S&P Global Ratings

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Central Bank of Savings Banks Finland Plc

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Central Bank of Savings Banks Finland Plc

*(**Editor's Note:** The scores below relate to the GCP, leading to an ICR of 'BBB+/Stable/A-2' on core group members. GCP--Group credit profile. ICR--Issuer credit rating.)*

SACP	bbb+	
Anchor	a-	
Business Position	Weak	-2
Capital and Earnings	Very Strong	+2
Risk Position	Moderate	-1
Funding	Average	0
Liquidity	Adequate	

+

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

+

Additional Factors	0

Issuer Credit Rating
BBB+/Stable/A-2

Major Rating Factors

Strengths:	Weaknesses:
• Very strong capitalization. • Low-risk lending profile and high collateralization. • Mutual business model.	• Concentrated business operations. • Limited geographic presence in Finland's growth centers. • Limited business and earnings diversification.

Outlook: Stable

S&P Global Ratings' stable outlook on Central Bank of Savings Banks Finland PLC (Sp Central Bank) reflects our view that the Saving Bank Group's strategic development and capital levels counterbalance what we see as a weak economic recovery in Finland's export-oriented economy, which could undermine the Finnish banking sector's performance during the next two years.

We could revise the outlook on Sp Central Bank to negative if we saw that the integration within the group was being hampered, such that the group's future growth prospects became restricted.

Given our view of potentially increasing economic imbalances in Finland, we view a positive rating action as unlikely.

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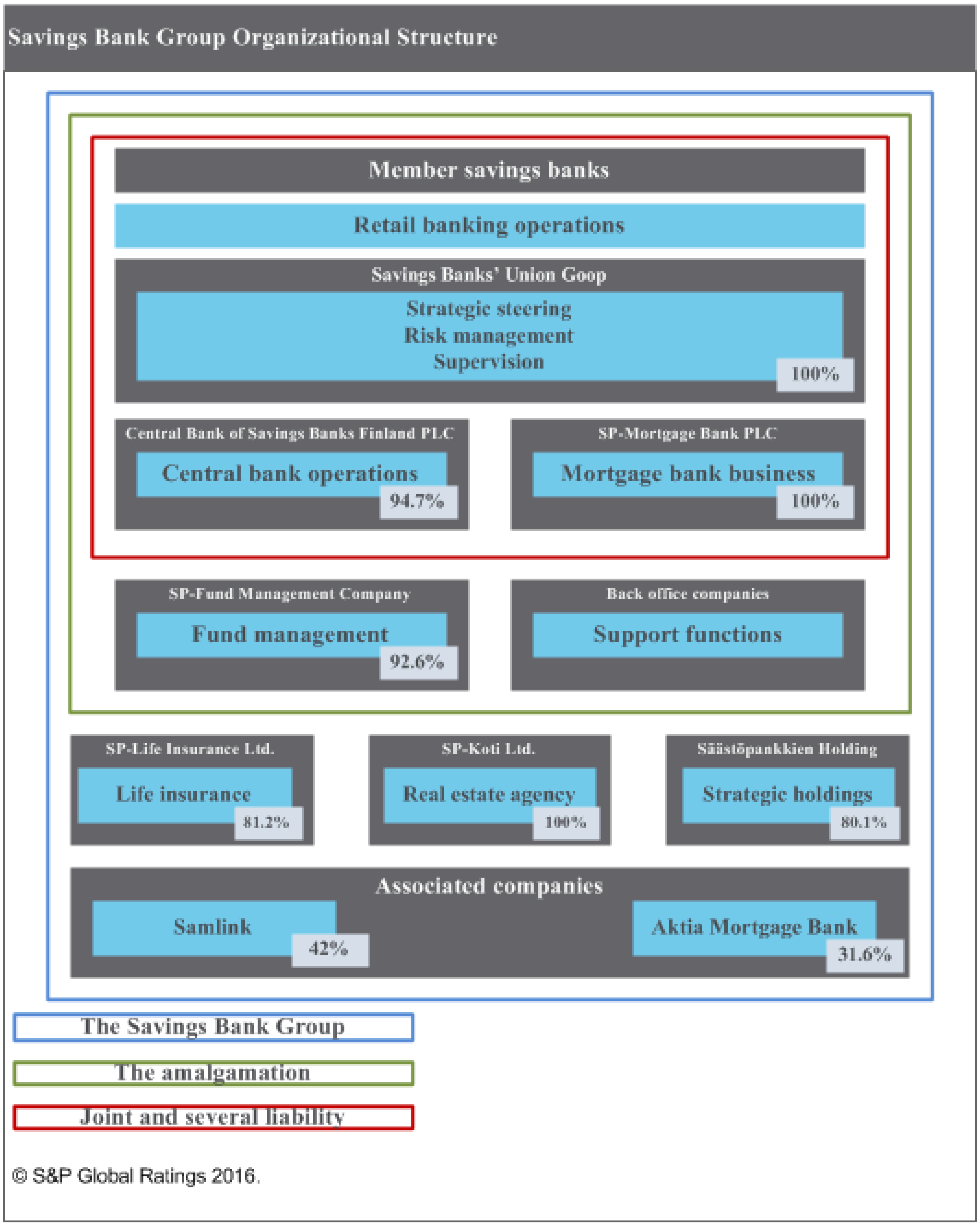
Rationale

Sp Central Bank is the central credit institution of Savings Bank Group, and the ratings therefore reflect the wider group's franchise and creditworthiness. Since December 2014, the group's 23 member savings banks, the Savings Banks' Union Coop, and Sp Central Bank have operated as a single entity for regulatory purposes under a joint and several guarantee scheme established by Finland's Act on Amalgamation. Under the joint and several liability scheme, the member institutions share liability for each other's debt.



The long-term rating on Sp Central Bank reflects our 'a-' anchor for Finnish banks, and Savings Bank Group's weak business position based on its concentrated business operations, focused primarily on retail mortgages and lending to small and midsize enterprises (SME), and its short track record of operating as an amalgamation. The long-term rating also reflects the group's very strong capital and earnings, mainly due to our expectation of an increase in our risk-adjusted capital (RAC) ratio to about 16.0% by year-end 2016. The rating equally reflects the group's moderate risk position, due to concentration risks in its loan book, partly mitigated by a high level of collateralization; its average funding and adequate liquidity, owing to sound funding metrics; its funding profile, dominated by customer deposits; and its comfortable liquidity position. We assess the unsupported group credit profile (GCP) at 'bbb+'.

In terms of customer deposits, Savings Bank Group is the fourth-largest banking group in Finland, with a 5% share of customer deposits. We therefore consider the group to have moderate systemic importance in Finland. However, we believe that the prospects for extraordinary government support appear uncertain for banks in Finland, and we no longer factor any such support into the GCP.

We view Sp Central Bank as integral to the Savings Bank Group's operation, and therefore equalize our long-term rating on Sp Central Bank with the unsupported GCP.

Anchor: 'a-' for banks operating only in Finland

We use our Banking Industry Country Risk Assessment's economic risk and industry risk scores to determine a bank's anchor, the starting point in assigning an issuer credit rating under our criteria. Our anchor for a commercial bank operating only in Finland is 'a-', based on an economic risk score of '2' and an industry risk score of '3'.

We view Finland as a competitive and resilient economy with high education levels. However, the country depends on exports of investment goods, and therefore on cyclical industries or sectors, and its economy is subject to sub-par growth due to the fragile recovery in Europe. Moreover, lack of reforms to increase competiveness could pressure the economy. Low corporate and moderate household debt, and a very strong payment culture, contribute to sound leverage.

Diverse Nordic banking groups largely control Finland's concentrated banking industry, which in our view is underpinned by robust profitability and stability. Deposits dominate funding, but the sector is a net external debtor, reflecting significant loan growth over the past decade and the country's lack of a deep domestic debt market.

Table 1

Savings Bank Group Key Figures

	--Year-ended Dec. 31--		
(Mil. €)	**2015**	**2014**	**2013**
Adjusted assets	8,588.4	7,942.3	7,358.4
Customer loans (gross)	6,338.6	5,648.9	5,301.4
Adjusted common equity	860.0	821.3	763.8
Operating revenues	232.7	226.7	226.3
Noninterest expenses	156.9	153.0	149.4
Core earnings	57.6	46.6	66.0

Business position: Concentrated business model and still-low presence in Finnish growth centers

We consider Savings Bank Group's business position to be weak, reflecting the group's concentrated business model, its still-weak franchise in growth centers, and its short track record of operating as cohesive banking group.

Savings Bank Group is a midsize banking group in Finland, with total assets of €9.2 billion as of Dec. 31, 2015. The group consists of 23 member savings banks; Sp Central Bank (covering central bank operations); Savings Banks' Union Coop (the central institution in charge of strategic steering, risk management, and supervision); and specialized institutions, such as Sp Fund Management Company and Sp Life Insurance. While the savings banks belong to the oldest banks in Finland, the current integrated banking group was only created under the amalgamation act in December 2014. Due to the very small size of some of the member banks, we expect to see mergers within the amalgamation in the coming two years, as the group puts more emphasis on efficiency.

The group has a sound retail franchise, with a countrywide branch network and some 470,000 customers. Although the group holds a stable market share of 4.6% in customer lending and 4.8% in customer deposits, we consider the group's still-limited presence in domestic growth centers as a weakness. We understand that the group targets expansion into such regions, but we consider this challenging given the harsher competition and well-established presence of larger players. By customer group, we understand that the group will focus on young adults, families, and savers in the private customer group, and on small businesses, self-employed professionals, and forestry and agricultural customers in the SME group. Sp Central Bank started credit card operations in December 2015 by acquiring the credit card portfolio of its customers from Nets Ltd., and will in future act as card issuer for the Savings Bank Group.

In our view, Savings Bank Group's geographic concentration and narrow product focus on mainly residential mortgage lending and SME lending represent the main weaknesses of the business model. These factors may expose the bank to potential volatility in the real estate market in Finland, or to a downturn in the Finnish economy.

The group's asset management and life insurance companies expand its product offering, and we expect their contribution to revenues to increase over time from a combined 15% of operating revenues and 30% of operating profit as of Dec. 31, 2015. Due to their limited size and low market shares in fund savings and insurance savings in Finland, in our view the asset management and insurance operations currently bring only marginal diversification benefits to the group.

Savings Bank Group's revenues consist of interest income (50%-55% of total income), fee and commission income (30% of total income), and other income (about 15% of income)--a split that we expect will remain unchanged in the coming years.

We consider that Savings Bank Group shares prudent strategy and risk policies, in line with its domestic peers. The group's strategy and risk management are steered by the central institution, Savings Banks Union Coop. We observe that the group is making good progress in establishing a group-wide risk culture and guidelines. We believe that despite its ambitions to grow the franchise over the coming years, the group will maintain a low risk appetite and conservative lending standards, which we expect will provide stability to its financial position. Although Savings Bank Group still has a fairly short track record of operating as a cohesive banking group, we regard its legal set-up as a mutual group as positive. We believe that this set-up will support the group's long-term financial targets, and that it aligns well with the group's prudent approach to managing risks.

Table 2

Savings Bank Group Business Position			
	--Year-ended Dec. 31--		
(%)	**2015**	**2014**	**2013**
Loan market share in country of domicile	4.6	4.7	N/A
Deposit market share in country of domicile	4.8	4.9	N/A
Total revenues from business line (currency in millions)	232.7	226.7	226.3
Commercial & retail banking/total revenues from business line	86.9	99.0	88.4
Asset management/total revenues from business line	14.9	5.4	5.9
Other revenues/total revenues from business line	(1.8)	(4.4)	5.8
Return on equity	6.7	5.8	N/A

N/A--Not applicable.

Capital and earnings: Very strong capitalization, underpinned by stable earnings

We assess Savings Bank Group's capital and earnings as very strong. This is primarily due to our expectation that our RAC ratio for Savings Bank Group will grow to about 16% by year-end 2016, mainly due to profit retention, compared with 15.7% on Dec. 31, 2015. The redemption of the investment in wind-down entity Aktia Real Estate Mortgage Bank in early 2017 will increase the RAC ratio to above 18% by year-end 2017.

In our view, Savings Bank Group's earnings are relatively stable, driven by the sound retail and SME franchise. We expect that the group will be able to maintain healthy margins in new loans, resulting in overall net interest margins of 1.55%-1.60% (versus 1.67%-1.71% in 2014-2015) in the loan portfolio in 2016-2017. Combined with lower funding costs, this should support relatively stable net interest income. Furthermore, we anticipate improving net fee and commission income, driven by fees from payment transfers, lending, and mutual funds (up by 8% in 2015). We estimate net profits of €60 million-€65 million in 2016-2017 (€58 million in 2015). This will, in our view, enable steady capital build-up, because the profits are almost fully retained.

We expect moderate loan growth of 3% in Savings Bank Group's loan origination, owing to still-sluggish demand for mortgage and consumer loans in Finland. Furthermore, we expect that Savings Bank Group will transfer its share of loans from Aktia Real Estate Mortgage Bank (AREMB), estimated at €360 million as of June 2016, to its own balance sheet by the end of 2016, leading to the repayment of the group's investment in AREMB. This, combined with anticipated annual loan growth of 3%, will lead to an increase in credit risk-weighted assets (RWAs) of 9% in 2016 and 3% in 2017, and to a substantial decrease in market risk RWAs related to Savings Bank Group's declining stake in AREMB.

A revision of our view of currently low economic risk in Finland would lead us to lower our RAC ratio on Savings Bank Group because we would use higher risk weights on exposures in our calculation. However, we do not think that such a scenario would change our assessment of the bank's very strong capital and earnings, underpinned by a projected RAC ratio that is well beyond 15%.

We consider Savings Bank Group's quality of capital, consisting mainly of paid-in capital, and its earnings, to be adequate. Our projection does not currently include issuance of additional loss-absorbing capital. We expect that the group's earnings capacity will improve over time, owing to stable operating revenues and expenses and our expectation of low loan losses. This is reflected in the improving three-year average earnings buffer of about 110 basis points (bps) for the group, which is approaching that of the group's peer Nordic regional banks.

The amalgamation of Savings Bank Group comfortably fulfils regulatory capital requirements, with a common equity tier 1 capital ratio of 17.8% as of Dec. 31, 2015.

Table 3

Savings Bank Group Capital And Earnings

	--Year-ended Dec. 31--		
(%)	2015	2014	2013
Tier 1 capital ratio	17.8	16.9	15.8
S&P RAC ratio before diversification	15.7	15.0	N.M.
S&P RAC ratio after diversification	13.5	12.3	N.M.
Adjusted common equity/total adjusted capital	100.0	100.0	100.0
Net interest income/operating revenues	53.7	53.8	48.9
Fee income/operating revenues	29.6	28.0	26.0
Market-sensitive income/operating revenues	8.2	10.6	11.3
Noninterest expenses/operating revenues	67.4	67.5	66.0
Preprovision operating income/average assets	0.9	0.9	N/A
Core earnings/average managed assets	0.7	0.6	N/A

N/A--Not applicable. N.M.--Not meaningful.

Table 4

Savings Bank Group Risk-Adjusted Capital Framework Data

	Exposure*	Basel II RWA	Average Basel II RW (%)	Standard & Poor's RWA	Average Standard & Poor's RW (%)
Credit risk					
Government and central banks	755,323,673	464,786	0	42,590,483	6
Institutions	182,792,696	79,826,213	44	31,388,082	17
Corporate	623,155,811	867,793,206	139	402,379,339	65
Retail	6,554,920,274	2,367,819,591	36	2,097,028,446	32
Of which mortgage	4,814,062,054	1,542,079,451	32	1,155,963,571	24
Securitization§	0	0	0	0	0
Other assets	310,097,979	266,118,588	86	238,762,541	77
Total credit risk	8,426,290,432	3,582,022,384	43	2,812,148,890	33
Market risk					
Equity in the banking book†	543,966,786	620,464,297	125	1,875,403,488	345
Trading book market risk	--	47,482,749	--	71,224,123	--
Total market risk	--	667,947,045	--	1,946,627,611	--
Insurance risk					
Total insurance risk	--	--	--	302,202,150	--
Operational risk					
Total operational risk	--	393,758,788	--	415,939,445	--

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Table 4

Savings Bank Group Risk-Adjusted Capital Framework Data (cont.)

	Basel II RWA		Standard & Poor's RWA	% of Standard & Poor's RWA
Diversification adjustments				
RWA before diversification	4,643,728,218		5,476,918,097	100
Total Diversification/Concentration Adjustments	--		906,242,665	17
RWA after diversification	4,643,728,218		6,383,160,762	117
	Tier 1 capital	**Tier 1 ratio (%)**	**Total adjusted capital**	**Standard & Poor's RAC ratio (%)**
Capital ratio				
Capital ratio before adjustments	824,531,254	17.7	859,961,000	15.7
Capital ratio after adjustments‡	824,531,254	17.8	859,961,000	13.5

*Exposure at default. §Securitization exposure includes the securitization tranches deducted from capital in the regulatory framework. †Exposure and Standard & Poor's risk-weighted assets for equity in the banking book include minority equity holdings in financial institutions. ‡Adjustments to Tier 1 ratio are additional regulatory requirements (e.g. transitional floor or Pillar 2 add-ons). RWA--Risk-weighted assets. RW--Risk weight. RAC--Risk-adjusted capital. Sources: Company data as of Dec. 31, 2015, Standard & Poor's.

Risk position: Concentration risk, due to a focus on retail mortgage and SME lending in Finland

We view Savings Bank Group's risk position as moderate. This reflects concentration risk in the group's loan book, which, in our view, exposes it to potential volatility in the domestic real estate market and a potential downturn in the Finnish economy.

Saving Bank Group focuses mainly on low-risk lending to private customers (74% of the portfolio), SMEs (18% of the portfolio), and agricultural and forestry clients (about 9% of the portfolio), based on prudential underwriting standards. However, we still consider that the regionally focused retail mortgage loan book amounting to €4.1 billion (66% of the total loan book) exposes the bank to concentration risk and makes it vulnerable to real estate price developments in Finland. The concentration is partly mitigated by the retail loan book's high granularity and adequate collateralization. We note that about 7% of the total loan stock has loan-to-value ratios above 80% and 15% above 70%, which is somewhat weaker than Saving Bank Group's other rated Finnish peers.

In our view, Savings Bank Group's SME loan book of €1.1 billion does not show significant single-name or sector concentration, and is highly collateralized by residential and other real estate collateral (87.5%), or by other collateral (11%). We believe that these exposures are adequately captured in our RAC framework.

We expect that Savings Bank Group will maintain its prudential risk culture and underwriting standards, especially in mortgage lending. The central institution monitors the risk indicators and the application of unified underwriting standards within the amalgamation. The member institutions have no trading operations. Consequently, we believe that the group's asset quality will remain sound over the next two years. The ratio of nonperforming loans was 1.03% of customer loans on Dec. 31, 2015, which, in our view, reflects the group's portfolio structure.

Despite our view of growing economic imbalances in the Finnish household sector, we expect that Savings Bank Group will maintain a low level of credit losses, at about 9-11 bps over the next two years (10 bps in 2015 and 19 bps in 2014 due to the harmonizing of the group impairment policy). This is in line with the average impairments of the amalgamation in 2004-2014. We believe that the potential increase in credit losses could result from the group's SME exposures, rather than from the private customer portfolio.

Table 5

Savings Bank Group Risk Position			
	--Year-ended Dec. 31--		
(%)	**2015**	**2014**	**2013**
Growth in customer loans	12.2	6.6	N.M.
Total diversification adjustment / S&P RWA before diversification	16.5	22.2	N.M.
Total managed assets/adjusted common equity (x)	10.7	10.2	10.1
New loan loss provisions/average customer loans	0.1	0.2	N/A
Net charge-offs/average customer loans	0.1	0.2	N/A
Gross nonperforming assets/customer loans + other real estate owned	1.0	1.1	1.1
Loan loss reserves/gross nonperforming assets	39.9	N/A	N/A

N/A--Not applicable. N.M.--Not meaningful.

Funding and liquidity: Stable customer deposits dominate the funding profile

We consider Savings Bank Group's funding to be average. Our view is based on the group's sound retail franchise and proximity to customers that should continue to provide the group with a comparably stable and granular inflow of deposits (78% of the funding base). Savings Bank Group holds a healthy market share of about 5% in the customer deposits in Finland. A major part of the customer deposits comes from households, followed by SME clients. Therefore, we expect Savings Bank Group's stable funding ratio will remain at a comfortable level of about 105%-110% over 2016-2017 (106% as of Dec. 31, 2015).

We believe that Savings Bank Group has diversified its funding mix by tapping the capital market through an unsecured issuance under its €2 billion euro medium-term note program, and from 2016, through a secured issuance by launching covered bond operations at Sp-Mortgage Bank. This will allow the group to accelerate its loan growth, following sluggish development over the past two years caused by funding constraints. In our view, the group's funding mix will continue to represent a relatively balanced asset-liability structure, demonstrated by a long-term funding ratio of about 92% that is in line with the ratios of its domestic competitors. Following the transfer of the assets from AREMB, the group's loan-to-deposit ratio has slightly weakened to 107%, but still remains below that of domestic peers operating purely in retail banking.

Our assessment of Savings Bank Group's liquidity as adequate mirrors our estimate of the bank's one-year liquidity ratio (broad liquid assets to short-term funding) at 1.8x as of Dec. 31, 2015. On this date, the group had a liquidity position of about €1.2 billion, consisting mainly of cash and securities, which we understand to a high extent are eligible for repurchase (repo) agreement transactions at the Finnish Central Bank. Consequently, we believe that in a severe liquidity crisis involving the closure of access to capital market funding and a significant deposit outflow, Savings Bank Group could survive for more than 12 months with access to the central bank through the repo activity in its liquidity book.

Table 6

Savings Bank Group Funding And Liquidity			
	--Year-ended Dec. 31--		
(%)	2015	2014	2013
Core deposits/funding base	78.2	83.2	86.7
Customer loans (net)/customer deposits	106.7	97.3	94.5
Long term funding ratio	91.9	92.2	93.9
Stable funding ratio	105.8	108.3	108.1
Short-term wholesale funding/funding base	9.1	8.8	6.8
Broad liquid assets/short-term wholesale funding (x)	1.8	2.0	2.3
Net broad liquid assets/short-term customer deposits	9.6	11.4	11.2
Short-term wholesale funding/total wholesale funding	41.6	52.1	51.1
Narrow liquid assets/three-month wholesale funding (x)	3.0	4.2	3.2

External support:No notches of uplift to the group credit profile

In terms of customer deposits, Savings Bank Group is the fourth-largest banking group in Finland, with a share of almost 5% in customer deposits. We therefore consider Savings Bank Group to have moderate systemic importance in Finland

We believe that the prospect of extraordinary government support for Finnish banks is now uncertain, following the full implementation of the EU Bank Recovery and Resolution Directive, including bail-in powers. We therefore classify Finland's tendency to support private sector commercial banks as uncertain.

We view the Finnish resolution regime as effective under our additional loss-absorbing capacity (ALAC) criteria because, among other factors, we believe it contains a well-defined bail-in process under which authorities would permit non-viable systemically important banks to continue critical functions as going concerns following a bail-in of eligible liabilities. That said, the Finnish authorities have not identified Savings Bank Group as subject to a well-defined bail-in process, which is a pre-condition for us to include ALAC support into our ratings on a bank.

Additional rating factors: None

No additional factors affect this rating.

Related Criteria And Research

Related Criteria

- Bank Rating Methodology And Assumptions: Additional Loss-Absorbing Capacity, April 27, 2015
- Group Rating Methodology, Nov. 19, 2013
- Quantitative Metrics For Rating Banks Globally: Methodology And Assumptions, July 17, 2013
- Revised Market Risk Charges For Banks In Our Risk-Adjusted Capital Framework, June 22, 2012
- Banks: Rating Methodology And Assumptions, Nov. 9, 2011
- Banking Industry Country Risk Assessment Methodology And Assumptions, Nov. 9, 2011
- Bank Capital Methodology And Assumptions, Dec. 6, 2010
- Methodology For Mapping Short- And Long-Term Issuer Credit Ratings For Banks, May 4, 2010
- Use Of CreditWatch And Outlooks, Sept. 14, 2009

- Commercial Paper I: Banks, March 23, 2004

Related Research

- Banking Industry Country Risk Assessment Update: May 2016, May 17, 2016
- Nordic Banks Stay Resilient To Negative Rate Noir, March 24, 2016
- Banking Industry Country Risk Assessment: Finland, Jan. 25, 2016
- Central Bank of Savings Banks Finland Downgraded To 'BBB+' On Government Support And ALAC Review; Outlook Stable, Dec. 2, 2015
- Central Bank of Savings Banks Finland Ltd. Rated 'A-/A-2'; Outlook Negative, April 7, 2015
- Nordic Banks Extend Their Capital Advantage Despite Lower Revenues, Nov. 27, 2015

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 May 23, 2016)

Central Bank of Savings Banks Finland Plc	
Counterparty Credit Rating	BBB+/Stable/A-2
Senior Unsecured	BBB+
Counterparty Credit Ratings History	
02-Dec-2015	BBB+/Stable/A-2
07-Apr-2015	A-/Negative/A-2
Sovereign Rating	
Finland (Republic of)	AA+/Negative/A-1+

*Unless otherwise noted, all ratings in this report are global scale ratings. Standard & Poor's credit ratings on the global scale are comparable across countries. Standard & Poor's 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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