

Rating Action: Moody's assigns first-time Ba2 issuer rating to EEPK (Luxembourg); outlook stable

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Standalone credit assessment of Commerzbank's Luxembourg subsidiary at E / caa2

Frankfurt am Main, January 08, 2015 -- Moody's Investors Service, ("Moody's") has today assigned a first-time issuer rating of Ba2 to EEPK (Erste Europaeische Pfandbrief- und Kommunalkreditbank Aktiengesellschaft in Luxemburg S.A.), with a stable outlook, and a standalone bank financial strength rating (BSFR) of E, equivalent to a baseline credit assessment (BCA) of caa2.

EEPK's status as a wind-down entity for the Luxembourg-based international public-finance portfolio of Commerzbank AG (deposits Baa1 negative; BFSR D+ stable/BCA ba1) constrains EEPK's earnings generation capacity, thereby positioning EEPK's standalone credit strength in the E BFSR category. In addition, Moody's considers that the quality of the bank's portfolio and limited capital levels are additional rating constraints.

EEPK's ratings benefit from a very high degree of support from its parent, Commerzbank. As a foreign subsidiary of Commerzbank, EEPK's long-term rating does not incorporate any systemic support from the German government (Aaa stable). The outlook on EEPK's issuer rating is stable, in line with the stable outlook on Commerzbank's BFSR. EEPK's E BFSR does not carry an outlook.

RATINGS RATIONALE

EEPK was created on 1 September 2014 as a result of the merger of two Luxembourg-based Commerzbank subsidiaries: Hypothekenbank Frankfurt International S.A. (HFI, unrated), a wind-down entity that contained the international public finance portfolio in Luxembourg held by Hypothekenbank Frankfurt AG (HF, deposits Baa3 negative; BFSR E no outlook/BCA caa2), and the previous EEPK entity, which held a portfolio of public-sector loans refinanced through 'Lettres de Gage' (covered bonds). End of June 2012, HFI was put into wind-down together with HF (collectively the former Eurohypo), as part of Commerzbank's state-aid ruling.

Moody's considers EEPK's asset quality to be moderate. The combined public-finance portfolio of EUR17.2 billion as of year-end 2013 contains considerable concentrations to public sector creditors in the US (total exposure: EUR4.8 billion), the UK (EUR2.2 billion), Spain (EUR1.9 billion) and Italy (EUR1.8 billion). EUR2.3 billion exposures of former HFI were accounted for as non-investment grade risk. HFI, prior to its merger with EEPK, had a negative difference of book values to market values of EUR755 million as of June 2014.

EEPK's substantial leverage at 2.86% (equity as a percentage of total assets) on the back of EUR676 million equity is a further rating constraint. The bank's pro forma common equity tier 1 (CET1) capitalisation of 16.8% as of 1 September 2014 benefits from a 0% risk-weight for public-sector exposures in the European Economic Area for the portfolios of former HFI. The bank is funded by 'Lettres de Gage' and obtains senior funding mainly from the Commerzbank group (EUR7.1 billion at year-end 2013 for former HFI).

Moody's has incorporated a very high degree of support into EEPK's ratings. This support assessment reflects Commerzbank's substantial funding to EEPK and a letter of comfort (LoC) whereby Commerzbank ensures that EEPK will be able to meet its contractual obligations. Given the funding with 'Lettres de Gage' (covered bonds) Moody's considers Commerzbank to continue to be committed to wind down the bank in an orderly fashion, also in order to avoid spill-over effects for Commerzbank's franchise in the German covered bond market. The rating agency understands that Commerzbank's commitment to unwinding EEPK in an orderly fashion is also part of an agreement that Commerzbank reached with the European Commission.

Moody's joint default analysis (JDA) uses Commerzbank's BCA of ba1 because EEPK does not receive any systemic support from the German government. The rating is placed one notch below Commerzbank's BCA to reflect some remaining, though remote, tail risk of a future break up.

What Could Change the Rating -- Up / Down

Upward pressure on EEPK's rating could develop on the back of a strengthening of its creditworthiness, following

a possible orderly wind-down and a further strengthening of its capital base. EEPK's ratings would also benefit from improvements in Commerzbank's fundamental credit strength; i.e., if Moody's were to adjust Commerzbank's BCA upwards, positive pressure would develop on the uplift and hence EEPK's issuer rating.

The support from Commerzbank incorporated into the rating is key for EEPK's issuer rating. If Commerzbank were no longer committed to the orderly unwinding of EEPK and opted to withdraw the LoC, EEPK's rating could face a multiple notch downgrade as a result of a review of the support uplift factored into EEPK's ratings.

Further pressure would likely develop for EEPK's rating in the event of a significant worsening of the credit quality for the more critical parts of EEPK's exposures (exposures to local authorities in the US, and regional creditors in Italy and Spain).

The principal methodology used in these ratings was Global Banks published in July 2014. Please see the Credit Policy page on www.moodys.com for a copy of this methodology.

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