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Research Update:

Deutsche Pfandbriefbank AG 'BBB-/A-3' Ratings Affirmed On U.S. Exit; Outlook Stable

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Overview

- We think that Deutsche Pfandbriefbank AG (PBB)'s announced exit from the U.S. commercial real estate (CRE) market simplifies its credit risk profile but weighs on near-term earnings and narrows its franchise.
- PBB is considering acquiring a small Germany-based asset manager that could support PBB's domestic franchise but is unlikely to improve its business position materially.
- We therefore affirmed our 'BBB-/A-3' long- and short-term issuer credit ratings and related issue ratings.
- The stable outlook considers that the wind-down costs and the potential acquisition are manageable from a capital perspective.

Rating Action

On June 24, 2025, S&P Global Ratings affirmed its 'BBB-/A-3' long- and short-term issuer credit ratings on Germany-based Deutsche Pfandbriefbank AG (PBB). The outlook remains stable.

We also affirmed our 'BBB/A-2' long- and short-term resolution counterparty ratings on PBB and affirmed all issue ratings.

Rationale

In our view, PBB's exit from the U.S. market is broadly neutral to its credit profile. On June 18, 2025, PBB announced that it will fully wind down its loss-making U.S. business through portfolio sales, securitization, and gradual run-off strategies. This represents a shift from its October 2024 stance, when it still considered the U.S. East Coast a core market while exiting the West Coast.

We view this exit as an inevitable step, given the ongoing weakness of its second-tier U.S. franchise and recent substantial credit losses. Transitioning to a more stable and profitable business model focused on its European core markets could gradually enhance its lending book's risk profile. However, amid high competition, prospects remain uncertain and PBB's exit from the large U.S. market narrows its franchise and revenue diversification.

We expect that wind-down costs will be manageable from a capital perspective. Although PBB reaffirmed its financial targets for 2027, it withdrew its 2025 guidance due to potential losses from restructuring costs and U.S. portfolio revaluations in preparation for the disposal process, as current portfolio returns lag below market rates. This could result in a net loss in its 2025 financial accounts, counterbalanced in our risk-adjusted capital (RAC) ratio forecast by reduced risk-weighted assets as a result of exiting the U.S.

PBB aims to demonstrate tangible progress in profitability and resilience. The management team has responded to challenging U.S. CRE markets and development portfolios by reducing its reliance on wholesale markets and actively managing the balance sheet to enhance earnings and capitalization. However, progress toward the 2027 goals remains limited, in our view. Specifically, improvements in PBB's risk-return profile have been slow so far, and there has been limited progress in building its asset management and brokerage services. Fees are forecast to contribute about 10% of operating revenues by 2027, which requires inorganic growth in the asset management segment. We will evaluate whether the planned acquisition of a Germany-based real estate manager will help to meet these objectives, but we are uncertain about PBB's economies of scale in offering competitive products in these segments. Our ratings reflect PBB's structurally weak profitability and anticipate a return to meaningful profits by 2026, exceeding 2024 levels, with steady progress thereafter.

Higher credit losses could further pressure ratings. We think that CRE valuations and transaction volumes in the U.S. and Europe are nearing or have already passed their cyclical lows, reducing downside risks to PBB's credit profile. Consequently, we expect loan loss provisions to decrease further in 2025--excluding any one-off impacts from the U.S. disposal--to approximately 35 basis points (bps) and about 25 bps-30 bps in 2026, down from 45 bps in 2024. However, we acknowledge significant uncertainty regarding future economic conditions and interest rates; a deeper recession in Europe or another spike in interest rates could adversely affect asset quality and its bottom-line profitability beyond our base case.

Outlook

The stable outlook reflects our view that PBB will absorb the ongoing challenges posed by challenging CRE markets and the related cost of risk with preprovision earnings over the next two years. We also expect the bank to manage the U.S. exit effectively and keep related costs at a manageable level. The outlook assumes that PBB will uphold strong capitalization, return to sustainable profitability from 2026, maintain a resilient funding profile, and preserve sufficient loss-absorbing capacity.

Downside scenario

We could lower our ratings over the next two years if:

- CRE markets show renewed signs of stress due to increasing rates or weaker economic developments, which could increase risks to PBB's asst quality and capitalization;
- There are material strategic revisions to PBB's business model beyond the exit from the U.S., and a failure to increase its resilience, while competitive pressure weighs on profitability; and
- A decline in investor confidence restricts PBB's market access at reasonable spreads for a prolonged period.

Upside scenario

We consider an upgrade as remote and dependent on PBB materially improving its business diversification and resilience by successfully implementing its 2027 strategy, along with significantly increasing its fee income contribution and improving its CRE book diversification. An upgrade would also require PBB to materially improve its risk-adjusted profitability and significantly reduce its nonperforming loans.

Rating Component Scores

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Issuer Credit Rating	BBB-/Stable/A-3
SACP	bb+
Anchor	bbb+
Business position	Constrained (-2)
Capital and earnings	Strong (1)
Risk position	Constrained (-2)
Funding and liquidity	Adequate and Adequate (0)
Comparable ratings analysis	0
Support	1
ALAC support	1
GRE support	0
Group support	0
Sovereign support	0
Additional factors	0
SACP--Stand-alone credit profile. ALAC--Additional loss-absorbing capacity. GRE--Government-related entity.	

Related Criteria

- General Criteria: Hybrid Capital: Methodology And Assumptions, Feb. 10, 2025
- 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: Principles Of Credit Ratings, Feb. 16, 2011

Related Research

- Research Update: Deutsche Pfandbriefbank Outlook Revised To Stable On Stabilizing Asset Quality; 'BBB-/A-3' Ratings Affirmed, March 11, 2025
- Deutsche Pfandbriefbank AG, Jan. 17, 2025
- German Banking Outlook 2025: Resilient In The Face Of Adversity, Jan. 23, 2025
- Deutsche Pfandbriefbank Continues To Navigate Difficult Commercial Real Estate Markets, Aug. 14, 2024
- Deutsche Pfandbriefbank's First Quarter Results Show A Mixed Picture, May 14, 2024
- Deutsche Pfandbriefbank Downgraded To 'BBB-/A-3' On Challenges From Commercial Real Estate; Outlook Negative, Feb. 14, 2024

Ratings List

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at https://disclosure.spglobal.com/ratings/en/regulatory/ratings-criteria for further information. A description of each ofS&PGlobal Ratings' ratingcategories is contained in"S&PGlobal Ratings Definitions"at https://disclosure.spglobal.com/ratings/en/regulatory/article/-/view/sourceId/504352. Complete ratings information is available to RatingsDirect subscribers at www.capitaliq.com. All ratings referenced herein can be found onS&PGlobal Ratings'public website at www.spglobal.com/ratings.

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