

Pressure rising for Nordic niche banks

13 Mar 2024

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During the 4th quarter, Nordic consumer banks...

- continued to increase credit loss provisions;
- increased Stage 2 (impaired) and Stage 3 (non-performing) loans;
- experienced turbulence in non-performing markets;
- maintained capital ratios; and
- offset losses with strong margins and cost efficiency.

The pressure is rising for Nordic consumer banks

Nordic
Credit
Rating

SECTOR COMMENT

13 Mar. 2024

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The fourth quarter of 2023 saw a further increase in credit losses and marginal declines in earnings for niche consumer banks in the Nordic region. Most of the banks in our sample of nine regional consumer banks maintained strong earnings and cost efficiency in the quarter, which continued to offset elevated loan-loss provisions. In addition, the proportion of loans showing increasing signs of weakness (Stage 2 loans) is rising, and banks continue to indicate that payment patterns could be at risk as economic conditions worsen.

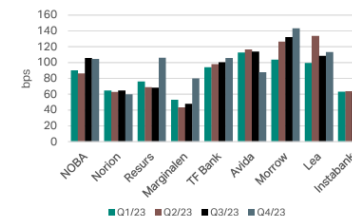
We expect interest rates across the region to remain elevated in early 2024 before the rate paths begin to deviate. Yield curves indicate a steep reduction in market rates in Sweden and the eurozone, and a more gradual decline in Norway. These declines could provide relief to indebted borrowers, though we maintain our view that loan-loss provisions will remain elevated throughout 2024. Furthermore, we anticipate that earnings margins will face pressure due to intensified competition for profitable loan growth and deposit funding. We expect this combination of negative factors to drive weaker performance across the sector in 2024.

Thus far in 2024, NCR's rating on Resurs Bank was put on negative outlook in January to reflect our expectation that the bank's asset quality metrics will deteriorate further and remain worse for longer, compared with previous assessments (see related research (i)). This occurred after the bank announced a significant increase in loss provisions and weakening customer behaviour in December. Also in January, the Swedish government released a proposal to remove the interest rate tax deductibility of consumer loans, which is likely to lead to higher costs for the banks as they adapt. Additionally, on 25 Jan. 2024, the Swedish regulator announced an investigation into Marginalen's risk management and credit risk compliance with applicable regulations.

LOAN-LOSS PROVISIONS AND IMPAIRED LOANS ON THE RISE

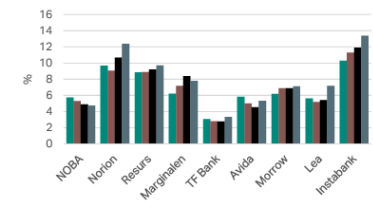
Additional interest rate hikes in all markets in 2023 continue to put stress on the repayment capacity of Nordic households. During the fourth quarter, asset quality indicators jumped, with weighted average credit provisions rising to 96bps of average net loans (excluding the effects of the Resurs securitisation described below) from an average of 84bps in the previous three quarters. Resurs's increase in fourth quarter reserves because of rising delinquencies in December account for around 4bps of the sample's 12 basis point increase.

Figure 1. Nordic consumer banks' loan-loss provisions to average net loans, Q1 2023–Q4 2023



Source: bank reports. Resurs's Q4/23 provisions exclude the one-off impact of securitising non-performing loans.

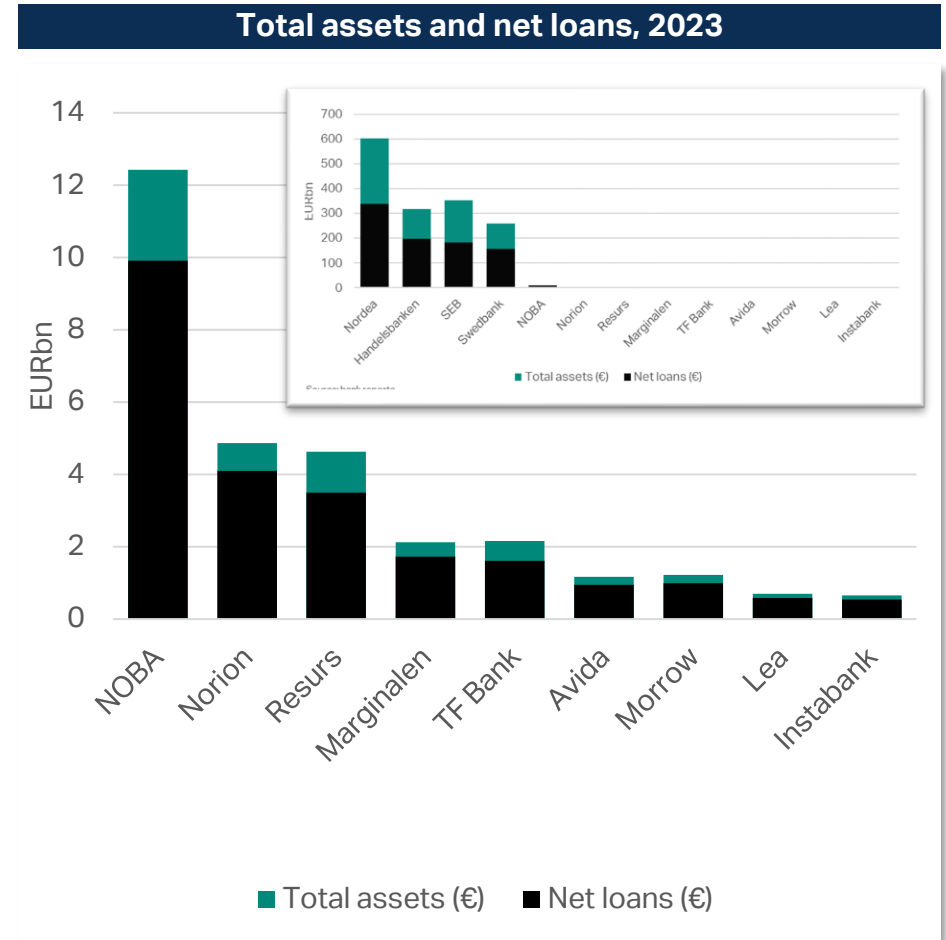
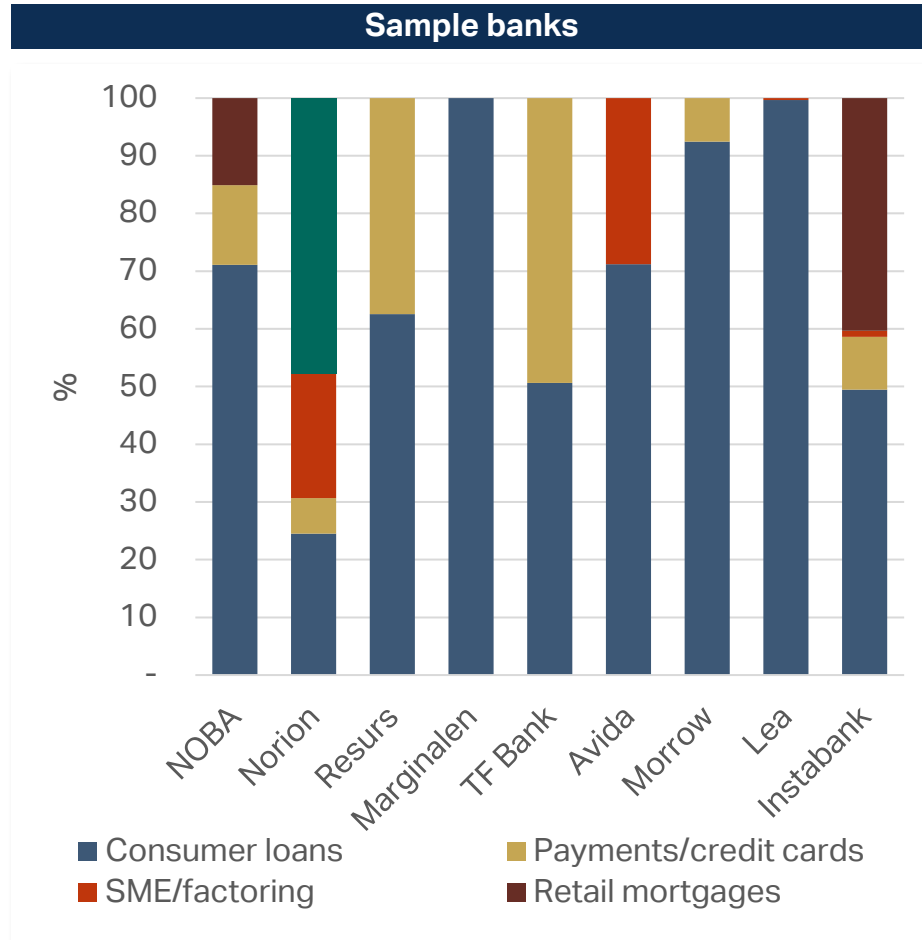
Figure 2. Nordic consumer banks' net Stage 2 loans to net loans, Q1 2023–Q4 2023



Source: bank reports.

Nordic niche banks

Nine niche banks are the focus of our quarterly reviews



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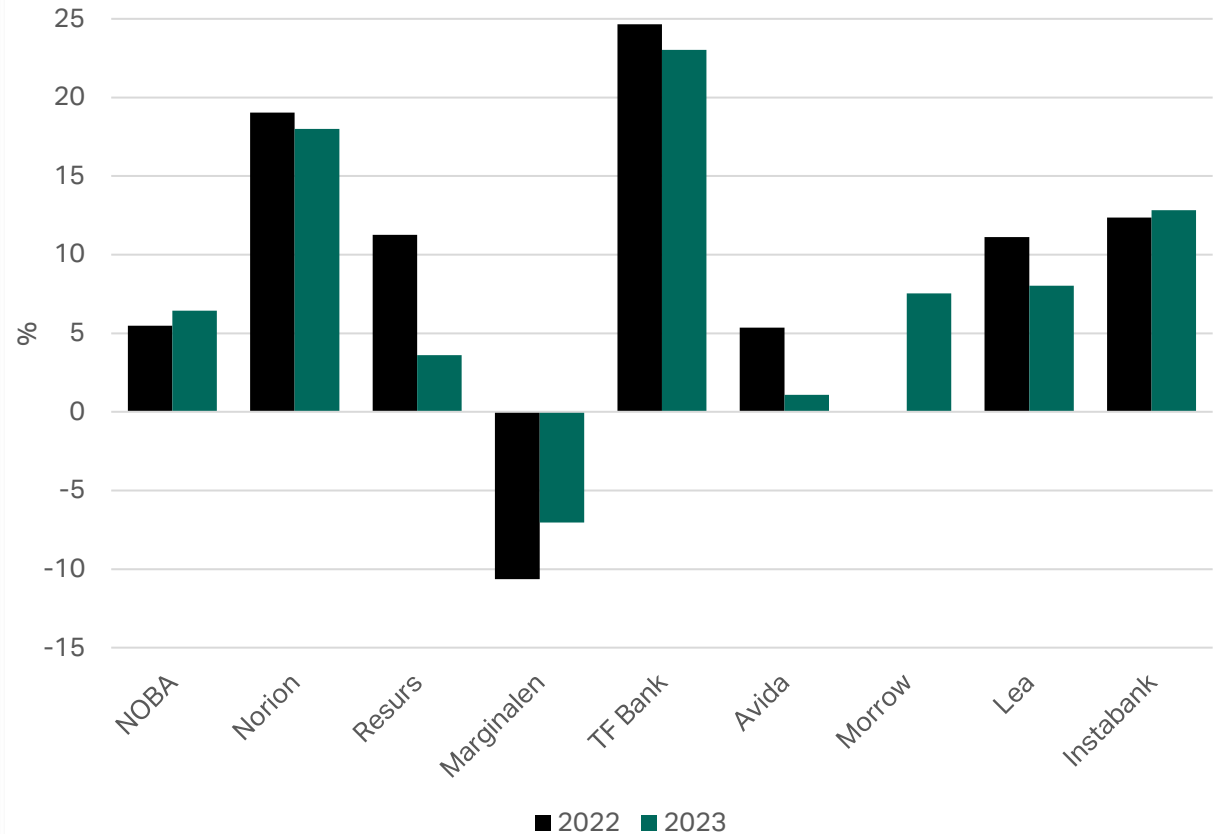
- 1. 2023 performance summary**
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Maintained profitability despite higher losses

Small changes in average RoE compared with last year

Return on ordinary equity

- Despite higher interest rates, average return on ordinary equity fell to 8.2% from 8.7%
- In comparison, average risk-adjusted pre-provision earnings¹ increased to 6.1% for 2023 from 5.0% in 2022.

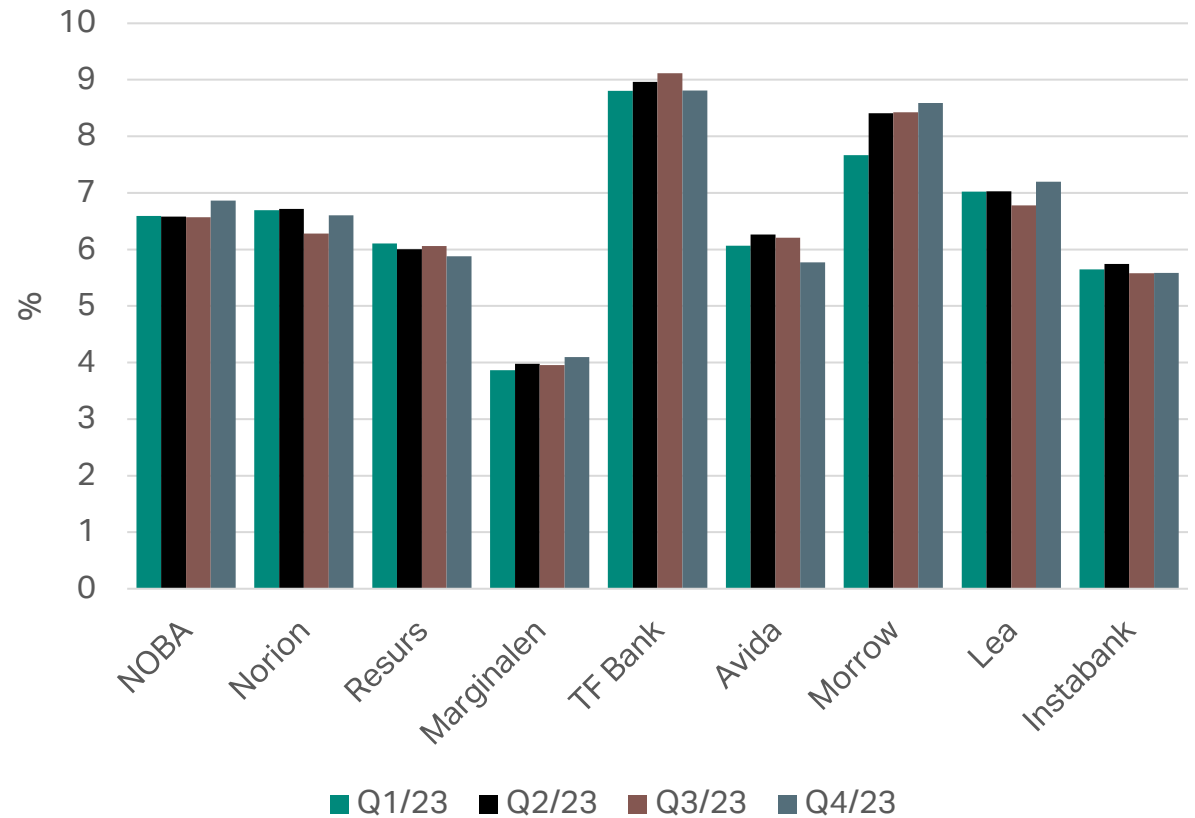


Net interest margins have stabilized for now

Most likely past this cycle's peak

Annualized quarterly net interest margins 2023

- Average margins have risen consistently since 2020, and were up 24bps for the full year 2023 vs 2022
- Improved pre-provision earnings have also supported lower cost-income ratios (40.1% 2023 vs 47.5% 2022)
- We expect stable, or somewhat decreasing, margins in 2024
 - Lower interest rates, weaker loan demand and high competition for deposits
 - As well as increased non-payments

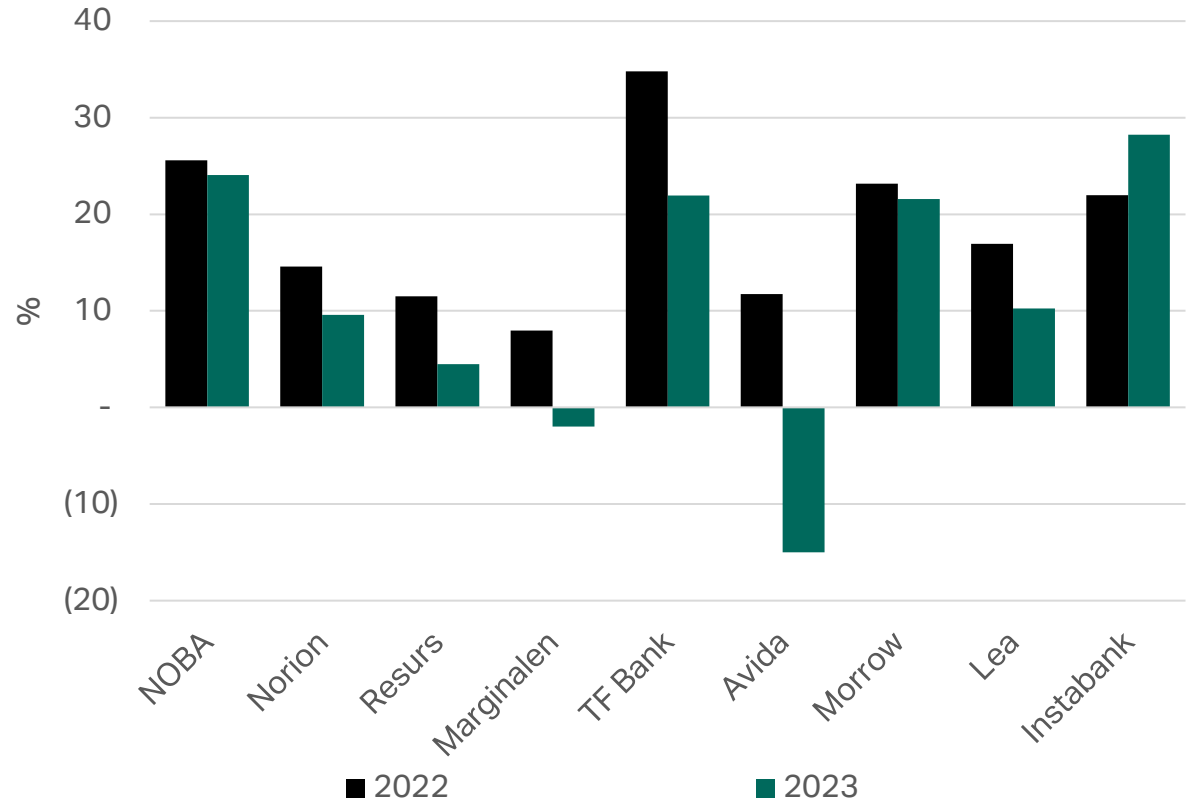


Loan growth has slowed

Full-year growth still strong for most of the banks

Annual growth in net loans

- Net loans grew 11.5% in 2023 vs 18.7% in 2022
- Material slow down in the fourth quarter, growth LTM to Q3 2023 was 15.8%
 - Fourth quarter average growth 0.95%, compared with average quarterly growth of 3.3% Q1-Q3
- Depreciation in Norwegian krone impacted reported loan volumes



SEK/EUR	NOK/EUR	DKK/SEK	DKK/NOK	SEK/NOK
-0.2%	6.5%	0.4%	-5.9%	-6.3%

Change from last trading day 2022 to last trading day 2023.

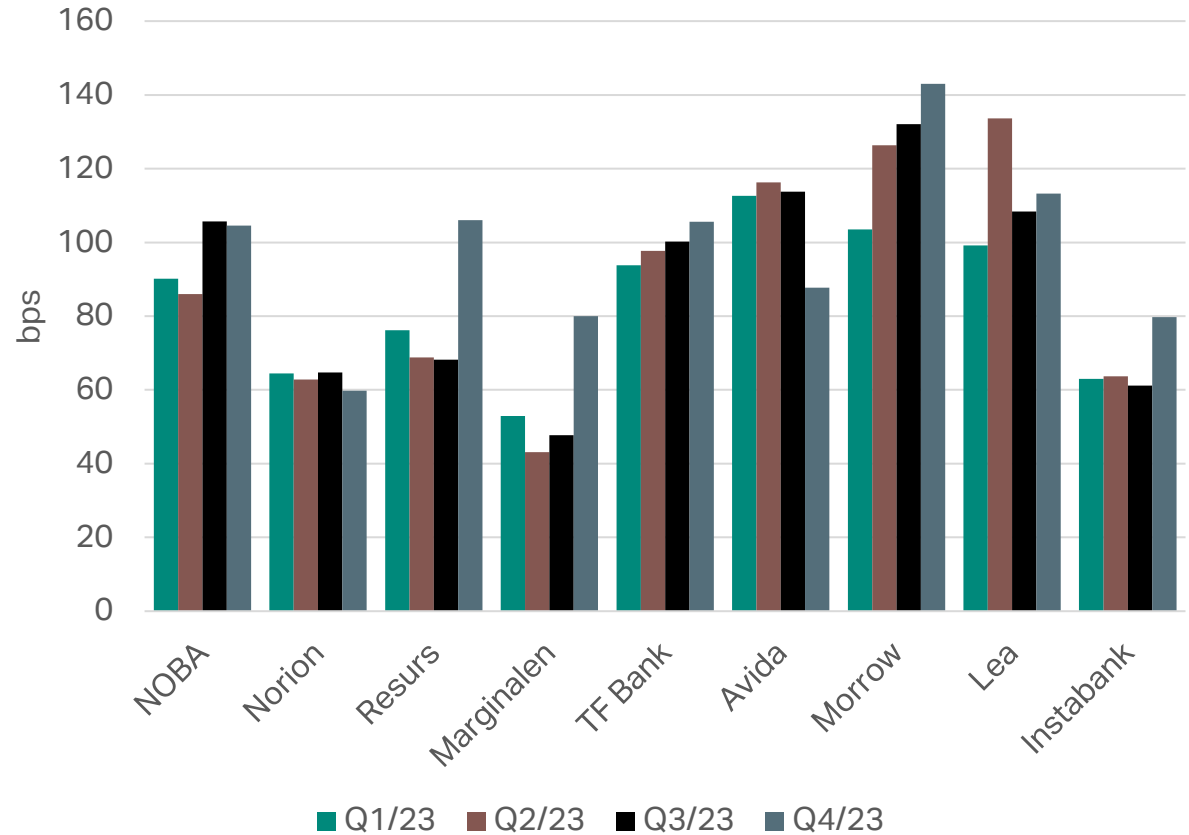
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Loan loss provisions

Quarterly loan loss provisions as a share of net loans

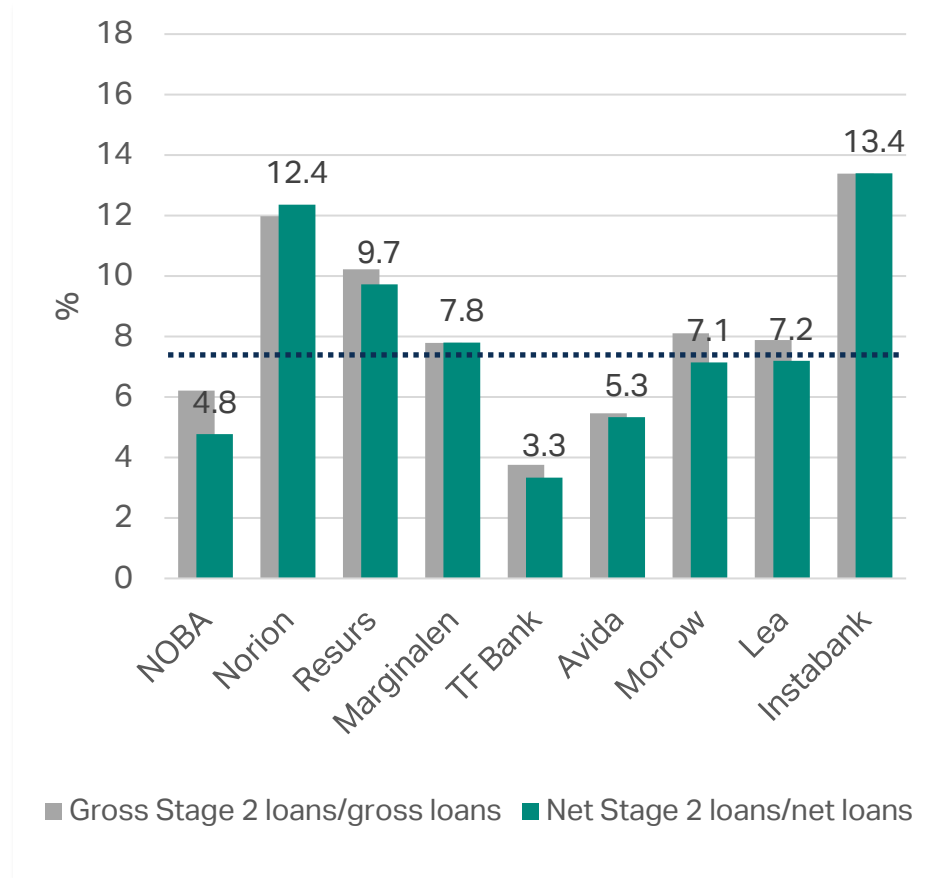
- The trend of increasing credit losses continued in the fourth quarter.
- Weighted average loss provisions rose to 96bps in the quarter, from an average of 84bps in the first three quarters of 2023.
- An increase in provisions by Resurs accounted for one-third of the increase.
- One-off impacts for Marginalen and Instabank were associated with IFRS 9 model calibrations.
- Avida's sale of non-performing loan portfolios and a reduced focus on new consumer lending reduced provision levels.



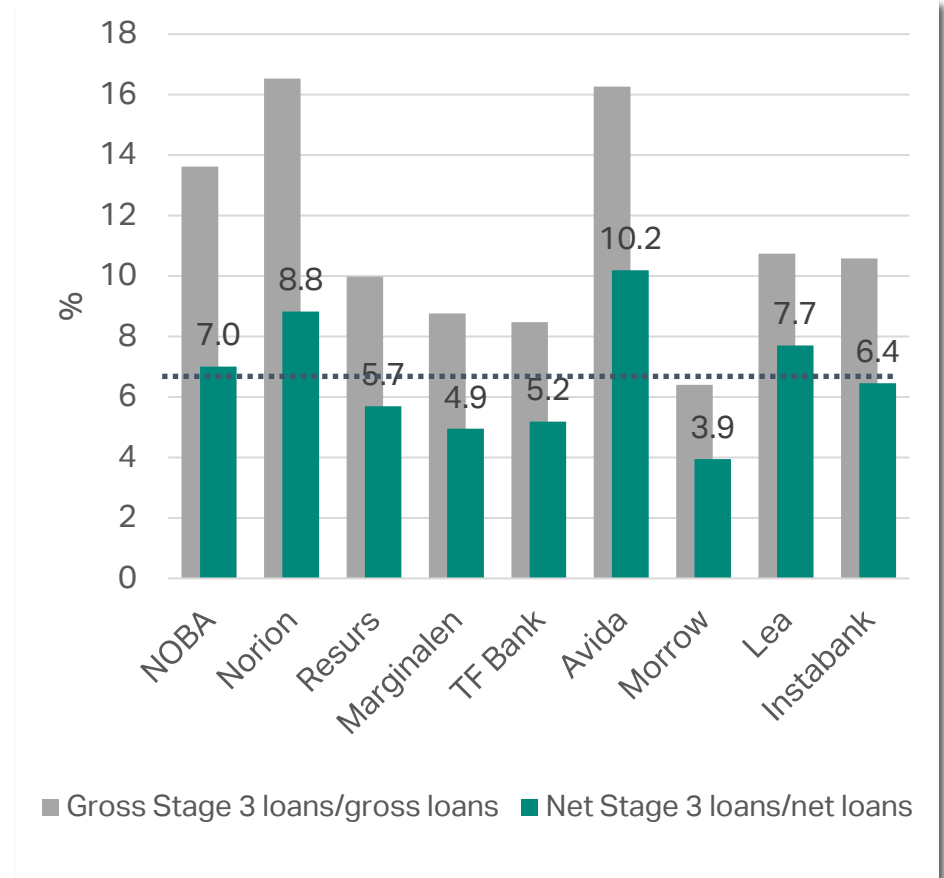
A rise in impaired and non-performing loans

Asset quality metrics weakened by 20 to 30 bps in the fourth quarter

Stage 2 – Impaired loans



Stage 3 – non-performing loans

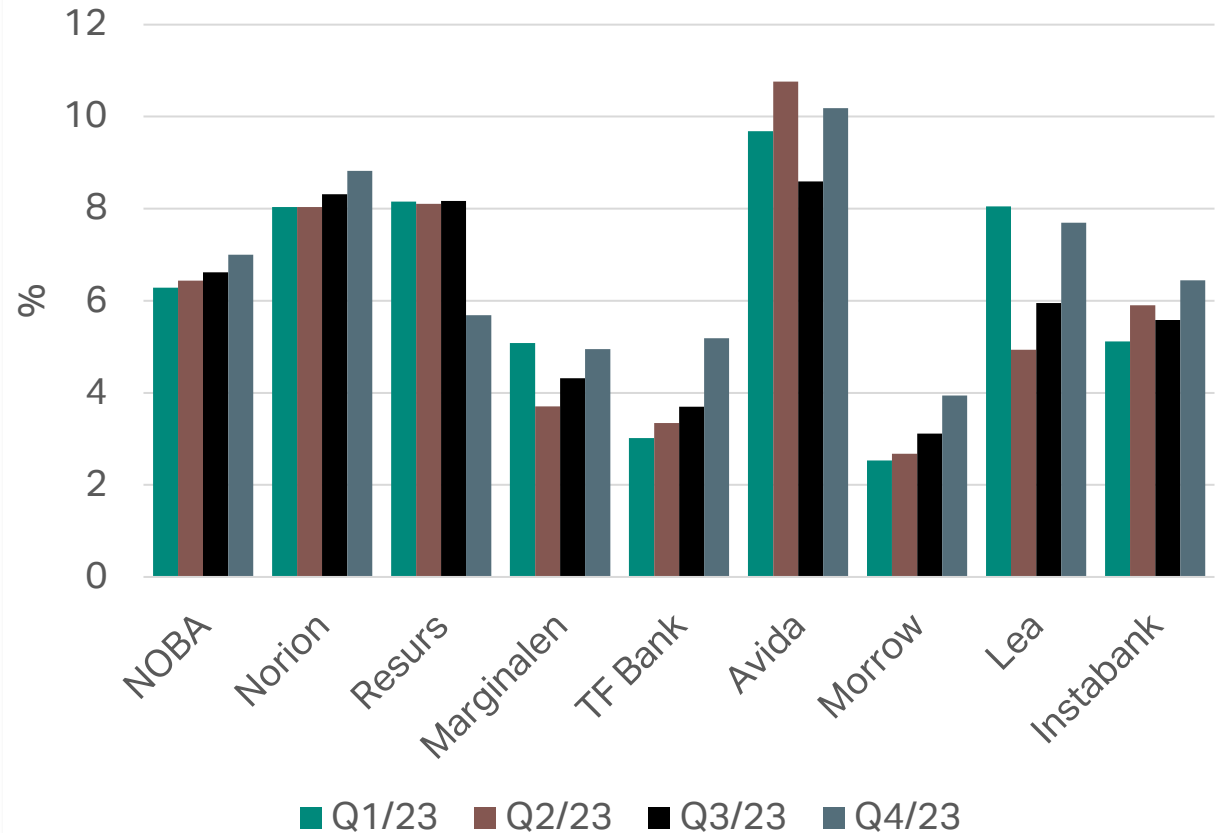


The market for non-performing loans has weakened

Market disruptions have resulted in increasing Stage 3 non-performing loans

Net Stage 3 loans / net loans

- Net stage 3 non-performing loans (NPLs) increased for the second quarter in a row.
- The ability to off load NPLs has been materially affected by the weakness of debt purchasing companies.
- The EU's NPL backstop increased the capital impact of maintaining NPLs on balance sheet.
- Resurs securitised 39% of its net NPLs, as a sign that banks are considering alternative solutions.
- Financial guarantees of a secured book of NPLs and third-party risk transfer and SPV solutions are other alternatives.



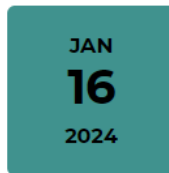
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2024 so far

Intense start for the (Swedish) niche bank sector

- Resurs Bank issues profit warning following rapid increase in loan losses, combined with IT investment write-down
 - Outlook on credit rating revised to negative over concerns of asset quality development and capital ratios
- Swedish FSA¹ launches an investigation into Marginalen Bank's credit process, based on observations from 2023 SREP²
- Swedish government launches proposal to remove tax deductibility for unsecured lending, effective already next year



Resurs Holding meddelar lägre resultat för det fjärde kvartalet 2023. Som följd kommer styrelsen inte föreslå halvårsutdelning.

REGULATORY

FI undersöker Marginalen Bank

2024-01-25 | UNDERSÖKNINGAR PÅGÅENDE BANK

FI undersöker hur Marginalen Bank AB följer tillämpliga bestämmelser om riskhantering avseende bland annat krediter

Åtgärder för att motverka överskuldsättning

Publicerad 25 januari 2024

För att motverka överskuldsättning remitterar Finansdepartementet idag ett förslag som innebär att ränteavdrag på konsumtionslån utan trygga säkerheter avtrappas.

Tax deductibility of consumer loans

21%-30% interest rate deduction up for removal.

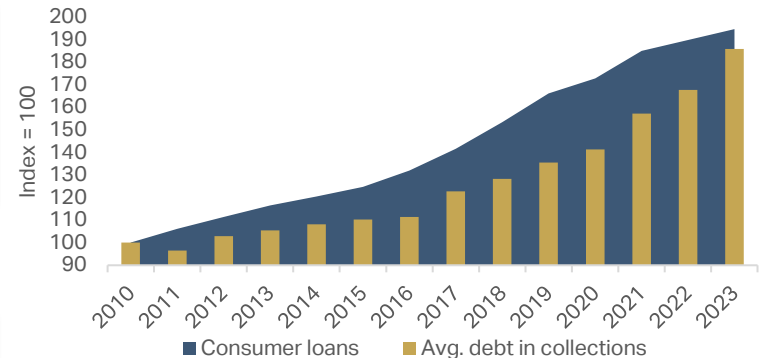
Details

- Under Swedish tax law, net interest costs are deductible with up to 30% of the annual amount
- Proposed change: only mortgages and loans secured to cars/boats
- Phase-out 50% for tax year 2025, and 100% for tax year 2026

Expected impact

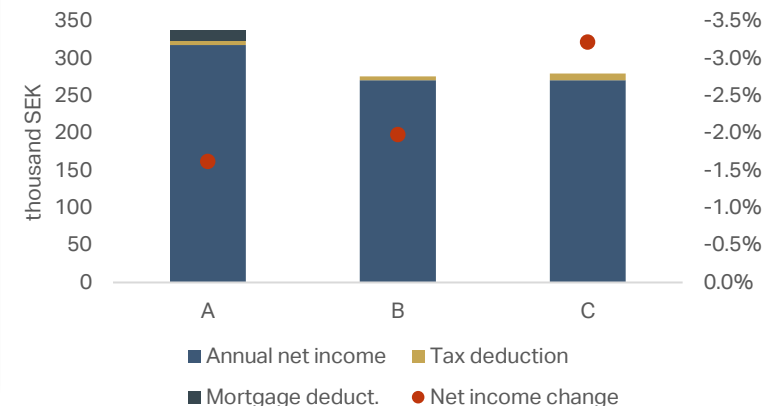
- Expected impact in SEK should be limited for most borrowers
- Implying we should see an increase in losses in Q1-Q2 2026, but not a floodwave
- Unlikely that banks *directly* include the deduction in calculations – however, we believe removing this buffer will lead to stricter requirements
- In effect from 1 Jan 2025 – this year will require speedy adaption

What's driving the political attention



Source: Statistics Sweden, the Swedish Enforcement Authority.

Impact on annual net income



Source: Statistics Sweden, the Swedish Tax Agency.

Expectations for 2024...

- interest rates to fall and macroeconomic factors to weaken in all markets
- declining margins due to rising funding costs
- credit provisions to rise further
- banks to adapt growth and risk appetite to capital needs and provision requirements
- finalisation of the Swedish proposals and continued political focus on consumers' inability to repay debts



NCR-rated niche banks

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

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Thank you



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