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Transaction Update: Bank of Aland PLC (Category FIN Mortgage Covered Bonds)

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Ratings Detail

Reference Rating Level	a-	+	Jurisdictional-Supported Rating Level	aa-	+	Maximum Achievable Covered Bond Rating	aaa	=	Covered Bond Rating	
Resolution Regime Uplift	+2		Jurisdictional Support Uplift	+3		Collateral Support Uplift	+4		AAA/Stable	
Systemic Importance	Very Strong		Jurisdictional Support Assessment	Very Strong		Overcollateralization Adjustment	0		Rating Constraints	aaa
Adjusted Issuer Credit Rating	bbb		Legal Framework	Very Strong		Liquidity Adjustment	0		Counterparty Risk	aaa
GRE And Sovereign Support	0		Systemic Importance	Very Strong		Available Credit Enhancement	+4		Country Risk	aaa
Issuer Credit Rating	BBB		Sovereign Credit Capacity	Very Strong						

Major Rating Factors

Strengths

- High level of available credit enhancement compared with target credit enhancement.
- One unused notch of collateral based-uplift.
- Well-seasoned residential mortgage loans.

Weaknesses

- Commingling and bank account risk that is not addressed either structurally or by the legal framework.

Outlook: Stable

The stable outlook on Standard & Poor's Ratings Services rating on Finland-based Bank of Aland's Category FIN mortgage covered bonds reflects that we would not automatically lower the ratings on the covered bonds if we were to lower the long-term rating on Bank of Aland by one notch. The program is eligible for four notches of uplift above the reference rating level (RRL), but currently requires only three notches to achieve a 'AAA' rating.

Rationale

On May 5, 2015, we affirmed our ratings on Bank of Aland PLC's Finnish mortgage covered bond program and related issuances ("Ratings On Finland-Based Bank of Aland's Category FIN Covered Bonds Raised To 'AAA' On New Criteria; Outlook Stable," published on RatingsDirect). Our rating process follows the methodology and assumptions outlined in our covered bonds criteria.

From our analysis of the program, we have concluded that the assets in the cover pool are isolated from the risk of a bankruptcy or the insolvency of the issuer. This asset isolation allows us to assign a higher rating to the covered bonds than our long-term issuer credit rating (ICR) on Bank of Aland.

The cover pool comprises Finnish residential mortgages, as well as substitute assets.

We consider the mortgage operations of the issuer to be prudent, and we believe satisfactory procedures are in place to support our ratings on the covered bonds.

In accordance with our covered bonds criteria, we include uplift in the ratings on the covered bonds from the adjusted ICR, taking into account a resolution regime that is favorable to covered bonds (we consider covered bonds' systemic importance to be very strong; see "Resolution regime analysis"). We assess the RRL at 'a-', including two notches of uplift above the ICR for our view of the resolution regime. We assess the jurisdiction-supported rating level (JRL) at 'aa-', three notches above the RRL owing to our assessment of jurisdictional support as very strong (see "Jurisdictional support analysis"). In addition, the covered bonds could benefit from up to four notches of collateral-based uplift above the JRL. This leaves one unused notch of uplift. The issuer has publicly stated a commitment to cover the overcollateralization at the 'AAA' level or four notches of collateral-based uplift and six months of liquidity.

As of March 31, 2015, the cover pool comprised €992.1 million of Finnish residential and commercial mortgages, as well as €168.3 million in substitute assets. Our measure of the portfolio's weighted-average foreclosure frequency (WAFF; the level of defaults) for the mortgages is 21.22%. The weighted-average loss severity (WALS; estimated losses given default) is 13.24%, based on a 'AAA' stress level, calculated according to our criteria (see "Methodology And Assumptions For Analyzing Mortgage Collateral In Finnish And Norwegian Covered Bonds," published on Dec. 10, 2014, on RatingsDirect). The available credit enhancement of 63.07% is above the 26.89% credit enhancement commensurate with a 'AAA' rating. With a JRL of 'aa-', the program only needs to mitigate credit risk at the 'AAA' level (the expected losses incurred by the cover pool in a 'AAA' stress scenario) and 75% of the refinancing costs (the additional collateral required to raise funds against assets to repay maturing covered bonds).

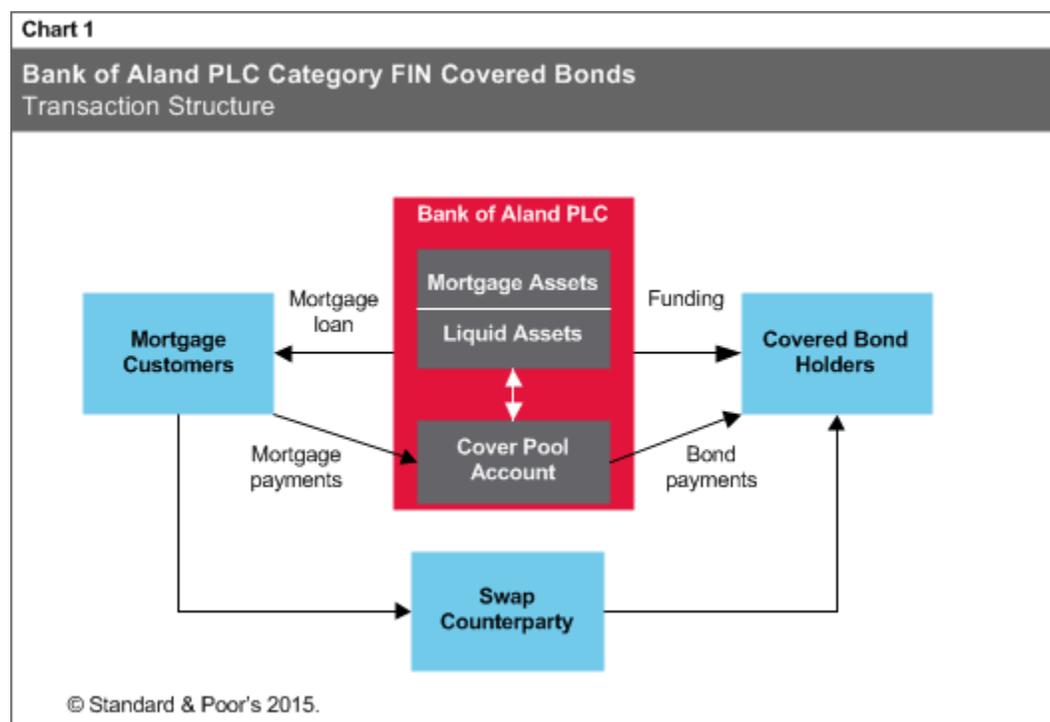
Lastly, the ratings on the program and related issuances are not constrained by legal, operational, or counterparty risks.

Program Description

Table 1

Program Overview*	
Jurisdiction	Finland
Year of first issuance	2012
Covered bond type	Legislation-enabled
Outstanding covered bonds (mil. €)	711.5
Redemption profile	Hard bullet
Underlying assets	Residential mortgages
Jurisdictional support uplift	3
Unused notches for jurisdictional support	0
Target credit enhancement (%)	26.89
Available credit enhancement (%)	29.33
Collateral support uplift	4
Unused notches for collateral support	1
Total unused notches	1

*Based on data as of March 31, 2015.



Bank of Aland is a relatively small bank with a strong presence in the Finnish region of the Aland Islands. The bank's operations in Finland are concentrated in the Aland Islands and a branch network in southern and western Finland. The bank focuses on offering private banking to high-net-worth clients, complemented by operations in Sweden.

Under its €2 billion covered bond program, Bank of Aland maintains two separate cover pools, each backing a separate set of covered bonds. The "Category FIN" covered bonds have a preferential claim on a pool of Finnish mortgage assets, while the "Category SWE" covered bonds are collateralized by a separate pool of Swedish mortgages.

Both sets of covered bonds are issued under the terms of Finnish Covered Bond Act. This transaction update covers the Category FIN covered bonds only.

The covered bonds constitute a senior secured unsubordinated obligation and rank pari passu with other obligations secured by the same cover register. In the event of bankruptcy, the pools would be separate and independent of each other.

Table 2

Program Participants			
Role	Name	Rating	Rating dependency
Issuer	Bank of Aland PLC	BBB/Negative/A-3	Yes
Arranger	Bank of Aland PLC	BBB/Negative/A-3	No
Originator	Bank of Aland PLC	BBB/Negative/A-3	No
Servicer	Bank of Aland PLC	BBB/Negative/A-3	No
Bank account provider	Bank of Aland PLC	BBB/Negative/A-3	No
Bank account provider (liquid assets)	Nordea Bank PLC	AA-/Negative/A-1+	No
Swap account provider	Skandinaviska Enskilda Banken AB	A+/Negative/A-1	Yes
Swap account provider	Swedbank Mortgage AB	A+/Stable/A-1	Yes

Rating Analysis

Legal and regulatory risks

In our legal risk analysis, we applied our European legal criteria (see "Europe Asset Isolation And Special-Purpose Entity Criteria--Structured Finance," published on Sept. 13, 2013). The Finnish Covered Bond Act of 2010 sets out the legal framework for issuing Finnish covered bonds. In our opinion, the Finnish 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.

If the issuer defaults, bondholders can initiate regular insolvency proceedings. In addition, under the Covered Bond Act, they have a preferential claim to a cover pool. The cover pool can comprise residential mortgage loans, commercial mortgage loans, public-sector loans, and substitute assets from European Economic Area countries.

Under the legal framework, the cover pool's assets must be registered in the issuer's cover pool, in order to be isolated from the issuer's other assets in the event of insolvency. The issuer must report the information in the register to the Finnish regulator monthly. The register also includes the counterparties to derivative contracts, which must be able to survive the issuer's insolvency.

If the issuer were to become insolvent, the Finnish regulator would appoint a special cover pool administrator to supervise the covered bondholders' interests. If necessary, the administrator can sell assets or accelerate the payment of the covered bonds if it considers this to be in the bondholders' best interests, subject to Finnish regulatory approval.

To facilitate liquidity management, up to 20% of a mortgage cover pool can include substitute assets, such as state, municipal, or other public-sector/financial entities.

Under the Covered Bond Act, the issuer's bankruptcy would not result in the covered bonds' early redemption, or the suspension of payments to bondholders. Accordingly, we rate the covered bonds on the basis of their legal final maturity.

Operational and administrative risks

In June 2015, we conducted a review of the issuer's origination, underwriting, collection, and default management procedures for the cover pool assets. We also reviewed the cover pool management and administration and have not observed any major changes or new risks arising. We consider that the issuer actively manages the cover pool and has strict underwriting and loan management policies.

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

Resolution regime analysis

As part of our covered bonds criteria, our analysis considers any resolution regime in place in Finland to determine the RRL. As Finland is part of the EU and is required to implement the EU's Bank Recovery And Resolution Directive (BRRD), this analysis considers the support provided by its eventual adoption. As such, we assign two notches of uplift from the adjusted ICR, resulting in an RRL of 'a-'.

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 from the liquidation of collateral assets in the open market. Our assessment of the expected jurisdictional support for Finnish mortgage covered bond programs is "very strong" (see "Assessments For Jurisdictional Support According To Our Covered Bond Criteria," published on Dec. 22, 2014). 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 issuer's mortgage covered bonds of 'aa-'.

Collateral support analysis

We base our analysis on the loan-level data provided by the issuer as of March 31, 2015. The cover pool primarily comprises Finnish residential mortgages (85.49%). The remainder consists of substitute assets (14.51%).

Since May 2014, the WAFF has increased to 21.22% from 19.25% and the WALs has increased to 13.24% from 11.26%.

The increase in WAFF and WALs is mainly the result of the application of our new criteria for analyzing mortgage collateral in Finnish covered bonds. In contrast to the previous analysis, we use only the original valuation under the current criteria. The original LTV (OLTV) of 73.70% in the current analysis compares unfavorably to the current LTV of 60.69% used in the previous analysis.

The substitute assets included in the cover pool consist mainly of covered bonds as well as sovereign debt and we

consider this sub-pool as having low granularity, based on our public sector criteria (see "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. Therefore, in assessing portfolio credit risk under a 'AAA' stress scenario, we assume that all assets with an asset rating input below 'AAA' (currently 52.41% of the sub-pool) are in default. The weighted-average recovery rate is 29.26%.

Table 3

Cover Pool Composition				
	--March 31, 2015--		--March 31, 2014--	
Asset type	Value (mil. €)	Percentage of cover pool (%)	Value (mil. €)	Percentage of cover pool (%)
Residential Mortgages	991.84	85.49	894.09	87.99
Substitute assets	168.34	14.51	122.04	12.01
Total	1,160.18	100	1,016.12	100

Table 4

Key Credit Metrics		
	As of March 31, 2015	As of March 31, 2014
Average loan size (€)	70,357	114,832
Weighted-average LTV ratio (%)	73.70	60.69
Weighted-average loan seasoning (months)*	56.39	37.79
Balance of loans in arrears (%)	1.79	1.47
Buy-to-let loans (%)	9.36	9.17
Credit analysis results:		
Weighted-average foreclosure frequency (WAFF; %)	21.22	19.25
Weighted-average loss severity (WALS; %)	13.24	11.26
AAA credit risk (%)	19.56	10.5
Country averages:		
WAFF (%)	N/A	11.4
WALS (%)	N/A	6.04
AAA credit risk (%)	N/A	2.86

*Seasoning refers to the elapsed loan term. N/A--Not available.

Table 5

Covered Pool Assets By Loan Size		
	As of March 31, 2015	As of March 31, 2014
(€)	--Percentage of cover pool (%)--	
0-100,000	19.06	24.23
100,000-200,000	30.50	31.69
200,000-300,000	19.04	17.57
300,000-400,000	9.68	7.73
400,000-500,000	6.03	4.28
500,000-600,000	2.67	1.84
Above 600,000	13.01	12.67

Table 6

LTV Ratios		
	As of March 31, 2015	As of March 31, 2014
(%)	--Percentage of cover pool (%)--	
0-30	13.63	8.35
30-60	50.85	35.94
0 - 60	64.48	44.29
60 - 70	22.47	21.71
70 - 80	12.90	17.14
80-90	0.05	10.47
90-100	0.03	6.38
Above 100	0.06	0.00
Total Above 80	0.14	16.85

Table 7

Loan Seasoning Distribution*		
	As of March 31, 2015	As of March 31, 2014
	--Percentage of cover pool (%)--	
Less than 18 months	17.06	35.58
18-60 months	44.40	43.12
Above 60 months	38.54	21.30
Weighted-average loan seasoning (months)	56	37

*Seasoning refers to the elapsed loan term.

Table 8

Geographic Distribution Of Loan Assets		
	As of March 31, 2015	As of March 31, 2014
Region	--Percentage of cover pool (%)--	
Southern Finland	49.83	51.30
Western Finland	30.30	29.08
Åland	19.50	19.32
Eastern Finland	0.20	0.11
Lapland	0.11	0.12
Oulu (A)	0.06	0.06
Oulu (B)	0	0

Table 9

Collateral Uplift Metrics		
	As of March 31, 2015	As of March 31, 2014
Asset WAM (years)	5.73	6.85
Liability WAM (years)	3.38	3.96
Available credit enhancement	63.07	52.2
Required credit enhancement for first notch of collateral uplift (%)	22.00	N/A
Required credit enhancement for second notch of collateral uplift (%)	24.45	N/A

Table 9

Collateral Uplift Metrics (cont.)		
Required credit enhancement for third notch Collateral Uplift (%)	26.89	N/A
Target credit enhancement for maximum uplift (%)	29.33	19.12
Potential collateral-based uplift (notches)	4	N/A
Adjustment for liquidity (Y/N)	N	N/A
Adjustment for committed overcollateralization (Y/N)	N	N/A
Collateral support uplift (notches)	3	N/A

WAM--Weighted-average maturity. N/A--Not applicable.

According to our covered bonds criteria, the maximum potential collateral-based uplift on a covered bond program above the JRL is four notches. We then look to make adjustments to the maximum collateral-based uplift by reviewing the coverage of six months of liquidity and the level of commitment for the overcollateralization. The issuer has a liquidity commitment and overcollateralization commitment published on its website that is in line with our criteria. Therefore, we do not adjust the collateral support uplift for liquidity or committed overcollateralization.

By applying our credit and cash flow stresses, we calculate a target credit enhancement of 29.33%. This is above the 19.12% target credit enhancement in March 2014. The increase is the result of the higher WAFF and WALs for mortgage assets and our more severe default and recovery assumptions for substitute assets.

Given the JRL of 'aa-', overcollateralization that covers 'AAA' credit risk and 75% of refinancing costs is required to achieve the maximum rating. We calculate the credit enhancement needed to cover 'AAA' credit risk and 75% of refinancing costs at 26.89%. This is lower than the available credit enhancement of 63.07%.

Counterparty risk

We have identified several potential counterparty risks to which the covered bonds are exposed. However, these are either mitigated through structural mechanisms, or we have taken them into account in our modelling. Accordingly, we consider that they do not constrain our ratings on the covered bonds.

We have identified account bank and commingling risk as a relevant counterparty risk that is not addressed structurally or by law. We have considered the frequency of our access to information on the program's available credit enhancement to estimate the size of the account bank and commingling risk--currently 11.05% of the additional credit enhancement--and take the view that overcollateralization sufficiently mitigates this risk.

The swaps in place cover interest rate and currency mismatches between the mortgage loans in the cover pool and the payments due to covered bondholders. Swap agreements in line with our criteria govern the program's asset swaps and liability swaps, which provide various replacement options if the swap providers are downgraded below 'A-'. We factor the remaining interest rate risk into our cash flow calculation.

Accordingly, counterparty risk does not constrain the maximum achievable ratings on the covered bonds.

Country risk

When applicable, we cap our ratings on mortgage covered bond programs under our updated criteria for rating single-jurisdiction securitizations above the sovereign foreign currency rating (RAS criteria; see "Methodology And

Assumptions For Ratings Above The Sovereign--Single-Jurisdiction Structured Finance," published on Sept. 19, 2014). Given the current ratings on Finland (AA+/Stable/A-1+), our rating on the program is not limited by the RAS criteria. We assess the program's sensitivity to country risk as "moderate." Due to the absence of one-year liquidity coverage, we can rate the covered bonds three notches above the rating of Finland.

Related Criteria And Research

Related Criteria

- Methodology And Assumptions For Analyzing Mortgage Collateral In Finnish And Norwegian Covered Bonds, Dec. 10, 2014
- Covered Bonds Criteria, Dec. 9, 2014
- Updated Cash Flow Assumptions For Modeling Certain Covered Bonds, 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
- Methodology And Assumptions For Ratings Above The Sovereign--Single-Jurisdiction Structured Finance, Sept. 19, 2014
- Europe Asset Isolation And Special-Purpose Entity Criteria--Structured Finance, Sept. 13, 2013
- Counterparty Risk Framework Methodology And Assumptions, June 25, 2013
- Covered Bond Ratings Framework: Methodology And Assumptions, June 26, 2012
- Understanding Standard & Poor's Rating Definitions, June 3, 2009
- Methodology And Assumptions: Update To The Cash Flow Criteria For European RMBS Transactions, Jan. 6, 2009

Related Research

- Outlook Assumptions For The Finnish Residential Mortgage Market, Jan. 12, 2015
- Banking Industry Country Risk Assessment: Finland, Jan. 29, 2015
- Assessments For Jurisdictional Support According To Our Covered Bond Criteria, Dec. 22, 2014
- Assessments For Target Asset Spreads According To Our Covered Bond Criteria, Dec. 22, 2014
- Summary: Finland, Dec. 19, 2014
- Bank of Aland PLC, Nov. 28, 2014
- Covered Bond Monitor: Technical Note, Feb. 14, 2006

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