

Rating Action: Moody's confirms Sparebanken Hedmark's A2/P-1 deposits ratings; outlook stable

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Standalone BFSR affirmed but BCA lowered to baa2 from baa1

London, 02 July 2013 -- Moody's Investors Service has today confirmed Sparebanken Hedmark's A2 long-term and Prime-1 short-term deposit ratings and lowered the bank's baseline credit assessment (BCA) to baa2 from baa1 within the C- standalone bank financial strength rating (BFSR) category. All ratings now carry a stable outlook.

The lowering of the BCA primarily reflects Moody's view that the increased ownership stake in Bank 1 Oslo Akershus AS (unrated) increases Sparebanken Hedmark's risk profile.

The confirmation of the long-term and short term deposit ratings reflects Moody's expectation that Sparebanken Hedmark will benefit from support from the SpareBank 1 Alliance if needed.

Today's rating actions conclude the review for downgrade on Sparebanken Hedmark's deposit ratings initiated on 4 March 2013.

RATINGS RATIONALE

On 18 January 2013, Sparebanken Hedmark announced that it will increase its stake in Bank 1 Oslo Akershus to 40.5% from 12.0%, purchasing shares from fellow SpareBank 1 Alliance members SpareBank 1 SR-Bank ASA (deposits A2 stable; BFSR C-/BCA baa2 stable), SpareBank 1 SMN (A2 stable; C-/baa2 stable) and SpareBank 1 Nord-Norge (A2 stable; C-/baa1 stable). The transaction was approved by the Ministry of Finance on 26 April 2013 and will be reflected in the bank's forthcoming Q2 2013 results.

--- LOWERING OF THE BCA

The lowering of the BCA to baa2 from baa1 reflects Moody's view that the increased ownership stake increases Sparebanken Hedmark's risk profile, notwithstanding some franchise benefits.

In particular, the rating agency expects that the increased stake in Bank 1 Oslo Akershus renders Sparebanken Hedmark's revenue profile less stable, because it increases the portion of revenue stemming from ownership interests and exposes Sparebanken Hedmark to the volatility in Bank 1 Oslo Akershus's profitability. In addition, Moody's believes that the downside risk may not be limited to Sparebanken Hedmark's direct ownership interest in the bank (NOK946 million or around 15% of Sparebanken Hedmark's equity capital at end-March 2013). This is because the rating agency expects that as a strategic owner, Sparebanken Hedmark may have to provide support to Bank 1 Oslo Akershus if it encounters difficulties.

Moody's views Bank 1 Oslo Akershus's credit profile as generally weaker than that of Sparebanken Hedmark, in particular because of (1) the rapid growth in its loan book (+18% in 2012 including loans transferred to the Alliance covered bond companies); (2) lack of efficiency of its operations (2012 cost-to-income close to 70%); and (3) its substantial exposure to the real-estate sector through both its lending and brokerage activities.

The transaction's negative impact on Sparebanken Hedmark's capital is largely mitigated by its recent Tier 2 issuance, which means that the bank estimates its Tier 1 ratio will be reduced by less than two percentage points post-transaction, compared to 15.8% reported at end-March 2013 (calculated under Basel II rules, including the transitional floor); however, the effect is expected to be somewhat more pronounced under Basel III. Nevertheless, this level continues to compare well with those reported by most other rated Norwegian savings banks.

Whilst in Moody's view the benefits to Sparebanken Hedmark's franchise are marginal as the increased involvement in Bank 1 Oslo Akershus is primarily regarded as an investment at this stage, the rating agency positively notes that there could be some limited benefits in terms of cross-selling of products between the two banks which operate in neighbouring counties.

Moody's also notes the potential challenges in exerting control on a partially-owned company, although the bank at this stage avoids the further integration of Bank 1 Oslo Akershus's operations, and the risks related to such integration. Sparebanken Hedmark will also likely benefit from Bank 1 Oslo Akershus's local expertise, because the two banks remain separate entities as per the transaction.

--- CONFIRMATION OF THE DEPOSIT RATINGS

The confirmation of Sparebanken Hedmark's deposit ratings reflects Moody's expectation that Sparebanken Hedmark will benefit from support from the SpareBank 1 Alliance. The rating agency believes that, following the transaction and the lowering of Sparebanken Hedmark's standalone credit assessment, the capacity of the overall Alliance to provide support to its members is broadly unchanged, and expects that such support will be extended to Sparebanken Hedmark if needed. As for the other rated banks in the Alliance, Sparebanken Hedmark's deposit ratings incorporate a low probability of Alliance support, which at the lower BCA level translates into one notch of rating uplift under Moody's joint-default analysis.

WHAT COULD MOVE THE RATINGS UP/DOWN

Upward rating momentum could develop if Sparebanken Hedmark (1) reduces the downside risks to its asset quality, e.g., the high credit concentration and substantial exposure to the real-estate segment (which we view as typically more volatile); and/or (2) strengthens its liquidity position with increased buffers and reduced asset-liability mismatches. At the same time, the bank will have to demonstrate that it is able to manage the risks involved with its increased exposure to Bank 1 Oslo Akershus in a way that does not significantly impair its ability to generate stable earnings.

Whilst the current BCA incorporates a degree of expected further deterioration, further downward pressure could arise from (1) deterioration in Sparebanken Hedmark's funding position, e.g., reduced ability to access capital markets or deposit outflows; and/or (2) higher-than-expected losses in its loan book, or losses stemming from its ownership interests. In addition, downwards pressure could be exerted on the ratings due to external factors, such as a less supportive macroeconomic environment and/or substantially adverse developments in the Norwegian real-estate market. The deposit ratings could be downgraded if Moody's considers that the probability of Alliance or systemic support has reduced.

The data referred to in this press release is generally sourced from Sparebanken Hedmark's most recent interim report and audited annual reports as well as press releases published on the Oslo Børs's website.

Headquartered in Hamar, Norway, Sparebanken Hedmark reported total consolidated assets of NOK44.3 billion (EUR5.6 billion) at the end of March 2013.

The principal methodology used in this rating was Global Banks published in May 2013. Please see the Credit Policy page on www.moody.com for a copy of this methodology.

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