FITCH AFFIRMS NORWEGIAN SAVINGS BANKS

Fitch Ratings-London-04 November 2015: Fitch Ratings has affirmed SpareBank 1 Nord-Norge's (SNN) Long-term Issuer Default Rating (IDR) at 'A', SpareBank 1 SMN's (SMN), SpareBank 1 SR-Bank's (SR) and Sparebanken Vest's (SV) Long-term IDRs at 'A-', and Sandnes Sparebank's (Sandnes) Long-term IDRs at 'BBB'. The Outlooks on all Long-term IDRs are Stable. A full list of rating actions is at the end of this rating action commentary.

The rating actions were part of Fitch's periodic review of Norwegian savings banks.

KEY RATING DRIVERS
IDRS, VRS AND SENIOR DEBT
The affirmations of SNN's, SMN's, SR's and SV's (collectively Sparebanken) ratings are based on their strong regional franchises, healthy profitability, resilient asset quality and sound capital ratios. The ratings also factor in risks arising from the significant rises in property prices in recent years, geographically concentrated lending, and liquidity management in the context of the banks' wholesale funding reliance. SNN's ratings are one notch higher than those of its Sparebanken peers, reflecting stronger capitalisation and a more retail-orientated business model, particularly for its funding structure.

Sandnes' ratings reflect its adequate profitability, improving asset quality, good capitalisation, as well as its entrenched regional presence in south-western part of Norway, although its smaller franchise relative to its domestic peers and geographical concentration constrain the ratings.

The Sparebanken's and Sandnes' profitability remains resilient, underpinning solid internal capital generation. The banks' regional franchises support stable revenue generation, and cost efficiency is acceptable. Despite continued low oil prices, Fitch expects relatively modest loan impairment charges in 2016. Lending margins for retail mortgage loans are under pressure given increased competition, but should remain satisfactory. The banks benefited from the repricing of corporate deposits in 9M15, and Fitch expects this to continue into 2016.

The Sparebanken's asset quality is strong, driven by a relatively stable operating environment and conservative underwriting standards. Concentration risk relating to large exposures is reducing, and Fitch expects the banks to continue to implement low risk business models that focus on retail and small and medium-sized (SME) customers. A significant house price correction is a key sensitivity for the banks. While Fitch does not expect such a scenario to lead to a significant deterioration of the quality of the banks' retail lending, reduced consumption would most likely negatively impact their SME portfolios.

SNN is less exposed to this risk, given the relatively lower house prices in northern Norway compared with other parts of the country and the large public sector presence. SR has relatively high sector concentration risk, given its exposure to the oil sector in south-west Norway.

Sandnes' unreserved impaired loans has started to come down and represented less than 20% of Fitch Core Capital at end-June 2015 (around 25% at end-2012), a manageable amount in Fitch's view. Impaired loans, essentially relating to legacy commercial real estate (CRE) loans, also declined to 2.6% (of which 2.1 percentage points are performing) of gross loans at end-June 2015 (3.1% at end-2012). Although of reasonable credit quality, and management's significant efforts into reducing concentration in this segment since its peak in 2008, the bank's CRE portfolio remains a key risk. The bank's efforts in shortening maturities and reducing high loan-to-value CRE lending are positive.

Similar to most Nordic peers, the Sparebanken and Sandnes rely on wholesale funding to varying degrees. The Sparebanken have maintained access to domestic and international funding markets, in particular for covered bonds through SpareBank 1 Boligkreditt (S1B; a joint funding vehicle of Alliance member banks) and Sparebanken Vest Boligkreditt. Fitch believes that the banks will retain significant liquidity portfolios to mitigate this risk. SNN's funding profile is stronger than its Sparebanken peers, driven by a greater retail deposit base. During 2015, SR set up their wholly-owned covered bond vehicle while SMN and SNN are in the process to do so. These aim mainly to avoid any restrictions on large exposures in times of stress but are also set up as back-up issuers to S1B.

The Sparebanken's capital adequacy ratios compare well with those of international peers. Leverage is low in a European context, with tangible common equity/tangible assets generally between 6%-11% at end-September 2015. SNN's risk-weighted capitalisation, as well as its leverage, is somewhat stronger than its Sparebanken peers.

Sandnes uses the standardised approach to calculate its capital requirements for both retail and corporate exposures, which leads to higher risk weights than peers and slightly lower reported capital ratios. However, leverage is low in a European context and is in line with its Norwegian peers, with a tangible equity to tangible assets ratio of 7.1% at end-June 2015. Nonetheless, the small absolute volume of equity makes it vulnerable to shocks.

SUPPORT RATING AND SUPPORT RATING FLOOR
The Sparebanken's Support Ratings of '3' and Support Rating Floors of 'BB+' reflect Fitch's view that there is a moderate probability of support, if required from the Norwegian authorities, given their strong regional franchises.

In addition, there is a possibility of institutional support from the members of the Alliance. However, Fitch understands that no legal obligation arises from membership of the Alliance to support member banks and therefore does not factor this into the ratings.

Sandnes' Support Rating reflects Fitch's view of an only low extraordinary support probability from the Norwegian authorities, given the bank's very limited market shares in Norway, hence its Support Rating Floor is 'No Floor'.

SUBORDINATED DEBT AND OTHER HYBRID SECURITIES
Subordinated debt and other hybrid capital issued by the Sparebanken are all notched down from the banks' VRs. Therefore, their respective ratings have been affirmed.

The ratings are in accordance with Fitch's 'Global Bank Rating Criteria' reflecting each instrument's respective non-performance and relative loss severity risk profiles, which vary considerably.

SNN's and SMN's subordinated debt instruments are notched down once from the banks' VRs to reflect the notes' higher expected loss severity relative to senior unsecured creditors.

SV's hybrid Tier 1 securities are rated four notches below the bank's VRs to reflect the higher loss severity risk of these securities relative to average recoveries (two notches from the VR) as well as high risk of non-performance (an additional two notches).

SUBSIDIARY AND AFFILIATED COMPANY
S1B's IDRs are aligned with those of the largest Alliance members, SR and SMN, as together with SNN (rated one notch higher), these are the most likely source of support. At end-September 2015, the combined ownership of SR, SMN and SNN was 52.5%. The ownership reflects the amount of loans sold to S1B and is updated at least on a yearly basis. S1B's IDRs reflect its key role as a

covered bond funding vehicle for its shareholder banks by securing competitively priced funding and access to a diversified investor base.

The Alliance banks are contractually obliged to buy covered bonds from S1B if an expected shortfall is identified 60 days prior to the maturity of the bond. The obligation from the shareholder banks is pro-rated depending on the ownership, and in case one or more banks are unable to fulfil their requirements, the other banks are obliged to meet the shortfall up to two times their original shares. These bonds are eligible as collateral for repo with the Norwegian central bank.

The Alliance banks are also contractually required to maintain a minimum Tier 1 capital ratio of 9% at S1B. Similar to the liquidity support the obligation is pro-rated based on each bank's shareholding and is capped at two times the original allocation. As the combined ownership of the three Fitch-rated Alliance banks exceeds 50%, their combined obligation would exceed any liquidity or capital shortfall identified by S1B.

Given S1B's close integration in the Alliance, including operational support and servicing of the mortgage assets, no VR is assigned.

RATING SENSITIVITIES

IDRS, VRS AND SENIOR DEBT

The Stable Outlooks on the Sparebanken's ratings reflect Fitch's expectation that house prices are likely to stabilise or moderately fall in the short to medium term, that the banks will further reduce their single name concentration, and that they will continue to strengthen capital ratios and maintain healthy liquidity buffers.

An upgrade is unlikely given the already high ratings in the context of their company profiles and geographical and lending concentration. The structural reliance on wholesale funding is also a rating sensitivity.

The Sparebanken's ratings could be downgraded if credit growth surpassed internal capital generation, materially weakening capitalisation. The ratings are also sensitive to a significant house price correction, should the banks be unable to absorb losses via earnings, or deterioration in the CRE exposure. The correction would probably lead to a drop in private consumption, affecting corporate lending quality, which Fitch expects to be the key driver of losses. A further sensitivity is prolonged low oil prices, which would likely lead to higher unemployment, lower private consumption and weaker corporate lending quality. In addition, this scenario would likely be followed by difficulties in obtaining competitively priced funding in the wholesale funding markets which is a further ratings sensitivity.

The Stable Outlook reflects Fitch's expectation of the operating environment in Norway remaining relatively sound, supporting Sandnes' asset quality and working out of impaired exposures, and maintained access to market funding. An upgrade is currently unlikely because the bank's small size makes it relatively sensitive to shocks, particularly in the context of its narrow geographical operating market and still some exposure to legacy CRE exposures.

Sandnes' ratings are sensitive to reduced activity in the region should it lead to a significant house price correction or increased losses in the corporate sector. A dislocation in debt capital markets making Sandnes unable to obtain competitively priced funding is a further sensitivity.

SUPPORT RATING AND SUPPORT RATING FLOOR

The Support Ratings and Support Rating Floors are potentially sensitive to changes in Fitch's assumptions about the ability (as reflected in its ratings) or willingness of the Norwegian state to provide timely support to the bank, if required. They are also sensitive to a change in Fitch's assumptions around the availability of sovereign support for banks more generally.

In Fitch's view, there is a clear intention ultimately to reduce implicit state support for financial institutions in the EU, as demonstrated by a series of legislative, regulatory and policy initiatives. Norway is not an EU member country and has done little so far to update its bank resolution framework. Fitch's base case is that it will look to adopt a flexible approach to bank support/ resolution decisions for its largest banks. All the Sparebanken banks have SRs of '3' and SRFs of 'BB+', and these are unlikely to be affected unless Norway adopts a much less flexible approach to resolution than Fitch currently anticipates. An upward revision of Sandnes' SRF of 'No Floor' would be contingent on a positive change in Fitch's view of the systemic importance of the bank, which is unlikely.

SUBORDINATED DEBT AND OTHER HYBRID SECURITIES
Subordinated debt and other hybrid capital issued by the Sparebanken are all notched down from the banks' VRs, and are therefore sensitive to any change in the VRs. The securities' ratings are also sensitive to changes in Fitch's assessment of their non-performance risk relative to that captured in the banks' VRs.

SUBSIDIARY AND AFFILIATED COMPANIES
S1B's ratings are sensitive to the same factors that might drive a change in the parent banks' ratings. The Stable Outlook is in line with that on the ratings of S1B's rated parents. As S1B's ratings are driven by expected support, downside risk to the ratings could arise if one or more of the largest owners were downgraded, or if Fitch believed their willingness or ability to support had diminished. S1B's IDR could be downgraded if SR's, SMN's and SNN's (the Fitch rated alliance members) combined ownership in S1B reduced materially, as in this event their combined obligation to provide support would not be sufficient to cover any liquidity or capital shortfall identified in S1B.

These rating actions have no impact on the ratings of the covered bonds issued by S1B and Sparebanken Vest Boligkreditt.

The rating actions are as follows:

SpareBank 1 Nord-Norge:
Long-term IDR affirmed at 'A'; Outlook Stable
Short-term IDR affirmed at 'F1'
Viability Rating affirmed at 'a'
Support Rating affirmed at '3'
Support Rating Floor affirmed at 'BB+'
Senior unsecured debt affirmed at 'A'/'F1'
Subordinated debt affirmed at 'A-'

SpareBank 1 SMN:
Long-term IDR affirmed at 'A-'; Outlook Stable
Short-term IDR affirmed at 'F2'
Viability Rating affirmed at 'a-'
Support Rating affirmed at '3'
Support Rating Floor affirmed at 'BB+'
Senior unsecured debt affirmed at 'A-'/'F2'
Subordinated debt affirmed at 'BBB+'

SpareBank 1 SR-Bank:
Long-term IDR affirmed at 'A-'; Outlook Stable
Short-term IDR affirmed at 'F2'
Viability Rating affirmed at 'a-'

Support Rating affirmed at '3'
Support Rating Floor affirmed at 'BB+'
Senior unsecured debt affirmed at 'A-'/'F2'

SpareBank 1 Boligkreditt:
Long-term IDR affirmed at 'A-'; Outlook Stable
Short-term IDR affirmed at 'F2'
Support Rating affirmed at '1'

Sparebanken Vest:
Long-term IDR affirmed at 'A-'; Outlook Stable
Short-term IDR affirmed at 'F2'
Viability Rating affirmed at 'a-'
Support Rating affirmed at '3'
Support Rating Floor affirmed at 'BB+'
Senior unsecured debt affirmed at 'A-'/'F2'
Hybrid capital instruments affirmed at 'BB+'

Sandnes Sparebank:
Long-term IDR affirmed at 'BBB'; Outlook Stable
Short-term IDR affirmed at 'F3'
Viability Rating affirmed at 'bbb'
Support Rating affirmed at '5'
Support Rating affirmed at 'No Floor'

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Applicable Criteria
Global Bank Rating Criteria (pub. 20 Mar 2015)
https://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=863501