SCOPE Scope Ratings

Totens Sparebank Boligkreditt

Mortgage Covered Bonds

The AAA rating with a Stable Outlook assigned to the mortgage covered bonds Obligasjoner med fortrinnsrett issued by Totens Sparebank Boligkreditt (TSBB) are based on the bank's issuer rating A-/Positive, enhanced by governance-support and one additional notch of cover pool support based uplift. Governance support factors, in total, provide a rating uplift of up to five 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 Norway.

The covered bond programme

Cut-off date	Cover pool	Cover asset type	Covered bonds	Rating/Outlook
30 Jun 2024	NOK 3.36bn	Mortgage	NOK 2.68bn	AAA/Stable

Cover pool support is the primary rating driver. Together with the programme's governance support, it can provide 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' risk, 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.

Figure 1: Covered bond rating building blocks

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 bonds 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-

current uplift →

current uplift →

Covered bond rating
AAA

Outlook
Stable

Rating action
Affirmation

Last rating action
6 Aug 2024

Issuer rating
A-

Outlook
Positive

Last rating action
19 Jan 2024

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

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Stable Outlook

Scope's Stable Outlook on the mortgage covered bonds reflects the credit quality of the issuer, governance support factors and the strength of the cover pool. Together they allow for a cushion against a downgrade of up to two notches. The rating may be downgraded upon: i) an issuer rating downgrade by more than two notches; ii) a deterioration in Scope's view on governance support factors relevant to the issuer and Norway 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

On 15 January 2024, the boards of Totens Sparebank and SpareBank 1 Østlandet approved a plan for merging the two banks. We expect the necessary regulatory approvals to be receive in due course to allow for a planned full legal merger by 1 November 2024. The issuer rating has been affirmed and the outlook changed to positive reflecting the expected strengthening of the business model. SpareBank 1 Østlandet uses Sparebank 1 alliance joint covered bond issuing entity and we understand that as a result, Totens Boligkreditt will we orderly wound down following the scheduled maturities. We expect that the credit quality of the covered bond programme will not be impacted as it will continue to benefit from an active management also reflecting that the parent continues to rely on covered bond refinancing.

Since our last analysis one year ago the cover pool has already decreased by 32% to NOK 3.36bn, reflecting both reduced lending due to the rising interest rates as well as limited new issuance reflecting the above upcoming changes. The indexed loan-to-value ratio (LTV) decreased moderately to 49.9% (from 52.9%). The geographic distribution remains stable. Excess spread available to the programme has decreased, reflecting decreased loan margins.

Rating drivers and mitigants

Positive rating drivers	Negative rating drivers and mitigants
• Strong legal covered bond framework • Strong resolution regime and systemic importance of covered bonds in Norway • Best Cover pool complexity categorization allowing for the highest cover pool support • Strong cover pool support allowing for maximum uplift	• Mid to low systemic importance currently constrains governance support uplift

Upside rating-change drivers	Downside rating-change drivers
• The ratings are on the highest level achievable • Additional issuer downgrade protection if we were able to assign a higher systemic importance to the issuer and its covered bonds • 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 two notches. • Reduction of the provided overcollateralisation below the level of rating supporting OC which currently is at 6.0% • The rating may also be downgraded upon a deterioration governance support factors and the interplay between complexity and transparency by together more than two notches

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The issuer

TSSB is a fully owned subsidiary of Totens Sparebank and plays a key role as the covered bond issuing entity of the group.

Subject to approval from the Norwegian FSA, Totens Sparebank and SpareBank 1 Ostlandet intend to merge on 1 November 2024. With NOK 180bn in assets as of Q1 2024, SpareBank 1 Ostlandet, will act as the acquiring bank, and will acquire all the assets, rights and obligations of Totens Sparebank, including TSBB (NOK 22bn in assets, Q1 2024) upon completion of the merger. The merged bank will continue under the name of SpareBank 1 Ostlandet and be part of the SpareBank 1 Alliance, the largest banking alliance in Norway.

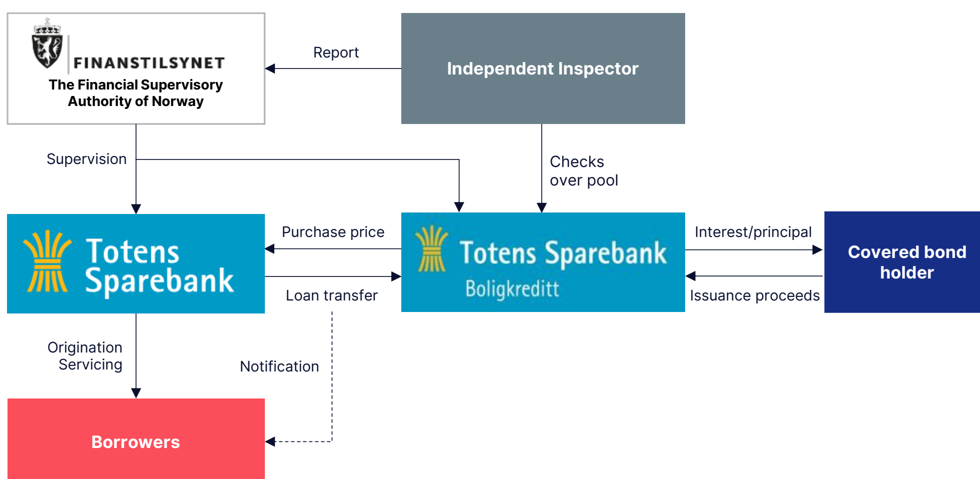
Scope considers the proposed merger to be credit positive for Totens Sparebank. Geographic and business diversification would increase, strengthening its business model. Further, the merged bank would become the fourth largest savings bank in the country, with a leading position in the Inland region. The merged bank would be better placed to manage increasing competition and address growing regulatory requirements. Further, the two banks share a common goal to support the economy and community in the Inland region. For more information, please check the issuer's report published on 19 Jan 2024.

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. 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.

Under this framework, covered bond 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.

Figure 2: Issuance structure



Source: Scope Ratings

Governance credit support analysis

Five notches from legal framework and resolution regime

Governance credit support is a key rating driver for TSBB' mortgage covered bonds. It provides an uplift of five notches. It combines our view on the legal framework for mortgage covered bonds in Norway together with our assessment on the Norway resolution regime and the systemic relevance for covered bonds in general and specific to TSBB. For more information, please check our report on Legal framework analysis: Norway.

Legal framework and structural support analysis

Two notches reflecting strong legal framework

The relevant legal framework is based on the relevant section in the country's Financial Institutions Act (Lov om finansforetak og finanskonsern) and related regulation on mortgage companies (I forskrift 9. desember 2016 nr. 1502 om finansforetak og finanskonsern (finansforetaksforskriften)). Both were introduced in 2007. The Act was amended to transpose the European CBD and came into force 8 July 2022, in parallel with the application date in the EU. The Act provides the general structure of the main framework and references to regulations provided by the Ministry of Finance (Finanstilsynet). The Norwegian regulation on capital requirements and national adaptation of CRR/CRD IV provides further details on the requirements for Norwegian covered bonds and issuers. We consider the Norway's covered bond framework to be strong, fully meeting our criteria for protecting investors. Therefore, we assign the highest credit differentiation of two notches.

Segregation of cover pool upon insolvency

The Norwegian legislation gives covered bondholders preferential claims over the cover pool if the issuer is placed under public administration. The term "covered bonds", (in Norwegian "obligasjoner med fortrinnsrett" or "OMF") is protected by law. The assets in the pool remain with the estate if the issuer is placed under public administration but bondholders and derivatives counterparties have exclusive, equal and proportionate preferential claims over the cover pool, and the administrator is committed to assuring timely payments, provided the pool provides full cover to claims. The issuer maintains a register of issued covered bonds and of the cover assets assigned to them, including derivatives agreements.

Ability to continue payments after issuer insolvency

Under the Norwegian legislation, owners of covered bonds and derivatives counterparties have a direct claim to timely payments with funds covered by preferential rights. Only if timely payment is not possible i.e. after maturity extension is triggered and no distressed liquidity situation emerges, can payments on the covered bonds be suspended. Covered bonds will not, however, be subject to automatic acceleration in the event of special administration or liquidation under public administration of the credit institution.

The administrator's is to ensure proper management of the cover pool and that holders of covered bonds and derivatives counterparties receive agreed and timely payments. Assets can be sold, and new covered bonds can be issued. The administrator can also enter new derivatives contracts or change existing contracts. The entire collateral can only be sold if this provides full coverage of all senior costs as well as the costs incurred by covered bond investors (including any deferred or accrued interest and costs).

Asset eligibility and risk management principles

The credit institution shall ensure that payment flows from the cover pool enable the institution to honour its payment obligations towards holders of covered bonds and derivatives counterparties. It shall establish a liquidity reserve to be included in the cover pool as substitute assets in addition to carrying out stress tests periodically to ensure satisfactory liquidity management.

The Act specifies valuation requirements for the mortgage portfolio. The value of the property securing the mortgage claim shall be "reasonable" and not higher than its market value. The valuation must be carried out according to recognised principles by a competent and independent person but can be based on statistical models. It must be monitored and renewed as necessary.

Programme enhancements remain available

The public administrator must ensure proper management of assets securing covered bonds and that the provisions on composition of collateral, liquidity, currency and interest rate risk are continuously complied with.

According to the law, the value of the assets must at all times cover the value of the covered bonds. Any excess collateralisation, yielding more than is necessary to cover bondholders' or derivatives counterparties' claims, may constitute a general bankruptcy claim. While this may limit the preferential position of covered bond investors, it is up to the special administrator to judge if available over-collateralisation (OC) is excessive. We do not expect that any special administrator would release assets as long as it has to ensure timely and full payment of covered bonds according to the law.

The law further specifies a concentration limit of 5% for individual exposures.

The regulation specifies minimum over-collateralisation levels that are dependent on the collateral type. Norwegian mortgage covered bonds benefit from nominal overcollateralisation that has increased to 5% (from 2% earlier). Domestic public-sector covered bond programmes are only required to maintain 2% minimum OC. Export Credit Agencies or internationally backed public-sector covered bond programmes must provide 10% minimum OC.

The cover pool's interest yield must always be higher than the sum of the costs associated with covered bond funding including derivatives.

The collateral requirements allow for loans secured by housing association shares, mortgage loans, or loans secured by pledges in other real property assets. Mortgage collateral must be located within European Economic Area (EEA). Additionally, assets can consist of assets guaranteed by a state or public body, claims against credit institutions or receivables from derivatives agreements.

According to the regulation, the collateral pool securing a European Covered Bond (Premium) can only consist of claims that meet the requirements of article 129 of the Capital Requirements Regulation. This restricts funding coverage for mortgage covered bonds to the asset's loan-to-value threshold of 80% (from 75% earlier) for residential mortgages and 60% for commercial mortgages. The regulation further specifies that mortgages on holiday properties qualify only up to a loan-to-value of 60%. The amount of substitute assets is restricted according to their credit quality step category

Covered bond oversight

Norwegian issuers are subject to a supervisory regime involving both an independent monitor (cover pool monitor) and the Norway's national supervisor, Finanstilsynet – the Financial Supervisory Authority (FSA).

The FSA must approve new covered bond issuance programmes and can reject issuance in case of solvency doubts. The cover-pool monitor must be a State-authorised auditor and be different from the firm auditing the parent or the covered bond issuer.

At least quarterly, the monitor checks that the requirements for collateral, OC, liquidity, registration and investor information are met and reports at least annually to the FSA. If the monitor has reason to believe that the requirements have not been met, it must notify the FSA as soon as possible.

Resolution regime and systemic importance analysis

Three notches reflecting Resolution regime and systemic importance of the issuer

TSBB's mortgage 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.

Availability and strength of statutory provisions

Norwegian covered bonds are explicitly excluded from bail-in, both as a consequence of the transposition into national law of the EU Bank Recovery and Resolution Directive (2014/58/EU – BRRD) and, very explicitly, section 11-6 of the Financial Institutions Act.

Norway is in the EAA but is not part of the EU. Relevant EU rules are normally incorporated into the EEA Agreement before being enacted into Norwegian law. This includes the BRRD as well as the European CBD.

The main legal Act applicable to Norwegian banks is the Act on Financial Undertakings and Financial Groups (Financial Undertakings Act) which has been in effect since 1 January 2016. This Act consolidates the main financial regulations and implements (among others) the Capital Requirements Regulation (575/2013) (CRR), Capital Requirements Directive (2013/36/EU) (CRD IV) and the Bank Recovery and Resolution Directive (2014/59/EU) (BRRD).

Systemic importance of issuer

The issuer's business model, systemic importance, liability and capital structure can incentivise regulators to use available resolution tools. We assess on an issuer-specific basis the likelihood that a covered bond programme will be maintained as an actively managed going-concern funding programme. The Norwegian banking market is dominated by the two largest banks/mortgage companies. Resolution for such systemically important banks is highly likely. For smaller, typically regional saving banks with wholly owned covered bond issuers, low-to-moderate covered bond issuing activities and market share translates into low to moderate systemic importance. Such banks generally only issue into the domestic market. The most likely resolution scenario would be a transfer or takeover by another bank. An orderly wind-down of the covered bond issuer is another plausible scenario. As seen throughout Norway, banking alliances play an important role in sustaining individual small banks' efficiencies and business franchises. This includes shared ownership of companies offering a range of financial products, such as insurance, leasing and securities services as well as covered bond funding. The number of participating banks and their size in relation to the whole market act as a guide for us to determine their systemic importance.

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.

Systemic relevance of covered bonds

We classify Norwegian residential mortgage covered bonds as a systemic important refinancing product. In Norway, 23 specialised covered bond issuers are active, issuing residential,

commercial and public sector-backed covered bonds. Since the introduction of covered bonds in 2007, covered bonds have become a key pillar in each bank's funding toolkit. They allow banks to better match longer-dated mortgage financing with stable and also longer-dated wholesale funding, which they are also able to source in the euro market or in USD.

Since 2007, covered bonds outstanding have soared to EUR 135bn or NOK 1.35trn at the end of 2022. Outstanding covered bonds to GDP has doubled to more than 40% at the end of 2020 compared to 2010 and reduced to a still high 24pc at the end of 2022. Annual issuance regularly hovers around EUR 34.6bn. Globally, Norway was the tenth by the total outstanding covered bonds. Mortgage covered bonds make up around 98% (or around EUR 133bn). Most are secured by residential mortgages.

Covered bonds provide Norwegian banks with funding stability when capital markets-based wholesale funding has been challenging. Ongoing access to investors as well as ability to use covered bonds as collateral with the central bank prompted peak issuance volumes shortly after the Global Financial Crisis in 2008 (EUR 26bn) as well as during the pandemic crisis (EUR 32.8bn).

Proactive stakeholder community

The country's covered bond issuers actively co-operate under the umbrella of the Norwegian Covered Bond Council to promote the product and initiate any changes to the framework, such as the March 2017 increase in minimum OC to 2% to avoid potential challenges for cover-pool derivatives due to the European Market Infrastructure Regulation as well as its involvement during the transposition of the European covered bond directive (CBD). Domestic covered-bond investors such as banks and insurers actively use covered bonds not only as a substitute for long-dated and rare NOK-denominated government debt but also to manage liquidity. Norway's central bank has demonstrated its support for covered bonds by using them in its repo operations and running a covered bond-to-government debt swap programme between 2008 and 2014. Norway's FSA also has an active interest given the widespread use of covered bonds to refinance residential mortgage lending. Norway was also first out of the blocks to align its covered bond framework with the CBD and met the European deadline to transpose the directive into national law. These are further signs for the high systemic importance of the product and the activity of the local community. For shared ownership companies, we further analyse the implicit and explicit support documented in the companies' service agreements. The cohesion between the owners can be weaker if compared to a 100%-owned covered bond company. As a consequence, we expect to see strong documented shareholder support with regard to liquidity, over-collateralisation and operations (servicing in regard to the treatment of nonperforming loans) to strengthen the coherence of the involved parties.

Cover pool analysis

TSBB's mortgage covered bond rating is cover pool-supported, allowing for three out of three notches of uplift to support highest ratings. Governance support provides for a five-notch rating uplift and an effective floor against a deterioration in cover pool credit quality.

CPC assessment

Our assessment on the interplay between complexity and transparency translates into a CPC category of 'low' risk. The assessment on the interplay between complexity and transparency allows for 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 two notches, assuming OC does not become a constraining factor.

The CPC category of low-risk stems from the availability of detailed, regular, current and forward-looking transparency and reporting on key credit and market risk factors relevant to the analysis. We took into account information on the issuer's lending products; underwriting, credit and market risk management; and high transparency on its origination and issuance strategy. We had full access to all relevant counterparty risk information.

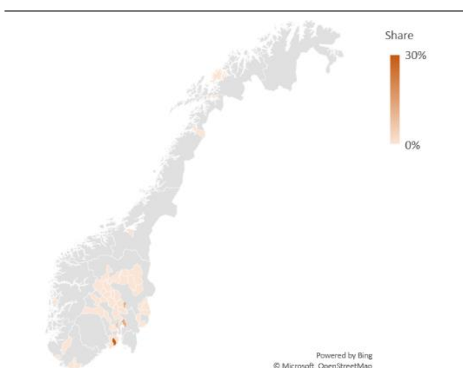
Cover pool composition

The cover pool is 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 (53.9%), Akershus, Østfold og Buskerud (33.9%), and Oslo (10.1%).

The mortgage pool consists of 1,855 loans granted to 1,795 obligors with an average loan size of NOK 1.6m (around EUR 139,000). The 10 largest obligors only accounts for 2.8%. Granularity has slightly fallen since our last review, also reflecting the mortgage portfolio's decline by 32%.

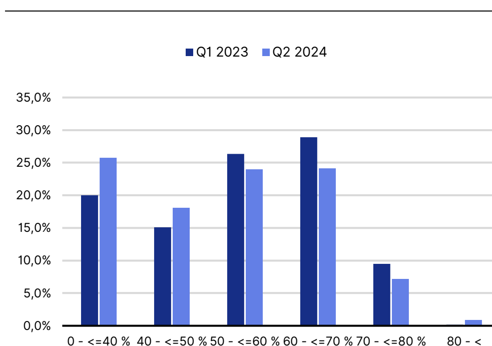
Around 80% of the portfolio is made up of single-family houses and apartments, the remaining are agricultural houses and housing in associations. The indexed LTV is 49.9%, down 3pp since our last review.

Figure 3: Geographical distribution



Source: Scope Ratings, TSBB

Figure 4: LTV distribution



Source: Scope Ratings, TSBB

Cover pool characteristics

Reporting date	Jun 2024	Mar 2023
Balance (NOK bn)	3.36	4.95
Residential (%)	89.4	91.4
Substitute (%)	10.6	8.6

Property type (%)

Reporting date	Jun 2024	Mar 2023
Single/double-family house	71.5	71.6
Apartment	10.6	12.9
Shares*	8.0	7.8
Others	9.9	7.7

* Shares in housing associations

General information

Reporting date	Jun 2024	Mar 2023
No. of loans	1,855	2,651
No. of obligors	1,795	2,549
Avg. size (NOK mn)	1.6	1.7
Top 10 (%)	2.8	2.0
LTV (%)	49.9	52.9

Interest rate type (%)

Reporting date	Jun 2024	Mar 2023
Floating	100	100
Fixed	0.0	0.0

Repayment type (%)

Reporting date	Jun 2024	Mar 2023
Annuity / Linear	90.3	92.4
Interest-only	9.7	7.6

Asset risk analysis

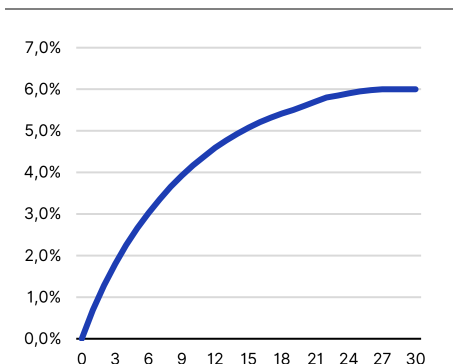
Strong credit quality translates into low credit risk

The asset quality of the cover pool remains solid comprising Norwegian, mainly owner-occupied residential mortgage loans with low LTVs.

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 bb+ credit quality. Our analysis is based on line-by-line data, provided by the issuer.

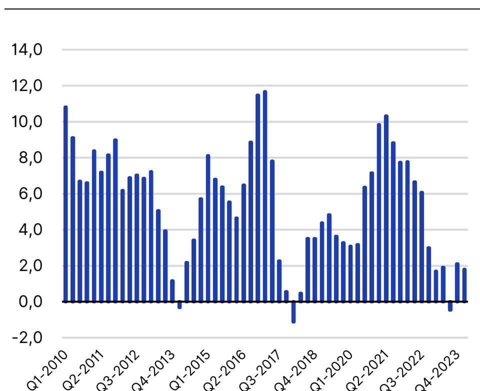
Considering the mortgage loans' seasoning and scheduled lifetime amortisation, the programme's cumulative term defaults results into a mean term default rate of 6% which compares to 6.3% one year ago. The coefficient of variation is 50% unchanged since the last analysis.

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



Source: Scope Ratings

Figure 6: Annual house price growth in Norway (qtq)



Source: OECD, Scope Ratings

Stressed mortgage recovery rates reduced to 71.5% from 75.5% in the previous analysis. This mainly driven by the higher Security value haircut (SVH) which offsets the lower LTV effect. Our stressed market value haircut (MVD) has been established as 46.9% for Norway. Our residential SVH are a function of market value declines (MVD) and fire-sale discounts (FSD).

Norway security value haircuts

Region	Base MVD	Stressed MVD	Firesale discount	Sale costs	Stressed SVH
Norway	5%	46.9%	20%	10%	57.5%

MVD: market value decline / SVH: security value haircut

Our base recovery expectation remains very strong at 99.4%. 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 10% 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. We calculated the stress recovery rate for the substitute assets of 52% based on the actual assets.

Cash flow risk analysis

The unchanged rating-supporting overcollateralisation is 5.0%.

Supporting overcollateralisation of 5%

We have calculated asset margins based on loan-by-loan data, resulting in a weighted average of 130bps (down from 147bps). Compared to last year there is less excess spread during the life of the programme. This partially reflects the mandatory notification period for borrowers floating mortgage rates that does not allow an instantaneous change following a change of the reference rate. Slightly higher funding costs (32bps vs 31bps) have also affected excess spread.

The programme is most sensitive to a combination of high prepayments and rising interest rates This is mainly driven by high prepayments, which generate large cash balances.

The programme is exposed to asset-liability mismatches. The weighted average life of the cover pool of 9.0 years (based on provided loan terms and asset cash flows) is higher than the outstanding covered bonds' 2.95 years (accounting for their soft-bullet structure; down from 3.5 years in the previous analysis). Mismatches even persist with prepayments of 15% that would reduce the weighted average life to five years.

Asset-liability mismatches

	Assets	Liabilities
NOK (%)	100	100
Fixed (%)	0	0
Floating (%)	100	100
WAL (years)	9	2.95*

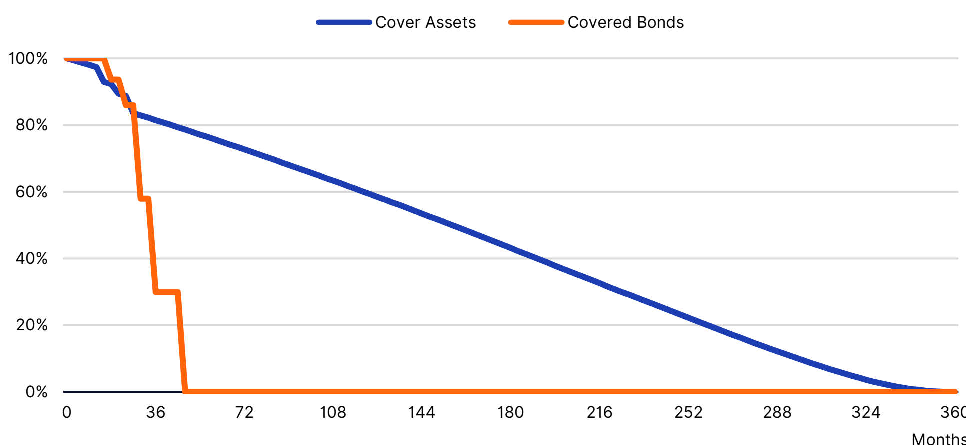
*incl. extension

If cash from assets repayments and prepayments is insufficient to pay principal and interest rate for covered bonds, we model asset sales incorporating a 150bps discount for mortgage loans on top of the stressed interest rates. Currently, available liquidity benefits from 10.6% 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. We do not expect foreign currency-denominated issuances.

In the cash flow analysis, we have assumed a recovery lag of 24 months. 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.

Figure 7: Amortisation profile



Source: Scope Ratings, TSBB

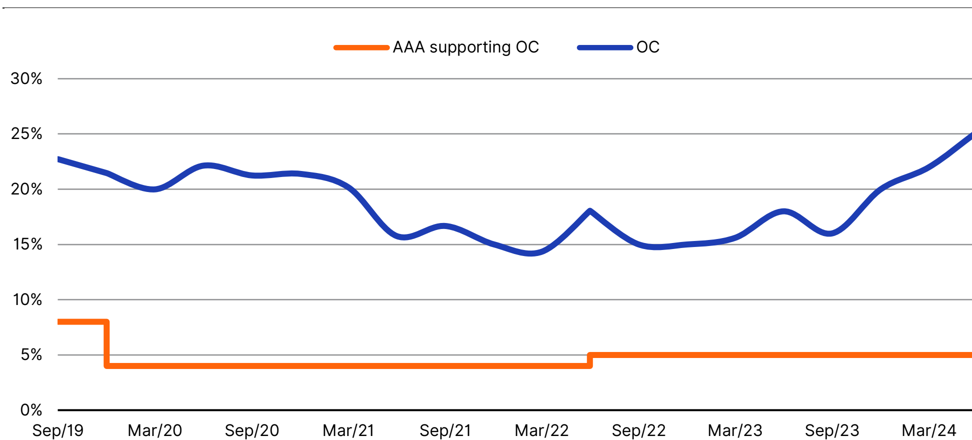
We complemented our base case cash flow results with additional analysis, testing sensitivities to a 50% margin compression, frontloaded defaults, 25% prepayments and a liquidity premium up to 200 bp. None of such calculation resulted into an adjustment of our rating supporting overcollateralisation.

Availability of overcollateralisation

The current rating of TSBB allows us to account for the provided oc. 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. We do not expect the merger to impact the programme's risk profile nor the provision of sufficient oc.

Overcollateralisation fully taken into account

Figure 8: Available OC versus current rating-supporting level



Source: Scope Ratings, TSBB

Other risk considerations

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 comfort from legal obligations required to maintain the European Covered Bond (Premium) label. An issuer is obliged to only have very limited exposures to entities with a minimum credit quality step 3 (BBB category) which effectively ensures a replacement of deteriorating counterparties. In addition, we view positive that collections are generally made via direct debit, allowing for a relatively swift redirection of payments if needed.

Counterparty exposure does not limit the rating, Counterparty risk mitigated by alignment of interests between stakeholders

Country risk is not a key risk factor that constrains the covered bond rating. Norway is currently rated AAA/Stable. 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 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.

Country risk is not a key rating driver

Governance factors are a key for the analysis of Norway covered bonds as such drive our legal and resolution regime analysis. In our quantitative analysis performed for the covered bonds issued by TSBB we however have not directly included 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.

No impact from ESG

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 notches buffer against an issuer downgrade

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 increase the rating-supporting OC requirement to 6%.

As a consequence, the rating may be downgraded upon: i) an issuer rating downgrade by more than two notches; ii) a deterioration in Scope's view on governance support factors relevant to the issuer and Norway 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	30-Jun-2024	31-Mar-2023
Issuer name	TSBB	TSBB
Country	Norway	Norway
Covered bond name	Obligasjoner med fortrinnsrett (Norwegian mortgage-covered bonds)	Obligasjoner med fortrinnsrett (Norwegian mortgage-covered bonds)
Covered bond legal framework	Norwegian legal covered bond framework	Norwegian legal covered bond framework
Cover pool type	Residentialmortgage loans	Residentialmortgage loans
Composition	Residential = 89.4%	Residential = 91.5%
	Substitute = 10.6%	Substitute = 8.5%
Issuer rating	AAA/Stable	AAA/Stable
Current covered bond rating	AAA/Stable	AAA/Stable
Covered bond maturity type	Soft bullet	Soft bullet
Cover pool currencies	NOK (100%)	NOK (100%)
Covered bond currencies	NOK (100%)	NOK (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	2	2
Cover pool (NOK bn)	3.36	4.53
thereof, substitute assets (NOK bn)	0.35	0.42
Covered bonds (NOK bn)	2.6	4.3
Overcollateralisation: current/legal minimum	15.2%/5%	15.6%/5%
Overcollateralisation to support current rating	5%	5%
Overcollateralisation upon a one-notch issuer downgrade	5%	5%
Weighted average life of assets (Scope calculated)	9 years	9.3 years [1]
Weighted average life of liabilities (extended)	2.95 years	3.5 years
Number of loans	1,855	2,651
Average loan size (NOK mn)	1.6	1.7
Top 10	2.80%	2.00%
Interest rate type assets	Floating 100%	Floating 100%
	Fixed 0%	Fixed 0%
Interest rate type liabilities	Floating 100%	Floating 100%
	Fixed 0%	Fixed 0%
Weighted average loan to lending value	49.90%	52.90%
Geographic split	Norway = 100%	Norway = 100%
Default measure (residential/substitute)	Inverse Gaussian/ Non-Parametric	Inverse Gaussian/ Non-Parametric
Weighted average annualised default rate (residential/substitute)	6.0% / 0.32%	6.3% / 0.32%
Weighted average coefficient of variation (residential/substitute)	50% / na	50% / na
Weighted average recovery assumption (Dmax) (residential/substitute)	71.5% / 52%	75.5% / 50%
Share of loans > three months in arrears (NPL)	0.00%	0.00%
Interest rate stresses (max/min)	-1 to 10%	-1 to 10%
FX stresses (max/min; currency-dependent)	n/a	n/a
Max liquidity premium	150bps / 107bps	150bps / 200bps
Average servicing fee	25bps / 10bps	25bps / 10bps

[1] Calculated based on provided cash flows

Source: Scope Ratings

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Related research

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Norway's residential housing boom is over: prices starting to fall, Nov 2022
Scope affirms Totens Sparebank's issuer rating of A- and changes Outlook to Positive, Jan 2024

Applied methodologies

Covered Bond Rating Methodology, July 2024

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