

Rating Action: Moody's reviews covered bonds issued by Hypo NOE, Hypo Tirol and Heta AR for upgrade

Global Credit Research - 25 May 2016

London, 25 May 2016 -- Moody's Investors Service has today placed on review for upgrade the covered bonds of Hypo NOE Gruppe Bank AG (Hypo NOE, not publicly rated), Hypo Tirol Bank AG (Hypo Tirol, CR assessment Baa3(cr), on review for upgrade) and Heta Asset Resolution AG (Heta AR, Backed SUR Ca, on review for upgrade):

- Mortgage covered bonds issued by Hypo NOE Gruppe Bank AG (Hypo NOE, not publicly rated), Aa1 placed on review for upgrade;
- Public-sector covered bonds issued by Hypo NOE, Aa1 placed on review for upgrade;
- Mortgage covered bonds issued by Hypo Tirol Bank AG (Hypo Tirol, CR assessment Baa3(cr), on review for upgrade), Aa3 placed on review for upgrade;
- Public-sector covered bonds issued by Hypo Tirol, Aa1 placed on review for upgrade; and
- Public-sector covered bonds issued by Heta Asset Resolution AG (Heta AR, Backed SUR Ca, on review for upgrade): Ba2 placed on review for upgrade.

RATINGS RATIONALE

The rating reviews follow the review for upgrade of the covered bond issuers (see "Moody's takes rating actions on Heta, Pfandbriefbank (Oesterreich) and 2 Austrian regional mortgage banks," published 23 May 2016. The covered bond anchors of the respective issuers may be positively affected following the rating review of the entities. As a result, the expected loss of the covered bonds might fall. In this scenario, the covered bonds' ratings would not be constrained at the currently assigned levels, based on our timely payment framework as explained below.

KEY RATING ASSUMPTIONS/FACTORS

Moody's determines covered bond ratings using a two-step process: an expected loss analysis and a TPI framework analysis.

EXPECTED LOSS: Moody's uses its Covered Bond Model (COBOL) to determine a rating based on the expected loss on the bond. COBOL determines expected loss as (1) a function of the probability that the issuer will cease making payments under the covered bonds (a CB anchor event); and (2) the stressed losses on the cover pool assets following a CB anchor event.

Moody's may use a CB anchor of CR assessment plus one notch in the European Union or otherwise where an operational resolution regime is particularly likely to ensure continuity of covered bond payments.

The cover pool losses are an estimate of the losses Moody's currently models following a CB anchor event. Moody's splits cover pool losses between market risk and collateral risk. Market risk measures losses stemming from refinancing risk and risks related to interest-rate and currency mismatches (these losses may also include certain legal risks). Collateral risk is derived from the collateral score, which measures losses resulting directly from the cover pool assets' credit quality.

TPI FRAMEWORK: Moody's assigns a "timely payment indicator" (TPI), which measures the likelihood of timely payments to covered bondholders following a CB anchor event. The TPI framework limits the covered bond rating to a certain number of notches above the CB anchor.

--- Hypo NOE Mortgage Covered Bonds ---

The CB anchor for this programme is CR assessment plus one notch.

The cover pool losses are 25.1%, with market risk of 18.2% and collateral risk of 6.9%. The collateral score for this programme is currently 10.4%. The over-collateralisation in this cover pool is 62.7%, of which the issuer provides 12.5% on a "committed" basis. The minimum OC level that is consistent with the Aa1 rating is 19.5%, of which the issuer should provide 12.5% in a "committed" form. These numbers show that Moody's is relying on "uncommitted" OC in its expected loss analysis.

The current TPI is "Probable". The TPI Leeway is not disclosed.

All numbers in this section are based on the most recent Performance Overview (based on data, as per 31 December 2015).

--- Hypo NOE Public-Sector Covered Bonds ---

The CB anchor for this programme is CR assessment plus one notch.

The cover pool losses are 25.9%, with market risk of 13.4% and collateral risk of 12.5%. The collateral score for this programme is currently 24.9%. The over-collateralisation in this cover pool is 49.4%, of which the issuer provides 6.5% on a "committed" basis. The minimum OC level that is consistent with the Aa1 rating is 23%, of which the issuer should provide 6.5% in a "committed". These numbers show that Moody's is relying on "uncommitted" OC in its expected loss analysis.

The current TPI is "High". The TPI Leeway is not disclosed.

All numbers in this section are based on the most recent Performance Overview (based on data, as per 31 March 2016).

--- Hypo Tirol Mortgage Covered Bonds ---

The CB anchor for this programme is CR assessment plus one notch.

The cover pool losses are 24.4%, with market risk of 17.8% and collateral risk of 6.5%. The collateral score for this programme is currently 9.8%. The over-collateralisation in this cover pool is 347.9%, of which the issuer provides 6.0% on a "committed" basis. The minimum OC level that is consistent with the Aa3 rating is 8.5%, of which the issuer should provide 0.5% in a "committed" form. These numbers show that Moody's is relying on "uncommitted" OC in its expected loss analysis.

Based on the current TPI of "Probable", the TPI Leeway for this programme is 0 notches. This implies that Moody's might downgrade the covered bonds because of a TPI cap if it lowers the CB anchor all other variables being equal.

All numbers in this section are based on the most recent Performance Overview (based on data, as per 31 December 2015).

--- Hypo Tirol Public-Sector Covered Bonds ---

The CB anchor for this programme is CR assessment plus one notch.

The cover pool losses are 14.8%, with market risk of 12.5% and collateral risk of 2.3%. The collateral score for this programme is currently 4.7%. The over-collateralisation in this cover pool is 27%, of which the issuer provides 9.5% on a "committed" basis. The minimum OC level that is consistent with the Aa1 rating is 11.5%, of which the issuer should provide 3.5% in a "committed". These numbers show that Moody's is relying on "uncommitted" OC in its expected loss analysis.

Based on the current TPI of "High", the TPI Leeway for this programme is 0 notches. This implies that Moody's might downgrade the covered bonds because of a TPI cap if it lowers the CB anchor all other variables being equal.

All numbers in this section are based on the most recent Performance Overview (based on data, as per 31 December 2015).

--- Heta AR Public-Sector Covered Bonds ---

The CB anchor for this programme is the senior unsecured rating.

The cover pool losses are 51.4%, with market risk of 38.3% and collateral risk of 13.2%. The collateral score for this programme is currently 26.4%. The over-collateralisation in this cover pool is 257.4%, of which the issuer provides 38.5% on a "committed" basis. The minimum OC level that is consistent with the Ba2 rating is 64.5%, of which the issuer should provide 21.5% in a "committed" form. These numbers show that Moody's is relying on "uncommitted" OC in its expected loss analysis.

The current TPI is "High". The TPI Leeway is not disclosed.

All numbers in this section are based on the most recent Performance Overview (based on data, as per 31 December 2015).

FACTORS THAT WOULD LEAD TO AN UPGRADE OR DOWNGRADE OF THE RATINGS:

The CB anchor is the main determinant of a covered bond programme's rating robustness. A change in the level of the CB anchor could lead to an upgrade or downgrade of the covered bonds. The TPI Leeway measures the number of notches by which Moody's might lower the CB anchor before the rating agency downgrades the covered bonds because of TPI framework constraints.

A multiple-notch downgrade of the covered bonds might occur in certain circumstances, such as (1) a country ceiling or sovereign downgrade capping a covered bond rating or negatively affecting the CB Anchor and the TPI; (2) a multiple-notch downgrade of the CB Anchor; or (3) a material reduction of the value of the cover pool.

RATING METHODOLOGY

The principal methodology used in these ratings was "Moody's Approach to Rating Covered Bonds" published in August 2015. Please see the Ratings Methodologies page on www.moody.com for a copy of this methodology.

REGULATORY DISCLOSURES

For further specification of Moody's key rating assumptions and sensitivity analysis, see the sections Methodology Assumptions and Sensitivity to Assumptions of the disclosure form.

Moody's did not use any stress scenario simulations in its analysis.

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