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Basellandschaftliche Kantonalbank

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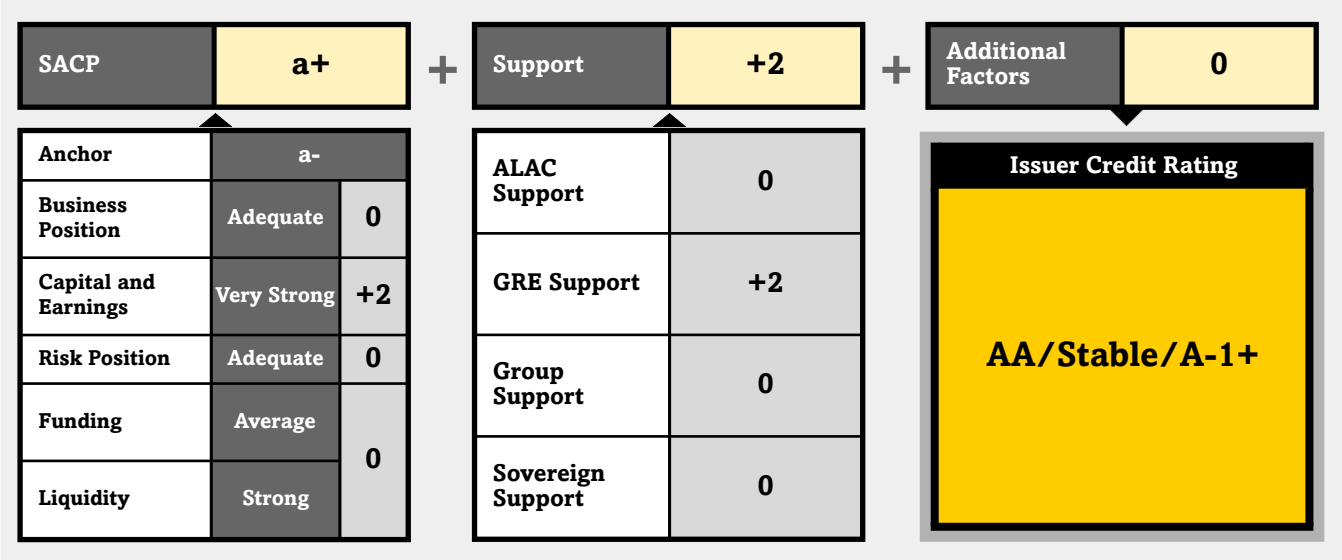
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Related Criteria

Related Research

Basellandschaftliche Kantonalbank



Major Rating Factors

Strengths:	Weaknesses:
<ul style="list-style-type: none"> • Close ties with the Canton of Basel-Country, facilitated by majority ownership and a statutory guarantee. • A strong retail banking franchise in the Canton of Basel-Country and to a lesser extent in nearby cantons. • Sound financial profile underpinned by very strong capitalization and stable earnings. 	<ul style="list-style-type: none"> • Concentration risk due to focus on residential mortgage lending in its home region. • Limited geographic, business, and earnings diversification. • Limited growth potential.

Outlook: Stable

S&P Global Ratings' stable outlook on Switzerland-based Basellandschaftliche Kantonalbank (BLKB) reflects that on the bank's majority owner and guarantor, the Canton of Basel-Country. We expect that BLKB's status as a government-related entity (GRE) and the extremely high likelihood of support will not change in the foreseeable future. Moreover, we expect that BLKB will maintain its sound financial profile, underpinned by its very strong capitalization and sound earnings capacity over the next two years. Our base case assumes that the Swiss economy will remain relatively resistant amid the pandemic.

We could take a negative rating action if BLKB's ties with Basel-Country were to loosen or if changes to the canton's statutory guarantee were made. However, we currently consider this scenario unlikely and, if it happens, we expect BLKB's existing obligations would be grandfathered. All else being equal, if BLKB's stand-alone credit profile (SACP) were to worsen moderately, we would expect our current issuer credit rating to benefit from additional support from the canton.

A positive rating action stemming solely from the improvement of BLKB's SACP is remote because we do not expect BLKB to adjust its comparatively concentrated business model. However, a positive rating action on the canton would trigger an upgrade of BLKB.

Rationale

We expect BLKB's banking franchise will continue to benefit from a strong market position in its home region, with franchise strength and the low risk-operating environment in Switzerland offsetting risks from limited geographic, business, and earnings diversification. We consider BLKB's superior capital position to be its main rating strength, underlined by our projected risk-adjusted capital (RAC) ratio of over 28% in the next 24 months. BLKB's risk profile is characterized by its regional loan portfolio, balanced by high collateralization levels and sound asset quality, which we expect to prove resilient through the current economic downturn. Our views of its funding and liquidity profile are supported by the bank's largely deposit-funded business model and sound metrics.

We consider BLKB to be a GRE with an extremely high likelihood of receiving timely and sufficient extraordinary support from Basel-Country if needed. We base this opinion on BLKB's very important role for and integral link with its home canton. This provides a two-notch uplift from the 'a+' SACP to arrive at the 'AA' issuer credit rating.

Anchor: 'a-' for banks operating only in Switzerland

Our criteria use our Banking Industry Country Risk Assessment's economic risk and industry risk scores to determine a bank's anchor, the starting point in assigning an issuer credit rating. Our anchor for a bank operating mainly in Switzerland is 'a-'. We view the trends for both economic and industry risk as stable.

We expect Switzerland's economy to contract materially in 2020 due to COVID-19, but to fully recover over the coming two years. Under this base case, we think the Swiss banking sector will remain resilient, supported by the country's diversified and competitive economy, very high household income levels, and a proven stress-resilient corporate sector. We think the Swiss authorities' material support measures for domestic firms and households should

cushion the short-term effect on Swiss banks' loan books. Additionally, we view positively banks' prudent loan underwriting standards and high collateralization of residential mortgage loans, which dominate most banks' customer portfolios. Considering these factors, we expect only a limited increase in credit losses, from historical low levels. We also expect that affordability risk in the housing market could slightly reduce over the coming years as price growth in the owner-occupied segment is likely to remain muted in the wake of the pandemic. However, a particular and ongoing risk is the investment property segment (estimated 30% of the market) where we had already observed signs of a price correction before the pandemic.

Our view of industry risk in Switzerland encompasses the stability of the domestic banking sector and our expectation that damage from the pandemic will remain contained. We view positively the limited presence of foreign players, the banks' high capitalization levels in an international comparison, and their low reliance on capital markets for funding. In our view, the Swiss regulator's initiatives remain more stringent than those in other European banking sectors. We expect that banks' net interest margins will further gradually decline in a permanent low interest-rate environment, as higher-yield assets mature and retail deposit rates remain floored at zero. However, we expect that repricing of lending products, additional fee income from investment advisory-related activities, and ongoing cost management can offset some of the pressure. We consider risk for Swiss banks from tech disruption as limited as of today, given the population's preference for cash payments, the small size of the market with high barriers of entry, and technologically well-equipped banks.

Table 1

Basellandschaftliche Kantonalbank--Key Figures					
--Year-ended Dec. 31--					
(Mil. CHF)	2020*	2019	2018	2017	2016
Adjusted assets	29,047.2	27,272.1	25,334.5	24,203.9	23,681.6
Customer loans (gross)	21,794.7	21,207.9	20,298.6	19,636.1	19,097.6
Adjusted common equity	2,431.5	2,423.1	2,330.0	2,223.4	2,106.9
Operating revenues	185.9	368.1	361.5	370.3	372.4
Noninterest expenses	98.7	195.2	192.5	194.4	184.9
Core earnings	79.8	169.5	164.4	171.8	183.1

*Data as of June 30. CHF--Swiss Franc.

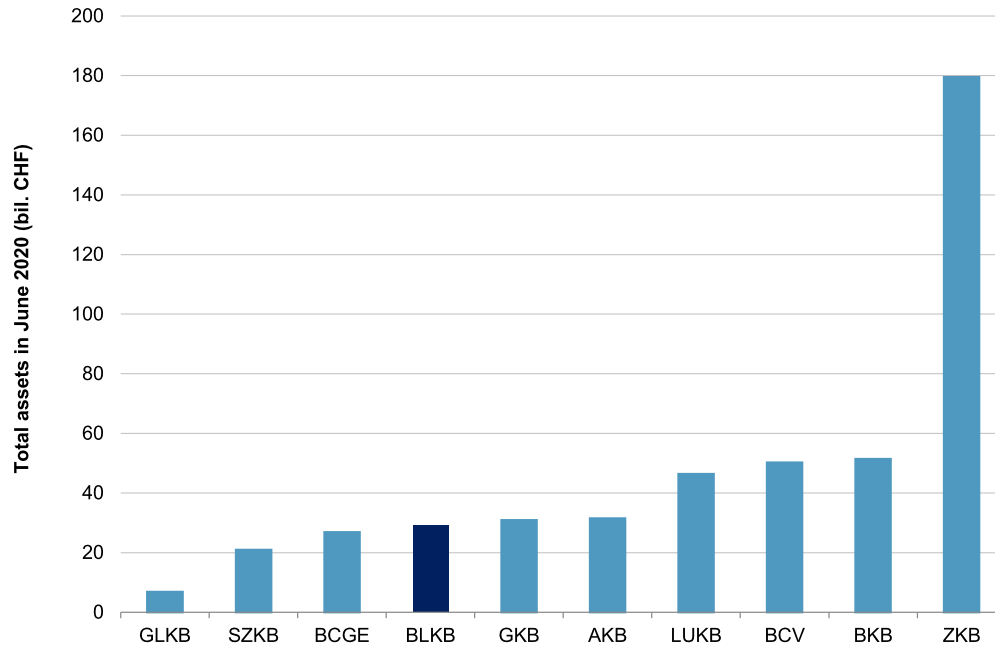
Business position: A well-established regional franchise in the Canton of Basel-Country

We expect BLKB's business profile to remain focused on its strong retail franchise in Basel-Country and to a lesser extent in neighboring cantons. In our view, its competitive position remains on par with peers' in Switzerland and in countries with similar industry risk, such as Germany, France, and Belgium.

Chart 1

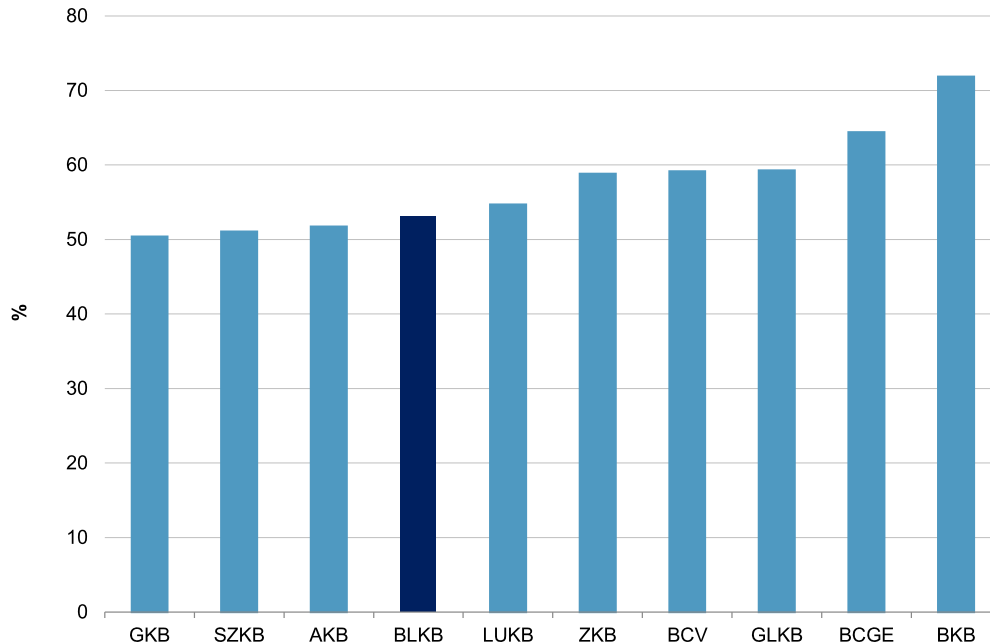
Basellandschaftliche Kantonalbank Is A Midsize Swiss Cantonal Bank

BLKB versus rated peers



Source: S&P Global Ratings. CHF--Swiss franc. Data as of June 30, 2020.
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We view as negative BLKB's reliance on its relatively small, even if economically strong, home region. We consider this rating weakness to be compensated by its market leadership in retail banking with a strong focus on residential mortgage lending, which comprises 90% of the loan book. Also, BLKB's sound efficiency with its 47% cost-to-income ratio and track record of exceptional business stability over the economic cycle support our assessment. We expect BLKB to continue its conservative operating stance, supported by the canton, which prioritizes stability ahead of returns.

Chart 2**BLKB's Efficiency Is Better Than The Average For Rated Cantonal Bank Peers**
Cost to Income Ratio

Source: S&P Global Ratings. Data for the period Mid-year 2020.
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Lending to small and midsize enterprises (SMEs) accounts for around 10% of the loan portfolio. Since the beginning of the pandemic the bank has supported SME customers by pledging loans worth Swiss franc (CHF) 147 million under the Federal Loan Program. BLKB's remaining business activities are accompanied by asset management and private banking operations and, to a lesser extent, client-initiated trading activities. However, non-lending operations provide only a modest contribution to earnings diversification, a business model that we do not expect to change in the next few years.

BLKB divested its equity holding in Swissquote--a provider of online financial and trading services--but we understand that its involvement in e-mortgage loans will continue. This allows BLKB to offer loans countrywide, allowing some diversification outside its home region. However, we expect the share of e-mortgage loans to remain low at around 5% of BLKB's mortgage loan book.

BLKB proactively executes strategic initiatives to adapt to changing banking industry trends such as digitalization and more sustainable banking. BLKB has also built up its own strategic funds focusing on assets that meet sustainability criteria. BLKB's increasing sustainability focus supports our view that the bank is continually transforming of its strategies.

Table 2

Basellandschaftliche Kantonalbank--Business Position	--Year-ended Dec. 31--				
	2020*	2019	2018	2017	2016
(%)					
Loan market share in country of domicile	N/A	1.7	1.7	1.7	1.7
Deposit market share in country of domicile	N/A	1.4	1.4	1.4	1.4
Total revenues from business line (currency in millions)	187.1	370.9	381.7	394.0	385.0
Commercial & retail banking/total revenues from business line	100.0	100.0	100.0	100.0	100.0
Return on average common equity	4.2	5.6	5.7	5.9	6.3

*Data as of June 30. N/A--Not applicable.

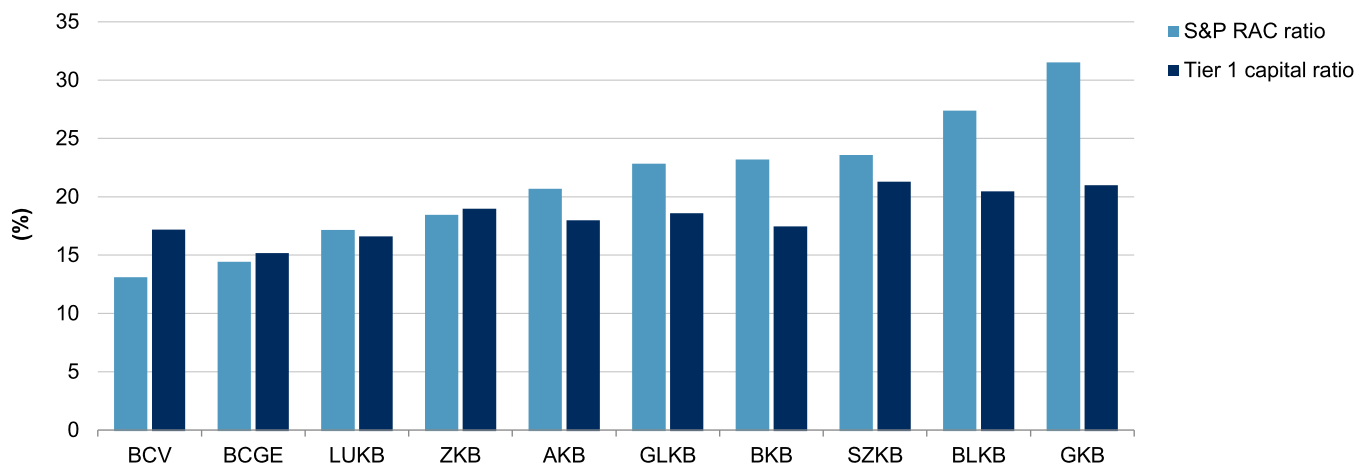
Capital and earnings: Very strong capitalization supported by stable earnings

We consider BLKB's stable earnings generation and exceptional capitalization levels to be a key rating strength. We do not anticipate a change in the bank's capital policy and expect BLKB's RAC ratio to increase beyond 28% over the next 18-24 months from 27.3% at year-end 2019. Although its recent loan growth has been higher than average, with up to 5.5%, we expect the bank to maintain a RAC ratio among the highest in a global comparison (see chart 3). Our base case assumes that the Swiss economy will remain resilient amid the pandemic and that any negative effects on the bank will be very limited.

Chart 3

BLKB's Risk-Adjusted Capitalization Is Among The Highest Of Rated Cantonal Banks

Bar chart subtitle



Source: S&P Global Ratings. Ratios as of Dec. 31, 2019.

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We view BLKB's earnings capacity as strong and predictable. BLKB's returns figures are slightly below those of domestic peers' but we currently do not consider this a significant factor given its solid profits in recent years.

Despite some progress in diversifying its revenue sources into fees and commissions, BLKB has one of the highest

interest income dependencies among its cantonal bank peers. Provided that new business does not compensate for decreasing interest rates, we expect BLKB's net interest income to reduce further over the next few years. With a higher focus on digitization initiatives and the need for investments, we project the bank's cost-to-income ratio to increase marginally over the next two-to-three years. We expect its dividend policy to remain in line with that of previous years with a total payout of CHF80 million-CHF90 million yearly. BLKB's three-year average earnings buffer is expected to decline marginally to about 1.2% of our risk-weighted assets figure (an earnings buffer of 1.0% indicates adequate earnings to cover normalized losses). This will support further capital buildup.

BLKB's regulatory core equity tier 1 ratio stood at 19.4% as of June 30, 2020, which is very high in a global comparison but lower than the bank's RAC ratio because we apply lower risk weights on Swiss retail loans than the Swiss regulator. We believe that Basel-Country, which owns 74% of BLKB and holds 100% of voting rights, remains supportive of BLKB's capital position and that BLKB will not be required to make major or extraordinary dividend distributions that might weaken its RAC ratio.

Table 3

Basellandschaftliche Kantonalbank--Capital And Earnings					
	--Year-ended Dec. 31--				
(%)	2020*	2019	2018	2017	2016
Tier 1 capital ratio	19.4	20.4	20.4	20.0	19.9
S&P Global Ratings' RAC ratio before diversification	N/A	27.3	26.8	26.1	26.1
S&P Global Ratings' RAC ratio after diversification	N/A	18.5	19.3	19.1	18.8
Adjusted common equity/total adjusted capital	100.0	100.0	100.0	100.0	100.0
Net interest income/operating revenues	72.8	73.1	74.6	74.6	77.5
Fee income/operating revenues	19.6	18.4	18.4	17.4	15.4
Market-sensitive income/operating revenues	6.6	7.1	4.7	6.5	5.8
Cost to income ratio	53.1	53.0	53.3	52.5	49.7
Preprovision operating income/average assets	0.6	0.7	0.7	0.7	0.8
Core earnings/average managed assets	0.6	0.6	0.7	0.7	0.8

*Data as of June 30. N/A--Not applicable.

Table 4

Basellandschaftliche Kantonalbank RACF [Risk-Adjusted Capital Framework] Data					
	Exposure*	Basel III RWA	Average Basel III RW(%)	S&P Global RWA	Average S&P Global RW (%)
Credit risk					
Government & central banks	4,975,603,474.9	264,688,525.5	5.3	37,281,275.7	0.7
Of which regional governments and local authorities	0.0	0.0	0.0	0.0	0.0
Institutions and CCPs	1,519,453,347.5	421,884,466.7	27.8	237,770,308.0	15.6
Corporate	1,783,438,276.9	1,616,261,277.4	90.6	1,174,727,457.5	65.9
Retail	20,028,463,356.2	8,575,131,149.2	42.8	6,085,332,009.3	30.4
Of which mortgage	16,685,218,230.0	6,503,739,057.1	39.0	3,879,948,742.9	23.3
Securitization§	0.0	0.0	0.0	0.0	0.0

Table 4

Basellandschaftliche Kantonalbank RACF [Risk-Adjusted Capital Framework] Data (cont.)					
Other assets†	0.0	0.0	0.0	0.0	0.0
Total credit risk	28,306,958,455.5	10,877,965,418.8	38.4	7,535,111,050.5	26.6
Credit valuation adjustment					
Total credit valuation adjustment	--	12,064,250.0	--	0.0	--
Market Risk					
Equity in the banking book	63,291,805.7	75,244,141.7	118.9	423,904,463.2	669.8
Trading book market risk	--	44,126,962.5	--	66,190,443.8	--
Total market risk	--	119,371,104.2	--	490,094,906.9	--
Operational risk					
Total operational risk	--	0.0	--	854,995,138.6	--
	Exposure	Basel III RWA	Average Basel II RW (%)	S&P Global RWA	% of S&P Global RWA
Diversification adjustments					
RWA before diversification	--	11,923,100,773.0	--	8,880,201,096.0	100.0
Total Diversification/ Concentration Adjustments	--	--	--	4,230,058,791.1	47.6
RWA after diversification	--	11,923,100,773.0	--	13,110,259,887.1	147.6
		Tier 1 capital	Tier 1 ratio (%)	Total adjusted capital	S&P Global RAC ratio (%)
Capital ratio					
Capital ratio before adjustments		2,430,904,379.0	20.4	2,423,070,000.0	27.3
Capital ratio after adjustments‡		2,430,904,379.0	20.4	2,423,070,000.0	18.5

*Exposure at default. §Securitization Exposure includes the securitization tranches deducted from capital in the regulatory framework. †Exposure and S&P Global Ratings' risk-weighted assets for equity in the banking book include minority equity holdings in financial institutions. ‡Adjustments to Tier 1 ratio are additional regulatory requirements (e.g. transitional floor or Pillar 2 add-ons). RWA--Risk-weighted assets. RW--Risk weight. RAC--Risk-adjusted capital. CHF--Swiss Franc. Sources: Company data as of 'Dec. 31 2019', S&P Global Ratings.

Risk position: Conservative underwriting of new mortgage lending and strong financial health of Swiss customers keeps nonperforming loans low

BLKB's business model focuses on low-risk well-collateralized lending categories such as mortgages, SMEs, and corporates, with only a small exposure to market-sensitive business.

BLKB's loan book of about CHF21.8 billion on June 30, 2020, shows concentration risk stemming from its residential real estate loans in Basel-Country and neighboring cantons. Assuming only limited negative effects from the pandemic on the Swiss economy, we expect BLKB's risk profile to be supported by its historically strong asset quality and high granularity and collateralization levels in the loan portfolio (average loan-to-value ratio of 54% for mortgage loans).

Like its domestic peers, BLKB remains exposed to risks related to a potential correction in Swiss residential real estate markets--but we do not see this as imminent. Positively, we believe the bank will maintain its conservative underwriting standards in new mortgage lending, helping it to report low nonperforming loans. We project a marginal increase in the cost of risk in 2020 and 2021 in relative terms, anticipating a negative but manageable impact from the

pandemic on the Swiss credit portfolio.

To diversify its loan book, BLKB selectively participates in syndicated corporate loans to large corporations across Switzerland. However, we do not believe that this activity, which currently represents less than 5% of BLKB's lending and predominately focuses on highly rated corporations, will expose BLKB to elevated credit risks that would impair its risk profile.

Table 5

Basellandschaftliche Kantonalbank--Risk Position					
	--Year-ended Dec. 31--				
(%)	2020*	2019	2018	2017	2016
Growth in customer loans	5.5	4.5	3.4	2.8	2.4
Total diversification adjustment/S&P Global Ratings' RWA before diversification	N/A	47.6	39.1	37.1	39.3
Total managed assets/adjusted common equity (x)	11.9	11.3	10.9	10.9	11.2
New loan loss provisions/average customer loans	0.1	0.0	0.0	0.0	0.0
Gross nonperforming assets/customer loans + other real estate owned	N/A	0.0	0.1	0.1	0.2
Loan loss reserves/gross nonperforming assets	N/A	N.M.	1,232.6	674.3	422.7

*Data as of June 30. N/A--Not applicable. N.M.--Not meaningful.

Funding and liquidity: The bank's strong retail franchise provides funding stability

We expect that BLKB's stable funding ratio will remain comfortable at 115%-120% over the next two years and its funding profile should stay in line with domestic peers. Its funding benefits from a high level of core customer deposits, constituting 69% of the total funding base on June 30, 2020, and from its strong equity base, comprising about 9% of total assets. We consider that the bank's customer deposits will remain very stable, also amid downturns, owing to its business stability backed by the statutory guarantee of its liabilities from Basel-Country. Evidence of this stability has been the flight to quality observed during the most recent crises and the continuous increase in customer deposits over recent years, despite the low interest rates the bank has offered.

However, the loan portfolio continues to exceed the deposit base. Customer loans to deposits has ranged between 115% and 120% over the past five years (114% at June 30, 2020) indicating BLKB's reliance on other funding means. BLKB takes advantage of wholesale funding, mainly covered and unsecured bonds.

Our assessment of BLKB's liquidity as strong mainly reflects our estimate of the bank's one-year liquidity ratio (broad liquid assets to short-term wholesale funding) at almost 2.5x on June 30, 2020. Its use of short-term wholesale funding (mainly repurchase agreements) remains at a low 9.7% of the funding base. We consider the bank's liquidity coverage--consisting mainly of securities eligible for repurchase at the Swiss central bank--to be strong. This indicates the availability of sufficient liquid assets to withstand a lack of access to wholesale funding for more than 12 months.

Table 6

Basellandschaftliche Kantonalbank--Funding And Liquidity					
	--Year-ended Dec. 31--				
(%)	2020*	2019	2018	2017	2016
Core deposits/funding base	68.6	71.1	73.4	76.8	73.9
Customer loans (net)/customer deposits	120.7	120.4	120.5	116.7	120.3

Table 6

Basellandschaftliche Kantonalbank--Funding And Liquidity (cont.)					
	--Year-ended Dec. 31--				
(%)	2020*	2019	2018	2017	2016
Long-term funding ratio	91.1	92.3	94.1	96.4	94.1
Stable funding ratio	115.5	114.2	112.8	107.0	112.3
Short-term wholesale funding/funding base	9.7	8.4	6.6	4.0	6.5
Broad liquid assets/short-term wholesale funding (x)	2.5	2.6	2.9	3.0	2.9
Net broad liquid assets/short-term customer deposits	21.4	19.3	17.3	10.3	16.8
Short-term wholesale funding/total wholesale funding	31.0	29.2	24.6	17.2	24.9
Narrow liquid assets/3-month wholesale funding (x)	12.6	4.3	7.7	4.1	4.3

*Data as of June 30.

Support: Uplift due to support from the Canton of Basel-Country

We regard BLKB as a GRE and see an extremely high likelihood that BLKB's owner, Basel-Country, would provide timely and sufficient support to BLKB. We base our assessment on the bank's integral link with Basel-Country, which we expect will provide timely support to BLKB. Our assessment is underpinned by the owner's full control of the bank (100% of the voting rights) and its provision of a statutory guarantee for the bank's liabilities. BLKB plays very important role for the canton, owing to the significant impact of its activities on the local economy. Because of this, we add a two-notch uplift to BLKB's 'a+' SACP to derive the long-term rating. We do not envisage that the bank's GRE status or our view of an extremely high likelihood of extraordinary government support will change in the medium term.

We expect the existing cantonal guarantees to remain in the medium term. However, although beyond our outlook horizon, we consider the potential risk that future agreements between Switzerland and the EU regarding preferential market access might include the removal of cantonal guarantees for all banks.

BLKB benefits from Basel-Country's statutory guarantee, which ultimately covers all of BLKB's liabilities, excluding nonvoting participation certificates ("Partizipationskapital"). However, we note that the guarantee does not explicitly ensure timely repayment, as defined by our criteria. Nevertheless, we believe that the canton has strong incentives to help BLKB meet its obligations on time, owing to the bank's importance to the regional economy and to prevent reputational damage.

Environmental, Social and Governance: New initiatives promoting sustainable finance

ESG factors have a neutral impact on our assessment of BLKB's creditworthiness. Social and environmental credit factors are in line with those of peers in the Swiss banking industry. We expect BLKB to benefit from its sustainability initiatives in the future. The bank also projects to be carbon-neutral by the year 2030. The offering of additional sustainable financial services supports further business growth and we expect volumes to increase over the upcoming years. We view governmental ownership and control by the canton as beneficial for BLKB's governance standards, which we reflect in our assessment.

Related Criteria

- 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
- Criteria - Financial Institutions - Banks: Quantitative Metrics For Rating Banks Globally: Methodology And Assumptions, July 17, 2013
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011
- Criteria - Financial Institutions - Banks: Banks: Rating Methodology And Assumptions, Nov. 9, 2011
- Criteria - Financial Institutions - Banks: Banking Industry Country Risk Assessment Methodology And Assumptions, Nov. 9, 2011

Related Research

- COVID-19: Swiss Banking Sector To Remain Resilient, June 17, 2020
- Swiss Canton of Basel-Country 'AA+/A-1+' Ratings Affirmed; Outlook Stable, May 8, 2020
- Tech Disruption In Retail Banking: Swiss Banks Are In No Rush To Become Digital Frontrunners, Feb. 13, 2020
- Banking Industry Country Risk Assessment: Switzerland, Nov. 20, 2019

Anchor Matrix										
Industry Risk	Economic Risk									
	1	2	3	4	5	6	7	8	9	10
1	a	a	a-	bbb+	bbb+	bbb	-	-	-	-
2	a	a-	a-	bbb+	bbb	bbb	bbb-	-	-	-
3	a-	a-	bbb+	bbb+	bbb	bbb-	bbb-	bb+	-	-
4	bbb+	bbb+	bbb+	bbb	bbb	bbb-	bb+	bb	bb	-
5	bbb+	bbb	bbb	bbb	bbb-	bbb-	bb+	bb	bb-	b+
6	bbb	bbb	bbb-	bbb-	bbb-	bb+	bb	bb	bb-	b+
7	-	bbb-	bbb-	bb+	bb+	bb	bb	bb-	b+	b+
8	-	-	bb+	bb	bb	bb	bb-	bb-	b+	b
9	-	-	-	bb	bb-	bb-	b+	b+	b+	b
10	-	-	-	-	b+	b+	b+	b	b	b-

Ratings Detail (As Of November 10, 2020)*

Basellandschaftliche Kantonalbank

Issuer Credit Rating

AA/Stable/A-1+

Senior Unsecured

AA

Ratings Detail (As Of November 10, 2020)*(cont.)

Issuer Credit Ratings History

01-Dec-2014	AA/Stable/A-1+
20-Jan-2014	AA+/Negative/A-1+
03-Jul-2012	AAA/Negative/A-1+

Sovereign Rating

Switzerland	AAA/Stable/A-1+
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Related Entities**Basel-Country (Canton of)**

Issuer Credit Rating	AA+/Stable/A-1+
Senior Unsecured	AA+

*Unless otherwise noted, all ratings in this report are global scale ratings. S&P Global Ratings' credit ratings on the global scale are comparable across countries. S&P Global Ratings' credit ratings on a national scale are relative to obligors or obligations within that specific country. Issue and debt ratings could include debt guaranteed by another entity, and rated debt that an entity guarantees.

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