MOODY'S
INVESTORS SERVICE

# Rating Action: Moody's affirms Ringkjobing Landbobank's ratings; outlook stable

**23 May 2018**

Limassol, May 23, 2018 -- Moody's Investors Service (Moody's) has today affirmed Ringkjobing Landbobank A/S' (Ringkjobing) long-term deposit rating at A1 and its long-term issuer rating at A2, both with a stable outlook. At the same time, Moody's affirmed the bank's short-term deposit and issuer ratings at P-1, and its baseline credit assessment (BCA) and Adjusted BCA at a3. Ringkjobing's long- and short-term CR Assessments were also affirmed at Aa3(cr)/P-1(cr).

Today's rating action follows Ringkjobing's recently announced intention to merge with Nordjyske Bank A/S (Nordjyske - unrated). Ringkjobing will absorb Nordjyske's assets and liabilities, and will be the surviving legal entity.

The rating affirmation and stable outlook reflect Moody's expectation that the credit profile of Ringkjobing will remain broadly unchanged, despite the slightly weaker profile of Nordjyske, because the merged bank will maintain robust capitalization and profitability, while weaker initial asset quality of Nordjyske will be offset by increased loan book diversification.

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

RATINGS RATIONALE

-- RESILIENT CREDIT PROFILE FOLLOWING MERGER

The rating action was triggered by the announcement on 18 April 2018 of a merger agreement between Ringkjobing and Nordjyske. The merger requires formal approval by relevant authorities and the banks' shareholders, with extraordinary general meetings to be held in June.

The affirmation reflects Moody's view that Ringkjobing's credit profile will remain broadly unchanged despite a moderate reduction in the bank's capitalisation and profitability immediately following the envisioned transaction. Also, although the bank's problem loan ratio will increase in the short term, the acquisition will help reduce Ringkjobing's high credit concentrations and potentially contain asset quality volatility in the long run.

Moody's estimates that the bank's pro-forma tangible common equity to risk-weighted assets ratio will decline to a still robust 16% after the merger, from 18.8% as of March 2018, and that common equity tier 1 (CET1) will decrease by around 150 basis points to about 14.5%, still above the bank's previously communicated minimum capital target of around 14% and well above regulatory requirements. The rating agency's continued favourable assessment of the bank's capitalisation is also underpinned by a shareholders' equity-to-total assets that will remain solid, at around 15%, one the highest such ratios among those of Nordic and international banks.

The rating agency notes that the bank's problem loan ratio will rise to an estimated pro-forma 8%, from 4% as of year-end 2017, mainly as a result of Nordjyske's exposure to the troubled agriculture sector (11% of Nordjyske's loans and guarantees as of year-end 2017). However, this increase will be partly mitigated by a material reduction in credit concentrations, Rinkgjobing's 20 largest exposures were equivalent to 138% of its CET1 capital as of March 2018. Nordjyske's retail portfolio made up 46% of total compared to 29% for Ringkjobing as of year-end 2017 helping to diversify the combined portfolio. Exposure to the volatile real estate sector will likely remain high however, estimated at around 14% for the merged entity as of year-end 2017. Problem loan provisioning coverage, on a pro-forma basis will remain relatively robust at an estimated 75%, based on year-end 2017 results for both banks.

Moody's expects profitability to remain relatively strong with a net income to tangible assets of about 1.8% for 2018-19, albeit at a slightly more modest level when compared with a net income ratio of 2.3% in 2017. Also, the bank's cost-to-income ratio is expected to rise to around 40% in 2018, from a very cost efficient 31% in 2017, which the synergies extracted from the merger should gradually improve over time. Ringkjobing estimates one-off merger costs at DKK125 million in 2018, while the bank expects aggregate cost synergies of

DKK100 million in 2019 and 2020.

Moody's points out that the merger entails execution risks, especially given the similar size of the two entities (Ringkjobing had total assets of DKK27.0 billion in March 2018 and Nordjyske DKK20.3 billion); however, the two banks have similar cultures, and both banks use the same key product suppliers, such as Bankdata for IT solutions and Totalkredit for mortgage lending, partly mitigating these risks.

Meanwhile, Moody's expects that the transaction will not have any material impact on the merged entity's market funding reliance and liquidity because Nordjyske is almost exclusively funded by deposits and Ringkjobing has received a commitment for a Tier 2 capital issuance of DKK800 million for terms of 10 and 12 years that will help fund the DKK165 million that will be paid as cash consideration for the transaction and the bank's share buy-back program.

-- OUTLOOK STABLE

The stable outlook reflects Moody's views that 1) the bank's still strong capacity to generate capital internally can allow it to rebuild its regulatory capital buffers; 2) although Nordjyske had higher through-the-cycle credit losses than Ringkjobing, Moody's expects that as a merged entity, future losses would be lower as Ringkjobing will apply its own underwriting standards going forward; 3) if the bank is successful in managing execution risks, it could also stand to benefit from potential cross selling opportunities to Nordjyske's clientele, particularly from its niches such as lending to health professionals and their practices, and private banking.

-- LOSS GIVEN FAILURE ANALYSIS

The ratings affirmation also reflects Moody's expectation of the merged bank's liability structure and the rating agency's Advanced Loss Given Failure (LGF) analysis, which considers the risks faced by different debt and deposit classes across the liability structure should the bank enter resolution.

Moody's Advanced LGF analysis of the merged bank's volume of deposits, senior and subordinated liabilities, including the above-mentioned Tier 2 issuances, continues to indicate a very low loss-given-failure and results in two notches of rating uplift for Ringkjobing's A1 rated deposits from its a3 Adjusted BCA. For Ringkjobing's A2 issuer rating, Moody's LGF analysis continues to indicate low loss-given-failure, leading to one notch of rating uplift. Issuer ratings are opinions of the bank's ability to honour senior unsecured debt and debt-like obligations.

WHAT COULD CAUSE RATINGS TO GO UP / DOWN

Upward pressure on Ringkjobing's ratings could develop from (1) a seasoning of the bank's combined portfolio with low losses and a further significant reduction in concentrations, particularly to volatile sectors, leading to lower susceptibility to adverse events; (2) an improvement in asset-quality metrics, especially in relation to agricultural lending; and (3) a substantial improvement in the bank's liquidity.

Upward rating momentum for the long-term ratings of Ringkjobing could also develop as a result of a change in the bank's funding structure, such as the issuance of higher volumes of senior unsecured debt or subordinated debt that would result in additional notching uplift under Moody's LGF framework.

Downward pressure on Ringkjobing's ratings could emerge from (1) a further weakening in capital metrics below current expectations after the potential merger, or if the bank's capital buffers do not rise in line with any increase in regulatory capital requirements; (2) higher through-the-cycle losses, compared to the low levels experienced in the past for Ringkjobing, or, an increase in credit concentrations to single borrowers or higher risk sectors; (3) a persistent weakening of the bank's recurring earnings power and operating efficiency, for example from a failure to extract above-mentioned cost synergies; or (4) an increase in the bank's reliance on market funding from the current low level.

Ringkjobing's long-term ratings could also be downgraded following a significant decrease in the bank's junior deposits or senior and subordinated debt, leading to fewer notches of rating uplift under Moody's Advanced LGF analysis.

LIST OF AFFECTED RATINGS

Issuer: Ringkjobing Landbobank A/S

Affirmations:

....LT Bank Deposits, Affirmed A1, Outlook Remains Stable

....ST Bank Deposits, Affirmed P-1

....LT Issuer Ratings, Affirmed A2, Outlook Remains Stable

....ST Issuer Ratings, Affirmed P-1

....Adjusted Baseline Credit Assessment, Affirmed a3

....Baseline Credit Assessment, Affirmed a3

....LT Counterparty Risk Assessment, Affirmed Aa3(cr)

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

Outlook Actions:

....Outlook, Remains Stable

PRINCIPAL METHODOLOGY

The principal methodology used in these ratings was Banks published in April 2018. Please see the Rating Methodologies page on www.moodys.com for a copy of this methodology.

REGULATORY DISCLOSURES

For ratings issued on a program, series or category/class of debt, this announcement provides certain regulatory disclosures in relation to each rating of a subsequently issued bond or note of the same series or category/class of debt or pursuant to a program for which the ratings are derived exclusively from existing ratings in accordance with Moody's rating practices. For ratings issued on a support provider, this announcement provides certain regulatory disclosures in relation to the credit rating action on the support provider and in relation to each particular credit rating action for securities that derive their credit ratings from the support provider's credit rating. For provisional ratings, this announcement provides certain regulatory disclosures in relation to the provisional rating assigned, and in relation to a definitive rating that may be assigned subsequent to the final issuance of the debt, in each case where the transaction structure and terms have not changed prior to the assignment of the definitive rating in a manner that would have affected the rating. For further information please see the ratings tab on the issuer/entity page for the respective issuer on www.moodys.com.

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