Totens Sparebank Boligkreditt

Norwegian Mortgage-Covered Bonds – Performance Update

Rating rationale (summary)

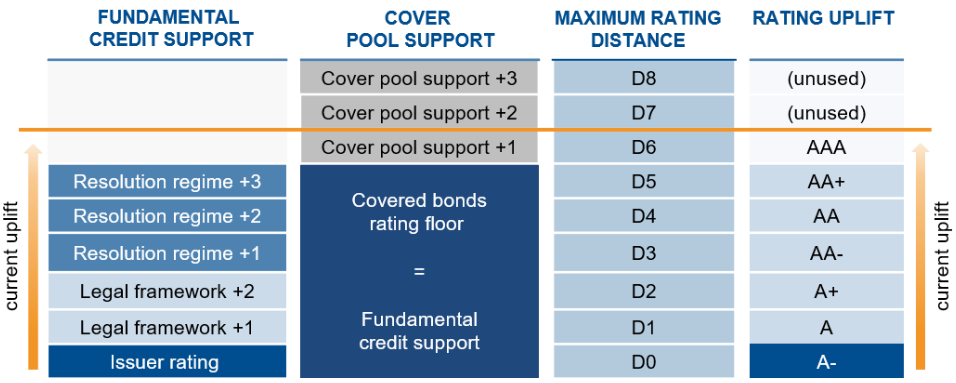
The AAA ratings with a Stable Outlook on the Norwegian covered bonds (obligasjoner med fortrinnsrett) issued by Totens Sparebank Boligkreditt (TSBB) are based on the bank's issuer rating of A- enhanced by six notches of cover pool support.

Cut-off date	Cover pool	Cover asset type	Covered bonds	Rating/Outlook
30 June 2021	NOK 4.49bn	Residential mortgage loans	NOK 3.97bn	AAA/Stable

TSBB is a wholly owned, specialised credit institution dedicated to providing secured covered bond funding for its parent, Totens Sparebank (TSB). Our A- issuer rating with a Stable Outlook on TSBB reflects its full ownership by TSB (A-/Stable) and its ability to refinance residential mortgage loans using covered bonds.

Fundamental credit support factors from the Norwegian legal and resolution framework provide an issuer-specific five-notch uplift above the bank's rating. This effectively forms a rating floor at AA+. Cover pool support enables the programme to be rated AAA, with another notch of uplift reflecting the credit strength of the covered bond programme.

The interplay between complexity and transparency is classified with a cover pool complexity (CPC) score of '1', allowing the maximum uplift of up to three notches on top of the fundamental uplift. From this, the programme can further benefit from a two-notch buffer against an issuer downgrade as the maximum theoretical uplift constitutes eight notches, as opposed to the six notches needed to achieve the highest rating for these covered bonds.



Stable Outlook

The Stable Outlook on the covered bond rating reflects: i) the continuous availability of high overcollateralisation (OC), which provides a buffer against a rise in credit and market risks; ii) our view that the European covered bond harmonisation will not negatively impact the fundamental support factors relevant for the issuer and Norwegian mortgage-covered bonds in general; and iii) our view of a stable credit quality of the issuer.

Changes since the last performance update

Since June 2020, the cover pool has increased to NOK 4.60bn (+30%). This was driven by new business that resulted from a rise in gross lending as well as the ongoing asset reallocation from mortgage loans previously registered in the EIKA covered bond programme. The indexed loan-to-value ratio (LTV) improved to 53.1% (down from 55.5%), mainly fuelled by strong house price increases over the same period.

Ratings & Outlook

Covered bond rating	**AAA**
Outlook	Stable
Rating action	Affirmation
Last rating action date	8 Oct 2021
Issuer rating	**A-**
Outlook	Stable
Last rating action	Affirmation
Last rating action date	8 Nov 2021

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Related Research

Scope affirms Totens Sparebank Boligkreditt's mortgage covered bonds at AAA/Stable, 8 October 2021

Scope affirms Toten Sparebank's issuer rating of A- with Stable Outlook

Updated analytical report on Totens Sparebank

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Bloomberg: RESP SCOP

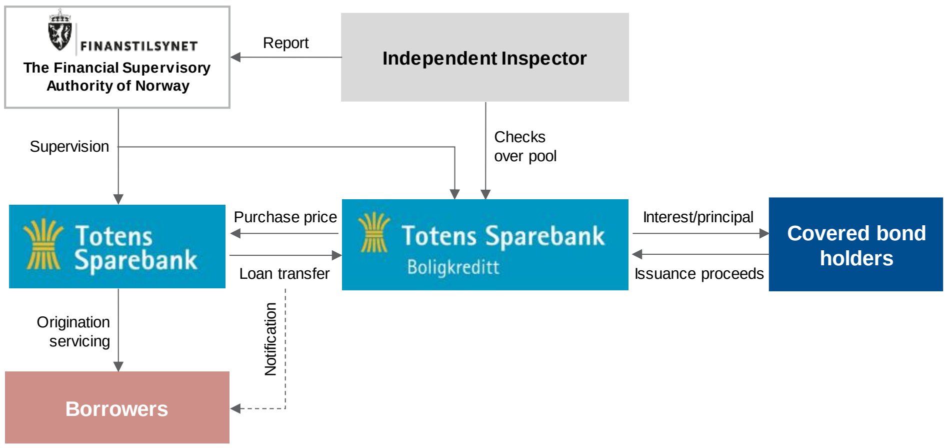
The issuer

The A-/Stable issuer rating also applies to TSBB, a wholly owned subsidiary of TSB. TSBB provides secured funding for its parent through the issuance of covered bonds. Established in 1854, TSB is a savings bank with a strong market position in south-eastern Norway. Macroeconomic conditions in Norway are supportive, with the country having recovered from a fall in oil prices in 2014. The bank operates primarily in the Mjos region, where agriculture, manufacturing and the public sector are important economic drivers. Over 70% of the bank's lending concerns residential mortgages. For further details on our bank credit analysis, see the full bank rating report available on www.scoperatings.com.

Programme structure

The Norwegian legal covered bond framework is mainly based on the relevant section on covered bonds in the country's Financial Institutions Act and related regulation on mortgage credit institutions, both introduced in 2007. Under this framework, issuance is permitted only through specialist covered bond issuers. Like TSBB, most issuers of covered bonds (generally called Boligkreditt, or specialised residential mortgage institutions) are subsidiaries that rely on loans originated by their respective parent banks. The parent banks generally also provide most of the services for these subsidiaries, allowing the latter to keep staff numbers low.

Issuance structure



Source: Scope Ratings

Fundamental credit support analysis

Fundamental credit support factors enhance the covered bond rating by five notches above TSBB's issuer rating. This is based on our view of: i) Norway's covered bond legal framework; and ii) the resolution regime and systemic importance of TSBB's covered bonds.

Two notches of uplift based on legal framework analysis…

We consider the Norwegian covered bond framework to be one of Europe's strongest, meeting our criteria for protecting investors. Therefore, we assign the highest credit differentiation of two notches.

… and three notches of uplift to reflect the resolution regime and systemic importance

TSBB's covered bonds benefit from an additional three-notch uplift to reflect their exemption from bail-in and the support from a strong stakeholder community. This is based on: i) a moderate to high likelihood that the covered bond issuer will be maintained in a resolution scenario; and ii) the high systemic importance of covered bonds in Norway. However, we also recognise the low visibility and importance of TSBB as a covered bond issuer. Generally, we provide four additional notches of support for Norwegian covered bonds issued by resolvable and very visible entities. For more information, see our related research.

Pool characteristics

Reporting date	June 2021	June 2020
Balance (NOK bn)	4.49	3.54
Residential (%)	97.7	96.9
Substitute (%)	2.3	3.1

Property type (%)

Reporting date	June 2021	June 2020
Single-family houses	71.2	72.0
Apartments	12.7	11.2
Shares*	8.0	8.5
Holiday homes	4.1	3.8
Others	4.0	4.5

*Shares in housing associations

General information

Reporting date	June 2021	June 2020
No. of loans	2,662	2,163
Avg. loan size (NOK m)	1.7	1.6
Top 10 (%)	1.9	2.2
Remaining life (years)	13.4	13.2
LTV (%)*	53.1	55.5

*Indexed

Interest rate type (%)

Reporting date	June 2021	June 2020
Floating	100	100
Fixed	0	0

Repayment type (%)

Reporting date	June 2021	June 2020
Bullet	5.7	6.5
Amortising	94.3	93.5

Cover pool analysis

TSBB's mortgage-covered bond ratings are cover pool-supported, providing six of the eight notches of uplift needed to achieve the highest rating. Fundamental credit support provides for a five-notch rating uplift and an effective floor against a deterioration in cover pool credit quality. Our assessment on the interplay between complexity and transparency translates into a CPC score of '1', which allows for the maximum three-notch uplift on top of the fundamental uplift.

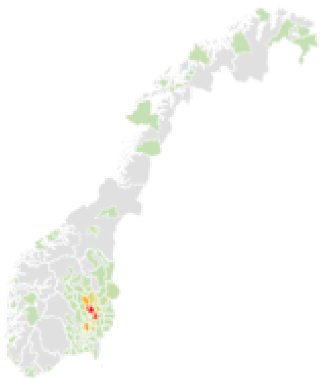
The minimum supporting OC needed to achieve the highest rating remains unchanged at 4%, supported by the sound credit metrics of the cover pool and the low market risks. Market risks arise from maturity mismatches, which are partly mitigated by the bonds' soft-bullet structure.

Cover pool composition

The cover pool is predominantly secured by Norwegian residential mortgage loans denominated in Norwegian krone. The cover pool also comprises substitute assets, mainly other highly rated Norwegian covered bonds. As of June 2021, the bank operates primarily in the Mjos region in south-eastern Norway, namely Innlandet (54.7%), Viken (33.1%), and Oslo (9.9%).

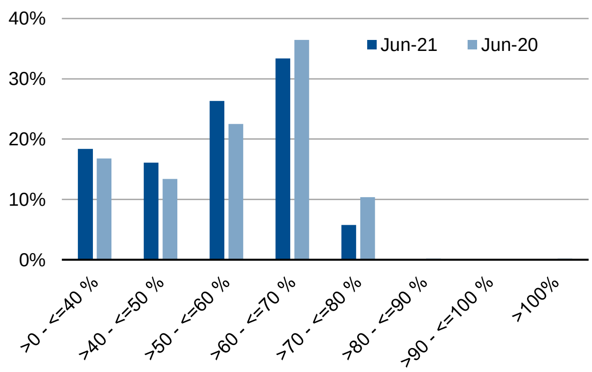
The mortgage pool consists of 2,662 loans granted to 2,585 obligors with an average loan size of NOK 1.69m. The largest obligor only accounts for 0.2%. Granularity has improved since our last review, reflecting the mortgage portfolio's growth by 30% and by 67% since June 2019.

Figure 1: Regional distribution



Source: Scope Ratings, TSBB

Figure 2: LTV distribution (indexed)



Source: Scope Ratings, TSBB

Most of TSBB's cover pool continues to be backed by mortgage loans granted to residential borrowers secured by single-family houses (71%), followed by apartments and shares in housing associations. The indexed LTV is 53.1%, 2.4pp down since our last review, fuelled by strong house price increases over the same period.

Asset risk analysis

Strong credit quality translates into low credit risk

The credit quality of the cover pool remains strong, supported by a stable economy even throughout the pandemic. We assume an annual average default probability of 21bps throughout the legal term of the underlying loans. This is different to the 42bps considered in last year's analysis as the annual average default probability now includes amortisation.

Our projection of default on mortgage loans uses an inverse Gaussian distribution, based on available credit performance data provided by the bank (in particular, historical delinquencies and portfolio loss rates) and benchmarking. We have further maintained our assumption of a coefficient of variation of 50% for the mortgage assets.

For the mortgage loans, we estimate a weighted average recovery rate of 99.8% (from 98.3%) under a base case and 70.0% (from 72.1%) under the most stressful scenario.

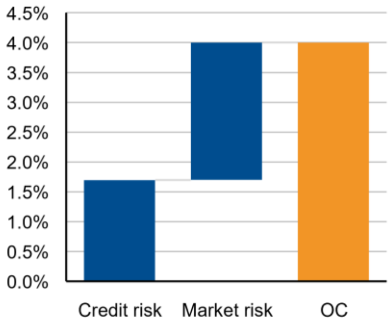
The base recovery rate is supported by the portfolio's low average LTV; the stressed rate is driven by updated market value declines reflecting Norwegian house price growth beyond levels we consider sustainable. The programme is further exposed to prior liens that result from senior claims pledged to Eika Boligkreditt, the secured funding platform used by TSB in tandem to its own. The share of prior liens, however, is decreasing (to 7% from 12%) in line with the TSB's usage of Eika's covered bond programme.

Due to the immaterial share of substitute assets, we considered the sub-pool as a single exposure to a financial institution rated A- combined with a typical three-year maturity and a stressed recovery rate of 50%.

Cash flow risk analysis

The unchanged supporting OC of 4.0% mainly reflects the programme's market risks, accounting for 2.4 pp (from 1.7 pp). Market risks are driven by maturity mismatches arising from the long weighted average life of the assets, at 13.4 years, compared to that of the covered bonds, at 4.5 years (extended). Under a low prepayment scenario (1%), the programme may be forced to sell assets at a discount to meet timely payments on the covered bonds.

Supporting OC breakdown



Source: Scope Ratings

Credit risks contribute 1.6% to the supporting OC and benefitted from a higher weight of amortisation taken into account in the analysis. This effectively reduces the lifetime mean default rate to 21 bps.

As of 30 June 2021, the available OC was 15.8%. This provides protection against market and credit risks and is well above the unchanged 4.0% minimum that supports the cover pool uplift.

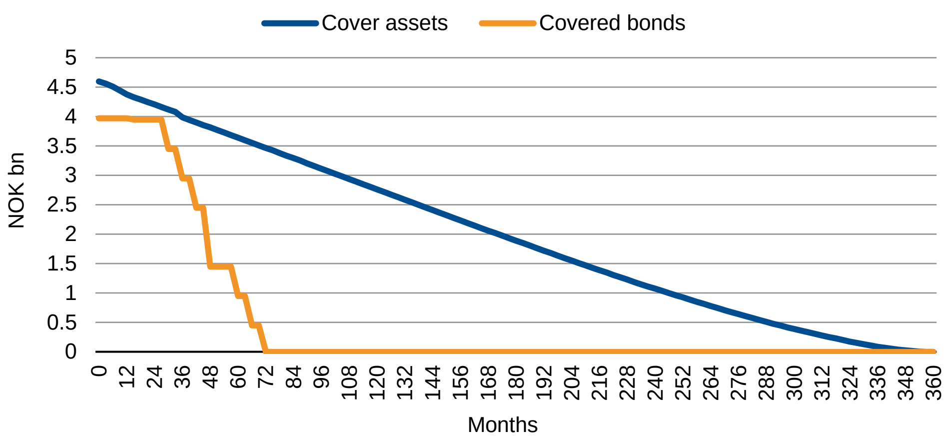
Other market risks are limited as cover assets and bonds have floating rates. There is no foreign exchange risk as assets and liabilities are denominated in Norwegian krone. At this stage we do not expect any foreign currency-denominated issuances.

Asset-liability mismatches

	Assets	Liabilities
NOK	100%	100%
Fixed	0.0%	0.0%
Floating	100%	100%
Scheduled WAL (years)	13.4	4.5[1]

[1]Considering one-year extension

Figure 3: Amortisation profile



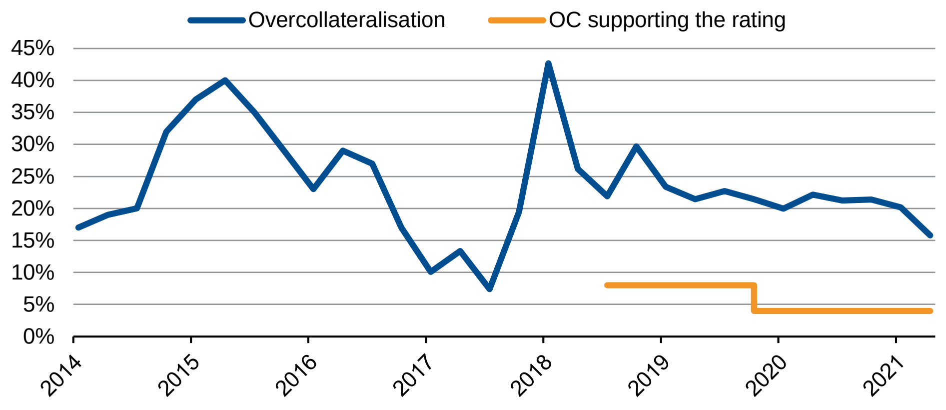
Source: Scope Ratings, TSBB

Availability of overcollateralisation

Overcollateralisation fully taken into account

The current rating of TSBB allows us to fully account for the provided OC. We are not aware of plans that would significantly change the programme's risk profile or reduce the available OC to levels that would no longer support the current rating uplift.

Figure 4: Available OC versus rating-supporting level



Source: Scope Ratings

Other risk considerations

Counterparty risk mitigated by alignment of interests between stakeholders

The rated covered bonds have counterparty exposures to the issuer, as well as to the issuer's parent as loan originator, servicer, bank account provider and paying agent. However, if a regulator were to intervene, we believe the strong alignment of interests between the bank and the covered bond holders would prevent any negative impact. We also take a positive view of the fact that collections are generally made via direct debit, allowing for a relatively swift redirection of payments if needed.

Country risk does not affect the rating

Sovereign risk does not limit the ratings of TSBB's mortgage covered bonds. We believe the risks of an institutional framework meltdown, legal insecurity or currency-convertibility problems are currently remote.

No impact from ESG

We have not directly included ESG aspects in our rating of the covered bonds issued by TSBB. The issuer currently has no specific ESG underwriting guidelines that would provide for positive/negative adjustments to the terms and conditions of a mortgage loan if minimum ESG conditions are met/not met. However, we understand TSB works on making ESG-related risks a part of the bank's credit underwriting process.

Due to data constraints, we could not perform a specific analysis of environmental or social factors, or their impact on the cover assets' probability of default or recovery proceeds. At the same time, we have indirectly included environmental aspects in our analysis as collateral valuations reflect the condition of the collateral.

The bank follows environmental, sustainability and corporate governance-related guidelines. The bank also operates an endowment scheme from which it regularly donates to regional charities. TSB actively seeks to contribute to growth and development in the region, which indirectly strengthens the bank's local market position.

Sensitivity analysis

Two-notch buffer against potential change in issuer rating

TSBB's mortgage-covered bond ratings benefit from a buffer against an issuer downgrade of up to two notches. Assuming the issuer's willingness to support the highest ratings as well as a stable covered bond programme risk profile, a one-notch downgrade would increase the supporting OC to 5.0%.

Summary of covered bond characteristics

Reporting date	30 June 2021	30 June 2020	30 June 2019	30 Sept 2018
Issuer name	Totens Sparebank Boligkreditt			
Country	Norway			
Covered bond name	Obligasjoner med fortrinnsrett (Norwegian mortgage covered bonds)			
Covered bond legal framework	Norwegian legal covered bond framework			
Cover pool type	Residential mortgage loans			
Composition	Residential = 97.7%	Residential = 96.9%	Residential = 91.4%	Residential = 90.8%
	Substitute = 2.3%	Substitute = 3.1%	Substitute = 8.6%	Substitute = 9.2%
Issuer rating	A-/Stable	A-/Stable	A-/Stable	A-/Stable
Current covered bond rating	AAA/Stable	AAA/Stable	AAA/Stable	AAA/Stable
Covered bond maturity type	Soft bullet	Soft bullet	Soft bullet	Soft bullet
Cover pool currencies	NOK (100%)	NOK (100%)	NOK (100%)	NOK (100%)
Covered bond currencies	NOK (100%)	NOK (100%)	NOK (100%)	NOK (100%)
Fundamental cover pool support	5	5	5	5
Maximum achievable covered bond uplift	8	8	8	8
Potential covered bond rating buffer	2	2	2	2
Cover pool (NOK bn)	4.49	3.54	2.76	2.08
thereof, substitute assets (NOK bn)	0.10	0.11	0.24	0.21
Covered bonds (NOK bn)	3.97	2.90	2.28	1.71
Overcollateralisation: current / legal minimum	15.8% / 2%	22.1% / 2%	21.2% / 2%	21.9% / 2%
Overcollateralisation to support current rating	4%	4%	4%	8%
Overcollateralisation upon a one-notch issuer downgrade	5.0%	5.5%	5.5%	9%
Weighted average life of assets	13.4 years	13.2 years	12.5 years	12 years
Weighted average life of liabilities [1]	4.5 years	4.4 years	4.5 years	2.6 years
Number of loans	2.662	2,163	1,713	1,452
Average loan size (NOK m)	1.7	1.6	1.5	1.4
Top 10 residential	1.9%	2.2%	2.9%	3.9%
Interest rate type – assets	Floating 100%	Floating 100%	Floating 100%	Floating 100%
	Fixed 0%	Fixed 0%	Fixed 0%	Fixed 0%
Interest rate type – liabilities	Floating 100%	Floating 100%	Floating 100%	Floating 100%
	Fixed 0%	Fixed 0%	Fixed 0%	Fixed 0%
Weighted average LTV (indexed)	53.1%	55.5%	52.6%	53.1%
Geographic split (top 3)	Innlandet = 55%	Oppland = 45%	Oppland = 45%	Oppland = 47%
	Viken = 33%	Akershus = 28%	Akershus = 26%	Akershus = 26%
	Oslo = 10%	Oslo = 12%	Oslo = 13%	Hedmark = 12%
Default measure	Inverse Gaussian/ Non-Parametric	Inverse Gaussian/ Non-Parametric	Inverse Gaussian/ Non-Parametric	Inverse Gaussian/ Non-Parametric
Weighted average default rate (mortgage/substitute)	6.0% / 0.32%	10.5%/ 0.15%	9.5%/ 0.21%	9.5%/ 0.11%
Weighted average coefficient of variation (mortgage/substitute)	50% / na	50%/ 1,696%	50%/ 1,353%	50%/ 1,375%
Weighted average recovery assumption (D0/D6)[2]	99.8% / 70.0%	98.3% / 72.1%	97.3% / 77.7%	99.0% / 66.5%
Share of loans > three months in arrears (NPL)	0.00%	0.00%	0.04%	0.04%
Interest rate stresses (max./min.; currency-dependent)	-1 to 10%	-1 to 10%	-1 to 10%	-1 to 10%
FX stresses (max./min.; currency-dependent)	n/a	n/a	n/a	n/a
Max liquidity premium	150bps	150bps	150bps	150bps
Average servicing fee	25bps	25bps	25bps	25bps

[1] Including the 12-month extension

[2] D0 and D8 denote the stresses commensurate with the rating distance between our credit view on the issuer and the covered bond ratings.

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