# Brage Finans AS
# Issuer Rating Report

SCOPE

STABLE
A-

## Overview

Scope assigns a first-time Issuer Rating of A- to Brage Finans AS. The rating agency also assigns a first-time rating to the company's senior unsecured debt at A-. All ratings have a Stable Outlook.

## Highlights

- Founded in June 2010, Brage Finans (Brage) is a Norwegian finance company offering primarily equipment leasing for business clients and car loans for individuals. The current split of activities is about 70% corporate and 30% retail. The business, however, is likely to become more evenly balanced as management expects future growth to be driven by retail car loans.
- Brage serves as the finance company for its owners, 12 solid savings banks located along the coast of Norway, from Sparebanken Sor in Agder / Telemark to Helgeland Sparebank in Nordland. Combined, the owner banks have more than 100 local offices, forming an essential part of the company's distribution network. With five of eight members on the board coming from the banks, the owners steer the strategic direction of the company. In addition, the owner banks have consistently provided capital and credit facilities to support Brage's development.
- The business has demonstrated robust growth, starting with equipment leasing for the owner banks (2010), then car loans for the owner banks (2013), and then distribution through equipment (2015) and car dealers (2017). Brage became profitable after less than three years in operation and returns have continued to increase. At the same time, credit quality has remained strong underpinned by a diverse credit portfolio, a low to moderate risk appetite in line with that of the owner banks and a favourable macro environment.
- The nature of Brage's business, however, entails greater asset risk than traditional banking focused on mortgage lending. Meanwhile, leasing offers higher margins, but counterparties are often small businesses in cyclical sectors like construction and manufacturing.
- Brage is a licensed finance company regulated and supervised by the Norwegian FSA. The company is subject to many of the same requirements as banks, including in the areas of solvency and liquidity. Brage maintains reassuring prudential metrics in line with the relatively stringent requirements in Norway.
- As it is not authorised to collect deposits, Brage relies on wholesale funding and is a frequent issuer in the domestic debt market.

### Ratings & Outlook

| | |
|---|---|
| Issuer rating | A- |
| Outlook | Stable |
| Senior unsecured debt rating | A- |


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Bloomberg: SCOP

## Rating drivers (summary)

**The rating drivers, in decreasing order of importance in the rating assignment, are:**

- Successful mid-size player in attractive Norwegian finance market focused on lease financing for business assets and car loans for individuals.
- Strategic and close relationship with solid owner banks supports business growth.
- Strong asset quality and reassuring prudential metrics.
- A reliance on wholesale funding balanced by the cash flow generative nature of the business and active liquidity management.

## Rating-change drivers

**Continued sustainable growth** with increasing business diversification while maintaining satisfactory levels of profitability and without a material increase in risks. Reducing the reliance on confidence-sensitive market funding would also be viewed positively.

**Change in nature of relationship between Brage and its owner banks.** The close and strategic relationship between Brage and its owners is a key factor in our rating assessment. The owner banks provide strategic direction, business opportunities and funding. If an unexpected need for equity were to arise, the owners would likely be the first resource. As well, the owner banks are informal partners in expertise sharing. Brage's head office is in the same building as Sparebanken Vest who holds the largest ownership stake.

**Material deterioration in the regional economies where Brage's activities are concentrated.** Leasing is closely linked to the economic cycle and business investment, with industrial equipment, machinery and commercial vehicles accounting for nearly 65% of leased assets.[1] A weaker economic environment could impact Brage's earnings and asset quality.

[1] Source: Association of Norwegian Finance Houses, Annual Report 2018.

## Rating drivers (details)

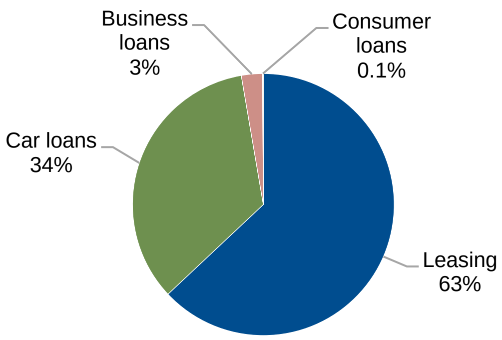
**Successful mid-size player in attractive Norwegian finance market focused on lease financing for business assets and car loans for individuals**

Brage Finans' (Brage) origins stem from senior management's idea of establishing a local finance company to capture business opportunities. In Norway, foreign finance companies are significant players, accounting for approximately 40% of lending volume.[2] The senior management team, comprising of the CEO, the Deputy CEO, the CFO and the head of credit, have extensive experience in the finance industry and have been with the company since its founding in 2010.

**Business expected to be more balanced between leasing and car loans in future**

Brage offers primarily lease financing and loans to businesses (often SMEs) and car loans to individuals. There is a very small proportion of unsecured consumer loans as this is offered by the owner banks. Management, however, is wary of this product and does not actively market it (Figure 1). Future growth potential is expected to be strongest in the car loan market as Brage more closely integrates its product offering on the mobile banking platforms of the owner banks. Consequently, management foresees the business mix becoming more diversified and more evenly balanced between business and retail customers.

**Figure 1: Brage's business profile**




Note: Net credit portfolio of NOK 11.3bn as of 30 September 2019.
Source: Company data, Scope Ratings

**Figure 2: Geographic footprint of owner banks**


Source: Company data.

Lease financing is available for a wide range of movable assets, including construction machinery, agricultural equipment, trucks, and vans. Brage buys and owns the asset while the client pays a monthly rental fee for use of the asset. At the end of the lease period, usually three to seven years, the client normally buys the asset or continues leasing for a minimal amount. There is limited residual value risk as the contracts are mostly full pay-out leases.

**Focused on geographical markets of owner banks**

Brage focuses mainly on the geographical markets of its owner banks which include Hordaland, Rogaland and Vest-Agder (Figure 2). As new distribution channels have been added, the proportion of business derived from the owner banks has declined but

[2] Norges Bank. Norway's Financial System, 2018.

remains substantial at more than half. In addition to the more than 100 local offices of the owner banks, Brage also distributes products through over 270 equipment and car dealers and directly via its own branch offices and digital platforms. The company's three-pronged distribution strategy has supported strong growth.

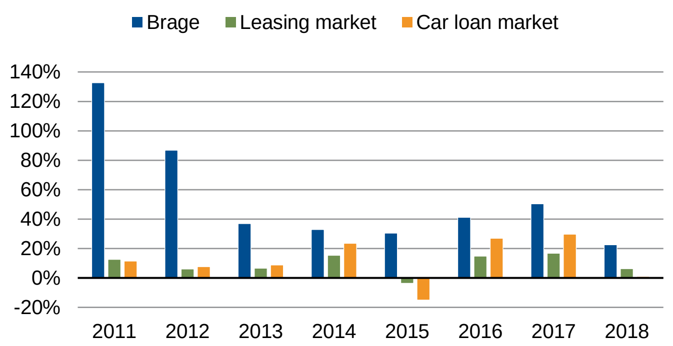
The finance market in Norway is characterised by three large players who roughly equally account for about 55% of new business volume (DNB Finans, Santander Consumer Bank AS and the combined Nordea Finans Norway and SG Finans).[3] Other players include the finance companies of auto manufacturers and bank-owned finance companies.

**Market share has grown over time**

As of 30 September 2019, Brage had a market share of 4.8% of the overall financing market. Meanwhile, new business market share in the movable asset leasing and car loan segments were 6.6% and 4.3%, respectively.[4] Over time, the company has successfully increased market share in the segments it operates in.

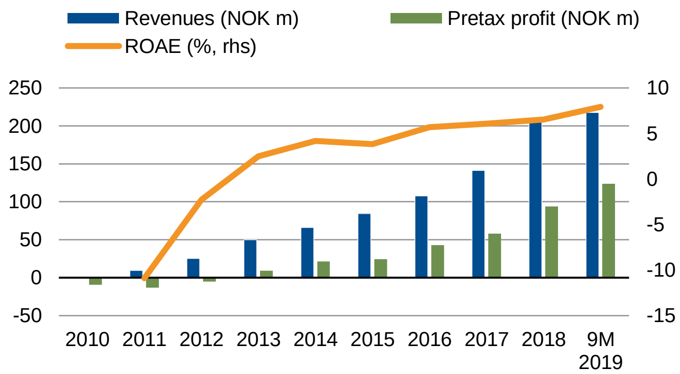
Volume growth in the leasing market is linked to the overall economy as well as the investment cycle. In 2015, both the leasing and car loan markets declined but Brage experienced positive growth, facilitated by the addition of equipment dealers as a new distribution channel (Figure 3).

**Figure 3: Brage's new business sales growth vs. market**




Note: Leasing market data excludes the leasing of land and buildings as Brage is not active in these segments. Source: Company data, Association of Norwegian Finance Houses, Scope Ratings.

**Figure 4: Brage's earnings development**




Source: Company data, Scope Ratings.

**Strategic and close relationship with solid owner banks supports business growth**

Brage is owned by 12 well-established and solid savings banks, with their ownership stakes reflecting their distribution capacity. Overall, the banks are profitable and display sound prudential metrics (Figure 5). While the banks are independent, they cooperate and jointly own product and service companies to better serve customers, increase efficiency, and maintain their competitive positions. For example, the owner banks are also joint owners in Frende Forsikring, an insurance company, and Norne Securities, an investment bank.

**Owner banks incentivised to refer high quality clients**

Brage serves as the finance company for its owner banks. Due to the commission arrangement in place, the owner banks are incentivised to refer high quality customers to Brage. The banks receive a commission based on their distribution volumes and half of net interest income after funding costs and credit losses in their specific portfolios. For 9M 2019, the banks received commissions of NOK 24.5m out of a total of NOK 37.6m paid. Including the commission paid to the owner banks, Brage's reported ROE was 8.6% while excluding the commission, the reported ROE was 10.2%.

[3] Market share data is for 2018 and reflects the activity of members of the Association of Norwegian Finance Houses. Members' activities include leasing, factoring, car financing, credit cards and consumer loans. In December 2019, Nordea Finans Norway announced that it was acquiring SG Finans.
[4] Source: Association of Norwegian Finance Houses

**Figure 5: Selected metrics of owner banks**

| | Stake in Brage (%) | Assets (NOK bn) | Return on Avg Assets (%) | Return on Avg Equity (%) | Costs % Income | NPLs % Gross loans | CET1 capital ratio (%) |
|---|---|---|---|---|---|---|---|
| **Sparebanken Vest** | 49.99% | 199.1 | 1.1 | 13.3 | 36.7 | 0.2 | 16.6 |
| **Sparebanken Sør** | 20.77% | 125.8 | 0.9 | 9.2 | 38.9 | 1.0 | 15.3 |
| **Helgeland Sparebank** | 8.58% | 34.2 | 0.8 | 8.3 | 41.2 | 1.8 | 15.9 |
| **Fana Sparebank** | 5.34% | 26.2 | 0.7 | 7.6 | 52.0 | 0.8 | 17.1 |
| **Haugesund Sparebank** | 3.11% | 11.4 | 0.9 | 9.1 | 38.8 | 1.7 | 16.3 |
| **Voss Sparebank** | 2.18% | 4.7 | 1.1 | 6.7 | 41.1 | 0.1 | 24.1 |
| **Flekkefjord Sparebank** | 2.03% | 6.9 | 0.6 | 5.4 | 49.7 | 0.7 | 22.7 |
| **Skudenes & Aakra Sparebank** | 1.84% | 9.6 | 1.0 | 9.9 | 33.7 | 0.4 | 17.5 |
| **Søgne & Greipstad Sparebank** | 1.67% | 4.6 | 0.8 | 7.4 | 47.3 | 0.6 | 16.8 |
| **Luster Sparebank** | 1.59% | 3.8 | 0.9 | 7.2 | 47.6 | 1.1 | 19.7 |
| **Lillesands Sparebank** | 1.51% | 3.5 | 0.7 | 6.1 | 45.3 | 0.3 | 18.8 |
| **Etne Sparebank** | 1.40% | 2.0 | 0.8 | 8.5 | 46.1 | 0.5 | 16.6 |

Note: Data as of 30 September 2019.
Source: Company data, SNL, Scope Ratings.

When evaluating Brage's performance, the owner banks also consider the commissions they receive. The company's overall financial objective is to generate a return in line with the owner banks' own return targets. Management's planned actions for improving returns include optimising the product mix, increasing non-capital-intensive products such as payment insurance, reducing funding costs and improving efficiency.

As of 30 September 2019, the company's cost income ratio had reached 30% when adjusted for commissions paid to the owner banks, with management targeting a cost income ratio around 25%. Brage continues to gradually enhance its IT systems and client facing digital platforms but there is no need for major investments as the systems are relatively new and up to date.

**Owner banks have consistently provided capital and funding**

Since Brage was founded, the owner banks have consistently provided capital and funding to support growth and to ensure a sound solvency position. Over the years, the owner banks have contributed nearly NOK 1.5bn in capital. In addition, the owner banks provide loans and credit facilities. As of 30 September 2019, Brage had NOK 600m in loans and a NOK 600m undrawn credit facility from the owner banks. For the owner banks, Brage is a means to further strengthen customer relationships and a relevant source of fee and commission income.

### Strong asset quality and reassuring prudential metrics

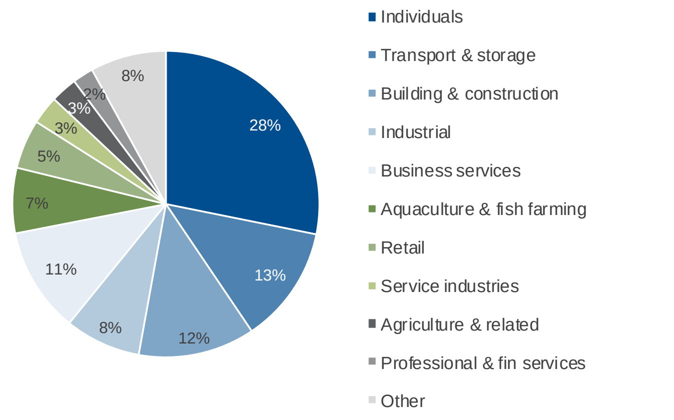
Brage's credit quality has been strong, with non-performing loans averaging 0.3% of gross loans over the last nine years (Figure 8). We note that Brage classifies non-performing loans as those which are more than 67 days past due (the industry standard) while banks typically use 90 days past due. The company performs its own credit assessment of all clients, including those which have been referred by the owner banks. Credit and concentration risks are also actively managed and monitored.

**Diversified and granular portfolio**

As the car loan business has grown, retail customers have become an increasing proportion of the portfolio (9M 2019: 28%). Within the corporate portfolio, the largest exposures are to construction, transport and storage, and business services, industries which tend to be more cyclical. However, these are also some of the businesses most likely to use lease financing and the macro environment in Norway remains supportive.

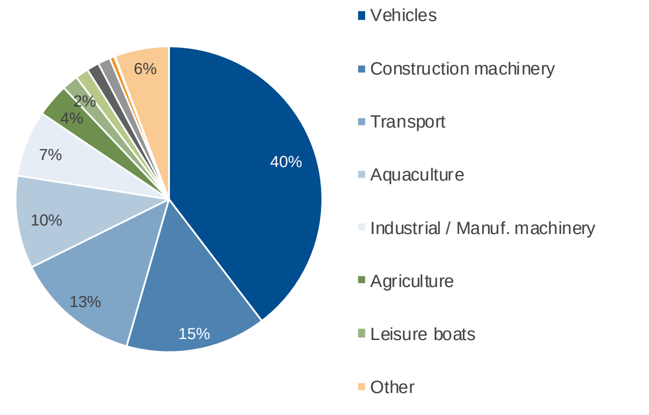
The portfolio is diversified by both industry and asset type, with concentration risk being low (Figures 6 and 7). As of 30 September 2019, 56% of the portfolio was comprised of customer engagements totalling less than NOK 5m each. This same portion of the portfolio accounted for more than 98% of customers, with an average contract value of around NOK 300,000. Meanwhile, less than 8% of the portfolio was comprised of customer engagements totalling more than NOK 50m. In addition, nearly 85% of the portfolio was comprised of contracts for individual assets with values below NOK 5m.

**Figure 6: Portfolio by industry (%)**




Notes: Data as of 30 September 2019.
Source: Company data, Scope Ratings.

**Figure 7: Portfolio by asset type (%)**



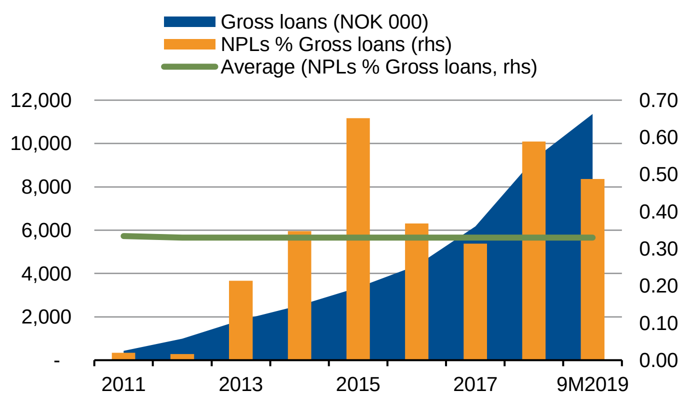

Notes: Data as of 30 September 2019. Asset types not listed in the legend above each account for less than 1.5% of the portfolio.
Source: Company data, Scope Ratings.

**Supervised by Norwegian FSA and subject to most of the same requirements as banks**

Licensed as a finance company, Brage is regulated and supervised by the Norwegian FSA. The company is subject to most of the same requirements as banks, including in the areas of solvency and liquidity. Brage maintains reassuring prudential metrics in line with relatively stringent requirements (Figure 9). We further note that the company uses the standardised approach for calculating capital requirements. As of 30 September 2019, Brage's leverage ratio was 15%, well in excess of the 5% requirement.

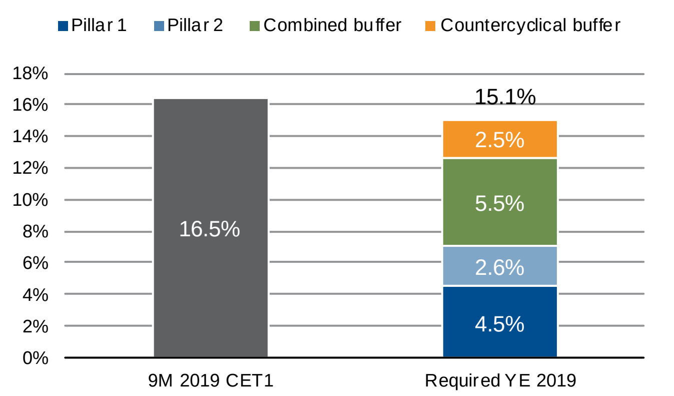
Since year-end 2019, Brage has been subject to a CET1 capital requirement of 15.1%, which includes a Pillar 2 requirement of 2.6%. With the final implementation of CRR/CRD IV in Norway, the SME discount was introduced from 31 December 2019. Management estimates that this will benefit the company's CET1 capital ratio by about 130bps. Meanwhile, from end-2022, the systemic risk buffer requirement will increase to 4.5% from the current 3%.

**Figure 8: Development of asset quality**




Source: Company data, Scope Ratings.

**Figure 9: CET1 capital position vs. requirements**




Source: Company data, Scope Ratings.

### A reliance on wholesale funding balanced by the cash flow generative nature of the business and liquidity management

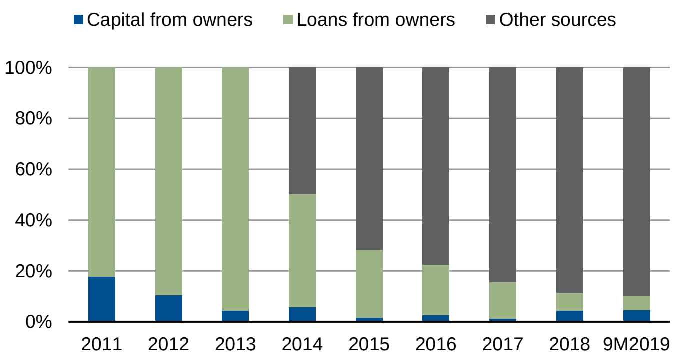
As Brage has grown, management has successfully obtained different sources of funding to support its development. Over time, the proportion of funding from the owner banks has declined while market funding has become important (Figure 10). In 2014, Brage issued senior unsecured debt for the first time and in 2015 began issuing capital instruments. In 2018, Brage also obtained a NOK 175m six-year loan from the Nordic Investment Bank to support SMEs with lease financing for movable assets.

**Funded primarily from debt markets as not authorised to collect deposits**

The company has become a frequent issuer in the domestic market and management regularly meets with investors. Brage is currently developing a green framework to be incorporated into credit policies and which could eventually be used to identify assets to support the issuance of green bonds.

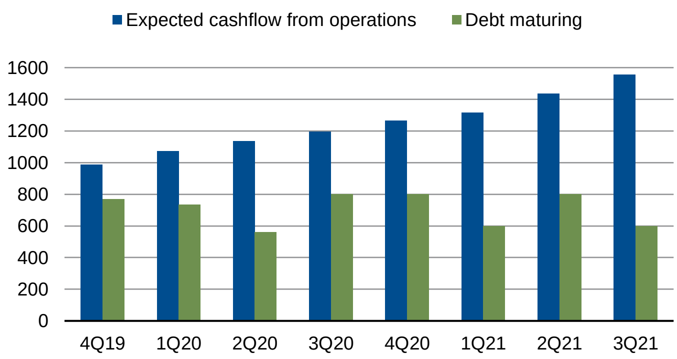
To manage liquidity and funding risks, Brage aims to ensure that quarterly operating cash flows from customer payments are more than sufficient to cover future debt maturities (Figure 11). There are internal limits for the amount of debt that can be borrowed and the amount of debt maturing each quarter. In addition, the company maintains a liquidity buffer held in cash and bond funds. As of 30 September 2019, the LCR and NSFR were 138% and 112%, respectively.

**Figure 10: Funding sources (%)**




Note: Other sources include a loan from the Nordic Investment Bank, senior unsecured debt and capital securities. Source: Company data, Scope Ratings.

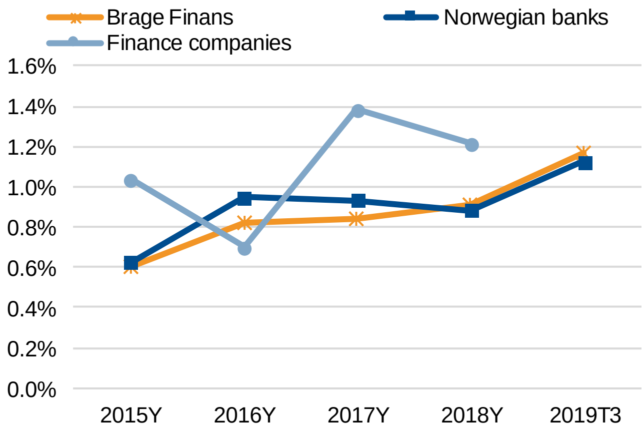
**Figure 11: Expected cash flows vs debt maturities (NOK m)**



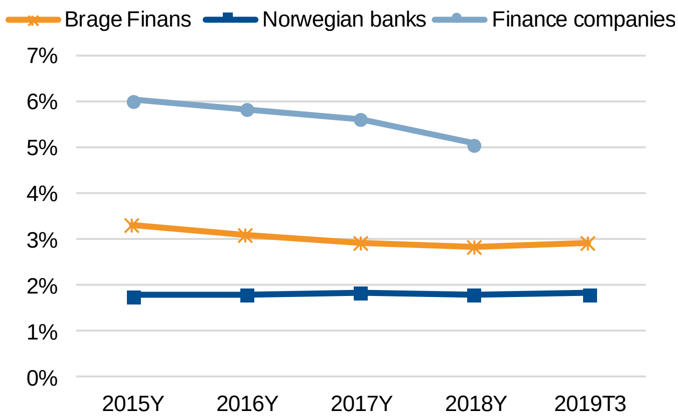

Source: Company data, Scope Ratings.

## I. Appendix: Peer comparison

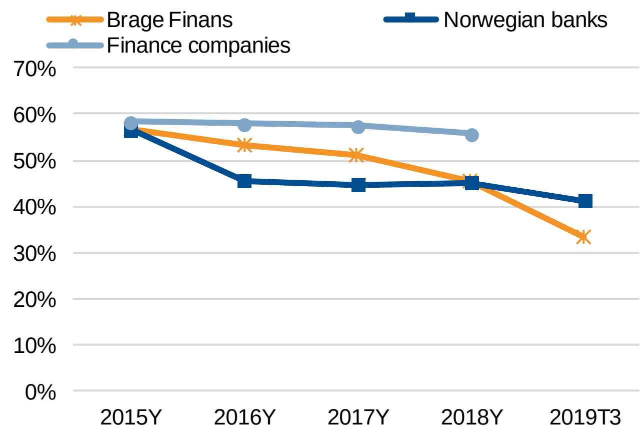
**Return on average assets (%)**



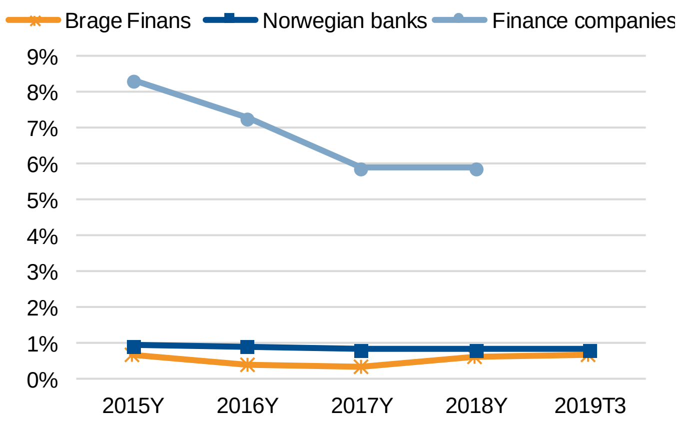

**Net interest margin (%)**



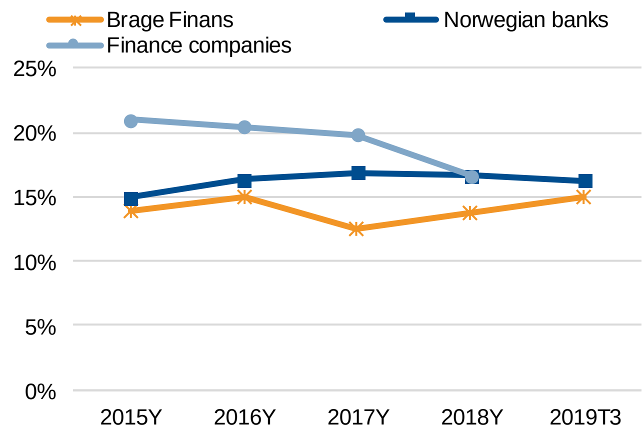

**Costs % Income**



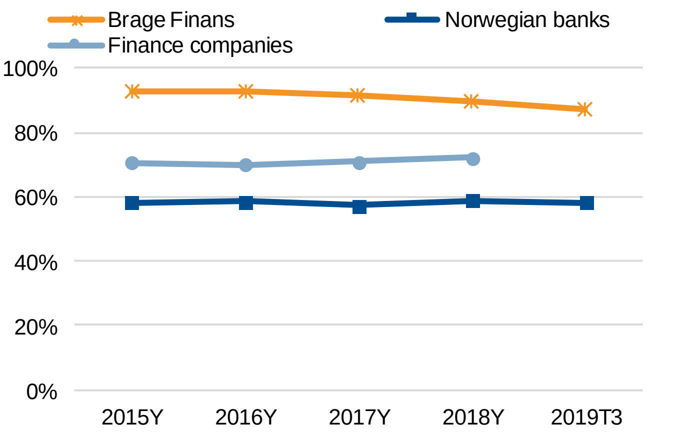

**Problem loans % Gross loans**




**CET1 capital ratio (%, transitional basis)**




**Asset risk intensity (RWAs % Total assets)**




Notes: 9M 2019 data is not sufficiently available for the Finance companies peer group to show figures in the above charts. Capital related data is unavailable for BNP Paribas Lease Group SA and Credit Agricole Leasing & Factoring SA.

Norwegian banks: Brage Finans, BN Bank, Sandes Sparebank, SpareBank 1 Nordvest, Totens Sparebank, Sparebanken Vest, Sparebanken Sor, Helgeland Sparebank, Fana Sparebank, Haugesund Sparebank, Jaeren Sparebank.

Finance companies: Brage Finans, SG Finans, Nordea Finans, Santander Consumer Bank AS, LeasePlan Corporation NV, BNP Paribas Lease Group SA, Credit Agricole Leasing & Factoring SA, UniCredit Leasing SpA, Alba Leasing SpA.

Source: SNL

## II. Appendix: Selected Financial Information – Brage Finans AS

| | 2015Y | 2016Y | 2017Y | 2018Y | 9M 2019 |
|---|---|---|---|---|---|
| **Balance sheet summary (NOK m)** | | | | | |
| **Assets** | | | | | |
| Cash and interbank assets | 19 | 82 | 179 | 237 | 324 |
| Total securities | 0 | 30 | 41 | 63 | 94 |
| of which, derivatives | NA | NA | NA | NA | NA |
| Net loans to customers | 3,331 | 4,355 | 6,148 | 9,248 | 11,325 |
| Other assets | 97 | 44 | 54 | 78 | 115 |
| **Total assets** | **3,447** | **4,512** | **6,423** | **9,626** | **11,858** |
| **Liabilities** | | | | | |
| Interbank liabilities | 800 | 800 | 800 | 775 | 775 |
| Senior debt | 2,050 | 2,915 | 4,581 | 7,230 | 8,715 |
| Derivatives | NA | NA | NA | NA | NA |
| Deposits from customers | 0 | 0 | 0 | 0 | 0 |
| Subordinated debt | 45 | 95 | 95 | 170 | 235 |
| Other liabilities | NA | NA | NA | NA | NA |
| **Total liabilities** | **2,937** | **3,869** | **5,560** | **8,314** | **9,904** |
| Ordinary equity | 510 | 643 | 762 | 1,212 | 1,778 |
| Equity hybrids | 0 | 0 | 100 | 100 | 175 |
| Minority interests | 0 | 0 | 0 | 0 | 0 |
| **Total liabilities and equity** | **3,447** | **4,512** | **6,423** | **9,626** | **11,858** |
| *Core tier 1/ common equity tier 1 capital* | 446 | 624 | 737 | 1,185 | 1,714 |
| **Income statement summary (NOK m)** | | | | | |
| Net interest income | 97 | 120 | 157 | 232 | 238 |
| Net fee & commission income | -13 | -13 | -18 | -29 | -26 |
| Net trading income | 0 | 0 | 1 | 1 | 1 |
| Other income | 0 | 1 | 1 | 3 | 4 |
| **Operating income** | **84** | **108** | **141** | **208** | **218** |
| Operating expenses | 48 | 58 | 72 | 94 | 72 |
| **Pre-provision income** | **37** | **50** | **69** | **114** | **146** |
| Credit and other financial impairments | 12 | 7 | 11 | 20 | 22 |
| Other impairments | 0 | 0 | 0 | 0 | 0 |
| Non-recurring items | 0 | 0 | 0 | 0 | 0 |
| **Pre-tax profit** | **24** | **43** | **58** | **94** | **124** |
| Discontinued operations | 0 | 0 | 0 | 0 | 0 |
| Other after-tax Items | 0 | 0 | 0 | 0 | 0 |
| Income tax expense | 6 | 10 | 12 | 18 | 27 |
| Net profit attributable to minority interests | 0 | 0 | 0 | 0 | 0 |
| **Net profit attributable to parent** | **18** | **33** | **46** | **75** | **96** |

Source: SNL

## III. Appendix: Selected Financial Information – Brage Finans AS

| | 2015Y | 2016Y | 2017Y | 2018Y | 9M 2019 |
|---|---|---|---|---|---|
| **Funding and liquidity** | | | | | |
| Net loans/ deposits (%) | NA | NA | NA | NA | NA |
| Liquidity coverage ratio (%) | NA | 95.0% | 109.0% | 125.0% | 138.0% |
| Net stable funding ratio (%) | NA | NA | NA | 129.0% | 112.0% |
| **Asset mix, quality and growth** | | | | | |
| Net loans/ assets (%) | 96.6% | 96.5% | 95.7% | 96.1% | 95.5% |
| Problem loans/ gross customer loans (%) | 0.7% | 0.4% | 0.3% | 0.6% | 0.5% |
| Loan loss reserves/ problem loans (%) | 93.5% | 97.8% | 109.5% | 49.1% | 67.4% |
| Net loan growth (%) | 32.7% | 30.7% | 41.2% | 50.4% | 29.9% |
| Problem loans/ tangible equity & reserves (%) | 4.2% | 2.5% | 2.3% | 4.2% | 2.8% |
| Asset growth (%) | 32.8% | 30.9% | 42.4% | 49.9% | 30.9% |
| **Earnings and profitability** | | | | | |
| Net interest margin (%) | 3.3% | 3.1% | 2.9% | 2.8% | 3.0% |
| Net interest income/ average RWAs (%) | 3.5% | 3.2% | 3.1% | 3.2% | 3.3% |
| Net interest income/ operating income (%) | 115.1% | 111.4% | 111.2% | 111.6% | 109.5% |
| Net fees & commissions/ operating income (%) | -15.4% | -12.4% | -13.1% | -13.7% | -12.0% |
| Cost/ income ratio (%) | 56.7% | 53.4% | 51.2% | 45.3% | 33.0% |
| Operating expenses/ average RWAs (%) | 1.7% | 1.6% | 1.4% | 1.3% | 1.0% |
| Pre-impairment operating profit/ average RWAs (%) | 1.3% | 1.4% | 1.4% | 1.6% | 2.1% |
| Impairment on financial assets / pre-impairment income (%) | 33.4% | 14.5% | 15.7% | 17.6% | 15.3% |
| Loan loss provision/ average gross loans (%) | 0.4% | 0.2% | 0.2% | 0.3% | 0.3% |
| Pre-tax profit/ average RWAs (%) | 0.9% | 1.2% | 1.2% | 1.3% | 1.7% |
| Return on average assets (%) | 0.6% | 0.8% | 0.8% | 0.9% | 1.2% |
| Return on average RWAs (%) | 0.7% | 0.9% | 0.9% | 1.0% | 1.4% |
| Return on average equity (%) | 3.8% | 5.7% | 6.1% | 6.5% | 7.9% |
| **Capital and risk protection** | | | | | |
| Common equity tier 1 ratio (%, fully loaded) | 13.9% | 14.9% | 12.6% | 13.7% | 16.5% |
| Common equity tier 1 ratio (%, transitional) | 13.9% | 14.9% | 12.6% | 13.7% | 16.5% |
| Tier 1 capital ratio (%, transitional) | 13.9% | 14.9% | 14.3% | 14.9% | 18.1% |
| Total capital ratio (%, transitional) | 15.3% | 17.2% | 15.9% | 16.9% | 20.4% |
| Leverage ratio (%) | NA | 12.5% | 11.8% | 12.5% | 15.0% |
| Asset risk intensity (RWAs/ total assets, %) | 93.0% | 92.5% | 91.3% | 89.6% | 87.8% |

Source: SNL

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