

Research Update:

Swiss Glarner Kantonalbank Upgraded To 'AA' On People's Vote To Stop Privatization Plans; Outlook Stable

May 4, 2022

Overview

- On May 1, 2022, the people of the Swiss Canton of Glarus voted against proposed changes to cantonal bank law that would have resulted in a reduction of the current government's ownership of Glarner Kantonalbank (GLKB) toward 33% and a removal of the cantonal bank guarantee.
- The vote and our expectation of good financial prospects for the bank mean we no longer consider that the likelihood of timely and sufficient extraordinary government support to GLKB from the Canton of Glarus will weaken.
- We raised the long-term issuer credit rating on GLKB to 'AA' from 'AA-' and affirmed our 'A-1+' short-term rating.
- The stable outlook reflects our view that GLKB would receive extraordinary government support from its majority owner, the Canton of Glarus, if needed, because of its integral link to and very important role for the canton. It also reflects our view that the bank will not deviate from its proven business model with close ties to the cantonal economy.

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Rating Action

On May 4, 2022, S&P Global Ratings raised its long-term issuer credit rating on GLKB to 'AA' from 'AA-' and affirmed the 'A-1+' short-term rating. The outlook is stable.

We also affirmed our 'BBB' issue rating on GLKB's tier 2 subordinated notes.

Rationale

The upgrade follows our review of GLKB's creditworthiness, taking into consideration the halt to the bank's privatization plans following the people's vote. We now no longer expect a weakening of GLKB's role and link to the majority owner, the Canton of Glarus, nor a gradual decline in the likelihood of extraordinary government support. The vote in favor of keeping majority bank ownership and retaining the cantonal bank guarantee is a strong indication that GLKB will continue to have an integral link with and very important role for the canton.

Also essential to our assessment is our view of good financial prospects for the bank, reducing the incentive for a potential revival of the discussion. We do not expect renewed attempts through the government or parliament to change the existing cantonal bank law. This is on the back of the canton's history of direct votes that have been persistent and unchallengeable for the foreseeable future.

The rejected proposals included some material changes to the existing law. These included:

- GLKB's legal entity would have changed from a public limited company under special law into a public company under private law in order to enable further privatization under existing Swiss law;
- The canton's existing 58% equity stake and voting rights would have gradually reduced toward a minimum of 33% in subsequent periods; and
- The cantonal guarantee for GLKB's new debt obligations would have been removed. We understand that existing obligations would have been grandfathered until maturity.

Multiple factors resulted in the estimated 60:40 voting results against the change of the existing cantonal bank law. We understand that the annual dividend payments to the canton and the majority control of GLKB to steer the bank's key decisions were the most relevant reasons to keep the status quo.

GLKB is one of the most important financial institutions in Glarus with a market share of roughly 50% in mortgage loans and 40% in retail deposits. We currently assess the likelihood that the Canton of Glarus would provide timely and sufficient support to the bank as extremely high, based on the bank's integral link with and very important role for the canton. Our ratings on GLKB include multiple notches of uplift for potential extraordinary government support on top of its 'a-' stand-alone credit profile (SACP), resulting in the 'AA' long-term issuer credit rating.

Our assessment of GLKB's SACP currently incorporates significant ongoing implicit support benefits. This is mainly because of lower funding costs and a sticky deposit base, which support the overall profitability and stability of the bank's performance, in our view. We expect no deviation from the proven business model and strategy as a leading bank for retail and smaller corporate clients in the home canton and selected regions in German-speaking Switzerland.

Outlook

The stable outlook reflects our view that GLKB would receive extraordinary support from its majority owner, the Canton of Glarus, if needed. Consequently, the likelihood of a downgrade is remote over the next two years because, in the event of a moderate deterioration of GLKB's own creditworthiness, we would include additional support from the canton into our ratings, assuming all else remained equal.

We expect a continuation of the current business model with strong roots in the Canton of Glarus and complementary business activities through online mortgages in German-speaking Switzerland.

Downside scenario

We could lower the rating if we concluded that GLKB's ties with the canton had loosened, or if renewed attempts to change the current cantonal bank law emerged. That said, we consider this scenario unlikely after the people in Glarus voted against the government's proposal to change the cantonal bank law in May 2022. In addition, a negative rating action could occur if we were to lower our assessment of the canton's creditworthiness.

Upside scenario

A positive rating action on the canton would trigger an upgrade of GLKB. However, improvements in GLKB's SACP would not translate into an upgrade.

Ratings Score Snapshot

Ratings Score Snapshot -- Glarner Kantonalbank

	To	From
Issuer Credit Rating	AA/Stable/A-1+	AA-/Negative/A-1+
SACP	a-	a-
Anchor	a-	a-
Business Position	Moderate (-1)	Moderate (-1)
Capital and Earnings	Very Strong (+2)	Very Strong (+2)
Risk Position	Adequate (0)	Adequate (0)
Funding and Liquidity	Moderate and Adequate (-1)	Moderate and Adequate (-1)
Support	(+4)	(+4)
ALAC Support	(0)	(0)
GRE Support	(+4)	(+4)
Group Support	(0)	(0)
GRE Support	(0)	(0)
Additional Factors	(0)	(-1)

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

ESG credit indicators: E-2, S-2, G-2

Related Criteria

- General Criteria: Hybrid Capital: Methodology And Assumptions, March 2, 2022
- Criteria | Financial Institutions | General: Financial Institutions Rating Methodology, Dec. 9,

2021

- Criteria | Financial Institutions | Banks: Banking Industry Country Risk Assessment Methodology And Assumptions, 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: Rating Government-Related Entities: Methodology And Assumptions, March 25, 2015
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Related Research

- Swiss and Liechtenstein Bank Ratings Affirmed Under Revised FI Criteria, Feb. 8, 2022
- Banking Industry Country Risk Assessment: Switzerland, Jan. 6, 2021

Ratings List

Ratings Affirmed

Glarner Kantonalbank

Subordinated	BBB
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Upgraded; Outlook Action; Ratings Affirmed

	To	From
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Glarner Kantonalbank

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