

Rating Action: Moody's downgrades Irish bank ratings

Global Credit Research - 18 Apr 2011

No impact on stand-alone financial strength ratings

London, 18 April 2011 -- Moody's Investors Service has today downgraded the ratings of several Irish banks following Moody's rating action on the Irish government's bond ratings which have been downgraded by two notches to Baa3 with a negative outlook from Baa1. Today's bank rating actions are:

- Moody's has downgraded by two notches the long-term bank deposit ratings of Allied Irish Banks (Allied Irish), Bank of Ireland (BoI), EBS Building Society (EBS) and Irish Life & Permanent (IL&P), and that of ICS Building Society (ICS) by one notch. BoI and ICS are now rated Ba1. Allied Irish, EBS and IL&P are now rated Ba2. The short-term bank deposit rating at these five institutions has been downgraded to Not-Prime, from P-2 for BoI and from P-3 for the other four institutions.
- Moody's has downgraded by one notch the unguaranteed senior unsecured debt ratings of Allied Irish, EBS and IL&P to Ba3 and BoI to Ba2.
- The outlook on the long-term bank deposit and unguaranteed senior unsecured debt ratings of these institutions is negative, in line with the outlooks on the government rating and on the stand-alone ratings of the banks.
- This action concludes the review on these ratings initiated on February 11, 2011.
- Moody's has also downgraded to Baa3 the debt guaranteed under the Irish government's Eligible Liabilities Scheme. This refers to the government-backed senior debt of five institutions -- Allied Irish, Anglo Irish, BoI, EBS and IL&P.

RATINGS RATIONALE

The rating actions announced today are best understood as: (i) the reduction in the level of systemic support embedded in our deposit ratings following the downgrade of the sovereign rating; and (ii) the removal of systemic support from the unguaranteed senior unsecured debt ratings meaning that these are now placed at the same level as the stand-alone ratings of the banks.

RATIONALE FOR THE DOWNGRADE OF BANK DEPOSIT RATINGS

The bank deposit ratings of Allied Irish, BoI, EBS, ICS and IL&P have been downgraded following the two-notch downgrade of the Irish government bond rating. At Ba1/N-P (for BoI and ICS) and Ba2/N-P (for Allied Irish, EBS and IL&P) these ratings continue to incorporate one notch of rating uplift from the banks' stand-alone ratings, reflecting the explicit support received by the institutions and Moody's expectation that further support for the deposits would likely be forthcoming in the event of need. This is based on the supportive attitude of the Irish government towards depositors as witnessed recently by the transfer orders to sell the deposits of Anglo Irish Bank and Irish Nationwide Building Society to Allied Irish and IL&P. The Ba1 bank deposit rating of ICS is now at the same level as that of its parent BoI. This reflects that, given the high level of integration of ICS in BoI and Moody's view that a sale of the institution is now less certain, it is unlikely that the government would differentiate support between deposits at the two institutions.

RATIONALE FOR THE REMOVAL OF SYSTEMIC SUPPORT FROM THE UNGUARANTEED SENIOR UNSECURED DEBT RATINGS

The new Irish government has already committed to supporting the banking system in its capital requirements following the announcement of the PCAR stress tests (Prudential Capital Assessment Review) and the PLAR (Prudential Liquidity Assessment Review) restructuring and deleveraging process (see "Moody's comments on Irish Banks following announcement of new capital requirements; no impact on senior ratings", 1 April 2011). However, Moody's believes that there is a high level of uncertainty around whether the government would extend further support to the banking sector if required (beyond the EUR35 billion that has been committed to as part of the EU/IMF support package). As a result, Moody's is no longer incorporating any systemic support in the unguaranteed senior unsecured debt ratings of the domestic Irish banks and these are now placed at the same level as the stand-alone ratings of the banks. However the unguaranteed senior unsecured debt ratings are not positioned below the stand-alone ratings as we do not see any imminent risk of distressed exchanges or specific unguaranteed senior unsecured debt burden sharing legislation for the "going concern" banks. In the event that the risk for unguaranteed senior unsecured debt was to increase then the banks' unguaranteed senior unsecured debt ratings would likely face further multi-notch downgrades.

NO IMPACT ON STAND-ALONE BFSRS

There are no rating implications for the standalone bank financial strength ratings (BFSRs) of the banks because (i) the overall losses incorporated into the capital requirements for the four institutions are in line with those that Moody's has been using in its own scenario analysis (the overall three-year provision charge of EUR27.7 billion compares to Moody's expected losses of approximately EUR32 billion); and (ii) the four banks' standalone ratings -- D for BoI, mapping to Ba2 on the long-term scale and D- for AIB, EBS and IL&P, mapping to Ba3 -- already incorporate a significant recapitalisation of up to EUR35 billion in total made available under the EU/IMF support package.

Furthermore, the BFSRs continue to reflect: (i) the banks' significant short-term funding pressures which have led to the high reliance on external funding; and (ii) the uncertain operating environment meaning that asset quality and earnings are likely to remain extremely weak. In addition, Moody's considers that the deleveraging process could further exacerbate asset quality and earnings pressures.

No deadline has been provided by which the PCAR capital requirement must be raised and Moody's assumes that the capital will be injected in the near future. However, if the capital is not forthcoming for any reason, then the BFSRs would likely come under downward pressure.

A key factor in any future upward pressure on BFSRs will be whether the measures outlined in the PCAR and PLAR process can now begin to restore confidence in the Irish banking system. However, for the foreseeable future, Moody's expects that the banks will continue to face funding difficulties; therefore the ongoing liquidity support from the Eurosystem remains vital. Moody's considers that the announcement by the ECB

that it will now accept all debt instruments backed by the Irish government as collateral against ECB loans as a credit positive for the banking sector.

ANGLO IRISH AND IRISH NATIONWIDE BUILDING SOCIETY

Neither Anglo Irish Bank Corporation (Anglo Irish) nor Irish Nationwide Building Society (INBS) were included in the PCAR and PLAR process (both banks are rated Caa1 on review for possible downgrade/Not-Prime for senior debt and bank deposits with BFSRs of E, mapping to Caa1 on the long term scale).

Moody's understands that a further assessment of the capital requirements for Anglo Irish and INBS will be completed in May and as a result, the Caa1 unguaranteed senior unsecured debt ratings and long-term bank deposit ratings remain on review for possible downgrade. Moody's aims to complete its review of these ratings shortly after this process is completed. The review continues to focus on the new government's stance towards senior creditors, and the remaining depositors of the two institutions, including the remaining deposits. If the risk increases that senior creditors will be forced to bear losses, the ratings would likely face further downgrades.

GOVERNMENT GUARANTEED DEBT

In line with the sovereign rating action, Moody's has downgraded to Baa3 (negative outlook) from Baa1 the government-backed senior debt of AIB, Anglo Irish, BoI, EBS and IL&P which have each issued public debt under the Eligible Liabilities Guarantee scheme (see "Moody's downgrades Ireland to Baa3 from Baa1; outlook remains negative", 15 April 2011). The assigned government-backed Baa3 ratings are based on the unconditional and irrevocable guarantee from the Irish government (see "Moody's to assign backed-Aa1/Prime-1 ratings to debt securities covered by the Irish government's new guarantee", 7 January 2010).

The principal methodologies used in this rating were Bank Financial Strength Ratings: Global Methodology published in February 2007, and Incorporation of Joint-Default Analysis into Moody's Bank Ratings: A Refined Methodology published in March 2007.

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