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Various Positive Rating Actions Taken On Irish Banks On Improving Industry Credit Profile

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- We believe that the Irish banking system continues to make progress working through its past failings.
- As a result, we believe that its industry risk profile is now less of an outlier among eurozone banking systems, which are increasingly subject to harmonized regulation.
- We are affirming the ratings on Bank of Ireland Group PLC and Allied Irish Banks PLC and revising the outlooks on them to positive from stable.
- We are also affirming the ratings on Ulster Bank Ireland DAC, Permanent TSB Group Holdings PLC, and KBC Bank Ireland PLC. The outlook on all three remains positive.

LONDON (S&P Global Ratings) Dec. 12, 2017--S&P Global Ratings said today that it took various rating actions on Irish banks. Specifically, we:

- Affirmed the ratings on non-operating holding company (NOHC) Bank of Ireland Group PLC (BOIG) at 'BBB-/A-3' and revised the outlook to positive from stable. In addition, we affirmed the ratings on its main operating bank, Bank of Ireland, at 'BBB/A-2' and revised the outlook to positive from stable.
- Affirmed the ratings on Allied Irish Banks PLC (AIB) at 'BBB-/A-3' and revised the outlook to positive from stable. At the same time, we affirmed the 'BB+/B' ratings on AIB's U.K. subsidiary, AIB Group (U.K.) PLC and revised the outlook to positive from stable.

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- Affirmed the 'BBB/A-2' ratings on Ulster Bank Ireland DAC (Ulster Bank). The outlook remains positive.
- Affirmed the 'B+/B' ratings on NOHC Permanent TSB Group Holdings PLC (PTSB) and the 'BB/B' ratings on its main operating bank Permanent TSB PLC. The outlook on both entities remains positive.
- Affirmed the 'BBB-/A-3' ratings on KBC Bank Ireland PLC (KBCI). The outlook remains positive.

RATIONALE

The positive rating actions reflect our view that the Irish banking system is successfully working through its past failings. We believe that its industry risk profile is now less of a negative outlier relative to other eurozone banking systems.

The banking system's progress since the financial crisis and the early track record of the Single Supervisory Mechanism under the leadership of the European Central Bank (ECB) lead us to believe that past supervisory failings should weigh less upon the industry risks facing Irish banks. For example, since 2017, banks have been required to demonstrate a more proactive plan to reduce their nonperforming exposures. The vast majority of Irish banking assets are now directly or indirectly supervised by the ECB. In our view, the failings of the Irish regulator were one of the main factors that led to the collapse of the Irish banking system in 2008.

This is not to say that Irish banks don't continue to face difficulties with the local regulator and politicians. Recently, Irish banks were scolded by the Minister of Finance over their handling of some tracker mortgage customers. The banks have been ordered, in strident terms, to rectify the situation, including through customer redress. We view this proactive approach as a jolt to the banking system and evidence that the required conduct standards have changed permanently. In our view, they are likely to be embedded in all aspects of their business activities.

Also supporting our updated industry view are the improvements that we have observed in Irish banks' funding profiles, albeit from an extremely weak position at the time of their recapitalization in 2011. We expect our measure of systemwide core deposits (including 100% of retail deposits and 50% of corporate deposits) to cover around 76% of systemwide domestic loans at end-2017. This metric compares well with some peers, although we note its dramatic improvement (it was 41% at end-2011) primarily relates to the significant scale of deleveraging and the recovery from a low base in the confidence in Irish banks from corporate depositors. We have also seen early evidence of debt issuance by one Irish NOHC, which will contribute towards their regulatory requirement for own funds and eligible liabilities (MREL) requirements.

The improving funding profile has supported recovery in net interest margins. Future profit growth will likely require better business volumes and greater progress on operating efficiency. We assume that further margin expansion is unlikely and the benefits of provision releases will wane.

At present, we are not overly concerned with the high house price inflation this year as we don't believe this is a credit-fuelled bubble and, in our view, Ireland's housing market is still in recovery following its severe crash. Sustained growth of more than 10% will eventually give us pause for thought, however. Nationally, house prices rose by 12.8% over the 12 months to September 2017 according to the Central Statistics Office, accelerating the previously steady recovery since the trough in early 2013. House prices are still, on average, around one-quarter below their 2007 peak.

Total credit growth has been negative in 2017, for the ninth straight year by our calculations. We believe that credit growth will turn positive in 2018, a position which will become more obvious in 2019. Mortgage loans, which account for the vast majority of household debt, will be the key factor.

Against a favorable backdrop of an expanding economy, falling unemployment, and low rates, we expect domestic systemwide credit losses to have been exceptionally low in full-year 2017, with net provision releases in some cases. We assume the systemwide loan loss rate to be up to 20 basis points (bps) in 2017, significantly below our assumption in our January 2017 Banking Industry Country Risk Assessment (BICRA) publication of 30bps in 2017. For 2018 and 2019, we maintain our view of a more normal level of around 30bps credit losses. These assumptions do not explicitly factor the impact of the new accounting standard, International Financial Reporting Standard (IFRS) 9.

The banking system's large stock of nonperforming loans (NPLs; we define these as impaired loans, plus loans that are 90 days past due but are not impaired, and performing forborne loans) and a still-high level of mortgage arrears (including a meaningful proportion of very long-term arrears of 720 days plus) remains among the most significant challenges facing the industry. We estimate that NPLs will be around 21% of domestic systemwide loans at end-2017 (down from around 27% at end-2016). While we expect a further reduction in NPLs (we assume to about 12% by end-2019) a more material reduction depends on proactive initiatives by banks.

As a result the anchor, or starting point, for rating a typical Irish bank remains at 'bbb-' but has the potential to improve to 'bbb' over the next two years. In particular, we could improve our funding assessment if the banking system proves able to maintain a retail funding profile with firmer evidence that our metric of deposits to loans will remain above 75% on a sustainable basis as lending growth recovers; and we see further evidence of wide, affordable access to the wholesale markets. We would also need to gain confidence that the recovery in pre-provision profitability will not reverse. With regard to an improved assessment of economic risk we would need to see evidence of a substantial further reduction in NPLs before we could consider this. We note that continued house price inflation above 10% and any potential risks to Ireland from its close trading partner, the U.K., leaving the EU may also cause us to resist a stronger assessment.

We have incorporated these revised assumptions into our ratings on five rated Irish banks, as explained further below. The ratings on Barclays Bank Ireland PLC, a core subsidiary of Barclays Bank PLC under our group rating methodology, are unaffected by this review.

BANK OF IRELAND GROUP PLC

The positive outlook on BOIG reflects the at least one-in-three chance over our two-year outlook horizon that we could improve our view of Irish banking industry risk. If this occurs, and at that time we continue to believe that the group is demonstrating a clear prospect of solid business and earnings growth, then we could revise upward the unsupported group credit profile (UGCP) by one notch to 'bbb+' and therefore the ratings. Less likely, but still plausible over this timeframe, we could also revise upward the UGCP if BOIG significantly improved its asset quality metrics to be broadly in line with higher rated peers, while continuing to demonstrate predictable earnings from both its Irish and U.K. franchises.

We could revise the outlook back to stable if our view of Irish banking industry risk worsened, or if the group's business and earnings predictability faltered.

BANK OF IRELAND

The positive outlook mirrors the rationale for the action on BOIG but also incorporates our belief that we could apply a notch for additional-loss absorbing capacity (ALAC). This factor would only benefit the ratings on Bank of Ireland because we do not include notches for ALAC support in the ratings on NOHCs.

If we revised upward the anchor and applied a one-notch adjustment for ALAC, we would not raise the rating on Bank of Ireland upward by two notches, at least in the near term. This is because, in our view, its overall creditworthiness is not yet consistent with 'A' category rated banks.

We could revise the outlook to stable if our view of Irish banking industry risk worsened, if we did not believe that sufficient progress had been made to build ALAC, or if we believed that a higher rating could not be justified relative to higher rated peers. This could be the case, for example, if we believed that the business were in a negative transition.

ALLIED IRISH BANKS PLC

The positive outlook on AIB reflects the at least one-in-three chance that we could improve our view of Irish banking industry risk over our two-year outlook horizon. This could lead us to revise upward AIB's UGCP by one notch to 'bbb', and therefore raise the ratings.

While less likely in the short term, we could also upgrade AIB if we included one notch of ALAC support in the ratings on the bank, or if it continued to make steady progress in reducing its stock of nonperforming assets (NPAs) to levels more aligned with those of peers in the coming 18-24 months. The former depends on the bank's MREL and issuance plans, and the bank's ALAC buffer would need to exceed the required thresholds of 5% for a bank with a starting point of 'bbb-' or higher.

We could revise the outlook back to stable if our view of Irish banking industry risk worsened. We could also revise the outlook back to stable if AIB's capital management becomes more aggressive as it gradually returns to full private ownership, such that we no longer believed its RAC ratio would sustainably exceed 10%.

The positive outlook on AIB Group (U.K.) PLC, AIB's wholly owned subsidiary, reflects the positive outlook on AIB.

ULSTER BANK IRELAND DAC
The positive outlook on Ireland-based Ulster Bank reflects our positive outlook on the main operating entities of the Royal Bank of Scotland Group PLC (RBS)--Ulster Bank's ultimate parent--that are likely to form the future ring-fenced part of RBS.

We could upgrade Ulster Bank over the coming 18-24 months if we upgraded RBS' future ring-fenced operating subsidiaries. Although less likely, we could also consider an upgrade if Ulster Bank demonstrated an improved operating performance and risk profile at least in line with that of the parent, which would enable us to equalize its ratings with RBS' GCP.

We would revise our outlook on Ulster Bank to stable if we took a similar action on the RBS group's future ring-fenced entities. We could also revise the outlook to stable if we observed that the Republic of Ireland was becoming less integral to the RBS group's strategy and the links between Ulster Bank and the RBS group were weakening as a result.

PERMANENT TSB GROUP HOLDINGS PLC
PTSB's UGCP remains unchanged at 'bb'.

The positive outlook on PTSB reflects the at least one-in-three chance that our view of Irish banking industry risk could improve over the coming two years. All other factors remaining the same, an improved view of the banking industry in Ireland could lead us to revise upward PTSB's UGCP--and therefore raise the ratings--by one notch, given PTSB's domestic focus.

Although less likely over our 12-month horizon, we could raise the ratings on PTSB if we observed that its NPAs and mortgage arrears had converged toward levels more in line with those of its domestic and international peers, while capitalization remained at a level commensurate with a strong assessment. This would be measured by our RAC ratio of above 10%. This reflects our view that PTSB's enhanced focus on reducing NPAs should support gradual improvements in its asset quality, operating performance, and earnings capacity.

We could revise the outlook back to stable if our view of Irish banking industry risk worsened. We could also revise the outlook to stable if we considered that PTSB's efforts to reduce NPAs had derailed its path to earnings recovery and its ability to maintain capital sustainably above 10%.

PERMANENT TSB PLC

The positive outlook on PTSB, the primary operating company of the group, mirrors that on Permanent TSB Group Holdings PLC, the NOHC. We could lower or raise the ratings if we revised the UGCP downward or upward, as explained above.

While less likely in the short term, we could also raise the ratings if we believed PTSB could build a sufficiently large ALAC buffer, subject to evidence of issuance. This would only benefit the ratings on the operating company, Permanent TSB PLC, because we do not include notches for ALAC support in the ratings on NOHCs.

KBC BANK IRELAND

KBCI's stand-alone credit profile remains unchanged at 'bb'.
The positive outlook reflects that we could raise the ratings by one notch in the next 12-24 months if our view of Irish industry risk improved, or if we thought that on a stand-alone basis, KBCI would generate recurring and more predictable statutory earnings, which would indicate its strategic repositioning was working successfully.

While less likely, we could also raise the ratings if, for example, we observed improving performance, successful developments in KBCI's retail franchise, and profitable bancassurance operations that were more reflective of KBC Group's overall business strategy. This could lead us to revise upward our group status assessment for KBCI.

While we view KBCI's strategy as logical, we consider management's attempt to reposition the KBCI franchise as a work in progress. We could therefore revise the outlook back to stable if we believed that the bank were lagging its peers in terms of working through its large stock of NPAs, or if we considered that management were unlikely to develop KBCI into a retail-focused bank that could generate solid and sustainable earnings.

BICRA SCORE SNAPSHOT*

Ireland

	To	From
BICRA Group	5	5
Economic risk	5	5
Economic resilience	Low risk	Low risk
Economic imbalances	Intermediate risk	Intermediate risk
Credit risk in the economy	Very high risk	Very high risk
Industry risk	5	6
Institutional framework	Intermediate risk	High risk

Competitive dynamics	Intermediate risk	Intermediate risk
Systemwide funding	High risk	High risk
Trends		
Economic risk trend	Stable	Stable
Industry risk trend	Positive	Stable

*Banking Industry Country Risk Assessment (BICRA) economic risk and industry risk scores are on a scale from 1 (lowest risk) to 10 (highest risk). For more details on our BICRA scores on banking industries across the globe, please see "Banking Industry Country Risk Assessment Update" published monthly on RatingsDirect.

RELATED CRITERIA

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- Criteria - Financial Institutions - Banks: Bank Hybrid Capital And Nondeferrable Subordinated Debt Methodology And Assumptions, Jan. 29, 2015
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- General Criteria: Methodology: Use Of 'C' And 'D' Issue Credit Ratings For Hybrid Capital And Payment-In-Kind Instruments, Oct. 24, 2013
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- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009
- Criteria - Financial Institutions - Banks: Commercial Paper I: Banks, March 23, 2004

RELATED RESEARCH
- Banking Industry Country Risk Assessment: Ireland, Dec. 12, 2017
- Banking Industry Country Risk Assessment Update, Dec. 7, 2017
- Republic of Ireland Ratings Affirmed At 'A+/A-1'; Outlook Stable, Dec. 1, 2017
- European Banking Union 2.0: The Creation Of A True Single Market? Nov 6, 2017
- Irish Banks: Getting Back To Where They Once Belonged, March 20, 2017
- S&P To Publish Economic And Industry Risk Trends For Banks, March 12, 2013
- Analytical Linkages Between Sovereign And Bank Ratings, Dec. 6, 2011

Ratings List

Ratings Affirmed; Outlook Action

	To	From
Bank of Ireland Group PLC		
Counterparty Credit Rating	BBB-/Positive/A-3	BBB-/Stable/A-3
Bank of Ireland		
Counterparty Credit Rating	BBB/Positive/A-2	BBB/Stable/A-2
Allied Irish Banks PLC		
Counterparty Credit Rating	BBB-/Positive/A-3	BBB-/Stable/A-3
AIB Group (U.K.) PLC		
Counterparty Credit Rating	BB+/Positive/B	BB+/Stable/B

Ratings Affirmed

Ulster Bank Ireland DAC	
Counterparty Credit Rating	BBB/Positive/A-2
Permanent TSB Group Holdings PLC	
Counterparty Credit Rating	B+/Positive/B
Permanent TSB PLC	
Counterparty Credit Rating	BB/Positive/B
KBC Bank Ireland PLC	
Counterparty Credit Rating	BBB-/Positive/A-3

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Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. Complete ratings information is available to subscribers of RatingsDirect at www.capitaliq.com. All ratings affected by this rating action can be found on the S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column. Alternatively, call one of the following S&P Global Ratings numbers:

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