

Rating Action: Moody's changes rating outlook to negative for five Norwegian banks following proposed BRRD legislation; ratings affirmed

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Limassol, July 10, 2017 -- Moody's Investors Service ("Moody's") has today changed the outlook to negative from stable on the deposit and senior debt ratings of five regional savings banks Sparebanken Vest, SpareBank 1 SMN, SpareBank 1 Ostlandet, SpareBank 1 Nord-Norge and Sparebanken Sor. The rating agency has also maintained the negative outlook assigned to the deposit and debt ratings of DNB Bank ASA and SpareBank 1 SR-Bank ASA, and the stable outlook assigned to Kommunalbanken AS's (KBN) senior unsecured debt and issuer rating. The deposit, senior debt, and issuer ratings of all of the above banks, where applicable, as well as the subordinated debt rating of KBN, were affirmed reflecting the broadly unchanged standalone creditworthiness and liability structures of the banks.

The negative outlooks were triggered by the proposed legislation introduced to the Norwegian parliament on 21 June 2017 by the Ministry of Finance, to implement the EU's bank recovery and resolution directive (BRRD) and the deposit guarantee scheme directive (<https://www.regjeringen.no/en/aktuelt/new-rules-on-deposit-guarantee-schemes-and-bank-recovery-and-resolution/id2558196>). If the law proposal is enacted, the rating agency expects that Norwegian banks will benefit from a lower probability of government support, which will exert downward pressure on the ratings. Today's rating action signals Moody's intention to more closely align its support assumptions for Norwegian banks to those of its European peers under BRRD resolution framework.

Moody's decision to affirm the ratings and maintain a stable outlook on state-owned KBN reflects the rating agency's view that it is likely to maintain its current assessment of very high government support for this state-owned entity.

Today's rating action covers all Norwegian banks whose ratings currently benefit from an uplift due to government support assumptions. A full list of the affected ratings is provided at the end of this press release.

RATINGS RATIONALE

PROPOSED BRRD LAW TRIGGERS NEGATIVE OUTLOOK FOR FIVE SAVINGS BANKS

On 21 June 2017, the Norwegian Ministry of Finance forwarded to the parliament proposed draft legislation with a new set of rules to prevent and manage bank failures, which fully corresponds to the EU's bank recovery and resolution directive (BRRD). The legislative proposal entails a new set of rules regarding recovery and resolution plans, early intervention and resolution tools, including bail-in powers.

The proposal designates the Financial Authority (FSA) of Norway as the resolution authority and allows it to impose losses on creditors at the point of non-viability, through a "bail-in" of an amount equal to 8% of an entity's total assets. In accordance with the stricter approach towards government support included in the newly proposed legislation, which is more closely in line with the EU's BRRD, Moody's has changed the deposit and senior debt rating outlook on five Norwegian banks, where applicable, (Sparebanken Vest, SpareBank 1 SMN, SpareBank 1 Ostlandet, SpareBank 1 Nord-Norge and Sparebanken Sor) to negative from stable. These five Norwegian banks' ratings currently incorporate one notch of rating uplift due to the rating agency's moderate government support assumption driven by their systemic importance. Moody's said that its government support assumptions are likely to be revised lower, once the proposed legislation is passed into law by the parliament.

Accordingly, the negative outlook reflects the future direction of these banks' deposits and senior debt ratings over the next 12-18 months. The rating agency expects the approval of the new law by the parliament to take effect after a period of more than three months, given the current summer closure of the parliament and the upcoming parliamentary elections in Norway in September.

NEGATIVE OUTLOOK MAINTAINED FOR DNB BANK AND SPAREBANK 1 SR-BANK

The rating agency said that the negative outlook on the deposit and senior debt ratings of DNB Bank and

SpareBank 1 SR-Bank was maintained, reflecting both existing idiosyncratic asset quality challenges and the impact of the proposed new BRRD legislation. Currently, Moody's assumes a high government support assumption for DNB Bank - the largest bank in Norway - resulting in two notches of rating uplift, and moderate support for SpareBank 1 SR-Bank, resulting in one notch of rating uplift, in line with the other five savings banks mentioned above. The existing negative rating outlook reflects the downside risks stemming from their oil-related exposure and the impact on their financial performance from higher loan loss provisions, although Moody's recognizes that their overall standalone credit profiles have been relatively resilient so far.

STABLE OUTLOOK MAINTAINED FOR KBN

Moody's has maintained KBN's stable outlook, signaling the maintenance of its very high government support assumptions for this state-owned financial institution. The rating agency believes that despite the upcoming BRRD law implementation, KBN will continue to benefit from a very high support from the Norwegian government due to: (1) its state ownership and control; (2) its role as the government's tool to enact policies related to local governments; and (3) its public policy mandate to provide low cost financing to the Norwegian local government sector where its current market share is close to 50%. Moody's also believes that the government has the willingness and ability to provide financial support to KBN to cover any capital shortfall.

RATING AFFIRMATIONS FOR ALL AFFECTED BANKS

The affirmation of the banks' ratings shown at the end of this press release, is predominantly driven by Moody's view that the standalone creditworthiness and liability structure of these banks remain broadly unchanged. Moody's said that it will revise its government support assumptions, once the proposed legislation is passed into law by the parliament and in effect the resolution framework is implemented in Norway.

WHAT COULD CHANGE THE RATING UP/DOWN

DNB BANK

Upward pressure on DNB's debt and deposit rating is unlikely in the near term given the negative outlook. The outlook could return to stable if DNB: (1) further reduces its asset vulnerability, especially in relation to oil-related and offshore exposures as well as to historically more volatile segments, such as shipping and CRE; (2) maintains strong and stable earnings generation without increasing its risk profile; and (3) preserves sustained access to international capital markets.

Downwards pressure on the ratings could develop if: (1) DNB's financing conditions become challenging; (2) its asset quality were to deteriorate beyond our expectations and lead to further increase of the bank's credit costs; (3) its credit profile substantially deteriorates due to adverse developments in the Norwegian oil, offshore and real-estate markets; (4) DNB increases its involvement in more risky operations such as capital market activities; and/or (5) government support reduces due to the implementation of a resolution regime in Norway.

REGIONAL SAVINGS BANKS

Upward rating momentum is currently unlikely given the negative outlook on all six savings banks affected by this rating action. Over time, upward pressure could develop if these banks demonstrate: (1) reduced exposure to more volatile sectors such as the oil and commercial real estate related sectors; (2) diversified access to capital markets and improved liquidity; and/or (3) stronger earnings generation without an increase in risk profiles.

Downward rating pressure would develop on these banks ratings if: (1) Moody's expects their problem loan ratios to increase above its current system-wide expectation of approximately 2%; (2) profitability deteriorates further from expected levels; (3) the banks fail to sustain their market position; and/or (4) government support reduces due to the implementation of a resolution regime in Norway.

KBN

The likelihood of an upgrade of KBN's BCA is limited because it is already at the higher end of peers' and banks' BCAs globally. An upgrade of the BCA will not translate into a higher senior unsecured rating which is already at Aaa.

Downward pressure on KBN's rating could arise as a result of: (1) weaker asset quality which is currently unlikely; (2) a dilution of KBN's public policy mandate; (3) a weaker position in the debt capital markets; (4)

sustained weaker financial performance, which is currently unlikely; (5) a decrease in the probability of government support resulting from any amendment to the BRRD or lower willingness of the government to support; or (6) a downgrade of Norway's sovereign ratings.

The principal methodology used in these ratings was Banks published in January 2016. Please see the Rating Methodologies page on www.moodys.com for a copy of this methodology.

LIST OF AFFECTED RATINGS

Affirmations:

..Issuer: DNB Bank ASA

.... LT Bank Deposits, Affirmed Aa2 Negative

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

....Senior Unsecured Regular Bond/Debenture, Affirmed Aa2 Negative

....Senior Unsecured Regular Bond/Debenture, Affirmed (P)Aa2

..Issuer: DNB Bank ASA, New York Branch

.... LT Deposit Note/CD Program, Affirmed Aa2 Negative

..Issuer: Kommunalbanken AS

.... LT Issuer Rating, Affirmed Aaa Stable

.... Senior Unsecured Regular Bond/Debenture, Affirmed Aaa Stable

.... Subordinate Regular Bond/Debenture, Affirmed Aa3

..Issuer: SpareBank 1 Nord-Norge

.... LT Issuer Rating, Affirmed A1 Negative From Stable

.... LT Bank Deposits, Affirmed A1 Negative From Stable

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

.... Senior Unsecured Regular Bond/Debenture, Affirmed A1 Negative From Stable

..Issuer: SpareBank 1 Ostlandet

.... LT Issuer Rating, Affirmed A1 Negative From Stable

.... LT Bank Deposits, Affirmed A1 Negative From Stable

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

..Issuer: SpareBank 1 SMN

.... LT Issuer Rating, Affirmed A1 Negative From Stable

.... LT Bank Deposits, Affirmed A1 Negative From Stable

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

.... Senior Unsecured Regular Bond/Debenture, Affirmed A1 Negative From Stable

..Issuer: SpareBank 1 SR-Bank ASA

.... LT Issuer Rating, Affirmed A1 Negative

.... LT Bank Deposits, Affirmed A1 Negative

.... ST Bank Deposits, Affirmed P-1
.... Senior Unsecured Regular Bond/Debenture, Affirmed A1 Negative
..Issuer: Sparebanken Sor
.... LT Issuer Rating, Affirmed A1 Negative From Stable
.... LT Bank Deposits, Affirmed A1 Negative From Stable
.... ST Bank Deposits, Affirmed P-1
..Issuer: Sparebanken Vest
.... LT Bank Deposits, Affirmed A1 Negative From Stable
.... ST Bank Deposits, Affirmed P-1
.... Senior Unsecured Regular Bond/Debenture, Affirmed A1 Negative From Stable

Outlook Actions:

..Issuer: DNB Bank ASA
....Outlook, Remains Negative
..Issuer: DNB Bank ASA, New York Branch
....Outlook, Remains Negative
..Issuer: Kommunalbanken AS
....Outlook, Remains Stable
..Issuer: SpareBank 1 Nord-Norge
....Outlook, Changed To Negative From Stable
..Issuer: SpareBank 1 Ostlandet
....Outlook, Changed To Negative From Stable
..Issuer: SpareBank 1 SMN
....Outlook, Changed To Negative From Stable
..Issuer: SpareBank 1 SR-Bank ASA
....Outlook, Remains Negative
..Issuer: Sparebanken Sor
....Outlook, Changed To Negative From Stable
..Issuer: Sparebanken Vest
....Outlook, Changed To Negative From Stable

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