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Rating Action: Moody's takes rating actions on Irish banks

Global Credit Research - 19 Sep 2016

Rating actions follow the change in the country's Macro Profile to 'Strong' from 'Moderate+'

London, 19 September 2016 -- Moody's Investors Service has today upgraded the deposit ratings of three Irish banks: Allied Irish Banks, p.l.c. (AIB), Bank of Ireland (BoI) and Permanent tsb p.l.c. (PTSB). The deposit ratings on KBC Bank Ireland PLC (KBCI), Ulster Bank Limited (UBL) and Ulster Bank Ireland DAC (UBID) were affirmed. The rating actions were driven by a sharply improved operating environment, which led to an increase in the Macro Profile of Ireland (A3 positive) to 'Strong' from 'Moderate+' under Moody's banking methodology, as well as favourable developments in other credit fundamentals, notably asset quality.

As part of the same action, Moody's upgraded the baseline credit assessments (BCA) of AIB, BoI, PTSB, UBID and UBL and affirmed the BCA of KBCI. The rating agency upgraded the senior unsecured ratings of AIB and PTSB and affirmed the senior unsecured ratings of BoI. Moody's maintained the positive outlook on BOI, AIB and UBL's long-term senior unsecured debt ratings and changed the outlook to positive from stable on the long-term senior ratings of UBID and PTSB. The outlook on the deposit rating of KBCI remains stable.

"The main driver for the rating actions is the improvement in credit conditions in the banking system following the rapid and material deleveraging of the private sector, as well as stronger funding conditions as most banks have regained the ability to issue different debt instruments. These positive developments have been reflected in an increase in Moody's Macro Profile for Ireland," says Laurie Mayers, an Associate Managing Director at Moody's. "The rating actions also incorporate the strengthening of the banks' credit fundamentals, especially the progress they have made in reducing non-performing assets, improving the quality of earnings and strengthening their capital metrics."

A full list of affected ratings can be found at the end of this press release.

RATINGS RATIONALE

Moody's rating methodology for banks includes an assessment of each individual country's operating environment, expressed as a Macro Profile, which is designed to capture system-wide factors that are predictive of the propensity of banks to fail. The Macro Profile assigned to each bank informs the financial factors, which are key inputs into the determination of each bank's baseline credit assessment (BCA).

Today's actions reflect the following considerations: (1) the increase in Ireland's Macro Profile to 'Strong' from 'Moderate+'; and (2) improvements in other credit fundamentals, notably asset quality, capital and profitability.

CHANGE IN THE MACRO PROFILE TO 'STRONG' FROM 'MODERATE+'

Moody's has changed Ireland's Macro Profile to 'Strong' from 'Moderate+' to reflect the improvements in the banks' funding conditions and the deleveraging of the private sector.

Following the banking crisis, capital market conditions for the Irish banks have materially improved, with the three largest domestic banks (AIB, BOI and PTSB) able to issue capital and hybrid capital instruments in 2015. The rating agency believes that Irish banks will continue to maintain their access to the market at competitive prices during 2016, and will potentially increase their debt issuance.

Irish private sector debt remains very high compared to other European peers', but is rapidly declining. Irish households' debt-to-gross disposable income ratio decreased to 170% at end-2015 from 185% at end-2014. The Irish banking sector remains highly concentrated, which provides banks with pricing power.

SPECIFIC ANALYTICAL FACTORS FOR THE SIX BANKS

AIB

The upgrade of AIB's ratings was driven by the upgrade of the bank's BCA to ba2 from ba3.

AIB's BCA of ba2 reflects the bank's: (1) very high, albeit decreasing, stock of problem loans compared to European peers, partly mitigated by the relatively high coverage levels and strong operating environment; (2) solid capital levels, with a relatively high tangible common equity (TCE) over risk-weighted assets (RWA) ratio of 16.7%; (3) still modest core profitability, partly offset by improvements in quality of earnings and recovery toward a sustainable business model; and (4) a funding profile rebalanced toward customer deposits and a comfortable liquidity position.

The positive outlook on AIB's long-term deposit and debt ratings reflects the improving trends in asset quality and quality of earnings.

AIB's long-term debt and deposit ratings could be upgraded as a result of: (1) an upgrade in its standalone ba2 BCA; or (2) a significant increase in the bank's bail-in-able debt. The bank's BCA could be upgraded because of: (1) a further reduction in non-performing loans; (2) an increase in solvency ratios beyond Moody's expectations; and (3) a sustained improvement in pre-provision profitability.

AIB's ratings could be downgraded as a result of: (1) a downgrade of its standalone ba2 BCA; or (2) redemption of maturing subordinated instruments without their replacement. AIB's BCA could be downgraded because of: (1) a deterioration in the bank's asset risk metrics; (2) a weakening of its solvency profile; and (3) a worsening of its core profitability ratios.

BOI

The upgrade of BOI's deposit ratings was driven by the upgrade of the bank's BCA to ba1 from ba2.

The upgrade of BOI's BCA reflects the bank's: (1) significant improvements in asset quality, reflected in the bank's problem loan ratio, which declined to 9.7% as of June 2016 from 13.6% a year earlier; (2) maintenance of adequate capital levels despite headwinds, such as the negative impact of the defined benefit plan deficit volatility; (3) improved profitability, in particular, stronger core income generation; and (4) lower reliance on market funding, reflected in a decline in the market funds to tangible banking assets ratio to 9.3% as of June 2016 from 11.5% as of June 2015. Moody's believes the bank's funding structure will now stabilize close to the current level.

The Baa2 senior unsecured rating was affirmed because the upgrade of the bank's BCA was offset by a reduction of one notch in the uplift resulting from Moody's Advanced Loss Given Failure (LGF) analysis. The senior unsecured rating now benefits from only one notch of uplift from Moody's Advanced LGF analysis and one notch of government support, which remains unchanged at one notch.

The positive outlook on BOI's long-term deposits and senior debt ratings reflects the improving trends in the bank's financial strength, in particular Moody's expectation of a further reduction of problem loans. The positive outlook on senior debt also reflects Moody's expectation of additional subordinated debt issuance, which would reduce its loss-given-failure.

BOI's long-term debt and deposit ratings could be upgraded as a result of: (1) an upgrade in its standalone ba1 BCA; or (2) a significant increase in the bank's bail-in-able debt. The bank's BCA could be upgraded driven by: (1) further reductions in non-performing loans; (2) improved capital metrics; while maintaining (3) stable profitability, funding and liquidity metrics.

BOI's ratings could be downgraded as a result of: (1) a downgrade of its standalone ba1 BCA; or (2) the redemption of maturing subordinated instruments without their replacement. BOI's BCA could be downgraded because of: (1) a deterioration in the bank's asset quality; (2) increased volatility of its capital metrics; (3) a deterioration of its profitability metrics; or (4) a significant increase in the use of confidence sensitive wholesale funding or a material reduction in liquid assets.

KBCI

The affirmation of KBCI's ratings was driven by the affirmation of the bank's BCA of b3 and its adjusted BCA of ba1.

The affirmation of KBCI's BCA reflects the bank's: (1) improved profitability after net income-to-tangible banking assets increased to 0.6% in 2015 from -0.6% in 2014, according to Moody's calculations; (2) reduced reliance on its parent, KBC Group, for funding following a 22% increase in customer deposits in 2015; and (3) the maintenance of solid capital ratios, albeit still below those of peers. However, the BCA remains constrained by the bank's still high level of problem loans, which is reflected in a 47.4% problem loan ratio as of December

2015, down from 51.5% as of December 2014.

The stable outlook on the deposit ratings reflects Moody's view that further positive pressure on the bank's credit fundamentals is, however, unlikely to affect the bank's adjusted BCA, which is more heavily influenced by KBC's own creditworthiness, as reflected in five notches of affiliate support.

KBCI's long-term deposit ratings could be upgraded as a result of a significant increase in the bank's bail-in-able debt. The bank's BCA could be upgraded due to: (1) significant improvements in asset quality while maintaining adequate capital metrics; (2) continued positive profitability; and (3) a further reduction of the bank's reliance on its parent for funding.

KBCI's ratings could be downgraded as a result of: (1) a downgrade of its standalone BCA; (2) a reduction in the amount of deposits that Moody's considers to be bail-in-able or 'junior'; or (3) a reduction in the likelihood of support from KBC. KBCI's BCA could be downgraded because of: (1) a significant deterioration in the bank's capital level; (2) a reversal in the improving profitability trend; (3) a deterioration in asset quality; or (4) an increase in its reliance on KBC group's funding.

PTSB

Moody's upgrade of PTSB's ratings was driven by its upgrade of the bank's BCA to b3 from caa1.

The upgrade of PTSB's BCA reflects the bank's: (1) strengthened capital metrics following deleveraging and capital issuances with a TCE/ RWA ratio of 17.4% as of June 2016, up from 14.5% as of December 2015; (2) further reduction of downside risk as the bank's problem loan ratio declined to 20.2% as of June 2016 from 21.1% as of December 2015; (3) improving profitability after the bank reported a return to statutory profitability during the first half of 2016; and (4) stable wholesale funding profile, albeit with heavy reliance on monetary authority funding, and adequate liquidity levels.

The positive outlook on PTSB's long-term deposits and senior debt ratings reflects the improving trends in the bank's credit fundamentals, despite the potential decline in the capital and profitability metrics following a potential disposal of its remaining UK non-core portfolio.

PTSB's long-term debt and deposit ratings could be upgraded as a result of: (1) an upgrade of its standalone b3 BCA; or (2) a significant increase in the bank's bail-in-able debt. The bank's BCA could be upgraded due to: (1) continued solid capital metrics following the sale of the remaining UK assets; (2) improved asset quality metrics; and (3) reduced reliance on wholesale funding.

PTSB's ratings could be downgraded as a result of: (1) a downgrade of its standalone b3 BCA; or (2) the redemption of maturing instruments without their replacement. PTSB's BCA could be downgraded because of: (1) a significant deterioration in the bank's capital level; (2) a reversal in the improving profitability trend; (3) a deterioration in asset quality; or (4) a significant increase in the use of confidence sensitive wholesale funding or a material reduction in liquid assets.

UBID

The affirmation of UBID's ratings was driven by the affirmation of the bank's adjusted BCA of ba1. UBID's standalone assessment was upgraded by three notches to ba2 from b2 because of the change of the Macro Profile and strong improvements in its credit fundamentals; however, the bank's adjusted BCA is more heavily influenced by support from its parent, the The Royal Bank of Scotland plc (RBS, A3/A3 positive, ba1).

The bank's BCA of ba2 incorporates: (1) its rapidly reducing stock of problem loans, albeit still high compared to peers'; (2) solid capital levels, which Moody's expects to decline over the outlook period, but to remain adequate in relation to the bank's risk profile; (3) weak, but improving quality of earnings and pre-provision profitability; and (4) balanced funding profile and comfortable liquidity positions.

The adjusted BCA of ba1 incorporates a very high likelihood of affiliate support from RBS. This reflects Moody's view that UBID remains an integral part of RBS's current strategy.

Moody's changed the outlook on all of UBID's long-term ratings to positive from stable in line with the outlook on the ratings of its parent, RBS.

UBID's BCA could be upgraded if the bank continues to strengthen its credit fundamentals, reduces the amount of legacy and non-performing assets on its balance sheet and improves its pre-provision profitability.

An upgrade of the parent's BCA, resulting in a positive change in UBID's adjusted BCA, would also positively affect all ratings. UBID's deposit and issuer ratings could also be upgraded if the bank were to issue significant amounts of senior and/or subordinated long-term debt.

UBID's BCA could be downgraded because of a decline in its capital levels beyond what is already factored into Moody's assessment, a strong increase in the use of market funding and a deterioration in the liquidity position. A downgrade of RBS's BCA could result in a reduced capacity to support UBID and therefore downgrades to all UBID's instrument ratings.

UBL

The affirmation of UBL's ratings was driven by the affirmation of the bank's adjusted BCA at ba1. UBL's standalone assessment was upgraded to ba1 from b1 and fully aligned with the BCA of RBS, the bank's parent.

Moody's upgrade of the bank's BCA to the same level of its parent's standalone assessment was driven by various factors. Firstly, UBL is managed as a unit of the larger RBS retail division, devoted entirely to banking activities in Northern Ireland with its treasury, risk management and some middle and back offices integrated within those of RBS. Secondly, from a regulatory perspective, UBL is already an integral part of RBS, as the bank's capital and liquidity position are assessed at the group level by the regulator. Thirdly, the rating agency expects that with the introduction of the ring-fencing reform, UBL will be part of the ring-fenced sub-group. Finally, from a resolution perspective, UBL is already part of RBS's resolution perimeter in the UK. This is already reflected in the bank's ratings, which are positioned at the same as those of RBS.

The positive outlook on UBL's long-term ratings is primarily driven by the outlook on UBL's parent company, RBS.

Given the high level of integration between UBL and its parent, an upgrade or downgrade of RBS's ratings and/or BCA could trigger an upgrade or downgrade of the bank's ratings and/or BCA.

The principal methodology used in these ratings was Banks published in January 2016. Please see the Ratings Methodologies page on www.moodys.com for a copy of this methodology.

Upgrades:

..Issuer: Permanent tsb p.l.c.

.... LT Bank Deposits (Foreign Currency and Local Currency), Upgraded to Ba3 Positive from B1 Stable

.... Senior Unsecured Regular Bond/Debenture, Upgraded to B1 Positive from B2 Stable

.... Senior Unsecured MTN, Upgraded to (P)B1 from (P)B2

.... Subordinate MTN, Upgraded to (P)Caa1 from (P)Caa2

.... Junior Subordinate MTN, Upgraded to (P)Caa2 from (P)Caa3

.... Adjusted Baseline Credit Assessment, Upgraded to b3 from caa1

.... Baseline Credit Assessment, Upgraded to b3 from caa1

.... Counterparty Risk Assessment, Upgraded to Ba2(cr) from Ba3(cr)

..Issuer: Bank of Ireland

.... LT Bank Deposits (Foreign Currency and Local Currency), Upgraded to Baa1 Positive from Baa2 Positive

.... Subordinate Regular Bond/Debenture, Upgraded to Ba2 from Ba3

.... Junior Subordinated Regular Bond/Debenture, Upgraded to Ba3 (hyb) from B1 (hyb)

.... Subordinate MTN, Upgraded to (P)Ba2 from (P)Ba3

.... Pref. Stock, Upgraded to B1 (hyb) from B2 (hyb)

.... Pref. Stock Non-cumulative, Upgraded to B1 (hyb) from B2 (hyb)

.... Adjusted Baseline Credit Assessment, Upgraded to ba1 from ba2

.... Baseline Credit Assessment, Upgraded to ba1 from ba2

.... Counterparty Risk Assessment, Upgraded to A3(cr) from Baa1(cr)

..Issuer: Bristol & West plc

....Subordinate Regular Bond/Debenture, Upgraded to Ba2 from Ba3

..Issuer: Ulster Bank Ireland DAC

.... Baseline Credit Assessment, Upgraded to ba2 from b2

..Issuer: Ulster Bank Limited

.... Baseline Credit Assessment, Upgraded to ba1 from b1

..Issuer: Allied Irish Banks, p.l.c.

.... LT Bank Deposits (Foreign Currency and Local Currency), Upgraded to Baa2 Positive from Baa3 Positive

.... ST Bank Deposits (Foreign Currency and Local Currency), Upgraded to P-2 from P-3

.... Senior Unsecured Regular Bond/Debenture, Upgraded to Baa3 Positive from Ba1 Positive

.... Subordinate Regular Bond/Debenture, Upgraded to Ba3 from B1

.... Pref. Stock Non-cumulative, Upgraded to B2 (hyb) from B3 (hyb)

.... Senior Unsecured MTN, Upgraded to (P)Baa3 from (P)Ba1

.... Subordinate MTN, Upgraded to (P)Ba3 from (P)B1

.... Junior Subordinate MTN, Upgraded to (P)B1 from (P)B2

.... Other Short Term, Upgraded to (P)P-3 from (P)NP

.... Adjusted Baseline Credit Assessment, Upgraded to ba2 from ba3

.... Baseline Credit Assessment, Upgraded to ba2 from ba3

.... Counterparty Risk Assessment, Upgraded to Baa1(cr) from Baa2(cr)

Issuer: EBS d.a.c.

.... LT Bank Deposits (Foreign Currency and Local Currency), Upgraded to Baa2 Positive from Baa3 Positive

.... Senior Unsecured Regular Bond/Debenture, Upgraded to Baa3 Positive from Ba1 Positive

.... ST Bank Deposits (Foreign Currency and Local Currency), Upgraded to P-2 from P-3

.... Adjusted Baseline Credit Assessment, Upgraded to ba2 from ba3

.... Baseline Credit Assessment, Upgraded to ba2 from ba3

.... Counterparty Risk Assessment, Upgraded to Baa1(cr) from Baa2(cr)

Affirmations:

..Issuer: KBC Bank Ireland PLC

.... LT Bank Deposits (Foreign Currency and Local Currency), Affirmed Ba1 Stable

.... ST Bank Deposits (Foreign Currency and Local Currency), Affirmed NP

.... Backed Commercial Paper, Affirmed P-1

.... Adjusted Baseline Credit Assessment, Affirmed ba1

.... Baseline Credit Assessment, Affirmed b3

.... Counterparty Risk Assessment, Affirmed Baa1(cr)

.... Counterparty Risk Assessment, Affirmed P-2(cr)

..Issuer: Permanent tsb p.l.c.

.... ST Bank Deposits (Foreign Currency and Local Currency), Affirmed NP

.... Other Short Term, Affirmed (P)NP

.... Counterparty Risk Assessment, Affirmed NP(cr)

..Issuer: Bank of Ireland

.... LT Issuer Rating, Affirmed Baa2 Positive

.... Senior Unsecured Regular Bond/Debenture, Affirmed Baa2 Positive

.... Senior Unsecured MTN, Affirmed (P)Baa2

.... ST Bank Deposits (Foreign Currency and Local Currency), Affirmed P-2

.... ST Deposit Note/CD Program, Affirmed P-2

.... Commercial Paper, Affirmed P-2

.... Other Short Term, Affirmed (P)P-2

.... Counterparty Risk Assessment, Affirmed P-2(cr)

..Issuer: Ulster Bank Ireland DAC

.... LT Issuer Rating, Affirmed Ba1 Positive From Stable

.... LT Bank Deposits (Foreign Currency and Local Currency), Affirmed Baa3 Positive From Stable

.... ST Issuer Rating, Affirmed NP

.... ST Bank Deposits (Foreign Currency and Local Currency), Affirmed P-3

.... Adjusted Baseline Credit Assessment, Affirmed ba1

.... Counterparty Risk Assessment, Affirmed Baa1(cr)

.... Counterparty Risk Assessment, Affirmed P-2(cr)

..Issuer: Ulster Bank Limited

.... LT Issuer Rating, Affirmed A3 Positive

.... LT Bank Deposits (Foreign Currency and Local Currency), Affirmed A3 Positive

.... ST Bank Deposits (Foreign Currency and Local Currency), Affirmed P-2

.... Adjusted Baseline Credit Assessment, Affirmed ba1

.... Counterparty Risk Assessment, Affirmed A3(cr)

.... Counterparty Risk Assessment, Affirmed P-2(cr)

..Issuer: Allied Irish Banks, p.l.c.

.... Counterparty Risk Assessment, Affirmed P-2(cr)

..Issuer: EBS d.a.c.

.... Counterparty Risk Assessment, Affirmed P-2(cr)

Withdrawals:

..Issuer: AIB North America, Inc.

.... LT Bank Deposits (Local Currency), Withdrawn RWR, previously rated Baa3 Positive

..Issuer: Allied Irish Banks, NY

.... ST Bank Deposits (Local Currency), Withdrawn , previously rated P-3

Outlook Actions:

..Issuer: KBC Bank Ireland PLC

....Outlook, Remains Stable

..Issuer: Permanent tsb p.l.c.

....Outlook, Changed To Positive From Stable

..Issuer: Bank of Ireland

....Outlook, Remains Positive

..Issuer: Ulster Bank Ireland DAC

....Outlook, Changed To Positive From Stable

..Issuer: Ulster Bank Limited

....Outlook, Remains Positive

..Issuer: Allied Irish Banks, p.l.c.

....Outlook, Remains Positive

..Issuer: EBS d.a.c.

....Outlook, Remains Positive

..Issuer: AIB North America, Inc.

....Outlook, Changed To Rating Withdrawn From Positive

..Issuer: Allied Irish Banks, NY

....Outlook, Changed To Rating Withdrawn From No Outlook

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