Falling interest rates yet to impact Nordic niche banks

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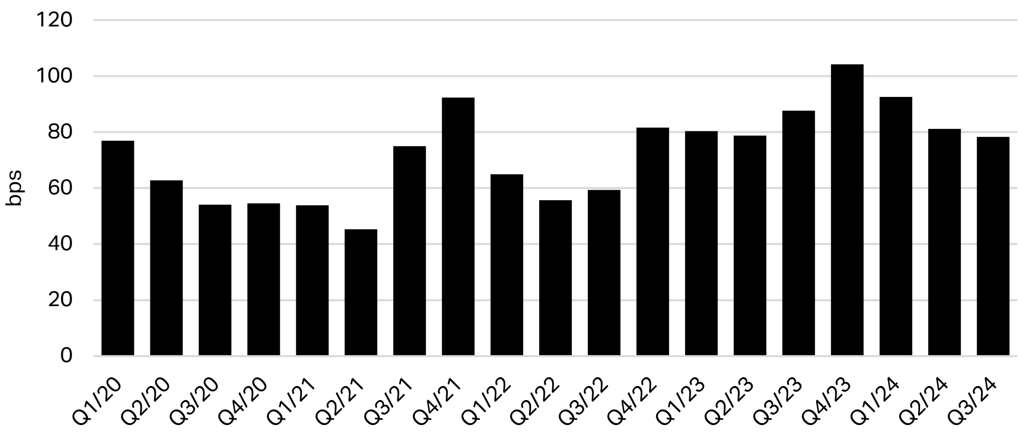
Nordic niche banks experienced decline in credit losses, reaching a two-year low, and improvements in risk-adjusted earnings and cost efficiency in the third quarter. Most of our sample of eight niche banks maintained capital ratios and strong earnings, which offset elevated loan-loss provisions in the period. Despite an uptick in transaction activity, non-performing (Stage 3) loans continued to rise as a proportion of overall lending for most banks.

Further reductions in policy rates and clear signals that rates will continue to fall, combined with increased risk appetite, have created positive momentum in the capital markets. The banks in our sample have issued senior unsecured bonds and Tier 2 capital instruments multiple times since September. This access could prove important given the Swedish regulator's revised guidance for calculating regulatory funding and liquidity metrics, which has caused a stir among banks using deposit distribution platforms such as Raisin and Avanza (see Relevant Research (i)).

Figure 1. Nordic niche banks' quarterly loss provisions to average net loans, Q1 2020 to Q3 2024



Source: bank reports.

Since our report in September, Ronneby UK Limited confirmed it had acquired 87% of Resurs Holding's outstanding shares after the final bid period closed on 4 Oct. 2024 (see Relevant Research (ii)). Conversely, NOBA Bank confirmed in late August that its owners are considering a possible initial public offering for the bank following the July completion of an intragroup merger that simplified its structure.

There have been further developments in the planned migration of bank headquarters to Sweden for Morrow Bank and Lea Bank. Morrow Bank completed its acquisition of two Swedish consumer loan portfolios with a value of NOK 2.3bn, around 35% of loan exposure. The bank also created a new Swedish legal entity and applied for a Swedish banking license in the fourth quarter. Morrow Bank expects a decision on its licence in the second quarter of 2025 and intends to move its headquarters to Sweden in 2026. Lea Bank received a bank licence in Sweden via its Swedish subsidiary Lea Bank AB and will move its headquarters to Sweden through an internal merger. Finnish-based niche bank Multitude Bank PLC acquired a 9.9% stake in Lea Bank with an agreement to acquire an additional 8.7% stake and become the bank's largest owner, upon approval of either the Norwegian or Swedish regulator, depending on timing.

Avida Finans announced its acquisition of Santander Consumer Bank's credit card and SME lending business in Sweden and Norway. The portfolio is around SEK 4bn and increases Avida's loan book by about 40%. Avida Finans will publish its third quarter results on 28 Nov. 2024 and has therefore been excluded from this quarterly report.

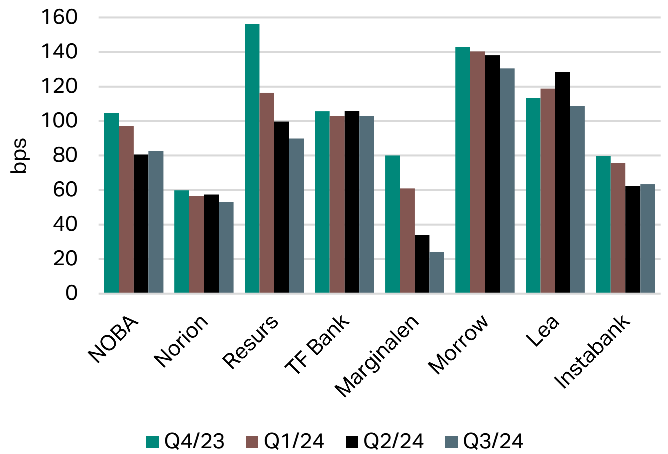
LOAN-LOSS PROVISIONS FALL TO TWO-YEAR LOW

Credit losses fell modestly for the banks in our sample in the third quarter, with weighted average provisions falling to 78bps of average net loans, from 81bps in the second quarter. Loss levels across our sample remain elevated compared with historical levels, but fell to their lowest level since the third quarter of 2022.

Lea Bank and Resurs Bank saw the biggest declines in provisions among the sample in the third quarter. Marginalen Bank reduced its provisions in the third quarter, although some of the reduction appears to be related to the securitisation of SEK 1bn of the bank's own non-performing loans (NPL) described below. Morrow Bank's loss ratio fell, although the material increase in the loan book makes comparison with previous quarters difficult. NOBA Bank, Norion Bank, Instabank and TF Bank reported only marginal changes in provisions during the third quarter.

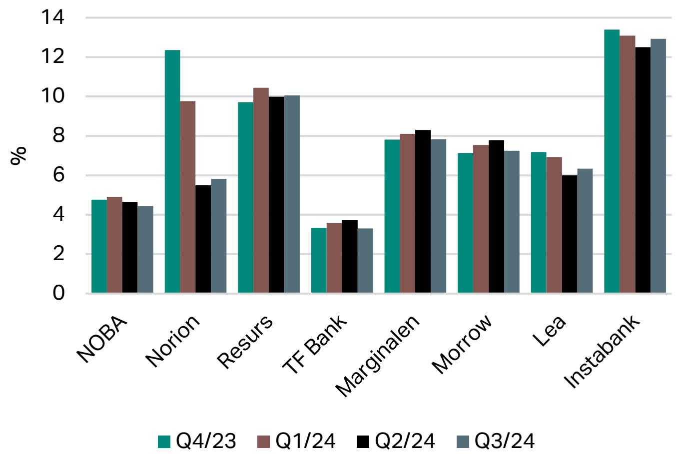
The level of net Stage 2 impaired loans fell modestly for the sample to 6.0% in the third quarter (6.1% in the second quarter), a positive sign for future credit losses.

Figure 2. Nordic niche banks' loan-loss provisions to average net loans, Q4 2023–Q3 2024



Source: bank reports.

Figure 3. Nordic niche banks' net Stage 2 loans to net loans, Q4 2023–Q3 2024



Source: bank reports.

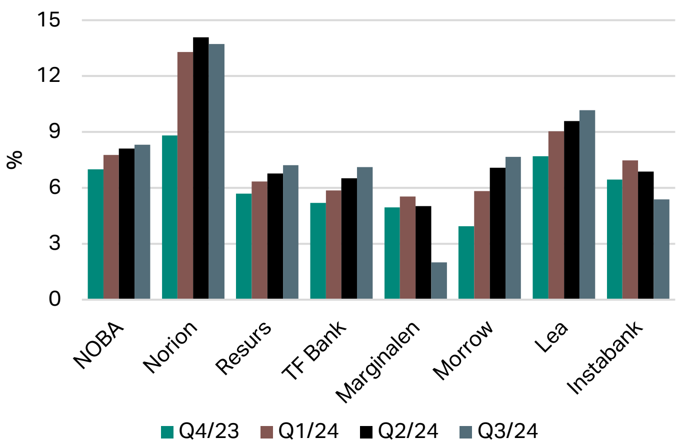
NON-PERFORMING LOANS RISE FURTHER AS MARKET DEVELOPS SOLUTIONS

Despite continued disruption in the Nordic NPL market, banks managed to offload NPLs in the second half of 2024 to offset the punitive impacts of the European NPL backstop on capital ratios. NOBA Bank completed a previously announced SEK 700m NPL securitisation in Sweden in July, while Marginalen Bank securitised NPLs worth SEK 1bn. Instabank sold SEK 300m in non-performing Finnish consumer loans during the third quarter for a net profit.

As a result of the completed transactions above, the weighted average of net Stage 3 loans for our sample fell marginally to 8.5% in the third quarter (8.6% in the second quarter). However, the underlying trend remains clear and negative, with the majority of banks in our sample reporting an increasing share of NPLs. In addition to the transaction-related reductions for Instabank and Marginalen, Norion Bank's Stage 3 loans declined during the third quarter, driven by a reduction in the proportion of Stage 3 consumer loans.

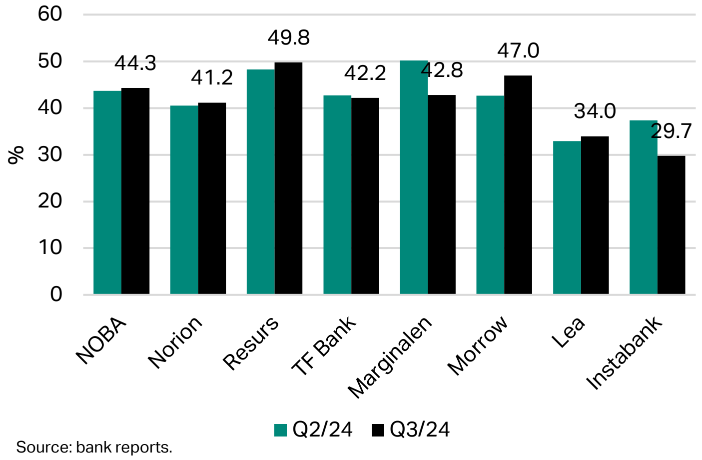
TF Bank created a new subsidiary, Rediem, which acquired SEK 1.3bn in NPLs from TF bank. According to a letter of intent, more than 80% of Rediem will be sold to Alektum Holding, Erik Selin Fastigheter and G4 Capital AB on 31 Dec. 2024. In October, Norion Bank (with Erik Selin as chairperson) announced that it will make a strategic investment in Alektum Holding. The owners aim for Rediem to be defined as a specialised debt restructurer on 1 Jan. 2025, which could lead to these mentioned banks offloading NPLs and reducing the capital impact of the European NPL backstop regulation. Weaker NPL markets should be reflected by higher provisioning for Stage 3 NPLs, though this has yet to happen. Using a weighted average, Stage 3 coverage ratios increased marginally to 43.7% for the weighted sample in the third quarter, from 43.2% in the second quarter and from 46.8% in third-quarter 2023. The banks with the largest coverage ratio changes in the third quarter – Marginalen, Morrow and Instabank – were affected by NPL transaction activity.

Figure 4. Nordic niche banks' net Stage 3 NPLs to net loans, Q4 2023–Q3 2024



Source: bank reports.

Figure 5. Nordic niche banks' Stage 3 coverage ratios, Q2 2024–Q3 2024



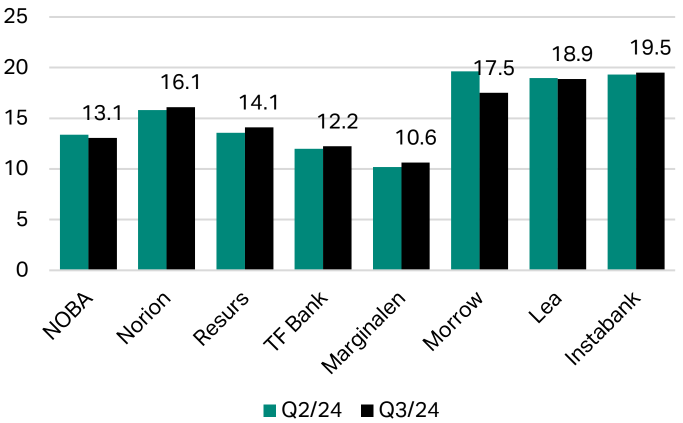
Source: bank reports.

Norion Bank's Stage 3 coverage ratios were stable for consumer loans at a relatively high 55.1% in the third quarter (54.4% in the second quarter) and 21.0% (20.4%) for corporate and real-estate exposure. The secured nature of the real estate portfolio warrants a lower coverage ratio for such lending, but real estate loans remain a risk, which we reflect in our negative outlook on the bank.

CAPITAL RATIOS STAGNANT DESPITE STRONG EARNINGS

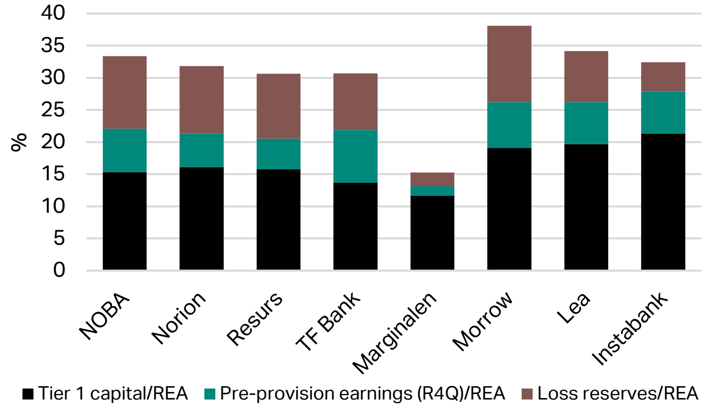
Weighted average common equity Tier 1 (CET1) ratios in our sample remained at 14.1% in the third quarter. For the majority of our sample, capital movements were minimal, although Morrow Bank's acquisition of SEK 3.2bn combined with its own organic growth led to lower capital ratios. As expected, NOBA Bank's CET1 ratio fell by nearly 30bps in the third quarter as a result of its intragroup merger. The bank's Tier 1 ratio was 15.3% and we expect it to maintain its Tier 1 ratio above 15% for the remainder of 2024. We expect NOBA Bank's capital ratios will benefit from the implementation of new capital regulations in 2025, primarily due to the low leverage in its equity-release mortgage loans to elderly borrowers.

Figure 6. Nordic niche banks' CET1 ratios, Q2 2024–Q3 2024



Source: bank reports. Marginalen Bank's ratios relfect consolidated capital.

Figure 7. Nordic niche banks' loss-absorbing buffers as a proportion of REA, Q3 2024



Source: bank reports. REA-risk exposure amount. LTM-last 12 months. Marginalen Bank's ratios relfect consolidated REA.

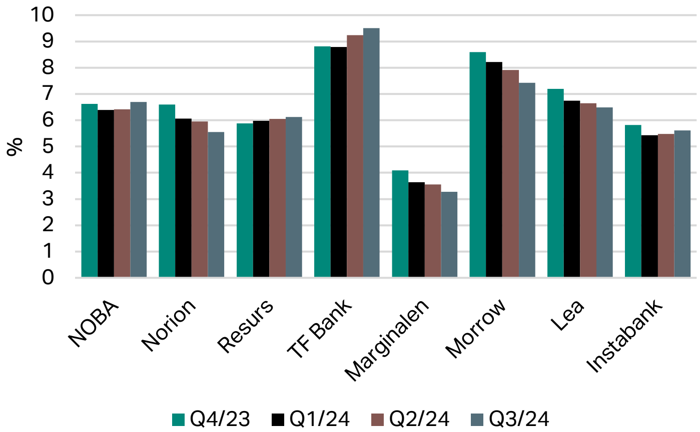
Marginalen Bank's capital situation improved somewhat during the third quarter. On a standalone basis, the bank reported a CET1 ratio of 10.0% (up from 9.9% in the second quarter), 0.2% above its minimum regulatory requirement. On a consolidated basis, parent ESCO Marginalen AB reported a CET1 ratio of 10.6% (10.2%), 1.3% above requirements. A material portion of the capital improvement was due to the securitisation of SEK 1.0bn of Marginal Bank's loans in an agreement with UK private equity company Christofferson, Robb & Co. Marginalen Bank received a warning from the Swedish regulator for its management of large loan exposures during the quarter, and an appeal against the Swedish regulator's Pillar 2 guidance of 5% for Marginalen Bank and 2% for ESCO Marginalen remains unsettled. We continue to follow the bank's situation.

MARGINS CONTINUE DOWNWARD TREND

Net interest margins stabilised in the third quarter after a dramatic fall in the first quarter. The weighted average net interest margin in our sample improved slightly to 6.39% in the third quarter (6.34% in the second quarter), led by improvements for NOBA Bank and TF Bank. The Swedish regulator's changed stance on deposit distribution platforms could affect banks' funding costs as the banks adapt their funding profiles to support their regulatory funding and liquidity metrics (see related research (i)).

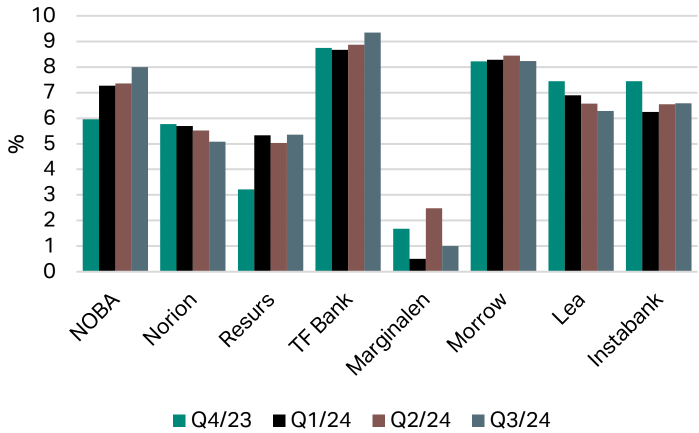
However, we believe positive momentum in capital market financing and falling policy rates will reduce banks' funding costs. Norion Bank, Resurs Bank and NOBA Bank issued a total of SEK 3.1bn in senior unsecured bonds since May 2024. TF Bank, Morrow Bank and Norion Bank have also issued Tier 2 capital instruments since September.

Figure 8. Nordic niche banks' annualised net interest margins, Q4 2023–Q3 2024



Source: bank reports.

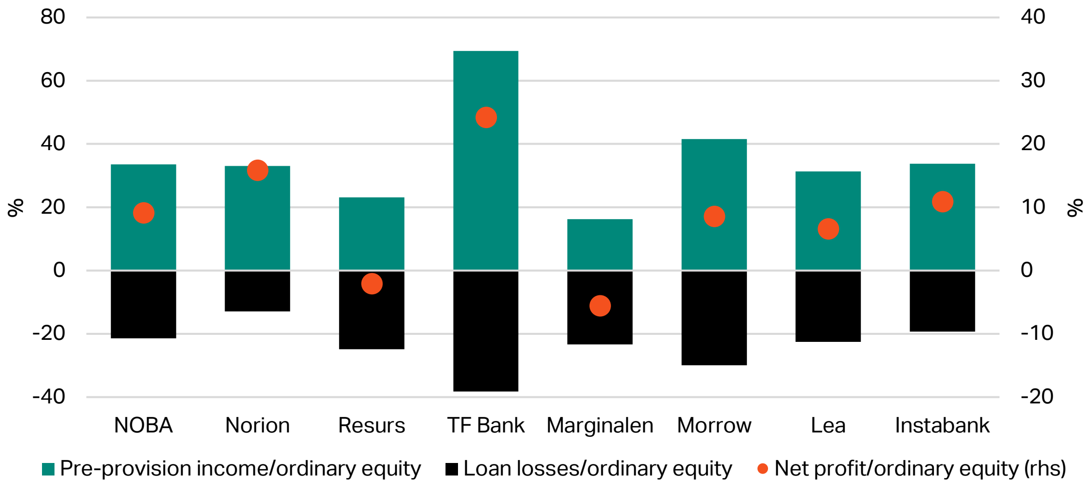
Figure 9. Nordic niche banks' annualised pre-provision income to average REA, Q4 2023–Q3 2024



Source: bank reports.

For most of the banks in our sample, the stabilisation in net interest margins and cost efficiency imply strong risk-adjusted earnings. Weighted average pre-provision earnings as a proportion of average risk exposure amount improved further to 6.5% during the third quarter from 6.3% in the second. Cost efficiency also improved among the larger banks in our sample.

Figure 10. Nordic niche banks' pre-provision income, loan losses and net profit as a share of average ordinary equity, 12 months to 30 Sep. 2024

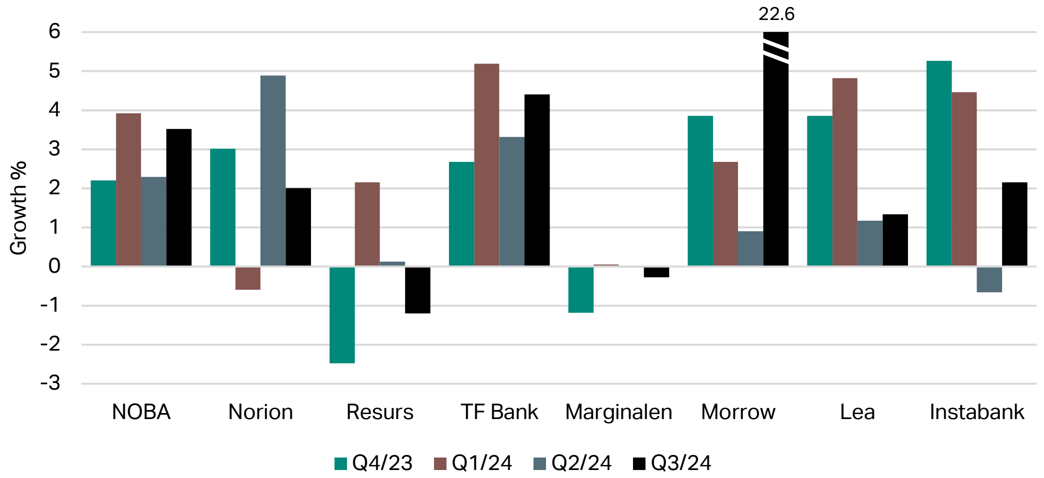


Source: bank reports.

Most of the banks in our sample have generated adequate capital and posted strong returns on ordinary equity over the past 12 months, despite higher losses. TF Bank reported a strong return of 24.2% over the past year due to increased scale and cost efficiency, offsetting relatively high credit provisions. Norion Bank (15.9%) and Instabank (10.9%) have also achieved double-digit returns over the past year. In addition, material improvements in scale and efficiency, and a reduction in merger-related costs in recent quarters improved NOBA Bank's return on ordinary equity to 9.1% in the year ending in the third quarter (10.9% year-to-date). Resurs Holding's negative return on equity over the last 12 months was affected by one-off events in 2023. The bank has steadily improved its return on equity in each of the first three quarters of 2024, despite high provision levels, and reported a year-to-date return on equity of 3.0%. Marginalen Bank had a -5.5% return on equity due to net losses over the past year due to one-off charges, including a corrected accounting error in accrued interest. The bank's core earnings are also weak due to elevated credit losses and weaker-than-peer net interest margins.

LENDING GROWTH REMAINS MUTED ACROSS THE SECTOR

Figure 11. Nordic niche banks' net loan growth, Q4 2023–Q3 2024



Source: bank reports.

Excluding Morrow Bank, weighted average net loan growth across our sample remained unchanged at 2.2% in the third quarter. Morrow Bank's acquisitions increased its loan book by 22.6% during the third quarter. TF Bank continued its strong growth in credit cards (8.1%) and in Germany (12.8%). In contrast, Resurs Holding saw a contraction in consumer loans, primarily due to a reduction in its Norwegian exposures.

SWEDISH INTERPRETATION OF REGULATORY FUNDING METRICS CREATES A STIR

On 30 Sep. 2024, the Swedish Financial Supervisory Authority (SFSA, in Swedish: Finansinspektionen) released a legal position requiring financial institutions under its supervision to classify retail deposits from deposit distribution platforms as if they were deposits from deposit brokers (see related research (i)). The announcement came on the last day of the third quarter, giving affected banks little time to adapt their funding strategies for reported liquidity coverage ratios (LCR) and net stable funding (NSFR) ratios for the third quarter. The rules are binding for LCR as of 31 Oct. 2024 and for NSFR as of 31 Dec. 2024.

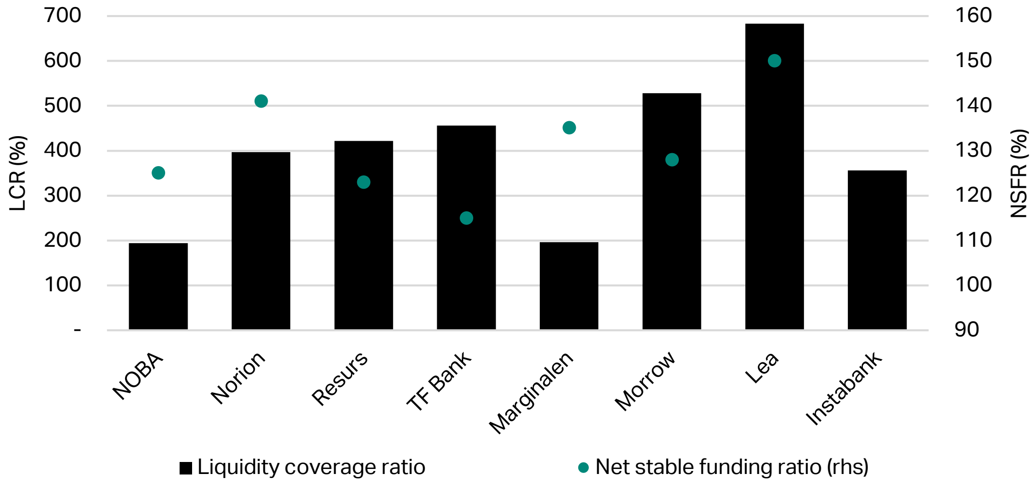
Notably, TF Bank and Marginalen Bank commented that the SFSA changes had no impact on their regulatory ratios. TF Bank announced that it is already compliant with the new factors and weights prescribed by the SFSA. In its third quarter report, Marginalen Bank indicated that it was unaffected because it has "never relied on external deposit platforms".

The other Swedish banks in our sample reported with varying degrees of transparency. Resurs Holding commented only that it will adapt its financing strategy, expecting deposit platforms to be less attractive and costs of deposits to increase. On the opposite end of the spectrum, Norion Bank provided five quarters of historical regulatory ratios it had calculated using the new method. The figures indicate that the bank's NSFR would have been just above the 100% regulatory limit over the last year.

NOBA Bank, which reported its third quarter results in mid-November, calculated its first regulatory LCR ratio under the new requirements (148% as of 31 Oct. 2024) and indicated that its NSFR at 30 Sep. 2024 would have been 107% under the new rules.

Upon moving their regulatory headquarters to Sweden, Lea Bank and Morrow Bank will be subject to the Swedish approach in the future, but maintain relatively strong ratios as of 30 Sep. 2024.

Figure 12. Nordic niche banks' regulatory funding and liquidity metrics, 30 Sep. 2024



Source: bank reports.

NCR-RATED NICHE BANKS

The following table summarises NCR's ratings on Nordic niche banks as of 20 Nov. 2024.

Figure 13. NCR ratings on Nordic niche banks

	Resurs Bank	Norion Bank	NOBA Bank Group
Long-term issuer rating	BBB	BBB-	BBB
Outlook	Negative	Negative	Stable
Subfactors:			
Operating environment (20%)	bbb-	bbb-	bbb-
Risk appetite (50%)	bbb	bb+	bbb
Market position (15%)	bb+	bb	bbb-
Performance indicators (15%)	bbb+	bbb+	bbb+
Ownership adjustment	0	0	0

See NCR's company rating reports for details.

RELEVANT RESEARCH

(i) Swedish niche lenders face regulatory changes in funding metrics, 21 Oct. 2024.
(ii) NCR Comments: Resurs Bank 'BBB' rating and outlook unchanged following finalised bid, 15 Oct. 2024.
(iii) Nordic consumer banks' earnings continue to offset elevated provisions, 10 Sep. 2024.
(iv) NCR Comments: Resurs Bank 'BBB' rating and outlook unchanged following acquisition offer, 25 Jun. 2024.
(v) Credit loss uncertainty rises for Nordic consumer banks, 11 Jun. 2024.
(vi) The pressure is rising for Nordic consumer banks (report), (webinar slides), 13 Mar. 2024.
(vii) Nordic consumer banks increase credit losses, 29 Nov. 2023

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