S&P Global Ratings

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Research Update:

Thurgauer Kantonalbank Assigned 'AA/A-1+' Ratings; Outlook Stable

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Overview

- We consider Thurgauer Kantonalbank (TKB) to be a government-related entity (GRE) benefiting from an extremely high likelihood of support by its majority owner, the Canton of Thurgau. The bank plays an important role in contributing to the development of the canton's economy and is integral to the canton, which also guarantees TKB's senior obligations.
- We view TKB as having a solid franchise in its home canton and very strong capitalization, while its asset quality is sound and its funding and liquidity adequate--in line with most of its Kantonalbank peers.
- As a result, we have assigned our 'AA/Stable/A-1+' long- and short-term issuer credit ratings to TKB.
- The stable outlook reflects our expectation that TKB will maintain its GRE-status, securing its link to and role for the canton over the next 24 months.

Rating Action

On Jan. 9, 2025, S&P Global Ratings assigned its 'AA/A-1+' long- and short-term issuer credit ratings to Switzerland-based Thurgauer Kantonalbank (TKB). The outlook is stable.

Rationale

Our ratings are based on the expectation that TKB will protect its market position in its home Canton of Thurgau, where it enjoys GRE-status. TKB focuses on mortgage and small and midsize enterprise (SME) lending, specifically in its home Canton of Thurgau. As a publicly owned cantonal bank, it contributes to the development of Thurgau's economy and its operations are deeply rooted in the region. Outside activities to neighboring German or Swiss regions (Zürich and St. Gallen) are fairly limited. As a result, and similar to its Swiss cantonal peers, we assign TKB our 'a-' anchor (the starting point for deriving an issuer credit rating) under our Banking Industry and Country Risk Assessment.

TKB's business position assessment reflects its solid franchise in its home canton, which offsets risks from its concentrated business model and significant competition in all business areas. In our opinion, TKB's local focus allows for a stable and long-standing customer base. We expect Swiss clients will remain fairly sticky and conservative, at least in the medium term, allowing the bank to develop its digital offering and user experience in line with market standards. In our view, TKB's strong regional share of about 50%, coupled with the exceptional resilience of Swiss households and corporates, offsets the risks resulting from the bank's relatively small size and concentration in local mortgages. Over the medium term, we expect the bank will aim to diversify its operations by expanding its asset management offering to reduce its dependency on and exposure to retail mortgages.

Interest income accounts for two thirds of TKB's profits. The bank is focused on expanding its share of fee income by continuing to grow assets under management (AuM). For the first half of 2024, TKB increased AuM by about Swiss franc (CHF) 219 million net new money, reaching a total of CHF11 billion. However, we don't expect a material change in the revenue split in the medium term.

We view TKB's capital and earnings capacity as the key rating strength. We calculate TKB's risk-adjusted capital (RAC) ratio at 30.9% at year-end 2023, which is among the strongest globally. Our ratio is higher than the total capital ratio of 19.3% (versus the requirement of 13.3%). This is explained by the high share of retail mortgages (94% of total exposure), which under our risk-adjusted capital framework are associated with very low risk weights in Switzerland, significantly below regulatory risk weights. Earnings generation and general profitability are solid, underpinned by a relatively (compared to peers') low cost-income ratio of about 48% and return on average equity at 6%. These ratios largely reflect the currently high interest margins and we don't expect them to persist. We expect some normalization of performance in 2025-2026; we forecast RAC will increase to about 32.4% in 2026. Our main assumptions are:

- Loan book growth of about 3%-4% per year, reflecting reviving loan demand and rising house prices.
- Broad stagnation of interest income, as margin squeeze offsets lending growth.
- Operational costs to increase by about 3%, on average, mainly reflecting wage inflation and digitalization efforts.
- Net income trending at about CHF150 million annually.
- Dividend payout ratio of 40%-60% of net profit.

We project the three-year average earnings buffer, which measures the capacity of a bank's earnings to cover normalized losses, will trend comfortable at about 1.7% over the medium term. This indicates a strong first line of defense against potential future losses in a potentially deteriorating economic environment. As with other cantonal bank peers, TKB's nonperforming assets were very low at 0.6% at end-2024, a level that we expect to persist, reflecting prudent underwriting standards and strong resilience of the bank's customer base. Furthermore, in our view, the bank's risk management framework adequately addresses non-financial risks such as cyber risk.

We view TKB's liquidity as solid and its funding as in line with its Kantonalbank peers. TKB focuses on retail deposits, which cover almost two thirds of its funding base. We view TKB's customer deposit base as sticky, with trust being supported by the cantonal guarantee and ownership. The bank's wholesale funding share at 39.3% of the funding base is higher than the peer average, but it preliminary comprises covered bonds, which we regard as a stable funding source. Our key funding metric--the stable funding ratio--was 108% at end-2023, which is in line with the peer group average. Our main liquidity ratio, which indicates the coverage of short-term wholesale funding by broad liquid assets, was 2.1x as per end-2023. This demonstrates the bank has a sound buffer to cover an extended period without access to market funding in an adverse scenario.

We also factor in some intrinsic advantages from the cantonal ownership and guarantee into our stand-alone credit profile (SACP) assessment for the bank. We note that the cantonal backbone improves availability and lowers the cost of market funding for the bank.

We expect TKB will maintain its integral link with and very important role for the Canton of Thurgau. We consider the bank to be a GRE with an extremely high likelihood of timely extraordinary support from the Canton of Thurgau in case of need. Our assessment encompasses, among other factors, the canton's long-term commitment and guarantees for senior obligations, as outlined in the underlying bank law. Given that it has operated since 1871 and its high market share in deposits and loans, we consider TKB to play a very important role in contributing to the development of the canton's economy. In our view, a potential default would cause significant financial stress for the canton.

Outlook

The stable outlook on TKB reflects our expectation that the bank's GRE-status, entailing an extremely high likelihood of support from the Canton of Thurgau, will remain unchanged over the next 24 months. Our ratings on TKB are sensitive to our assessment of the owner's ability and willingness to support the bank. The rating is not sensitive to the deterioration of the bank's SACP, as we expect that GRE support would protect the current rating level.

Downside scenario

A weakening of the role for or the link with the Canton of Thurgau would lead us to revise downward our assessment of the bank's GRE support. If this scenario were to occur, we would expect TKB's existing obligations to be grandfathered. However, this scenario is unlikely over the next 24 months.

Upside scenario

We are unlikely to upgrade TKB, considering the already very high rating level and the bank's small size and concentrated business model. All else remaining equal, we could raise our ratings on TKB if we considered the canton's creditworthiness had strengthened, leading to an increased ability to support the bank during times of financial stress.

Ratings Score Snapshot

	To
Issuer Credit Rating	**AA/Stable/A-1+**
SACP	a+

	To
Issuer Credit Rating	**AA/Stable/A-1+**
Anchor	a-
Business position	Adequate (0)
Capital and earnings	Very Strong (+2)
Risk position	Adequate (0)
Funding and liquidity	Adequate and adequate (0)
Comparable ratings analysis	0
Support	+2
ALAC support	
GRE support	+2
Group support	
Sovereign support	
Additional factors	

SACP--Stand-alone credit profile.

Related Criteria

- Criteria | Financial Institutions | General: Risk-Adjusted Capital Framework Methodology, April 30, 2024
- 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
- 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

- Banking Industry Country Risk Assessment: Switzerland, July 30, 2024

Ratings List

New Ratings	
Thurgauer Kantonalbank	
Issuer Credit Rating	AA/Stable/A-1+

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