

RatingsDirect®

Bank of Aland PLC

Primary Credit Analyst:

Olivia Fleischmann, Stockholm (46) 8-440-5904; olivia.fleischmann@spglobal.com

Secondary Contact:

Salla von Steinaecker, Frankfurt (49) 69-33-999-164; salla.vonsteinaecker@spglobal.com

Table Of Contents

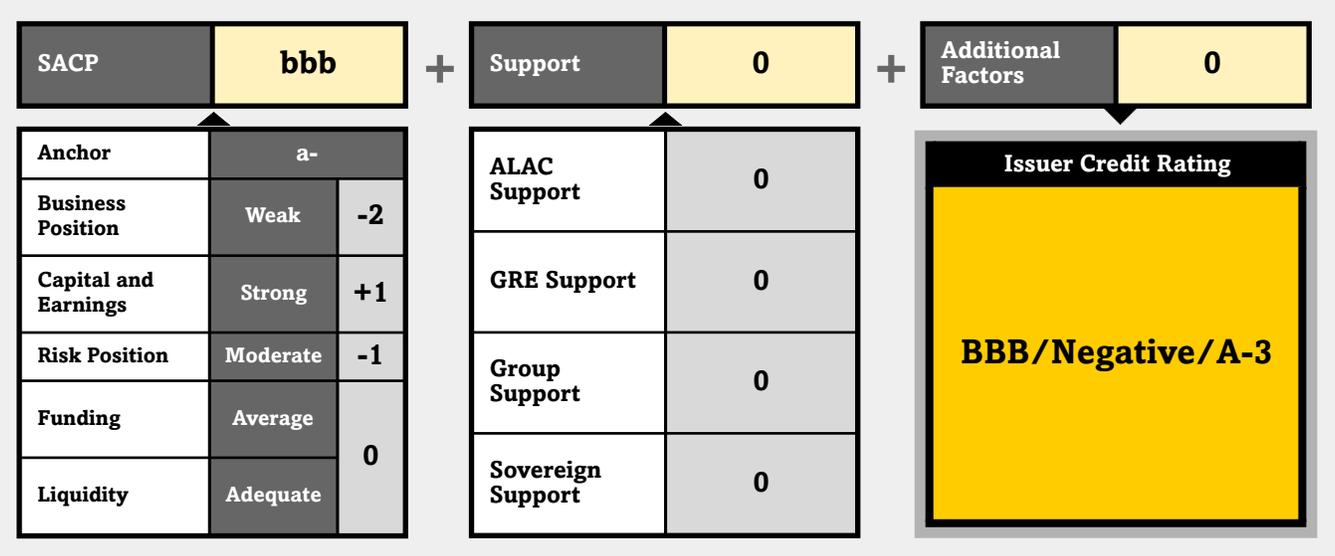
Major Rating Factors

Outlook

Rationale

Related Criteria And Research

Bank of Åland PLC



Major Rating Factors

Strengths:	Weaknesses:
<ul style="list-style-type: none"> Strong capitalization. Business operations in economically robust regions in Finland and Sweden. Sound funding profile benefitting from stable customer deposits. 	<ul style="list-style-type: none"> Concentration risk due to focus on retail and private banking. Niche market position given geographic and franchise selection. Lower cost efficiency than peers, distorted by non-banking activities.

Outlook: Negative

S&P Global Ratings' negative outlook on Finland-based Bank of Åland reflects our view that the bank's core markets of Finland and Sweden face heightened economic risks that could hinder the performance of their banking sectors over the next two years. This could have a negative impact on Finnish banks, including Bank of Åland, and ultimately lead us to lower our anchor on Finnish banks to 'bbb+' from 'a-'.

Consequently, we could take a negative rating action if we see economic risks in Finland worsen, as indicated by a further buildup of imbalances, or by unemployment dampening loan growth and leading to asset price corrections, which could weaken asset quality. Bank of Åland's strong capitalization is likely to provide some counterbalance for any further downward pressure on the ratings.

We could revise the outlook to stable if believed that the operating environment in Finland had improved, corresponding to a stabilization of economic risks. We consider a positive rating action as remote over the next 18-24 months.

Rationale

Our ratings on the consolidated Bank of Åland group reflect its 'a-' anchor, and our assessments of the bank's weak business position, strong capital and earnings, moderate risk position, average funding, and adequate liquidity. The bank's stand-alone credit profile (SACP) is 'bbb'.

We do not factor in any extraordinary government support as we see Bank of Åland as having low systemic importance in Finland. This is in addition to our view that we see the likelihood of the Finnish government supporting its banking sector as uncertain following the implementation of the EU Bank Recovery and Resolution Directive on Jan. 1, 2016. Our long-term counterparty credit rating on Bank of Åland is 'BBB'.

Anchor: 'a-' for banks operating in Finland

We use our Bank Industry Country Risk Assessment (BICRA) 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 Finland is 'a-', based on our economic risk score of '2' and our industry risk score of '3'. However, in determining the 'a-' anchor for Bank of Åland, we consider the weighted-average economic risk of all the countries to which the bank is exposed, namely, Finland and Sweden. Under our BICRA methodology, Sweden has similar economic and industry risk scores to Finland.

We view Finland as a competitive and resilient economy with high education levels. However, the country depends on exports by cyclical industries linked to investments, and its economy is subject to sub-par growth due to the fragile recovery in Europe. Moreover, lack of reforms to increase competitiveness could pressure the economy. Low corporate and moderate household debt and a very strong payment culture contribute to sound leverage.

Diverse Nordic banking groups largely control Finland's concentrated banking industry, which in our view is underpinned by robust profitability and stability. Deposits dominate funding, but the sector is a net external debtor, reflecting significant loan growth over the past decade and the country's lack of a deep domestic debt market.

Table 1

Bank of Åland PLC Key Figures					
--Year-ended Dec. 31--					
(Mil. €)	2016*	2015	2014	2013	2012
Adjusted assets	4,705.0	4,592.6	4,284.7	3,877.6	3,626.3
Customer loans (gross)	3,642.6	3,628.8	3,358.7	3,120.5	2,919.3
Adjusted common equity	193.7	193.4	179.6	171.3	168.9
Operating revenues	60.7	124.9	120.6	108.0	96.6
Noninterest expenses	46.0	91.6	96.4	92.0	94.0
Core earnings	9.8	24.3	17.6	8.9	(1.6)

*Data as of June 30.

Business position: Weak, due to concentrated franchise in its home markets

We consider Bank of Åland's business position to be weak, reflecting its concentrated retail private banking franchise in Finland's Åland Islands, and selected growth areas on the Finnish mainland and in Sweden

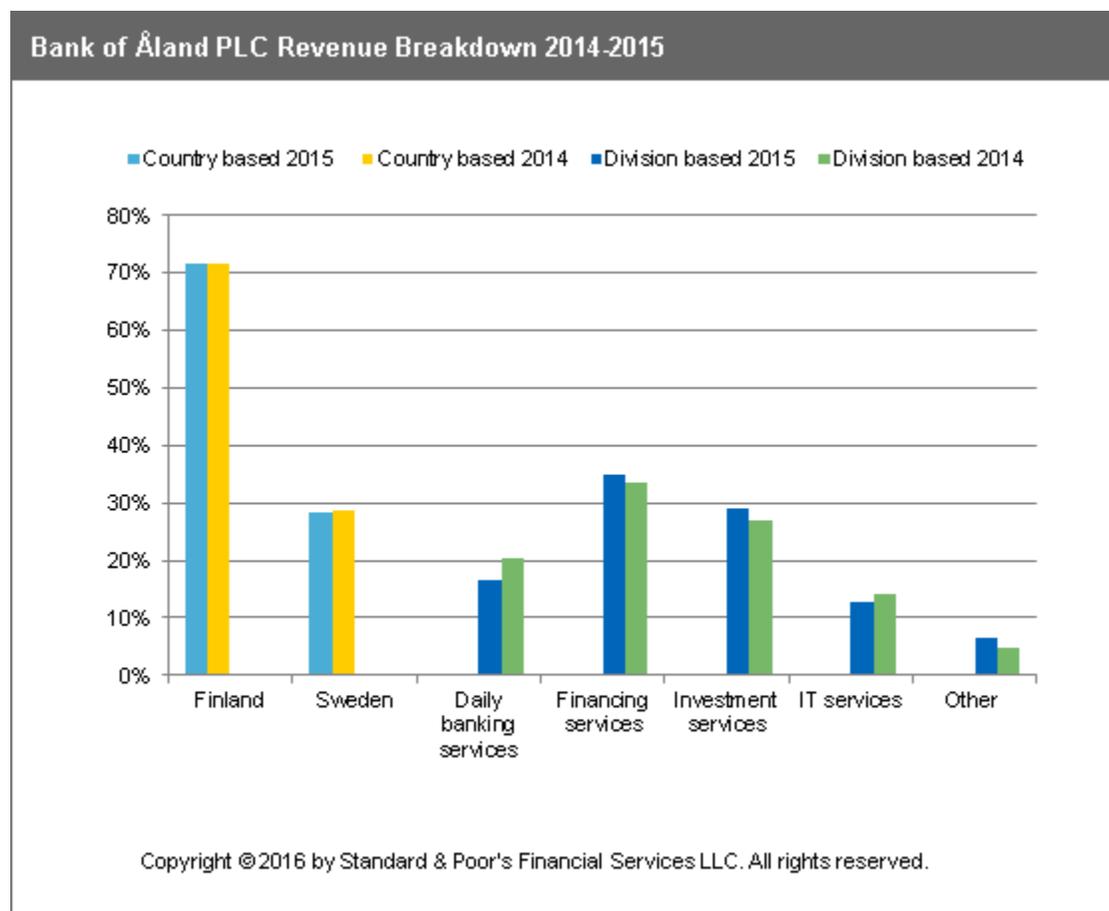
Bank of Åland reported total assets of €4.7 billion (assets under management of €3.8 billion) as of June 30, 2016, and has about 90,000 customers. The bank holds a leading position in its wealthy home region, Finland's Åland Islands, which represents approximately 15% of the bank's revenues. That said, the bank holds only a marginal market share in Finland, a market which is dominated by cooperative banking group and large pan-Nordic banking groups.

The bank focuses on being a specialty provider of retail private banking services, offering both basic and advanced private banking products. Complimenting this are the bank's asset management operations, which have enabled Bank of Åland to service affluent customers in selected regions in Finland since the 1980s and in Sweden since 2009.

Following Bank of Åland's 2009 acquisition of parts of Kaupthing Bank in Sweden, the bank has grown its private banking and asset management activities, which has helped diversify the franchise. In June 2015, the bank merged with Ålandsbanken Asset Management Company to further integrate this business and to improve the bank's efficiency in catering for both Finnish and Swedish clients.

We expect the revenue and profit contribution of the Swedish franchise will continue to increase over time. It represented 28% of revenues and 20% of net operating profit as of year-end 2015, primarily owing to volume growth (see chart 1).

Chart 1



Bank of Åland's main sources of earnings are interest and fee income, and we believe that the bank benefits from a loyal customer base. There is some volatility related to fee-based income, as much of this is driven by asset management and brokerage fees, which tend to be affected by swings in the market.

In terms of segment breakdown, we expect Bank of Åland's private banking operations to remain the main contributor to both revenues and operating profits, followed by retail banking. The bank has also initiated various opportunistic partnerships with financial technology companies, such as Dreams and Trustly, in order to help broaden its distribution channels.

Other non-bank activities that contribute positively to Bank of Åland's profits are the IT company CrossKey, a company that provides banking technology consulting services, and credit card company CompassCard. The bank is likely to remain the sole shareowner of both companies. We believe that CrossKey's relatively higher level of expenses, which have weighed on the bank's overall cost-efficiency metrics, will improve over the coming years.

In our view, management remains focused on a long-term prudent strategy, which is underpinned by a strong local shareholder collective.

Table 2

Bank of Åland PLC Business Position					
	--Year-ended Dec. 31--				
(%)	2016*	2015	2014	2013	2012
Total revenues from business line (currency in millions)	60.7	124.9	120.6	108.0	110.4
Retail banking/total revenues from business line	36.7	47.1	47.3	43.0	41.4
Commercial & retail banking/total revenues from business line	36.7	47.1	47.3	43.0	41.4
Trading and sales income/total revenues from business line	N/A	N/A	2.2	3.3	9.1
Payments and settlements/total revenues from business line	6.4	7.1	7.1	7.5	6.8
Asset management/total revenues from business line	32.6	33.2	29.1	32.6	17.7
Other revenues/total revenues from business line	24.2	12.7	14.3	13.5	25.0
Investment banking/total revenues from business line	N/A	N/A	2.2	3.3	9.1
Return on equity	9.2	11.9	8.6	3.7	6.4

*Data as of June 30. N/A--Not applicable.

Capital and earnings: Strong capitalization, supported by gradually improving earnings

We assess Bank of Åland's capital and earnings as strong, reflecting our expectation that the bank's risk-adjusted capital (RAC) ratio will remain in the range of 13.0%-13.5% over the next 18-24 months.

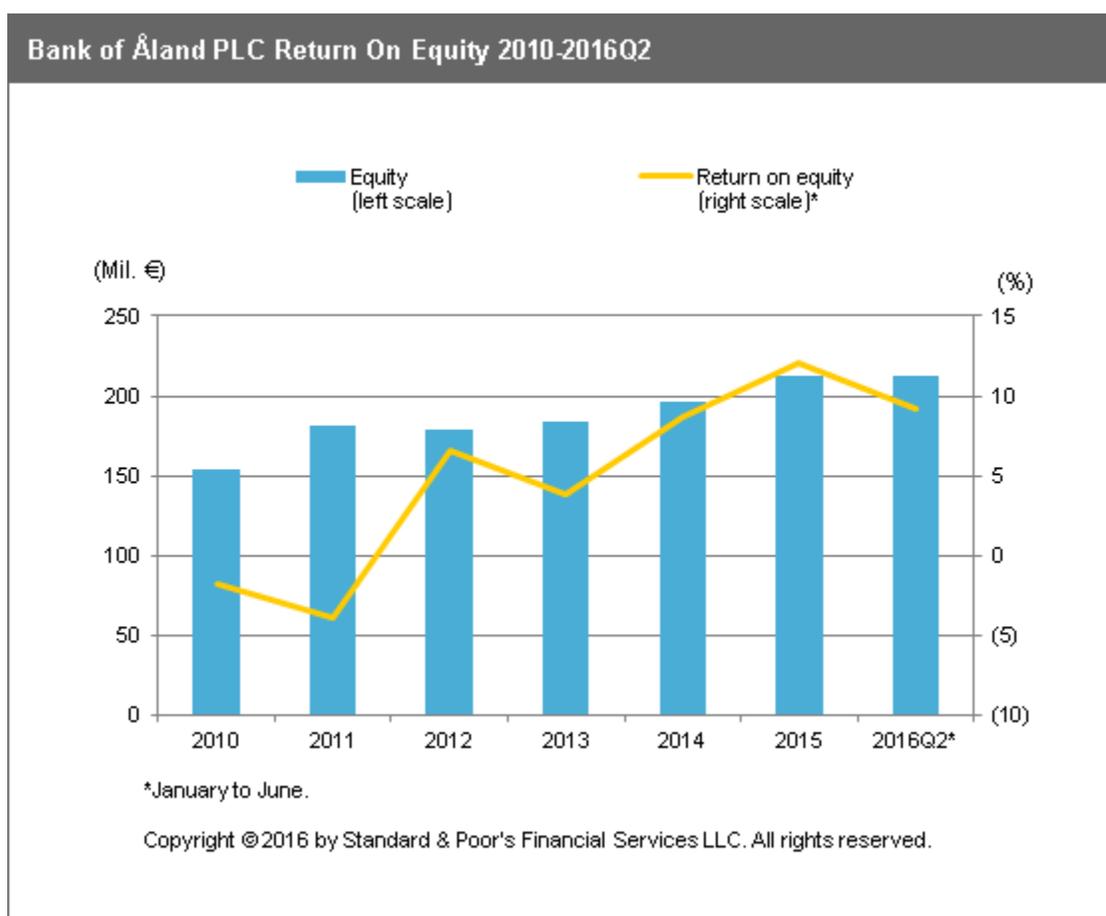
As of Dec. 31, 2015, Bank of Åland's RAC ratio was 13%, an increase from 11.2% at year-end 2014. Total adjusted capital (TAC)--our measure of loss-absorbing capital for banks--was supported by capital build-up through retained earnings in the first nine months, and was also affected by a one-off transaction. Over the course of 2015, Bank of Åland merged with its asset management company, financing the transaction through an increase of shares issued to the employees. This led to a €12 million increase in share capital for the bank's consolidated equity position.

Also included in our TAC measure are €8.603 million of subordinated instruments that include a 25% principal write-down clause, our threshold for classifying the instruments as having intermediate equity content. These

instruments currently represent approximately 4% of the bank's capital base. The remainder of the capital base is composed of common equity, meaning that the quality of capital remains sound.

Our forecast for Bank of Åland's capital level includes an expectation that the bank will maintain a 35%-50% dividend payout ratio. We believe that Bank of Åland's ongoing revenue growth and cost-saving efforts will continue to underpin earnings growth (see chart 2). This is supported by increased loan volumes, as we believe that the bank will maintain an above-average pace of 6%-7% lending growth. The Swedish operations in particular are likely to continue to grow as a share of the loan book, and as a share of the assets under management, which will be positive for Bank of Åland's operating profits over the next 18-24 months.

Chart 2



In the medium term, we anticipate that net interest and net fee income will contribute equal amounts to revenues, as the asset management and private banking services are focus areas for Bank of Åland's strategy. As such, we forecast that the bank will maintain annual net profits of near €30 million for the next two years, translating into a three-year average earnings buffer of 140-145 basis points (bps).

Table 3

Bank of Åland PLC Capital And Earnings					
--Year-ended Dec. 31--					
(%)	2016*	2015	2014	2013	2012
Tier 1 capital ratio	12.4	11.9	10.9	10.8	10.9
S&P RAC ratio before diversification	N.M.	13.0	11.2	10.5	10.7
S&P RAC ratio after diversification	N.M.	11.1	9.7	9.0	9.4
Adjusted common equity/total adjusted capital	95.7	95.7	100.0	100.0	100.0
Net interest income/operating revenues	45.3	43.2	40.9	39.2	42.6
Fee income/operating revenues	36.4	37.2	38.3	39.3	33.9
Market-sensitive income/operating revenues	5.6	6.4	5.6	6.8	7.6
Noninterest expenses/operating revenues	75.8	73.3	80.0	85.2	97.3
Preprovision operating income/average assets	0.6	0.7	0.6	0.4	0.1
Core earnings/average managed assets	0.4	0.5	0.4	0.2	(0.0)

*Data as of June 30. N.M.--Not meaningful.

Table 4

Bank of Åland PLC Risk-Adjusted Capital Framework Data					
(Mil. €)	Exposure*	Basel II RWA	Average Basel II RW (%)	Standard & Poor's RWA	Average Standard & Poor's RW (%)
Credit risk					
Government and central banks	417	0	0	13	3
Institutions	536	106	20	79	15
Corporate	734	541	74	423	58
Retail	3,032	681	22	733	24
Of which mortgage	2,610	549	21	612	23
Securitization§	0	0	0	0	0
Other assets	64	60	93	63	98
Total credit risk	4,783	1,389	29	1,311	27
Market risk					
Equity in the banking book†	3	4	188	24	918
Trading book market risk	--	0	--	0	--
Total market risk	--	4	--	24	--
Insurance risk					
Total insurance risk	--	--	--	0	--
Operational risk					
Total operational risk	--	174	--	223	--
(Mil. €)		Basel II RWA		Standard & Poor's RWA	% of Standard & Poor's RWA
Diversification adjustments					
RWA before diversification		1,582		1,558	100
Total Diversification/Concentration Adjustments		--		265	17

Table 4

Bank of Åland PLC Risk-Adjusted Capital Framework Data (cont.)				
RWA after diversification	1,582		1,823	117
(Mil. €)	Tier 1 capital	Tier 1 ratio (%)	Total adjusted capital	Standard & Poor's RAC ratio (%)
Capital ratio				
Capital ratio before adjustments	188	11.9	202	13.0
Capital ratio after adjustments‡	188	11.9	202	11.1

*Exposure at default. §Securitization exposure includes the securitization tranches deducted from capital in the regulatory framework. †Exposure and Standard & Poor's 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). RWA--Risk-weighted assets. RW--Risk weight. RAC--Risk-adjusted capital. Sources: Company data as of Dec. 31, 2015, Standard & Poor's.

Risk position: Moderate, due to concentration risks in terms of geographic and single-name exposures

We view Bank of Åland's risk position as moderate, reflecting the concentration risks in its loan book.

We expect that the bank will continue to have limited geographic diversity, a limited number of client segments, and some large single-name exposures. We anticipate that the bank's loan portfolio will continue to be retail focused (69% of the gross loan book), while growth in the corporate portfolio will mainly result from collateralized real estate financing in Sweden. Further growth in Sweden is likely to be positive from a diversification perspective, and will be unlikely to lead to an accumulation of high-risk exposures given the bank's prudent underwriting standards and the sound collateralization of these exposures.

A continued reduction in Bank of Åland's shipping finance portfolio will be supportive of the bank's asset quality. This portfolio currently represents about €59 million, that is, less than 2% of total lending. We continue to expect shipping exposures to decline toward €50 million.

We view positively the bank's focus on wealthy individuals and their related corporations, its prudent underwriting standards, and its strategy of engaging mainly in collateralized lending. Moreover, the bank's product offering rests primarily on vanilla retail banking and related asset management products. Furthermore, it has no exposure to European peripheral countries, nor does it use complex financial instruments.

Bank of Åland has managed its loan book well over the recent economic cycle. Over the past few years, the bank has averaged 12 bps annually in loan losses, and while net charge-offs increased in 2015 as a result of a few large exposures, loan losses were below average at 9bps for 2015. We believe that over the coming years, the bank's losses will be near or below an average level of 12-13 bps, which is broadly in line with the Finnish market average. We generally believe that the bank has adequately provisioned for troubled shipping exposures and that new lending in Sweden is prudently underwritten. We therefore expect that losses will remain below our estimated normalized loss level of €10 million over the credit cycle (see chart 3).

Chart 3

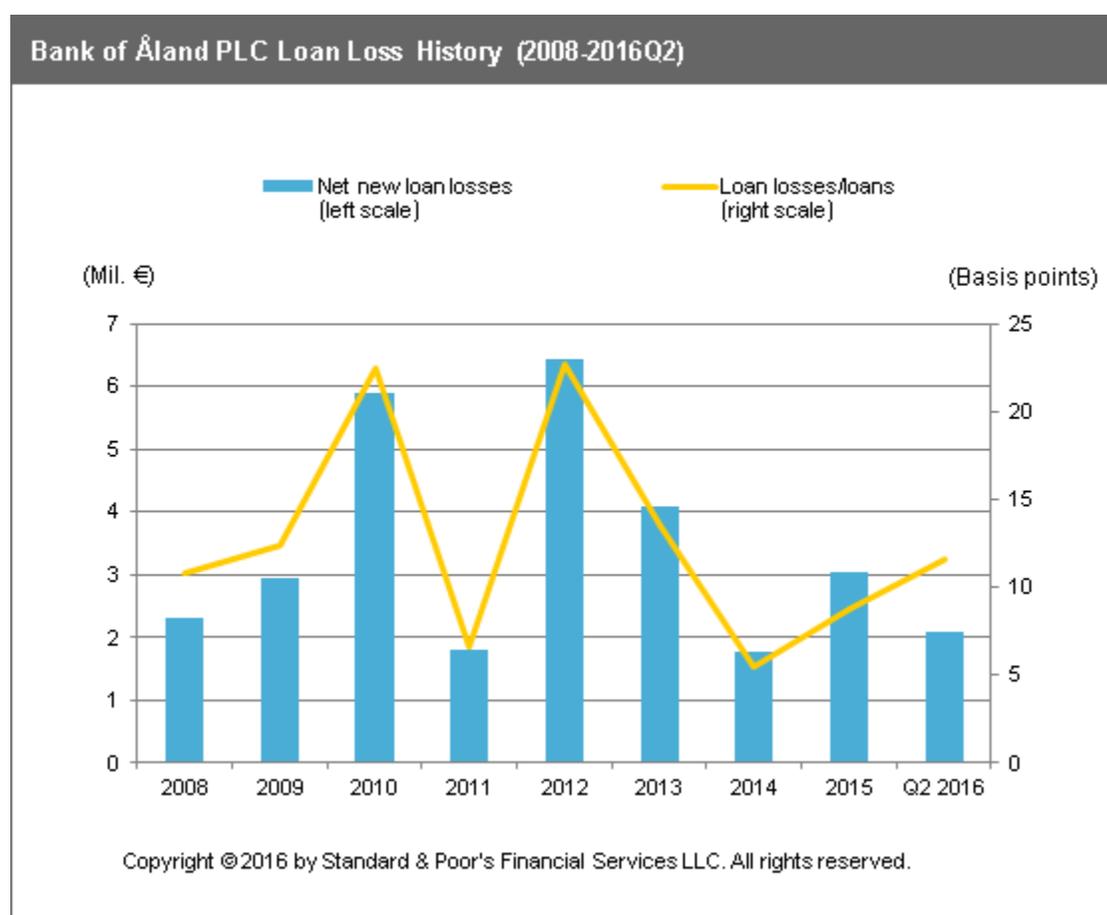


Table 5

Bank of Åland PLC Risk Position

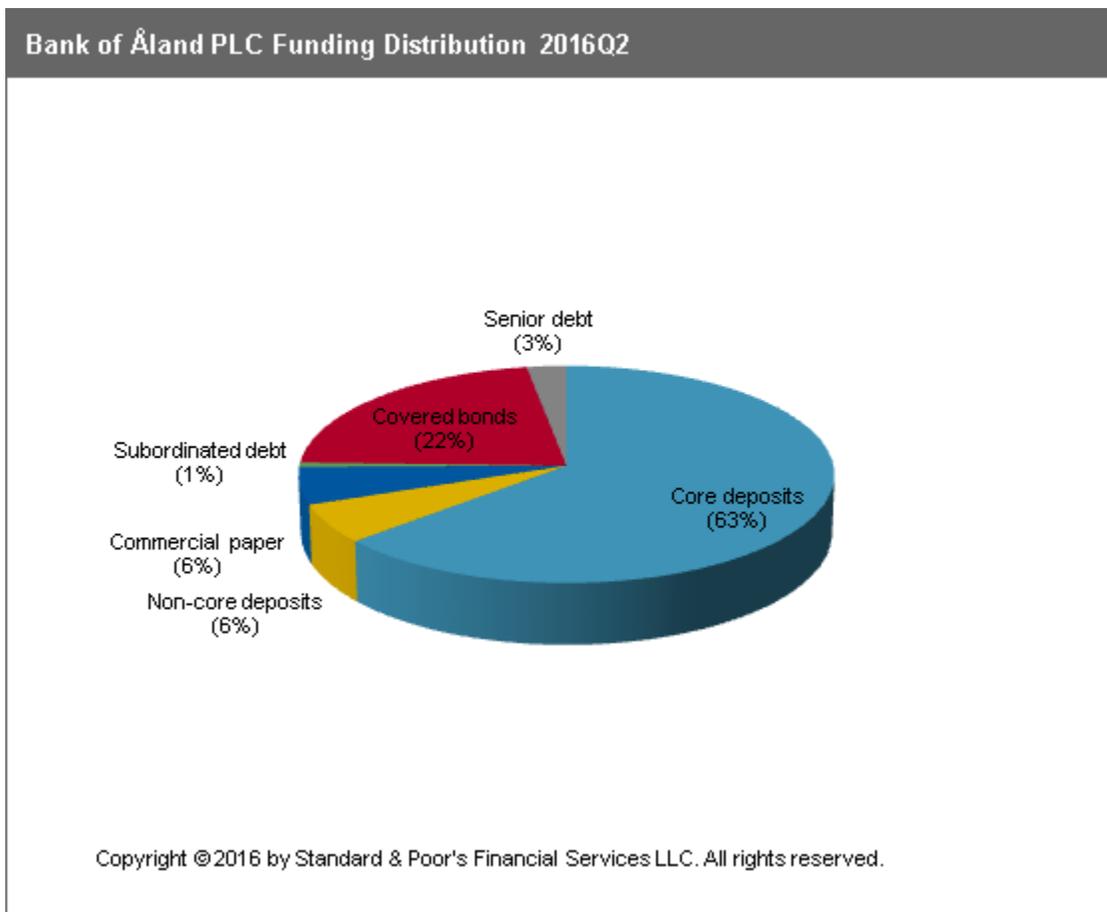
(%)	--Year-ended Dec. 31--				
	2016*	2015	2014	2013	2012
Growth in customer loans	0.8	8.0	7.6	6.9	6.3
Total diversification adjustment / S&P RWA before diversification	N.M.	17.0	15.6	16.1	14.3
Total managed assets/adjusted common equity (x)	24.4	23.8	23.9	22.7	21.5
New loan loss provisions/average customer loans	0.1	0.1	0.1	0.1	0.2
Net charge-offs/average customer loans	0.0	0.2	0.1	0.1	0.1
Gross nonperforming assets/customer loans + other real estate owned	0.9	1.1	0.9	0.5	0.6
Loan loss reserves/gross nonperforming assets	43.9	28.8	53.8	105.4	73.7

*Data as of June 30. N.M.--Not meaningful.

Funding and liquidity: Average, owing to stable customer deposit base

Bank of Åland's funding is average in our opinion, owing to a stable and granular core customer deposit base covering 64% of the bank's funding needs, and a fairly balanced stable funding ratio of 106% as of June 30, 2016. The customer deposits are not significantly concentrated, and we expect them to remain a stable source of funding.

To aid lending growth, the bank has been using a larger share of wholesale funding (see chart 4), which is now predominantly made up of covered bonds since the bank launched a covered bond program in the second half of 2012. The covered bond program has been using primarily Finnish covered mortgage pools as collateral and has successively added issuance using Swedish covered pools since they were first introduced in 2014. The average maturity of Bank of Åland's funding profile is approximately 3.3 years, which the bank is likely to maintain as it continues to expand its investor base beyond Finland and Sweden.

Chart 4

We assess the Bank of Åland's liquidity as adequate, reflecting a ratio of broad liquid assets to short-term wholesale funding of 1.3x as of year-end 2015. This ratio indicates the bank's approximate one-year liquidity and is somewhat volatile given maturing long-term funding and changes in assets held with other banks.

Bank of Åland has gradually increased its liquidity reserve to approximately €905 billion as of June 30, 2016. This consists of cash and securities, which all are eligible for repurchase agreement transactions at the Finnish or Swedish central banks. We anticipate that Bank of Åland's liquidity will improve over the next 18-24 months. The bank's metrics are slightly weaker than those of its Nordic peers, but upcoming regulatory coverage requirements will compel further improvement.

Table 6

Bank of Åland PLC Funding And Liquidity					
	--Year-ended Dec. 31--				
(%)	2016*	2015	2014	2013	2012
Core deposits/funding base	63.5	58.7	55.2	60.4	64.0
Customer loans (net)/customer deposits	131.0	143.7	151.9	142.6	136.6
Long term funding ratio	89.0	87.3	79.6	82.0	84.1
Stable funding ratio	105.7	101.6	92.1	92.6	93.6
Short-term wholesale funding/funding base	11.5	13.4	21.4	18.9	16.7
Broad liquid assets/short-term wholesale funding (x)	1.7	1.3	0.8	0.8	0.9
Net broad liquid assets/short-term customer deposits	12.5	6.5	(8.0)	(6.7)	(3.6)
Short-term wholesale funding/total wholesale funding	31.4	32.3	47.8	47.6	46.4
Narrow liquid assets/three-month wholesale funding (x)	2.5	1.9	1.4	1.4	1.6

*Data as of June 30.

External support: No notches of uplift to the SACP

We do not factor any external support into our assessment of Bank of Åland. We believe the prospect of extraordinary government support for Finnish banks is uncertain, following the full implementation of the EU Bank Recovery and Resolution Directive, including bail-in powers.

In addition, we assess the Bank of Åland as having low systemic importance in Finland, given the marginal market share of customer loans and deposits in Finland, and since the Finnish authorities have not identified Bank of Åland as being subject to a well-defined bail-in process. Consequently, we do not include support from additional loss absorbing capacity into the long-term rating on Bank of Åland.

Additional rating factors: none

No additional factors affect this rating.

Related Criteria And Research

Related Criteria

- Banks: Bank Hybrid Capital And Nondeferrable Subordinated Debt Methodology And Assumptions, Jan. 29, 2015
- General Criteria: Group Rating Methodology, Nov. 19, 2013
- Banks: Quantitative Metrics For Rating Banks Globally: Methodology And Assumptions, July 17, 2013
- Banks: Revised Market Risk Charges For Banks In Our Risk-Adjusted Capital Framework, June 22, 2012
- Banks: Rating Methodology And Assumptions, Nov. 9, 2011
- Banking Industry Country Risk Assessment Methodology And Assumptions, Nov. 9, 2011
- Bank Capital Methodology And Assumptions, Dec. 6, 2010
- Use Of CreditWatch And Outlooks, Sept. 14, 2009
- Banks: Commercial Paper I: Banks - March 23, 2004

Related Research

- Nordic Banks' Capital Growth Tapers Off, Aug. 2, 2016
- Ratings On Bank of Åland's Category FIN Covered Bonds Affirmed At 'AAA' Following Review, June 16, 2016

- Ratings On Finland-Based Bank of Åland's Category SWE Covered Bonds Affirmed At 'AAA' Following Review, April 25, 2016
- Banking Industry Country Risk Assessment: Finland, Jan. 25, 2016

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 August 17, 2016)

Bank of Åland PLC

Counterparty Credit Rating

BBB/Negative/A-3

Senior Secured

AAA

Senior Secured

AAA/Stable

Counterparty Credit Ratings History

20-Nov-2012

BBB/Negative/A-3

10-Aug-2012

BBB/Stable/A-3

Sovereign Rating

Finland (Republic of)

AA+/Negative/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.

Additional Contact:

Financial Institutions Ratings Europe; FIG_Europe@spglobal.com

Copyright © 2016 by S&P Global Market Intelligence, a division of S&P Global Inc. All rights reserved.

No content (including ratings, credit-related analyses and data, valuations, model, software or other application or output therefrom) or any part thereof (Content) may be modified, reverse engineered, reproduced or distributed in any form by any means, or stored in a database or retrieval system, without the prior written permission of Standard & Poor's Financial Services LLC or its affiliates (collectively, S&P). The Content shall not be used for any unlawful or unauthorized purposes. S&P and any third-party providers, as well as their directors, officers, shareholders, employees or agents (collectively S&P Parties) do not guarantee the accuracy, completeness, timeliness or availability of the Content. S&P Parties are not responsible for any errors or omissions (negligent or otherwise), regardless of the cause, for the results obtained from the use of the Content, or for the security or maintenance of any data input by the user. The Content is provided on an "as is" basis. S&P PARTIES DISCLAIM ANY AND ALL EXPRESS OR IMPLIED WARRANTIES, INCLUDING, BUT NOT LIMITED TO, ANY WARRANTIES OF MERCHANTABILITY OR FITNESS FOR A PARTICULAR PURPOSE OR USE, FREEDOM FROM BUGS, SOFTWARE ERRORS OR DEFECTS, THAT THE CONTENT'S FUNCTIONING WILL BE UNINTERRUPTED, OR THAT THE CONTENT WILL OPERATE WITH ANY SOFTWARE OR HARDWARE CONFIGURATION. In no event shall S&P Parties be liable to any party for any direct, indirect, incidental, exemplary, compensatory, punitive, special or consequential damages, costs, expenses, legal fees, or losses (including, without limitation, lost income or lost profits and opportunity costs or losses caused by negligence) in connection with any use of the Content even if advised of the possibility of such damages.

Credit-related and other analyses, including ratings, and statements in the Content are statements of opinion as of the date they are expressed and not statements of fact. S&P's opinions, analyses, and rating acknowledgment decisions (described below) are not recommendations to purchase, hold, or sell any securities or to make any investment decisions, and do not address the suitability of any security. S&P assumes no obligation to update the Content following publication in any form or format. The Content should not be relied on and is not a substitute for the skill, judgment and experience of the user, its management, employees, advisors and/or clients when making investment and other business decisions. S&P does not act as a fiduciary or an investment advisor except where registered as such. While S&P has obtained information from sources it believes to be reliable, S&P does not perform an audit and undertakes no duty of due diligence or independent verification of any information it receives.

To the extent that regulatory authorities allow a rating agency to acknowledge in one jurisdiction a rating issued in another jurisdiction for certain regulatory purposes, S&P reserves the right to assign, withdraw, or suspend such acknowledgement at any time and in its sole discretion. S&P Parties disclaim any duty whatsoever arising out of the assignment, withdrawal, or suspension of an acknowledgment as well as any liability for any damage alleged to have been suffered on account thereof.

S&P keeps certain activities of its business units separate from each other in order to preserve the independence and objectivity of their respective activities. As a result, certain business units of S&P may have information that is not available to other S&P business units. S&P has established policies and procedures to maintain the confidentiality of certain nonpublic information received in connection with each analytical process.

S&P may receive compensation for its ratings and certain analyses, normally from issuers or underwriters of securities or from obligors. S&P reserves the right to disseminate its opinions and analyses. S&P's public ratings and analyses are made available on its Web sites, www.standardandpoors.com (free of charge), and www.ratingsdirect.com and www.globalcreditportal.com (subscription) and www.spcapitaliq.com (subscription) and may be distributed through other means, including via S&P publications and third-party redistributors. Additional information about our ratings fees is available at www.standardandpoors.com/usratingsfees.

STANDARD & POOR'S, S&P and RATINGSDIRECT are registered trademarks of Standard & Poor's Financial Services LLC.