Bausparkasse Wüstenrot AG

Mortgage Covered Bonds

The AAA rating with a Stable Outlook assigned to the Austrian mortgage covered bonds issued by Bausparkasse Wüstenrot AG are based on the bank's sound issuer quality, enhanced by cover pool support based uplift. Cover pool support is the primary rating driver. Together with the programmes governance support, it provides seven notches of uplift above the issuer rating. We classified the interplay between complexity and transparency with a cover pool complexity (CPC) category of low, allowing the maximum additional uplift from cover pool support of 3 notches on top of the governance support uplift. Together, the programme benefits from a one-notch buffer against an issuer downgrade.

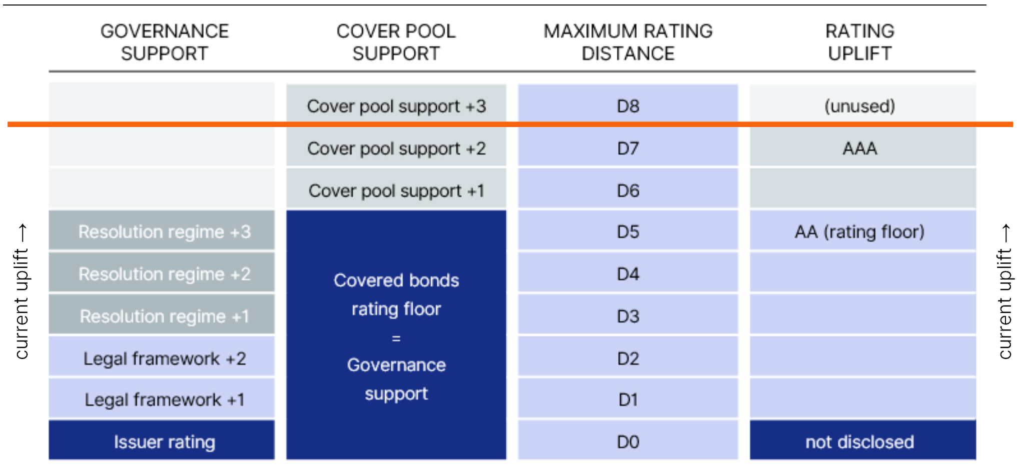
The covered bond programme

Cut-off date	Cover pool	Cover asset type	Covered bonds	Rating/Outlook
31 Dec 2023	EUR 2.05bn	Mortgage	EUR 1.56bn	**AAA/Stable**

Governance support factors, in total, provide a rating uplift of up to 5 notches and, effectively, a floor against a deterioration in cover pool credit quality. This reflects our assessment of the strong governance support provided by the legal covered bond and resolution framework in Austria.

The bonds are covered by a portfolio of domestic, well-distributed and seasoned residential mortgage loans across Austria. 73% of the loans benefit from a first lien mortgage, while the remaining are mostly supported by a guarantee in relation to subsidized housing. The loans benefit from a moderate loan-to-value (LTV) ratio of 57%, based on the eligible cover balance. The whole loan loan-to-value stands at 68.5%. The programme is exposed to interest rate mismatches. 80% of the mortgage loans are fixed rate which compares to 97% of the covered bonds. Most of the assets have interest resets before their final maturity date. Further, a weighted average life of 6.8 years for the bonds compares to 12.5 years for the asset portfolio, exposing the programme against asset sales under discount. No currency risk is present as all assets and bonds are denominated in EUR.

Figure 1: Covered bond rating building blocks



Covered bond rating
AAA

Outlook
Stable

Rating action
Affirmation

Last rating action
25 March 2024

Issuer rating
not disclosed

Outlook
not disclosed

Last rating action
not disclosed

Lead Analyst (covered bonds)

Mathias Pleißner
+49 69 66 77 389-39
m.pleissner@scoperatings.com

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Scope affirms AAA rating of Wüstenrot's Austrian mortgage-covered bonds, with Stable Outlook, March 2024

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Outlook Stable

Scope's Stable Outlook on the mortgage covered bonds reflects the Outlook on our private issuer rating and the strength of the cover pool, which could provide additional uplift. The rating may be downgraded upon: i) an issuer rating downgrade by more than 1 notch; ii) a deterioration in Scope's view on governance support factors relevant to the issuer and Austrian covered bonds in general and on the interplay between complexity and transparency, and/or iii) the inability of the cover pool to provide an additional uplift in case the issuer rating is downgraded.

Changes since the last performance update

Since our last analysis as of the first quarter 2023, the cover pool increased by 28% and the covered bonds by 21%, respectively. Interest rate mismatches slightly reduced with fixed rate mortgage loans up by 4.2% to 80% which compares to 97.2% of fixed covered bonds. Maturity mismatches remained relatively stable. Credit risk remains low and supported by a moderate and relatively stable loan-to-value (whole loan) of 68.5% (down from 69.1%).

Austrian house prices have seen some corrections. Since they peaked in Q3 2022 Austrian residential property prices on average have lost 4.2% (to Q4 2023) in value. Prices in Vienna have even depreciated by 5.4%.

Scope revised Austria's sovereign Outlook to Negative from Stable and affirmed ratings at AAA. Dependence on Russian energy imports and persistent divergence of the fiscal trajectory from highly-rated peers drives Outlook revision. A wealthy, diversified economy, favourable debt profile and sound external position are credit strengths. Country risk is not a key risk factor that constrains the covered bond rating.

Rating drivers and mitigants

Positive rating drivers	Negative rating drivers and mitigants
• Strong legal covered bond framework • Moderate to strong Resolution regime and systemic importance analysis only constrained by moderate to low systemic relevance of Wüstenrot • Potential deterioration of the issuers credit quality can be buffered with one unused notch from cover pool support	• Governance support uplift constrained by the issuer's size and relevance

Upside rating-change drivers	Downside rating-change drivers
• The ratings are on the highest level achievable • Additional issuer downgrade cushion could further arise from a rating upgrade of the issuer	• The rating may be downgraded upon an issuer downgrade by more than one notch • The rating may also be downgraded upon a deterioration of our assessment related to the programme's governance support factors and/or the interplay between complexity and transparency by together more than one notch • The rating may also be subject to a downgrade if the cover pool is unable to provide an additional uplift in case the issuer rating is downgraded or our governance analysis deteriorates

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The issuer

We maintain a private rating on Wüstenrot

We maintain and monitor a private issuer rating on Bausparkasse Wüstenrot AG, the only independent building society in Austria.

Wüstenrot is part of the Austrian Wüstenrot Group, which offers home financing, savings products, checking accounts, life and non-life insurance products (including health and mobility insurance) as well as investment products. The building society focuses on long-term, tax-advantaged saving products. Such proceeds are used to grant retail mortgages, which Wüstenrot originates through third-party banks and its own nationwide network of financial advisors. In addition, the insurance subsidiary develops life and non-life insurance products that are sold through its own network.

The building society is operating in a supportive environment that is highly supportive for banking activities, given the country's euro area membership, its wealthy, diversified and internationally competitive economy and its commitment to medium-term fiscal consolidation. The regulatory environment is strong, with a well-established and proactive banking supervisor, a comprehensive resolution regime and a consistent track record of promoting financial stability. Wüstenrot is jointly supervised by the Single Resolution board as well as the FMA, the Austrian Financial supervisory authority.

The group's environmental and social initiatives are well established, but do not distinguish from the industry average.

Wüstenrot's earnings and risk profile is supported by the bank's moderate but stable profitability which is based on very long-term relationships on both the loan and the deposit side.

Capital adequacy has benefited from profit retention in recent years. Funding and liquidity profile are sound as Wüstenrot is able to support loan growth by market debt. The dependence on wholesale funding is low; the bank uses senior preferred and covered bond issuance to diversify its funding profile and to comply with MREL requirements.

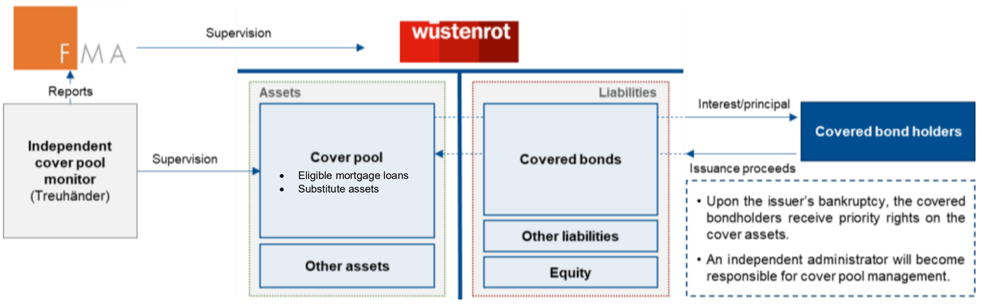
Programme structure

On balance sheet structure: Registered cover assets receive the status of a special estate

Covered bond issuance is governed by the Austrian Covered Bond Act (PfandBG) which implements the EU's Covered Bond Directive entered into force on July 8, 2022. This applies to all Covered Bonds issued from July 8, 2022. Wüstenrot has updated its debt issuance program to reflect the amended legislation and does since then issue covered bonds under the new covered bond law. As a bank and covered bond issuer, Wüstenrot is supervised by Austria's Financial Market Authority (FMA).

Cover assets remain on the bank's balance sheet as long as the issuer is solvent. If issuer insolvency proceedings are started, the cover assets receive the status of a special estate (Sondermasse), which segregates it from the remaining insolvency estate of the bank. For more details, see our legal framework analysis.

Figure 2: Issuance structure



Source: Scope Ratings

Governance credit support analysis

Governance credit support is a key rating driver for Wüstenrot's mortgage covered bonds. It provides an uplift of five notches. It combines our view on the legal framework for mortgage covered bonds in Austria together with our assessment on the Austrian resolution regime and the systemic relevance for covered bonds in general and specific to Wüstenrot.

Together five notches from legal framework and resolution regime

Legal framework analysis

We consider the Austrian's covered bond framework to be strong, fully meeting our criteria for protecting investors. Therefore, we assign the highest credit differentiation of two notches. The relevant legal framework is based on the Covered Bond Act (Pfandbriefgesetz or PfandBG). The legislation came into force on 8 July 2022, transposing the European Covered Bond Directive into local law. Issuances made before are not required to fulfill the requirements of the Austrian Covered Bond Act and are grandfathered with their original terms and conditions.

Two notches reflecting strong legal framework

Segregation of cover pool upon insolvency
The Austrian framework benefits from an 'on-balance sheet' cover pool. Cover assets are ringfenced by registration in the cover register ensuring a legally valid, binding and enforceable segregation upon the issuer's insolvency. Setting off against the cover pool is not allowed. When the issuer becomes insolvent, the cover pool receives the status of a special estate (Sondermasse), which segregates it from the remaining insolvency estate. The insolvency of the issuer will generally not impact the structure, terms and conditions of loans granted or the covered bonds issued. Covered bonds will not accelerate upon the insolvency or resolution of the issuer. If proceeds from the sale of cover pool assets are insufficient to repay the covered bonds, investors have third recourse to the general insolvency estate of the issuer.

Ability to continue payments after issuer insolvency
The Austrian Covered Bond Act highlights that resolution or insolvency of the issuer will not affect the ability to make the promised payments on covered bonds or derivatives in the cover pool. Following insolvency of the issuer, Austria's financial market supervisor (FMA) appoints a special administrator (besonderer Verwalter), that is responsible for managing the cover pool and to ensure full and timely payment of covered bonds according to their terms and conditions.

Asset eligibility and risk management principles
The Austrian framework ensures high standards regarding asset eligibility and replacement criteria. For mortgage covered bonds it allows for residential and commercial assets within the EEA, Switzerland and the United Kingdom. Underlying properties must be adequately insured against physical damage and the insurance must be part of the cover pool. Building plots and buildings under construction are eligible for up to 10% of the cover pool. Substitute and liquid assets (max. 15% of the covered bonds outstanding) can comprise exposures to eligible public-sector issuers, financial institutions, deposits and cash. Residential mortgage loans are eligible up to 80% of the properties' market or mortgage lending value; commercial mortgage loans are eligible up to 60% of the properties' market or mortgage lending value. However, the full loan amount is part of the cover pool register. Property valuation must be conducted by a party not involved in the mortgage lending process and shall be current at the time of inclusion into the cover pool. Values of commercial properties must be monitored at least once a year, at least every three years for residential properties.

Liquidity risk can be managed by issuing soft-bullet covered bonds. Only if such soft-bullet bonds are issued, the special administrator can have sole rights to extend the maturity of a covered bond by up to 12 months. In addition, the issuer is required to maintain sufficient amounts of highly-liquid assets in the cover pool to cover shortfalls for at least 180 days. Shortfalls are calculated based on the initial maturity date.

The Covered Bond Act does not provide explicit guidance on the management of other market risks. However, issuers have to ensure that a dedicated covered bond risk management department is independent from the operating business and has the relevant knowledge and capacities to monitor, assess and manage the risks of the covered bond programme. Derivatives can be registered and rank pari passu with covered bonds.

For now, Wüstenrot has not issued soft bullet bonds but addressed liquidity risks by maintaining liquid, high quiality substitute assets. Due to special regulation for saving banks covered bond funding is subject to limits in regards to asset encumbrance. For Wüstenrot, total outstanding covered bonds account for around 23% with a current limit at 30%.

Programme enhancements remain available

Neither a regulatory action nor an issuer's event of default impacts the ability to manage the covered bond structure. The special administrator has the right to collect payments, sell cover assets and enter bridge financings, if necessary. Derivatives in the cover pool will not terminate upon the issuer's insolvency and will remain available to service the covered bond programme.

Austrian covered bonds must provide a mandatory minimum nominal overcollateralisation (OC) of 2% in addition to expected wind-down costs; generally, also quantified at 2%. This will effectively provide for a minimum nominal OC of 4% that issuers need to maintain. Issuers can commit to higher OC levels, either on a nominal or net present value basis. Upon issuer insolvency, excessive or not explicitly committed OC above the legal minimum may be commingled with the general insolvency estate. However, it will generally be challenging to prove what amounts are deemed excessive. In addition, every removal of cover assets from the cover register and every new issue must be approved by the trustee. This was also evidenced with the failed Hypo Alpe Adria Bank. Even though their covered bonds had recourse to a very high level of OC, such were not released to increase the potential recoveries of unsecured debtholders.

Covered bond oversight

The FMA must approve covered bond issuance programmes. After the approval is granted by the FMA in co-operation with the Austrian National Bank (OeNB), regulators and supervisors perform special oversight over the programme. The FMA has the right to order special audits on the cover pool and can also order the issuer to carry out corrective measures. In addition, issuers have to appoint either an internal or external trustee (Treuhänder). The internal trustee would be represented by the risk management department. The trustee must ensure that cover assets comply with regulations, sign off (de)- registration of cover assets, hedging agreements and the issuance of new covered bonds. Where a breach has occurred or where the trustee sees the quality of the cover pool at risk, the trustee has to notify the FMA immediately. The issuer's insolvency will not impact the trustee's role and duties to avoid negative impacts from adverse management. Upon the issuer's insolvency, the insolvency court appoints a dedicated special administrator tasked with managing the cover pool (with the FMA's approval). The special administrator can be complemented by a 'Kurator', who represents joint covered bond holders.

Resolution regime and systemic importance analysis

Three notches reflecting resolution regime and systemic importance

Wüstenrots' covered bonds benefits from the country's transposition of the Bank Recovery and Resolution Directive that explicitly excludes covered bonds from being bailed in. It also benefits from the relevance of covered bonds within the country and a strong stakeholder community. Our assessment is limited by the size and relevance of Wüstenrot as an Austrian bank and mortgage covered bond issuer. This assessment translated into three notches, out of the four notches achievable.

Availability of statutory provisions

With the 1 January 2015 enactment of the Federal Act on the Recovery and Resolution of Banks (BaSAG), Austria implemented the EU's Bank Recovery and Resolution Directive (BRRD). Austria was among the first to actively use the restructuring provisions and also demonstrated how such provisions can work in favour of covered bond investors. When the FMA ordered a moratorium on Heta Asset Resolution AG – the workout entity of failed Hypo Alpe Adria Bank, senior unsecured debt was bailed-in but Heta's public-sector covered bonds were neither impacted by the moratorium nor bailed-in.

Strength of statutory provisions

Austrian covered bonds are explicitly excluded from bail-in. The issuer's business model, systemic importance, liability and capital structure allows the use of available resolution tools if needed. Wuestenrot is the only independent provider of Bausparkasse products in Austria. Thus, we would expect a higher incentive for the regulator to keep Wuestenrot as a going concern compared to comparably sized standard retail banks in the 'overbanked' Austrian retail market. At the same time, the small size of the issuer and its moderate to low systemic importance (see below) make an orderly wind-down more likely compared to a going concern as a mortgage covered bond issuer in Austria.

Systemic importance of issuer

Systemic relevance of Wüstenrot as a covered bond issuer is assessed to be moderate to low. As Austria's third largest building society, Wüstenrot benefits from strong brand recognition as the oldest and only remaining independent building society in Austria. However, as niche players, Austrian building societies only have limited product offering and suffered from an interest environment that has made their savings products less attractive to retail clients in the past. With assets at around EUR 7bn as of YE 2023, Wüstenrot is a relatively small player in the Austrian market but benefits from a significant market share in the highly regulated building deposit market. The granting of a banking licence in 2022 marks a milestone in the expansion and complementation of the business into a bancassurance provider offering banking, building society and insurance products from a single source. On the other hand, interconnectedness remains low. Wüstenrot is mainly regulated by the FMA. As a building society, Wüstenrot is also subject to specific Austrian building society regulation governing lending and deposit taking.

Systemic relevance of covered bonds

We classify Austrian mortgage covered bonds with a moderately high systemic relevance. As of end-2022, the outstanding volume accounted for more than 17% of Austrian GDP, which puts it into the upper third among European peers. 2022 was a record year in new mortgage covered bond issuance accounting for EUR 21.6bn which compares to EUR 6.1bn ten years ago. Twenty-three banks, comprising all large and most mid-size banks in Austria, are licensed to issue covered bonds. The number of 39 active covered bond programmes indicates that most issuers use both mortgage and public-sector covered bonds, as well as different programmes under the previous legislative frameworks. Austrian covered bonds are now increasingly placed with international investors, evidencing their importance to the issuers' funding toolkit. Between 2019 and early 2022, 11 Austrian banks publicly placed covered bonds in benchmark format. We also see an increasing trend of publicly placed sub-benchmark covered bonds from smaller issuers. The broader use of covered bonds across the banking landscape reduces the concentration of relative market shares.

Proactive stakeholder community

The importance of mortgage lending for banks and the increasing use of covered bonds as their main refinancing tool supports our view that the regulator should have an increasing interest in safeguarding covered bonds as an essential bank funding tool, especially in times of crisis. The 'Banks and Insurance' section of the Austrian Federal Economic Chamber (Wirtschaftskammer Österreich or WKO) has become the main platform for issuers to discuss their interests. provides information on the market, especially for international investors, and further aligns brand presence. WKO also represents issuers within the 'European Covered Bond Council', the European industry lobby. Supervisors have honoured the BRRD in previous situations and covered bonds have not been impacted.

Cover pool analysis

Wüstenrot's mortgage covered bond ratings are cover pool-supported, providing two of the seven notches of uplift needed to achieve the highest rating. Governance 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 category of 'Low'. The assessment on the interplay between complexity and transparency could add up to three additional notches above the issuer rating enhanced by governance support. Consequently, the combined credit support could allow to maintain the covered bond rating at the highest level under a hypothetical issuer downgrade by up to one notch, assuming OC does not become a constraining factor.

CPC assessment

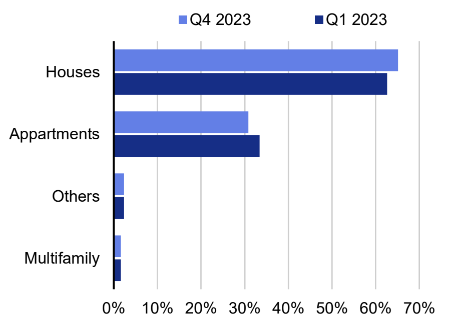
The CPC category of 'Low'-risk stems from Wüstenrot's management of the interplay between complexity and the level of transparency provided to stakeholders. Wüstenrot's covered bonds benefit from low complexity due to its high granularity and common loan types. Our assessment takes into account the mandatory cover-pool disclosures that have to be published on the issuer's website, at least on a quarterly basis. Effectively, most Austrian issuers including Wüstenrot provide such information using the ECBC's 'Harmonised Transparency Template' or its Austrian surrogate, the 'Austrian Transparency Template'. In addition, we receive information on the bank's lending products; underwriting and credit risk procedures and benefit from high visibility on origination and issuance strategy as well as to all relevant counterparty risk information.

Cover pool composition

Wüstenrot's mortgage covered bonds are secured by a portfolio of domestic and well-distributed residential mortgage loans across Austria. The low and relatively stable weighted average loan-to-value (LTV) ratio of 57.0% on an eligible-loan basis and the moderate whole-loan LTV ratio indicate a moderate-strong protection against credit losses in the event of borrower default. Although the whole loan secures outstanding covered bonds, only the eligible portion determines the maximum amount of bonds that can be issued. The Austrian Covered Bond Act stipulates a maximum (eligible) LTV ratio of 80% for residential mortgage assets. Wüstenrot limits mortgage loans to an eligible LTV ratio of 60% on a voluntary basis. As of Q4 2023 an insignificant share of 0.4% of mortgage loans (eligible loan part) does range between 60% to 80% based on Scopes calculated LTV.

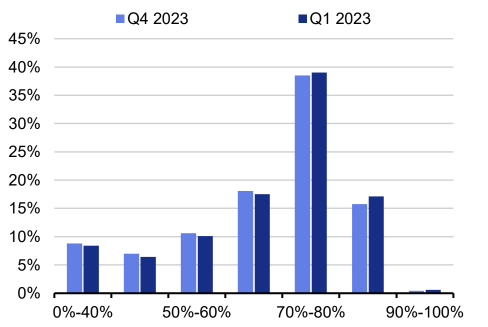
80% of the mortgage loans are fixed, which compares to 75.8% nine months ago. However, these loans are not fixed for life. The average remaining time to interest reset stands at 11.5 years, which compares to an average time to final maturity of the mortgage loans of 29.1 years. This exposes the mortgage loans to some interest rate risks. However, most of the bank's mortgage loans have embedded interest rate caps and floors, mitigating strong interest rate sensitivity after interest reset. The pool has no large concentrations and is very granular.

Figure 3: Property type distribution



Source: Scope Ratings, Wüstenrot

Figure 4: LTV distribution (whole loan)



Source: Scope Ratings, Wüstenrot

Cover pool characteristics

Reporting date	Dec 2023	March 2023
Balance (EUR bn)	2.05	1.63
Residential (%)	98.3	97.9
Commercial (%)	0.0	0.0
Substitute (%)	1.7	2.1

Property type (%)

Reporting date	Dec 2023	March 2023
Single/double-family house	65.1	62.7
Apartment	30.8	33.4
Multifamily	1.7	1.6
Others	2.4	2.3

General information

Reporting date	Dec 2023	March 2023
No. of loans (tsd)	16.7	13.8
Avg. size (EUR tsd)	122.0	125.4
Top 10 (%)	0.3	0.4
Remaining life* (years)	12.5	13.0
WA whole-loan LTV (%)	68.5	69.1
WA eligible-loan LTV (%)	57.0	57.5

*Scope calculated

Interest rate type (%)

Reporting date	Dec 2023	March 2023
Floating	20.0	24.2
Fixed	80.0	75.8

Repayment type (%)

Reporting date	Dec 2023	March 2023
Annuity / Linear	100	100
Interest-only	0.0	0.0

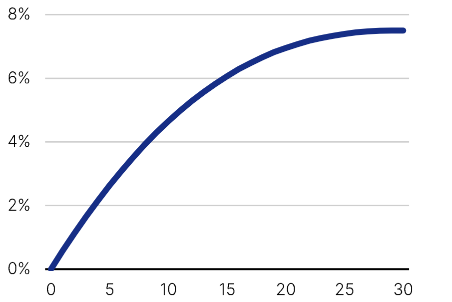
Asset risk analysis

Strong cover pool quality from a portfolio of granular domestic residential assets

The cover pool's credit quality is strong. Our projection of default applicable to Wüstenrot's granular residential mortgage assets uses an inverse Gaussian distribution. Our analysis is based on the bank's internal scores provided on a loan-by-loan basis and mapped to our ratings scale. We have considered publicly available credit performance data as well as historical originator performance.

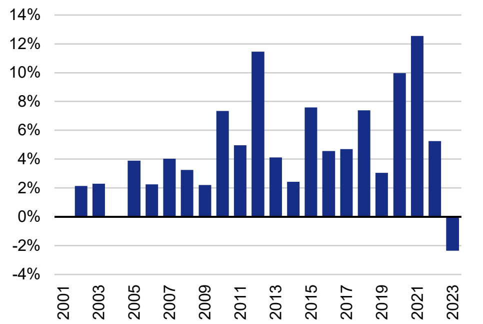
Our assessment results into an unchanged mean term default rate of 7.5%, corresponding to a one-year PD of 60bps considering our calculated weighted average life of 12.5 years. The coefficient of variation is 50% and based on benchmarking of comparable granular mortgage pools.

Figure 5: Expected term defaults, cumulative (DP/years)



Source: Scope Ratings

Figure 6: Annual house price growth in Austria



Source: oenb, Scope Ratings

Stressed recovery rates slightly decreased to 87.6%, down from 90% assessed nine months ago. This mainly reflects the reduction of property prices since our last analysis and a corresponding value depreciation over the entire asset portfolio. Since its peak in Q3 2022, prices dropped by 5% in Vienna and between 3-4% for flats and houses in the rest of Austria.

Our recovery rate calculations reflect rating distance-dependent security value declines as well as assumptions regarding the Austrian housing market and its unique characteristics. Our stressed market value decline assumptions decreased by around 2.5% compared to our last analysis. This does address market value increases below the sustainable average. Our base market value decline assumption remains at 10%, addressing additional value corrections in Austria.

Austrian security value haircuts

Region	Base MVD	Stressed MVD	FSD	Stressed SVH*	Stressed SVH (old)
Flats Vienna	10%	60.0%	20%	67.5	70.0
Houses Vienna	10%	37.5%	20%	47.5	50.0
Flats rest of Austria	10%	40.0%	20%	52.5	55.0
Houses rest of Austria	10%	37.5%	20%	47.5	50.0

MVD: market value decline / SVH: security value haircut / FSD: fire sale discount
* Excluding 7% variable cots and EUR 4,000 of fixed costs

Due to the generally dynamic management to the composition of substitute assets as well as their limited size we conservatively assumed the sub-pool as a single exposure against a financial institution and used the minimum credit quality stipulated by the covered bond legislation, combined with a three-year maturity.

Cash flow risk analysis

Supporting overcollateralisation of 6% allows for highest ratings and is well below the oc maintained

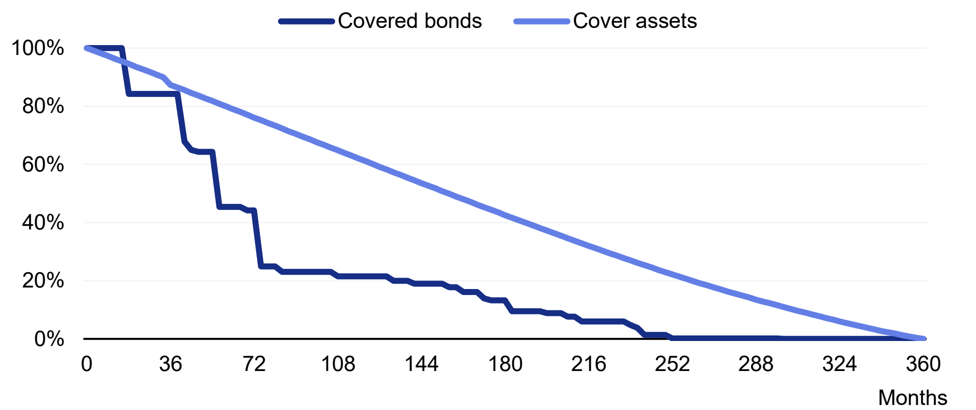
The unchanged rating-supporting OC of 6% reflects the mortgage programme's sensitivity to a combination of high prepayments (15%) with a stressed lower-for-longer interest rate scenario. This is mainly driven by interest rate mismatches with a surplus in floating (or resetting) assets. As such, high prepayments and low interest rates will significantly lower the programmes excess spread. In contrast, a low prepayment scenario (1%) under which assets need to be sold under discount is less penalizing – also supported by the liabilities' moderately long Scope calculated WAL of 6.8 years which compares to 12.5 years for the assets.

Cover pool support could provide additional rating stability. Our cash flow analysis shows, that if the issuer would be downgraded by one notch, the currently maintained nominal overcollateralisation of 29% would still be sufficient to support the highest achieveable rating on the mortgage covered bonds.

In the event of recourse to the cover pool and where available asset cash flows are not sufficient to pay the bond's maturing liability, we have assumed stressed asset sales used to cure liquidity shortfalls. We have applied a 150bp refinancing spread for the Austrian mortgage loans, which constitute of private domestic residential.

For the mortgage loans, we have built an amortisation schedule by using line by line data as provided by Wüstenrot. We have modelled fixed loan resets according to the individual reset date and assumed such loans to convert into floating rate with a margin equivalent to the current floating margin – interest caps have been disregarded. The liability profile was established based on line-by-line data provided. The amortisation profile of the substitute assets follows a generic three-year bullet amortisation.

Figure 7: Amortisation profile



Source: Scope Ratings, Wüstenrot

Asset-liability mismatches

	Assets	Liabilities
EUR (%)	100	100
Fixed (%)	80.0	97.2
Floating (%)	20.0	2.8
WAL (years)*	12.5	6.8

*Scope calculated

In addition, we have assumed servicing fees of 25bp. Default timing was expected to follow the scheduled amortisation profile with a recovery lag of 30 months. There is no foreign exchange risk as assets and liabilities are denominated in EUR.

We complemented our base case cash flow results with additional analysis, testing sensitivities to alternative interest rate scenarios, lower asset margins, loan refinancing at current fixed spot rates and frontloaded defaults.

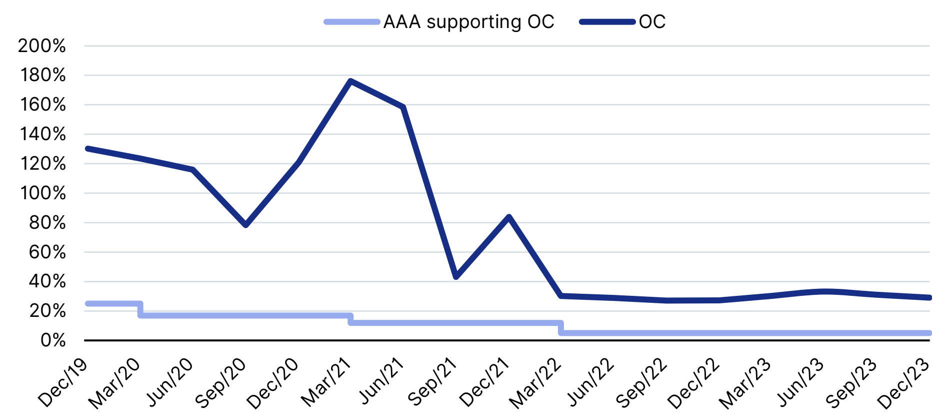
Availability of overcollateralisation

Supportive level of available overcollateralisation fully taken into account

The sound private rating of Wüstenrot allows us to account for the provided OC. Wüstenrot typically provides significantly higher levels of OC compared to the minimum stipulated by the legal framework (currently 2% plus wind down costs). This demonstrates the issuer's willingness and ability to support the covered bond programme's strong credit quality.

We are not aware that any change to the programme may alter its risk profile or reduce the available OC to levels that would no longer support the current rating uplift.

Figure 8: Available OC versus current rating-supporting level



Source: Scope Ratings, Wüstenrot

Other risk considerations

Counterparty exposure does not limit the rating

The rated covered bonds have counterparty exposures to Wüstenrot's roles as originator, servicer, account bank and paying agent. No documented replacement mechanisms would automatically shield the covered bonds from a credit deterioration due, for instance, to the counterparties providing bank accounts. However, in such a scenario we believe the strong alignment of interests between the bank and covered bondholders would prevent negative impacts before a regulator intervenes. We also take a positive view of the fact that most collections are made via direct debit, allowing for a relatively swift redirection of payments if needed.

In addition, we expect that a regulatory intervention in Wüstenrot would involve the use of available resolution tools with the aim of maintaining the issuer. We do not expect the active management and servicing of the cover pool to be severely impacted in such a scenario.

Country risk not a key rating driver

Country risk is not a key risk factor that constrains the covered bond rating. Austria is currently rated AAA/Negative by Scope. We have no evidence that transfer risk (e.g. risk of capital controls), convertibility risk (e.g. risk of eurozone exit), the risk of an institutional meltdown are pertinent risk factors for Austria.

Governance factors are key drivers and reflected in our governance uplift and CPC assessment

Governance factors are key for the analysis of Austrian covered bonds as such drive our legal and resolution regime analysis. In addition, our CPC category measures the issuer's management of the interplay between complexity and the level of transparency provided to investors which allows for the maximum additional cover pool support uplift of three notches.

We have not directly included environmental and social aspects in our rating of the covered bonds issued by Wüstenrot. The issuer currently does not apply specific ESG underwriting guidelines that provide for adjustments to the terms and conditions of a mortgage loan if minimum ESG conditions are met/not met. Similarly, information provided on collateral does not allow us to determine energy efficiency or differences in recovery proceeds.

Sensitivity analysis

One notch buffer against an issuer downgrade

Wüstenrots' mortgage covered bond ratings do benefit from a buffer against an issuer downgrade of up to one notch. 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 rating-supporting OC requirement to 7%.

As a consequence, the rating may be downgraded upon: i) an issuer rating downgrade by more than one notch; ii) a deterioration in Scope's view on governance support factors relevant to the issuer and Austrian covered bonds in general and on the interplay between complexity and transparency, and/or iii) the inability of the cover pool to provide an additional uplift in case the issuer rating is downgraded.

Summary of covered bond characteristics

Reporting date	31 Dec 2023	31 March 2023
Issuer name	Bausparkasse Wüstenrot AG	
Country	Austria	
Covered bond name	Hypothekenpfandbrief	
Covered bond legal framework	Austrian legal covered bond framework (Pfandbriefgesetz)	
Cover pool type	Residential mortgage loans	
Composition	98.3%	97.9%
	0.0%	0.0%
	1.7%	2.1%
Issuer rating	not disclosed	not disclosed
Current covered bond rating	AAA / Stable	AAA / Stable
Covered bond maturity type	Hard bullet	Hard bullet
Cover pool currencies	EUR (100%)	EUR (100%)
Covered bond currencies	EUR (100%)	EUR (100%)
Governance cover pool support	5	5
Maximum additional uplift from cover pool complexity category	3	3
Maximum achievable covered bond uplift	8	8
Potential covered bond rating buffer	1	1
Cover pool (EUR mn)	2,045.9	1,598.7
thereof, substitute assets (EUR mn)	34.0	34.2
Covered bonds (EUR mn)	1,585.4	1,311.9
Overcollateralisation: current/legal minimum	29.1% / 2%[1]	24.5% / 2%[1]
Overcollateralisation to support current rating	6%	6%
Overcollateralisation upon a one-notch issuer downgrade	7%	7%
Weighted average life of assets (Scope calculated)	12.5 years	13.4 years
Weighted average life of liabilities	6.8 years	7.5 years
Number of loans	16,704	13,851
Average loan size (EUR '000)	122.0	115.4
Top 10	0.3%	0.4%
Interest rate type assets	Floating = 20%	Floating = 24.2%
	Fixed = 80.0%	Fixed = 75.8%
Interest rate type liabilities	Floating = 2.8%	Floating = 3.4%
	Fixed = 97.2%	Fixed = 96.6%
Weighted average loan to lending value (eligible loan, Scope calculated)	57.0%	57.5%
Weighted average loan to lending value (whole loan)	68.5%	69.1%
Geographic split	Austria = 100%	Austria = 100%
Default measure (mortgage)	Inverse Gaussian	Inverse Gaussian
Weighted average annualised default rate	60bps	56bps
Weighted average coefficient of variation	50%	60%
Weighted average recovery assumption (D0;D8)[1]	99.5%; 87.6%	100%; 90.0%
Interest rate stresses (max/min)	10% / -1%	10% / -1%
FX stresses (max/min; currency-dependent)	na	na
Max liquidity premium	150bps	150bps
Average servicing fee	25bps	25bps

Source: Scope Ratings
[1]plus around 2% for wind down costs

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

Credit view on Bausparkasse Wüstenrot

Our credit view on Bausparkasse Wüstenrot AG (Wüstenrot) reflects the following assessments:

Wüstenrot group is a cooperative financial services group that operates primarily as Bausparkasse Wüstenrot (BWAG), which in turn owns Wüstenrot Versicherungs-AG. The group offers housing finance, financial provision, life and non-life insurance products (including health and mobility) as well as general insurance-based investment products. As niche players, Austrian building societies have steadily lost market share in recent years due to their limited product offering and an interest rate environment that has led to a reduction in the number of savings contracts with their retail customers. Nevertheless, the group has achieved stable results thanks to its conservative risk strategy, good cost management and successful diversification into insurance. With the digital Wüstenrot Bank AG, the group aims to become a true full-service financial institution in Austria, offering current accounts, savings, financing, insurance and pension products. Although the intrinsic risk profile and strategy are well developed and relevant, diversification and market position are considered a relatively greater challenge to the business model in the current environment.

The operating environment in Austria is highly supportive for banking activities, given the country's euro area membership, its wealthy, diversified and internationally competitive economy and its commitment to medium-term fiscal consolidation. The government has a favourable public debt profile and private sector debt is low. The Austrian banking system is highly fragmented and over-banked, with the largest financial institutions having extensive operations in the CEE region. Capitalisation and asset quality continue to improve steadily and profitability has recovered strongly, benefiting from recent interest rate hikes. The regulatory environment is sound, with a well-established and proactive banking supervisor, a comprehensive resolution regime and a consistent track record of promoting financial stability. Wüstenrot is locally regulated and not directly supervised by the ECB due to its small size. As a building society Wüstenrot is also subject to specific Austrian building society regulation governing lending and deposit taking.

The bank’s environmental and social initiatives are well established, but do not distinguish the bank from the industry average. Digitalisation has been recognised by management as a driver for the bank’s sustainable business development. However, the potential is still underexplored also in comparison with the Austrian banking market.

BWAG's moderate but stable profitability is based on very long-term relationships on both the loan and deposit side. The bank has countered the increasing pressure on margins in recent years by successfully managing its cost base. Asset quality has been strong for several years, but we expect a slight increase in NPLs in 2024 due to a deteriorating economic environment. Nevertheless, we expect BWAG's profitability to remain stable over the next two years.

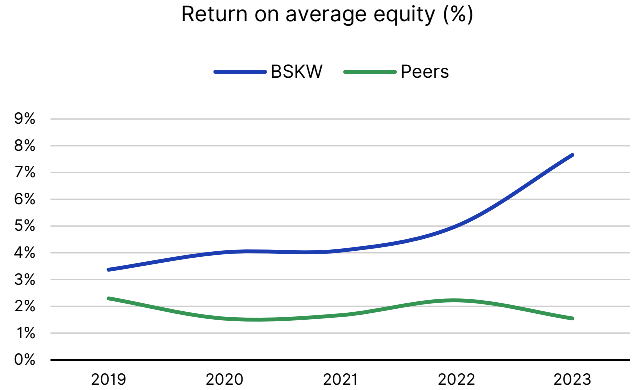
Capital adequacy is strong (CET1 ratio 760 bp above SREP minimum), having benefited from profit retention in recent years and the downstream merger of BWA Beteiligungs- und Verwaltungs-AG (former direct parent of BWAG) into BWAG. The funding and liquidity profile is sound, as BWAG is able to support loan growth with marketable debt. Dependence on wholesale funding is low, but the bank is increasingly using senior preferred and covered bond issuance to diversify its funding profile and meet MREL requirements.

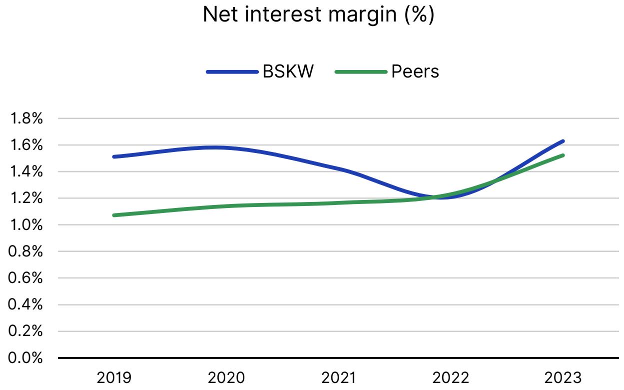
Credit view change-drivers

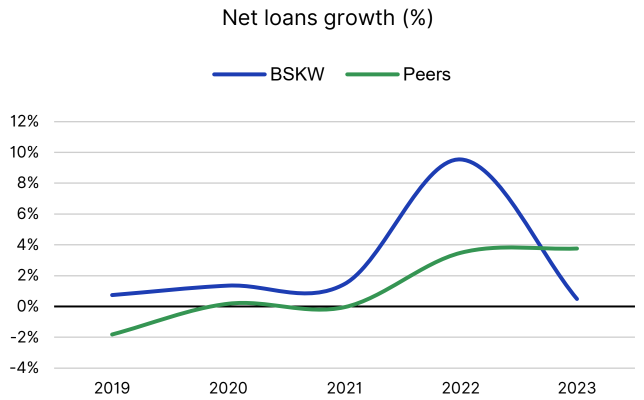
Our credit view could be positively impacted by successful expansion of the business profile through the implementation of a new digital bank and insurance offerings in the core Austrian retail market as well as stable long-term profitability achieved by diversifying income streams.

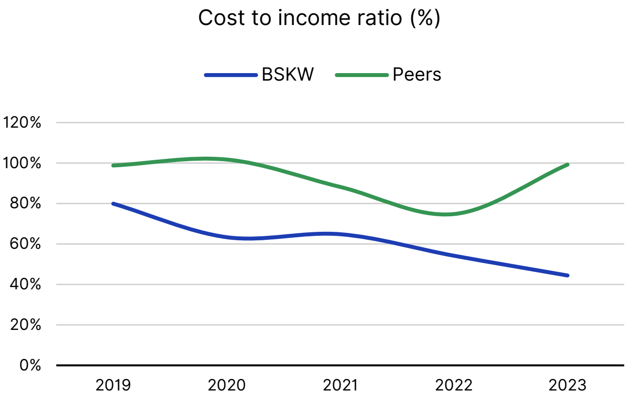
Our credit view could be negatively impacted by an unexpected change in the bank's underwriting standards following its expansion into digital retail banking, any risks arising from subsidiaries (insurance or CEE based) or significant deterioration in the bank's economic environment, i.e. the real estate sector in Austria and particularly the mortgage market.

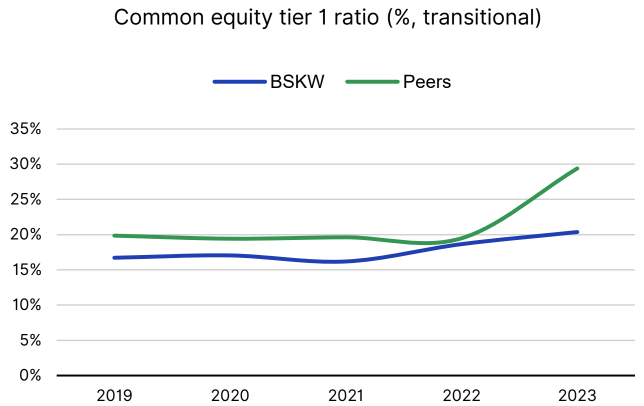
Peer comparison

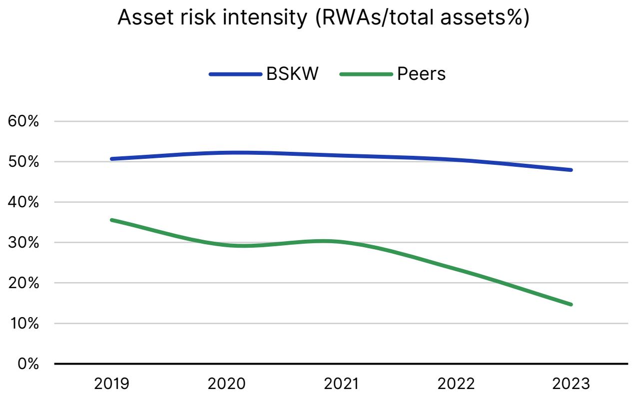












Peers: ALTE LEIPZIGER Bauspar AG, Bausparkasse der österreichischen Sparkassen AG (S Bausparkasse), Bausparkasse Mainz AG, Debeka Bausparkasse AG, start:Bausparkasse AG, Wüstenrot Bausparkasse AG
Source: SNL, Scope Ratings

Selected financial information I – Bausparkasse Wüstenrot AG

	2019	2020	2021	2022	2023
Balance sheet summary (EUR m)					
Assets					
Cash and interbank assets	311.1	295.0	213.4	233.6	227.1
Total securities	892.4	722.8	617.1	542.6	646.5
of which, derivatives	0.0	1.2	0.4	NA	73.4
Net loans to customers	4,846.3	4,911.4	4,982.5	5,458.0	5,484.0
Other assets	515.9	534.6	528.1	625.7	569.2
Total assets	**6,565.7**	**6,463.7**	**6,341.0**	**6,860.0**	**6,926.9**
Liabilities					
Interbank liabilities	34.1	72.0	192.9	232.2	234.2
Senior debt / Senior secured	271.0	326.0	966.9	1,518.3	1,894.5
Derivatives	61.1	93.4	50.9	106.5	89.4
Deposits from customers	5,434.2	5,212.3	4,330.2	4,205.8	3,934.3
Subordinated debt	100.0	100.0	100.0	100.0	0.0
Other liabilities	89.1	60.4	138.7	20.8	44.4
Total liabilities	**5,989.6**	**5,864.0**	**5,779.6**	**6,183.7**	**6,196.8**
Ordinary equity	576.1	599.7	561.5	676.3	730.1
Equity hybrids	0.0	0.0	0.0	0.0	0.0
Minority interests	0.0	0.0	0.0	0.0	0.0
Total liabilities and equity	**6,565.7**	**6,463.7**	**6,341.0**	**6,860.0**	**6,926.9**
Core tier 1/ common equity tier 1 capital	*556.9*	*576.0*	*529.4*	*645.7*	*676.3*
Income statement summary (EUR m)					
Net interest income	91.1	94.6	83.4	72.8	102.6
Net fee & commission income	8.2	7.1	10.4	20.6	17.2
Net trading income	NA	NA	NA	NA	NA
Other income	NA	NA	NA	NA	NA
Operating income	**134.9**	**103.3**	**106.8**	**102.9**	**124.2**
Operating expenses	107.7	65.4	69.2	55.8	55.2
Pre-provision income	**27.2**	**37.9**	**37.6**	**47.1**	**69.0**
Credit and other financial impairments	-8.8	10.8	7.6	-3.0	-0.9
Other impairments	14.4	1.6	2.1	7.4	7.9
Non-recurring income	NA	NA	NA	NA	0.0
Non-recurring expense	NA	NA	NA	NA	0.0
Pre-tax profit	**21.5**	**25.5**	**27.9**	**42.6**	**62.0**
Income from discontinued operations	0.0	0.0	0.0	0.0	0.0
Income tax expense	2.4	1.8	4.2	11.7	8.2
Other after-tax Items	0.0	0.0	0.0	0.0	0.0
Net profit attributable to minority interests	0.0	0.0	0.0	0.0	0.0
Net profit attributable to parent	**19.1**	**23.6**	**23.7**	**30.9**	**53.8**

Source: SNL, Scope Ratings
Note: Reclassified financial information could differ from "as reported financials"

Selected financial information II – Bausparkasse Wüstenrot AG

	2019	2020	2021	2022	2023
Funding and liquidity					
Net loans/ deposits (%)	89.18%	94.23%	115.06%	129.77%	139.39%
Liquidity coverage ratio (%)	396.50%	318.30%	340.30%	265.10%	291.60%
Net stable funding ratio (%)	138.30%	133.20%	132.60%	126.00%	130.40%
Asset mix, quality and growth					
Net loans/ assets (%)	73.81%	75.98%	78.58%	79.56%	79.17%
Problem loans/ gross customer loans (%)	1.18%	1.19%	NA	NA	NA
Loan loss reserves/ problem loans (%)	52.25%	58.31%	NA	NA	NA
Net loan growth (%)	0.73%	1.34%	1.45%	9.54%	0.48%
Problem loans/ tangible equity & reserves (%)	9.46%	9.27%	NA	NA	NA
Asset growth (%)	0.44%	-1.55%	-1.90%	8.18%	0.98%
Earnings and profitability					
Net interest margin (%)	1.51%	1.58%	1.42%	1.21%	1.63%
Net interest income/ average RWAs (%)	2.68%	2.82%	2.51%	2.16%	3.03%
Net interest income/ operating income (%)	67.56%	91.54%	78.13%	70.78%	82.62%
Net fees & commissions/ operating income (%)	6.06%	6.90%	9.75%	20.07%	13.86%
Cost/ income ratio (%)	79.86%	63.33%	64.80%	54.21%	44.47%
Operating expenses/ average RWAs (%)	3.17%	1.95%	2.08%	1.66%	1.63%
Pre-impairment operating profit/ average RWAs (%)	0.80%	1.13%	1.13%	1.40%	2.03%
Impairment on financial assets / pre-impairment income (%)	-32.29%	28.58%	20.25%	-6.32%	-1.31%
Loan loss provision/ average gross loans (%)	-0.18%	0.22%	NA	NA	NA
Pre-tax profit/ average RWAs (%)	0.63%	0.76%	0.84%	1.27%	1.83%
Return on average assets (%)	0.29%	0.36%	0.37%	0.47%	0.78%
Return on average RWAs (%)	0.56%	0.70%	0.71%	0.92%	1.59%
Return on average equity (%)	3.37%	4.02%	4.08%	5.00%	7.65%
Capital and risk protection					
Common equity tier 1 ratio (%, fully loaded)	NA	NA	NA	NA	NA
Common equity tier 1 ratio (%, transitional)	16.73%	17.05%	16.20%	18.65%	20.36%
Tier 1 capital ratio (%, transitional)	16.73%	17.05%	16.20%	18.65%	20.36%
Total capital ratio (%, transitional)	20.19%	20.32%	19.41%	21.54%	20.36%
Leverage ratio (%)	8.20%	8.60%	7.90%	8.70%	9.40%
Asset risk intensity (RWAs/ total assets, %)	50.71%	52.25%	51.54%	50.47%	47.95%
Market indicators					
Price/ book (x)	NA	NA	NA	NA	NA
Price/ tangible book (x)	NA	NA	NA	NA	NA
Dividend payout ratio (%)	NA	NA	NA	NA	NA

Source: SNL, Scope Ratings
Note: Reclassified financial information could differ from "as reported financials"

Lead Analysts

Covered bond
Mathias Pleißner, Frankfurt
+49 69 66 77 389-39
m.pleissner@scoperatings.com

Bank
Christian van Beek
+49 69 667 389-67
c.beek@scoperatings.com

Related research

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Governance support in Austria's new covered bond framework allows for six-notch uplift, June 2022

Applied methodologies

Covered Bond Rating Methodology, May 2023

Scope Ratings GmbH

Lennéstraße 5
D-10785 Berlin
scoperatings.com

Phone: +44 20 7824 5180
Fax: +49 30 27891-100
info@scoperatings.com

in
Bloomberg: RESP SCOP
Scope contacts

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