

Japan Housing Finance Agency's Series T-3 Structured Issuance Assigned Preliminary 'AAA (sf)' Rating

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OVERVIEW

- The JHF series T-3 fixed-rate residential mortgage-secured pass-through notes are a securitization JHF is to issue. A pool of residential mortgage loans will ultimately back the notes.
- We are assigning our preliminary 'AAA (sf)' rating to the notes based on our view of the transaction's legal structure, credit support, and pool characteristics, among other factors.
- Because of the structure of this transaction, the rating on the notes depends to an extent on JHF's credit quality.

TOKYO (S&P Global Ratings) Nov. 16, 2018--S&P Global Ratings today said it has assigned its preliminary 'AAA (sf)' rating to Japan Housing Finance Agency's (JHF) series T-3 fixed-rate residential mortgage-secured pass-through notes. The issue amount for the notes when the transaction closes in late November will be ¥100 billion.

The JHF series T-3 notes are a securitization JHF is to issue. A pool of residential mortgage loans directly extended by JHF's predecessor, Government Housing Loan Corp. (GHLC), will ultimately back the notes. We base the preliminary rating on the notes on our view of the transaction's legal structure, credit support, and pool characteristics, among other factors.

Subsequent information may lead us to assign a final rating that differs from the preliminary rating. We will assign a final rating after JHF finalizes the amount and exact terms of the notes and we complete a full rating analysis, including a review of the final pool, cash flow modeling, final structure, transaction documents, and legal opinion.

Our preliminary rating reflects our opinion on the likelihood of the timely payment of interest, or interest distribution in the case of beneficiary certificates, allowing for a three-month grace period, and the ultimate repayment of principal by the transaction's legal final maturity date.

Our preliminary rating reflects the following:

- We assume a foreclosure frequency for the expected loan receivables of about 15.3% under a stress level commensurate with our 'AAA' rating and about 2.5% under a stress level commensurate with our 'B' rating (base-case scenario). These rates, which reflect our view of the credit quality of the underlying assets, are prior to applying adjustments for the transaction's convertible pro rata pay structure.
- We also assume a loss severity rate of about 14% for defaulted receivables under our 'AAA' stress scenario.
- We apply projected losses (net loss rate after accounting for recoveries from defaulted loans) subject to a floor of 0.35% in our base-case scenario and 4.0% at the 'AAA' rating level, as set out in our Japanese RMBS criteria (see "Methodology And Assumptions For Rating Japanese RMBS," published Dec. 19, 2014).
- We conducted a cash flow analysis based on the foreclosure frequency and loss severity rate assumptions. As a result, under the stress level sized for our 'AAA' rating, we concluded that interest payments and principal repayments on the notes and beneficiary certificates (subsequent to a beneficiary trigger event) would be made as scheduled (allowing for a three-month grace period with respect to payment of interest, or interest distribution in the case of the beneficiary certificates).
- Prior to a beneficiary certificate trigger event and if receivables in the collateral pool default or are delinquent for four months, JHF will eliminate these receivables from the collateral pool and amortize the notes by the amount of these receivables to maintain the initial level of overcollateralization in the trust. After a beneficiary certificate trigger event, the overcollateralization will mitigate the credit risk of the transaction's underlying mortgage loans and interest rate risk (interest on the mortgage loans less the sum of interest payments on the beneficiary certificates and transaction costs).
- In our view, the transaction has limited exposure to setoff risk because a pool of residential mortgage loans directly extended by GHLC ultimately backs the notes and JHF is not a deposit-taking financial institution.
- After considering the structural features of this transaction--including the transfer of collections from the collateral receivables, the level of liquidity protection, and the lack of a credit enhancement floor--we believe the rating on the notes depends to an extent on JHF's credit quality.

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RELATED CRITERIA

- Ratings Above The Sovereign - Structured Finance: Methodology And Assumptions, Aug. 8, 2016
- Methodology And Assumptions For Rating Japanese RMBS, Dec. 19, 2014
- Global Framework For Assessing Operational Risk In Structured Finance Transactions, Oct. 9, 2014
- Global Framework For Cash Flow Analysis Of Structured Finance Securities, Oct. 9, 2014
- Counterparty Risk Framework Methodology And Assumptions, June 25, 2013
- Methodology: Credit Stability Criteria, May 3, 2010
- Standard & Poor's Revises Criteria Methodology For Servicer Risk Assessment, May 28, 2009

RELATED RESEARCH

- Japan Structured Finance 2018 Outlook: Securitized Assets Set For Another Steady Performance, Dec. 26, 2017
- Japanese Structured Finance Scenario And Sensitivity Analysis 2017: The Effects Of The Top Five Macroeconomic Factors, Dec. 26, 2017
- Outlook Assumptions For The Japanese Residential Mortgage Market, Dec. 25, 2017
- Global Structured Finance Scenario And Sensitivity Analysis 2016: The Effects Of The Top Five Macroeconomic Factors, Dec. 16, 2016
- Overview Of Japan Housing Finance Agency's Structured Notes, April 21, 2015
- Stable Japanese RMBS Fundamentals Reflect Low Unemployment And Interest Rates, Nov. 11, 2014

PRELIMINARY RATING ASSIGNED

Japan Housing Finance Agency

¥100 billion JHF series T-3 fixed-rate residential mortgage-secured pass-through notes due January 2033

Preliminary rating	Amount	Coupon type	Overcollateralization ratio
AAA (sf)	¥100 bil.	Fixed rate	2.5%

The transaction's closing date will be Nov. 30, 2018.

NOTES

We define the overcollateralization ratio as: $1 - (A+B)/(C-D-E)$

A: the rated obligations and equally ranked obligations

B: prior obligations to the rated obligations

C: underlying assets (including cash)

D: liquidity reserves

E: obligations, except for senior, mezzanine, or subordinate obligations (seller's interest, etc.)

The full report will be available in Japanese on S&P Global Research Online at www.researchonline.jp. An English-language report will be available to subscribers of RatingsDirect at www.capitaliq.com. Ratings information can

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