SSB Boligkreditt AS

Norwegian Covered Bonds – Performance Update

STABLE
AAA

Rating rationale (summary)

The AAA rating with a Stable Outlook assigned to the Norwegian mortgage-covered bonds issued by SSB Boligkreditt AS (SSBB) is based on the bank's A- issuer rating enhanced by six notches of cover pool support. Five notches of the support reflect our assessment of the strong governance support provided by the Norwegian legal covered bond and resolution framework.

Cut-off date	Cover pool	Cover asset type	Covered bonds	Rating/Outlook
31 Dec 2022	NOK 12.9bn	Residential mortgage loans	NOK 10.6bn	AAA/Stable

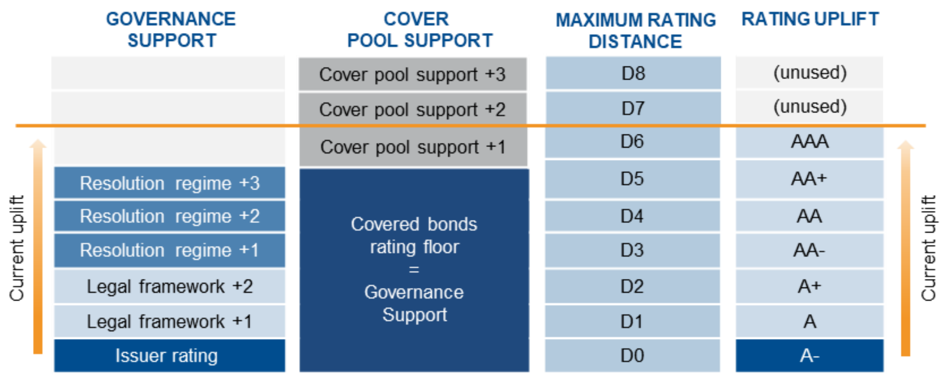
SSBB is a wholly owned, specialised credit institution dedicated to providing secured covered bond funding for its parent, Sandnes Sparebank. The issuer rating on SSBB reflects its full ownership by Sandnes (both banks rated A-/Stable) and the high likelihood of support from its parent in case of need.

Governance support factors from the Norwegian legal and resolution framework provide a 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 one notch of uplift reflecting the credit strength of the covered bond programme.

We have assigned the covered bonds a cover pool complexity (CPC) category of 'Low' for the interplay between the programme's complexity and transparency provided to investors. This allows for a maximum additional uplift of three notches on top of the governance 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 two-notch buffer against an issuer downgrade as the maximum theoretical uplift constitutes eight notches, as opposed to the six notches used to achieve the highest rating for these covered bonds.

Figure 1: Covered bond rating building blocks



Changes since the last performance update

Since December 2021, the cover pool as well as the outstanding covered bonds have further increased by around +25%. At the same time, the programme's overall credit metrices have remained largely unchanged. The programme's minimum supporting overcapitalisation (OC) has increased to 6.0%, from 4.0% previously. The increase in the supporting OC reflects our increased house price haircuts in southwestern Norway and lower margins provided by the low-risk residential mortgage assets.

Ratings & Outlook

Issuer rating	**A-**
Outlook	Stable
Last rating action	Affirmation
Last rating action date	22.03.2023
Covered bond	**AAA**
Outlook	Stable
Rating action	Affirmation
Last rating action date	18.04.2023

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Related Research

Scope affirms AAA rating on SSB Boligkreditt's Norwegian mortgage-covered bonds, Outlook Stable
April 2023

Scope affirms A- issuer rating of Sandnes Sparebank with Stable Outlook
March 2023

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Bloomberg: RESP SCOP

The issuer

SSBB's ratings reflect those of its parent bank, Sandnes. Founded in 1875, Sandnes is a local savings bank operating in the county of Rogaland in southwest Norway. The bank is the second largest savings bank in Rogaland, competing with SpareBank 1 SR-Bank, DNB, Danske Bank and others. Historically, Sandnes had a focus on corporate lending and real estate development. Over the last few years, however, management has successfully shifted the priority to retail customers. Having returned to its savings bank roots, Sandnes continues to develop and strengthen its business franchise.

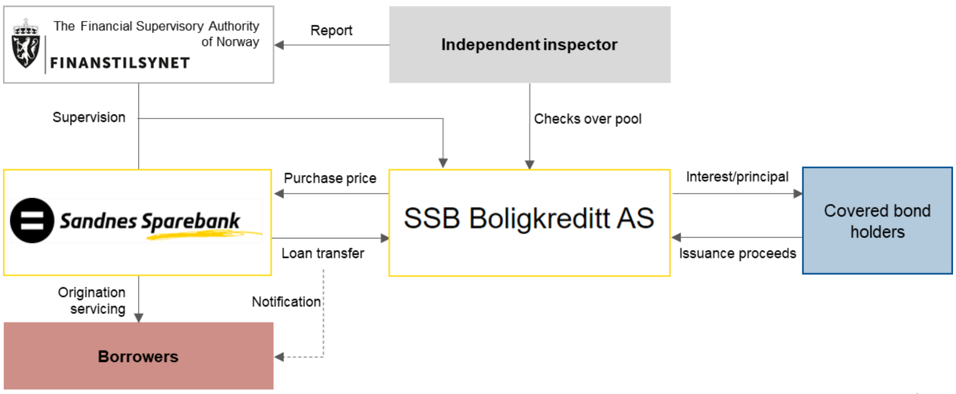
For further details on our bank credit analysis, see the full bank rating report available on www.scoperatings.com.

Programme structure

Specialised mortgage bank issuing covered bonds

The Norwegian legal covered bond framework is mainly based on the relevant section on covered bonds in the Financial Institutions Act together with a related regulation on mortgage credit institutions. The Act was amended to reflect the European 'Covered Bond Directive' and came into force 8 July 2022. Under this framework, issuance is permitted only through specialist covered bond issuers. Most issuers of covered bonds (called Boligkreditt, or specialised residential mortgage institutions) are subsidiaries that rely on loans originated by their respective parent banks. A Boligkreditt issues covered bonds whose proceeds are used to purchase mortgage assets from its parent bank(s).

Figure 2: Current issuance structure



Source: Scope Ratings

Governance credit support analysis

Governance credit support factors enhance the covered bond rating by five notches above SSBB's issuer rating. This reflects: i) Norway's covered bond legal framework; and ii) the resolution regime and systemic importance of SSB'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.

… plus three notches of resolution regime uplift

SSBB's covered bonds benefit from an additional three-notch uplift that reflects 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 SSBB as a covered bond issuer.

For more information on our view of the Norwegian resolution regime, please refer to Legal framework analysis: Norway.

SSB Boligkreditt AS
Norwegian Covered Bonds - Performance Update

Cover pool characteristics

Reporting date	Dec 2022	Dec 2021
Balance (NOK bn)	12.9	10.5
Residential (%)	91.9	93.2
Substitute (%)	8.1	6.8

Property type (%)

Reporting date	Dec 2022	Dec 2021
Single-family house	80.0	79.7
Apartment	20.0	20.3
Others	0.0	0.1

General information

Reporting date	Dec 2022	Dec 2021
No. of loans	7,010	6,144
No. of obligors	5,764	5,187
Avg. size (NOK m)	1.7	1.9
Top 10 (%)	0.9	0.8
WA maturity (y)	20.0	19.3
LTV (%)	51.1	52.0

Interest rate type (%)

Reporting date	Dec 2022	Dec 2021
Floating	100.0	100.0
Fixed	0.0	0.0

Repayment type (%)

Reporting date	Dec 2022	Dec 2021
Annuity	80.2	80.2
Interest-only	19.8	19.9

Cover pool analysis

SSBB's mortgage-covered bond ratings are cover pool-supported, with six out of eight possible notches currently needed to achieve the highest rating. Governance support provides for a five-notch rating uplift and, effectively, a 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' which allows for a maximum three notch uplift on top of the governance uplift.

The minimum supporting OC needed to achieve the highest rating was increased to 6.0%. This is supported by the sound credit metrics of the cover pool and low market risks. Market risks arise from maturity mismatches that are partly mitigated by the bonds' soft-bullet structure.

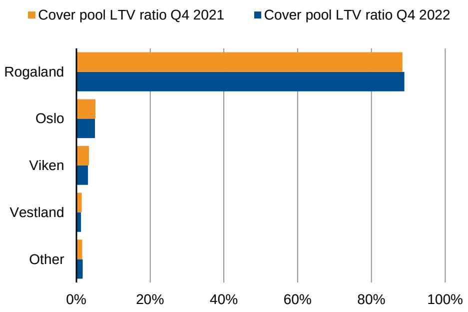
Cover pool composition

The cover pool is secured by Norwegian residential mortgage loans denominated in Norwegian kroner. The mortgage pool consists of 7,010 loans granted to 5,764 obligors with an average loan size of NOK 1.7m (around EUR 160,000). The 10 largest obligors only account for 0.9%.

Around 80% of the portfolio is made up of single-family houses and terraced houses, the remaining 20% are apartments.

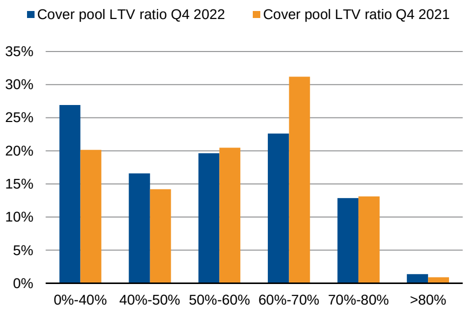
The bank operates primarily in the Stavanger region in southwestern Norway. Hence, as of December 2022, 89.0% of the mortgage loans are exposed to the region of Rogaland, 5.0% to Oslo and 3.1% to Viken. The remaining are spread across Norway.

Figure 3: Regional distribution



Source: Scope Ratings, SSBB

Figure 4: Loan-to-value distribution



Source: Scope Ratings, SSBB

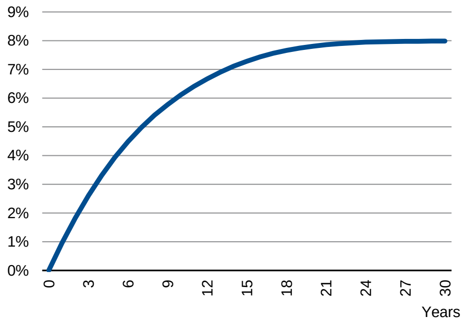
The weighted average LTV ratio of 51.1% (down from 52.0%) is based on the current outstanding balance. Flexible loans make up around 20% of the cover pool. These loans have an embedded credit line, which can be drawn on without new credit approval. Flexible loans will only be granted if the loan's LTV ratio does not exceed 60%.

Asset risk analysis

Strong credit quality translates into low credit risk

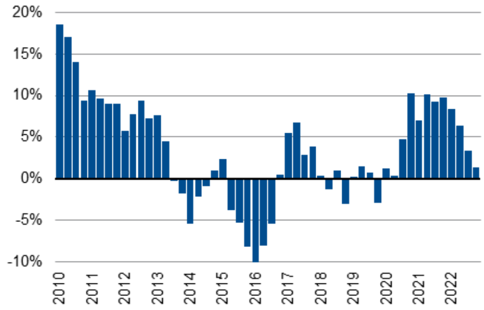
The cover pool's credit quality remains strong. We assume an unchanged annual average default probability of 41 bps. Our projection of default on mortgage loans uses an inverse Gaussian distribution, based on available credit performance data provided by the bank (in particular, historical delinquencies, portfolio loss rate) and benchmarking. The average borrower's PD is commensurate with a BB+ rating. This translates into an unchanged cumulative term default rate of 8.0%. We have further maintained our assumption of a coefficient of variation of 60% for the mortgage assets. This factors in the higher sensitivity to economic shocks in the western regions of Norway.

Figure 5: Expected term defaults, cumulative



Source: Scope Ratings, SSBB

Figure 6: House price growth Stavanger, annualised



Source: Scope Ratings, Statistics Norway

Stressed mortgage recovery rates worsened to 73.0%, down from around 80% assessed a year ago. This is driven by more conservatively estimated haircuts in the southwestern region of Norway reflecting property value growth above its sustainable level in the recent years. We further assume base market value haircuts of 10% across the country to account for imminent value corrections, bringing house prices back to more sustainable levels again.

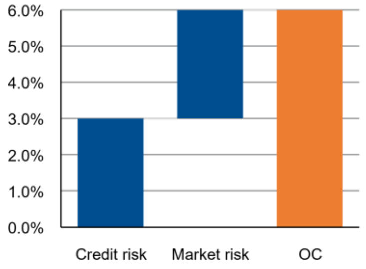
Our base recovery expectation remains strong at 98%. We keep the fire sale discount unchanged at 20%. The fire sale discount is applied to properties sold under non-standard market or distressed conditions. In our recovery analysis, we do further assume 2.5% in variable costs and NOK 70,000 in fixed costs.

Figure 7: Norwegian Security Value Haircuts (SVH)

Region	Base MVD	Stressed MVD	Fire sale Discount	Stressed SVH
Oslo	10%	55.0%	20%	65.0%
Southwestern	10%	42.5%	20%	55.0%
Rest of Norway	10%	42.5%	20%	55.0%

We analysed the substitute asset defaults with a non-parametric distribution using a Monte Carlo method. The applied correlation factor of up to 22% was based on the assets' regional exposure and type. We derived the default expectation based on individual credit assessments of the issuers. The low default rate of 0.1% and very high coefficient of variation reflect high individual credit quality but also very high obligor concentration. The asset recovery rate for the substitute asset assumptions ranged between 100% in the base case and 60% in the most stressed scenario.

Supporting OC breakdown

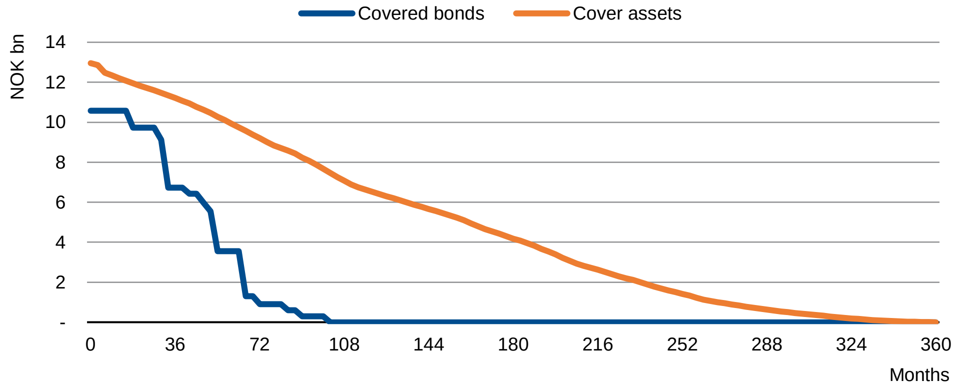


Source: Scope Ratings

Cash flow risk analysis

The rating-supporting OC of 6.0% equally reflects the programme's market risks, from asset-liability maturity mismatch risk accounting for 3.0 pp (up from 2 pp) and credit risk accounting for 3.0 pp (up from 2 pp). The programme has a sensitivity to low prepayments, which creates large liquidity gaps and accordingly the need for stressed assets sales under a discount.

Figure 8: Amortisation profile



Source: Scope Ratings, SSB

Asset-liability mismatches

	Assets	Liabilities
NOK	100%	100%
Fixed**	0.0%	0.0%
Floating**	100%	100%
WAL (years)	11.4	4.1*

*incl. one year extension **post hedging

As of Q4 2022, the weighted average life of the outstanding covered bonds is 4.1 years when accounting for their soft-bullet structure. In comparison the (scheduled) weighted average life of the cover pool of 11.4 years.

We further assume that assets will be sold at a discount of up to 150 bps if the cash accumulated from cover pool amortisation is insufficient to pay timely interest and principal on the covered bonds. The programme benefits from 8.1% of liquid substitute assets.

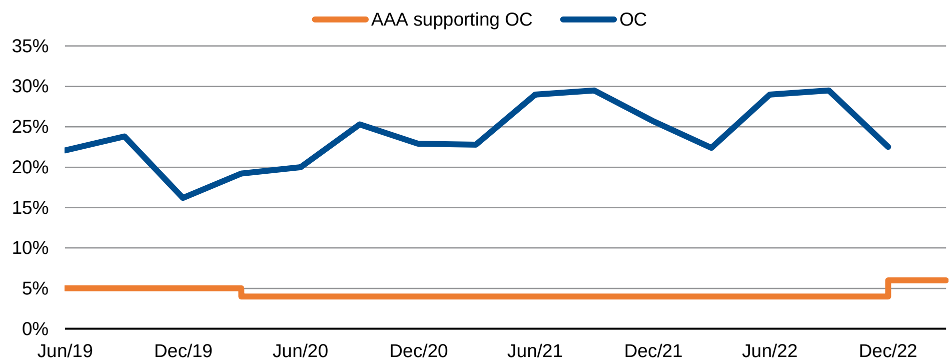
Other market risks are limited as cover assets have floating rates, and fixed covered bonds are hedged into floating rates. Also, there is no foreign exchange risk as both assets and liabilities are denominated in Norwegian krone. At this stage, we do not expect foreign currency-denominated issuances.

Availability of overcollateralisation

Overcollateralisation fully taken into account

The current rating of SSBB allows us to fully account for the provided OC of 22.5% which is above the level of overcollateralisation supporting the programme's AAA rating. We are not aware of plans that would significantly change the risk profile or reduce available OC to levels that would no longer support the current rating uplift.

Figure 9: Available overcollateralisation versus current rating-supporting level



Source: Scope Ratings, SSBB

Other risk considerations

Counterparty risk mitigated by alignment of interests

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 view positively the fact that collections are generally made via direct debit, allowing for a relatively swift redirection of payments if necessary.

The rated covered bonds are further exposed to counterparty exposure from hedging of fixed rate liabilities into floating rates. Those agreements are contracted with four different banks of which one is Sandnes. The corresponding documentations (CSA/ISDA schedules) are in line with our counterparty methodology.

Sovereign risk does not affect the ratings

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

Established green bond framework

SSBB is an active green bond issuer with NOK 300m in green bonds currently outstanding. According to its Green Bond Framework, the bank uses its green bond proceeds to finance and/or refinance, in part or in full, new and/or existing green eligible residential buildings.

As of December 2022, the sum of eligible cover assets in the cover pool accounts for NOK 2.8bn (around 22% of the mortgage cover pool) which provides strong headroom for additional green bond issuance.

So far, we see little evidence for a better credit performance by green mortgages. We therefore did not include information of environmental factors and their impact on the cover assets' probability of default or recovery proceeds. At the same time, we have indirectly included environmental aspects because collateral valuations reflect the age, condition and quality of the collateral.

Sensitivity analysis

Two-notch buffer against potential change in issuer rating

SSBB'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 result in a rating-supporting OC of 7.0%.

Summary of covered bond characteristics

Reporting date	31 Dec 2022	31 Dec 2021	31 March 2021
Issuer name	SSB Boligkreditt AS		
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 = 91.9%	Residential = 93.2%	Residential = 91.7%
	Substitute = 8.1%	Substitute = 6.8%	Substitute = 8.3%
Issuer rating	A-/Stable	A-/Stable	A-/Stable
Current covered bond rating	AAA/Stable	AAA/Stable	AAA/Stable
Covered bond maturity type	Soft bullet	Soft bullet	Soft bullet
Cover pool currencies	NOK (100%)	NOK (100%)	NOK (100%)
Covered bond currencies	NOK (100%)	NOK (100%)	NOK (100%)
Governance support	5	5	5
Maximum additional uplift from CPC category	3	3	3
Maximum achievable covered bond uplift	8	8	8
Potential covered bond rating buffer	2	2	2
Cover pool (NOK bn)	12.9	10.5	10.14
thereof, substitute assets (NOK bn)	1.0	0.7	0.8
Covered bonds (NOK bn)	10.6	8.36	8.26
Overcollateralisation: current / legal minimum	22.5% / 5%	25.7% / 2%	22.8% / 2%
Overcollateralisation to support current rating	5.0%	4.0%	4.0%
Overcollateralisation upon a one-notch issuer downgrade	6.0%	5.0%	5.0%
Weighted average life of assets	11.4 years	11.2 years	11.4 years
Weighted average life of liabilities [1]	4.1 years	4.2 years	4.8 years
Number of obligors	5,764	5,187	5,215
Average loan size (NOK m)	1.7	1.9	1.8
Top 10 residential	0.9%	0.8%	1.1%
Interest rate type – assets	Floating 100%	Floating 100%	Floating 100%
	Fixed 0%	Fixed 0%	Fixed 0%
Interest rate type – liabilities (hedged)	Floating 100%	Floating 100%	Floating 100%
	Fixed 0%	Fixed 0%	Fixed 0%
Weighted average LTV (indexed)	51.1%	52.0%	52.7%
Geographic split (top 3)	Rogaland = 89.0%	Rogaland = 88.4%	Rogaland = 89.6%
	Oslo = 5.0%	Oslo = 5.2%	Oslo = 3.7%
	Viken = 3.1%	Viken = 3.4%	Viken = 3.1%
Default measure	Inverse Gaussian/non-parametric	Inverse Gaussian/non-parametric	Inverse Gaussian/non-parametric
Weighted average default rate (mortgage/substitute)	41 bps / 8.0%	41 bps / 8.0%	42 bps / 8.0%
Weighted average coefficient of variation (mortgage/substitute)	60%	60%	60%
Weighted average recovery assumption (D0/D8)[2]	98.0% / 73.0%	99.1% / 79.8%	98.8% / 81.9%
Share of loans > three months in arrears (NPL)	0.0%	0.0%	0.0%
Interest rate stresses (max./min.; currency-dependent)	-1 to 10%	-1 to 10%	-1 to 10%
FX stresses (max./min.; currency-dependent)	n/a	n/a	n/a
Max liquidity premium	150 bps	150 bps	150 bps
Average servicing fee	24 bps	24 bps	24 bps

[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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