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Oberbank AG's Mortgage Covered Bond Program And Related Issuances Rated 'AAA'; Outlook Stable

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OVERVIEW

- We have assigned our 'AAA' ratings to Oberbank's mortgage covered bonds.
- As of Sept. 30, 2016, the cover pool comprises residential and commercial mortgages in Austria.
- Our ratings reflect our review of the program under our covered bonds criteria and an available credit enhancement commensurate with a 'AAA' rating.
- The stable outlook reflects the availability of unused collateral-based uplift.

MADRID (S&P Global Ratings) March 20, 2017--S&P Global Ratings today assigned its 'AAA' credit ratings to the mortgage covered bond program and related issuances ("hypothekarisch fundierte Bankschuldverschreibungen") issued by Austria-based Oberbank AG. The outlook is stable.

Oberbank issues the mortgage covered bonds under its €725 million debt issuance program or using stand-alone documentation. The covered bonds constitute direct, unconditional, secured, and unsubordinated obligations of the issuer, and rank pari passu among themselves.

As of Sept. 30, 2016, the outstanding mortgage covered bonds amounted to €199

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million and were backed by a €790.4 million cover pool register, in accordance with the Austrian law on secured bank bonds ("Gesetz betreffend fundierte Bankschuldverschreibungen"). As of Sept. 30, 2016, the cover pool comprised solely Austrian residential and commercial mortgage loans. Going forward, the issuer also plans to add German residential and commercial mortgages, to a limited extent.

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

From our analysis of Oberbank's covered bond program and the Austrian legislative covered bond framework, we have concluded that the assets in the cover pool are isolated from the risk of the issuer's insolvency.

In accordance with our covered bonds criteria, we have determined the issuer's reference rating level (RRL), and attributed notches of uplift from this level through our determination of jurisdictional support and collateral-based support in order to determine the maximum achievable covered bond rating.

Accordingly, the RRL can be two notches above the long-term issuer credit rating, excluding any uplift that reflects the likelihood of extraordinary government support. In determining these two notches, we consider the following factors:

- The issuer is domiciled in Austria, which is subject to the EU's Bank Recovery And Resolution Directive (BRRD); and
- We assess Austrian mortgage covered bonds as having very strong systemic importance.

We incorporate the likelihood of the covered bonds receiving jurisdictional support to determine the jurisdiction-supported rating level (JRL). Our assessment of jurisdictional support for mortgage covered bonds in Austria is very strong, therefore the mortgage covered bonds can receive up to three notches of jurisdictional uplift above the RRL.

Our criteria allow for up to four potential notches of collateral-based uplift above the JRL. From these potential four notches we deduct two notches: one for the lack of a commitment to maintain at least six months of liquidity and one because the overcollateralization is uncommitted.

When applicable, we cap our ratings on mortgage covered bonds under our structured finance ratings above the sovereign criteria (RAS criteria; see " Criteria - Structured Finance - General: Ratings Above The Sovereign - Structured Finance: Methodology And Assumptions," published on Aug. 8, 2016). Given our current ratings on Austria (AA+/Stable/A-1+), the maximum rating on the covered bond program is 'AAA'. Accordingly, we classify the sensitivity of mortgages to country risk as moderate. Combined with Austria's sovereign rating, this allows for four notches of uplift for the covered bond ratings above the 'AA+' long-term rating on Austria.

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

The stable outlook reflects the availability of unused collateral-based uplift, which could protect the ratings on the covered bonds should the credit quality of the issuer deteriorate.

CREDIT ANALYSIS

We have analyzed the credit quality of the assets in covered bond program by conducting a loan-by-loan analysis of the mortgage pool. We estimated the foreclosure frequency and the loss severity and, by multiplying these two elements together, calculated the potential loss associated with each loan. To quantify the potential losses associated with the entire pool, we calculated a weighted-average foreclosure frequency (WAFF) and a weighted-average loss severity (WALS) at each rating level. In the absence of any additional factors, we estimate the required loss protection from the product of these two variables. We assume that the probability of foreclosure is a function of both borrower and loan characteristics and to become more likely (and the realized loss on a loan more severe) as the economy deteriorates.

We analyze the commercial mortgage collateral backing the covered bonds by applying our assumptions in the criteria "Criteria - Structured Finance - Covered Bonds: Methodology And Assumptions: Analyzing European Commercial Real Estate Collateral In European Covered Bonds," published on March 31, 2015.

We analyze the residential mortgages in this covered bond program under our " General Criteria: Principles Of Credit Ratings". Specifically, we apply the methodology and assumptions for U.K. residential mortgage-backed securities described in our European residential loans criteria (see "Criteria - Structured Finance - General: Methodology And Assumptions: Assessing Pools Of European Residential Loans," published on Dec. 23, 2016), and incorporate the following adjustments:

- 'AAA' base foreclosure frequency: 13%;
- 'AA' base foreclosure frequency: 9%;
- 'A' base foreclosure frequency: 6.5%;
- 'BBB' base foreclosure frequency: 5%;
- 'AAA' market value decline 46%;
- 'AA' market value decline: 43%;
- 'A' market value decline: 37%;
- 'BBB' market value decline: 33%; and
- Jumbo loan valuation limit: €500,000.

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In addition, we apply a geographic concentration adjustment, by multiplying the base foreclosure frequency by 1.05x where the population of an Austrian state that is exposed to a cover pool exceeds double the population distribution.

At the postcode level, if more than 10% of the assets are in a particular postcode, we would adjust the base foreclosure frequency by 1.5x.

The criteria applicable to our cash flow analysis for this covered bond program are stated in our European residential loans criteria.

POTENTIAL EFFECTS OF PROPOSED CRITERIA CHANGES

Our ratings are based on our criteria, including those set out in "Criteria - Structured Finance - General: Methodology And Assumptions: Assessing Pools Of European Residential Loans," published on Dec. 23, 2016. We also apply our " General Criteria: Principles Of Credit Ratings" to analyze the residential mortgages in this covered bond program.

On June 27, 2016, we published "Request For Comment: Methodology And Assumptions For Analyzing Pools Of Austrian, Danish, And Swedish Residential Loans".

As a result of this request for comment, the criteria which we apply in rating these Austrian covered bonds in the future may differ from the criteria we are currently applying. This may affect the ratings on the outstanding covered bonds issued by Oberbank. Until we adopt new criteria, we will continue to rate and surveil these covered bonds using our existing criteria (see "Related Criteria").

RELATED CRITERIA

- Criteria - Structured Finance - General: Methodology And Assumptions: Assessing Pools Of European Residential Loans, Dec. 23, 2016
- Criteria - Structured Finance - General: Ratings Above The Sovereign - Structured Finance: Methodology And Assumptions, Aug. 08, 2016
- Criteria - Structured Finance - Covered Bonds: Counterparty Risk Analysis In Covered Bonds, Dec. 21, 2015
- 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. 09, 2014

- Legal Criteria: Europe Asset Isolation And Special-Purpose Entity Criteria--Structured Finance, Sept. 13, 2013
- Criteria - Structured Finance - General: Counterparty Risk Framework Methodology And Assumptions, June 25, 2013
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011
- General Criteria: Methodology: Credit Stability Criteria, May 03, 2010
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009

RELATED RESEARCH

- Global Covered Bond Characteristics And Rating Summary Q4 2016, Jan. 13, 2017
- Republic of Austria 'AA+/A-1+' Ratings Affirmed; Outlook Stable, Sept. 16, 2016
- Assessments For Target Asset Spreads According To Our Covered Bonds Criteria, Aug. 15, 2016
- Assessments For Jurisdictional Support According To Our Covered Bonds Criteria, July 20, 2016
- Request For Comment: Methodology And Assumptions For Analyzing Pools Of Austrian, Danish, And Swedish Residential Loans, June 27, 2016
- Covered Bond Monitor: Technical Note, Aug. 12, 2015