S&P Global
Ratings

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Research Update:

Commerzbank Outlook Revised To Positive On Improving Resilience From Strengthening Earnings; 'A-/A-2' Affirmed

November 10, 2023

Overview

- Commerzbank has reached key milestones in its multiyear transformation and realignment of its business model, primarily focused on deep cost and efficiency measures, and now shows improving profitability.
- This has laid the foundation to further improve its structural profitability under its ambitious revised strategic agenda announced Nov. 8, 2023.
- We have therefore revised our rating outlook on Commerzbank to positive from stable and affirmed our 'A-/A-2' ratings.
- The positive outlook indicates that we could raise the ratings if Commerzbank delivers on its financial targets and we observe strengthening resilience, while the bank maintains solid balance-sheet metrics.

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Rating Action

On Nov. 10, 2023, S&P Global Ratings revised its rating outlook on Commerzbank AG to positive from stable and affirmed its 'A-/A-2' long- and short-term issuer credit ratings.

We affirmed our ratings on the bank's senior unsecured, senior subordinated, and hybrid issues.

Rationale

We believe better earnings prospects can strengthen Commerzbank`s resilience.
Commerzbank has achieved key milestones in its multiyear transformation and realignment of its business model, which it began in early 2021 and focused primarily on deep cost and efficiency measures. The bank has exceeded many of its interim financial targets, strongly supported by rising interest rates in the eurozone and Poland. We think the successful turnaround has laid the

foundation for building a track record of improving profitability. We expect that better earnings generation would strengthen Commerzbank's resilience, since it provides additional capacity to absorb risks that may materialize and fund ongoing investments into the business model.

Management targets a material increase in profitability under its revised strategic plan. On Nov. 8, 2023, Commerzbank disclosed details of its strategic initiatives to increase its return on tangible equity (ROTE) to about 11%.5 by 2027 from the previous target of 7.3% and achieve an efficiency ratio of 55% after 60%. The bank reported a ROTE of 8.6% and efficiency ratio of 60% in the first nine months in 2023. Increasing the amount of less-cyclical and capital-light fee income through various product initiatives, and repricing of banking services, are intended to fuel higher earnings. Moreover, interest income is expected to continue to rise further toward 2027, despite the expectation of lower interest margins. If management executes the strategy as planned and improves earnings generation, resulting in greater resilience, we will likely consider revising our assessment of Commerzbank's stand-alone credit profile (SACP) to 'bbb+' from 'bbb'. An improvement would hinge on our perception that the revised strategy won't lead to higher risk-taking to increase profitability and we see ongoing solid going- and gone-concern capital and liquidity buffers supporting the ratings.

We see Commerzbank's goals as ambitious and that full achievement will be sensitive to market conditions beyond management`s control. In our view, it remains uncertain whether the bank will be able to substantially increase its fee income, after it shrank in 2023, primarily due to lower securities activity by private customers. It also remains unclear whether interest income can strengthen further from the expected cyclical peak in 2023, since we expect interest margins in Poland and Germany to decline again from 2024. Success will also largely depend on how the sentiment in the German economy translates into growth of the loan book, interest rate levels, the path of deposit volumes and rates in Germany, as well as revenue contribution from those modelled deposits, with some factors outside the bank's control. It also remains uncertain whether the Polish subsidiary mbank can contribute substantially to Commerzbank's financial objectives in the medium term. Similarly, it's unclear whether cost increases can be curtailed in an inflationary environment and asset quality can be maintained in the face of economic and geopolitical challenges.

We expect costs from mbank's Swiss franc retail mortgage portfolio to moderate from 2024. We expect mbank to continue to incur significant costs from its exposure to legacy foreign currency-denominated mortgage loans because the associated litigation risk remains significant. We view this primarily as a risk to mbank's earnings, rather than capital, since mbank delivers strong operational performance absent any exceptional costs. In our base-case scenario, we assume continued high provisions but expect them to be significantly lower than in 2023. This should result in a significant improvement in mbank's net profit and support the group's financial objectives.

Commerzbank is committed to distributing excess capital, thereby putting pressure on its risk-adjusted capital buffers. In line with management's updated capital policy, we forecast meaningful and increasing capital distributions. These, in combination with a return to more material lending growth, will, in our view, likely reduce its risk-adjusted capital ratio to less than 10% from 2025 (see "Commerzbank's New Capital Policy Underpins Expectations And Higher Profit Targets May Add Support In The Medium Term," published Sept. 29, 2023). All distributions remain subject to a minimum common equity tier 1 (CET1) of 13.5% and a minimum 250-basis-point (bps) buffer against the maximum distributable amount (MDA). Commerzbank's

CET1 ratio was 14.6% on Sept. 30, 2023, 448 bps above the MDA threshold for 2023, leaving plenty of room for capital distributions.

Outlook

Our positive rating outlook on Commerzbank reflects our view that better earnings generation could strengthen the bank's resilience. We could raise the ratings in the next 12 months if management executes on its strategic measures and improves the bank's structural profitability. A positive rating action would also depend on the bank maintaining a robust balance sheet, solid capital buffers, and liquidity metrics.

Upside scenario

If we see Commerzbank strengthening its business position by establishing a track record of stronger, more consistent profitability, we could revise our assessment of its SACP to 'bbb+' and raise our long- and short-term ratings on the bank and its debt instruments.

We may alternatively raise the ratings if we have greater confidence that the RAC ratio would remain solidly above 10% while the bank maintained strong asset quality.

Downside scenario

We could revise the outlook to stable if management seemed likely unable to improve the bank's structural profitability, or if our economic forecasts weaken sharply, implying pressure on fee income and materially higher credit losses than currently anticipated.

Ratings Score Snapshot

	To	From
Issuer Credit Rating	**A-/Positive/A-2**	**A-/Stable/A-2**
SACP	bbb	bbb
Anchor	bbb+	bbb+
Business position	Moderate (-1)	Moderate (-1)
Capital and earnings	Adequate (0)	Adequate (0)
Risk position	Adequate (0)	Adequate (0)
Funding	Adequate (0)	Adequate (0)
Liquidity	Adequate (0)	Adequate (0)
Comparable ratings analysis	0	0
Support	+2	+2
ALAC support	+2	+2
GRE support	0	0
Group support	0	0
Sovereign support	0	0

	To	From
Issuer Credit Rating	**A-/Positive/A-2**	**A-/Stable/A-2**
Additional factors	0	0

SACP--Stand-alone credit profile. ALAC--Additional loss-absorbing capacity. GRE--Government-related entity.

Related Criteria

- General Criteria: Hybrid Capital: Methodology And Assumptions, March 2, 2022
- 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: 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: Principles Of Credit Ratings, Feb. 16, 2011

Related Research

- Commerzbank's New Capital Policy Underpins Expectations And Higher Profit Targets May Add Support In The Medium Term, Sept. 29, 2023
- Rating Actions On Three Polish Banks Reflect Differing Provisioning Needs Following ECJ Ruling, June 27, 2023
- Banking Industry Country Risk Assessment: Germany, June 6, 2023
- Commerzbank AG Upgraded To 'A-/A-2' On Stronger Bail-In-Able Debt Buffer; Outlook Stable, March 23, 2023
- German Banks In 2023: Well Placed To Withstand Economic Challenges, Feb. 21, 2023

Ratings List

Ratings Affirmed	
Commerzbank AG	
Resolution Counterparty Rating	A/--/A-1
Commerzbank AG	
Senior Unsecured	A-

Senior Unsecured	A-p	
Senior Subordinated	BBB-	
Subordinated	BB+	
Junior Subordinated	BB-	
Commercial Paper	A-2	
Commerzbank U.S. Finance Inc.		
Commercial Paper	A-2	
Dresdner Funding Trust I		
Junior Subordinated	BB-	
Ratings Affirmed; CreditWatch/Outlook Action		
	To	**From**
Commerzbank AG		
Issuer Credit Rating	A-/Positive/A-2	A-/Stable/A-2

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.spglobal.com/ratings for further information. A description of each of S&P Global Ratings' rating categories is contained in "S&P Global Ratings Definitions" at https://disclosure.spglobal.com/ratings/en/regulatory/article/-/view/sourceId/504352. Complete ratings information is available to RatingsDirect subscribers at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.spglobal.com/ratings. Alternatively, call S&P Global Ratings' Global Client Support line (44) 20-7176-7176.