MOODY'S
INVESTORS SERVICE

CREDIT OPINION

15 July 2021

Update

Rate this Research

RATINGS

Skandiabanken AB

Domicile	Sweden
Long Term CRR	Aa3
Type	LT Counterparty Risk Rating - Fgn Curr
Outlook	Not Assigned
Long Term Debt	Not Assigned
Long Term Deposit	A2
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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Skandiabanken AB

Update to following rating action and publication of new Banks Methodology

Summary

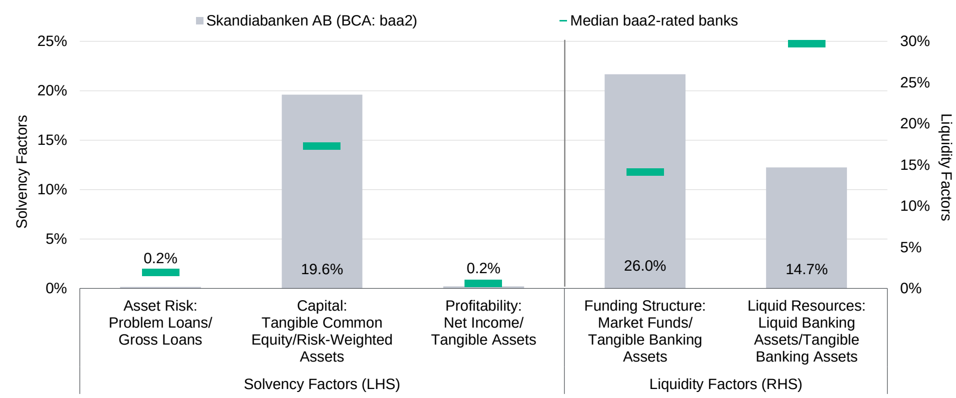
We assign Skandiabanken AB (Skandiabanken) A2/Prime-1 long-term and short-term deposit ratings with a positive outlook, a baa2 Baseline Credit Assessment (BCA) and an a3 Adjusted BCA. We also assign long-term and short-term Counterparty Risk (CR) Assessments of Aa3(cr)/Prime-1(cr).

Skandiabanken's baa2 BCA reflects the bank's very low asset risk as a Swedish mortgage lender, strong capital and healthy funding structure focusing on retail deposits. These strengths are balanced against Skandiabanken's historically above-market growth rate in mortgage lending, as well as the bank's low efficiency and weak profitability. The Adjusted BCA of a3 reflects our very high assumption of affiliate support from the bank's parent, Livförsäkringsbolaget Skandia, ömsesidigt (Skandia Liv, A2 stable).

Skandiabanken's A2 long-term deposit rating also includes a one-notch uplift resulting from our Advanced Loss Given Failure (LGF) analysis, reflecting our view that the bank's junior depositors face a low unexpected Loss Given Failure.

Exhibit 1

Rating Scorecard — Key financial ratios



These are our Banks Methodology scorecard ratios. Asset risk and profitability ratios reflect the weaker of either the latest reported or three-year average ratios. The capital ratio is the latest reported figure. Funding structure and liquid resources ratios reflect the latest year-end figures.
Source: Moody's Financial Metrics

Credit strengths

» Very strong asset quality

» Strong capitalisation

» Very strong support from Skandia group

Credit challenges

» Historically high lending growth

» Lower-than-peer efficiency and weak profitability

Outlook

The positive outlook on Skandiabanken's deposit ratings reflects that Skandiabanken's internal MREL requirements to its parent may result in greater protection to the bank's senior creditors.

Factors that could lead to an upgrade

» An upgrade to the rating of Skandia Liv could result in higher ratings on the bank.

» Skandiabanken's BCA could be upgraded if the bank continues to deliver on its cost efficiency program resulting in increased recurring profitability over time. However, a higher BCA would not necessarily lead to a higher adjusted BCA and higher ratings.

» The long-term deposit ratings could also be upgraded if Skandiabanken's changing liability structure results in higher volumes of loss absorbing obligations leading to higher protection to depositors in case of failure.

Factors that could lead to a downgrade

Although currently unlikely, downward pressure could emerge if:

» A downgrade to Skandia Liv's ratings leading to a reduced level of affiliate support uplift, or a change in our assessment of the probability of parental support would result in a lower Adjusted BCA.

» Although we consider this less likely, a significant deterioration in the bank's fundamentals, including asset quality and capitalisation, could lead to a downgrade of the BCA and most likely of the Adjusted BCA.

Key indicators

Exhibit 2

Skandiabanken AB (Consolidated Financials) [1]

	03-21[2]	12-20[2]	12-19[2]	12-18[2]	12-17[2]	CAGR/Avg.[3]
Total Assets (SEK Million)	91,467.0	89,934.0	81,707.0	72,044.0	69,407.0	8.9[4]
Total Assets (USD Million)	10,493.8	10,950.8	8,728.4	8,126.0	8,477.2	6.8[4]
Tangible Common Equity (SEK Million)	4,498.0	4,403.0	4,150.0	3,622.0	3,621.0	6.9[4]
Tangible Common Equity (USD Million)	516.0	536.1	443.3	408.5	442.3	4.9[4]
Problem Loans / Gross Loans (%)	0.2	0.2	0.1	0.1	0.0	0.1[5]
Tangible Common Equity / Risk Weighted Assets (%)	19.6	19.6	19.7	19.4	15.4	18.7[6]
Problem Loans / (Tangible Common Equity + Loan Loss Reserve) (%)	2.8	3.3	1.4	1.5	0.4	1.9[5]
Net Interest Margin (%)	0.9	1.0	1.0	1.1	1.2	1.0[5]
PPI / Average RWA (%)	1.4	1.3	0.5	0.4	0.8	0.9[6]
Net Income / Tangible Assets (%)	0.3	0.3	0.2	0.1	0.2	0.2[5]
Cost / Income Ratio (%)	69.7	71.9	87.7	94.4	81.2	81.0[5]
Market Funds / Tangible Banking Assets (%)	27.2	26.0	25.8	22.5	22.4	24.8[5]
Liquid Banking Assets / Tangible Banking Assets (%)	14.0	14.7	12.4	15.6	13.8	14.1[5]
Gross Loans / Due to Customers (%)	181.7	174.8	175.3	147.8	152.6	166.4[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

Further to the publication of our revised methodology in July 2021, for issuers that have "high trigger" Additional Tier 1 instruments outstanding, not all ratios included in this report reflect the change in treatment of these instruments.

Profile

Skandiabanken AB (Skandiabanken) is a Stockholm-based bank that provides retail banking products and services, as well as mutual funds, and equity trading in Sweden. While the bank does not have any branches, it sells banking services through the branch network of the wider Skandia group. As of end-March 2021, Skandiabanken's consolidated asset base was SEK91.5 billion (€8.9 billion) and the bank had a market share of around 2% in the Swedish mortgage market.

For further information on the bank's profile, please see Skandiabanken AB: Key Facts and Statistics - 9M September 2018, published on 13 November 2018.

Recent developments

We expect real GDP in all G-20 countries to grow compared with last year, but some countries will take longer than others to return to full capacity. Fiscal and monetary policy response, as well as pandemic management, will continue to play a key role.

However, our outlook for the Swedish banking system remains stable. We expect the operating environment in Sweden to remain weak in 2021, following the pandemic-induced disruption in 2020. Although support measures by authorities designed to counterbalance the slowdown have mitigated the immediate economic and financial restrictions, we expect a rise in business closures and unemployment, as some measures come to an end. In Sweden, we expect asset quality to decline in 2021, although from a strong starting point and despite the likely recovery in economic growth. The most affected sectors are leisure and accommodation, while mortgage impairments are likely to rise only marginally, if at all.

Detailed credit considerations

A limited standalone franchise with growing importance in the wider Skandia group

On 30 September 2020, Skandiabanken's ownership was transferred to the ultimate parent in the group, Skandia Liv, a leading Swedish life insurer, from Skandia Insurance Company Ltd (SICL), the unit linked policy provider within the group.

Skandiabanken focuses on mortgage lending and aims to grow its fees and commissions by increasing the volume of customer transactions, both savings and payments. The bank sells its products on the internet, by phone and through the branch network of the wider Skandia insurance group (54 branches). We consider it a monoline business focused on mortgages, with earnings highly dependent on retail interest income, which represented around 82% of its operating income in 2020. This structural dependence results in a one-notch qualitative downward adjustment to the bank's BCA for Business Diversification, an adjustment shared with most Swedish mortgage lenders.

Skandiabanken has ambitious growth targets. Despite growing significantly in the last few years (see exhibit 3), with a reported SEK76 billion mortgage loans at year-end 2020, the bank just missed its volume target of SEK80 billion in mortgages.

In 2018, the bank started targeting Skandia group's customers offering large rebates for occupational insurance clients with low loan-to-value (LTV) ratios. This strategy gathered significant interest and Skandiabanken's lending increased by 20% in 2019. However, loan growth slowed to 5.4% in 2020. If the bank succeeds in reaching its current target of SEK80 billion in mortgage lending, a 5% growth from that as of year-end 2020, it will be better placed to improve its efficiency without significantly altering its risk profile.

In October 2015, Skandiabanken spun off its Norwegian business, which had accounted for 54% of its total lending as of 30 September 2015.

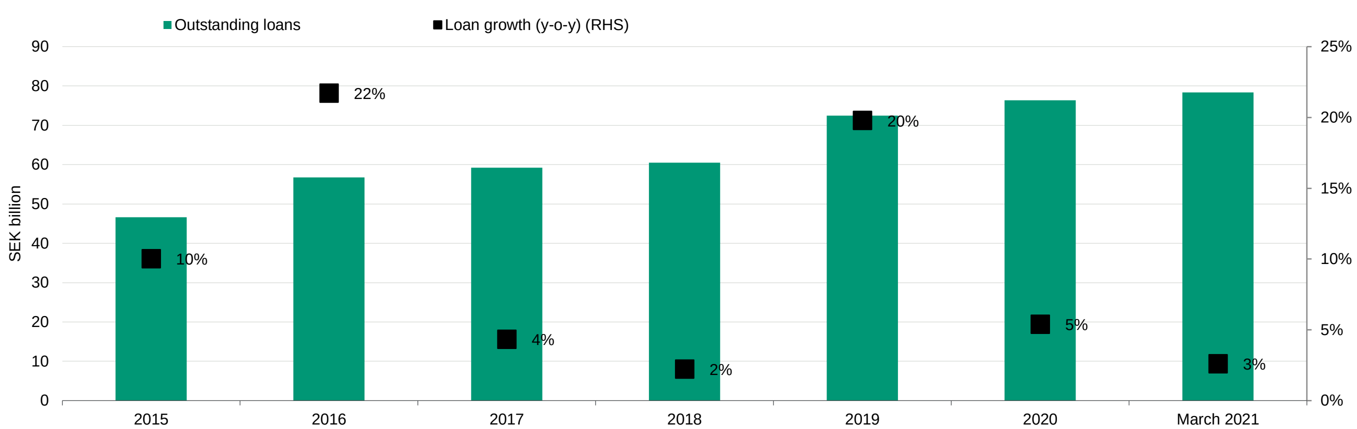
Strong asset quality reflecting low risk mortgage lending, which will remain resilient in the aftermath of the economic recession

While the pandemic-led disruption has led to a deterioration in the Swedish economy and higher levels of unemployment, the large government support packages to households and businesses have so far mitigated the risk of an important deterioration in asset quality. Although the economic impact from the disruption will be negative for Swedish banks, we expect Skandiabanken's asset quality to remain stable because of its focus on low risk mortgage lending. In August 2021 the temporary amortisation relief will be discontinued which may a have a potential but limited impact on borrowers repayment capacity.

Our aa3 Asset Risk score reflects Skandiabanken’s very low problem loan ratio — in line with that of its Swedish mortgage peers — balanced against its significant lending growth over the last few years, resulting from the strategic plan to increase the bank’s market share and size (see Exhibit 3).

Skandiabanken's loan book grew to SEK78.4 billion as of end-March 2021, from SEK76.4 billion by year-end 2020, a 2.6% increase in the first three months of 2021. Skandiabanken aims to sustain its mortgage lending growth by offering its customers a transparent pricing model and rates that are among the lowest in the market. By increasing cross-selling to Skandia group's clients with low LTVs, the bank is able to grow while maintaining prudent asset quality metrics. Skandiabanken also had placements with the Swedish National Debt Office amounting to SEK2.7 billion as of the end of March 2021.

Exhibit 3
Skandiabanken's lending growth was 2.6% in the first three months of 2021
Outstanding loans to the public



Source: Moody's Investors Service

Skandiabanken's problem loan ratio as of the end of March 2021 was 0.16%, up from 0.08% as of year-end 2019, which is comparable to domestic mortgage lenders, but considerably lower than most European peers. The bank updated its definition of probability of default in fourth quarter 2020, which resulted in an increase in the number of loans in stage 3. Skandiabanken considers that these additional loans have sound collateral and hence a low need for provisions, leading to a reduction in the reserves ratio for stage 3. Skandiabanken's loan book consists almost entirely of mortgages, 96% of total lending as of end-March 2021. Its asset quality has benefited from low interest rates and the Swedish households' ability to service their debt amid the ongoing disruptions caused by the coronavirus pandemic and Skandiabanken's loan loss provisions/gross loans remained low at 0.02% as of year-end 2020 compared with 0.01% as of year-end 2019.

The LTV ratio of the bank's mortgage portfolio (exposure-weighted) stood at a low around 51% as of end of March 2021. The bank implemented stricter underwriting standards by introducing caps on the debt-to-income ratio in 2016 and higher stressed interest rates in its loan approval process in 2017. The bank's current underwriting standards are aligned with those of its peers.

High capitalisation, benefitting from affiliate support from its insurance parent

We view Skandiabanken's capitalisation as strong, given its business model, which is focused on low risk mortgage lending. Our aa3 assigned Capital score reflects the bank's strong capitalisation, but also the increasing leverage. The relatively weak internal capital generation is partly mitigated by the parent having a history of supporting Skandiabanken through direct capital injections (2014 and 2015).

As of March 2018, Skandiabanken received approval from the SFSA to apply the internal ratings-based (IRB) approach for exposures with collateral in real estate. As of end-March 2021, the bank reported a Common Equity Tier 1 capital ratio of 18.1%, compared with 18.5% as of year-end 2020, which also includes the 25% mortgage risk weight floor in Pillar I. Skandiabanken's tangible common equity/total tangible assets was 4.9% as of end-March 2021, and we therefore apply a negative adjustment due to the leverage ratio being below 5%.

Gradual improvement in profitability due to cost efficiency measures and increased business volumes

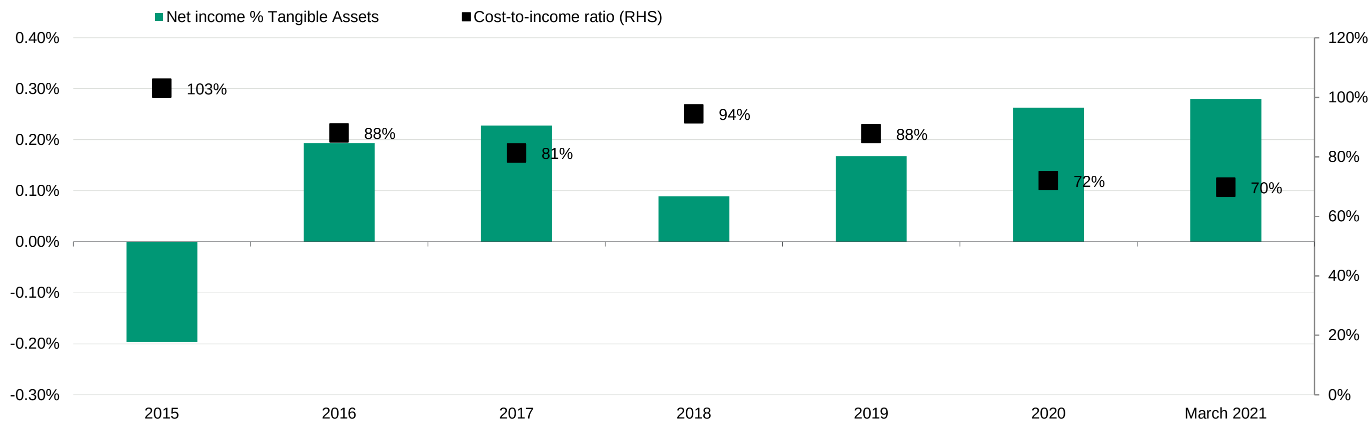
The b3 Profitability score reflects Skandiabanken's weaker-than-peer profitability, with net income/tangible assets of 0.28% for the first three months of 2021, resulting from its more aggressive pricing strategy and its relatively low efficiency. We expect profitability to gradually improve over the next 12-18 months due to continued cost reduction efforts and growing business volumes. While the strategy to grow volumes by focusing on low margin mortgages to Skandia group customers will not necessarily help their net interest margin, the higher lending volumes will support the bank's cost efficiency.

Skandabanken's profitability improved by 33% with net income of SEK64 million in January-March 2021 compared to SEK48 million for the same period the previous year. The improvement was mainly related to reduced fee and commission costs as well as credit costs.

Skandiabanken's net income increased to SEK236 million in 2020, compared to SEK137 million in 2019. This increase was driven by a 13.8% year-on-year increase in net interest income. The bank's operating expenses amounted to SEK728 million for 2020, lower than the SEK792 million in 2019, primarily due to 10% year-on-year lower administrative expenses. The bank's cost-to-income ratio decreased in 2020 to 72% from around 88% in 2019 (see Exhibit 4), which is a clear improvement, but still significantly weaker compared to Swedish peers, which report a weighted average cost-to-income ratio near or below 45%.

In the coming years, Skandiabanken plans to reduce its cost base and increase efficiency through economies of scale, and targets a cost-to-income ratio of 60%. Because of its limited size, we expect that it will be difficult to reduce IT costs, regulatory and compliance costs, as well as general administration costs, significantly, and, believe that improvements in the bank's cost-to-income ratio primarily will come from increased revenue derived from lending growth.

Exhibit 4
Skandiabanken is gradually improving efficiency



Source: Moody's Investors Service

A retail-based funding profile and adequate liquidity

The a3 Funding Structure score captures Skandiabanken's high proportion of retail deposits and our expectation of an increase in the bank's reliance on wholesale funding to support balance-sheet growth. This reliance is, however, mitigated by the fact that most of the issuance will be in SEK denominated covered bonds, which we consider more resilient than most other covered bonds as they benefit from a large domestic investor base. We reflect this feature by making an additional positive adjustment for covered bonds denominated in local currency for all Swedish banks.

The bank's retail deposits were SEK43.1 billion as of end-March 2021, or 50% of the non-equity funding. Most of these retail deposits are internet based because the bank does not have its own branch network and we consider these to be more price and confidence sensitive than deposits sourced through branches. Skandiabanken's loan-to-deposit ratio was 188% as of end-March 2021, compared with 175% as of year-end 2020. Skandiabanken's funding as of end of March 2021 included issued debt securities of SEK36.2 billion in covered bonds, SEK5.2 billion of senior unsecured funding and internally issued to the parent SEK0.5 billion senior non-preferred debt and SEK0.5 billion of subordinated debt.

On 31 December 2019, Skandiabanken took a SEK500 million subordinated loan from its ultimate owner, Skandia Liv. This loan is eligible for bail-in and can therefore be counted towards fulfilling the bank's minimum requirements for own funds and eligible liabilities (MREL), which is 4.8% of its total liabilities and own funds from 1 January 2021. The bank intends to issue senior non-preferred debt to fulfil its subordination requirements ahead of the deadline on 1 January 2024. However, the revised Bank Recovery and Resolution Directive (BRRD2), which is in the process of being implemented in Sweden may alter the MREL requirements. The new requirements will be communicated in December 2021.

The bank's liquid resources/tangible banking assets was 11.0% as of end-March 2021, and its reported liquidity reserves were SEK11.5 billion. The portfolio consists mainly of cash and balances with central banks, and highly rated government securities and secured and unsecured debt issued by financial institutions, mostly in the Nordics. Skandiabanken reported a liquidity coverage ratio of 301% as of end-March 2021, up from 238% as of year-end 2019. Skandiabanken's liquidity is adequate as captured by our ba1 assigned Liquid Resources score.

Source of facts and figures cited in this report

Bank-specific figures originate from the banks' reports and Moody's Banking Financial Metrics. All figures are based on our own chart of accounts and may be adjusted for analytical purposes. Please refer to the document Financial Statement Adjustments in the Analysis of Financial Institutions, published on 9 August 2018.

ESG considerations

In line with our general view for the banking sector, Skandiabanken has a low exposure to environmental risks. See our Environmental risk heat map for further information.

The most relevant social risks for banks arise from the way they interact with their customers. Social risks are particularly high in the area of data security and customer privacy, which are partly mitigated by sizeable technology investments and banks' long track record of handling sensitive client data. Fines and reputational damage because of product mis-selling or other types of misconduct are a further social risk. Societal trends are also relevant in a number of areas, such as shifting customer preferences towards digital banking services increasing information technology cost, ageing population concerns in several countries affecting demand for financial services or socially driven policy agendas that may translate into regulation that affects banks' revenue base. Overall, banks, including Skandiabanken, face moderate social risks. See our Social risk heat map for details.

Governance is highly relevant for Skandiabanken, as it is to all participants in the banking industry. Corporate governance weaknesses can lead to a deterioration in a bank's credit quality, while governance strengths can benefit its credit profile. Governance risks are largely internal rather than externally driven. For Skandiabanken, risks related to governance are considered low, and we do not apply any corporate behaviour adjustment to the bank.

Support and structural considerations

Affiliate support

The a3 Adjusted BCA incorporates our assessment of a very high probability of support from the bank's parent Skandia Liv in the event of need. The Skandia insurance group has a history of supporting Skandiabanken through direct capital injections, with SEK1.7 billion in 2015 and SEK981 million in 2014.

Loss Given Failure (LGF) analysis

We apply our Advanced LGF analysis to Skandiabanken as the bank is subject to the EU BRRD, 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. Given the bank's focus on retail deposits, we assume the bank's junior deposits to account for 10% of total deposits, in line with other retail mortgage banks.

The considerable buffer of outstanding senior unsecured debt and junior deposits provides a loss-absorption buffer in case of failure, and indicates a one notch uplift in the bank's deposit rating above the a3 Adjusted BCA, as indicated by our Advanced LGF analysis.

Skandiabanken is subject to internal MREL requirements, and we expect Skandiabanken to issue junior senior debt to the parent Skandia Liv in order to meet its subordination requirements. We include this additional loss absorbing capacity in our LGF analysis of Skandiabanken.

Government support considerations

Because of the relatively small size of its retail operations, we assume a low probability of government support for Skandiabanken's long-term deposit ratings.

Counterparty Risk (CR) Assessment

Skandiabanken's CR Assessment is Aa3(cr)/P-1(cr)

Skandiabanken's CR Assessment is positioned at Aa3(cr)/P-1(cr), based on the buffer against default provided by junior deposits, senior unsecured and subordinated debt, and does not benefit from any government support, in line with the deposit debt ratings.

Counterparty Risk Ratings (CRRs)

Skandiabanken's CRRs are Aa3/P-1

The CRRs are positioned three notches above Skandiabanken's Adjusted BCA of a3, reflecting extremely low loss given failure from the high volume of instruments that are subordinated to CRR liabilities.

Rating methodology and scorecard factors

Exhibit 5
Skandiabanken AB

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	0.2%	aa1	↔	aa3	Sector concentration	Loan growth
Capital						
Tangible Common Equity / Risk Weighted Assets (Basel III - transitional phase-in)	19.6%	aa2	↔	aa3	Nominal leverage	
Profitability						
Net Income / Tangible Assets	0.2%	b1	↔	b3	Return on assets	
Combined Solvency Score		a1		a3		
Liquidity						
Funding Structure						
Market Funds / Tangible Banking Assets	26.0%	baa2	↑↑	a3	Market funding quality	
Liquid Resources						
Liquid Banking Assets / Tangible Banking Assets	14.7%	ba1	↔	ba1	Stock of liquid assets	
Combined Liquidity Score		baa3		baa2		
Financial Profile				baa1		
Qualitative Adjustments				Adjustment		
Business Diversification				-1		
Opacity and Complexity				0		
Corporate Behavior				0		
Total Qualitative Adjustments				-1		
Sovereign or Affiliate constraint				Aaa		
BCA Scorecard-indicated Outcome - Range				baa1 - baa3		
Assigned BCA				baa2		
Affiliate Support notching				-		
Adjusted BCA				a3		

Balance Sheet	in-scope (SEK Million)	% in-scope	at-failure (SEK Million)	% at-failure
Other liabilities	39,314	43.0%	42,334	46.3%
Deposits	43,144	47.2%	40,124	43.9%
Preferred deposits	38,830	42.5%	36,888	40.4%
Junior deposits	4,314	4.7%	3,236	3.5%
Senior unsecured bank debt	5,200	5.7%	5,200	5.7%
Junior senior unsecured bank debt	500	0.5%	500	0.5%
Dated subordinated bank debt	500	0.5%	500	0.5%
Equity	2,742	3.0%	2,742	3.0%
Total Tangible Banking Assets	91,400	100.0%	91,400	100.0%

Debt Class	De Jure waterfall		De Facto waterfall		Notching		LGF Notching Guidance vs. Adjusted 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 Rating	13.3%	13.3%	13.3%	13.3%	3	3	3	3	0	aa3
Counterparty Risk Assessment	13.3%	13.3%	13.3%	13.3%	3	3	3	3	0	aa3 (cr)
Deposits	13.3%	4.1%	13.3%	9.8%	1	2	1	1	0	a2

Instrument Class	Loss Given Failure notching	Additional notching	Preliminary Rating Assessment	Government Support notching	Local Currency Rating	Foreign Currency Rating
Counterparty Risk Rating	3	0	aa3	0	Aa3	Aa3
Counterparty Risk Assessment	3	0	aa3 (cr)	0	Aa3(cr)	
Deposits	1	0	a2	0	A2	A2

[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 6

Category	Moody's Rating
SKANDIABANKEN AB	
Outlook	Stable
Counterparty Risk Rating	Aa3/P-1
Bank Deposits	A2/P-1
Baseline Credit Assessment	baa2
Adjusted Baseline Credit Assessment	a3
Counterparty Risk Assessment	Aa3(cr)/P-1(cr)
PARENT: LIVFOERSAEKRINGSBOLAGET SKANDIA, OEMSESIDIGT	
Outlook	Stable
Insurance Financial Strength	A2

Source: Moody's Investors Service

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