

Transaction Update: Bank of Aland PLC

Category FIN Mortgage Covered Bonds

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Table Of Contents

Major Rating Factors

Outlook: Stable

Rationale

Program Description

Rating Analysis

Related Criteria And Research

Transaction Update: Bank of Aland PLC

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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	+	Assigned Jurisdictional Support Uplift	+3	+	Collateral Support Uplift	+4	=	AAA/Stable	
									Rating Constraints	aaa
Systemic Importance	Very Strong		Jurisdictional Support Assessment	Very Strong		Overcollateralization Adjustment	0		Counterparty Risk	aaa
Adjusted Issuer Credit Rating	bbb					Liquidity Adjustment	0			
GRE And Sovereign Support	0		Legal Framework	Very Strong		Potential Collateral-Support Uplift	+4		Country Risk	aaa
Issuer Credit Rating	BBB		Systemic Importance	Very Strong						
			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 S&P Global Ratings' credit ratings on Bank of Aland PLC's Category FIN mortgage covered bonds reflects the one unused notch of uplift, which means that we would not automatically lower the ratings on the covered bonds if we were to lower our long-term rating on Bank of Aland by one notch.

Rationale

S&P Global Ratings is publishing this transaction update as part of its annual review of Bank of Aland's Category FIN covered bond program.

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.

We consider that the Finnish legal and regulatory framework, effectively isolate the cover pool assets for the benefit of the covered bondholders. This asset isolation allows us to assign a higher rating to the covered bonds than our long-term ICR.

We believe satisfactory operational procedures are in place to support our ratings on the covered bonds.

Bank of Aland 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 to Finland. These factors increase the likelihood that Bank of Aland 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 assess the reference rating level (RRL) as 'a-'.

We considered the likelihood for the provision of jurisdictional support. Based on a strong jurisdictional support assessment for mortgage programs in Finland, we assigned three notches of uplift from the RRL. Therefore we assess the jurisdiction-supported rating level (JRL) as 'aa-'.

We have reviewed the asset information provided as of Dec. 31, 2016. The portfolio comprises solely Finnish residential mortgage loans and a substitute assets sub-portfolio. Based on our cash flow analysis, we believe that the available credit enhancement exceeds the required credit enhancement for a 'AAA' rating.

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

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

Program Description

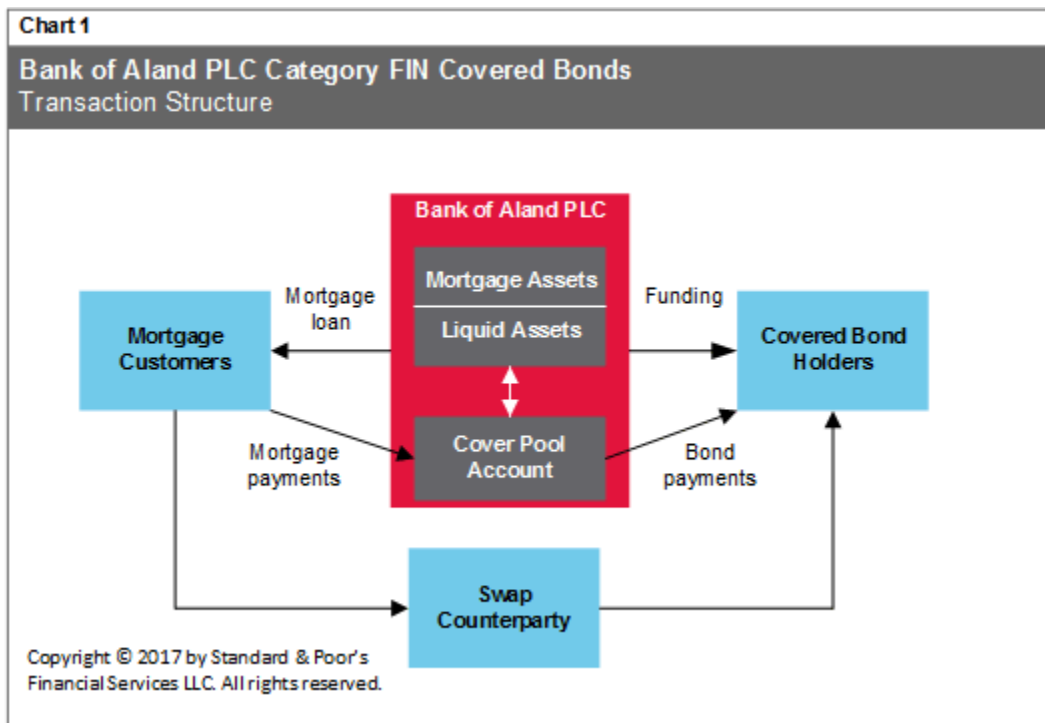
Table 1

Program Overview*	
Jurisdiction	Finland
Year of first issuance	2012
Covered bond type	Legislation-enabled
Outstanding covered bonds (mil. €)	1,023.81
Redemption profile	Hard and soft bullet
Underlying assets	Residential mortgages
Jurisdictional support uplift	3

Table 1

Program Overview* (cont.)	
Unused notches for jurisdictional support	0
Target credit enhancement (%)	30.65§
Available credit enhancement (%)	48.96
Collateral support uplift	4
Unused notches for collateral support	1
Total unused notches	1

*Based on data as of Dec. 31, 2016. §Given the JRL of 'aa-', overcollateralization that covers 'AAA' credit risk and 75% of refinancing costs or 27.17% of credit enhancement is required to achieve the 'AAA' rating.



Bank of Aland is a relatively small regional Scandinavian 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/Stable/A-2	Yes
Arranger	Bank of Aland PLC	BBB/Stable/A-2	No
Originator	Bank of Aland PLC	BBB/Stable/A-2	No
Servicer	Bank of Aland PLC	BBB/Stable/A-2	No
Bank account provider	Bank of Aland PLC	BBB/Stable/A-2	No
Swap account provider	Skandinaviska Enskilda Banken AB	A+/Stable/A-1	Yes
Swap account provider	Swedbank Mortgage AB	AA-/Negative/A-1+	Yes

Rating Analysis

Legal and regulatory risks

In our legal risk analysis, we applied our legal criteria (see "Asset Isolation And Special-Purpose Entity Methodology," published on March 29, 2017). 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 2016, 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.

We also believe that it is highly likely that a replacement cover pool manager could be appointed if the issuer were to become insolvent. We consider Finland to be an established covered bond market and we believe that the mortgage assets in Bank of Aland's cover pool do not comprise product features that would materially limit the range of available replacement cover pool managers or servicers.

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 Bonds Criteria," published on July 20, 2016). 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 Dec. 31, 2016. The cover pool primarily comprises Finnish residential mortgages (90.78%). The remainder consists of substitute assets (9.22%).

Since December 2015, the weighted-average foreclosure frequency (WAFF) has increased to 19.32% from 16.97% and the weighted-average loss severity (WALS) has increased to 18.32% from 17.77%.

The WAFF increased because of several factors, primarily the increase of the interest-only share of the loans in the cover pool, the increase in the percentage of loans in arrears, and an increase in the share of loans that have a loan to income adjustment. The WALS has increased due to the increases in the weighted-average loan-to-value ratio and in the share of jumbo valuations.

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 45.08% of the sub-pool) are in default. The weighted-average recovery rate is 30%.

Table 3

Cover Pool Composition				
Asset type	-Dec. 31, 2016--		-Dec. 31, 2015--	
	Value (mil. €)	Percentage of cover pool (%)	Value (mil. €)	Percentage of cover pool (%)
Residential mortgages	1,400.09	90.78	1,228.72	89.36
Substitute assets	142.20	9.22	146.30	10.64
Total	1,542.29	100	1,375.02	100

Table 4

Key Credit Metrics		
	As of Dec. 31, 2016	As of Dec. 31, 2015
Weighted-average original LTV ratio	69.57	69.75
Weighted-average cover pool LTV ratio	55.81	54.55
Weighted-average loan seasoning (months)*	49.35	53.10
Balance of loans in arrears (%)	0.63	0.15
Buy-to-let loans (%)	10.90	10.48
Credit analysis results:		
Weighted-average foreclosure frequency (WAFF; %)	19.32	16.97
Weighted-average loss severity (WALS; %)	18.32	17.77
AAA credit risk (%)	16.71	18.51

*Seasoning refers to the elapsed loan term. LTV--Loan to value.

Table 5

Covered Pool Assets By Loan Size		
	As of Dec. 31, 2016	As of Dec. 31, 2015
(€)	--Percentage of cover pool (%)--	
0-100,000	14.29	16.59
100,000-200,000	26.55	28.09
200,000-300,000	20.26	19.98
300,000-400,000	11.78	10.55
400,000-500,000	5.75	5.98
500,000-600,000	3.46	3.56
Above 600,000	17.92	15.24

Table 6

Loan-To-Value Ratios		
	As of Dec. 31, 2016	As of Dec. 31, 2015
(%)	--Percentage of cover pool (%)--	
0-30	6.90	7.80
30-60	47.00	50.80
0 - 60	53.90	58.60
60 - 70	45.53	39.14
70 - 80	0.57	2.27
80-90	0.00	0.00
90-100	0.00	0.00
Above 100	0.00	0.00
Total above 80	0.00	0.00

Table 7

Loan Seasoning Distribution*		
	As of Dec. 31, 2016	As of Dec. 31, 2015
	--Percentage of portfolio (%)--	
Less than 18 months	26.94	22.83
18-60 months	42.53	42.52
Above 60 months	29.90	34.50
Weighted-average loan seasoning (months)	49.35	53.10

*Seasoning refers to the elapsed loan term.

Table 8

Geographic Distribution Of Loan Assets		
	As of Dec. 31, 2016	As of Dec. 31, 2015
Region	--Percentage of cover pool (%)--	
Southern Finland	49.94	49.78
Western Finland	28.53	28.96
Åland	21.06	20.86
Eastern Finland	0.29	0.19
Lapland	0.02	0.10
Oulu	0.15	0.10

Table 9

Collateral Uplift Metrics		
	As of Dec. 31, 2016	As of Dec. 31, 2015
Asset WAM (years)	6.35	6.06
Liability WAM (years)	3.79	3.50
Available credit enhancement	48.96	49.38
Required credit enhancement for first notch of collateral uplift (%)	20.20	21.05
Required credit enhancement for second notch of collateral uplift (%)	23.68	23.60
Required credit enhancement for third notch of collateral uplift (%)	27.17	26.14

Table 9

Collateral Uplift Metrics (cont.)		
	As of Dec. 31, 2016	As of Dec. 31, 2015
Target credit enhancement for maximum uplift (%)	30.65	28.68
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.

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 30.65%. This is below the 28.68% target credit enhancement in December 2016. The increase is mainly the result of the decrease in excess spread.

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 27.17%. This is lower than the available credit enhancement of 48.96%.

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 10.77% of the additional credit enhancement--and take the view that overcollateralization sufficiently mitigates this risk.

The swaps in place partially cover interest rate and fully cover 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. We factor the remaining interest rate risk (floating to fix) 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 (see "Ratings Above The Sovereign - Structured Finance: Methodology And Assumptions," published on Aug. 8, 2016). Given the current ratings on Finland (AA+/Stable/A-1+), our rating on the program is not limited by these 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

- Asset Isolation And Special-Purpose Entity Methodology, March 29, 2017
- Methodology and Assumptions: Assessing Pools Of European Residential Loans, Dec. 23, 2016
- Ratings Above The Sovereign - Structured Finance: Methodology And Assumptions, Aug. 8, 2016
- Counterparty Risk Analysis In Covered Bonds, Dec. 21, 2015
- Covered Bond Ratings Framework: Methodology And Assumptions, June 30, 2015
- Methodology And Assumptions For Assessing Portfolios Of International Public Sector And Other Debt Obligations Backing Covered Bonds And Structured Finance Securities, Dec. 9, 2014
- Covered Bonds Criteria, Dec. 9, 2014
- Counterparty Risk Framework Methodology And Assumptions, June 25, 2013
- Credit Stability Criteria, May 3, 2010
- Use Of CreditWatch And Outlooks, Sept. 14, 2009

Related Research

- Global Covered Bond Characteristics And Rating Summary Q1 2017, April 20, 2017
- Assessments For Jurisdictional Support According To Our Covered Bonds Criteria, July 20, 2016
- Bank of Aland PLC, Aug. 17, 2016
- Assessments For Target Asset Spreads According To Our Covered Bonds Criteria, Aug. 15, 2016

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