

Research

Bank of Aland PLC

Primary Credit Analyst:

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

Secondary Contact:

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

Table Of Contents

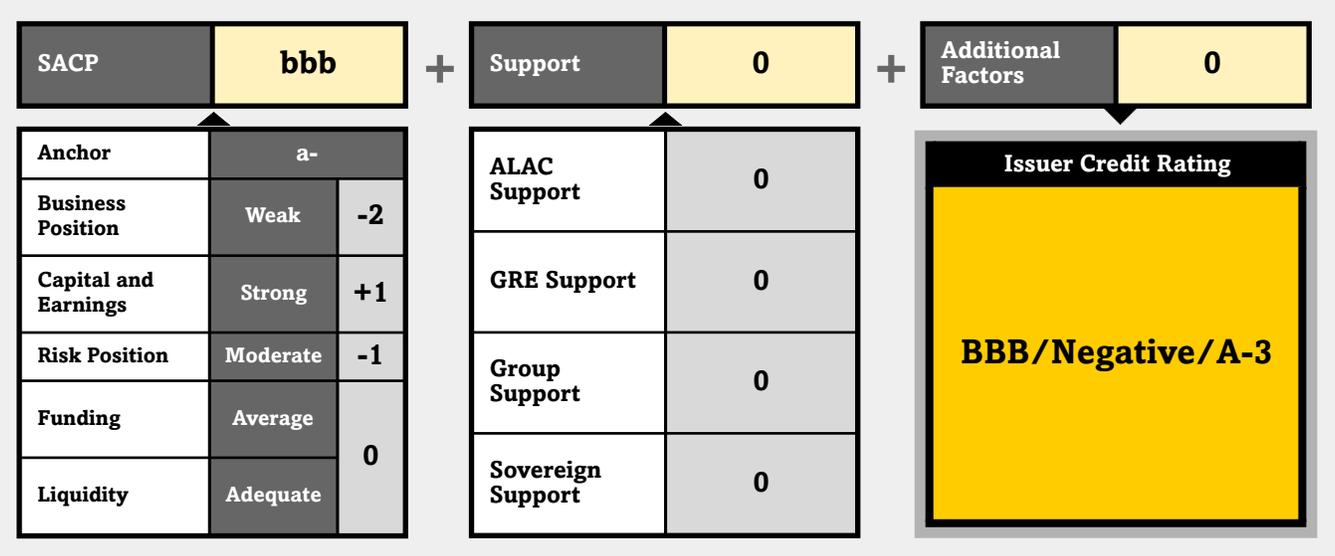
Major Rating Factors

Outlook

Rationale

Related Criteria And Research

Bank of Aland 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

Standard & Poor's Ratings Services' outlook on Finland-based Bank of Åland is negative, reflecting our view that Finland's weak economic recovery could hamper the banking sector's performance over the next two years, which could have a negative impact on Finnish banks, including Bank of Åland. This could lead us to lower our anchor on Finnish banks, including Bank of Åland, to 'bbb+' from 'a-'.

As such, we could take a negative rating action if we see economic risks in Finland worsen, as indicated by a further buildup of imbalances or where increases in unemployment dampen loan growth and lead to asset price corrections, which could potentially impact asset quality. Bank of Aland'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 we believed that the operating environment in Finland had improved, corresponding to a stabilization of economic risks. Bank of Aland has increased its geographical scope of revenue and lending, and while we consider a positive rating action remote, we see this as a constructive development for the bank.

Rationale

Our ratings on Bank of Åland reflect its 'a-' anchor, and our assessments of its "weak" business position, "strong" capital and earnings, "moderate" risk position, "average" funding, and "adequate" liquidity, as our criteria define these terms. The stand-alone credit profile (SACP) is 'bbb'.

We consider Bank of Åland as having "low" systemic importance and consequently factor no potential extraordinary government support into the ratings. Our long-term counterparty credit rating on Bank of Åland is 'BBB'.

Anchor: 'a-' reflecting operations in Finland and Sweden

Our criteria 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'. The 'a-' anchor for Bank of Åland draws on our BICRA methodology and our view of the weighted-average economic risk in countries the bank is exposed to, namely Finland (70% of exposures at default (EaD) and Sweden (30% of EaD).

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 levels, 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. €)	2015*	2014	2013	2012	2011
Adjusted assets	4,490.0	4,284.7	3,877.6	3,626.3	3,389.0
Customer loans (gross)	3,542.3	3,358.7	3,120.5	2,919.3	2,745.8
Adjusted common equity	191.2	179.6	171.3	168.9	158.4
Operating revenues	92.4	120.6	108.0	96.6	100.0
Noninterest expenses	66.8	96.4	92.0	94.0	97.4
Core earnings	19.0	17.6	8.9	(1.6)	(0.2)

*Data as of Sept. 30. N.A.--Not available. N/A--Not applicable. N.M.--Not meaningful.

Business position: Weak due to concentrated franchise in home markets

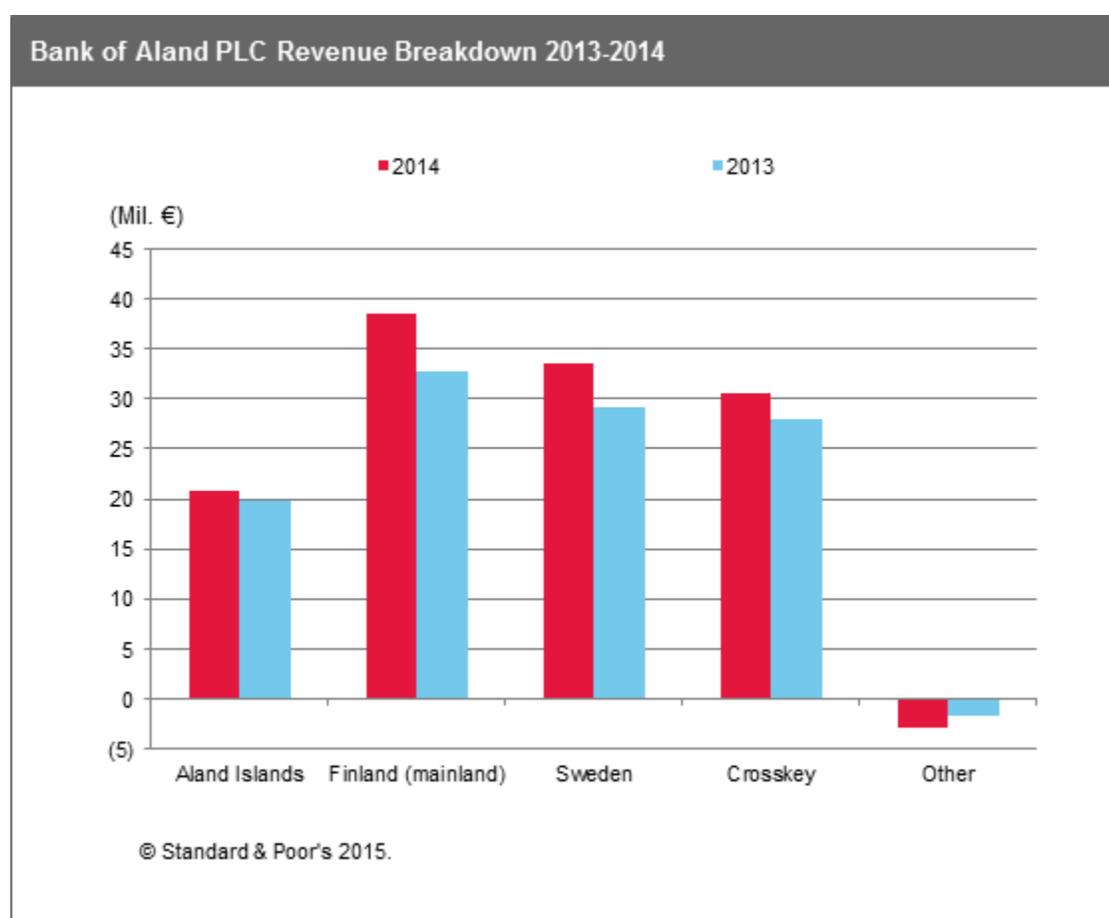
We consider Bank of Åland's business position to be "weak," reflecting its materially concentrated retail bank franchise in Åland Islands, Finland, and its niche position in the Swedish market.

Bank of Åland, with reported total assets of €4.5 billion and assets under management of €3.7 billion as of Sept. 30, 2015, and about 85,000 customers, holds a leading position in its wealthy home region, Finland's Åland Islands. The

bank is a niche provider of retail private banking, offering both basic and advanced private banking services. When coupled with asset management operations, this has enabled Bank of Åland to service affluent customers in selected regions in Finland since the 1980s and in Sweden since 2009. We positively note that these customer relationships appear to be long-standing, providing stability to Bank of Åland's franchise. Following the 2009 acquisition of parts of Kaupthing Bank in Sweden, the bank has grown in both private banking and asset management activities, which has helped diversify the franchise. In June 2015, Alandsbanken Asset Management Company was merged with the bank to further integrate the business and to improve the 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 34% of revenues and 17% of net operating profit as of year-end 2014, primarily owing to volume growth (see chart 1).

Chart 1



Bank of Åland's main sources of earnings are interest and fee income (about 40% of operating revenues each), and we believe 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 tends to be affected by moves in the market. By business segment the private banking operations are expected to remain the main contributor to both revenues and operating profits (38% of revenues and 63% of net operating profit in first nine months 2015) followed by retail banking

(26% and 14%, respectively).

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 (IT-segment: 22% of revenues and 13% of net operating profit in first nine months 2015), and credit card company CompassCard. The bank is likely to remain the sole shareowner of both companies.

In our view, management remains focused on a long-term prudent strategy, which is underpinned by a strong local shareholder collective. We expect the bank to improve its overall efficiency metrics over the coming years which we note are distorted by the non-banking activities with comparatively higher level of expenses.

Table 2

Bank of Åland PLC Business Position					
	--Year-ended Dec. 31--				
(%)	2015*	2014	2013	2012	2011
Total revenues from business line (currency in millions)	92.4	120.6	108.0	110.4	99.2
Retail banking/total revenues from business line	71.0	47.3	43.0	41.4	26.0
Commercial & retail banking/total revenues from business line	71.0	47.3	43.0	41.4	26.0
Trading and sales income/total revenues from business line	N/A	2.2	3.3	9.1	1.9
Payments and settlements/total revenues from business line	N/A	7.1	7.5	6.8	5.3
Asset management/total revenues from business line	7.5	29.1	32.6	17.7	35.4
Other revenues/total revenues from business line	21.5	14.3	13.5	25.0	31.4
Investment banking/total revenues from business line	N/A	2.2	3.3	9.1	1.9
Return on equity	12.6	8.6	3.7	6.4	-3.9

*Data as of Sept. 30 in line with new segment reporting. N.A.--Not available. N/A--Not applicable. N.M.--Not meaningful.

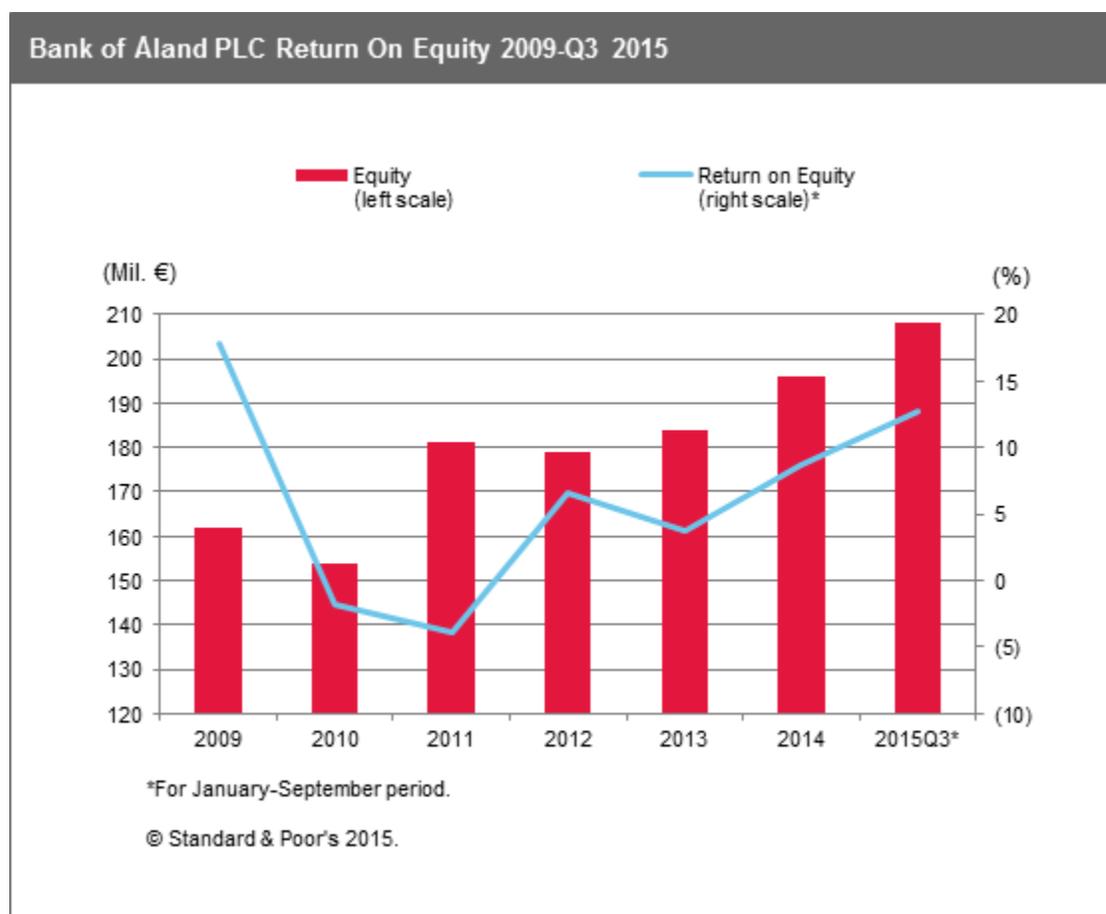
Capital and earnings: Strong capitalization supported by gradually improving earnings

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 12.0%-12.5% over the next 18-24 months.

As of June 30, 2015, Bank of Åland's RAC ratio was 12.3%, which marks an increase from the 11.2% level at year-end 2014. The total adjusted capital, our measure of loss-absorbing capital for banks was supported by the capital build-up through retained earnings in the first nine months but also impacted by one-offs. With the merger of Bank of Åland's asset management company, the bank's consolidated equity position posted a €12 million increase in share capital but the net effect was negative €1.3 million. Furthermore, in May, Bank of Åland issued €8.6 million subordinated instruments that include a 25% write-down clause, which is the threshold for "intermediate" equity content. As such, they qualify for "intermediate equity" treatment and are included in our TAC measure for the bank according to our criteria, representing approximately 4% of the bank's capital base. The remainder of the capital base is composed of common equity, meaning that 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 translate into positive earnings growth (see chart 2). This is underpinned by increased loan volumes, where we believe the bank will maintain an above-average pace of 6%-7% lending growth. The Swedish operations in particular are likely to

growth as a share of the loan book, and in addition to increases in assets under management, will be positive for profits in 2016-2017.

Chart 2

In the medium term, we anticipate net interest and net fee income have a balanced share of revenues, as the asset management and private banking services are focus areas for Bank of Åland's strategy. Furthermore, we anticipate Swedish operations will continue to grow in both lending and assets under management and therefore contribute positively to profits from over the coming 18-24 months.

Table 3

Bank of Åland PLC Capital And Earnings

	--Year-ended Dec. 31--				
(%)	2015*	2014	2013	2012	2011
Tier 1 capital ratio	11.9	10.9	10.8	10.9	8.4
S&P RAC ratio before diversification	12.3	11.2	10.5	10.7	11.0
S&P RAC ratio after diversification	10.5	9.7	9.0	9.4	9.6
Adjusted common equity/total adjusted capital	95.7	100.0	100.0	100.0	100.0
Net interest income/operating revenues	42.4	40.9	39.2	42.6	43.1
Fee income/operating revenues	38.2	38.3	39.3	33.9	38.7

Table 3

Bank of Åland PLC Capital And Earnings (cont.)					
Market-sensitive income/operating revenues	6.0	5.6	6.8	7.6	2.0
Noninterest expenses/operating revenues	72.3	80.0	85.2	97.3	97.4
Provision operating income/average assets	0.8	0.6	0.4	0.1	0.1
Core earnings/average managed assets	0.6	0.4	0.2	0.0	0.0

*Data as of Sept. 30. N.A.--Not available. N/A--Not applicable. N.M.--Not meaningful.

Risk position: Moderate due to concentration risks, both 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 the bank will continue to have limited geographic diversity, a limited number of client segments, and some large single exposures. We anticipate that the bank's loan portfolio will continue to be retail focused (66% of the loan portfolio), while the 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 unlikely lead to an accumulation of high-risk exposures. Continued reduction in Bank of Åland's shipping finance portfolio will be supportive of asset quality, which currently is about €63 million, i.e., less than 2% of total lending, and is expected to decline over time 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. The bank has averaged approximately 12 bps annually in loan-losses over the past eight years, which is better than the Finnish market average. We expect annual loan losses will be about 5-10 bps, as we believe the bank has adequately provisioned for troubled shipping exposures and that new lending in Sweden is prudently underwritten. We therefore expect losses will remain well below our estimated normalized loss level of €10 million over the credit cycle (see chart 3).

Chart 3

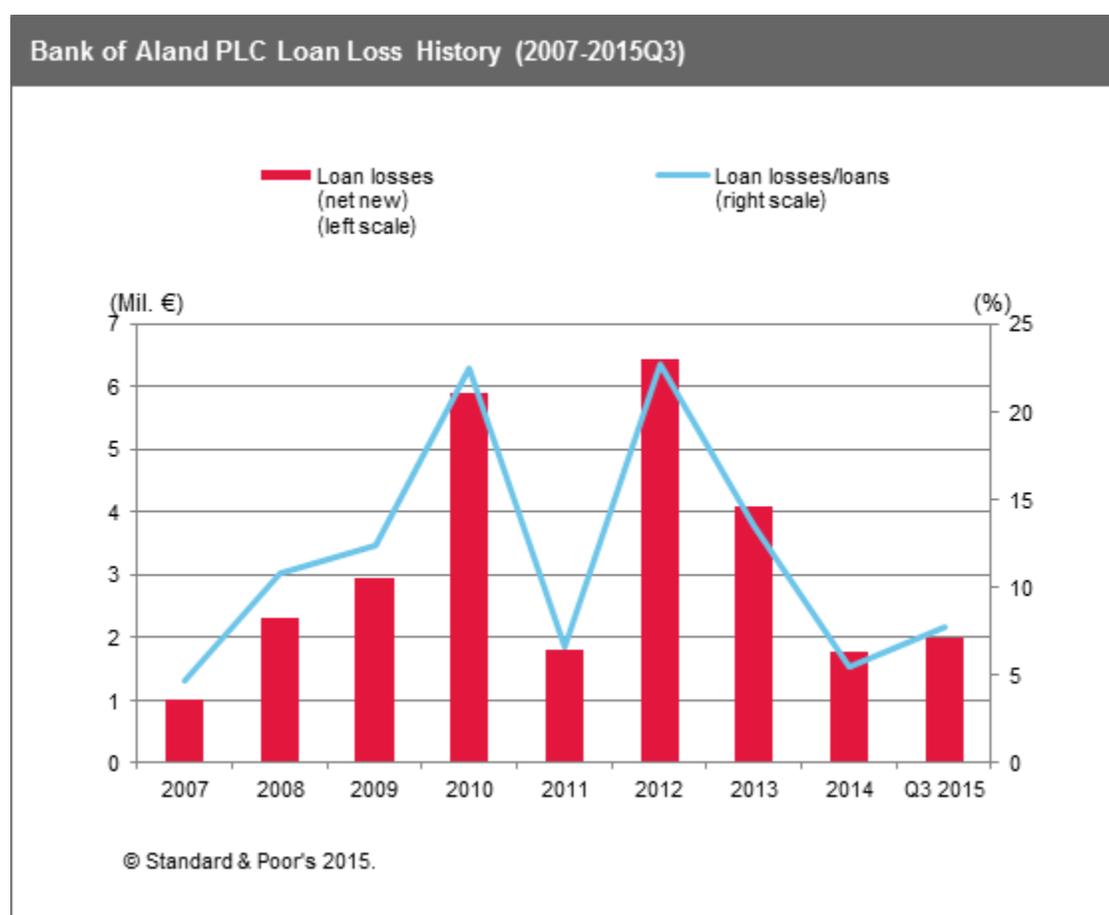


Table 5

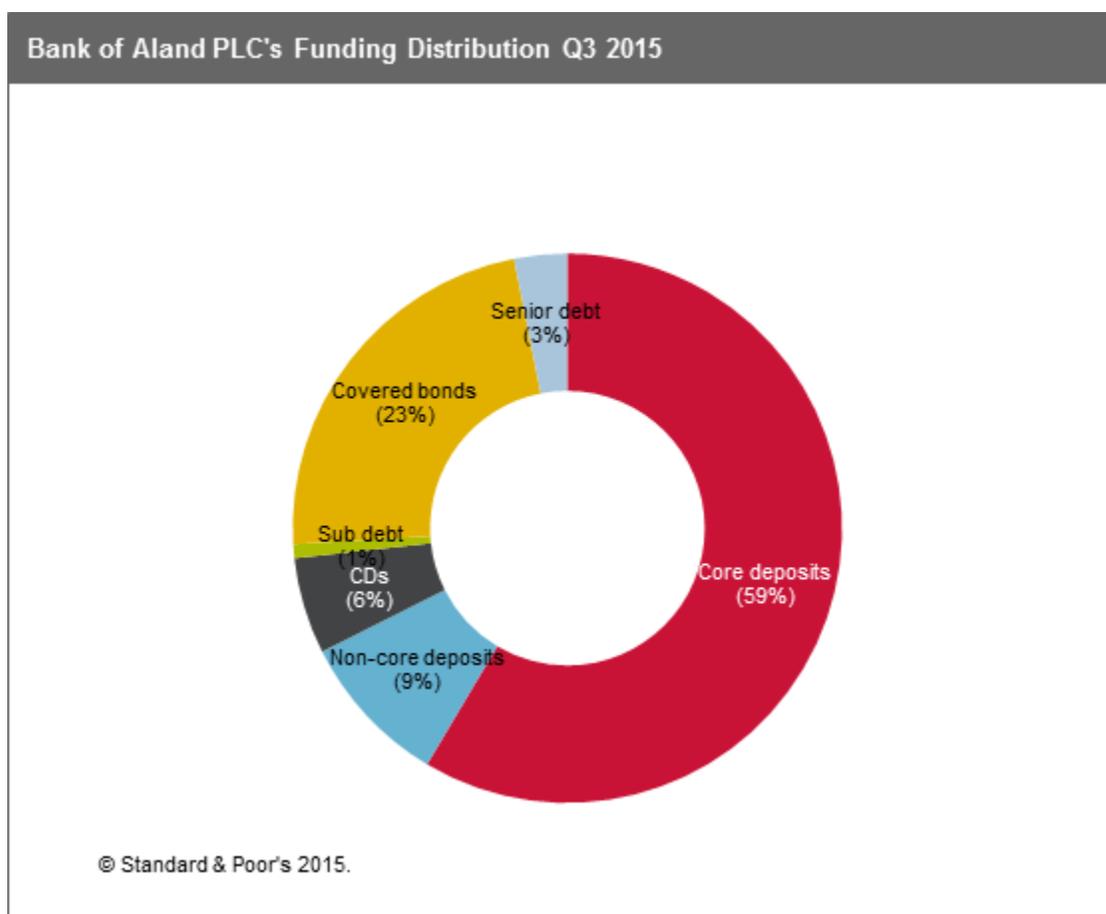
Bank of Åland PLC Risk Position					
	--Year-ended Dec. 31--				
(%)	2015*	2014	2013	2012	2011
Growth in customer loans	7.3	7.6	6.9	6.3	2.3
Total diversification adjustment / S&P RWA before diversification	17.31	15.6	16.1	14.3	14.7
Total managed assets/adjusted common equity (x)	23.5	23.9	22.7	21.5	21.5
New loan loss provisions/average customer loans	0.1	0.1	0.1	0.2	0.1
Net charge-offs/average customer loans	0.3	0.1	0.1	0.1	0.0
Gross nonperforming assets/customer loans + other real estate owned	1.4	0.9	0.5	0.6	0.7
Loan loss reserves/gross nonperforming assets	22.3	53.8	105.4	73.7	45.7

*Data as of Sept. 30. RWA--Risk-weighted assets. 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 59% of the bank's funding needs and a fairly balanced stable funding ratio of 92% as of Sept. 30, 2015. 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 3.5 years, which is likely to be maintained or lengthened as the bank 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 (BLAST) of 0.8x as of Sept. 30, 2015. The ratio indicates the bank's approximate one-year liquidity and is somewhat volatile given maturing long-term funding and changes in asset position held with other banks. Bank of Åland has gradually increased its liquidity reserve to approximately €675 billion as of Sept. 30, 2015. This consists of cash and securities, which all are eligible for repurchase agreement transactions at the Finnish or Swedish central bank. We anticipate that Bank of Åland's liquidity will improve over the next 18-24 months. The bank's metrics are slightly weaker than other Nordic peers, but upcoming regulatory coverage requirements will compel further improvement.

Table 6

Bank of Aland PLC Funding And Liquidity					
	--Year-ended Dec. 31--				
(%)	2015*	2014	2013	2012	2011
Core deposits/funding base	58.5	55.2	60.4	64.0	69.4
Customer loans (net)/customer deposits	144.8	151.9	142.6	136.6	127.5
Long term funding ratio	81.4	79.6	82.0	84.1	76.5
Stable funding ratio	92.0	92.1	92.6	93.6	85.3
Short-term wholesale funding/funding base	19.5	21.4	18.9	16.7	24.7
Broad liquid assets/short-term wholesale funding (x)	0.8	0.8	0.8	0.9	0.6
Net broad liquid assets/short-term customer deposits	(7.7)	(8.0)	(6.7)	(3.6)	(14.2)
Short-term wholesale funding/total wholesale funding	46.9	47.8	47.6	46.4	80.9
Narrow liquid assets/3-month wholesale funding (x)	1.4	1.4	1.4	1.6	1.3

*Data as of Sept. 30.

External support: No notches of uplift to the stand-alone credit profile

We consider Bank of Åland to have "low" systemic importance due to the marginal market share on customer loans and deposits in Finland, and we consequently do not factor any extraordinary government support into the ratings.

Additional rating factors:none

No additional factors affect this rating

Related Criteria And Research

Related Criteria

- Use Of CreditWatch And Outlooks, Sept. 14, 2009
- Bank Capital Methodology And Assumptions, Dec. 6, 2010
- Banks: Methodology For Mapping Short- And Long-Term Issuer Credit Ratings For Banks, May 4, 2010
- Banks: Rating Methodology And Assumptions, Nov. 9, 2011
- Banking Industry Country Risk Assessment Methodology And Assumptions, Nov. 9, 2011
- Banks: Revised Market Risk Charges For Banks In Our Risk-Adjusted Capital Framework, June 22, 2012
- Banks: Quantitative Metrics For Rating Banks Globally: Methodology And Assumptions, July 17, 2013
- Banks: Bank Hybrid Capital And Nondeferrable Subordinated Debt Methodology And Assumptions, Jan. 29, 2015
- Quantitative Metrics For Rating Banks Globally: Methodology And Assumptions, July 17, 2013

Related Research

- Nordic Banks Extend Their Capital Advantage Despite Lower Revenues, Nov. 27, 2015
- Transaction Update: Bank of Aland PLC (Category FIN Mortgage Covered Bonds), Aug. 27, 2015
- Ratings On Finland-Based Bank of Aland's Category FIN Covered Bonds Raised To 'AAA' On New Criteria; Outlook Stable, May 5, 2015
- Ratings On Finland-Based Bank of Aland's Category SWE Covered Bonds Raised To 'AAA' On New Criteria; Outlook Stable, April 22, 2015
- Nordic Banks Face Credit Pressures From Bail-In Regulations And Economic Risks, March 9, 2015
- Banking Industry Country Risk Assessment: Finland, Jan. 3, 2015

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 December 21, 2015)

Bank of Aland 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. Standard & Poor's credit ratings on the global scale are comparable across countries. Standard & Poor's 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@standardandpoors.com

Copyright © 2015 by Standard & Poor's Financial Services LLC (S&P), a subsidiary of The McGraw-Hill Companies, Inc. All rights reserved.

No content (including ratings, credit-related analyses and data, 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 S&P. The Content shall not be used for any unlawful or unauthorized purposes. S&P, its affiliates, 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, 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) in connection with any use of the Content even if advised of the possibility of such damages.

Credit-related analyses, including ratings, and statements in the Content are statements of opinion as of the date they are expressed and not statements of fact or recommendations to purchase, hold, or sell any securities or to make any investment decisions. 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's opinions and analyses do not address the suitability of any security. S&P does not act as a fiduciary or an investment advisor. 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.

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 non-public information received in connection with each analytical process.

S&P may receive compensation for its ratings and certain credit-related 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 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.