

ISSUER COMMENT

Moody's Comments on the Intended Merger of Sparebanken Sør and Sparebanken Pluss

Analyst Contacts:

LONDON +44.20.7772.5454

Soline Poulain +44.20.7772.1628

Analyst
soline.poulain@moodys.com

Simon Harris +44.20.7772.1576

Managing Director - Financial Institutions
simon.harris@moodys.com

On 12 March 2013, Sparebanken Sør (A3 stable, C-/baa2 stable)¹ and Sparebanken Pluss (A2 stable, C-/baa1 stable) announced that they intend to merge their operations. The transaction is contingent on approval from the two banks' Boards of Trustees, expected by June 2013, and regulatory approvals. The merger is expected to be effective by 1 January 2014.

If the transaction proceeds, we expect the combined bank's rating to be close to the rating level of the two individual banks, i.e., A3 for Sparebanken Sør and A2 for Sparebanken Pluss, although we will also factor in our assessment of the risks related to the integration process.

Sparebanken Sør and Sparebanken Pluss are two similar-sized banks, operating in southern Norway, where they are major players in retail and SME lending, with reported total assets of NOK44.5 billion and NOK44.1 billion at year-end 2012, respectively. On a national basis, the combined entity would be the fifth largest savings bank in terms of total assets. The merger would create a dominant player in Southern Norway; we estimate the combined market share in the counties of Aust-Agder and Vest-Agder would be around 35% for lending and 55% for deposits.²

In addition, the banks' robust retail banking operations, their currently sound asset quality and their sizeable deposit bases would continue to support the combined bank's credit profile. We expect that the retail-focus of the combined bank would continue to support asset quality. Loans to the retail sector have historically performed well and accounted for 62% to 70% of Sparebanken Pluss's and Sparebanken Sør's total loans, respectively, at year-end 2012. The combined bank's credit profile would also reflect a robust earnings base from the banks' retail operations (between 60%-70% of 2012 core revenue).³ This source of earnings has proven resilient over recent years and we expect there will be an opportunity for the bank to increase its lending margin in this segment, in light of the ongoing re-pricing movement in Norway in preparation of the likely increase in regulatory capital.⁴

¹ The ratings are the banks' deposit ratings, their standalone bank financial strength ratings/baseline credit assessments and the corresponding rating outlooks.

² Moody's calculation based on lending per county from Statistics Norway

³ Excluding unallocated revenue and treasury functions.

⁴ Please also see "Increased Capital Requirement for Mortgages Is Credit Positive for Norwegian Banks", in [Moody's Credit Outlook](#), 11 March 2013.

However, we expect that the combined bank would continue to face challenges related to maintaining good asset quality in its loans and its reliance on market funding. In particular, we see some downside risks related to high household indebtedness and increased house prices in Norway. In addition, we consider that loan-book concentration towards the real-estate and construction sectors, which is significant at both banks (20%-25% of gross loans at year-end 2012), poses the main risk to asset quality. It will also be crucial that the combined entity establishes risk-management processes that ensure a consistent assessment of the credit risk of the combined loan book.

Both banks' funding is underpinned by a sizeable deposit base, which covered around 55% of gross loans at year-end 2012, but exhibits some reliance on market funding, increasingly in the form of covered bonds. We expect that dependence on market funding and therefore investor sentiment will remain a key risk at the combined bank, although in line with other medium-sized Norwegian savings banks.

We view both banks' capital levels as adequate (around 13.5%-14.2% at year-end 2012, calculated under the standardised method) and expect that the combined entity would show similar levels.

Furthermore, if the transaction proceeds, we expect that the ability of the newly appointed management to efficiently integrate the two banks' operations and design a coherent strategy will be key drivers in our assessment of the combined entity's credit strength.

Given its regional importance and in light of the Norwegian government's strong ability to extend support to the domestic financial sector, we would continue to assume a high probability of systemic support for the combined bank, in case of need.

We will monitor developments and will take appropriate rating actions when the legal issues regarding the merger are resolved and we have more clarity on how the banks will implement the merger.

 Report Number: 151607

 Author
 Soline Poulain

 Editor
 Gregory Davies

 Production Specialist
 Cassina Brooks

© 2013 Moody's Investors Service, Inc. and/or its licensors and affiliates (collectively, "MOODY'S"). All rights reserved.

CREDIT RATINGS ISSUED BY MOODY'S INVESTORS SERVICE, INC. ("MIS") AND ITS AFFILIATES ARE MOODY'S CURRENT OPINIONS OF THE RELATIVE FUTURE CREDIT RISK OF ENTITIES, CREDIT COMMITMENTS, OR DEBT OR DEBT-LIKE SECURITIES, AND CREDIT RATINGS AND RESEARCH PUBLICATIONS PUBLISHED BY MOODY'S ("MOODY'S PUBLICATIONS") MAY INCLUDE MOODY'S CURRENT OPINIONS OF THE RELATIVE FUTURE CREDIT RISK OF ENTITIES, CREDIT COMMITMENTS, OR DEBT OR DEBT-LIKE SECURITIES. MOODY'S DEFINES CREDIT RISK AS THE RISK THAT AN ENTITY MAY NOT MEET ITS CONTRACTUAL, FINANCIAL OBLIGATIONS AS THEY COME DUE AND ANY ESTIMATED FINANCIAL LOSS IN THE EVENT OF DEFAULT. CREDIT RATINGS DO NOT ADDRESS ANY OTHER RISK, INCLUDING BUT NOT LIMITED TO: LIQUIDITY RISK, MARKET VALUE RISK, OR PRICE VOLATILITY. CREDIT RATINGS AND MOODY'S OPINIONS INCLUDED IN MOODY'S PUBLICATIONS ARE NOT STATEMENTS OF CURRENT OR HISTORICAL FACT. CREDIT RATINGS AND MOODY'S PUBLICATIONS DO NOT CONSTITUTE OR PROVIDE INVESTMENT OR FINANCIAL ADVICE, AND CREDIT RATINGS AND MOODY'S PUBLICATIONS ARE NOT AND DO NOT PROVIDE RECOMMENDATIONS TO PURCHASE, SELL, OR HOLD PARTICULAR SECURITIES. NEITHER CREDIT RATINGS NOR MOODY'S PUBLICATIONS COMMENT ON THE SUITABILITY OF AN INVESTMENT FOR ANY PARTICULAR INVESTOR. MOODY'S ISSUES ITS CREDIT RATINGS AND PUBLISHES MOODY'S PUBLICATIONS WITH THE EXPECTATION AND UNDERSTANDING THAT EACH INVESTOR WILL MAKE ITS OWN STUDY AND EVALUATION OF EACH SECURITY THAT IS UNDER CONSIDERATION FOR PURCHASE, HOLDING, OR SALE.

ALL INFORMATION CONTAINED HEREIN IS PROTECTED BY LAW, INCLUDING BUT NOT LIMITED TO, COPYRIGHT LAW, AND NONE OF SUCH INFORMATION MAY BE COPIED OR OTHERWISE REPRODUCED, REPACKAGED, FURTHER TRANSMITTED, TRANSFERRED, DISSEMINATED, REDISTRIBUTED OR RESOLD, OR STORED FOR SUBSEQUENT USE FOR ANY SUCH PURPOSE, IN WHOLE OR IN PART, IN ANY FORM OR MANNER OR BY ANY MEANS WHATSOEVER, BY ANY PERSON WITHOUT MOODY'S PRIOR WRITTEN CONSENT.

All information contained herein is obtained by MOODY'S from sources believed by it to be accurate and reliable. Because of the possibility of human or mechanical error as well as other factors, however, all information contained herein is provided "AS IS" without warranty of any kind. MOODY'S adopts all necessary measures so that the information it uses in assigning a credit rating is of sufficient quality and from sources MOODY'S considers to be reliable including, when appropriate, independent third-party sources. However, MOODY'S is not an auditor and cannot in every instance independently verify or validate information received in the rating process. Under no circumstances shall MOODY'S have any liability to any person or entity for (a) any loss or damage in whole or in part caused by, resulting from, or relating to, any error (negligent or otherwise) or other circumstance or contingency within or outside the control of MOODY'S or any of its directors, officers, employees or agents in connection with the procurement, collection, compilation, analysis, interpretation, communication, publication or delivery of any such information, or (b) any direct, indirect, special, consequential, compensatory or incidental damages whatsoever (including without limitation, lost profits), even if MOODY'S is advised in advance of the possibility of such damages, resulting from the use of or inability to use, any such information. The ratings, financial reporting analysis, projections, and other observations, if any, constituting part of the information contained herein are, and must be construed solely as, statements of opinion and not statements of fact or recommendations to purchase, sell or hold any securities. Each user of the information contained herein must make its own study and evaluation of each security it may consider purchasing, holding or selling.

NO WARRANTY, EXPRESS OR IMPLIED, AS TO THE ACCURACY, TIMELINESS, COMPLETENESS, MERCHANTABILITY OR FITNESS FOR ANY PARTICULAR PURPOSE OF ANY SUCH RATING OR OTHER OPINION OR INFORMATION IS GIVEN OR MADE BY MOODY'S IN ANY FORM OR MANNER WHATSOEVER.

MIS, a wholly-owned credit rating agency subsidiary of Moody's Corporation ("MCO"), hereby discloses that most issuers of debt securities (including corporate and municipal bonds, debentures, notes and commercial paper) and preferred stock rated by MIS have, prior to assignment of any rating, agreed to pay to MIS for appraisal and rating services rendered by it fees ranging from \$1,500 to approximately \$2,500,000. MCO and MIS also maintain policies and procedures to address the independence of MIS's ratings and rating processes. Information regarding certain affiliations that may exist between directors of MCO and rated entities, and between entities who hold ratings from MIS and have also publicly reported to the SEC an ownership interest in MCO of more than 5%, is posted annually at www.moody.com under the heading "Shareholder Relations — Corporate Governance — Director and Shareholder Affiliation Policy."

For Australia only: Any publication into Australia of this document is pursuant to the Australian Financial Services License of MOODY'S affiliate, Moody's Investors Service Pty Limited ABN 61 003 399 657AFSL 336969 and/or Moody's Analytics Australia Pty Ltd ABN 94 105 136 972 AFSL 383569 (as applicable). This document is intended to be provided only to "wholesale clients" within the meaning of section 761G of the Corporations Act 2001. By continuing to access this document from within Australia, you represent to MOODY'S that you are, or are accessing the document as a representative of, a "wholesale client" and that neither you nor the entity you represent will directly or indirectly disseminate this document or its contents to "retail clients" within the meaning of section 761G of the Corporations Act 2001. MOODY'S credit rating is an opinion as to the creditworthiness of a debt obligation of the issuer, not on the equity securities of the issuer or any form of security that is available to retail clients. It would be dangerous for retail clients to make any investment decision based on MOODY'S credit rating. If in doubt you should contact your financial or other professional adviser.