

Bausparkasse Wüstenrot AG

Austrian Mortgage-Covered Bonds – Performance Update



The AAA rating with a Stable Outlook assigned to the Austrian mortgage-covered bonds issued by Bausparkasse Wüstenrot AG (Wüstenrot) is based on sound issuer credit quality, enhanced by seven notches of cover pool support. Of that, five notches reflect our assessment of the strong governance support provided by the Austrian legal covered bond and resolution framework.

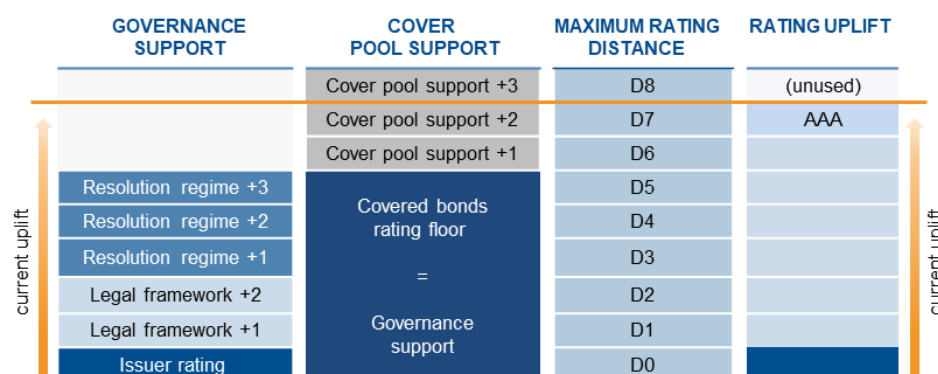
Cut-off date	Cover pool	Cover asset type	Covered bonds	Rating/Outlook
31 March 2023	EUR 1,632.9m	Residential mortgage loans	EUR 1,311.9m	AAA/Stable

Wüstenrot is the oldest and the only remaining independent building society in Austria. Together with its insurance subsidiary, Wüstenrot Versicherungs-AG, Wüstenrot forms a nationwide bancassurance franchise that is supported by distribution agreements with leading commercial banks, such as Bank Austria and BAWAG.

Governance support factors from the Austrian legal and resolution framework provide a five-notch uplift above the bank's rating, which effectively forms a rating floor.

We assign a cover pool complexity (CPC) category of 'Low' for the issuer's management of the interplay between complexity and the level of transparency provided to investors. This allows for a maximum additional uplift of three notches on top of the governance support uplift and enables the programme to be rated AAA, reflecting the credit strength of the covered bond programme.

The programme could further benefit from a one-notch buffer against an issuer downgrade as the maximum theoretical uplift constitutes eight notches, as opposed to the seven notches used to achieve the highest rating for these covered bonds.



Stable Outlook

Scope's Stable Outlook on the covered bonds reflects the outlook on the private issuer rating enhanced by a rating buffer of one notch from unused cover pool support.

Changes since the last performance update

Since our last analysis one year ago, the volume of covered bonds and assets increased by more than 25%. Further increases are likely as the bank's regulatory cap to issue covered bonds has been eased. Today the bank can issue up to 30% of covered bonds relative to its total assets. In addition, it has received a general banking licence, which will allow it to widen its product offering and attract customers that had previously not been in its target group. As a result, the programme could benefit from further asset and liability diversification.

Ratings & Outlook

Issuer rating	N/D*
Outlook	N/D*
Last rating action	N/D*
Last rating action date	N/D*
Covered bond rating	AAA
Outlook	Stable
Rating action	Affirmed
Last rating action date	10 May 2023

*N/D – Not disclosed; Scope has assigned a private, monitored issuer rating to the bank. The issuer has solicited the assigned rating and participated in the rating process.

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Related Research

Scope Ratings affirms at AAA/Stable the Austrian mortgage-covered bonds issued by Wüstenrot May 2023

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

Austrian lending limits will not ensure financial stability if interest rate-risk is excluded May 2022

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Bloomberg: SCOP

Only independent Bausparkasse in Austria

The issuer

We maintain and monitor a private issuer rating on Wüstenrot, the only independent building society in Austria. Wüstenrot is part of the Austrian Wüstenrot Group, which offers home financing, savings products, life and non-life insurance products (including health and mobility insurance) as well as investment products. As a building society, the bank focuses on long-term, tax-advantaged saving products and invests the funds in retail mortgages, which it 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. Wüstenrot does not have access to a larger capital- and liquidity-supporting group structure. Regarding the bank's capital-raising abilities, potential support from its majority owner is limited.

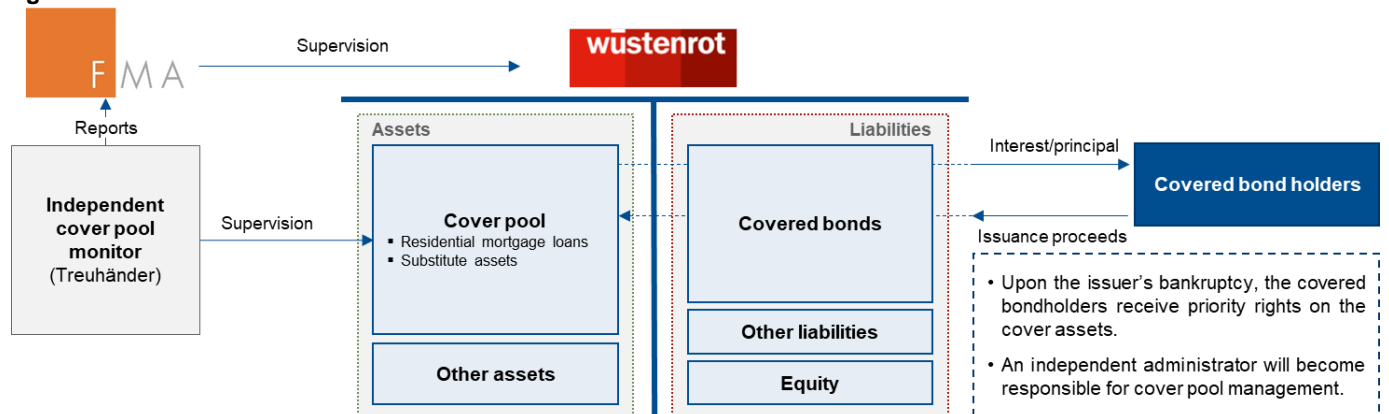
Wüstenrot received an Austrian banking licence in December 2022 and is now able to provide its own digital banking offerings for private customers, including current accounts and other savings and lending products. This strategic expansion offers potential and a more stable business model that could benefit the bank's credit profile and its covered bond programme, but also poses risks given the highly competitive market environment for online banks in Austria.

Programme structure

Wüstenrot issues covered bonds using an on-balance sheet structure. Its issuances are governed by the new Austrian Covered Bond Act (PfandBG) and supervised by Austria's Financial Market Authority (FMA).

On-balance sheet framework

Figure 1: Issuance structure



Source: Scope Ratings

Governance support analysis

Two notches of legal framework uplift...

We continue to assign the maximum legal framework uplift of two notches following our analysis of the Austrian covered bond framework. Updated legislation came into force on 8 July 2022 and transposed the European Covered Bond Directive into local law. The new framework consolidated and improved the three previous sets of legislation and aligned them more closely with best practices from other covered bond frameworks in Europe.

... plus three notches of resolution regime uplift

Wüstenrot's covered bonds benefit from an additional three-notch uplift that reflects their exemption from bail-in and 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; ii) the moderate systemic importance of covered bonds in Austria and the low visibility and importance of Wüstenrot as a covered bond issuer; and iii) increased market visibility and higher domestic stakeholder cohesiveness. Our latest assessment of relevant governance support factors for Austrian covered bonds is available [here](#).

Reporting date	March 2023	March 2022
Balance (EUR m)	1,632.9	1,301.4
Residential	97.9%	98.1%
Substitute	2.1%	1.9%

Reporting date	March 2023	March 2022
No. of loans	13,851	11,469
Avg. size (EUR '000s)	115.4	113.5
Top 10	0.4%	0.5%
Remaining life (y)	27.9	26.5
Seasoning (y)	4.1	3.5
WA whole-loan LTV	69.1%	70.6%
WA eligible-loan LTV	51.5%	51.8%

Reporting date	March 2023	March 2022
Houses	62.7%	62.6%
Flats	33.4%	33.3%
Multi-family houses	1.6%	1.5%
Other	2.3%	2.5%

Reporting date	March 2023	March 2022
Annuity	100%	100%
Interest-only	0.0%	0.0%

Reporting date	March 2023	March 2022
Fixed	75.8%	71.5%
Floating	24.2%	28.5%

Cover pool analysis

Wüstenrot's mortgage-covered bond ratings are cover pool-supported, with seven out of eight possible notches needed to support the highest credit quality. Governance support provides a five-notch rating uplift and, effectively, a floor against a deterioration in cover pool credit quality.

The minimum supporting OC needed to achieve the highest rating remains at 6.0%, reflecting a stable, high-quality cover pool, low interest rate risk and moderate asset-liability mismatches.

Cover pool composition

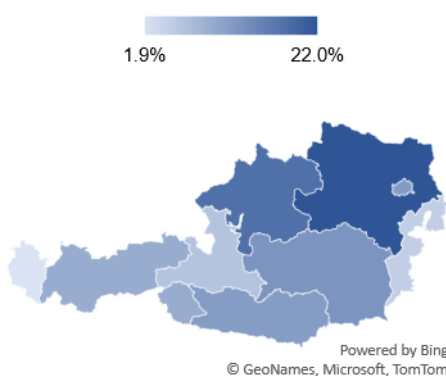
The cover pool comprises domestic commercial and well-distributed residential mortgage loans across Austria. The low and relatively stable weighted average loan-to-value (LTV) ratio of 51.5% (not indexed) on an eligible-loan basis and the whole-loan LTV ratio indicate strong protection against credit 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 new Austrian Covered Bond Act stipulates a maximum (eligible) LTV ratio of 80% for residential mortgage assets. We acknowledge, however, that mortgage loans are still limited to the eligible LTV ratio of 60% on a voluntary basis.

75.8% of the mortgage loans are fixed, which compares to 71.5% one year ago. However, these loans are not fixed for life. The average remaining time to interest reset stands at 11 years, which compares to an average time to final maturity of the mortgage loans of 25.3 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.

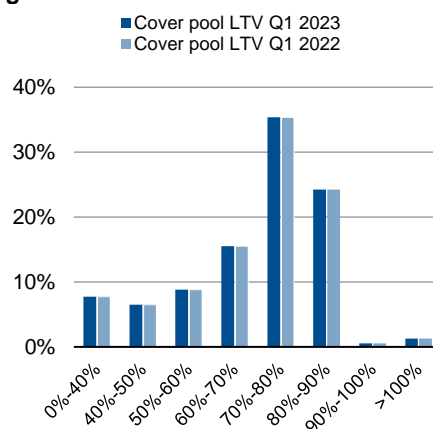
The pool has no large concentrations and is very granular, with an average loan size of around EUR 115,000. All loans are amortising.

Figure 2: Regional distribution



Source: Scope Ratings, Wüstenrot

Figure 3: Whole loan LTV distribution



Source: Scope Ratings, Wüstenrot

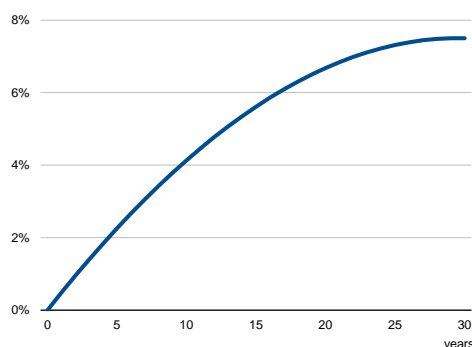
Asset risk analysis

In total, credit risk accounts for an unchanged 2 pp of the supporting OC. This is relatively low, reflecting the stable mean default rate of 7.5%, with a corresponding one-year PD of 48 bps, a coefficient of variation of 60%. The parameters for the default distribution were derived using the bank's loan-by-loan risk assessments.

High credit quality translates into minimal credit risk

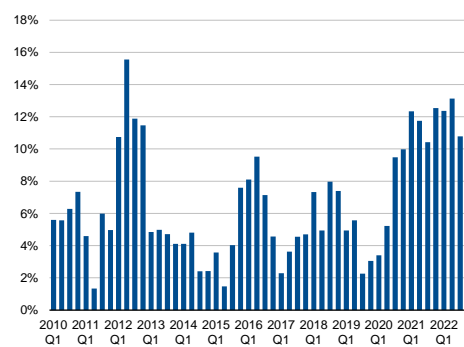
We further estimate an unchanged weighted average recovery rate of 100% under a base case scenario (D0) and 90% under the most stressful scenario (D8). Our recovery rate calculations reflect rating distance-dependent market value declines as well as assumptions regarding the Austrian housing market and its unique characteristics. Stressed security value haircuts range between 50.0% and 70.0% depending on the property's location.

Figure 4: Expected cum. term defaults



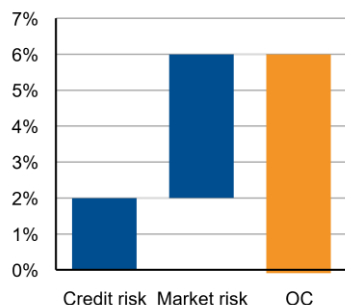
Source: Scope Ratings, Wüstenrot

Figure 5: Annual house price growth



Source: Scope Ratings, OeNB

Supporting OC breakdown



Source: Scope Ratings

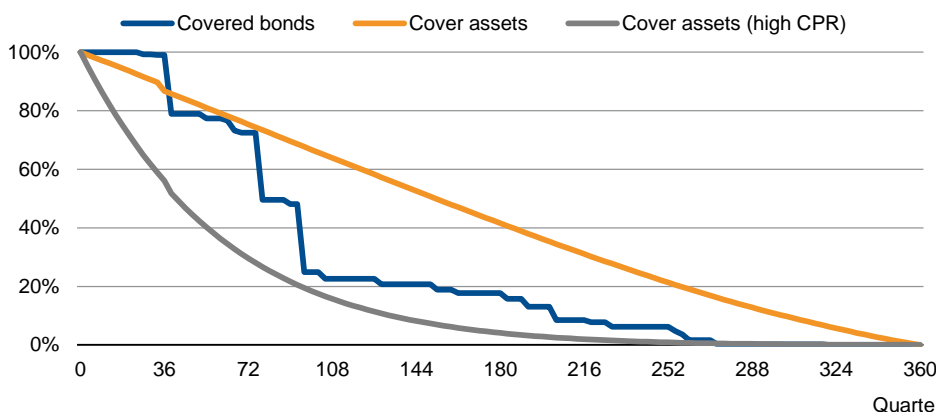
Cash flow risk analysis

The unchanged rating-supporting OC of 6.0% reflects the programme's sensitivity to high prepayments in combination with a stressed lower-for-longer interest rate scenario. Combined, these factors result in costs of carry for the programme. Consequently, market risks account for 4 pp of the 6.0% supporting OC.

As of Q1 2023 the weighted average life (WAL) of the outstanding covered bonds decreased to 8.6 years from 9.4 years. In a high prepayment (15%) scenario, the WAL of the assets falls to less than five years. This creates a gap between the cover assets and the covered bonds and triggers fire sales of mortgage loans under discount.

As is typical of Austrian mortgage-covered bonds, there is structural interest rate risk. Around 25.0% of the cover assets pay a variable rate, and most of the fixed-rate bonds will be reset before their final legal maturity, while 95.6% the covered bonds pay fixed rates for life.

Figure 6: Amortisation profile (relative)



Source: Scope Ratings, Wüstenrot

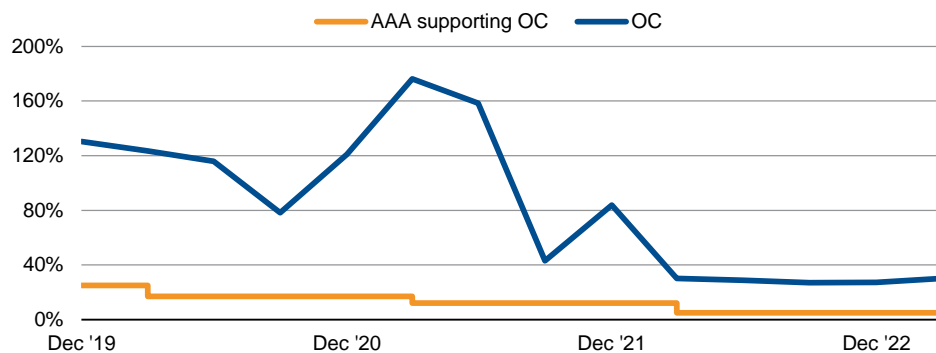
Asset-liability mismatches

	Assets	Liabilities
EUR	100%	100%
Fixed	75.8%	96.6%
Floating	24.2%	3.4%
Scope WAL (years)	13.4	8.6

Availability of overcollateralisation

Wüstenrot typically provides significantly higher levels of OC than 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.

Figure 7: Available OC versus rating-supporting level



Source: Scope Ratings, Wüstenrot

Governance factors remain key...

ESG risk

Governance considerations, such as the strength of supervision and prudent management, play a major role in our covered bond analysis, translating into our governance support uplift. In addition, our CPC category measures the issuer's management of the interplay between complexity and the level of transparency provided to investors. For Wüstenrot, this allows for the maximum additional cover pool support uplift of three notches on top of the fundamental uplift.

... but no impact from environmental and social aspects

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.

Counterparty risk mitigated by alignment of interests

Other risk considerations

The rated bonds are exposed to Wüstenrot's roles as originator, servicer, account provider 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.

Sovereign risk does not currently affect the ratings

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.

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

One-notch rating buffer to potential change in issuer rating

Sensitivity analysis

Wüstenrot's mortgage-covered bond ratings 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 rating-supporting OC to 7.0%.



Bausparkasse Wüstenrot AG

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Appendix II: Summary of covered bond characteristics

Reporting date	31 March 2023	31 March 2022
Issuer name	Bausparkasse Wüstenrot AG	
Country	Austria	
Covered bond name	Hypothekendarlehenbrief (Hypf) Austrian mortgage-covered bonds issued under the PfandG	
Covered bond legal framework	Austrian legal covered bond framework	
Cover pool type	Residential mortgages	
Composition	Residential = 97.9% Substitute assets = 2.1%	Residential = 98.1% Substitute assets = 1.9%
Issuer rating	N/D	
Current covered bond rating	AAA/Stable	
Covered bond maturity type	Hard bullets	
Cover pool currencies	EUR (100%)	
Covered bond currencies	EUR (100%)	
Governance support	5	
CPC category	Low	
Maximum achievable covered bond uplift	8	
Potential covered bond rating buffer	1	
Cover pool/eligible assets (EUR m)	1,891.3 / 1,598.7	
of which substitute assets and deposits (EUR bn)	34.2	
Covered bonds (EUR m)	1,311.9	
Overcollateralisation: current/legal minimum	22.5% / 2.0%	
Overcollateralisation to support current rating	6.0%	
Overcollateralisation upon a one-notch issuer downgrade	7.0%	
Weighted average life of assets	13.4	
Weighted average life of liabilities	8.6	
Number of loans	13,851	
Average loan size (EUR)	115.42	
Top 10 exposures	0.4%	
Interest rate type – assets (fixed/floating)	75.8%	
	24.2%	
Interest rate type – liabilities (fixed/floating)	96.6%	
	3.4%	
Weighted average whole-loan LTV (unindexed)	69.1%	
Weighted average eligible-loan LTV (unindexed)	51.5%	
Geographic split (top three)	Lower Austria (22.0%) Upper Austria (18.1%) Styria (13.1%)	Lower Austria (22.1%) Upper Austria (17.9%) Styria (12.7%)
Default measure	Inverse Gaussian	
Mean default rate	7.5%	
Coefficient of variation	60.0%	
Recovery assumption (D0 / Dmax)	100% / 90.0%	
Max. liquidity premium	150 bps	
Servicing fee	25 bps	

D0 and Dmax denote the stresses commensurate with the rating distance from the minimum and maximum achievable covered bond uplift.



Bausparkasse Wüstenrot AG

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