Brage Finans AS
Issuer Rating Report

A- STABLE

Scope's credit view (summary)

The **A- issuer rating** reflects Brage Finans' focused leasing and car financing business, solid credit fundamentals and strategic relationship with its owner banks.

Brage Finans (Brage) serves as the finance company for its owners, primarily well-established and solid savings banks located in western and southern Norway. Combined, the owner banks have more than 100 local offices, forming an essential part of the company's distribution network. With four of seven members on the board coming from the banks, the owners steer the strategic direction of the company. In addition, the owner banks have consistently provided capital and funding to support Brage's growth and development.

The nature of Brage's business entails greater asset risk than traditional banking focused on mortgage lending. Leasing offers higher margins, but counterparties are often small businesses in cyclical sectors like construction and manufacturing. Nevertheless, performance in 2020 was resilient with the company reporting a return on equity of 9% when adjusting for commissions paid to the owner banks. Asset quality remained sound with Stage 3 exposures accounting for 1.6% of the credit portfolio as of year-end 2020.

As a licensed finance company regulated and supervised by the Norwegian FSA, Brage is subject to most of the same requirements as banks, including in the areas of solvency and liquidity. Brage maintains reassuring prudential metrics in line with relatively stringent requirements. As it is not authorised to collect deposits, Brage relies on wholesale funding and is a frequent issuer in the domestic debt market. With an independently assessed green bond framework in place, the company is enabled to issue green bonds.

Outlook

The **Stable Outlook** reflects the expectation that Brage's operating performance and asset quality will remain sound in the face of potential challenges posed by the Covid-19 pandemic as well as rapid business growth.

Credit strengths	Credit weaknesses
• Ability to manage rapid growth while maintaining sound asset quality • Reassuring prudential metrics • Supportive relationship with solid owner banks	• Focused business entailing greater asset risk than traditional banking • Exposure to SMEs in cyclical industries • Reliance on market funding

Positive rating-change drivers	Negative rating-change drivers
• Continued sustainable growth underpinned by increasing business and geographic diversification	• Change in supportive nature of relationship with owner banks • Deterioration in the regional economies where activities are concentrated, impacting earnings and/or asset quality

Ratings & Outlook

Issuer rating	A-
Senior unsecured debt rating	A-
Outlook	Stable

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Issuer profile

Brage Finans (Brage) is a Norwegian finance company offering primarily equipment leasing for business clients and car loans for individuals. Its origins stem from management's idea of establishing a local finance company to capture business opportunities. The senior management team, comprised of the CEO, the Deputy CEO, the CFO, and the head of credit, have extensive experience in the finance industry and have been with the company since its founding in June 2010. Brage serves as the finance company for its owners, 13 banks. The business started with equipment leasing for the owner banks (2010), then car loans for the owner banks (2013), and then expanded with equipment (2015) and car dealers (2017). A group of 10 savings banks has joined as distributors since 2021.

Successful mid-size player in attractive Norwegian finance market focused on lease financing for business assets and car loans for individuals

Business expected to be more balanced between leasing and car loans

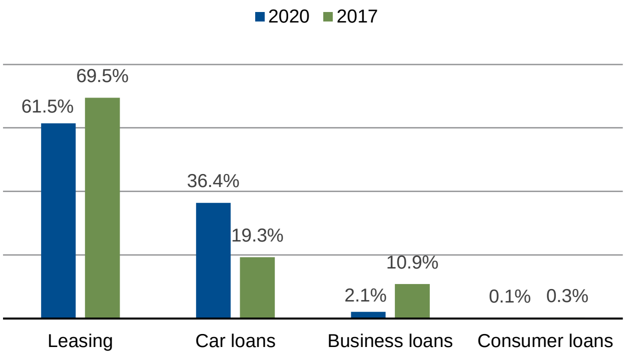
Brage offers primarily lease financing and loans to businesses and car loans to individuals. There is a very small proportion of unsecured consumer loans as this is offered by the owner banks. Management, however, is wary of this product and does not actively market it. Future growth potential is expected to be strongest in car loans as Brage more closely integrates its product offering onto the mobile banking platforms of the owner banks. Consequently, management foresees the business mix becoming more diversified and evenly balanced between business and retail customers. Leasing currently accounts for about 62% of the credit portfolio (Figure 1).

Lease financing is available for a wide range of movable assets, including construction machinery, agricultural equipment, trucks, and vans. Brage buys and owns the asset while the client pays a monthly rental fee for using the asset. At the end of the lease period, usually three to seven years, the client normally buys the asset or continues leasing for a minimal amount. There is limited residual value risk as the contracts are mostly full pay-out leases.

Owner banks are important distributors

Brage focuses on the geographical markets of the owner banks which are in western and southern Norway (Figure 2). The largest exposure is to western Norway (31%), followed by Rogaland (22%) and Agder (15%). As new distribution channels have been added, the proportion of business derived from the owner banks has declined but remains substantial at around 40%.

Figure 1: Development of credit portfolio (%)



Notes: Car loans include both retail and business clients. Portfolio size of NOK 14.2bn in 2020 and NOK 6bn in 2017.
Source: Company data, Scope Ratings

Figure 2: Geographic footprint of owner banks

Source: Company data.

Addition of car and equipment dealers has fuelled growth

In addition to the more than 100 local offices of the owner banks, Brage distributes products through nearly 300 equipment and car dealers and directly via its own sales offices and digital platforms. From January 2021, a group of ten local savings banks (Lokalbank alliance) primarily located in the eastern part of Norway joined as distributors which will add further geographic diversification to the business. Brage's multi-pronged distribution strategy has supported strong growth (Figure 3).

In Norway, foreign finance companies are material players, accounting for approximately 30% of finance lending volume[1]. Three large players roughly equally account for about 55% of new business volume (DNB Finans, Santander Consumer Bank AS and Nordea Finans). Other players include the finance companies of auto manufacturers and bank-owned finance companies.

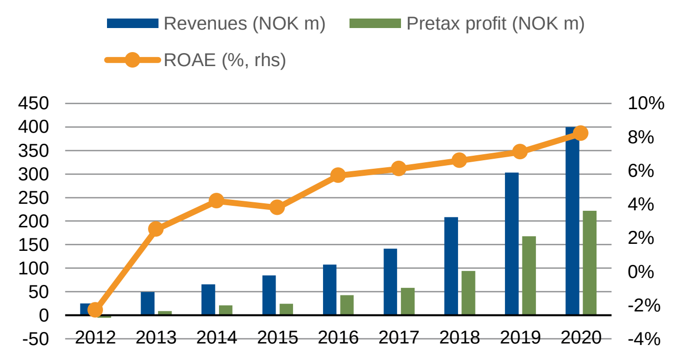
Steadily increasing market share

As of year-end 2020, Brage had a market share of 5.6% of the overall financing market. Meanwhile, new business market share in the movable asset leasing and car loan segments were 7.1% and 5.3%, respectively, up from 6.6% and 4%, respectively as of year-end 2018[2]. Over time, the company has successfully increased market share in the segments it operates in.

Volume growth in the leasing market is linked to the overall economy as well as the investment cycle. The leasing market has generally grown each year since 2010. The exceptions were in 2015 when the Norwegian economy suffered from a sharp drop in oil prices and in 2020 due to the Covid-19 pandemic (Figure 4).

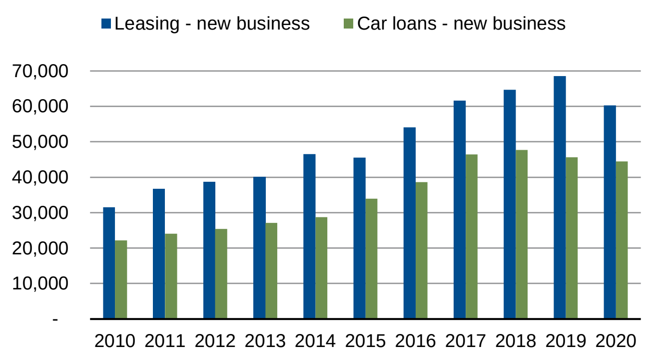
In the latest regional network survey published by Norges Bank in March 2021, businesses are expecting a slight increase in investment for the first time since February 2020. All sectors except for oil services expect higher investment in 2021 than in 2020.

Figure 3: Brage become profitable after less than three years in operation



Source: Company data, Scope Ratings.

Figure 4: Industry new business volumes - leasing and car loan markets (NOK m)



Source: Association of Norwegian Finance Houses, Scope Ratings.

[1] Norges Bank, 2020 Norway's Financial System.
[2] Market share data reflects the activity of members of the Association of Norwegian Finance Houses. Members' activities include leasing, factoring, car financing, credit cards and consumer loans.

Strategic and close relationship with solid owner banks supports business growth

Brage is owned primarily by well-established and solid savings banks, with their ownership stakes reflecting their distribution capacity (Figure 5). Due to the departure of Helgeland Sparebank for strategic reasons, the ownership structure changed in March 2021. Two new banks who already act as distributors became owners, Spareskillingsbanken and Naeringsbanken ASA[3]. As well, Sparebanken Sor increased its ownership stake by 6%. There may be further minor changes in the future as Sparebanken Sor's increased stake may be sold to existing or new owners.

Figure 5: Selected metrics of owner banks

	Stake in Brage (%)	Assets (NOK bn)	Return on Avg Assets (%)	Return on Avg Equity (%)	Costs % Income	NPLs % Gross loans	CET1 capital ratio (%)
Sparebanken Vest	49.99%	221.3	0.9	11.7	35.8	0.3	18.0
Sparebanken Sør	26.77%	142.1	0.8	8.1	39.1	0.9	15.7
Fana Sparebank	5.34%	29.3	0.5	4.9	58.6	0.4	16.9
Haugesund Sparebank	3.11%	12.1	1.0	8.0	38.4	1.5	20.6
Voss Sparebank	2.18%	5.1	0.7	4.5	47.9	0.1	28.1
Spareskillingsbanken	2.08%	10.1	0.6	4.4	48.3	1.3	25.4
Flekkefjord Sparebank	2.03%	7.1	0.5	3.9	55.4	0.7	25.3
Skudenes & Aakra Sparebank	1.84%	10.2	1.0	9.2	40.3	0.8	20.7
Søgne & Greipstad Sparebank	1.67%	4.7	0.9	7.9	50.9	0.1	18.2
Luster Sparebank	1.59%	3.9	0.8	5.6	40.0	0.8	23.8
Lillesands Sparebank	1.51%	3.6	0.9	6.9	50.7	0.2	21.6
Etne Sparebank	1.40%	2.0	1.5	12.7	42.0	0.3	16.7
Naeringsbanken ASA	0.50%	2.6	0.7	4.5	55.7	0.1	17.7

Notes: Ownership stake as of March 2021. Financial data as of year-end 2020.
Source: Company data, SNL, Scope Ratings.

Overall, the banks are profitable and display sound prudential metrics. While the banks are independent, they cooperate and jointly own product and service companies to better serve customers, increase efficiency, and maintain their competitive positions. For example, many of the owner banks are also joint owners in Frende Forsikring, an insurance company, and Norne Securities, an investment bank.

Owner banks incentivised to refer high quality clients

Brage serves as the finance company for the owner banks. Due to the commission arrangements in place, the owner banks are incentivised to refer high quality customers to Brage. The commissions paid to the banks is based on their distribution volumes as well the credit losses in their specific portfolios. In addition to commission income, Brage provides a means for the owner banks to strengthen customer relationships.

With four of seven members on the board coming from the banks, the owners steer the strategic direction of the company. Management's overall financial objective is to generate a return in line with the owner banks' own return targets. When evaluating Brage's performance, the owner banks also consider the commissions they receive. Adjusting for the commissions paid to the owner banks, Brage reported a return on equity of 9%.

[3] Naeringsbanken ASA is a business focused bank owned primarily by businesses in Hedmark and Oppland. The bank started operations in 2017.

Management aims to further improve returns by increasing non capital-intensive products such as payment insurance and reducing funding costs. In 2020, the company's cost income ratio reached 26% when adjusted for commissions paid to the owner banks, in line with management's target of around 25%. Brage continues to gradually enhance its IT systems and client facing digital platforms but there is no need for major investments as the systems are relatively new and up to date.

Sound asset quality and reassuring prudential metrics

Business entails greater asset risk than traditional banking

The nature of Brage's business entails greater asset risk than traditional banking focused on mortgage lending. Leasing offers higher margins, but counterparties are often small businesses in cyclical sectors. Within the corporate portfolio, the largest exposures include construction as well as transport and storage, industries which tend to be more cyclical. As the car financing business has grown, retail customers have become an increasing proportion of the portfolio (2020: 30%).

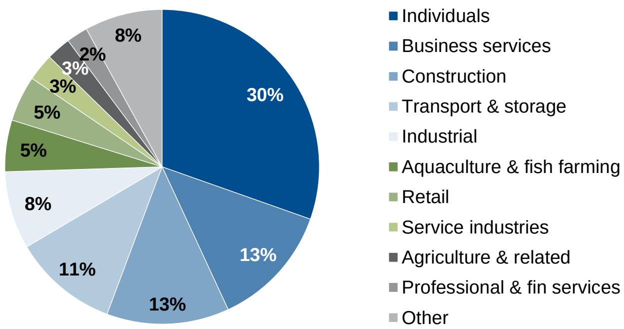
Brage performs its own credit assessment of all clients, including those which have been referred by the owner banks. ESG considerations such as the environmental performance of equipment and vehicles are part of the credit approval and risk assessment process. Credit and concentration risks are also actively managed and monitored. In response to the Covid-19 pandemic, management increased risk monitoring and tightened credit policies.

The credit portfolio has proven to be resilient during the pandemic. Brage has low exposure to more impacted industries such as hospitality and oil and offshore. Last year, the company granted a limited number of three-month payment deferrals, primarily to business customers. The proportion of the portfolio subject to payment deferrals has returned to pre-pandemic levels at 0.6%. Asset quality remains sound with Stage 3 exposures accounting for 1.6% of the portfolio as of year-end 2020.

Diversified portfolio supports asset quality

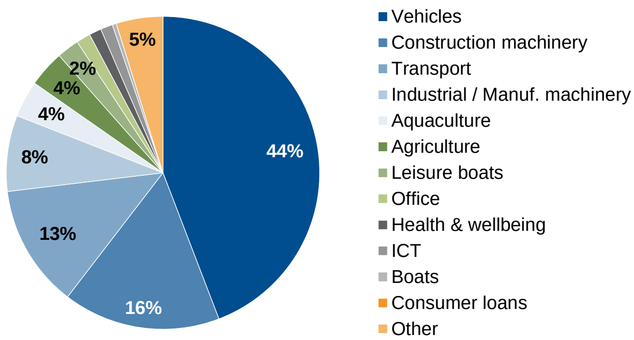
The portfolio is diversified by both industry and asset type, with concentration risk being low (Figures 6 and 7). As of year-end 2020, over 85% of the portfolio was comprised of contracts on individual assets with values below NOK 5m each. Further, 59% of the portfolio was comprised of customer engagements totalling less than NOK 5m each. This same portion of the portfolio accounted for nearly 99% of contracts, with an average contract value of around NOK 210,000. Meanwhile, less than 10% of the portfolio was comprised of customer engagements totalling more than NOK 50m.

Figure 6: Portfolio by industry (%)



Notes: Data as of year-end 2020.
Source: Company data, Scope Ratings.

Figure 7: Portfolio by asset type (%)



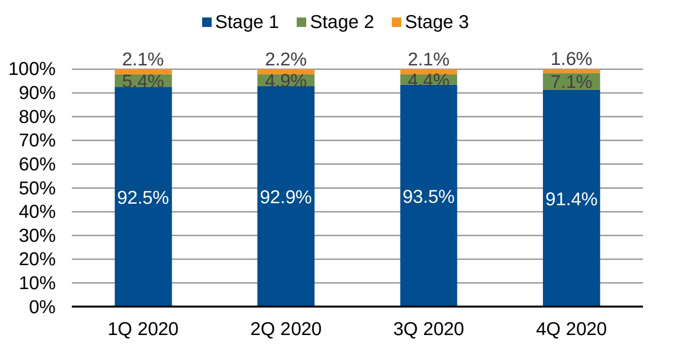
Notes: Data as of year-end 2020.
Source: Company data, Scope Ratings.

Supervised by Norwegian FSA and subject to similar requirements as banks

Licensed as a finance company, Brage is regulated and supervised by the Norwegian FSA. The company is subject to most of the same requirements as banks, including in the areas of solvency and liquidity. With the support of the owner banks, Brage maintains reassuring prudential metrics in line with relatively stringent requirements. Over the years, the owner banks have contributed nearly NOK 1.5bn in capital to support growth and to ensure a sound solvency position. As of year-end 2020, the owner banks also provided NOK 600m in loans.

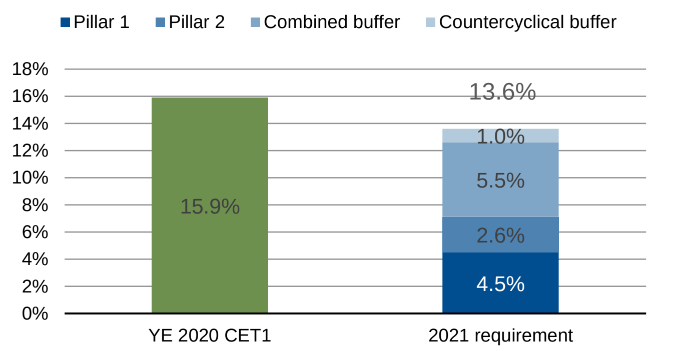
Brage's CET1 capital position was 15.9% as of year-end 2020, compared to a requirement of 13.6% (Figure 9). To mitigate the impact of the pandemic, the countercyclical capital buffer was lowered to 1% from 2.5% in March 2020. This buffer is expected to return to the level of 2.5% as the economy recovers. In addition, from end-2022, the systemic risk buffer requirement will increase to 4.5% from the current 3%. Meanwhile, Brage's capital position is expected to benefit from the implementation in Norway of the second SME discount contained in CRR II.

Figure 8: Asset quality development (%)



Source: Company data, Scope Ratings.

Figure 9: CET1 capital position vs. requirements



Source: Company data, Scope Ratings.

A reliance on market funding balanced by the cash flow generative nature of the business and liquidity management

Funded primarily by debt as not authorised to collect deposits

As Brage has grown, management has successfully obtained different sources of funding to support its development. Over time, the proportion of funding from the owner banks has declined while market funding has become important (Figure 10). In 2014, Brage issued senior unsecured debt for the first time and in 2015 began issuing capital instruments. As well, in 2018 Brage obtained its first loan of NOK 175m from the Nordic Investment Bank to support SMEs with lease financing. Last year, another loan of NOK 250m was obtained to support sustainable financing and which has been used so far for green car loans.

Green bonds a potential funding source

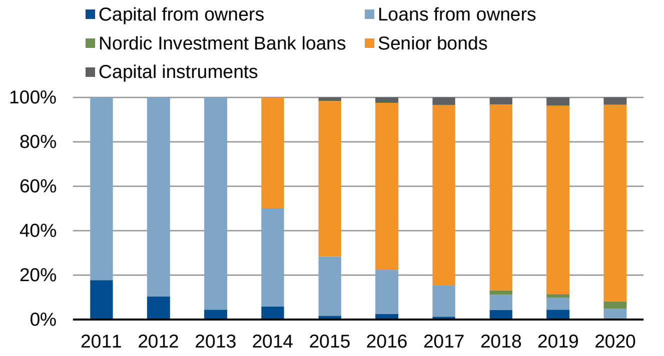
While the company has yet to issue green bonds, Brage has established a green bond framework which has been independently assessed by CICERO as being "dark green"[4]. This is the highest score and was based on an assessment of the framework's alignment with the Green Bond Principles, the project categories, and Brage's governance. Per the framework, proceeds from green bonds would be used to finance a portfolio of loans and leases concerning clean transport and machinery, renewable energy, and sustainable aquaculture.

[4] CICERO Shades of Green scores range from "dark green" to "brown" and assess how projects and solutions correspond to the long-term vision of a low carbon and climate resilient future.

To manage liquidity and funding risks, Brage aims to ensure that quarterly operating cash flows from customer payments are more than sufficient to cover future debt maturities (Figure 11). There are internal limits on the amount of debt that can be borrowed and the amount of debt maturing each quarter. In addition, the company maintains a liquidity buffer comprised of cash and bond funds. As of year-end 2020, the LCR and NSFR were 174% and 118%, respectively.

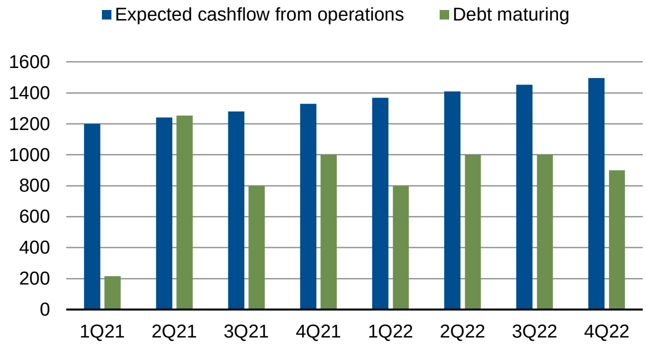
Brage managed through the market disruption caused by the pandemic last year with no difficulties. Further, the owner banks indicated a willingness to provide support if it were needed.

Figure 10: Funding sources (%)



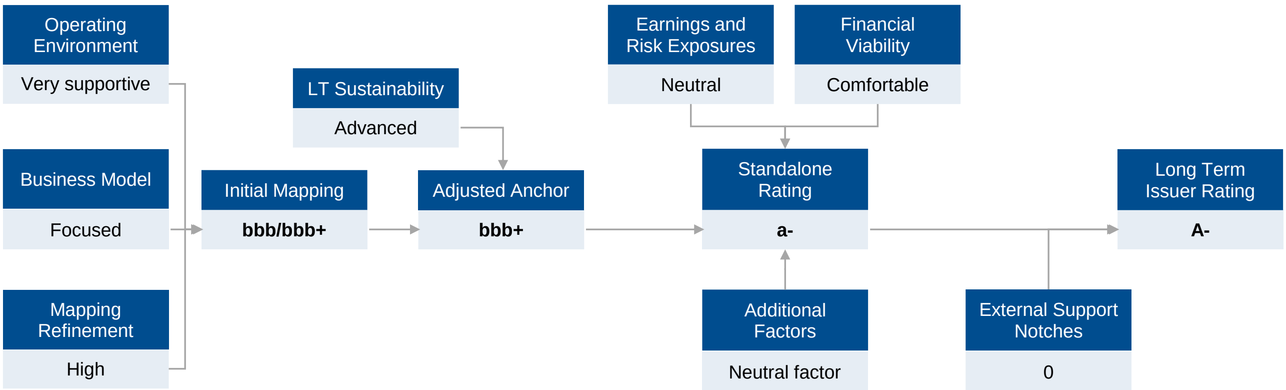
Source: Company data, Scope Ratings.

Figure 11: Expected cash flows vs debt maturities as of year-end 2020 (NOK m)



Note: With the issuance of NOK 1.75bn in debt issued in Feb 2021, the debt maturing in 2Q21 has been reduced to NOK 400m as of March 2021.
Source: Company data, Scope Ratings.

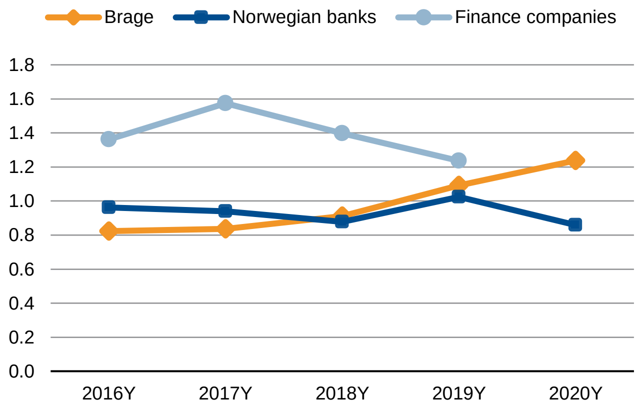
I. Appendix: Overview of the rating process



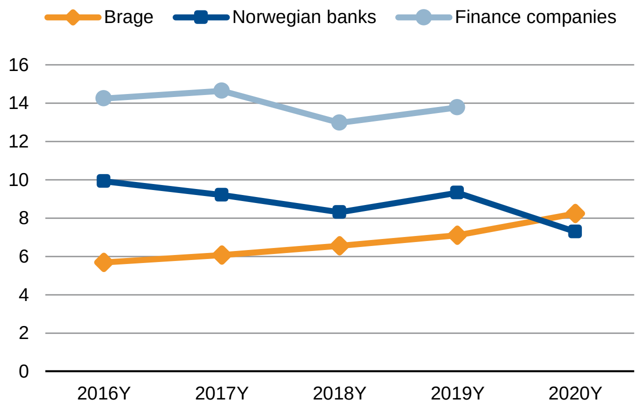
Step		Assessment	Summary rationale
STEP 1	Operating environment	Very supportive	• Wealthy economy with well-developed capital markets and a solid track record of economic resilience to shocks • Relatively stringent and active regulator • Growing finance market
		Supportive	
		Moderately supportive	
		Constraining	
		Very constraining	
	Business model	Very resilient	• Focused leasing and car financing business • Serves as finance company for owners • Activities focused primarily in western and southern Norway
		Resilient	
		Consistent	
		Focused	
		Narrow	
	Mapping refinement	High	• Supportive owners with solid credit fundamentals
		Low	
	Initial mapping	**bbb/bbb+**	
	Long-term sustainability	Best in class	• Sustainability considerations are incorporated in business strategy and risk processes • Independently assessed green bond framework allows for green bond issuance
		Advanced	
		Developing	
		Lagging	
	Adjusted anchor	**bbb**	
STEP 2	Earnings capacity & risk exposures	Very supportive	• While leasing is a higher margin business, it entails greater asset risk than traditional banking focused on mortgage lending • Exposed to SMEs in more cyclical industries • Commission agreement with owners supports asset quality
		Supportive	
		Neutral	
		Constraining	
		Very constraining	
	Financial viability management	Ample	• Comfortably meets relatively stringent requirements • Owner banks have consistently provided capital and funding support • A reliance on market funding as not authorised to collect deposits
		Comfortable	
		Adequate	
		Limited	
		Stretched	
		At risk	
	Additional factors	Significant support factor	• No further considerations
		Material support factor	
		Neutral	
		Material downside factor	
		Significant downside factor	
	Standalone	**a-**	
STEP 3	External support	Not applicable	
Issuer rating		**A-**	

II. Appendix: Peer comparisons

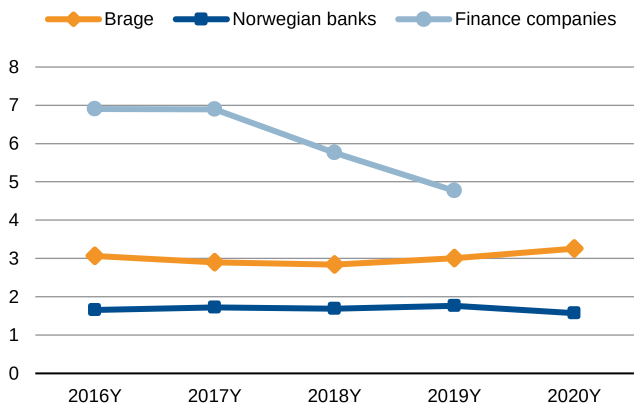
Return on average assets (%)



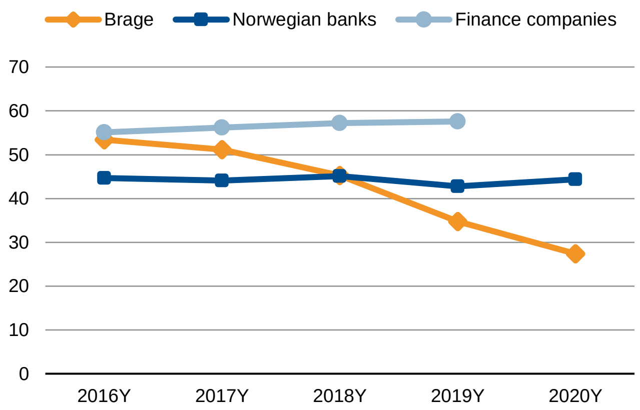
Return on average equity (%)



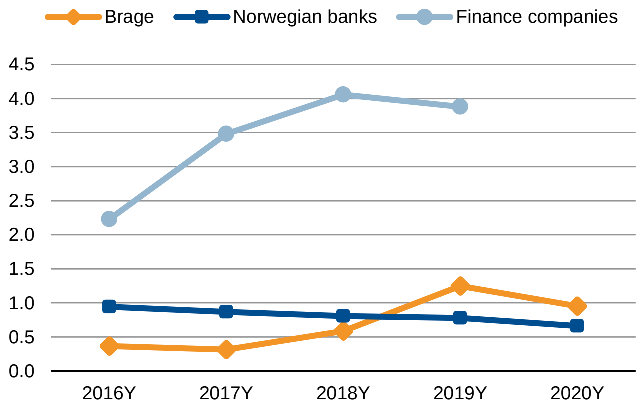
Net interest margin (%)



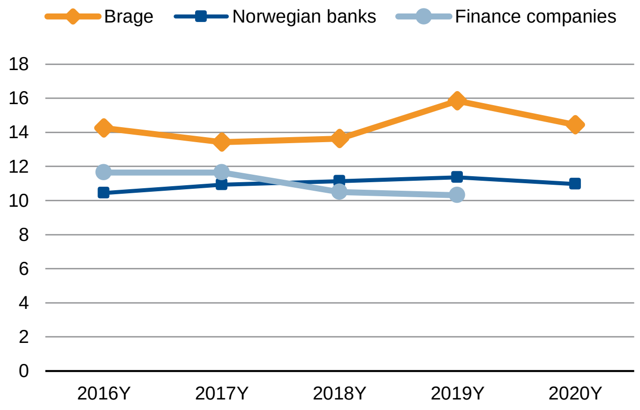
Costs % Income



Problem loans % Gross loans



Total equity % Total assets



Note: Insufficient 2020 data for finance companies.
Norwegian banks: BN Bank, Jaeren Sparebank, Sandnes Sparebank, Totens Sparebank, SpareBank 1 Nordvest, SpareBanken Sor 1, Helgeland Sparebank, Fana Sparebank, Sparebanken Vest.
Finance companies: Nordea Finans Sverige AB, Nordea Finance Equipment AS, Santander Consumer Bank AS, BNP Paribas Lease Group SA, Credit Agricole Leasing & Factoring SA, Alba Leasing SpA.
Source: SNL

III. Appendix: Selected Financial Information – Brage Finans AS

	2016Y	2017Y	2018Y	2019Y	2020Y
Balance sheet summary (NOK m)					
Assets					
Cash and interbank assets	82	179	237	281	389
Total securities	30	41	63	105	117
of which, derivatives	NA	NA	NA	NA	NA
Net loans to customers	4,355	6,148	9,248	11,973	14,150
Other assets	44	54	78	103	104
Total assets	**4,512**	**6,423**	**9,626**	**12,462**	**14,759**
Liabilities					
Interbank liabilities	800	800	775	775	1,026
Senior debt	2,915	4,581	7,230	9,250	11,140
Derivatives	NA	NA	NA	NA	NA
Deposits from customers	0	0	0	0	0
Subordinated debt	95	95	170	235	236
Other liabilities	NA	NA	NA	NA	NA
Total liabilities	**3,869**	**5,560**	**8,314**	**10,487**	**12,628**
Ordinary equity	643	762	1,212	1,801	1,956
Equity hybrids	0	100	100	175	175
Minority interests	0	0	0	0	0
Total liabilities and equity	**4,512**	**6,423**	**9,626**	**12,462**	**14,759**
Core tier 1/ common equity tier 1 capital	*624*	*737*	*1,185*	*1,770*	*1,923*
Income statement summary (NOK m)					
Net interest income	120	157	232	331	440
Net fee & commission income	-13	-18	-29	-37	-48
Net trading income	0	1	1	3	-1
Other income	1	1	3	6	8
Operating income	**108**	**141**	**208**	**303**	**400**
Operating expenses	58	72	94	105	110
Pre-provision income	**50**	**69**	**114**	**198**	**290**
Credit and other financial impairments	7	11	20	30	69
Other impairments	NA	NA	NA	NA	NA
Non-recurring income	NA	NA	NA	NA	NA
Non-recurring expense	NA	NA	NA	NA	NA
Pre-tax profit	**43**	**58**	**94**	**168**	**222**
Income from discontinued operations	0	0	0	0	0
Income tax expense	10	12	18	47	53
Other after-tax Items	0	0	0	0	0
Net profit attributable to minority interests	0	0	0	0	0
Net profit attributable to parent	**33**	**46**	**75**	**121**	**169**

Source: SNL

IV. Appendix: Selected Financial Information – Brage Finans AS

	2016Y	2017Y	2018Y	2019Y	2020Y
Funding and liquidity					
Net loans/ deposits (%)	NA	NA	NA	NA	NA
Liquidity coverage ratio (%)	95%	109%	125%	262%	174%
Net stable funding ratio (%)	NA	NA	129%	116%	118%
Asset mix, quality and growth					
Net loans/ assets (%)	96.5%	95.7%	96.1%	96.1%	95.9%
Problem loans/ gross customer loans (%)	0.4%	0.3%	0.6%	1.2%	1.0%
Loan loss reserves/ problem loans (%)	97.8%	109.5%	49.1%	28.2%	52.5%
Net loan growth (%)	30.7%	41.2%	50.4%	29.5%	18.2%
Problem loans/ tangible equity & reserves (%)	2.5%	2.3%	4.2%	7.6%	6.3%
Asset growth (%)	30.9%	42.4%	49.9%	29.5%	18.4%
Earnings and profitability					
Net interest margin (%)	3.1%	2.9%	2.8%	3.0%	3.3%
Net interest income/ average RWAs (%)	3.2%	3.1%	3.2%	3.4%	4.0%
Net interest income/ operating income (%)	111.4%	111.2%	111.6%	109.2%	110.1%
Net fees & commissions/ operating income (%)	-12.4%	-13.1%	-13.7%	-12.3%	-11.9%
Cost/ income ratio (%)	53.4%	51.2%	45.3%	34.7%	27.4%
Operating expenses/ average RWAs (%)	1.6%	1.4%	1.3%	1.1%	1.0%
Pre-impairment operating profit/ average RWAs (%)	1.4%	1.4%	1.6%	2.0%	2.6%
Impairment on financial assets / pre-impairment income (%)	14.5%	15.7%	17.6%	15.0%	23.7%
Loan loss provision/ average gross loans (%)	0.2%	0.2%	0.3%	0.3%	0.5%
Pre-tax profit/ average RWAs (%)	1.2%	1.2%	1.3%	1.7%	2.0%
Return on average assets (%)	0.8%	0.8%	0.9%	1.1%	1.2%
Return on average RWAs (%)	0.9%	0.9%	1.0%	1.3%	1.5%
Return on average equity (%)	5.7%	6.1%	6.5%	7.1%	8.2%
Capital and risk protection					
Common equity tier 1 ratio (%, fully loaded)	NA	NA	NA	NA	NA
Common equity tier 1 ratio (%, transitional)	14.9%	12.6%	13.7%	17.4%	15.9%
Tier 1 capital ratio (%, transitional)	14.9%	14.3%	14.9%	19.1%	17.4%
Total capital ratio (%, transitional)	17.2%	15.9%	16.9%	21.4%	19.3%
Leverage ratio (%)	12.5%	11.8%	12.5%	14.9%	13.3%
Asset risk intensity (RWAs/ total assets, %)	92.5%	91.3%	89.6%	81.6%	81.7%

Source: SNL

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