

# MOODY'S INVESTORS SERVICE

## Rating Action: Moody's takes rating actions on two Danish banks to reflect MREL issuances

24 Apr 2019

Limassol, April 24, 2019 -- Moody's Investors Service (Moody's) has today upgraded the long-term deposit and senior unsecured MTN program ratings of Sydbank A/S (Sydbank) to A1 and (P)A1, from A2 and (P)A2 respectively. The outlook on the deposit rating changed to stable from positive. Moody's also affirmed Sydbank's short-term deposit rating at P-1 and its short-term program rating at (P)P-1. At the same time, Moody's affirmed Ringkjobing Landbobank A/S' (Ringkjobing) long- and short-term deposit ratings at A1/P-1 and its long- and short-term issuer ratings at A2/P-1, and revised the outlook on both long-term ratings to positive from stable.

Today's rating actions reflect current and expected volumes of loss-absorbing debt, particularly from issuances of junior senior unsecured debt (also broadly known as non-preferred senior debt), that would reduce the loss severity for junior depositors and senior unsecured creditors in the unlikely event of bank failure and resolution according to Moody's forward-looking Advanced Loss Given Failure (LGF) analysis on the banks' liability structures. Moody's expectations are anchored against bank-specific minimum requirements for own funds and eligible liabilities (MREL) that are set by the Danish Financial Supervisory Authority (FSA).

The full list of the affected ratings and assessments can be found at the end of this press release.

### RATINGS RATIONALE

#### ACTION REFLECTS LOWER LOSS-GIVEN-FAILURE FOR SENIOR CREDITORS

The key driver for today's rating actions is Moody's expectation of ongoing higher volumes of junior senior debt, in response to the Danish FSA's bank-specific MREL. These higher amounts would afford a larger buffer for more senior classes of debt, such as junior depositors and senior unsecured debt (senior preferred debt), and potentially lower loss-given-failure.

Junior senior debt, introduced in 2018 in Denmark, is senior to subordinated debt and regulatory capital instruments and junior to other ordinary unsecured claims. This type of debt satisfies the subordination requirement, whereby from 2022 MREL must be met exclusively with capital and junior debt instruments that are written-down or converted into equity before simple creditors in resolution or bankruptcy.

Sydbank and Ringkjobing both operate in Denmark and are subject to the EU's Bank Recovery and Resolution Directive (BRRD), which Moody's considers an operational resolution regime. In accordance with Moody's methodology, the agency applies its forward-looking Advanced LGF analysis to the banks' liabilities, considering the risks faced by different debt and deposit classes across the liability structure should either of the banks enter resolution.

In its forward-looking LGF analysis Moody's attaches a high degree of confidence to the likelihood that these banks will strive to continue to fulfil MREL along with the subordination requirement.

Bank-specific reasons for the rating actions are outlined below.

#### -- SYDBANK A/S

The upgrade to A1 from A2 and (P)A1 from (P)A2 respectively of Sydbank's long-term deposit and senior unsecured MTN program ratings reflects Moody's Advanced LGF analysis based on recently issued volumes of junior senior debt and the agency's expectation of the bank's liability structure evolution. The LGF analysis for the bank indicates that junior depositors and senior unsecured creditors are likely to face extremely low loss-given-failure leading to a three notch uplift from the bank's baa1 Adjusted Baseline Credit Assessment (BCA), from which these ratings are notched, up from a two notch uplift previously.

Sydbank has recently issued a total of EUR1 billion (equivalent to around DKK7.4 billion) in junior senior debt and meets an MREL of 29.5% based on the bank's risk exposure amount (REA) as of the end of 2017 that will

apply from July 2019 through a combination of this junior senior debt, hybrid instruments and common equity. MREL will rise to 30% as of 30 September 2019 because of an increase in the countercyclical capital buffer in Denmark.

Moody's expects that Sydbank will maintain these volumes of loss-absorbing debt, which along with broadly flat tangible banking asset growth over the coming year, provide a greater cushion to protect senior creditors resulting in the higher uplift under the agency's Advanced LGF framework.

Sydbank's baa1 standalone BCA and Adjusted BCA remain unaffected and reflect the bank's (1) solid capitalisation with a common equity tier 1 (CET1) capital ratio of 17.3% as of December 2018; (2) sound funding structure and liquidity profile; and (3) relatively sustained profitability, although similar to peers it is under pressure by the low interest rate environment. These positive credit attributes are balanced against credit concentrations, including to single borrowers and some higher-risk or volatile sectors, and the bank's through-the-cycle asset quality performance.

The stable outlook on the bank's long-term deposit rating reflects that the LGF uplift incorporated in that rating is now the highest possible under the framework and also Moody's expectation that the bank's key credit characteristics will be supported by a benign domestic operating environment over the next 12-18 months, despite continued pressure on the bank's earnings from the persistent low interest rate environment.

#### -- RINGKJOBING LANDBOBANK A/S

The change in outlook to positive on Ringkjøbing's A1 long-term deposit and A2 long-term issuer ratings reflects the bank's funding plan and the likely evolution of its liability structure. Moody's expects that the bank, in line with its public disclosures, will gradually issue higher volumes of junior senior debt through to the end of 2021, which will provide additional subordination to the bank's deposits and senior unsecured debt, thereby reducing their expected loss-given-failure.

Under the rating agency's Advanced LGF framework, this evolution could eventually result in further rating uplift for Ringkjøbing's senior creditors from the two notches that the bank's deposit rating and from the one notch the issuer rating currently enjoy above the bank's a3 Adjusted BCA.

In December 2018, the Danish FSA determined an MREL for Ringkjøbing at 19.7% based on the bank's REA as of the end of 2017, which applied from 1 January 2019. The bank meets the requirement because it chose to grandfather senior debt issued before 1 January 2018 as part of its MREL. However, it has to replace this debt with junior senior issuances, or, with hybrid debt and equity to meet the subordination requirement by 2022. Ringkjøbing had DKK299 million in junior senior debt outstanding as of the end of 2018 and expects to issue around DKK1 billion of junior senior debt in each of 2019 and 2020.

Ringkjøbing's a3 standalone BCA and Adjusted BCA remain unaffected and reflect the bank's (1) still strong capitalisation following the recent merger with Nordjyske Bank A/S, with a 15.0% reported common equity Tier 1 (CET1) ratio as of end-December 2018 and a 14.5% shareholders' equity-to-total assets ratio; (2) high, albeit reduced profitability following the merger; and (3) solid funding profile, reflecting ample deposits and low reliance on market funding. However, the bank's BCA is counterbalanced by elevated asset risks from a somewhat concentrated loan book by geography and industry.

#### WHAT COULD CHANGE THE RATING UP/DOWN

The outlook on Ringkjøbing's long-term deposit and issuer ratings is positive, reflecting Moody's expectation that increased volumes of junior debt could improve the bank's senior creditors' position in a resolution scenario. Sydbank's deposit and senior unsecured ratings already benefit from the highest possible uplift under the LGF framework and therefore additional amounts of junior debt would not lead to further rating uplift.

The banks' ratings could also be upgraded following an improvement in their fundamental credit profiles, as indicated by the banks' BCAs, for instance if asset quality improves, especially if credit concentrations reduce, along with other issuer-specific developments.

The positive outlook on Ringkjøbing would be revised to stable, however, if the bank does not issue junior debt volumes in line with Moody's expectation or if its liability structure changes in a way that negatively affects the volume or subordination amounts of these instruments. There could also be negative rating pressure on both banks' deposit and relevant senior unsecured and issuer ratings if there is a shift in the banks' funding mix, such as lower subordinated instrument volumes, which could result in lower rating uplift than currently assumed under Moody's Advanced LGF framework.

The ratings could be downgraded due to a deterioration in the banks' fundamental credit profile, for instance if the rating agency observes: (1) a deterioration in asset quality or if their risk profile deteriorates (for example, as a result of increased exposures to more volatile asset classes); (2) a persistent weakening of the banks' recurring earnings power and operating efficiency; (3) weaker capital ratios that are below current expectations; and/or (4) a substantial increase in market funding reliance.

## PRINCIPAL METHODOLOGY

The principal methodology used in these ratings was Banks published in August 2018. Please see the Rating Methodologies page on [www.moodys.com](http://www.moodys.com) for a copy of this methodology.

## LIST OF ALL AFFECTED RATINGS

Issuer: Sydbank A/S

..Upgrades:

....Senior Unsecured Medium-Term Note Program, Upgraded to (P)A1 from (P)A2

.... Long-term Bank Deposits, Upgraded to A1 from A2, Outlook Changed To Stable From Positive

..Affirmations:

.... Long-term Counterparty Risk Assessment, Affirmed A1(cr)

.... Short-term Counterparty Risk Assessment, Affirmed P-1(cr)

.... Long-term Counterparty Risk Rating, Affirmed A1

.... Short-term Counterparty Risk Rating, Affirmed P-1

....Junior Subordinate Medium-Term Note Program, Affirmed (P)Baa3

....Junior Senior Unsecured Medium-Term Note Program, Affirmed (P)Baa1

....Subordinate Medium-Term Note Program, Affirmed (P)Baa2

....Other Short-term, Affirmed (P)P-1

....Pref. Stock Non-cumulative, Affirmed Ba1 (hyb)

....Junior Senior Unsecured Regular Bond/Debenture, Affirmed Baa1

....Subordinate Regular Bond/Debenture, Affirmed Baa2

.... Short-term Bank Deposits, Affirmed P-1

..Outlook Action:

....Outlook Changed To Stable From Positive

Issuer: Ringkjøbing Landbobank A/S

..Affirmations:

.... Long-term Counterparty Risk Assessment, Affirmed Aa3(cr)

.... Short-term Counterparty Risk Assessment, Affirmed P-1(cr)

.... Long-term Counterparty Risk Rating, Affirmed Aa3

.... Short-term Counterparty Risk Rating, Affirmed P-1

.... Long-term Issuer Rating, Affirmed A2, Outlook Changed To Positive From Stable

.... Short-term Issuer Rating, Affirmed P-1

.... Long-term Bank Deposits, Affirmed A1, Outlook Changed To Positive From Stable

.... Short-term Bank Deposits, Affirmed P-1

..Outlook Action:

....Outlook Changed To Positive From Stable

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