

NCR comments: Sörmlands Sparbank H2 2020 report

Our 'BBB+' issuer and issue ratings on Sörmlands Sparbank are unchanged following the publication of the bank's full-year 2020 results.

Core earnings improve due to cost efficiency investments

Sörmlands Sparbank's business volumes increased by 7% to SEK 48.3bn during 2020. The bank increased on-balance-sheet lending growth in the course of the year by 11% compared with end-2019, while increased savings resulted in a 9% rise in customer deposits and investment assets transferred to asset managers Swedbank Robur AB and Indecap Fonder AB. While the bank added SEK 1.2bn in loans to its balance sheet, a portion of this growth came at the expense of a SEK 0.6bn reduction in loans transferred to Swedbank AB.

The larger lending volumes and lower expenses added scale to the bank's core earnings. Net interest income improved by 11.5%, while core pre-provision income rose to SEK 87m from SEK 49m a year earlier. The bank's bottom line was negatively impacted by regulatory guidance to withhold dividends, which negatively affected dividend revenues from Swedbank during 2020 and resulted in a 36% decline in pre-provision income, including dividends and other revenues.

The bank made more progress than we anticipated toward its goal of reducing its core cost-income ratio in the second half of 2020. Expenses declined by 5% year on year, reducing core cost-to-income levels to 77% from 87% a year earlier (we expected 81% for 2020). Similarly, the bank's core risk-adjusted return (net interest and fee income divided by our adjusted risk exposure amount) of 1.0% in 2020 exceeded expectations (0.8% in our 2020 estimates and 0.6% in 2019). The bank aims to achieve a 60% core cost-income ratio by 2022, and we project further improvement as investments made in 2020 affect 2021 and 2022 cost levels.

Sörmlands Sparbank's 2021 revenues will benefit from Swedbank's anticipated return to dividend payments. Initially, Swedbank will pay 25% of its 2020 and 2019 profits to shareholders (SEK 7.25 per share) according to current dividend restrictions. Given the bank's 6.57m shares in Swedbank, and other strategic holdings, this should result in dividend income of about SEK 50m in the first half of 2021. Restrictions on bank dividends will be reconsidered by the Swedish financial supervisory authority after 30 Sep. 2021, which could result in additional dividend income before year-end.

Material credit loss reversals associated with legacy exposure from 2016

Sörmlands Sparbank made a large reversal in resolving a legacy non-performing exposure. In total, the bank reported a SEK 37m reversal in 2020, including a SEK 61m (48 bps of net lending) reversal in the second half of the year. Similarly, gross Stage 3 non-performing loans continued to fall, to 173bps of net loans, or 116bps net of loss reserves (255bps and 126bps, respectively, at end-2019), but remain well above the bank's peer group average (approximately 65bps).

Capital ratios improve stable despite asset growth

Sörmlands Sparbank's capital ratios fell slightly to 21.9% in 2020 from 22.1% at end-2019. We expect the bank to improve its capital ratios given improved cost efficiency and the expected increase in dividend revenue.

This commentary does not constitute a rating action.

If you have any questions, please contact:

Sean Cotten, chief rating officer, +46735600337, sean.cotten@nordiccreditrating.com

Geir Kristiansen, credit rating analyst, +4790784593, geir.kristiansen@nordiccreditrating.com

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Attachments

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