MOODY'S

Rating_Action: Moody's affirms Sydbank's A1 deposit ratings; outlook remains stable

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Stockholm, January 17, 2023 -- Moody's Investors Service ("Moody's") has today affirmed Sydbank A/S's (Sydbank) A1/P-1 long-term and short-term foreign and local currency deposit ratings, (P)A1 senior unsecured Medium Term Note Programme (MTN) rating, A3 junior senior unsecured debt ratings, (P)A3 junior senior unsecured MTN rating, Baa2 foreign currency subordinate debt rating, (P)Baa2 subordinate foreign currency MTN rating, Ba1(hyb) preferred stock non-cumulative ratings, (P)P-1 foreign currency other short term rating, baa1 Baseline Credit Assessment (BCA) and Adjusted BCA, A1/P-1 long-term and short-term Counterparty Risk Ratings (CRRs), and the A1(cr)/P-1(cr) long-term and short-term Counterparty Risk Assessments (CR Assessments). The outlooks on the long-term deposit ratings remain stable.

The key drivers for the affirmation of the long-term deposit ratings of A1 is the affirmation of the BCA of baa1, and three notches of uplift according to Moody's Advanced Loss Given Failure (LGF) analysis.

The baa1 BCA balances Sydbank's growing Danish corporate banking franchise, its declining levels of problem loans to gross loans, strong capitalization, improving profitability, and a strong liquidity profile, against mounting risks in the macroeconomic environment. Moody's assesses that high inflation and subdued economic growth will lead to a deterioration in asset prices and borrowers' repayment capacity, thus leading to moderate deterioration in asset quality and potential loan loss provisions, offsetting some of the gains in net interest margins.

The stable outlook on the long-term deposit debt ratings reflects Moody's view that Sydbank has sufficient buffers in term of very strong capitalisation and improving net interest margins to manage a deterioration in borrowers' repayment capacity during the next 12 to 18 months.

RATINGS RATIONALE

BASELINE CREDIT ASSESSMENT

Sydbank's BCA of baa1 balances the bank's strong solvency and liquidity profile, against the downside risks in the operating environment which constrains borrowers' repayment capacity, leading to a deterioration in asset risk metrics.

Sydbank's asset risk has improved in recent years as the bank has decreased its problematic exposures toward clients within agriculture, with problem loans to gross loans gradually declining to 1.73% at the end of September 2022 from 3.56% at the end of 2020. However, Moody's expects a moderate deterioration in the bank's loan portfolio during 2023 as borrowers' ability to repay is constrained due to high inflation and subdued economic activity. Moody's expects banks' SME lending to be relatively more affected by repayment constraints than mortgages, which Sydbank generally transfers to partnering mortgage credit institutions.

Capitalisation will continue to be robust, with tangible common equity to risk weighted assets of 20.73% at the end of September 2022 due to strong internal capital generation. Moody's expects capitalization to remain strong, remaining around 2 percentage points above the bank's CET1 target of 14.5%. Although the bank will continue distributing 30% to 50% in dividends and use share buyback programs, Moody's expects internal capital generation to support organic growth.

Profitability, with net income to tangible assets of 0.94% for the first nine months of 2022, will be supported by the positive interest rate environment, partly offset by slower business growth, resulting in net income to tangible assets of approximately 1%. Due to volatility in the operating environment, results can be volatile in the coming year.

DEPOSIT DEBT RATINGS

Sydbank's A1 deposit debt ratings incorporate the baa1 adjusted BCA and three notches of uplift as indicated by LGF, due to the large volumes of loss absorbing liabilities protecting depositors and creditors in case of failure indicating an extremely low loss severity.

OUTLOOK

The stable outlook on the long-term deposit debt ratings reflects the agency's view that the bank's strong buffers in of excess capital and strong recurring profitability will be sufficient to absorb a moderate increase in asset risk over the next 12 to 18 months.

FACTORS THAT COULD LEAD TO AN UPGRADE OR DOWNGRADE OF THE RATINGS

Sydbank's ratings could be upgraded following a reduction in credit concentrations and if the bank demonstrates 1) a sustained improvement in the bank's profitability without an increase in its risk profile; or 2) strong asset quality through an important economic downturn; and 3) maintained strong capitalization and low capital leverage.

Sydbank's long-term deposit ratings, CR Assessment and CRRs, already have the maximum uplift as per our loss given failure framework and would therefore not receive further uplift from increased subordination or issuance volumes. The junior senior ratings could be upgraded if higher volumes of senior non-preferred debt and subordinated liabilities are maintained as a percentage of tangible banking assets.

Factors that could lead to a downgrade of Sydbank's ratings include 1) a significant deterioration in asset quality beyond the bank's historical performance; 2) an increase in concentrations and exposures to more volatile asset classes; or 3) a persistent weakening in the bank's recurring earnings power and operating efficiency.

Downward pressure on the bank's long-term deposit ratings would also arise if there is a shift in the bank's funding mix, such as lower loss-absorbing instrument volumes or a significant reduction in junior deposit amounts, which would result in lower rating uplifts than currently assumed.

PRINCIPAL METHODOLOGY

The principal methodology used in these ratings was Banks Methodology published in July 2021 and available at https://ratings.moodys.com/api/rmc-documents/71997. Alternatively, please see the Rating Methodologies page on https://ratings.moodys.com for a copy of this methodology.

REGULATORY DISCLOSURES

For further specification of Moody's key rating assumptions and sensitivity analysis, see the sections Methodology Assumptions and Sensitivity to Assumptions in the disclosure form. Moody's Rating Symbols and Definitions can be found on https://ratings.moodys.com/rating-definitions.

For ratings issued on a program, series, category/class of debt or security this announcement provides certain regulatory disclosures in relation to each rating of a subsequently issued bond or note of the same series, category/class of debt, security 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 issuer/deal page for the respective issuer on https://ratings.moodys.com.

For any affected securities or rated entities receiving direct credit support from the primary entity(ies) of this credit rating action, and whose ratings may change as a result of this credit rating action, the associated regulatory disclosures will be those of the guarantor entity. Exceptions to this approach exist for the following disclosures, if applicable to jurisdiction: Ancillary Services, Disclosure to rated entity, Disclosure from rated entity.

The ratings have been disclosed to the rated entity or its designated agent(s) and issued with no amendment resulting from that disclosure.

These ratings are solicited. Please refer to Moody's Policy for Designating and Assigning Unsolicited Credit Ratings available on its website https://ratings.moodys.com.

Regulatory disclosures contained in this press release apply to the credit rating and, if applicable, the related rating outlook or rating review.

Moody's general principles for assessing environmental, social and governance (ESG) risks in our credit analysis can be found at https://ratings.moodys.com/documents/PBC_1288235.

The Global Scale Credit Rating on this Credit Rating Announcement was issued by one of Moody's affiliates outside the UK and is endorsed by Moody's Investors Service Limited, One Canada Square, Canary Wharf, London E14 5FA under the law applicable to credit rating agencies in the UK. Further information on the UK endorsement status and on the Moody's office that issued the credit rating is available on https://ratings.moodys.com.

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