

ECB guidance dampens prospects for Nordic bank dividends

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On 15 Dec. 2020 the ECB amended its dividend recommendations for European banks. The new recommendations open up the possibility of limited dividend payments in 2021 and soften the current limits, which have restricted dividends or share buy backs since late March 2020 and remain in place until the end of the year. The new guidance will have a significant impact on Nordic banks' dividend distributions in 2021, even if earnings performance would support higher dividend payments.

The key components of the recommendation are that banks are to be conservative in their dividend payments and/or share buy backs, but that banks with solid capital positions could be allowed to pay dividends in 2021. The maximum dividend payment will be the lower of:

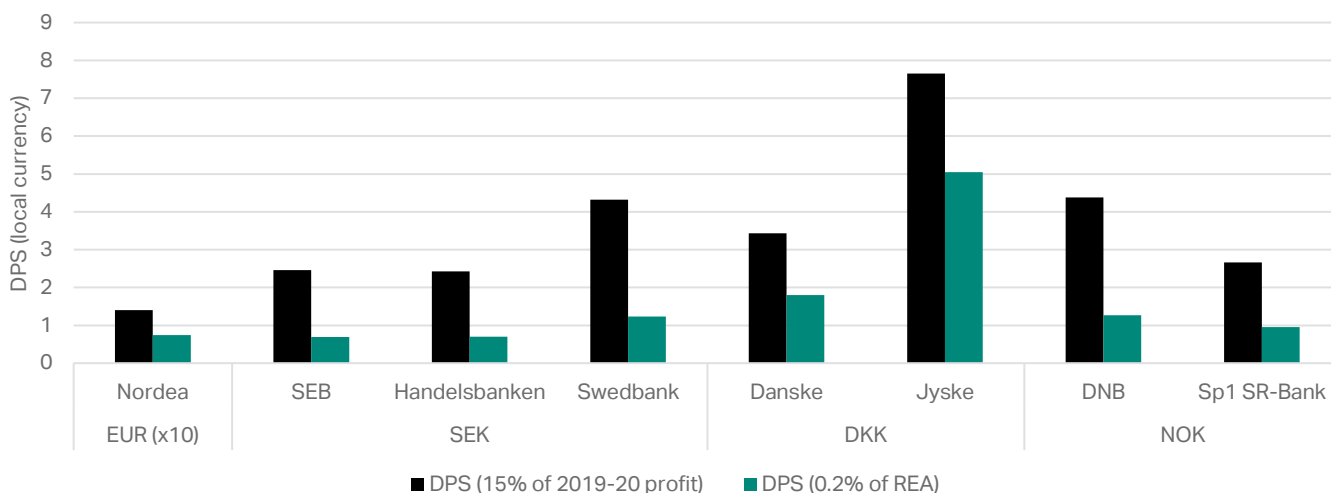
- 15% of total 2019 and 2020 net profits; or
- 20bps of the common equity Tier 1 (CET1) ratio.

The recommendations will initially remain in place through 30 Sep. 2021. However if the macroeconomic situation has improved, there will be an opportunity for banks to pay additional dividends, assuming that the current guidance is not extended and national regulators do not prefer to maintain a conservative approach given the dramatic reductions in countercyclical buffers and government support programmes in place across the Nordic region.

20 BPS OF RISK EXPOSURE AMOUNT IS THE KEY CONSTRAINT ON NORDIC BANKS

Nordic Credit Rating (NCR) expects Nordic regulators, which often share regulatory authority over Nordic banks with the ECB, to adopt these recommendations. NCR has analysed how these restrictions will impact large Nordic banks and discovered that the key constraint on the banks' ability to reward shareholders is the limit of 20bps in terms of the CET1 ratio, calculated as 20bps of the risk exposure amount (REA) as of 30 Sep. 2020. Given that we expect the banks in our sample to earn on average 150bps of REA during 2020, the 20bps constraint will lead to material improvements in their average CET1 ratio, improving overall credit strength.

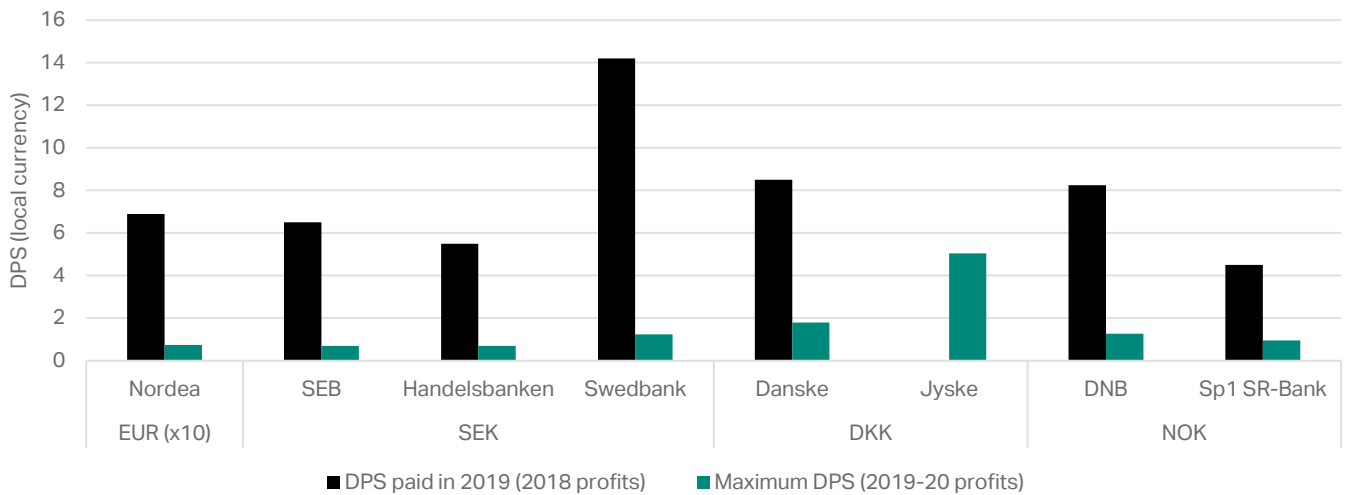
Figure 1. Dividend per share (DPS) constraints based on ECB recommendations



2021 DIVIDENDS WELL BELOW 2019 LEVELS

The new restrictions result in maximum allowable dividend payments for 2021 that are well below those paid in 2019 based on 2018 profits. For the banks in our sample, the maximum dividend for 2021 will be 10-20% of 2019 payments and would reflect about 10-20% of 2020 net profits (using consensus estimates for the fourth quarter of 2020). These levels can be compared with payments in 2019 which were in most cases well over 50% of 2018 profits. We note that to pay the maximum 2021 levels in Figure 2, banks would need approval from their respective regulators and that some banks could have already announced their intention to withhold dividends in 2021 to preserve capital.

Figure 2. Maximum DPS for 2021 dividends compared with actual 2019 dividend payments

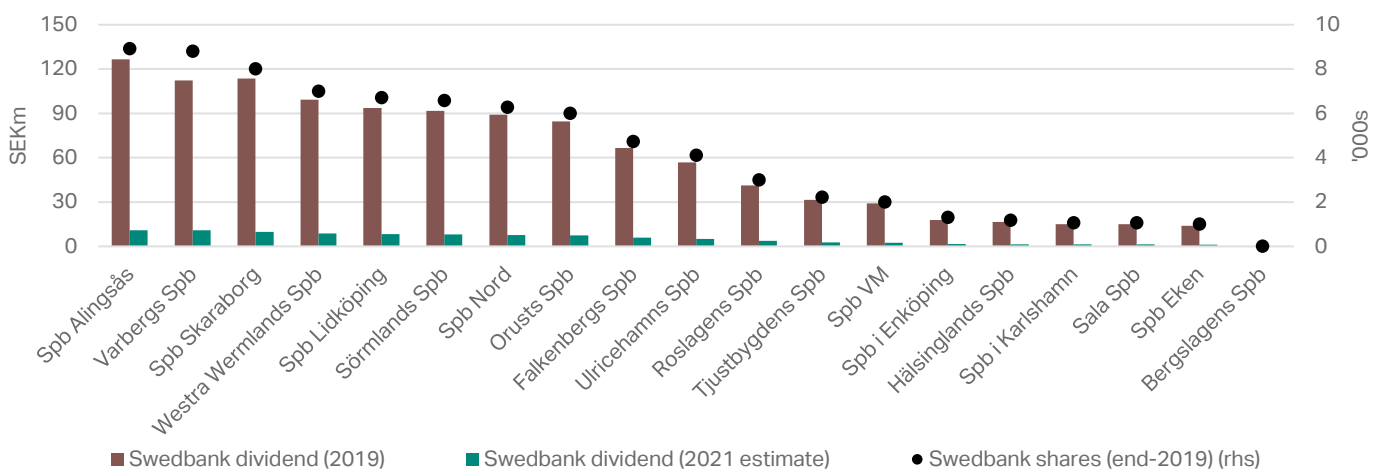


SWEDBANK'S DIVIDEND RESTRICTION AFFECTS EARNINGS FOR SWEDISH SAVINGS BANKS

Given recent comments from the Swedish Finance Department, Swedish regulators are likely to align with the new ECB guidance. As NCR has described in previous articles, Swedish savings banks are heavily invested in Swedbank shares and have varying degrees of reliance on dividend revenues (see [Swedish savings banks face challenges in remainder of 2020](#), published 15 Jun. 2020). For this reason, the relatively low dividend now likely will affect Swedish savings banks' 2021 earnings, assuming Swedbank is unable to increase its 2021 payment after the ECB guidance expires in September 2021.

For savings banks rated by NCR, our 2021 assumption has previously been about 50% of 2020 profits to be paid in 2021. The ECB's latest constraints lower our expectations. This, however, does not affect our earnings assessments on rated banks given our focus on core interest and fee earnings.

Figure 3. Swedish savings banks 2019 and estimated 2021 dividends from Swedbank



Source: Bank reports. Spb-Sparbank(en).

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