

RatingsDirect®

Danske Bank A/S

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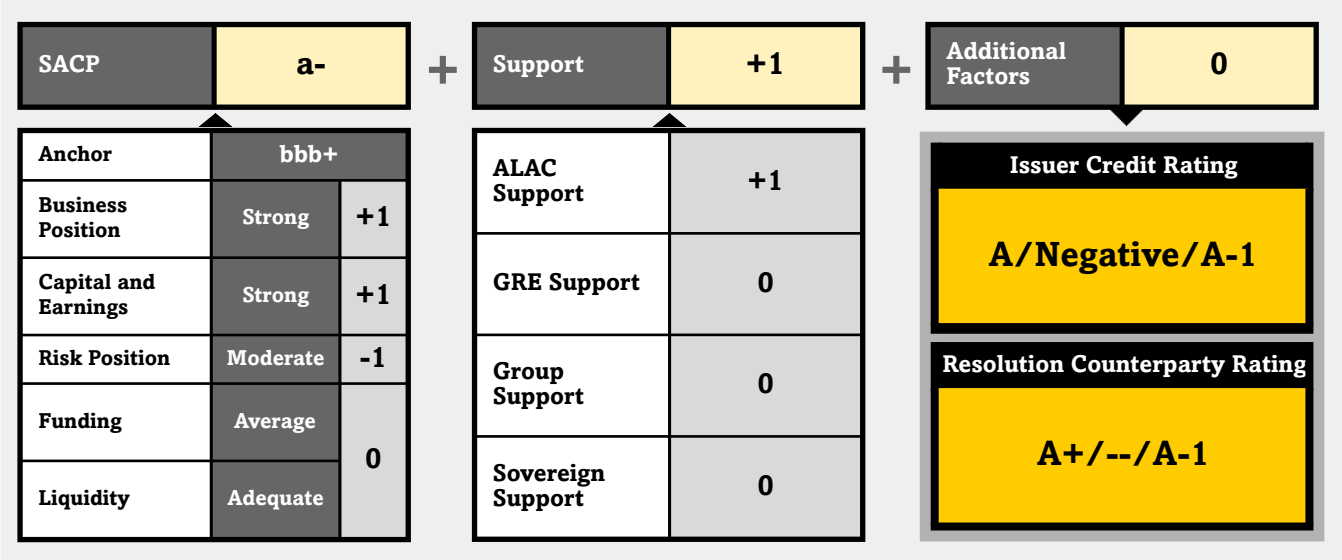
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Related Criteria

Related Research

Danske Bank A/S



Major Rating Factors

Strengths:	Weaknesses:
<ul style="list-style-type: none"> Denmark's leading commercial bank, life insurer, and commercial pension provider. Diversified revenues by Pan-Nordic lines of business. Strong capitalization and earnings. 	<ul style="list-style-type: none"> Uncertainties related to Estonian anti-money laundering case, in particular with regard to potential legal fine and additional reputational damages. Dependence on wholesale funding and external debt, which causes higher confidence sensitivity.

Outlook: Negative

S&P Global Ratings' negative outlook on Denmark-based Danske Bank A/S reflects the uncertain outcome of the ongoing regulatory investigations into its Estonian branch, and the possible damage to its reputation.

We could lower our issuer credit ratings within the next 18-24 months if Danske Bank's franchise suffers lasting damage, or if we believe potential regulatory penalties would materially weaken the bank's capital and earnings. At present, we expect our risk-adjusted capital (RAC) ratio for Danske Bank will remain within the 10%-11% range, but we see possible risks to this outcome. We could also lower the ratings if further control and governance weaknesses are identified, or if Danske Bank fails to address the organizational and management deficiencies revealed by the regulatory Estonian branch investigation.

We could consider revising the outlook to stable if we have greater clarity over the likely outcome of the regulatory investigations, if potential regulatory penalties are manageable, if Danske Bank's business position shows resilience, and if we see an improving economic environment in Denmark.

Our negative outlook on Danica Pension Livsforsikringsaktieselskab (A-/Negative--) reflects that on Danske Bank, because we consider it to be a core subsidiary of the bank that would receive support under all foreseeable circumstances if needed.

Rationale

The 'A' long-term rating on Danske Bank reflects our assessment that it will maintain its leading franchise as the second-largest bank in the Nordic banking markets.

It also reflects our view that the bank will maintain its dominant domestic role and its particular strength in capital and earnings. The rating also reflects our assessment that Danske Bank's risk position has weakened. In particular, this takes into account restructuring needs and time to regain market confidence following a series of detected material organizational and management failures in client onboarding and the prevention of money laundering and corrupt practices at its operations in Estonia in 2007-2015. Our major concern remains that a number of regulators may look into this case and that the amount of any penalties and regulatory actions remain uncertain; therefore uncertainty with regards to prospective capitalization remains high.

We expect that Danske Bank's funding and liquidity will remain neutral to its ratings, given our view that the bank will continue to have untarnished access to broad capital markets and liquidity despite reputational issues.

We estimate that Danske Bank's additional loss-absorbing capacity (ALAC) buffer will be just below 5% of risk-weighted assets in 2018 and eventually exceed 5% in the following two years. As such, we add one notch of ALAC support in the long-term rating.

Although we view Danica as a core group entity, which would be supported by Danske Bank under all foreseeable circumstances if needed, our 'A-' ratings on Danica are at the same level as Danske Bank's unsupported credit profile, because we don't believe that it would benefit from the bank's ALAC.

Anchor: 'bbb+' because the main operations are in Denmark

We use our Banking Industry Country Risk Assessment's economic risk and industry risk scores to determine a bank's anchor, the starting point in assigning an issuer credit rating. Our anchor for a commercial bank operating only in Denmark is 'bbb+', based on an economic risk score of '3' and an industry risk score of '3'. For Danske Bank, we also consider its diversified exposures in Sweden, Norway, Finland, the U.K., and other European countries; that said, its blended economic risk score is still '3' because the majority of exposures are in Denmark.

Our assessment of economic risk for Denmark reflects our view that Danish banks benefit from operating in a high-income, open economy with mature political and institutional settings that promote fiscal discipline and growth-stimulating policies. The economy is competitive, diverse, and continues to expand. We note that despite GDP growth household debt's share of GDP remains one of the highest of all global BICRAs per our metrics--and a constraint to our assessment of economic risk. However, credit conditions have been improving in recent years, and we expect credit losses for the system to remain low in 2019. While we observed a decline in the coverage of nonperforming loans, it remains higher than pre-crisis levels, and in line with 2009 levels in nominal terms. We view the trend for economic risk in Denmark as positive. It reflects our expectations that Denmark will sustain its current economic growth and competitiveness, and also our expectations that household debt will remain stable or slightly shrink relative to GDP to about 114%-111% through 2019-2020 from 115% in 2017 and expected 115% for 2018.

Our assessment of Denmark's industry risk is supported by the improvement in the banking sector's profitability over the past 10 years. More specifically, it benefits from cost-efficiency measures, decreasing credit losses, and higher mortgage margins, rather than a generally higher risk appetite. We note the banking sector is more reliant on functioning wholesale markets than peers. However, we also acknowledge the continued stability and strong track record of the Danish covered bond market. We consider the regulatory environment in Denmark to be in line with that of other EU countries.

We note that the 2017 Financial Action Task Force (FATF) report was critical toward Denmark's AML framework. We view positively the various measures Denmark has taken in 2017-2018 to address shortcomings. In particular it adopted the Anti-Money Laundering Act in June 2017, and the exchange of information between authorities has strengthened. Danish parliament agreed to significantly increase the range of penalties for money laundering. In addition, the authorities have significantly increased resources allocated to the enforcement of the rules. We continue to incorporate these concerns in our analysis of our issuer credit rating on Danske Bank.

Table 1

Danske Bank A/S Key Figures					
--Fiscal year ending Dec. 31--					
(Mil. DKK)	2018	2017	2016	2015	2014
Adjusted assets	3,095,886	3,123,419	3,091,634	2,928,908	3,093,164
Customer loans (gross)	1,803,311	1,748,500	1,734,172	1,664,640	1,634,286
Adjusted common equity	129,756	122,765	120,337	134,997	130,498
Operating revenues	46,956	49,483	49,336	47,086	46,294
Noninterest expenses	27,204	25,321	24,190	23,982	24,847
Core earnings	15,505	20,581	19,922	18,527	13,740

DKK--Danish krone.

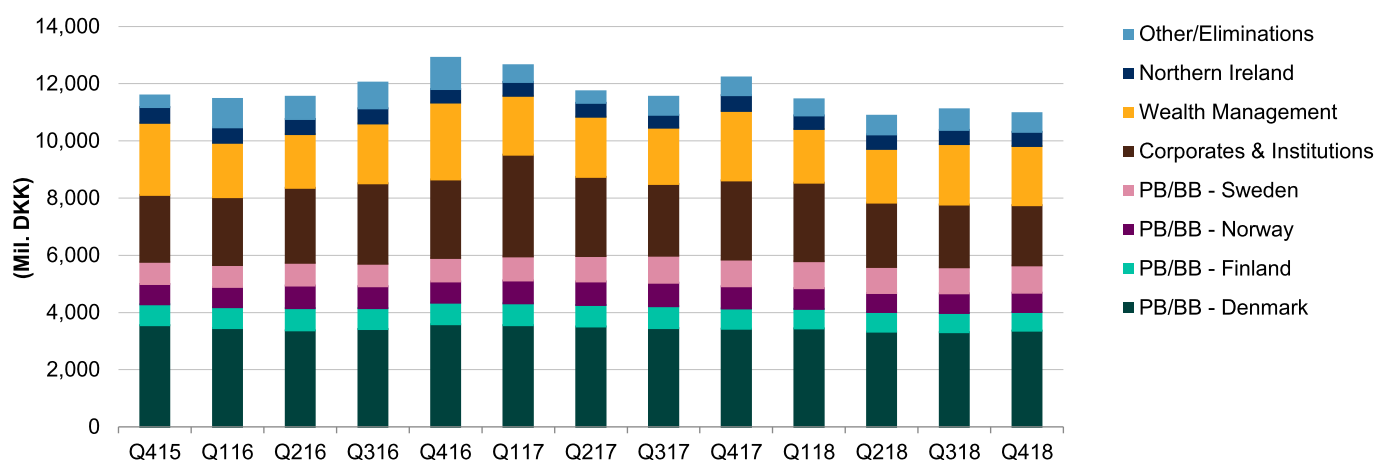
Business position: A leading Danish commercial bank with a good market position in other Nordic countries, so far not significantly affected by AML case

We expect that Danske Bank will maintain its diverse earnings capacity based on its leading franchise as the second-largest bank in the Nordic banking markets. We anticipate that, despite the Estonian case garnering huge attention, overall reputational damages to the bank will remain manageable, given that we have not observed significant customer outflow in 2018. We also view as supportive of the rating Danske's proactive approach in retail and commercial customers outreach. We expect the group will remain highly diversified from operations primarily in Denmark, Finland, Sweden, and Norway, with aggregate adjusted assets of Danish krone (DKK) 3,095 billion (about \$460 billion) as of Dec. 31, 2018.

Danske Bank is the second-largest bank in the Nordics and in addition to having a 25%-30% market share in Denmark, it is one of two banks with material personal, corporate, and capital markets businesses in each of the Nordic markets.

Chart 1

Danske Bank A/S Revenues By Business Division



DKK--Danish krone.

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We continue to expect that Danske will focus on gradually improving efficiency by increasing revenues on its existing cost base and with expansion in Sweden and Norway planned through 2020 as part of its Nordic integrator strategy.

Table 2

Danske Bank A/S Business Position					
	--Fiscal year ending Dec. 31--				
(%)	2018	2017	2016	2015	2014
Loan market share in country of domicile	26.6	26.6	26.6	26.1	26.5
Deposit market share in country of domicile	27.8	27.9	28.7	27.8	27.1
Total revenues from business line (mil. DKK)	46,956	50,583	49,836	47,086	46,294
Return on average common equity	9.2	13.1	13.2	8.8	2.6

N/A Not Applicable. DKK--Danish krone.

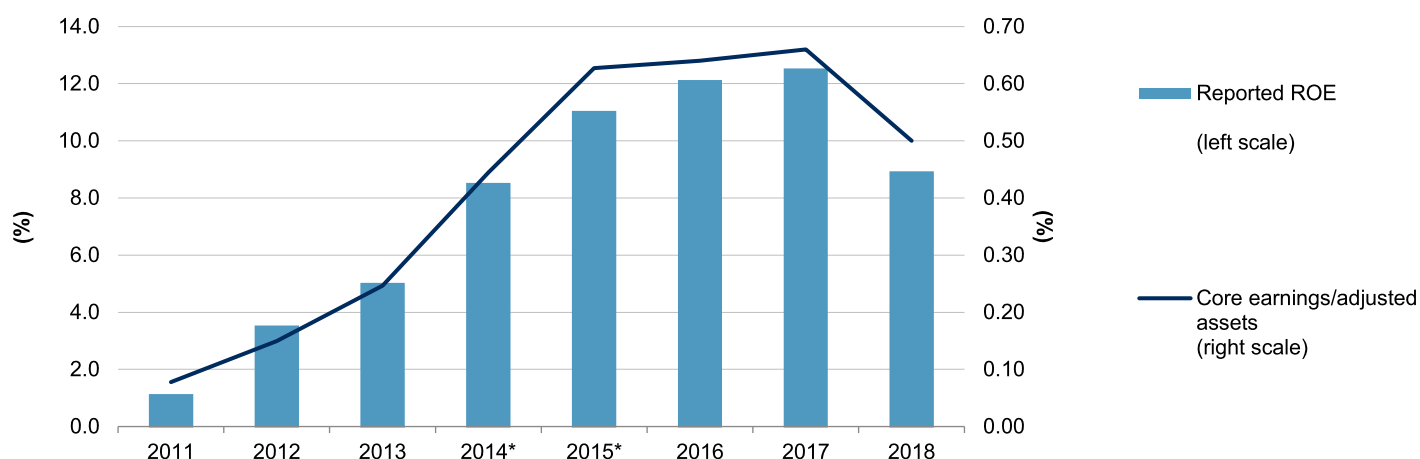
Capital and earnings: Strong capital levels, supported by discontinuance of buy-backs, but legal fines remain uncertain

We expect that Danske Bank's capital and earnings will remain a key rating strength, with its risk-adjusted capital (RAC) ratio at 10.7% at June 2018. We forecast that Danske Bank's strong earnings performance will continue to support a RAC ratio of 10%-11% in the next two years. In our base case, we expect Danske Bank's capital levels will not be materially damaged by any large one-offs, namely legal fines. We view as positive for the rating Danske Bank's decision to discontinue its share back-buy program in 2018 to preserve superior capital standards, and to fulfil the Danish FSA's additional DKK10 billion pillar II add-on requirement. In addition, we acknowledge Danske's potential additional capital flexibility, given its ability to reduce its currently high dividend accruals in the event of unexpected stress.

We note that 2018 earnings were somewhat weaker than in 2017 due to mostly sluggish trading results, and that reported return on equity (ROE) after tax was still a relatively high 8.9% for 2018 (12.5% for full-year 2017). The bank's 2018 performance was supported by another year of reserve releases, with credit costs at minus 0.02% for the full 2018. We expect ROE will fluctuate around 10% in coming years.

Chart 2

Danske Bank A/S Return On Equity After Tax



*Excluding goodwill impairment.

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Table 3

Danske Bank A/S Capital And Earnings

(%)	--Fiscal year ending Dec. 31--				
	2018	2017	2016	2015	2014
Tier 1 capital ratio	20.1	20.1	19.1	18.5	16.7
S&P Global Ratings' RAC ratio before diversification	N/A	11.5	10.5	10.1	9.0
S&P Global Ratings' RAC ratio after diversification	N/A	12.2	11.0	11.6	10.4
Adjusted common equity/total adjusted capital	84.6	86.9	89.4	92.3	95.8

Table 3

Danske Bank A/S Capital And Earnings (cont.)					
	--Fiscal year ending Dec. 31--				
(%)	2018	2017	2016	2015	2014
Double leverage	60.3	57.1	66.3	69.6	70.0
Net interest income/operating revenues	61.8	60.4	65.5	70.8	74.8
Fee income/operating revenues	22.1	21.9	20.6	22.7	21.2
Market-sensitive income/operating revenues	(21.8)	39.1	26.1	14.7	21.0
Noninterest expenses/operating revenues	57.9	51.2	49.0	50.9	53.7
Provision operating income/average assets	0.6	0.7	0.7	0.7	0.6
Core earnings/average managed assets	0.4	0.6	0.6	0.5	0.4

Note: Reported under International Financial Reporting Standards. N/A--Not applicable. N.M.--Not meaningful. RAC--Risk-adjusted capital.

Table 4

Danske Bank A/S Risk-Adjusted Capital Framework Data					
(DKK 000s)	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	605,364,607	7,423,707	1	10,429,077	2
Institutions and CCPs	311,643,922	37,872,355	12	51,411,407	16
Corporate	989,847,535	352,430,163	36	635,600,501	64
Retail	992,574,351	169,780,251	17	313,643,977	32
Of which mortgage	883,653,970	138,671,901	16	239,607,539	27
Securitization§	2,981,343	549,219	18	1,723,780	58
Other assets†	31,554,252	43,620,695	138	72,158,834	229
Total credit risk	2,933,966,010	611,676,391	21	1,084,967,577	37
Credit valuation adjustment					
Total credit valuation adjustment	--	4,975,000	--	19,431,244	--
Market risk					
Equity in the banking book	1,493,239	1,650,927	111	13,485,955	903
Trading book market risk	--	33,881,903	--	57,394,761	--
Total market risk	--	35,532,831	--	70,880,716	--
Operational risk					
Total operational risk	--	76,526,553	--	97,998,090	--
(DKK 000s)		Basel III RWA		S&P Global Ratings' RWA	% of S&P Global Ratings' RWA
Diversification adjustments					
RWA before diversification		728,710,775		1,273,277,627	100
Total Diversification/Concentration Adjustments		--		(241,488,300)	(19)
RWA after diversification		728,710,775		1,031,789,327	81

Table 4

Danske Bank A/S Risk-Adjusted Capital Framework Data (cont.)				
(DKK 000s)				
	Tier 1 capital	Tier 1 ratio (%)	Total adjusted capital	S&P Global Ratings' RAC ratio (%)
Capital ratio				
Capital ratio before adjustments	151,149,983	20.7	136,130,000	10.7
Capital ratio after adjustments†	151,149,983	20.0	136,130,000	13.2

*Exposure at default. §Securitization exposure includes the securitization tranches deducted from capital in the regulatory framework. †Other assets includes deferred tax assets (DTAs) not deducted from ACE. ‡Adjustments to Tier 1 ratio are additional regulatory requirements (e.g. transitional floor or Pillar 2 add-ons). RWA--Risk-weighted assets. RW--Risk weight. RAC--Risk-adjusted capital. DKK--Danisk krone. Sources: Company data as of June 30, 2018, S&P Global Ratings.

Risk position: A relative weakness due to historical failures in risk management and uncertainty of future regulatory fines

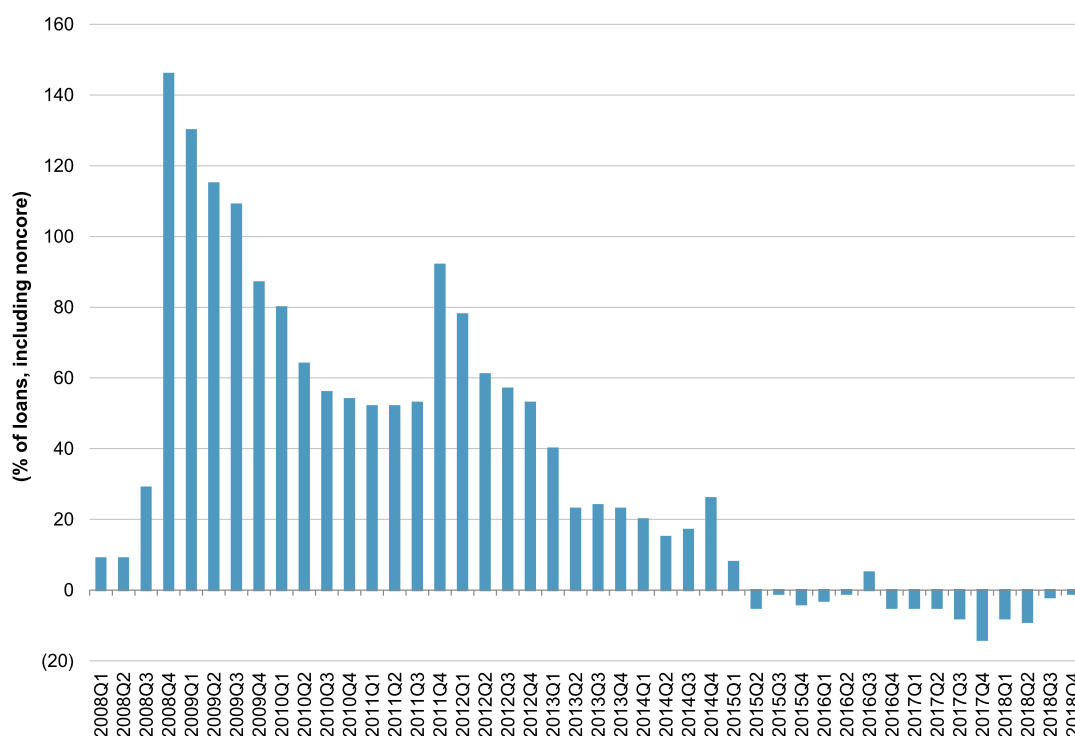
We expect Danske's risk position to remain a relative rating weakness. In particular, it takes into account restructuring needs and time to regain market confidence.

Our current view of the bank's risk position is based on historical failures in risk management and our view that it is too early to gauge the effectiveness of the bank's ongoing actions to address the identified shortcomings. It also includes our assessment of significant uncertainty with regards to RAC projections in view of potential regulatory fines. At the same time, we note that Danske Bank has significant capacity to absorb fines, due to excess capital (above 20% total capital ratio) and strong earnings capacity.

That said, we do not have particular concerns on the asset quality. Due to improvements in Nordic economies' asset quality, the bank's gross nonperforming assets are on declining trend, and we expect its asset quality will remain strong in 2019-2020. The bank continued to report net reversals in 2018. We expect that loan losses will remain low in most parts of the portfolio in the coming two years, given low interest rates and good credit conditions, but we expect some gradual build-up in reserves.

Chart 3

Danske Bank A/S Net Impairment Charges



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Table 5

Danske Bank A/S Risk Position					
	--Fiscal year ending Dec. 31--				
(%)	2018	2017	2016	2015	2014
Growth in customer loans	3.1	0.8	4.2	1.9	0.6
Total diversification adjustment/S&P Global Ratings' RWA before diversification	N/A	(6.1)	(4.7)	(13.0)	(13.9)
Total managed assets/adjusted common equity (x)	27.6	28.8	29.0	24.4	26.5
New loan loss provisions/average customer loans	0.0	(0.1)	0.0	0.0	0.2
Net charge-offs/average customer loans	0.0	0.0	0.0	0.0	0.1
Gross nonperforming assets/customer loans + other real estate owned	1.7	1.9	2.7	3.4	4.4
Loan loss reserves/gross nonperforming assets	70.8	62.4	56.9	55.9	56.9

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

Funding and liquidity: Leading deposit-taker in Denmark, with markets remaining open, but wider rates than previously

We expect that Danske Bank's funding and liquidity will remain a neutral to the ratings, since we believe that the bank will continue to have untarnished access to broad capital markets and liquidity despite reputational issues.

Danske Bank has a leading position as a deposit-taker in Denmark and a significant role in the well-functioning Danish

mortgage market. While Danske Bank has a higher share of covered bond financing than many of its international peers (21% of total liabilities), we see the stability of the Danish covered bond market and its unique features as supportive of a neutral funding assessment.

While rates for Danske Bank have widened, mostly reflecting investors' uncertainty with regards to Estonian case evolution, markets remain open for Danske as supported by significant oversubscription to its senior nonpreferred issuance in January 2019. We also note that the widening of spreads is not leading to material refinancing costs due to the term and instrument structure of Danske Bank's liabilities.

Danske Bank has a 28.4% domestic deposit market share, and granular core deposit franchises in each of its primary markets, with core deposits comprising close to 40% of liabilities.

The group's stable funding ratio was 93.5% at year-end 2018 and 103.6% in December 2017, and we expect it will stay at current levels with potential to gradually improve as the bank continues to refinance debt with long-term notes and covered bonds.

Danske Bank's liquidity is adequate, in our view, on the basis that it is in line with that of its Nordic peers, and we expect it will improve as a result of reducing short-term covered bond issuance in Denmark. The bank's broad liquid assets represented 1.29x its short-term wholesale funding in December 2018, which indicates a balanced profile, in our view.

Table 6

Danske Bank A/S Funding And Liquidity					
	--Fiscal year ending Dec. 31--				
(%)	2018	2017	2016	2015	2014
Core deposits/funding base	37.5	34.7	34.1	34.4	30.9
Customer loans (net)/customer deposits	198.7	189.1	198.2	199.1	207.5
Long-term funding ratio	75.3	69.9	70.5	70.9	64.2
Stable funding ratio	93.5	103.6	100.5	99.3	93.6
Short-term wholesale funding/funding base	26.3	32.0	31.3	31.0	37.9
Broad liquid assets/short-term wholesale funding (x)	1.3	1.2	1.1	1.1	1.0
Net broad liquid assets/short-term customer deposits	17.8	14.9	11.7	7.7	(4.2)
Short-term wholesale funding/total wholesale funding	41.5	48.5	47.2	47.0	54.7

Support: One notch of ALAC support

We include one notch of uplift in the long-term rating, since we believe Danske Bank has a significant amount of additional loss-absorbing capacity (ALAC) and will maintain it in the coming years. To fulfil its new minimum requirement for own funds and eligible liabilities, Danske Bank is replacing large portions of maturing senior unsecured debt with senior nonpreferred instruments, thereby accumulating a material amount of ALAC. Danske Bank has a positive track record of placing about DKK25.5 billion of senior nonpreferred debt during the first nine months of 2018 and additional \$3 billion in January 2019. We estimate that Danske Bank's ALAC buffer will be just below 5% of risk-weighted assets in 2018 and eventually exceed 5% in the following two years.

Core subsidiaries: Danica Pension Livsforsikringsaktieselskab at the level of the bank's unsupported credit profile

We rate Danica at the level of the bank's unsupported credit profile, since we view Danica as a core group entity, but don't believe it will benefit from the bank's ALAC.

Resolution Counterparty Ratings (RCR)

Following the completion of our RCR jurisdiction assessments on Denmark, we assigned 'A+/A-1' RCRs to Danske Bank (see "24 European Banking Groups Assigned Resolution Counterparty Ratings," published June 29, 2018).

An RCR is a forward-looking opinion of the relative default risk of certain senior liabilities that may be protected from default with an effective bail-in resolution process for the issuing financial institution.

Additional rating factors:None

No additional factors affect this rating.

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: Assessing Bank Branch Creditworthiness, Oct. 14, 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

Related Research

- Nordic Banks Sport Strong Capital--And It's Not Likely To Soften, Oct. 17, 2018
- Nordic Bank Ratings Continue To Stand Tall, Aug. 16, 2018

- Banking Industry Country Risk Assessment: Denmark, March 7, 2018

Anchor Matrix										
Industry Risk	Economic Risk									
	1	2	3	4	5	6	7	8	9	10
1	a	a	a-	bbb+	bbb+	bbb	-	-	-	-
2	a	a-	a-	bbb+	bbb	bbb	bbb-	-	-	-
3	a-	a-	bbb+	bbb+	bbb	bbb-	bbb-	bb+	-	-
4	bbb+	bbb+	bbb+	bbb	bbb	bbb-	bb+	bb	bb	-
5	bbb+	bbb	bbb	bbb	bbb-	bbb-	bb+	bb	bb-	b+
6	bbb	bbb	bbb-	bbb-	bbb-	bb+	bb	bb	bb-	b+
7	-	bbb-	bbb-	bb+	bb+	bb	bb	bb-	b+	b+
8	-	-	bb+	bb	bb	bb	bb-	bb-	b+	b
9	-	-	-	bb	bb-	bb-	b+	b+	b+	b
10	-	-	-	-	b+	b+	b+	b	b	b-

Ratings Detail (As Of February 27, 2019)

Danske Bank A/S	
Issuer Credit Rating	A/Negative/A-1
<i>Nordic Regional Scale</i>	--/--/K-1
Resolution Counterparty Rating	A+/--/A-1
Certificate Of Deposit	
<i>Foreign Currency</i>	A/A-1
Commercial Paper	A-1
Junior Subordinated	BB+
Senior Secured	AAA/Stable
Senior Subordinated	BBB+
Senior Unsecured	A
Senior Unsecured	A/A-1
Short-Term Debt	A-1
Subordinated	BBB
Issuer Credit Ratings History	
25-Sep-2018	A/Negative/A-1
05-Apr-2018	A/Positive/A-1
13-Jul-2015	A/Stable/A-1
29-Apr-2014	A/Negative/A-1
05-Feb-2004 <i>Nordic Regional Scale</i>	--/--/K-1
Sovereign Rating	
Denmark	AAA/Stable/A-1+
Related Entities	
Danica Pension Livsforsikringsaktieselskab	
Issuer Credit Rating	A-/Negative/--

Ratings Detail (As Of February 27, 2019) (cont.)

Subordinated	BBB
Danske Bank A/S, Swedish Branch	
Issuer Credit Rating	A/Negative/A-1
Danske Hypotek AB	
Senior Secured	AAA/Stable
Realkredit Danmark A/S	
Senior Secured	AA-/Negative
Senior Secured	AAA/Stable
Short-Term Secured Debt	A-1+

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