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Eksportfinans ASA

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Eksportfinans ASA

SACP	bbb+

Anchor	a-	
Business Position	Moderate	-1
Capital and Earnings	Very Strong	+2
Risk Position	Moderate	-1
Funding	Below Average	-1
Liquidity	Adequate	

\+

Support	0
ALAC Support	0
GRE Support	0
Group Support	0
Sovereign Support	0

\+

Additional Factors	0

Issuer Credit Rating
BBB+/Positive/A-2

Major Rating Factors

Strengths:	Weaknesses:
• Very robust capitalization. • Successful management of the wind-down of the loan book and funding.	• Residual exposure to structured funding and derivatives. • Operational and liquidity risks during the wind-down.

Outlook: Positive

The positive outlook on Norway-based Eksportfinans ASA reflects S&P Global Ratings' view that the likelihood of the company's orderly wind-down will continue to increase as the funded loan book reduces.

We could upgrade Eksportfinans in the next two years if the significant maturities and associated reduction in the loan book, alongside decreased derivative exposures over the next two years, heighten the likelihood of full and timely repayment of senior debt. The reductions in Eksportfinans' balance sheet and risks should improve its risk-adjusted capital (RAC) buffers from already exceptional levels. We could also revise our assessment of Eksportfinans' business position as a result of an increased possibility of a stable wind-down, for instance if the company was to be acquired by one of its higher-rated owner banks, improving the likelihood of it meeting its debt obligations.

We could revise our outlook to stable on signs of operational instability during Eksportfinans' wind-down process, or if its capital position materially weakened due to extraordinary dividend payments to its owner banks. We view the latter scenario as unlikely, though, unless it occurs in conjunction with the sale of the company.

Rationale

The ratings and positive outlook on Eksportfinans point to our view of a likely increased possibility of an orderly wind-down of Eksportfinans in the coming two years. In our view, further reduction of the balance sheet, supported by the institution's exceptional capitalization, diminishes the likelihood of nonpayment of Eksportfinans' senior creditors. The institution still relies on a considerable share of structured products in its overall funding mix. However, the decrease in nonpayment risk due to the balance-sheet contraction, and the significant banks and government guarantees in place, largely offset this additional risk.

Anchor: 'a-' owing to high share of exposure in Norway and credit guarantees

We use our Banking Industry Country Risk Assessment's (BICRA's) economic risk and industry risk scores to determine a bank's anchor, the starting point in assigning an issuer credit rating. The anchor for Eksportfinans is 'a-', based on our economic risk score of '2' and industry risk score of '3' for Norway.

We differentiate between our outlook on Eksportfinans and the present negative trend we see in the Norwegian banking sector's economic risk. This distinction reflects our view that the guarantees by Eksportfinans' highly rated Norwegian government and owner banks mitigate the factors we consider in our BICRA that could contribute to a potential downward revision in the anchor for Norwegian banks.

Our assessment of low economic risk in Norway is supported by the country's wealthy government, underpinned in turn by returns from its global investment fund and a predictable political environment. The Norwegian economy is undergoing a structural transformation following the contraction in oil prices. As a result, the Norwegian krone has weakened, and its depreciation has helped increase the competitiveness of Norwegian exports. This has buoyed mainland GDP growth, in particular, while maintaining positive headline GDP growth. The Norwegian central bank has maintained an expansive monetary policy stance to support the country's structural shift. Low interest rates and competition between banks for mortgage loans, in addition to a shortage of housing in the greater Oslo region, has meant house prices in the area have increased at an accelerated pace. However, in the oil-concentrated Rogaland and Vestland regions, real estate prices have been much more subdued, underscoring the diverging regional developments and making targeted monetary policy difficult. Increasing asset values have led to further household debt growth, which continues to outpace disposable income growth and poses mounting risks for the economy, in our view. Bank losses, meanwhile, have been amplified over the past year as a result of the reduced level of investment in oil and oil-related sectors. That said, we believe the rise in credit losses will remain manageable for banks with diverse national exposures, given low levels of unemployment, the government's fiscal stimulus initiatives, and strong social safety nets.

Our view of industry risk is supported by Norway's banking regulator, which has proactively implemented relatively high capital requirements, in addition to improving banks' liquidity. It has also taken steps to introduce banking crisis legislation in 2018. We further note the government's track record and ability to provide impartial liquidity support to the sector. The market is dominated by DNB Bank, other Scandinavian banks, and domestic savings bank alliances, although we observe intense competition for market share in mortgage lending, which has depressed lending margins in recent years. Tentative signs of improved margins have surfaced, as banks look to increase lending margins and their funding costs improve. Restrictions on domestic investments by Norway's Government Pension Fund Global (GPFG) have resulted in a sizable outflow of capital, some of which is repatriated through banks' use of international wholesale funding. However, Norway's expanding bond market, banks' receipt of funding from foreign parent companies and likely liquidity support from the government help offset some of the risks from what we see as a structural lack of deposits.

Table 1

Eksportfinans ASA Key Figures

		--Year ended Dec. 31--				
(Mil. NOK)	**2017***	**2016**	**2015**	**2014**	**2013**	**2012**
Adjusted assets	23,993	33,170	65,140	85,626	100,788	157,397
Customer loans (gross)	11,823	17,270	24,462	33,372	47,363	71,879
Adjusted common equity	6,697	6,983	6,713	6,713	6,721	6,216
Operating revenues	(293)	(641)	(406)	(5,599)	(6,679)	(24,515)
Noninterest expenses	90	107	142	180	165	144
Core earnings	(287)	177	172	130	566	829

*Data as of Sept. 30. NOK--Norwegian krone.

Business position: Increasing cash flow stability following large debt maturities

Eksportfinans manages the wind-down of its balance sheet in an orderly fashion, facing a decreasing overall non-payment risk as loans continue to mature. In addition, compared with its peers, Eksportfinans benefits from important guarantee mechanisms from the Norwegian government and Nordic financial institutions.

Eksportfinans' ownership has been very stable over the past decade. The bank is owned by the Norwegian government (15%) and 23 banks (85%, with the main shareholders being DNB Bank ASA, Nordea Bank AB, and Danske Bank A/S, which together account for 71.3% of the capital.

The run-off of Eksportfinans' business is a consequence of the Norwegian government's decision in November 2011 to terminate the company's responsibility for commercial interest reference-rate loans under the Organisation for Economic Cooperation and Development's consensus agreement of 1978. Since then, the company has been in run-off, a process that will likely take several years, given the long-dated loans and financing on its balance sheet. We expect Eksportfinans' balance sheet, which amounted to Norwegian krone (NOK)23 billion ($2.8 billion) as of Sept. 30, 2017 will continue to reduce in line with the company's forecasts (see chart 1), and that its balance sheet will contract by about one-third annually over the coming two years as a substantial portion of the debt matures, further reducing the risk of nonpayment. Following the maturity of a consistent portion of outstanding loans in 2017, the company's balance-sheet size decreased by 28% compared with 2016, to representing just 11% of total assets at the end of 2011, just after Eksportfinans lost its government mandate.

Chart 1

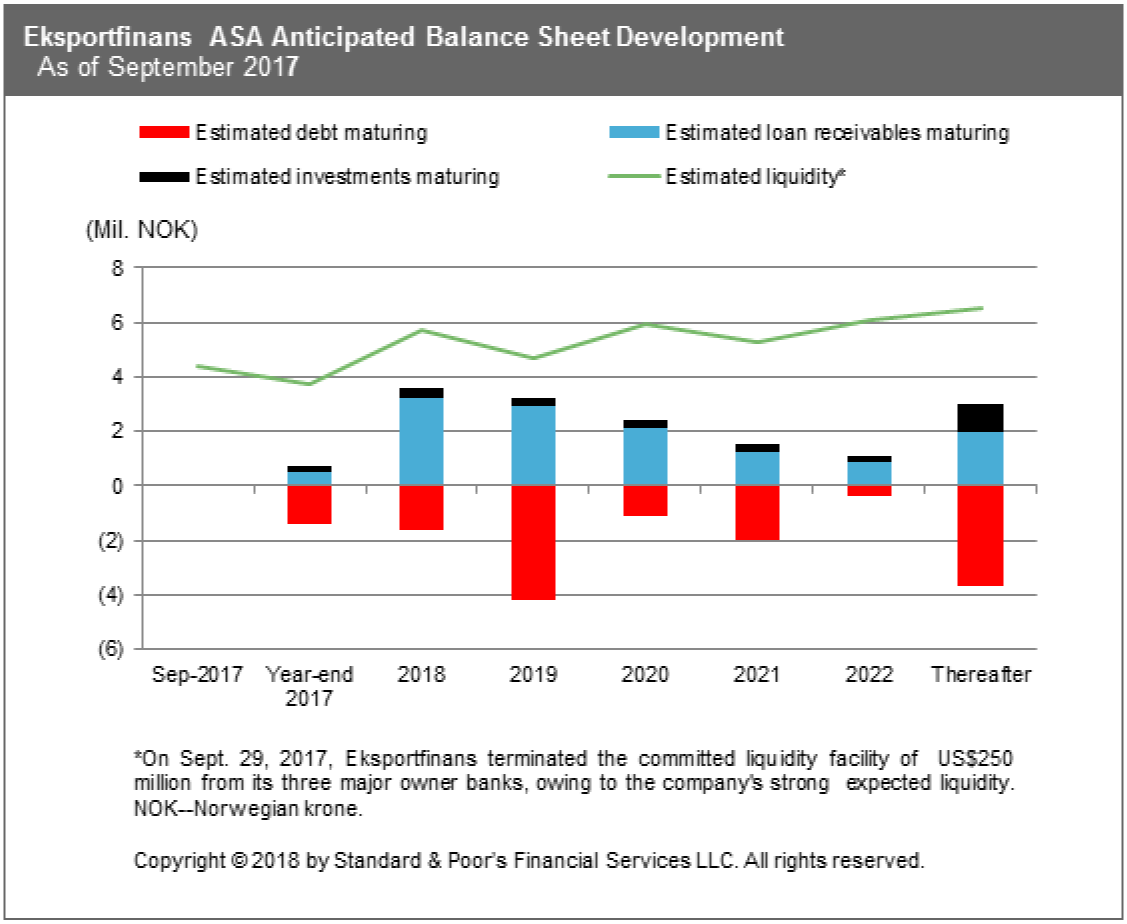

Table 2

Eksportfinans ASA Business Position

	--Year ended Dec. 31--					
(%)	**2017***	**2016**	**2015**	**2014**	**2013**	**2012**
Total revenues from business line (mil. NOK)	(293)	(401)	(438)	(406)	(5,599)	(6,679)
Commercial banking/total revenues from business line	100	100	100	100	100	100
Return on equity	0.5	2.3	2.3	1.8	8.0	13.0

*Data as of Sept. 30. NOK--Norwegian krona.

Capital and earnings: Very strong capital metrics, driven by continued balance-sheet reduction

We base our assessment of Eksportfinans' capital and earnings on its very robust capitalization. In addition, most of the company's assets carry low risk weights, given the guarantees by financial institutions with comparatively high ratings or by the Norwegian sovereign.

As of June 30, 2017, we measured Eksportfinans' risk-adjusted capital (RAC) ratio at 87.1%, compared with 74.1% at year-end 2016 (using our updated RAC methodology "Criteria - Financial Institutions - General: Risk-Adjusted Capital Framework Methodology," published July 20, 2017, on RatingsDirect) and 35.9% in 2015. This improvement was mostly due to a significant reduction in the liquidity reserve, outstanding loan contracts maturing, and a reduction in market risk associated with hold-to-maturity asset-backed securities in Eksportfinans' liquidity portfolio. By the end of 2018, we expect the RAC ratio will remain at over 100%, which is exceptionally high by global standards.

Based on its reporting under International Financial Reporting Standards, Eksportfinans has continued to show negative earnings. This is primarily due to the fluctuations in value of unrealized losses and gains related to its own debt. Excluding the effect of the revaluation of derivatives in the hold-to-maturity portfolio and the unwinding of unrealized gains on its own debt, the company's earnings in the first nine months of 2017 decreased versus the same period in 2016. Reasons for this are mostly the gains booked in the first half of 2016, related to a company's office property and lower net interest income in 2017. Nevertheless, these items do not materially affect our view of capital, since we exclude revaluation reserves from our measures, and considering the very high ratios and increasing share of equity in the balance sheet as assets unwind. In our view, the low returns on equity could accelerate an eventual acquisition or, less likely, a significant pay-out of capital at Eksportfinans.

Table 3

Eksportfinans ASA Capital And Earnings

		--Year ended Dec. 31--				
(%)	**2017***	**2016**	**2015**	**2014**	**2013**	**2012**
Tier 1 capital ratio	77.1	61.0	36.5	24.3	36.8	25.0
S&P Global Ratings' RAC ratio before diversification	N.M.	74.1	35.9	33.9	31.6	25.9
S&P Global Ratings' RAC ratio after diversification	N.M.	40.9	27.7	25.7	22.6	23.0
Adjusted common equity/total adjusted capital	100.0	100.0	100.0	100.0	100.0	100.0
Net interest income/operating revenues	(52.6)	(40.6)	(92.1)	(8.2)	(10.4)	(5.1)
Fee income/operating revenues	0.3	0.2	0.5	0	0	0
Market-sensitive income/operating revenues	152.2	140.9	195.1	108.4	110.5	105.3
Noninterest expenses/operating revenues	(30.7)	(16.7)	(35.0)	(3.2)	(2.5)	(0.6)
Preprovision operating income/average assets	(1.8)	(1.5)	(0.7)	(6.2)	(5.3)	(13.3)
Core earnings/average managed assets	(1.3)	0.4	0.2	0.1	0.4	0.4

*Data as of Sept. 30. RAC--Risk-adjusted capital. N.M.--Not meaningful.

Table 4

Eksportfinans ASA Risk-Adjusted Capital Framework Data As Of June 30, 2017

(NOK 000s)	**Exposure***	**Basel III RWA (2)**	**Average Basel III RW (%)**	**S&P Global Ratings' RWA**	**Average S&P Global Ratings' RW (%)**
Government and central banks	490,246	780,527	159	16,766	3
Institutions and CCPs	7,563,561	2,235,348	30	1,627,159	22
Corporate	13,825,828	3,038,072	22	1,510,789	11
Retail	0	0	0	0	0
Of which mortgage	0	0	0	0	0
Securitization§	139,013	27,800	20	69,507	50
Other assets†	311,423	2,423	1	775,890	249
Total credit risk	22,330,071	6,084,170	27	4,000,110	18
Total credit valuation adjustment	--	1,374,000	--	1,786,200	--

Table 4

Eksportfinans ASA Risk-Adjusted Capital Framework Data As Of June 30, 2017 (cont.)					
Equity in the banking book	0	0	0	0	0
Trading book market risk	--	866,263	--	1,299,394	--
Total market risk	--	866,263	--	1,299,394	--
Total operational risk	--	587,857	--	689,116	--
RWA before diversification	--	8,912,290	--	7,774,819	100
Total diversification/concentration adjustments	--	--	--	6,408,030	82
RWA after diversification	--	8,912,290	--	14,182,849	182
		Tier 1 capital	**Tier 1 ratio (%)**	**Total adjusted capital**	**S&P Global Ratings' RAC ratio (%)**
Capital ratio before adjustments		6,446,000	72.3	6,770,000	87.1
Capital ratio after adjustments‡		6,446,000	72.3	6,770,000	47.7

*Exposure at default. §Securitization exposure includes the securitization tranches deducted from capital in the regulatory framework. †Other assets includes deferred tax assets not deducted from adjusted common equity. ‡For Tier 1 ratio, adjustments are additional regulatory requirements (e.g. transitional floor or Pillar 2 add-ons). RWA--Risk-weighted assets. RW--Risk weights. RAC--Risk-adjusted capital. CCPs--Central counterparty clearing house. NOK--Norwegian krone. Sources: Company data as of June 30, 2017, S&P Global Ratings.

Risk position: High share of structured funding and counterparty concentrations

Our assessment of Eksportfinans' risk position reflects our view of the complexity of the company's structured funding, which comprises more than one-third of all bond debt at end-September 2017. In addition, Eksportfinans depends on access to the derivatives market to control risk.

Derivative risk management places considerable demands on the company's administrative and system resources, in our view. We understand that Eksportfinans' would have access to the key personnel of its major owner banks if it were to lose staff in risk functions associated with its funding or derivatives management.

We believe that strong government and bank guarantees continue to mitigate Eksportfinans' credit risk. Most of its loan portfolio is guaranteed either by the Norwegian Export Credit Guarantee Agency (40%) or Norwegian banks (40%). The majority of guarantees from Norwegian banks are provided by DNB Bank ASA (A+/Stable/A-1), which guaranteed 29% of outstanding loans as of Dec. 31, 2016. Given the guarantees, direct corporate risk exposure is limited, but the company is still exposed to a small number of key financial entities used to offload the risk inherent in its structured borrowings.

Furthermore, credit losses have been minimal over the company's operating history. Nonperforming loans decreased by 95% between September 2016 and September 2017 (from NOK614 million to NOK29 million). Moreover, at end-September 2017, all nonperforming loans were guaranteed either by the Norwegian government via the Guarantee Institute for Export Credits or by private banks, most of which operate in Norway.

Table 5

Eksportfinans ASA Risk Position						
		--Year ended Dec. 31--				
(%)	**2017***	**2016**	**2015**	**2014**	**2013**	**2012**
Growth in customer loans	(42.1)	(29.4)	(26.7)	(29.5)	(34.1)	(25.5)

Table 5

Eksportfinans ASA Risk Position (cont.)						
		--Year ended Dec. 31--				
(%)	2017*	2016	2015	2014	2013	2012
Total diversification adjustment / S&P Global Ratings' RWA before diversification	N.M.	81.08	29.5	31.8	39.9	12.8
Total managed assets/adjusted common equity (x)	3.58	4.8	9.5	12.8	15.0	25.3
Growth in adjusted assets	(36.9)	(49.1)	(23.9)	(15.0)	(36.0)	(26.4)
Gross nonperforming assets/customer loans + other real estate owned	0.2	0.5	2.1	1.6	0.4	0.9

*Data as of Sept. 30. RWA--Risk-weighted assets. N.M.--Not meaningful.

Funding and liquidity: Below average funding, given the uncertain nature of structured funding

We assess Eksportfinans' funding as below average and its liquidity position as adequate, resulting in a combined assessment of moderate. In our opinion, this balances the use of structured funding with uncertain maturities against the owners' stated willingness to assist in an orderly run-off.

In the company's baseline assumption of maturity of its balance sheet, excess cash flows are present throughout the unwinding (see chart 1 above).

Structured funding had reduced to about NOK7.2 billion as of end-September 2017, but remains at one-third of all outstanding debt.

More specifically, as of end-September 2017, almost 58% of the company's structured funding is subject to triggers and calls and, as such, has an uncertain maturity dependant on market movements and trends in interest rates, exchange rates, and stock prices, and which could deviate from the baseline scenario in chart 1 above. Contractually, these instruments are long term in nature, many expiring after 2021. However, the maturities could be materially shortened due to triggers associated primarily with currency movements between the U.S. dollar and the Japanese yen, the Australian dollar and the yen, and trends in the NIKKEI 225 equity index.

In 2017, Eksportfinans returned to the capital market by issuing NOK2 billion (about $245 million) of senior unsecured debt and by reactivating its €500 million commercial paper program, with NOK573 million outstanding as of end-September. The institution subsequently cancelled the $250 million credit facility granted by its main owner banks in September 2017, indicating increased leeway with its cash flow and an ability to manage liquidity squeezes during stages of the wind-down. In addition, we think Eksportfinans could create further liquidity by repurchasing or selling its less-liquid portfolio hedge agreement portfolio, if necessary.

The recent balance-sheet contraction and capital market issues have produced an improvement in our metrics for Eksportfinans, with the stable funding ratio up to 100.6% at the end of September 2017, after two years decreases in 2015 and 2016, at 73.4% and 67.8% respectively. Moreover, the ratio of broad liquid assets to short-term whole sale funding showed consistent improvement over the past 9 months, advancing to 1.57x at the end of September 2017 from 0.42x at year-end 2016. We previously did not incorporate the contingent liquidity represented by Eksportfinans' liquidity facility in our funding and liquidity ratios.

In our metrics, we assume that all loans require stable funding over one year, which is less relevant for a company in run-off. We expect that loans maturing from the end of 2017 on will mature without complications and reduce the balance sheet according to the company's forecast. Lastly, we do not see material cash flow risks given the current improvements in the company's liquidity and funding ratios.

Table 6

Eksportfinans ASA Funding And Liquidity						
		--Year ended Dec. 31--				
(%)	2017*	2016	2015	2014	2013	2012
Core deposits/funding base	0	0	0	0	0	0
Long-term funding ratio	87.8	60.3	48.7	72.9	75.4	66.6

*Data as of Sept. 30.

External support: No notches included in the rating despite strong owners

The Norwegian government's decision in November 2011 to terminate the company's responsibility for commercial interest reference-rate loans support our conclusion that Eksportfinans has low systemic importance in Norway's banking sector.

Additional rating factors: None

No additional factors affect this rating.

Related Criteria

- Criteria - Financial Institutions - General: Risk-Adjusted Capital Framework Methodology, July 20, 2017
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- Criteria - Financial Institutions - Banks: Quantitative Metrics For Rating Banks Globally: Methodology And Assumptions, July 17, 2013
- Criteria - Financial Institutions - Banks: Banks: Rating Methodology And Assumptions, Nov. 9, 2011
- Criteria - Financial Institutions - Banks: Banking Industry Country Risk Assessment Methodology And Assumptions, Nov. 9, 2011
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009
- Criteria - Financial Institutions - Banks: Commercial Paper I: Banks, March 23, 2004

Related Research

- Norway-Based Eksportfinans Outlook Revised To Positive On Continued Balance Sheet Contraction; Affirmed At 'BBB+/A-2', Nov. 23, 2017
- Banking Industry Country Risk Assessment: Norway, March 14, 2017

Anchor Matrix

Industry Risk	Economic Risk									
	1	**2**	3	4	5	6	7	8	9	10
1	a	a	a-	bbb+	bbb+	bbb	-	-	-	-
2	a	a-	a-	bbb+	bbb	bbb	bbb-	-	-	-
3	a-	**a-**	bbb+	bbb+	bbb	bbb-	bbb-	bb+	-	-
4	bbb+	bbb+	bbb+	bbb	bbb	bbb-	bb+	bb	bb	-
5	bbb+	bbb	bbb	bbb	bbb-	bbb-	bb+	bb	bb-	b+
6	bbb	bbb	bbb-	bbb-	bbb-	bb+	bb	bb	bb-	b+
7	-	bbb-	bbb-	bb+	bb+	bb	bb	bb-	b+	b+
8	-	-	bb+	bb	bb	bb	bb-	bb-	b+	b
9	-	-	-	bb	bb-	bb-	b+	b+	b+	b
10	-	-	-	-	b+	b+	b+	b	b	b-

Ratings Detail (As Of January 18, 2018)

Eksportfinans ASA	
Counterparty Credit Rating	BBB+/Positive/A-2
Commercial Paper	
Local Currency	A-2
Senior Unsecured	BBB+
Short-Term Debt	A-2
Counterparty Credit Ratings History	
23-Nov-2017	BBB+/Positive/A-2
28-Nov-2016	BBB+/Stable/A-2
29-Feb-2016	BBB/Positive/A-2
05-Dec-2014	BBB-/Positive/A-3
20-May-2014	BB+/Positive/B
31-Mar-2014	BB+/Negative/B
26-Mar-2014	BB+/Watch Neg/B
Sovereign Rating	
Norway (Kingdom of)	AAA/Stable/A-1+

*Unless otherwise noted, all ratings in this report are global scale ratings. S&P Global Ratings' credit ratings on the global scale are comparable across countries. S&P Global Ratings' credit ratings on a national scale are relative to obligors or obligations within that specific country. Issue and debt ratings could include debt guaranteed by another entity, and rated debt that an entity guarantees.

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