

# SpareBank 1 SR-Bank

## Key Rating Drivers

**Low-Risk Model, Regional Concentration:** SpareBank 1 SR-Bank's (SR-Bank) ratings reflect its stable and low-risk business model, healthy profitability, resilient asset quality and sound capital ratios. The ratings also factor in risks arising from a moderate franchise with a geographically concentrated loan portfolio, from exposures to potentially volatile oil and property prices, as well as from its liquidity management in the context of its reliance on wholesale funding.

**Focus on Retail and SMEs:** Fitch Ratings expects SR-Bank to continue to implement its solid strategy based on a low-risk business model and a focus on retail and SME customers. SR-Bank has successfully reduced concentration risks relating to large exposures in recent years.

**Strong Asset Quality:** Fitch expects SR-Bank's asset quality to remain strong driven by its conservative underwriting standards and a stable operating environment. Impaired loans (defined as Stage 3 loans under IFRS9) accounted for 1.2% of gross loans at end-September 2019. SR-Bank operates in a region where the economic contribution from the oil industry is high, but it has decreased its exposure to this sector over the past five years.

The offshore service vessel (OSV) segment was the driver of SR-Bank's loan impairment charges (LICs) in 2016-2018.

**Healthy Profitability:** SR-Bank's regional franchise and strong client relationships support healthy pre-impairment profitability and stable revenue generation. Interest margins are healthy and cost-efficiency good, with an average cost/income ratio below 45% in the past four years.

Loan impairment charges have been moderate at around 15% of pre-impairment profitability on average in the past four years. Loan impairment charges are expected to be low in the medium term, and largely limited to the OSV segment.

**Strong Capitalisation:** SR-Bank's risk-weighted capital ratios compare well with those of international peers. We expect the bank to maintain sound buffers over its minimum regulatory requirements. Its leverage ratio is strong in a European context, with a Basel leverage ratio of 7.5% at end-September 2019.

**Wholesale Funding Reliance:** SR-Bank relies on wholesale funding like most Nordic banks, and particularly on covered bond issuance through its own wholly owned covered bond vehicle. Fitch expects the bank to retain a large liquidity portfolio to mitigate refinancing risk

## Rating Sensitivities

**Stable Outlook:** The Stable Outlook reflects Fitch's expectation that the operating environment in Norway will remain strong, with loan impairment charges largely contained to the OSV segment. We expect the bank to further reduce single-name concentration, continue to strengthen capital ratios and maintain healthy liquidity buffers.

**Rating Upside:** Positive rating pressure could arise in the medium term from sustained asset-quality improvements, most likely through a continued successful restructuring of the OSV portfolio. The rating upside is limited due to the geographical concentration.

**Property Prices Correction:** Fitch does not expect that a significant property price correction would lead to significant quality deterioration in the bank's mortgage lending, but reduced consumption could negatively affect its SME portfolio. SR-Bank is less exposed to this risk, due to low house prices in the south-west of Norway compared to the national average.

## Ratings

### Foreign Currency

Long-Term IDR	A-
Short-Term IDR	F2

Viability Rating	a-
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Support Rating	5
Support Rating Floor	NF

### Sovereign Risk

Long-Term Foreign-Currency IDR	AAA
Long-Term Local-Currency IDR	AAA
Country Ceiling	AAA

### Outlooks

Long-Term Foreign-Currency IDR	Stable
Sovereign Long-Term Foreign-Currency IDR	Stable
Sovereign Long-Term Local-Currency IDR	Stable

## Applicable Criteria

[Bank Rating Criteria \(October 2018\)](#)

[Short-Term Ratings Criteria \(May 2019\)](#)

## Related Research

[SpareBank 1 SR-Bank - Ratings Navigator \(September 2019\)](#)

[The Major Sparebanken of the SpareBank 1 Alliance \(January 2020\)](#)

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## Debt Rating Classes

Rating level	Rating
Senior preferred	A-/F2
Tier 2 subordinated	BBB+

Source: Fitch Ratings

Senior preferred notes are rated in line with SR-Bank's Issuer Default Ratings. Subordinated debt instruments are rated one notch below the bank's Viability Rating for loss severity, reflecting our expectation of below-average recovery prospects relative to senior unsecured creditors. No notching is applied for incremental non-performance risk because the write-down of the notes will only occur once the point of non-viability is reached and there is no coupon flexibility before non-viability.

On 15 November 2019, Fitch published *Exposure Draft: Bank Rating Criteria*, which included proposals to alter the notching of certain debt securities.

## Ratings Navigator – Standalone Assessment

### SpareBank 1 SR-Bank

ESG Relevance:

**Banks**  
Ratings Navigator

	Peer Ratings	Operating Environment	Company Profile	Management & Strategy	Risk Appetite	Asset Quality	Earnings & Profitability	Capitalisation & Leverage	Funding & Liquidity	Viability Rating	Support Rating Floor	Issuer Default Rating
aaa										aaa	AAA	AAA
aa+		↑								aa+	AA+	AA+
aa										aa	AA	AA
aa-		↓								aa-	AA-	AA-
a+					↓		↓	↓	↓	a+	A+	A+
a	↓		↓	↓	↓	↓	↓	↓	↓	a	A	A
a-	↓		↓							a-	A-	A- Stable
bbb+	↓		↓			↓			↓	bbb+	BBB+	BBB+
bbb	↓									bbb	BBB	BBB
bbb-	↓									bbb-	BBB-	BBB-
bb+	↓									bb+	BB+	BB+
bb	↓									bb	BB	BB
bb-	↓									bb-	BB-	BB-
b+	↓									b+	B+	B+
b	↓									b	B	B
b-	↓									b-	B-	B-
ccc+										ccc+	CCC+	CCC+
ccc										ccc	CCC	CCC
ccc-										ccc-	CCC-	CCC-
cc										cc	CC	CC
c										c	C	C
f										f	NF	D or RD

## Sovereign Support Assessment

Support Rating Floor	Value		
Typical D-SIB SRF for sovereign's rating level (assuming high propensity)	A+ to A-		
Actual country D-SIB SRF	NF		
<b>Support Rating Floor:</b>	<b>NF</b>		
Support Factors	Positive	Neutral	Negative
<b>Sovereign ability to support system</b>			
Size of banking system relative to economy			✓
Size of potential problem	✓		
Structure of banking system			✓
Liability structure of banking system		✓	
Sovereign financial flexibility (for rating level)		✓	
<b>Sovereign propensity to support system</b>			
Resolution legislation with senior debt bail-in			✓
Track record of banking sector support		✓	
Government statements of support		✓	
<b>Sovereign propensity to support bank</b>			
Systemic importance			✓
Liability structure of bank		✓	
Ownership		✓	
Specifics of bank failure		✓	
<b>Policy banks</b>			
Policy role			
Funding guarantees and legal status			
Government ownership			

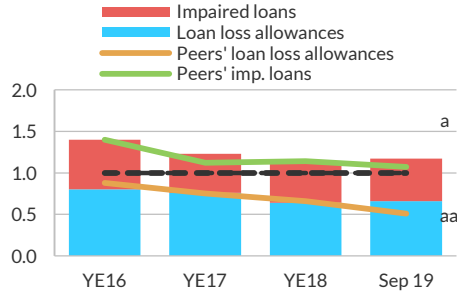
### Bar Chart Legend

Vertical bars – VR range of Rating Factor  
 Bar Colors – Influence on final VR  
 ■ Higher influence  
 ■ Moderate influence  
 ■ Lower influence  
 Bar Arrows – Rating Factor Outlook  
 ↑ Positive    ↓ Negative  
 ⇅ Evolving    □ Stable

The Bank Resolution and Recovery Directive was adopted in Norway on 1<sup>st</sup> of January 2019. It provides a framework for resolving banks that is likely to require senior creditors participating in losses, if necessary, instead of or ahead of a bank receiving sovereign support. In addition, SR-Bank is not defined as a systemically important bank in Norway. We assign a Support Rating of '5' and a Support Rating Floor of 'No Floor' for SR-Bank.

## Asset Quality

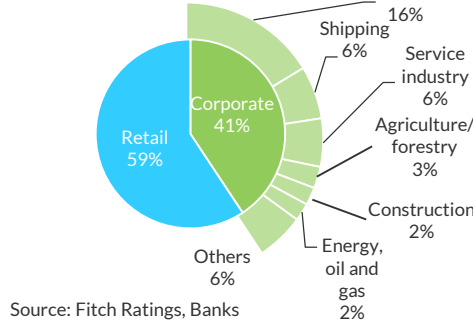
(% gross loans)



Source: Fitch Ratings, Banks

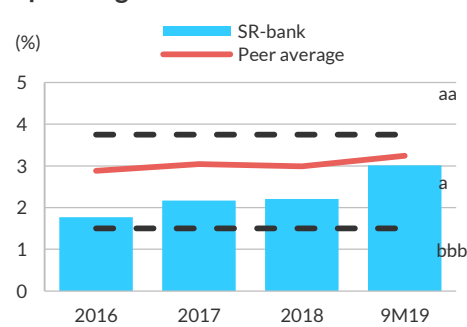
## Lending Structure

End-September 2019



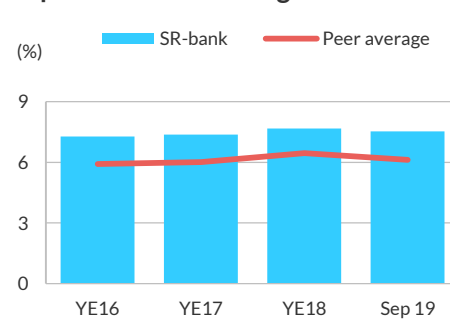
Source: Fitch Ratings, Banks

## Operating Profit/RWAs



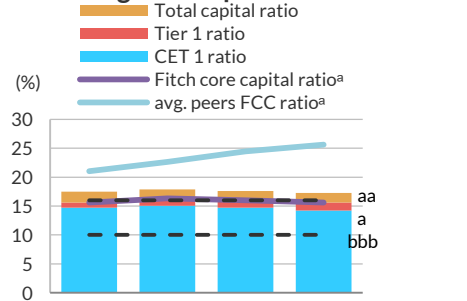
Source: Fitch Ratings, Banks

## Reported Basel Leverage Ratios



Source: Fitch Ratings, Banks

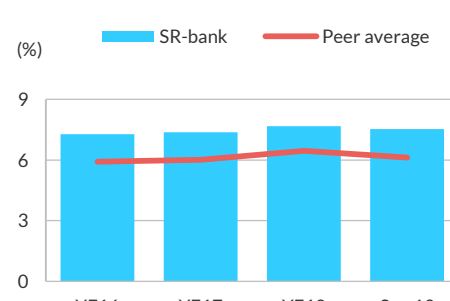
## Risk-Weighted Capital Ratios



<sup>a</sup> Fitch Core Capital used as benchmark line

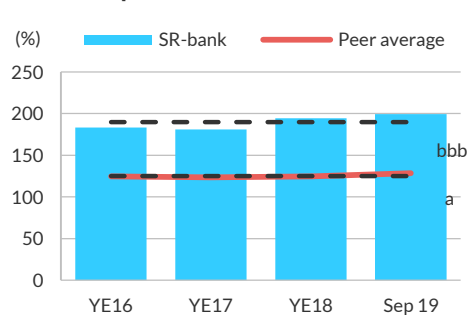
Source: Banks, Fitch Ratings

## Reported Basel Leverage Ratios



Source: Fitch Ratings, Banks

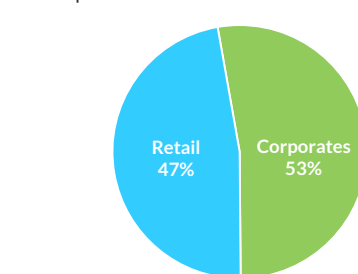
## Loans/Deposits Ratios



Source: Fitch Ratings, Banks

## Deposit Structure

End-September 2019



Source: Fitch Ratings, Banks

## Note on Peer Charts:

Peer average includes Caja Rural de Navarra, Sociedad Cooperativa de Credito (CRN, VR: 'bbb+'), SpareBank 1 SMN (a-), SpareBank 1 Nord-Norge (a), SR-Bank (a-), Leeds Building Society (Leeds, a-), Belfius Bank SA/NV (Belfius, a-), Skipton Building Society (Skipton, a-), Coventry Building Society (Coventry, a-), de Volksbank N.V. (deVolks, a-) and ABN AMRO Bank N.V. (ABN, a).

Leeds, Belfius, Skipton, Coventry ABN and de Volks' interim six months results were included in the latest average calculation while CRN was excluded from the latest average calculation due to data unavailability.

Black dashed lines in charts represent indicative quantitative ranges and corresponding implied scores for Fitch's core financial metrics for banks operating in the environments that Fitch scores in the 'aa' category.

Summary Financials and Key Ratios

	30 Sep 19 9 months (NOKm) Unaudited	31 Dec 18 Year end (NOKm) Audited - unqualified	31 Dec 17 Year end (NOKm) Audited - unqualified	31 Dec 16 Year end (NOKm) Audited - unqualified
<b>Summary income statement</b>				
Net interest & dividend income	2,956	3,451	3,173	2,887
Net fees and commissions	1,053	1,432	1,518	1,439
Other operating income	1,078	562	629	548
Total operating income	5,087	5,445	5,320	4,874
Operating costs	1,800	2,229	2,167	2,032
Pre-impairment operating profit	3,287	3,216	3,153	2,842
Loan & other impairment charges	96	324	543	778
Operating profit	3,191	2,892	2,610	2,064
Other non-operating items (net)	n.a.	0	0	94
Tax	552	596	524	403
Net income	2,639	2,296	2,086	1,755
Other comprehensive income	-87	149	8	-116
Fitch comprehensive income	2,552	2,445	2,094	1,639
<b>Summary balance sheet</b>				
<b>Assets</b>				
Gross loans	203,575	192,105	172,554	157,638
- Of which impaired	2,380	2,133	2,117	2,211
Loan loss allowances	1,352	1,227	1,317	1,266
Net loans	202,223	190,878	171,237	156,372
Interbank	1,898	1,696	1,608	4,334
Derivatives	6,765	5,268	5,541	4,315
Other securities & earning assets	37,701	33,921	36,579	26,080
Total earning assets	248,587	231,763	214,965	191,101
Cash and due from banks	404	717	207	1,079
Other assets	2,613	1,581	1,446	1,228
Total assets	251,604	234,061	216,618	193,408
<b>Liabilities</b>				
Customer deposits	102,181	98,814	95,384	85,913
Interbank and other short-term funding	976	1,995	2,335	1,583
Other long-term funding	115,952	105,052	92,417	82,073
Trading liabilities and derivatives	5,044	3,889	3,787	2,515
Total funding	224,153	209,750	193,923	172,084
Other liabilities	3,235	1,904	1,962	2,188
Pref. shares and hybrid capital	1,821	1,372	994	848
Total equity	22,395	21,035	19,739	18,288
Total liabilities and equity	251,604	234,061	216,618	193,408

Summary Financials and Key Ratios (Cont.)

	30 Sep 19 9 months (NOKm) Unaudited	31 Dec 18 Year end (NOKm) Audited - unqualified	31 Dec 17 Year end (NOKm) Audited - unqualified	31 Dec 16 Year end (NOKm) Audited - unqualified
<b>Ratios (annualised as appropriate)</b>				
<b>Profitability</b>				
Operating profit/RWA	3.0	2.2	2.2	1.8
Net interest income/average earning assets	1.6	1.6	1.6	1.5
Non-interest expense/gross revenues	42.6	43.9	44.3	45.3
Net income/average equity	16.2	11.3	11.1	10.0
<b>Asset quality</b>				
Impaired loans ratio	1.2	1.1	1.2	1.4
Growth in gross loans	6.0	11.3	9.5	1.6
Loan loss allowances/impaired loans	56.8	57.5	62.2	57.3
Loan impairment charges/average gross loans	0.1	0.2	0.3	0.5
<b>Capitalisation</b>				
Fitch Core Capital ratio	15.6	16.0	16.4	15.6
Tangible common equity ratio	8.8	9.0	9.1	9.4
CET 1 ratio	14.2	14.7	15.1	14.7
Basel leverage ratio	7.5	7.7	7.4	7.3
Net impaired loans/FCC	4.7	4.3	4.1	5.2
<b>Funding &amp; liquidity</b>				
Loans/customer deposits	199.2	194.4	180.9	183.5
LCR	153.0	167.0	168.0	174.0
Customer deposits/funding	46.3	47.7	49.9	50.4
NSFR	115.0	121.0	119.0	n.a.

Source: Fitch Ratings, Fitch Solutions

## Environmental, Social and Governance Considerations

### FitchRatings SpareBank 1 SR-Bank

Banks  
Ratings Navigator

#### Credit-Relevant ESG Derivation

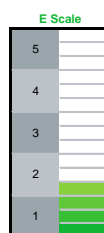
SpareBank 1 SR-Bank has 5 ESG potential rating drivers

- SpareBank 1 SR-Bank has exposure to compliance risks including fair lending practices, mis-selling, repossession/foreclosure practices, consumer data protection (data security) but this has very low impact on the rating.
- Governance is minimally relevant to the rating and is not currently a driver.

				Overall ESG Scale	
key driver	0	issues	5		
driver	0	issues	4		
potential driver	5	issues	3		
not a rating driver	4	issues	2		
	5	issues	1		

#### Environmental (E)

General Issues	E Score	Sector-Specific Issues	Reference
GHG Emissions & Air Quality	1	n.a.	n.a.
Energy Management	1	n.a.	n.a.
Water & Wastewater Management	1	n.a.	n.a.
Waste & Hazardous Materials Management; Ecological Impacts	1	n.a.	n.a.
Exposure to Environmental Impacts	2	Impact of extreme weather events on assets and/or operations and corresponding risk appetite & management; catastrophe risk; credit concentrations	Company Profile; Management & Strategy; Risk Appetite; Asset Quality



#### How to Read This Page

ESG scores range from 1 to 5 based on a 15-level color gradation. Red (5) is most relevant and green (1) is least relevant.

The Environmental (E), Social (S) and Governance (G) tables break out the individual components of the scale. The left-hand box shows the aggregate E, S, or G score. General Issues are relevant across all markets with Sector-Specific Issues unique to a particular industry group. Scores are assigned to each sector-specific issue. These scores signify the credit-relevance of the sector-specific issues to the issuing entity's overall credit rating. The Reference box highlights the factor(s) within which the corresponding ESG issues are captured in Fitch's credit analysis.

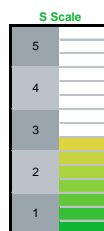
The Credit-Relevant ESG Derivation table shows the overall ESG score. This score signifies the credit relevance of combined E, S and G issues to the entity's credit rating. The three columns to the left of the overall ESG score summarize the issuing entity's sub-component ESG scores. The box on the far left identifies the [number of] general ESG issues that are drivers or potential drivers of the issuing entity's credit rating (corresponding with scores of 3, 4 or 5) and provides a brief explanation for the score.

Classification of ESG issues has been developed from Fitch's sector and sub-sector ratings criteria and the General Issues and the Sector-Specific Issues have been informed with SASB's Materiality Map.

Sector references in the scale definitions below refer to Sector as displayed in the Sector Details box on page 1 of the navigator.

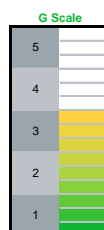
#### Social (S)

General Issues	S Score	Sector-Specific Issues	Reference
Human Rights, Community Relations, Access & Affordability	2	Services for underbanked and underserved communities: SME and community development programs; financial literacy programs	Company Profile; Management & Strategy; Risk Appetite
Customer Welfare - Fair Messaging, Privacy & Data Security	3	Compliance risks including fair lending practices, mis-selling, repossession/foreclosure practices, consumer data protection (data security)	Operating Environment; Company Profile; Management & Strategy; Risk Appetite
Labor Relations & Practices	2	Impact of labor negotiations, including board/employee compensation and composition	Company Profile; Management & Strategy
Employee Wellbeing	1	n.a.	n.a.
Exposure to Social Impacts	2	Shift in social or consumer preferences as a result of an institution's social positions, or social and/or political disapproval of core banking practices	Company Profile; Financial Profile



#### Governance (G)

General Issues	G Score	Sector-Specific Issues	Reference
Management Strategy	3	Operational implementation of strategy	Management & Strategy
Governance Structure	3	Board independence and effectiveness; ownership concentration; protection of creditor/stakeholder rights; legal /compliance risks; business continuity; key person risk; related party transactions	Management & Strategy; Earnings & Profitability; Capitalisation & Leverage
Group Structure	3	Organizational structure; appropriateness relative to business model; opacity; intra-group dynamics; ownership	Company Profile
Financial Transparency	3	Quality and frequency of financial reporting and auditing processes	Management & Strategy



CREDIT-RELEVANT ESG SCALE	
How relevant are E, S and G issues to the overall credit rating?	
5	Highly relevant, a key rating driver that has a significant impact on the rating on an individual basis. Equivalent to "higher" relative importance within Navigator.
4	Relevant to rating, not a key rating driver but has an impact on the rating in combination with other factors. Equivalent to "moderate" relative importance within Navigator.
3	Minimally relevant to rating, either very low impact or actively managed in a way that results in no impact on the entity rating. Equivalent to "lower" relative importance within Navigator.
2	Irrelevant to the entity rating but relevant to the sector.
1	Irrelevant to the entity rating and irrelevant to the sector.

The highest level of ESG credit relevance is a score of '3'. ESG issues are credit-neutral or have only a minimal credit impact on the entity, either due to their nature or to the way in which they are being managed by the entity. For more information on our ESG Relevance Scores, visit [www.fitchratings.com/esg](http://www.fitchratings.com/esg).

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