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Research Update:

Finnish OP Corporate Bank Ratings Affirmed At 'AA-/A-1+'; Outlook Stable

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Overview

- We expect Finland-based OP Corporate Bank PLC (OP) to continue to strengthen its capital base over the next two years while building up a sizable cushion of bail-inable debt instruments over a four-year horizon.
- Relative to the risks that OP undertakes, capital remains a ratings strength for the bank.
- We are affirming our 'AA-/A-1+' ratings on OP.
- The stable outlook reflects our expectation that all factors driving our ratings are unlikely to change over the next 18-24 months.

Rating Action

On July 27, 2018, S&P Global Ratings affirmed its 'AA-/A-1+' long- and short-term issuer credit ratings on Finland-based OP Corporate Bank PLC (OP). The outlook is stable.

We also affirmed our 'A-' issue ratings on subordinated debt instruments issued by OP Corporate Bank PLC.

At the same time, we affirmed the 'A+' long-term issuer credit rating and insurer financial strength ratings on core subsidiary OP Insurance Ltd. The outlook is stable.

Rationale

The ratings on OP continue to reflect our view that capital remains a ratings strength, relative to the risks that the bank undertakes. The strong domestic franchise of the wider OP Financial Group (comprising about 157 member cooperative banks) and the bank's diversified business model, both of which have resulted in sound and predictable operating profitability, also support the rating.

We consider that, in line with its strategy, the bank has further boosted its capital and earnings position to a level that we now consider to be very strong. This is mainly because we now project the bank's risk-adjusted capital (RAC) ratio at 16.5%-17.0% by December 2020, compared with 14.6% on Dec. 31, 2017, and up from 12.7% on Dec. 31, 2016. The increase in the 2017 RAC ratio calculation was mostly due to a combination of higher retained earnings, lower deductions for equity in the insurance subsidiary, and contained inflation of risk-weighted assets. Moreover, as management is targeting a common equity Tier 1 (CET1) ratio of 22% by end-2019 (up from 20.0% at end-March 2018), we expect the bank to continue to build additional capital by issuing profit shares and organically through solid earnings retention. Specifically, while ultra-low interest rates in Europe and heavy investments in digitalization and service improvements remain a constraint, the sustained business volumes--both in banking (+5% year-on-year loan growth expected this year and next) and insurance--coupled with still-low provisioning levels, will support bottom-line profitability.

However, our improved assessment of capitalization does not affect the rating since it is offset by a downward revision of our view of the bank's risk profile. Nevertheless, we continue to assess the combination of capital and risk as a rating strength for OP's creditworthiness. We believe OP maintains sound underwriting standards and asset quality in its lending book, but our assessment of the bank's risk profile takes into account its geographic concentration in Finland and the higher exposure to real estate in its loan book compared with peers operating in environments with similar economic risks.

We maintain our positive view of the group's business position. Specifically, we view OP as a dominant player in the Finnish market, where it benefits from market shares of 20%-40% in both banking and insurance activities. The bank's business diversification supports the resilience and predictability of earnings, as around a third of its profit before tax comes from insurance and wealth management activities.

In our view, the group's funding mix remains sound and dominated by customer deposits. It also has proven access to capital markets. The group has gradually increased its liquidity buffers, which now cover maturing short-term wholesale debt by about 2x as of March 2018.

We maintain one notch of uplift in the group credit profile, and so the long-term ratings on OP, since we still consider that the group will increase its additional loss-absorbing capacity (ALAC) over the next four years. Based on our new assessment of capital, we estimate that the ALAC buffer equalled 2% of S&P Global Ratings' risk-weighted assets at year-end 2017 and project that it will increase beyond our threshold of 5.0% for a one-notch uplift by end-2021. This reflects our expectation of: 1) the group's capital build-up in line with our RAC ratio forecasts; 2) a gradual replacement of maturing capital instruments with ALAC-eligible instruments; and 3) future regulatory requirements leading the group to maintain or moderately increase its existing buffer of loss-absorbing capacity.

Although we regard OP Insurance Ltd. as a core group entity, we believe the Finnish resolution framework will exclude insurance activities from a bail-in process of OP Financial Group. For this reason, we equalize our long-term ratings on OP Insurance with our 'a+' assessment of OP Financial Group's unsupported group credit profile.

Outlook

The stable outlook on OP reflects our expectation that the creditworthiness of the wider OP Financial Group is unlikely to change over the next two years and that the support mechanism within the group--underpinned by the joint liability between members of the group--remains unchanged. Owing to OP Financial Group's position as a leading bancassurance group, we expect it will continue to benefit from the improving operating environment over the next two years, which should translate into stable high earnings and retention of capital reserves. Specifically, this reflects our expectation that our RAC ratio for the bank will reach a sustainable level above 15% in the next two years and that the bank will continue to build up its regulatory minimum requirement for own funds and eligible liabilities (MREL), which we consider a rating strength in our one-notch uplift for ALAC.

We could lower the rating if we considered that the bank's ALAC buffer was unlikely to exceed our threshold of 5% of S&P Global Ratings' risk-weighted assets over a two-to-four-year ramp-up period.

An upgrade is remote at this stage.

The stable outlook on OP Insurance reflects that on its parent, OP Corporate Bank.

Ratings Score Snapshot

	To	From
Issuer Credit Rating	AA-/Stable/A-1+	AA-/Stable/A-1+
SACP	a+	a+
Anchor	a-	a-
Business Position	Strong (+1)	Strong (+1)
Capital and Earnings	Very Strong (+2)	Strong (+1)
Risk Position	Moderate (-1)	Adequate (0)
Funding and Liquidity	Average and Adequate (0)	Average and Adequate (0)
Support	(+1)	(+1)
ALAC Support	(+1)	(+1)
GRE Support	(0)	(0)
Group Support	(0)	(0)
Sovereign Support	(0)	(0)
Additional Factors	(0)	(0)

Related Criteria

- Criteria - Financial Institutions - General: Methodology For Assigning Financial Institution Resolution Counterparty Ratings, April 19, 2018
- Criteria - Financial Institutions - General: Risk-Adjusted Capital Framework Methodology, July 20, 2017
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings , April 7, 2017
- Criteria - Financial Institutions - Banks: Bank Rating Methodology And Assumptions: Additional Loss-Absorbing Capacity, April 27, 2015
- Criteria - Financial Institutions - Banks: Bank Hybrid Capital And Nondeferrable Subordinated Debt Methodology And Assumptions, Jan. 29, 2015
- General Criteria: Group Rating Methodology, Nov. 19, 2013
- Criteria - Financial Institutions - Banks: Quantitative Metrics For Rating Banks Globally: Methodology And Assumptions, July 17, 2013
- Criteria - Financial Institutions - Banks: Banks: Rating Methodology And Assumptions, Nov. 9, 2011
- Criteria - Financial Institutions - Banks: Banking Industry Country Risk Assessment Methodology And Assumptions, Nov. 9, 2011
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009
- Criteria - Financial Institutions - Banks: Commercial Paper I: Banks, March 23, 2004

Ratings List

Ratings Affirmed

OP Corporate Bank PLC	
Issuer Credit Rating	AA-/Stable/A-1+
Resolution Counterparty Rating	AA-/--/A-1+
Senior Unsecured	AA-
Subordinated	A-
Commercial Paper	A-1+
OP Insurance Ltd	
Issuer Credit Rating	
Local Currency	A+/Stable/--
Financial Strength Rating	
Local Currency	A+/Stable/--