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10 SEPTEMBER 2015

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RATINGS

SpareBank 1 SR-Bank ASA

LT Issuer Rating	A1
LT Bank Deposits	A1
ST Bank Deposit	Prime-1
BCA / Adjusted BCA	baa2 / baa1

KEY METRICS:

SpareBank 1 SR - Bank ASA

NOK millions	2014	2013	2012
Total Assets	174,926	156,985	141,543
Tangible Common Equity	15,324	13,855	12,522
Net income / tangible assets	1.11%	1.19%	0.90%

Source: Moody's Banking Financial Metrics (adjusted)

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Sparebank 1 SR Bank ASA-Norway

Prudent Underwriting Upholds Strong Performance In Challenging Environment

Summary Opinion

SpareBank 1 SR Bank ASA (A1/A1 Stable, baa2)[1], Norway's largest savings bank by assets, is the most exposed to the oil sector out of the savings banks we rate in the country. Despite the sharp drop in the price of oil over the past year, clouding the country's economic outlook, we believe the bank, which is based in the oil hub of Stavanger, is well positioned to weather these challenges - absent any further shocks that will accelerate and deepen the downturn.

» **SpareBank 1 SR Bank's direct exposure to the oil industry is manageable, made up predominantly of shipping finance, which is well collateralised with a majority of new vessels under long contracts.** Oil-related lending accounts for 11%[2] of the bank's on balance sheet exposure-at-default, and we expect strong underwriting criteria will continue to help manage its exposure to corporate risks and defaults and problem loans to increase in line with the Norwegian banking sector over the next 12 months.

» **Even though the bank's exposure to commercial real estate - the biggest area of concern for Norwegian lenders - is high, and we have observed increases in vacancy rates in many areas of Stavanger, SpareBank 1 SR Bank benefits from a selective lending policy that has favoured commercial premises over office developments.** Also, we do not expect the softening of economic growth to translate into a more substantial increase of problem loans in the bank's residential property portfolio looks resilient, thanks to generous unemployment benefits.

» **We expect the operating environment in and around Stavanger to stabilise in 2016, after this year's 15% year on year slump in petroleum investment,** as (a)the majority of oil companies' cost cutting and divestment will be completed and (b) most of the oil investments for the next 4 years relate to the Johan Sverdrup field, one of the last "elephant" projects (located 155km west of Stavanger) with a breakeven price at $32 per barrel, which is significantly below the $75 per barrel of some of the existing oilfields.

» **Credit markets have recognised SpareBank 1 SR Bank's strong fundamentals, as its first standalone covered bond issuance in June was well received.** The bank issued a NOK2 billion (US$241 million) covered bond backed by prime Norwegian residential mortgages in June 2015 via SR-Boligkreditt ASA (Aaa covered bond ratings)[3] for the first time, with pricing in-line with larger, well-diversified peers.

Strict underwriting standards have limited risks and defaults in the corporate sector

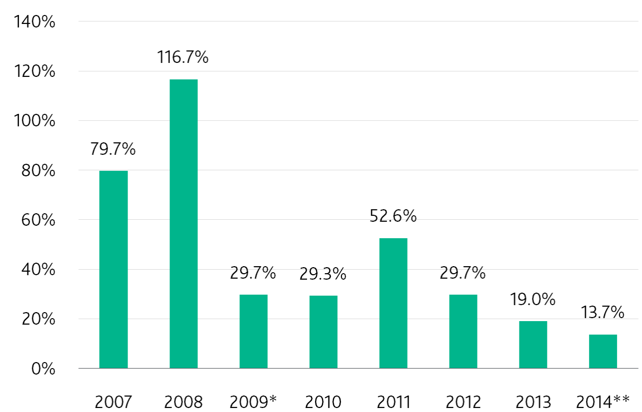
SpareBank 1 SR Bank's problem loans have remained stable at just below 1% during 2015, notwithstanding the challenging operating environment on the back of decreased petroleum sector investments, low oil prices and being located in and having its fortunes tied to the economy of the country's oil hub of Stavanger. While we expect problem loans to increase over the next 12 months, they will be in line with the rest of the Norwegian banking sector,[4] absent any further shock that would deepen the economic slowdown. However, if oil prices plateau at a significant lower level than our expectations [5] problem loans might increase further.

During Norway's high economic growth years, fueled by a thriving petroleum sector, SpareBank 1 SR improved the risk profile of its loan book and strengthen its capital base. The low stock of bad loans reflects Norway's benign economic development of recent years, as well as SpareBank 1 SR Bank's proactive risk management, lending to a diverse range of businesses in different industries, including a strong focus on retail businesses and a continuous effort in recent years to reduce single client concentrations (see Exhibit 1 and 2).

To limit increase on the risk profile in its commercial portfolio, the bank is planning to introduce new calculation methods. These methods will allow it to restructure through repricing to better reflect the risk profile of the loan in a less favourable economic environment and in some cases terminate the engagement.

Exhibit 1

Commitments exceeding 10% of net regulatory capital have reduced

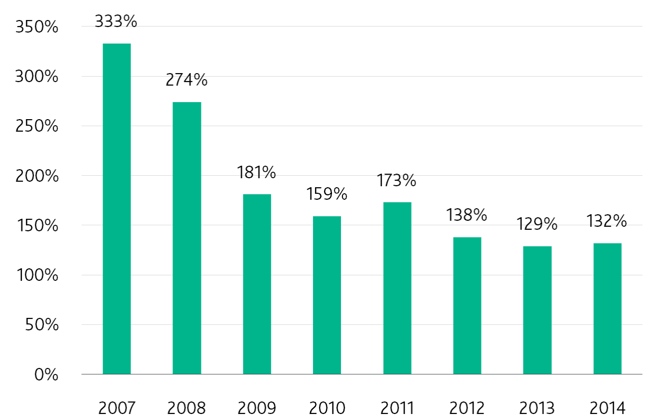


* In 2009, the bank issued additional equity certificates and a Tier 1 perpetual bond issuance
** Only one commitment with SpareBank 1 Boligkreditt AS continues to exceed 10% of capital

Source: SpareBank 1 SR Bank ASA

Exhibit 2

The bank has also reduced its top 20 commitments as a % of Tier 1 capital



Source: SpareBank 1 SR bank ASA

Oil related exposure is significant but well monitored and risk profile has been overall stable

Oil related lending accounted for 11% of SpareBank 1 SR Bank's total on balance sheet exposure-at-default (9% including transferred covered bonds) at end May 2015, making the bank the most exposed to the petroleum sector among its rated Norwegian peers. However, risk has remained manageable over the past 12 months following the drop in the oil prices, and we expect this to continue over the next year.

Sparebank 1 SR Bank's most direct exposure to the oil producing sector is through offshore ship-lending (7.4% of total lending at end June 2015), through which it finances vessels used in all stages of the oil exploration and producing cycle. Approximately 10% of this exposure (0.8% of total lending) is related to seismic vessels - ships that scan the geology below the seabed for oil - that are engaged in the most risky early part of the cycle and directly affected by CAPEX reductions by the big oil companies. The vast majority of the offshore portfolio is exposed to the operational sector via platform supply vessels and rigs, accounting for almost 60% of the offshore portfolio.

The bank reviews these exposures and collateral values bi-annually and in the case of price declines or a minimum value close breach, it requests additional collateral and in some cases asks for the loan to be paid down. We view that such measures position the bank well to weather the headwinds posed by declining vessel prices driven by oversupply and lower oil prices. The average loan to value (LTV) of SpareBank 1 SR Bank's offshore portfolio was almost 60% at the end of August 2015.

In addition, the bank has mostly financed vessels that have been built over the past five years (accounting for almost 50% of offshore lending) while only a small part of the exposure is against older vessels, making the bank's portfolio more robust in a market downturn. New built vessels tend to be more attractive, and once contracts expire, we expect they are more likely to maintain a higher utilization even in the current environment. Almost 80% of the vessels the bank finances are under contract, with 64% of these contracts to be renewed after the end of 2017, providing more stability to the bank's offshore portfolio in a low oil price environment. Only 12% of the offshore vessels in the bank's portfolio operate in the spot market.

SpareBank 1 SR Bank has also lent to exploration and production companies (approximately 1.4% of gross loans) of which more than two-thirds is reserve-based lending, a form of financing where a loan is secured by the oil and gas reserves of fields that are currently in production or where production is expected to commence shortly. The remaining part of this portfolio is secured by a tax refund from the Norwegian state and has no direct oil price risk.

Real estate exposure is high but has been reduced over the years

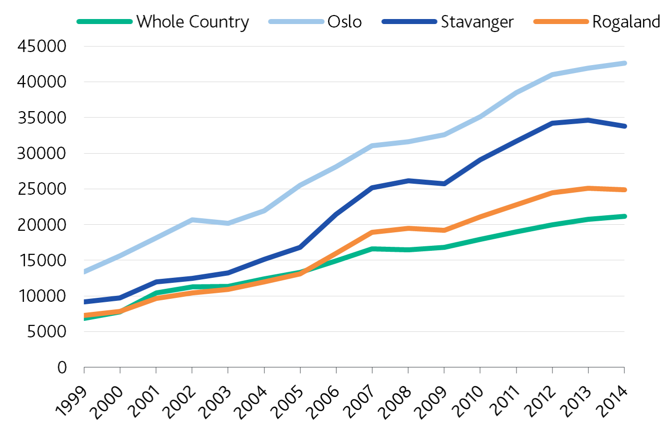
In the last twelve months regional house price appreciation in Norway appears to have leveled off and regional house prices are now overall stable, with growth rates lagging Oslo and other big cities after the sharp drop in the price of oil forced most of the big oil companies to cut costs and lay off staff. We expect this trend to continue as the employment market stabilises in the next 12 months.

Real estate prices in the area of Stavanger appreciated significantly more than the national average since 2005, mainly driven by the generous salaries paid in the booming oil industry (see Exhibit 3 and 4).

We believe that overall the household sector is resilient and we do not expect an increase in mortgage-related problem loans, as the state pays generous unemployment benefits, the labour market is flexible and interest rates are low.

Exhibit 3

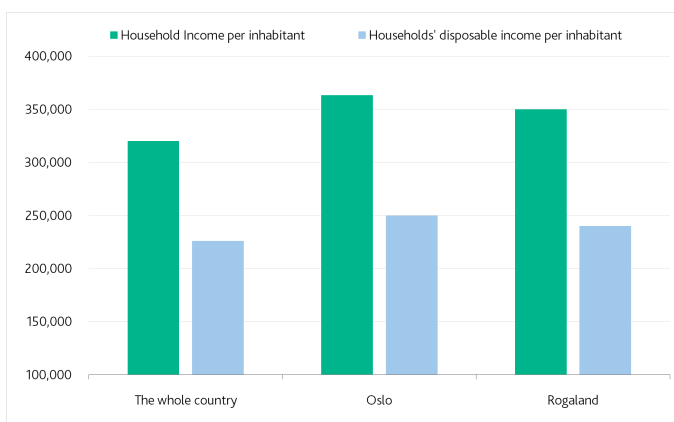
Used detached houses price evolution (price per square meter)



Source: Statistics Norway

Exhibit 4

Regional Household Income and Disposable Income per Inhabitant (latest available data, December 2012)



Source: Statistics Norway

Commercial real estate is the main area of concern for all of Norway's lenders and the Stavanger economy's dependence on the oil industry makes it particularly vulnerable. SpareBank 1 SR Bank's portfolio has not seen any problem loan increases over the past 12 months and for the coming year we expect an only moderate deterioration from current levels in-line with larger and more diversified peers.

While vacancy rates increased in Stavanger, their increase was mainly driven by office developments (old buildings and sublease) with the Forus and the Stavanger border areas noticing the biggest increases to 13.1% and 9.4% at end-May 2015 from 10.8% and 6.3% at end-October 2014 respectively, due to oversupply and the spillover from lower oil prices.

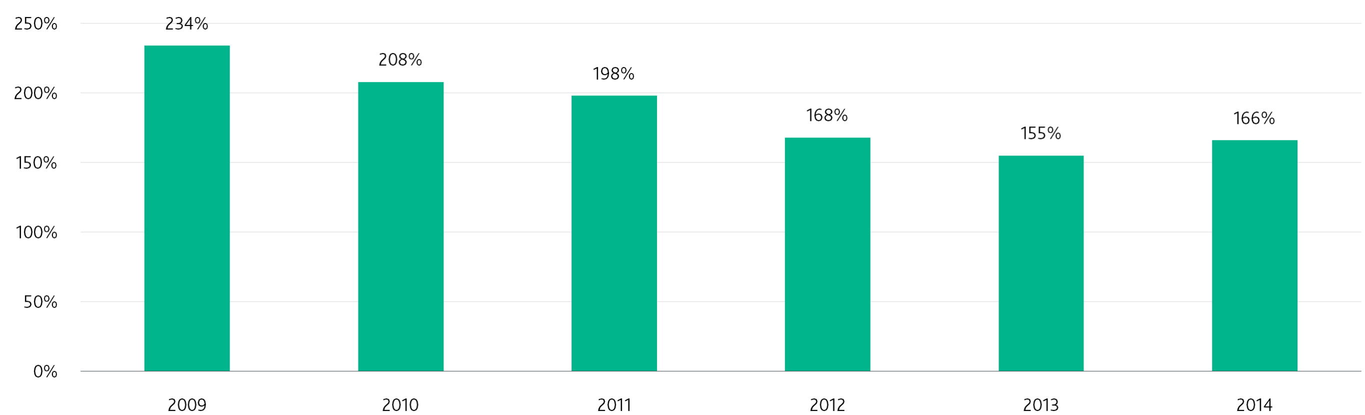
Sparebank 1 SR Bank's exposure to office construction is very limited, accounting for 3.8% of its corporate loans at end-2014 (1.3% of total loans), while the real estate portfolio is characterised by lending to commercial properties for leasing with long term contracts and the vacancy rate is limited. This selective underwriting provides an additional cushion for the bank's portfolio in this less favorable operating environment.

About 2% of the bank's loan book - NOK3.5 billion at end-2014 - accounts for real estate let to companies operating directly or indirectly in the oil industry and so far that loan book has been robust.

The bank has reduced its construction and real estate concentration to 116% of Tier 1 Capital at end-2014 from 342% at end-2008 as it focused on diversifying its portfolio (Exhibit 5), mainly through long standing relationships with companies with strong long-term prospects.

Exhibit 5

Commercial Real Estate Exposure as % of Tier 1 Capital



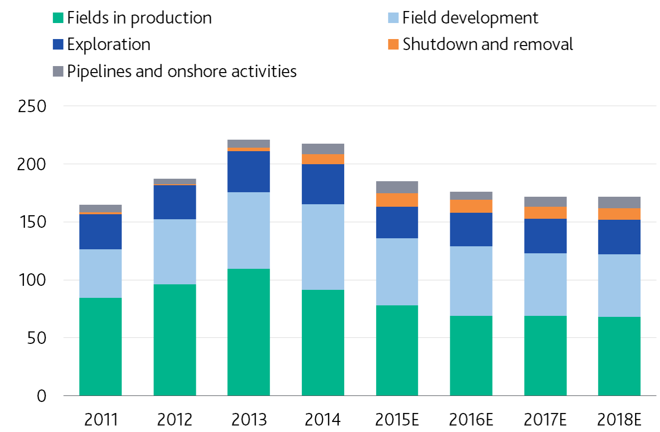
Source: SpareBank 1 SR Bank ASA

We expect the operating environment to stabilise from 2016 onwards

The lower oil price has started to feed through Stavanger's economy, with unemployment in the region outpacing the rest of Norway,[6] rising to 3.1% at the end of June 2015, above the Norwegian average of 2.8%. We expect Stavanger's economy and petroleum investments to stabilise in the second half of 2016 as the pull-back that many oil companies and their suppliers started in 2013 will trough this year (see Exhibit 8). The majority of the oil companies operating in Norway's continental shelf have already realised improved efficiency in their operations.

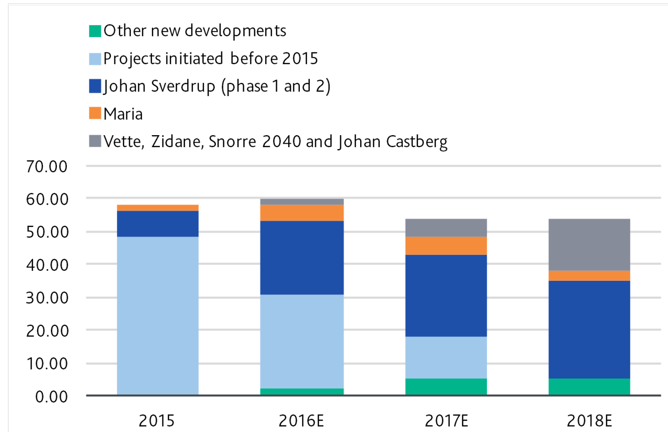
In addition, the majority of field development activities comes from the Johan Svedrup field with a break-even price of US$32[7] per barrel, for stage one of the field development, making current investment estimates from the central bank more resilient to lower oil prices (see Exhibit 9).[8]

Exhibit 6
Petroleum Investments (NOK billions)



Source: Norges Bank

Exhibit 7
Field Development (NOK billions)



Source: Norges Bank

SpareBank 1 SR Bank ASA is an established borrower in the domestic and Euro market

SpareBank 1 SR Bank tested the covered bond market on its own in June 2015 via a NOK2.0 billion issuance through its fully owned subsidiary SR-Boligkreditt ASA. The issue was priced 35bps above the three-month NIBOR rate, in-line with peers (Exhibit 6) and setting a favorable precedent for further issuances throughout the challenging period ahead.

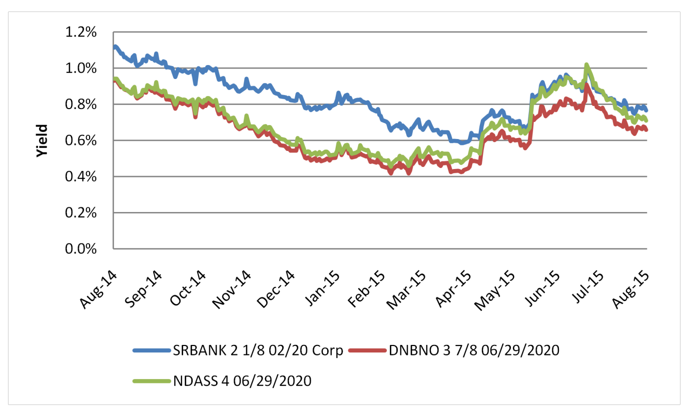
The bank set up its own covered bond entity SR-Boligkreditt ASA in March 2015 to optimise its funding mix as well as to eliminate possible constraints due to regulatory limits on large exposures. While SpareBank 1 SR Bank will continue using the SpareBank 1 Alliance covered bond entities (Sparebank 1 Boligkreditt and Naeringskreditt) as its primary covered bond issuers, the bank will also continue to actively issue through its own subsidiary.

Exhibit 8
Covered Bond Issuance Comparison

Issuer	Issue Date	Ammount	Expiry	Coupon
SR Boligkreditt AS	16-Jun-15	NOK 2.5bn	18-Dec-17	3m NIBOR + 0.20bps
	04-Jun-15	NOK 2bn	10-Sep-20	3m NIBOR + 0.35bps
SpareBank 1 Boligkreditt AS	16-Jun-15	NOK 6.3bn	Jun-21	3m NIBOR + 0.22bps
Sparebanken Sor Boligkreditt	30-Mar-15	NOK 2.0bn	24-Sep-20	3m NIBOR + 0.32bps
More Boligkreditt AS	26-Jan-2015	NOK 0.75bn	10-May-19	3m NIBOR + 0.47bps

Source: Oslo Stock Exchange

Exhibit 9
Senior Unsecured Bond Comparison: SpareBank 1 SR Bank, DNB Bank, Nordea Bank



Source: Bloomberg

SpareBank 1 SR Bank is more dependent on market funding than its peers, accounting for 44% of tangible banking assets (including mortgages transferred to covered bond companies), while its liquidity coverage ratio was 111% at end of June 2015. However, covered bonds account for 37% of total market funding which is less sensitive than market funding more generally, thanks to a combination of its typical long-dated and over-collateralized nature.

Peer Group:

- DNB Bank ASA
- SpareBank 1 Nord-Norge
- SpareBank 1 SMN
- Sparebanken Hedmark
- Sparebanken Vest
- Sparebanken Sor
- Sparebanken More
- Sparebanken Oest
- Sparebanken Sogn og Fjordane
- Helgeland Sparebank
- Fana Sparebank

Methodology Used:

- Banks

Credit Opinions:

- SpareBank 1 SR Bank ASA
- DNB Bank ASA
- SpareBank 1 Nord-Norge
- SpareBank 1 SMN
- Sparebanken Hedmark
- Sparebanken Vest
- Sparebanken Sor
- Sparebanken More
- Sparebanken Oest
- Sparebanken Sogn og Fjordane
- Helgeland Sparebanken
- Fana Sparebank
- Statoil ASA

Moody's Related Research

Banking System Outlook:

» Norway, July 2015

Banking System Profile:

» Norway, March 2014

Macro Profile:

» Banking: Norway Macro Profile: Very Strong -, March 2015

Analyses:

» Norway, Government of, June 2015

» Global Oil and Natural Gas Industry: Rise in Oil Inventories Compounds Risk of New Iranian Crude Exports

To access any of these reports, 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 The ratings shown here are the bank's deposit rating, senior unsecured rating and its baseline credit assessment

2 Including the covered bonds transferred this figure is 8.9%

3 New Issue Report: SR-Boligkreditt AS Mortgage Covered Bonds

4 Banking System Outlook: Norway

5 Moody's Oil & Natural Gas Price Assumptions

6 Norway, Government of, June 2015

7 Norges største industriprosjekt – utbygging og drift av Johan Sverdrup-feltet med status for olje- og gassvirksomheten

8 Moody's Oil & Natural Gas Price Assumptions

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