

Outlook On Three Icelandic Covered Bond Programs Revised To Positive Following Action On Iceland; Ratings Affirmed

May 25, 2023

Overview

- On May 12, 2023, we affirmed our 'A/A-1' long- and short-term sovereign credit ratings on Iceland, and revised the outlook on the ratings to positive from stable.
- Following this action and the application of our criteria, we affirmed our 'A' ratings on Islandsbanki hf, Landsbankinn hf, and Arion Bank hf's mortgage covered bonds. We also revised the outlook on the ratings to positive from stable.
- Our outlook on these ratings reflects the positive outlook on our long-term sovereign rating on Iceland.

FRANKFURT (S&P Global Ratings) May 25, 2023--S&P Global Ratings today revised to positive from stable its outlooks on Islandsbanki hf. (issuer credit rating [ICR]: BBB/Stable/A-2), Landsbankinn hf. (ICR: BBB/Stable/A-2), and Arion Bank hf.'s (ICR: BBB/Negative/A-2) mortgage covered bond programs and related issuances. We also affirmed our 'A' ratings on these three programs.

Today's rating actions follow our May 12, 2023 action on Iceland (see "Iceland Outlook Revised To Positive From Stable On Improving Public Finances And Strong Growth; 'A/A-1' Ratings Affirmed").

Our ratings on Landsbankinn hf., Islandsbanki, and Arion Bank's mortgage covered bond programs reflect the application of our covered bonds criteria, our structured finance sovereign risk criteria, and the remaining criteria referenced in the related criteria section below.

Under our covered bonds criteria, in determining the reference rating level (RRL), we add two notches above the ICR on Islandsbanki, Landsbankinn, and Arion Bank to reflect the increased probability that the issuer can service its covered bonds. Consequently, we have assessed the RRL as 'a-', two notches above the 'BBB' long-term ICR on each issuer.

Given our strong jurisdictional assessment of mortgage covered bonds in Iceland, under these criteria, we can assign up to two notches of jurisdictional uplift above the RRL. As our long-term sovereign rating on Iceland is 'A', the uplift is capped at the sovereign rating, and therefore these programs receive only one notch of jurisdictional support uplift, which results in a jurisdiction-supported rating level (JRL) of 'a'. This implies one unused notch of jurisdictional support that would protect the ratings in the event of an issuer downgrade by one notch.

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Under our structured finance sovereign risk criteria, a foreign-currency obligation backed by local- or foreign-currency assets in a single jurisdiction is capped at the transfer and convertibility (T&C) assessment for that jurisdiction, unless there are structural mitigants for T&C risk.

In the absence of such mitigants, the ratings on the euro-denominated covered bonds, but also on all existing and Icelandic krona-denominated covered bonds, are currently capped at the T&C assessment for Iceland, which is at the same rating level of the sovereign, 'A'.

Further, the ratings on the covered bonds are not constrained by counterparty, legal, and operational risks, in our view.

Consequently, following the revised outlook to positive from stable on our sovereign ratings on Iceland, we revised the outlook to positive from stable on our 'A' ratings on these three mortgage covered bond programs and related issuances. We also affirmed our 'A' ratings on the covered bonds.

The positive outlook reflects that a positive rating action on the sovereign, considering the T&C assessment is at the same level of the sovereign, will result in a positive rating action on the covered bonds, all else being equal. However, a negative rating action on the issuers will not have an impact on the respective covered bonds. This is because each of the three programs benefit from one unused notch of uplift that would protect the rating in an event of an issuer downgrade, all other things remaining equal.

Related Criteria

- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings , Oct. 10, 2021
- Criteria | Structured Finance | General: Counterparty Risk Framework: Methodology And Assumptions , March 8, 2019
- Criteria | Structured Finance | General: Incorporating Sovereign Risk In Rating Structured Finance Securities: Methodology And Assumptions , Jan. 30, 2019
- Legal Criteria: Structured Finance: Asset Isolation And Special-Purpose Entity Methodology , March 29, 2017
- Criteria | Structured Finance | Covered Bonds: Covered Bond Ratings Framework: Methodology And Assumptions , June 30, 2015
- Criteria | Structured Finance | Covered Bonds: Covered Bonds Criteria , Dec. 9, 2014
- General Criteria: Principles Of Credit Ratings , Feb. 16, 2011

Related Research

- Iceland Outlook Revised To Positive From Stable On Improving Public Finances And Strong Growth; 'A/A-1' Ratings Affirmed, May 12, 2023
- Iceland-Based Arion Bank Outlook Revised To Negative On Uncertain Capital Trajectory; Ratings Affirmed At 'BBB/A-2', May 10, 2023
- Transaction Update: Landsbankinn hf. Covered Bond Programme, April 20, 2023
- Global Covered Bond Insights Q2 2023: The Implications Of Rising Interest Rates, April 12, 2023

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- Islandsbanki hf, Aug 19, 2022
- Ratings Raised On Landsbankinn hf And Arion Bank hf's Icelandic Covered Bond Programs On Effective Icelandic Resolution, May 27, 2022
- Resolution Counterparty Ratings Jurisdiction Assessment For Iceland Completed, May 17, 2022
- Glossary of Covered Bond Terms, April 27, 2018
- S&P Global Ratings Definitions, Nov. 10, 2021

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