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Transaction Update: Oberoesterreichische Landesbank AG Mortgage Covered Bond Program

Hypotheken Pfandbriefe

Primary Credit Analyst:
Judit O Papp, Frankfurt + 49 693 399 9319; judit.papp@spglobal.com

Research Contributor:
Tushar Karmokar, CRISIL Global Analytical Center, an S&P affiliate, Mumbai

Table Of Contents

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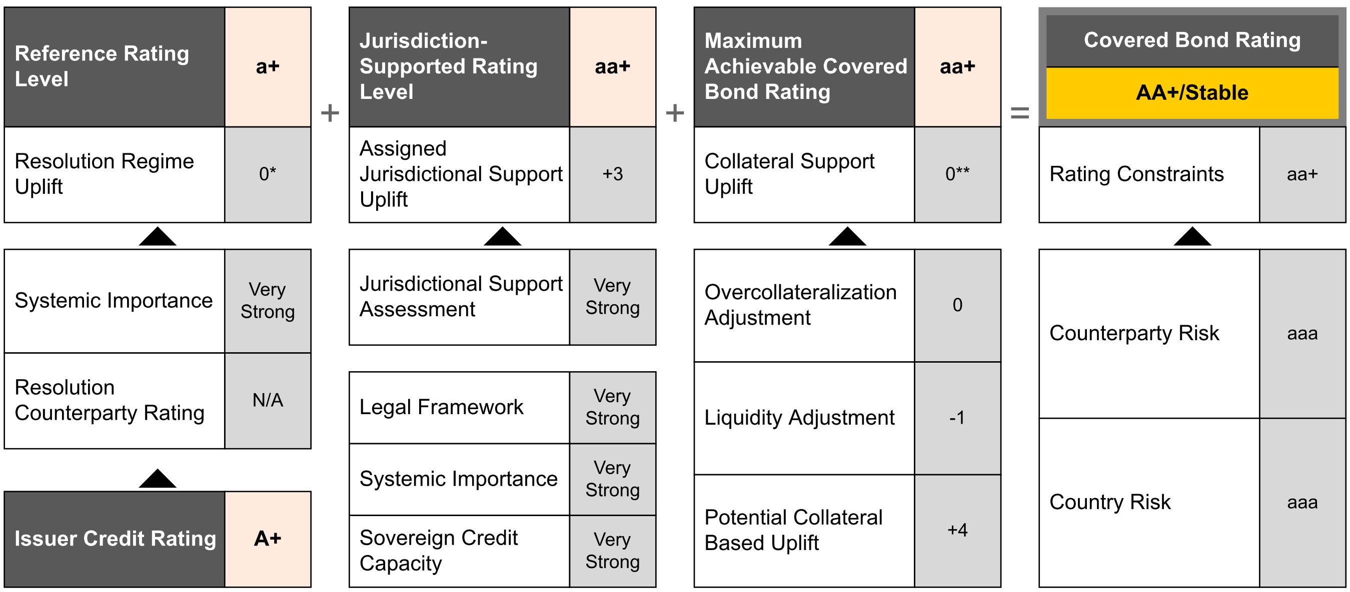
Ratings Detail



*We do not elevate the reference rating level above the issuing bank's issuer credit rating (ICR) because the expectation of external government support is already incorporated into the ICR. N/A--Not applicable.
** The program does not benefit from collateral-based uplift because there is no commitment to maintain sufficient overcollateralization in the program that would support a rating above the current 'aa+'

Major Rating Factors

Strengths

- Very strong jurisdictional support assessment for mortgages in Austria enables the program to reach a 'AA+' rating without any collateral support.
- The issuer's public commitment to the current rating supports a stable outlook on the rating with low overcollateralization requirement.

Weaknesses

- High asset concentration in the State of Upper Austria.
- The lack of loan-by-loan data reduces transparency in the collateral analysis.

Outlook: Stable

The stable outlook on the covered bonds ratings reflects the issuer's commitment to the current rating.

In the absence of any unused notches to the rating, the outlook on the covered bonds typically reflects the outlook on the issuer (Oberoesterreichische Landesbank AG, HYPO OOE, A+/Negative/A-1). However, the issuer has publicly committed to maintain the level of overcollateralization that is in line with the current 'AA+' rating level for the covered bonds. Therefore, the overcollateralization commitment supports the stable outlook on the program.

Rationale

We are publishing this transaction update as part of our periodic review of Hypo OOE's covered bond program and related issuances.

Our covered bond ratings process follows the methodology and assumptions outlined in our "Covered Bonds Criteria," published on Dec. 9, 2014, and "Covered Bond Ratings Framework: Methodology And Assumptions," published on June 30, 2015.

Our ratings reflect our reference rating level (RRL) of 'a+' and a jurisdiction-supported rating level (JRL) of 'aa+. The program does not benefit from collateral-based uplift because there is no commitment to maintain sufficient overcollateralization in the program that would support a rating above the current 'aa+'.

Under our resolution regime analysis, we determined an RRL of 'a+'. The issuer is domiciled in Austria, which is subject to the EU's Bank Recovery and Resolution Directive (BRRD). This fact and our very strong assessment of the systemic importance of mortgage covered bonds in Austria would generally enable the program to benefit from up to two notches of uplift above the issuer credit rating (ICR) on the issuer (see "Assessments For Jurisdictional Support According To Our Covered Bonds Criteria," published on Nov. 27, 2020). However, we typically do not elevate the RRL above the ICR on the issuing bank for issuers for which the expectation of external government support is incorporated into the ICR, as determined under our bank criteria. In particular, if an issuer is a government-related entity (GRE), the RRL is typically equal to the ICR.

We then consider the likelihood for the provision of jurisdictional support, which for mortgage programs in Austria we assess as very strong. This leads us to apply up to three notches of uplift from the RRL. The jurisdictional supported rating on the covered bonds cannot be higher than our long-term rating on the Austrian sovereign. As we rate Austria at 'AA+' the program can benefit from all three available notches of jurisdictional supported uplift. Therefore, we assess the jurisdiction-supported rating level (JRL) at 'aa+'.

We have reviewed the asset information provided as of June 30, 2021. The program's underlying assets comprise €2.019 billion of residential mortgage loans, €0.623 billion commercial mortgages, and €45 million substitute assets. The available credit enhancement of 38.03% in the program exceeds the target credit enhancement. However, the issuerś overcollateralization commitment extends to a rating no higher than 'AA+'. Therefore, in line with our covered bonds criteria, we do not assign any collateral based uplift (see "Related Criteria"). Consequently, the program does not benefit from any unused notches of uplift.

The ratings on the program and related issuances are currently not constrained by legal, operational, counterparty, or sovereign risks.

We have based our analysis on the criteria articles referenced in the "Related Criteria" section.

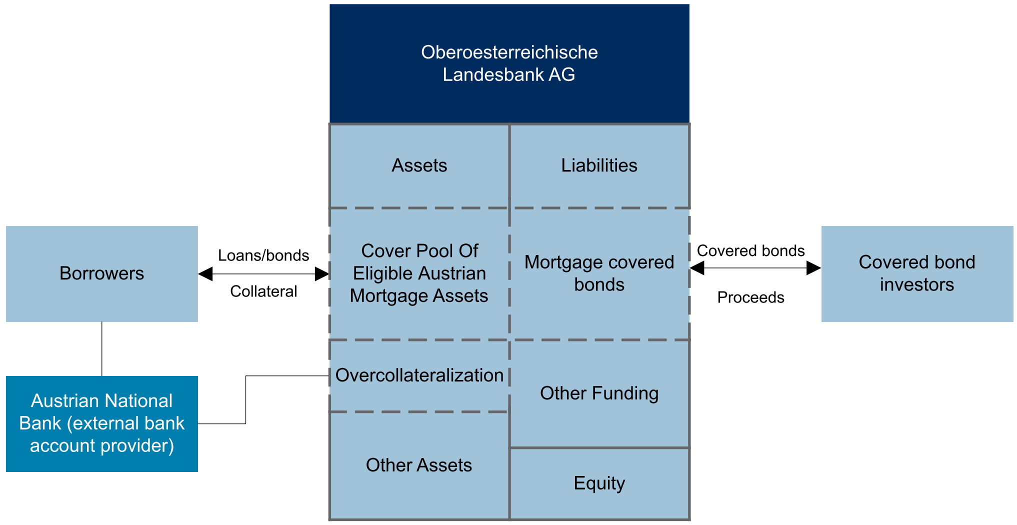
Program Description

Table 1

Program Overview*	
Jurisdiction	Austria
Year of first issuance	2016
Covered bond type	Legislation-enabled
Outstanding covered bonds (bil. €)	1.946
Redemption profile	Hard bullet
Underlying assets	Residential and commercial mortgages, substitute assets
Jurisdictional support uplift	3
Unused notches for jurisdictional support	0
Target credit enhancement (%)	24.74
Available credit enhancement (%)	38.03
Collateral support uplift	0
Unused notches for collateral support	0
Total unused notches	0

*Based on data as of June 30, 2021.

Oberoesterreichische Landesbank AG



HYPO OOE is a small commercial bank in Upper Austria with a strong focus on its home state. The bank carries out state-related banking services, with a dominant focus on niche segments in Upper Austria, mainly public-sector lending and related real estate financing, promotion of subsidized housing programs, and residential mortgages, as well as financing of medical services and corporations. In the area of subsidized housing, the bank has an exclusive partnership with Upper Austria. The bank's main shareholders are the State of Upper Austria (51%) and Raiffeisenlandesbank Oberoesterreich AG (41%).

We consider HYPO OOE to be a GRE with a high likelihood of receiving timely and sufficient extraordinary government support from the state of Upper Austria if needed.

The covered bonds constitute a senior secured unsubordinated obligation, rank pari passu with other obligations secured by the cover register, and are governed by the Austrian Covered Bond Act ("Pfandbriefgesetz"). All covered bonds are issued with a hard-bullet maturity.

Table 2

Program Participants

Role	Name	Rating	Rating dependency
Issuer	Oberösterreichische Landesbank AG	A+/ Negative/ A-1	Yes
Bank account provider	Austrian National Bank	NR	Yes
Servicer	Oberösterreichische Landesbank AG	A+/ Negative/ A-1	No
Originator	Oberösterreichische Landesbank AG	A+/ Negative/ A-1	No

Rating Analysis

Legal and regulatory risks

We base our legal analysis on our "Asset Isolation And Special-Purpose Entity Methodology," published on March 29, 2017, and our covered bond ratings framework.

The covered bonds are governed by the Austrian Mortgage Bond Act ("Pfandbriefgesetz"). Under the Act, the issuer is regulated and supervised by the Financial Market Authority (FMA). The covered bonds are secured by a separate pool of assets and the FMA appoints a trustee to monitor the management of the cover pool. The Mortgage Bond Act includes, among other provisions, a 2% minimum nominal overcollateralization, and a mandatory reporting requirement. The Act does not specify a minimum liquidity requirement that the issuer has to maintain.

On April 1, 2021, the Austrian government published a draft proposal to merge Austria's three covered bonds laws into one aligned with the EU harmonization directive. The expected key changes in the Austrian Pfandbriefgesetz relate to loan-to-value (LTV) requirements, increasing the minimum overcollateralization to 5%, the introduction of 180 days' liquidity coverage, joint funding, and rules for the extension of maturities (see "Austrian Covered Bonds Harmonization Proposal Merges Three Laws Into One," published on June 10, 2021). Most of these items affect Hypo OOE's covered bond program.

Austria has not enacted the harmonized EU legislation in July 2021 and therefore, is losing transition time before the next deadline in 2022 (see "Covered Bond Harmonization In The EU Remains A Work in Progress," published on July 13, 2021).

From our analysis, we have concluded that the cover pool assets are effectively isolated from the insolvency of the issuer for the benefit of the covered bondholders. Upon issuer insolvency, a cover pool administrator is appointed by a court to continue the management of the cover pool and to satisfy the claims of the covered bondholders. The protection of the assets and continued management of the cover pool allows us to assign a higher rating to the covered bond program than we would to the long-term ICR on the issuer.

Operational and administrative risks

Based on our regular contact with the issuer, we consider that the issuer actively manages the cover pool and has strict underwriting and loan management policies. The issuer has systems in place to ensure timely payment on outstanding covered bonds.

We also believe that there is a high likelihood that a replacement cover pool manager could be appointed if the issuer became unable to manage the program following its default. We consider the high likelihood of a replacement servicer as part of the cash-flow analysis based on the standardized characteristics of the assets and we model a stressed fee in order to reflect the need to incentivize a replacement servicer.

Our analysis of operational and administrative risk follows the principles laid out in our covered bond ratings framework (see "Related Criteria").

Resolution regime analysis

Our analysis considers any resolution regime in place in Austria to determine the RRL. The RRL on the issuer, which is the starting point for any further uplift in our analysis, is 'a+'.

The issuer is domiciled in Austria, which is subject to the EU's Bank Recovery and Resolution Directive (BRRD). Resolution regimes like the BRRD increase the probability that an issuer could service its covered bonds even following a default on its senior unsecured obligations because the law exempts covered bonds from bail-in risk if there is a bank resolution. We consider this as an internal form of support because the bail-in of certain creditors of the issuer does not require direct government support. Additionally, our assessment of the systemic importance for Austrian mortgage covered bonds programs is very strong.

Based on these two facts we would typically add two notches of resolution support to the issuer credit rating. However, we view Hypo OOE as a GRE and incorporate potential sovereign support in the ICR. Therefore, the resulting RRL equals the ICR ('A+').

Jurisdictional support analysis

In our jurisdictional support analysis, we assess the likelihood that a covered bond program facing stress would receive support from a government-sponsored initiative instead of from the liquidation of collateral assets in the open market. Based on a very strong jurisdictional support assessment for mortgage programs in Austria, we assigned three notches of uplift from the RRL and assess the JRL as 'aa+'. The program does not benefit from any unused notches of jurisdictional support uplift.

Collateral support analysis

In addition to residential (75%), and commercial mortgage assets (23%), the cover pool includes a small share of substitute assets (2%).

Since our previous review, we have updated our criteria for the assessment of pools of Austrian residential mortgage loans. We have based our updated analysis on the specific adjustments defined for Austria under our global residential loans criteria, effective for Austria since January 8, 2021. We continue to base our analysis of commercial assets on our covered bonds CRE criteria and the analysis of the substitute assets on our public sector criteria (see "Related Criteria").

We base our analysis on the stratified mortgage data provided by the issuer as of June 30, 2021. We have transferred the data to the loan level format, under conservative assumptions (e.g. for loan-to-value [LTV] ratios provided under a bucket, we assumed the LTV at the highest level of the bucket) and following an LTV distribution that is representative for the issuer's portfolio, in order to assess the credit analysis via our loan level model.

Most of the residential assets are owner-occupied properties, the commercial assets are split between loans on multifamily homes (58%) and ownership associations (42%). The latter are cooperative housing with the ultimate collateral being for residential purposes.

Most of the mortgage assets show a form of interest subsidy from the regional state and due to the government involvement, which results in a low margin. We do not currently give any benefit to the interest subvention specified above, which exists only if the interest rises above a pre-specified level. In the current low interest environment, there is limited to no benefit for the cover pool, and in cases where there is a subvention in place the borrowers remain ultimately liable for the full interest payments on their loans. Additionally, we do not have a stronger credit performance history available compared to standard mortgage assets without this additional feature.

Credit analysis

The lower weighted-average foreclosure frequency (WAFF, currently 10.26% vs 14.15% in the previous pool-cut) is mainly due to the lower default rate on the residential portfolio.

For the residential portion of the cover pool, our WAFF and WALS results are 5.59% and 3.91%, respectively. The main factor leading to the decrease in the residential WAFF from 10.90% in the previous analysis, is the adjustment due to regional concentration. The cover pool's exposure to Upper Austria is very high at 97% and it exceeds our 35.0% concentration limit for that region. Therefore, under our global residential loans criteria we increase the base foreclosure frequency on the excess exposure by 1.2x. Our previous methodology applied a lower adjustment factor (1.1x) on the entire exposure within the region exceeding the concentration limit. The overall effect of the updated adjustment in Hypo OOE's cover pool is positive. Further positive impact came from basing the expected defaults on the weighted-average effective LTV ratio (calculated weighting 80% of the original LTV and 20% of the current LTV) instead of the weighted-average original LTV used previously.

The lower WALS (3.91% vs 4.52% previously) on the residential subpool is mainly due to the lower current LTV ratios.

The WAFF on the commercial assets remained fairly stable (25.42% vs 25.22%) while the WALS increased to 31.15% from 26.50% previously, mainly due to higher current LTV ratios in this segment.

The overall WAFF and WALS figures in Hypo OOE's cover pool are below the average figures that we calculate for the Austrian programs that we rate (20.79% and 29.67%, respectively).

The below tables provide an overview of the program's key characteristics.

Table 3

Cover Pool Composition

	As of June 30, 2021		As of June 30, 2020	
Asset type	**Value (mil.€)**	**Percentage of cover pool**	**Value (mil.€)**	**Percentage of cover pool**
Residential mortgages	2,018,836,774	75.15	2,098,963,937	76.69
Commercial mortgages	622,737,461	23.18	593,046,279	21.67
Substitute assets	45,000,000	1.67	45,000,000	1.64
Total	2,686,574,235	100	2,737,010,216	100

Table 4

Key Credit Metrics

	As of June 30, 2021	As of June 30, 2020
	Percentage of cover pool	
Residential mortgages		
Weighted-average original LTV ratio (%)	66.30	59.90
Weighted-average current LTV ratio (%)	28.48	35.09

Table 4

Key Credit Metrics (cont.)		
Weighted-average effective LTV ratio (%)	58.71	N/A
Weighted-average loan seasoning (months)	114.54	106.24
Balance of loans in arrears (%)	0.10	**0.38**
Buy-to-let loans (%)	3.40	3.77
Commercial mortgages		
Weighted-average whole-loan LTV ratio (%)	40.63	38.38
Weighted-average cover pool LTV ratio (%)	39.62	38.38
Credit analysis results		
Weighted-average foreclosure frequency (WAFF; %)	10.26	14.15
Weighted-average loss severity (WALS; %)	10.33	9.51
'AAA' credit risk (%)	17.98 22.45	
LTV--Loan to value. Seasoning refers to the elapsed loan term.		

Table 5

Cover Pool Assets By Loan Size		
	As of June 30, 2021	**As of June 30, 2020**
(€ '000s)	**Percentage of mortgage cover pool balance**	
0-500	84.39	86.39
500-1,000	5.66	5.59
1,000-2,500	5.51	4.77
2,500-5,000	1.67	1.13
5,000-10,000	1.67	1.00
Greater than 10,000	1.10	1.12

Table 6

Loan Seasoning Distribution*		
	As of June 30, 2021	**As of June 30, 2020**
	Percentage of portfolio	
Less than 18 months	6.08	5.84
18-60	26.55	25.55
More than 60	67.37	68.61
Weighted-average loan seasoning (months)*	114.54	106.24

*Seasoning refers to borrower's relationship term, as loans are often refinanced.

Table 7

Geographic Distribution Of Loan Assets		
	As of June 30, 2020	**As of June 30, 2020**
	'Percentage of portfolio	
Burgenland	0.16	0.14
Carinthia (Kaernten)	0.03	0.03
Lower Austria (Niederoesterreich)	2.14	1.53
Upper Austria (Oberoesterreich)	90.08	92.33

Table 7

Geographic Distribution Of Loan Assets (cont.)		
	As of June 30, 2020	**As of June 30, 2020**
Salzburg	0.56	0.19
Styria (Steiermark)	3.37	2.42
Tyrol (Tirol)	0.17	0.14
Vorarlberg	0.01	0.01
Vienna (Wien)	1.81	1.58

Table 8

Collateral Uplift Metrics		
	As of June 30, 2021	**As of June 30, 2020**
Asset WAM (years)	8.65	8.65
Liability WAM (years)	7.32	8.19
Available credit enhancement	38.03	37
'AAA' credit risk	17.98	22.45
Required credit enhancement for first notch of collateral uplift (%)	19.67	23.86
Required credit enhancement for second notch of collateral uplift (%)	21.36	25.27
Required credit enhancement for third notch of collateral uplift (%)	23.05	26.68
Target credit enhancement for maximum uplift (%)	24.74	28.09
Potential collateral-based uplift (notches)	4	4
Adjustment for liquidity (Y/N)	N	N
Adjustment for committed overcollateralization (Y/N)	Y	Y
Collateral support uplift (notches)	0	0

WAM--Weighted-average maturity.

Cash flow analysis

Our analysis of the covered bonds' payment structure shows that the cash flows from the cover pool assets would be sufficient, at the given rating level, to make timely payment of interest and ultimate payment of principal on the legal final maturity.

The asset-liability mismatch is relatively low in the program and the target credit enhancement for the maximum potential rating ('AAA') is dominated by various credit risks (default risk and interest rate risk). As there are no commitments for liquidity coverage we deduct one notch from the available four notches of collateral-based uplift.

The program commits to hold sufficient overcollateralization to maintain the current 'AA+' rating, which it can achieve with jurisdictional support only and without any collateral above the legal minimum (2% nominal overcollateralization). Therefore, we give no benefit to the available overcollateralization in excess of the 2% in our collateral analysis. The program therefore does not benefit from any unused notches of collateral based uplift.

Counterparty risk

The ratings on the program and related issuances are not constrained by counterparty risks. Cover pool related inflows enter dedicated accounts with Austrian National Bank, the only account provider for the program. In the absence of a replacement framework, the ratings on the covered bonds are weak-linked to the creditworthiness of the account bank.

There are no derivatives registered in the cover pool.

We analyzed the counterparty risks according to our current counterparty criteria (see "Counterparty Risk Framework: Methodology And Assumptions," published on March 8, 2019).

Sovereign risk

Under our structured finance sovereign risk criteria, covered bonds issued in a jurisdiction that is within a monetary union and do not include structural coverage of refinancing need over a 12-month period exhibit moderate sensitivity to country risk. As a result, we can rate these covered bonds up to four notches above the sovereign rating (see Incorporating Sovereign Risk In Rating Structured Finance Securities: Methodology And Assumptions," published Jan. 30, 2019). Given our 'AA+' long-term rating on Austria, country risk does not constrain our rating on the covered bonds.

Environmental, social, and governance factors

Our rating on Hypo OOE's mortgage covered bonds do not incorporate any collateral-based uplift. Consequently, we consider that environmental and social credit factors have a neutral effect on the analysis of Hypo OOE's cover pool. The social angle of the bank's market leadership in Upper Austria's cooperative housing development, its support for first-time buyers, and the low LTV ratios in the residential loan portfolio are potential credit positive factors. The program is governed by the Austrian covered bond law ("Pfandbriefgesetz"), a legal framework that lacks liquidity provisions. We generally adjust the maximum achievable uplift for covered bonds issued under this framework due to the absence of liquidity provision. This factor does not affect Hypo OOE's covered bonds because the program does not make use of any collateral-based uplift. Hypo OOE is committed to maintain overcollateralization in the program that is commensurate with the current rating. We reflect this commitment in the stable outlook on the current rating.

Related Criteria

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- Global Framework For Payment Structure And Cash Flow Analysis Of Structured Finance Securities, Dec. 22, 2020
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- Principles Of Credit Ratings, Feb. 16, 2011

Related Research

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- Covered Bond Harmonization In The EU Remains A Work in Progress, July 13, 2021
- Austrian Covered Bonds Harmonization Proposal Merges Three Laws Into One, June 10, 2021
- Oberoesterreichische Landesbank AG 'A+/A-1' Ratings Affirmed; Outlook Remains Negative, Nov. 24. 2020
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- Assessments For Target Asset Spreads According To Our Covered Bonds Criteria, Nov. 27, 2020
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- S&P Global Ratings' Covered Bonds Primer, June 20, 2019
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