

Rating Action: Moody's affirms Hamburg Commercial Bank's ratings and changes the outlook to positive from stable

14 Dec 2020

Frankfurt am Main, December 14, 2020 -- Moody's Investors Service (Moody's) has today affirmed Hamburg Commercial Bank AG (HCOB)'s Baa2 long-term senior unsecured debt, issuer and deposit ratings and changed the outlook on these to positive from stable. At the same time, the rating agency affirmed HCOB's ba2 Baseline Credit Assessment (BCA) and Adjusted BCA.

Today's rating affirmations with a positive outlook reflects Moody's assessment of the progress made by HCOB towards establishing itself as a profitable member of the German private banks' deposit guarantee scheme with the target of achieving full membership by year-end 2021. Strongly rising capitalization, in particular, has improved the prospects of HCOB sustainably improving its financial profile.

Ratings of HCOB's affiliates, including those that benefit from a public law guarantee and funding vehicles were unaffected by today's rating action.

A full list of affected ratings and rating inputs can be found at the end of this press release.

RATINGS RATIONALE

-- AFFIRMATION OF HCOB'S BASELINE CREDIT ASSESSMENT

The affirmation of HCOB's ba2 BCA reflects that the bank has been on track towards meeting its overall transformation plan which foresees a drastic deleveraging of its balance sheet, significant strengthening of its capitalisation and asset quality as well as an improved risk-return profile of its assets.

The bank's financial strength is underpinned by a very strong Tangible Common Equity ratio which Moody's believes will comfortably exceed 20% of risk-weighted assets by year-end 2020, and by strong leverage metrics. Whereas Moody's expects the bank's capitalisation to consolidate somewhat from its exceptionally strong current level when benchmarked with domestic peers, capital will remain a key strength of the bank's solvency.

Whereas HCOB has yet to establish a track record of sustained profit generation, progress in reducing operating and funding costs has improved its capacity to absorb the industry-wide pressure on net interest income, HCOB's dominant source of revenues.

HCOB's asset risk profile is marked by the bank's focus on higher yielding loans, predominantly asset-based lending activities, in particular to commercial real estate (CRE) and shipping finance. The rating agency considers these to be generally more exposed to cyclical risks. Consequently, HCOB's nonperforming loan ratio, that has been around 2-3% more recently can be vulnerable to increases from concentrated exposure risks to these areas. Moody's continues to view concentration risk as a key vulnerability for HCOB and the very high focus on asset-based finance is a key constraint for HCOB's BCA. Moody's reflects this in a negative qualitative adjustment due to HCOB's quasi monoline business model.

-- AFFIRMATION OF HCOB'S SENIOR UNSECURED DEBT AND DEPOSIT RATINGS

The affirmation of HCOB's ratings reflects the affirmation of its BCA and Adjusted BCA, unchanged results from Moody's Advanced Loss Given Failure (LGF) analysis and unchanged results from the rating agency's assumption for government support.

The rating agency's Advanced LGF analysis results in three notches of uplift for deposits and senior unsecured debt for HCOB, based on an extremely low loss-given-failure. For junior senior unsecured debt instruments, a very low loss-given-failure results in two notches of uplift from HCOB's ba2 Adjusted BCA, based on the rating agency's expectation that during 2021 HCOB's continued deleveraging will raise the share of liabilities ranking below junior senior unsecured debt within the bank's funding mix.

Because Moody's considers HCOB an institution with limited systemic relevance, the rating agency assumes a

low probability of government support, resulting in no additional uplift to the bank's ratings.

-- OUTLOOK CHANGE TO POSITIVE FROM STABLE

The outlook change to positive reflects management's achievements over the past years of strengthening the bank's financial profile, in particular its solvency and the possibility of a one notch upgrade of the bank's BCA in case of continued improvement of HCOB's creditworthiness. It further reflects Moody's expectation that the bank's liability structure does not change in a way that it would indicate a higher loss-given-failure than presently.

On the basis of its improving capitalisation and cost structures, Moody's believes a successful transition of HCOB from the public banks' institutional protection scheme towards the private banks' voluntary deposit guarantee fund is likely and not overly challenged by the pandemic. A full membership in the private banks' deposit guarantee fund would have a positive signaling effect and further support the bank's efforts to diversify and lengthen its funding structure.

FACTORS THAT COULD LEAD TO AN UPGRADE OR DOWNGRADE OF THE RATINGS

HCOB's Baa2 long-term senior unsecured debt and deposit ratings may be upgraded in case of an upgrade of its ba2 BCA; HCOB's senior unsecured debt and deposit rating classes already benefit from the maximum achievable uplift of three notches under Moody's Advanced LGF analysis.

An upgrade of HCOB's BCA would be subject to the establishment of a track record of sustainable profit generation without incurring significant renewed asset risks, the maintenance of strong capitalisation despite economic friction, the bank's ability to maintain an ample buffer of liquid resources, or a successful diversification of the bank's funding profile if this results in lower dependence on market funding, or a combination of these.

HCOB's Baa2 long-term senior unsecured debt and deposit ratings could be downgraded if the bank's BCA is downgraded or if the transformation of its liability structure leads to a less favourable outcome under Moody's Advanced LGF analysis.

A downgrade of HCOB's BCA could result from a pronounced negative deviation of HCOB's future financial performance from the solvency and liquidity metrics that Moody's currently expects. In particular, underperformance within HCOB's cyclical exposures to CRE and shipping loans, or a failure of HCOB to execute its transition plan for its funding profile may result in a BCA downgrade.

Based on Moody's Advanced LGF analysis, in particular, the bank's junior senior unsecured debt ratings could be downgraded if the temporarily reduced share of lower-ranking liabilities is not replenished within the context of the bank's planned deleveraging and liability and capital structure transformation.

LIST OF AFFECTED RATINGS

Issuer: Hamburg Commercial Bank AG

..Affirmations:

....Long-term Counterparty Risk Ratings, affirmed Baa2

....Short-term Counterparty Risk Ratings, affirmed P-2

....Long-term Bank Deposits, affirmed Baa2, outlook changed to Positive from Stable

....Short-term Bank Deposits, affirmed P-2

....Long-term Counterparty Risk Assessment, affirmed Baa2(cr)

....Short-term Counterparty Risk Assessment, affirmed P-2(cr)

....Long-term Issuer Ratings, affirmed Baa2, outlook changed to Positive from Stable

....Short-term Issuer Ratings, affirmed P-2

....Baseline Credit Assessment, affirmed ba2

...Adjusted Baseline Credit Assessment, affirmed ba2

...Senior Unsecured Regular Bond/Debenture, affirmed Baa2, outlook changed to Positive from Stable

...Senior Unsecured Medium-Term Note Program, affirmed (P)Baa2

...Junior Senior Unsecured Regular Bond/Debenture, affirmed Baa3

...Junior Senior Unsecured Medium-Term Note Program, affirmed (P)Baa3

...Subordinate Medium-Term Note Program, affirmed (P)Ba3

...Other Short Term, affirmed (P)P-2

..Outlook Action:

...Outlook changed to Positive from Stable

PRINCIPAL METHODOLOGY

The principal methodology used in these ratings was Banks Methodology published in November 2019 and available at https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_1147865 . Alternatively, please see the Rating Methodologies page on www.moodys.com for a copy of this methodology.

REGULATORY DISCLOSURES

For further specification of Moody's key rating assumptions and sensitivity analysis, see the sections Methodology Assumptions and Sensitivity to Assumptions in the disclosure form. Moody's Rating Symbols and Definitions can be found at: https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_79004.

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