

Totens Sparebank Issuer Rating Report


A- STABLE

Scope's credit view (summary)

The **A- issuer rating** reflects Totens Sparebank's strong market position in its local area in south-east Norway, resilient profitability, and sound solvency position. As a savings bank, the group continues to focus on retail customers in its local area with residential mortgages accounting for over 70% of lending. Management targets a return on equity of 10% and a cost-income ratio below 40%.

Like with other Norwegian banks, Totens Sparebank relies to some extent on market funding, including covered bonds. Customer deposits account for about half of funding. At the same time, the group maintains a high-quality liquidity portfolio well in excess of upcoming maturities within the next twelve months.

Under Scope's bank rating methodology, the "long-term sustainability" assessment (ESG factor) captures how relevant environmental, social and governance (ESG) factors as well as an issuer's preparedness for digital transition (D), may impact creditworthiness and the ability to repay debt. As part of the first-time implementation of this methodology, Scope has assigned an assessment of "developing" to Totens Sparebank. The group is in the process of upgrading its core technology infrastructure. Further, ESG-related risks are starting to be integrated into the credit underwriting process.

The A- issuer rating of Totens Sparebank Boligkreditt AS, a wholly owned subsidiary, is aligned with that of Totens Sparebank. Through the issuance of covered bonds, Totens Sparebank Boligkreditt provides secured funding for its parent. Scope rates the covered bonds issued by Totens Sparebank Boligkreditt at AAA.

Outlook

The **Stable Outlook** reflects our expectation that Totens Sparebank's operating performance will remain resilient, supported by a strong economic outlook for the Norwegian economy.

Credit strengths

- Strong market position in local area
- Solid profitability with good cost efficiency and low credit impairments
- Sound solvency position

Credit weaknesses

- As with other Norwegian banks, a reliance on market funding
- Operations limited to one region

Positive rating-change drivers

- Sustained profitable growth with increased geographic diversification, accompanied by sound prudential metrics

Negative rating-change drivers

- Deterioration in operating environment which materially impairs the bank's earnings capabilities
- Loss of benefits and economies of scale from being a member of an alliance

Ratings & Outlook

Issuer rating	A-
Preferred senior unsecured debt rating	A-
Non-preferred senior unsecured debt rating	BBB+
Outlook	Stable

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Bloomberg: RESP SCOP

Issuer profile

Established in 1854, Totens Sparebank (Totens) is a savings bank headquartered in Lena in south-east Norway. The bank operates with five branches in the broader Mjos region, where agriculture, manufacturing and the public sector are important industries.

The bank serves retail and corporate customers, offering payment solutions, savings and pension products, investment funds, insurance, and financing. Totens is a founding member and one of the largest banks in the Eika Alliance.

In Ostre Toten and Vestre Toten where the bank has a long history, Totens enjoys retail market shares of 40-50% and corporate market shares of about 25%. In other municipalities where the bank has a shorter history, market shares are around 10-15%.

Totens first issued equity capital certificates (ECC) in 1995 and is listed on the Oslo Stock Exchange. As of 30 September 2021, ECC-holders owned 51% of the bank.

Savings bank with strong market position in an economically sound local area

Strong market position in home market

As a savings bank with strong roots in its local area, Totens aims to contribute to growth and development in the region. Customers, employees, and local municipalities are all represented in the bank's highest governing body, the general assembly. As well, a portion of earnings are used to support associations, sport, and culture in the local community. The bank receives around 350 applications for donations each year. Further, the bank sponsors about 80 sport and cultural organisations.

Management has defined the Mjos region as the bank's primary market and the areas immediately adjacent as its secondary market. Per bank policy, at least 70% of lending should be within the primary market (3Q 2021: 77%).

Focused on retail customers

The bank's focus on personal customers is reflected in its loan portfolio, with lending to retail customers accounting for over 70% of the total (Figure 2). Most of this is residential mortgage lending. Within the bank's defined secondary market, financing extended to businesses is generally limited to existing clients and companies where customer relationships exist with key employees.

Figure 1: Five branches serving focused market area

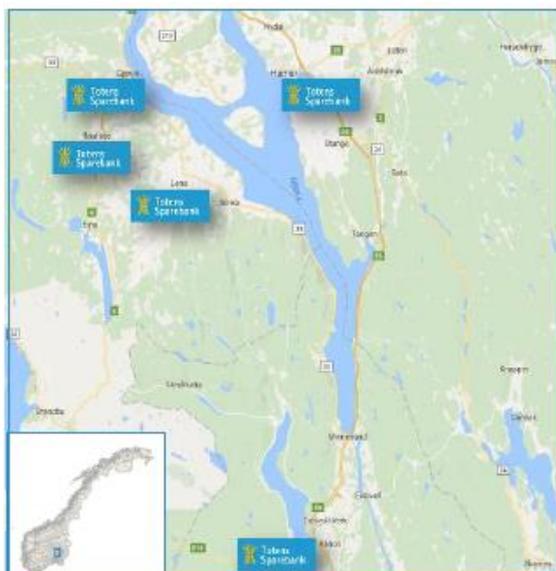
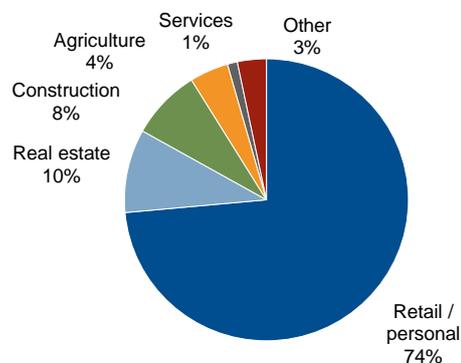


Figure 2: Loan portfolio by sector



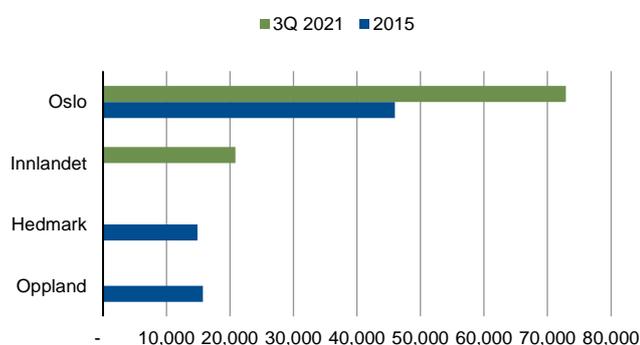
Note: Data as of 30 Sep 2021. Gross loans of NOK 17.9bn, excluding NOK 2.4bn in retail loans transferred to Eika Boligkreditt. Source: Bank, Scope Ratings.

Region with lower and more stable unemployment rates

With approximately 200,000 residents, the Mjos region in south-east Norway has low exposure to the more cyclical oil and gas industry. Meanwhile, the proportion of people employed in the public sector is higher than the national average. Ostre Toten is one of the largest agricultural municipalities in the country while Vestre Toten is one of the most industrial. In addition, the region is home to the Norwegian University of Science and Technology with approximately 3,900 students.

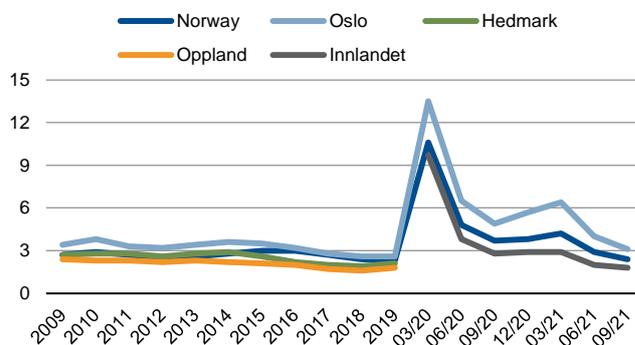
House prices in the bank's main market are at a lower absolute level and have not increased to the same degree as in the Oslo area. The Mjos region, which is part of Innlandet county, also tends to have lower and more stable unemployment rates compared to other parts of the country.

Figure 3: Average price per square metre (NOK)



Note: Data for detached houses. From Jan 2020, Hedmark and Oppland merged to form Innlandet. Source: Statistics Norway.

Figure 4: Unemployment rates (%)



Note: From Jan 2020, Hedmark and Oppland merged to form Innlandet. Source: NAV.

Solid profitability with good cost efficiency and low credit impairments

Membership in alliance key for competitive position

Totens aims to be an independent and profitable bank offering customers competitive financial products and services. The bank's membership in the Eika Alliance is a key factor in maintaining a competitive position. The alliance seeks to strengthen the position of its member banks which together represent the fourth largest banking group in the country. Through jointly owned product companies, member banks can offer a range of products such as insurance, credit cards and mutual funds to their customers.

In addition, the alliance provides a means to achieve economies of scale in banking operations, IT infrastructure and the fulfilment of legal requirements. In December 2020, the alliance entered into a five-year agreement with TietoEVERY to provide its members with updated core banking and payment solutions. Totens will be migrating to the new core system in 1H 2023 and has so far booked NOK 22m in costs related to the transition. Migration costs are expected to be recovered through cost saves over the next four to five years.

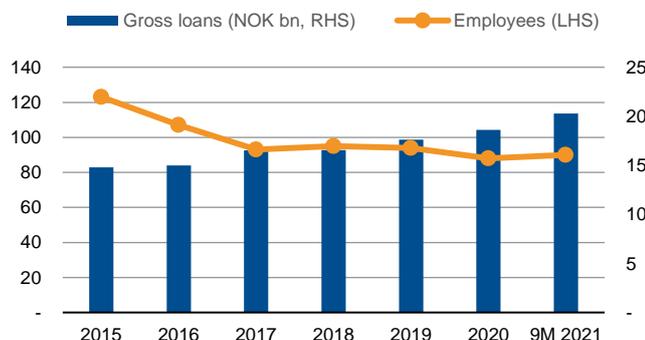
Over the years, management has taken action to improve the bank's efficiency such as disposing of non-core banking activities (real estate brokerage) and cutting the number of branches to five from ten and reducing the number of staff. Management aims for a cost-income ratio below 40% over the long-term (9M 2021: 43% or 39% excluding non-recurring items).

Operating performance has so far been resilient

The bank's earnings and asset quality have remained resilient during the economic downturn caused by the Covid-19 pandemic (Figure 6). Following provisions of

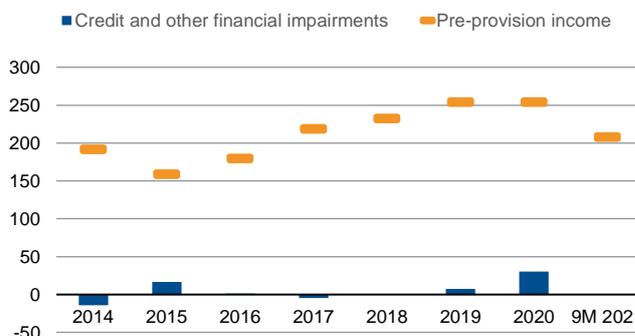
NOK 30m in 2020, the bank has experienced credit releases of NOK 0.3m for the first nine months of this year. Management maintains NOK 13.9m in precautionary provisions for uncertainties related to the pandemic.

Figure 5: Gross loans vs number of employees



Note: Includes loans transferred to Eika Boligkreditt.
Source: Bank, Scope Ratings.

Figure 6: Pre-provision income vs impairments (NOK m)



Source: Bank, Scope Ratings.

Sound prudential metrics

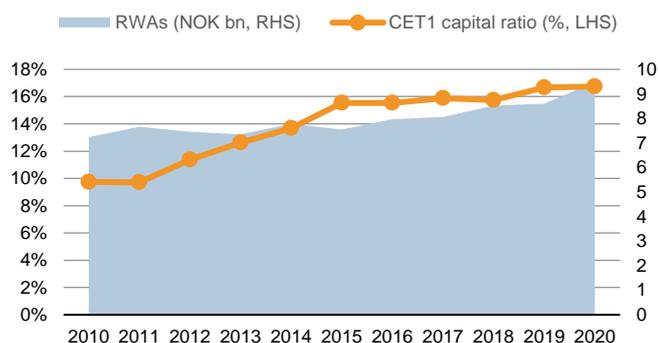
Currently meets expected future requirements

Totens is well positioned against current and future expected solvency requirements (Figure 8). As of 30 September 2021, the CET1 capital ratio was an estimated 15.7% (proportional consolidation basis) while the leverage ratio was 8.2%, compared to requirements of 12.6% and 5%, respectively.

The minimum CET1 capital requirement for domestic oriented Norwegian banks is a relatively high 11%, which includes a 3% systemic risk buffer and a countercyclical buffer of 1%. In response to the Covid-19 pandemic, the countercyclical buffer rate was lowered to 1% from 2.5% in March 2020. In addition, Totens is subject to a relatively low Pillar 2 requirement of 1.6%.

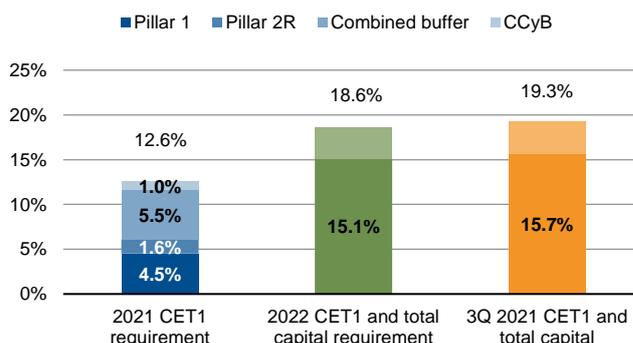
As the Norwegian economy has recovered, the countercyclical buffer rate is set to increase to 1.5% from 1% on 30 June 2022 and to 2% on 31 December 2022. In addition, the systemic risk buffer will increase to 4.5% from 3% at year-end 2022 for banks like Totens using the standardised approach. In its capital planning, management has also considered the eventual return of the countercyclical buffer rate to 2.5%. Normally, management targets a 0.8% buffer above requirements to cover potential fluctuations in growth and losses as well as regulatory uncertainties.

Figure 7: CET1 capital (%) and RWA (NOK bn development)



Source: Bank, Scope Ratings.

Figure 8: Capital position vs current and future requirements



Notes: Combined buffer comprises capital conservation and systemic risk buffers. CCyB is countercyclical capital buffer. Source: Bank, Scope Ratings.

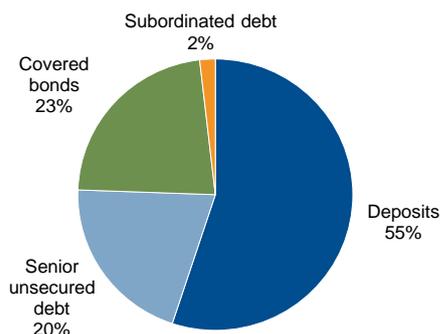
Managed reliance on market funding

Customer deposits remain the largest source of funding (Figure 8). The bank focuses on retail deposits rather than larger corporate deposits which may be less stable. At the same time, management does not intend to greatly increase the proportion of deposit funding as it prefers to maintain an active presence in capital markets by issuing regularly in sufficient size.

As with other Norwegian banks, Totens depends on market funding, including relatively stable covered bonds. Totens has access to two covered bond vehicles – Eika Boligkreditt, the issuing entity for the Eika Alliance and Totens Sparebank Boligkreditt, its own. Over time, management has increasingly used the bank’s own covered bond vehicle rather than that of the alliance. As of 3Q 2021, NOK 2.4bn in loans had been transferred to Eika Boligkreditt.

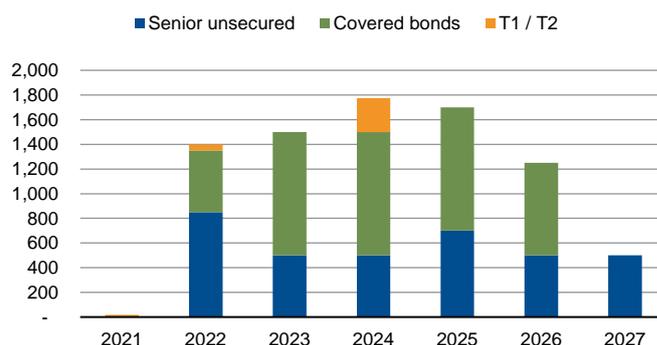
Mitigating risks related to the use of market funding, Totens maintains a high-quality liquidity portfolio (primarily government and covered bonds). As of 30 September 2021, the portfolio amounted to NOK 2.2bn, equivalent to more than three times the amount of wholesale funding due within the next twelve months.

Figure 9: Funding profile (30 Sep 2021)



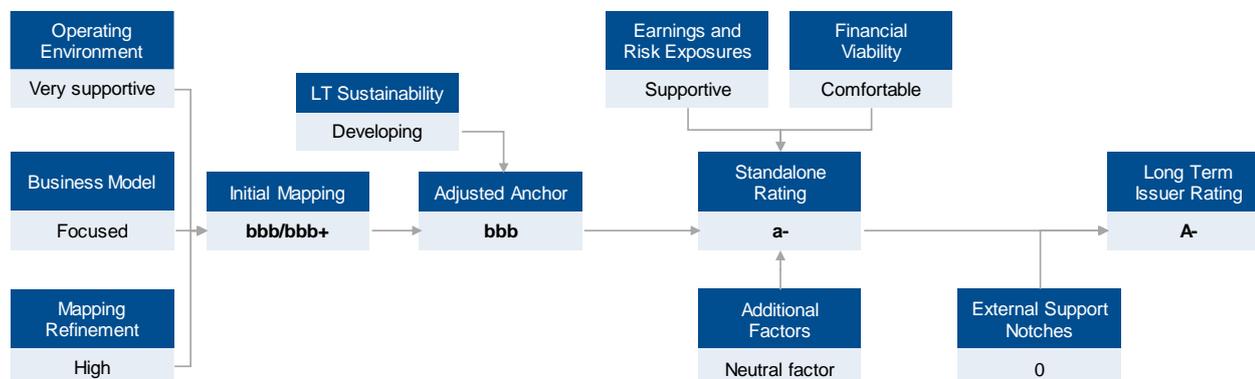
Source: Bank, Scope Ratings.

Figure 10: Funding maturity profile (NOK m)



Note: Data as of 30 Sep 2021.
Source: Bank, Scope Ratings.

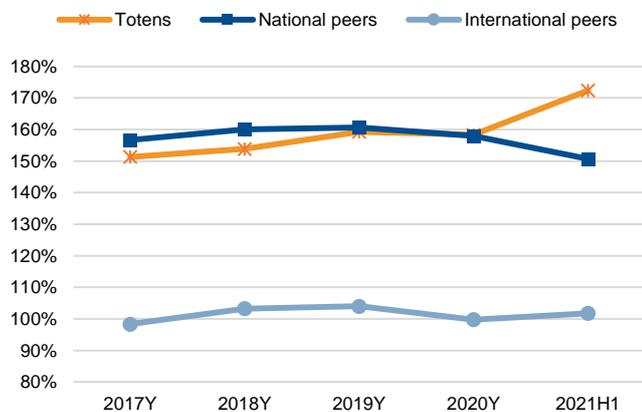
I. Appendix: Overview of the rating process



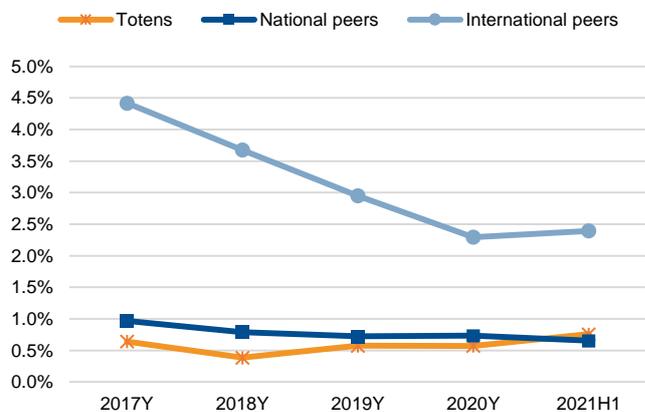
Step		Assessment	Summary rationale
STEP 1	Operating environment	Very supportive	<ul style="list-style-type: none"> Wealthy economy with well-developed capital markets and a solid track record of economic resilience Supportive competitive environment Relatively stringent and active financial regulator
		Supportive	
		Moderately supportive	
		Constraining	
		Very constraining	
	Business model	Very resilient	<ul style="list-style-type: none"> Savings bank with a focus on retail customers and residential mortgage lending Membership in alliance brings significant benefits Operations concentrated in one region
		Resilient	
Consistent			
Mapping refinement	Focused	<ul style="list-style-type: none"> Strong market position in local area with resilient operating performance 	
	Narrow		
Initial mapping	a/a-		
Long-term sustainability	Best in class	<ul style="list-style-type: none"> Has started to integrate ESG risks in underwriting process Migrating to an updated core banking system in 1H 2023 	
	Advanced		
	Developing		
	Lagging		
Adjusted anchor	a+		
STEP 2	Earnings capacity & risk exposures	Very supportive	<ul style="list-style-type: none"> Solid profitability with good cost efficiency and low credit impairments Resilient asset quality throughout pandemic
		Supportive	
		Neutral	
		Constraining	
	Financial viability management	Very constraining	<ul style="list-style-type: none"> Comfortably meets regulatory requirements Reliance on market funding, including more stable covered bonds Maintains high quality liquidity portfolio
		Ample	
		Comfortable	
		Adequate	
		Limited	
	Additional factors	Stretched	<ul style="list-style-type: none"> No further considerations
At risk			
Significant support factor			
Material support factor			
Standalone	Neutral		
	Material downside factor		
	Significant downside factor		
External support	Not applicable		
Issuer rating	A-		

II. Appendix: Peer comparison

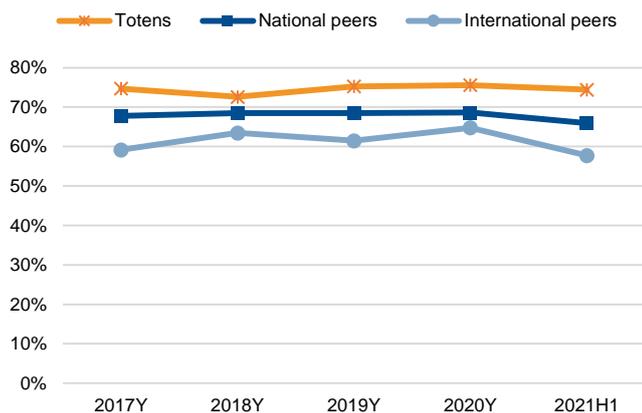
Net customer loans % Deposits



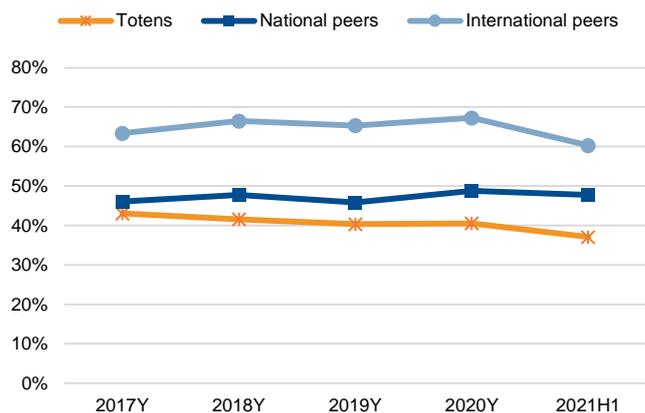
Problem loans % Gross customer loans



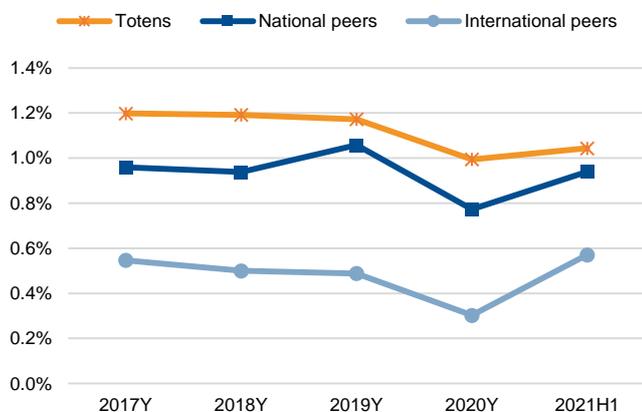
Net interest income % Operating income



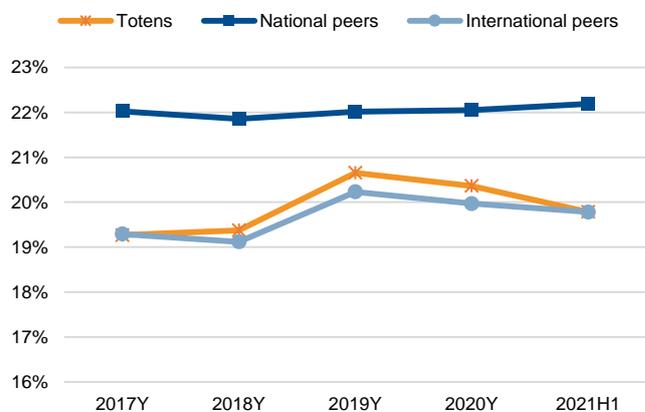
Costs % Income



Return on average assets (%)



Total capital ratio (% , transitional)



National peers: BN Bank, Landkreditt, Sandnes Sparebank, SpareBank 1 Nordmore, Fana Sparebank, Jaeren Sparebank, SpareBank 1 Ostlandet, DNB.
 International peers: Bausparkasse Wustenrot AG, Oberbank AG, Banca Popolare di Sondrio SCpa, Credito Emiliano SpA, Kutxabank SA, Unicaja Banco SA, TSB Banking Group plc, Principality Building Society, Sparbanken Sjuharad AB.
 Note: 1H 2021 data unavailable for TSB Banking Group plc.
 Source: SNL.



III. Appendix: Selected financial information – Totens Sparebank

	2017Y	2018Y	2019Y	2020Y	2021 9M
Balance sheet summary (NOK m)					
Assets					
Cash and interbank assets	169	89	101	146	201
Total securities	1,982	2,208	2,398	2,730	2,591
of which, derivatives	42	26	11	17	6
Net loans to customers	12,366	13,330	14,468	15,679	17,779
Other assets	102	81	98	102	99
Total assets	14,619	15,708	17,065	18,658	20,671
Liabilities					
Interbank liabilities	0	2	21	207	6
Senior debt	4,523	4,986	5,752	6,200	NA
Derivatives	11	7	8	5	8
Deposits from customers	8,171	8,664	9,085	9,904	10,034
Subordinated debt	180	181	200	200	200
Other liabilities	126	106	98	102	NA
Total liabilities	13,011	13,945	15,165	16,618	18,527
Ordinary equity	1,481	1,635	1,757	1,896	2,001
Equity hybrids	128	128	143	143	143
Minority interests	0	0	0	0	0
Total liabilities and equity	14,619	15,708	17,065	18,658	20,671
<i>Core tier 1/ common equity tier 1 capital</i>	<i>1,280</i>	<i>1,344</i>	<i>1,434</i>	<i>1,588</i>	<i>1,608</i>
Income statement summary (NOK m)					
Net interest income	286	288	320	323	254
Net fee & commission income	68	71	74	81	57
Net trading income	9	16	1	-12	2
Other income	20	21	31	36	17
Operating income	383	397	425	427	330
Operating expenses	165	165	171	173	123
Pre-provision income	218	232	254	254	207
Credit and other financial impairments	-5	0	7	30	0
Other impairments	0	0	0	0	0
Non-recurring income	0	0	0	0	9
Non-recurring expense	0	0	0	0	22
Pre-tax profit	223	232	246	224	195
Income from discontinued operations	0	0	0	0	0
Income tax expense	51	50	53	44	40
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	173	182	193	180	155

Source: SNL



IV. Appendix: Selected financial information – Totens Sparebank

	2017Y	2018Y	2019Y	2020Y	2021 9M
Funding and liquidity					
Net loans/ deposits (%)	151%	154%	159%	158%	177%
Liquidity coverage ratio (%)	168%	174%	192%	166%	193%
Net stable funding ratio (%)	136%	139%	138%	137%	NA
Asset mix, quality and growth					
Net loans/ assets (%)	84.6%	84.9%	84.8%	84.0%	86.0%
Problem loans/ gross customer loans (%)	0.6%	0.4%	0.6%	0.6%	0.6%
Loan loss reserves/ problem loans (%)	114.0%	137.0%	94.5%	107.6%	77.1%
Net loan growth (%)	1.0%	7.8%	8.5%	8.4%	17.9%
Problem loans/ tangible equity & reserves (%)	4.7%	2.8%	4.2%	4.2%	4.9%
Asset growth (%)	3.4%	7.4%	8.6%	9.3%	14.4%
Earnings and profitability					
Net interest margin (%)	2.0%	1.9%	1.9%	1.8%	1.7%
Net interest income/ average RWAs (%)	3.6%	3.5%	3.6%	3.6%	3.5%
Net interest income/ operating income (%)	74.7%	72.6%	75.3%	75.6%	76.8%
Net fees & commissions/ operating income (%)	17.7%	17.9%	17.3%	18.9%	17.3%
Cost/ income ratio (%)	43.0%	41.5%	40.3%	40.5%	37.1%
Operating expenses/ average RWAs (%)	2.1%	2.0%	1.9%	1.9%	1.7%
Pre-impairment operating profit/ average RWAs (%)	2.7%	2.8%	2.8%	2.8%	2.8%
Impairment on financial assets / pre-impairment income (%)	-2.2%	0.1%	2.9%	11.9%	-0.1%
Loan loss provision/ average gross loans (%)	0.0%	0.0%	0.1%	0.2%	0.0%
Pre-tax profit/ average RWAs (%)	2.8%	2.8%	2.8%	2.5%	2.7%
Return on average assets (%)	1.2%	1.2%	1.2%	1.0%	1.1%
Return on average RWAs (%)	2.1%	2.2%	2.2%	2.0%	2.1%
Return on average equity (%)	11.0%	11.0%	10.6%	9.4%	10.0%
Capital and risk protection					
Common equity tier 1 ratio (% , fully loaded)	NA	NA	NA	NA	NA
Common equity tier 1 ratio (% , transitional)	15.9%	15.8%	16.7%	16.7%	15.9%
Tier 1 capital ratio (% , transitional)	17.3%	17.3%	18.3%	18.3%	17.3%
Total capital ratio (% , transitional)	19.3%	19.4%	20.7%	20.4%	19.3%
Leverage ratio (%)	9.1%	9.1%	9.0%	9.1%	8.2%
Asset risk intensity (RWAs/ total assets, %)	55.1%	54.3%	50.4%	50.8%	48.9%

Source: SNL



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