

Rating Action: Moody's affirms 22 German banks' senior unsecured debt ratings; changes 16 outlooks to negative

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Actions reflect amendments to European Union's (EU) Bank Recovery and Resolution Directive

Frankfurt am Main, December 12, 2017 -- Moody's Investors Service has today affirmed the senior unsecured debt ratings of 22 German banks, including several of their rated subsidiaries and supported entities, as well as changed the outlooks on 16 of these ratings to negative.

Today's actions follow the agreement to an amendment to the EU's Bank Recovery and Resolution Directive (BRRD), which requires member states to introduce a class of non-preferred senior debt and therefore aims to improve the consistency between creditor hierarchies across the EU. This development is expected to be credit negative for investors in senior unsecured bonds issued by German banks. In this context, the outlook change to negative for most of the banks included in today's ratings action reflects Moody's view that, once the directive's amendment is transposed into German law, unsecured bonds that meet the definition of article 46f of the German Banking Act (§46f KWG) could rank pari passu with future junior senior bonds. This may call into question the moderate probability of government support Moody's currently considers warranted for senior unsecured debt instruments issued by the banks included in this rating action.

The issuer ratings of the affected banks, which follow the senior unsecured ratings of these entities, were also affirmed and their outlooks changed to negative from stable, where applicable, as the outlook assignments for issuer ratings mirror the respective senior unsecured debt rating outlooks.

Most other ratings and rating inputs for the banks included in today's rating action have been unaffected.

Please click on this link http://www.moodys.com/viewresearchdoc.aspx?docid=PBC_198022 for the List of Affected Credit Ratings. This list is an integral part of this Press Release and identifies each affected issuer.

Moody's also published a special comment entitled "FAQ on credit impact of changes to EU insolvency hierarchy on German bank debt", providing more background on today's rating action. Subscribers will be able to access the report under the following link: http://www.moodys.com/researchdocumentcontentpage.aspx? docid=PBC 1100106

A separate rating announcement for Commerzbank AG has been published today and can be found under: https://www.moodys.com/research/Moodys-affirms-Commerzbanks-A2-deposit-and-Baa1-unsecured-debt-ratings--PR 375754

RATINGS RATIONALE

OUTLOOK CHANGES ON SENIOR UNSECURED DEBT REFLECT THE DECLINING PROBABILITY OF GOVERNMENT SUPPORT UPON TRANSPOSITION OF THE BRRD AMENDMENT INTO GERMAN LAW

On November 2017, the European Council and European Parliament agreed to amend the EU's BRRD to introduce a subordinated ("non-preferred", or junior) senior unsecured debt class in all EU member countries. Transposition into national law will be required by year-end 2018, before EU banks become subject to total loss absorbing capacity (TLAC) requirements, or to minimum requirements for own funds and eligible liabilities (MREL).

The amended directive text, which was agreed upon between Parliament, European Commission and the member states in a European trialogue, enables Germany to maintain its current statutory subordination of senior unsecured bank bonds that meet the definition of §46f KWG below other types of senior unsecured liabilities. These include institutional deposits, operating liabilities and bonds with embedded options or a range of other structurally complex features. At the same time, Germany will be able to rank the stock of outstanding plain vanilla senior unsecured bank bonds pari passu with future new issuance of contractually subordinated non-preferred, or junior senior debt.

Whereas German lawmakers may consider special characteristics of the domestic bank liabilities, Moody's believes the joint European aim to more effectively harmonise bank debt rankings in national insolvency laws will prompt Germany to limit the degree of national deviation from the liability structures in place in other EU member states.

The negative outlooks assigned to most senior unsecured debt ratings of the banks affected by today's rating action reflect Moody's view that German legislators may effectively rank pari passu current statutorily subordinated senior unsecured debt with the new class of non-preferred senior debt (or junior senior debt), although Germany might opt to only include instruments issued after a certain date or within a certain time period. Moody's believes that the resolution authorities would expect such a combined debt tranche to absorb losses, if resolution tools were applied, or in the case of an insolvency. If such a legal change happened, the rating agency expects it would lower its government support assumption for these instruments to low, given that they would be clearly designated as loss absorbing. This reduction in support would result in the removal of the rating uplift of one notch currently incorporated into the ratings of these instruments.

The rating outlooks on the issuer ratings of German banks, which currently benefit from one notch of rating uplift followed the direction of outlook changes applied to senior unsecured debt instrument ratings.

Those senior unsecured debt ratings of German banks that already carried a negative outlook prior to today's rating action were affirmed with a negative outlook today. These negative outlooks now also reflect the additional downward pressure related to the rating agency's considerations around government support.

Moody's changed the outlooks on the Aa3 senior unsecured debt ratings of DZ BANK AG and DVB Bank S.E. to negative from positive. The outlook change to negative additionally reflects that Moody's no longer expects upward pressure on these ratings from a more favourable result of its Advanced Loss Given Failure (LGF) analysis. The rating agency bases its LGF analysis on DZ BANK's liability structure at the banking group level, which is relevant for both issuers.

The developing outlook on the affirmed Baa3 senior unsecured debt rating of HSH Nordbank AG was maintained in today's rating action. This already captures a high probability that Moody's will, in due course, remove the government support included in the bank's senior unsecured debt ratings. The rating pressure from weakening support, however, may be offset by other factors that will likely drive the bank's ratings in 2018.

WHAT COULD CHANGE THE RATINGS UP/DOWN

Moody's may downgrade by one notch those German banks' senior unsecured debt instrument ratings that currently incorporate one notch of government support if German legislative changes rank outstanding senior unsecured debt instruments pari-passu with future issuance of junior senior debt.

Moody's may upgrade senior unsecured debt instruments if 1) a bank's improved BCA, or a more favourable LGF result for this debt class, more than offsets the downward pressure from weakening government support; or 2) in the event that Germany transposes BRRD amendments in such a manner that results in existing senior unsecured debt instruments being given greater preferential treatment in the liquidation or resolution hierarchies. This would also result in upward rating pressure on banks' issuer ratings.

Ratings pressure in either direction may occur due to: (1) Fundamental developments that result in upgrades or downgrades of a bank's BCA; (2) any change in Moody's assessment of the strength and/or availability of parental support or cross-sector support -- the latter is generally applicable to banks that are members of a mutualist sector's institutional protection scheme; (3) alterations in a bank's liability structure that changes the expected loss severity for particular liability classes; and/or (4) for all rating classes, any change in Moody's assumptions regarding the likelihood of government support being available.

Changes in the severity of loss for certain liability classes and therefore pressure on results of Moody's Advanced LGF analysis may develop if the individual banks' subordinated instruments increase (or decrease), and/or if senior unsecured debt increases (or decreases) relative to their tangible banking assets. This could result in additional (or fewer) notches of uplift resulting from Moody's LGF analysis.

For bank-specific rating drivers, please refer to the respective banks' latest Credit Opinions.

PRINCIPAL METHODOLOGY

The principal methodology used in these ratings was Banks published in September 2017. Please see the Rating Methodologies page on www.moodys.com for a copy of this methodology.

REGULATORY DISCLOSURES

Please click on this link http://www.moodys.com/viewresearchdoc.aspx?docid=PBC_198022 for the List of Affected Credit Ratings. This list is an integral part of this Press Release and provides, for each of the credit ratings covered, Moody's disclosures on the following items:

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