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Transaction Update: OP Mortgage Bank

€15 Billion Medium-Term Covered Bond Program

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Ratings Detail

Reference Rating Level	**aa+**
Resolution Regime Uplift	+2
Systemic Importance	Very Strong
Adjusted Issuer Credit Rating	aa-
GRE And Sovereign Support	0
Issuer Credit Rating	**AA-***

+

Jurisdiction-Supported Rating Level	**aa+**
Assigned Jurisdictional Support Uplift	+3
Jurisdictional Support Assessment	Very Strong
Legal Framework	Very Strong
Systemic Importance	Very Strong
Sovereign Credit Capacity	Very Strong

+

Maximum Achievable Covered Bond Rating	**aaa**
Collateral Support Uplift	+3
Overcollateralization Adjustment	-1
Liquidity Adjustment	0
Potential Collateral-Based Uplift	+4

=

Covered Bond Rating	**AAA/Stable**
Rating Constraints	aaa
Counterparty Risk	aaa
Country Risk	aaa

*We use the long-term rating on OP Corporate Bank PLC, which reflects the creditworthiness of OP Financial Group to which

Major Rating Factors

Strengths

- The cover pool's assets are seasoned Finnish residential mortgage loans, which have low current weighted-average loan-to-value (LTV) ratios compared with Scandinavian peers.
- The interest rate characteristics of the mortgage assets are matched to the liabilities through swaps.
- The ratings on the covered bonds benefit from three unused notches of jurisdictional support and two unused notches of collateral based uplift.

Weaknesses

- There is no legally binding obligation for the issuer to provide excess overcollateralization to maintain the currently assigned rating on the program.
- Due to the high level of fixed installment mortgages included in the cover pool, any increase in interest rates will result in delayed principal repayment of the mortgage assets and a potential borrower payment shock.

Outlook: Stable

S&P Global Ratings' stable outlook on the ratings on OP Mortgage Bank's mortgage covered bonds reflects that we would not automatically lower the ratings on the covered bonds if we were to lower the issuer credit rating (ICR), all else remaining equal. This is because the program benefits from five unused notches of uplift.

We would lower the ratings on the covered bonds if we were to lower our long-term ICR on the issuer by more than five notches, or if the overcollateralization commensurate with the rating exceeded the available overcollateralization.

Rationale

We are publishing this transaction update as part of our periodic review of OP Mortgage Bank (OPMB)'s covered bond program and related issuances.

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.

From our analysis of OPMB's program and the Finnish legislative covered bond framework, we have concluded that the assets in the cover pool are isolated from the issuer's insolvency risk. The asset isolation allows us to potentially rate the covered bond program at a higher rating level than the long-term ICR on the issuer.

We conducted a review of OPMB's mortgage operations, which we view as prudent. We believe there are sufficiently prudent and effective underwriting and servicing procedures in place to support our ratings on the covered bonds.

The issuer is a core entity to its parent, the OP Financial Group, and we derive the starting point of our analysis from the long-term ICR on OP Corporate Bank, whose rating reflects the creditworthiness of the wider OP Financial Group.

Under our covered bonds criteria, we first assess the reference rating level (RRL), which for OPMB's covered bonds is 'aa+'. This reflects the ICR of the issuer, minus any notches of uplift for extraordinary sovereign support incorporated in the ICR (in this case, none), plus two notches of uplift to reflect our view of the protection offered to covered bondholders by the bail-in provisions specified under the EU's Bank Recovery and Resolution Directive (BRRD) in Finland.

We then consider the likelihood for the provision of jurisdictional support, which for mortgage programs in Finland we assess as very strong. This leads us to apply up to three notches of uplift from the RRL. However, the jurisdictional support uplift is limited by our long-term rating on the Finnish sovereign, 'AA+'. Therefore, we assess the jurisdiction-supported rating level (JRL) as the same level as the RRL on the program, 'aa+'.

We have reviewed the asset information provided as of June 30, 2018. The program's underlying assets comprise €13.363 billion of Finnish residential mortgage loans. Based on our cash flow analysis, the available credit enhancement in the program exceeds the target credit enhancement, which means that covered bonds are eligible for up to four notches of collateral-based uplift. We reduce the potential collateral-based uplift by one notch due to the lack of committed overcollateralization commensurate with the ratings. We consider that the soft-bullet structure of the liabilities covers liquidity risk for 180 days.

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

We have based our analysis on our relevant criteria (see "Related Criteria").

Program Description

Table 1

Program Overview*	
Jurisdiction	Finland
Year of first issuance	2011
Covered bond type	Legislation-enabled
Outstanding covered bonds (bil. €)	11,735
Redemption profile	Yes
Underlying assets	Finnish residential mortgage loans
Jurisdictional support uplift	3
Unused notches for jurisdictional support	3
Target credit enhancement (%)	4.2
Available credit enhancement (%)	14.27
Collateral support uplift	3
Unused notches for collateral support	2
Total unused notches	5

*Based on cash flows as of June 30, 2018.

OPMB established the €15 billion mortgage covered bond program to issue a series of covered bonds, which are secured on a cover pool of residential mortgage loans. The assets are registered in the cover asset register and the covered bondholders have a priority claim on the cover pool's assets. The program's first issuance was in 2011. OPMB established the new program following the enactment of the new Finnish Covered Bond Act in 2010.

The issuer is a part of the OP Financial Group, a statutory amalgamation of the Finnish cooperative banks. The group is a financial consortium under the Act on Amalgamations of Deposit Banks. The group established OPMB to refinance its prime mortgage assets by issuing covered bonds. Its funding plans are an integral part of the cooperative group's funding strategy. OPMB is also subject to the Covered Bond Act, which provides specific regulations for a Finnish covered bond issuer.

The Finnish covered bond law allows deposit banks and credit societies to participate indirectly in the issue of covered bonds by means of intermediary loans granted by a mortgage credit bank.

The program's covered bonds are the issuer's direct unconditional and unsubordinated debt obligations and rank pari passu among themselves. The covered bonds are secured on a cover pool of euro-denominated Finnish residential mortgage loans. The outstanding liabilities are all denominated in euro.

Chart 1

OP Mortgage Bank Covered Bond Program

Transaction Structure

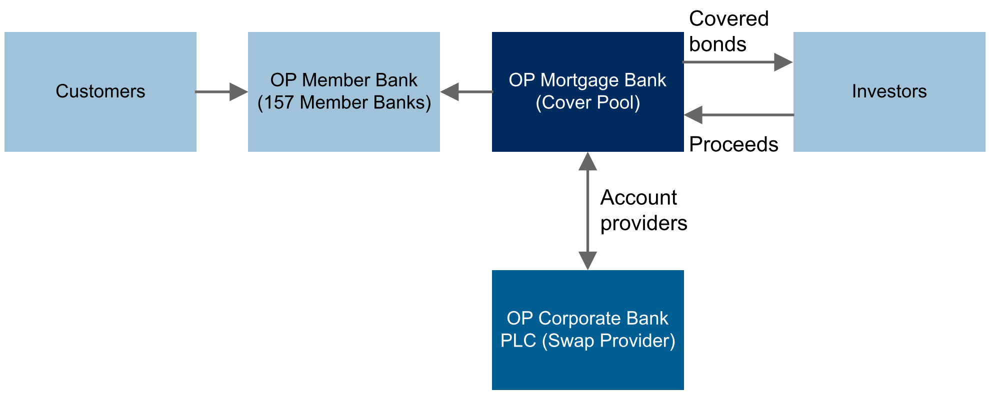

Table 2

Program Participants			
Role	**Name**	**Rating**	**Rating dependency**
Issuer	OP Mortgage Bank	N/A*	Yes
Originator	OP Mortgage Bank	N/A§	No
Bank account provider	OP Corporate Bank PLC	AA-/Stable/A-1+	Yes
Swap counterparty	OP Corporate Bank PLC	AA-/Stable/A-1+	Yes

*The issuer is a core entity to its parent, the OP Financial Group. Therefore, we derive the ratings on the covered bonds by applying notches of uplift to the long-term ICR on OP Corporate Bank PLC, whose rating reflects the creditworthiness of the wider OP Financial Group. §Mortgage loan origination by member banks of the wider OP Financial Group. N/A--Not applicable.

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 OP Corporate Bank.

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 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.

The Finnish covered bond law allows deposit banks and credit societies to participate indirectly in the issue of covered bonds by means of intermediary loans granted by a mortgage credit bank. The cover pool includes as of June 2018 38% of mortgages funded by intermediary loans. We consider the security of the collateral backing intermediary loans to be comparable to direct transferred mortgage loans. We therefore consider all intermediary loans as would they already be transferred to the cover pool.

If the issuer becomes 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 temporarily 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

The mortgage loan business is OP Financial Group's core business. OP Financial Group's central cooperative institution is headquartered in Helsinki and sets the group's basic lending criteria, supplies administrative assistance, and is responsible for debt collection. OPMB can set additional limits to the lending criteria and actively selects loans to be included in the cover pool, manages the cover pool, and issues covered bonds. OPMB's credit risks are reported and compared with the set risk limits on a monthly basis and an internal audit is carried out at least once a year. The cover pool may include loans in arrears, which have installments that are 90 days overdue or less. These loans are not part of the program's eligible balance. The cover pool currently includes 0.03% of loans that are more than 30 days in arrears.

We consider the issuer's underwriting and servicing standards to be sufficient to support our ratings on the covered bonds. In our opinion, there is no operational risk from the cover pool's management and loan origination that would constrain the covered bond ratings to the same level as the long-term ICR. Furthermore, we believe that it is highly likely that a replacement servicer would 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 the cover pool do not have product features that would materially limit the range of available replacement cover pool managers or servicers.

Our analysis of operational and administrative risks follows the guidelines in our criteria (see "Covered Bond Ratings Framework: Methodology And Assumptions," published on June 30, 2015).

Resolution regime analysis

OPMB is domiciled in Finland, which is part of the EU's BRRD. We assess the systemic importance of Finnish mortgage covered bond programs as very strong (see "Assessments For Jurisdictional Support According To Our Covered Bonds Criteria," published on Nov. 3, 2017). Under our covered bonds criteria, this means the RRL can be two notches above the adjusted long-term ICR (adjusted by removing the uplift allocated to reflect extraordinary government support to the issuer). This uplift recognizes that resolution regimes like the BRRD increase the probability that an issuer could service its covered bonds even following a default on its senior unsecured obligations because the law exempts covered bonds from bail-in risk if there is a bank resolution. We consider this as an internal form of support, because the bail-in of certain creditors of the issuer does not require direct government support. As a result, we assess the RRL as 'aa+'.

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 Nov. 3, 2017). Under our covered bonds criteria, this means that the program can receive up to three notches of jurisdictional uplift above the RRL considering the current sovereign rating on Finland. This leads to a JRL for OPMB's mortgage covered bonds of 'aa+'. The JRL cannot exceed the rating of the sovereign providing the support to the covered bond.

Collateral support analysis

The cover pool is entirely comprised by Finnish residential mortgage loans. We base our analysis on loan-by-loan data as of a cut-off date of June 30, 2018.

Table 3

Cover Pool Composition

	June 30, 2018		June 30, 2017	
Asset type	**Value (mil. €)**	**Percentage of cover pool (%)**	**Value (mil. €)**	**Percentage of cover pool (%)**
Finnish residential mortgage loans	13,363	100	11,944	100
Substitute assets	0	0	0	0
Other asset type	0	0	0	0
Total	13,363	100	11,944	100

The cover pool includes loans granted to borrowers with multiple loan parts and, in some occasions, backed by different properties. These loans currently represent on average about 45% of the property's current value. Finnish property prices have generally risen since 1996 but have stabilized in recent years. House prices and income levels have tended to move in tandem, suggesting that the housing market is not overvalued.

The weighted-average seasoning of the portfolio is approximately six years and the interest rate on almost 99.5% of the loans is floating.

We assess the credit quality of a typical residential mortgage cover pool by estimating the credit risk associated with each loan in the pool. The analysis of the residential mortgage loans is based on our European residential loans criteria (see "Methodology And Assumptions: Assessing Pools Of European Residential Loans," published on Aug. 4, 2017).

We then calculate the aggregate risk to assess the overall credit quality of the cover pool. In order to quantify the potential losses associated with the entire pool, we weight each loan's foreclosure frequency and loss severity by its percentage of the total pool balance. The product of the weighted-average foreclosure frequency (WAFF) and weighted-average loss severity (WALS) estimates the required loss protection, assuming all other factors remain unchanged.

As of the cut-off date, the WAFF is 16.53% and the WALS is 7.50%. The WAFF and WALS incorporate our covered bonds criteria guidance (see "Criteria Guidance: Covered Bonds Criteria," published on May 2, 2018).

Table 4

Key Credit Metrics

	June 30, 2018	March 31, 2017
Average loan size (€)	52,984	50,495
Weighted-average LTV ratio (%)	44.46	42.2
Weighted-average original LTV ratio (%)	68.34	64.6
Weighted-average loan seasoning (months)*	70.79	71.6
Balance of loans in arrears (%)	0.03	0.04
Buy-to-let loans (%)	0.59	0.64
Self-employed borrowers	3.33	2.17

*Seasoning refers to the elapsed loan term. LTV--Loan to value. N/A--Not applicable.

Table 5

Covered Pool Assets By Loan Size

	June 30, 2018	March 31, 2017
(€ '000s)	Percentage of cover pool (%)	
0 to 100	49.0	53.3
100 to 200	36.2	35.0
200 to 300	9.9	8.3
300 to 400	2.8	2.1
400 to 500	1.1	0.7
500 to 600	0.5	0.3
Greater than 600	0.5	0.3

Table 6

Current LTV Ratios

	June 30, 2018	March 31, 2017
(%)	Percentage of cover pool (%)	
0-60	79.94	83.43
60-70	14.31	13.11
70-80	3.88	3.25
80-90	1.12	0.18
90-100	0.49	0.02
Above 100	0.26	0.02
Total above 80	1.87	0.21

Table 6

Current LTV Ratios (cont.)

	June 30, 2018	March 31, 2017
(%)	Percentage of cover pool (%)	
Weighted-average LTV ratios	44.46	42.19

LTV--Loan-to-value.

Table 7

Original LTV Ratios

	As of June 30, 2018	As of March 31, 2017
(%)	Percentage of cover pool (%)	
0-60	33.65	37.85
60-70	15.54	17.25
70-80	15.59	16.48
80-90	14.41	14.13
90-100	7.45	5.93
Above 100	13.35	8.36
Total above 80	35.22	28.42
Weighted-average LTV ratios	68.34	64.57

LTV--Loan-to-value.

Table 8

Loan Seasoning Distribution*

	June 30, 2018	March 31, 2017
	Percentage of portfolio (%)	
Less than 18 months	14.0	10.4
18 to 60	31.9	36.6
More than 60	54.2	53.0
Weighted-average loan seasoning (months)	70.8	71.6

*Seasoning refers to the elapsed loan term.

Table 9

Geographic Distribution Of Loan Assets

	June 30, 2018	March 31, 2017
	Percentage of cover pool (%)	
Southern Finland	46.6	46.0
Eastern Finland	9.0	9.7
Western Finland	33.3	33.4
Oulu	9.7	9.4
Lapland	1.3	1.4
Aland	0.2	0.1
Total	100	100

According to our 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. For OPMB, all covered bonds include a 12-month maturity extension, which we consider to satisfy the six-month liquidity coverage. OPMB does not provide a commitment for overcollateralization. Therefore, we adjust the maximum collateral-based uplift to three notches.

We conducted our cash flow analysis by applying our European residential loans criteria.

The cover pool consists of 63% equal installment mortgage loans with variable maturity. The installment paid by the borrower must always cover interests, but may lead to the extension of repayments should the whole installment be used for interest. Of the pool, 25.0% are variable interest loans, while 5.7% are constant annuities where installment remains the same. The loan period will not change as interest rates change, but any residual payment is due on the final repayment date. Such loans attract an adjustment of credit risk in line with our criteria. Our analysis of the covered bonds' payment structure shows that the assets' cash flows would be sufficient to make timely payment of interest and ultimate payment of principal to the bondholders at a 'AAA' level.

By applying our credit and cash flow stresses, we calculate a target credit enhancement of 4.20%. The target credit enhancement is less than the available credit enhancement of 14.27%, allowing for the full three notches of collateral-based uplift. With a JRL of 'aaa', the program is only required to cover 'AAA' credit risk to achieve the 'AAA' rating, which corresponds to an overcollateralization of 2.5%.

Table 10

Collateral Uplift Metrics

	As of June 30, 2018
Asset WAM (years)	6.56
Liability WAM (years)	5.4
Available credit enhancement	14.27
Required credit enhancement for first notch of collateral uplift (%)	2.50
Required credit enhancement for second notch of collateral uplift (%)	2.50
Required credit enhancement for third notch collateral uplift (%)	3.20
Target credit enhancement for maximum uplift (%)	4.20
Potential collateral-based uplift (notches)	4
Adjustment for liquidity (Y/N)	N
Adjustment for committed overcollateralization (Y/N)	Y
Collateral support uplift (notches)	3

WAM--Weighted-average maturity.

Counterparty risk

We have identified various potential counterparty risks to which the program is exposed. However, as these are either structurally addressed or mitigated by the inclusion of replacement language in line with our current counterparty criteria, we believe that they do not constrain the rating from a counterparty risk perspective (see "Counterparty Risk Framework Methodology And Assumptions," published on June 25, 2013).

Bank account provider

OP Corporate Bank is the cover pool's bank account provider. Its commitment to replace itself if its short-term rating falls below 'A-1' mitigates bank account risk.

Commingling risk

The borrowers make payments to the bank account of the member banks that originated the loans. These funds are credited to the cover pool account on a daily basis. OPMB has a claim against OP Corporate Bank for any amounts credited to this account, and OP Corporate Bank waives all deposit set-off rights against these funds. If the short-term rating on OP Corporate Bank falls below 'A-1', it will open and maintain an issuer collection account with a bank rated at least 'A-1'. All borrower payments following a downgrade of OP Corporate Bank would be transferred to the issuer's collection account on daily basis. If the long-term ICR on OP Corporate Bank falls below 'BBB', within 30 days, the issuer will notify all borrowers to pay directly to the issuer's collection account, thereby mitigating commingling risk.

Swaps

OPMB has entered into hedging agreements with OP Corporate Bank to address interest rate mismatches between the assets and liabilities. There are no currency mismatches, as all of the assets and liabilities are euro-denominated. The interest rate swap documentation is consistent with our counterparty criteria for achieving a maximum rating of 'AAA'. Additionally, OP Corporate Bank has committed to replace itself as swap counterparty should we lower the ICR to below 'A', or 'BBB+' if it posts collateral. We therefore consider the swaps in our cash flow modeling.

Country risk

We assess country risk by applying our structured finance ratings above the sovereign criteria (see "Ratings Above The Sovereign - Structured Finance: Methodology And Assumptions," published on Aug. 8, 2016). Under these criteria, we consider that the assets in the pool have a moderate sensitivity to country risk. According to our criteria, due to the 12-month maturity extension feature of the issued covered bond, we can rate the covered bond up to four notches above the rating on the sovereign, Finland (AA+/Stable/A-1+). Based on the current sovereign rating, country risk does not constrain our rating on the covered bond.

Potential Effects Of Proposed Criteria Changes

Our ratings are based on our applicable criteria, including our "Covered Bonds Criteria," published on Dec. 9, 2014. However, the resolution regime analysis section of these criteria is under review (see "Methodology For Assigning Financial Institution Resolution Counterparty Ratings," published on April 19, 2018, and "Request For Comment: Methodology For Incorporating The Effect Of Resolution Regimes Into Covered Bond Ratings," published on Jan. 31, 2017). As a result of this review, we may amend certain paragraphs of our covered bonds criteria. This change may affect the ratings on the outstanding covered bonds issued under this covered bond program. Until this time, we will continue to rate and surveil these covered bonds using our existing criteria (see "Related Criteria").

Related Criteria

- Methodology And Assumptions: Assessing Pools Of European Residential Loans, Aug. 4, 2017

- Asset Isolation And Special-Purpose Entity Methodology, March 29, 2017
- Ratings Above The Sovereign - Structured Finance: Methodology And Assumptions, Aug. 8, 2016
- Criteria - Structured Finance - Covered Bonds: Counterparty Risk Analysis In Covered Bonds, Dec. 21, 2015
- Covered Bond Ratings Framework: Methodology And Assumptions, June 30, 2015
- Covered Bonds Criteria, Dec. 9, 2014
- Counterparty Risk Framework Methodology And Assumptions, June 25, 2013
- Criteria - Structured Finance - General: Global Derivative Agreement Criteria, June 24, 2013
- General Criteria: Methodology: Credit Stability Criteria, May 3, 2010
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009

Related Research

- Criteria Guidance: Covered Bonds Criteria, May 2, 2018
- Glossary Of Covered Bond Terms, April 27, 2018
- Request For Comment: Methodology For Incorporating The Effect Of Resolution Regimes Into Covered Bond Ratings, Jan. 31, 2017
- Assessments For Target Asset Spreads According To Our Covered Bonds Criteria, Nov. 3, 2017
- Assessments For Jurisdictional Support According To Our Covered Bonds Criteria, Nov. 3, 2017