

CREDIT OPINION

26 May 2017

Update

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RATINGS
Ringkjøbing Landbobank A/S

Domicile	Ringkøbing, Denmark
Long Term Deposit	A1
Type	LT Bank Deposits - Fgn Curr
Outlook	Stable

Please see the [ratings section](#) at the end of this report for more information. The ratings and outlook shown reflect information as of the publication date.

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Ringkjøbing Landbobank A/S

Update to Discussion of Key Credit Factors

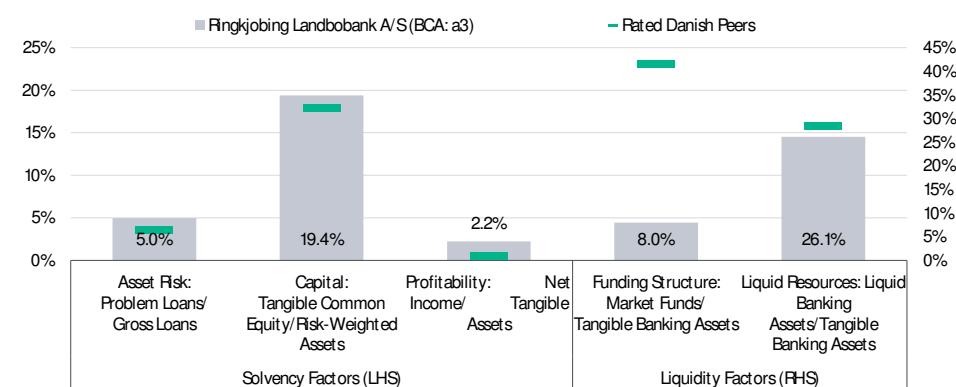
Summary Rating Rationale

We assign A1 long-term deposit ratings with stable outlook to Ringkjøbing Landbobank (Ringkjøbing), as well as an a3 standalone baseline credit assessment (BCA). Ringkjøbing's long-term Counterparty Risk Assessment (CR Assessment) is Aa3(cr).

Ringkjøbing's deposit ratings reflect (1) the bank's a3 BCA and Adjusted BCA; and (2) the results of our Advanced Loss Given Failure (LGF) analysis, which takes into account the severity of loss faced by the different liability classes in the unlikely event of the bank's failure and its resolution under the European Banking Recovery and Resolution Directive, providing two notches of rating uplift to Ringkjøbing's deposit ratings; and (3) our assumption of a "low" probability of government support, resulting in no additional rating uplift for Ringkjøbing's long-term ratings.

Ringkjøbing's a3 BCA reflects its (1) high and resilient profitability, as demonstrated throughout the financial crisis; as well as (2) its strong capitalisation; and (3) solid funding profile, reflecting ample deposits. At the same time, Ringkjøbing's standalone BCA is constrained by its relatively elevated problem loan level and somewhat concentrated loan book by geography and industry.

Exhibit 1

Key Financial Ratios Ringkjøbing versus Rated Danish peers (end- 2016)


Source: Moody's Banking Financial Metrics

Credit Strengths

- » Solid capital base and leverage ratio
- » Good earnings from core activities and high operating efficiency
- » Solid funding profile, reflecting sizeable deposit

Credit Challenges

- » Elevated problem loan level and somewhat concentrated loan book by geography and industry

Rating Outlook

- » Ringkjøbing's long-term deposit ratings carry a stable outlook reflecting our expectation that the bank will be able to sustain its credit profile, which will be supported by the benign domestic operating environment over the next 12 to 18 months, despite continued pressures from the persistent low interest-rate environment on the bank's earnings.

Factors that Could Lead to an Upgrade

- » An upgrade of Ringkjøbing's deposit ratings would be subject to an upgrade of the bank's BCA, which could result from: (1) improved asset quality; and (2) a significant reduction of loan and sector concentrations, leading to a lower susceptibility to adverse events.
- » An upgrade of Ringkjøbing's deposit ratings could also be triggered by a decrease in the expected loss severity following a shift in the bank's funding mix towards more lower ranking instruments, which could lead to more rating uplift as a result of our LGF analysis.

Factors that Could Lead to a Downgrade

- » A downgrade of Ringkjøbing's deposit ratings could be triggered following (1) a downgrade of the bank's BCA; and/or (2) an increase in the expected loss severity following a shift in the bank's funding mix, which could result in less rating uplift result of our LGF analysis.
- » A downgrade of Ringkjøbing's BCA could be triggered by (1) a deterioration in asset quality or capital metrics; (2) a persistent weakening of the bank's recurring earnings power and operating efficiency; and/or (3) an increase in the bank's reliance on market funding from the current low level.

This publication does not announce a credit rating action. For any credit ratings referenced in this publication, please see the ratings tab on the issuer/entity page on www.moody's.com for the most updated credit rating action information and rating history.

Key Indicators

Exhibit 2

Ringkjøbing Landbobank A/S (Consolidated Financials) [1]

	3-17 ²	12-16 ²	12-15 ²	12-14 ²	12-13 ³	CAGR/Avg ⁴
Total Assets (DKK million)	24,440	24,258	22,384	21,238	19,583	7.1 ⁵
Total Assets (EUR million)	3,287	3,262	2,999	2,852	2,625	7.2 ⁵
Total Assets (USD million)	3,515	3,441	3,258	3,451	3,617	-0.9 ⁵
Tangible Common Equity (DKK million)	3,500	3,554	3,294	3,098	2,901	5.9 ⁵
Tangible Common Equity (EUR million)	471	478	441	416	389	6.1 ⁵
Tangible Common Equity (USD million)	503	504	480	504	536	-1.9 ⁵
Problem Loans / Gross Loans (%)	-	5.0	5.7	6.7	8.1	6.4 ⁶
Tangible Common Equity / Risk Weighted Assets (%)	19.3	19.4	18.9	19.5	19.5	19.3 ⁷
Problem Loans / (Tangible Common Equity + Loan Loss Reserve) (%)	-	20.4	24.5	27.3	31.6	25.9 ⁶
Net Interest Margin (%)	2.6	2.9	2.9	3.1	3.4	3.0 ⁶
PPI / Average RWA (%)	4.4	4.0	3.9	4.4	4.1	4.2 ⁷
Net Income / Tangible Assets (%)	2.6	2.2	2.0	2.1	1.8	2.2 ⁶
Cost / Income Ratio (%)	27.0	31.0	32.1	30.7	31.7	30.5 ⁶
Market Funds / Tangible Banking Assets (%)	7.1	8.0	7.3	10.3	10.4	8.6 ⁶
Liquid Banking Assets / Tangible Banking Assets (%)	23.9	26.1	20.7	25.0	27.4	24.6 ⁶
Gross Loans / Due to Customers (%)	103.0	100.5	107.4	106.4	104.1	104.3 ⁶

[1] All figures and ratios are adjusted using Moody's standard adjustments [2] Basel III - fully-loaded or transitional phase-in; LOCAL GAAP [3] Basel II; LOCAL GAAP [4] May include rounding differences due to scale of reported amounts [5] Compound Annual Growth Rate (%) based on time period presented for the latest accounting regime [6] Simple average of periods presented for the latest accounting regime. [7] Simple average of Basel III periods presented

Source: Moody's Financial Metrics

Detailed Rating Considerations

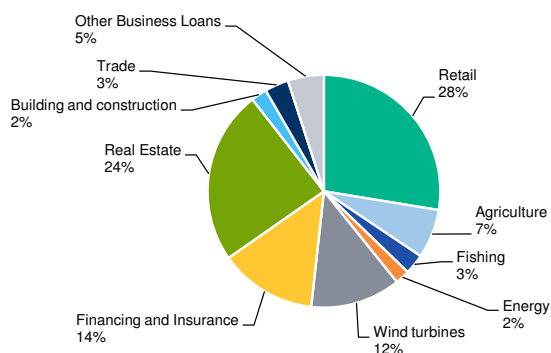
ELEVATED PROBLEM LOAN LEVEL AND CONCENTRATED LOAN BOOK BY INDUSTRY AND GEOGRAPHY

Our assigned ba2 Asset Risk score indicates that asset risk remains a relative weakness for Ringkjøbing, reflecting the continued elevated level of problem loans both relative to pre-crisis levels and to similarly highly rated peers across Europe, a key weakness for the bank. However, the trend in asset quality has been positive with problem loans (defined as gross loans subject to individual impairment) decreasing to 5.0% of gross loans at the end-2016 from 5.7% in 2015. The improvement reflects a reduction in problem loans, which declined to DKK913 million from DKK1,039 million, and the 1% increase of gross loans to DK18.4 billion. The bank's coverage ratio (measured as total loan loss reserves as a percentage of problem loans) improved to 102% at end-2016 from 90% in 2015, the highest coverage ratio among rated Danish banks, mainly due to a very high level of generic loan loss reserves.

At end-2016, around 40% of the bank's lending was to customers within the core region of western and central Jutland, while 10% of lending was outside Denmark. Much of the lending outside the core region is within the bank's chosen niche areas. The bank's loan and guarantee portfolio consists around 14% of lending to the wind turbine sector, 28% to private customers, 15% to real estate, 14% to finance companies, almost 7% to agriculture (excluding fishing and mink production), and the remainder to other corporates. We note that the bank has allocated considerable provisions for write-downs on agriculture, in particular.

We believe Ringkjøbing manages an unseasoned loan portfolio, reflecting significant loan growth of around 39% between 2012 and 2015. While outstanding loans were relatively unchanged during 2016, growth picked up again during 1Q2017, increasing the bank's gross loan portfolio by 3.9% to DKK19.1 billion.

Exhibit 3

Breakdown of Ringkjøbing Landbobank's loan portfolio by sector at end-2016

Source: Moody's, company reports

Given Ringkjøbing's narrow banking franchise, the bank exhibits relatively large customer concentrations in comparison with other European peers as measured by its top 20 largest exposures relative to Tier 1 capital. We note that a majority of the 20 largest exposures are outside the core area of central and western Jutland and therefore not concentrated locally and that a significant share of the large exposures are to highly rated Danish mortgage bonds. At end-2016, Ringkjøbing had total large exposures of 29.5% of the bank's capital measured, according to the Danish FSA's methodology, compared with 63.4% at end-2015.

We consider Ringkjøbing's ability to control sector- and single-name concentration as an important rating driver. We note that the bank's exposure to the real estate market (15.0% of the loan book at the end-2016) is more limited than that of many other Danish regional banks. However, the bank does have some exposures to the real estate market in Germany, and its exposure to the agricultural sector could continue to prove problematic in light of the generally high debt levels of Danish farmers.

SOLID CAPITAL BASE AND LEVERAGE RATIO

Our assigned aa2 Capital score strongly supports Ringkjøbing's standalone credit profile, reflecting its high capital with ample buffers in excess of regulatory minima. At end-March 2017, Ringkjøbing's reported Common Equity Tier 1 (CET1) ratio was 16.4%, a small decline compared with 16.9% at end-2016 (2015: 17.1%).

The bank's buffer in excess of its 9.0% individual solvency requirement at end-2016, which includes the FSA's Pillar 1 and Pillar 2 components, remained above seven percentage points, making capital a relative strength for the bank. Ringkjøbing mainly applies the standardized approach to calculate credit related risk-weighted assets. Therefore, the bank's risk density, measured as risk-weighted assets (RWA) compared with total assets, is relatively high at 74% at end-March 2017 (2016: 76%), rendering the bank less sensitive to potential amendments in regulatory methods to calculating RWA, including floor requirements. We note that the bank's high profitability and strong track record point to a high capacity to generate capital internally. Accordingly, we expect that the bank will sustain strong capital buffers over the foreseeable future.

Ringkjøbing Landbobank has one of the highest leverage ratio (measured as equity to assets) among Nordic and international banks. At 14.3% at end-March 2017, almost unchanged compared with 14.7% at end-2016, Ringkjøbing's leverage ratio is significantly higher than the 4%-10% level recorded by most of its Nordic peers.

GOOD EARNINGS FROM CORE ACTIVITIES COUPLED WITH HIGH OPERATING EFFICIENCY

Our assigned a3 Profitability score reflects Ringkjøbing's strong earnings track record and high profitability, which provides ample capacity to absorb losses through internal capital generation, in case of need. During 2016, Ringkjøbing reported a return on assets (ROA) of 2.2%, compared with 2.1% in 2015. During 1Q17, the improving trend continued, as underpinned by an annualized ROA of 2.4%.

We expect that the benign operating environment in Denmark will further support Ringkjøbing's earnings, as impairment charges are likely to further decline from an already very low level. During 2016, the bank's impairment charges as a percentage of core earnings have declined to 7% from 9% in 2015 (2014: 14%), and trended down further to 3% during 1Q17.

Further, Ringkjøbing remains one of Denmark's most efficient banks, with a 31% cost-to-income ratio in 2016 (measured as operating income divided by operating expenses) and 27% during 1Q17. In our view, the bank's lean and low-cost business model remains a key driver for its high risk-adjusted profitability compared with that of regional peers and its ability to further grow its lending activities raises Ringkjøbing's leeway to cope with the challenges from low interest rates.

In 2016, Ringkjøbing reported pre-tax profits of DKK661 million, compared with DKK588 million in 2015. For 1Q17, the bank's pre-tax profits of DKK198 million increased by around 25% (compared to the same period last year), mostly as a result of the reduction in impairment charges and a positive contribution from fair value gains of its investment securities, which included DKK596 million in shares.

SOLID FUNDING PROFILE AND ADEQUATE LIQUIDITY

Ringkjøbing's solid funding profile strongly supports the bank's BCA. At end-March 2017, deposits accounted for around 76% of assets, almost unchanged compared with 2016 and 2015. The bank's very low dependence on confidence-sensitive wholesale funding is also underpinned by a balanced loan-to-deposit ratio of 103% at end-March 2017, compared with 101% in 2016 (2015: 107%). These strengths are reflected in our aa3 Funding Structure score.

Market funding, which accounted for 7.1% of the bank's tangible banking assets at end-March 2017 compared with 8.0% in 2016, has been relatively stable since 2011. As with most Danish regional and local banks, Ringkjøbing can secure its mortgage loan financing via the specialised mortgage lenders Nykredit/Totalkredit and DLR. The loan funding by the specialised mortgage lenders will not show on the bank's balance sheet as the mortgage loans are transferred in full.

We consider Ringkjøbing's liquidity adequate compared with its lending driven business model, as well as its high and stable deposit base. This view is reflected in our baa1 score for Liquid Resources. At end-March 2017, liquid assets accounted for around 24% of assets, a small decrease from 26% at end-2016. At end-March 2017, Ringkjøbing reported a liquidity coverage ratio (LCR) of 160%, in excess of the Danish FSA's minimum requirement of 100%, which applies to systemically important financial institutions in Denmark (although Ringkjøbing is not a systemically important financial institution).

Notching Considerations

Loss Given Failure

Ringkjøbing Landbobank is subject to the EU Bank Recovery and Resolution Directive (BRRD), which we consider an Operational Resolution Regime. We apply our advanced Loss Given Failure (LGF) analysis to Ringkjøbing's liabilities, considering the risks faced by the different debt deposit classes across its liability structure at failure. We assume residual tangible common equity of 3% and losses post-failure of 8% of tangible banking assets, a 25% run-off in "junior" wholesale deposits and a 5% run-off in preferred deposits. These are in line with our standard assumptions.

For Ringkjøbing's A1 rated deposits, our LGF analysis indicates an very low loss-given failure, leading to a two-notch uplift from the bank's a3 Adjusted BCA from which these ratings are notched.

Government Support

The implementation of the EU BRRD has caused us to reconsider the potential for government support to benefit certain creditors. We continue to consider the probability of government support to Ringkjøbing to be low and hence do not assign any systemic support to the bank's ratings.

COUNTERPARTY RISK (CR) ASSESSMENT

CR Assessments are opinions of how counterparty obligations are likely to be treated if a bank fails and are distinct from debt and deposit ratings in that they (1) consider only the risk of default rather than both the likelihood of default and the expected financial loss suffered in the event of default and (2) apply to counterparty obligations and contractual commitments rather than debt or deposit instruments. The CR Assessment is an opinion of the counterparty risk related to a bank's covered bonds, contractual performance obligations (servicing), derivatives (e.g., swaps), letters of credit, guarantees and liquidity facilities.

Ringkjøbing's CR Assessment is positioned at Aa3(cr)/Prime-1(cr). The CR Assessment is positioned three notches above the bank's a3 Adjusted BCA, based on the substantial cushion against default provided to the senior obligations represented by the CR Assessment

by subordinated instruments. The main difference with our Advanced LGF approach used to determine instrument ratings is that the CR Assessment captures the probability of default on certain senior obligations, rather than expected loss, thereby focusing purely on subordination and taking no account of the volume of the instrument class.

Rating Methodology and Scorecard Factors

Exhibit 4

Ringkjøbing Landbobank A/S

Macro Factors

Weighted Macro Profile **Strong +** **100%**

Factor	Historic Ratio	Macro Adjusted Score	Credit Trend	Assigned Score	Key driver #1	Key driver #2
Solvency						
Asset Risk						
Problem Loans / Gross Loans	5.8%	baa2	← →	ba2	Sector concentration	Geographical concentration
Capital						
TCE / RWA	19.3%	aa2	← →	aa2	Risk-weighted capitalisation	
Profitability						
Net Income / Tangible Assets	2.2%	aa2	← →	aa3	Return on assets	
Combined Solvency Score		a1		a3		
Liquidity						
Funding Structure						
Market Funds / Tangible Banking Assets	8.0%	a1	← →	a1	Extent of market funding reliance	
Liquid Resources						
Liquid Banking Assets / Tangible Banking Assets	26.1%	a3	← →	a3	Stock of liquid assets	
Combined Liquidity Score		a2		a2		
Financial Profile						
Business Diversification				0		
Opacity and Complexity				0		
Corporate Behavior				0		
Total Qualitative Adjustments				0		
Sovereign or Affiliate constraint:				Aaa		
Scorecard Calculated BCA range				a2-baa1		
Assigned BCA				a3		
Affiliate Support notching				0		
Adjusted BCA				a3		

Balance Sheet	in-scope (DKK million)	% in-scope	at-failure (DKK million)	% at-failure
Other liabilities	4,772	19.5%	6,665	27.3%
Deposits	18,565	76.0%	16,671	68.2%
Preferred deposits	13,738	56.2%	13,051	53.4%
Junior Deposits	4,827	19.7%	3,620	14.8%
Dated subordinated bank debt	371	1.5%	371	1.5%
Equity	733	3.0%	733	3.0%
Total Tangible Banking Assets	24,441	100%	24,441	100%

Debt class	De jure waterfall		De facto waterfall		Notching		LGF notching guidance versus BCA	Assigned LGF notching	Additional notching	Preliminary Rating Assessment
	Instrument volume + Subordination	Sub-ordination	Instrument volume + Subordination	Sub-ordination	De jure	De facto				
Counterparty Risk Assessment	19.3%	19.3%	19.3%	19.3%	3	3	3	3	0	aa3 (cr)
Deposits	19.3%	4.5%	19.3%	4.5%	2	2	2	2	0	a1

Instrument class	Loss Given Failure notching	Additional Notching	Preliminary Rating Assessment	Government Support notching	Local Currency Rating	Foreign Currency Rating
Deposits	2	0	a1	0	A1	A1

Source: Moody's Financial Metrics

Ratings

Exhibit 5

Category	Moody's Rating
RINGKJOBING LANDBOBANK A/S	
Outlook	Stable
Bank Deposits	A1/P-1
Baseline Credit Assessment	a3
Adjusted Baseline Credit Assessment	a3
Counterparty Risk Assessment	Aa3(cr)/P-1(cr)

Source: Moody's Investors Service

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