MOODY'S
INVESTORS SERVICE

Credit Opinion: Aktia Bank p.l.c.

Global Credit Research - 07 Mar 2012

Helsinki, Finland

Ratings

Category	Moody's Rating
Outlook	Stable
Bank Deposits	A3/P-2
Bank Financial Strength	C-
Baseline Credit Assessment	(Baa2)
Adjusted Baseline Credit Assessment	(Baa2)
Senior Unsecured -Dom Curr	A3
Other Short Term -Dom Curr	*(P)P-1

* Placed under review for possible downgrade on November 25, 2011

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Key Indicators

Aktia Bank p.l.c. (Consolidated Financials)[1]

	[2]**12-11**	[2]**12-10**	[2]**12-09**	[2]**12-08**	**Avg.**
Total Assets (EUR million)	**9,993.1**	**9,924.3**	**9,539.5**	**9,519.9**	[3]**1.6**
Total Assets (USD million)	**12,972.5**	**13,313.9**	**13,686.7**	**13,233.1**	[3]**-0.7**
Tangible Common Equity (EUR million)	**326.2**	**318.0**	**309.3**	**300.0**	[3]**2.8**
Tangible Common Equity (USD million)	**423.5**	**426.7**	**443.7**	**417.0**	[3]**0.5**
Net Interest Margin (%)	**1.3**	**1.5**	**1.7**	**0.4**	[4]**1.2**
PPI / Avg RWA (%)	**1.3**	**2.3**	**2.5**	**-0.7**	[5]**1.4**
Net Income / Avg RWA (%)	**0.7**	**1.5**	**1.1**	**-0.5**	[5]**0.7**
(Market Funds - Liquid Assets) / Total Assets (%)	**30.0**	**26.8**	**26.6**	**11.6**	[4]**23.7**
Core Deposits / Average Gross Loans (%)	**52.9**	**52.5**	**52.1**	**56.8**	[4]**53.6**
Tier 1 Ratio (%)	**10.6**	**10.1**	**9.5**	**9.3**	[5]**9.9**
Tangible Common Equity / RWA (%)	**8.8**	**8.7**	**8.9**	**9.1**	[5]**8.9**
Cost / Income Ratio (%)	**73.0**	**59.3**	**56.8**	**204.9**	[4]**98.5**

Source: Moody's

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

Opinion

RECENT CREDIT DEVELOPMENTS

On 29 February 2012, Moody's downgraded Aktia Bank's standalone bank financial strength rating (BFSR) to C- (mapping to

Baa2 on the long-term scale) from C (mapping to A3), its long-term debt and deposit ratings to A3 from A1 and its short-term debt and deposit ratings to Prime-2 from Prime-1. The outlook on all ratings is stable.

The rating action concluded the review for downgrade implemented on 25 November 2011 following concerns surrounding the bank's weakening profitability and reliance on market funding, particularly covered bonds.

The downgrade primarily reflects Moody's expectations that Aktia Bank's income generation will remain under pressure (due to expiration of the positive effects of interest rate hedges as well as the competitive Finnish operating environment) and reiterates concerns over the bank's high reliance on market funding, particularly on covered bonds issued through Aktia Real Estate Mortgage Bank.

SUMMARY RATING RATIONALE

Moody's rates Aktia Bank A3/P-2/C-.

The bank's standalone C- financial strength rating (BFSR), which maps to Baa2 on the long term scale, is supported by Aktia Bank's established - albeit small - franchise, prudent risk and liquidity management and good financial fundamentals, particularly asset quality and capital adequacy. Key elements constraining the BFSR include the bank's limited position in the competitive banking market, which is likely to lead to continued pressure on its profitability and a high borrower risk concentration.

Aktia Bank's A3/Prime-2 global local currency (GLC) deposit ratings and (P)A3 unsecured debt rating are supported by (i) the bank's Baa2 standalone financial strength and (ii) the Aaa local currency deposit ceiling of Finland, which we consider the underlying support provider. As a result of Aktia Bank's importance to the Finnish economy (including via its role as the central financial institution for independent savings banks and local co-operative banks) Moody's assesses a high probability of systemic support for the bank in the event of a stress situation. Consequently, Aktia Bank's GLC deposit rating benefits from a two-notch uplift from the standalone financial strength.

Rating Drivers

- Stable regional franchise includes role as the central financial institution for independent savings banks and local co-operative banks-

- High reliance on market funding, albeit through established covered bond franchise

- Good asset quality despite high single-borrower concentration

- Weakening operating profitability due to the expiration of beneficial interest rate hedges and a competitive operating environment

Rating Outlook

The outlook on all ratings is stable

What Could Change the Rating - Up

Over time, a return to sustainable earnings growth while maintaining strong asset quality could provide upward pressure on the ratings

What Could Change the Rating - Down

In case Aktia Bank's earnings do not stabilise over the next 12 -- 18 months, or in case of a more-than-expected deterioration of asset quality, renewed pressure could arise on the bank's ratings.

DETAILED RATING CONSIDERATIONS

Detailed considerations for Aktia Bank's currently assigned ratings are as follows:

Bank Financial Strength Rating

Moody's assigns a BFSR of C- to Aktia Bank. The main elements underpinning the BFSR are the bank's good asset quality and satisfactory capitalisation. Key elements constraining the BFSR include its limited market position in the competitive banking market, which is likely to lead to sustained pressure on its profitability and high borrower risk concentration.

Franchise

Aktia Bank is the fourth-largest bank in Finland by total assets, with a focus on the retail market. In addition, it acts as a strategic partner for independent savings banks and local co-operative banks.

Aktia Bank has more than 70 own branches, located mainly in the coastal areas of Finland, around Helsinki and the country's largest inland towns. The bank's market share in retail mortgages is around 4% but is less significant in corporate loans at around 1%. The bank also reported a market share of around 7% in mutual funds at end 2011.

About 84% of the loan portfolio is to retail customers, 11% to SMEs and 4% to housing associations.

Given the focus on retail lending Moody's estimates that around 70% of Aktia Bank's earnings stem from more stable sources such as the retail banking and asset management operations. This reflects Aktia's role as product provider for savings banks and cooperative banks, which also use Aktia Mortgage Bank to fund their mortgage loans.

Profitability

Aktia Bank reports moderate profitability in line with its focus on retail banking. 2011 pre-tax profit amounted to EUR 33.5 million, down from EUR 70.9 million in 2010, mainly reflecting a decline in net interest income due to the expiration of beneficial long term interest rate hedges. Total net interest income - including hedge income - declined to EUR 128.2 million in 2011 from EUR 149.2 million in 2010, while, positively, the bank managed to increase net interest income on its lending and deposit operations to EUR 63.0 million in 2011 from EUR 54.8 million in 2010.

Write-downs on credits and other commitments decreased to EUR 10.5 million in 2011 from EUR 12.9 million in 2010 but accounted to 20% of pre-provision income in 2011 (16%) on the back of lower operating income.

Cost efficiency deteriorated significantly in 2011 on the back of decreasing operating income and increased to 73% from 59% in 2010.

We expect some further weakening in operating income mainly due to the strong competition and the continuing run off of Aktia's beneficial long term interest rate hedges.

Market Funding

Aktia Bank's funding profile has shifted from deposits - which had contributed up to 80% of funding in the 1990s and 60% in the mid-2000s - to market funding. Still, deposits remain one of the most important source of funding accounting for around 40% in at end December 2011.

45% of total funding comprises market funding excluding interbank. Covered bonds issued by Aktia Real Estate Mortgage Bank represent a growing proportion of market funds, 80% as at end 2011 (EUR 3.3 billion).

In regards to market funding, we note that the covered bonds (rated Aa1 by Moody's) issued via the subsidiary Aktia Real Estate Mortgage Bank are included in Aktia Bank's market funding as a whole, although approximately half of the loans at year-end 2011 were granted and are managed by independent savings banks and local co-operative banks. Aktia Bank has 70% of votes and 49.9% of shares in Aktia Real Estate Mortgage Bank with the rest owned by 31 savings banks (37.9% of equity and 20% of votes) and 36 local cooperative banks (12.2% of equity and 10% of votes). This reflects the origination of mortgage loans that are distributed by the branch network of the co-operating banks and funded through the Mortgage Bank.

The bank's liquid assets account for around 27% of total assets (end December 2011) and historically have consisted mainly of highly rated covered bonds and senior bonds of financial institutions.

We consider Aktia's reliance on market funding as a risk in view of the continued fragility of global capital markets and believe that the bank may be negatively affected by these difficulties as well as increase its funding costs, which would put additional pressure on the already depressed margins.

Capital Adequacy

At end December 2011, Aktia Bank's total capital and Tier 1 ratios stood at 16.2% and 10.6% respectively up from 15.9% and 10.1% at YE2010. The bank is currently applying the standardised Basel II approach when assessing the capital requirements for credit risk but has also applied for the IRB approach to the Finnish FSA.

Asset Quality

Despite some single-name concentrations, Aktia Bank enjoys relatively good asset quality, reflecting its focus on the retail sector (around 80% of its loan portfolio is related to residential mortgages with another 4% to other retail).

Aktia Bank's total loan book stood at EUR 7.1 billion at end December 2011, with around EUR 3.9 billion of this on the balance sheet of its mortgage company, which is consolidated into Aktia Bank's accounts. Lending growth in 2011 for Aktia Bank (including loans in the mortgage company) was 7% (10% for 2010). Excluding the loans from savings and POP banks the loan growth was 3%.

Aktia Bank's reported problem loans (defined as net loans over 90 days past due) accounted for 0.84% of gross loans at end December 2011, up from 0.54% at YE2010. The increase was primarily driven by the increase of overdue loans to households.

The borrower concentration risk - as measured by the 20 largest exposures in relation to Tier 1 capital or pre-provision profit - is high. Although this is a constrain on the overall risk positioning score, it is in line with many other Nordic banks of similar size. When excluding exposures rated above A3, the concentration is more limited at around 73% of Tier 1 capital. Industry concentration risk is relatively well contained due to the bank's dominating focus on the retail sector, which accounted for around 85% of total loans at end December 2011. The largest industry sector is commercial real estate, which represents around 4% of total lending and around 80% of Tier 1 capital.

Global Local Currency Deposit Rating (Joint Default Analysis)

Moody's assigns a long-term GLC deposit rating of A3 to Aktia Bank.

This rating is supported by (i) the bank's Baa2 standalone financial strength and (ii) the Aaa local currency deposit ceiling of Finland, its underlying support provider. In view of Aktia Bank's moderate market shares in both deposits and loans and its role as the central financial institution to independent savings banks and local co-operative banks, Moody's assesses a high probability of systemic support for the bank in the event of a stress situation, resulting in a two-notch uplift from the Baa2 BCA.

Foreign Currency Deposit Rating

The A3 foreign currency deposit rating and (P)A3 unsecured debt rating of Aktia Bank are unconstrained given that Finland has a country ceiling of Aaa.

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

Aktia Bank p.l.c.

Rating Factors [1]	A	B	C	D	E	Total Score	Trend
Qualitative Factors (50%)						C+	
Factor: Franchise Value						C	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					x		
- Borrower Concentration					x		
- Industry Concentration		x					
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			2.04%				
Net Income / Average RWA - Basel II			1.10%				
Factor: Liquidity						D+	Weakening
(Mkt funds-Liquid Assets) / Total Assets					27.78%		
Liquidity Management			x				
Factor: Capital Adequacy						B+	Neutral
Tier 1 Ratio - Basel II		10.07%					

Tangible Common Equity / RWA - Basel II	8.81%						
Factor: Efficiency						**C**	**Weakening**
Cost / Income Ratio			63.06%				
Factor: Asset Quality						**C+**	**Neutral**
Problem Loans / Gross Loans	--	--	--	--	--		
Problem Loans / (Equity + LLR)	--	--	--	--	--		
Lowest Combined Score (15%)						**D+**	
Economic Insolvency Override						**--**	
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