomes more balanced.

The credit loss component of only 2.7% reflects the high quality of SCB AG's cover assets. As of October 2017, ordinary cover assets entirely consisted of German residential housing loans. The programme's credit loss is a secondary rating driver, driven by limited expected defaults together with the maximum low loan-to-value (LTV) anchored in the German Pfandbrief Act.

Breakeven OC Components



Source: Fitch

In absence of a lowest OC of the last 12 months for this new programme, Fitch relies on the issuer's intention to hold at least 19.5% OC in the medium term. Since inception of the programme in June 2017, the lowest OC reported was 454.0%.

Programme Review

Fitch will periodically review the credit quality of the cover pool and perform a cash flow analysis to assess whether the OC taken into account by the agency provides protection against identified risks commensurate with the rating of the covered bonds issued by SCB AG under this programme. Cover pool and covered bonds information is updated on a quarterly basis and displayed on Fitch's covered bond surveillance tool (available at www.fitchratings.com) and in the quarterly *Covered Bonds Surveillance Snapshot*.

Disclaimer

References in this report to the content and impact of relevant legislation and/or regulation represent Fitch's interpretation. Fitch relies on legal opinions or memoranda provided by issuers' and/or other outside legal counsel. As Fitch has always made clear, Fitch does not provide legal advice or confirm that a country's legal or regulatory framework, the legal opinions or memoranda, or any other programme documents or any structures are sufficient for any purpose. The disclaimer at the foot of this report makes it clear that this report does not constitute legal, tax and/or structuring advice from Fitch, and should not be used or interpreted as legal, tax and/or structuring advice from Fitch. Should readers of this report need legal, tax and/or structuring advice, they are urged to contact relevant advisers in the relevant jurisdictions.

Appendix 1: Analysis of Structural and Legal Aspects of the Programme

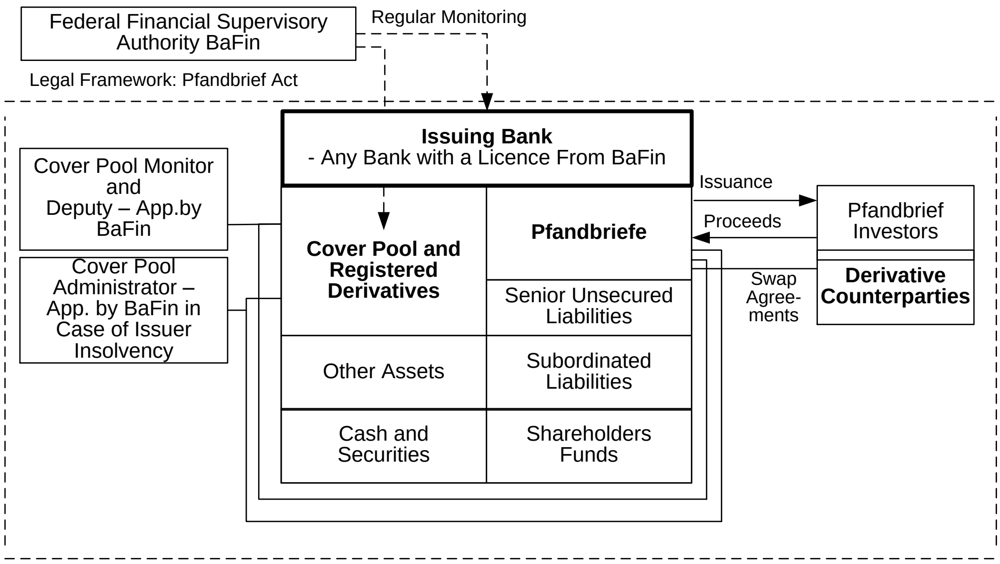
1.1.Programme Overview and Basis for Dual Recourse

SCB AG can issue hard-bullet Pfandbriefe under this programme, which are secured by a dynamic pool of German residential mortgage loans. These are recorded in a dedicated cover register that does not belong to the insolvency estate of the issuer but constitutes a separate, bankruptcy-exempt estate. The issuer was granted a Pfandbrief licence in September 2016.

As long as the issuer is solvent, it will repay covered bond obligations when due pari passu among themselves and with their senior liabilities, irrespective of the performance of the cover assets. On a second recourse, if issuer insolvency proceedings are started, outstanding covered bonds and registered cover assets will form a separate legal estate in the form of a so-called “Pfandbriefbank with limited business activity”. The scope of this Pfandbriefbank with limited business activities is restricted mainly to administration of the mortgage loans and repayment of covered bond obligations.

1.2.Issuance Template

Diagram of a Pfandbrief Issuance



Source: Fitch

1.3. Flow of Funds Within the Programme

Generally, mortgage loans are cover pool eligible up to 60% of their mortgage lending value. Upon registration of a loan in the cover register, it becomes part of the cover pool. The issuance proceeds of the mortgage covered bonds flow in the general bank account and are not earmarked for the funding of mortgage loan origination.

Covered bond repayment will also be made from this account unless there has been an enforcement of the recourse to the cover pool. Fitch understands that upon its appointment, the alternative manager (Sachwalter) is the sole party entitled to disburse incoming cash flows from the cover assets to satisfy covered bond payments becoming due. The Sachwalter is appointed by BaFin at the latest upon issuer insolvency.

Priority of Payments

Two different priorities of payment for application of cash flows received from the cover assets exist. These depend on the timing of the appointment of the alternative manager.

Priority of Payments Prior to Alternative Manager Appointment

Prior to the appointment of an alternative manager, all cash flows from the asset portfolio flow to the general bank account. Whenever covered bond payments, interest or principal, are due, the issuer must settle these in full and timely according to the bonds' terms and conditions. The issuer also bears all administrative costs related to the cover pool and the bonds.

The issuer is accountable for compliance with all legal requirements, in particular adherence with all eligibility criteria, minimum OC and liquidity requirements.

Post-Alternative Manager Appointment Priority of Payments

Following its appointment, the Sachwalter holds the exclusive right to manage cover assets. This includes liquid assets and incoming cover asset interest and principal repayments. This right is not limited to the amount registered in the cover pool but extends to the whole loan. The Sachwalter will deduct appropriate administration costs from the incoming mortgage loan cash flows.

Subsequently, the Sachwalter is responsible for separating the incoming whole loan cash flows according to their legal status, i.e. cash flows will be split between cover pool loan part and junior ranking loan parts. Cash flows of junior ranking loan parts will be transferred to the general insolvency estate. From the cash flows of the registered loan parts, the Sachwalter will deduct administrative costs relating to the cover pool, such as remuneration and special cover pool audit costs. Cash flows of the syndicated loan parts will then be transferred to the creditor. All remaining funds must be used to repay the mortgage Pfandbriefe according to their terms and conditions.

Payments to privileged derivative counterparties rank pari passu with covered bond payments.

Should monies remain after all administration costs are satisfied and all privileged liabilities have been redeemed in full, the alternative manager will pass these on to the general insolvency estate.

The flow of funds may be affected by the table of events on the following page.

Table of Events and Relevant Consequences to the Issuer and the Bondholders

Event	Trigger	Consequence	Payer	Acceleration	Timely payments	Full repayment
Initial (before any of the following events).	None.	The issuer makes scheduled payments to the covered bonds out of its resources. All costs incurred are borne by the issuer. Any funds in connection with privileged swap agreements are to be paid directly to or by the issuer.	Issuer	No	Interest and principal to be paid on their due date.	Principal payments to be met in full by the issuer.
Appointment of Sachwalter.	Commencement of issuer insolvency proceedings; or as a measure in case of danger as per Art.46 Kreditwesengesetz.	Upon commencement of insolvency proceedings cover pool, privileged derivatives and covered bonds are legally separated into the PBwLBA. BaFin proposes at least one and up to three Sachwalter. The responsible court formally appoints the Sachwalter. Upon appointment, the Sachwalter is the only party allowed to dispose of cover assets including incoming payments on the cover assets. Covered bond payments are settled by the Sachwalter according to their terms and conditions. Swap payments rank pari passu and are also settled by the Sachwalter. Expenses are deducted from incoming cash flows before settling bond and swap payments.	Pfandbrief-bank with limited banking activity.	No	Interest and principal remain due as scheduled.	Principal payments to be met in full by the Pfandbriefbank with limited banking activity.
Default of the Pfandbriefbank with limited banking activity.	Default on any of its obligations, including covered bonds, or overindebtedness of the Pfandbriefbank with limited banking activity.	BaFin files an application for commencement of insolvency proceedings against the Pfandbriefbank with limited business activity. All covered bonds become immediately due and payable at their early redemption amount plus accrued interest.	Insolvency estate of the Pfandbrief-bank with limited business activity.	Yes	No	Depending on the proceeds deriving from the portfolio sale.

Source: Pfandbriefgesetz, Fitch

1.4. Structural Features of the Programme

SCB AG's mortgage covered programme is based on the Pfandbrief legislation. The programme does not contain any additional structural features.

1.5 German Legislative Covered Bonds Framework

The table below is based on Fitch's understanding of certain aspects of the applicable regime and is not a substitute for the original texts and/or German legal advice.

Main Characteristics of German Legislative Pfandbriefe

German Pfandbrief Act (January 2015)

Issuers	Financial institutions with a licence to issue Pfandbriefe.
Supervision	German Federal Financial Supervisory Authority (Bundesanstalt für Finanzdienstleistungsaufsicht, BaFin).
Mortgage collateral	• Residential or commercial mortgages; • Geographical scope to the EU/EEA, Switzerland, the US, Canada, Japan, Australia, New Zealand or Singapore; • Up to 20% of the outstanding Pfandbriefe can be substitute assets.
LTV limits for mortgage loans	60% LTV based on the mortgage lending value.
Public-sector assets	• Public-sector assets; • Geographical scope to the EU/EEA; • For assets from the US, Canada, Japan and Switzerland, the debtor must be assigned to credit quality step 1; • Up to 10% of the outstanding Pfandbriefe can be substitute assets.
Transfer of assets	Integrated template, assets remain on the issuer's balance sheet.
Cover register	Cover register is required for the respective cover pool.
Cover pool monitor	Independent trustee appointed by BaFin.
Cover pool administrator	A dedicated cover pool administrator (Sachwalter) would take over the management of the cover assets and outstanding liabilities post issuer default. He would be appointed by a court at the request of BaFin, at the latest upon the issuer's insolvency.
Minimum OC	• 0% nominal value; • 2% stressed net present value (NPV). The NPV is detailed in a specific net present value regulation (Barwertverordnung) including procedures, stress scenarios and risk models. The approach can be static or dynamic, or based on internal models.
Treatment of swap counterparties	Derivative counterparties rank pari passu with the claims of the covered bondholders.
PBwLBA	Pfandbriefbank with limited business activity (Pfandbriefbank mit beschränkter Geschäftstätigkeit). The cover pool constitutes an insolvency-free asset and continues to exist post issuer default as a PBwLBA to ensure the timely payment of the liability obligations. The PBwLBA would be managed by the cover pool administrator.

Source: Pfandbriefgesetz, Fitch

Appendix 2: Transaction Parties

Important Features of Counterparties

Counterparties	Role	Long-, Short-Term Ratings	Comments
Santander Consumer Bank AG	Issuer Originator Servicer Account bank	A-/Stable/F2	

Source: Fitch, Programme documents

No privileged derivatives are registered to the cover pool, thus no swap provider exists.

A qualified trustee has been appointed by BaFin.

Appendix 3: Other Payment Continuity Risk Considerations

Asset Segregation

Fitch expects that ring-fencing of the cover pool will be effective given the “all-or-nothing” nature of this risk. The ring-fencing of cover assets from any claims from unsecured creditors of the defaulted financial institution is achieved by virtue of law – often in the form of an exemption to normal bankruptcy legislation, or through a transfer of the assets to a bankruptcy-remote special-purpose vehicle acting as a guarantor of the issued covered bonds.

Asset Segregation: No Impact on PCU

Component driver	Fitch assessment
Segregation of cover pool from other creditors of issuer	Cover assets are segregated through their registration in the cover register (Deckungsregister). Registered assets form a special estate (PBwLBA) and are exclusively available for the claims of the bondholders and privileged derivative counterparties.
Excess OC immune from claims from other creditors	Residual risk remains as the German covered bond law states that assets should be given back to the general insolvency estate if they are “obviously not necessary” to cover the claims of the bondholders, the minimum OC and the costs of the Pfandbriefbank with limited business activity (PBwLBA).
Asset and liability claw back risk	Remote risk of asset and liability claw back as circumstances in which claw back may occur are rare and rather hypothetical.
Commingling risk	Residual risk remains as prior to the commencement of insolvency proceedings or appointment of a Sachwalter collections received are not separated from the general bank account in the issuer’s name. No structural mitigating factors are in place. After beginning of insolvency proceedings or appointment of a Sachwalter commingling is legally prohibited.
Set-off risk for deposits	Set-off against assets entered into the pool is excluded by law. Netting is only allowed for derivative contracts belonging to the same pool and from the same counterparty. No privileged derivatives are registered to the cover pool of SCB AG.

Source: Fitch

Alternative Management

Systemic Alternative Management

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 (in cases 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.

This regulated programme benefits from the statutory role of BaFin to appoint a suitably qualified alternative manager for the covered bond programme to manage a designated institution’s covered bond activities upon an issuer’s insolvency.

Systemic Alternative Management: No Impact on PCU

Component driver	Fitch assessment
Administrator takes exclusive care of covered bondholders? When are they appointed?	A special administrator (Sachwalter) will service the pool in the interest of the bondholders. The special administrator will be appointed at the latest at insolvency of the issuer by BaFin. Prior appointment is possible.
Importance of timeliness of payments in the legal provisions	The Pfandbrief Act highlights that liabilities should be repaid on their due date.
Substitute manager able to sell cover assets or borrow to make timely payments	The special administrator has the power to sell assets and take bridge-financing, take out loans or issue new Pfandbriefe.
Regulatory oversight	BaFin.

Source: Fitch

Cover Pool-Specific Alternative Management

Fitch focuses on the likely ease of the transferability of relevant data and IT systems to an alternative manager and buyer, with such quality and ease also judged on the quality and quantity of data provided to Fitch.

Cover Pool Alternative Management: No Impact on PCU

Component drivers	Fitch assessment
Cover assets, debtors' accounts and privileged swaps clearly identified within IT systems	Market standard systems are in place that ensure identification of that registered assets of SCB AG.
Standardised or custom-made IT systems used	Fitch considers used systems to be well known in the market, enabling an alternative manager to easily start managing the programme.
Automation and speed of cover pool reporting	All Fitch templates will be provided at least on a quarterly basis and produced fully automated. Only minor data limitations exist.
Adequate filing of loan documentation, evidence of security	Loan files for residential loans are available partially in electronic and paper based form.

Source: Fitch

Privileged Derivatives

Fitch considers programmes encompassing privileged hedging agreements to be more vulnerable to a potential insolvency of the issuer. No privileged derivatives are registered to the mortgage covered bonds of SCB AG.

Appendix 4: Origination and Servicing

Origination and Underwriting

SCB AG's mortgage loan origination stands out through its strong standardised and automatized processes. The issuer has clearly defined mortgage lending criteria based on its general credit-policy, including LTV limits, maximum loan terms and specifications for high risk regions. Changes to these criteria have to be approved by the risk and product management department, while changes to the credit-policy need board approval.

Loans are originated using different channels, mainly through SCB AG's own branch network (77% of newly originated loans at end-2016) and to a lesser extent through different mortgage brokers. Performance of brokerage firms is checked quarterly in terms of volume production and application quality. The issuer further uses its strong position in consumer finance to cross-sell its retail mortgage products.

Regardless of the origination channel, underwriting processes are centralised and are supported by standardised and consistent processes, IT systems and risk management. All borrowers are subject to a credit scoring process. No loan is approved based solely on the collateral value. Loan approval depends on an individual decision within SCB AG's risk department, but the issuer plans to simplify this by introducing automated loan approval for standard low risk mortgages. In our view, the negative impact of these changes on the cover pool credit quality is limited and no forward-looking underwriting hit is applied.

SCB follows a two-step appraisal process. First, before loan approval, the middle office calculates an indicative market value based on information and documents provided by the borrower. Following loan approval, an on-site-visit is conducted by a third-party appraisal firm. Over the life of the loan the collateral market values are monitored constantly using regional and property type specific market data. Significant negative price developments will trigger a revaluation. Assets being revalued are flagged as not cover pool eligible until the evaluation process is completed. Flagged assets already in the cover pool will be removed accordingly.

Servicing

The covered bond programme is managed with market standard software, allowing for a daily registration of newly added loans. The trustee is able to perform sample checks at any time using remote access to the cover pool management system. The trustee has also possibility to request paper files and additional information. In case of a detected input error upon cover pool registration, the asset will directly (automatically) be removed from the cover pool and eventually re-registered after correction.

Loans in arrears, regardless of their size or the delinquency amount, are excluded from the cover pool after permission by the trustee. After one day past due (dpd), the loan is automatically handed over to SCB's Collection Business Unit. SCB AG's collection process is also highly standardised. This includes automatic dunning letters as well as minimum numbers of calls to the debtor. In this early stage, standard refinancing measures can be agreed.

After 60 dpd an in-detail analysis will be conducted by specialists including a review of the customers' credit history and its current credit profile. The loan will either be restructured or the termination process will be started. Servicing of terminated loans is outsourced to an external debt collection agency, aiming at novation of (transferring) the loan. If not successful, the collateral will be realised, either by sale or as a last resort by foreclosure.

Business Continuity

SCB AG has business continuity plans in place, supported by back-up facilities. Fitch's understanding is that the issuer's business continuity plans are sufficiently robust to allow for the restart of operations at alternative locations without any significant interruption.

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.