Scope affirms Bank Burgenland's Austrian mortgage covered bond rating at AAA/Stable

The rating on Hypo-Bank Burgenland AG's Austrian mortgage covered bonds (Hypothekenpfandbriefe) reflects the issuer's A- rating enhanced by six notches from governance and cover pool support.

Rating action

Scope Ratings GmbH (Scope) has affirmed the AAA rating on the Austrian mortgage covered bonds (Hypothekenpfandbriefe) issued by Hypo-Bank Burgenland AG (Bank Burgenland). The Outlook is Stable.

Download the performance report.

Key rating drivers

Covered bond rating anchor: A-. The issuer rating forms the starting point of the covered bond rating. It reflects the bank's well-established, profitable and regionally focused banking operations in the Austrian regions of Burgenland, Vienna, Carinthia and Styria. Bank Burgenland's business model is well diversified focusing on real estate financing, supported by good market positions in retail and private banking as well as asset management and custodian banking for institutional investors (See detailed rating report here).

Governance support (plus five notches). This rating uplift reflects the high likelihood of covered bonds being maintained as a going concern in the event of regulatory action in the issuer well as a smooth transition from the first (issuer) to the second recourse (cover pool) if needed. It consists of three notches from our resolution regime and systemic importance assessment and two notches from Scope's legal framework and structural support assessment.

Scope's legal framework and structural support analysis for Bank Burgenland's covered bonds considers: 1) the cover pool's valid segregation from the insolvency estate of the issuer's parent; 2) the very high likelihood of bond payments continuing after insolvency; 3) the strong legal and programme specific asset eligibility and risk management principles; 4) that enhancements to the covered bond programme remain available after an insolvency of the issuer; and 5) the dedicated regulatory oversight for Austrian covered bonds (ESG factor).

The resolution regime and systemic importance assessment considers: 1) the existence of statutory provisions (Bank Recovery and Resolution Directive) that protect the covered bonds against regulatory actions in a resolution scenario; 2) the strength of statutory provisions including their exemption from being bailed-in; 3) the high systemic relevance of covered bonds in Austria but only moderate relevance of Bank Burgenland as a covered bond issuer and; 4) Austrian's cohesive stakeholder community (ESG factor).

Cover pool support (plus up to three notches). This rating uplift reflects the impact of the second recourse.

The current overcollateralisation (OC) of 88.1% is well above the rating supporting OC of 10%. The rating-supporting OC is sufficient to mitigate:

- **Credit risk – granular mixed mortgage portfolio.** The covered bonds are covered by a portfolio of mortgage loans to private residential (48.3%) and commercial borrowers (51.7%). Commercial loans do mainly include exposures with housing corporations but also hospitality, services, retail or manufacturing. Together, the portfolio consists of 6,930 loans with the top 10 accounting for 18.8%. The portfolio benefits from a moderate averaged indexed eligible-loan-to-value of 49.9% and a seasoning of 5.4 years. Scope has calculated a weighted average annualised default rate of 1.14% for the residential and 1.66% for the commercial sub-portfolio. The coefficient of variation is 55% and 71%, respectively. Stressed recovery rates are 75.8% and 57.7%.

- **Market risk – interest rate mismatches prevail.** The covered bonds are exposed to market risks. Interest rate mismatches are driven by the 87.6% fixed rate mortgage bonds which compare to 43.6% of fixed rate mortgage loans. In addition, maturity mismatches arise from the bonds' remaining life of 9.5 years which compares to 7.1% of the cover assets. The bonds do not benefit from maturity extensions. However, maturity mismatches can be managed with call rights of the issuer that reduce the bonds' remaining life to around 5 years - if executed. The EUR2.5m of substitute assets do comply with the legal requirement to manage short term liquidity requirements but do not substantially mitigate maturity mismatches. No exchange risk exists as both, assets and covered bonds are denominated in EUR.

All else equal, an OC of 16.5% would shield the current rating against a two-notch issuer downgrade.

One or more key drivers of the credit rating action are considered an ESG factor.

Outlook and rating sensitivities

The **Stable Outlook** on Bank Burgenland's covered bonds reflect Scope's view on the stable credit performance of the issuer, and that governance support or cover pool support factors will not materially change.

Upside scenarios are not applicable as the ratings are the highest achievable.

The **downside scenarios** for the ratings and Outlooks are (individually or collectively):

- An issuer rating/Outlook downgrade by three notches

- A reduction in the governance support uplift by three notches or more

- A deterioration in the programme's interplay between complexity and transparency that worsens Scope's CPC assessment and reduces the number of notches from cover pool support

- Available or committed OC falling below rating-supporting level

Environmental, social and governance (ESG) factors

Governance is a key rating driver. For more detail, please refer to 'governance support' and 'cover pool support' (CPC assessment) under the 'key rating drivers' section above.

Quantitative analysis and assumptions

For its quantitative analysis Scope applied assumptions as laid down in the covered bond methodology.

Stress testing

No stress testing was performed.

Cash flow analysis

The cover pool support uplift is based on a cash flow analysis using Scope Ratings' covered bond model (Covered Bonds Expected Loss Model Version 1.2). The model applies Credit Rating distance-dependent stresses to scheduled cash flows to simulate the impact of increasing credit and market risks. The outcome of the analysis is an expected loss rate and an expected weighted average life for the instruments based on the generated cash flows.

Methodology

The methodology used for this Credit Rating and Outlook, (Covered Bond Rating Methodology, 26 July 2024), is available on https://scoperatings.com/governance-and-policies/rating-governance/methodologies.
The models used for this Credit Rating and Outlook are (Covered Bonds Expected Loss Model Version 1.2. and Portfolio Model Version 1.1), available in Scope Ratings' list of models, published under https://scoperatings.com/governance-and-policies/rating-governance/methodologies.
Information on the meaning of each Credit Rating category, including definitions of default, recoveries, Outlooks and Under Review, can be viewed in 'Rating Definitions – Credit Ratings, Ancillary and Other Services', published on https://www.scoperatings.com/governance-and-policies/rating-governance/definitions-and-scales. Historical default rates of the entities rated by Scope Ratings can be viewed in the Credit Rating performance report at https://scoperatings.com/governance-and-policies/regulatory/eu-regulation. Also refer to the central platform (CEREP) of the European Securities and Markets Authority (ESMA): http://cerep.esma.europa.eu/cerep-web/statistics/defaults.xhtml. A comprehensive clarification of Scope Ratings' definitions of default and Credit Rating notations can be found at https://www.scoperatings.com/governance-and-policies/rating-governance/definitions-and-scales. Guidance and information on how environmental, social or governance factors (ESG factors) are incorporated into the Credit Rating can be found in the respective sections of the methodologies or guidance documents provided on https://scoperatings.com/governance-and-policies/rating-governance/methodologies.
The Outlook indicates the most likely direction of the Credit Rating if the Credit Rating were to change within the next 12 to 18 months.

Solicitation, key sources and quality of information

The Rated Entity and/or its Related Third Parties participated in the Credit Rating process.
The following substantially material sources of information were used to prepare the Credit Rating: the Rated Entity and Scope Ratings' internal sources.
Scope Ratings considers the quality of information available to Scope Ratings on the Rated Entity or instrument to be satisfactory. The information and data supporting the Credit Rating originate from sources Scope Ratings considers to be reliable and accurate. Scope Ratings does not, however, independently verify the reliability and accuracy of the information and data.
Prior to the issuance of the Credit Rating action, the Rated Entity was given the opportunity to review the Credit Rating and Outlook and the principal grounds on which the Credit Rating and Outlook are based. Following that review, the Credit Rating and Outlook were not amended before being issued.

Regulatory disclosures

The Credit Rating and Outlook are issued by Scope Ratings GmbH, Lennéstraße 5, D-10785 Berlin, Tel +49 30 27891-0. The Credit Rating and Outlook are UK-endorsed.
Lead analyst: Mathias Pleißner, Executive Director
Person responsible for approval of the Credit Rating: Karlo Fuchs, Managing Director
The Credit Rating/Outlook was first released by Scope Ratings on 15 November 2017. The Credit Rating/Outlook was last updated on 22 November 2023.

Potential conflicts

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With more than 300 employees operating from offices in Berlin, Frankfurt, London, Madrid, Milan, Oslo and Paris, Scope Group is the leading European provider of independent credit ratings, ESG analysis and fund research. Based on forward-looking and innovative methodologies, Scope offers a European perspective that contributes to greater diversity of opinion for institutional investors worldwide. Scope Ratings is registered in accordance with the EU rating regulation and operating in the European Union with ECAI status. Scope Ratings is the only European rating agency accepted by the ECB for the Eurosystem Credit Assessment Framework (ECAF). The shareholders of Scope Group include CEO and founder Florian Schoeller and anchor shareholder Stefan Quandt, numerous senior personalities in European finance and industry as well as institutional investors from several European countries. More on www.scopegroup.com

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