

Research Update:

Bank of Ireland Ratings Lowered To 'A-/A-2' On Economic And Market Conditions In Ireland; Outlook Stable

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Overview

- We have revised our opinion regarding economic and industry risk in Ireland and our expectations regarding future credit losses.
- We have also assessed the likely impact of participation in Ireland's National Asset Management Agency (and associated restructuring on Bank of Ireland (BOI)).
- We are lowering our counterparty credit ratings on BOI to 'A-/A-2', and removing them from CreditWatch negative.
- The stable outlook reflects our expectation that the government will remain highly supportive of BOI, BOI's core Irish banking franchise will remain materially intact, and it will raise significant equity capital in 2010, from the market or the government or both.

Rating Action

On Jan. 26, 2010, Standard & Poor's Ratings Services lowered its long- and short-term counterparty credit ratings on Bank of Ireland (BOI; the trading name of the Governor and Company of the Bank of Ireland) to 'A-/A-2' from 'A/A-1'. At the same time, the long- and short-term counterparty credit ratings were removed from CreditWatch, where they were placed with negative implications on May 1, 2009, and Sept. 30, 2009, respectively. The outlook is stable. Issuance guaranteed by the Republic of Ireland (AA/Negative/A-1+) is not affected by today's rating action.

Rationale

The rating action reflects our opinion of BOI's prospects in light of our updated view on economic and industry risk in the bank's core markets, together with our expectations regarding future credit losses. It also factors in our view of the likely impact of its participation in Ireland's National Asset Management Agency (NAMA) and associated restructuring and capital raising. We have lowered the ratings due to our view that the environment will remain challenging over the medium term and BOI's financial profile will be weaker than we had previously expected, with capital expected to be only adequate by our measures and the bank continuing to make losses through 2011.

The ratings on BOI reflect its very strong domestic franchise, high systemic importance, and the consequent strong support that we expect it to continue to receive from the Irish government. We factor four notches of support into the ratings on BOI above its stand-alone credit profile (SACP). With total

reported assets of €184 billion (\$267 billion) at Sept. 30, 2009, BOI ranks alongside its main competitor, Allied Irish Banks PLC (AIB; A-/Negative/A-2) as the leading player in Irish banking.

BOI is set to benefit materially from the government's NAMA plan, which, from February 2010, will see BOI transfer up to €16 billion of its higher risk property- and construction-related loan exposures in exchange for a smaller amount of government-backed bonds. We expect this move to reduce uncertainty about future credit losses and improve BOI's liquidity. However, it will likely also trigger substantial realized losses, impairing capital. We expect that BOI will subsequently raise equity capital. Potential sources include liability management exercises, existing shareholders, and the Irish government.

Despite loan book risk reduction and capital raising, the bank's medium-term prospects are, in our view, rather weak. We expect economic and market conditions in Ireland and, to a lesser extent, the U.K. to remain unsupportive of bank earnings, leading to continued margin pressure, weak client activity, and still-elevated credit losses on non-NAMA loans through 2011. We consider it likely that the bank will continue to be loss-making through this period.

Due to its receipt of state aid, BOI has had to submit a restructuring plan to the EC, demonstrating a return to viability within a reasonable timeframe. The EC may or may not choose to impose conditions as part of its approval of this plan. While the EC's stance remains uncertain, we think it likely that BOI's core Irish banking franchise will remain materially intact. BOI has already announced that, at the EC's request, it intends to exercise its right to defer coupon payments on those capital instruments where there is no legal obligation to pay.

Outlook

The stable outlook reflects our expectation that the government will remain highly supportive of BOI. We also expect that BOI's SACP will gradually strengthen over the long term, supported in particular by a largely unchanged business profile.

We consider that the likelihood of positive rating action is remote within the rating horizon. Such a move could, however, result from a materially improved economic and industry risk environment in Ireland, including a more rapid and stronger improvement in macroeconomic and market conditions than we currently expect. Negative rating action would most likely follow from a weakening of government support, or a fundamental weakening in BOI's core Irish banking franchise, or a failure to materially bolster capital in 2010.

Related Research

- Assumptions For Credit Stress Testing Irish Banks, Jan. 26, 2010
- Determining Credit Loss Assumptions For Irish Banks, Jan. 26, 2010

- Review Of Irish Banks On Implementation Of Credit Loss Assumptions And BICRA Change Leads To Rating Actions, Jan. 26, 2010
- Irish BICRA Changed To Group 4 From Group 3 On Higher Economic And Industry Risk, Jan. 26, 2010
- Ratings On Bank of Ireland's Hybrid Issues Lowered To 'CC' On Deferral Announcement, Jan. 19, 2010
- Group Methodology For Financial Services Companies, March 19, 2004
- FI Criteria: Bank Rating Analysis Methodology Profile, March 18, 2004

Ratings List

Downgraded; CreditWatch/Outlook Action

	To	From
Bank of Ireland		
Counterparty Credit Rating	A-/Stable/A-2	A/Watch Neg/A-1
Senior Unsecured	A-	A/Watch Neg
Subordinated	BBB+	A-/Watch Neg
Commercial Paper	A-2	A-1/Watch Neg

NB: This list does not include all ratings affected.

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