MOODY'S
INVESTORS SERVICE

Rating Action: Moody's upgrades Allied Irish Banks' deposits and senior unsecured ratings to Baa3 and Ba1 respectively; outlook is positive

Global Credit Research - 20 Nov 2015

Standalone BCA upgraded to ba3 from b1

London, 20 November 2015 -- Moody's Investor Service (Moody's) has today upgraded Allied Irish Banks, p.l.c. (AIB)'s long-term deposit ratings to Baa3 from Ba1 and senior unsecured debt ratings to Ba1 from Ba2. At the same time, the rating agency upgraded the bank's standalone baseline credit assessment (BCA) to ba3 from b1, while the senior subordinated rating and the junior subordinated rating were affirmed at B1 and (P)B2 respectively.

"The rating actions take into account two main factors: firstly the impact that the proposed capital actions announced on 6 November will have on the bank's solvency and liability profile , and secondly the improvements in the bank's credit fundamentals, which we expect to continue in the next year, as indicated by the positive outlook. The proposed capital actions will, from one side, improve AIB's solvency profile, measured by our Tangible Common Equity (TCE). However, on the other side, they affect the level of subordination in the bank's liability structure and, therefore, impact our Advanced Loss Given Failure (LGF) Analysis", said Dany Castiglione, Moody's lead analyst on AIB.

"The strong profitability in the first six months of 2015 has materially improved AIB's solvency and profitability, bringing the bank's TCE over Risk Weighted Assets (RWA) to 8.8% as of June 2015 from 5.7% of end-2014. According to our calculations and including Q3 results recently announced by the bank, the proposed capital actions will drive the TCE ratio to 10.9% on a pro-forma basis. Additionally, according to our Advanced LGF analysis, these actions will also reduce the buffer available to subordinated and junior subordinated bond holders, resulting in an affirmation of these ratings at their current levels of B1 and (P)B2 respectively despite the upgrade of the BCA" continued Castiglione.

Concurrently, Moody's upgraded the bank's long-term Counterparty Risk Assessment (CR Assessment) to Baa2(cr) from Baa3(cr). The bank's short-term CR Assessment and deposits ratings were upgraded to P-2(cr) from P-3(cr) and to P-3 from NP, respectively. The short-term debt rating was affirmed at (P) NP.

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

RATINGS RATIONALE

UPGRADE OF THE BANK'S BCA REFLECTS IMPROVEMENTS IN FINANCIAL FUNDAMENTALS

Moody's upgrade of AIB's BCA and adjusted BCA to ba3 from b1 reflects the bank's improving internal capital generation and strengthening of its solvency profile, a trend that is expected to continue well into 2016. Asset quality is improving as well, driven by a decline in problem loans and an increase in coverage.

AIB's problem loans ratio went down to 24.5% as of June 2015 from 29.2% of end-2014, owing to the favourable operating environment and the restructuring activity conducted by the bank. The stock of problem loans further decreased to EUR16 billion at end-9M2015 from EUR18 billion of end-1H2015. The coverage ratio, calculated as problem loans over the sum of TCE and loan loss reserves, went down to 115.8% as of end-1H2015 from 136.0% of end-2014. Moody's expects AIB's asset quality to continue improving, driven by reduced levels of new arrears formation and gradual reduction in the stock of problem loans. However, while the reduction in non-residential problem loans is expected to proceed at a faster pace, the stock of residential problem loans will decline more slowly, given the reluctance to repossess properties in Ireland.

AIB's profitability continued to improve in in the first six months of 2015, with the bank recording a net income of EUR840 million (1H2014: EUR411 million), boosted by EUR540 million write-backs on its loan portfolio. Moody's expects the bank's quality of earnings to increase, becoming less reliant on write-backs, and to strengthen further in the outlook period owing to the benign economic environment, declining cost of risk, which is deemed sustainable, and favourable competitive landscape. Drags to profitability continue to be the large, albeit declining, stock of non-earning assets, the high level of tracker mortgages and still subdued, but quickly improving, demand for new business.

The internal capital generation, combined with the loan deleveraging, has materially improved the bank's solvency profile and the agency anticipates the TCE ratio to further improve in the outlook period. Finally, now that AIB has clarified its capital structure, Moody's does not anticipate any major obstacle to the bank's privatisation.

UPGRADE OF DEPOSITS AND SENIOR UNSECURED RATINGS INCORPORATES REDEMPTIONS AND ISSUANCE PLANS

The upgrade of AIB's long-term deposit and senior debt ratings to Baa3 and Ba1 respectively, the upgrade of the short-term deposit ratings to Prime-3 from Not-Prime and the affirmation of the short-term debt rating at (P)NP are based on the bank's BCA and the results of Moody's Advanced LGF Analysis. Moody's analysis is forward looking and incorporates the bank's proposed capital actions announced on 6 November.

AIB is subject to an Operational Resolution Regime through the EU Bank Resolution and Recovery Directive. Moody's has used the following assumptions: tangible common equity of 3% and losses post-failure of 8% of tangible banking assets, a 25% run-off in "junior" wholesale deposits, a 5% run-off in preferred deposits, and assign a 25% probability to deposits being preferred to senior unsecured debt. These assumptions are in line with the standard assumptions used by Moody's for most banks.

Based upon the above, Moody's Advanced LGF Analysis indicates that AIB's deposits are likely to face very low loss-given-failure, due to the loss absorption provided by subordinated debt and, potentially, by senior unsecured debt should deposits be treated preferentially in a resolution, as well as the substantial volume of deposits themselves. This results in a Preliminary Rating Assessment (PRA) of ba1, two notches above the BCA. AIB's senior unsecured debt is likely to face a low loss-given-failure due to the loss absorption provided by its own volume and the amount of debt subordinated to it. This results in a PRA of ba2, one notch above the BCA.

Moody's assumption of a moderate probability of government support for AIB's creditors results in a one-notch uplift to the PRA, and a long-term deposit rating of Baa3. The agency assigns the same support probability to bank-level senior unsecured debt, resulting in a senior unsecured rating of Ba1.

On the basis of the bank's balance sheet structure at 30 June 2015 and considering its proposed capital actions and funding plan, Moody's Advanced LGF Analysis indicates that AIB's subordinated and junior subordinated debt are likely to face a high and a very high loss-given-failure, due to the lack of further subordinated instruments. This suggests a rating of B1 for subordinated debt and (P)B2 for junior subordinated debt. In the previous analysis, based on end-2014 data, the ratings were the same, benefitting from the large buffer provided by the EUR3.5 billion 2009 Preference Shares. The intention to partly repay the 2009 Preference Shares offsets the impact of the upgrade of the BCA resulting in the affirmation of the subordinated and junior subordinated debt ratings at their current levels.

RATIONALE FOR THE CR ASSESSMENT

As part of today's action, Moody's also upgraded AIB's long-term CR Assessment to Baa2(cr) from Baa3(cr), four notches above the BCA of ba3. The short-term CR Assessment has been upgraded to P-2(cr) from P-3(cr). The CR Assessment is driven by the banks' standalone BCA and by the amount of subordinated instruments likely to shield counterparty obligations from losses, accounting for three notches of uplift relative to the BCA, as well as one notch of government support, in line with the agency's support assumptions on the bank's deposits and senior unsecured debt.

RATIONALE FOR THE POSITVE OUTLOOK

The positive outlook on AIB's long-term senior deposit and debt ratings reflects the improving trends in asset quality, solvency, profitability and funding. It also reflects the bank's clarified capital structure, which should pave the way to the privatisation of the bank.

WHAT COULD CHANGE THE RATING UP/DOWN

AIB's long-term debt and deposit ratings could be upgraded as a result of (1) an increase of its standalone ba3 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 the agency expectation; and (3) sustained improvement in the bank's profitability and efficiency.

AIB's ratings could be downgraded as a result of (1) a lowering of its standalone ba3 BCA; or (2) redemption of maturing subordinated instruments without their replacement.

AIB's BCA could be downgraded because of: (1) a non-anticipated deterioration in the bank's asset quality metrics; (2) a weakening of its solvency profile; and (3) a worsening of its profitability ratios.

PRINCIPAL METHODOLOGY

The principal methodology used in these ratings was Banks published in March 2015. Please see the Credit Policy page on www.moodys.com for a copy of this methodology.

LIST OF AFFECTED RATINGS

Issuer: AIB North America, Inc.

.... Long-Term Deposit Rating, Upgraded to Baa3/Positive from Ba1/Stable

....Outlook, Positive

Issuer: Allied Irish Banks, NY

.... Short-Term Deposit Rating, Upgraded to P-3 from NP

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

.... Adjusted Baseline Credit Assessment, Upgraded to ba3 from b1

.... Baseline Credit Assessment, Upgraded to ba3 from b1

.... Long-Term Counterparty Risk Assessment, Upgraded to Baa2(cr) from Baa3(cr)

.... Short-Term Counterparty Risk Assessment, Upgraded to P-2(cr) from P-3(cr)

.... Long-Term Deposit Ratings, Upgraded to Baa3/Positive from Ba1/Stable

.... Short-Term Deposit Ratings, Upgraded to P-3 from NP

.... Senior Unsecured Regular Bond/Debenture, Upgraded to Ba1/Positive from Ba2/Stable

.... Senior Unsecured Medium-Term Note Program, Upgraded to (P)Ba1 from (P)Ba2

.... Subordinate Regular Bond/Debenture, Affirmed B1

.... Subordinated Medium-Term Note Program, Affirmed (P)B1

.... Junior Subordinated Medium-Term Note Program, Affirmed (P)B2

.... Short-Term Medium-Term Note Program, Affirmed (P)NP

....Outlook, Positive

Issuer: EBS Ltd

.... Adjusted Baseline Credit Assessment, Upgraded to ba3 from b1

.... Baseline Credit Assessment, Upgraded to ba3 from b1

.... Long-Term Counterparty Risk Assessment, Upgraded to Baa2(cr) from Baa3(cr)

.... Short-Term Counterparty Risk Assessment, Upgraded to P-2(cr) from P-3(cr)

.... Long-Term Deposit Ratings, Upgraded to Baa3/Positive from Ba1/Stable

.... Short-Term Deposit Ratings, Upgraded to P-3 from NP

.... Senior Unsecured Regular Bond/Debenture, Upgraded to Ba1/Positive from Ba2/Stable

....Outlook, Positive

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