MOODY'S INVESTORS SERVICE

CREDIT OPINION
24 July 2018

New Issue

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Slovenska Sporitelna, a.s. - Mortgage Covered Bonds

New Issue – Slovak covered bonds

Ratings

Exhibit 1

Cover Pool (€)	Ordinary Cover Pool Assets	Covered Bonds (€)	Rating
3,186,436,735	Residential Mortgage Loans	1,130,078,920	Aaa

The ratings address the expected loss posed to investors. Our 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.

Source: Moody's Investors Service

Summary

The covered bonds issued by Slovenska Sporitelna, a.s. (SLSP or the issuer) under its covered bond programme are full recourse to the issuer and are secured by a cover pool of assets consisting of residential mortgage loans in Slovakia. The programme includes mortgage bonds under Slovakia's prior legal framework, that were converted into covered bonds on 23 July 2018 following the update of the legal framework as of January 2018.

Credit strengths include the covered bonds' full recourse to the issuer, the support provided by the Slovak legal framework for covered bonds, which provides for the issuer's regulation and supervision, and the high credit quality of the cover pool.

Credit challenges include the covered bonds' high level of dependency on the issuer. As with most covered bonds in Europe, there are few restrictions on the future composition of the cover pool. There is also a risk of set-off between borrowers' deposits and mortgage loans in the cover pool.

Our credit analysis takes into account the cover pool's credit quality, which is reflected in the collateral score of 7.4%, and the current over-collateralisation (OC) of 182% (on a nominal value basis), based on data as of 31 May 2018 (the cut-off date).

Credit strengths

» ***Recourse to the issuer***: The covered bonds are full recourse to SLSP (A1(cr)). (See "Covered bond analysis")

» ***Support provided by the Slovak legal framework***: The covered bonds are governed by the Slovak covered bond legislation that provides for the issuer's regulation and supervision and sets certain minimum requirements for the covered bonds and the cover pool. (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 cover pool consists of residential mortgage loans backed by properties in Slovakia. The collateral quality is reflected in the collateral score, which is currently at 7.4%. (See "Cover pool analysis")

» ***Refinancing risk*****:** Following a covered bond (CB) anchor event, refinancing risk for Slovak mortgage covered bonds is mitigated through the management of the covered bond programme by the general insolvency administrator, as well as by the Slovak covered bond law's requirement that liquidity gaps between scheduled cash receipts and payments be covered for 180 days. A CB anchor event occurs when the issuer, or another entity within the issuer group that supports the issuer, ceases to service the payments on the covered bonds. (See "Covered bond description" and "Covered bond analysis")

» ***Currency risk***: Currency risk is currently well matched in this programme. All the assets and liabilities are denominated in euros. (See "Covered bond analysis")

Credit challenges

» ***High level of dependency on the issuer:*** As with most covered bonds, before the issuer's insolvency 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. Also, similar to most covered bonds in Europe, this programme has few restrictions on the future composition of the cover pool. These changes could affect the credit quality of the cover pool as well as its overall refinancing and market risks. Furthermore, 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")

» ***Market risks***: Following a CB anchor event, covered bondholders may need to rely on proceeds that are raised via the sale of, or borrowed against, cover pool assets to make timely payment 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 risk. (See "Covered bond analysis")

» ***Set-off risk***: In a bank insolvency the Slovak deposit guarantee scheme (SDGS) only enables depositors to claim for the amount of deposits exceeding the depositor's liabilities to the affected bank. Therefore, the SDGS does not effectively reduce set-off risk. (See "Cover pool analysis")

» ***Time subordination****:* After a CB anchor event, later-maturing covered bonds are subject to time subordination. Principal cash collections may be used on a first-come, first-served basis, paying earlier-maturing covered bonds before later-maturing covered bonds. This subordination could lead to the erosion of OC before any payments are made to later-paying covered bonds. (See "Covered bond analysis")

» ***Risk to liquidity reserve*****:** Should scheduled cash collections under the 180 day liquidity coverage test be interrupted, the programme would not benefit from any designated source of liquidity to cover the resulting shortfall. (See "Covered bond analysis")

Key characteristics

Exhibit 2
Covered bond characteristics

Moody's Programme Number:	450
Issuer:	Slovenska Sporitelna, a.s.
Covered Bond Type:	Residential mortgage covered bonds
Issued under Covered Bonds Law:	Yes
Applicable Covered Bonds Law:	Slovak covered bond legislation
Entity used in Moody's TPI analysis:	Slovenska Sporitelna, a.s.
CR Assessment:	A1(cr)
CB Anchor:	CR assessment +1 notch
Senior unsecured/deposit rating:	A1
Total Covered Bonds Outstanding:	EUR 1.1 billion
Main Currency of Covered Bonds:	EUR (100%)
Extended Refinance Period:	No
Principal Payment Type:	Hard bullet
Interest Rate Type:	Floating rate covered bonds (12%), fixed rate covered bonds (88%)
Committed Over-Collateralisation:	5% (on a nominal basis)
Current Over-Collateralisation:	182% (on a nominal basis), based on data as of the cut-off date
Intra-group Swap Provider:	n/a
Monitoring of Cover Pool:	Cover pool monitor
Trustees:	n/a
Timely Payment Indicator:	Improbable
TPI Leeway:	1 notch

Sources: SLSP, Moody's Investors Service

Exhibit 3
Cover pool characteristics

Size of Cover Pool:	EUR 3,186,436,735
Main Collateral Type in Cover Pool:	Residential (100%)
Main Asset Location of Ordinary Cover Assets:	Slovakia (100%)
Main Currency:	EUR (100%)
Loans Count:	82,338
Number of Borrowers:	77,174
WA unindexed LTV:	53.8%
WA indexed LTV:	51.2%
WA Seasoning:	38 months
WA Remaining Term:	239 months
Interest Rate Type:	Fixed rate assets (reset date > 1 year) (80.7%)
Collateral Score:	7.4%
Cover Pool Losses:	27.1%
Further Cover Pool Details:	See Appendix 1
Pool Cut-off Date:	31 May 2018

Sources: SLSP, Moody's Investors Service

Covered bond description

The covered bonds issued under the mortgage covered bond programme of SLSP are full recourse to the issuer. Upon a CB anchor event, covered bondholders would have access to a cover pool of residential mortgage loan receivables and any susbstitute assets.

Structure description

The bonds

All outstanding covered bonds have a bullet repayment at maturity, without any extension period for the repayment of the bonds. However, the Slovak covered bond legislation provides a potential extension period after issuer default for covered bonds issued from 1 January 2018 onwards. (See “The legal framework in detail - After CB anchor event”)

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 would have priority claims over a pool of assets (cover pool). (See “Cover pool description” and “Cover pool analysis”)

The level of OC in the programme is 182% on a nominal basis, based on data as of the cut-off date.

The current covered bond rating relies on a level of OC that meets the minimum legal requirements of the Slovak covered bond legislation, whereby the OC must exceed the principal balance of the bonds by 5%. Based on data as of the cut-off date, 19.5% OC is sufficient to maintain the current covered bond rating. Thus, the OC that our analysis currently relies on is in uncommitted form (save for the 5% legal minimum).

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.

The updated Slovak legal framework for covered bonds

The covered bonds are governed by the Banking Act, the Bonds Act and the Insolvency Act (together, the Slovak covered bond legislation).

Typical legal structure

» The issuer may only be a Slovak bank, that is, a bank established in the Slovak Republic and holding a Slovak banking license.

» Issuers issue covered bonds from their own balance sheets, with the cover pool assets staying on balance sheet, but ring-fenced by registration in the cover pool register.

Supervision and control

» The issuer must obtain a specific prior consent of the National Bank of Slovakia (NBS) for the performance of activities related to the covered bond programme.

» The issuers are regulated by the banking regulator (NBS).

» NBS shall appoint a cover pool monitor and a replacement cover pool monitor. (See “The legal framework in detail - Before CB anchor event - Cover pool monitor”)

Limits on programme size

There are no limits on programme size under the Slovak covered bond legislation.

The legal framework in detail - Before CB anchor event

<u>Asset and cover bond eligibility</u>

Types of assets permitted in cover pool/types of covered bonds

The covered bond law only allows the issuance of mortgage covered bonds. Assets eligible for the cover pool are (1) residential mortgage loans, (2) substitute assets, (3) qualifying derivative contracts, and (4) liquid assets. Residential mortgage loans must represent at least 90% of the value of the cover pool.

Residential loans must fulfill the following criteria, among others:

» A maximum tenor of 30 years

» The mortgaged property shall be in Slovakia

» With some minor exceptions, the issuer has a first-ranking mortgage over the property.

Residential loans may secure property under construction, including undeveloped land that is zoned for residential purposes.

Maximum LTVs for mortgage-backed assets

» Covered bonds issued from 1 January 2018 onwards:

  » Mortgage loan balance must not exceed 80% (LTV threshold) of the value of the mortgaged property at the time of registration of the loan in the cover pool register.

  » If the LTV increases up to a maximum of 100% because of a decrease in the property value, only the loan amount up to the LTV threshold can be taken into account for the calculation of the OC.

  » If the LTV increases to more than 100% owing to a decrease in the property value, the loan amount cannot be included in the calculation of the OC and the issuer must immediately remove the loan from the cover pool register.

» Mortgage bonds issued before 2018 converted into covered bonds:

  » Mortgage loan balance must not exceed 70% of the value of the mortgaged property.

Valuation requirements

The value of a mortgaged property is determined exclusively by the issuer on the basis of the overall evaluation of the respective mortgaged property. This evaluation can only be based on the permanent characteristics of the property, the potential long-term income, the sustainability of the value of the property, the market conditions and the use of the property. The value of the mortgaged property has to be documented in a way that allows for its review.

The issuer is obliged to monitor and periodically evaluate the value of the property in accordance with detailed requirements. The value must be verified at least once in three years, and within one year upon a material change in the real estate market situation or if there is a risk of significant decrease of price of the property compared with prevailing market conditions.

» The property must be evaluated and monitored by a qualified surveyor not involved in the loan generation process. There is no legal obligation to use an external surveyor.

» The property value may be determined and verified either by an individual estimate of the potential purchase price under standard market conditions, or based on a statistical data set, provided data of sufficient quality is available.

Foreign assets in cover pool

The mortgaged property must be located in the Slovak Republic.

Substitute assets

Substitute assets may comprise up to 10% of the value of the cover pool.

Substitute assets may consist of (1) deposits with a central bank, (2) cash, (3) government bonds, and (4) deposits with Slovak or foreign banks or debt securities issued by such banks, subject to CRR requirements. The Slovak covered bond legislation requires substitute assets to have a risk weight that corresponds to the risk weight of a credit quality step 1 or credit quality step 2 institution according to Capital Requirements Regulation.

Derivatives in the cover pool

The issuer must register in the cover pool any derivative contracts entered into to hedge interest and currency mismatches between the covered bonds and the cover pool assets.

Derivative contracts in the cover pool must comply with the requirements set forth under European Market Infrastructure Regulation in respect of covered bonds hedging swaps and they must meet the qualifying criteria for hedge accounting under IFRS 9.

Derivatives are included in the calculation of the cover pool's value only when they are used to mitigate currency risk or to mitigate interest rate risk of substitute assets.

We understand that is it unlikely (although there are some contradictory provisions in the law) that hedge counterparties could rank equally with covered bondholders in relation to the cover pool assets, but would instead rank equally with unsecured creditors of the issuer.

Management of cover pool

Legal minimum OC

Minimum OC of at least 5% on a nominal basis is required. The calculation of the OC is based on the nominal value of assets and liabilities together with accrued interest.

Cover tests and management of key risks

Asset coverage

Asset cover must be maintained on a nominal basis and is required to be calculated monthly.

The value of the underlying loans in the cover pool and that of the covered bonds is calculated on the basis of residual nominal value together with accrued interest. The substitute assets, hedging derivatives (to the extent eligible) and liquid assets are valued at market value.

Failure by the issuer to comply with the matching test or other requirements would entitle the NBS to take a range of actions against the issuer under banking legislation.

Interest rate and currency risk

The issuer is obliged to carry out a stress test at least once per year, covering credit risk, interest rate risk, currency risk, liquidity risk, counterparty risk, operational risk and the risk of a decrease in the value of immovable property. The parameters of the stress test are to correspond with the parameters used in the evaluation of capital adequacy of the issuer.

During the stress test, the issuer has to prove that it is able to keep the coverage level at the statutory value during the stress period. The NBS can require the issuer to provide documentation on form, extent, methods and results of the stress test.

Liquidity risk

The issuer is required to check on an ongoing basis the overall maturity matching of cash flow generated by the cover pool with the payments due under the covered bonds during the following 180 days. If payments are higher than cash flow generated, the issuer is obliged to cover the difference with a buffer of liquid assets, which would form part of the cover pool.

The liquid assets include Level 1 and Level 2A assets[1] and exposures to institutions under Article 129(1)(c) of the Capital Requirements Regulation.

Committed OC/OC quality

Committed OC is expected to be enforceable. The law provides that issuers can stipulate different coverage ratios, higher than the minimum OC of 5%, for different issuances. In such a case, the issuer is obliged to maintain the highest of such ratios for the entire programme until the repayment of the issuance in respect of which the issuer set that level of OC.

OC should initially consist of eligible assets (i.e. LTV threshold at or below 80%) because only loans with LTV at or below 80% may be added to the cover pool. Prior to issuer default, nonperforming loans and loans with LTVs higher than 100% are required to be removed from the cover pool so these will not comprise OC. Loans with LTV higher than 80% but not exceeding 100% may remain in the cover pool, but only the amount up to the LTV threshold would be used to calculate the legal OC.

Treatment of ineligible assets

Assets that become ineligible before issuer default will either be removed from the cover pool register or excluded from the coverage calculation. Regardless of eligibility, to the extent assets have been registered in the cover pool they will form part of the cover pool.

Treatment of nonperforming assets

Nonperforming assets may not be taken into account for the calculation of OC and shall be removed from the cover pool after the consent of the cover pool monitor.

Cover pool monitor

NBS shall appoint a cover pool monitor and a replacement cover pool monitor, on its own initiative or at the proposal of the issuer. Both must be independent from the issuer. The cover pool monitor supervises the process of issuing covered bonds, monitors compliance with the register and the legal requirements such as OC, and reports annually to NBS. The cover pool monitor must also consent to any deregistration of an asset from the register, with the exception of those loans in the cover pool that are repaid.

Role of regulator

The covered bond law does not specify a significant role for the regulator in cover pool management over and above its usual supervisory duties, such as granting and revoking the license to issue covered bonds, or appointing and recalling a cover pool monitor and its deputy. The regulator may also resolve disputes between the issuer and the cover pool monitor.

Cover pool register

The covered bond law requires that the issuer maintains a register of cover pool assets (including mortgage loans, substitute assets, derivatives and liquid assets), issued covered bonds and costs. The issuer and the cover pool monitor (including his or her deputy) are jointly and severally liable to the covered bondholders for the accuracy of the register.

Further details concerning data in the register will be set out in a decree that has not been published yet.

The cover pool is likely to be fixed upon declaration of bankruptcy, so it should include any assets that become ineligible following the declaration of bankruptcy, for example because of becoming nonperforming or not fulfilling the LTV requirement.

Cover pool audit

The cover pool monitor checks the cover pool register and statutory compliance.

The legal framework in detail - After CB anchor event

Issuer default - General

For European jurisdictions subject to the Bank Resolution and Recovery Directive (BRRD)[2], authorities will have wide powers to resolve failing banks prior to an issuer default. Slovakia transposed the EU BRRD into local law through the Act 371/2014 on resolution in the financial market and on amendments to certain laws (Act), in November 2014 and it came into force on 1 January 2015.

Main relevant insolvency law(s)

Act No. 7/2005 Coll. on Bankruptcy and Restructuring, as amended by Act No. 279/2017 Coll.

Triggers for issuer default

Issuer default would be typically triggered by a declaration of bankruptcy in relation to the issuer.

Appointment of administrator before issuer default

There is no cover pool administrator under the Slovak covered bond legislation. The issuer's general insolvency administrator will administer the cover pool in case of bankruptcy.

Responsibility for cover pool administration following issuer default

After the declaration of bankruptcy, the cover pool and the issuer will be run by the same general insolvency administrator. However, the cover pool will be segregated from the general insolvency estate of the issuer and will form a separate covered bond estate.

Role of the regulator at time of issuer default

The covered bond law does not specify a special role for the regulator at the time of issuer default. The regulator will continue to supervise the issuer and the covered bond programme.

Unsecured claim (additional)

The covered bondholders have an unsecured claim over the issuer's assets for any shortfall in the proceeds of the covered bond estate. The insolvency administrator is required to prepare a payment plan for the separate covered bond estate and general bankruptcy estate without undue delay. We understand that the insolvency administrator would likely not delay payment to unsecured creditors of the proceeds under the general bankruptcy estate payment plan, but should set aside a portion of the proceeds to which covered bondholders might become entitled in due course.

Cover pool asset and cash flow segregation and priority rights

Segregation of cover pool assets

If the bankruptcy proceedings are initiated against the issuer, the cover pool will form the covered bond estate, which is segregated from any other assets of the issuer. The covered bond estate will be administered by the general insolvency administrator.

Priority right of covered bondholders vs. unsecured creditors

The covered bond law provides that covered bondholders have priority over all assets registered in the cover pool.[3]

Priority between covered bondholders and others entitled to a claim on the cover pool

The proceeds from the covered bond estate may only be used to satisfy the claims of the covered bondholders, after the costs of the administration on liquidation of the covered bonds estate, including administrator's fees, have been discharged.

Derivatives counterparties would not have a priority right in respect of the cover pool, so they would not rank pari passu with covered bondholders.

Priority for OC

Covered bondholders and other permitted claimants will have priority claim with respect to OC, both up to and in excess of the legal minimum OC.

Protection of cash flow from cover pool assets (commingling risk)

The general insolvency administrator will administer the covered bond programme in bankruptcy. Because the issuer must maintain separate analytic records of the covered bonds in its accounting system it should be possible to identify cover pool cash flows in relevant collections accounts. This reduces the risk that cash will be commingled.

However, if for any reason cash flow is commingled in the same bank account (for example, as a result of an error), the covered bondholders will have a priority right in respect of identified cash flow from cover pool assets.

Set-off

Set-off against cover pool assets is permitted under the Insolvency Act. (See "Cover Pool Analysis")

Security

No additional security interest is created over the cover pool.

Rights to foreign assets

Eligible loans cannot be secured by properties outside Slovakia.

<u>Management of cover pool</u>

Duties and powers of administrator/covered bond administrator

There is no specific role of cover pool administrator under the Slovak covered bond legislation. The programme will be managed by the general insolvency administrator of the issuer in bankruptcy.

The general insolvency administrator is in charge of the covered bond programme and will effectively run it as a separate estate from the bankruptcy estate. The insolvency administrator has an obligation to administer the covered bond programme with professional care.

The general insolvency administrator has a duty to continue administrating the programme, including servicing of the cover pool loans and allocation of cash to covered bondholders.

The cover pool monitor will continue in its role after issuer default, and will become a member of the creditors committee of the issuer.

Can an administrator/covered bond administrator enter into contracts for hedging post-issuer default?

We understand that in principle the issuer's insolvency administrator would be entitled to enter into new hedging derivatives as long as it is in the best interests of the covered bondholders. However there are no specific rules on this in the covered bond law.

Restrictions on enforcement of cover pool assets by administrator/covered bond administrator

We are not aware of any particular restrictions on the administrator’s ability to enforce the issuer’s rights with respect to loans and securities in the cover pool.

Ongoing role of regulator

NBS is not expected to act as servicer or administrator of last resort. The regulator appoints the general insolvency administrator and will continue to be involved in the general oversight of the covered bond programme, including approving the transfer of the covered bond programme, or approving a second 12-month extension period on the covered bonds, amongst other things.

Liquidity reserve for interest payments

The covered bond law provides for a reserve of liquid assets based on covering a rolling 180 days of net outgoing cash flow. (See “Covered bond description - The legal framework in detail - Before CB anchor event - Liquidity risk”)

<u>Refinancing the covered bonds</u>

Specific provisions in the law for liquidity to address refinancing risk - General

See “Covered bond description - The legal framework in detail - Before CB anchor event - Liquidity risk” above in respect of the mandatory test ensuring liquidity for payments up to the next 180 days.

Should the general insolvency administrator, together with the cover pool monitor, determine that the management of the covered bond programme is likely to result in a lower rate of satisfaction of the covered bondholders, it shall notify the NBS of the intention to transfer the covered bond programme or part of it to a third party (that must be a Slovak bank). Following this notification, the maturity of any covered bonds that would otherwise fall due within the first 12 month period will automatically be extended by 12 months[4] Note, however, that the maturity extension will not apply to any mortgage bonds issued before 01 January 2018, regardless of whether they are converted into covered bonds or not.

It is also possible for the issuer to consent to a transfer of the covered bond programme along these lines in the case of an involuntary administration. Involuntary administration is a temporary preventative measure, similar to a restructuring, that may be imposed by NBS.

If the covered bond programme is not transferred during the first 12 months, maturities can be extended by another 12 months, on request to the NBS.[5] This second extension to would apply to principal amounts falling due either (1) as a result of the previous extension, or (2) for the first time during the second 12 month period.

Either the first or second maturity extension may terminate earlier than 12 months if the NBS refuses its consent to the transfer.

If the general insolvency administrator fails to transfer the covered bond programme, it is entitled to realise the receivables arising under mortgage loans in the cover pool by transferring them to a bank, including foreign banks.

If the transfer of the covered bond programme cannot be achieved and the general insolvency administrator considers that the management of the covered bond programme may result in a lower rate of satisfaction of the covered bondholders, it shall terminate the management of the covered bond programme as a part of the business of the bankrupt issuer, and the covered bonds will accelerate.

Following the termination of the management of the covered bond programme, the general insolvency administrator shall notify this termination to the mortgage loan borrowers and there is a period of time, not shorter than three months, during which they have the right to prepay their mortgage loans voluntarily, without any prepayment fees. After this period, prepayment of the claims corresponding to the mortgage loans can be enforced pursuant to Slovak law.

Transfer of cover pool assets together with liabilities

This is possible and contemplated under the law, in combination with maturity extensions. See above *Specific provisions in the law for liquidity to address refinancing risk - General*.

Sale of cover pool assets

Sale of cover pool assets is not initially envisaged, rather it is expected that the covered bond programme will be transferred in full to a single transferee or broken up and transferred in full to multiple transferees (i.e. so that no part remains with the issuer).

Sale of cover pool assets is permitted only when the general insolvency administrator fails to transfer the covered bond programme within the timeline envisaged under the law. The mortgage loans are the only assets that can be sold, and foreign banks can also be transferees, unlike in the transfer process, where only Slovak banks can be transferees. In deciding to sell assets the insolvency administrator must act with professional care to determine whether such sales will lead to a higher rate of satisfaction of the covered bondholders.

Can the administrator enter into liquidity loans or repo agreements, or both?

The law does not specifically provide for either liquidity loans or repo financing to be available to refinance covered bonds. In principle, the insolvency administrator, acting in the best interests of the covered bondholders, would be entitled to make new borrowings. However, liquidity loan providers would not be entitled to priority or pari passu status with covered bondholders, so would not be incentivised to provide loans.

Acceleration of covered bonds

Upon issuer default the covered bonds will continue to make payments as long as the programme has not been terminated by the administrator (and subject to any maturity extensions).

Under the general insolvency rules, termination will occur if:

» At any time, the NBS gives instruction to the administrator to terminate the management of the covered bond programme;

» the administrator determines at any time, acting with professional care, that termination of the covered bond programme and acceleration will be actually beneficial to covered bondholders; or

» The administrator fails to transfer the covered bond programme to another bank or banks within the timeline envisaged under the law and the administrator considers that the level of satisfaction of the covered bondholders is likely to decrease in case of continuing the management of the programme (including asset sales).

Time subordination

When assessing if the management of the covered bond programme would reduce the degree of satisfaction of the covered bondholders, the Slovak covered bond legislation specifies that fair satisfaction of holders of later-maturing covered bonds shall also be taken into account.

Furthermore, the consequence of an acceleration of the covered bond programme is that all claims under the covered bonds will become immediately due and payable. Thus if acceleration occurs, holders of later-maturing covered bonds will be protected against time subordination.

Covered bond 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 would be made in a timely fashion following a CB anchor event, which we measure using the Timely Payment Indicator. (See “Timely Payment Indicator”)

Primary analysis

Issuer analysis - Credit quality of the issuer

The issuer's CR assessment is A1(cr). (For a description of the issuer's rating drivers, see Credit Opinion, published in May 2018)

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 Slovakia is the CR assessment plus one notch.

Issuer analysis - Dependency on the issuer's credit quality

The credit quality of the covered bonds depends primarily on the credit quality of the issuer. If the issuer's credit strength were to 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 were to decrease.

In the event that the CB anchor deteriorates, the issuer would have the ability, but not the obligation, to increase the OC in the cover pool. Failure to increase the level of OC under these circumstances could lead to a negative rating action.

Reasons for the high level of dependency of the covered bonds on 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 and remove assets from the cover pool, issue further bonds and enter new hedging arrangements. Such actions could reduce 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, which creates substitution risk. Nevertheless, cover pool quality over time will be protected by, among other things, the requirements of the Slovak covered bond legislation, which specifies what types of assets are eligible. (See “Covered bond description - Legislation”)

Refinancing risk

Following a CB anchor event, the natural amortisation of the cover pool assets alone cannot be relied on to repay the 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 subject to volatility. 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”)

The refinancing-positive aspects of this covered bond programme include:

» A portfolio of prime residential mortgage loans is perceived to be of better credit quality and thus could improve sale conditions.

» The 180 day liquidity requirement could provide more time for arranging and negotiating the terms of refinancing.

The refinancing-negative aspects of this covered bond programme include:

» All covered bonds outstanding have a bullet repayment at maturity, without any contractual extension period for the repayment of the bonds. The maturity of covered bonds issued after 1 January 2018 can be extended up to 24 months under the covered bond law, however the maturity of the bonds issued before 2018 cannot be extended. (See “Additional analysis - Extension period”)

» The relatively small size of the Slovak economy and low systemic importance of covered bonds as a funding tool could make it difficult to sell a relatively large mortgage portfolio at moderate prices.

Interest rate and currency risk

As with the majority of European covered bonds, there is potential for interest rate and currency risks, which could arise from the different payment promises on, and durations of, the cover pool and the covered bonds.

Exhibit 4
Overview of assets and liabilities

	WAL Assets (Years)	WAL Liabilities (Years)	Assets (%)	Liabilities (%)
Fixed rate	10.9	3.4	80.7%	88.0%
Variable rate	9.9	1.3	19.3%	12.0%

WAL = weighted average life
n/a = not applicable
Sources: SLSP, Moody's Investors Service

In the event of issuer insolvency, we currently do not assume that the general insolvency administrator would always be able to efficiently manage any natural hedge between the cover pool and the covered bonds. Therefore, following a CB anchor event, our model would separately assess 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.

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

» No currency risk. Currently, all the assets and liabilities are denominated in euros.

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

» All mortgage loans in the cover pool have a fixed rate. After a CB anchor event, a potential sale of fixed-rate assets to meet payments due on covered bonds could lead to a crystallisation of mark-to-market losses caused by interest rate movements. However, the short duration of the cover assets (average reset in 2.65 years) reduces their sensitivity to interest rate risk in case of a cover pool sale.

» Although low, there is an interest rate mismatch between assets and liabilities. As of the date of this report, the issuer has not entered any swaps into the cover pool register. If swaps are entered into, the probability that covered bondholders will be exposed to the effect of market rate movements depends on the strength of the hedging arrangements and the likelihood that the issuer will fail to make its swap payments.

Timely Payment Indicator

Our Timely Payment Indicator (TPI) assesses the likelihood that timely payments would 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 level of OC. We have assigned a TPI of Improbable to these covered bonds.

Based on the current TPI of Improbable, the TPI leeway for this programme is one notch. This one-notch leeway implies that we might downgrade the covered bonds' rating because of a TPI constraint if we were to lower the CB anchor by more than one notch, all other variables being equal.

The TPI-positive aspects of this covered bond programme include:

» The issuer is required to cover potential liquidity gaps over the next 180 days between payments expected to be received under the cover pool assets and payments due under the outstanding covered bonds. See "Covered bond description - The legal framework in detail - Before CB anchor event - Liquidity risk".

» The Slovak covered bond legislation and the level of government support provided to covered bonds in Slovakia.

» The other refinancing-positive factors discussed in "Covered bond analysis - Refinancing risk" above.

The TPI-negative aspects of this covered bond programme include:

» Although acting with professional care and protecting the interest of the covered bondholders, the general insolvency administrator has the discretion to accelerate the covered bonds after failing to transfer the covered bond programme, potentially creating refinancing risk.

» All covered bonds outstanding have a bullet repayment at maturity, without any contractual extension period for the repayment of the bonds. The maturity of covered bonds issued after 1 January 2018 can be extended under the covered bond law for up to 24 months, however the maturity of the bonds issued before 2018 cannot be extended. See "Additional Analysis - Extension period" below.

» Set-off: See "Cover pool analysis - Additional cover pool analysis - Set-off risk".

The Slovak covered bond legislation does not provide for the appointment of a special administrator for the covered bonds after issuer insolvency who must prioritise the interests of covered bondholders and have the powers necessary for that purpose. Nevertheless, the general insolvency administrator owes a separate duty of professional care to the covered bondholders, must consult the cover pool monitor in some decisions, and has the power to transfer the programme and sell the cover pool assets.

Additional analysis

Liquidity

Before issuer default, the Slovak covered bond legislation requires the issuer to cover any projected liquidity gaps for the next 180 days and to maintain a minimum OC level of 5%. However, the covered bond programme would not benefit from any designated source of liquidity if scheduled cash flow collections were to be interrupted and lead to greater than expected liquidity gaps.

After an issuer default, and provided that the transfer of the covered bond programme to another entity fails, the general insolvency administrator would have the ability to sell a portion of the cover pool to make timely payments on the bonds.

Extension period

Based on the Slovak covered bond legislation, principal payments on covered bonds maturing up to 24 months after issuer default can be extended by:

» for bonds maturing within 12 months of issuer default, two consecutive periods of 12 months from their scheduled maturity[6]; and

» for bonds maturing 12-24 months after issuer default, 12 months from their scheduled maturity.

However, the maturity of the mortgage bonds issued before January 2018 and converted into covered bonds cannot be extended. See "Covered bond description - The legal framework in detail - Before CB Anchor Event - Duties and powers of administrator/covered bond administrator".

The existence of these converted mortgage bonds in the covered bond programme limits the effectiveness of the extension period to mitigate refinancing risk. These bonds can also negatively affect the transfer of the covered bond programme if they become due and payable during the search for a potential transferee.

Time subordination

After a CB anchor event, but prior to acceleration of the covered bonds, later-maturing covered bonds would be subject to time subordination. Principal cash collections may be used on a first-come, first-served basis, paying earlier-maturing covered bonds before later-maturing covered bonds. Such payments could result in the erosion of OC before any payments are made to later-paying covered bonds. The risk of time subordination is partially mitigated by the insolvency administrator's obligation to consider the interests of the holders of later-maturing covered bonds.

Cover pool description

Pool description as of 31 May 2018

The cover pool consists of residential mortgage loans, based on data as of the cut-off date. All the properties backing the loans and the rights are in Slovakia. The cover pool assets total €3.18 billion, which back €1.13 billion in covered bonds, resulting in an OC level of 182% on a nominal-value basis. Furthermore, the issuer will register €110 million Slovak government bonds as liquid assets in the cover pool.

For SLSP's underwriting criteria, see "Appendix: Income underwriting and valuation".

Exhibits below show more details about the cover pool characteristics.

Residential mortgage loans

Exhibit 5
Cover pool summary

Overview	
Asset type:	Residential
Asset balance:	3,186,436,735
Average loan balance:	38,699
Number of loans:	82,338
Number of borrowers:	77,174
Number of properties:	92,385
WA remaining term (in months):	239
WA seasoning (in months):	38

Details on LTV	
WA unindexed LTV (*):	53.8%
WA indexed LTV:	51.2%
Valuation type:	Lending Value
LTV threshold:	n/a
Junior ranks:	13.7%
Prior ranks:	0.0%

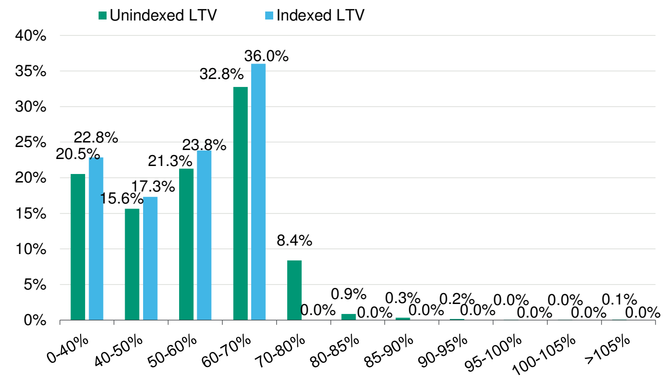
Specific Loan and Borrower characteristics	
Loans with an external guarantee in addition to a mortgage:	0.0%
Interest only Loans:	0.0%
Loans for second homes / Vacation:	0.0%
Buy to let loans / Non owner occupied properties:	0.0%
Limited income verified:	0.0%
Adverse credit characteristics (**):	0.0%

Performance	
Loans in arrears (≥ 2months - < 6months):	0.0%
Loans in arrears (≥ 6months - < 12months):	0.0%
Loans in arrears (≥ 12months):	0.0%
Loans in a foreclosure procedure:	0.0%

Multi-Family Properties	
Loans to tenants of tenant-owned Housing Cooperatives:	0.0%
Other type of Multi-Family loans (***):	0.0%

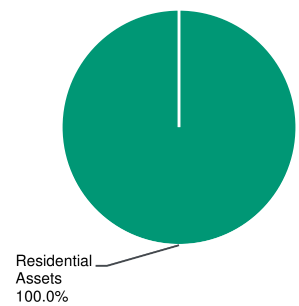
n/d: information not disclosed by Issuer
n/a: information not applicable
Sources: SLSP, Moody's Investors Service

Exhibit A
Balance per LTV band



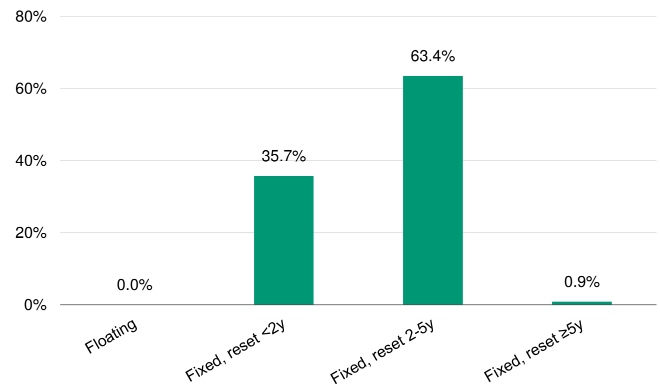
Sources: SLSP, Moody's Investors Service

Exhibit B
Percentage of residential assets



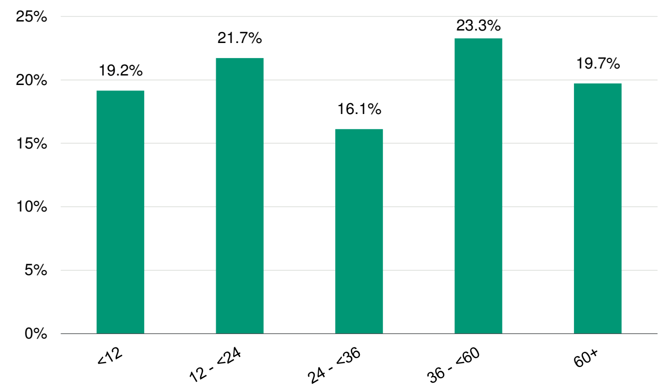
Sources: SLSP, Moody's Investors Service

Exhibit C
Interest rate type



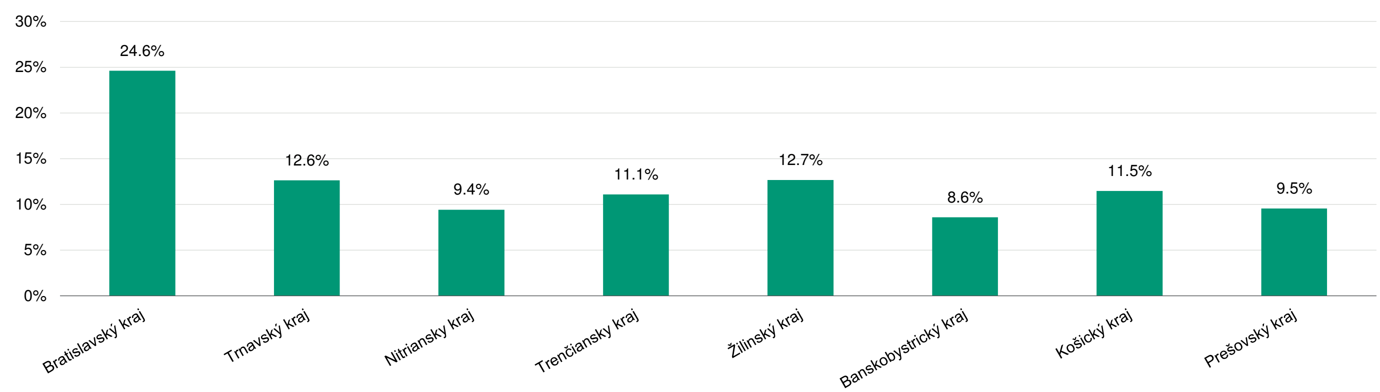
Sources: SLSP, Moody's Investors Service

Exhibit D
Seasoning (in months)



Source:

Exhibit E
Main country regional distribution



Sources: SLSP, Moody's Investors Service

Liquid assets

The issuer will also register €110 million Slovak government bonds as liquid assets used to cover the 180 days liquidity buffer required by law, which will form part of the cover pool and will be included in the calculation of the OC.

Cover pool monitor

Pursuant to the Slovak covered bond legislation, the regulator (NBS) has appointed a cover pool monitor and a backup cover pool monitor. (See "Covered bond description - The Legal Framework in Detail - Before CB Anchor Event - Cover pool monitor")

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

We calculate the collateral score for the cover pool using a scoring model to assess the credit risk for the residential assets in the cover pool. Our analysis takes into account, among other factors, the LTV ratios of the mortgage loans, the seasoning and the geographical distribution.

For this programme, the collateral score of the current pool is 7.4% as of the cut-off date. For details, see "Moody's related research - Moody's Global Covered Bonds Monitoring Overview: Q4 2017".

The following factors support the credit quality of the pool:

» All the assets are performing as of the cut-off date of this report.

» All loans are granted to individuals and are secured by a first economic lien on residential properties in Slovakia.

» The WA unindexed LTV of the residential assets is relatively low at 53.8%. Furthermore, the weighted average seasoning of the loans is 38 months, a relatively high figure.

» All residential mortgage loans are denominated in euros (local currency). Therefore, borrowers are not exposed to currency risk.

On the other hand, we take into account in our analysis the following portfolio characteristics as credit negative:

» Some properties also secure other, junior-ranking, housing loans, resulting in higher borrower leverage. In total, these additional liens amount to 13.7% of the cover pool.

» Although property valuations are usually carried out by an external appraiser, the issuer is not bound by this valuation. Furthermore, the issuer has used internal desktop valuations for some properties backing mortgage loans with balances lower than €40,000.

Additional cover pool analysis

Set-off risk

Deposit compensation in Slovakia operates on a net basis, meaning that mortgage loan borrowers would set-off their mortgage loan obligations against their bank deposits before claiming only the difference, or net amount, from the SDGS.

We expect set-off rights to generally be available to depositors with mortgage loans. Set-off in respect of the obligations of a bankrupt Slovak entity and its counterparty is generally permitted, subject to some limitations including registration of the claim. Obligations that arise before insolvency cannot be set off against obligations that arise after insolvency, however we understand a Slovak court is likely to treat a mortgage loan as a single pre-insolvency claim that can be set off against a bank deposit that is also a pre-insolvency claim.

The right of set-off could be constrained by the market practice of including contractual limitations on set-off in mortgage agreements, however there is a risk that such provisions would be held non-enforceable on the basis of consumer protection legislation, insolvency or otherwise.

Our expected loss model takes into account the impact of set-off risk operating on a net basis through an addition to the collateral score.

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.moodys.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.moodys.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 lack of data availability could negatively affect the ratings or, in some cases, our ability to continue to rate the covered bonds.

Appendix: 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
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
For the purpose of any IST:	
7 Is it confirmed that income after tax is sufficient to cover both interest and principal?	Yes
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 all period of repayment. No exceptions.
9 Does the age of the borrower constrain the period over which principal can be amortised?	Yes
10 Are any stresses made to interest rates when carrying out the IST? If so when and for what type of products?	Yes, regulated by Central Bank (+2% p.a.) in case of secured loans.
11 Are all other debts of the borrower taken into account at the point the loan is made?	Yes
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 living expenses prepared by the Ministry of Labour, social affairs and Family. These are published in each year and relevant for all Banks. The percentage of post-tax income that is assumed to be available for debt repayment is up to 60 % (maximum).
Other comments	None

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
3 How are valuations carried out where an external valuer not used?	There is a group of valuations where we used internal value instead of external valuators - transactions for flats up to EUR 40,000 exposure (application of Internal Desktop Valuation Tool) and setting of Internal Collateral Values in Housing Development Projects during construction phase.
4 What qualifications are external valuers required to have?	University degree in construction, certification of the University of Žilina as appraisal expert, approbation of the Ministry of Justice as court sworn valuators for constructions, conclusion of a personal indemnity insurance and have at least 5 year experience.
5 What qualifications are internal valuers required to have?	The qualification is the same as for external valuers. In addition proven long-term reliability and performance quality is required.

6 Do all external valuations include an internal inspection of a property?	Yes
7 What exceptions?	None
8 Do all internal valuations include an internal inspection of a property?	No
9 What exceptions?	None

Source: Slovenska Sporitelna

Moody's related research

Rating Methodology

» Moody’s Approach to Rating Covered Bonds, December 2016 (1044142)

Special Comments

» Covered Bonds: Slovakian bank's conversion of old covered bonds is credit positive, June 2018 (PBS_1129444)

» Tighter Underwriting Standards Are Credit Positive for Slovak Covered Bonds, March 2017 (PBS_1062934)

» Amendments to Slovakia's covered bond law are credit positive, November 2017 (PBS_1097616)

» Amended covered bond law will reduce liquidity risk - a credit positive, February 2018 (PBC_1108757)

» Moody's Global Covered Bonds Monitoring Overview: Q4 2017, June 2018 (PBS_1127159)

Credit Opinion

» Slovenska Sporitelna, a.s.

Webpages

» Covered Bonds: www.moodys.com/coveredbonds

» Covered Bond Legal Frameworks: www.moodys.com/Pages/CoveredBondLegalFrameworks.aspx

To access any of these reports or webpages, 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

1 Categories under EU liquidity coverage ratio requirements

2 Directive 2014/59/EU of the European Parliament and the Council establishing a framework for the recovery and resolution of credit institutions and investment firms, 15 May 2014.

3 This does not apply to covered bondholders that are related parties to the issuer; these will be treated as unsecured creditors.

4 During the first month, the issuer is obliged to fulfill liabilities arising from the covered bond programme within original maturity periods.

5 The maturity of the mortgage bonds issued before 1 January 2018, even after being converted into covered bonds, cannot be extended.

6 During the first month, the issuer is obliged to fulfill liabilities arising from the covered bond programme within original maturity periods.

REPORT NUMBER 1132579

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