

Research Update:

Jyske Bank A/S And Jyske Realkredit A/S Ratings Affirmed On Acquisition Of Svenska Handelsbanken Unit; Outlook Stable

June 21, 2022

Overview

- On June 20, 2022, Jyske Bank A/S announced that it has reached a final agreement to acquire Svenska Handelsbanken's activities in Denmark.
- We believe the acquisition cements Jyske Bank's core product lines and footprint in Denmark, with the consolidated entity reinforcing the group's solid domestic franchise in retail and commercial banking with sufficient financial flexibility to absorb the financial effects.
- We see the execution risks as being somewhat mitigated by Jyske Bank's favorable track record of achieving synergies and executing its long-term strategy of profitable growth in the Danish market.
- The highly collateralized retail and small and midsize enterprise portfolio will also support the bank's sound asset quality metrics.
- As a result, we affirmed our 'A/A-1' ratings on Jyske Bank A/S and its core subsidiary Jyske Realkredit A/S.
- The stable outlooks for both entities reflect our expectation that the group will maintain its strong risk adjusted capital ratio and good asset quality, which will require a conservative approach to capital distribution over the medium term.

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Rating Action

On June 21, 2022, S&P Global Ratings affirmed its 'A/A-1' long- and short-term issuer credit ratings on Jyske Bank A/S and its core subsidiary Jyske Realkredit A/S. The outlooks on both entities are stable. We also affirmed our 'A+/A-1' long- and short-term resolution counterparty ratings (RCR) on Jyske Bank A/S.

Rationale

The affirmation reflects the group's overall stable financial profile and its so far successful strategic vision to profitably expand and diversify its operations through acquisitions in the Danish market. Following the announced acquisition of Svenska Handelsbanken's Danish activities with total lending of Danish krone (DKK) 66 billion, we expect the bank to swiftly integrate the acquired customer base and focus on strengthening its franchise and recurring core profitability. Jyske Bank will continue to develop its sound domestic franchise as the fourth-largest domestic player by market share, in our view. Although its revenue streams are diversified, combining retail and corporate lending with fee and commission income, they remain geographically concentrated in Denmark.

Over the next two years, we project the risk-adjusted capital (RAC) ratio at about 10.5%-11.0% compared with 12.3% in 2021. This incorporates lending growth of about 14% in 2022 due to the portfolio acquisition, and a slow down to 1% per year during 2023-2024. We also assume low provisioning levels and moderate growth in risk-weighted assets (RWAs) due to the high share of small and midsize enterprise lending and mortgage loans in the acquired business. We expect the acquisition to contribute to stable earnings for Jyske Bank. In addition, the bank is planning to support its capital position by issuing DKK1.5 billion of additional tier 1 (AT1) instruments. Following the merger, we anticipate the bank will continue its current capital management policy and achieve its target common equity Tier 1 (CET1) ratio of 15%-17% over the medium term. This will require a conservative approach to capital distribution, sustained fee income, and improved operating efficiency.

Although execution risks inherent to the acquisition could pose concerns, we believe this is somewhat offset by good asset quality and the track record of inorganic growth. Jyske Bank's favorable track record of successful acquisitions supports our view that execution will be manageable. We also project asset quality will remain stable. Jyske Bank's gross nonperforming loans (NPLs) stood at 1.8% of total loans at year-end 2021 and 2% on March 31, 2022, and we project NPLs will be broadly stable over the next 24 months after the merger. Cost of risk decreased in 2021 and remained at the same level in first-quarter 2022 (negative 5 basis points [bps]) and we expect it to moderate about 2 bps in the coming years. On a stand-alone basis, Jyske Bank's asset quality is supported by the highly collateralized mortgage portfolio (75% of the loan book at Jyske Bank) with a low average loan to value (LTV) of 46% at year-end 2021, down from 60% at year-end 2017. In our view, Svenska Handelsbanken's Danish activities comprise a healthy portfolio that match the overall asset quality of the acquirer's loan book.

We consider Jyske Bank's funding average and liquidity adequate and expect these factors to remain in line with peers over the next two years. We believe that the funding gap will be smoothly financed by Danish covered bonds, as well as the issuance of DKK2.5 billion in AT1 and Tier 2 instruments. As a result, we continue to believe that the group's funding profile will consolidate bank and mortgage financing and will compare well to that of domestic peers over the next two years. The group's stable funding ratio stood at 93.5% on Dec. 31, 2021, and we expect it to remain stable at roughly that level over the medium term. We view Jyske Bank's liquidity as adequate, with our one-year liquidity ratio (broad liquid assets to short-term wholesale funding) at 0.89x on Dec. 31, 2021. The bank's regulatory liquidity coverage ratio (LCR) was 416% at year-end 2021 versus 339% at year-end 2020. Jyske Bank has an internal guideline setting the minimum LCR at 150% under normal market conditions, compared with a minimum regulatory requirement

of 100%.

The buffer of bail-in-able debt should continue to support the long-term issuer credit rating.

At year-end 2021 the additional loss-absorbing capacity (ALAC) buffer equaled 5.8%. We expect Jyske Bank will continue building up its ALAC reserves and that they will remain above 3% of S&P Global Ratings' RWA, adding further protection for senior creditors.

Outlook

The stable outlook reflects our expectation that Jyske Bank will maintain its RAC ratio amid the ongoing acquisition. We anticipate Jyske Bank's RAC ratio and ALAC buffer will remain sustainably above 10% and 3% of S&P Global Ratings' RWAs respectively over the next two years, supported by the issuance of new AT1 capital.

We also expect that credit loss provisions will remain contained, and Jyske Bank will continue to report sound asset quality metrics in its expanded portfolio broadly in line with its domestic peers. Furthermore, we anticipate the bank will be able to finance the funding gap stemming from the transaction mainly by issuing covered bonds and AT1 capital, with markets remaining accessible.

Downside scenario

We could take a negative rating action if substantial execution risks emerge over the medium term, contrary to what we currently expect in our base-case scenario. This could materialize if higher costs and lower earnings retention result in a significant decrease in the bank's RAC to below 10%.

We continue to see margin development as a negative trigger. Therefore, we could also lower the rating if long-term trends in lending growth and margins highlight a weaker business franchise, or if the bank's profitability materially underperforms that of peers in the coming 12-24 months. Similarly, we could lower the rating if ALAC materially declines, contrary to our current expectations.

Upside scenario

Although we see an upgrade as unlikely at this stage, we could take a positive rating action if the ALAC buffer increases sustainably above 6%, with improved creditworthiness a prerequisite for a higher rating.

Ratings Score Snapshot

Jyske Bank A/S--Rating Component Scores

Issuer Credit Rating	A/Stable/A-1
SACP	a-
Anchor	bbb+
Economic risk	2
Industry risk	4
Business position	Adequate

Jyske Bank A/S--Rating Component Scores (cont.)

Issuer Credit Rating	A/Stable/A-1
Capital and earnings	Strong
Risk position	Adequate
Funding	Adequate
Liquidity	Adequate
Comparable ratings analysis	0
Support	+1
ALAC support	+1
GRE support	0
Group support	0
Sovereign support	0
Additional factors	0

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

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

Related Criteria

- 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: Hybrid Capital: Methodology And Assumptions, July 1, 2019
- 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: Principles Of Credit Ratings, Feb. 16, 2011

Related Research

- Nordic Banks' Solid Financials Mitigate Increased Geopolitical Uncertainties, April 12, 2022
- Four Danish Bank Ratings Affirmed Under Revised FI Criteria, Feb. 4, 2022
- Jyske Bank A/S, Oct. 25, 2021

Ratings List

Ratings Affirmed

Jyske Bank A/S

Issuer Credit Rating	A/Stable/A-1
Nordic Regional Scale	--/--/K-1
Certificate Of Deposit	A-1
Senior Unsecured	A
Senior Subordinated	BBB+
Subordinated	BBB
Junior Subordinated	BB+
Commercial Paper	A-1
Resolution Counterparty Rating	A+/-/-/A-1

Jyske Realkredit A/S

Issuer Credit Rating	A/Stable/A-1
Resolution Counterparty Rating	A+/-/-/A-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

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