Various Rating Actions Taken On AIB Group, Bank of Ireland, And Permanent TSB On Prospects Of Stronger Creditworthiness

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- We expect AIB Group PLC (AIB) and Bank of Ireland Group PLC (BOI) will remain broadly on track to achieve nonperforming exposure (NPE) ratios of about 3% and Permanent TSB Group Holdings PLC (PTSB) to stabilize its NPE ratio below 4% in 2023-2024, on the back of still-low unemployment and healthy underwriting standards.
- This progressive improvement in the banks' asset quality would place them in line with better performing and higher-rated European peers, in our view.
- Furthermore, higher interest rates, greater scale and a continuous focus on cost discipline will benefit AIB, BOI, and PTSB's operating profitability, also supporting their overall creditworthiness.
- By year-end 2023, we expect PTSB to reach a buffer of subordinated bail-in-able debt large enough to benefit from two notches of ratings uplift.
- We therefore raised the ratings on PTSB's main operating bank, Permanent TSB PLC, to 'BBB/A-2' from 'BBB-/A-3' and affirmed the 'BB-/B' ratings on nonoperating holding company (NOHC) PTSB Group Holdings PLC. The outlooks are positive on both entities.
- We revised our outlooks on AIB Group PLC, Bank of Ireland Group PLC, and their respective operating companies to positive and affirmed the ratings.

DUBLIN (S&P Global Ratings) Dec. 22, 2022--S&P Global Ratings today took the following rating actions:

- We raised our long- and short-term issuer credit ratings (ICRs) on main operating bank Permanent TSB PLC to 'BBB/A-2' from 'BBB-/A-3' and the long-term resolution counterparty rating (RCR) to 'BBB+' from 'BBB'. We affirmed the short-term RCR. The outlook is positive.
- We affirmed the 'BB-/B' long- and short-term ICRs on nonoperating holding company Permanent TSB Group Holdings PLC. The outlook is positive.
- We revised the outlooks to positive from stable on AIB Group PLC and Allied Irish Banks PLC. We also affirmed our 'BBB-/A-3' long- and short-term ICRs on holding company AIB Group PLC, our 'A-/A-2' long- and short-term ICRs and our 'A/A-1' long- and short-term RCRs on Allied Irish Banks, and all our issue ratings on the group's debt.
- We revised the outlooks to positive from stable on Bank of Ireland Group PLC and Bank of Ireland. We also affirmed our 'BBB-/A-3' long- and short-term ICRs on holding company Bank of

Ireland Group PLC, our 'A-/A-2' long- and short-term ICRs, and our 'A/A-1' long- and short-term RCRs on Bank of Ireland, and all our issue ratings on the group's debt.

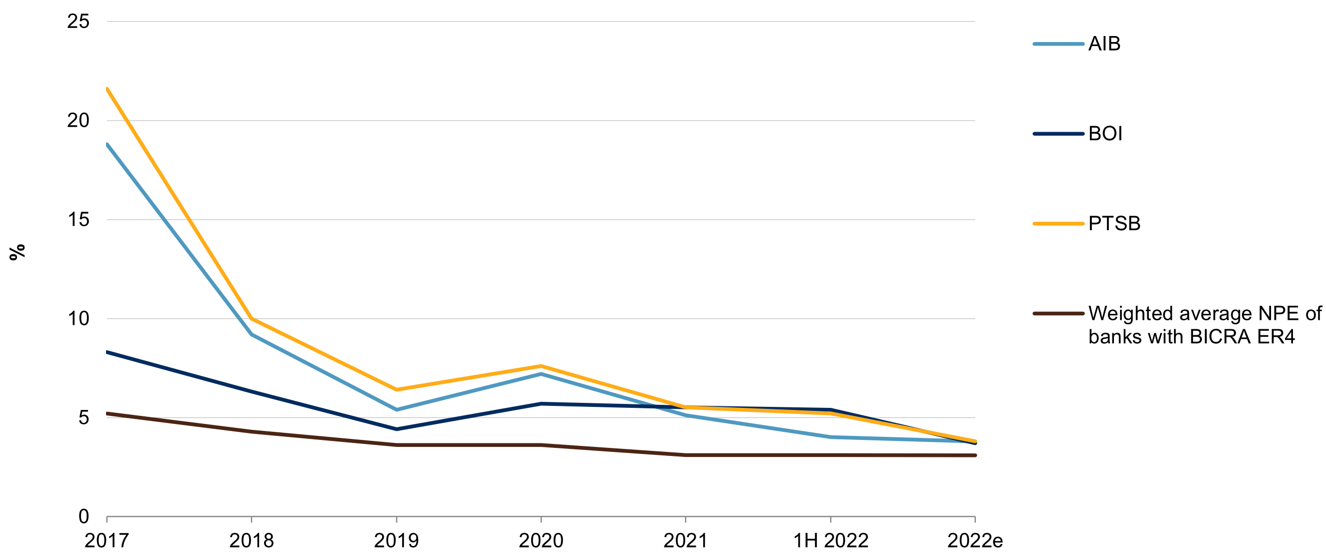
Rationale

We expect Irish banks to continue reducing their nonperforming loans over the next 18-24 months and stabilize them at the European banking system average. Irish banks' asset quality has been improving over the past decade thanks to continuous balance sheet clean-ups and healthy underwriting standards for new loan generation. At year-end 2022, we estimate NPEs at about 3.8% of gross loans for AIB and PTSB, and about 3.7% for BOI (including the NPE disposal transaction in the fourth quarter), down from 21.6%, 23%, and 11.4% respectively in 2016. Elevated inflation and increasing interest rates will pressure the private sector's debt-servicing capacity but we expect the impact to be manageable, and all three banks to stabilize their stock of NPEs – AIB and BOI at about 3% of total loan exposures and PTSB at below 4%. The acquisition of performing assets (from KBC Bank Ireland by BOI and from Ulster Bank by AIB and PTSB) will also help in this process. We anticipate additional problem loans will emerge, mostly among small and midsize enterprises (SMEs). Residential mortgages--comprising 50.3% of gross loans for AIB as of mid-year 2022, 53% for BOI, and 97% for PTSB--will likely hold up thanks to still-high employment and low average loan-to-value (LTV) ratios averaging 49% for AIB, 54% for BOI, and 56% for PTSB at June 30, 2022.

Chart 1

Irish Banks' NPE Ratio Is Approaching The Weighted Average For Countries With Similar Economic Risk

Nonaccrual loans / customer loans (gross)



NPE--Nonperforming exposure. e--Estimate. BICRA--Banking Industry Country Risk Assessment. ER--Economic risk. Source: S&P Global Ratings.

Like other European countries, Ireland's economy is set to slow next year amid a tough global environment but it should continue to outperform peers over the next two years, supporting banks' asset quality. We note downside risk attached to our macroeconomic forecast but under our current base-case scenario we expect the underlying Irish economy to expand 1.2% in 2023 versus 0% for the wider eurozone. Slowing economic activity will spill over to the labor market but we expect unemployment will increase only moderately to a peak of 5.2% in 2023 from our estimate of 4.6% in 2022. We see most risk to Irish banks from inflation, which is anticipated to remain high at 7% in 2023. This will weigh on both operating costs and the debt-service capacity of borrowers.

Despite a weakening macroeconomic environment, higher interest rates and a continuous focus on cost discipline will improve Irish banks' operating profitability. The gradual repricing of loans, containment of funding costs given the large share of nonsensitive deposits, and larger scale from portfolio acquisitions, position AIB, BOI, and PTSB well to benefit from increasing interest rates. The share of net interest income in operating revenue will expand to about 78% for AIB, 80% for BOI, and 90% for PTSB by year-end 2024, largely on the back of the consolidating market and acquisitions of loan portfolios from exiting Ulster Bank and KBC Bank Ireland. AIB and BOI are also on track to increase their top-line results after expanding their product offerings in insurance and wealth management and diversifying revenue sources over the past year. Although inflation will pressure costs, higher interest rates and sector consolidation will mean stronger revenue growth, which should help reduce cost to income to below 60% for AIB and BOI and to below 70% for PTSB over the next two years.

The upgrade of Permanent TSB PLC reflects our expectation that the group will reach and maintain a buffer of subordinated bail-in-able debt large enough to benefit from two notches of ratings uplift. We estimate our additional loss-absorbing capacity (ALAC) ratio at 6.8% by year-end 2022 versus 5.1% at year-end 2021. Management has plans for further issuances in 2023 to remain compliant with its 27.11% minimum requirement for own funds and eligible liabilities (MREL), including combined buffer requirements, by the January 2024 deadline. We incorporate this plan into our forecast and envisage ALAC will further improve and stay sufficiently above our 8% threshold over the next two years for the main operating bank to qualify for two notches of ratings uplift. The buffer is likely to comprise only a limited number of instruments. Therefore, we apply a higher threshold to PTSB than our standard 6%. We do not incorporate notches for ALAC support in our ratings on NOHC Permanent TSB Group Holdings PLC because the build-up of bail-in buffers only benefits the creditors of the operating entity. As a result, the ratings on the NOHC remain two notches below the 'bb+' group stand-alone credit profile (SACP).

AIB Group PLC (Holdco) And Allied Irish Banks (Opco)

Primary analyst: Letizia Conversano

Our ratings on AIB Group are based on its positioning as one of the major players in the Irish market and good franchise, which we expect to further expand over the next 18-24 months. They also reflect our view that the bank will continue to rely on a sound capital base, with buffers able to absorb potential macroeconomic headwinds and to back-up its expansionary activities.

Outlook

The positive outlooks on AIB Group PLC and Allied Irish Banks reflect our expectations that the group's asset quality won't deteriorate over the next 18-24 months, meaning it doesn't deviate from its path toward the 3% NPE ratio target. These expectations are mainly based upon still relatively supportive--although slowing--domestic economic growth in 2023 and 2024, as well as solid underwriting standards.

Upside scenario: We could raise our long- and short-term ICRs on AIB Group and Allied Irish banks over the next 18-24 months if the bank's asset quality metrics are not significantly hit by the domestic economic slowdown, with its NPE ratio continuing to improve toward the about 3% target, alongside a continued strong franchise and resilient profitability.

Downside scenario: We could revise our outlook to stable over the next 18-24 months if we observe a deterioration of the bank's asset quality, significantly delaying the achievement of its NPE ratio target.

Ratings score snapshot

Group SACP: bbb

- Anchor: bbb
- Business Position: Adequate (0)
- Capital and Earnings: Strong (+1)
- Risk Position: Moderate (-1)
- Funding and Liquidity: Adequate and Adequate (0)
- Comparable Rating Analysis: 0

Support: +2

- ALAC Support: +2
- GRE Support: 0
- Group Support: 0
- Sovereign Support: 0

Additional Factors: 0

ESG Credit Indicators: E-2, S-2, G-2

Bank of Ireland Group (Holdco) And Bank of Ireland (Opco)

Primary analyst: Anastasia Turdyeva

The ratings on BOI are based on our view of the group's strong domestic franchise with an improving trajectory for efficiency and profitability metrics over the next two years. They also reflect robust capitalization that should help the group to withstand macroeconomic challenges ahead and support its growth plans. Our ratings on the operating company factor the group's ability to maintain a buffer of bail-in-able debt large enough to provide protection to senior debtholders in a resolution scenario.

Outlook

The positive outlooks on Bank of Ireland Group PLC and Bank of Ireland reflect our expectation that the group's creditworthiness could improve if, despite challenging times ahead, it contains asset quality deterioration with its NPE ratio approaching 3%, further revenue diversification, controlled cost pressure, and strengthening profitability. These expectations are based upon still relatively supportive--although slowing--domestic economic growth in 2023 and 2024, as well as solid underwriting standards.

Upside scenario: We could raise the ratings on both the operating and holding companies over the next 18-24 months if we see the NPE ratio stabilize at about 3% despite challenging credit conditions and slowdowns in the economies where the group operates. However, an upgrade would also require the group to follow its updated business model to become more sustainable, with stable and robust risk-adjusted returns through the cycle, in line with higher-rated peers.

Downside scenario: We could revise the outlook to stable if, contrary to our expectations, the group's asset quality metrics deteriorate amid more negative macroeconomic developments than we currently expect, delaying NPE stabilization.

Ratings score snapshot

Group SACP: bbb

- Anchor: bbb
- Business Position: Adequate (0)
- Capital and Earnings: Strong (+1)
- Risk Position: Moderate (-1)
- Funding and Liquidity: Adequate and Adequate (0)
- Comparable Rating Analysis: 0

Support: +2

- ALAC Support: +2
- GRE Support: 0
- Group Support: 0
- Sovereign Support: 0

Additional Factors: 0

ESG Credit Indicators: E-2, S-2, G-2

Permanent TSB Group Holdings PLC (Holdco) And Permanent TSB PLC (Opco)

Primary analyst: Anastasia Turdyeva

The ratings on PTSB Group are based on our view of its significant geographical and business concentration and limited scale, which we expect will improve over the next 12-18 months. They also reflect the group's sound capitalization, with buffers sufficient to support its expansion plans and cope with macroeconomic challenges. Our ratings on the operating company factor the group's ability to maintain a buffer of bail-in-able debt large enough to provide protection to senior debtholders in a resolution scenario.

Outlook

The positive outlooks on Permanent TSB Group Holdings and Permanent TSB PLC (PTSB) reflect our expectations that the group will continue to reduce its NPE ratio and stabilize it at below 4% of gross loans. We also expect that the group's operating profitability, supported by the loan portfolio acquired from Ulster Bank and rising interest rates, will finally turn positive, somewhat mitigating the structural risks arising from its limited scale and meaningful business and geographical concentrations. These expectations are based upon relatively supportive--although slowing--domestic economic growth over the next two years.

Upside scenario: We could raise the ratings on both the operating and holding companies over the next 12-18 months if asset quality metrics do not deteriorate amid a challenging operating environment and its NPE ratio stabilizes below 4%. However, an upgrade would also require the group to achieve a stronger franchise and more sustainable risk-adjusted returns in line with higher-rated peers.

Downside scenario: We could revise the outlook to stable if, contrary to our expectations, we observe a delay in the group's profitability improvement and asset quality metrics deteriorate, postponing NPE stabilization.

Ratings score snapshot

Group SACP: bb+

Anchor: bbb

- Business Position: Constrained (-2)
- Capital and Earnings: Strong (+1)
- Risk Position: Moderate (-1)
- Funding and Liquidity: Adequate and Adequate (0)
- Comparable Rating Analysis: 0

Support: +2

- ALAC Support: +2
- GRE Support: 0
- Group Support: 0
- Sovereign Support: 0

Additional Factors: 0

ESG Credit Indicators: E-2, S-2, G-2

Related Criteria

- General Criteria: Hybrid Capital: Methodology And Assumptions, March 2, 2022
- Criteria | Financial Institutions | General: Financial Institutions Rating Methodology, Dec. 9, 2021
- Criteria | Financial Institutions | Banks: Banking Industry Country Risk Assessment Methodology And Assumptions, Dec. 9, 2021
- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021

- General Criteria: Group Rating Methodology, July 1, 2019
- 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
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Related Research

- Banking Industry Country Risk Assessment Update: December 2022, Dec. 20, 2022
- Lifting Of Government-Imposed Pay Restrictions Is Beneficial For Irish Banks' Talent Acquisition And Retention, Nov. 30, 2022
- Ireland Outlook Revised To Positive On Fiscal And Macroeconomic Resilience; 'AA-/A-1+' Ratings Affirmed, Nov. 18, 2022
- Outlooks On Two Largest Irish Banks Revised To Stable On Easing Profitability Pressure; Ratings Affirmed, May 16, 2022

Ratings List

*** * * * * * * * * * * * * * * AIB Group PLC * * * * * * * * * * * * * * ***		
Ratings Affirmed		
Allied Irish Banks PLC		
Resolution Counterparty Rating	A/--/A-1	
Ratings Affirmed; Outlook Action		
	To	**From**
AIB Group PLC		
Issuer Credit Rating	BBB-/Positive/A-3	BBB-/Stable/A-3
Allied Irish Banks PLC		
Issuer Credit Rating	A-/Positive/A-2	A-/Stable/A-2
*** * * * * * * * * * * * Bank of Ireland Group PLC * * * * * * * * * * * ***		
Ratings Affirmed		
Bank of Ireland		
Resolution Counterparty Rating	A/--/A-1	
Ratings Affirmed; Outlook Action		
	To	**From**
Bank of Ireland Group PLC		
Issuer Credit Rating	BBB-/Positive/A-3	BBB-/Stable/A-3
Bank of Ireland		
Issuer Credit Rating	A-/Positive/A-2	A-/Stable/A-2

* * * * * * * * * * * Permanent TSB Group Holdings PLC * * * * * * * * * *		
Ratings Affirmed		
Permanent TSB Group Holdings PLC		
Issuer Credit Rating	BB-/Positive/B	
Upgraded		
	To	**From**
Permanent TSB PLC		
Issuer Credit Rating	BBB/Positive/A-2	BBB-/Positive/A-3
Permanent TSB PLC		
Resolution Counterparty Rating	BBB+/--/A-2	BBB/--/A-2