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## Research Update:

# Bank of Ireland 'BBB-/A-3' Ratings Affirmed On Government Support And ALAC Review; Outlook Positive

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## Research Update:

# Bank of Ireland 'BBB-/A-3' Ratings Affirmed On Government Support And ALAC Review; Outlook Positive

## Overview

- We believe the prospect of extraordinary government support for Irish banks is now uncertain in view of the country's well-advanced and effective resolution regime.
- We are therefore removing the one notch of uplift for government support that we had previously incorporated into the long-term counterparty credit ratings on Bank of Ireland (BOI).
- We are also removing the negative adjustment that we had previously incorporated into the rating.
- We consider that there is a degree of uncertainty regarding BOI's path to increasing its additional loss-absorbing capacity (ALAC) above our 4.75% threshold, given pending regulatory guidance.
- We are affirming the long- and short-term counterparty credit ratings on BOI at 'BBB-/A-3'.
- The positive outlook reflects our expectation that we may raise the ratings on BOI over the next one-to-two years if we expect that capitalization, as indicated by the risk-adjusted capital (RAC) ratio, will comfortably and sustainably exceed 7%.

## Rating Action

As previously announced on Dec. 2, 2015, Standard & Poor's Ratings Services affirmed the long- and short-term counterparty credit ratings on Bank of Ireland (BOI) at 'BBB-/A-3'. The outlook is positive.

We also affirmed the issue ratings on the subordinated and hybrid capital instruments issued by these entities because we maintained the unsupported group credit profile (GCP) at 'bbb-'.

## Rationale

We believe that the prospect of extraordinary government support for the Irish banking sector is now uncertain following the expected full implementation of the EU Bank Recovery and Resolution Directive, including bail-in powers, from Jan. 1, 2016. We do not completely exclude the possibility of such support and we consider that systemically important Irish institutions such as BOI face several more years of structural and balance sheet reforms to address their "resolvability" (mitigating the systemic impact if they fail). Nevertheless,

we believe the Irish government's ability and willingness to provide support is lower and less predictable under the enhanced resolution framework. We have therefore reclassified the tendency of Ireland to support private sector commercial banks as "uncertain" under our criteria, and removed the one notch that we previously included for government support in the long-term counterparty credit rating on BOI. At the same time, we have also removed the negative adjustment that we had previously incorporated into the rating, reflecting our view of BOI's transition to sustainable profitability and its rating level relative to peers'. Therefore, our reassessment of government support does not affect the counterparty credit rating on BOI.

We view the Irish resolution regime as "effective" under our ALAC criteria because, among other factors, we believe it contains a well-defined bail-in process under which authorities would permit non-viable systemically important banks to continue critical functions as going concerns following a bail-in of eligible liabilities.

We calculate that BOI's ALAC was 3.7% of Standard & Poor's risk-weighted assets (RWAs) at year-end 2014. We expect that this ratio would have reduced to slightly below 3% at year-end 2015. This incorporates both BOI's AT1 issuance from earlier this year as well as the upward revision of our capital and earnings assessment on BOI to "moderate" from "weak" in July 2015. We include in this assessment the eligible Tier 1 and Tier 2 capital instruments that were issued under Irish and English law or feature contractual recognition of bail-in. We believe these issues have the capacity to absorb losses without triggering a default on senior obligations.

We believe that BOI will continue to increase its ALAC buffer over our projection period, both on the back of steady internal capital generation and the issuance of ALAC-eligible instruments. That said, we do not incorporate any notches of ALAC uplift at this time given that guidelines from the Irish regulator on the resolution approach, build-up of bail-in capacity, and the transition timeline are pending. Furthermore, the build-up of total adjusted capital (TAC) could potentially lead us to revise our assessment of BOI's capital and earnings to "adequate" from "moderate" currently. The resulting reduction of excess TAC (going concern capital over and above the amount needed to maintain the current unsupported GCP) will likely lower the trajectory of ALAC build.

We have lowered the threshold for BOI's first notch of ALAC uplift to 4.75% (from the default 5.0%) because we qualitatively adjust for BOI's insurance operations that we expect would be outside the scope of required bail-in capitalization.

We have maintained the unsupported GCP at 'bbb-' based on BOI's leading market position in Ireland, meaningful U.K. franchise, and expected steady internal capital generation on the back of improving macroeconomic conditions in Ireland.

## Outlook

The positive outlook indicates that we may raise the ratings on BOI over the next one-to-two years if we expect that capitalization, as indicated by the Standard & Poor's risk-adjusted capital (RAC) ratio, will comfortably and sustainably exceed 7%. For example, this could result from an improvement in our view of the macroeconomic risks that BOI faces, which in turn would lower the risk weights that we apply to its exposures.

We may also upgrade BOI if we include one notch of support for ALAC. However, we view this scenario as less likely over the outlook horizon.

We could revise the outlook to stable if we perceive that BOI's dividend policy, its longer term growth in Standard & Poor's RWAs, and its risk appetite, do not warrant an upward revision of the bank's GCP.

## Ratings Score Snapshot

	To	From
Issuer Credit Rating	BBB-/Positive/A-3	BBB-/Positive/A-3
SACP	bbb-	bbb-
Anchor	bbb-	bbb-
Business Position	Strong (+1)	Strong (+1)
Capital and Earnings	Moderate (-1)	Moderate (-1)
Risk Position	Adequate (0)	Adequate (0)
Funding and Liquidity	Average and Adequate (0)	Average and Adequate (0)
Support	0	0
ALAC Support	0	0
GRE Support	0	0
Group Support	0	0
Sovereign Support	0	+1
Additional Factors	0	-1

## Related Criteria And Research

### Related Criteria

- General Criteria: Methodology: Use Of 'C' And 'D' Issue Credit Ratings For Hybrid Capital And Payment-In-Kind Instruments - October 24, 2013
- General Criteria: Ratings Above The Sovereign--Corporate And Government Ratings: Methodology And Assumptions - November 19, 2013

- General Criteria: Rating Government-Related Entities: Methodology And Assumptions - March 25, 2015
- Criteria - Financial Institutions - Banks: Assessing Bank Branch Creditworthiness - October 14, 2013
- Criteria - Financial Institutions - Banks: Commercial Paper I: Banks - March 23, 2004
- General Criteria: Principles For Rating Debt Issues Based On Imputed Promises - December 19, 2014
- General Criteria: Standard & Poor's National And Regional Scale Mapping Tables - September 30, 2014
- General Criteria: National And Regional Scale Credit Ratings - September 22, 2014
- General Criteria: Criteria For Assigning 'CCC+', 'CCC', 'CCC-', And 'CC' Ratings - October 01, 2012
- General Criteria: Group Rating Methodology - November 19, 2013
- 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 - January 29, 2015
- Criteria - Financial Institutions - Banks: Quantitative Metrics For Rating Banks Globally: Methodology And Assumptions - July 17, 2013
- Criteria - Financial Institutions - Banks: Revised Market Risk Charges For Banks In Our Risk-Adjusted Capital Framework - June 22, 2012
- Criteria - Financial Institutions - Banks: Banks: Rating Methodology And Assumptions - November 09, 2011
- Criteria - Financial Institutions - Banks: Banking Industry Country Risk Assessment Methodology And Assumptions - November 09, 2011
- Criteria - Financial Institutions - Banks: Bank Capital Methodology And Assumptions - December 06, 2010
- Criteria - Financial Institutions - Banks: Methodology For Mapping Short- And Long-Term Issuer Credit Ratings For Banks - May 04, 2010
- General Criteria: Use Of CreditWatch And Outlooks - September 14, 2009

## **Related Research**

- Most European Bank Ratings Affirmed Following Government Support And ALAC Review, Dec. 2, 2015
- Credit FAQ: How Standard & Poor's Applied Its Government Support And ALAC Criteria To European Banks In December 2015, Dec. 2, 2015
- Standard & Poor's To Conclude Its Review Of Systemic Support For Remaining EU Banks By Early December 2015, Oct. 1, 2015
- Government And ALAC Support Ratings Uplift For Systemically Important European Banking Groups, Oct. 1, 2015
- How The Regulatory Reform Process Could Reshape Banks' Business Models And Affect Issuer Ratings, Aug. 18, 2014
- Standard & Poor's Takes Various Rating Actions On European Banks Following Government Support Review, April 29, 2014
- Credit FAQ: The Rating Impact Of Resolution Regimes For European Banks, April 29, 2014

## Ratings List

### Ratings Affirmed

#### Bank of Ireland

Counterparty Credit Rating	BBB-/Positive/A-3
Senior Unsecured	BBB-
Subordinated	BB
Junior Subordinated	B+
Preference Stock	B+
Commercial Paper	A-3

#### Bank of Ireland U.K. Holdings PLC

Junior Subordinated*	B+
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\*Guaranteed by Bank of Ireland.

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