MOODY'S
INVESTORS SERVICE

Rating Action: Moody's assigns Aa2 rating to Zuercher Kantonalbank's Tier 2 subordinated debt

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Frankfurt am Main, April 04, 2022 -- Moody's Investors Service (Moody's) has today assigned a Aa2 foreign currency subordinated debt rating to the proposed new Euro-denominated Tier 2 capital-eligible debt of Zuercher Kantonalbank (ZKB). The subordinated debt instrument carries a point of non-viability (PONV) loss absorption feature and has a six-year maturity with a one-off issuer call date after five years.

The rating is subject to the receipt of final documentation, the terms and conditions of which are not expected to change in any material way from the draft documents that Moody's has reviewed.

All other ratings and rating assessments as well as corresponding outlooks of ZKB are unaffected by today's rating action.

RATINGS RATIONALE

ASSIGNMENT OF Aa2 SUBORDINATED DEBT RATING

The Aa2 rating assigned to the proposed subordinated debt instrument reflects ZKB's aa1 Adjusted Baseline Credit Assessment (BCA), which incorporates a three-notch affiliate support uplift from the bank's a1 BCA because of a maintenance guarantee from the bank's sole owner, the Canton of Zurich. The maintenance guarantee requires the canton to inject capital into ZKB, in case of need, until the canton defaults itself. The Aa2 rating further incorporates the results of Moody's Advanced Loss Given Failure (LGF) analysis, yielding a one-notch downward adjustment from the bank's Adjusted BCA, as well as Moody's assumption of a low probability of sovereign government support for loss-absorbing instruments, resulting in no rating uplift.

Given the proposed volume of subordinated debt and limited loss protection from subordination in the form of residual equity and Additional Tier 1 (AT1) instruments, the rating agency's Advanced LGF analysis indicates a high loss given failure for ZKB's proposed subordinated debt instrument, resulting in a one-notch downward adjustment from the bank's aa1 Adjusted BCA to reflect the expected loss severity of these instruments at the bank's PONV.

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

An upgrade of ZKB's subordinated debt rating could be driven by an upgrade of the bank's BCA, which could result from a combination of materially reduced concentration risks, significantly higher profitability, and an outsized shift in funding towards granular deposits. The instrument's rating could also be upgraded because of an improved result from Moody's Advanced LGF analysis, in particular if caused by meaningful issuance of instruments subordinated to the proposed Tier 2 instrument, thereby leading to lower loss given failure for the bank's subordinated debt.

A downgrade of ZKB's subordinated debt rating could be prompted by a downgrade of the bank's BCA, which could be driven by increased asset risk combined with a lower buffer from its capital ratios and depressed profitability. Furthermore, a deteriorating liquidity profile could exert downward pressure on the bank's BCA. A downgrade of the subordinated debt rating could also result from a deterioration of the canton's creditworthiness or if the guarantee framework the canton provides to ZKB were altered

PRINCIPAL METHODOLOGY

The principal methodology used in this rating was Banks Methodology published in July 2021 and available at https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_1269625 . 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.

For ratings issued on a program, series, category/class of debt or security this announcement provides certain regulatory disclosures in relation to each rating of a subsequently issued bond or note of the same series, category/class of debt, security or pursuant to a program for which the ratings are derived exclusively from existing ratings in accordance with Moody's rating practices. For ratings issued on a support provider, this announcement provides certain regulatory disclosures in relation to the credit rating action on the support provider and in relation to each particular credit rating action for securities that derive their credit ratings from the support provider's credit rating. For provisional ratings, this announcement provides certain regulatory disclosures in relation to the provisional rating assigned, and in relation to a definitive rating that may be assigned subsequent to the final issuance of the debt, in each case where the transaction structure and terms have not changed prior to the assignment of the definitive rating in a manner that would have affected the rating. For further information please see the ratings tab on the issuer/entity page for the respective issuer on www.moodys.com.

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The rating has been disclosed to the rated entity or its designated agent(s) and issued with no amendment resulting from that disclosure.

This rating is solicited. Please refer to Moody's Policy for Designating and Assigning Unsolicited Credit Ratings available on its website www.moodys.com.

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Moody's general principles for assessing environmental, social and governance (ESG) risks in our credit analysis can be found at http://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_1288235 .

The Global Scale Credit Rating on this Credit Rating Announcement was issued by one of Moody's affiliates outside the UK and is endorsed by Moody's Investors Service Limited, One Canada Square, Canary Wharf, London E14 5FA under the law applicable to credit rating agencies in the UK. Further information on the UK endorsement status and on the Moody's office that issued the credit rating is available on www.moodys.com.

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