

# RatingsDirect®

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## PostFinance AG

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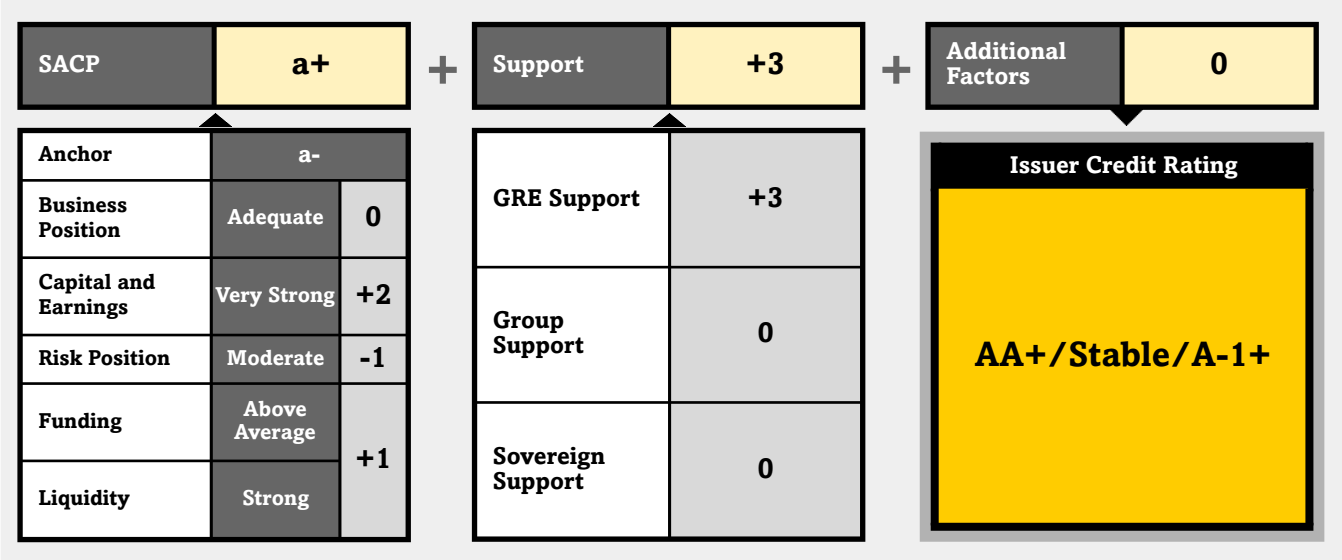
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# PostFinance AG



## Major Rating Factors

Strengths:	Weaknesses:
<ul style="list-style-type: none"> <li>Legally mandated provider of essential banking services in Switzerland.</li> <li>Robust capitalization underpinned by sound earnings.</li> <li>Above-average funding profile and superior liquidity position.</li> </ul>	<ul style="list-style-type: none"> <li>Narrow business model, due to a legal restriction to extending loans to Swiss households and companies.</li> <li>Large single-name and sector concentrations in the investment portfolio.</li> </ul>

## Outlook: Stable

Standard & Poor's Ratings Services' stable outlook on PostFinance AG reflects that on its ultimate owner, the Swiss Confederation. The outlook also reflects our view of PostFinance as a government-related entity (GRE) with an extremely high likelihood of receiving extraordinary government support if needed, which we expect will continue over the next two years. We also anticipate that the company will maintain a sound stand-alone credit profile (SACP).

In the unlikely event of a change in PostFinance's role for and link with the Swiss government, we may review our assessment of PostFinance as a GRE.

We could revise the SACP downward if PostFinance adopted less prudent capital and investment policies, leading to higher risks in its investment portfolio. However, the ratings would be unaffected as long as the SACP is at or above 'bb+' according to our GRE criteria.

Rating upside is remote at this stage because we do not believe the bank is able to adjust its comparatively concentrated business model over the medium term.

## Rationale

The starting point for our ratings on PostFinance is the 'a-' anchor, which reflects blended economic risk from investment exposures and its operation in Switzerland. We consider PostFinance to have an "adequate" business position, as our criteria define this term, as one of the largest deposit-taking institutions in Switzerland. It also has "very strong" capital and earnings, mainly based on our projection of a risk-adjusted capital (RAC) ratio of about 30% over the next 12-18 months. Moreover, PostFinance has a "moderate" risk position, owing to single-name and sector concentrations in its large investment portfolio; "above average" funding; and "strong" liquidity as cash provider to the domestic interbank market. The SACP is 'a+'.

We consider that PostFinance plays a critical role for the Swiss government and that it has a very strong link with the state. Consequently, we see an extremely high likelihood of extraordinary government support for PostFinance and add three notches of uplift to SACP.

### Anchor: 'a-' to reflect economic risk in the investment portfolio and industry risk in Switzerland

Our bank criteria use our Banking Industry Country Risk Assessment (BICRA) to determine a bank's anchor, the starting point in assigning an issuer credit rating. Our anchor for a commercial bank operating only in Switzerland is 'a-'.

The BICRA score includes our evaluation of economic risk. In this respect, we view Switzerland as a highly diversified and competitive economy, benefiting from one of the highest GDPs per capita in the world and very robust government finances. We believe that large parts of the Swiss banking market demonstrate a conservative risk and lending culture, which has accompanied moderate growth of house prices and loan portfolios.

Because PostFinance has no lending business, we consider the weighted-average economic risk in countries PostFinance is exposed to through its large investment portfolio. About 30% of the portfolio relates to countries with comparatively higher economic risk than Switzerland. Therefore the anchor is sensitive to an increase of exposures in such countries.

The Swiss banking industry is supported by its sizable and very stable customer deposit base. Pure domestic Swiss banks have not loosened credit standards in recent years, thanks to sound earnings potential from core products. We consider regulatory standards to be more stringent than in other developed countries.

**Table 1**

<b>PostFinance AG Key Figures</b>		
	<b>--Year-ended Dec. 31--</b>	
<b>(Mil. CHF)</b>	<b>2014*</b>	<b>2013</b>
Adjusted assets	119,760.5	115,218.0
Customer loans (gross)	10,423.4	9,895.0
Adjusted common equity	5,104.5	4,907.0
Operating revenues	778.0	1,481.0
Noninterest expenses	490.0	992.0
Core earnings	218.9	410.3

**Table 1****PostFinance AG Key Figures (cont.)**

\*Data as of June 30.

CHF--CHF-Swiss Franc.

**Business position: One of the largest retail banks in Switzerland, but with a narrow business model**

We regard PostFinance's business position as "adequate." This reflects our view of PostFinance as one of Switzerland's largest retail banks, with 2.9 million customers and a solid market share of 14% in customer deposits. The bank has a public mandate to provide essential banking services in Switzerland.

PostFinance is a fully-owned subsidiary of Die Schweizerische Post AG (DSP; nonoperating holding company of the Swiss Post group), and its assets totaled Swiss franc (CHF) 121 billion (about €120 billion) as of June 30, 2014. PostFinance was legally separated from DSP on June 26, 2013. Since receiving a full banking license in 2013, it is now regulated by the Swiss Financial Market Supervisory Authority and has become a member of the Swiss Deposit Protection scheme. Under Swiss postal law, PostFinance provides basic services for payment transactions on behalf of DSP and is party to two-thirds of the payment transactions in Switzerland. PostFinance's services are available in the Swiss Post group's about 1,700 post offices, including through 45 PostFinance branches in larger post centers.

We do not expect PostFinance's business model to change in the medium term. PostFinance is legally not permitted to lend but indirectly provides mortgages and other loans through partner banks, which act as risk-takers, to complement its product offering. Foreign operations are limited to payment transactions abroad and we don't expect PostFinance to expand beyond the current scope. We view positively PostFinance efforts to test new products as evidenced by the establishment of its subsidiary TWINT AG, which is active in the development of new mobile payment systems. We expect this to be key to remaining competitive amid extremely rapid changes in payment systems.

Without lending business, PostFinance will likely continue placing its excess liquidity at the Swiss National Bank and in international capital markets. Consequently, the main source (60%-65%) of its comparatively stable revenue is net interest income from its large bond portfolio. Net commission income from payment services, PostFinance cards, sale of savings and investment products, and loan intermediation generates 20% of income; and other activity, including foreign currency trading, the remaining 10%. Although we anticipate that the service and advisory business will gain importance over time, we don't expect PostFinance's revenue structure to change significantly over the next two years.

In our view, management demonstrates a low risk appetite and we expect it to maintain its conservative investment policy defined by country, counterparty, and rating limits. The owner's targets are reasonable and support our assessment of PostFinance's prudent management and strategy.

**Table 2****PostFinance AG Business Position**

	<u>--Year-ended Dec. 31--</u>	
(%)	2014*	2013
Loan market share in country of domicile	0.0	0.0
Total revenues from business line (currency in millions)	782.0	1,552.0
Commercial & retail banking/total revenues from business line	100.0	100.0
Return on equity	3.5	3.9

**Table 2****PostFinance AG Business Position (cont.)**

\*Data as of June 30.

**Capital and earnings: Robust capitalization following the separation from DSP**

We view PostFinance's capital and earnings as "very strong" compared with all banks we rate globally.

We project PostFinance's risk-adjusted capital (RAC) ratio to be about 30% over the next 18-24 months, after 29.3% on Dec. 31, 2013. The forecast RAC ratio is one of the highest among all banks we rate globally.

In our base case, we expect PostFinance to generate relatively stable net interest income of CHF950 million-CHF1,000 million in 2015-2016 from its investment portfolio. We anticipate PostFinance will increase its investment activity in the capital markets in 2015, under its conservative policy. The recent decision by the Swiss National Bank (SNB) to introduce negative interest rates on sight deposits placed at the central bank (increased to 0.75% on balances exceeding a given exemption threshold on Jan. 15, 2015) could accelerate the process. At the same time, we anticipate a gradual increase of net commission and fee income from growth in current activities and of foreign currency trading income.

PostFinance will, in our view, remain the main profit contributor to the Swiss Post group and we expect it to upstream a major part of its net annual profit of CHF200 million-CHF250 million (under Swiss bank accounting guidelines) to DSP in 2015-2016. However, we expect amortization of goodwill (CHF200 million annually until 2022) to allow PostFinance to build up its capital over the next years until goodwill is fully amortized.

PostFinance's quality of capital is very strong, in our view, because its total adjusted capital (TAC), our measure of loss-absorbing capital, consists mainly of paid-in capital. We believe PostFinance's earnings will remain stronger than the industry average, supporting the bank's solid capital position. We estimate PostFinance's three-year average earnings buffer to be higher than 200 basis points, which indicates that its earnings have an excellent capacity to cover normalized losses. However, PostFinance's operating efficiency is weaker than that of Swiss peers, in our view; we project the cost-to-income ratio at 65%-70% over the next two years.

**Table 3****PostFinance AG Capital And Earnings**

	<b>--Year-ended Dec. 31--</b>	
(%)	<b>2014*</b>	<b>2013</b>
Tier 1 capital ratio*	21.67	20.35
S&P RAC ratio before diversification	N.M.	29.27
S&P RAC ratio after diversification	N.M.	28.11
Adjusted common equity/total adjusted capital	100.00	100.00
Net interest income/operating revenues	62.60	63.07
Fee income/operating revenues	10.28	10.67
Market-sensitive income/operating revenues	13.37	11.68
Noninterest expenses/operating revenues	62.98	66.98
Preprovision operating income/average assets	0.48	N/A
Core earnings/average managed assets	0.37	N/A

**Table 3****PostFinance AG Capital And Earnings (cont.)**

\*Data as of June 30.

N.A.--Not available. N/A--Not applicable. N.M.--Not meaningful.

**Table 4****PostFinance AG RACF [Risk-Adjusted Capital Framework] Data**

CHF	Exposure*	Basel II RWA	Average Basel II RW (%)	Standard & Poor's RWA	Average Standard & Poor's RW (%)
<b>Credit risk</b>					
Government and central banks	35,816,870,603	0	0	2,184,646,799	6
Institutions	25,837,367,256	0	0	3,168,045,557	12
Corporate	2,973,067,806	0	0	1,934,739,376	65
Retail	0	0	0	0	0
Of which mortgage	0	0	0	0	0
Securitization	24,000,000	0	0	4,800,000	20
Other assets	954,000,000	0	0	858,600,000	90
Total credit risk	65,605,305,665	0	0	8,150,831,732	12
<b>Market risk</b>					
Equity in the banking book¶	911,400,000	0	0	5,838,625,000	641
Trading book market risk	--	0	--	0	--
Total market risk	--	0	--	5,838,625,000	--
<b>Insurance risk</b>					
Total insurance risk	--	--	--	0	--
<b>Operational risk</b>					
Total operational risk	--	0	--	2,776,875,000	--
		<b>Basel II RWA</b>		<b>Standard &amp; Poor's RWA</b>	<b>% of Standard &amp; Poor's RWA</b>
<b>Diversification adjustments</b>					
RWA before diversification		0		16,766,331,732	100
Total adjustments to RWA		--		687,566,606	4
RWA after diversification		0		17,453,898,338	104
		<b>Tier 1 capital</b>	<b>Tier 1 ratio (%)</b>	<b>Total adjusted capital</b>	<b>Standard &amp; Poor's RAC ratio (%)</b>
<b>Capital ratio</b>					
Capital ratio before adjustments		N/A	20.35	4,907,000,000	29.3
Capital ratio after adjustments§		N/A	20.35	4,907,000,000	28.1

\*Exposure at default. €Securitisation Exposure includes the securitisation tranches deducted from capital in the regulatory framework. ¶Exposure and Standard & Poor's 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, 2013, Standard & Poor's.

### Risk position: Large concentration risks in the investment portfolio

Our assessment of PostFinance's overall risk position as "moderate" mainly reflects single-name and sector concentrations in its ample investment portfolio. Because PostFinance is not allowed to extend loans, it invests most of its liquidity in high quality securities.

PostFinance's investments totaled about CHF68 billion (55% of total assets) on June 30, 2014, comprising mainly covered bonds (38% of investment portfolio) and public-sector bonds (52%). We expect the portfolio's quality to remain very high--57% rated 'AAA' or 96% at least 'A'--in line with PostFinance's conservative investment rules, although the risks from single-name exposures will likely stay high. We note also that PostFinance's exposure to bonds issued by sovereign governments on Europe's periphery, mainly Spain and Italy, has decreased to CHF395 million representing a manageable 8% of TAC.

PostFinance records most of the financial assets as "held to maturity," which reduces earnings volatility. Furthermore, PostFinance has no trading book, but is marginally exposed to market risk from foreign currency positions in international payment transactions.

We understand PostFinance has never engaged in cross-border business, and wealth management is not part of its business strategy. However, in December 2013, PostFinance registered as a "Category 2" bank with a program of the U.S. Department of Justice (DOJ) and Swiss officials that aims to resolve investigations into tax-related offenses of Swiss banks connected with undeclared U.S.-related accounts. Banks in Category 2 could face prosecution and fines depending on the size of undeclared U.S. client assets. We do not expect PostFinance to face any significant financial risks from potential prosecution and expect it to easily manage these risks with its earnings capacity.

**Table 5**

PostFinance AG Risk Position		
	--Year-ended Dec. 31--	
(%)	2014*	2013
Growth in customer loans	N.M.	N.M.
Total diversification adjustment / S&P RWA before diversification	N.M.	4.1
Total managed assets/adjusted common equity (x)	23.8	23.8
New loan loss provisions/average customer loans	0.6	N/A
Net charge-offs/average customer loans	N.M.	N.M.

\*Data as of June 30.

N.A.--Not available. N/A--Not applicable. N.M.--Not meaningful.

### Funding and liquidity: Ample liquidity, owing to customer deposits of more than CHF109 billion

We consider PostFinance's funding "above average" and its liquidity position "strong," reflecting its close ties to the Swiss government and its superior funding and liquidity metrics.

With customer deposits of about CHF109 billion on June 30, 2014, representing 90% of total liabilities, PostFinance is a cash provider in the domestic interbank market. Customer deposits comprise equal shares of granular and very stable retail and business accounts.

In our view, PostFinance's sensitivity to customer confidence is very low, thanks to the ownership structure and a

partial state guarantee on deposits under the Swiss Postal Law, as demonstrated by the constant net new money inflow. The Swiss government guarantees up to CHF100,000 of a customer's deposit until 2018 (in addition to amounts under the Swiss Deposit Protection Scheme), as well as obligations existing when the current postal law went into effect, until maturity. PostFinance doesn't rely on wholesale funding, which is reflected in its superior stable funding ratio of above 650% as of June 30, 2014.

We consider liquidity "strong" because PostFinance's liquidity sources would allow it to operate for more than 12 months in the event of sudden customer withdrawals, without resorting to the debt capital markets. This is demonstrated by PostFinance's ratio of broad liquid assets to short-term wholesale funding of about 20x as of June 30, 2014, which is superior to that of global banks. Since mid-2011, PostFinance has been placing excess liquidity with the SNB, where it now holds a liquidity buffer of more than CHF40 billion. We do not expect a significant reduction in PostFinance's liquidity position at SNB in the short term, despite the negative interest on sight deposits at SNB. Furthermore, we expect the group to maintain a substantial portfolio of unencumbered assets eligible for sale and repurchase transactions with the SNB.

**Table 6**

<b>PostFinance AG Funding And Liquidity</b>		
	<b>--Year-ended Dec. 31--</b>	
<b>(%)</b>	<b>2014*</b>	<b>2013</b>
Core deposits/funding base	95.4	97.7
Customer loans (net)/customer deposits	9.5	9.1
Long term funding ratio	95.7	97.9
Stable funding ratio	656.3	614.2
Short-term wholesale funding/funding base	4.5	2.2
Broad liquid assets/short-term wholesale funding (x)	19.8	39.6
Net broad liquid assets/short-term customer deposits	89.2	88.1
Short-term wholesale funding/total wholesale funding	98.1	96.3
Narrow liquid assets/3-month wholesale funding (x)	20.0	40.3

\*Data as of June 30.

### **Support: Three notches of uplift for potential government support**

We consider PostFinance to be a GRE with an "extremely high" likelihood of extraordinary government support, which adds three notches of uplift to the SACP of 'a+'. However, we expect that, if needed, this support would be provided indirectly through the Swiss Post group's nonoperating holding company--DSP--in line with the legal framework in place.

Our view of an extremely high likelihood of extraordinary support reflects our assessment of PostFinance's:

- Critical role for the government as part of the Swiss Post group, which is to fulfil the legal mandate of providing essential services to the Swiss population. As such, PostFinance remains in our view one of the most important GREs in Switzerland, with a central role of meeting the government's political objectives; and
- Very strong link with the Swiss government, which owns PostFinance through DSP and approves its strategy. We believe that PostFinance will remain a core member of the Swiss Post group in the foreseeable future. We consider the possibility of a full or partial privatization of PostFinance to be very remote over the medium to long term, even



though Swiss Postal Law allows a minority shareholding by a third-party investor.

Disruptions of PostFinance's services could severely hamper Switzerland's banking system; therefore, we view PostFinance as systemically important. However, we factor in only the higher outcome from our support framework, based on PostFinance's GRE status.

### Additional rating factors: None

No additional factors affect this rating.

## Related Criteria And Research

### Related Criteria

- Banks: Rating Methodology And Assumptions, Nov. 9, 2011
- Banking Industry Country Risk Assessment Methodology And Assumptions, Nov. 9, 2011
- Rating Government-Related Entities: Methodology And Assumptions, Dec. 9, 2010
- Bank Capital Methodology And Assumptions, Dec. 6, 2010

### Related Research

- Switzerland Ratings And BICRA Unaffected By Swiss National Bank's Change In Exchange Rate Policy, Jan. 15, 2015
- Banking Industry Country Risk Assessment Update, Jan. 12, 2015
- Banking Industry Country Risk Assessment: Switzerland, Jan. 7, 2015
- Various Ratings Actions On Swiss Banking Groups On Rising Economic Imbalances, Dec. 1, 2014
- Swiss Confederation 'AAA/A-1+' Ratings Affirmed; Outlook Stable, Nov. 21, 2014
- Die Schweizerische Post AG, Jan. 23, 2014
- Swiss Financial Services Provider PostFinance AG Assigned 'AA+/A-1+' Ratings; Outlook Stable, June 28, 2013

### 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 January 30, 2015)

#### PostFinance AG

Counterparty Credit Rating

AA+/Stable/A-1+

## Ratings Detail (As Of January 30, 2015) (cont.)

### Counterparty Credit Ratings History

28-Jun-2013 AA+/Stable/A-1+

### Sovereign Rating

Swiss Confederation (Unsolicited Ratings) AAA/Stable/A-1+

### Related Entities

#### Die Schweizerische Post AG

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

#### Swiss Confederation (Unsolicited Ratings)

Issuer Credit Rating AAA/Stable/A-1+

Transfer & Convertibility Assessment AAA

\*Unless otherwise noted, all ratings in this report are global scale ratings. Standard & Poor's credit ratings on the global scale are comparable across countries. Standard & Poor's credit ratings on a national scale are relative to obligors or obligations within that specific country.

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