

Research Update:

Luzerner Kantonalbank Outlook Revised To Positive On The Canton's Improved Fiscal Performance; Ratings Affirmed

May 24, 2022

Overview

- In our view, Luzerner Kantonalbank's (LUKB's) credit quality benefits from the bank being a government-related entity with an extremely high likelihood of receiving support from its majority owner and guarantor, the Canton of Lucerne.
- The canton's financial performance has improved, indicating a stronger ability to support LUKB if needed.
- We therefore revised the outlook on LUKB to positive from stable, and affirmed our 'AA/A-1+' issuer credit ratings. We also affirmed all issue ratings on the cantonal bank's debt.
- The positive outlook indicates LUKB's importance to the canton and the latter's improved ability to provide support, if needed, over the next 12-24 months.

PRIMARY CREDIT ANALYST

Lukas Freund
Frankfurt
+ 49-69-3399-9139
lukas.freund
@spglobal.com

SECONDARY CONTACT

Anna Lozmann
Frankfurt
+ 49 693 399 9166
anna.lozmann
@spglobal.com

Rating Action

On May 24, 2022, S&P Global Ratings revised its outlook on Luzerner Kantonalbank to positive from stable. We affirmed our 'AA/A-1+' long- and short-term issuer credit ratings on LUKB, as well as our issue ratings on the bank's senior unsecured and hybrid debt.

Rationale

The outlook revision indicates the Canton of Lucerne's improved ability to support LUKB, if needed. Due to higher tax revenue, increased profit distribution from the Swiss National Bank, and subsidies, the canton's fiscal performance has strengthened, offsetting increased expenditures. We assume that the canton's enduring stronger fiscal performance suggests that it is better placed to support LUKB in times of stress.

We expect LUKB to maintain its integral link and very important role for Lucerne. We consider LUKB to be a government-related entity (GRE). LUKB has an important role in contributing to the development of the canton's economy and an integral link to the canton, including benefitting from a guarantee. In the event of financial stress at LUKB, we believe there is an extremely high likelihood that the canton would provide sufficient and timely support to the bank, since a default could severely damage the canton's reputation.

LUKB's capitalization will continue to be a rating strength, and we expect the bank will show above-average growth rates. In our view, the canton's planned capital increase of Swiss franc (CHF) 500 million in 2023 will support the bank's growth. We expect the bank to expand further outside its home canton, focusing mainly on residential mortgage lending. In addition, the bank has been increasingly involved in short-term mortgage financing as well as structured products, leading to above-average growth figures compared with cantonal bank peers.

Outlook

Our positive outlook on LUKB indicates an improved ability of its owner, the Canton of Lucerne, to support the bank in times of stress. We expect that, over the coming two years, LUKB will continue to benefit from an extremely high likelihood of support from Lucerne.

Upside scenario

We could consider an upgrade of LUKB over the next two years if Lucerne's creditworthiness were to improve materially, strengthening its ability to support the bank.

A positive rating action stemming solely from the improvement of LUKB's stand-alone credit profile (SACP) is remote over the next two years. This is because we do not expect LUKB to significantly adjust its comparatively concentrated business model.

Downside scenario

We would consider revising our outlook on LUKB to stable if Lucerne's financial prospects were to wane, indicating a weaker ability to provide support. We could lower our issuer credit rating if LUKB's ties with the canton weakened or if there were changes to the canton's state guarantee, which we deem unlikely for the time being.

The sensitivity of the rating on LUKB to a potential downward revision of the SACP remains very limited. However, if we concluded that the bank's risk appetite had become less prudent than peers' over our outlook horizon, or if our risk-adjusted capital ratio for the bank became increasingly dependent on the issuance of hybrid instruments, we could revise down the SACP and consequently lower our issue ratings on LUKB's subordinated debt.

Ratings Score Snapshot

Luzerner Kantonalbank Ratings Score Snapshot

	To	From
Issuer Credit Rating	AA/Positive/A-1+	AA/Stable/A-1+

Luzerner Kantonalbank Ratings Score Snapshot (cont.)

	To	From
SACP	a+	a+
Anchor	a-	a-
Business Position	Adequate (0)	Adequate (0)
Capital and Earnings	Very strong (2)	Very strong (2)
Risk Position	Adequate (0)	Adequate (0)
Funding and	Adequate and	Adequate and
Liquidity	Adequate (0)	Adequate (0)
Support	(+2)	(+2)
ALAC Support	0	0
GRE Support	(+2)	(+2)
Group Support	0	0
Sovereign Support	0	0
Additional Factors	0	0

ESG credit indicators: E-2, S-2, G-2

Related Criteria

- Criteria | Financial Institutions | Banks: Banking Industry Country Risk Assessment Methodology And Assumptions, Dec. 9, 2021
- Criteria | Financial Institutions | General: Financial Institutions Rating Methodology, Dec. 9, 2021
- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- General Criteria: Hybrid Capital: Methodology And Assumptions, July 1, 2019
- General Criteria: Group Rating Methodology, July 1, 2019
- Criteria | Financial Institutions | General: Risk-Adjusted Capital Framework Methodology, July 20, 2017
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- General Criteria: Rating Government-Related Entities: Methodology And Assumptions, March 25, 2015
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Ratings List

Ratings Affirmed

Luzerner Kantonalbank	
Senior Unsecured	AA
Subordinated	A-
Junior Subordinated	BBB

Ratings Affirmed; Outlook Action

	To	From
Luzerner Kantonalbank		
Issuer Credit Rating	AA/Positive/A-1+	AA/Stable/A-1+

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. A description of each of S&P Global Ratings' rating categories is contained in "S&P Global Ratings Definitions" at https://www.standardandpoors.com/en_US/web/guest/article/-/view/sourceId/504352 Complete ratings information is available to subscribers of RatingsDirect at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column. Alternatively, call one of the following S&P Global Ratings numbers: Client Support Europe (44) 20-7176-7176; London Press Office (44) 20-7176-3605; Paris (33) 1-4420-6708; Frankfurt (49) 69-33-999-225; or Stockholm (46) 8-440-5914

Copyright © 2022 by Standard & Poor's Financial Services LLC. All rights reserved.

No content (including ratings, credit-related analyses and data, valuations, model, software or other application or output therefrom) or any part thereof (Content) may be modified, reverse engineered, reproduced or distributed in any form by any means, or stored in a database or retrieval system, without the prior written permission of Standard & Poor's Financial Services LLC or its affiliates (collectively, S&P). The Content shall not be used for any unlawful or unauthorized purposes. S&P and any third-party providers, as well as their directors, officers, shareholders, employees or agents (collectively S&P Parties) do not guarantee the accuracy, completeness, timeliness or availability of the Content. S&P Parties are not responsible for any errors or omissions (negligent or otherwise), regardless of the cause, for the results obtained from the use of the Content, or for the security or maintenance of any data input by the user. The Content is provided on an "as is" basis. S&P PARTIES DISCLAIM ANY AND ALL EXPRESS OR IMPLIED WARRANTIES, INCLUDING, BUT NOT LIMITED TO, ANY WARRANTIES OF MERCHANTABILITY OR FITNESS FOR A PARTICULAR PURPOSE OR USE, FREEDOM FROM BUGS, SOFTWARE ERRORS OR DEFECTS, THAT THE CONTENT'S FUNCTIONING WILL BE UNINTERRUPTED OR THAT THE CONTENT WILL OPERATE WITH ANY SOFTWARE OR HARDWARE CONFIGURATION. In no event shall S&P Parties be liable to any party for any direct, indirect, incidental, exemplary, compensatory, punitive, special or consequential damages, costs, expenses, legal fees, or losses (including, without limitation, lost income or lost profits and opportunity costs or losses caused by negligence) in connection with any use of the Content even if advised of the possibility of such damages.

Credit-related and other analyses, including ratings, and statements in the Content are statements of opinion as of the date they are expressed and not statements of fact. S&P's opinions, analyses and rating acknowledgment decisions (described below) are not recommendations to purchase, hold, or sell any securities or to make any investment decisions, and do not address the suitability of any security. S&P assumes no obligation to update the Content following publication in any form or format. The Content should not be relied on and is not a substitute for the skill, judgment and experience of the user, its management, employees, advisors and/or clients when making investment and other business decisions. S&P does not act as a fiduciary or an investment advisor except where registered as such. While S&P has obtained information from sources it believes to be reliable, S&P does not perform an audit and undertakes no duty of due diligence or independent verification of any information it receives. Rating-related publications may be published for a variety of reasons that are not necessarily dependent on action by rating committees, including, but not limited to, the publication of a periodic update on a credit rating and related analyses.

To the extent that regulatory authorities allow a rating agency to acknowledge in one jurisdiction a rating issued in another jurisdiction for certain regulatory purposes, S&P reserves the right to assign, withdraw or suspend such acknowledgment at any time and in its sole discretion. S&P Parties disclaim any duty whatsoever arising out of the assignment, withdrawal or suspension of an acknowledgment as well as any liability for any damage alleged to have been suffered on account thereof.

S&P keeps certain activities of its business units separate from each other in order to preserve the independence and objectivity of their respective activities. As a result, certain business units of S&P may have information that is not available to other S&P business units. S&P has established policies and procedures to maintain the confidentiality of certain non-public information received in connection with each analytical process.

S&P may receive compensation for its ratings and certain analyses, normally from issuers or underwriters of securities or from obligors. S&P reserves the right to disseminate its opinions and analyses. S&P's public ratings and analyses are made available on its Web sites, www.standardandpoors.com (free of charge), and www.ratingsdirect.com (subscription), and may be distributed through other means, including via S&P publications and third-party redistributors. Additional information about our ratings fees is available at www.standardandpoors.com/usratingsfees.

STANDARD & POOR'S, S&P and RATINGSDIRECT are registered trademarks of Standard & Poor's Financial Services LLC.