Norwegian banking sector outlook to stable from negative

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Nordic Credit Rating (NCR) said today that it had revised its outlook on the Norwegian banking sector to stable from negative, while affirming its 'a-' assessment of the industry.

The outlook revision reflects our higher expectations for housing prices, employment, and the international cycle, which are reflected in higher scores for each subfactor of the overall assessment (see table below).

In our last review of the sector earlier this year, we revised our assessment score down by one notch to its current level (see NCR sees increased risk for Norwegian banks, published 3 Apr. 2020), mainly to reflect the initial impact of COVID-19 on the sector.

The stable outlook reflects our expectations of a flatter U-shaped recovery rather than the sharp V- or, in the worst case, W-shaped rebound that we anticipated previously. In our view, countries and markets are better prepared for any renewed upsurge in COVID-19, while localised outbreaks should prove easier to manage than national shutdowns. We note that the Norwegian government's finances are very strong as a result of higher tax income and lower support payments than we previously anticipated, allowing for continued stimulus and support for the most vulnerable sectors and individuals.

Norwegian banks outperformed our earlier expectations in the first half. An initial fall in income due to capital market tightening had been mostly corrected in the second quarter, while net interest margins in Norway have fallen due to lower policy rates. The country's banks have taken credit losses based on economic projections, increasing loss reserves against future actual losses. Financial Supervisory Authority restrictions have led many banks to cancel dividends for 2019, further improving their buffers. A sharp increase in customer deposits has supported liquidity. Property prices remain relatively stable and property lending remains the primary form of exposure within the wider Nordic banking market.

Given our downward revision of Norwegian banks' operating environment in April, NCR now believes that the remaining risk factors are more likely to affect individual institutions or banks than the wider banking sector and are better reflected in the outlooks and ratings on individual banks. They include external problems affecting supply chains, long-term shutdowns or low-production levels (under which furloughs could become layoffs), increasing corporate default, and the longer-term impact of changing market dynamics on commercial property prices.

A national banking sector assessment is a component of NCR's issuer ratings on financial institutions operating in that country. Depending on the nature of the rated entity's exposure and geographic profile, the score can affect up to 20% of the overall credit rating on an issuer.

Norway – scoring of national indicators (previous score in parentheses)

SUBFACTOR	SCORE	RATIONALE
Sovereign strength	aa	Major credit rating agency average: AAA, minimum: AAA.
Output growth	bb	We expect negative economic growth in 2020 due to COVID-19, but note that a rebound is already underway and expect positive growth in 2021.
Credit growth	bbb	Credit growth has been running at more than twice GDP growth, but is slowing due to revised regulations, rising interest rates, and high debt levels. So far, the effect of COVID-19 has been minimal.
Housing prices	a (bbb)	Low interest rates appear to have curbed the negative impact of COVID-19.
Unemployment	a (bbb)	Unemployment is sharply down from a peak in April.
Available stable funding	a	Available stable funding in the form of stable deposits and domestic covered bonds exceeds monetary financial institution private-sector loans in most foreseeable market conditions.
International cycle	bb (b)	Global growth prospects are weakening, though supported by significant monetary stimulus. We expect a rebound in 2021. In our assessment, asset prices are at or near their peak levels.

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