

## CREDIT OPINION

17 May 2017

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## Closing Date

2011

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# Sparebanken Oest Boligkreditt Mortgage Covered Bonds

## Norwegian Covered Bonds

### Ratings

Cover Pool (NOK)	Ordinary Cover Pool Assets	Covered Bonds (NOK)	Rating
9,421,935,106	Residential Mortgage Loans	8,164,360,000	Aaa

Note: The ratings address the expected loss posed to investors. Moody's ratings address only the credit risks associated with the transaction.

Other non-credit risks have not been addressed, but may have a significant effect on yield to investors.

### Summary Rating Rationale

We have assigned a definitive long-term rating of Aaa to the covered bonds issued under the mortgage covered bond programme of Sparebanken Oest Boligkreditt AS (Sparebanken Oest Boligkreditt, the issuer). The covered bonds are full recourse to the issuer and the issuer is a stand-alone legal entity wholly owned by Sparebanken Oest (the parent; deposits A3 stable; adjusted baseline credit assessment baa2; counterparty risk (CR) assessment A2(cr)). The issuer itself is not rated. The covered bond rating is linked to the credit strength of the parent company of the issuer, principally because Sparebanken Oest has established a revolving credit facility for the issuer's benefit. The covered bonds are governed by the Norwegian covered bond legislation. Following a CB anchor event<sup>1</sup>, the covered bondholders will have priority claims over a pool of assets (cover pool) consisting of Norwegian residential mortgage loans. As of 31 December 2016, over-collateralisation (OC) in place is 15.4% on a nominal basis, of which the issuer has committed to maintain 11.0% (on a nominal basis). The minimum OC level that is consistent with the current Aaa rating is 4.5%. We have assigned a Timely Payment Indicator (TPI) of High to the covered bonds issued by Sparebanken Oest Boligkreditt.

The rating takes into account, among other factors:

- » The credit strength of the issuer.
- » The cover pool's credit quality, which is reflected in the collateral score of 5.0% (4.2% excluding systemic risk) and the current over-collateralisation of 15.4% (on a nominal basis) as of 31 December 2016 (the cut-off date).
- » The support provided by the Norwegian legal framework for covered bonds.

### Credit Strengths

- » *Recourse to the issuer:* The covered bonds are full recourse to the issuer. See "Covered Bonds Analysis".

- » *Support provided by the Norwegian legal framework:* The covered bonds are governed by the Norwegian covered bond legislation, which includes several strong features. See "Covered Bond Description".
- » *High credit quality of the cover pool:* The covered bonds are supported by a cover pool of high-quality assets. The assets are residential mortgage loans backed by properties located in Norway. The collateral quality is reflected in the collateral score, which is currently 5.0% (4.2% excluding systemic risk). See "Cover Pool Analysis".
- » *Refinancing risk:* Refinancing risk for Norwegian residential mortgage covered bonds is lower than in other jurisdictions as the issuer has the ability to reset loan rates on floating-rate residential mortgages at six weeks notice to the borrower. In the event of the issuer's default, the insolvency administrator will be able to similarly reset loan rates. Further, covered bonds issued under this programme will benefit from a 12-month extension period. See "Covered Bond Analysis".
- » *Interest rate and currency risks:* As of the cut-off date, all the assets in the cover pool are floating rate and denominated in NOK. However, some of the outstanding covered bonds are fixed rate and/or denominated in SEK. Interest rate and currency mismatch risks are hedged by way of swap agreements entered into by the issuer with swap counterparties that are not part of the issuer's group. The swap agreements provide for collateral posting and replacement triggers. See "Covered Bond Analysis".
- » *Liquidity matching requirements:* In accordance with the Norwegian covered bond legislation, the issuer has established liquidity risk guidelines and limits. These guidelines state that the net liquidity inflow should at all times be positive for the following twelve month period, on a rolling basis. Liquidity gaps are reported based on projected monthly liquidity inflows and outflows, on the basis of contractual loan redemption plans. Stress tests on liquidity are also carried out.
- » *Regulatory oversight:* In its capacity as a regulated financial institution (*kredittforetak*) under the terms of the Norwegian covered bond legislation, the issuer has obtained a licence from the Norwegian Financial Services Authority (FSAN or *Finanstilsynet*) to issue covered bonds (*obligasjoner med fortrinnsrett*), and is subject to ongoing supervision. See "Structure Description".
- » *Pool monitoring:* There is an external cover pool monitor (*uavhengig gransker*) responsible for monitoring various operations with respect to the cover pool. This is mandatory by operation of the Norwegian covered bond legislation.
- » *Set-off risk:* Set-off risk is well addressed by the combination of the Norwegian covered bond legislation and the transaction structure of the issuer's covered bond programme. See "Covered Bond Analysis".

## Credit Challenges

- » *High level of dependency on the issuer:* As with most covered bonds, before a CB anchor event, the issuer can materially change the nature of the programme. For example, the issuer can add new assets to the cover pool, issue new covered bonds with varying promises, and enter into new hedging arrangements. As with most covered bonds in Europe, there are few restrictions on the future composition of the cover pool. These changes could affect the cover pool's credit quality as well as the overall refinancing risk and market risks. Further, if the quality of the collateral deteriorates below a certain threshold, the issuer would have the ability, but not the obligation, to increase the OC in the cover pool. See "Covered Bond Analysis".
- » *Credit quality of the cover pool:* In line with Norwegian market standards, most of the loans in the cover pool (100% in this case) feature floating interest rates. This exposes the borrowers to the risk of increasing debt service payments in case of increasing interest rates, possibly leading to higher pool arrears. See "Cover Pool Analysis".
- » *Market risks:* Following a CB anchor event, covered bondholders may need to rely on proceeds being raised through the sale of, or borrowing against, cover pool assets in order to make timely payments of principal on the bonds. Following a CB anchor event, the market value of these assets may be subject to high volatility. In addition, covered bondholders may be exposed to interest rate and currency risk. See "Covered Bond Analysis".

This publication does not announce a credit rating action. For any credit ratings referenced in this publication, please see the ratings tab on the issuer/entity page on [www.moodys.com](http://www.moodys.com) for the most updated credit rating action information and rating history.

## Key Characteristics

Exhibit 1

### Covered Bonds Characteristics

Issuer:	Sparebanken Oest Boligkreditt AS
Covered Bond Type:	Mortgage covered bond
Issued under Covered Bond Law:	Yes
Applicable Covered Bonds Law:	Norwegian covered bond legislation
Entity used in Moody's TPI analysis:	Sparebanken Oest
CR Assessment:	A2(cr)
CB Anchor:	CR assessment +1 notch
Senior unsecured/deposit rating:	A3
Total Covered Bonds Outstanding:	NOK 8,164,360,000
Main Currency of Covered Bonds:	NOK (97%)
Extended Refinance Period:	Yes, one year refinancing period
Principal Payment Type:	Soft bullet
Interest Rate Type:	Floating rate covered bonds (83.5%), fixed rate covered bonds (16.5%)
Committed Over-Collateralisation:	11%
Current Over-Collateralisation:	15.4% (on a nominal basis)
Intra-group Swap Provider:	No
Monitoring of Cover Pool:	Cover pool monitor, mandatory by operation of the Norwegian covered bond legislation
Trustees:	n/a
Timely Payment Indicator:	High
TPI Leeway:	3 notches

Source: Moody's Investors Service; based on information provided by the issuer as of 31/12/2016

Exhibit 2

### Cover Pool Characteristics

Size of Cover Pool:	NOK 9,421,935,106
Main Collateral Type in Cover Pool:	Residential (96.0%)
Main Asset Location of Ordinary Cover Assets:	Norway (100%)
Main Currency:	NOK (100%)
Loans Count:	6,404
Number of Borrowers:	6,294
WA unindexed LTV (whole loan):	56.90%
WA indexed LTV (whole loan):	47.50%
WA Seasoning:	47 months
WA Remaining Term:	232 months
Interest Rate Type:	Fixed rate assets(0%), floating rate assets (100%)
Collateral Score:	5% (4.2% excluding systemic risk)
Cover Pool Losses:	9.8%
Further Cover Pool Details:	See <i>Cover Pool Overview</i>
Pool Cut-off Date:	31 December 2016

Source: Moody's Investors Service; based on information provided by the issuer as of 31/12/2016

## Covered Bond Overview

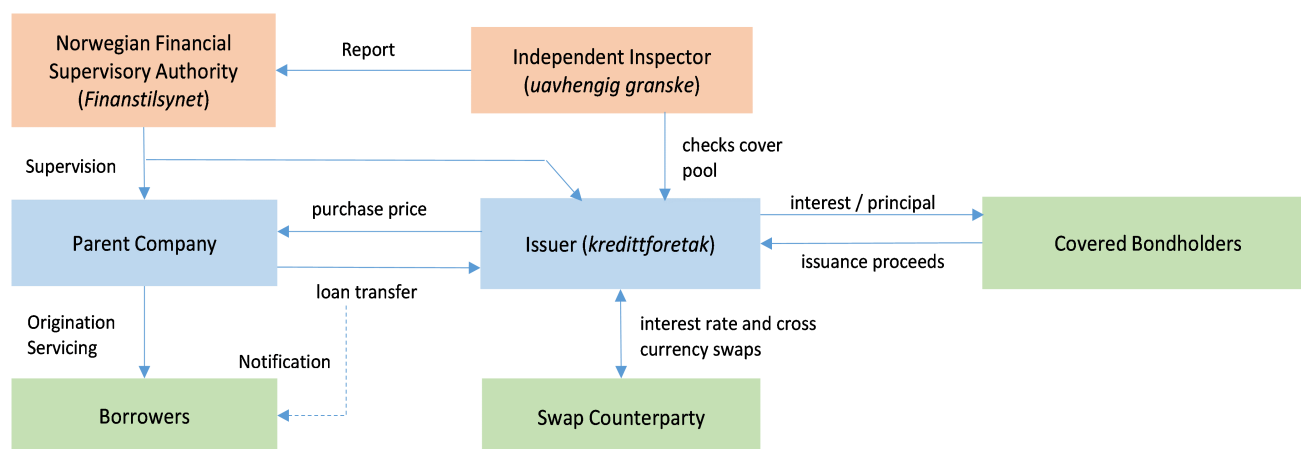
The covered bonds are governed by the Norwegian covered bond legislation and benefit from recourse to both the issuer and the cover pool. Our rating reflects these features.

## Covered Bond Description

The covered bonds are full recourse to the issuer. Upon occurrence of a CB anchor event, covered bondholders will have a priority claim on the cover pool.

## Structure Diagram

Exhibit 3



## Structure Description

### THE BONDS

All outstanding bonds benefit from a 12-month maturity extension.

### ISSUER RECOURSE

The covered bonds are full recourse to the issuer. Therefore, the issuer is obliged to repay principal and pay interest on the covered bonds.

### RECOURSE TO COVER POOL AND OVER-COLLATERALISATION

If the issuer becomes insolvent, the covered bondholders will have priority claims over a pool of assets (cover pool). See "Cover Pool Description" for the cover pool characteristics and "Cover Pool Analysis" for our analysis of the pool.

As of the cut-off date, the level of over-collateralisation (OC) in the programme was 15.4% on a nominal value basis and the committed OC was 11%. The minimum OC level that is consistent with the current Aaa rating was 4.5%. This shows that our analysis currently relies on OC that is in committed form.

Although the issuer has the ability to increase the OC in the cover pool if collateral quality deteriorates below a certain threshold, the issuer does not have any obligation to do so. The failure to increase OC following a deterioration of the collateral could lead to a negative rating action.

### LEGAL FRAMEWORK

The covered bonds are governed by the Norwegian covered bond legislation. There are a number of above-average strengths in this legislation, which include *inter alia* the following: (i) non-performing assets are excluded from cover pool tests, and therefore are less likely to dilute pool quality; (ii) set-off is excluded in respect of any asset in the cover pool; (iii) because issuers are specialist credit

institutions, the default of the parent or group supporting the issuer would not necessarily trigger the immediate default or insolvency of the issuer; (iv) the issuer must limit interest rate risk (unless swapped) by reference to the potential losses resulting from a parallel shift of one percentage point in all interest-rate curves and "distortion" of the interest rate curves; (v) swap counterparties must post collateral or provide other security if their credit quality reduces.

A description of the general legal framework under the Norwegian covered bond legislation is contained in our Sector In-depth Report [Norway - Legal Framework for Covered Bonds](#).

#### OTHER STRUCTURAL FEATURES

In its capacity as a regulated financial institution under the terms of the Norwegian covered bond legislation, Sparebanken Oest Boligkreditt has obtained a license from the NFSA to issue covered bonds. The license and its subsequent maintenance are subject to the issuer satisfying, on an ongoing basis, several requirements in respect of procedures and risk control systems set out by the Norwegian covered bond legislation and other applicable regulations.

## Covered Bonds Analysis

Our credit analysis of the covered bonds primarily focuses on the issuer's credit quality, refinancing risk, interest rate risk and currency risk, as well as the probability that payments on the covered bonds will be made in a timely fashion following a CB anchor event, which we measure using the Timely Payment Indicator (TPI), explained further below.

### Primary Analysis

#### ISSUER ANALYSIS

*Credit quality of the issuer:* Sparebanken Oest Boligkreditt is unrated.

The reference point for the issuer's credit strength in our analysis is the "CB anchor", which for covered bond programmes under the covered bond law in Norway is the CR assessment plus one notch<sup>2</sup>.

The covered bond rating is linked to the credit strength of the issuer's parent company, Sparebanken Oest, mainly because the parent has established a revolving credit facility for the benefit of the issuer. Sparebanken Oest's commitment to the covered bond programme is further underlined by the range of functions it carries out on behalf of the issuer. The support provided by the parent also means that the reference point for our analysis will be the CB anchor of Sparebanken Oest.

*Dependency on the issuer's credit quality:* The credit quality of the covered bonds is primarily dependent on the credit quality of the covered bonds issuer. Should the issuer's credit strength deteriorate, there would be a greater risk that a CB anchor event would occur, leading to refinancing risk for the covered bonds; consequently the credit quality of the covered bonds would deteriorate unless other credit risks decrease.

In case of deterioration of the CB anchor, the issuer would have the ability, but not obligation, to increase the OC in the cover pool. Failure to increase the level of OC under these circumstances could lead to negative rating actions.

Reasons for the high level of linkage of the covered bonds with the issuer also include exposure to decisions made by the issuer in its discretion as manager of the covered bond programme. For example, before a CB anchor event, the issuer may add new assets to the cover pool, issue further bonds and enter new hedging arrangements. Such actions could negatively affect the value of the cover pool.

#### REFINANCING RISK

Following a CB anchor event, the "natural" amortization of the cover pool assets alone cannot be relied on to repay principal. We assume that funds must be raised against the cover pool at a discount if covered bondholders are to receive timely principal payment. Where the portion of the cover pool that is potentially exposed to refinancing risk is not contractually limited, our expected loss analysis typically assumes that this amount is in excess of 50% of the cover pool.

After a CB anchor event, the market value of these assets may be volatile. Examples of the stressed refinancing margins we use for different types of prime-quality assets are published in our rating methodology (see Moody's Related Research: Moody's Approach to Rating Covered Bonds).

Aspects of this covered bond programme that are refinancing-positive include:

- » Provisions to allow for a principal refinancing period of 12 months, which should, in the event of a CB anchor event, improve the sales value of the cover pool and increase chances of timely principal payments on the covered bonds.
- » The ability of the issuer to increase the interest rate charged on floating-rate loans to the underlying borrowers, with a notice period of six weeks, enabling margins on the cover pool assets to increase to cover funding costs. This right also applies to any potential bankruptcy administrator in charge of the cover pool after a CB anchor event.

Aspects of this covered bond programme that are refinancing-negative include:

- » The lack of a separate cover pool administrator following a CB anchor event. The Norwegian covered bond legislation provides for a public administration board to be appointed for both the insolvency estate and management of the cover pool. While the manager is not dedicated to the cover pool, he or she should, however, face a minimum of conflicts as the issuer is a specialist institution with few creditors outside the cover pool.

#### INTEREST-RATE AND CURRENCY RISK

As with the majority of European covered bonds, there is potential for interest rate and currency mismatches, which could arise from the different payment promises and durations made on the cover pool and the covered bonds. For example, following a CB anchor event, covered bondholders may be exposed to interest rate risk that arises from different interest rates, and the duration of those interest rates, on the cover pool versus the covered bonds.

Following a CB anchor event, our model separately assesses the impact of increasing and decreasing interest rates on the expected loss of the covered bonds, taking the path of interest rates that leads to the worst result. The interest rate and currency stresses used over different time horizons are published in our Rating Methodology (see Moody's Related Research: Moody's Approach to Rating Covered Bonds).

Exhibit 4

#### Overview Assets and Liabilities

	WAL Assets (Years)	WAL Liabilities (Years)	Assets (%)	Liabilities (%)
Fixed rate	n/a	7.2	0.0%	16.5%
Variable rate	10.5	3.2	100.0%	83.5%

WAL = weighted-average life

Source: Moody's Investors Service; based on information provided by the issuer as of 31/12/2016

Aspects specific to this programme that are credit positive for interest rate and currency mismatches include:

- » All loans in the cover pool have a floating rate and are denominated in NOK.
- » The issuer has entered into hedging arrangements with external swap counterparties with a view to mitigating interest rate and currency risks. The hedging agreements include collateral posting and replacement triggers.

On the other hand, we consider the following programme feature to be credit negative for interest rate and currency mismatches:

- » All cover pool assets are denominated in Norwegian Kroner (NOK), whereas 3.5% of the bonds are denominated in SEK. This introduces some, although minor, currency risk, which however is somewhat mitigated by the hedging arrangements in place.

#### TIMELY PAYMENT INDICATOR

Our Timely Payment Indicator (TPI) assesses the likelihood that timely payments will be made to covered bondholders following a CB anchor event, and thus determines the maximum rating a covered bond programme can achieve with its current structure while allowing for the addition of a reasonable amount of OC. We have assigned a TPI of High to these covered bonds.

Based on the current TPI of High, the TPI Leeway for this programme is 3 notches. This implies that we might downgrade the covered bonds' rating because of a TPI cap if we lower the CB anchor by more than 3 notches, all other variables being equal.

TPI-positive aspects of this covered bond programme include:

- » The covered bonds' extended refinancing period of 12 months.
- » The issuer's ability to reset loan rates on floating-rate residential mortgages on six weeks notice to the borrower. In the event of issuer default, the administrator will be able to similarly reset loan rates.
- » The hedging arrangements in place.
- » The credit quality of the cover pool assets, which is reflected by the collateral score of 5.0% (4.2% excluding systemic risk).

TPI-negative aspects of this covered bond programme include:

- » The lack of a separate cover pool administrator following a CB anchor event. The Norwegian covered bond legislation provides for a public administration board, who runs the cover pool in the interest of the covered bondholders, to be appointed following a CB anchor event. However, the bankruptcy administrator will also be responsible for running the estate of the insolvent issuer, which would lead to some conflicts. This risk is mitigated by the specialist nature of the issuer, meaning it has few creditors other than the covered bondholders.
- » The currency risk, as referred to above. This risk, however, is somewhat mitigated by the hedging arrangements entered into by the issuer.

### Additional Analysis

#### SCENARIOS FOLLOWING A CB ANCHOR EVENT

Following a CB anchor event, the Norwegian covered bond legislation would not contemplate the dissolution of the issuer, nor would it include any acceleration event or event of default. Following a CB anchor event, any one or more of the following scenarios may occur:

- » Despite a CB anchor event in relation to the parent, the issuer is able to remain solvent, in which case the issuer may continue to operate the covered bond programme for the time being. However the issuer or parent may decide to terminate arrangements by which the parent provides services to the issuer.
- » Should the issuer become insolvent, payments to the creditors with a preferential claim over the cover pool (which includes covered bondholders and, if derivatives form part of the cover pool, derivative counterparties) could be continued by the public administration board of the issuer. The public administration board would be appointed by the Ministry of Finance, and would be responsible for running the general insolvency estate and the cover pool of the issuer.
- » Should the issuer become insolvent, the public administration board may decide that it may not be able to repay covered bondholders in full and introduce a halt of payments. The creditors would be informed of the halt of payments and the date on which it is to be introduced. All preferential claims over the cover pool would be calculated by discounting them to present value as of the date when payments have been halted. The liquidation proceeds from the cover pool would be used to repay the claims of all preferential creditors of the cover pool on a present value basis.

#### TIME SUBORDINATION

After a CB anchor event, the Norwegian covered bond legislation does not contemplate the acceleration of the covered bonds. Principal cash collections may be used on a first-come, first-served basis, paying earlier-maturing covered bonds prior to later-maturing covered bonds. This could lead to the OC being eroded before any payments are made to later-paying covered bonds, although the possibility for a halt of payments mitigates this risk.

## Cover Pool Overview

Following a CB anchor event, we determine the value of the cover pool, and therefore any losses, assuming a stressed environment.

## Cover Pool Description

### Pool Description as of 31 December 2016

As of 31 December 2016, the cover pool comprises 96% residential mortgage loans and 4% substitute assets. All properties that are serving as security for the loans are located in Norway.

On a nominal value basis, the cover pool assets total NOK 9.4 billion and are backing equivalent NOK 8.2 billion covered bonds. This translates into an OC level on a nominal basis of 15.4%.

For Sparebanken Oest Boligkreditt's underwriting criteria, see Appendix: Income Underwriting and Valuation.

### RESIDENTIAL MORTGAGE LOANS

Residential mortgage loans account for 96% of the total cover pool.

The high credit quality of the cover pool is evidenced, among other things, by the following features:

- » These loans consist of prime, first-lien Norwegian residential mortgage loans originated by the parent and secured against properties that are geographically well dispersed across Norway.
- » The current weighted-average (WA) indexed loan-to-value (LTV) of the residential mortgage loans is 42.6% (excluding junior ranking loan parts outside the cover pool). This ratio is low, in line with LTVs observed for other residential loans backing covered bonds that we rate in Norway.
- » All the residential mortgages are floating interest rate loans. These loans have an average seasoning of 47 months. All of them are denominated in NOK.



Exhibit 5 below shows more details about the cover pool characteristics.

Exhibit 5

### Residential Assets

Overview	
Asset type:	Residential
Asset balance:	9,043,379,937
Average loan balance:	1,412,146
Number of loans:	6,404
Number of borrowers:	6,294
Number of properties:	6,395
WA remaining term (in months):	232
WA seasoning (in months):	47
Details on LTV	
WA unindexed LTV: Whole loan / Senior loan (*):	56.9% / 52.2%
WA indexed LTV: Whole loan / Senior loan:	47.5% / 42.6%
Valuation type:	Market Value
LTV threshold:	75.00%
Junior ranks (**):	4.70%
Prior ranks:	0.00%

n/d: information not disclosed by Issuer

n/a: information not applicable

Specific Loan and Borrower characteristics	
Loans with an external guarantee in addition to a mortgage:	0.00%
Interest only Loans (***) / FlexLoans (****):	20.4% / 9.9%
Loans for second homes / Vacation:	0.00%
Buy to let loans / Non owner occupied properties:	1.90%
Limited income verified:	0.00%
Adverse credit characteristics (*****):	0.00%
Performance	
Loans in arrears (≥ 2months - < 6months):	0.00%
Loans in arrears (≥ 6months - < 12months):	0.00%
Loans in arrears (≥ 12months):	0.00%
Loans in a foreclosure procedure:	0.00%
Multi-Family Properties	
Loans to tenants of tenant-owned Housing Cooperatives:	n/d
Other type of Multi-Family loans (*****):	n/d

Chart A:  
Balance per LTV-band

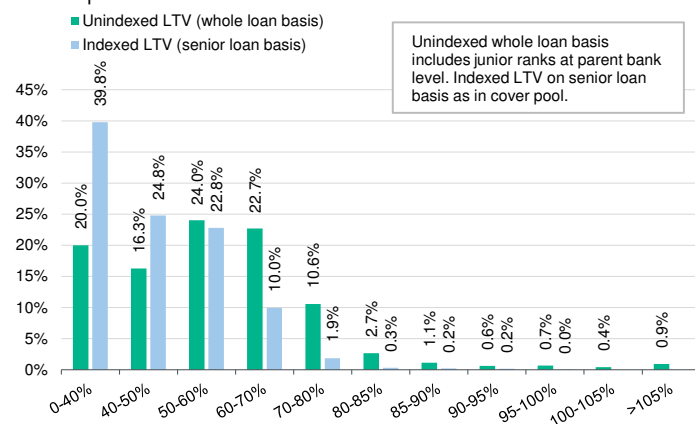


Chart B:  
Percentage of residential assets

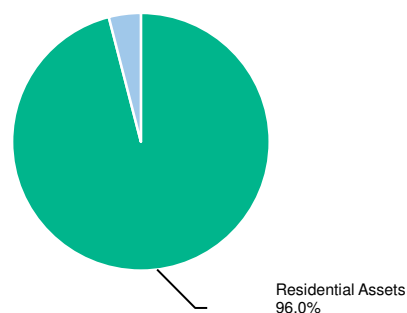


Chart C:  
Interest rate type

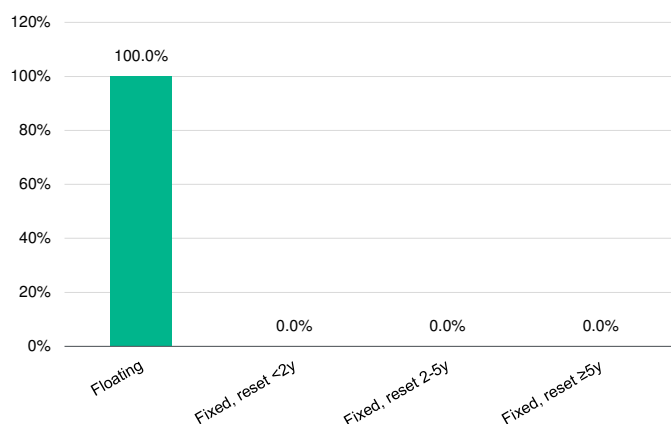


Chart D:  
Seasoning (in months)

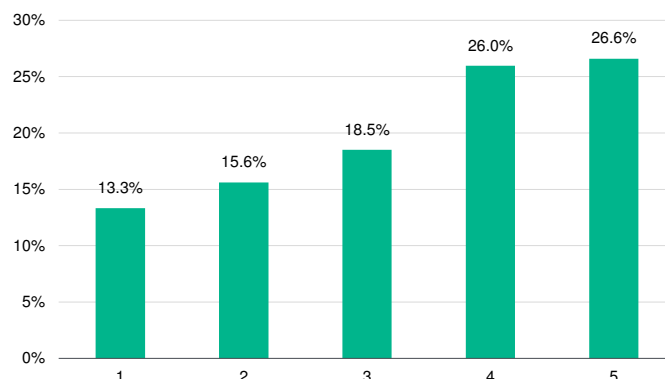
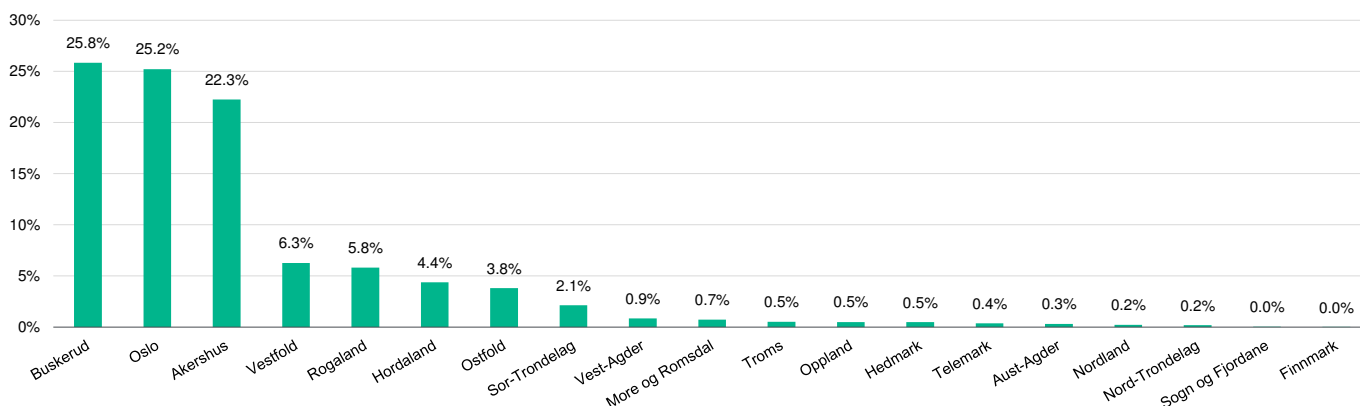


Chart E:  
Main country regional distribution



(note \*) may be based on property value at time of origination or further advance or borrower refinancing, (note \*\*) Internal junior ranks as a percentage of total residential asset balance, i.e. total amount of junior lien loans outside of the cover pool (but on the books of the issuing bank) that are secured on the same properties as the first lien loans in the cover pool. (note \*\*\*) This category includes loans which currently are in an initial interest only period before they start amortising. (note \*\*\*\*) FlexLoans have an amortisation profile and can be re-drawn by the customer up to a certain limit. (note \*\*\*\*\*) Typically borrowers with a previous personal bankruptcy or borrowers with record of court claims against them at time of origination. (note \*\*\*\*\*) This "other" type refers to loans directly to Housing Cooperatives and to Landlords of Multi-Family properties (not included in Buy to Let). This figure represents a percentage of the total cover pool.

Source: Moody's Investors Service; based on information provided by the issuer as of 31/12/2016

## SUBSTITUTE ASSETS

Substitute assets account for 4% of the total cover pool. They consist of Norwegian and supranational bonds and / or loans.

### Substitution

Exposure to decisions made by the issuer in its discretion as manager of the cover pool creates additional risk. For example, before a CB anchor event, the issuer may remove assets from the cover pool and/or add new assets to the cover pool. Such actions could negatively affect the value of the cover pool.

As with most covered bonds in Europe, there are few contractual restrictions on the future composition of the cover pool, creating substitution risk. Nevertheless, cover pool quality over time will be protected by, among other things, the requirements of the Norwegian covered bond legislation that specify the types of assets that are eligible (see [Norway – Legal Framework for Covered Bonds](#), section entitled "Asset and Covered Bond Eligibility").

## Cover Pool Analysis

Our credit analysis of the pool takes into account specific characteristics of the pool, as well as legal risks.

### Primary Cover Pool Analysis

The result of the cover pool analysis is the collateral score. We calculate the collateral score using a scoring model to assess the credit risk for the residential mortgages in the cover pool.

For this programme, the collateral score of the current pool is 5.0% (4.2% excluding systemic risk) which is comparable to the average collateral score in other Norwegian mortgage covered bonds (see Moody's Related Research: Moody's Global Covered Bonds Monitoring Overview: Q3 2016).

From a credit perspective, Moody's views the following portfolio characteristics as positive:

- » All of the mortgage loans are performing as of the cut-off date of this report.
- » The WA unindexed LTV of the residential mortgages is relatively low at 47.5% on a senior loan basis excluding junior ranking loan parts not transferred to the cover pool. Furthermore, the weighted average seasoning of the loans is 47 months, relatively high figure.
- » Borrowers' income is always independently verified, and the income restricts the amount that can be lent.

On the other hand, we regard the following portfolio characteristics as credit negative:

- » In line with the Norwegian market standard, all loans in the cover pool feature floating interest rates. This exposes the borrowers to the risk of increasing debt service payments in case of increasing interest rates, possibly leading to higher pool arrears. This risk is partially mitigated by a standard 5 percentage points stress applied to affordability testing.
- » Around 20.4% of the loans in the cover pool are interest only loans. This category includes loans which currently are in an initial interest only period before they start amortizing. This loan product may increase default risk if it leads to large principal payment obligations for borrowers at the end of the interest only period.
- » As it is common in Norway, valuations backing loans may be based on an automated valuation method (AVM) provided by Eiendomsverdi. These valuations do not include a physical inspection of the property.

### Additional Cover Pool Analysis

#### COMMINGLING RISK

The payment flows with respect to the assets in the cover pool are transferred daily from the Sparebanken Oest account to the issuer's account held at Sparebanken Oest. Following a CB anchor event the insolvency administrator has the right and the ability to redirect all payments made by Norwegian Interbank Clearing System (NICS) to a suitable issuer collection account within very short time frame.

#### CLAW-BACK RISK

All borrowers will be notified at the time the loans are transferred from the parent to the issuer. Provided that the borrowers have been notified and that the transfer has been performed in accordance with market practice, it cannot be subject to clawback by the transferor or any public administration board appointed in respect of the transferor.

## Methodology and Monitoring

The primary methodology we use in rating the issuer's covered bonds is "Moody's Approach to Rating Covered Bonds", published in December 2016. Other methodologies and factors that may have been considered in the rating process can also be found on <http://www.moody.com>. In addition, we publish a weekly summary of structured finance credit, ratings and methodologies, available to all registered users of our website, at [www.moody.com/SFQuickCheck](http://www.moody.com/SFQuickCheck).

We expect the issuer to deliver certain performance data to us on an ongoing basis. In the event that this data is not made available to us, our ability to monitor the ratings may be impaired. This could negatively affect the ratings or, in some cases, our ability to continue to rate the covered bonds.

## Income Underwriting and Valuation

### A. Residential Income Underwriting

1 Is income always checked?	Yes
2 Does this check ever rely on income stated by borrower ("limited income verification") ?	No. We use Experian.
3 Percentage of loans in Cover Pool that have limited income verification	None
4 If limited income verification loans are in the Cover Pool, describe what requirements lender has in place for these loans.	Not applicable
5 Does income in all cases constrain the amount lent (for example through some form of Income Sufficiency Test ("IST"))?	Yes
6 If not, what percentage of cases are exceptions.	No exceptions. The Ministry of Finance has adopted a new regulation on requirements for new residential mortgage loans.
For the purpose of any IST:	
7 Is it confirmed that income after tax is sufficient to cover both interest and principal?	Yes – and living expenses
8 If so over what period is it assumed principal will be paid (typically on an annuity basis)? Any exceptions?	Payment of interest and principal on an annuity basis over 30 years.
9 Does the age of the borrower constrain the period over which principal can be amortised?	Yes on a case to case basis.
10 Are any stresses made to interest rates when carrying out the IST? If so when and for what type of products?	Yes- 5 %-points
11 Are all other debts of the borrower taken into account at the point the loan is made?	Yes. All known debt. From tax return scheme etc.
12 How are living expenses of the borrower calculated? And what is the stated maximum percentage of income (or income multiple if relevant) that will be relied on to cover debt payments. (specify if income is pre or post tax)	Expenses are based on standard indices prepared by the National Institute for Consumer Research. These are published in [ <a href="http://www.sifo.no/page/English/Meny_knapper/10237/10281">http://www.sifo.no/page/English/Meny_knapper/10237/10281</a> ]. The percentage of [post tax] income that is assumed to be available for debt repayment varies depending on a lot of factors. Number of children, income group etc.
Other comments	

### B. Residential Valuation

1 Are valuations based on market or lending values?	Market values
2 Are all or the majority of valuations carried out by external valuers (with no direct ownership link to any company in the Sponsor Bank group)?	Yes. We are using Eiendomsverdi. Regulated by law.
3 How are valuations carried out where an external valuer not used?	NA
4 What qualifications are external valuers required to have?	Surveyor, real estate brokers, Eiendomsverdi.
5 What qualifications are internal valuers required to have?	NA
6 Do all external valuations include an internal inspection of a property?	No
7 What exceptions?	Most market values based on valuations from Eiendomsverdi.
8 Do all internal valuations include an internal inspection of a property?	NA
9 What exceptions?	NA
Other comments	

## Moody's Related Research

### Rating Methodology

- » [Moody's Approach to Rating Covered Bonds, December 2016 \(PBS\\_1044142\)](#)

### Special Comments

- » [Moody's Global Covered Bonds Monitoring Overview: Q3 2016, November 2016 \(PBS\\_1052892\)](#)
- » [Norway – Legal Framework for Covered Bonds, October 2016](#)
- » [European Covered Bond Legal Frameworks: Moody's Legal Checklist, December 2005 \(SF66418\)](#)

### Performance Overview

- » [Sparebanken Oest Boligkreditt Mortgage Covered Bonds, May 2017 \(SF452381\)](#)

### Webpage

- » [www.moody's.com/coveredbonds](http://www.moody's.com/coveredbonds)

To access any of these reports, click on the entry above. Note that these references are current as of the date of publication of this report and that more recent reports may be available. All research may not be available to all clients.

## Endnotes

- <sup>1</sup> This is the probability that the issuer or another rated entity (which is normally in the issuer group) ceases to make payments under the covered bonds. It should be noted that a CB Anchor Event does not necessarily mean there has been a late or missed payment on the covered bonds. The likelihood of timely payments continuing on the covered bonds following a CB Anchor Event is measured by our TPI.
- <sup>2</sup> See Moody's Sector Comment "[Bank Resolution Regime Strengthen Norwegian Covered Bonds and Improve Their Ratings](#)", August 2015.

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