

Sörmlands Sparbank AB (publ)

Rating Action Report

LONG-TERM RATING

BBB+

OUTLOOK

Positive

SHORT-TERM RATING

N3

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'BBB+' long-term issuer rating affirmed**

Nordic Credit Rating (NCR) said today that it had revised the outlook on its 'BBB+' long-term issuer rating on Sweden-based Sörmlands Sparbank AB (publ) to positive from stable. At the same time the long-term rating, the 'N3' short-term issuer rating and the 'BBB+' senior unsecured issue rating were affirmed.

Rating rationale

The outlook revision reflects significant improvements in Sörmlands Sparbank's capital and earnings in recent years. The bank is well equipped to manage higher loan losses, lower credit growth, and increased competition for customer deposits. We remain cautious about the downside economic risk in the bank's area of operation and the potential impact on its performance. Moreover, we are likely to remain cautious until we see greater clarity about the national and local economy and the direction of interest rates. A higher rating would be contingent on the bank maintaining its current earnings performance and outstanding capital ratios, while improving its asset quality metrics.

We have lowered our assessment of the operating environment given the historical volatility of the bank's area of operation and pressure on the regional commercial and residential real estate sectors due to persistent inflation and sharp interest rate increases over the past 18 months. Conversely, we have raised our assessment of earnings due to improvements in key ratios and the cost base, which have reduced core cost income towards 50% in 2023 from 87% in 2019. While we expect net interest margins to peak later this year, the bank has a high proportion of fixed-interest mortgages set to reprice over the next two years and we expect earnings to remain strong through 2025.

Positive outlook

The positive outlook reflects our view that Sörmlands Sparbank's stronger capital and earnings provide solid buffers for managing an economic downturn in its core markets. Uncertainty about the local economy, as well as credit risk associated with regional commercial and residential real estate are already reflected in the rating. We would likely raise the rating to reflect a further elevation of earnings and capital levels and a reduced likelihood of a material downturn. In our base-case assessment, we expect continued strong capital ratios, supported by dividends from Swedbank AB.

We could raise the rating to reflect reduced economic uncertainty in the bank's region of operation and improvements in asset quality. We could also raise the rating if the bank maintains core pre-provision income above 2.5% of risk exposure amount (REA) and a common equity Tier 1 (CET1) capital ratio sustainably above 25%.

We could revise the outlook to stable to reflect a more significant downturn in the operating environment than we currently expect, that negatively impacts asset quality, loan growth, and/or funding access. We could also revise the outlook to stable to reflect a persistent decline in core earnings and capital, with core earnings falling below 2.5% of REA or a CET1 ratio below 25%.

Rating list	To	From
Long-term issuer credit rating:	BBB+	BBB+
Outlook:	Positive	Stable
Short-term issuer credit rating:	N3	N3
Senior unsecured issue rating:	BBB+	BBB+

Figure 1. Sörmlands Sparbank rating scorecard

Subfactors	Impact	To	From
National factors	10.0%	a-	a-
Regional, cross border, sector	10.0%	bb+	bbb-
Operating environment	20.0%	bbb	bbb
Capital	17.5%	aa-	aa-
Funding and liquidity	15.0%	a	a
Risk governance	5.0%	bbb+	bbb+
Credit risk	10.0%	bbb-	bbb-
Market risk	-	-	-
Other risks	2.5%	a	a
Risk appetite	50.0%	a	a
Competitive position	15.0%	bbb	bbb
Earnings	7.5%	a-	bbb
Loss performance	7.5%	bbb	bbb
Performance indicators	15.0%	bbb+	bbb
Indicative credit assessment		bbb+	bbb+
Transitions		Neutral	Neutral
Peer calibration		Neutral	Neutral
Borderline assessments		Neutral	Neutral
Stand-alone credit assessment		bbb+	bbb+
Material credit enhancement		Neutral	Neutral
Rating caps		Neutral	Neutral
Support analysis		Neutral	Neutral
Issuer rating		BBB+	BBB+
Outlook		Positive	Stable
Short-term rating		N3	N3

Figure 2. Capital structure ratings

Seniority	To	From
Senior unsecured	BBB+	BBB+

Type of credit rating:	Long-term issuer credit rating Short-term issuer credit rating Issue credit rating
Publication date:	The rating was first published on 02 Nov. 2020.
Office responsible for the credit rating:	Nordic Credit Rating AS (NCR), Oslo, Norway. NCR is a registered credit rating agency under Regulation (EC) No 1060/2009.
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Were ESG factors a key driver behind the change to the credit rating or rating outlook?	No.
Methodology used when determining the credit rating:	NCR's Financial Institutions Rating Methodology published on 18 Feb. 2022 NCR's Rating Principles published on 24 May 2022 NCR's Group and Government Support Rating Methodology published on 18 Feb. 2022 The methodology and principles documents provide analytical guidance to NCR's rating activities including but not limited to, assumptions, parameters, cash flow analysis, and stress-testing. NCR's methodologies and principles can be found on our website nordiccreditrating.com/governance/policies . The historical default rates of entities and securities rated by NCR will be viewed on the central platform (CEREP) of the European Securities and Markets Authority (ESMA) .
Materials used when determining the credit rating:	Annual- and quarterly reports of the rated entity, Bond prospectuses, Company presentations, Data provided by external data providers, External market reports, Meetings with management of the rated entity, Non-public information, Press reports/public information, Website of rated entity.
Potential conflicts of interest:	The rating is NCR's independent opinion of the rated entity's relative creditworthiness. The rating is solicited, i.e. it is prepared for a fee paid by the rated entity. At the time of analysis and publication neither NCR nor any of the analysts or persons involved in the rating process held any interest, ownership interest or securities in the rated entity. NCR does not have any direct or indirect shareholder with a holding of more than 5% of NCR's shares and votes. For further information, please refer to NCR's conflict of interest policy which is available on: https://nordiccreditrating.com/governance/policies
Additional information:	Prior to publication, the rating was disclosed to the rated entity. The issuer was given 24 hours (of which 8 business hours) to remark on factual errors and/or the inadvertent inclusion of confidential information, if applicable. The rating was not amended after the review by the issuer. No stress test or cash flow forecasting was performed. NCR's rating is an opinion regarding the relative creditworthiness of an entity or an instrument. It is not a prediction, guarantee or recommendation to buy, hold or sell securities. NCR assigns outlooks to issuer ratings to indicate where they could move in the near term, normally 12–18 months. Further information on the rating process, rating definitions and limitations is available on our website: nordiccreditrating.com/governance/policies .
Ancillary services provided:	No ancillary services were provided.
Regulations:	This rating was issued and disclosed under Regulation (EC) No 1060/2009.
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