

# Financial Institutions Ratings

## Danske Bank – AT1 rating report



### Security Ratings

|   |           |
|---|-----------|
| Outlook   | On review |
| 5.75% EUR 750m Perpetual Non-Cumulative Resettable Additional Tier 1 Capital Notes              | BBB-      |
| 5.875% EUR 750m Perpetual Non-Cumulative Resettable Additional Tier 1 Capital Notes             | BBB-      |
| Floating DKK 3bn Perpetual Non-Cumulative Additional Tier 1 Capital Notes                       | BBB-      |
| 6.125% USD 750m Perpetual Non-Cumulative Resettable Additional Tier 1 Convertible Capital Notes | BBB-      |

The ratings have not been solicited by the issuer; the analysis is based solely on public information.

### Rating rationale

Scope assigns long-term ratings of **BBB-** (on review for possible upgrade) to Danske Bank's four Additional Tier 1 (AT1) notes (the Notes) listed in the table above. For details on the rated instruments, see the next page. The ratings are based on the following considerations:

- Senior unsecured debt (eligible for MREL): A, on review for possible upgrade
- Minimum notches down from the senior unsecured debt rating: 4
- Additional notches: 0

Our methodology states that when rating capital instruments the starting point for notching-down is the MREL/TLAC-eligible senior unsecured debt rating, and no longer the issuer rating. Please refer to Scope's Bank Capital Instruments Rating Methodology published in May 2018 for more details.

The minimum four notches reflect the deeply subordinated status of AT1 capital instruments in the priority of claims, their going concern loss-absorbing features and investors' exposure to coupon-cancellation risks.

Despite high triggers at 7%, we believe that given the high distance to the triggers, both for Danske Bank A/S and for the group, a further notch is not warranted.

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Bloomberg: SCOP

The release of this rating report does not constitute a rating action. Last rating action was assigned on 9 October 2014. For further information on the last rating action and regulatory information please click [here](#)

### Issuer credit profile

Scope assigns Danske Bank an Issuer Rating of A+, on review for possible upgrade.

The ratings are driven by the group's strong franchise as the leading universal bank in its domestic market, Denmark. Having largely recovered from the financial crisis, the group has managed to improve its returns, even in an environment of subdued growth and negative interest rates. While Danske pursues a Nordic universal bank strategy, its measured expansion outside of Denmark helps to manage the usual risks associated with fast growth in mature markets.

The relatively high dependence on market funding is substantially mitigated by the large and stable component of covered bonds. In 2017, Danske Bank reported a 13.6% ROE, ahead of its 12.5% long-term target.

We continue to monitor the group's expansion in Norway and Sweden in light of the potentially less favourable market dynamics in these countries.

### Summary terms

|                   |   |
|-------------------|---|
| <b>Issuer</b>     | <b>Danske Bank A/S</b>  |
| <b>Issue Date</b> | <b>March 2014</b>   |
| <b>Amount</b>     | EUR 750m  |
| <b>Coupon</b>     | <ul style="list-style-type: none"> <li>5.75% fixed until first call date, reset every six years thereafter</li> </ul>   |
| <b>Format</b>     | <ul style="list-style-type: none"> <li>Perpetual non-cumulative resettable AT1 capital notes, callable on 6 April 2020 and on any interest payment date thereafter</li> </ul> |
| <b>ISIN</b>       | XS1044578273  |

|                   |   |
|-------------------|---|
| <b>Issue date</b> | <b>February 2015</b>  |
| <b>Amount</b>     | EUR 750m  |
| <b>Coupon</b>     | <ul style="list-style-type: none"> <li>5.875% fixed until first call date, reset every seven years thereafter</li> </ul>  |
| <b>Format</b>     | <ul style="list-style-type: none"> <li>Perpetual non-cumulative resettable AT1 capital notes, callable on 6 April 2022 and on any interest payment date thereafter</li> </ul> |
| <b>ISIN</b>       |   |

|                   |  |
|-------------------|--|
| <b>Issue date</b> | <b>November 2016</b>   |
| <b>Amount</b>     | DKK 3bn  |
| <b>Coupon</b>     | <ul style="list-style-type: none"> <li>Floating: CIBOR + 4.75%</li> </ul>  |
| <b>Format</b>     | <ul style="list-style-type: none"> <li>Perpetual non-cumulative resettable AT1 capital notes, callable on 23 Nov 2021 and on any interest payment date thereafter</li> </ul> |
| <b>ISIN</b>       | DK0030386610   |

|                   |  |
|-------------------|--|
| <b>Issue date</b> | <b>March 2017</b>  |
| <b>Amount</b>     | USD 750m   |
| <b>Coupon</b>     | <ul style="list-style-type: none"> <li>6.125% fixed until first call date, reset every seven years thereafter at 7Y Mid-Swap rate + 2.229%</li> </ul>                                      |
| <b>Format</b>     | <ul style="list-style-type: none"> <li>Perpetual non-cumulative resettable AT1 convertible capital notes, callable on 28 March 2024 and on any interest payment date thereafter</li> </ul> |
| <b>ISIN</b>       | XS1586367945   |

| Main risks                                   |  |
|--|--|
| <b>Coupon cancellation</b>                   | <ul style="list-style-type: none"> <li>Fully discretionary</li> <li>Mandatory to the extent that               <ul style="list-style-type: none"> <li>there are insufficient distributable items to pay the coupon on the security;</li> <li>the combined buffer requirement is not met and if coupons were paid, the amount of such payments would exceed the Maximum Distributable Amount; or</li> <li>the relevant regulator requires such coupons to be cancelled</li> </ul> </li> </ul>   |
| <b>Principal loss absorption</b>             | <ul style="list-style-type: none"> <li>Upon trigger breach</li> <li>EUR and DKK notes: Automatic writedown upon trigger event. At the issuer's discretion, the principal amount may be written up to a maximum of the original principal amount, on a pro-rata basis with Parity Trigger Loss Absorbing Instruments, up to the reinstatement limit</li> <li>USD notes: Automatic conversion into shares upon trigger event at greater of current market price and USD 23.97.</li> <li>Statutory loss absorption at point of non-viability</li> </ul> |
| <b>Trigger for principal loss absorption</b> | <ul style="list-style-type: none"> <li>Danske Bank A/S CET1 ratio &lt; 7% and/or</li> <li>Danske Bank Group CET1 ratio &lt; 7%</li> </ul>  |

Source: Prospectus. Scope Ratings

## Key risks

### A. Coupon cancellation

#### Key risk: Coupon cancellation

Coupon payments on the Notes are fully discretionary and are subject to distribution restrictions

Coupons must be cancelled if the issuer has insufficient distributable items, if the combined buffer requirement is not met and coupon payments exceed the Maximum Distributable Amount (MDA), or if the regulator requires that coupon payments be restricted.

At the end of December 2017, Danske Bank Group disclosed Available Distributable Items of DKK 133bn. Also at the end of 2017 Danske Bank reported DKK 117.5bn of Available Distributable on an unconsolidated basis (1Q18: DKK 112 bn), giving us comfort that its ability to pay coupons is not limited by any lack of distributable items.

#### Combined Buffer Requirement (CBR)

In line with CRD IV, mandatory restrictions on distributions apply if Danske's CET1 ratio falls below its CBR (defined as the total of the capital conservation buffer, the countercyclical buffer and the systemic risk buffer). For 2019, Danske's CBR is currently expected to consist of:

- a 2.5% capital conservation buffer
- a 3.0% systemic risk buffer
- a 0.8 % countercyclical capital buffer for exposures in Norway and Sweden (both set at 2%) and Denmark (set at 0.5%).

The systemic risk buffer is being phased in from 2015 to 2019 and the capital conservation buffer from 2016 to 2019.

Countercyclical buffers have been in place from 2015. A new countercyclical buffer was recommended by the Danish Systemic Risk Council December 2017 for exposures in Denmark, with the level set at 0.5%. This is to be applied from end-March 2019. Danske estimates that this will increase the Group's fully phased in CET1 requirement for 2019 by c.0.2%. This is included in our calculations.

Including the minimum 4.5%, in order to avoid distribution restrictions the required CET1 ratio is expected to be 10.8% in 2019. This does not include the Pillar 2 requirement, which under Danish rules does not affect the MDA calculation. The latest disclosure points to a CET1 requirement under Pillar 2 of 1.4%. However, it is our view that a regulator would consider a breach of the total solvency need, including Pillar 2 and buffers, when deciding on whether to cancel the coupons on the Notes.

**Table 1: Combined buffer requirements Danske Bank group**

|   | 2017         | Q1 2018     | 2019         |
|---|--------------|-------------|--------------|
| <b>Required CET1 associated with distribution restrictions:</b> | <b>8.1%</b>  | <b>9.4%</b> | <b>10.8%</b> |
| Combined buffer (CBR)   |              |             |              |
| - Capital conservation  | 1.25%        | 1.88%       | 2.50%        |
| - Systemic  | 1.80%        | 2.40%       | 3.00%        |
| - Countercyclical   | 0.50%        | 0.60%       | 0.80%        |
| Pillar 2 CET1 requirement*                                      | 1.50%        | 1.40%       | 1.40%        |
| Pillar 1 CET1 requirement                                       | 4.50%        | 4.50%       | 4.50%        |
| Danske Bank Group CET1, transitional (%)                        | 17.6%        | 16.4%       |              |
| <b>Distance to CET1 requirement incl. CBR (%)</b>               | <b>9.6%</b>  | <b>7.0%</b> |              |
| <b>Distance to CET1 requirement incl. CBR (DKK bn)</b>          | <b>72.1</b>  | <b>53.2</b> |              |
| Danske Bank Group Tier 1, transitional (%)                      | 20.1%        | 18.9%       |              |
| Required Tier 1 incl. CBR (%)                                   | 9.6%         | 10.9%       | 12.3%        |
| <b>Distance to Tier 1 requirement incl. CBR (%)</b>             | <b>10.5%</b> | <b>8.0%</b> |              |
| Danske Bank Group total capital, transitional (%)               | 22.6%        | 21.4%       |              |
| Required total capital, incl. CBR (%)                           | 11.6%        | 12.9%       | 14.3%        |
| <b>Distance to total capital requirement incl. CBR (%)</b>      | <b>11.1%</b> | <b>8.5%</b> |              |
| RWAs (DKK bn)   | 753          | 755         |              |

Note: \*under current Danish rules, Pillar 2 does not count towards automatic MDA restrictions.  
Source: Company data, Scope Ratings

The Group's CET1 ratio is currently well above requirements. As various capital buffers are phased in, the gap between Danske's CET1 ratio and the requirements is expected to decline but to remain solidly above the required level. Danske's target CET1 range of 14-15% provides an ample buffer, even to the fully phased-in requirement of 10.8%, or 12.2% if we were to prudently include Pillar 2 in the calculation.

## B. Principal loss absorption

### Key risk: Principal loss absorption

The mechanism for loss absorption is temporary write-down (EUR and DKK notes); or equity conversion (USD notes)

The two triggers are:

- Danske Bank A/S CET1 ratio < 7% and/or
- Danske Bank Group CET1 ratio < 7%

Furthermore, the Notes are all subject to the provisions of the Bank Recovery and Resolution Directive (BRRD), which empowers relevant authorities to permanently write down or convert into equity AT1 capital instruments, such as the Notes, in the course of resolution or before, at the point of non-viability.

#### Distance to trigger

At Q1 2018, Danske Group's transitional CET1 ratio was 16.4%, compared to the 7% trigger level in the securities. Therefore, the distance to trigger is 9.4%, or DKK 71.1bn, based on a risk exposure amount of DKK 755bn.

We expect the Group's CET1 capital ratio to remain comfortably above the trigger level in light of its stated target of 14-15%. Danske Bank states that this implies a management buffer of 200-300 bps in relation to the fully loaded CET1 capital requirement.

Danske Bank A/S's CET1 ratio stood at 18.3% as of 1Q18, hence the distance to trigger would be even more material when considering the parent company's solo trigger.

**Table 2: Distance to trigger – Danske Bank (group)**

|  | 2017         | Q1 2018     | 2019 |
|--|--------------|-------------|------|
| Trigger level                            | 7.0%         | 7.0%        | 7.0% |
| Danske Bank Group CET1, transitional (%) | 17.6%        | 16.4%       |      |
| <b>Distance to trigger (%)</b>           | <b>10.6%</b> | <b>9.4%</b> |      |
| <b>Distance to trigger (DKK bn)</b>      | <b>80.0</b>  | <b>71.1</b> |      |

Source: Company data, Scope Ratings



## Financial Institutions Ratings

### Danske Bank – AT1 rating report

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