

ISSUER COMMENT

20 March 2020



RATINGS

SpareBank 1 Nord-Norge

Domicile	Norway
Long Term CRR	Aa3
Type	LT Counterparty Risk Rating - Fgn Curr
Outlook	Not Assigned
Long Term Debt	Aa3
Type	Senior Unsecured - Fgn Curr
Outlook	Stable
Long Term Deposit	Aa3
Type	LT Bank Deposits - Fgn Curr
Outlook	Stable

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.

Helgeland Sparebank

Domicile	Norway
Long Term CRR	A2
Type	LT Counterparty Risk Rating - Fgn Curr
Outlook	Not Assigned
Long Term Debt	Not Assigned
Long Term Deposit	A3
Type	LT Bank Deposits - Fgn Curr
Outlook	Stable

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.

Sparebank 1 Nord-Norge and Helgeland Sparebank

Strategic partnership between Norwegian savings banks is credit positive for both

On 18 March, [SpareBank 1 Nord-Norge](#) (SNN, Aa3/Aa3 stable, a3¹) and [Helgeland Sparebank](#) (A3 stable, baa2) [announced](#) a strategic partnership in Norway's Helgeland region. The transaction is credit positive for both banks because they will accrue long-term benefits through the collaboration, provided that execution risks are properly managed.

As part of the agreement, Helgeland Sparebank will acquire the majority of SNN's Helgeland region loan portfolio, which comprises mostly retail mortgages and totals NOK10.2 billion. In addition, Helgeland Sparebank will join the SpareBank 1 Alliance. SNN will become the second-largest shareholder in Helgeland Sparebank with approximately 20% stake.

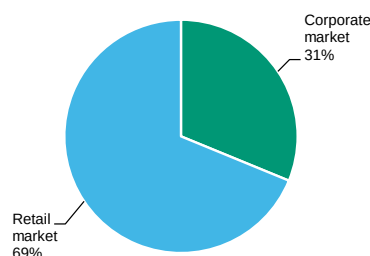
Helgeland Sparebank will finance the transaction with a public offering of up to NOK800 million, which will maintain its current capitalisation. The offering is subscribed and underwritten by SNN and the foundation Sparebankstiftelsen Helgeland, which owns 35% of Helgeland Sparebank's equity certificates. The parties expect to complete the transaction during the first half of 2021, pending regulatory approvals.

Acquiring SNN's portfolio, which excludes some large corporate exposures in the Helgeland region, will improve the granularity of Helgeland Sparebank's loan portfolio. On a pro forma basis, retail lending would rise to 74% of Helgeland Sparebank's total loan book, in line with the average of other Norwegian local savings banks, from 69% at year-end 2019 (see Exhibits 1 through 3). Helgeland Sparebank's performance was volatile during 2018 mainly because of impairments in a number of large corporate exposures.

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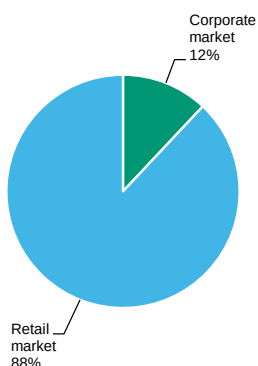
Exhibit 1

Helgeland Sparebank's loan portfolio at year-end 2019

The net amount of the loan portfolio was NOK27.3 billion at year-end 2019.

Source: Company reports

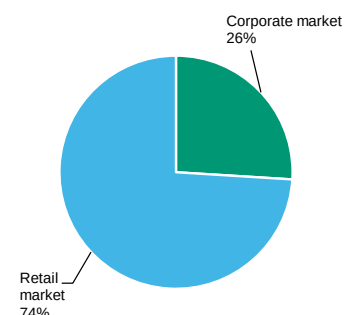
Exhibit 2

Composition of the Sparebank 1 Nord-Norge loan portfolio that Helgeland Sparebank will acquire

The net amount of the loan portfolio was NOK10.2 billion, including 6,800 borrowers at year-end 2019.

Source: Company investor presentation

Exhibit 3

Helgeland Sparebank's loan portfolio pro forma for the SNN portfolio acquisition

Pro-forma net amount of the loan portfolio is NOK34.2 billion at year-end 2019.

Sources: Company reports and Moody's Investors Service

By becoming a shareholder in, and user of, the SpareBank1 Alliance's covered bond company [Sparebank 1 Boligkredit AS](#) (A2 stable), Helgeland Sparebank will improve its market access to reach a broader investor base and potentially reduce funding costs. Helgeland Sparebank substantially relies on market funding, primarily in the form of senior debt and covered bonds, and issues covered bonds through its own wholly owned covered bond company. At year-end 2019, covered bonds accounted for slightly more than 60% of its total market funds. However, Helgeland Sparebank currently does not have the capacity to make large benchmark issuances, ultimately restricting its potential investor base and increasing its refinancing risk.

SNN is a much larger bank, with total assets of NOK111 billion, compared with NOK34 billion for Helgeland Sparebank at year-end 2019. SNN's financial performance has been robust and will support Helgeland Sparebank in strengthening its risk management, accounting and compliance policies and procedures. Being part of the SpareBank1 Alliance, will also give Helgeland Sparebank access to new products and services and IT systems, enhancing its business potential and reducing costs.

However, the transaction is complex with substantial execution risks, particularly for Helgeland Sparebank, which will undergo a significant transformation. Challenges include onboarding new customers as part of the portfolio acquisition, transitioning to new service providers, and terminating agreements with existing partners.

If the transaction is managed successfully, the partnership has the potential to generate additional earnings for Helgeland Sparebank of NOK80-NOK120 million during 2022-24, although the bank estimates onetime integration costs at NOK90-NOK110 million. Helgeland Sparebank said it will consider raising its annual return-on-equity target to 11% from 10% in 2023.

For SNN, this transaction offers further potential for consolidation, strengthening the SparkeBank 1 Alliance franchise in northern Norway. SNN estimates that the minority stake in Helgeland Sparebank will yield higher returns to the bank than the loan book it is selling from a region characterized by strong competition and tight lending margins.

The transaction will likely strengthen SNN's annual earnings by NOK25-NOK35 million during 2022-24 from the approximately 20% ownership in Helgeland Sparebank, provided Helgeland Sparebank delivers on its performance targets. This will improve SNN's return on equity by 30-40 basis points, which was already a very high 15.9% in 2019, including some one-off gains.

The deal will also free up around NOK300 million of capital for SNN, which adds up to 20-30 basis points to the bank's Common Equity Tier 1 ratio, which was 16.7% in December 2019. In addition, it will likely reduce joint costs and sale of services directly or

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through Helgeland Sparebank's subsidiaries, while the strategic partnership creates a more efficient platform for banking operations in the Helgeland region.

However, the spread of the coronavirus is leading to increased uncertainty regarding both banks' asset quality and future profitability because it is likely to slow first-half economic activity, despite the [Government of Norway's](#) (Aaa stable) proposed measures to soften the economic effects.

Moody's related publications

- » [Sparebank 1 Nord-Norge: Update to credit analysis following rating upgrade](#), 9 March 2020
- » [Helgeland Sparebank: Update following rating affirmation](#), 6 March 2020
- » [Banks - Norway: Norway's banks and covered bonds will benefit from government measures to soften coronavirus' effects](#), 19 March 2020

To access any of these reports, click on the entry above. Note that these references are current as of the date of publication of this report and that more recent reports may be available. All research may not be available to all clients.

Endnotes

- ¹ The bank ratings shown in this report are the bank's deposit rating, senior unsecured debt rating (where available) and Baseline Credit Assessment.

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