MOODY'S RATINGS

CREDIT OPINION
11 September 2024

Update

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RATINGS

Sparebanken Sor

Domicile	Kristiansand, Norway
Long Term CRR	A1
Type	LT Counterparty Risk Rating - Fgn Curr
Outlook	Not Assigned
Long Term Debt	(P)A1
Type	Senior Unsecured MTN - Fgn Curr
Outlook	Not Assigned
Long Term Deposit	A1
Type	LT Bank Deposits - Fgn Curr
Outlook	Positive

Please see the ratings section at the end of this report for more information. The ratings and outlook shown reflect information as of the publication date.

Contacts

Paula Jouandet-Dahlen +46.851.791.280
VP-Senior Analyst
paula.jouandetdahlen@moodys.com

Juliana Cerenkova +46.8.5179.1254
Ratings Associate
juliana.cerenkova@moodys.com

Nondas Nicolaides +357.25.693.006
VP-Sr Credit Officer
nondas.nicolaides@moodys.com

Simon James Robin Ainsworth +44.207.772.5347
Associate Managing Director
simon.ainsworth@moodys.com

Sparebanken Sor

Update following outlook change to positive

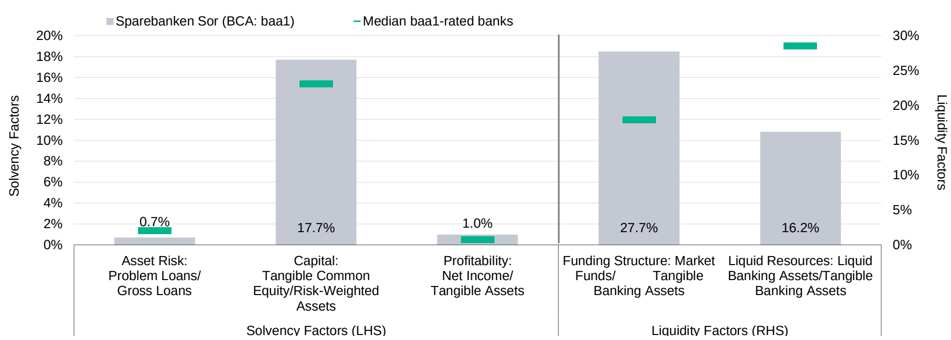
Summary

Sparebanken Sor's A1 long-term deposit and issuer ratings, and the Baa1 junior senior long-term debt rating are driven by the bank's Baseline Credit Assessment (BCA) of baa1 and the application of our Advanced Loss Given Failure (LGF) analysis. Sparebanken Sor's ratings do not benefit from any government support.

The bank's BCA reflects its strong capital buffers and asset-quality metrics, with nonperforming loans (NPLs)/gross loans of around 0.7% as of June 2024. The bank's corporate book is however exposed to risks stemming from (i) high single-borrower concentration, making it vulnerable in the event of a potential default of one of its large customers, and (ii) the bank's sizable exposure to commercial real estate, where borrowers are particularly exposed to the high rate environment.

Looking ahead, we expect Sparebanken Sor's credit profile to be gradually aligned with that of Sparebanken Vest (Deposits Aa3 stable, BCA of a3), assuming a successful completion of the announced merger with the latter, providing to the merged entity a strengthened geographical footprint and less concentrated loan portfolio.

Exhibit 1
Rating Scorecard- Key financial ratios



These ratios are calculated based on our Banks Methodology scorecard. The bank's problem loan and profitability ratios are the weaker of the average of the latest three year-end ratios and the latest reported ratio. The bank's capital ratio is the latest reported figure. The bank's funding structure and liquid resources ratios are the latest year-end figures.
Source: Moody's Banking Financial Metrics

Credit strengths

» Resilient asset quality, with two-thirds of lending to private mortgage borrowers and close to zero exposure to the oil and offshore sectors

» Strong capital levels with a robust leverage ratio

Credit challenges

» Some single borrower and sector loan concentrations, which increase asset risk

» Reliance on market funding, which renders the bank vulnerable to fluctuations in investor sentiment

Rating outlook

The outlook for Sparebanken Sor's deposit and issuer ratings is positive reflecting our view that the bank's credit profile and ratings would be gradually aligned with those of Sparebanken Vest, should the acquisition and subsequently the anticipated legal merger successfully conclude.

Factors that could lead to an upgrade

The ratings on Sparebanken Sor could be upgraded following the successful completion of the merger with Sparebanken Vest.

Factors that could lead to a downgrade

Given the positive long-term deposit and issuer ratings outlook, we are unlikely to downgrade Sparebanken Sor's ratings during the outlook period. However, failure to proceed with the merger would likely result in Sparebanken Sor's ratings outlook reverting to stable. The ratings could also be downgraded as result of a reduction in the volumes of loss absorbing liabilities protecting depositors and creditors in case of failure.

Key indicators

Exhibit 2
Sparebanken Sor (Consolidated Financials) [1]

	06-24[2]	12-23[2]	12-22[2]	12-21[2]	12-20[2]	CAGR/Avg.[3]
Total Assets (NOK Billion)	165.7	155.7	157.4	144.2	142.1	4.5[4]
Tangible Common Equity (NOK Billion)	15.5	15.6	14.6	13.5	12.6	6.0[4]
Problem Loans / Gross Loans (%)	0.7	0.8	0.5	0.7	0.9	0.7[5]
Tangible Common Equity / Risk Weighted Assets (%)	17.7	18.4	18.3	17.1	16.2	17.5[6]
Problem Loans / (Tangible Common Equity + Loan Loss Reserve) (%)	5.8	6.6	4.2	5.5	7.7	6.0[5]
Net Interest Margin (%)	2.0	1.9	1.6	1.3	1.3	1.6[5]
PPI / Average RWA (%)	2.8	2.6	1.9	1.7	1.7	2.1[6]
Net Income / Tangible Assets (%)	1.3	1.1	0.8	0.8	0.7	0.9[5]
Cost / Income Ratio (%)	36.0	38.0	42.9	43.7	42.8	40.7[5]
Market Funds / Tangible Banking Assets (%)	28.2	27.7	29.7	27.9	31.4	29.0[5]
Liquid Banking Assets / Tangible Banking Assets (%)	19.0	16.2	18.8	16.9	17.8	17.7[5]
Gross Loans / Due to Customers (%)	178.0	184.7	189.4	185.4	187.2	184.9[5]

[1] All figures and ratios are adjusted using Moody's standard adjustments. [2] Basel III - fully loaded or transitional phase-in; IFRS. [3] May include rounding differences because of the scale of reported amounts. [4] Compound annual growth rate (%) based on the periods for the latest accounting regime. [5] Simple average of periods for the latest accounting regime. [6] Simple average of Basel III periods.
Sources: Moody's Ratings and company filings

Profile

Sparebanken Sor is a regional Norwegian bank, with consolidated assets of NOK165.7 billion (€14.5 billion) as of June 2024, providing retail and corporate banking services to individuals, companies and public authorities, mainly in southern Norway. Its products include financing, savings facilities, placements, insurance, pensions and payment facilities. It was the ninth-largest bank in Norway in terms of consolidated assets as of year-end 2023.

Recent developments

On 28 August, Sparebanken Sor announced the agreement to merge with Sparebanken Vest (Aa3 stable, a3) in forming the largest savings bank in Norway. The all-share merger is subject to approvals from the general assemblies of both banks and regulatory authorities, including the Norwegian FSA and Competition Authority, with an aim to complete the legal merger by the end of the second quarter of 2025. The combination of the two savings banks would create the largest savings bank in Norway with a pro forma gross lending book of NOK429 billion across retail (56%), Bulder (13%), a digital retail bank, and corporates (31%), at end June 2024. The announcement continues the ongoing consolidation trend among the Norwegian savings banks that has taken place in recent years, largely driven by increased regulatory demands and complexity.

The enlarged bank would hold consolidated assets of NOK517 million (on a pro forma basis at end June 2024), including the financing company Brage Finans, which will be majority-owned by the new entity. Ownership in other product companies in Frendegruppen would also increase.

The two banks estimate annual cost reductions in the range of NOK350-400 million by 2028, primarily related to natural attrition of staff, scale advantages in procurement and IT related costs. In addition, while capital requirements for the merged entity will likely rise as a larger and systemically important bank, capital synergies are also likely to emerge resulting from the application of Sparebanken Vest's Internal ratings-based (IRB) model to Sparebanken Sor's portfolio (currently under the standardised approach).

Detailed credit considerations

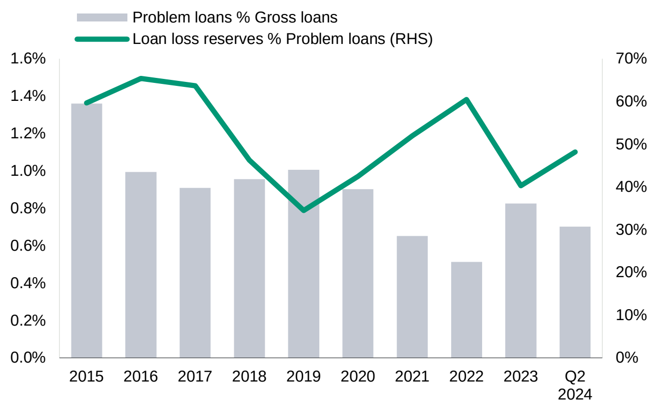
Resilient asset quality metrics, but the loan book is exposed to risks stemming from high credit concentrations and sizable commercial real estate exposures

Sparebanken Sor's problem loans (Moody's definition) were 0.7% of gross loans as of June 2024, decreasing slightly from 0.8% as of December 2023 (with a nominal decrease of NOK133 million over the first six months of 2024). The ratio is in line with other large Norwegian savings banks and lower than the average of 1.6% of banks globally with a BCA of baa1. The level of problem loans has been relatively stable over the past seven years (see Exhibit 3).

Sparebanken Sor's allowance for loan losses was NOK445 million as of June 2024 (December 2023: NOK426 million) and total provisioning coverage increased to 48.2% from 40.3% as of December 2023 reducing the risks to the bank's earnings and capital from its existing stock of problem loans (see Exhibit 4).

Exhibit 3

Sparebanken Sor's problem loan ratio has remained consistently below 1% over the past years

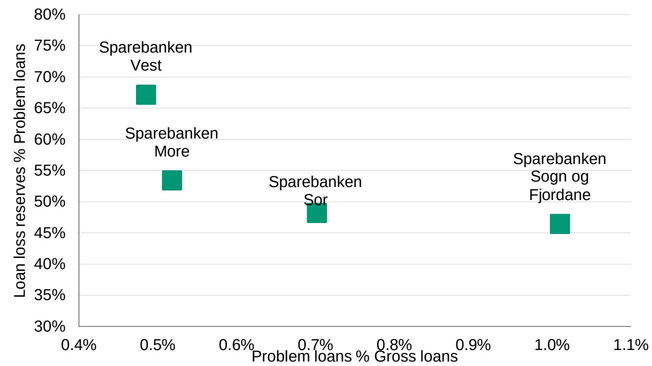


Sources: Sparebanken Sor's disclosures and Moody's Ratings

Exhibit 4

...and is well positioned among similarly rated regional peers

Data as of June 2024



Source: Banks' disclosures, Moody's Ratings

Sparebanken Sor's loan book is dominated by retail mortgages, representing around 64% of the gross loan book as of June 2024, which has been resilient historically with low default levels. We consider the bank's low average loan-to-value (LTV) of around 56% for mortgages a mitigating factor to a potential fall in house prices.

However, the bank has also significant concentration in the real estate and construction sectors, at around 23.5% of gross loans as of June 2024 (property management accounting for 17.5%, real estate development for 4.2%, and building and construction for 1.8%). This poses risks to future loan book performance in the scenario of any significant reduction in property prices in the region. Most of the bank's outstanding impairments relate to its corporate exposures, of which over half relate to property management, development and construction sectors, all of which are particularly sensitive to the current high rate environment.

Furthermore, the bank's corporate book has certain single-borrower concentration, especially to commercial real estate (CRE) clients, making it vulnerable in the event of a potential default of one of its large customers.

Our downward adjustment to the bank's Asset Risk score to baa2 captures these concentration risks, in addition to the limited geographical diversification compared with larger Nordic commercial banks, as Sparebanken Sor is mainly exposed to southern Norway.

In anticipation of the developments around the merger with Sparebanken Vest, we estimate that the resulting entity's asset quality will improve compared with that of Sparebanken Sor as the problem loans ratio will decrease slightly and the retail portfolio will take up a larger part of the gross loans at 69% (including Bulder). We further acknowledge the improved geographical footprint of the combined entity.

Strong capital levels with a robust leverage ratio

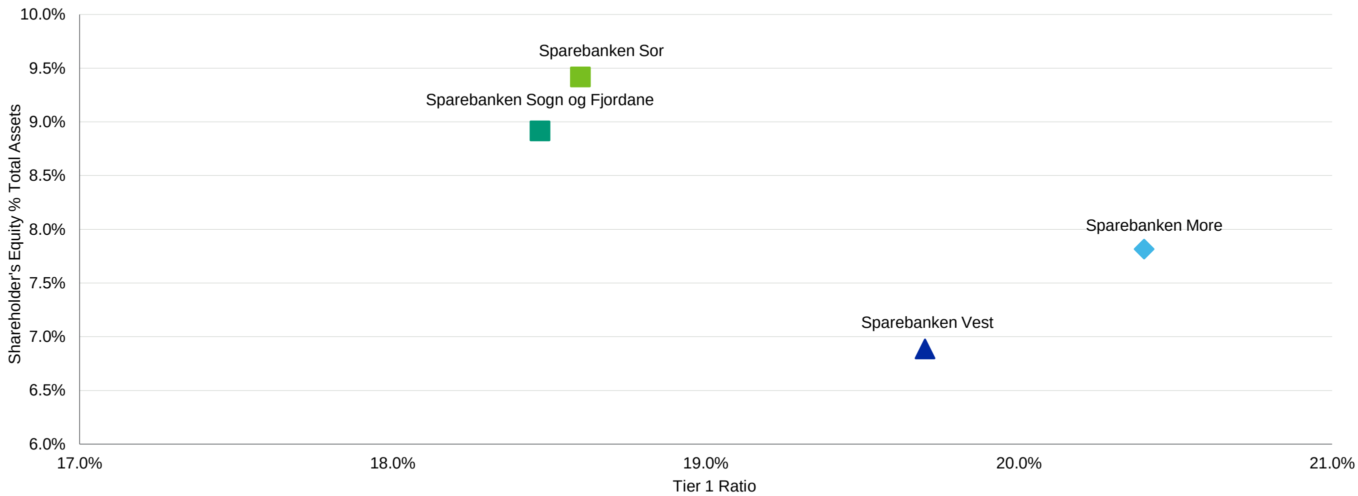
Sparebanken Sor's capitalisation is strong relative to its risk profile, with a Common Equity Tier 1 ratio of 16.7% as of June 2024, well above its regulatory minimum of 14.9%, and above its target of 16.2% as of June 2024. It has one of the highest leverage ratio among Norwegian savings banks, at 9.2% in June 2024.

The bank is the only one of the large regional banks in Norway that still applies the standard method in its RWA calculations and is process to apply to the Financial Supervisory Authority for an approval to use the Internal Ratings-Based (IRB) approach to calculate RWA, but the process is lengthy.

The planned merger is viewed as advantageous for the combined entity, supported by capital synergies generated by applying Sparebanken Vest's Internal ratings-based (IRB) model to Sparebanken Sor's portfolio (currently under the standardised approach). The banks have identified net NOK2 billion of capital synergies in addition to NOK2.1 billion stemming from the implementation of Basel IV. However, as the merger creates a larger and systemically important financial institution, capital requirements are likely to rise.

Exhibit 5

Sparebanken Sor's capital levels are comparable with its similarly rated peers



Based on Q2 2024 Moody's-adjusted data, Sparebanken Sor and Sparebanken Sogn og Fjordane use the standard method, while Sparebanken More use Internal Ratings-Based (foundation) and Sparebanken Vest use the advanced Internal Ratings-Based approach for their risk-weighted assets and capital calculation.
Source: Moody's Financial Metrics

Our assigned Capital score is aa2 which reflects both the bank's strong leverage ratio and risk-adjusted capital ratios but also the bank's low level of equity certificates (EC) in the capital structure. However, the EC ratio in line with most domestic peers.

Improved profitability on the back of strong net interest margin and efficient cost structure

Sparebanken Sor relies predominantly on stable interest income from lending, but earnings diversification is limited compared to peers, with net interest income representing around 86% of its net revenue in Q2 2024. The bank reported an annualized net interest margin of 2.81% for retail loans and 3.18% for corporate loans in June 2024, up from 2.76% and 3.18%, respectively, the year before, reflecting the increase in interest rate and somewhat offset by increased competition among its peers. Over the next 12-18 months, we expect margin to remain strong, combined with stable loan growth (4.6% year on year as of June 2024).

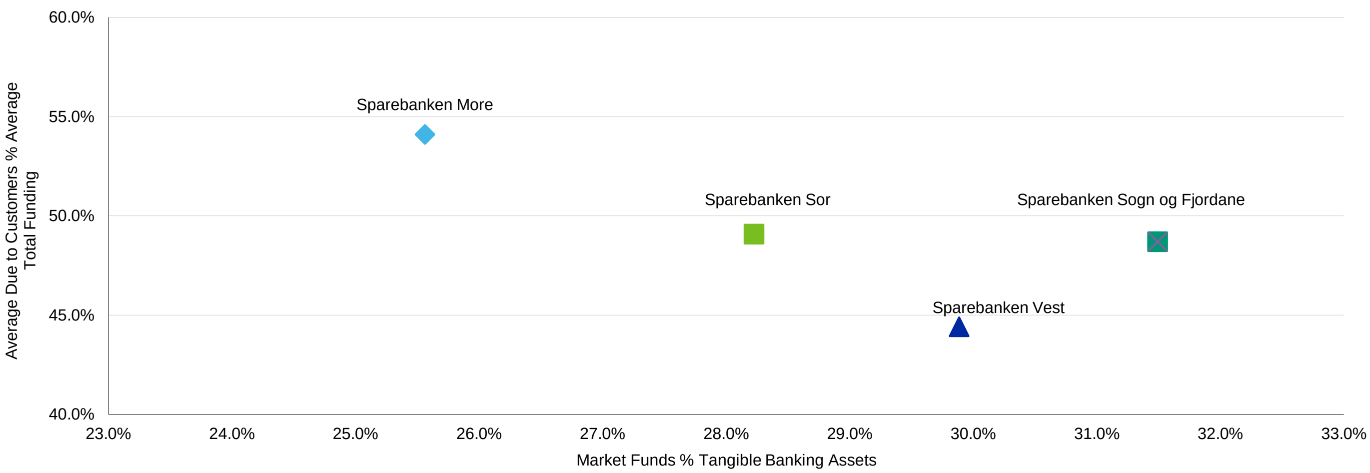
The bank's cost-efficient structure and set-up, despite spending on digitalisation and channel interaction, should continue to support its core pre-provision income and bottom-line also during times of stress. The bank has reported a cost-to-income ratio of 35.5% (excluding net income from financial instruments) for the six months of 2024, lower than the reported ratio of 37.0% a year earlier and well within the bank's 40% target.

Reliance on market funding renders the bank vulnerable to fluctuations in investor sentiment

Sparebanken Sor's funding is underpinned by a strong deposit base, which amounts to roughly 49% of non-equity funding. Nevertheless, a large part of its sizeable deposit base are deposits from corporates and municipalities (31% and 22% respectively), which are more sensitive to market confidence and pricing as they are typically larger and uninsured, although deposits from municipalities benefit from multi-years agreements enhancing their stickiness. The bank also remains reliant on market funding, which accounted for 28% of tangible banking assets as of June 2024, and which renders the bank susceptible to changes in investor sentiment.

A sizeable and growing portion of market funds is in the form of covered bonds, which provide the bank with an important source of funding. Using our methodology for banks, we reflect the stability of covered bonds relative to unsecured market funding through an adjustment to the bank's market funds/tangible assets ratio. Nonetheless, our Funding Structure score reflects our view that the bank's overall funding profile remains a weakness relative to the other scorecard metrics.

Exhibit 6
Reliance on market funding remains a fundamental weakness for the bank, a common attribute of Norwegian banks



Based on Q2 2024 Moody's-adjusted data.
Source: Moody's Financial Metrics

Sparebanken Sor also maintains sizeable buffers of high-quality liquid assets. As of June 2024, liquid assets accounted for around 19% of tangible banking assets, comprising cash and deposits with the central bank and the securities portfolio that consists in a vast majority of Aaa-rated instruments in the form of Norwegian covered bonds and bonds from the government and other public entities.

These holdings are mostly Norwegian securities and covered bonds of other local banks, which could be a source of vulnerability from a concentration risk perspective and in case of a systemic liquidity crunch, but, at the same time, these holdings reduce the bank's currency exposure. The bank reported a consolidated liquidity coverage ratio (LCR) of 170% as of June 2024, well above the regulatory requirement and mitigating to a some extent the market funding dependence concerns that we have.

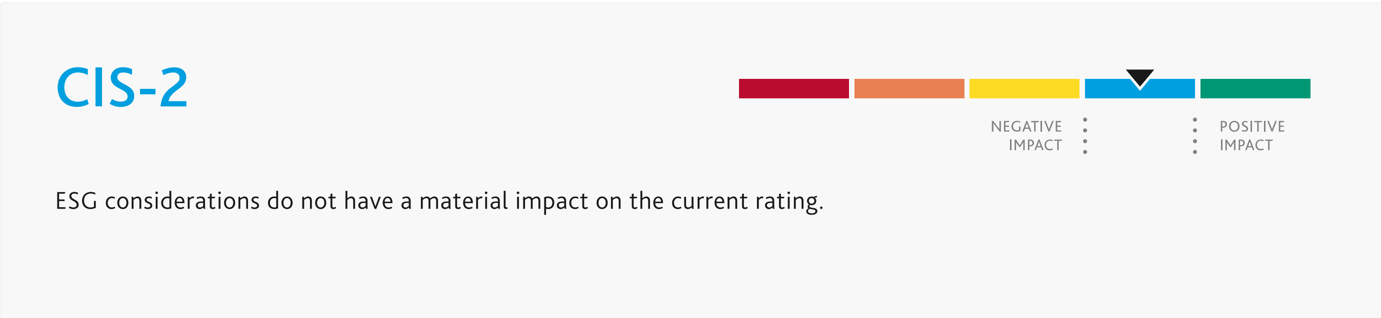
Source of facts and figures cited in this report

Unless noted otherwise, we have sourced data relating to systemwide trends and market shares from the central bank. Bank-specific figures originate from banks' reports and Moody's Banking Financial Metrics. All figures are based on our own chart of accounts and may be adjusted for analytical purposes. Please refer to the document Financial Statement Adjustments in the Analysis of Financial Institutions published on 8 April 2024.

ESG considerations

Sparebanken Sor's ESG credit impact score is CIS-2

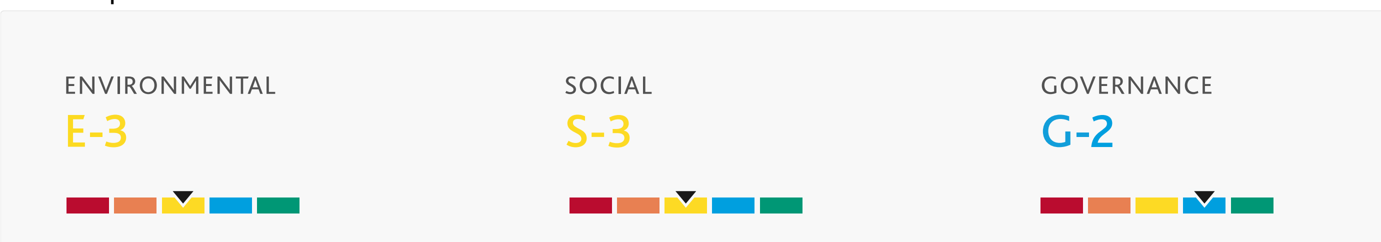
Exhibit 7
ESG credit impact score



Source: Moody's Ratings

Sparebanken Sor's **CIS-2** reflects that ESG considerations do not have a material impact on the current ratings.

Exhibit 8
ESG issuer profile scores



Source: Moody's Ratings

Environmental

Sparebanken Sor faces moderate environmental risks because of its portfolio exposure to carbon transition. These risks are primarily related to its corporate portfolio, through the commercial real estate sector. In line with its peers, the bank is facing mounting business risks and stakeholder pressure to meet broader carbon transition goals. In response, the bank is developing its climate risk and portfolio management capabilities.

Social

Sparebanken Sor faces moderate social risks related to customer relations and associated regulatory and litigation risks, requiring high compliance standards. The exposure to customer relation risks is lower than its international peers, given the bank's untarnished customer conduct track record supported by the social mandate of the Savings Bank's model. Sparebanken Sor is a digitally advanced bank in Norway, with a robust IT infrastructure and strong capabilities to mitigate cyber and personal data risks.

Governance

Sparebanken Sor faces not material governance risks, and its risk management, policies and procedures are in line with industry practices. Despite sectoral and geographical concentrations, due to its limited reach, the bank benefits from strong underwriting standards which mitigate some of these concerns. The bank has a track record of sound capital and liquidity management and earnings stability while losses have been low, even at times of market turbulence. Being a regional savings bank, 26% of the bank is owned by the community foundation, in the form of listed equity certificates. The bank's Supervisory Board comprises of representatives of EC holders, the foundation and employees. Related governance risks are however mitigated by Norway's developed institutional framework.

ESG Issuer Profile Scores and Credit Impact Scores for the rated entity/transaction are available on Moodys.com. In order to view the latest scores, please click here to go to the landing page for the entity/transaction on MDC and view the ESG Scores section.

Support and structural considerations

Loss Given Failure (LGF)

Norway implemented the EU's Bank Recovery and Resolution Directive (BRRD) on 1 January 2019, and BRRD2 was incorporated into Norwegian law on 1 June 2022, which results in lower subordination requirements for non-preferred senior volumes. For our resolution analysis, we apply our advanced Loss Given Failure (LGF) analysis, using our standard assumptions for a bank operating in an operational resolution regime (ORR) country.

Our Advanced LGF analysis includes a forward-looking approach on the bank's near-term bail-in-able debt issuance and indicates a very low loss given failure for junior depositors and senior unsecured creditors, resulting in a three-notch uplift of the relevant ratings from the bank's baa1 Adjusted BCA. These ratings incorporate our forward-looking view on expected future debt issuance.

Government support

Following the implementation of the BRRD law in Norway on 1 January 2019, we assume a low probability of government support for the bank's senior debt and deposits, resulting in no rating uplift.

Methodology and scorecard

About Moody's bank scorecard

Our Scorecard is designed to capture, express and explain in summary form our rating committee's judgement. When read in conjunction with our research, a fulsome presentation of our judgement is expressed. As a result, the output of our Scorecard may materially differ from that suggested by raw data alone (though it has been calibrated to avoid the frequent need for strong divergence). The Scorecard output and the individual scores are discussed in rating committees and may be adjusted up or down to reflect conditions specific to each rated entity.

Rating methodology and scorecard factors

Exhibit 9
Rating Factors

Macro Factors							
Weighted Macro Profile	**Very Strong -**	**100%**					
Factor		**Historic Ratio**	**Initial Score**	**Expected Trend**	**Assigned Score**	**Key driver #1**	**Key driver #2**
Solvency							
Asset Risk							
Problem Loans / Gross Loans		0.7%	aa1	↔	baa2	Geographical concentration	Sector concentration
Capital							
Tangible Common Equity / Risk Weighted Assets (Basel III - transitional phase-in)		17.7%	aa2	↔	aa2	Access to capital	
Profitability							
Net Income / Tangible Assets		1.0%	baa1	↔	baa2	Earnings quality	
Combined Solvency Score			aa3		a3		
Liquidity							
Funding Structure							
Market Funds / Tangible Banking Assets		27.7%	baa2	↔	baa3		
Liquid Resources							
Liquid Banking Assets / Tangible Banking Assets		16.2%	baa2	↔	baa2		
Combined Liquidity Score			baa2		baa3		
Financial Profile					baa1		
Qualitative Adjustments					Adjustment		
Business Diversification					0		
Opacity and Complexity					0		
Corporate Behavior					0		
Total Qualitative Adjustments					0		
Sovereign or Affiliate constraint					Aaa		
BCA Scorecard-indicated Outcome - Range					a3 - baa2		
Assigned BCA					baa1		
Affiliate Support notching					0		
Adjusted BCA					baa1		

Balance Sheet	**in-scope (NOK Million)**	**% in-scope**	**at-failure (NOK Million)**	**% at-failure**
Other liabilities	69 732	42.1%	77 186	46.6%
Deposits	73 083	44.1%	65 629	39.6%
Preferred deposits	54 081	32.7%	51 377	31.0%
Junior deposits	19 002	11.5%	14 251	8.6%
Senior unsecured bank debt	7 050	4.3%	7 050	4.3%
Junior senior unsecured bank debt	7 100	4.3%	7 100	4.3%
Dated subordinated bank debt	2 000	1.2%	2 000	1.2%
Preference shares (bank)	1 672	1.0%	1 672	1.0%
Equity	4 968	3.0%	4 968	3.0%
Total Tangible Banking Assets	165 605	100.0%	165 605	100.0%

Debt Class	De Jure waterfall		De Facto waterfall		Notching		LGF Notching Guidance vs. Adjusted BCA	Assigned LGF notching	Additional Notching	Preliminary Rating Assessment
	Instrument volume + subordination	Sub-ordination	Instrument volume + subordination	Sub-ordination	De Jure	De Facto				
Counterparty Risk Rating	22.4%	22.4%	22.4%	22.4%	3	3	3	3	0	a1
Counterparty Risk Assessment	22.4%	22.4%	22.4%	22.4%	3	3	3	3	0	a1 (cr)
Deposits	22.4%	9.5%	22.4%	13.8%	3	3	3	3	0	a1
Senior unsecured bank debt	22.4%	9.5%	13.8%	9.5%	3	2	3	-	-	-
Junior senior unsecured bank debt	9.5%	5.2%	9.5%	5.2%	0	0	0	0	0	baa1

Instrument Class	Loss Given Failure notching	Additional notching	Preliminary Rating Assessment	Government Support notching	Local Currency Rating	Foreign Currency Rating
Counterparty Risk Rating	3	0	a1	0	A1	A1
Counterparty Risk Assessment	3	0	a1 (cr)	0	A1(cr)	
Deposits	3	0	a1	0	A1	A1
Senior unsecured bank debt	-	-	-	0	(P)A1	(P)A1
Junior senior unsecured bank debt	0	0	baa1	0	Baa1	

[1] Where dashes are shown for a particular factor (or sub-factor), the score is based on non-public information.
Source: Moody's Ratings

Ratings

Exhibit 10

Category	Moody's Rating
SPAREBANKEN SOR	
Outlook	Positive
Counterparty Risk Rating	A1/P-1
Bank Deposits	A1/P-1
Baseline Credit Assessment	baa1
Adjusted Baseline Credit Assessment	baa1
Counterparty Risk Assessment	A1(cr)/P-1(cr)
Issuer Rating	A1
Senior Unsecured MTN	(P)A1
Junior Senior Unsecured -Dom Curr	Baa1
SPAREBANKEN SOR BOLIGKREDITT AS	
Outlook	Positive
Counterparty Risk Rating	A1/P-1
Counterparty Risk Assessment	A1(cr)/P-1(cr)
Issuer Rating	A1

Source: Moody's Ratings

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