FitchRatings

RATING ACTION COMMENTARY

Fitch Upgrades Permanent TSB Group to 'BBB-'; Outlook Stable

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Fitch Ratings - Frankfurt am Main - 29 Feb 2024: Fitch Ratings has upgraded Permanent TSB Group Holdings plc's (PTSBGH) Long-Term Issuer Default Rating (IDR) to 'BBB-' from 'BB+' and Viability Rating (VR) to 'bbb-' from 'bb+'. The Long-Term IDR of the group's operating subsidiary, Permanent TSB plc (PTSB), has been upgraded to 'BBB' from 'BBB-'. The Outlooks on the Long-Term IDRs are Stable. A full list of rating actions is below.

The upgrade reflects Fitch's view of the improved operating environment for Irish banks and PTSBGH's strengthened credit profile. Our assessment of the operating environment incorporates our view of the banking sector's improved fundamentals and our expectation that sustained robust domestic economic growth and significantly reduced household indebtedness will support banks' performance.

PTSBGH's business and financial profiles have strengthened following the acquisition of assets from an exiting bank that have provided significant scale and revenue benefits. We also expect recent structural improvement in asset quality and profitability to be sustained.

KEY RATING DRIVERS

Small Irish Mortgage Lender: PTSBGH's ratings reflect its small domestic franchise, which lacks the scale and breadth of the two dominant larger Irish banks, and its simple but undiversified business model that is concentrated on a small market. The ratings also reflect the bank's moderate risk profile and asset quality, satisfactory capitalisation, improved profitability, and a stable but undiversified funding profile underpinned by a granular and stable deposit base.

Simple, Concentrated Business Model: PTSBGH is Ireland's third-largest commercial bank, although its asset base considerably trails that of its two large domestic peers. It operates exclusively in its home market, with a strategy that is focused on retail banking and a product offering dominated by mortgage loans and savings. Residential mortgage loans accounted for about 95% of the bank's total gross loans at end-June 2023.

Risk Profile Moderate; Execution Risk: Fitch expects PTSBGH to maintain a conservative risk appetite, given its focus on low-risk residential mortgage lending in Ireland. Planned growth in SME lending and asset finance poses some risk in the medium term due to the bank's more limited record in these segments. However, we expect the risks will be contained and should not result in a material change in the bank's risk profile as growth will be fairly modest overall and highly granular, while SME lending will be mostly secured on property.

Average Credit Quality: The bank's impaired loan ratio was stable at 3.2% at end-June 2023, and was in line with that of domestic peers. We expect some near-term asset quality weakening due to the lagged impact of higher rates and lingering macroeconomic uncertainty. However, deterioration is likely to be modest and moderate loan growth should keep the ratio close to 3% over the next 24 months.

Adequate Profitability: Profitability improved considerably in 1H23, as we had expected, benefitting from a significantly larger asset and revenue base and higher net interest margin due to more favourable asset yields and deposit margins. We expect the operating profit to be sustained above 1% of risk-weighted assets (RWAs; 1H23: 1.5%) from end-2023.

Satisfactory Capitalisation, Improved Capital Generation: Our view of capitalisation considers PTSBGH's satisfactory buffers above regulatory minimum requirements, its moderate risk profile, and improved internal capital generation. Its fully loaded common equity Tier 1 (CET1) ratio of 14.4% at end-June 2023 was above its long-term target minimum of around 14%.

Stable Deposit Funding: Stable and granular retail deposits form the bulk of PTSBGH's funding (about 83% at end-June 2023), underpinning Fitch's assessment of the bank's stable funding and satisfactory liquidity. Wholesale funding is limited to building resolution buffers but is more sensitive to investor confidence and more expensive than at larger Irish peers.

Holdco VR Equalised with Opco: Fitch assesses the group on a consolidated basis. PTSBGH acts as the holding company of the Permanent TSB group and the issuing entity to meet the group's minimum requirements for own funds and eligible liabilities (MREL). PTSBGH's VR is aligned with that of PTSB, to reflect the absence of material double leverage at the holding company and prudent liquidity management.

RATING SENSITIVITIES

Factors that Could, Individually or Collectively, Lead to Negative Rating Action/Downgrade

We believe the VRs have strong headroom at the new rating level. However, a downgrade could be triggered by a severe and prolonged deterioration of the operating environment for banks in Ireland, affecting borrowers' repayment capacity and weakening PTSBGH's business and financial profiles.

A downgrade could also be triggered by a sharp and sustained increase in the impaired loan ratio above 4%. This may result from sustained high levels of growth in non-mortgage lending and would lead to a reassessment of the group's risk profile. This would pressure profitability and capitalisation through higher impairment charges and lower internal capital generation and a downgrade would also require the operating profit to fall and be sustained below 1% of RWAs and the CET1 ratio to be maintained below 14%.

PTSBGH's VR would also be downgraded if the holding company's double leverage is sustained above 120%, which we do not expect.

Factors that Could, Individually or Collectively, Lead to Positive Rating Action/Upgrade

An upgrade would require successful execution of the growth strategy over a sustained period without a significant increase in problem loans, as reflected in an impaired loan ratio sustained below 3%, while maintaining its moderate risk profile and satisfactory capitalisation with the CET1 ratio above 14%.

An upgrade could also result from improved profitability, as reflected in the operating profit rising close to 2% of RWAs on a sustained basis, and a stronger business profile as reflected in greater earnings diversification, while maintaining its market share of residential mortgage lending.

OTHER DEBT AND ISSUER RATINGS: KEY RATING DRIVERS

PTSB's Long-Term IDR is notched up once from the VR to reflect additional protection to external senior creditors afforded by internal MREL debt buffers. These buffers are underpinned by the group's strategy to fulfil MREL exclusively with holding company senior unsecured and more junior debt. Under the group's single-point-of-entry resolution strategy, senior debt issued at the holding level is channeled to PTSB and statutorily subordinated to external senior creditors. We expect the buffer to remain large and sustainable. Our expectation is based on PTSB's need to maintain compliance with its MREL of 28.1% (including the combined buffer requirement) of RWAs from 1 January 2024.

PTSBGH's and PTSB's Short-Term IDRs of 'F3' are mapped to their Long-Term IDRs of 'BBB-' and 'BBB', respectively.

The long-term ratings for PTSBGH's and PTSB's EUR15 billion euro note issuance programme are aligned with their respective Long-Term IDRs. This is because we believe default on senior unsecured obligations from the programme would equate to a default of the issuers themselves and we expect recoveries to be average.

No Sovereign Support Assumed: PTSBGH's and PTSB's Government Support Ratings (GSR) of 'no support' reflect Fitch's view that senior creditors cannot rely on extraordinary support from the Irish authorities in the event that the group becomes non-viable. In our opinion, the EU's Bank Recovery and Resolution Directive and Single Resolution Mechanism provide a framework that is likely to require senior creditors to participate in losses for resolving the bank.

OTHER DEBT AND ISSUER RATINGS: RATING SENSITIVITIES

The Short-Term IDRs are sensitive to changes in the issuers' respective Long-Term IDRs.

The long-term ratings on the euro note issuance programme are sensitive to changes in the issuers' respective Long-Term IDRs.

An upgrade of the GSRs would be contingent on a positive change in the sovereign's propensity to support its banks. While not impossible, this is highly unlikely, in Fitch's view.

VR ADJUSTMENTS

The operating environment score of 'a-' is below the 'aa' category implied score due to the following adjustment reasons: size and structure of economy (negative) and reported and future metrics (negative).

The asset quality score of 'bbb-' is above the 'bb' category implied score due to the following adjustment reason: historical and future metrics (positive).

The earnings and profitability score of 'bbb-' is above the 'bb' category implied score due to the following adjustment reason: historical and future metrics (positive).

The capitalisation & leverage score of 'bbb' is below the 'a' category implied score due to the following adjustment reason: risk profile and business model (negative).

The funding & liquidity score of 'bbb' is below the 'a' category implied score due to the following adjustment reason: non-deposit funding (negative).

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

ESG CONSIDERATIONS

The highest level of ESG credit relevance is a score of '3', unless otherwise disclosed in this section. A score of '3' means ESG issues are credit neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. Fitch's ESG Relevance Scores are not inputs in the rating process; they are an observation on the relevance and materiality of ESG factors in the rating decision. For more information on Fitch's ESG Relevance Scores, visit https://www.fitchratings.com/topics/esg/products#esg-relevance-scores.

RATING ACTIONS

ENTITY / DEBT	RATING			PRIOR
Permanent TSB plc	LT IDR	BBB Rating Outlook Stable	Upgrade	BBB- Rating Outlook Positive
	ST IDR	F3	Affirmed	F3
	Viability	bbb-	Upgrade	bb+

	Government Support	ns	Affirmed		ns
senior unsecured	LT	BBB	Upgrade		BBB-
Permanent TSB Group Holdings plc	LT IDR	BBB- Rating Outlook Stable	Upgrade		BB+ Rating Outlook Positive
	ST IDR	F3	Upgrade		B
	Viability	bbb-	Upgrade		bb+
	Government Support	ns	Affirmed		ns
senior unsecured	LT	BBB-	Upgrade		BB+

VIEW ADDITIONAL RATING DETAILS

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APPLICABLE CRITERIA

Bank Rating Criteria (pub. 01 Sep 2023) (including rating assumption sensitivity)

ADDITIONAL DISCLOSURES

Dodd-Frank Rating Information Disclosure Form

Solicitation Status

Endorsement Policy

ENDORSEMENT STATUS

Permanent TSB Group Holdings plc	EU Issued, UK Endorsed
Permanent TSB plc	EU Issued, UK Endorsed

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