S&P Global
Ratings

RatingsDirect®

Liechtenstein-Based LGT Bank And VP Bank Ratings Affirmed After Review Of Government Support; LGT Off Watch

Primary Credit Analysts:
Harm Semder, Frankfurt (49) 69-33-999-158; harm.semder@spglobal.com
Heiko Verhaag, Frankfurt (49) 69-33-999-215; heiko.verhaag@spglobal.com

Secondary Contact:
Salla von Steinaecker, Frankfurt (49) 69-33-999-164; salla.vonsteinaecker@spglobal.com

- We now consider the likelihood of extraordinary government support for banks in Liechtenstein to be uncertain, and we are therefore removing the one-notch uplift for such support in our ratings on systemically important Liechtenstein banks, LGT Bank and VP Bank.
- We consider the country's bank resolution framework to be effective, which allows us to include uplift for additional loss-absorbing capacity (ALAC) in our ratings on individual systemically important banks.
- We are affirming our ratings on LGT Bank at 'A+/A-1' with a stable outlook, as we view its earnings and risk metrics to be better than peers' and because we consider its earnings and recapitalization plans to finance its large-scale private banking acquisition to be sound.
- We are affirming our ratings on VP Bank at 'A-/A-2' and revising the outlook to positive to reflect the potential ramp-up of an ALAC buffer, on which we expect to have more clarity within the next 24 months.

FRANKFURT (S&P Global Ratings) March 2, 2017--S&P Global Ratings today took rating actions on two systemically important Liechtenstein banks, LGT Bank AG and VP Bank AG:

- We affirmed our long- and short-term counterparty credit ratings on LGT Bank AG at 'A+/A-1'. At the same time, we removed the ratings from CreditWatch negative where we had placed them on Dec. 9, 2016. The outlook is stable.

1809125 | 302487482

- We affirmed our 'A-/A-2' long- and short-term counterparty credit ratings on VP Bank AG. We revised the outlook to positive from stable.

These rating actions follow the introduction of a bank resolution framework in the Principality of Liechtenstein effective on Jan. 1, 2017. The action on LGT Bank also reflects our review of its earnings and recapitalization plans to finance its large-scale private banking acquisition from ABN AMRO.

Liechtenstein recently implemented the recovery and resolution act (Sanierungs- und Abwicklungsgesetz) into national law, which provides the authorities with bail-in powers over domestic banks. This leads us to believe that prospects for extraordinary government support before any burden-sharing by senior unsecured creditors now appear uncertain, even for systemically important banks such as LGT Bank and VP Bank.

We do not rule out the possibility that systemically important banks in Liechtenstein might receive extraordinary government support, but we now see the predictability of such support as materially reduced. That said, if such a bank experienced financial difficulties and we saw clear evidence that government support would be forthcoming, we could still reflect this "additional short-term support" in our ratings on individual banks.

Accordingly, we have reclassified our view of the Liechtenstein government's tendency to support private sector commercial banks as uncertain. Although we consider that LGT Bank has high systemic importance and VP Bank moderate systemic importance in Liechtenstein, we have now removed the additional notch of uplift that we incorporated in each rating for extraordinary government support.

Following our review of the Liechtenstein recovery and resolution act, which transposes all key parts of the EU Banking Recovery and Resolution Directive, including its bail-in provisions, into national law, we assess the Liechtenstein resolution regime as sufficiently effective under our additional loss-absorbing capacity (ALAC) criteria. Among other factors, we believe the authorities would most likely apply a bail-in process to permit nonviable systemically important banks to continue critical functions as going concerns following a bail-in of eligible liabilities. We consider that the new resolution regime would also allow for the effective recapitalization of a failing systemic bank, aided by associated liquidity or funding support to cope with the likely loss of market access. We believe the resolution authority to have the means to support a going-concern bank if required.

While senior unsecured liabilities are technically exposed to bail-in, we expect that the Financial Markets Authority (FMA) in Liechtenstein will require banks to maintain additional buffers of junior instruments (known as MREL, minimum requirement for eligible liabilities) in a manner that offers a material level of protection to senior unsecured creditors. However, there is not yet any final public guidance on the potential design of the local MREL framework or bank-specific buffers. We expect the FMA to closely watch MREL implementation in the EU and potentially wait for harmonization of bail-in hierarchies across the EU, given the different approaches (see "As The Tier 3 Ball Starts To Roll, European Banks Continue To Plot Their Bail-In Buffers," June 6, 2016).

We note that the systemic banks we rate in Liechtenstein have only limited amounts of subordinated capital instruments outstanding to fulfill MREL requirements, but have meaningful amounts of senior unsecured debt instruments. Furthermore, LGT and VP Bank appear to currently have limited incentives to issue significant amounts of additional MREL-eligible instruments, considering these banks' very high regulatory Tier 1 capital ratios.

With these factors in mind, we see the possibility that Liechtenstein's authorities may consider one of the two main alternative routes in Europe: Ask banks to issue a substantial volume of new, contractually subordinated debt, as is happening for French banks, or to pursue statutory subordination, similar to that effected by the German law change on Jan. 1, 2017. Under this route, certain long-term senior unsecured bonds of German banks were juniorized, leading them to be subordinated to senior unsecured claims in resolution and liquidation. As a result, we reclassified nonsystemic German banks' affected instruments as senior subordinated debt, typically lowering our issue credit ratings by a notch to reflect the subordination. At the same time, ALAC buffers of systemically important banks in Germany might increase significantly from inclusion of existing senior subordinated debt in our ALAC measure. (For further details, see "Various German Banks' Snr Unsecured Debt Lowered/Affirmed After Notes Review; Off Watch; Four Banks Remain On Watch," Feb. 9, 2017.)

We expect the FMA to provide further guidance on MREL toward the end of 2017. We will continue to closely monitor the evolution of the framework to reflect potential future changes in creditor hierarchies and systemic banks' eventual ramp-up of what might prove to be substantial and sustained ALAC buffers, above our minimum thresholds for ratings uplift.

The paragraphs below provide an overview of our rationale for the related rating actions we have taken on each bank.

LGT BANK

We affirmed our long- and short-term counterparty credit ratings on LGT Bank at 'A+/A-1'. At the same time, we removed the ratings from CreditWatch with negative implications, where we placed them on Dec. 9, 2016. The outlook is stable.

Our ratings affirmation reflects our expectation that LGT Bank will demonstrate sustainable superior earnings and risk metrics compared with peers, while smoothly operating its enlarged businesses. This leads us to add a one-notch adjustment, which offsets our removal of a one-notch uplift for extraordinary government support.

Our assessment of LGT Bank's stand-alone credit profile (SACP) remains at 'a' because we consider as sound its management's earnings and recapitalization plans to finance its acquisition of ABN AMRO's private banking business in Hong Kong, Singapore, and Dubai. Accordingly, we maintain our assessment of LGT Bank's capital and earnings as adequate, because we estimate the bank's risk-adjusted capital (RAC) ratio will remain comfortably in the 7.0%-10.0% range for the next two years.

We consider the acquisition represents a major step in LGT Bank's consistent growth strategy to diversify in Asia and the Middle East. Although the acquisition is large--approximately $20 billion in assets under management--LGT Bank's management has a tested track record of smooth operational and organizational integration of acquisitions in recent years, albeit smaller ones. The completion of the transaction is set to take place in the second quarter of 2017 and LGT Bank considers it is likely to receive the remaining approvals from the relevant authorities.

Moreover, our current ratings on LGT Bank continue to reflect our views on the bank's:

- Adequate business position, reflecting the bank's entrenched position as the leading financial institution in Liechtenstein and its well-established international franchise in private banking.
- Adequate capital and earnings.
- Strong risk position, considering that credit risk is very low, since lending does not constitute a main activity for the bank, the loan portfolio is principally collateralized, and the bank demonstrates an outstanding loan-loss track record, also in comparison with its private bank peers.
- Average funding and adequate liquidity, since the bank is chiefly a deposit-funded institution.

LGT Bank's stable outlook reflects our expectation that over a 24-month-horizon the bank will maintain its robust earnings, capital, and risk profile while defending its strong domestic home market franchise and pursuing its accelerated international growth strategy.

Although not expected, we would consider lowering the ratings if LGT Bank were to fail to replenish its weakened capitalization adequately from its inorganic growth strategy as measured by falling below our 7% RAC ratio threshold, or if the bank were to experience major performance, risk, or integration setbacks. We consider an upgrade to be even less likely, because this would require the bank to materially increase its sustainable RAC and ALAC buffers to mitigate bail-in risk to senior unsecured creditors while at the same time demonstrating a robust superior franchise and financial metrics in line with peers at a higher rating level.

VP BANK

We affirmed our long- and short-term counterparty credit ratings on VP Bank at 'A-/A-2' and revised the outlook to positive.

Following the change in the likelihood of government support in Liechtenstein to uncertain, we removed the one notch of government support and simultaneously removed the negative one-notch adjustment that anticipated the waning government support in the rating composition.

Our current ratings on VP Bank continue to reflect our views on the bank's:

- Weak business position, reflecting the bank's niche position in the global private-banking business.
- Very strong capital and earnings, also in a global context.
- Adequate risk position, considering that credit risk is very low, since lending activities are highly collateralized.
- Average funding and adequate liquidity, since the bank is chiefly a deposit-funded institution.

The outlook revision to positive from stable reflects two factors: primarily our view that the bank could potentially benefit from one notch of ALAC uplift, but also the possibility of improvement in its business position.

VP Bank already has total adjusted capital around 3% beyond the minimum threshold for the assigned capital and earnings score, and could yet qualify for ALAC uplift. A statutory subordination of its senior unsecured bonds or a ramp up of contractually subordinated instruments could lift the ALAC buffer above our 5% threshold for ALAC uplift. We expect to have more clarity on the local MREL framework in the next 12-24 months.

We could also consider an upgrade if we saw progress in VP Bank's business position, such that the bank increases its assets under management organically and so improves its performance compared with its peer group.

We could revise the outlook to stable if the national implementation of an MREL framework and VP Bank's entity-specific buffers are not likely to result in a sufficient sustainable ALAC buffer to protect senior unsecured creditors. We could also revise the outlook to stable if we saw fewer prospects for an improving business position.

RELATED CRITERIA

- General Criteria: Guarantee Criteria, Oct. 21, 2016
- Criteria - Financial Institutions - Banks: Bank Rating Methodology And Assumptions: Additional Loss-Absorbing Capacity, April 27, 2015
- General Criteria: Group Rating Methodology, Nov. 19, 2013
- Criteria - Financial Institutions - Banks: Quantitative Metrics For

Rating Banks Globally: Methodology And Assumptions, July 17, 2013
- Criteria - Financial Institutions - Banks: Revised Market Risk Charges For Banks In Our Risk-Adjusted Capital Framework, June 22, 2012
- Criteria - Financial Institutions - Banks: Banking Industry Country Risk Assessment Methodology And Assumptions, Nov. 09, 2011
- Criteria - Financial Institutions - Banks: Banks: Rating Methodology And Assumptions, Nov. 09, 2011
- Criteria - Financial Institutions - Banks: Bank Capital Methodology And Assumptions, Dec. 06, 2010
- Criteria - Financial Institutions - Banks: Methodology For Mapping Short- And Long-Term Issuer Credit Ratings For Banks, May 04, 2010
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009
- Criteria - Financial Institutions - Banks: Commercial Paper I: Banks, March 23, 2004

RELATED RESEARCH
- Various German Banks' Snr Unsecured Debt Lowered/Affirmed After Notes Review; Off Watch; Four Banks Remain On Watch, Feb. 9, 2017
- Liechtenstein-Based LGT Bank 'A+/A-1' Ratings On CreditWatch Negative On Private Banking Business Acquisition, Dec. 9, 2016
- Banking Industry Country Risk Assessment: Liechtenstein, Dec. 6, 2016
- LGT Bank AG, Sept. 2, 2016
- VP Bank AG, Aug. 12, 2016
- As The Tier 3 Ball Starts To Roll, European Banks Continue To Plot Their Bail-In Buffers, June 6, 2016

RATINGS LIST

* * * * * * * * * * * * * * * * LGT Bank AG * * * * * * * * *

Ratings Affirmed; CreditWatch Action

	To	From
LGT Bank AG		
Counterparty Credit Rating	A+/Stable/A-1	A+/Watch Neg/A-1
Senior Unsecured	A+	A+/Watch Neg
LGT Finance Ltd.		
Senior Unsecured*	A+	A+/Watch Neg

*Guaranteed by LGT Bank AG.

* * * * * * * * * * * * * * * * VP Bank AG * * * * * * * * * *

Ratings Affirmed; Outlook Action

	To	From
VP Bank AG		

Counterparty Credit Rating	A-/Positive/A-2	A-/Stable/A-2
Senior Unsecured	A-	A-

Additional Contact:
Financial Institutions Ratings Europe; FIG_Europe@spglobal.com