

Rating Action: Moody's assigns (P)A1 ratings to Sparebanken Sor's EMTN Programme

Global Credit Research - 19 Aug 2016

Limassol, August 19, 2016 -- Moody's Investors Service (Moody's) has today assigned (P)A1 provisional senior unsecured local and foreign currency long-term ratings to the EUR3 billion Euro Medium-Term Note (EMTN) programme of Sparebanken Sor, in line with the bank's A1 long-term deposit and issuer ratings. Securities issued under the programme will constitute direct, unconditional, unsecured and unsubordinated obligations of Sparebanken Sor.

RATINGS RATIONALE

The (P)A1 long-term local and foreign-currency ratings assigned to the senior unsecured new EMTN programme are aligned with Sparebanken Sor's issuer and deposit ratings, reflecting that the debt securities will be direct, unconditional and unsecured obligations of Sparebanken Sor and will rank equally with all other unsecured and unsubordinated present and future obligations of the bank. Under the programme, Sparebanken Sor may issue notes up to a maximum aggregate amount of EUR3 billion.

Sparebanken Sor's ratings are driven by its baa1 baseline credit assessment (BCA) as well as two notches of uplift following the application of Moody's advanced Loss Given Failure (LGF) analysis and one notch of uplift resulting from the rating agency's Moderate Government Support assumption. Sparebanken Sor's BCA reflects its strong asset quality metrics, with ratios of non-performing loans (NPLs) to gross loans of 1.1% and loan loss reserves to NPLs of 62.3% as of March 2016, broadly in line with its domestic, similarly-rated savings banks peers. The bank's baa1 BCA also captures Moody's expectation of a further increase in Sparebanken Sor's capital buffers as it reaches its 14.5% common equity tier 1 (CET1) target by year-end 2016, from 13.6% as of June 2016 (14.1% including 80% of interim profit). Finally, the bank's baa1 BCA incorporates its moderate profitability with a 0.55% return on tangible assets and its high reliance on market funding, a common attribute of Norwegian banks, with market funds accounting for 31% of tangible banking assets as of March 2016.

Sparebanken Sor's deposit and issuer ratings carry a negative outlook assigned on 16 March 2016. The negative outlook reflects Moody's expectation of increased asset risk in the bank's loan book as a result of the slowdown in Norway's economic growth driven by a reduction in petroleum investments.

As Moody's issues provisional ratings in advance of the final issuance under the programme, these ratings only represent Moody's preliminary credit opinion. Moody's will endeavour to assign definitive ratings to actual issuances from the EMTN programme. A definitive rating may differ from a provisional rating if the terms and conditions of the issuance are materially different from those of the programme reviewed.

Moody's will disseminate the future assignment of any definitive ratings through its Client Service Desk.

WHAT COULD CHANGE THE RATING UP/DOWN

Upward rating momentum is currently unlikely given the negative issuer rating outlook. A reversal of the outlook to stable could follow if the bank demonstrates: (1) resilience in its financial metrics in Norway's softening operating environment, including asset quality and profitability; or (2) reduced exposure to more volatile sectors such as the construction and real-estate sectors below 100% of Tier 1; and/or (3) diversified access to capital markets and improved liquidity.

Future downward rating pressure could follow: (1) our expectation that the bank's problem loans ratio would rise above Moody's system-wide expectation of approximately 2%; (2) an increase of top-20 loan concentration as a percentage of Core Tier 1 capital above 150%; and/or (3) a reduction in the bank's profitability, with net profits falling below 0.4% of tangible assets. A reduction in uplift as a result of our LGF analysis or a revision of government support assumptions could lead to downward rating pressure.

PRINCIPAL METHODOLOGY

The principal methodology used in these ratings was Banks published in January 2016. Please see the

Ratings Methodologies page on www.moodys.com for a copy of this methodology.

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