New Issue: Holmes Master Issuer PLC

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New Issue: Holmes Master Issuer PLC

Ratings Detail

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<tr>
<th>Class</th>
<th>Rating*</th>
<th>Class size (mil. £)</th>
<th>Minimum credit enhancement (%)§</th>
<th>Redemption type</th>
<th>Interest</th>
<th>Step-up margin</th>
<th>Step-up date</th>
<th>Legal final maturity</th>
</tr>
</thead>
<tbody>
<tr>
<td>Series 2023-2</td>
<td>AAA (sf)</td>
<td>750.0</td>
<td>15.0</td>
<td>Scheduled amortization</td>
<td>Compounded daily SONIA plus 0.54%</td>
<td>Compounded daily SONIA plus 1.08%</td>
<td>July 2028</td>
<td>October 2072</td>
</tr>
<tr>
<td>A1</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Z-VFN</td>
<td>NR</td>
<td>315.0</td>
<td>N/A</td>
<td>N/A</td>
<td>Compounded daily SONIA only</td>
<td>N/A</td>
<td>N/A</td>
<td>October 2072</td>
</tr>
</tbody>
</table>

*Our rating addresses timely receipt of interest and ultimate repayment of principal on the class A1 notes. §This represents the program-level credit enhancement and comprises the first reserve fund and subordination. SONIA--Sterling Overnight Index Average. NR--Not rated. N/A--Not applicable.

Transaction Summary

• S&P Global Ratings assigned its 'AAA (sf)' credit rating to Holmes Master Issuer PLC's series 2023-2 class A1 notes. The issuer has also altered the size of the unrated class Z-VFN (variable funding notes).

• The pool comprises owner-occupied mortgage loans secured against properties in the U.K. We consider the collateral to be prime, based on the overall performance of Santander UK PLC's (the originator) residential mortgage book and its lending criteria, and the low level of loans in arrears in the trust.

• Credit enhancement for the class A1 notes comprises subordination and the reserve fund.

• The transaction has a revolving structure, so the pool's characteristics can change. To avoid a deterioration in the pool's credit quality, the transaction documents stipulate that asset substitution can only occur if certain conditions are met.

• About £1.3 billion additional assets were added to the trust as part of this issuance. After this issuance, the trust's size stood at £3.61 billion.

• Most of the additional assets were originated in the past two years (about 45.79%) and as a result exhibit lower seasoning, a higher current loan to value (LTV) ratio, and a higher loan to income (LTI) ratio on a weighted-average basis when compared to loans already contained within the trust.

• There are no rating constraints in the transaction under our counterparty, operational risk, or structured finance sovereign risk criteria. We consider the issuer to be bankruptcy remote.

The Credit Story

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Concerns and mitigating factors

### Overview

<table>
<thead>
<tr>
<th>Strengths</th>
<th>Concerns and mitigating factors</th>
</tr>
</thead>
<tbody>
<tr>
<td>The trust has low historical losses. Since the middle of 2019, the Holmes Master Issuer trust has exhibited stronger arrears performance than several of the other U.K. master trusts that have issued notes that we have rated.</td>
<td>New mortgages can be added to the trust, which could lead to deterioration in the portfolio's credit quality or to reduced margins. Under the transaction documents, new mortgage loans are subject to certain eligibility criteria, which aim to ensure that the pool does not deteriorate in credit quality immediately and that the mortgage margin cannot drop below a minimum level.</td>
</tr>
<tr>
<td>Securitization is an integral part of the lender's funding strategy. The Holmes Master Issuer trust was first established in 2000. Santander UK is an experienced originator and has been active in the securitization market for a long time.</td>
<td>The class Z-VFN can be reduced (without the requirement for a rating agency confirmation [RAC]) on each interest payment date to the minimum subordination level through a refinancing contribution. We have considered this as part of our cash flow analysis.</td>
</tr>
<tr>
<td>Santander UK has a strong position in the U.K. mortgage market and is currently the third-largest residential mortgage lender in the U.K. based on the value of mortgages outstanding and the fourth-largest residential mortgage lender based on gross lending.</td>
<td>The structure allows for the delinked issuance of notes. This means that subordinated tranches with earlier optional redemption dates could redeem before more senior tranches, leaving the senior tranches exposed to the risk of shrinking subordination. Under the transaction documents, the subordinated tranches can redeem before the senior tranches only if there is sufficient subordination below the existing senior tranches.</td>
</tr>
<tr>
<td>Collateral is a mix of well-seasoned and newly originated assets, with the overall pool having a weighted-average seasoning of 76 months. Of the pool, 36.4% has seasoning more than 60 months. In our view, more-seasoned performing loans exhibit lower risk profiles than less-seasoned loans.</td>
<td>Santander UK is a deposit-taking institution. If it were to become insolvent, borrowers could set off their mortgage payments against their deposits. The amount exposed to set-off risk crystallizes at the point of the borrowers' notification. Deposit set-off is considered in the minimum seller share and is re-evaluated on an ongoing basis.</td>
</tr>
<tr>
<td>Santander UK, via its subsidiaries, is an experienced mortgage servicer.</td>
<td>Many loans in the pool include flexible features and allow borrowers to take payment holidays, make overpayments, and draw on the loan by the amount of any previous overpayments. The seller funds the payment holidays and any additional drawings. If the seller becomes insolvent, the obligation to fund the flexible drawings will not transfer to the trust. Instead, the trust will be exposed to the risk of borrowers trying to set off their mortgage payments against their opportunity costs for the undrawn flexible amount. This risk is sized in the minimum seller share.</td>
</tr>
<tr>
<td>The pool has a low current indexed LTV ratio of 55.35%, which is most likely to incur lower loss severities if the borrower defaults.</td>
<td>Substitutions of assets will end if a balance is recorded against any principal deficiency ledger (PDL) other than that of the class Z-VFN. We consider this a concern for the transaction because the class Z-VFN constitutes most of the credit enhancement available to the rated tranches and because the further addition of loans may not be stopped soon enough if portfolio quality deteriorates over time. In our analysis, we rely on other stop-substitution triggers, such as the delinquency trigger, and we take this into account when analyzing the transaction.</td>
</tr>
<tr>
<td></td>
<td>We expect U.K. inflation to peak in 2023. Our credit and cash flow analysis and related assumptions consider the transaction's ability to withstand the potential repercussions of the current economic environment—including higher inflation, an increase in the cost of living, and interest rate rises—such as higher defaults and longer recovery timing due to a potential backlog in court cases. Considering these factors, we believe that the available credit enhancement is commensurate with the rating assigned. As the situation evolves, we will update our assumptions and estimates accordingly.</td>
</tr>
</tbody>
</table>

### Environmental, Social, And Governance (ESG)

Our analysis considers a transaction's potential exposure to ESG credit factors. For RMBS, we view the exposure to environmental credit factors as average, social credit factors as above average, and governance credit factors as below average (see "ESG Industry Report Card: Residential Mortgage-Backed Securities," published on March 31, 2021).

In our view, the exposure to social credit factors is in line with the sector benchmark. Social credit factors are generally considered above average because housing is viewed as one of the most basic human needs, and conduct risk presents...
a direct social exposure for lenders and servicers, particularly as regulators are increasingly focused on ensuring fair treatment of borrowers. For RMBS, social risk is generally factored into our base-case assumptions.

The transaction's exposure to environmental credit factors is also in line with the sector benchmark. Physical climate risks could severely damage properties and reduce their value, decreasing recoveries if borrowers default. We believe that well-diversified portfolios reduce exposure to extreme weather events.

In our view, the exposure to governance credit factors is relatively higher than the sector benchmark given new mortgages can be added to the trust resulting in the risk of loosening underwriting standards or potential adverse selection. However, Santander UK has strong internal control frameworks with significant relevant experience at key stages of the process. Finally, the origination process is subject to regular post-completion scrutiny and checking and oversight. Under the transaction documents, new mortgage loans are subject to certain eligibility criteria, which aim to ensure that the pool does not deteriorate in credit quality.

Changes From Holmes Master Issuer Series 2023-1 PLC

Since we rated the series 2023-1 class A1 notes, no key changes have taken place within the Holmes Master Issuer trust.

Originator And Servicer

Santander UK originated the loans in the portfolio between 1995 and 2023. It is the third-largest residential mortgage lender in the U.K. based on the value of mortgages outstanding. Its principal activity is retail banking, which includes residential mortgage lending. We consider Santander's underwriting standards to be among the best in the market, and the Holmes trust's asset performance has exhibited this historically. Santander UK also services the portfolio, although certain obligations under the mortgage administration agreement have been delegated to Santander Operations Ltd., a wholly owned subsidiary of Banco Santander S.A., which manages possession-to-sale. Westcot Credit Services, which is independent of Banco Santander, handles some early stage arrears. While outsourcing can have benefits, it can also create additional management issues. However, overall, we consider Santander UK's outsourcing activity to be well organized and beneficial.

Collateral

For Holmes Master Issuer's series 2023-2 issuance, we have received loan-level data as of July 31, 2023. The £3,612,354,370 pool comprises 40,865 loan parts originated by Santander UK. The assets are owner-occupied mortgage loans secured against properties in the U.K. As part of this issuance, £1,299,509,295.79 additional assets were sold to the trust. Overall, the quality of data provided is in line with our standards.

Subject to meeting certain conditions, the seller can continue to sell additional loans to the trust (see "sale of new loans" section below).
We received a yearly pool audit report rather than an audit as part of this issuance, so we continue to apply an adjustment to our weighted-average foreclosure frequency (WAFF) assumptions because we have historically observed some small error count in this pool.

We present below the stratification for the pool at cutoff.

Table 1

<table>
<thead>
<tr>
<th>Collateral key features*</th>
<th>Holmes Master Issuer Series 2023-2</th>
<th>Holmes Master Issuer Series 2023-1</th>
<th>Holmes Master Issuer Series 2022-1</th>
<th>Holmes Master Issuer Series 2018-2</th>
</tr>
</thead>
<tbody>
<tr>
<td>Pool cutoff date</td>
<td>July 31, 2023</td>
<td>Dec. 31, 2022</td>
<td>June 30, 2022</td>
<td>June 30, 2018</td>
</tr>
<tr>
<td>Principal outstanding of the pool (bil. £)</td>
<td>3.612</td>
<td>2.442</td>
<td>2.015</td>
<td>5.206</td>
</tr>
<tr>
<td>Number of loan parts</td>
<td>40,865</td>
<td>38,380</td>
<td>39,022</td>
<td>91,993</td>
</tr>
<tr>
<td>Average loan balance (£)</td>
<td>146,172</td>
<td>120,322</td>
<td>103,797</td>
<td>105,051</td>
</tr>
<tr>
<td>Weighted-average indexed current LTV ratio (%)</td>
<td>55.3</td>
<td>47.4</td>
<td>41.9</td>
<td>53.6</td>
</tr>
<tr>
<td>Weighted-average original LTV ratio (%)</td>
<td>68.9</td>
<td>67.6</td>
<td>69.0</td>
<td>72.9</td>
</tr>
<tr>
<td>Weighted-average effective LTV ratio (%)</td>
<td>66.0</td>
<td>63.6</td>
<td>63.6</td>
<td>N/A</td>
</tr>
<tr>
<td>Weighted-average seasoning (months)</td>
<td>76</td>
<td>113</td>
<td>150</td>
<td>116</td>
</tr>
<tr>
<td>First-time buyers (%)</td>
<td>20.5</td>
<td>12.9</td>
<td>10.9</td>
<td>12.3</td>
</tr>
<tr>
<td>Fast-track loans (%)</td>
<td>8.7</td>
<td>15.2</td>
<td>22.4</td>
<td>27.5</td>
</tr>
<tr>
<td>Self-employed (%)</td>
<td>21.6</td>
<td>28.0</td>
<td>33.3</td>
<td>N/A</td>
</tr>
<tr>
<td>Loan to income &gt;3.25x (%)</td>
<td>56.1</td>
<td>48.4</td>
<td>43.6</td>
<td>N/A</td>
</tr>
<tr>
<td>Interest only and part and part (%)</td>
<td>23.5</td>
<td>38.5</td>
<td>47.6</td>
<td>47.9</td>
</tr>
<tr>
<td>Buy-to-let (%)</td>
<td>0.0</td>
<td>0.0</td>
<td>0.0</td>
<td>0.0</td>
</tr>
<tr>
<td>Total CCJs (%)</td>
<td>0.3</td>
<td>0.5</td>
<td>0.7</td>
<td>1.4</td>
</tr>
<tr>
<td>Bankruptcy (%)</td>
<td>0.0</td>
<td>0.1</td>
<td>0.1</td>
<td>0.9</td>
</tr>
<tr>
<td>Loan purpose: equity release, debt consolidation, and cash-out</td>
<td>12.1</td>
<td>16.0</td>
<td>18.9</td>
<td>19.8</td>
</tr>
<tr>
<td>Fixed-floating loans (%)</td>
<td>69.2</td>
<td>49.4</td>
<td>26.8</td>
<td>18.7</td>
</tr>
<tr>
<td>Float-life loans (%)</td>
<td>30.6</td>
<td>50.3</td>
<td>73.1</td>
<td>80.3</td>
</tr>
<tr>
<td>Lien</td>
<td>All first lien</td>
<td>All first lien</td>
<td>All first lien</td>
<td>All first lien</td>
</tr>
<tr>
<td>Jumbo valuations (%)</td>
<td>11.2</td>
<td>14.1</td>
<td>15.3</td>
<td>34.9</td>
</tr>
<tr>
<td>‘AAA’ RMVD (%)</td>
<td>61.0</td>
<td>61.0</td>
<td>61.1</td>
<td>64.0</td>
</tr>
<tr>
<td>Full valuation (%)</td>
<td>68.8</td>
<td>70.4</td>
<td>74.4</td>
<td>74.0</td>
</tr>
<tr>
<td>Over/undervaluation applied</td>
<td>32.9</td>
<td>33.2</td>
<td>33.6</td>
<td>N/A</td>
</tr>
<tr>
<td>Current arrears greater than or equal to one month (%)</td>
<td>0.12</td>
<td>0.19</td>
<td>0.17</td>
<td>0.30</td>
</tr>
</tbody>
</table>

*Calculations are according to S&P Global Ratings’ methodology. LTV—Loan-to-value. CCJ—County court judgment. N/A—Not applicable. RMVD—Repossession market value declines.

The additions to the pool for the 2023-2 issuance cause an increase in our WAFF and weighted-average loss severity (WALS) assumptions compared with the series 2023-1 issuance (see “Credit Analysis And Assumptions”). The increase in WAFF is primarily driven by the increase in original LTV (about 1.2%), the increase in LTI (about 7.7% in the over 3.25x bracket), increase in fixed-floating loans (approximately 22.0%), reduction in the percentage of full valuations (about
1.5%), and increase in first-time buyers (approximately 7.5%). The increase in WALS is primarily driven by the 8.0% increase in current LTV.

Asset description
The portfolio comprises first-lien U.K. owner-occupied loans originated between 1995 and 2023. Of the portfolio, 23.5% comprises interest-only loans. Since there is no mandatory capital repayment over the term of the loan, the outstanding principal balance might not be paid by the end of the loan term. We have captured this risk by applying an adjustment to foreclosure frequency on the interest-only loans.

We also applied an adjustment for those cases where the borrower increased the size of the loan when remortgaging or there were previous debts consolidated in a new mortgage loan (12.1%). The additional leverage might increase the risk of default when compared to a refinance in which no further funds are drawn.

Of the pool, 21.6% of the loans were advanced to self-employed borrowers. We have captured this risk in our credit analysis through our self-employed adjustment.

The assets are well distributed geographically. However, there is some concentration in Greater London (22.7%), South East (20.3%), and East Anglia (13.3%). There is no exposure to any region exceeding the thresholds defined in our criteria.

The pool's weighted-average seasoning is 76 months. We consider seasoned performing loans to be less likely to default.

The weighted-average original LTV ratio is 68.7%. We consider that borrowers with lower LTVs are less likely to default on their obligations compared to borrowers with minimal equity in their property. The pool has a low weighted-average indexed current LTV ratio of 55.3%, which is most likely to incur lower loss severities if the borrower defaults.

Total arrears have remained low within the trust since the middle of 2019 and currently stand at 0.12%.
Chart 1

Original and current LTV ratio distribution

LTV—Loan to value.

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Chart 2

Joint LTI ratio--geographic distribution

LTI--Loan to income. OLTV--Original loan to value.

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Chart 3

Joint LTI ratio--employment

LTI--Loan to income. OLTV--Original loan to value.

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Chart 4

Geographic distribution

Scotland 5.17%
Northwest England 8.15%
Northeast England 2.07%
Yorkshire & Humberside 4.84%
East Midlands 5.54%
East Anglia 13.30%
Southeast England (inc. Greater London) 43.07%
Wales 2.92%
Southwest England 9.09%
Northern Ireland 0.00%
The portfolio contains both flexible loans and cashback loans. Once borrowers have made overpayments, flexible loans allow them to make underpayments, take payment holidays, or make cash withdrawals up to the value that they have overpaid. The seller is solely responsible for funding drawings under any flexible loans. For cashback loans, the lender must pay an amount to the borrower at some point in the future. Following the sale of these loans to the mortgage trust, the obligation to fund cashback amounts remains with the seller. The set-off risk for this product is mitigated via the seller share in the mortgages trust.

**Sale of new loans**

Under the transaction documents, the seller can sell new loans to the trust as long as they meet certain conditions. We considered this in our analysis. The conditions are as follows:

- The proportion of loans in the trust that are more than three monthly payments in arrears must be lower than 4%.
- The ratio of the total amount of arrears for loans in arrears of more than two months to the interest due on the loans in the previous 12 months must not exceed 2%.
- On the most recent interest payment date (IPD), Holmes Funding Ltd. (Funding) must not have had any PDL debit balance (other than the unrated PDL).
- The short-term rating on the seller must be at least ‘A-3’.
- The transaction must pass the WAFF, WALS, and yield tests.
- The first reserve fund must be at its required level.
- The number of new loans sold during any of Funding’s interest periods must not exceed 15% of the trust property’s number of loans at the beginning of that interest period.
Credit Analysis And Assumptions

We applied our global RMBS criteria to the pool in order to derive the WAFF and the WALS at each rating level.

The WAFF and WALS assumptions increase at each rating level because notes with a higher rating should be able to withstand a higher level of mortgage defaults and loss severity. Our credit analysis reflects the characteristics of loans, properties, and associated borrowers. Our WAFF and WALS assumptions also reflect that the sale of new assets into the trust can continue as long as the product of WAFF and WALS does not increase by more than 25 basis points.

Table 2
Portfolio WAFF and WALS

<table>
<thead>
<tr>
<th>Rating level</th>
<th>WAFF (%)</th>
<th>WALS (%)</th>
<th>Credit coverage (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2023-2 issuance</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>AAA</td>
<td>12.21</td>
<td>30.08</td>
<td>3.67</td>
</tr>
<tr>
<td>AA</td>
<td>8.76</td>
<td>23.25</td>
<td>2.04</td>
</tr>
<tr>
<td>2023-1 issuance</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>AAA</td>
<td>9.27</td>
<td>22.77</td>
<td>2.11</td>
</tr>
<tr>
<td>AA</td>
<td>7.07</td>
<td>15.99</td>
<td>1.13</td>
</tr>
</tbody>
</table>

WAFF--Weighted average foreclosure frequency. WALS--Weighted average loss severity.

Chart 6

'AAA' cumulative WAFF distribution of the initial pool

WAFF--Weighted-average foreclosure frequency. FF--Foreclosure frequency. CF--County court judgment. LTV--Loan to value.

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Macroeconomic And Sector Outlook

The information in this section reflects our most recent published economic forecasts. The current U.K. macroeconomic outlook remains uncertain and has recently been subject to significant changes within short timeframes. In addition to increased energy costs and the overall cost of living, rate rise expectations remain fluid against a backdrop of a stagnating macroeconomic environment. The rating assigned reflects this market uncertainty and our overall analysis considers the implications of a further deterioration in credit conditions.

Table 3

<table>
<thead>
<tr>
<th>U.K. housing market statistics</th>
<th>2022</th>
<th>2023f</th>
<th>2024f</th>
<th>2025f</th>
<th>2026f</th>
</tr>
</thead>
<tbody>
<tr>
<td>Nominal house prices, % change y/y</td>
<td>9.6</td>
<td>(6.6)</td>
<td>(4.9)</td>
<td>1.4</td>
<td>3.0</td>
</tr>
<tr>
<td>Real GDP, % change</td>
<td>4.1</td>
<td>0.0</td>
<td>0.9</td>
<td>1.6</td>
<td>1.7</td>
</tr>
<tr>
<td>CPI inflation (%)</td>
<td>9.1</td>
<td>7.0</td>
<td>2.4</td>
<td>1.6</td>
<td>1.8</td>
</tr>
<tr>
<td>Unemployment rate</td>
<td>3.7</td>
<td>4.2</td>
<td>4.6</td>
<td>4.3</td>
<td>4.2</td>
</tr>
</tbody>
</table>

Sources: S&P Global Ratings. Y/Y--Year on year. CPI--Consumer Price Index. f--Forecast.

Transaction Summary

The series 2023-2 issuance comprised one class A1 note with a scheduled amortization redemption profile.

Holmes Master Issuer is a public limited company incorporated in England and Wales. It conforms to our definition of a special-purpose entity (SPE). It was established to issue the notes and to make term advances from the note proceeds to Funding, which is Holmes Master Issuer's funding vehicle, under the intercompany loan agreement. It may issue further notes and make further term advances to Funding. Funding, which is also an SPE, uses the term advances' proceeds received under the intercompany loans to purchase a share of the trust property.
Class Z-VFN

In October 2021, the issuer redeemed the then outstanding series 2016-1 Z notes and at the same time issued an unrated Z-VFN class of notes. The class Z-VFN provides credit enhancement for all new and existing series of notes issued under the master trust. As per the documentation, on any IPD, the class Z-VFN’s balance may be reduced via a refinancing contribution from Santander UK, so long as the required subordination level (15%) is maintained. We have accounted for this in our cash flow analysis. The required subordination can come from either the class Z-VFN or the reserve fund.

Reserve fund

The reserve fund represents approximately 3.0% of the issued and currently outstanding rated notes. The fund can meet senior fees and note interest and cover any PDL balances other than the unrated PDL. It may also be used to meet any deficit in Funding’s available principal receipts to repay bullet term advances on their final scheduled...
repayment dates, and it may be used for 'AAA' scheduled amortization and pass-through term advances on their legal final maturity dates.

The reserve fund has a required amount of £68,000,000. Once the series 2018-1 A3 notes fully redeem, the required amount will be 3% of the outstanding rated notes and therefore will amortize in line with the rated notes. There will be no floor.

**Liquidity reserve fund**
A liquidity reserve fund may be established, depending on the long-term unsecured rating on the seller. It will be funded and replenished from revenue receipts or principal receipts, according to the revenue or principal priorities of payments. The required amount will equal the excess of 3% of the notes' principal outstanding amount over the reserve fund's current balance. If funded it can be used to cover senior fees and interest on the intercompany loans (other than unrated loans). Furthermore, under certain circumstances, the liquidity reserve fund can be used to make scheduled principal payments on bullet loans and on 'AAA' scheduled amortization and pass-through term advances.

**Seller share**
The seller has a share in the pool of assets, called the seller share. The seller share may fluctuate over time as the seller sells new mortgages into the trust. A sale of new assets into the trust (as long as this purchase is not funded through the issuance of additional notes) or a refinancing contribution to reduce class Z-VFN will result in an increase of the seller share. In contrast, if the seller receives the principal receipts from the mortgages without selling new assets into the trust or increasing the class Z-VFN, this will result in a decrease of its share in the trust property. In addition, the seller share can be reduced by the issuance of additional notes without purchasing additional mortgage collateral. Furthermore, any losses allocated to the seller will result in a decrease of its share in the trust property.

The minimum seller share is a floor below which the seller share cannot drop (except after an asset trigger event). The minimum seller share aims to provide protection against certain risks, e.g., deposit set-off. In this transaction, the minimum seller share has the components $W + X + Y + Z + AA$, where:

- $W = 100\%$ of the aggregate cleared credit balances of all savings accounts opened for "flexible plus" loans in the trust property.
- $X = 4.4\%$ of the aggregate current balance of loans in the trust property, as calculated on the relevant distribution date, or 104.4\% of the aggregate of the Financial Services Compensation Scheme (FSCS) excess amounts if FSCS excess amounts can be determined.
- $Y = \text{The product of: } p \times q \times r$, where: $p = 8\%$; $q = \text{the flexible draw capacity, which is equal to the ratio of the maximum amount of cash withdrawal that borrowers may draw under flexible loans included in the trust property over the aggregate principal balance of actual flexible loan advances in the trust property as determined for the previous distribution period};$ and $r=3$.  
- $Z = \text{The sum of the amount of any loans in the trust that the seller has failed to, or been unable to, repurchase due to a breach in loan warranties, and any loss incurred as a result of the seller materially breaching any of its obligations under the mortgage sale agreement or servicing agreement}.$
- $AA = \text{The aggregate entitlement of borrowers to receive reward cashbacks and delayed cashbacks in respect of the reward loans' remaining life in the trust property.}$
W and X aim to address risks related to deposit set-off. Y addresses risks related to set-off resulting from flexible mortgages. Z covers the risk that the seller fails in the performance of its obligations. AA covers the risk that the seller fails to fund any cashback amounts.

Issuer swap agreement–interest rate
From time to time, notes that bear a fixed interest rate may be issued out of the master trust. Intercompany loans will pay interest at a floating rate linked to Sterling Overnight Index Average (SONIA). Our rating assumes that the issuer will hedge any such mismatches by means of an interest rate swap transaction.

Funding swap agreement–interest rate
The funding swap is split into separate transactions to cover fixed, tracker, and standard variable rate (SVR) loans based on different maturities. Interest on the mortgages contained in the pool is either fixed-rate, discounted, linked to Santander UK’s SVR, or linked to the Bank of England base rate (BBR). Funding pays interest to the issuer on the intercompany loans in British pound sterling based on SONIA. Funding has entered into an interest rate swap to mitigate the basis risk between SONIA and the mortgage rate receipts (BBR, Santander UK’s SVR, or fixed rates). The economics of the interest rate swap agreements work as follows (although payments are netted):

- The weighted-average rate charged on the fixed-rate loans is paid to the counterparty, and Funding receives SONIA plus a spread.
- For BBR-linked loans, the weighted-average BBR-linked rate is paid to the counterparty, and Funding receives SONIA plus a spread.
- For SVR-linked loans, the rate payable by Funding to the swap provider is based on Santander UK’s SVR, in line with what it is receiving on the assets, and Funding receives SONIA plus a spread.

The notional balance of the Funding level interest rate swap is based on the sum of intercompany loans, less PDLs. Under this definition, and under certain interest rate scenarios, Funding could find itself owing net amounts to the swap counterparty that it does not receive on the underlying loan collateral (i.e., in the presence of nonperforming loans). This potential mismatch is mitigated in the transaction by Funding paying the lesser of the product of the notional swap balance and the weighted-average rate, and the sum of interest receipts from collateral and other income.

Post-perfection SVR
The transaction features a post-perfection mechanism. After the legal title is transferred from the borrower to the issuer, the latter instructs the servicer to set the SVR equal to SONIA plus 2.95%. In our view, this mechanism mitigates potential basis risk that could arise on the SVR loans. We therefore do not apply basis risk haircuts.

Cash allocations
The mortgage trustee will allocate principal collections as follows before a trigger event:

- Until the start of a cash accumulation period or repayment requirement, all principal receipts from the trust property will be allocated to the seller, unless the seller share of the trust property is less than the minimum seller share.
- From the start of a cash accumulation period, or when the requirement to repay a term advance comes into effect, available principal receipts will be allocated to Funding up to the cash accumulation or repayment requirement on
the relevant distribution day. The remainder will be paid to the seller, unless the seller share of the trust property is lower than the minimum seller share.

An asset trigger event will occur when an amount is debited to the ‘AAA’ PDL.

A non-asset trigger event will occur if:

• An insolvency event occurs regarding the seller;
• The seller's role as servicer is terminated and a replacement is not found within 60 days; or
• The seller share is lower than the minimum seller share on two consecutive trust distribution dates.

Interest on the notes is payable quarterly in arrears on the 15th day of January, April, July, and October each year, with the first IPD following the 2023-2 issuance being October 2023.

The mortgage trustee will distribute interest income from the mortgage trust to Funding and the seller pro rata and pari passu according to their respective percentage shares of the trust property. Losses will be allocated pro rata according to Funding and the seller's respective shares in the trust property.

Trigger events
A trigger event can be an asset trigger event or a non-asset trigger event. If a non-asset trigger event occurs, all principal receipts generated from the trust property will be allocated to Funding until its share is reduced to zero, and then to the seller.

If an asset trigger event occurs, principal receipts will be allocated pro rata between Funding and the seller, according to their respective percentage shares of the trust property. These payments to the seller may reduce the seller share below the minimum seller share. If an asset trigger occurs while a non-asset trigger is in effect, the asset trigger will take priority.

Cash accumulation, bullet repayment, and scheduled amortization repayment
The intercompany loans are split into separate advances that match the underlying classes of notes. Funding repays the intercompany loans from payments received from its share of the trust property, and interest and principal on the notes are paid using amounts received under the loans.

The intercompany loans have repayment schedules matching the redemption schedules on the notes.

Under certain conditions, a class of scheduled redemption notes or bullet redemption notes will be deemed to be pass-through. From that date, the issuer will repay the notes to the extent that funds are available, and subject to the conditions regarding repayment on IPDs.

Bullet term advances and scheduled amortization term advances are deemed to be pass-through if:

• A trigger event occurs;
• The note trustee serves a note acceleration notice on the issuer; or
• The Funding security trustee serves an intercompany loan acceleration notice on Funding.
For the scheduled amortization maturities of the term advances, the mortgage trustee accumulates principal to repay the relevant term advance under the relevant intercompany loans over the preceding three months.

**Previous issuance**
At the time of assigning our rating to the series 2023-2 notes, there are currently three existing series outstanding under the Holmes Master Issuer trust. The current aggregate amounts of the various classes of notes in series 2018-1, 2022-1, and 2023-1 as of the July 2023 investor report are shown in table 1 below.

### Table 4

<table>
<thead>
<tr>
<th>Holmes Master Issuer outstanding notes</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Series</strong></td>
</tr>
<tr>
<td>2018-1</td>
</tr>
<tr>
<td>2022-1</td>
</tr>
<tr>
<td>2023-1</td>
</tr>
</tbody>
</table>

**Future issuance**
Holmes may issue further notes. Under the intercompany loan agreement, Funding will be able to enter into new intercompany loan agreements during the life of the transaction and draw additional term advances. An issuance of notes will finance each new intercompany loan. The transaction documents specify that this will be permitted only if we confirm that the new issue of notes will not adversely affect the then-current ratings on the existing notes.

**Delinked issuance platform**
The delinked structure allows for the issuance of single series of rated notes as long as sufficient levels of credit support are available to support that incremental issuance and as long as we confirm that the issuance will not have an adverse effect on our ratings on existing notes, under the transaction documents.

In this case, Funding enters into the global intercompany loan agreement with Holmes Master Issuer, which in turn issues a secured series of notes.

On each closing date, Funding pays an amount equal to the issue proceeds or the increase in the global intercompany loan to the mortgages trustee to acquire or increase its interest in the trust property. To fund the increase in the intercompany loan, Holmes Master Issuer issues a single series of notes.

Subordinated notes with shorter maturities than senior notes can only be redeemed if, after the redemption of the subordinated tranches, the level of subordination below the senior notes is at its required level.

**Cash Flow Modeling And Analysis**

We stress the trust's cash flows to test the credit and liquidity support that the assets, class Z-VFN, and reserves provide.

We apply these stresses to the cash flows at all relevant rating levels. In our stresses for all notes, the notes must pay full and timely interest and principal.
Our analysis considers two key scenarios;

- In the "originator solvent" scenario we assume that the originator, Santander UK, remains solvent throughout the life of the transaction. As a result, substitutions can occur (subject to the triggers specified in the transaction documents), the class Z-VFN can amortize as the originator can make a refinancing contribution, credit can be given to all the funding swaps (the originator is also the swap counterparty), and no commingling is applied (since the originator provides the bank accounts).

- In the "originator insolvent" scenario we assume that the originator becomes insolvent on day one of the transaction. As a result, substitutions are unable to occur, the class Z-VFN is unable to amortize, no credit is given to the funding swaps (which reduces interest generated by the assets), and a commingling liquidity stress is applied.

We also run various sensitivities in relation to higher-than-expected defaults, extended recovery timing, and different recession timings.

**Commingling risk**

According to the bank account agreement for the mortgage trustee guaranteed investment certificate account:

- Upon the loss of an 'A/A-1' rating (or 'A+' if the account bank has no short-term rating), the cash manager or the mortgage trustee will open a standby account with a bank with the required rating; and

- Upon the loss of an 'A-2/BBB+' rating, the standby account will be utilized.

We have incorporated the risk of a commingling liquidity stress resulting from this replacement framework in the "originator solvent" run in our cash flow analysis, because the downgrade language in not in line with our current counterparty criteria.

**Fees**

Contractually, the issuer is obliged to pay periodic fees to various parties providing services to the transaction such as servicers, trustees, and cash managers, among others. In our analysis, we applied a stressed servicing fee of 0.25% (the higher of 1.5x actual fees and 0.25%) to account for the potential increase in costs to attract a replacement servicer, based on our global RMBS criteria.

**Interest rate risk**

Funding has entered into an interest rate swap to mitigate the basis risk between SONIA and the mortgage rate receipts (BBR, Santander UK's SVR, or fixed rates). However, the SONIA-BBR and SONIA-SVR interest rate swaps do not have any replacement framework. Therefore, in our originator insolvent cash slow scenario we do not give credit to these swaps and apply basis risk to account for this risk.

**Default and recovery timings**

We used the WAFF and WALS derived in our credit analysis as inputs in our cash flow analysis (see table 5). At each rating level, the WAFF specifies the total balance of the mortgage loans we assume will default over the transaction's life. Defaults are applied on the outstanding balance of the assets as of the closing date. We simulate defaults following two paths (i.e., one front-loaded and one back-loaded) over a six-year period. During the recessionary period within each scenario, we assume 25% of the expected WAFF is applied annually for three years.
Table 5

Default timings for front-loaded and back-loaded default curves

<table>
<thead>
<tr>
<th>Year after closing</th>
<th>Front-loaded defaults (% of WAFF per year)</th>
<th>Back-loaded defaults (% of WAFF per year)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>25.0</td>
<td>5.0</td>
</tr>
<tr>
<td>2</td>
<td>25.0</td>
<td>10.0</td>
</tr>
<tr>
<td>3</td>
<td>25.0</td>
<td>10.0</td>
</tr>
<tr>
<td>4</td>
<td>10.0</td>
<td>25.0</td>
</tr>
<tr>
<td>5</td>
<td>10.0</td>
<td>25.0</td>
</tr>
<tr>
<td>6</td>
<td>5.0</td>
<td>25.0</td>
</tr>
</tbody>
</table>

WAFF—Weighted-average foreclosure frequency.

We assume recoveries on the defaulted assets will be received 18 months after default for owner-occupied properties.

Delinquencies
To simulate the effect of delinquencies on liquidity, we model a proportion of scheduled collections equal to one-third of the WAFF (in addition to assumed foreclosures reflected in the WAFF) to be delayed. We apply this in each of the first 18 months of the recession and assume a full recovery of these delinquencies will occur 36 months after they arise.

Prepayments
To assess the effect on excess spread and the absolute level of defaults in a transaction, we model both high and low prepayment scenarios at all rating levels (see table 6).

Table 6

Prepayment assumptions

<table>
<thead>
<tr>
<th></th>
<th>High</th>
<th>Low</th>
</tr>
</thead>
<tbody>
<tr>
<td>Pre-recession</td>
<td>30.0</td>
<td>4.0</td>
</tr>
<tr>
<td>During recession</td>
<td>3.0</td>
<td>3.0</td>
</tr>
<tr>
<td>Post-recession</td>
<td>30.0</td>
<td>4.0</td>
</tr>
</tbody>
</table>

Interest rates
We modeled two interest rate scenarios in our analysis: up and down.

Summary
In combination, the default timings, interest rates, and prepayment rates described above give rise to eight different scenarios at each rating level (see table 7).

Table 7

RMBS stress scenarios

<table>
<thead>
<tr>
<th>Total number of scenarios</th>
<th>Prepayment rate</th>
<th>Interest rate</th>
<th>Default timing</th>
</tr>
</thead>
<tbody>
<tr>
<td>8</td>
<td>High and low</td>
<td>Up and down</td>
<td>Front-loaded and back-loaded</td>
</tr>
</tbody>
</table>

Scenario analysis
We analyzed the effect of a moderate stress on our WAFF assumptions and its ultimate effect on our rating on the notes. We ran two stress scenarios to demonstrate the rating transition of a note, and the results are in line with our
credit stability criteria. Given the maturity date of the notes, we also tested the effect of later recession timings, and consider the rating to be robust.

Counterparty Risk

There are no counterparty constraints on the rating on the notes in this transaction. To the extent that the replacement framework outlined in the transaction documentation is not in line with our counterparty criteria, we have applied additional stresses in our cash flow analysis to account for this (see "Commingling risk" and "Interest rate risk" above).
### Table 8

<table>
<thead>
<tr>
<th>Institution/role</th>
<th>Current counterparty rating</th>
<th>Collateral posting trigger</th>
<th>Replacement trigger</th>
<th>Maximum supported rating</th>
</tr>
</thead>
<tbody>
<tr>
<td>Santander UK PLC as the mortgage trustee bank account provider, issuer bank account provider, master issuer non-sterling bank account provider, and funding bank account provider</td>
<td>A/Stable/A-1</td>
<td>N/A</td>
<td>A/A-1</td>
<td>AAA</td>
</tr>
<tr>
<td>Santander UK PLC as the funding swap provider (SONIA-Fixed swap only)</td>
<td>A+/--/A-1*</td>
<td>A-</td>
<td>A-</td>
<td>AAA</td>
</tr>
<tr>
<td>Bank of New York Mellon as the funding bank account provider</td>
<td>AA-/Stable/A-1+</td>
<td>N/A</td>
<td>A/A-1</td>
<td>AAA</td>
</tr>
</tbody>
</table>

Note: There are no counterparty constraints on the rating on the notes in this transaction. The replacement language in the documentation is in line with our current counterparty criteria. For a full list of transaction participants, please refer to the appendix. *Resolution counterparty rating. N/A—Not applicable.

### Sovereign Risk

Our long-term unsolicited sovereign credit rating on the U.K. is 'AA'. This enables the notes to achieve a maximum potential rating of 'AAA'. Therefore, our structured finance sovereign risk criteria do not constrain our rating in this transaction.

### Surveillance

We will maintain surveillance on the transaction until the notes are paid off or are otherwise retired. To do this, we will analyze regular servicer reports detailing the performance of the underlying collateral, monitor supporting ratings, and make regular contact with the servicer to ensure that it maintains minimum servicing standards and that any material changes in the servicer's operations are communicated and assessed.

Various factors could lead us to lower our rating on the notes, such as increasing foreclosure rates in the underlying pool and changes in the pool composition. We have analyzed the effect of increased defaults by testing the sensitivity of the rating to two different levels of movements.

Under our scenario analysis, the rating on the notes in both scenarios would not suffer a rating transition outside of that considered under our credit stability criteria.

We also conducted additional sensitivity analysis to assess the effect of, all else being equal, increased WAFF and WALS on our rating on the notes. For this purpose, we ran eight scenarios by either increasing stressed defaults and/or reducing expected recoveries as shown in the tables below.
Table 9

**Sensitivity stresses**

<table>
<thead>
<tr>
<th>WALS</th>
<th>WAFF</th>
<th>1.0x</th>
<th>1.1x</th>
<th>1.3x</th>
</tr>
</thead>
<tbody>
<tr>
<td>Base case</td>
<td>Sensitivity 1</td>
<td>Sensitivity 2</td>
<td>Sensitivity 3</td>
<td>Sensitivity 4</td>
</tr>
<tr>
<td>Sensitivity 1</td>
<td>Sensitivity 5</td>
<td>Sensitivity 6</td>
<td>Sensitivity 7</td>
<td>Sensitivity 8</td>
</tr>
</tbody>
</table>

Table 10

**Sensitivity analysis results**

<table>
<thead>
<tr>
<th>Series and class</th>
<th>Base Case</th>
<th>Sensitivity 1</th>
<th>Sensitivity 2</th>
<th>Sensitivity 3</th>
<th>Sensitivity 4</th>
<th>Sensitivity 5</th>
<th>Sensitivity 6</th>
<th>Sensitivity 7</th>
<th>Sensitivity 8</th>
</tr>
</thead>
<tbody>
<tr>
<td>Series 2023-2 A1</td>
<td>AAA</td>
<td>AAA</td>
<td>AAA</td>
<td>AAA</td>
<td>AAA</td>
<td>AAA</td>
<td>AAA</td>
<td>AAA</td>
<td>AAA</td>
</tr>
</tbody>
</table>

Appendix

**Transaction participants**

<table>
<thead>
<tr>
<th>Role</th>
<th>Participant</th>
</tr>
</thead>
<tbody>
<tr>
<td>Originator</td>
<td>Santander UK PLC</td>
</tr>
<tr>
<td>Arranger</td>
<td>Santander Corporate &amp; Investment Bank PLC</td>
</tr>
<tr>
<td>Seller</td>
<td>Santander UK PLC</td>
</tr>
<tr>
<td>Mortgage administrator</td>
<td>Santander UK PLC</td>
</tr>
<tr>
<td>Funding swap provider</td>
<td>Santander UK PLC</td>
</tr>
<tr>
<td>Master issuer non-sterling account bank</td>
<td>Santander UK PLC</td>
</tr>
<tr>
<td>Master issuer corporate service provider</td>
<td>Wilmington Trust SP Services (London) Ltd.</td>
</tr>
<tr>
<td>Funding account bank providers</td>
<td>Santander UK PLC and Bank of New York Mellon</td>
</tr>
<tr>
<td>Mortgage trustee account bank provider</td>
<td>Santander UK PLC</td>
</tr>
<tr>
<td>Issuer account bank provider</td>
<td>Santander UK PLC</td>
</tr>
</tbody>
</table>

**Related Criteria**

- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- Criteria | Structured Finance | General: Methodology To Derive Stressed Interest Rates In Structured Finance, Oct. 18, 2019
- Criteria | Structured Finance | General: Counterparty Risk Framework: Methodology And Assumptions, March 8, 2019
Related Research

- Economic Outlook U.K. Q3 2023: Higher Rates Start To Bite, June 26, 2023
- EMEA Structured Finance Chart Book: June 2023, June 21, 2023
- European RMBS Index Report Q1 2023, May 15, 2023
- U.K. Residential Mortgage Servicing Flexibility Could Ease Arrears Pain, April 26, 2023
- Credit Conditions Europe Q2 2023: Costs Rising To Cure Inflation, March 28, 2023
- Economic Outlook U.K. Q2 2023: Growth Eludes This Year Even As Inflation Eases, March 27, 2023
- Credit FAQ: Sharing is Caring: U.K. Shared-Ownership RMBS Explained, March 21, 2023
- Scenario Analysis: How Much Shock Can U.K. RMBS Take?, March 1, 2023
- European RMBS Outlook 2023: Permafrost Or Thaw?, Jan. 12, 2023
- European Structured Finance Outlook 2023: Close To The Edge, Jan. 12, 2023
- Economic Research: European Housing Prices: A Sticky, Gradual Decline, Jan. 11, 2023
- Residential Mortgage Market Outlooks Updated For 13 European Jurisdictions Following Revised Economic Forecasts, May 1, 2020
- 2017 EMEA RMBS Scenario And Sensitivity Analysis, July 6, 2017