

Research Update:

Swedish SBAB Bank AB Upgraded To 'A+/A-1' On A Stronger Bail-Inable Debt Buffer; Outlook Stable

February 17, 2023

Overview

- On Jan. 23, 2023, SBAB Bank AB (SBAB) issued Swedish krona (SEK) 3 billion of senior nonpreferred notes, further strengthening its additional loss-absorbing capacity (ALAC).
- Given the likely supportive resolution strategy for SBAB and its expanded subordinated recapitalization capacity, we see a further reduced risk of the bank defaulting on obligations to senior preferred creditors in the unlikely event that the bank fails.
- We therefore raised our long-term issuer credit rating on SBAB to 'A+' from 'A', and affirmed the 'A-1' short-term rating. We also raised our long-term resolution counterparty ratings to 'AA-/A-1+' from 'A+/A-1'.
- The stable outlook reflects our expectation that the bank will maintain its sound financial profile amid a weakened economic backdrop and sustain its ALAC buffer.

PRIMARY CREDIT ANALYST

Niklas Dahlstrom
Stockholm
+46 84405358
niklas.dahlstrom
@spglobal.com

SECONDARY CONTACT

Olivia K Grant
Stockholm
+ 46 84 40 5904
olivia.grant
@spglobal.com

Rating Action

On Feb. 17, 2023, S&P Global Ratings raised its long-term issuer credit rating on SBAB Bank AB to 'A+' from 'A'. We affirmed the short-term issuer credit rating at 'A-1'. The outlook is stable.

We also raised our resolution counterparty ratings to 'AA-/A-1+' from 'A+/A-1'.

Rationale

SBAB's substantial buffer of bail-inable debt instruments provides extra protection to senior preferred creditors. With its recent SEK3 billion senior nonpreferred issue, SBAB has further bolstered its ALAC buffer, which in the unlikely event of the bank's failure would facilitate both the loss-absorption and recapitalization of the bank. Notably, we consider it likely that the resolution authority would see SBAB as a systemic bank and employ a supportive resolution strategy, such as an open bank bail-in or potentially a sale of business, that would ensure that it continues to service its senior preferred obligations on time and in full. SBAB's stock of subordinated debt consists of tier 2 instruments amounting to SEK2 billion and senior nonpreferred notes of

approximately SEK15 billion, which we expect to equate to 8.5% of our forecast risk-weighted assets (RWA) at year-end 2023. We expect that the bank will then sustainably exceed our 8% threshold required for two notches uplift for ALAC support.

We project SBAB will maintain sound earnings generation, but that margin pressures will intensify. We forecast annual profits will remain stable at SEK1.9-SEK2.1 billion in 2023-2024--compared with SEK2.1 billion (€188 million) as of year-end 2022--with a return on average common equity of 10%-12%. This reflects our projection of muted loan growth and increased competition for deposits and mortgage market share in 2023-2024, in addition to our expectation that SBAB will maintain its lean operating model, with a cost-to-income ratio of about 35% (compared with 32.7% in 2022). Assuming also only a moderate pick-up in credit costs and an unchanged dividend policy of about 40% of net profits, this would support a risk-adjusted capital (RAC) ratio of 12%-13% (estimated 12.3% at end-2022) over the next two years.

We expect limited asset quality deterioration, despite a challenging macroeconomic backdrop.

As financial conditions for borrowers tighten, we project SBAB's nonperforming assets will rise moderately but remain contained in the range of 10-15 basis points (bps) in 2023-2024--compared with 7bps in 2022. Supporting our view are SBAB's sound lending standards and focus on low-risk residential mortgages (68% of total loans as of end-2022); our economists' expectation that unemployment will rise only slightly; and the supportive social safety net in Sweden for the short-term unemployed. That said, the bank's high concentration in Sweden's urban areas where the fall in residential real estate prices has been particularly steep poses downside risk to our base case. As of year-end 2022, the bank posted an average loan-to-value ratio of 71% for new lending (59% for the mortgage book stock as a whole) and an average debt-to-income ratio of 3.7x.

Covered bond issuance and adequate liquidity buffers provide a cushion to potential volatility in funding markets. We expect SBAB's high reliance on wholesale funding (69% of the funding base as of Dec. 31, 2022) will gradually lower as the bank continues to build its deposit base, which grew by 26% over 2022. That said, we expect competition for deposits within the Swedish banking market to further stiffen and that the cost would weigh more heavily on SBAB than larger peers that have broader deposit franchises and higher yielding assets. We therefore consider the bank's established covered bond franchise and adequate liquidity buffers to provide a degree of flexibility if funding conditions were to tighten. As of Dec. 31, 2022, our one-year liquidity metric (broad liquid assets to short-term wholesale funding) stood at 1.11x and the regulatory liquidity coverage ratio was reported at 219% on a consolidated level.

Outlook

The stable outlook on SBAB reflects our expectation that over the next two years the bank will maintain ALAC sustainably above our adjusted threshold of 8% for two notches of ALAC support, while maintaining robust capitalization. We also expect that the bank will remain focused on the Swedish retail mortgage market, but that its loan losses will remain low despite deteriorating macroeconomic conditions.

Downside scenario

We could lower our ratings if operating conditions deteriorate and this implies that asset quality

would be much weaker than we currently expect, or if the RAC ratio were to fall below 10%. Adverse developments such as these could notably weaken the bank's creditworthiness relative to similarly rated peers. We could also take a negative rating action if we see a lower likelihood that SBAB will sustain an ALAC buffer above our adjusted 8% threshold.

Upside scenario

An upgrade appears remote at this point.

Ratings Score Snapshot

	To	From
Issuer Credit Rating	A+/Stable/A-1	A/Stable/A-1
Stand-alone credit profile	a-	a-
Anchor	a-	a-
Business position	Moderate (-1)	Moderate (-1)
Capital and earnings	Strong (+1)	Strong (+1)
Risk position	Adequate (0)	Adequate (0)
Funding and	Adequate	Adequate
Liquidity	Adequate (0)	Adequate (0)
Comparable ratings analysis	0	0
Support	+2	+1
ALAC support	+2	+1
GRE support	0	0
Group support	0	0
Sovereign support	0	0
Additional factors	0	0

SACP—Stand-alone credit profile. ALAC—Additional loss-absorption capacity. GRE--Government-related entity.

ESG credit indicators: E-2, S-2, G-2

Related Criteria

- General Criteria: Hybrid Capital: Methodology And Assumptions, March 2, 2022
- Criteria | Financial Institutions | General: Financial Institutions Rating Methodology, Dec. 9, 2021
- Criteria | Financial Institutions | Banks: Banking Industry Country Risk Assessment Methodology And Assumptions, Dec. 9, 2021
- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021

- General Criteria: Group Rating Methodology, July 1, 2019
- General Criteria: Methodology For National And Regional Scale Credit Ratings, June 25, 2018
- 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
- General Criteria: Rating Government-Related Entities: Methodology And Assumptions, March 25, 2015
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Related Research

- SBAB Bank AB, Dec. 15, 2022
- Swedish Banks Can Weather A Housing Market Correction; BICRA Group Remains '2', Nov. 10, 2022
- Sweden 'AAA/A-1+' Ratings Affirmed; Outlook Stable, Oct. 28, 2022
- Dutch De Volksbank Upgraded To 'A' On Improved Clarity Around Sale Of Business Resolution Strategy; Outlook Stable, Oct. 26, 2022
- Belgian Argenta Spaarbank Upgraded To 'A' On Improved Clarity Around Sale Of Business Resolution Strategy; Outlook Stable, Oct. 25, 2022
- Credit Conditions Europe Q4 2022: Hunkering Down For Winter, Sept. 27 2022
- Nordic Banks: Robust Capital Provides Cushion Against Tougher Times, Sept. 6, 2022
- Bulletin: Single Resolution Board Says That Banks Must Go The Distance To Ensure Full Resolvability, July 13, 2022

Ratings List

Upgraded

	To	From
SBAB Bank AB (publ)		
Resolution Counterparty Rating	AA-/--/A-1+	A+/--/A-1

SBAB Bank AB (publ)

Senior Unsecured	A+	A
------------------	----	---

Upgraded; Ratings Affirmed

	To	From
SBAB Bank AB (publ)		
Issuer Credit Rating	A+/Stable/A-1	A/Stable/A-1

Ratings Affirmed

SBAB Bank AB (publ)

Issuer Credit Rating		
----------------------	--	--

Nordic Regional Scale --/--/K-1

SBAB Bank AB (publ)

Senior Subordinated BBB+

Subordinated BBB

Junior Subordinated BB

Commercial Paper A-1

Commercial Paper K-1

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. A description of each of S&P Global Ratings' rating categories is contained in "S&P Global Ratings Definitions" at https://www.standardandpoors.com/en_US/web/guest/article/-/view/sourceId/504352 Complete ratings information is available to subscribers of RatingsDirect at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column. Alternatively, call one of the following S&P Global Ratings numbers: Client Support Europe (44) 20-7176-7176; London Press Office (44) 20-7176-3605; Paris (33) 1-4420-6708; Frankfurt (49) 69-33-999-225; or Stockholm (46) 8-440-5914

Copyright © 2023 by Standard & Poor's Financial Services LLC. All rights reserved.

No content (including ratings, credit-related analyses and data, valuations, model, software or other application or output therefrom) or any part thereof (Content) may be modified, reverse engineered, reproduced or distributed in any form by any means, or stored in a database or retrieval system, without the prior written permission of Standard & Poor's Financial Services LLC or its affiliates (collectively, S&P). The Content shall not be used for any unlawful or unauthorized purposes. S&P and any third-party providers, as well as their directors, officers, shareholders, employees or agents (collectively S&P Parties) do not guarantee the accuracy, completeness, timeliness or availability of the Content. S&P Parties are not responsible for any errors or omissions (negligent or otherwise), regardless of the cause, for the results obtained from the use of the Content, or for the security or maintenance of any data input by the user. The Content is provided on an "as is" basis. S&P PARTIES DISCLAIM ANY AND ALL EXPRESS OR IMPLIED WARRANTIES, INCLUDING, BUT NOT LIMITED TO, ANY WARRANTIES OF MERCHANTABILITY OR FITNESS FOR A PARTICULAR PURPOSE OR USE, FREEDOM FROM BUGS, SOFTWARE ERRORS OR DEFECTS, THAT THE CONTENT'S FUNCTIONING WILL BE UNINTERRUPTED OR THAT THE CONTENT WILL OPERATE WITH ANY SOFTWARE OR HARDWARE CONFIGURATION. In no event shall S&P Parties be liable to any party for any direct, indirect, incidental, exemplary, compensatory, punitive, special or consequential damages, costs, expenses, legal fees, or losses (including, without limitation, lost income or lost profits and opportunity costs or losses caused by negligence) in connection with any use of the Content even if advised of the possibility of such damages.

Credit-related and other analyses, including ratings, and statements in the Content are statements of opinion as of the date they are expressed and not statements of fact. S&P's opinions, analyses and rating acknowledgment decisions (described below) are not recommendations to purchase, hold, or sell any securities or to make any investment decisions, and do not address the suitability of any security. S&P assumes no obligation to update the Content following publication in any form or format. The Content should not be relied on and is not a substitute for the skill, judgment and experience of the user, its management, employees, advisors and/or clients when making investment and other business decisions. S&P does not act as a fiduciary or an investment advisor except where registered as such. While S&P has obtained information from sources it believes to be reliable, S&P does not perform an audit and undertakes no duty of due diligence or independent verification of any information it receives. Rating-related publications may be published for a variety of reasons that are not necessarily dependent on action by rating committees, including, but not limited to, the publication of a periodic update on a credit rating and related analyses.

To the extent that regulatory authorities allow a rating agency to acknowledge in one jurisdiction a rating issued in another jurisdiction for certain regulatory purposes, S&P reserves the right to assign, withdraw or suspend such acknowledgment at any time and in its sole discretion. S&P Parties disclaim any duty whatsoever arising out of the assignment, withdrawal or suspension of an acknowledgment as well as any liability for any damage alleged to have been suffered on account thereof.

S&P keeps certain activities of its business units separate from each other in order to preserve the independence and objectivity of their respective activities. As a result, certain business units of S&P may have information that is not available to other S&P business units. S&P has established policies and procedures to maintain the confidentiality of certain non-public information received in connection with each analytical process.

S&P may receive compensation for its ratings and certain analyses, normally from issuers or underwriters of securities or from obligors. S&P reserves the right to disseminate its opinions and analyses. S&P's public ratings and analyses are made available on its Web sites, www.standardandpoors.com (free of charge), and www.ratingsdirect.com and www.globalcreditportal.com (subscription), and may be distributed through other means, including via S&P publications and third-party redistributors. Additional information about our ratings fees is available at www.standardandpoors.com/usratingsfees.

STANDARD & POOR'S, S&P and RATINGSDIRECT are registered trademarks of Standard & Poor's Financial Services LLC.