Bulletin:

Deutsche Pfandbriefbank's First Quarter Results Show A Mixed Picture

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This report does not constitute a rating action.

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FRANKFURT (S&P Global Ratings) May 14, 2024--S&P Global Ratings today said that Deutsche Pfandbriefbank AG's (pbb)'s first-quarter 2024 earnings confirm our view that ongoing challenging conditions in commercial real estate (CRE) markets, especially in the U.S., would lead to further material credit losses and reduced, but positive, earnings.

Pbb's published earnings and credit metrics are consistent with the expectations underpinning our rating action in February 2024 (see "Deutsche Pfandbriefbank Downgraded To 'BBB-/A-3' On Challenges From Commercial Real Estate; Outlook Negative," published on Feb. 14, 2024). The 'BBB-/A-3' long- and short-term ratings are based on our view that pbb will remain moderately profitable in 2024, with credit losses contained at about 35 basis points (bps)-45bps in our forecast, and that the bank can demonstrate solid capital, funding, and liquidity buffers to mitigate the risk of eroding investor confidence.

Pbb today reported €34 million pretax earnings for the quarter, again heavily affected by elevated credit losses of €47 million, but slightly up from the previous year's €32 million profit. However, to support profitability, the bank continues to opportunistically selling a significant amount of assets in the non-strategic portfolio and repurchasing liabilities below their nominal value. We understand pbb is planning further asset sales and active balance sheet management to improve capital efficiency, but also to increase the capital buffer in persistently difficult markets.

Positively, pbb did not record a material increase in nonperforming loans (NPLs) in the first quarter, and two NPLs were restructured and repaid. That said, our negative outlook reflects that we remain cautious on potential further asset quality deterioration in the U.S. office book, but also on the German portfolio. This is because higher-for-longer interest rates, especially in the U.S., will likely delay the recovery in CRE transaction activity and prices.

We note that pbb materially increased its retail deposit base in the first four months by about €1.5billion to €8.1 billion, with improved good average duration of 3.6 years. The vast majority of the total deposit base is covered by the statutory deposit protection scheme that supports deposit stability. This reduces the dependency on tapping the wholesale markets at high coupon expectations, and pbb confirmed that it sees no need to issue senior benchmarks in 2024. However, we expect that pbb could, if necessary, issue covered and senior issuances privately or into the market, as demonstrated by a tap of €100 million in mortgage covered bonds in the first quarter.

Delivering consistently supportive financials and improving investor confidence on asset quality will support cheaper funding access and is key for improving profitability.

We do not expect pbb to release details on strategic revisions until the capital markets day in autumn.