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INVESTORS SERVICE

CREDIT OPINION

5 July 2023

Update



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RATINGS

Sparbanken Syd

Domicile	Sweden
Long Term CRR	A3
Type	LT Counterparty Risk Rating - Fgn Curr
Outlook	Not Assigned
Long Term Debt	Not Assigned
Long Term Deposit	Baa1
Type	LT Bank Deposits - Fgn Curr
Outlook	Positive

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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Sparbanken Syd

Update to credit analysis following rating action

Summary

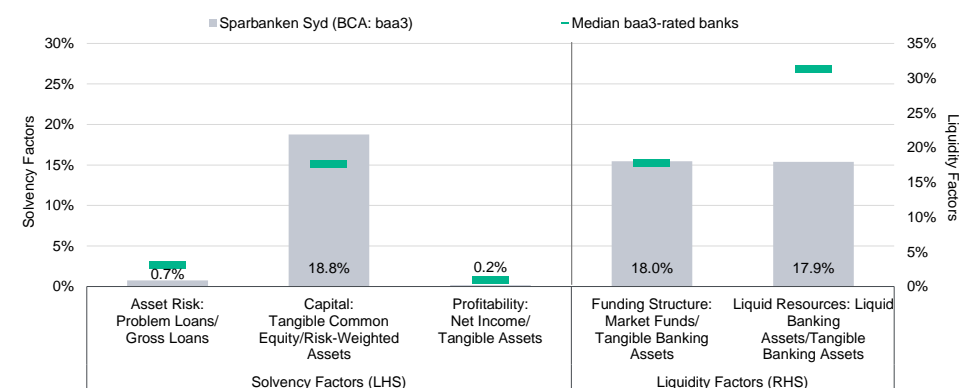
[Sparbanken Syd](#)'s issuer and deposit ratings of Baa1/P-2 incorporate the Baseline Credit Assessment (BCA) and Adjusted BCA of baa3, and two notches of uplift as indicated by our Advanced Loss Given Failure (LGF) analysis.

Sparbanken Syd's baa3 BCA reflects its stable asset quality and strong capitalisation, balanced against its consistently low profitability. During 2023, Sparbanken Syd initiated its partnership with [Borgo AB](#) (Baa2 stable, baa3)¹ (Borgo), a Sweden-based covered bond issuer. The partnership, which allows Sparbanken Syd to continue offering mortgages, reduces uncertainties regarding funding and capitalisation.

The bank's Counterparty Risk Assessment (CRA) is positioned at A3(cr)/P-2(cr) and Counterparty Risk Ratings (CRRs) are positioned at A3/P-2, incorporating three notches of uplift to the BCA according to our LGF analysis.

Exhibit 1

Rating Scorecard - Key financial ratios



These represent our [Banks Methodology](#) scorecard ratios, whereby asset risk and profitability reflect the weaker of either the latest reported or the average of the last three year-end and latest reported ratios. Capital is the latest reported figure. Funding structure and liquid resources ratios reflect the latest year-end figures.

Source: Moody's Financial Metrics™

Credit strengths

- » Good asset quality with low levels of problem loans, although exposed to geographical and sector concentrations
- » Sound capitalisation
- » Sizeable liquidity portfolio and large volume of deposits

Credit challenges

- » Weaker profitability and cost efficiency than those of its Nordic peers
- » Limited access to capital in case of need
- » Weak governance and limited effectiveness in implementing its business strategy

Outlook

The positive outlook on Sparbanken Syd's long-term deposit and issuer ratings reflects Moody's view that the bank's standalone creditworthiness could strengthen over the next 12 to 18 months. Moody's views the partnership with Borgo AB (publ), a long-term strategic alliance to fund Sparbanken Syd's mortgages, positively and assesses that it will reduce uncertainties regarding both funding needs and capitalization levels.

Factors that could lead to an upgrade

Sparbanken Syd's ratings could be upgraded if: 1) the bank continues originating mortgages through Borgo AB (publ) without significant disruptions; 2) the bank's profitability improves, supporting a stronger internal capital generation; combined with 3) sustained high capitalization; and 4) higher liquidity buffers due to increased liquid assets.

Factors that could lead to a downgrade

Although unlikely given the positive outlook, Sparbanken Syd's ratings could be downgraded if: 1) its profitability deteriorates significantly, leading to recurring losses and lower capital generation; or 2) the bank ventures into riskier segments to deploy its excess liquidity. Furthermore, the deposit and issuer ratings could be downgraded if loss-absorbing liabilities reduce, lowering the cushion of protection to depositors and creditors in case of failure.

This publication does not announce a credit rating action. For any credit ratings referenced in this publication, please see the issuer/deal page on <https://ratings.moody.com> for the most updated credit rating action information and rating history.

Key indicators

Exhibit 2

Sparbanken Syd (Unconsolidated Financials) [1]

	12-22 ²	12-21 ²	12-20 ²	12-19 ²	12-18 ²	CAGR/Avg. ³
Total Assets (SEK Million)	14,271.9	12,746.6	11,554.4	10,625.7	10,633.9	7.6 ⁴
Total Assets (USD Million)	1,369.7	1,408.9	1,406.9	1,135.1	1,199.4	3.4 ⁴
Tangible Common Equity (SEK Million)	1,251.5	1,207.1	1,189.5	1,181.8	1,179.2	1.5 ⁴
Tangible Common Equity (USD Million)	120.1	133.4	144.8	126.2	133.0	(2.5) ⁴
Problem Loans / Gross Loans (%)	0.4	0.8	1.0	1.0	1.0	0.8 ⁵
Tangible Common Equity / Risk Weighted Assets (%)	18.8	19.4	22.4	20.3	18.8	19.9 ⁶
Problem Loans / (Tangible Common Equity + Loan Loss Reserve) (%)	4.0	5.9	5.6	5.8	5.9	5.5 ⁵
Net Interest Margin (%)	1.8	1.5	1.6	1.6	1.6	1.6 ⁵
PPI / Average RWA (%)	1.0	0.5	0.4	0.1	0.5	0.5 ⁶
Net Income / Tangible Assets (%)	0.3	0.2	0.1	0.0	0.2	0.2 ⁵
Cost / Income Ratio (%)	82.0	91.2	93.1	97.1	89.0	90.5 ⁵
Market Funds / Tangible Banking Assets (%)	18.0	7.7	3.5	6.8	9.6	9.1 ⁵
Liquid Banking Assets / Tangible Banking Assets (%)	17.9	25.9	39.8	35.5	31.8	30.2 ⁵
Gross Loans / Due to Customers (%)	113.5	90.4	70.3	79.4	86.9	88.1 ⁵

[1] All figures and ratios are adjusted using Moody's standard adjustments. [2] Basel III - fully loaded or transitional phase-in; IFRS. [3] May include rounding differences because of the scale of reported amounts. [4] Compound annual growth rate (%) based on the periods for the latest accounting regime. [5] Simple average of periods for the latest accounting regime. [6] Simple average of Basel III periods.

Sources: Moody's Investors Service and company filings

Profile

Sparbanken Syd is Sweden's oldest savings bank, primarily operating in Skåne County in the southernmost parts of Sweden. Operating for nearly 200 years, the bank is well established in the region among retail as well as corporate customers. As of year-end 2022, the bank had total assets of SEK14.3 billion (€1.3 billion).

Sparbanken Syd is the only independent savings bank in Sweden and it is structured as a savings bank according to the Swedish Act on Savings Banks (1987:619), meaning that the bank has no external owners and is instead self owned. To ensure proper control, the bank is managed by 60 mandators, who are elected. The first 30 are chosen by the municipalities of Ystad, Simrishamn, Tomelilla, and Skurup. The remaining mandators are chosen independently by the first 30. The main responsibility of these mandators is to select and approve the bank's board of directors.

The bank has also established a foundation, the Sparbanken Syd Foundation for Growth, which aims to serve as a catalyst in the local community.

Recent developments

On 14 February 2022, Sparbanken Syd became an owner in Borgo and joined as a member of Borgo's board. Borgo, a Swedish covered bond issuer, is co-owned by ICA Banken, Ikano Bank, Söderberg & Partners, Ålandsbanken and other investors. The ownership allows Sparbanken Syd to use Borgo to originate mortgages. Previously, Sparbanken Syd financed their mortgages through an asset purchase program with SBAB, which was cancelled unilaterally by [SBAB Bank AB \(publ\)](#) (A1/A1, stable, baa1) (SBAB) in 2017, with a phasing out until December 2023.

Sparbanken Syd's distribution using Borgo started in 2023. The bank's transfer to Borgo of SEK3.1 billion of mortgages previously held on its own balance sheet was finalised on 13 March 2023.

On 8 May 2023, SEK4.8 billion of mortgages originally originated by Sparbanken Syd were repurchased by Borgo from SBAB.

End of partnership with SBAB

In late November 2017, SBAB unilaterally terminated an asset purchase programme it had previously established with Sparbanken Syd to fund the latter bank's mortgages. The funding arrangement enabled Sparbanken Syd (and other banks) to sell mortgages to SBAB, with most of the bank's mortgages (representing a large share of the bank's total lending) being funded through this channel. The white label partnership enabled Sparbanken Syd to sell its mortgages to SBAB and earning a commission, thereby moving them off the

balance sheet and reducing its funding needs, as well as credit risk and capital requirements, while maintaining customer relationships. The partnership formally ended in November 2019, and was finalised with the transfer of the final mortgages to Borgo in May 2023.

Detailed credit considerations

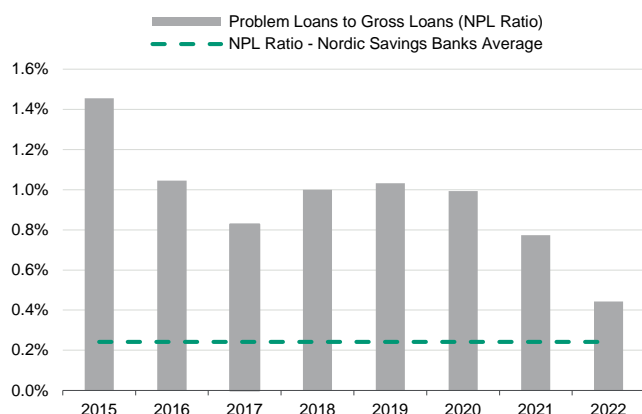
Moderate asset risk deterioration

The bank's asset risk is strong by global standards and has stabilised in recent years. Sparbanken Syd's problem loans to gross loans ratio decreased to 0.4% as of year-end 2022, significantly lower than the 1.5% reported in 2015 (see Exhibit 3).

The bank has a significant share of exposure to small and medium-sized enterprises (SMEs) in the Skåne region. Such a concentration can pose a higher risk in a downturn, and these customers account for around half of the risk that the bank retains on its balance sheet. On 13 March 2023, a large part of the bank's mortgages held on their own balance sheet, SEK3.1 billion, were transferred to Borgo, increasing the share of SME loans in the loan portfolio, which will likely add volatility to asset quality. After the sale, approximately SEK3.5 billion in mortgages remain on Sparbanken Syd's balance sheet.

Exhibit 3

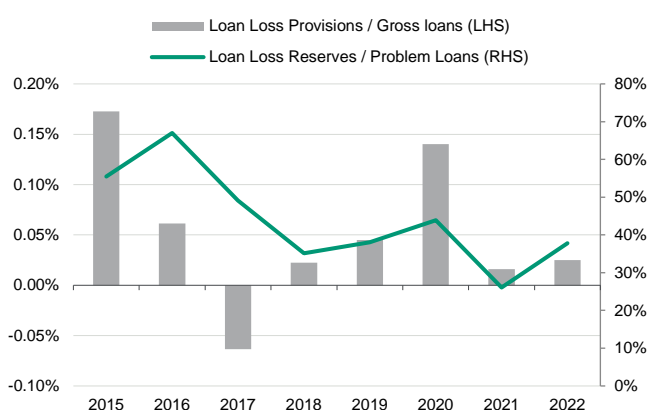
Asset risk has improved since 2015



Average of Nordic savings banks' problem loans/gross loans (including Skandiabanken AB and Lansforsakringar Bank AB) that we rate as of year-end 2022 or latest available.
Source: Moody's Investors Service

Exhibit 4

Sparbanken Syd has a low cost of risk



Source: Moody's Investors Service

Sparbanken Syd can now originate Borgo-financed mortgages, while it still finances mortgages on balance sheet that do not meet the terms of Borgo's cover pool.

The assigned Asset Risk score of baa1 reflects the low level of problem loans, as well as geographical and sector concentration risks.

Sound capitalisation, but weak internal capital generation

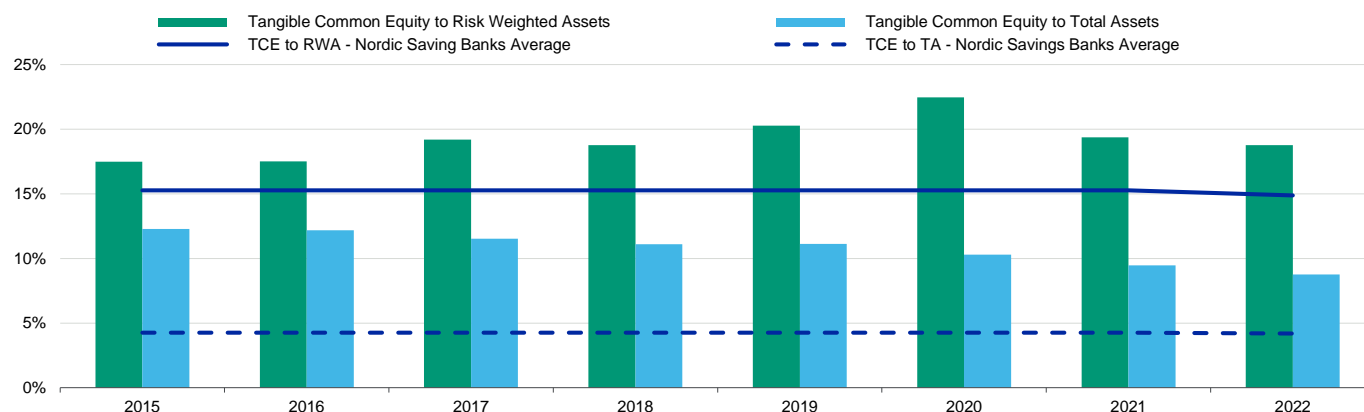
Sparbanken Syd's capitalisation is strong, with tangible common equity (TCE) to risk-weighted assets (RWA) of 18.8% and TCE to total assets of 8.8% as of year-end 2022. However, the bank's profitability is low, leading to weak internal capital generation. Furthermore, the bank has limited access to capital injections in case of need due to its ownership structure.

The bank reported a Common Equity Tier 1 (CET1) capital ratio of 18.2% as of year-end 2022, down slightly from 18.6% as of year-end 2021. Its total capital adequacy ratio decreased to 20.5% as of year-end 2022 from 21.0% as year-end 2021. The decrease in Sparbanken Syd's capital metrics relate to the significant increase in lending on its own balance sheet. However, we expect that capitalisation will increase during 2023 due to the sale of its mortgages portfolio.

The bank had a sizeable buffer above its regulatory minimum CET1 requirement of 13.6%, including a Pillar 2 requirement of 2.1%, at year-end 2022. Sparbanken Syd applies the standardised approach for measuring credit risk.

We expect raising additional capital in times of stress to be difficult given the bank's organisational structure as a savings bank without strategic corporate shareholders or direct capital market access.

Exhibit 5

Sparbanken Syd has strong capital metrics

Average of Nordic savings banks we rate (including Skandiabanken AB and Länsförsäkringar Bank) as of year-end 2022 or latest available.

Source: Moody's Investors Service

Sparbanken Syd's Capital score of a1 is two notches below the macro-adjusted score, reflecting our view of that the bank's capitalisation is strong albeit challenged by the weak internal capital generation and lacking access to capital in case of need.

Weak profitability due to limited economies of scale and ability to grow.

As a pure savings bank, Sparbanken Syd operates with low targets on return on equity, between 2% to 5%. Furthermore, its weak profitability is challenged by limited economies of scale.

Sparbanken Syd improved its net income to SEK46.5 million for 2022 compared to SEK19.1 million for the same period in 2021. Net interest income improved by 35% in 2022 because of rising interest rates. The repurchase of SEK4.8 billion of mortgages from SBAB by Borgo will provide similar fee earnings for Sparbanken Syd. However, the SEK3.1 billion of mortgages transferred from Sparbanken Syd's own balance sheet will provide less income given Borgo's administrative and funding fees, counterbalanced by easing capital allocation requirements and greater balance sheet flexibility.

The bank's operating expenses grew slightly to SEK289 million as of 2022 (2021: SEK272 million) due to increased personnel and IT costs. In addition, net fee and commission income decreased to SEK92 million in 2022 from SEK112 million in the year-earlier period, because of lower fund and insurance commissions linked to the stock market decline.

The bank's efficiency is weaker than peers but increased focus on cost control has helped improve the cost-to-income ratio to 82.0% in 2022 compared with 91% in 2021, efficiency remained significantly weaker than peers at and we expect this to remain a challenge.

Due to the additional liquidity and capital relief received through the sale of mortgages to Borgo, we expect SME lending to increase gradually, which will improve margins over time.

We assign Sparbanken Syd a Profitability score of b2, reflecting Sparbanken Syd's low profitability and ongoing profitability challenges.

Positive developments regarding Sparbanken Syd's funding strategy

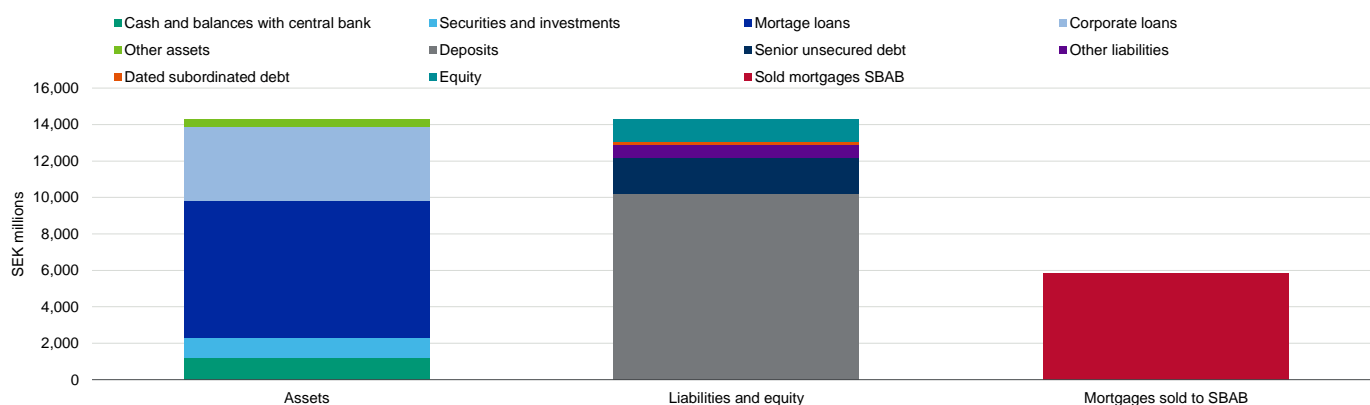
Sparbanken Syd is primarily deposit funded with deposit funding representing 78% of non-equity funding as of year-end 2022. The deposit volumes grew by 3% during 2022.

The agreement with Borgo reduces funding uncertainties, as future mortgages will mainly be originated by Borgo.

Exhibit 6

On 8 May 2023, Borgo repurchased SEK4.8 billion of mortgages previously held by SBAB.

Balance sheet as of 31 December 2022 and mortgages previously held by SBAB



Note: Approximately SEK3.5 billion in mortgages remain on Sparbanken Syd's balance sheet.

Source: Company reports

Sparbanken Syd had SEK2 billion senior unsecured debt outstanding at end of year 2022, resulting in a market funding ratio of 18.0%. Furthermore, the bank has a SEK150 million subordinated bond maturing in 2024 (not included in the market funding ratio).

We assign the bank a Funding Structure score of baa2, balancing the positive developments regarding the bank's funding strategy against the dependency on an external partner for funding and limited market access.

Liquid assets provide a buffer against increasing wholesale funding

We assign Sparbanken Syd a Liquidity score of a2, reflecting Moody's expectation that liquid resources will be ample following the sale of the majority of mortgages previously on its balance sheet. The liquid assets to tangible banking assets was 17.9% as of end of year 2022 including its stock of high-quality liquid assets, comprising highly rated covered bonds and government securities.

The transfer of SEK3.1 billion in mortgages to Borgo from Sparbanken Syd's own balance sheet is expected to lead to a liquidity surplus, leading to an expected liquidity ratio of almost 40%. We expect Sparbanken Syd to reduce the surplus and slowly come down to a liquidity ratio of around 30% over the coming years to, as Sparbanken Syd will increase lending to corporates.

ESG considerations

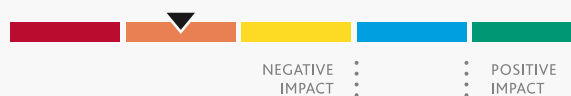
Sparbanken Syd's ESG Credit Impact Score is Highly Negative CIS-4

Exhibit 7

ESG Credit Impact Score

CIS-4

Highly Negative

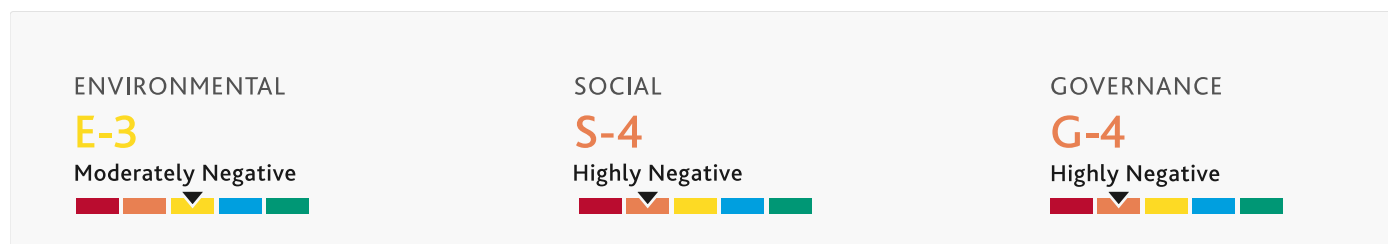


For an issuer scored CIS-4 (Highly Negative), its ESG attributes are overall considered as having a discernible negative impact on the current rating. The negative influence of the overall ESG attributes on the rating is more pronounced compared to an issuer scored CIS-3.

Source: Moody's Investors Service

Sparbanken Syd's **CIS-4** indicates that ESG considerations have a discernable rating impact due to the bank's high governance risk, incorporated in a one-notch negative rating adjustment for corporate behaviour. Environmental and social factors have a limited impact on the bank's credit profile.

Exhibit 8

ESG Issuer Profile Scores

Source: Moody's Investors Service

Environmental

Sparbanken Syd faces moderate environmental risks largely stemming from its portfolio exposure to carbon transition risk. Like its peers, Sparbanken Syd is facing mounting regulatory and stakeholder pressure to meet broader carbon transition goals. The bank's focus on sustainability will help mitigate the risks.

Social

Sparbanken Syd faces high industry-wide social risks related to customer relations and associated regulatory and litigation risks, requiring high compliance standards. These risks are mitigated by the bank's developed policies and procedures. High cyber and personal data risks are mitigated by the bank's strong IT framework and its cooperation with SDC as IT provider.

Governance

Sparbanken Syd's governance risks mainly reflect the bank's strategic challenges in addressing the low profitability and remaining execution risk in shifting funding source of its mortgages, reflected in a one notch negative adjustment for corporate behaviour. Sparbanken Syd's partnership with Borgo Hypotek AB for originating mortgages, has resolved the immediate funding challenges. However, there may still be structural challenges for Sparbanken Syd as a small shareholder in Borgo to get across their voice in strategic decisions. Sparbanken Syd is a community owned savings bank, with customer representatives voting at the annual general meetings. We consider these to be passive shareholders, reducing risks related to board independence and control. Governance risks are further mitigated by Sweden's developed institutional framework.

ESG Issuer Profile Scores and Credit Impact Scores for the rated entity/transaction are available on Moodys.com. In order to view the latest scores, please click [here](#) to go to the landing page for the entity/transaction on MDC and view the ESG Scores section.

Support and structural considerations**Affiliate support**

Sparbanken Syd is an independent savings bank and, consequently, the bank does not benefit from any affiliate support.

Loss Given Failure (LGF) analysis

We apply our Advanced LGF Analysis on Sparbanken Syd because the bank is subject to the European Union Bank Recovery and Resolution Directive, which we consider an operational resolution regime. For this analysis, we assume that equity and losses are 3% and 8%, respectively, of tangible banking assets in a failure scenario. We also assume a 25% runoff in junior wholesale deposits and a 5% runoff in preferred deposits. Moreover, we assign a 25% probability to junior deposits being preferred to senior unsecured debt. These are in line with our standard assumptions. We assume the bank's junior deposits account for 26% of total deposits, in line with banks with a diversified deposit base.

The deposit and issuer ratings have a very low loss rate given failure, indicated by a two notch uplift under Moody's Advanced LGF Analysis, because of the large volume of subordinated and senior unsecured debt, providing a cushion of protection to creditors in case of failure.

Government support

Sparbanken Syd's deposit market share was small at around 0.1% as of year-end 2021. Given the limited scope of the bank's operations and its low market share in deposits, we assume a low probability of government support in case of need. As a result, Sparbanken Syd's deposit and issuer ratings do not benefit from any uplift because of government support.

Counterparty Risk (CR) Assessment

The CR Assessment of Sparbanken Syd are A3(cr)/Prime-2(cr)

The CR Assessment is positioned at A3(cr)/P-2(cr), three notches above the Adjusted BCA of baa3, based on the buffer against default provided by junior deposits, senior unsecured debt and subordinated debt and does not benefit from any government support.

Counterparty Risk Ratings (CRRs)

The CRR's of Sparbanken Syd are A3/Prime-2

The CRRs at A3/P-2 are positioned three notches above the Adjusted BCA of baa3, reflecting extremely low loss given failure from the high volume of instruments that are subordinated to CRR liabilities.

Methodology and scorecard

About Moody's Bank Scorecard

Our scorecard is designed to capture, express and explain in summary form our Rating Committee's judgement. When read in conjunction with our research, a fulsome presentation of our judgement is expressed. As a result, the output of our scorecard may materially differ from that suggested by raw data alone (though it has been calibrated to avoid the frequent need for strong divergence). The scorecard output and the individual scores are discussed in rating committees and may be adjusted up or down to reflect conditions specific to each rated entity.

Rating methodology and scorecard factors

Exhibit 9

Sparbanken Syd

Macro Factors							
Weighted Macro Profile		Strong +	100%				
Factor	Historic Ratio	Initial Score	Expected Trend	Assigned Score	Key driver #1	Key driver #2	
Solvency							
Asset Risk							
Problem Loans / Gross Loans	0.7%	aa2	↔	baa1	Sector concentration	Geographical concentration	
Capital							
Tangible Common Equity / Risk Weighted Assets (Basel III - transitional phase-in)	18.8%	aa2	↔	a1	Access to capital		
Profitability							
Net Income / Tangible Assets	0.2%	b1	↓	b2	Expected trend		
Combined Solvency Score		a2		baa1			
Liquidity							
Funding Structure							
Market Funds / Tangible Banking Assets	18.0%	a3	↑↑	baa1	Lack of market access		
Liquid Resources							
Liquid Banking Assets / Tangible Banking Assets	17.9%	baa2	↑↑	a2	Expected trend		
Combined Liquidity Score		baa1		a3			
Financial Profile				baa1			
Qualitative Adjustments				Adjustment			
Business Diversification				0			
Opacity and Complexity				0			
Corporate Behavior				-1			
Total Qualitative Adjustments				-1			
Sovereign or Affiliate constraint				Aaa			
BCA Scorecard-indicated Outcome - Range				baa1 - baa3			
Assigned BCA				baa3			
Affiliate Support notching				0			
Adjusted BCA				baa3			
Balance Sheet		in-scope (SEK Million)	% in-scope	at-failure (SEK Million)	% at-failure		
Other liabilities		1,487	10.4%	2,529	17.7%		
Deposits		10,208	71.5%	9,167	64.2%		
Preferred deposits		7,554	52.9%	7,176	50.3%		
Junior deposits		2,654	18.6%	1,991	13.9%		
Senior unsecured bank debt		1,998	14.0%	1,998	14.0%		
Dated subordinated bank debt		150	1.1%	150	1.1%		
Equity		428	3.0%	428	3.0%		
Total Tangible Banking Assets		14,272	100.0%	14,272	100.0%		

Debt Class	De Jure waterfall		De Facto waterfall		Notching		LGF	Assigned	Additional	Preliminary
	Instrument	Sub-	Instrument	Sub-	De Jure	De Facto	Notching	LGF		
	volume +	ordination	volume +	ordination			Guidance	notching		Rating
	subordination		subordination				vs.			Assessment
							Adjusted			
							BCA			
Counterparty Risk Rating	32.0%	32.0%	32.0%	32.0%	3	3	3	3	0	a3
Counterparty Risk Assessment	32.0%	32.0%	32.0%	32.0%	3	3	3	3	0	a3 (cr)
Deposits	32.0%	4.1%	32.0%	18.1%	2	3	2	2	0	baa1
Senior unsecured bank debt	32.0%	4.1%	18.1%	4.1%	2	2	2	2	0	baa1

Instrument Class	Loss Given		Additional	Preliminary Rating	Government		Local Currency	Foreign
	Failure	notching			Support	notching	Rating	Currency
				Assessment				Rating
Counterparty Risk Rating	3		0	a3		0	A3	A3
Counterparty Risk Assessment	3		0	a3 (cr)		0	A3(cr)	
Deposits	2		0	baa1		0	Baa1	Baa1
Senior unsecured bank debt	2		0	baa1		0	Baa1	Baa1

[1] Where dashes are shown for a particular factor (or sub-factor), the score is based on non-public information.

Source: Moody's Investors Service

Ratings

Exhibit 10

Category	Moody's Rating
SPARBANKEN SYD	
Outlook	Positive
Counterparty Risk Rating	A3/P-2
Bank Deposits	Baa1/P-2
Baseline Credit Assessment	baa3
Adjusted Baseline Credit Assessment	baa3
Counterparty Risk Assessment	A3(cr)/P-2(cr)
Issuer Rating	Baa1
ST Issuer Rating	P-2

Source: Moody's Investors Service

Endnotes

¹ The ratings shown in this report are the long-term senior unsecured and long-term deposit ratings, and the Baseline Credit Assessment.

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