Totens Sparebank Boligkreditt

Norwegian Mortgage-Covered Bonds – Performance Update

Rating rationale (summary)

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

Cut-off date	Cover pool	Cover asset type	Covered bonds	Rating/Outlook
31 Mar 2023	NOK 4.95bn	Residential mortgage loans	NOK 4.28bn	AAA/Stable

Cover pool support is the primary rating driver. Together with the programme's governance support, it provides up to eight notches of uplift above the issuer rating. Only six notches are needed to raise the covered bond ratings to the highest achievable level.

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 three notches on top of the governance support uplift. Together, the programme benefits from a two-notch buffer against an issuer downgrade.

Governance support provides the covered bonds with five notches of uplift above the issuer rating. As such, only one additional notch from the cover pool support is needed to raise the covered bonds' ratings to the highest achievable level.

GOVERNANCE SUPPORT	COVER POOL SUPPORT	MAXIMUM RATING DISTANCE	RATING UPLIFT
	Cover pool support +3	D8	(unused)
	Cover pool support +2	D7	(unused)
	Cover pool support +1	D6	AAA
Resolution regime +3	Covered Bond Rating Floor = Governance Support	D5	AA+
Resolution regime +2		D4	AA
Resolution regime +1		D3	AA-
Legal framework +2		D2	A+
Legal framework +1		D1	A
Issuer rating		D0	A-

Stable Outlook

The Stable Outlook on the covered bonds reflects the rating buffer provided by our governance and cover pool support analyses, which shield the covered bond ratings from a multi-notch issuer rating deterioration.

Changes since the last performance update

Since June 2022, the cover pool has decreased by 7% to NOK 4.95bn, reflecting reduced lending due to the rising interest rates. The indexed loan-to-value ratio (LTV) increased moderately to 52.9% (from 52.0%). The geographic distribution remains stable. Excess spread available to the programme has decreased, reflecting decreased loan margins and higher funding costs.

Ratings & Outlook

Covered bond rating	**AAA**
Outlook	Stable
Rating action	Affirmation
Last rating action date	5 Sep 2023
Issuer rating	**A-**
Outlook	Stable
Last rating action	Affirmation
Last rating action date	21 Aug 2023

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Related Research

Scope affirms Totens Sparebank Boligkreditt's mortgage covered bonds at AAA/Stable, September 2023

Scope affirms Toten Sparebank's issuer rating of A- with Stable Outlook, August 2023

Legal framework analysis: Norway, September 2022

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The issuer

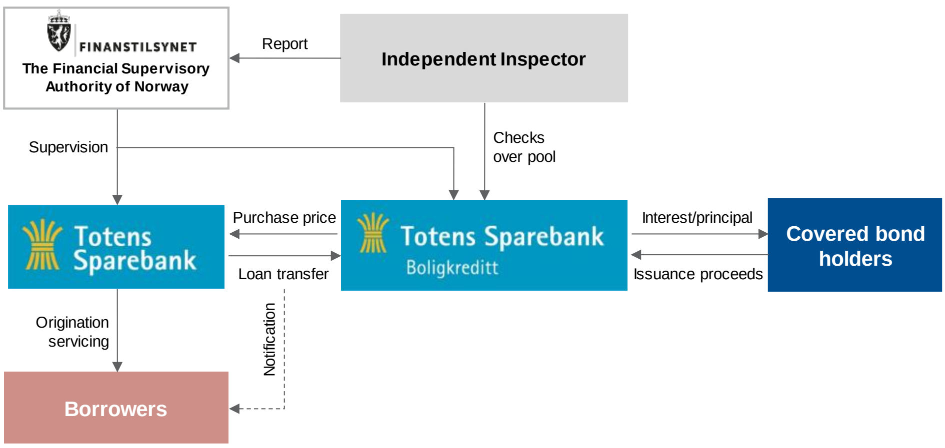
The A-/Stable issuer rating for Totens Sparebank (TSB) also applies to its wholly owned subsidiary TSBB. TSBB provides secured funding for its parent through the issuance of covered bonds. Established in 1854, TSB is a savings bank with a strong market position in south-eastern Norway. The A- issuer rating reflects that TSB enjoys a strong market position within its home market in the Mjos region of Norway. The savings bank primarily focuses on retail mortgage lending in its local region, supplemented with some lending to smaller corporates. TSB's competitive position is strengthened by its membership in the Eika Alliance, the fourth largest financial group in the country. For further details on our bank credit analysis, see the full bank rating report available on www.scoperatings.com.

Programme structure

The Norwegian legal covered bond framework is mainly based on the relevant section on covered bonds in the country's Financial Institutions Act (Lov om finansforetak og finanskonsern) and related regulation on mortgage credit institutions, both introduced in 2007. The act was last amended to transpose the European Covered Bond Directive, effective since 8 July 2022 in parallel with the application date in the EU. The act itself provides the general structure of the main framework and references the regulations of Norway's ministry of finance. As such, the Norwegian regulation on capital requirements and the national adaptation of CRR/CRD IV[1] provide further details on the requirements for Norwegian covered bonds and issuers.

Under this framework, issuance is permitted through specialist covered bond issuers. Like TSBB, most issuers of covered bonds (generally called Boligkreditt, or specialised residential mortgage institutions) are subsidiaries that rely on loans originated by their respective parent banks. The parent banks generally also provide most of the services for these subsidiaries, allowing the latter to keep staff numbers low.

Issuance structure



Source: Scope Ratings

[1] Forskrift om endring av forskrift 22. august 2014 nr. 1097 om kapitalkrav og nasjonal tilpasning av CRR/CRD IV (CRR/CRD IV-forskriften) og forskrift 9. desember 2016 nr. 1502 om finansforetak og finanskonsern (finansforetaksforskriften)

Governance credit support analysis

The Norwegian covered bond framework relevant for TSBB's mortgage-covered bonds combined with our positive view on the resolution regime provides the covered bonds with a governance-supported credit differentiation of five notches above the issuer's rating.

Legal framework analysis

Two notches of uplift based on legal framework analysis

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

The relevant legal framework (the act) was amended to transpose the European Covered Bond Directive and came into force on 8 July 2022 in parallel with the EU's application date. The act provides the general structure of the main framework and references the regulations of Norway's ministry of finance. The Norwegian regulation on capital requirements and the national adaptation of CRR/CRD IV provide further details on the requirements for Norwegian covered bonds and issuers.

Our analysis of the Norway's covered bond framework meets the criteria for assign the maximum credit differentiation under our methodology. Specifically, its provisions ensure that: i) the cover pool is segregated from the issuer's insolvency estate; ii) bond payments continue after insolvency; and iii) identified risks can be mitigated by overcollateralisation, which generally remains available after insolvency. Norwegian covered bonds also benefit from specific regulatory oversight (also see the related research listed on the first page).

Resolution regime analysis

Three notches of additional uplift reflecting resolution regime

TSBB'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 TSBB as a covered bond issuer.

The current capital structure would allow regulators to restructure TSB, including its mortgage subsidiary TSBB, using available resolution tools should the need arise. However, the most likely scenario is a transfer or take-over of TSBB by another bank. An orderly winddown is also plausible. As a result, investors might not benefit from the issuer being maintained as a going concern.

In our point of view, TSBB's covered bond issuing activities and market share only result in a low to moderate systemic importance. The bank only issues domestically, which should reduce negative repercussions on other issuers in the event of a failure. However, TSBB's low to moderate systemic importance also reflects the fact that most of the 23 Norwegian covered bond issuers are similarly subsidiaries of small to midsize banks. Even a failure of a covered bond issuer with the size and setup of TSBB could thus result in contagion, effectively creating systemic problems for other issuers reliant on this refinancing channel for their core product, residential mortgage lending.

For a more comprehensive assessment of the governance support factors relevant for Norwegian covered bonds, see our related research.

Pool characteristics

Reporting date	Mar 2023	June 2022
Balance (NOK bn)	4.95	5.35
Residential (%)	91.4	92.9
Substitute (%)	8.6	7.1

Property type (%)

Reporting date	Mar 2023	June 2022
Single-family houses	71.60	70.9
Apartments	12.92	13.7
Shares*	7.82	8.2
Holiday homes	4.01	3.7
Others	3.64	3.5

*Shares in housing associations

General information

Reporting date	Mar 2023	June 2022
No. of loans	2,549	2,865
Avg. loan size (NOK m)	1.71	1.7
Top 10 (%)	2.0	1.8
LTV (%)*	52.9	52.0

*Indexed

Interest rate type (%)

Reporting date	Mar 2023	June 2022
Floating	100	100
Fixed	0.0	0.0

Repayment type (%)

Reporting date	Mar 2023	June 2022
Bullet	7.6	6.8
Amortising	92.4	93.2

Cover pool analysis

TSBB's mortgage-covered bond ratings are cover pool-supported. Six of the up-to eight notches of uplift are used to support 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', which allows for the maximum three-notch uplift on top of the governance support uplift.

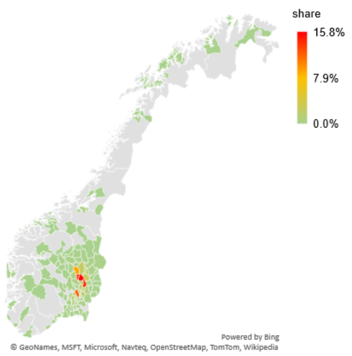
The minimum supporting overcollateralisation needed to achieve the highest rating is 5%, which is the Norwegian legal minimum. Cover pool support is supported by the sound credit metrics of the cover pool and the low market risks. Market risks arise from maturity mismatches, which are partly mitigated by the bonds' soft-bullet structure.

Cover pool composition

The cover pool is predominantly secured by Norwegian residential mortgage loans denominated in Norwegian krone. The cover pool also comprises substitute assets, mainly other highly rated Norwegian covered bonds. The cover pool composition broadly mirrors the area the bank operates in the Mjos region in south-eastern Norway, comprising Innlandet (51.9%), Viken (34.7%), and Oslo (10.0%).

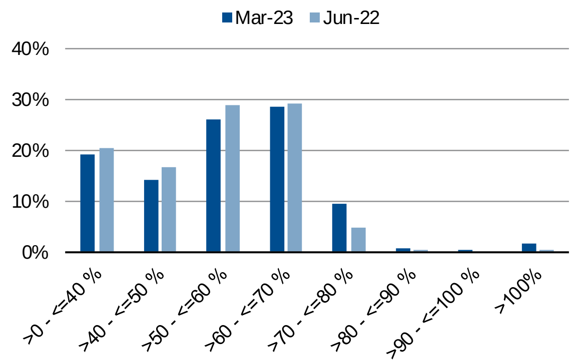
The mortgage pool consists of 2,651 loans granted to 2,549 obligors with an average loan size of NOK 1.7m. The 10 largest obligors account for 2.0%. Granularity has slightly fallen since our last review, also reflecting the mortgage portfolio's decline by 7%.

Figure 1: Regional distribution



Source: Scope Ratings, TSBB

Figure 2: LTV distribution (indexed)



Source: Scope Ratings, TSBB

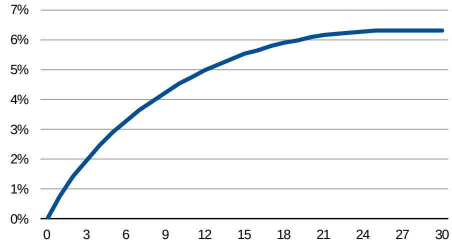
Most of TSBB's cover pool continues to be backed by mortgage loans granted to residential borrowers secured by single-family houses (71.6%), followed by apartments and shares in housing associations. The indexed LTV is 52.9%, up 0.9pp since our last review.

Asset risk analysis

Strong credit quality translates into low credit risk

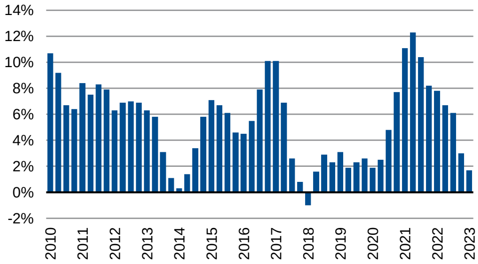
The cover pool's credit quality remains strong. Our projection of default on mortgage loans uses an inverse Gaussian distribution, based on available credit performance data provided by the bank (in particular, historical delinquencies, portfolio loss rate) and benchmarking. The average borrower probability of default is commensurate with a bbb- credit quality. This translates into a cumulative term default rate of 6.3%, which compares to last year's 6.0%. We have maintained our assumption of a 50% coefficient of variation for the mortgage assets.

Figure 3: Expected term defaults, cumulative



Source: Scope Ratings, TSBB

Figure 4: House price growth Norway, annualised



Source: Scope Ratings, statOECD

Stressed mortgage recovery rates[2] improved to 75.5% from 71.4% in the previous analysis. Lower stressed market value declines have helped to increase recovery rates, with overvaluations lower than in the previous year. Our stressed market value haircuts (MVD) dropped by 7.5% for the wider Oslo region and 2.5% for the rest of Norway but increased slightly in the country's south-west.

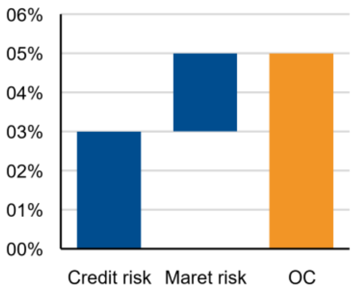
Figure 5: Norwegian security value haircuts (SVH)

Region	Base MVD	Stressed MVD	Firesale discount	Stressed SVH
Oslo	5%	47.5%	20%	57.5%
South-western	5%	40.0%	20%	52.5%
Rest of Norway	5%	40.0%	20%	52.5%

Our base recovery expectation remains very strong at 99.6%. We continue to assume a base market value decline of 5%, reflecting our expectation of a continued moderate fall in house prices due to declining demand in the region. We have also kept the fire-sale discount at 20%. The fire-sale discount is applied to properties sold under non-standard market or distressed conditions. Our recovery analysis also includes 2.5% of variable costs and NOK 70,000 of fixed costs.

Due to the low number of substitute assets (effective number lower than five), we considered the sub-pool as a single exposure to a financial institution rated A- combined with a typical three-year maturity and a 50% stressed recovery rate.

Supporting overcollateralisation breakdown



Source: Scope Ratings

Cash flow risk analysis

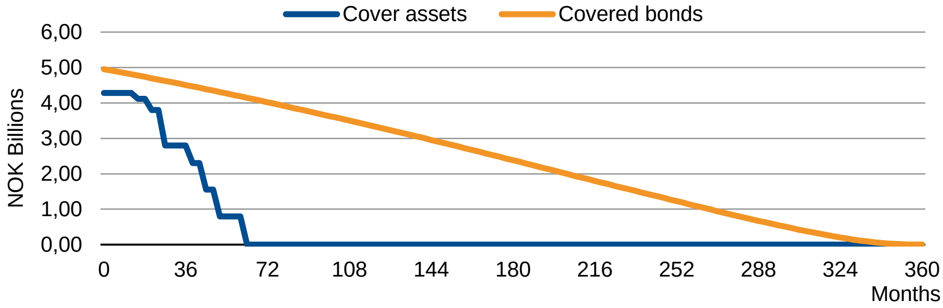
The unchanged rating-supporting overcollateralisation of 5.0% mainly reflects the programme's market risks, from asset-liability maturity mismatch risk accounting for 2pp (up from 1.5pp) and credit risk accounting for 3pp (down from 3.5pp).

Market risks are driven by the programme's sensitivity to high prepayments, which generate large cash balances. This amount of cash reduces the transaction's available excess spread, especially in sensitivity scenarios featuring both margin compression and front-loaded default timings. The higher market risk also reflects lower asset margins.

We have calculated asset margins based on loan-by-loan data, resulting in a weighted average for mortgage loans of 147bps (down from 155bps). This means generating lower excess spreads during the life of the programme. Some volatility in asset margin is also driven by the mandatory notification period that delays interest rate changes on mortgages. Slightly higher funding costs (31bps vs 29bps) have also affected excess spread.

[2] Commensurate with highest stresses (D8), applied stresses (D6) denote the stresses commensurate with the rating distance between TSBB's issuer rating and the covered bond ratings.

Figure 6 : Amortisation profile



Source: Scope Ratings, TSB

The programme is exposed to asset-liability mismatches. The weighted average life of the cover pool of 9.3 years (based on provided asset cash flows) is higher than the outstanding covered bonds' 3.5 years (accounting for their soft-bullet structure; down from 3.8 years in the previous analysis). Mismatches even persist with prepayments of 15% that would reduce the weighted average life to five years.

If cash from assets repayments and prepayments is insufficient to pay principal and interest rate for covered bonds, we model asset sales incorporating a 150 bp discount for mortgage loans on top of the stressed interest rates. Currently, available liquidity benefits from 8.6% of substitute assets in the cover pool.

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

Asset-liability mismatches

	Assets	Liabilities
NOK	100%	100%
Fixed**	0.0%	0.0%
Floating	100%	100%
WAL (years)	9.3**	3.5*

*incl. one year extension **own calculation

In the cash flow analysis, we have assumed a recovery lag of 24 months reflecting Norway's lean and digital sale procedures as well as the mostly regional asset exposure.

We calculated the bond's amortisation assuming the one-year maturity extensions were executed.

The programme's resilience against high (15%) and low (1%) prepayments as well as a set of rising and declining interest rate scenarios was tested. The covered bonds are most exposed to a high prepayment scenario in combination with low interest rates.

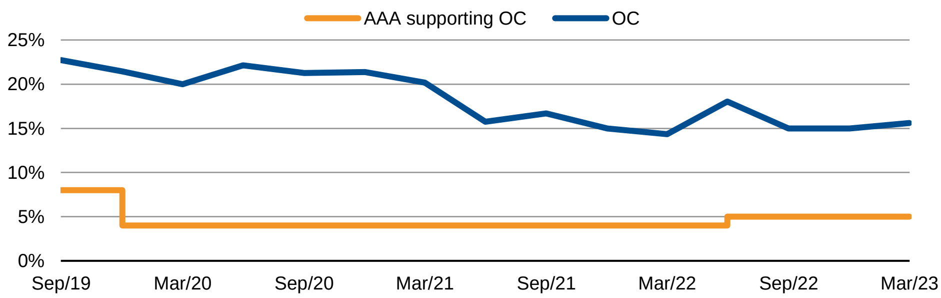
Further, we tested sensitivities towards a 50% margin compression, frontloaded defaults, 25% prepayments and a liquidity premium up to 200bps.

Availability of overcollateralisation

Overcollateralisation fully taken into account

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

Figure 7: Available overcollateralisation versus rating-supporting level



Source: Scope Ratings

Other risk considerations

Counterparty risk mitigated by alignment of interests between stakeholders

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

Country risk does not affect the rating

Country risk as specified in the methodology is not a key risk factor that constrains the covered bond rating. Norway is currently rated AAA with a Stable Outlook.

We have no evidence that transfer risk (e.g. risk of capital controls) and the risk of an institutional meltdown are pertinent risk factors in Norway. As the risks of an institutional framework meltdown, legal insecurity or currency-convertibility problems are currently remote, they do not constrain the rating of TSBB's covered bonds.

No impact from ESG

Governance factors are key for the analysis of Norwegian covered bonds and therefore drive our legal and resolution regime analysis. However, our quantitative analysis on TSBB's covered bonds does not directly include ESG aspects. This is because the issuer has no specific ESG underwriting guidelines that would result in positive/negative adjustments to the mortgage loans' terms and conditions if ESG conditions are met/not met. However, we understand that TSB is seeking to incorporate ESG risks in its underwriting.

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

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

Sensitivity analysis

Two-notch buffer against potential change in issuer rating

TSBB's mortgage-covered bond ratings benefit from a buffer against an issuer downgrade of up to two notches. Assuming the issuer's willingness to support the highest ratings as well as a stable covered bond programme risk profile, a two-notch downgrade would not affect supporting overcollateralisation.

Summary of covered bond characteristics

Reporting date	31 Mar 2023	30 June 2022	30 June 2021	30 June 2020
Issuer name	Totens Sparebank Boligkreditt			
Country	Norway			
Covered bond name	Obligasjoner med fortrinnsrett (Norwegian mortgage covered bonds)			
Covered bond legal framework	Norwegian legal covered bond framework			
Cover pool type	Residential mortgage loans			
Composition	Residential = 91.5	Residential = 92.9	Residential = 97.7%	Residential = 96.9%
	Substitute = 8.5	Substitute = 7.1	Substitute = 2.3%	Substitute = 3.1%
Issuer rating	A-/Stable	A-/Stable	A-/Stable	A-/Stable
Current covered bond rating	AAA/Stable	AAA/Stable	AAA/Stable	AAA/Stable
Covered bond maturity type	Soft bullet	Soft bullet	Soft bullet	Soft bullet
Cover pool currencies	NOK (100%)	NOK (100%)	NOK (100%)	NOK (100%)
Covered bond currencies	NOK (100%)	NOK (100%)	NOK (100%)	NOK (100%)
Governance support	5	5	5	5
Maximum achievable covered bond uplift	8	8	8	8
Potential covered bond rating buffer	2	2	2	2
Cover pool (NOK bn)	4.53	4.98	4.49	3.54
thereof, substitute assets (NOK bn)	0.42	0.38	0.10	0.11
Covered bonds (NOK bn)	4.3	5.35	3.97	2.90
Overcollateralisation: current/legal minimum	15.6%/5%	18.0% / 5%	15.8% / 2%	22.1% / 2%
Overcollateralisation to support current rating	5.0%	5.0%	4.0%	4.0%
Overcollateralisation upon a one-notch issuer downgrade	5.0%	5.0%	5.0%	5.5%
Weighted average life of assets	9.3 years [3]	8.9 years [3]	13.4 years	13.2 years
Weighted average life of liabilities [1]	3.5 years	3.9 years	4.5 years	4.4 years
Number of loans	2,651	2.865	2.662	2,163
Average loan size (NOK m)	1.7	1.7	1.7	1.6
Top 10 residential	2.0%	1.8%	1.9%	2.2%
Interest rate type, assets	Floating 100%	Floating 100%	Floating 100%	Floating 100%
	Fixed 0%	Fixed 0%	Fixed 0%	Fixed 0%
Interest rate type, liabilities	Floating 100%	Floating 100%	Floating 100%	Floating 100%
	Fixed 0%	Fixed 0%	Fixed 0%	Fixed 0%
Weighted average LTV (indexed)	52.9%	52.0%	53.1%	55.5%
Geographic split (top 3)	Innlandet = 52%	Innlandet = 53%	Innlandet = 55%	Oppland = 45%
	Viken = 35%	Viken = 35%	Viken = 33%	Akershus = 28%
	Oslo = 10%	Oslo = 10%	Oslo = 10%	Oslo = 12%
Default measure	Inverse Gaussian/ Non-Parametric	Inverse Gaussian/ Non-Parametric	Inverse Gaussian/ Non-Parametric	Inverse Gaussian/ Non-Parametric
Weighted average default rate (mortgage/substitute)	6.3% / 0.32%	6.0% / 0.32%	6.0% / 0.32%	10.5%/ 0.15%
Weighted average coefficient of variation (mortgage/substitute)	50% / na	50% / na	50% / na	50%/ 1,696%
Weighted average recovery assumption (D0/D6)[2]	99.6% / 81.5%	99.6% / 78.4%	99.8% / 77.4%	98.3% / 78.6%
Share of loans > three months in arrears (NPL)	0.00%	0.00%	0.00%	0.00%
Interest rate stresses (max./min.; currency-dependent)	-1 to 10%	-1 to 10%	-1 to 10%	-1 to 10%
FX stresses (max./min.; currency-dependent)	n/a	n/a	n/a	n/a
Max liquidity premium (mortgage/substitute)	150bps / 200bps	150bps / 200bps	150bps / 200bps	150bps / 200bps
Average servicing fee (mortgage/substitute)	25bps / 10bps	25bps / 10bps	25bps / 10bps	25bps / 10bps

[1] Including the 12-month extension
[2] D0 and D6 denote the stresses commensurate with the rating distance between our issuer rating and the covered bond ratings.
[3] Calculated based on provided cash flows

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