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Research Update:

Denmark-Based Jyske Bank Ratings Affirmed At 'A-/A-2'; Outlook Stable

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Table Of Contents

Overview

Rating Action

Rationale

Outlook

Ratings Score Snapshot

Related Criteria

Related Research

Ratings List

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Overview

- Jyske Bank continues to focus its growth initiatives on residential mortgage lending, thereby gradually reducing the overall risk profile of the loan book.
- In addition, we expect Jyske Bank will maintain a risk-adjusted capital (RAC) ratio higher than 10%, despite a significant amount of share buybacks and dividends.
- We are affirming our 'A-/A-2' ratings on Jyske Bank and its core subsidiary BRFkredit.
- The stable outlook reflects our expectation that the RAC ratio will not decline below 10% and that Jyske Bank's funding and liquidity profile and the quality of its assets will not deteriorate materially over our two-year rating horizon.

Rating Action

On June 20, 2017, S&P Global Ratings affirmed its 'A-' long-term and 'A-2' short-term counterparty credit ratings on Denmark-based Jyske Bank A/S and its core subsidiary BRFkredit. The outlooks on both entities remain stable.

Rationale

The affirmation reflects our expectation that Jyske Bank will maintain a risk-adjusted capital (RAC) ratio above 10% and that the overall quality of its assets will continue to improve as it increases the share of retail mortgage lending, primarily targeting existing clients. Jyske Bank plays a significant role in the Danish banking sector and has wide business diversity. We expect its capital and earnings performance will remain strong as it increases cost efficiency and scale, and that improvements in its asset quality will track developments in the Danish economy.

We expect Jyske Bank's RAC ratio will remain a strength at 10.5%-11.0% over the next two years, showing a slight improvement from 10.3% on Dec. 31, 2016, supported by strengthening of the risk profile of its lending assets. The bank is undergoing a capital optimization exercise through 2017 that includes share buybacks and dividend distributions. We have excluded the current buy-back program of Danish krone (DKK) 500 million (about €70 million), which runs from March to September 2017, from our year-end 2016 capital ratios. For our RAC ratio forecast, we assume total distributions of about 60% of net profit over the next two years. In our view, high capital distributions combined with

material loan growth could be a risk to the ratings. We view the quality of capital as high, with hybrids representing only 5% of the capital included in our RAC ratio calculation, and note that Jyske Bank has significant flexibility to reduce dividends and share buybacks if necessary.

We consider Jyske Bank's funding to be average and liquidity to be adequate. The group's funding profile is similar to that of domestic peers Danske Bank and Nordea Bank Danmark, which consolidate bank and mortgage financing in the group metrics. The group's stable funding ratio was 94% in March 2017, a decline from 98.6% in December 2016, mainly due to the increasing share of mortgage lending and higher share of debt maturing within one year at BRFkredit, the core mortgage bank subsidiary. We note a reduction in the volume of one-year covered bond refinancing, the structural support of the Danish covered bond market, as well as the soft-bullet nature of Danish covered bonds since the passage of a Danish law that took effect in April 2014 (see "Credit FAQ: Why Denmark's Proposed Covered Bond Law Doesn't Fully Eradicate Refinancing Risks," published Feb. 4, 2014, on RatingsDirect). Our one-year liquidity ratio (broad liquid assets to short-term wholesale funding) was 0.85x for Jyske Bank in March 2017, down from 1.05x in December 2016. We expect stabilization of the group's funding and liquidity metrics as BRFkredit's legacy bond series mature and BRFkredit smoothes its debt maturity profile.

Jyske Bank's asset quality continues to improve as the share of residential mortgage loans increases. In addition, BRFkredit's collateralized loan book provides regional and product diversification to Jyske Bank's loan book. Although nonperforming loans (NPLs) remain higher than the market average (5% in March 2017), we believe that risks associated with loans in the agricultural sector are well provisioned. Moreover, we see improvements in the commercial and residential real estate markets enhancing loan asset quality. We believe that reversals of previous loan loss reserves could materially reduce the impact of new loan loss provisions, which we project will be in 10 basis points to 15 basis point range over the next year or two.

In March 2017, Jyske Bank's consolidated assets totaled DKK570 billion, placing the bank just outside Europe's top-50 banks by size. The Jyske Bank group is the fourth-largest lender in Denmark and has a market share of about 10% in loans and core customer deposits, reflecting significant growth in mortgage lending since 2014. Despite a less commanding market position than the top players, Jyske Bank's retail banking and mortgage lending provide diverse revenue streams and nationwide coverage. We anticipate that the bank will continue to strive toward the higher cost efficiency seen in its Nordic peer group, which should result in aftertax returns on equity within the bank's official guidance of 8%-12%.

We align our ratings and outlook on BRFkredit with those on Jyske Bank because we view BRFkredit as a core subsidiary, since it is a vital part of Jyske Bank's future funding strategy for Danish residential and commercial mortgage loans. This is in line with how we see other banking group structures and covered bond-issuing subsidiaries in Denmark and the Nordics.

Outlook

The stable outlook reflects our view that Jyske Bank will maintain a RAC ratio sustainably above 10%, including our projected payout ratio and the bank's growth plans, balanced by the generally slow development of the Danish market and still low-margin environment.

Although presently unlikely, we could consider an upgrade if bail-in risks for senior unsecured creditors were reduced by the bank's development of a significant additional loss-absorbing capacity buffer.

We could consider a downgrade if capital distributions or volume growth were higher than expected or there was a material acquisition, resulting in the RAC ratio declining below 10%. We could also lower the ratings if Jyske Bank's asset quality metrics were to weaken, leading us to take a negative view of the bank's combined risk and capital position, or if Jyske Bank's funding and liquidity profile were to deteriorate significantly.

Ratings Score Snapshot

Counterparty Credit Rating	A-/Stable/A-2
SACP	a-
Anchor	bbb+
Business Position	Adequate (0)
Capital and Earnings	Strong (+1)
Risk Position	Adequate (0)
Funding and Liquidity	Average and (0)
	Adequate
Support	(0)
ALAC Support	(0)
GRE Support	(0)
Group Support	(0)
Sovereign Support	(0)
Additional Factors	(0)

Related Criteria

- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings , April 7, 2017
- General Criteria: S&P Global Ratings' National And Regional Scale Mapping Tables, June 1, 2016

- Criteria - Financial Institutions - Banks: Bank Rating Methodology And Assumptions: Additional Loss-Absorbing Capacity, April 27, 2015
- Criteria - Financial Institutions - Banks: Bank Hybrid Capital And Nondeferrable Subordinated Debt Methodology And Assumptions, Jan. 29, 2015
- General Criteria: National And Regional Scale Credit Ratings, Sept. 22, 2014
- General Criteria: Group Rating Methodology, Nov. 19, 2013
- Criteria - Financial Institutions - Banks: Quantitative Metrics For Rating Banks Globally: Methodology And Assumptions, July 17, 2013
- Criteria - Financial Institutions - Banks: Revised Market Risk Charges For Banks In Our Risk-Adjusted Capital Framework, June 22, 2012
- 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
- Criteria - Financial Institutions - Banks: Bank Capital Methodology And Assumptions, Dec. 6, 2010
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009
- Criteria - Financial Institutions - Banks: Commercial Paper I: Banks, March 23, 2004

Related Research

- Banking Industry Country Risk Assessment: Denmark, Dec. 19, 2016
- The Future Of Banking: Nordic Banks Looking Svelte In The Fintech Race, June 14, 2016
- Various Rating Actions On Four Danish Banks After Review Of Government Support And Additional Loss-Absorbing Capacity, July 13, 2015
- Various Rating Actions On Danish Banks On EU Bank Recovery And Resolution Directive To Be Implemented In Denmark, May 12, 2015
- Credit FAQ: The Danish Covered Bond Market Explained, July 15, 2014
- Credit FAQ: Why Denmark's Proposed Covered Bond Law Doesn't Fully Eradicate Refinancing Risks, Feb. 4, 2014

Ratings List

Ratings Affirmed

Jyske Bank A/S

Counterparty Credit Rating	A-/Stable/A-2
Nordic Regional Scale Rating	--/--/K-1
Certificate Of Deposit	A-2
Senior Unsecured	A-
Subordinated	BBB
Junior Subordinated	BB+
Commercial Paper	A-2

BRFkredit A/S

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Counterparty Credit Rating	A-/Stable/A-2
Senior Unsecured	A-

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Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. Complete ratings information is available to subscribers of RatingsDirect at www.globalcreditportal.com and at spcapitaliq.com. All ratings affected by this rating action can be found on the S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column. Alternatively, call one of the following S&P Global Ratings numbers: Client Support Europe (44) 20-7176-7176; London Press Office (44) 20-7176-3605; Paris (33) 1-4420-6708; Frankfurt (49) 69-33-999-225; Stockholm (46) 8-440-5914; or Moscow 7 (495) 783-4009.

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