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DNB Bank, Eiendomskreditt, Bank Norwegian Ratings Affirmed On Stabilizing Domestic Risks; DNB Bank Outlook Now Positive

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- House prices in Norway have fallen since the start of 2017, and we expect them to stabilize over the next two years.
- We expect the pace of household debt accumulation relative to income growth to ease from its comparatively high level.
- We now see Norway's economic risk trend as stable, further supported by subsiding risk of elevated credit losses from the oil and shipping sectors as a result of the improved global operating environment.
- We also believe an effective bank resolution regime will soon be in place, given the Norwegian parliament is currently finalizing its bank resolution framework.
- We are therefore revising our outlook on DNB Bank to positive and maintaining our negative outlooks on Eiendomskreditt and Bank Norwegian.
- Furthermore, we are affirming the ratings on DNB Bank, Eiendomskreditt, and Bank Norwegian.

STOCKHOLM (S&P Global Ratings) March 26, 2018--S&P Global Ratings said today that it took the following rating actions on three Norwegian banks:

- DNB Bank ASA: We revised the outlook to positive from stable and affirmed the 'A+/A-1' issuer credit ratings.
- Eiendomskreditt AS: We affirmed the 'BBB/A-2' issuer credit ratings and

maintained the negative outlook.
- Bank Norwegian AS: We affirmed the 'BBB/A-2' issuer credit ratings and maintained the negative outlook.

Our ratings and outlooks on the following banks are unaffected by our review of Norway under our Banking Industry Country Risk Assessment (BICRA): Eksportfinans ASA (BBB+/Positive/A-2); Storebrand Bank ASA (BBB+/Positive/A-2); and Gjensidige Bank ASA (A/Stable/A-1).

Norway's housing market has been adapting to various macroprudential policies, in addition to digesting increases in supply. As a result, house prices have fallen since the start of 2017, and we expect more balanced growth over the next two years. Although household debt as a share of disposable income remains higher than in other European countries, we expect the pace of debt accumulation relative to income growth to ease over the medium term. Therefore, we now see a stable economic risk trend. This is further supported by our view that the risk of elevated credit losses from the oil and shipping sectors is subsiding as a result of the improved global operating environment. Moreover, with Norway's crisis management framework, which draws upon the key parts of the EU's Banking Recovery and Resolution Directive (BRRD), being transposed into national law, we believe that Norway will soon have an effective resolution regime in place. Both of these factors led us to revise our outlook on DNB Bank to positive.

Our outlooks on Eiendomskreditt and Bank Norwegian remain negative, since both banks are specialized within their respective lending categories (domestic commercial real estate and pan-Nordic unsecured consumer lending). Commercial real estate financing has increased as a share of total lending in Norway, and as a result of prices generally increasing in various regions, we remain cautious on banks with substantial exposure and concentration risks. Bank Norwegian, meanwhile, continues its rapid pace of loan growth, particularly outside Norway, and as such, there is a risk that it could see a deterioration in its capital position and asset quality.

Our ratings and outlooks on Eksportfinans, Gjensidige Bank, and Storebrand Bank are unaffected: On Eksportfinans because the ratings and outlook primarily reflect our view of the company's expected wind-down path; our ratings on Gjensidige Bank and Storebrand Bank because the stabilizing economic environment should support the bank's operations, but not to the extent that would trigger a rating change. The stable outlook on Gjensidige Bank and the positive outlook on Storebrand Bank reflect the respective outlooks on their insurance company parents.

We have revised our view of the economic risk trend under our BICRA to stable from negative. Over the past several years, Norway has been navigating the aftermath of the oil price correction in 2014-2015, when the peak-to-trough price decline was about 70%. As a result, Norway has pursued an expansive fiscal and monetary policy stance to support the domestic economy throughout the cycle. There are now tailwinds that are strengthening Norway's economy as global activity improves and unemployment falls. As a result, the government is now pursuing a more balanced fiscal policy agenda.

Due to low interest rates and a fairly competitive banking market, annual private-sector credit growth has been 5%-6% over the past few years. However, real wages have been stagnating and as a result, the ratio of household debt to disposable income reached the relatively high level of 224% in 2017 as compared with that in other advanced economies. The growth in household debt has been primarily via mortgage lending, which led to a rapid rise in house prices over 2015-2016. The cumulative annual growth rate for national house prices was almost 15% during this period.

Now, however, thanks to an increased housing supply and the introduction of various macroprudential policies designed to curb household debt accumulation, house prices throughout most of Norway declined in 2017. The decline has been particularly steep in Oslo, where a lower loan-to-value requirement for secondary homes and a debt-to-income cap of 5x have had a larger impact than for the rest of the country. We project that house prices will stabilize and grow by approximately 2% over 2018-2019. This incorporates the view that the macroprudential policies the Norwegian Financial Supervisory Authority (FSA) recommended will be implemented to ensure that credit growth will not continue unchecked.

We expect that the global economic climate will remain supportive for both the oil and shipping sectors, which in turn supports our view of Norway's banking sector. While both oil and shipping are considered volatile sectors, we believe the peak of related credit losses was in 2016, when total credit losses reached 0.30%. Nonperforming loans are also expected to decline, since many of the past restructurings have led to an improvement in asset quality. Meanwhile, oil companies have improved their efficiency metrics and, as a result, have healthier operating margins. Our current forecast of oil prices remaining at about $55-$60 per barrel underpins this assessment.

Incorporated in our view of the banking sector is the strength of the sovereign and the flexibility of both the exchange rate and monetary policy. Norway remains among the richest nations in the world, with a GDP per capita of $75,400, pointing to a high capacity to service debt. The depreciation of the krone has also been beneficial to the exports sector and has helped boost mainland GDP over 2016-2017. As a result, during the economic contraction, real GDP growth reached 1.1% in 2016 and we now expect it to rebound and gradually move toward 2.0%.

After our BICRA review, we have also revised our view of government support for the banking sector to uncertain. We expect Norway's crisis management directive will be implemented soon, given that the legislation is now in the final stages of approval in parliament. We now consider support to the banking sector to be uncertain because the BRRD limits the government's ability to provide pre-emptive capital injections to banks in scenarios where systemwide financial stability is at risk and to avoid potential capital shortfalls at individual banks. This is particularly relevant for DNB Bank, a domestically systemically important bank.

Nevertheless, further clarity on the future structure of the minimum requirement for own funds and eligible liabilities (MREL) is needed to adequately assess DNB Bank's additional loss-absorbing capacity (ALAC). The Norwegian FSA, which is to become the resolution authority, published its views in a February 2017 commentary, where it appears to show preference for banks to use a new class of subordinated liabilities to meet MREL; however, this has yet to be finalized. Issuance of such instruments would create a meaningful buffer, which could then be bailed in ahead of senior unsecured debtholders.

- DNB BANK ASA

We have revised our outlook on DNB Bank to positive because we believe the bank will face with MREL over the medium term, which it will need to meet with subordinated liabilities. This has led us to remove the one notch of uplift for government support, which has been offset by a negative transitional notch in anticipation of Norway's implementation of its resolution regime. The potential issuance of bail-in-able debt supports our positive outlook on DNB Bank. Once the structure of MREL for DNB Bank is clarified, we believe we can better assess the sustainability of DNB Bank's ALAC buffer.

We believe DNB Bank will likely build a sustainable ALAC buffer over the next two to four years, given the now uncertain support from the government as a result of the BRRD's implementation. The ALAC buffer is expected to provide protection to senior bondholders. We anticipate that the Norwegian FSA will set MREL for DNB Bank in the next 12 months, which will clarify longer-term issuance plans for a class of senior nonpreferred instruments that will likely satisfy subordination requirements once fully implemented.

Furthermore, we believe that the economic risks in the Norwegian banking sector have now stabilized, supported by higher macroprudential requirements to curb household debt accumulation, and a supportive credit environment for volatile sectors, such as oil and shipping.

An upgrade would hinge on our view of DNB Bank's creditworthiness as being clearly and sustainably consistent with that of similarly rated international peers at that higher rating level, in particular regarding the funding profile.

We could revise the outlook to stable if we saw a lower likelihood of a substantial increase in the ALAC buffer. A negative rating action could also occur if, contrary to our expectations, we felt that asset quality improvements had slowed, which could result from a worsening in the operating climate in Norway, affecting some of DNB Bank's lending exposures.

- EIENDOMSKREDITT AS

We maintained our negative outlook on Eiendomskreditt to indicate that, despite economic risks in Norway having stabilized, we could lower the ratings within our two-year outlook horizon if Eiendomskreditt's growth strategy resulted in a material change in its risk appetite, a significant increase in loan concentrations, or increased operational risks, or if we saw early signs of asset quality deterioration.

We could revise the outlook to stable if we observed Eiendomskreditt successfully implementing its new growth strategy without compromising asset quality, while maintaining its elevated risk-adjusted capitalization and solid operational performance.

- BANK NORWEGIAN AS

We have maintained our negative outlook on Bank Norwegian, reflecting our view that the bank will continue its phase of rapid loan growth over the next two years. We view the maintenance of strong capital ratios and good profitability as important for the overall stability of the financial profile.

Bank Norwegian's stand-alone credit profile is unchanged at 'bbb'. While loan growth continues to be particularly high, the bank's capitalization has improved, owing to strong retained earnings and an equity contribution from its owners after an increase in the minimum regulatory capital requirement. However, over the next two years, we expect further significant loan growth in markets where Bank Norwegian has less of a presence currently, which could reduce the stability of its asset quality, capital position, and funding base.

We could lower the rating on Bank Norwegian in the next two years if we observe a more aggressive capital policy leading to its risk-adjusted capital ratio falling below 15%. We could also lower the rating if the bank's asset quality deteriorates more than we expect, or if we observe pressure on the bank's funding profile.

We could revise the outlook to stable if the bank maintains very strong capitalization and we view lending growth and the evolution of the business as being more sustainable. We anticipate this would be indicated, for example, by an improvement of asset-quality figures in Bank Norwegian's new markets.

BICRA SCORE SNAPSHOT: NORWAY

	To	From
BICRA Group	2	2
Economic risk	2	2
Economic resilience	Very low risk	Very low risk

Economic imbalances	Intermediate risk	Intermediate risk
Credit risk in the economy	Low risk	Low risk
Trend	Stable	Negative
Industry risk	3	3
Institutional framework	Intermediate risk	Intermediate risk
Competitive dynamics	Low risk	Low risk
Systemwide funding	Intermediate risk	Intermediate risk
Trend	Stable	Stable

*Banking Industry Country Risk Assessment (BICRA) economic risk and industry risk scores are on a scale from 1 (lowest risk) to 10 (highest risk). For more details on our BICRA scores on banking industries across the globe, please see "Banking Industry Country Risk Assessment Update," published monthly on RatingsDirect.

RELATED CRITERIA

- Criteria - Financial Institutions - General: Risk-Adjusted Capital Framework Methodology, July 20, 2017
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings , April 7, 2017
- Criteria - Financial Institutions - Banks: Bank Rating Methodology And Assumptions: Additional Loss-Absorbing Capacity, April 27, 2015
- Criteria - Financial Institutions - Banks: Bank Hybrid Capital And Nondeferrable Subordinated Debt Methodology And Assumptions, Jan. 29, 2015
- General Criteria: Group Rating Methodology, Nov. 19, 2013
- Criteria - Financial Institutions - Banks: Quantitative Metrics For Rating Banks Globally: Methodology And Assumptions, July 17, 2013
- Criteria - Financial Institutions - Banks: Banks: Rating Methodology And Assumptions, Nov. 9, 2011
- Criteria - Financial Institutions - Banks: Banking Industry Country Risk Assessment Methodology And Assumptions, Nov. 9, 2011
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009
- Criteria - Financial Institutions - Banks: Commercial Paper I: Banks, March 23, 2004

RELATED RESEARCH

- Banking Industry Country Risk Assessment Update: February 2018, Feb. 2, 2018
- Banking Industry Country Risk Assessment: Norway, March, 14, 2017

RATINGS LIST

Outlook Action; Ratings Affirmed

	To	From

DNB Bank ASA:		
Issuer Credit Rating	A+/Positive/A-1	A+/Stable/A-1

Ratings Affirmed

Eiendomskreditt AS	
Issuer Credit Rating	BBB/Negative/A-2
Bank Norwegian AS	
Issuer Credit Rating	BBB/Negative/A-2

NB: This list does not include all the ratings affected.

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