S&P Global Ratings

RatingsDirect®

Transaction Update: Eiendomskreditt AS (Commercial Mortgage Covered Bonds Program)

Primary Credit Analyst:
Casper R Andersen, Frankfurt + 49 69 33 999 208; casper.andersen@spglobal.com

Research Contributor:
Abha A. Korde, CRISIL Global Analytical Center, an S&P affiliate, Mumbai

Table Of Contents

Transaction Update: Eiendomskreditt AS (Commercial Mortgage Covered Bonds Program)

Ratings Detail

Reference Rating Level	bbb+
Resolution Regime Uplift	+2
Systemic Importance	Very Strong
Resolution Counterparty Rating	N/A
Issuer Credit Rating	BBB-

+

Jurisdiction-Supported Rating Level	a+
Assigned Jurisdictional Support Uplift	+3
Jurisdictional Support Assessment	Very Strong
Legal Framework	Very Strong
Systemic Importance	Very Strong
Sovereign Credit Capacity	Very Strong

+

Maximum Achievable Covered Bond Rating	aaa
Collateral Support Uplift	+4
Overcollateralization Adjustment	0
Liquidity Adjustment	0
Potential Collateral Based Uplift	+4

=

Covered Bond Rating	AAA/Stable
Rating Constraints	aaa
Counterparty Risk	aaa
Country Risk	aaa

Major Rating Factors

Strengths

- The issuer commits through a public statement to maintain a level of credit enhancement commensurate with the current rating.
- The cover pool includes sufficient overcollateralization to mitigate concentration risk.
- All the covered bonds present a soft bullet profile, meaning that liquidity risk is covered.

Weaknesses

- The 10 largest obligors in the cover pool currently account for almost one quarter of the total balance.
- The small number of total obligors in the cover pool has led to the application of a small pool adjustment to mitigate the risks attached to individual loans.
- At present, the program does not benefit from any unused notches of uplift.

Outlook: Stable

S&P Global Ratings' stable outlook on Eiendomskreditt AS' commercial mortgage covered bonds reflects that on the issuer, Eiendomskreditt AS (BBB-/Stable/A-3). All else being equal, any downgrade on the issuer credit rating (ICR) on Eiendomskreditt would automatically lead to a similar rating action on the covered bonds.

Rationale

We are publishing this transaction update following our periodic review of Eiendomskreditt's mortgage covered bond program and related issuances.

Our covered bond rating 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 the legal and regulatory framework for Norwegian covered bonds, we have concluded that the assets in the cover pool are isolated from the issuer's risk of a bankruptcy or insolvency. This asset isolation allows us to assign a higher rating to the covered bonds than our long-term ICR on Eiendomskreditt.

Based on our operational risk analysis, which covered 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 bonds.

The issuer is domiciled in Norway, which has implemented a resolution regime in line with the EU's Bank Recovery and Resolution Directive (BRRD). We assess the systemic importance of covered bonds in Norway as very strong. These factors increase the likelihood that Eiendomskreditt 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. Therefore, under our covered bonds criteria, we assessed the reference rating level (RRL) as 'bbb+', two notches higher than the long-term ICR on the issuer.

Based on a very strong jurisdictional support assessment for mortgage programs in Norway, we assigned three notches of uplift from the RRL. Therefore, we assess the jurisdiction-supported rating level (JRL) at 'a+'.

We based our credit analysis on data as of Sept. 30, 2023 and cash flow analysis as of Dec. 31, 2023. The cover pool comprises Norwegian commercial real estate mortgage loans, as well as substitute assets and cash. Based on our cash flow analysis, the available credit enhancement in the program exceeds the target credit enhancement. The total collateral-based uplift is not subject to any deductions given that Eiendomskreditt has provided a public commitment to hold the level of overcollateralization to maintain the rating, and that we consider the soft bullet structure of the liabilities to cover liquidity risk for 180 days. As a result, the covered bonds are able to reach a 'AAA' rating under our covered bonds criteria.

There are currently no rating constraints to the 'AAA' ratings due to counterparty or country risks.

The stable outlook on the ratings reflects the outlook on the issuer. This means that all else being equal, a downgrade on Eiendomskreditt would automatically lead to a similar rating action on the covered bond program.

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

Program Description

Table 1

Program overview*

Jurisdiction	Norway
Year of initial rating	2014
Covered bond type	Legislation-enabled
Outstanding covered bonds (bil. NoK)	4.8
Redemption profile	Soft bullet
Underlying assets	Commercial mortgages
Jurisdictional support uplift	3
Unused notches for jurisdictional support	0
Target credit enhancement (%)	26.92
Available credit enhancement (%)	29.72
Collateral support uplift	4
Unused notches for collateral support	0
Total unused notches	0

*Based on data as of Dec. 31, 2023. NOK--Norwegian krone.

Established in 1997 in Bergen, Eiendomskreditt is a specialist mortgage provider that traditionally focuses on the Southern Norwegian commercial real estate (CRE) sector. It is owned by two investment companies (holding 30% each), 65 Norwegian savings banks (holding 38% in total)--for which Eiendomskreditt functions as a covered bond funding vehicle.

While origination occurs in close cooperation with the owner banks and through in-house channels, DnB Bank AS is the main swap and account counterparty for the covered bond program.

Since our last review, the issuer has updated the program documentation to reflect the amended Norwegian covered bond law.

Eiendomskreditt AS Commercial Mortgage Covered Bonds
Transaction Structure

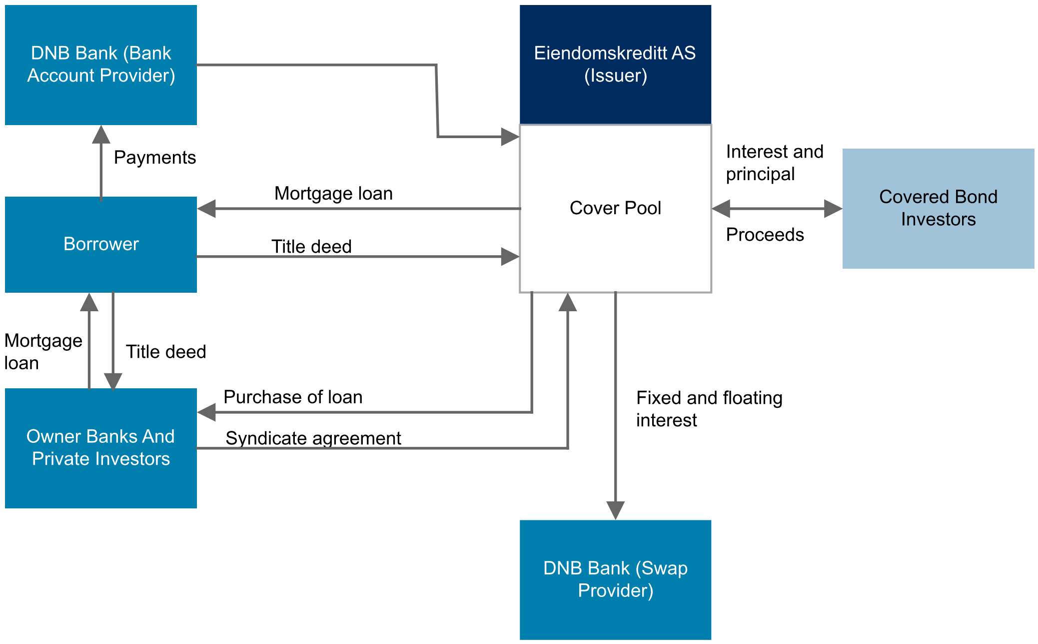

Table 2

Program participants

Role	Name	Rating	Rating dependency
Issuer	Eiendomskreditt AS	BBB-/Stable/A-3	Yes
Bank account provider	DNB Bank ASA	AA-/Stable/A-1+	Yes
Swap provider	DNB Bank ASA	AA-/Stable/A-1+	Yes

Rating Analysis

Legal and regulatory risks

We base our legal risk analysis on our legal criteria (see "Asset Isolation And Special-Purpose Entity Methodology," published on March 29, 2017).

In our opinion, the Norwegian covered bond legal framework is in line with the relevant legal requirements of our covered bond criteria. This enables us to rate the covered bonds above the long-term ICR on the issuer.

The Norwegian covered bond legislation was enacted in 2007, and was recently amended to transpose the EU Covered Bond Directive into the Norwegian legislation passed in June 2022 and effective as of July 8, 2022. The legislation complies with the European Banking Authority's Capital Requirement Directive and the Undertakings for Collective Investment in Transferable Securities. This makes Norwegian covered bonds eligible for reduced risk weighting when calculating capital adequacy.

The amendments include the introduction of a liquidity buffer, maturity extensions, loan-to-value (LTV) ratio, overcollateralization, and surveillance of the cover pool.

The Norwegian covered bond law defines the eligibility criteria for the type of assets that may and may not be included in the cover pool. The "Finanstilsynet," the Norwegian Financial Supervisory Authority (FSA), appoints an independent inspector to regularly review compliance, oversee the register for the cover pool, and ensure that the value of the cover pool always exceeds the issued covered bonds. The law also stipulates that the issuer must be a specialized credit institution and obtain a license from the Norwegian FSA.

A mortgage credit institution can include mortgage credit assets secured on residential and commercial properties within the European Economic Area (EEA) or the Organisation for Economic Co-operation and Development (OECD), and public sector credit assets granted to or guaranteed by a public body within the EEA and the OECD. It may also include supplementary assets, i.e., securities issued by eligible financial institutions within the EEA or the OECD.

According to the Norwegian covered bond law, in the event of issuer insolvency, bondholders have an exclusive preferential claim on the cover pool. Should an event occur, an administrator will be appointed to administer the cover pool and to ensure timely payments.

Although Eiendomskreditt engages in direct lending, some of the loans included in the cover pool have been originated under a syndicate agreement with an owner (agent) bank. A mortgage document and a promissory note are issued in connection with the agreement. The relationship between Eiendomskreditt and the agent bank is primarily regulated by the syndicate and the Promissory Note Act, in addition to the Financial Institutions Act, the Financial Contracts Act, and the Satisfaction of Claims Act. This relationship has been reviewed in detail, as has the syndicate agreement setup. We have concluded that there is no additional risk associated with these loans, neither in the event of default of Eiendomskreditt nor of the agent bank.

Eiendomskreditt is not a deposit-taking institution, and therefore setoff risk is not present for loans that are issued directly. However, as the agent bank does take deposits, we have reviewed the potential setoff risk associated with loans originated under the syndicate agreement. Our legal analysis has concluded that loans issued under a syndicate agreement are unlikely to present any additional setoff risk to the cover pool.

Operational and administrative risks

Eiendomskreditt is located in Bergen and has a small number of full-time employees, allowing the mortgage company to operate with low costs, which also supports the bank's earning capacity. Further oversight of Eiendomskreditt's operations is provided by the board of directors, which includes executives from the owner banks with the largest ownership share.

Eiendomskreditt's strategy is to continue to focus on distribution and cooperation with owner banks. Over the long term, the bank's objective is to maintain distribution evenly divided between its three origination channels (i.e., via owner banks, transaction market, and in-house), which we believe will strengthen the business stability of the bank. While the proportion of loan origination via the savings banks has varied over time, the business has supported

Eiendomskreditt's loan growth and contributed to a stable revenue generation. In recent years, Eiendomskreditt has successfully increased its own in-house loan generation as well as deals originated in the transaction market in cooperation with other banks and market participants.

We believe Eiendomskreditt's niche market position and focus on a single sector present a risk from both a revenue and credit risk perspective, as it could result in volatile origination volumes over time.

We consider Eiendomskreditt's underwriting process to be conservative, with LTV limits of 55% for commercial mortgage loans (less than the 60% specified in the legislation), although this limit is increased to 60% for loans backed by residential-use properties. This has allowed the mortgage company to operate with virtually no losses since it became operational in 1998. Furthermore, the lender performs its own credit analysis on all loans included in the cover pool, as well as the loans funded through the syndicate agreement.

Eiendomskreditt focuses on loans to small and midsize enterprises and expanding its customer base to reduce concentration risk. The bank has defined limits to the 10 and the 20 largest borrowers, which cannot add up to more than 30% and 50% of the cover pool, respectively.

In our opinion, there are no operational or administrative risks that would constrain the covered bond ratings to the same level as the long-term ICR.

Our analysis of operational and administrative risk follows the principles laid out in our covered bond ratings framework.

Resolution regime analysis

Eiendomksreditt is based in Norway, which has implemented a resolution regime similar to the EU's BRRD. We deem Norwegian covered bonds to have a very strong systemic importance, meaning that the program's RRL is equal to the greater of (i) the long-term ICR on the issuer, plus two notches; and (ii) the resolution counterparty rating (RCR) on the issuer. Given that the long-term ICR on the issuer is 'BBB-' and that we have not assigned an RCR, the RRL is 'bbb+'.

Jurisdictional support analysis

Under our analysis of jurisdictional support in our covered bonds criteria, we determine a JRL, which is our assessment of the creditworthiness of a covered bond program once we have considered the level of jurisdictional support, but before giving credit to the amount of collateral.

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 having to liquidate collateral assets in the open market. Our assessment of the expected jurisdictional support for Norwegian mortgage covered bond programs is very strong. Under our covered bonds criteria, this means that the program can receive up to three notches of jurisdictional uplift from the RRL. This leads to a JRL for Eiendomskreditt's mortgage covered bonds of 'a+'.

Collateral support analysis

We base our credit analysis on the loan-level data provided by the issuer as of Sept. 30, 2023. The cover pool primarily comprises Norwegian commercial mortgages, along with substitute assets and cash as of December 2023 (see table 3).

We base our credit analysis of mortgage assets on our commercial real estate criteria and our public sector criteria (see

"Methodology And Assumptions: Analyzing European Commercial Real Estate Collateral In European Covered Bonds," published on March 31, 2015 and "Methodology And Assumptions For Assessing Portfolios Of International Public Sector And Other Debt Obligations Backing Covered Bonds And Structured Finance Securities," published on Dec. 9, 2014).

Under the CRE criteria, typically, a smaller cover pool size attracts a credit enhancement adjustment that is calculated, using a formula, to reflect the greater risk from a higher borrower concentration. The default frequency for the cover pool is then based on an adjustment factor, in the same way as in our RMBS criteria, if the pool contains more than 150 loans but less than 250.

The current cover pool comprises less than 250 loans as of Sept. 30, 2023 and since we do not expect an immediate increase in the number of loans, we apply the small pool adjustment. We assess the credit quality of a typical mortgage cover pool by estimating the credit risk associated with each loan in the pool. We then calculate the aggregate risk to assess the cover pool's overall credit quality. In order 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 weighted-average foreclosure frequency (WAFF) and weighted-average loss severity (WALS) estimate the required loss protection, assuming all other factors remain unchanged.

Compared to our previous credit analysis, as of Sept. 30, 2022, the number of loans have decreased and the application of the small pool adjustment has further increased the expected foreclosure frequency to 49.12% from 42.85%. The expected loss given default (WALS) has increased to 47.85% from 43.99%.

The increase in the WAFF reflects the lower number of unrelated loans in the cover pool and the resulting application of the small pool adjustment, which we apply if a pool is not sufficiently granular, and the risks attached to individual loans may not be mitigated at the pool level.

The WALS has increased due to higher current LTV ratios marginally offset by a reduced weighted-average market value decline, as a result of increasing investment properties which attracts a lower value decline assumption than operational properties, according to our criteria.

Table 3

Cover pool composition

	--Sept. 30, 2023--		--Sept. 30, 2022--	
Asset type	**Value (mil. NOK)**	**Percentage of cover pool**	**Value (mil. NOK)**	**Percentage of cover pool**
Commercial mortgages	5430.5	87.20%	5517.13	89.32
Substitute assets	315	5.06%	242	3.92
Cash	234.02	3.76%	418	6.77
Total	6227.81		6177.13	

NOK--Norwegian krone.

Table 4

Commercial loans by property type

	Percentage of cover pool	
Property type	Sept. 30, 2023	Sept. 30, 2022

Table 4

Commercial loans by property type (cont.)		
Mixed commercial*	70.12	66.16
Housing association	3.51	3.76
Private rental/multifamily	10.32	9.71
Office	13.37	16.42
Industrial/warehouse	2.57	3.86
Other	0.11	0.08
Total mortgages	100	100

*We have reclassified the properties reported as mixed-commercial based on additional information received by the issuer.

Table 5

Key credit metrics		
	Sept. 30, 2023	**Sept. 30, 2022**
Weighted-average loan-to-value ratio (%)	45.62	42.95
Arrears above 30 days (%)	0	0
Credit analysis results:		
Weighted-average foreclosure frequency (%)	49.12	42.85
Weighted-average loss severity (%)	47.85	43.99

Table 6

LTV ratios		
	Percentage of cover pool	
(%)	**Sept. 30, 2023**	**Sept. 30, 2022**
0-40	23.09	32.62
40-60	76.91	67.38
60-70	0	0
Above 70	0	0
Weighted-average LTV ratios	45.62	42.95

LTV--Loan to value.

Table 7

Geographic distribution of loan assets		
	Percentage of cover pool	
Top five concentrations	**Sept. 30, 2023**	**Sept. 30, 2022**
East	53.85	55.51
West	30.74	31.88
North	3.26	3.24
South	4.93	4.31
Trondelag	7.22	5.06
Total	100	100

Table 8

Collateral uplift metrics

	Dec. 31, 2023	Sept. 30, 2022
Asset WAM (years)	4.68	5.63
Liability WAM (years)	3.81	4.22
Available credit enhancement	29.72	24.04
AAA credit risk (%)	25.4	18.38
Credit enhancement commensurate with first notch of collateral uplift (%)	25.78	19.14
Credit enhancement commensurate with second notch of collateral uplift (%)	26.16	19.9
Credit enhancement commensurate with third notch of collateral uplift (%)	26.54	20.65
Target credit enhancement for maximum uplift (%)	26.92	21.41
Largest obligor test (%)	15.11	14.2
Potential collateral-based uplift (notches)	4	4
Adjustment for liquidity (Y/N)	N	N
Adjustment for committed overcollateralization (Y/N)	N	N
Collateral support uplift (notches)	4	4

WAM--Weighted-average maturity.

Combining our credit and cash flow stresses, we calculate a target credit enhancement as of December 2023 of 26.92%, which exceeds the target credit enhancement of 21.41%. The results reflect the higher expected loss assumption due to the application of the small pool adjustment and a lower cash holding.

Under our criteria, for cover pools backed by commercial real estate collateral, we perform a largest obligor test. We define the largest obligor test as the assessment of the covered bonds' ability to withstand the default of a minimum number of the largest obligor exposures in the cover pool with a fixed recovery rate. The largest obligor test result is 15.11%, and does not constitute a floor to the credit enhancement level commensurate with a 'AAA' rating.

According to our covered bonds criteria, the maximum potential collateral-based uplift on a covered bond program above the JRL is four notches. We consider liquidity risk to be mitigated by the fact that all the bonds present one-year extendable maturities. Moreover, the issuer published a statement committing to a maintain a level of credit enhancement commensurate with the current rating. As a result, we do not make any adjustments to the four notches of uplift based on collateral support.

The available credit enhancement of 29.72% exceeds the target credit enhancement of 26.92%. With a JRL of 'a+' and four notches of collateral-based uplift with no deductions, the covered bonds can achieve a 'AAA' rating.

Counterparty risk

We have identified several counterparty risks to which the covered bonds are exposed. However, these are either mitigated through structural mechanisms, or we have considered them in our modeling. Therefore, they do not constrain our ratings on the covered bonds.

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

Account provider

DNB Bank ASA is the program's bank account provider. Under the account agreement, if DNB Bank is downgraded below 'A/A-1', it commits to replace itself with a bank rated at least 'A/A-1' or to obtain an appropriately rated guarantor. The remedy period is 60 calendar days. These mitigants support the 'AAA' rating.

Swaps

The program features a number of cover pool interest-rate swaps with a single counterparty, DNB Bank. The swaps in place cover interest rate mismatches between the mortgage loans in the cover pool and the payments due to covered bondholders.

Governing the swaps is an agreement that we reviewed under our counterparty risk criteria. There are rating triggers in place: if DNB Bank is downgraded below 'A/A-1,' it will start posting collateral in 10 calendar days, and if it is downgraded below 'A-/A-2,' it will replace itself in 60 calendar days. We deem the collateral posting framework outlined in the documentation to be strong.

To determine the maximum supported rating under the swap agreement, we interpolate the replacement trigger and the issuer's RRL. When doing so, we consider whether termination costs are senior or subordinated (or otherwise mitigated).

We understand that termination cost ranks are not subordinated but we believe the potential liquidity risk posed by termination costs is mitigated. The potential termination costs of the swaps currently registered in the cover pool is lower than the buffer between the program's available credit enhancement and the credit enhancement commensurate with the rating. Based on the nature of the swaps and historical evidence, we expect termination costs to be lower than the program's unused credit enhancement over time, which mitigates the risk in our view.

In light of this assessment, the risk posed by the swaps does not constrain the rating. Should potential termination costs exceed the transaction's unused credit enhancement, the maximum supported rating under our counterparty criteria would be lower.

Sovereign risk

We base our analysis of sovereign risk on the application of "Incorporating Sovereign Risk In Rating Structured Finance Securities: Methodology And Assumptions," published on Jan. 30, 2019. Under our criteria, this transaction displays moderate sensitivity to country risk and can be rated up to four notches above the sovereign. As the covered bonds are issued in a country that is not a member of a monetary union, and the program includes structural coverage of refinancing needs over a 12-month period (soft bullet covered bonds), the program can be rated up to four notches above the long-term sovereign rating. As Norway is currently rated 'AAA', country risk does not constrain the ratings on the program and its related issuances.

Environmental, Social, And Governance

Environmental, social, and governance credit considerations influence the credit quality of Eiendomskreditt's cover pool in a broadly similar way to other Norwegian issuers. The bank has introduced a green mortgage product, which offers borrowers a slightly lower margin and longer maturities and expected lower risk for the issuer. This compliments the issuer's green bond framework aligned to its green bond principles and internal guidelines for green lending. Eiendomskreditt has issued Norwegian krone (NOK) 650 million of green covered bonds and the issuer considers approximately NOK881 million of the cover pool as green mortgages. We will continue to monitor the impact of the green bond framework, but currently do not believe our credit analysis is affected by specific environment-related factors. To manage concentration risk, the issuer has implemented rules aimed at keeping the concentration of the largest borrowers below a certain threshold. All outstanding covered bonds present soft bullet maturities, hence we do not adjust the potential collateral-based uplift due to liquidity risk. Additionally, the program features a public commitment to maintain a level of assets in the cover pool commensurate with the current rating. Therefore, it can achieve all four notches of collateral-based uplift.

Related Criteria

- Global Framework For Payment Structure And Cash Flow Analysis Of Structured Finance Securities, Dec. 22, 2020
- Counterparty Risk Framework: Methodology And Assumptions, March 8, 2019
- Incorporating Sovereign Risk In Rating Structured Finance Securities: Methodology And Assumptions, Jan. 30, 2019
- Asset Isolation And Special-Purpose Entity Methodology, March 29, 2017
- Covered Bond Ratings Framework: Methodology And Assumptions, June 30, 2015
- Methodology And Assumptions: Analyzing European Commercial Real Estate Collateral In European Covered Bonds, March 31, 2015
- Covered Bonds Criteria, Dec. 9, 2014
- Methodology And Assumptions For Assessing Portfolios Of International Public Sector And Other Debt Obligations Backing Covered Bonds And Structured Finance Securities, Dec. 9, 2014
- Global Derivative Agreement Criteria, June 24, 2013
- Principles Of Credit Ratings, Feb. 16, 2011

Related Research

- Global Covered Bond Insights Q1 2024, Dec. 15, 2023
- Covered Bonds Outlook 2024: Stability Amid Turbulence, Dec. 13, 2023
- Eiendomskreditt AS, Dec. 11, 2023
- Sector And Industry Variables | Criteria | Structured Finance | Covered Bonds: Covered Bonds Criteria, Nov. 23, 2022
- Norway, Sept. 11, 2023
- Banking Industry Country Risk Assessment: Norway, Nov. 27, 2023
- Glossary Of Covered Bond Terms, April 27, 2018