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New Issue: The Mortgage Society Of Finland CBA Covered Bond Program

Primary Credit Analyst:
Natalie Swiderek, Madrid + 34 91 788 7223; natalie.swiderek@spglobal.com

Secondary Contact:
Phuong Nguyen, Paris (49) 0 69-33-999-313; phuong.nguyen@spglobal.com

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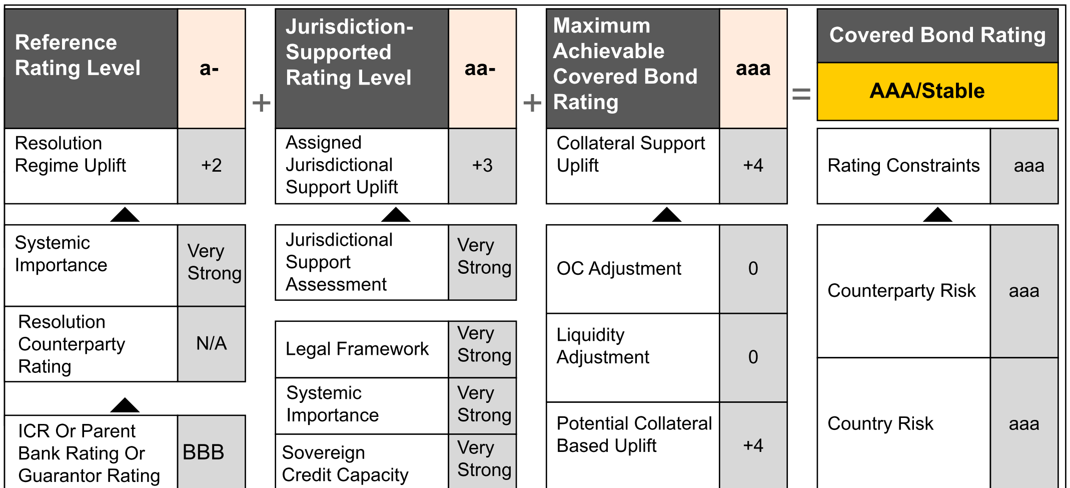
Ratings Detail



Note: As a starting point of the analysis, we may use the ICR of the parent or guarantor when the issuer is not rated, but it belongs to a group with a rated parent or payments under the covered bonds are guaranteed by another rated entity. ICR--Issuer credit rating. N/A--Not applicable.

Major Rating Factors

Strengths

- The cover pool comprises well-seasoned Finnish mortgage loans with lower current loan-to-value (LTV) ratios than other specialized mortgage lenders in the Nordics.
- The bonds' soft-bullet repayment profile mitigates short-term liquidity risk.
- The structure benefits from a public commitment by the issuer to maintain overcollateralization consistent with a 'AAA' rating.

Weaknesses

- Concentration of mortgages in the South of Finland, which we have considered in our determination of default frequency.
- Obligor concentrations within the sub portfolio of housing association loans, with the largest 10 borrowers representing almost 10% of the total mortgage loan balance. We have addressed this in our analysis through the largest obligor default concentration test.

Outlook: Stable

S&P Global Ratings' stable outlook on the 'AAA' ratings on the Mortgage Society of Finland's ("Suomen Hypoteekkiyhdistys", or Hypo) CBA mortgage covered bond program and the inaugural issuance reflects the stable outlook on the long-term issuer credit rating (ICR) on Hypo (BBB/Stable/A-2).

Rationale

We have assigned our 'AAA' credit ratings to Hypo's CBA covered bond program and its inaugural issuance (see "Mortgage Society of Finland CBA Covered Bond Program And First Issuance Assigned 'AAA' Rating; Outlook Stable," published on Nov. 28, 2022).

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.

From our analysis of Hypo's covered bond program and the Finnish covered bond legislation, we consider that the assets registered in the cover pool are effectively isolated for the benefit of the covered bondholders if the issuer becomes insolvent. The protection of the cover pool assets and the continued management of the cover pool allows us to rate the covered bonds higher than our long-term ICR on Hypo.

Based on our operational risk analysis, which covers a review of origination, underwriting, collection, and default management procedures, as well as cover pool management and administration, we believe satisfactory procedures are in place to support our ratings on the covered bond and the program.

Hypo is domiciled in Finland, which is subject to the EU's Bank Recovery and Resolution Directive (BRRD). We consider that mortgage covered bonds have a very strong systemic importance in Finland. These factors increase the likelihood that Hypo would continue servicing its covered bonds without accessing the cover pool or receiving jurisdictional support, even following a bail-in of its senior unsecured obligations. We have therefore assigned two-notches of uplift above our long-term ICR on Hypo to determine the covered bonds' reference rating level (RRL) of 'a-'.

We considered the likelihood of jurisdictional support. Based on a very strong jurisdictional support assessment for mortgage covered bonds in Finland, we assigned three notches of uplift from the RRL to determine the jurisdiction-supported rating level (JRL) of 'aa-'.

Our collateral support analysis is based on the asset information as of Aug. 15, 2022. The €385.7 million cover pool (current balance) comprises Finnish residential mortgage loans (26.48%) and loans to housing associations (73.52%). Based on our collateral support analysis, the available credit enhancement exceeds the target credit enhancement, which means that the covered bonds are eligible for up to four notches of collateral-based uplift above the JRL. We do not reduce the total collateral-based uplift owing to Hypo's commitment to maintain overcollateralization at the 'AAA' rating and because we consider that the liabilities' soft-bullet structure mitigates short-term liquidity risk.

There are no rating constraints to the 'AAA' ratings relating to legal, counterparty, or sovereign risks.

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

Program Description

Table 1

Program Overview*	
Jurisdiction	Finland
Year of first issuance	2022
Covered bond type	Legislation-enabled
Outstanding covered bonds (mil. €)	300
Redemption profile	Soft-bullet
Underlying assets	Finnish residential mortgage loans and loans to housing associations
Jurisdictional support uplift	3
Unused notches for jurisdictional support	0
Target credit enhancement (%)	15.82
Credit enhancement for current rating (third notch of collateral uplift, %)	12.74
Available credit enhancement (%)	28.56
Collateral support uplift	3
Unused notches for collateral support	1
Total unused notches	0†

*Based on cash flows as of November 2022. † Zero unused notches of collateral support after application of our counterparty risk criteria (see "Counterparty risk").

Founded in 1860, Hypo is the oldest private credit institution in Finland. It is licensed bank and a mutual company operating under Finland's Act on Mortgage Societies and is governed by its members. With total assets of about €3.3 billion and a loan portfolio of €2.7 billion as of June 31, 2022, it has a marginal market share of about 0.8% in Finnish home mortgages and 1.0% in the total lending market in 2021. It grants long-term loans to Finnish households and housing companies against a mortgage or other safeguarding collateral. Hypo is active in Helsinki, southern Finland, and specified growth centers in the rest of the country.

This is Hypo's second covered bond program. It is set up to issue covered bonds under Finland's Covered Bond Act, (CBA, 151/2022, as amended), which has been in place since July 8, 2022. The mortgage covered bonds will be issued under Hypo's €2.5 billion program for the issuance of senior preferred notes, subordinated debentures, and covered bonds.

The covered bond program was established in November 2016 and now incorporates two separate cover pools: the newly established cover pool governed by the CBA (the "CBA Covered Bond Program"), and Hypo's existing covered bonds (the "MCBA Covered Bond Program"), which continue to be governed by the Finnish Act on Mortgage Credit Bank Activities (688/2010, as amended). The covered bonds issued under the CBA Covered Bond Program rank pari passu among themselves but do not relate to the MCBA Covered Bond Program. Covered bondholders and derivative counterparties related to the CBA Covered Bond Program have a priority claim only on the assets registered in the

CBA Covered Bond Program. Similarly, covered bondholders and derivative counterparties related to the MCBA Covered Bond Program have a priority claim only on the assets registered under the MCBA covered bond program.

Covered bonds are a vital funding tool for Hypo, representing 42% of total funding as of March 31, 2022.

The covered bonds constitute direct unconditional and unsubordinated debt obligations of Hypo and are secured by a cover pool of eligible assets including residential mortgage loans and loans to housing associations registered in the cover pool, in line with the CBA.

The €300 million inaugural fixed-rate bond has a five-year scheduled maturity, with a one-year maturity extension. During the extension period, the bond pays one-month Euro Interbank Offer Rate (EURIBOR) plus a margin. To hedge the interest rate mismatch arising from the floating interest rate paying assets and the fixed interest rate paying covered bond the issuer entered into an interest rate hedge swap with Swedbank AB and Danske Bank A/S.

The mortgage borrowers pay their loan installments into external bank accounts in Hypo's name or in the name of its wholly owned subsidiary. We view the resulting account bank risk as mitigated by Hypo's commitment to replace these accounts within 90 calendar days should their long-term ICR drop below "BBB".

The covered bond benefits from Hypo's commitment to maintain overcollateralization sufficient to support a 'AAA' rating on the covered bond.

The Mortgage Society of Finland CBA Covered Bond Program

Transaction structure

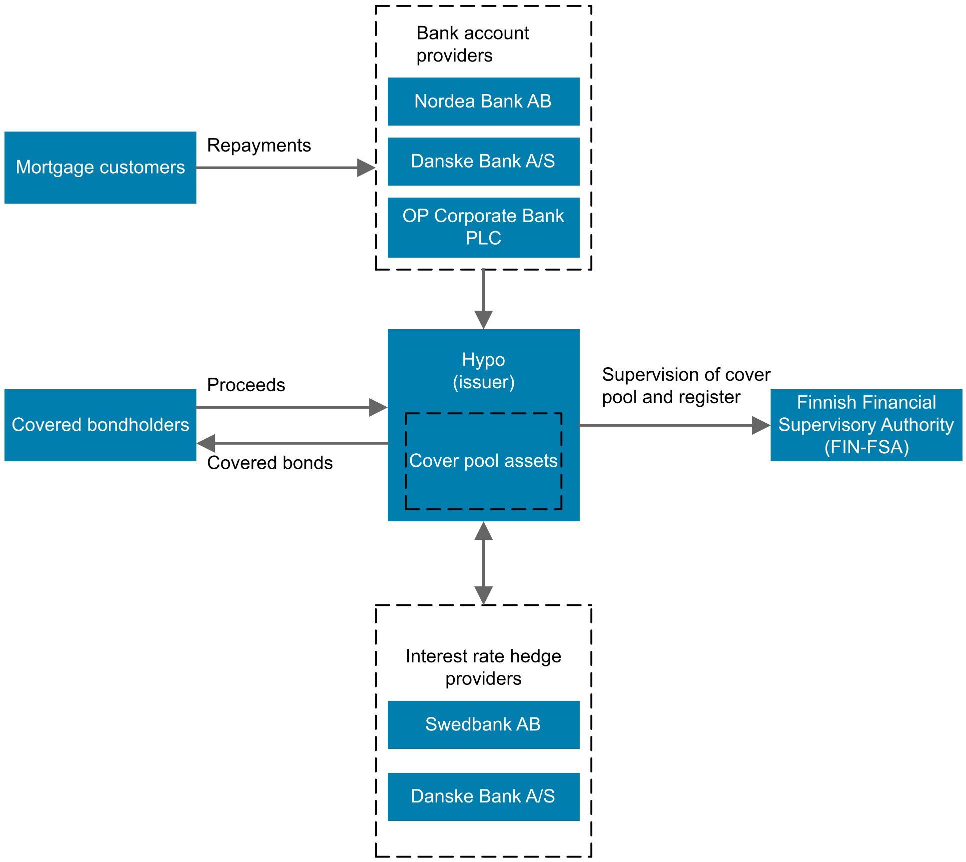


Table 2

Program Participants

Role	Name	Rating	Rating dependency
Issuer	The Mortgage Society of Finland	BBB/Stable/A-2	Yes
Originator	The Mortgage Society of Finland	BBB/Stable/A-2	No
Bank account provider	Nordea Bank Abp	AA-/Stable/A-1+	Yes
Bank account provider	Danske Bank A/S	A+/Negative/A-1	Yes
Bank account provider	OP Corporate Bank PLC	AA-/Stable/A-1+	Yes
Interest rate hedge provider	Swedbank AB	A+/Stable/A-1	Yes
Interest rate hedge provider	Danske Bank A/S	A+/Negative/A-1	Yes

Rating Analysis

Legal and regulatory risks

We base our legal analysis on our criteria "Asset Isolation and Special-Purpose Entity Methodology," published on March 29, 2017.

The covered bonds are governed by the CBA, which implemented the Covered Bond Directive into Finish legislation. The CBA applies since July 8, 2022 and repealed the MCBA.

In our opinion, the CBA satisfies the relevant legal aspects of our covered bond criteria. We have concluded that the assets in the cover pool are effectively isolated for the benefit of covered bondholders. The protection of the assets and the continued management of the cover pool allows us to rate the covered bond program above the long-term ICR on Hypo.

Under the CBA, the issuer's bankruptcy would not automatically trigger the covered bonds' early redemption or the suspension of payments to bondholders. Accordingly, we rate the covered bonds based on the legal final maturity.

The CBA requires issuers to have a license from the Finnish Financial Supervisory Authority (FIN-FSA) to issue covered bonds. Further, they must maintain a register for the covered bonds and the collateral forming the cover pool. The FIN-FSA monitors the management of the register, including the recording of assets, and the issuer must regularly report the information in the register to the FIN-FSA.

The CBA defines the eligibility criteria for the cover pool assets that comprise residential mortgage loans, commercial mortgage loans, public-sector loans, and substitute assets to facilitate liquidity management.

Derivatives are allowed for risk hedging purposes and must be registered in the cover register. Derivatives must also remain in force despite the issuer's bankruptcy, liquidation, or resolution.

The CBA allows deposit banks and credit societies to participate indirectly in the issuance of covered bonds via intermediary loans granted by a mortgage credit bank. Hypo's cover pool does not comprise any intermediary loans.

Under the CBA, issuers must have 2% overcollateralization on a net present value (NPV) basis. This requirement increases to 5% on an NPV basis if certain requirements of article 129 of the Capital Requirements Regulation are not fulfilled.

The CBA introduces a 180-day liquidity requirement whereby the cover pool must include sufficient substitute assets to meet the maximum net outflow connected to the covered bonds during the upcoming 180-day period. We understand that in calculating the net outflow related to the covered bonds, issuers may consider the extension of the maturity.

Under the CBA, an extension of the maturity of the covered bonds by up to 12 months is permissible, subject to approval by the FIN-FSA and certain conditions being met, including:

- The issuer being unable to obtain long-term financing from ordinary sources;

- The issuer being unable to meet the liquidity requirement under the CBA upon payment of the covered bonds; and
- Such extension not affecting the order of the maturity based on the original maturity dates of covered bonds secured by the same cover pool.

If the issuer becomes insolvent, the FIN-FSA would appoint a supervisor to supervise the management of the cover pool. While a bankruptcy administrator (appointed by a court) manages both the issuer's insolvency estate and the cover pool, the supervisor's role is to protect the interests of covered bondholders with powers to direct the issuer's general bankruptcy administrator.

Upon issuer insolvency, covered bondholders and derivative counterparties (including termination fees) have a preferential claim to the assets in the cover pool, which would be isolated from the issuer's other assets.

Under the CBA, covered bondholders and derivative counterparties have a priority of payment right to 100% of the properties' value, although only 80% of the market value of residential properties and 60% of the market value of commercial estate properties can be included in the determination of overcollateralization.

The CBA excludes set-off against cover pool assets and claw-back risk.

Operational and administrative risks

Our analysis of operational and administrative risks follows the guidelines in our criteria (see "Covered Bond Ratings Framework: Methodology And Assumptions," published on June 30, 2015).

Hypo focuses on very-low-risk lending--comprising mortgage loans to domestic retail customers (30% of total portfolio as of second-quarter 2022) and housing companies (68% of total portfolio). Hypo expects loan growth to be balanced between retail and housing company loans, reflective of its low-risk appetite.

Mortgage loans are euro denominated and mainly floating rate. As of March 31, 2022, Hypo's average loan book LTV ratio stood at 32.0%, which is well below that of many specialized mortgage lenders in the Nordics. Furthermore, mortgage loans are almost entirely amortizing with an average maturity of 19.7 years.

Hypo is active only in Helsinki, southern Finland, and specified growth centers in the rest of the country. Its sole physical branch is located in Helsinki with services complemented through online and telephone banking.

Hypo's underwriting policy comprises three main pillars:

- General terms (approved by the supervisory board), which lay down the core principles applicable to all lending activities such as requirements for collateral and overall collateral evaluation, and customer creditworthiness and cash flow sufficiency;
- Principles of credit risk management (approved by the board of directors), which include specific lending rules and principles such as acceptable collateral, collateral evaluation and haircuts, customer selection, minimum criteria for cash flow evaluation, LTV limits, the credit granting process, and reporting and auditing requirements; and
- Employee authorization (approved by Hypo's management group).

Hypo assesses the creditworthiness of potential customers through an internal grading system which for retail customers includes stress testing based on a 6%/25-year stress calculation, borrower solvency analysis, prior customer payment behavior analysis, and public credit default register checks. The borrower's solvency is assessed on monthly net income and housing costs as well as mandatory costs of living based on the household size. When calculating the collateral value, Hypo applies a haircut of 30-50%, depending on the type of collateral.

We understand that since the Finnish banking crisis in the 1990s, Hypo has not experienced credit losses from housing companies, housing companies with properties under construction, or housing investors, which demonstrates the bank's highly prudent risk approach. Its nonperforming loan (NPL) ratio stood at 0.1% as of Dec. 31, 2021, which is well below that of peers.

The FIN-FSA continues to focus strongly on ensuring strict underwriting criteria for household lending. It applies an 85% cap on loan-to-collateral ratios on new mortgage loans and a 95% cap for first-time buyers. Borrower's ability to pay the loan and handle the regular living costs is stress tested with a 6% interest rate.

Overall, we assess Hypo's lending and underwriting standards as conservative. Its pure focus on residential mortgage lending and loans to housing associations in growth centers in Finland, with low LTV ratios translates into higher asset quality compared with domestic peers.

In our opinion, there is no operational risk from the cover pool's management and loan origination that would constrain the rating on the covered bonds to the same level as our long-term ICR on Hypo.

We believe that a replacement cover pool manager would be available to manage the cover pool if the issuer were to become insolvent. We consider Finland to be an established covered bond market and we believe that the mortgage loans in Hypo's cover pool do not comprise product features that would materially limit the range of available replacement cover pool managers or servicers.

Resolution regime analysis

Hypo is domiciled in Finland, which is subject to the EU's BRRD. We assess the systemic importance for Finnish mortgage programs as very strong. Under our covered bonds criteria, this means the RRL will be the greater of (i) the ICR on Hypo, plus two notches; and (ii) the resolution counterparty rating (RCR) on the issuing bank, where applicable. Because we do not assign an RCR to Hypo, the RRL is 'a-', two notches above the ICR.

This uplift recognizes that 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.

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 market.

Our assessment of the expected jurisdictional support for Finnish mortgage programs is very strong. In addition, our sovereign rating on Finland (AA+/Stable/A-1+) does not constrain the JRL. Under our covered bonds criteria, the covered bonds therefore receive three notches of jurisdictional uplift over the RRL leading to a JRL of 'aa-'.

Collateral support analysis

Our analysis of the residential mortgage loans is based on the specific adjustments defined for Finland under our global RMBS criteria (see "Global Methodology And Assumptions: Assessing Pools Of Residential Loans," published on Jan. 25, 2019). Our analysis of the housing association loans is based under our commercial real estate criteria (CRE criteria; see "Methodology And Assumptions: Analyzing European Commercial Real Estate Collateral In European Covered Bonds," published on March 31, 2015).

We performed our analysis using loan-by-loan data provided by Hypo as of Aug. 15, 2022, and projected asset and liability cash flows provided by Hypo as of Nov. 11, 2022.

The cover pool comprises residential mortgage loans (26.48%) and housing association loans (73.52%) originated by Hypo. The cover pool has a current balance of €385.7 million. It is highly seasoned with low current LTV ratios (weighted-average current LTV of 23%). The cover pool does not include loans in arrears nor loans to borrowers with a negative credit history. 99% of loans pay a floating rate of interest and all mortgage loans are amortizing.

Under the CBA, mortgage loans are included in the cover pool for a covered bond for their total value, while compliance with the regulatory overcollateralization requirement must be based on 80% of the market value of residential properties and 60% for commercial properties. This approach differs from the MCBA, according to which mortgage loans were included in the cover pool only to a maximum amount corresponding to 70% of the property's value for residential housing loans and 60% for commercial mortgage loans.

Under the CBA, bondholders and derivative counterparties have a priority of payment right on 100% of the properties' value. We therefore determined the available overcollateralization on the entire current balance. At the same time, our determination of potential losses is also based on the entire current balance of the loans.

For the loans in the pool, our analysis estimated the foreclosure frequency and the loss severity in a 'AAA' stress scenario and, by multiplying the foreclosure frequency by the loss severity, the potential loss associated with each loan. To quantify the potential losses associated with the entire pool, we weight each loan's foreclosure frequency and loss severity by its percentage of the total pool balance. The product of the weighted-average foreclosure frequency (WAFF) and weighted-average loss severity (WALS) estimates the required loss protection, assuming all other factors remain unchanged. We assume that the probability of foreclosure is a function of both borrower and loan characteristics and will become more likely--and the realized loss on a loan more severe--as the economic environment deteriorates.

At a 'AAA' level of stress, for the combined mortgage portfolio the WAFF is 15.01% and the WALS is 5.22%. At the sub portfolio level, for the residential mortgage loans the WAFF is 3.86% and the WALS is 7.77%. For the housing association loans, the WAFF is 19.03% and the WALS is 4.30%.

The main drivers of the residential WAFF in this cover pool are low LTV ratios and high loan seasoning. Under our global RMBS criteria, we apply multiples to the base foreclosure frequency based on the effective LTV ratio. The residential loans' weighted-average effective LTV is 44.2% and is based solely on current whole loan LTVs. Given the current whole loan LTV distribution of the loans, most benefit from a reduction to their base foreclosure frequency. Further, the residential loans are highly seasoned (weighted-average seasoning of about 9.3 years). Additionally, about

91.5% is more than five years seasoned and thus benefits from a reduction to the base foreclosure frequency under our RMBS criteria. On the other hand, exposure to residential loans in the South of Finland (95.7%) exceeds our regional concentration limit of 50% and attracts a 1.2 times increase to their base foreclosure frequency of 13% on the excess above the limit.

The residential mortgage loans subportfolio contains about 9.6% equal installment mortgage loans. The maturity on these loans can extend (from origination) if the interest rate is high enough to make up for the entire installment. We believe this maturity extension mitigates an immediate payment shock on the borrowers. In addition, we note that these loans are well-seasoned with about 66% of their original balance amortized.

The main drivers behind the WALS for the residential mortgage loans in this pool are low current LTV ratios after house price indexation and market value decline assumptions. We have determined a relatively low weighted-average current LTV ratio for the residential subportfolio of 42%.

We observe continuous house prices development in Finland, with prices rising in some areas and declining in others. However, we have not observed an overheating of the real estate market, and currently our analysis considers Finnish residential properties as slightly undervalued.

The main drivers for the WAFF of the housing association loans are their low current LTVs and the high geographic concentration. The weighted-average current LTV ratio of the housing association loans is about 16.3%. Based on the LTV distribution of these loans, none of them attracts an increase to the base foreclosure frequency under our CRE criteria. However, in our view this subportfolio exhibits geographical concentration in the South of Finland (relative to the region's overall GDP contribution). In line with our CRE criteria, we have increased the base foreclosure frequency of housing association loans (17.5%) in the South of Finland by 1.1x.

Furthermore, our CRE criteria consider obligor concentration risk through the application of a largest obligor default test. To pass this test, when applying a 'AAA' stress, the available credit enhancement in the program must be at least equal to the loss related to the 10 largest obligors, as defined by the gross outstanding balance of the largest obligor loans in the cover pool. In line with our CRE criteria, we have determined a test result of 8.08%.

The below tables provide an overview on the cover pool's composition.

Table 3

Cover Pool Composition

	As of Aug. 15, 2022	
Asset type	**Value current balance (mil. €)**	**Percentage of cover pool (%)**
Residential mortgage loans (housing loans)	102.14	26.48
Housing association loans	283.54	73.52
Substitute assets	0	0
Total	385.68	100

Table 4

Key Credit Metrics

	As of Aug. 15, 2022	
	Residential Mortgage (housing) loans	**Commercial Mortgages (housing association loans)**
Average loan size (€)	103,384	589,842
Weighted-average effective LTV ratio (%)*	44.15	N/A
Weighted-average cover pool current LTV ratio (%)§	42.04	16.26
Weighted-average loan seasoning (months)†	111.6	103.06
Balance of loans in arrears (%)	0	0
Buy-to-let loans (%)	11.66	N/A
Self-employed borrowers (%)	6.62	N/A
Equal installment mortgages (%)	9.58	N/A
Credit analysis results:		
WAFF (%)	3.86	19.03
WALS (%)	7.77	4.3
Combined credit analysis results:		
WAFF (%)	**15.01**	
WALS (%)	**5.22**	
'AAA' credit risk (%)	**8.08‡**	

*The effective LTV corresponds to 100% of current indexed whole loan LTVs for the WAFF calculation. §Weighted-average current indexed LTV based on current balance. †Seasoning refers to the elapsed loan term. ‡Floored by the largest obligor default test result applicable under our CRE criteria. LTV--Loan to value. WAFF--Weighted-average foreclosure frequency. WALS--Weighted-average loss severity. N/A--Not applicable.

Table 5

Loan-To-Value Ratios

	As of Aug. 15, 2022	
Residential mortgages (housing loans, %)	**Effective whole loan LTV (%)***	**Cover pool current LTV (based on current balance, %)**
0-40	42.58	46.99
40-50	21.49	21.32
50-60	18.05	17.56
60-70	11.65	9.80
70-80	2.83	1.27
80-90	1.23	1.48
90-100	0.71	0.14
Above 100	1.45	1.43
Weighted-average LTV ratio	44.15	42.04
Commercial mortgages (housing association loans, %)		
0-40	N/A	96.61
40-50	N/A	2.44
50-60	N/A	0
60-70	N/A	0.95
70-80	N/A	0

Table 5

Loan-To-Value Ratios (cont.)

	As of Aug. 15, 2022	
Residential mortgages (housing loans, %)	**Effective whole loan LTV (%)***	**Cover pool current LTV (based on current balance, %)**
80-90	N/A	0
90-100	N/A	0
Above 100	N/A	0
Weighted-average LTV ratio	N/A	16.26

*100% of current indexed whole-loan LTV ratio. LTV--Loan-to-value. N/A--Not applicable.

Table 6

Loan Seasoning Distribution*

	As of Aug. 15, 2022	
	Residential mortgage loan seasoning (% of current residential loan balance)	**Commercial mortgage loan seasoning (% of current commercial loan balance)**
Less than 24 months	5.42	2.79
24-48	2.95	1.28
48-60	0.09	1.15
60-72	0.35	1.29
72-84	0.31	1.06
84-96	19.27	25.47
96-108	27.07	33.34
108-120	16.80	14.28
More than 120	27.73	19.33
Weighted-average loan seasoning (months)	111.6	103.06

*Seasoning refers to the elapsed loan term.

Table 7

Geographic Distribution Of Loan Assets

	As of Aug. 15, 2022	
	Percentage of residential loan balance current balance (%)	**Percentage of commercial loan balance (housing association loans, %)**
Southern Finland	95.72	87.41
Eastern Finland	0.28	0.07
Western Finland	3.65	12.10
Oulu	0.29	0.42
Lapland	0.05	0
Aland	0.00	0
Total	100	100

The results of our credit analysis including the combined portfolio's WAFF and WALS, represent inputs to our cash flow analysis. Our analysis of the covered bonds' payment structure shows that cash flows from the cover pool assets would be sufficient, at the given rating, to make timely payment of interest and ultimate principal to the covered bond on its legal final maturity.

We have modeled a €300 million inaugural covered bond with a scheduled maturity of five years and a one-year maturity extension and post swap cash flows.

We stress the cover pool's cash flows, incorporating various default patterns, default timings, and interest rate paths. We also stress cash flows under different prepayment rates, and delinquency assumptions, which we run at different points over the weighted-average life of the covered bonds.

The structure is exposed to an asset-liability maturity mismatch because the covered bonds' repayment profile is not aligned with that of the assets. Our model simulates a stressed sale of assets whenever a liquidity gap occurs in our analysis. The adjustment applied for residential and commercial mortgage assets is 425 basis points and 1000 basis points respectively, on top of the stressed interest rate at the time of the shortfall.

We also model the possibility that the spread on the mortgages compresses over time, due to defaults, prepayments, and product switches. To account for this, we reduce margins, assuming that a percentage of the higher-yielding loans exit the portfolio. We also stressed basis risk.

Our 'AAA' credit risk shows the amount of overcollateralization commensurate with our credit risk assessment. This figure is 8.08% and floored by the result of the largest obligor default test determined under our CRE criteria for the housing association loans.

Our target credit enhancement includes the additional credit enhancement that we expect is required to refinance the cover pool in a stressed environment. By applying our credit and cash flow stresses, we calculate a target credit enhancement of 15.82% below the available credit enhancement of 28.56%.

Because we consider there is an active secondary market for cover pool assets, the program can potentially achieve four notches of collateral-based uplift above the JRL. From this potential uplift, we make no deductions because Hypo's covered bond features a 12-month maturity extension, which satisfies the liquidity coverage requirement under our criteria. Furthermore, Hypo commits to maintaining an overcollateralization level commensurate with the assigned rating. Therefore, the maximum collateral uplift is four notches, allowing the covered bond to attain a 'AAA' rating.

With a JRL of 'aa-', the program requires three notches of collateral uplift to attain a 'AAA' rating. The overcollateralization commensurate with a 'AAA' rating equals 12.74%.

Resulting from the application of our counterparty risk criteria, there are no unused notches of collateral-based uplift in this program. This is because if we were to lower our long-term ICR on Hypo by one notch, we would also lower our ratings on the covered bond as per our counterparty risk criteria, all else being equal (see "Swaps").

Table 8

Collateral Uplift Metrics

	As of Nov. 11, 2022
Asset WAM (years)	8.13
Liability WAM (years)	5 (extendible 6)
Available credit enhancement	28.56
Required credit enhancement for coverage of 'AAA' credit risk (%)	8.08*

Table 8

Collateral Uplift Metrics (cont.)

	As of Nov. 11, 2022
Required credit enhancement for first notch of collateral uplift (%)	8.08*
Required credit enhancement for second notch of collateral uplift (%)	9.67
Required credit enhancement for third notch collateral uplift (%)	12.74
Target credit enhancement for maximum uplift (%)	15.82
Potential collateral-based uplift (notches)	4
Adjustment for liquidity (Y/N)	N
Adjustment for committed overcollateralization (Y/N)	N
Achievable collateral support uplift (notches)	4

*Floored by the largest obligor default test result applicable under our CRE criteria. WAM--Weighted-average maturity.

Counterparty risk

We analyze counterparty risk under our criteria (see "Counterparty Risk Framework: Methodology And Assumptions," published on March 8, 2019.

Bank account provider

Borrowers will make mortgage payments into external bank accounts, which are either in Hypo's name or in the name of its wholly owned subsidiary. Under our counterparty risk criteria, we consider the associated bank account risk as mitigated through Hypo's commitment to replace the account bank providers within 90 calendar days should their ICR drop below 'BBB'.

Swaps

The structure benefits from a liability hedge with Swedbank AB and Danske Bank A/S to hedge the risk arising from the interest mismatch from the variable interest earned on the assets and the fixed interest payable on the covered bonds.

To derive the maximum potential rating on the covered bonds under our counterparty criteria, we consider various factors, including whether the counterparty is related to the issuer, the seniority of termination payments, the replacement commitment, and the collateral posting framework.

In this case, the counterparties are unrelated to the issuer and entitled to termination payments that rank pari passu with payments on the covered bonds.

According to the swap documentation, the counterparties have committed to either replacing themselves or procure an eligible guarantee for their obligations under the swap, if the respective ICR and RCR fall below 'A-' in the case of Danske Bank, and the RCR falls below 'A-' in the case of Swedbank. Failure to do so within the specified time period is an additional termination event allowing the issuer to terminate the derivative agreement. Furthermore, if we lower our rating on a swap counterparty below 'A-', the counterparties have each committed to post collateral sufficient to cover the issuer's exposure to that counterparty, plus certain volatility risks in the swap value. We categorize the current collateral-posting framework for the counterparties in the derivative contracts as strong.

The collateral framework assessments, combined with the current RRL on Hypo ('a-') and the counterparties' replacement triggers, support a maximum potential rating of 'AAA' under our counterparty risk assessment. However, if we were to lower our long-term ICR on Hypo by one notch, we would also lower our ratings on the covered bond, all else equal. As a result, the covered bonds do not benefit from unused notches of ratings uplift.

Sovereign risk

We analyze sovereign risk according to our "Incorporating Sovereign Risk In Rating Structured Finance Securities: Methodology And Assumptions," published on Jan. 30, 2019. Under these criteria, covered bonds backed by mortgages issued in a jurisdiction that is within a monetary union that include structural coverage of refinancing needs over a 12-month period (provided by the 12-month extendible maturity profile of the soft-bullet bonds in this instance) exhibit low sensitivity to country risk. As a result, we can rate the covered bond up to five notches above the sovereign rating. Given our 'AA+' long-term rating on Finland, sovereign risk does not constrain our rating on the covered bonds.

Environmental, Social, And Governance

ESG Credit Indicators

E-1	**E-2**	E-3	E-4	E-5	S-1	**S-2**	S-3	S-4	S-5	G-1	**G-2**	G-3	G-4	G-5

ESG credit indicators provide additional disclosure and transparency at the entity level and reflect S&P Global Ratings' opinion of the influence that environmental, social, and governance factors have on our credit rating analysis. They are not a sustainability rating or an S&P Global Ratings ESG Evaluation. The extent of the influence of these factors is reflected on an alphanumerical 1-5 scale where 1 = positive, 2 = neutral, 3 = moderately negative, 4 = negative, and 5 = very negative. For more information, see our commentary "ESG Credit Indicators: Definition And Applications," published Oct. 13, 2021.

ESG factors have no material influence on our credit rating analysis of Hypo's mortgage covered bonds. The issuer currently does not offer specific mortgage products focused on environment or social factors, which could affect the credit results. The Finnish government guarantees part of the loan on certain residential mortgages but as we do not consider the guarantee timely, it does not affect the credit analysis. Hypo commits to maintain a level of overcollateralization in the program to maintain the rating on the covered bonds. Additionally, the bonds' soft-bullet repayment structure mitigates 180 days of liquidity risk. Both governance initiatives support the current ratings and the credit enhancement required for the rating.

Related Criteria

- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- Criteria | Structured Finance | General: Global Framework For Payment Structure And Cash Flow Analysis Of Structured Finance Securities, Dec. 22, 2020
- Criteria | Structured Finance | General: Counterparty Risk Framework: Methodology And Assumptions, March 8, 2019
- Criteria | Structured Finance | General: Incorporating Sovereign Risk In Rating Structured Finance Securities: Methodology And Assumptions, Jan. 30, 2019
- Criteria | Structured Finance | RMBS: Global Methodology And Assumptions: Assessing Pools Of Residential Loans, Jan. 25, 2019
- Legal Criteria: Structured Finance: Asset Isolation And Special-Purpose Entity Methodology, March 29, 2017
- Criteria | Structured Finance | Covered Bonds: Covered Bond Ratings Framework: Methodology And Assumptions, June 30, 2015
- Criteria | Structured Finance | Covered Bonds: Methodology And Assumptions: Analyzing European Commercial Real Estate Collateral In European Covered Bonds, March 31, 2015
- Criteria | Structured Finance | Covered Bonds: Covered Bonds Criteria, Dec. 9, 2014
- Criteria | Structured Finance | General: Global Derivative Agreement Criteria, June 24, 2013
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Related Research

- Mortgage Society of Finland CBA Covered Bond Program And First Issuance Assigned 'AAA' Rating; Outlook Stable, Nov. 28, 2022
- Mortgage Society of Finland CBA Covered Bond Program And First Issuance Assigned Preliminary 'AAA' Rating; Outlook Stable, Nov. 7, 2022
- Global Covered Bond Insights Q3 2022, Sept. 8, 2022
- The Mortgage Society of Finland, July 11, 2022
- ESG Credit Indicator Report Card: Covered Bonds, April 7, 2022
- Asset Price Risks: Inflated Property Values Mean Higher Loss Assumptions In European RMBS And Covered Bonds, March 21, 2022
- Norwegian And Finnish Covered Bond Market Insights 2022, Jan. 31, 2022
- S&P Global Ratings Definitions, Nov. 10, 2021
- Glossary Of Covered Bond Terms, April 27, 2018