

Update: Bank of Ireland Group PLC

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Update: Bank of Ireland Group PLC

| | | | | | | | | |
|-----------------------------|------------|-----------|---|--------------------------|-----------|---|---------------------------------------|--------------------------|
| Group SACP | bbb | | + | Support | +2 | + | Additional Factors | 0 |
| Anchor | bbb | | | ALAC Support | +2 | | Issuer Credit Rating | A-/Negative/A-2 |
| Business Position | Adequate | 0 | | GRE Support | 0 | | Resolution Counterparty Rating | A/--/A-1 |
| Capital and Earnings | Strong | +1 | | Group Support | 0 | | Holding Company ICR | BBB-/Negative/A-3 |
| Risk Position | Moderate | -1 | | Sovereign Support | 0 | | | |
| Funding | Average | 0 | | | | | | |
| Liquidity | Adequate | | | | | | | |

Group SACP--The group stand-alone credit profile of the Bank of Ireland group. The bank holding company rating shown applies to Bank of Ireland Group PLC, and is one notch below the group SACP. The issuer credit rating shown applies to the operating company, Bank of Ireland.

Credit Highlights

Issuer Credit Rating

BBB-/Negative/A-3

Overview

| Key strengths | Key risks |
|---|---|
| Strong franchise in Ireland, with a high market share across business lines and better diversity than Irish peers. | Continued strain on earnings due to low interest rates, ongoing transformation costs, and a challenging operating environment in Ireland. |
| Stable deposit base characterized by very low concentration risks and a low proportion of more volatile corporate deposits. | Significant level of problem loans that could further increase as pandemic-related risks persist and government support unwinds. |
| Significant buildup of additional loss-absorbing capacity (ALAC) with the continuous issuance of bail-in-able debt. | Geographic concentration in Ireland and the U.K. |

Profitability concerns continue to weigh on the bank's creditworthiness. Our negative outlook on BOI Group is driven by the structural challenges domestic banks are facing. These include the flat interest rate yield curve, negative rates that are not fully passed on to depositors, and modest growth opportunities. All this weighs on net interest income, which comprises more than three-quarters of the group's operating revenues. Strengthening revenues is the group's key challenge while it works through its transformation plan, with continuous investments in business and digital capabilities. However, BOI Group has seen some positive results in the first half of 2021 supported by an improving economic outlook and business activities, as well as its continuous commitment to cost reduction.

BOI Group has reported a 72% year-on-year increase in pre-provision income and about a 7% uptick versus first-half 2019. It has also reduced its operating costs (net of transformation investment) by a further 4%, which has supported the improvement in its cost-to-income ratio to 61% for the first half of 2021 from 64% in 2020.

The group's domestic franchise and cross-selling activities will likely further benefit from the two acquisitions announced earlier this year (if these transactions are finalized and well executed):

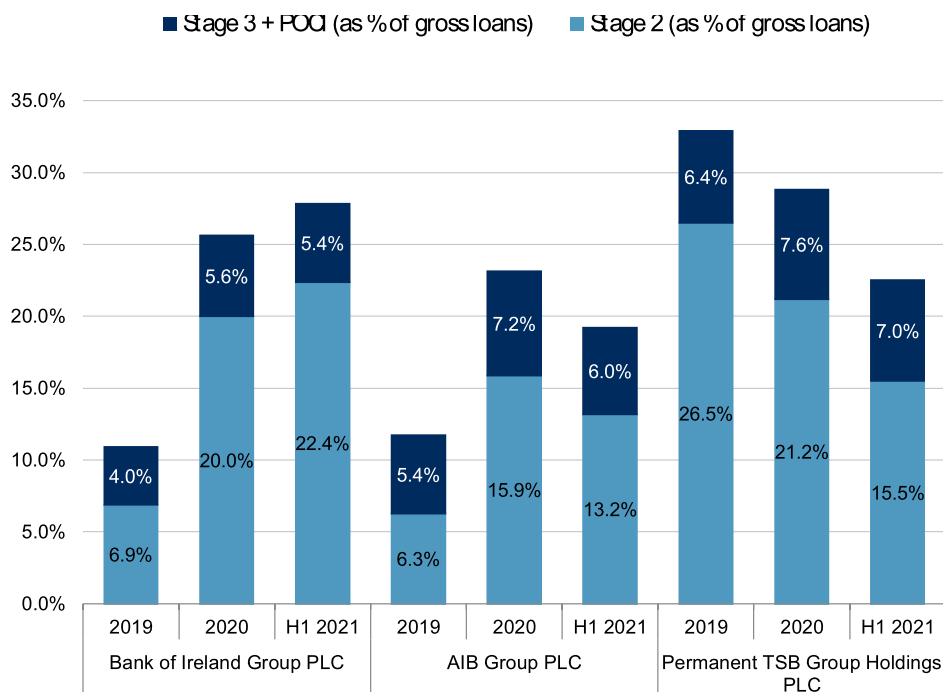
- A performing loan portfolio from KBC Group of about €9 billion (see "Bank of Ireland Group's Potential Acquisition Of KBC Ireland Assets Could Support Its Revenue And Domestic Position," published April 16, 2021); and
- J&E Davy, Ireland's leading provider of wealth management (with over €16 billion of assets under management) and capital markets services.

However, we believe that BOI Group's ability to deliver on updated targets (expected to be communicated in 2022), combined with continuous cost cutting, top-line growth, and good asset quality performance will be critical for its rating stability.

So far, asset quality has remained steady, but we expect some rise in NPLs as government support measures unwind.

After increasing to 5.7% at year-end 2020, from 4.4% at year-end 2019, BOI Group's nonperforming exposure (NPE) ratio trend reversed in the first six months 2021, decreasing modestly to 5.5% at end-June 2021. The decrease in NPE was mainly led by the securitization of €0.3 billion Irish mortgages. Similarly, the group's stage 3 and purchased or originated credit-impaired (POCI) loans as a proportion of gross customer loans reduced slightly to 5.4% at end-June 2021 from 5.6% at year-end 2020. The coverage of stage 3 loans remained stable at 30% as of end-June 2021.

Our broader analysis of asset quality also captures stage 2 loans. For BOI, total stage 2 loans have been increasing since the onset of the pandemic and stood at 22.5% of gross loans as of end-June 2021, up from 20.0% as of year-end 2020 and 6.9% as of year-end 2019. This trend is contradictory to other domestic players and is mainly led by BOI Group's larger post-model-management reclassification adjustment, which is applied to residential mortgages and SME portfolios. That said, the impact on P&L was minimal as the charge was already allocated in 2020: impairment charges were only €1 million as of end-June 2021. BOI Group anticipates a similar level of impairment charges over the second half of the year while keeping its management overlay of €229 million given that pandemic-related risks persist. Therefore, we continue to expect some increase in NPLs as borrowers' cash flows remain under pressure and governments begin to taper support measures, but we think that last year's provisioning provides a sufficient buffer for potential losses.

Chart 1**NPL Composition For Bank Of Ireland Group Versus Other Irish Banks (June 30, 2021)**

H1--First half. Source: Company accounts.

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Robust capitalization supports announced acquisitions. BOI Group's fully loaded common equity tier 1 (CET1) ratio improved to 14.1% at end-June 2021 from 13.4% at year-end 2020, and we expect the ratio to increase by another 30-50 basis points (bps) by end-2021 due to organic capital generation in second-half 2021. As such, we expect the group will have sufficient capital to support two upcoming acquisitions. We forecast our RAC ratio to approach the 10% threshold at the closing of the expected transactions, but to build a sufficient buffer above 10% over the outlook horizon.

We estimate that both deals will reduce the group's CET1 capital ratio by about 170-180 bps, but that it will remain above a targeted fully loaded CET1 ratio of about 13% (with still sufficient headroom above the minimum CET1 requirement of 9.77% for 2021). We believe the group is unlikely to pay dividends for 2021 results taking into account upcoming acquisitions, but we expect it will resume dividend payments after 2022.

We expect BOI Group's funding and liquidity will remain in line with domestic peers and be neutral to the ratings. BOI Group's funding profile benefits from its strong domestic franchise, especially its granular retail deposits, and it has limited reliance on short-term wholesale funding. The group's customer deposit volumes have increased 4.7% year-on-year as of end-June 2021. Though we expect customer deposit growth to gradually slow down once household consumption and corporate investment normalize and announced loan portfolio acquisition is executed, we still expect the funding and liquidity ratios to remain robust over the next two years.

As of June 2021, BOI Group's stable funding ratio (as per S&P Global Ratings' calculation) stood at 136% and its loan to deposit ratio was 85% (117% and 89% a year ago, respectively). Our measure of broad liquid assets to short-term wholesale funding was a high 19x on June 30, 2021. This partly reflects low wholesale funding despite a continuous build-up of its loss-absorption cushion.

Outlook

Bank of Ireland Group PLC

The negative outlook reflects our view that structural profitability issues--such as modest growth opportunities, persistently high costs, high capital requirements, and low revenue diversification--will continue weighing on the bank's earnings generation capacity over the next 18-24 months, despite our expectation of an economic rebound.

Downside scenario

We could lower the ratings if, despite committed cost discipline and investment in digitalization, the group's returns remain weak over the next two years, with profitability metrics that are not in line with international peers'.

Upside scenario

We could revise the outlook to stable if economic and operating conditions stabilize, while cost discipline allows the bank to sustain its preprovision income.

Bank of Ireland

The negative outlook on Bank of Ireland (BOI), the main operating bank, mirrors that on the BOI Group.

Downside scenario

We could lower the ratings on BOI if we lower the group's stand-alone assessment most likely because the group fails to improve its returns. We could also lower the ratings on BOI if the buffer of bail-in-able debt protecting senior creditors does not stay at or above 8.0% of our RWA metric and is no longer commensurate with a two-notch rating uplift. This could happen because of a less conservative capital policy than we currently expect or due to inflation of the risk-asset base.

Upside scenario

We could revise the outlook to stable if we see a stabilization in the operating environment and we also revise our outlook on BOI Group to stable.

Key Statistics

Table 1

| Bank of Ireland Group PLC--Key Figures | | | | | |
|---|------------------|------------------|------------------|------------------|------------------|
| --Fiscal year ended Dec. 31-- | | | | | |
| (Mil. €) | June 2021 | Dec. 2020 | Dec. 2019 | Dec. 2018 | Dec. 2017 |
| Adjusted assets | 130,455.0 | 114,259.0 | 113,484.0 | 108,732.0 | 107,354.0 |
| Customer loans (gross) | 79,347.0 | 78,823.0 | 80,795.0 | 78,061.0 | 78,487.0 |
| Adjusted common equity | 6,569.0 | 5,918.0 | 6,808.0 | 6,326.0 | 5,749.0 |
| Operating revenues | 1,419.0 | 2,641.0 | 2,949.0 | 2,833.0 | 3,007.0 |
| Noninterest expenses | 944.0 | 1,884.0 | 2,006.0 | 1,945.0 | 2,084.0 |
| Core earnings | 398.0 | N/A | 506.0 | 752.0 | 734.0 |

N/A--Not applicable.

Table 2

| Bank of Ireland Group PLC--Business Position | | | | | |
|--|------------------|------------------|------------------|------------------|------------------|
| --Fiscal year ended Dec. 31-- | | | | | |
| (Mil. €) | June 2021 | Dec. 2020 | Dec. 2019 | Dec. 2018 | Dec. 2017 |
| Loan market share in country of domicile | N/A | 25.5 | N/A | N/A | N/A |
| Total revenues from business line (currency in millions) | 1,420.0 | 2,654.0 | 2,949.0 | 2,849.0 | 3,011.0 |
| Commercial banking/total revenues from business line | 30.1 | 28.7 | 24.8 | 26.6 | 26.8 |
| Insurance activities/total revenues from business line | 8.7 | 6.4 | 10.3 | 6.8 | 7.3 |
| Other revenues/total revenues from business line | 0.5 | 1.0 | 2.3 | 0.4 | 0.5 |
| Return on average common equity | 7.6 | (8.2) | 4.1 | 6.8 | 7.5 |

N/A--Not applicable.

Table 3

| Bank of Ireland Group PLC--Capital And Earnings | | | | | |
|--|------------------|------------------|------------------|------------------|------------------|
| --Fiscal year ended Dec. 31-- | | | | | |
| (Mil. €) | June 2021 | Dec. 2020 | Dec. 2019 | Dec. 2018 | Dec. 2017 |
| Tier 1 capital ratio | 17.3 | 16.9 | 16.3 | 16.0 | 17.0 |
| S&P Global Ratings' RAC ratio before diversification | N/A | 10.4 | 11.2 | 11.2 | 10.2 |
| S&P Global Ratings' RAC ratio after diversification | N/A | 10.4 | 11.4 | 11.4 | 10.1 |
| Adjusted common equity/total adjusted capital | 87.1 | 85.9 | 91.7 | 92.6 | 92.2 |
| Double leverage | N.M. | 91.8 | 90.9 | 88.9 | 87.6 |
| Net interest income/operating revenues | 76.1 | 79.1 | 73.1 | 75.3 | 71.6 |
| Fee income/operating revenues | 8.9 | 9.7 | 10.3 | 10.5 | 10.8 |
| Market-sensitive income/operating revenues | 4.4 | 1.2 | 4.8 | 2.0 | 7.8 |
| Cost to income ratio | 66.5 | 71.3 | 68.0 | 68.7 | 69.3 |
| Preprovision operating income/average assets | 0.7 | 0.6 | 0.7 | 0.7 | 0.8 |
| Core earnings/average managed assets | 0.6 | N/A | 0.4 | 0.6 | 0.6 |

RAC--Risk-adjusted capital. N/A--Not applicable. N.M.--Not meaningful.

Table 4

| Bank of Ireland Group PLC--Risk-Adjusted Capital Framework Data | | | | | |
|---|-----------|----------------|-------------------------|-------------------------|------------------------------------|
| (Mil. €) | Exposure* | Basel III RWA | Average Basel III RW(%) | S&P Global Ratings' RWA | Average S&P Global Ratings' RW (%) |
| Credit risk | | | | | |
| Government and central banks | 24,923.0 | 298.0 | 1.0 | 839.0 | 3.0 |
| Of which regional governments and local authorities | 386.0 | 16.0 | 4.0 | 21.0 | 6.0 |
| Institutions and CCPs | 6,872.0 | 815.0 | 12.0 | 1,728.0 | 25.0 |
| Corporate | 24,344.0 | 19,772.0 | 81.0 | 20,507.0 | 84.0 |
| Retail | 55,170.0 | 16,855.0 | 31.0 | 29,189.0 | 53.0 |
| Of which mortgage | 46,206.0 | 10,816.0 | 23.0 | 21,000.0 | 45.0 |
| Securitization§ | 2,976.0 | 847.0 | 28.0 | 1,442.0 | 48.0 |
| Other assets† | 2,788.0 | 2,223.0 | 80.0 | 4,424.0 | 159.0 |
| Total credit risk | 117,073.0 | 40,810.0 | 35.0 | 58,129.0 | 50.0 |
| Credit valuation adjustment | | | | | |
| Total credit valuation adjustment | -- | 763.0 | -- | 0.0 | -- |
| Market risk | | | | | |
| Equity in the banking book | 188.0 | 1,989.0 | 1,058.0 | 1,830.0 | 973.0 |
| Trading book market risk | -- | 567.0 | -- | 851.0 | -- |
| Total market risk | -- | 2,556.0 | -- | 2,681.0 | -- |
| Operational risk | | | | | |
| Total operational risk | -- | 4,234.0 | -- | 5,568.0 | -- |
| | Exposure | Basel III RWA | Average Basel II RW (%) | S&P Global Ratings' RWA | % of S&P Global Ratings' RWA |
| Diversification adjustments | | | | | |
| RWA before diversification | -- | 48,363.0 | -- | 66,377.0 | 100.0 |
| Total diversification/ concentration adjustments | -- | -- | -- | (61.0) | 0.0 |
| RWA after diversification | -- | 48,363.0 | -- | 66,316.0 | 100.0 |
| | | Tier 1 capital | Tier 1 ratio (%) | Total adjusted capital | S&P Global Ratings' RAC ratio (%) |
| Capital ratio | | | | | |
| Capital ratio before adjustments | | 8,191.0 | 16.9 | 6,893.0 | 10.4 |
| Capital ratio after adjustments‡ | | 8,191.0 | 16.9 | 6,893.0 | 10.4 |

*Exposure at default. §Securitization exposure includes the securitization tranches deducted from capital in the regulatory framework. †Exposure and S&P Global Ratings' risk-weighted assets for equity in the banking book include minority equity holdings in financial institutions.

‡Adjustments to tier 1 ratio are additional regulatory requirements (e.g. transitional floor or pillar 2 add-ons). CCP--Calling party pays.

RWA--Risk-weighted assets. RW--Risk weight. RAC--Risk-adjusted capital. Sources: Company data as of Dec. 31, 2020, S&P Global Ratings.

Table 5

| Bank of Ireland Group PLC--Risk Position | | | | | |
|--|-----------|-----------|-----------|-----------|-----------|
| --Fiscal year ended Dec. 31-- | | | | | |
| (Mil. €) | June 2021 | Dec. 2020 | Dec. 2019 | Dec. 2018 | Dec. 2017 |
| Growth in customer loans | 1.3 | (2.4) | 3.5 | (0.5) | (4.7) |

Table 5

| Bank of Ireland Group PLC--Risk Position (cont.) | | | | | |
|---|--------------------------------------|------------------|------------------|------------------|------------------|
| (Mil. €) | --Fiscal year ended Dec. 31-- | | | | |
| | June 2021 | Dec. 2020 | Dec. 2019 | Dec. 2018 | Dec. 2017 |
| Total diversification adjustment/S&P Global Ratings' RWA before diversification | N/A | (0.1) | (1.7) | (1.1) | 0.7 |
| Total managed assets/adjusted common equity (x) | 22.8 | 22.6 | 19.4 | 19.5 | 21.3 |
| New loan loss provisions/average customer loans | 0.0 | 1.4 | 0.3 | (0.1) | 0.0 |
| Net charge-offs/average customer loans | 0.4 | 0.2 | 0.8 | 0.9 | 2.0 |
| Gross nonperforming assets/customer loans + other real estate owned | 9.9 | 8.8 | 7.2 | 9.5 | 10.9 |
| Loan loss reserves/gross nonperforming assets | 27.1 | 32.4 | 22.4 | 23.0 | 27.6 |

N/A--Not applicable. RWA--Risk-weighted asset.

Table 6

| Bank of Ireland Group PLC--Funding And Liquidity | | | | | |
|---|--------------------------------------|------------------|------------------|------------------|------------------|
| (Mil. €) | --Fiscal year ended Dec. 31-- | | | | |
| | June 2021 | Dec. 2020 | Dec. 2019 | Dec. 2018 | Dec. 2017 |
| Core deposits/funding base | 79.8 | 89.1 | 86.3 | 85.3 | 83.5 |
| Customer loans (net)/customer deposits | 85.2 | 86.5 | 94.7 | 96.9 | 100.5 |
| Long-term funding ratio | 98.3 | 97.9 | 96.5 | 97.9 | 93.3 |
| Stable funding ratio | 136.7 | 122.5 | 114.8 | 112.8 | 109.4 |
| Short-term wholesale funding/funding base | 1.9 | 2.3 | 3.8 | 2.3 | 7.3 |
| Broad liquid assets/short-term wholesale funding (x) | 19.5 | 11.6 | 6.1 | 9.3 | 3.2 |
| Net broad liquid assets/short-term customer deposits | 43.8 | 27.7 | 23.1 | 23.4 | 19.7 |
| Short-term wholesale funding/total wholesale funding | 8.9 | 19.3 | 26.7 | 15.2 | 43.0 |
| Narrow liquid assets/3-month wholesale funding (x) | 73.7 | 19.9 | 13.7 | 12.2 | 13.8 |

Related Criteria

- General Criteria: Hybrid Capital: Methodology And Assumptions, July 1, 2019
- General Criteria: Group Rating Methodology, July 1, 2019
- 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
- General Criteria: Guarantee Criteria, Oct. 21, 2016
- Criteria | Financial Institutions | Banks: Bank Rating Methodology And Assumptions: Additional Loss-Absorbing Capacity, April 27, 2015
- 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: Principles Of Credit Ratings, Feb. 16, 2011
- Criteria | Financial Institutions | Banks: Commercial Paper I: Banks, March 23, 2004

Related Research

- Banking Industry Country Risk Assessment Update: August 2021, August 24, 2021
- Bank of Ireland Group's Interim Results Provide A Buffer For Planned Deals, August 04, 2021
- EMEA Financial Institutions Monitor 3Q2021: Resilience Amid The Search For Stronger Profitability, July 16, 2021
- Ratings On Irish Banks Affirmed Amid Ongoing Profitability Pressure; Most Outlooks Still Negative, June 24, 2021
- Bank of Ireland Group's Potential Acquisition Of KBC Ireland Assets Could Support Its Revenue And Domestic Position, April 16, 2021
- Full Analysis: Bank of Ireland Group PLC, January 11, 2021

Ratings Detail (As Of September 30, 2021)*

Bank of Ireland Group PLC

| | |
|----------------------|-------------------|
| Issuer Credit Rating | BBB-/Negative/A-3 |
| Junior Subordinated | B |
| Senior Unsecured | A-3 |
| Senior Unsecured | BBB- |
| Subordinated | BB |

Issuer Credit Ratings History

| | |
|-------------|-------------------|
| 28-Apr-2020 | BBB-/Negative/A-3 |
| 24-Dec-2019 | BBB-/Stable/A-3 |
| 12-Dec-2017 | BBB-/Positive/A-3 |
| 14-Jul-2017 | BBB-/Stable/A-3 |

Sovereign Rating

| | |
|---------|-----------------|
| Ireland | AA-/Stable/A-1+ |
|---------|-----------------|

Related Entities

Bank of Ireland

| | |
|--------------------------------|-----------------|
| Issuer Credit Rating | A-/Negative/A-2 |
| Resolution Counterparty Rating | A/--/A-1 |
| Commercial Paper | |
| <i>Local Currency</i> | A-2 |
| Junior Subordinated | BB- |
| Preference Stock | BB- |
| Senior Unsecured | A- |
| Senior Unsecured | A-2 |
| Subordinated | BB+ |

*Unless otherwise noted, all ratings in this report are global scale ratings. S&P Global Ratings' credit ratings on the global scale are comparable

Ratings Detail (As Of September 30, 2021)*(cont.)

across countries. S&P Global Ratings' credit ratings on a national scale are relative to obligors or obligations within that specific country. Issue and debt ratings could include debt guaranteed by another entity, and rated debt that an entity guarantees.

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