MOODY'S INVESTORS SERVICE

Credit Opinion: Sparebanken More

Global Credit Research - 29 Mar 2011

Norway

Ratings

Category	Moody's Rating
Outlook	Negative(m)
Bank Deposits	A2/P-1
Bank Financial Strength	C-

Contacts

Analyst	Phone
Janne Thomsen/London	44.20.7772.5454
Oscar Heemskerk/London	
Simon Harris/London	
Soline Poulain/London	

Key Indicators

Sparebanken More (Consolidated Financials)[1]

	[2]**12-10**	[2]**12-09**	[2]**12-08**	[3]**12-07**	[3]**12-06**	**Avg.**
Total Assets (NOK billion)	**44.4**	**41.4**	**40.8**	**35.6**	**31.8**	[4]**8.8**
Total Assets (EUR million)	**5,699.2**	**4,994.0**	**4,191.4**	**4,486.2**	**3,867.9**	[4]**10.2**
Total Assets (USD million)	**7,645.8**	**7,165.0**	**5,826.3**	**6,559.1**	**5,100.4**	[4]**10.7**
Tangible Common Equity (NOK billion)	**3.2**	**2.9**	**2.5**	**2.3**	**2.2**	[4]**9.7**
Tangible Common Equity (EUR million)	**408.2**	**347.2**	**252.1**	**294.8**	**268.0**	[4]**11.1**
Tangible Common Equity (USD million)	**547.6**	**498.1**	**350.5**	**431.0**	**353.4**	[4]**11.6**
PPI / Avg RWA (%)	**2.3**	**2.1**	**1.9**	**2.0**	**1.8**	[5]**2.1**
Net Income / Avg RWA (%)	**1.6**	**1.3**	**1.1**	**1.4**	**1.3**	[5]**1.3**
(Market Funds - Liquid Assets) / Total Assets (%)	**32.6**	**35.6**	**36.3**	**31.8**	**32.8**	[6]**33.8**
Core Deposits / Average Gross Loans (%)	**66.3**	**61.4**	**60.8**	**65.2**	**60.6**	[6]**62.9**
Tier 1 Ratio (%)	**11.9**	**11.6**	**9.1**	**9.3**	**10.3**	[5]**10.8**
Tangible Common Equity / RWA (%)	**11.1**	**10.5**	**8.8**	**9.4**	**10.1**	[5]**10.1**
Cost / Income Ratio (%)	**44.8**	**46.5**	**48.1**	**49.5**	**51.8**	[6]**48.1**
Problem Loans / Gross Loans (%)	**2.4**	**3.0**	**2.7**	**3.1**	**2.6**	[6]**2.7**
Problem Loans / (Equity + Loan Loss Reserves) (%)	**24.9**	**32.0**	**32.8**	**35.4**	**27.5**	[6]**30.5**

Source: Moody's

[1] All ratios are adjusted using Moody's standard adjustments [2] Basel II; IFRS [3] Basel I; IFRS [4] Compound Annual Growth Rate based on IFRS reporting periods [5] Basel II & IFRS reporting periods have been used for average calculation [6] IFRS reporting periods have been used for average calculation

Opinion

SUMMARY RATING RATIONALE

Moody's rates Sparebanken Møre A2/C-/P-1.

The C- bank financial strength rating (BFSR), which translates into a baseline credit assessment (BCA) of Baa1, reflects Sparebanken Møre's sound local franchise and adequate financial fundamentals. However, the rating is constrained by the bank's high borrower concentration, its exposures to volatile corporate sectors and its less-seasoned loan book on the back of double-digit growth in 2006-2008.

The global local currency (GLC) deposit rating of A2 assigned to Sparebanken Møre is supported by the bank's Baa1 BCA and the Aaa local currency deposit ceiling of Norway, which is deemed the underlying support provider. Given the bank's importance to its region, and the region's importance to the national economy of Norway, Moody's assesses a high probability of systemic support in the event of a stress situation. Consequently, Sparebanken Møre's GLC deposit rating benefits from a two-notch uplift from its BCA.

Credit Strengths

- Sound market position in Møre and Romsdal

- Resilient earnings from banking operations

- Satisfactory capitalisation, strengthened in Q3 2009

- Around 60% of lending to retail customers (including loans transferred to Møre Boligkreditt), mostly mortgage loans

Credit Challenges

- Growing revenue, given the high competition in Norway

- Reducing credit risk concentrations, especially by single-name borrower

- Managing its exposure to volatile sectors, including property management, fisheries and the maritime industry

- Maintaining asset quality across the economic cycle

- Strengthening its liquidity position, which is heavily geared towards market funding

- Further developing risk management practices

Rating Outlook

The outlook on the C- BFSR is stable. Based on Moody's global bank financial strength rating methodology, a C- BFSR can be mapped to a BCA of Baa1 or Baa2. In light of the bleak outlook for some key sectors in the Møre and Romsdal county, namely export-related and local ship building industries, potential further impairments exceeding Moody's base stress assumptions could lead to a reassessment of the BFSR mapping. Lowering of the bank's BCA to Baa2 from Baa1 would result in a downgrade of the deposit rating. Therefore, a negative outlook has been assigned to the A2 deposit rating.

What Could Change the Rating - Up

An upgrade of the BFSR or the GLC deposit rating is unlikely, as reflected in the aforementioned negative outlook on the deposit rating.

What Could Change the Rating - Down

The BFSR could be downgraded if there is: (i) any deterioration in asset quality or capitalisation that exceeds Moody's expectations; or (ii) any sign that the bank is unable to sustain its market positions.

The GLC deposit rating could be downgraded if: (i) the BFSR deteriorates; or (ii) Moody's current assessment of the probability of systemic support for the bank declines.

DETAILED RATING CONSIDERATIONS

Detailed considerations for Sparebanken Møre's currently assigned ratings are:

Bank Financial Strength Rating

The assigned BFSR is one notch lower than the outcome of Moody's bank financial strength scorecard. Based on Moody's loss expectations for Sparebanken Møre's loan portfolio as well as high credit risk concentration, we believe that the bank's financial strength is more consistent with a C- BFSR.

Qualitative Factors (50% weighting)

Factor 1: Franchise Value

Trend: Neutral

Sparebanken Møre is a regional savings bank with a sound market position in western Norway in the county of Møre and Romsdal, where Moody's estimates it commands market shares of around 20% for lending and almost 30% for deposits. Its national market share is limited, just above 1%.

The bank operates as an independent savings bank, using an open-architecture business model to offer financial services including insurance and investment products. The bank has subsidiaries in leasing (Møre Finans) and real estate brokerage (Møre Eiendomsmegling), and established its own covered bond company, Møre Boligkreditt, in late 2008 for funding purposes.

In the region where it operates, Sparebanken Møre faces competition from larger players such as Nordea and DnB NOR, as well as from other local and regional savings banks. As a result, one of the bank's main challenges is maintaining and improving its market share. In that respect, we positively view the acquisition of a small local savings bank, Tingvoll Sparebank, towards the end of 2009, which strengthens the bank's presence in the north part of Møre and Romsdal.

Although we acknowledge Sparebanken Møre's strong presence in the region in which it operates, we note that the Norwegian banking market is highly competitive and that savings banks generally lack pricing power against the two national market leaders. In addition, the D+ score for franchise value is constrained by the bank's low geographic diversification.

Factor 2: Risk Positioning

Trend: Neutral

Sparebanken Møre follows the recommendations of the Oslo Stock Exchange for corporate governance. The bank's board of directors comprises seven members, including one employee representative. CEO Olav Arne Fiskerstrand is not a member of the board. Several members of the management group have extensive experience at the bank. Overall, Moody's does not believe there are corporate governance problems at Sparebanken Møre.

The bank's equity certificates (ECs) are listed on the Oslo Stock Exchange. Since the acquisition of Tingvoll Sparebank, the bank's largest EC holder is Sparebankstiftelsen Tingvoll with 10.2% of ECs. No other EC holders have a stake of more than 10% and the 20 largest EC holders owned less than 40% of the shares at YE 2010.

Sparebanken Møre's reports under IFRS and the accounts are audited by Ernst & Young. The annual financial disclosure is relatively good but we note that quarterly reports are not as extensive as some of its Nordic peers.

Risk management procedures at the bank are considered adequate. The overall guidelines for management and control are assessed at least annually by the board of directors. The head of risk management is responsible for establishing policies for a/o credit risk, market risk and funding risk, in line with board approved guidelines, and reports to the CEO. The overall score for risk management is constrained by limitations in risk management - e.g. in terms of credit risk modelling and risk pricing, stress testing as well as high risk concentrations in the loan portfolio.

Sparebanken Møre's market risk remains modest. Its exposure to interest rates is limited: interest rate risk at the parent bank was NOK5.7 million in relation to a 100 bps change in interest rates at YE 2010. Investments in shares and ECs amounted to NOK207 million at YE 2010, corresponding to around 6% of Tier 1 capital. This figure includes a 1.36% ownership in Eksportfinans. The bank also has limited foreign currency exposure.

High credit risk concentration is a constraining factor in the score for risk positioning and pushes it to C-.

Factor 3: Regulatory Environment

For a discussion about the regulatory environment, please see Moody's Banking System Outlook on Norway.

Factor 4: Operating Environment

Trend: Neutral

The operating environment score takes into account the economic stability, integrity and corruption in the country as well as the legal system. The unadjusted score for Norway's operating environment is B and is constrained by a score of C for economic stability, primarily as a result of volatility in oil prices. To reflect the fact that offshore revenues are allocated to the Government Pension Fund and have a limited impact on the mainland economy, we calculate the score for economic stability as the average of the standard deviations of GDP growth both including (25% weight) and excluding offshore revenue (75% weight), which results in an adjusted score of B. Consequently, the adjusted score for operating environment is B+.

For further discussion of the operating environment, please see Moody's latest Banking System Outlook on Norway.

Quantitative Factors (50% weighting)

Factor 5: Profitability

Trend: Weakening

Sparebanken Møre is reliant on net interest income, which represented some 70% of its operating income in 2010. This source of earnings improved in 2010, primarily as a result of good loan growth and reduced cost of funding. Fee & commission income accounted for around 12% of operating income during the year and is mainly related to fees from credit cards and loans.

Valuation changes in financial instruments continued to make a high contribution to earnings, chiefly due to a NOK74 million one-off gain from the merger between PBS and Nordito. We caution the sustainability of the elevated contribution from these types of earnings is uncertain due to their high reliance on market conditions.

Most of the improvement in Sparebanken Møre's net profitability in 2010 stemmed from a reduction in loan loss provisions (NOK31 million vs. NOK82 million in 2009). The year-on-year decrease is even more substantial when adjusting for a NOK35 million provision related to the guarantee provided to Eksportfinans that was booked in 2008 and largely reversed in 2009.

The score for profitability is C with a weakening trend, mainly reflecting our expectations that further growth in net interest income is uncertain. Additionally, while we note a some improvement in profits, a significant part of them stem from valuation changes financial instruments, which are typically more volatile sources of earnings.

Factor 6: Liquidity

Trend: Neutral

Sparebanken Møre's liquidity is underpinned by a strong deposit base, which accounts for around 60% of its total funding, and retail deposits that represent more than half of total deposits.

At YE 2010 the deposit-to-gross loan ratio was 64%, meaning the bank is reliant on market funding, most of which comes from the domestic market. The maturity profile of the bank's debt is relatively diversified: almost 90% of the market funding has a maturity longer than 12 months.

In addition, Sparebanken Møre's wholly-owned covered bond company, Møre Boligkreditt, provides it with an additional source of funding, something that Moody's views favourably. In 2009, covered bonds were mainly used in the no phased out government swap arrangement, whereby these instruments can be exchanged for government bonds. Sparebanken Møre Boligkreditt issued NOK1.85 billion covered bonds in the market in 2010 and we expect that covered bonds will remain an attractive source of funding for the bank.

At YE 2010 liquid assets accounted for 10% of total assets, including cash and deposits with the central bank and the securities portfolio, which mainly comprise senior bonds of banks and municipalities, as well as some corporate bonds and shareholdings. The bank does not have exposure to structured products. However, we note that holdings are concentrated on Norwegian securities, which could be a source of vulnerability.

The D+ score for liquidity, although lower than that of European counterparts, is in line with that of other Norwegian banks. It reflects Sparebanken Møre's reliance on market funding, although we note the positive impact of the bank's liquidity management as well as its access to covered bonds.

Factor 7: Capital Adequacy

Trend: Neutral

Sparebanken Møre exhibits good capitalisation. At YE 2010, the Tier 1 and total capital ratios, as calculated under Basel II's standardised approach, stood at 11.9% and 13.6%, respectively. These levels were strengthened in August 2009 with a NOK277 million Tier 1 hybrid issue that was raised in the market and are above the bank's board stated minimum targets of 10% for Tier 1 ratio and 12% total capital ratio.

We view the bank's capital buffer as adequate to withstand potential credit losses. However, hybrid capital made up close to 15% of the bank's Tier 1 capital at YE 2010, which is the maximum amount that can be included in Tier 1 in Norway. We caution that the quality to absorb losses of hybrid capital is below that of pure equity. In addition, these instruments could be excluded from Tier 1 capital according to the Basel Committee's propositions as they are currently presented.

Sparebanken Møre applies a standard approach in calculating its capital adequacy requirement for credit risk. Given the bank's large retail loan book, the capital requirement is estimated to be lower under Basel II IRB model. However, due to concentration issues, we do not expect the bank to release capital.

Sparebanken Møre scores A for capital adequacy.

Factor 8: Efficiency

Trend: Neutral

Sparebanken Møre's efficiency as measured by its cost-to-income ratio is good at 45% at YE 2010 (47% at YE 2009). At this level, the bank meets management's target of a ratio below 50% and ranks it among the most efficient Moody's-rated regional savings banks in Norway. The bank uses third party providers when selling services such as insurance and investment products, avoiding the fixed costs that would be related to in-house production.

However, we note that operating costs, mainly driven by salaries, increased by 6% in 2010, despite a one-off gain of NOK18 million related to a change in the pension legislation in Norway.

The bank scores B for cost efficiency. However, given the revenue pressure from a challenging operating environment, we would not expect major improvements in the cost-to-income ratio in the coming years. Additionally, going forward, cost containment might prove to be more difficult as an independent bank.

Factor 9: Asset Quality

Trend: Weakening

Sparebanken Møre 's loan portfolio is well diversified and around 60% of the bank's lending is to retail customers, mainly in the form of mortgages. We note that at YE 2010, 23% of retail loans were part of Møre Boligkreditt's covered pool.

However, we note some concentration towards the property management sector, which represented around 10% of total loans at YE 2010. In addition, corporate lending includes lending to fishing-related (8% of gross loans) and shipping (5% of gross loans) industries. These sectors have historically been characterised by higher volatility and could be a source of vulnerability.

Furthermore, operating in a small geographic region means the bank has significant single-borrower exposure, as measured by the 20 largest exposures in relation to Tier 1 capital or pre-provision income. In addition, we note a somewhat unseasoned loan portfolio, which reflects high pre-crisis lending growth (a year-on-year increase of 13% in 2008 and 14% in 2007).

At YE 2010, problem loans (defined as commitments in default in excess of three months and other bad and doubtful commitments) accounted for 2.4% of gross loans, down from 3% at YE 2009. The bank's loan loss reserve coverage is relatively low at around 45% of problem loans. Although this partly reflects the high proportion of retail mortgages in the loan book, we caution that the sustained increase in house prices in Norway may have underrated the level of provisioning by inflating collateral values. We further note that the bank has historically had a higher problem loan ratio and a lower problem loan coverage ratio than other Moody's-rated Norwegian banks. On the other hand, actual losses have remained at a low level in the past five years.

The score for asset quality is C. The economic environment in Norway, and in the county of Møre and Romsdal, is satisfactory, but slower economic growth, fewer exports and weaker domestic demand have been a challenge for the corporate sector. Further, with regards to retail loans, household indebtedness has increased in recent years, making customers more vulnerable to interest rates rises, although we take comfort in the still low unemployment levels in Norway. Overall, we consider the trend to be weakening but note lower levels of problem loans in 2010.

Global Local Currency Deposit Rating (Joint Default Analysis)

Moody's assigns a GLC deposit rating of A2 to Sparebanken Møre. The rating is supported by its Baa1 BCA and the Aaa local currency deposit ceiling of Norway, which is considered the underlying support provider. Given the bank's importance to its region, and the region's importance to the national economy of Norway, Moody's assesses as high the probability of systemic support in the event of a stress situation.

Foreign Currency Deposit Rating

Foreign currency deposit ratings are unconstrained given that Norway has a country ceiling of Aaa. Sparebanken Møre's foreign currency deposit rating is A2.

Foreign Currency Debt Rating

Foreign currency senior unsecured debt ratings are unconstrained given that Norway has a country ceiling of Aaa. Sparebanken Møre's foreign currency senior unsecured debt rating is A2.

ABOUT MOODY'S BANK RATINGS

Bank Financial Strength Rating

Moody's Bank Financial Strength Ratings (BFSRs) represent Moody's opinion of a bank's intrinsic safety and soundness and, as such, exclude certain external credit risks and credit support elements that are addressed by Moody's Bank Deposit Ratings. BFSRs do not take into account the probability that the bank will receive such external support, nor do they address risks arising from sovereign actions that may interfere with a bank's ability to honor its domestic or foreign currency obligations. Factors considered in the assignment of BFSRs include bank-specific elements such as financial fundamentals, franchise value, and business and asset diversification. Although BFSRs exclude the external factors specified above, they do take into account other risk factors in the bank's operating environment, including the strength and prospective performance of the economy, as well as the structure and relative fragility of the financial system, and the quality of banking regulation and supervision.

Global Local Currency Deposit Rating

A deposit rating, as an opinion of relative credit risk, incorporates the BFSR as well as Moody's opinion of any external support. Specifically, Moody's Bank Deposit Ratings are opinions of a bank's ability to repay punctually its deposit obligations. As such, they are intended to incorporate those aspects of credit risk relevant to the prospective payment performance of rated banks with respect to deposit obligations, which includes: intrinsic financial strength, sovereign transfer risk (in the case of foreign currency deposit ratings), and both implicit and explicit external support elements. Moody's Bank Deposit Ratings do not take into account the benefit of deposit insurance schemes which make payments to depositors, but they do recognize the potential support from schemes that may provide assistance to banks directly.

According to Moody's joint default analysis (JDA) methodology, the global local currency deposit rating of a bank is determined by the incorporation of external elements of support into the bank's Baseline Credit Assessment. In calculating the Global Local Currency Deposit rating for a bank, the JDA methodology also factors in the rating of the support provider, in the form of the local currency deposit ceiling for a country, Moody's assessment of the probability of systemic support for the bank in the event of a stress situation and the degree of dependence between the issuer rating and the Local Currency Deposit Ceiling.

National Scale Rating

National scale ratings are intended primarily for use by domestic investors and are not comparable to Moody's globally applicable ratings; rather they address relative credit risk within a given country. A Aaa rating on Moody's National Scale indicates an issuer or issue with the strongest creditworthiness and the lowest likelihood of credit loss relative to other domestic issuers. National Scale Ratings, therefore, rank domestic issuers relative to each other and not relative to absolute default risks. National ratings isolate systemic risks; they do not address loss expectation associated with systemic events that could affect all issuers, even those that receive the highest ratings on the National Scale.

Foreign Currency Deposit Rating

Moody's ratings on foreign currency bank obligations derive from the bank's local currency rating for the same class of obligation. The implementation of JDA for banks can lead to high local currency ratings for certain banks, which could also produce high foreign currency ratings. Nevertheless, it should be noted that foreign currency deposit ratings are in all cases constrained by the country ceiling for foreign currency bank deposits. This may result in the assignment of a different, and typically lower, rating for the foreign currency deposits relative to the bank's rating for local currency obligations.

Foreign Currency Debt Rating

Foreign currency debt ratings are derived from the bank's local currency debt rating. In a similar way to foreign currency deposit ratings, foreign currency debt ratings may also be constrained by the country ceiling for foreign currency bonds and notes; however, in some cases the ratings on foreign currency debt obligations may be allowed to pierce the foreign currency ceiling. A particular mix of rating factors are taken into consideration in order to assess whether a foreign currency bond rating pierces the country ceiling. They include the issuer's global local currency rating, the foreign currency government bond rating, the country ceiling for bonds and the debt's eligibility to pierce that ceiling.

About Moody's Bank Financial Strength Scorecard

Moody's bank financial strength model (see scorecard below) is a strategic input in the assessment of the financial strength of a bank, used as a key tool by Moody's analysts to ensure consistency of approach across banks and regions. The model output and the individual scores are discussed in rating committees and may be adjusted up or down to reflect conditions specific to each rated entity.

Rating Factors

Sparebanken More

Rating Factors [1]	**A**	**B**	**C**	**D**	**E**	**Total Score**	**Trend**
Qualitative Factors (50%)						**C**	
Factor: Franchise Value						**D+**	**Neutral**
Market Share and Sustainability			**x**				
Geographical Diversification					**x**		
Earnings Stability			**x**				

Earnings Diversification [2]							
Factor: Risk Positioning						**C-**	**Neutral**
Corporate Governance [2]	--	--	--	--	--		
- Ownership and Organizational Complexity	--	--	--	--	--		
- Key Man Risk	--	--	--	--	--		
- Insider and Related-Party Risks	--	--	--	--	--		
Controls and Risk Management		**x**					
- Risk Management			x				
- Controls	x						
Financial Reporting Transparency		**x**					
- Global Comparability	x						
- Frequency and Timeliness	x						
- Quality of Financial Information			x				
Credit Risk Concentration	--	--	--	--	--		
- Borrower Concentration	--	--	--	--	--		
- Industry Concentration	--	--	--	--	--		
Liquidity Management			**x**				
Market Risk Appetite	**x**						
Factor: Operating Environment						**B+**	**Neutral**
Economic Stability		**x**					
Integrity and Corruption		**x**					
Legal System	**x**						
Financial Factors (50%)						**C**	
Factor: Profitability						**C**	**Weakening**
PPI / Average RWA - Basel II			2.10%				
Net Income / Average RWA - Basel II			1.35%				
Factor: Liquidity						**D+**	**Neutral**
(Mkt funds-Liquid Assets) / Total Assets					24.18%		
Liquidity Management			x				
Factor: Capital Adequacy						**A**	**Neutral**
Tier 1 Ratio - Basel II	10.85%						
Tangible Common Equity / RWA - Basel II	10.13%						
Factor: Efficiency						**B**	**Neutral**
Cost / Income Ratio		46.46%					
Factor: Asset Quality						**C**	**Weakening**
Problem Loans / Gross Loans			2.67%				
Problem Loans / (Equity + LLR)			29.91%				
Lowest Combined Score (15%)						**D+**	
Economic Insolvency Override						**Neutral**	
Aggregate Score						**C**	
Assigned BFSR						**C-**	

[1] - Where dashes are shown for a particular factor (or sub-factor), the score is based on non public information [2] - A blank score under Earnings diversification or Corporate Governance indicates the risk is neutral