S&P Global Ratings

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Zuger Kantonalbank

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Zuger Kantonalbank

Rating Score Snapshot

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

SACP: a → **Support: +4** → **Additional factors: 0**

Anchor	a-	
Business position	Adequate	0
Capital and earnings	Very strong	+2
Risk position	Adequate	0
Funding	Adequate	0
Liquidity	Adequate	
CRA adjustment		-1

ALAC support	0
GRE support	+4
Group support	0
Sovereign support	0

Issuer credit rating
AA+/Stable/A-1+

ALAC--Additional loss-absorbing capacity. CRA--Comparable ratings analysis. GRE--Government-related entity. ICR--Issuer credit rating. SACP--Stand-alone credit profile.

Credit Highlights

Overview	
Key strengths	**Key risks**
Extremely high likelihood of support from the financially strong Swiss Canton of Zug.	Concentrated business model and higher risk appetite than most peers due to its material exposure to the property sector.
Very strong capitalization and sound asset quality.	Significant competition from neighboring cantonal and cooperative banks in the small canton of Zug.
Solid profitability.	

S&P Global Ratings expects Zuger Kantonalbank (ZGKB) to show resilience owing to its prudent lending policies. We forecast ZGKB will maintain its sound return on equity of 7.3%-8.0%% in the next two years, supported by its market leadership in Zug and expanding asset management business in northwestern Switzerland. At the same time, we expect the bank to continue its sound underwriting policy, which supports its resilience.

ZGKB's very strong capitalization and sound asset quality are rating strengths. We expect ZGKB to maintain its superior capitalization, as measured by our projected risk-adjusted capital (RAC) ratio of 29.5%-30.0% over 2024-2026. It was 26.7% at year-end 2023. Strong earnings generation capacity, stable and low payouts, and moderate business growth support our assessment, which puts ZGKB's capitalization among the world's strongest, together with some cantonal bank peers.

We expect ZGKB will maintain its integral link with and very important role for the Canton of Zug. Our analysis is supported by the cantonal guarantee, which is stipulated by law. We believe there is an extremely high likelihood that the canton would provide sufficient and timely support to the bank if needed.

Outlook

The stable outlook on ZGKB reflects our expectation that the bank's government-related entity (GRE) status, entailing an extremely high likelihood of support from the Canton of Zug, will remain unchanged over the next 24 months. Our ratings on ZGKB are sensitive to our assessment of the owner's ability and willingness to support the bank.

Downside scenario

If we perceived a weakening in ZGKB's role for or link with the canton, this could lead us to revise our assessment of the bank's GRE support. However, we do not envisage such a scenario in the next two years. Also, if this were to happen, we would expect ZGKB's existing obligations to be grandfathered. The sensitivity of the rating to a potential downward revision of the stand-alone credit profile (SACP) is very limited.

Upside scenario

We consider rating upside to be remote. We could consider revising ZGKB's SACP up if the bank demonstrates sustained and stable operations over the cycle without signs of weakening asset quality or earnings. However, a one-notch improvement of the SACP would not translate into a higher issuer credit rating.

Key Metrics

Zuger Kantonalbank--Key ratios and forecasts

	--Fiscal year ended Dec. 31--				
(%)	**2022a**	**2023a**	**2024f**	**2025f**	**2026f**
Growth in operating revenue	6.7	24.7	(2.8)-(3.4)	3.0-3.7	4.9-5.9
Growth in customer loans	3.7	5.1	2.3-2.9	2.3-2.9	2.2-2.7
Growth in total assets	2.7	1.6	3.0-3.7	3.1-3.8	3.1-3.7
Net interest income/average earning assets (NIM)	1.1	1.4	1.2-1.3	1.1-1.3	1.2-1.3
Cost to income ratio	52.9	51.2	53.8-56.6	52.9-55.6	50.8-53.4
Return on average common equity	6.9	8.5	7.0-7.7	7.1-7.9	7.6-8.4
Gross nonperforming assets/customer loans	0.2	0.2	0.2-0.2	0.2-0.2	0.2-0.2
Risk-adjusted capital ratio	23.7	26.7	28.3-29.2	28.6-29.5	29.1-30.0

All figures are S&P Global Ratings-adjusted. a--Actual. f--Forecast. NIM--Net interest margin.

Anchor: 'a-' For Banks Solely Operating In Switzerland

Our anchor for banks operating mainly in Switzerland, like Zuger Kantonalbank, is 'a-'. We consider the trend for economic and industry risk in Switzerland to be stable.

The Swiss private sector has proven its resilience against multiple external stress scenarios. We expect banks to maintain their strong asset quality, superior financial strength of Swiss households and corporations, and prudent underwriting standards amid a difficult global economic outlook. We anticipate the country's GDP to expand by 1.5% in 2025.

Overall, we see limited risks to Swiss banks' mortgage exposures as real estate price are supported by structural factors such as immigration, the scarcity of building land, and higher commodity prices over the coming years.

Our view of industry risk in Switzerland encompasses the stability of country's multitiered banking system government-guaranteed credit institutions viewed as safe havens. Proposals by the regulator and parliament could strengthen banks' corporate governance, supervision, and their access to liquidity during crises.

Tech disruption poses a moderate risk for the Swiss market, in our opinion. A lack of economies of scale in retail banking makes the country less attractive for international competitors. Swiss customers generally do not demand pure online retail banking products, and digital banks have yet to establish full alternatives to traditional banks, in our view.

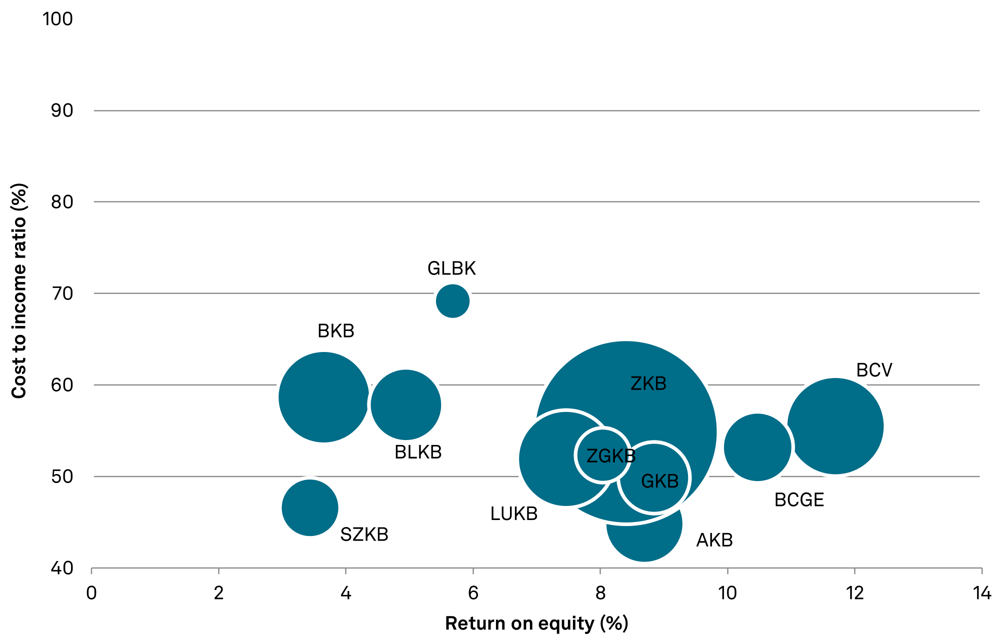
Business Position: Strong Home Turf, But Concentrated Business Model Amid Significant Competition

Based on ZGKB's strong regional franchise and very resilient customer base, we view its business profile as on par with domestically focused Swiss peers. ZGKB is a smaller-sized cantonal bank with a high market share of about 50% in retail and corporate banking in the Canton of Zug and surrounding cantons. Also supporting its market share is its increasing online offerings. The bank primarily finances retail mortgages and smaller corporate clients as well as more affluent clients in the Zug region.

Assets under management were CHF18.8 billion as of June 30, 2024. ZGKB plans to expand its asset and wealth management business outside the Canton of Zug due to limited growth potential within its home market. Due to several contenders, we consider this business as highly competitive–-requiring material investments in infrastructure and personnel.

Chart 1

ZGKB's efficiency remains at par with its peers



Data is as of H1 2024 .SZKB - Schwyzer Kantonalbank, ZGKB-Zuger Kantonalbank, GKB - Graubuendner Kantonalbank, AKB - Aargauische Kantonalbank, BKB - Basler Kantonalbank, GLKB - Glarner Kantonalbank, LUKB - Luzerner Kantonalbank, ZKB - Zuercher Kantonalbank, BLKB - Basellandschaftliche Kantonalbank, BCV - Banque Cantonale Vaudoise, BCGE - Banque Cantonale de Genev. Source: S&P Global Ratings.

We see the risk of disruption to ZGKB's business model from new digital competitors as moderate due to its strong customer franchise. That said, given its wealthier, more dynamic, and international client base, closing the gap with larger competitors would take significant investments, in our view. We view the bank's initiative to increase its digital and base product offerings as positive to avoid digital disruption.

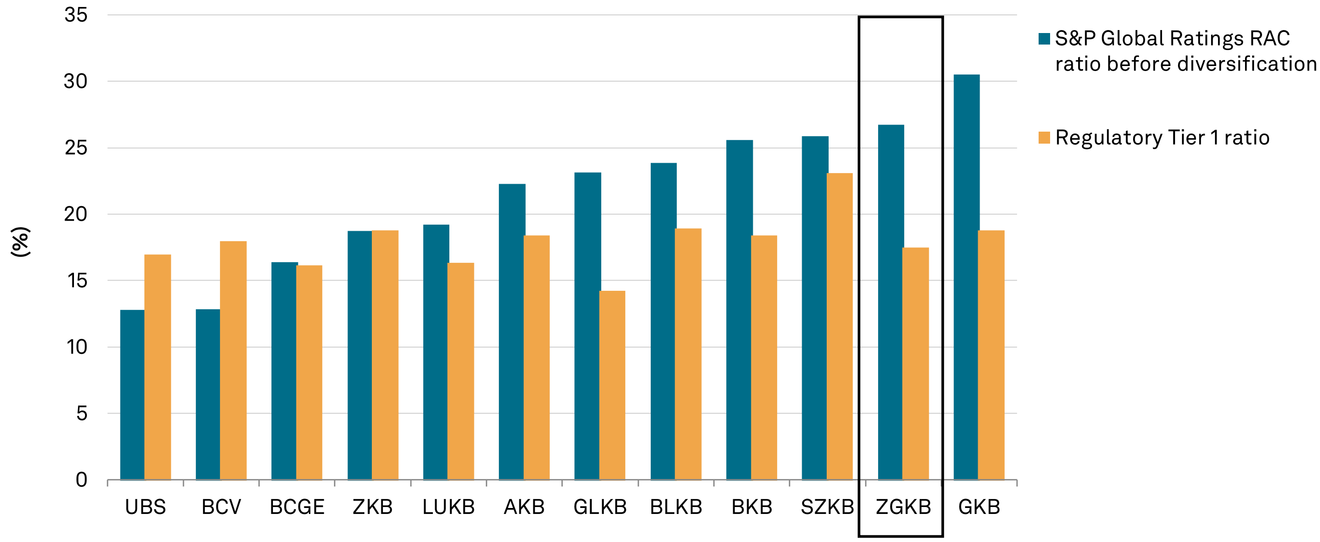
ZGKB's cost-to-income ratio increased to 52.3% as of midyear 2024, largely on par with cantonal bank peers. The bank's return on equity of 8.0% at midyear 2024 was slightly above those of most domestic peers. Similar to most domestic peers, we consider ZGKB's return on equity in the context of its very high equity base, which limits a wider international comparison.

Capital And Earnings: Very Strong Capitalization With Sound Earnings Generation Capacity

We consider ZGKB's solid capital position a rating strength, especially in comparison with global peers. The RAC ratio was 26.7% at year-end 2023, and we expect it to increase to around 29.6-30.1% until 2026. Our RAC forecast is underpinned by the expectation of stable retained earnings and only modest credit growth.

Chart 2

ZGKB has one of the highest capitalization globally



SZKB - Schwyzer Kantonalbank, GKB - Graubuendner Kantonalbank, AKB - Aargauische Kantonalbank, BKB - Basler Kantonalbank, GLKB - Glarner Kantonalbank, LUKB - Luzerner Kantonalbank, ZKB - Zuercher Kantonalbank, ZGKB - Zuger Kantonalbank, BLKB - Basellandschaftliche Kantonalbank, BCV - Banque Cantonale Vaudoise, BCGE - Banque Cantonale de Geneve, PF - PostFinance AG, , UBS- UBS Group AG, Migros - Migros Bank. Data as of year-end 2023.
Source: S&P Global Ratings.

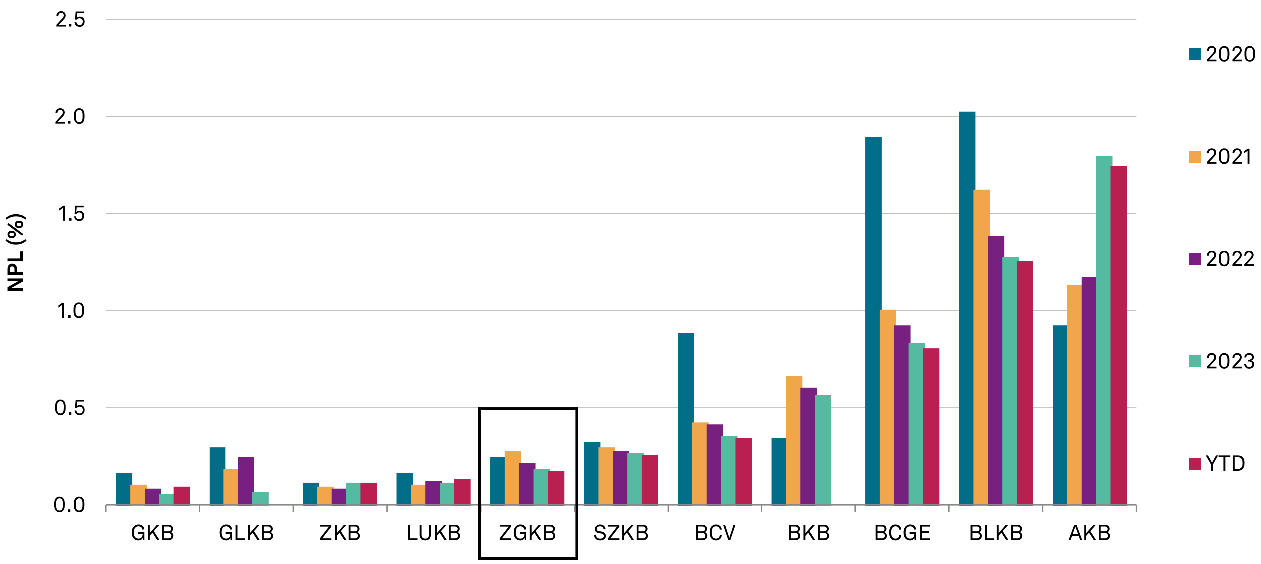
We project ZGKB's three-year average earnings buffer, which measures the capacity for a bank's earnings to cover normalized losses, will be strong at about 2.2% from 2024-2026, supported by its predictable and stable earnings. We do not assume any changes to the bank's dividend policy of distributing CHF220 per share, which amounts to about CHF63 million, to the Canton of Zug and other shareholders. We view ZGKB's capital as very high quality because its capital base consists solely of common equity.

Risk Position: Sound Underwriting Standards And Very Good Asset Quality

Similar to other cantonal bank peers, ZGKB's nonperforming assets were lower than the system average of 0.5% in 2023 at about 0.2% of customer loans. This is based on sound underwriting standards, demonstrated by very low loan-to-value figures with less than 2.2%% of the total portfolio being above 66%. We do not expect the bank will deviate from its underwriting criteria, which supports asset quality through the cycle.

Chart 3

ZGKB has sound asset quality metrics



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The bank's balance sheet is dominated by mortgage lending, accounting for about 94.4% of the total loans. ZGKB's approximate 12% share of commercial real estate properties is higher than that of peers, driven by the economic structure in its home canton, which attracts many international corporates due to its favorable tax regime. Due to the material exposure to commercial real estate, we think that the bank is more sensitive to economic downturns than its cantonal bank peers.

Exposures outside the canton currently account for 25% of the total portfolio, which is higher than for most peers given the small size of its home canton. We think that in terms of the risk profile, the activities in neighboring cantons are similar to those locally.

ZGKB engages in very limited trading activities, generating only marginal market risk. This risk comprises mainly interest rate risk from mismatches in asset-liability management, which are adequately hedged, in our view.

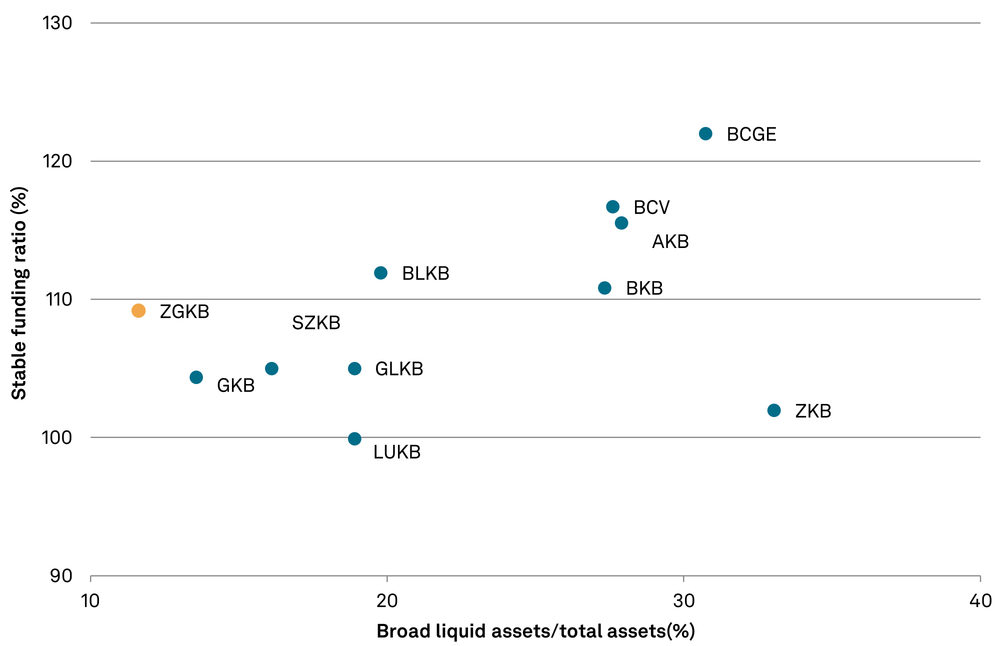
Funding And Liquidity: Strong Retail Deposit Franchise, With Low Reliance On Wholesale Funding And Adequate Liquidity

Our funding assessment for ZGKB remains in line with domestic peers. The guarantee provided by the canton implicitly supports funding and liquidity because it reinforces confidence, resulting in stable customer deposits.

We expect ZGKB's stable funding ratio will remain above 100% over the next two years--it was 109.2% as of June 2024--which is in line with that of other domestic banks. Core customer deposits accounted for 75.9% of the funding base on June 30, 2024, and we view this base as stable.

Chart 4

ZGKB funding and liquidity is in line with peers'



Data is as of H1 2024 .SZKB - Schwyzer Kantonalbank, ZGKB-Zuger Kantonalbank, GKB - Graubuendner Kantonalbank, AKB - Aargauische Kantonalbank, BKB - Basler Kantonalbank, GLKB - Glarner Kantonalbank, LUKB - Luzerner Kantonalbank, ZKB - Zuercher Kantonalbank, BLKB - Basellandschaftliche Kantonalbank, BCV - Banque Cantonale Vaudoise, BCGE - Banque Cantonale de Genev. Source: S&P Global Ratings.

We expect customer loans will continue to exceed customer deposits, at a loans-to-deposits ratio of 105%-115% in the next two years. Wholesale funding accounts for about 21% of the total funding base. Wholesale funding mostly consists of covered bonds, which we view as a reliable and stable source of funding in Switzerland, akin customer deposits. In our view, shareholder and guarantee structure will continue to support the bank's access to low-cost, long-term, wholesale funding.

Our liquidity ratio--broad liquid assets to total assets--was 11.6x for the same period, indicating a sound buffer to cover an extended period without access to market funding in an adverse scenario. Broad liquid assets to short-term wholesale funding equals 4.4x. These ratios are in line with most domestic peers'.

We do not think that the bank would be exposed to large withdrawals of customer deposits in times of stress owing to ZGKB's close ties with, and the statutory guarantee by, the canton. On the contrary, during increased market stress in early 2023, we observed a flight to quality that strengthened ZGKB's funding and liquidity.

Comparable Rating Analysis

We deduct one notch from the group's SACP under our comparable ratings analysis. We view the bank as more exposed to the economic cycle due to its substantial investment property portfolio (57.6% of mortgage loan portfolio at March 2024) and concentrated business model.

We believe that single-name concentrations in the corporate portfolio, driven by the canton's attractive tax regime, contribute to a weaker overall assessment compared with low-risk peers with higher SACPs. We therefore view ZGKB more in line with Swiss peers at the 'a' level, such as Luzerner Kantonalbank, Banque Cantonale de Geneve, and Banque Cantonale Vaudoise.

Support: Four Notches Of Uplift For Extremely High Likelihood Of Extraordinary Support

The long-term rating on ZGKB is four notches higher than its SACP. This reflects our opinion of an extremely high likelihood of timely and sufficient extraordinary government support from its owner, given the bank's integral link with and very important role for the canton.

This view is supported by ZGKB's contribution to the development of the canton and its state guarantee, incorporated in the law. The guarantee does not ensure timely repayment, under our definitions, but we believe that the canton has strong incentives to help the bank meet its obligations on time given the bank's importance to the regional economy.

We believe there is an extremely high likelihood that the canton would provide sufficient and timely support to the bank given that a default could severely damage Zug's reputation.

Environmental, Social, And Governance

ESG factors have no material influence on our credit rating analysis of ZGKB. As stipulated by law, the cantonal bank's mandate is focused on providing basic financial services to the canton's population and supporting economic development in the region. We view the bank's offering of transformation advice to clients as well as its sustainability in asset management as positive. However, environmental and social factors are only marginally supportive of our credit rating analysis.

Key Statistics

Table 1

Zuger Kantonalbank--Key figures

	--Fiscal year end Dec. 31--				
(Mil. CHF)	2024*	2023	2022	2021	2020
Adjusted assets	19,006	18,777	18,558	18,148	16,915
Customer loans (gross)	15,632	15,006	14,279	13,771	13,039
Adjusted common equity	1,453	1,386	1,313	1,334	1,302
Operating revenues	157	314	251	236	222
Noninterest expenses	82	160	133	122	114
Core earnings	61	124	100	100	98

*Data as of June 30. CHF--Swiss franc.

Table 2

Zuger Kantonalbank--Business position

	--Fiscal year end Dec. 31--				
(%)	2024*	2023	2022	2021	2020
Return on average common equity	8.0	8.5	6.9	5.4	5.5

*Data as of June 30.

Table 3

Zuger Kantonalbank--Capital and funding

	--Fiscal year ended Dec. 31--				
(%)	2024*	2023	2022	2021	2020
Tier 1 capital ratio	16.60	17.40	17.10	17.90	18.10
S&P Global Ratings' RAC ratio before diversification	N/A	26.66	23.70	23.57	N/A
S&P Global Ratings' RAC ratio after diversification	N/A	12.65	14.17	15.78	N/A
Adjusted common equity/total adjusted capital	100.00	100.00	100.00	100.00	100.00
Net interest income/operating revenues	65.93	67.35	62.71	64.13	67.03
Fee income/operating revenues	26.49	24.67	28.65	27.74	24.48
Market-sensitive income/operating revenues	5.42	6.17	6.42	5.72	5.76
Cost to income ratio	52.33	51.17	52.85	51.58	51.44
Preprovision operating income/average assets	0.79	0.82	0.64	0.65	0.66
Core earnings/average managed assets	0.65	0.66	0.54	0.57	0.60

*Data as of June 30. N/A--Not applicable. RAC--Risk-adjusted capital.

Table 4

Zuger Kantonalbank--Risk-adjusted capital framework data

(CHF 000s)	Exposure*	Basel III RWA	Average Basel III RW(%)	S&P Global Ratings RWA	Average S&P Global Ratings RW (%)
Credit risk					
Government & central banks	3,236,107	59,554	2	10,481	0
Of which regional governments and local authorities	124,986	10,007	8	4,499	4
Institutions and CCPs	59,251	12,282	21	9,103	15
Corporate	2,821,444	2,237,366	79	1,692,866	60

Table 4

Zuger Kantonalbank--Risk-adjusted capital framework data (cont.)					
Retail	12,829,407	4,911,944	38	2,866,843	22
Of which mortgage	12,131,597	4,380,512	36	2,448,156	20
Securitization§	0	0	0	0	0
Other assets†	115,402	68,410	59	103,862	90
Total credit risk	19,061,611	7,289,556	38	4,683,154	25
Credit valuation adjustment					
Total credit valuation adjustment	--	6,174	--	0	--
Market Risk					
Equity in the banking book	0	0	0	0	0
Trading book market risk	--	31,741	--	47,611	--
Total market risk	--	31,741	--	47,611	--
Operational risk					
Total operational risk	--	499,433	--	469,585	--
	Exposure	**Basel III RWA**	**Average Basel II RW (%)**	**S&P Global Ratings RWA**	**% of S&P Global Ratings RWA**
Diversification adjustments					
RWA before diversification	--	7,977,228	--	5,200,350	100
Total diversification/ Concentration adjustments	--	--	--	5,755,489	111
RWA after diversification	--	7,977,228	--	10,955,839	211
		Tier 1 capital	**Tier 1 ratio (%)**	**Total adjusted capital**	**S&P Global Ratings RAC ratio (%)**
Capital ratio					
Capital ratio before adjustments		1,385,524	17.4	1,386,425	26.7
Capital ratio after adjustments‡		1,385,524	17.4	1,386,425	12.7

*Exposure at default. §Securitization exposure includes the securitization tranches deducted from capital in the regulatory framework. †Exposure and S&P Global Ratings' 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. CCPs--Central counterparty clearing house. Sources: Company data as of Dec. 31, 2023, S&P Global Ratings.

Table 5

Zuger Kantonalbank--Risk position					
	--Fiscal year ended Dec. 31--				
(%)	**2024***	**2023**	**2022**	**2021**	**2020**
Growth in customer loans	8.35	5.09	3.69	5.61	2.51
Total diversification adjustment/S&P Global Ratings' RWA before diversification	N/A	110.68	67.20	49.42	N/A
Total managed assets/adjusted common equity (x)	13.11	13.57	14.17	13.60	12.99
New loan loss provisions/average customer loans	0.04	0.06	0.02	0.00	0.00
Gross nonperforming assets/customer loans + other real estate owned	0.17	0.18	0.21	0.27	0.24
Loan loss reserves/gross nonperforming assets	N/A	335.62	284.14	218.33	242.73

*Data as of June 30. N/A--Not applicable. RWA--Risk-weighted assets.

Table 6

Zuger Kantonalbank--Funding and liquidity					
	--Fiscal year ended Dec. 31--				
(%)	2024*	2023	2022	2021	2020
Core deposits/funding base	75.86	76.26	73.90	63.17	65.93
Customer loans (net)/customer deposits	118.28	113.88	112.70	130.36	127.66
Long-term funding ratio	97.31	98.27	95.87	84.60	89.49
Stable funding ratio	109.17	113.42	114.75	103.43	107.24
Short-term wholesale funding/funding base	2.91	1.88	4.46	16.70	11.44
Regulatory net stable funding ratio	143.00	146.80	148.00	137.00	N/A
Broad liquid assets/short-term wholesale funding (x)	4.37	8.33	4.10	1.20	1.63
Broad liquid assets/total assets	11.62	14.26	16.76	18.38	16.97
Broad liquid assets/customer deposits	16.75	20.49	24.77	31.76	28.27
Net broad liquid assets/short-term customer deposits	13.09	18.29	19.32	5.37	11.09
Regulatory liquidity coverage ratio (LCR) (%)	147.00	160.40	152.00	140.00	161.00
Short-term wholesale funding/total wholesale funding	12.05	7.90	17.11	45.35	33.58
Narrow liquid assets/3-month wholesale funding (x)	8.34	16.98	5.93	1.54	2.18

*Data as of June 30.

Zuger Kantonalbank--Rating component scores	
Issuer Credit Rating	**AA+/Stable/A-1+**
SACP	a
Anchor	a-
Economic risk	1
Industry risk	3
Business position	Adequate
Capital and earnings	Very strong
Risk position	Adequate
Funding	Adequate
Liquidity	Adequate
Comparable ratings analysis	-1
Support	+4
ALAC support	0
GRE support	+4
Group support	0
Sovereign support	0
Additional factors	0

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

Related Criteria

- Criteria | Financial Institutions | General: Risk-Adjusted Capital Framework Methodology, April 30, 2024
- 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
- 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 Detail (As Of December 17, 2024)*	
Zuger Kantonalbank	
Issuer Credit Rating	AA+/Stable/A-1+
Issuer Credit Ratings History	
08-Nov-2022	AA+/Stable/A-1+
Sovereign Rating	
Switzerland	AAA/Stable/A-1+

*Unless otherwise noted, all ratings in this report are global scale ratings. S&P Global Ratings' credit ratings on the global scale are comparable across countries. S&P Global Ratings' credit ratings on a national scale are relative to obligors or obligations within that specific country. Issue and debt ratings could include debt guaranteed by another entity, and rated debt that an entity guarantees.