

CREDIT OPINION

17 November 2021

Update

✓ Rate this Research

RATINGS

St. Galler Kantonalbank AG

| | |
|-------------------|---|
| Domicile | St. Gallen, Switzerland |
| Long Term CRR | Aa1 |
| Type | BACKED LT Counterparty Risk Rating - Fgn Curr |
| Outlook | Not Assigned |
| Long Term Debt | Aa2 |
| Type | BACKED Senior Unsecured - Dom Curr |
| Outlook | Stable |
| Long Term Deposit | Aa1 |
| Type | BACKED LT Bank Deposits |
| Outlook | Stable |

Please see the [ratings section](#) at the end of this report for more information. The ratings and outlook shown reflect information as of the publication date.

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St. Galler Kantonalbank

Update to credit analysis

Summary

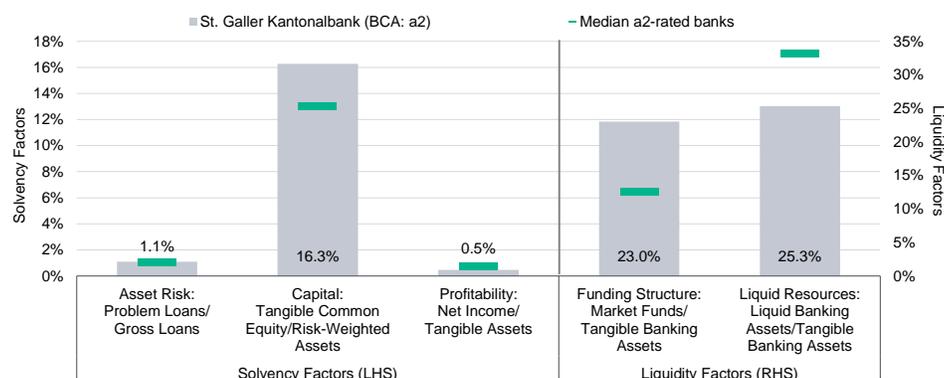
We assign Aa1(stable)/P-1 backed deposit ratings and an Aa2(stable) backed senior unsecured debt rating to [St. Galler Kantonalbank](#) (SGKB). Furthermore, we assign an a2 Baseline Credit Assessment (BCA) and an a1 Adjusted BCA to SGKB.

SGKB's Aa1 backed deposit ratings reflect its a2 BCA, one notch of rating uplift from affiliate support because of the majority ownership by the Canton of St. Gallen and the bank's important role in the region, and the application of our Advanced Loss Given Failure (LGF) analysis to its liabilities, which indicates an extremely low loss given failure and results in three notches of rating uplift. We do not incorporate rating uplift from sovereign government support in SGKB's deposit ratings due to the bank's small domestic market share and relatively low importance to the Swiss banking system.

SGKB's a2 BCA reflects the bank's solid capitalisation and its balanced liquidity and funding profiles benefitting from low funding costs and continued market access even in a more stressed environment owing to the canton's deficiency guarantee. The BCA also takes account of SGKB's sound asset quality, despite significant geographical concentrations.

Exhibit 1

Rating Scorecard SGKB - Key financial ratios



Source: Moody's Financial Metrics

Credit strengths

- » The Canton of St. Gallen provides a deficiency guarantee (fully guaranteeing all the bank's senior liabilities)
- » The bank's solid capital ratios provide a strong buffer against downside risks
- » Market funding reliance is balanced by the deficiency guarantee of the canton

Credit challenges

- » Geographically concentrated loan book with significant exposure to residential real estate
- » Only moderate profitability

Outlook

- » The stable outlook reflects our expectation that the key credit metrics of SGKB, including its liability structure, will remain broadly unchanged. We also do not expect any change in the guarantee framework the canton provides to SGKB.

Factors that could lead to an upgrade

- » Although unlikely given the already high level, SGKB's ratings could be upgraded if the bank's standalone creditworthiness improves significantly, resulting from a combination of materially reduced concentration risks, significantly higher profitability, and an improved combined liquidity profile.
- » The bank's backed senior unsecured debt rating could be upgraded if the creditworthiness of the Canton of St. Gallen improves. The bank's subordinated, junior subordinated, and senior unsecured debt ratings could also benefit from higher rating uplift from our Advanced LGF analysis, if material volumes of additional subordinated instruments were to be issued.

Factors that could lead to a downgrade

- » Downward pressure on the bank's ratings could result from a downgrade of the bank's BCA or from a material deterioration of the canton's creditworthiness. The bank's backed long-term ratings could also be downgraded as result of a change in the bank's liability structure potentially leading to a lower rating uplift as a result of our Advanced LGF analysis.
- » The bank's BCA could be downgraded if its asset risk – predominantly stemming from its real estate lending book – would increase as reflected in sustainably higher problem loans, combined with lower cushions from its capital ratios and depressed profitability. Furthermore, a deteriorating liquidity profile could exert downwards rating pressure.

This publication does not announce a credit rating action. For any credit ratings referenced in this publication, please see the ratings tab on the issuer/entity page on www.moody's.com for the most updated credit rating action information and rating history.

Key indicators

Exhibit 2

St. Galler Kantonalbank AG (Consolidated Financials) [1]

| | 06-21 ² | 12-20 ² | 12-19 ² | 12-18 ² | 12-17 ² | CAGR/Avg. ³ |
|--|--------------------|--------------------|--------------------|--------------------|--------------------|------------------------|
| Total Assets (CHF Billion) | 39.5 | 38.5 | 35.9 | 33.1 | 32.6 | 5.6 ⁴ |
| Total Assets (USD Billion) | 42.7 | 43.6 | 37.1 | 33.6 | 33.5 | 7.2 ⁴ |
| Tangible Common Equity (CHF Billion) | 2.6 | 2.6 | 2.6 | 2.4 | 2.3 | 3.0 ⁴ |
| Tangible Common Equity (USD Billion) | 2.8 | 2.9 | 2.7 | 2.4 | 2.4 | 4.6 ⁴ |
| Problem Loans / Gross Loans (%) | 1.0 | 1.1 | 1.1 | 1.2 | 2.1 | 1.3 ⁵ |
| Tangible Common Equity / Risk Weighted Assets (%) | 16.3 | 16.6 | 17.5 | 16.2 | 15.9 | 16.5 ⁶ |
| Problem Loans / (Tangible Common Equity + Loan Loss Reserve) (%) | 10.6 | 11.8 | 10.9 | 12.4 | 22.1 | 13.6 ⁵ |
| Net Interest Margin (%) | 0.8 | 0.8 | 0.9 | 0.9 | 0.9 | 0.9 ⁵ |
| PPI / Average RWA (%) | 1.4 | 1.3 | 1.3 | 1.2 | 1.3 | 1.3 ⁶ |
| Net Income / Tangible Assets (%) | 0.5 | 0.4 | 0.5 | 0.5 | 0.5 | 0.5 ⁵ |
| Cost / Income Ratio (%) | 56.5 | 59.2 | 59.9 | 62.2 | 59.9 | 59.6 ⁵ |
| Market Funds / Tangible Banking Assets (%) | 21.2 | 23.0 | 22.3 | 17.3 | 19.1 | 20.6 ⁵ |
| Liquid Banking Assets / Tangible Banking Assets (%) | 26.6 | 25.3 | 22.7 | 19.0 | 18.9 | 22.5 ⁵ |
| Gross Loans / Due to Customers (%) | 108.6 | 115.5 | 119.5 | 116.5 | 119.2 | 115.9 ⁵ |

[⁻] Further to the publication of our revised methodology in July 2021, only ratios from annual 2020 onwards included in this report reflect the change in analytical treatment of the "high-trigger" Additional Tier 1 instruments. [1] All figures and ratios are adjusted using Moody's standard adjustments. [2] Basel III - fully loaded or transitional phase-in; LOCAL GAAP. [3] May include rounding differences because of the scale of reported amounts. [4] Compound annual growth rate (%) based on the periods for the latest accounting regime. [5] Simple average of periods for the latest accounting regime. [6] Simple average of Basel III periods.

Sources: Moody's Investors Service and company filings

Profile

SGKB is a Swiss cantonal bank that operates mainly in the Canton of St. Gallen and Appenzell-Ausserrhoden, providing savings and credit services, as well as wealth management solutions to individuals and small and medium-sized businesses. The bank was founded in 1868 as a government-owned credit institution to promote regional economic development. As of 30 June 2021, the bank operated through a network of 40 banking outlets (including two German offices in Frankfurt and Munich) and employed about 1,100 full-time equivalent employees. As of the same date, the Canton of St. Gallen was the largest shareholder of the bank, with a 51% stake, which was reduced from 54.8% following a capital increase in May 2019. The canton is required by law to hold at least 51% of the bank's shares, which have been listed on the SIX Swiss Exchange since 2001.

For more information, please see our [Swiss Banking System Profile](#).

Weighted Macro Profile of Strong (+)

SGKB is focused on the Swiss market and its Weighted Macro Profile is therefore Strong (+), in line with the [Macro Profile](#) of Switzerland. The bank also has limited operations in Germany.

Detailed credit considerations

Narrow geographical focus and low loan-loss coverage are key drivers for asset risk

We assign an a2 Asset Risk score to SGKB, which is set two notches below the aa3 initial score. The negative adjustment reflects the bank's narrow geographical footprint and its more limited loan-loss coverage than that of its peers.

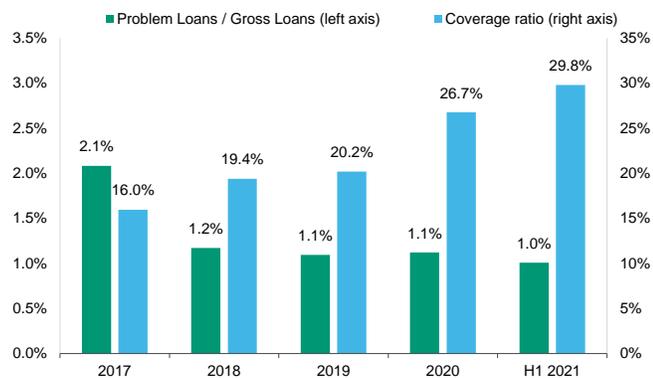
With problem loans/gross loans of 1.0% as of 30 June 2021, SGKB's problem loan ratio remains somewhat elevated compared to its Swiss banking peers, while its coverage ratio of 29.8% as of the same date also remains low when compared to its peers (despite a material improvement from the 20.2% recorded as of year-end 2019¹). The bank's exposure to regional large corporates as well as small and medium-sized enterprises results in higher problem loan ratios than what is reported for traditional retail mortgage loans in Switzerland. However, we believe that SGKB's risk management and controls allow for adequate assessment of the bank's inherent asset-quality risks, aided by a fair degree of diversification in its corporate loan book.

SGKB's residential and commercial mortgage loan book (CHF26.0 billion as of 30 June 2021), which is concentrated in the Canton of St. Gallen and Appenzell-Ausserrhoden, grew at a compound average growth rate of 4.4% during the 2008-2020 period, compared

with 3.9% for the Swiss market, partially driven by the takeover of Vadian Bank in 2014. The bank's mortgage book expanded by a further 2.8% during the first half of 2021 (H1 2021), which was again higher than the 2.6% growth in the overall Swiss domestic mortgage market. The above-average expansion of SGKB's mortgage book in recent years has increased the bank's susceptibility to potential shocks from the domestic real estate markets. However, we believe the bank would be well positioned to absorb any potential weakening of the Swiss housing market as its mortgage loan book is highly granular, with only a small proportion exhibiting a loan-to-value ratio above 60% (for further details, see our report [Swiss cantonal banks can absorb house price shock](#)).

Exhibit 3

SGKB's stock of problem loans decreased Coverage ratio remains below that of its peers

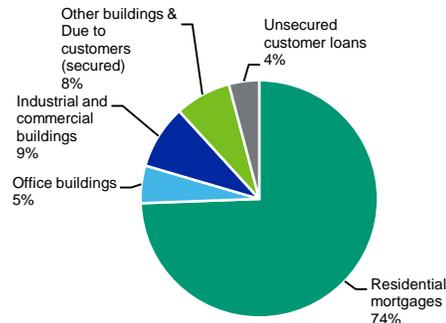


The problem loan ratio is in accordance with our definition; since 2018, according to IFRS9 reporting standards

Source: Company reports and Moody's Investors Service

Exhibit 4

SGKB's loan book largely consists of residential mortgages Total loan book: CHF28.1 billion as of year-end 2020



Source: Company reports and Moody's Investors Service

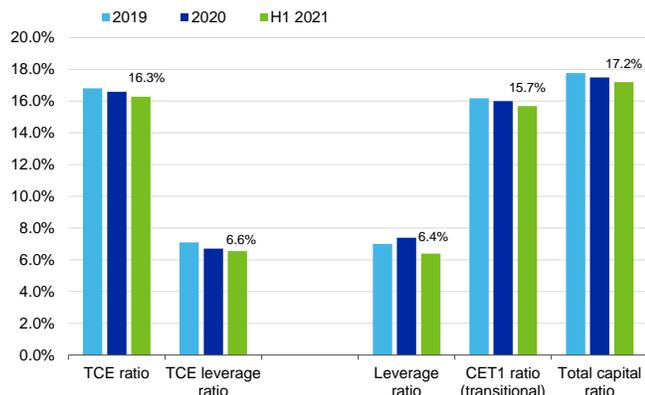
Solid capital ratios provide a growing buffer against downside risks

We assign a aa2 Capital score to SGKB, in line with the initial score. Our evaluation reflects the bank's tangible common equity (TCE) ratio of 16.3% as of 30 June 2021, slightly down from 16.6% as of year-end 2020, as well as its solid leverage ratios.

On 27 May 2019, SGKB completed a CHF176.5 million capital increase, which bolstered the bank's Common Equity Tier 1 (CET1) capital ratio by about one percentage point. Previously, SGKB's total regulatory capitalisation had benefitted from the issuance of new high-trigger Additional Tier 1 (AT1) and Tier 2 instruments in 2017. Overall, this helped to lift the bank's total capital ratio to 17.2% as of 30 June 2021 from 15.6% as of year-end 2016, providing a solid buffer against the 12.0% minimum total capital ratio requirement that the Swiss Financial Market Supervisory Authority (FINMA) has set for SGKB, given its classification as a Category 3 banking institution. On a CET1 basis, SGKB reported a 15.7% CET1 capital ratio as of 30 June 2021, which was slightly down from 16.0% as of year-end 2020 due to balance sheet and, hence, risk-weighted asset (RWA) growth. Compared to the bank's 7.8% minimum CET1 ratio requirement, the bank's headroom is still sizeable. No longer included in the bank's capital requirements is the countercyclical buffer requirement for residential mortgage exposures, which was revoked by the Swiss National Bank (SNB) and FINMA in March 2020 and which had resulted in a 1.0% add-on for SGKB in 2019.

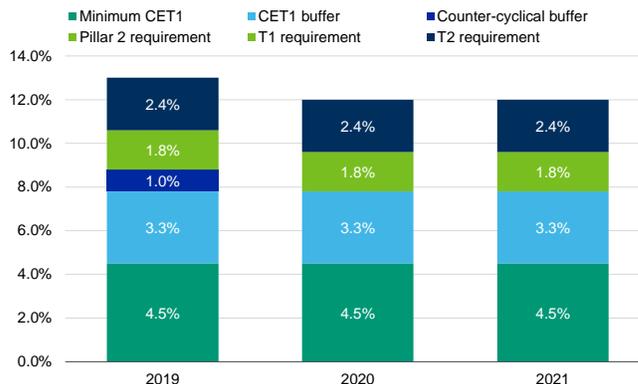
While the bank's risk-based capital ratios declined somewhat in H1 2021, SGKB reported a more material drop in its regulatory leverage ratio to 6.4% as of 30 June 2021, compared to 7.4% as of year-end 2020. This was due to the temporary exemption by FINMA, which allowed banks to exclude the deposits held at the SNB from the calculation of the leverage ratio in 2020. Based on our leverage measure of Tangible Common Equity (TCE) to tangible banking assets, the leverage ratio only softened marginally to 6.6% as of 30 June 2021 from 6.7% as of year-end 2020, reflecting a CHF0.7 billion or 1.7% increase in the balance sheet. In 2020, the bank's balance sheet had expanded more significantly by a CHF2.6 billion or 7.2%, reflecting an increase in liquid assets following the SNB's decision to increase the amount of sight deposits that banks can hold at 0% interest at the central bank²

Exhibit 5
SGKB exceeds its capital requirements



TCE = Tangible Common Equity (Moody's calculation); CET1 = Common Equity Tier 1
Source: Company reports and Moody's Investors Service

Exhibit 6
SGKB's capital requirements



Source: Company reports

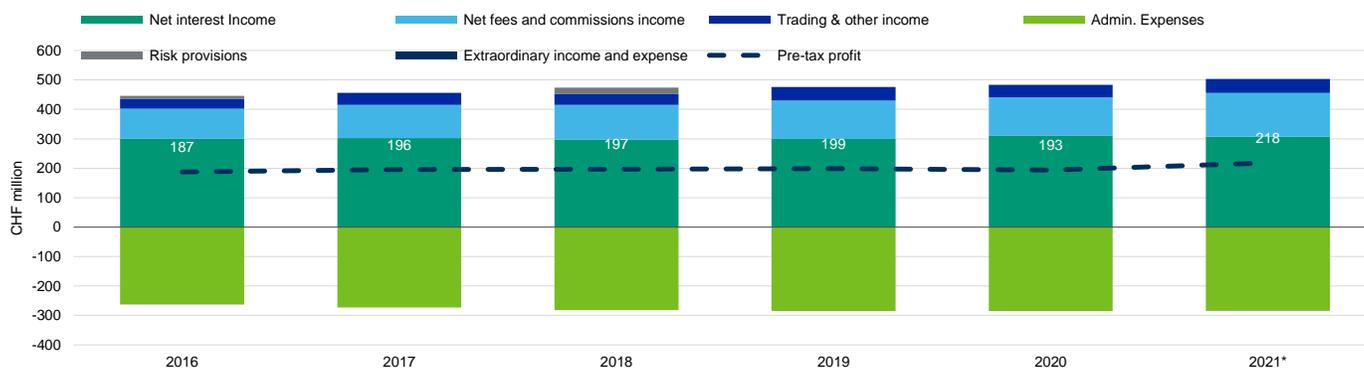
Adequate profitability metrics, despite a difficult market environment

We assign a ba1 Profitability score to SGKB, in line with the initial score, which is derived from the bank's 0.5% net income to tangible assets that was on recorded on average since 2018. The bank's return on assets has softened somewhat in recent years because of the ultralow interest-rate environment, which is likely to persist.

With net interest income representing about 60% of the bank's revenue and margin pressure continuing, SGKB aims to increase the share of fee and commission income from its wealth management operations to balance the impact of the ultralow interest-rate environment. This strategy was showing first signs of success in 2019 and 2020, as well as H1 2021. Hence, we expect SGKB's profitability, combined with continued sound cost discipline, to remain relatively resilient even if risk provisions start to rise again from the extremely low levels prior to the coronavirus crisis.

In H1 2021, SGKB reported an improved Moody's-adjusted net income of CHF92.5 million compared to H1 2020, when the bottom line result reached CHF84.5 million. The improvement was driven by higher net fee and commission income (up 14.6% or CHF9.5 million to CHF74.2 million) and higher trading revenues (up 27.5% or CHF4.5 million to CHF20.6 million) due to increased net new money, a beneficial performance of the stock market, and higher client trading activity, which more than offset a decline in net interest income (down 2.0% or CHF3.1 million to CHF153.5 million). Overall revenues thus increased by 5.2% or CHF12.5 million to CHF251.4 million, while operating expenses increased by 3.2% or CHF4.4 million to CHF142.2 million. Loan loss provisions and other provisions and losses were also still well contained and amounted to a net total of CHF2.2 million (CHF4.8 million in H1 2020).

Exhibit 7
SGKB's revenue is driven by net interest income



*annualised H1 2021 figures
Source: Company reports and Moody's Investors Service

Excellent access to capital markets and higher recourse to covered bonds imply strong market funding quality

The a1 assigned Funding Structure score is positioned three notches above the baa1 initial score. The score takes into account the deficiency guarantee provided by the Canton of St. Gallen on the bank's senior obligations.

Following several years of declines, SGKB's share of market funding has increased again in 2019 and 2020, because of the increase in the amount of sight deposits that banks can hold at 0% interest at the SNB, which are refinanced by market funding sources at negative rates in order to generate carry income. In the first half of 2021, market funds dropped again, however, reflecting a decline in interbank funding and the maturity of a CHF200 million senior unsecured bond.

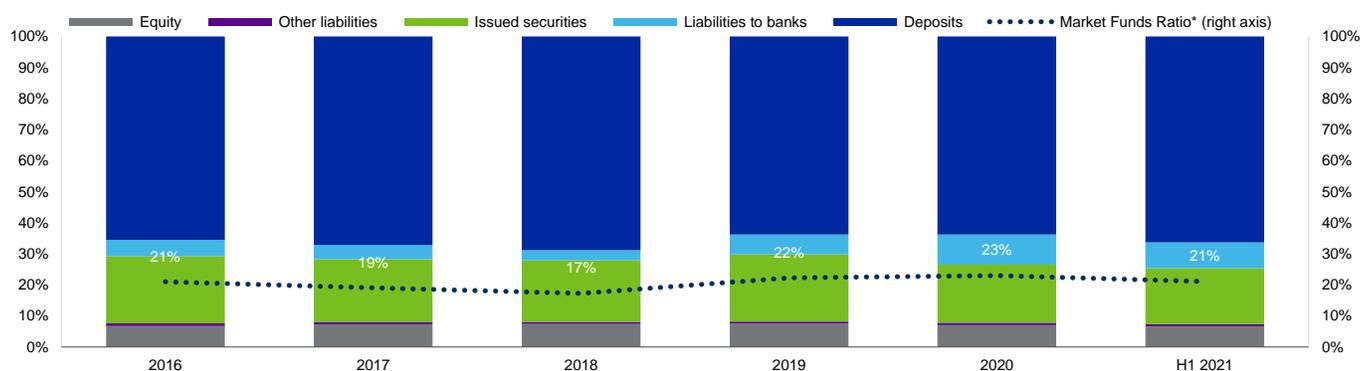
The bank's market funding to a large part consists of covered bonds (CHF4.1 billion as of 30 June 2021), limiting potential interest rate and refinancing risks for the bank owing to its more matched asset-liability profile. Market funding also comprised CHF3.3 billion of interbank deposits and CHF3.0 billion of senior unsecured funding as of 30 June 2021. Based on year-end 2020 data, 61% of the bank's covered bonds and 42% of its unsecured funding will mature after 2025.

SGKB's main funding source, however, remains its customer deposit base, which amounted to CHF26.0 billion as of first half end 2021 (66% of total assets; including Kassenobligationen), up from CHF24.3 billion as of year-end 2020.

Exhibit 8

SGKB has a strong deposit franchise

Market funding ratio increased again in 2019 and 2020



*Market funding ratio = Market funds/tangible banking assets.

Source: Company reports and Moody's Investors Service

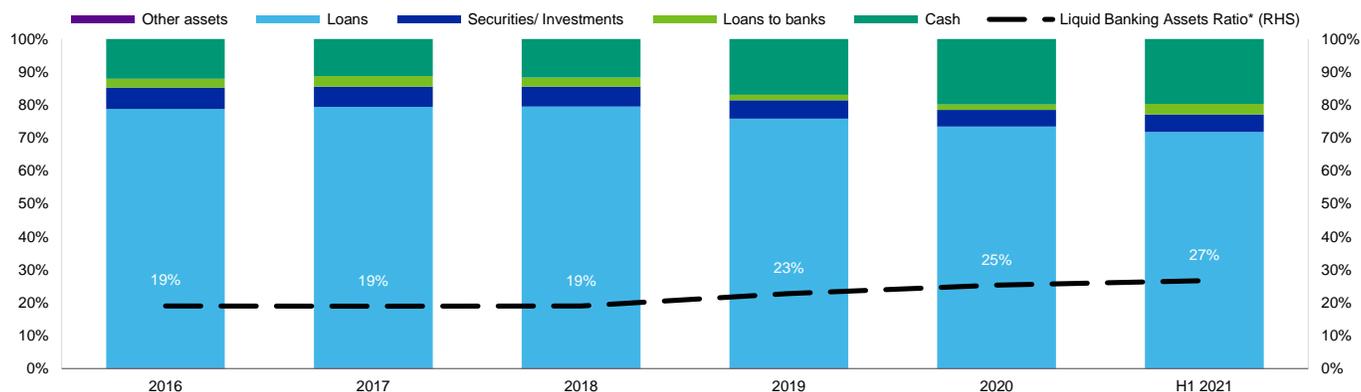
SGKB's liquid resources are adequate considering its market funding reliance

We assign a baa1 Liquid Resources score to SGKB, one notch below the a3 initial score, reflecting the bank's increased liquidity balances following the SNB's consecutive increase in the negative interest exemption threshold in November 2019 and April 2020, as well as some limited asset encumbrance.

As a share of tangible banking assets, SGKB's liquid assets of 26.6% exceeded the bank's market funds of 21.2% as of 30 June 2021. Although some of its domestic peers still have stronger reserves compared with their market funding reliance, we do regard the bank's liquid resources as adequate, also in light of the term structure of the market funding and the available guarantee, with both factors limiting refinancing risks.

During the first half of 2021, SGKB's cash and interbank assets increased to CHF9.0 billion from CHF8.2 billion, as a result of the higher volumes of sight deposits that can be placed at the SNB at 0% interest. Together with its CHF1.5 billion investment portfolio, which was broadly unchanged from year-end 2020, liquid assets thus represented 26.6% of SGKB's balance sheet as of 30 June 2021, up from 25.3% as of year-end 2020, while the bank's Liquidity Coverage Ratio (LCR) stood at 154% and 143% as of the same dates, respectively.

Exhibit 9

SGKB's liquidity balance has improved

*Liquid banking assets ratio = Liquid assets/tangible banking assets.

Source: Company reports and Moody's Investors Service

Environmental, social and governance (ESG) considerations

In line with our general view on the banking sector, SGKB has a low exposure to environmental risks (see our [environmental heat map](#)³ for further information).

For social risks, we also place SGKB in line with our general view for the banking sector, which indicates a moderate exposure (see our [social heat map](#)⁴). This includes considerations in relation to the coronavirus outbreak, given the substantial implications for public health and safety and the severe and extensive credit shock the pandemic has caused across many sectors, regions and markets.

Governance is highly relevant for SGKB, as it is to all participants in the banking industry. Governance risks are largely internal, rather than externally driven, and for SGKB, we do not have any particular governance concern⁵. Nonetheless, corporate governance remains a key credit consideration and requires ongoing monitoring.

Notching considerations

Affiliate support

SGKB benefits from parental support from the Canton of St. Gallen. Parental support reduces the probability of default, as it would be available to stabilise a distressed bank and not just compensate for losses in resolution.

We consider a high level of support, reflecting that the Canton of St. Gallen owns 51% of the share capital of SGKB, which, combined with the bank's economic and social role as a cantonal bank in the region, provides an incentive for the canton to inject capital into SGKB prior to failure, in case of need. In this assessment, we also consider the deficiency guarantee, which is an incentive for the canton to inject capital prior to failure. Parental support provides one notch of rating uplift from the a2 BCA, leading to an a1 Adjusted BCA.

Loss Given Failure analysis

SGKB is subject to Swiss banking regulations, which we consider an operational resolution regime. We therefore apply our Advanced LGF analysis, which takes into consideration the risks faced by the different debt and deposit classes across the liability structure at failure. In our Advanced LGF analysis, we assign a 100% probability to deposits being preferred to senior unsecured debt, thereby reflecting depositor preference by law in Switzerland.

We further assume residual tangible common equity of 3% and losses post-failure of 8% of tangible banking assets. In addition, we assume a 26% share of deposits being "junior" wholesale deposits, for which we factor in a 25% run-off prior to failure, while we assume a 5% run-off in preferred deposits. These ratios are in line with our standard assumptions. The results of our Advanced LGF analysis are:

- » For deposits and counterparty risk liabilities, our LGF analysis indicates an extremely low loss-given-failure, leading us to position their Preliminary Rating Assessments at aa1, three notches above the a1 Adjusted BCA.

- » For senior unsecured debt, our LGF analysis indicates a low loss-given-failure, leading us to position its Preliminary Rating Assessment at aa3, one notch above the a1 Adjusted BCA.
- » For junior subordinated debt (tier 2 hybrid instrument with a contractual write-down), our LGF analysis indicates a high loss-given-failure, leading us to position its Preliminary Rating Assessments at a2, one notch below the a1 Adjusted BCA.

High-trigger Additional Tier 1 (AT1) securities

The Baa1(hyb) rating assigned to SGKB's high-trigger AT1 instrument is positioned three notches below the bank's a1 Adjusted BCA. One notch reflects the high loss given failure that these securities are likely to face in a resolution scenario because of their deep subordination, small volume and limited protection from residual equity. Our rating for non-viability securities incorporates two additional notches to reflect the higher risk associated with the non-cumulative coupon skip and contractual write-down mechanisms, which could take effect before the issuer reaches the point of non-viability.

Government support considerations

We assess SGKB as government-backed by its regional authority, the Canton of St. Gallen, since it provides an explicit deficiency guarantee for its unsubordinated obligations.

However, since we expect that the Canton of St. Gallen will provide some support to SGKB prior to failure, and given the uplift provided by our Advanced LGF analysis for the bank's senior obligations, SGKB's backed deposit ratings, its backed Counterparty Risk Ratings and its backed Counterparty Risk Assessment do not benefit from further government support. The bank's Aa2 backed senior unsecured debt rating, however, incorporates one notch of (regional) government support uplift because of the deficiency guarantee.

SGKB's junior subordinate, and high-trigger AT1 instruments are not covered by the deficiency guarantee from the Canton of St. Gallen and we therefore assume a low likelihood of support, resulting in no government support uplift for these securities.

We also do not incorporate rating uplift from sovereign government support for SGKB's senior ratings due to the bank's small domestic market share and low importance to the Swiss banking system.

Counterparty Risk Ratings (CRRs)

SGKB's backed CRR are Aa1/P-1

The CRR are positioned three notches above the a1 Adjusted BCA because of uplift provided by our Advanced LGF analysis.

Counterparty Risk (CR) Assessment

SGKB's backed CR Assessment is Aa1(cr)/P-1(cr)

The CR Assessment is positioned three notches above the a1 Adjusted BCA because of uplift provided by our Advanced LGF analysis.

Because the CR Assessment captures the probability of default on certain senior operational obligations, rather than expected loss, we focus purely on subordination and take no account of the volume of the instrument class.

Methodology and scorecard

Methodology

The principal methodology we used in rating SGKB was [Banks Methodology](#), published in July 2021.

About Moody's Bank Scorecard

Our Bank Scorecard is designed to capture, express and explain in summary form our Rating Committee's judgment. When read in conjunction with our research, a fulsome presentation of our judgment is expressed. As a result, the output of our scorecard may materially differ from that suggested by raw data alone (though it has been calibrated to avoid the frequent need for strong divergence). The scorecard output and the individual scores are discussed in rating committees and may be adjusted up or down to reflect conditions specific to each rated entity.

Rating methodology and scorecard factors

Exhibit 10

St. Galler Kantonalbank AG

| Macro Factors | | | | | | | |
|---|-------------------------------|----------------------|---------------------------------|-----------------------|-----------------------------------|--------------------------------------|--|
| Weighted Macro Profile | | Strong + | 100% | | | | |
| Factor | Historic Ratio | Initial Score | Expected Trend | Assigned Score | Key driver #1 | Key driver #2 | |
| Solvency | | | | | | | |
| Asset Risk | | | | | | | |
| Problem Loans / Gross Loans | 1.1% | aa3 | ↔ | a2 | Geographical concentration | Collateral and provisioning coverage | |
| Capital | | | | | | | |
| Tangible Common Equity / Risk Weighted Assets (Basel III - transitional phase-in) | 16.3% | aa2 | ↔ | aa2 | Risk-weighted capitalisation | Expected trend | |
| Profitability | | | | | | | |
| Net Income / Tangible Assets | 0.5% | ba1 | ↔ | ba1 | Return on assets | Expected trend | |
| Combined Solvency Score | | a1 | | a2 | | | |
| Liquidity | | | | | | | |
| Funding Structure | | | | | | | |
| Market Funds / Tangible Banking Assets | 23.0% | baa1 | ↔ | a1 | Extent of market funding reliance | Market funding quality | |
| Liquid Resources | | | | | | | |
| Liquid Banking Assets / Tangible Banking Assets | 25.3% | a3 | ↔ | baa1 | Stock of liquid assets | Quality of liquid assets | |
| Combined Liquidity Score | | baa1 | | a2 | | | |
| Financial Profile | | | | | | | |
| Qualitative Adjustments | | | | Adjustment | | | |
| Business Diversification | | | | 0 | | | |
| Opacity and Complexity | | | | 0 | | | |
| Corporate Behavior | | | | 0 | | | |
| Total Qualitative Adjustments | | | | 0 | | | |
| Sovereign or Affiliate constraint | | | | Aaa | | | |
| BCA Scorecard-indicated Outcome - Range | | | | a1 - a3 | | | |
| Assigned BCA | | | | a2 | | | |
| Affiliate Support notching | | | | - | | | |
| Adjusted BCA | | | | a1 | | | |
| Balance Sheet | | | | | | | |
| | in-scope (CHF Million) | % in-scope | at-failure (CHF Million) | % at-failure | | | |
| Other liabilities | 9,118 | 23.1% | 11,270 | 28.5% | | | |
| Deposits | 26,007 | 65.9% | 23,354 | 59.1% | | | |
| Preferred deposits | 19,245 | 48.7% | 18,283 | 46.3% | | | |
| Junior deposits | 6,762 | 17.1% | 5,071 | 12.8% | | | |
| Senior unsecured bank debt | 2,976 | 7.5% | 3,476 | 8.8% | | | |
| Junior subordinated bank debt | 100 | 0.3% | 100 | 0.3% | | | |
| Preference shares (bank) | 100 | 0.3% | 100 | 0.3% | | | |
| Equity | 1,185 | 3.0% | 1,185 | 3.0% | | | |
| Total Tangible Banking Assets | 39,485 | 100.0% | 39,485 | 100.0% | | | |

| Debt Class | De Jure waterfall | | De Facto waterfall | | Notching | | LGF | Assigned LGF | Additional Notching | Preliminary Rating Assessment |
|---------------------------------------|-----------------------------------|----------------|-----------------------------------|----------------|----------|----------|-----|--------------|---------------------|-------------------------------|
| | Instrument volume + subordination | Sub-ordination | Instrument volume + subordination | Sub-ordination | De Jure | De Facto | | | | |
| Counterparty Risk Rating | 12.3% | 12.3% | 12.3% | 12.3% | 3 | 3 | 3 | 3 | 0 | aa1 |
| Counterparty Risk Assessment | 12.3% | 12.3% | 12.3% | 12.3% | 3 | 3 | 3 | 3 | 0 | aa1 (cr) |
| Deposits | 25.2% | 12.3% | 25.2% | 12.3% | 3 | 3 | 3 | 3 | 0 | aa1 |
| Senior unsecured bank debt | 12.3% | 3.5% | 12.3% | 3.5% | 1 | 1 | 1 | 1 | 0 | aa3 |
| Junior subordinated bank debt | 3.5% | 3.3% | 3.5% | 3.3% | -1 | -1 | -1 | -1 | 0 | a2 |
| Non-cumulative bank preference shares | 3.3% | 3.0% | 3.3% | 3.0% | -1 | -1 | -1 | -1 | -2 | baa1 |

| Instrument Class | Loss Given Failure notching | Additional notching | Preliminary Rating Assessment | Government Support notching | Local Currency Rating | Foreign Currency Rating |
|---------------------------------------|-----------------------------|---------------------|-------------------------------|-----------------------------|-----------------------|-------------------------|
| | | | | | | |
| Counterparty Risk Rating | 3 | 0 | aa1 | - | Aa1 | Aa1 |
| Counterparty Risk Assessment | 3 | 0 | aa1 (cr) | - | Aa1(cr) | |
| Deposits | 3 | 0 | aa1 | - | Aa1 | Aa1 |
| Senior unsecured bank debt | 1 | 0 | aa3 | - | Aa2 | |
| Junior subordinated bank debt | -1 | 0 | a2 | - | A2 (hyb) | |
| Non-cumulative bank preference shares | -1 | -2 | baa1 | - | Baa1 (hyb) | |

[1] Where dashes are shown for a particular factor (or sub-factor), the score is based on non-public information.

Source: Moody's Investors Service

Ratings

Exhibit 11

| Category | Moody's Rating |
|--------------------------------------|-----------------|
| ST. GALLER KANTONALBANK | |
| Outlook | Stable |
| Bkd Bank Deposits | Aa1/P-1 |
| Bkd Counterparty Risk Rating | Aa1/P-1 |
| Baseline Credit Assessment | a2 |
| Adjusted Baseline Credit Assessment | a1 |
| Bkd Counterparty Risk Assessment | Aa1(cr)/P-1(cr) |
| Bkd Senior Unsecured -Dom Curr | Aa2 |
| Jr Subordinate -Dom Curr | A2 (hyb) |
| Pref. Stock Non-cumulative -Dom Curr | Baa1 (hyb) |

Source: Moody's Investors Service

Endnotes

- 1** In 2020, SGKB for the first time accounted for the expected credit loss on its performing balance sheet and off-balance sheet exposures (following an approach similar to IFRS 9), which increased the bank's coverage ratio. The CHF36.1 million first-time implementation effect of this accounting change was mostly offset against the bank's reserve for general banking risk within shareholders' equity, which was reduced to zero as of year-end 2020 from CHF33.0 million as of year-end 2019, while the remaining CHF3.1 million charge was booked as loan loss provisions through the bank's income statement.
- 2** The SNB raised the negative interest exemption threshold for sight deposits to 25x the minimum reserve requirement from 20x on 1 November 2019, and to 30x on 1 April 2020.
- 3** Environmental risks can be defined as environmental hazards encompassing the impact of air pollution, soil/water pollution, water shortages, and natural and man-made hazards (physical risks). Additionally, regulatory or policy risks, such as the impact of carbon regulation or other regulatory restrictions, including related transition risks such as policy, legal, technology and market shifts, that could impair the evaluation of assets are an important factor. Certain banks could face a higher risk from concentrated lending to individual sectors or operations exposed to the aforementioned risks.
- 4** Social risk considerations represent a broad spectrum, including customer relations, human capital, demographic and societal trends, health and safety, and responsible production. The most relevant social risks for banks arise from the way they interact with their customers. Social risks are particularly high in the area of data security and customer privacy, which is partly mitigated by sizeable technology investments and banks' long track record of handling sensitive client data. Fines and reputational damage because of product mis-selling or other types of misconduct is a further social risk. Societal trends are also relevant in a number of areas, such as shifting customer preferences towards digital banking services increasing information technology costs, ageing population concerns in several countries affecting the demand for financial services or socially driven policy agendas that may translate into regulations that affect banks' revenue bases.
- 5** Corporate governance is a well-established key driver for banks and related risks are typically included in our evaluation of banks' financial profiles. Corporate governance weaknesses can lead to a deterioration in a bank's credit quality, while governance strengths can benefit its credit profile. Further, factors such as specific corporate behaviour, key person risk, insider and related-party risk, strategy and management risk factors, and dividend policy may be captured in individual adjustments to the BCA.

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