MOODY'S
RATINGS

CREDIT OPINION
9 July 2024

New Issue

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RATINGS

Lloyds Bank GmbH

Domicile	Berlin, Germany
Long Term CRR	A2
Type	LT Counterparty Risk Rating - Fgn Curr
Outlook	Not Assigned
Long Term Debt	Not Assigned
Long Term Deposit	A3
Type	LT Bank Deposits - Fgn Curr
Outlook	Stable

Please see the ratings section at the end of this report for more information. The ratings and outlook shown reflect information as of the publication date.

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Lloyds Bank GmbH

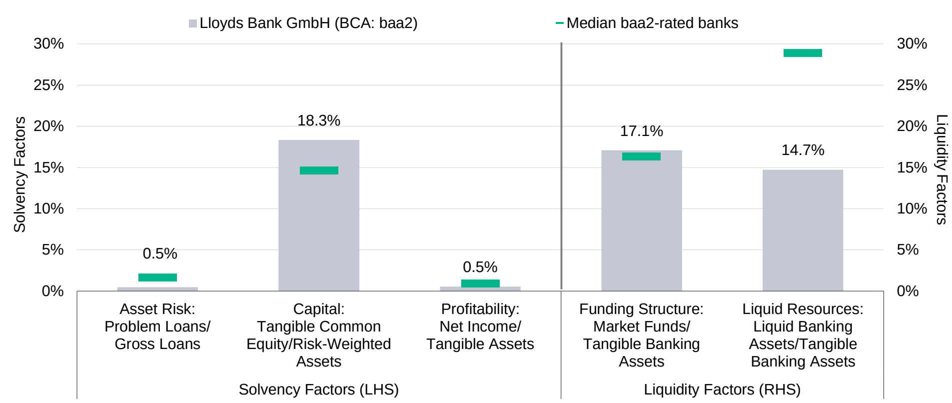
New issuer - Sound asset quality and granular deposit base constrained by high leverage and only adequate liquidity

Summary

On 4 July 2024, we assigned first-time A3/P-2 deposit ratings to Lloyds Bank GmbH (LB GmbH). LB GmbH's ratings reflect its baa2 BCA, two notches of affiliate support uplift, which is based on the assumption of very high support from its parent Lloyds Bank plc (A1 stable/ A1 stable, a3[1]) and results an a3 Adjusted BCA; no rating uplift from our Advanced Loss Given Failure (LGF) analysis, which incorporates the relative loss severity of a liability class; as well as no rating uplift from government support given the small size of the issuer relative to the banking sector in Germany.

LB GmbH's baa2 BCA reflects its overall sound combined solvency profile and a satisfying combined liquidity profile. The BCA also reflects the bank's narrow and quasi-monoline business focus on Dutch residential real estate lending, which exposes LB GmbH to considerable concentration risks in case of a severe property downturn and results in a lack of sufficient earnings diversification. LB GmbH's strong asset quality and capitalisation help offset risks from its concentrated lending books and high loan growth, as well as its low leverage ratio of below 4%. Further, LB GmbH's sustained, proven access to granular retail deposits is a relative strength. However, the bank's only moderate stock of liquid resources fluctuates alongside the bank's ability to raise and maintain deposits at attractive costs in a highly competitive market. LB GmbH's mainly German deposit base is largely decoupled from its mostly Dutch lending franchise, which could reduce the bank's ability to source cheap funding and maintain adequate liquidity ratios.

Exhibit 1
Rating Scorecard - Lloyds Bank GmbH - Key ratios



Source: Moody's Ratings

Credit strengths

» Granular loan book with sound asset quality

» Access to granular retail and, therefore, mostly statutorily guaranteed retail deposits

» Strong strategic and operational linkage with parent bank

Credit challenges

» Strong business focus results in lack of income diversification

» High, but only gradually improving, balance-sheet leverage

» Limited liquid resources

» Deposit franchise faces increasing competition and remains decoupled from the bank's lending assets

Rating outlook

» The stable outlook reflects our expectation of a largely stable financial profile over the next 12 months as well as our assumption of an unchanged liability structure over time.

Factors that could lead to an upgrade

» LB GmbH's ratings could be upgraded if the BCA of Lloyds Bank plc gets upgraded. In addition, LB GmbH's ratings may benefit from additional rating uplift from our Advanced LGF analysis through meaningful issuance of senior unsecured and subordinated debt instruments.

» LB GmbH's BCA could be upgraded if the bank significantly improves its leverage ratio and sustainably bolsters its cash and liquidity reserves while maintaining a low dependence on more confidence-sensitive market funding. However, this is likely to be offset by a reduction in affiliate support unless Lloyds Bank plc's BCA improves as well.

Factors that could lead to a downgrade

» LB GmbH's ratings could be downgraded if the bank's BCA is downgraded or if Lloyds Bank plc's BCA is downgraded, leading to fewer notches of affiliate support uplift. LB GmbH's ratings could also be downgraded if our Advanced LGF analysis indicates a higher loss severity for certain instrument classes, for example if deposits get replaced with covered bonds in a more pronounced manner than anticipated.

» LB GmbH's BCA could be downgraded if its combined solvency weakens, for example because of an increase in non-performing loans or its leverage ratio. The BCA could also be downgraded if the bank increase its market funding dependence beyond our current expectation or in case of a sustainably reduced level of liquidity reserves.

Key Indicators

Exhibit 2
Lloyds Bank GmbH (Consolidated Financials) [1]

	12-23[2]	12-22[2]	12-21[2]	12-20[2]	12-19[2]	CAGR/Avg.[3]
Total Assets (EUR Billion)	20.7	17.6	14.2	12.6	9.5	21.6[4]
Total Assets (USD Billion)	22.8	18.8	16.0	15.4	10.6	21.1[4]
Tangible Common Equity (EUR Billion)	0.7	0.6	0.5	0.4	0.3	21.1[4]
Tangible Common Equity (USD Billion)	0.8	0.6	0.6	0.5	0.4	20.6[4]
Problem Loans / Gross Loans (%)	0.4	0.4	0.6	0.9	0.9	0.7[5]
Tangible Common Equity / Risk Weighted Assets (%)	18.3	17.8	26.3	25.1	22.0	21.9[6]
Problem Loans / (Tangible Common Equity + Loan Loss Reserve) (%)	9.2	9.4	12.7	21.3	22.0	14.9[5]
Net Interest Margin (%)	1.5	1.3	1.3	1.7	1.4	1.4[5]
PPI / Average RWA (%)	4.8	4.2	4.3	6.1	4.3	4.7[6]
Net Income / Tangible Assets (%)	0.6	0.4	0.5	0.5	0.3	0.5[5]
Cost / Income Ratio (%)	36.2	44.2	50.1	41.5	43.3	43.0[5]
Market Funds / Tangible Banking Assets (%)	17.1	19.6	12.2	32.9	30.4	22.4[5]
Liquid Banking Assets / Tangible Banking Assets (%)	14.7	14.3	12.4	11.8	9.4	12.5[5]
Gross Loans / Due to Customers (%)	116.1	128.2	103.7	135.7	137.1	124.2[5]

[1] All figures and ratios are adjusted using Moody's standard adjustments. [2] Basel III - fully loaded or transitional phase-in; LOCAL GAAP. [3] May include rounding differences because of the scale of reported amounts. [4] Compound annual growth rate (%) based on the periods for the latest accounting regime. [5] Simple average of periods for the latest accounting regime. [6] Simple average of Basel III periods.
Sources: Moody's Ratings and company filings

Profile

Lloyds Bank GmbH (LB GmbH) is a small German bank based in Berlin with €20.7 billion in total assets as of 31 December 2023. The bank was founded in 2019 through the asset transfer of the Dutch and German branch of Bank of Scotland plc (A1 stable/A1 stable, a3[2]) and is now a fully owned subsidiary of Lloyds Bank plc with two offices, one in Berlin and one in Amsterdam.

LB GmbH is an online direct bank with a focus on retail banking products. In Germany, it advertises its deposits and retail lending products under the “Bank of Scotland” brand whereas in the Netherlands it uses the “Lloyds Bank” brand. As of year-end 2023, most of its loan book consisted of Dutch residential mortgages distributed through brokers, while the deposits funding the loan book mainly consisted of German retail deposits generated through online distribution channels.

As of year-end 2023, LB GmbH employed around 500 employees and had more than 150,000 customers in the Netherlands translating into a market share of 2% in the residential mortgage market in the Netherlands.

Weighted Macro Profile of Strong (+)

LB GmbH is a bank focused on the Dutch residential mortgage market and displays only limited lending exposures in Germany. As a result, we assign a Strong + Macro Profile to LB GmbH, in line with the Macro Profile of the Netherlands and Germany.

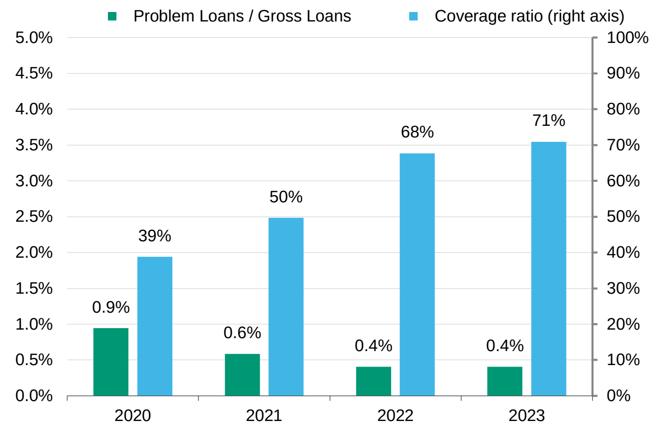
Detailed credit considerations

Strong loan growth and concentrations in residential mortgage lending drive asset risks

We assign an a2 Asset Risk score to LB GmbH, four notches below the aa1 initial score generated from a three-year average problem loan ratio of 0.5%. The negative adjustment captures the bank's high exposure and concentration to the Dutch residential mortgage market and takes account of the very strong loan growth in recent years which has increased risks potentially stemming from an unseasoned portfolio.

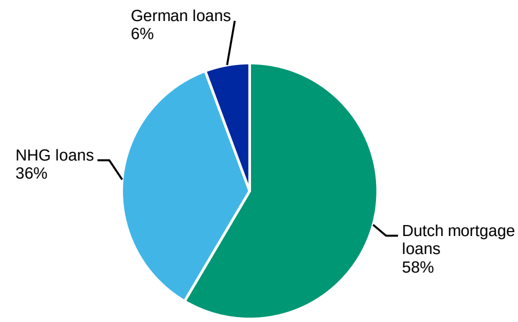
This strong concentration to the Dutch residential mortgage market is partially mitigated by the fact that around 38% of those loans are guaranteed by the National Mortgage Guarantee (NHG), effectively eliminating related credit risks. NHG is a guarantee provided to the mortgage lender by a government-backed foundation, the Dutch Homeownership Guarantee Fund (Stichting Waarborgfonds Eigen Woningen). In 2023, NHG loans were applicable for mortgages up to a volume of €405,000.

Exhibit 3
LB GmbH's asset quality is strong



Problem loan ratio is in accordance with our definition; the coverage ratio compares problem loans to specific and generic loan-loss reserves.
Sources: Company reports, Moody's Ratings

Exhibit 4
LB GmbH's loan book is narrowly focused on residential mortgages in the Netherlands (€17.5bn total as of year-end 2023)



Sources: Company reports, Moody's Ratings

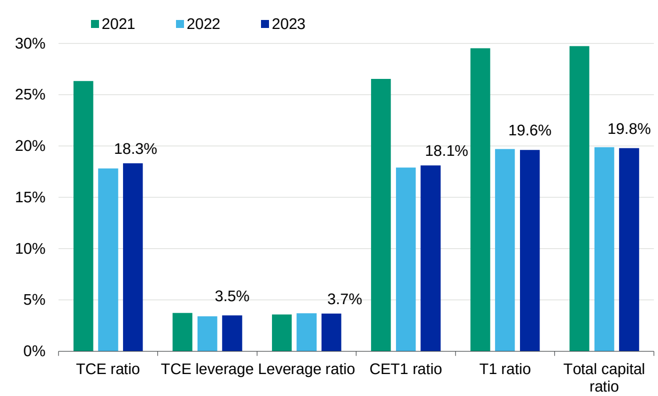
The bank's loan book grew 17.5% year-over-year in 2023 and comprised €17.5 billion of predominantly mortgages. Despite the strong increase in lending volumes, the bank did not compromise on its credit standards: Loan-to-value (LTV) ratios remained largely stable, with the majority of new business typically underwritten at below 75% LTV and a long fixed-rate period of above 10 years. Moreover, the bank's mortgage properties are well diversified across the Netherlands.

As of year-end 2023, the bank's stock of impaired loans slightly increased to €71 million, or 0.4% of total gross loans (2022: €61 million). The bank's cash coverage of problem loans of 71% as of year-end 2023 is adequate and in line with peers.

High balance-sheet leverage implies some vulnerability, despite strong risk-weighted capitalisation

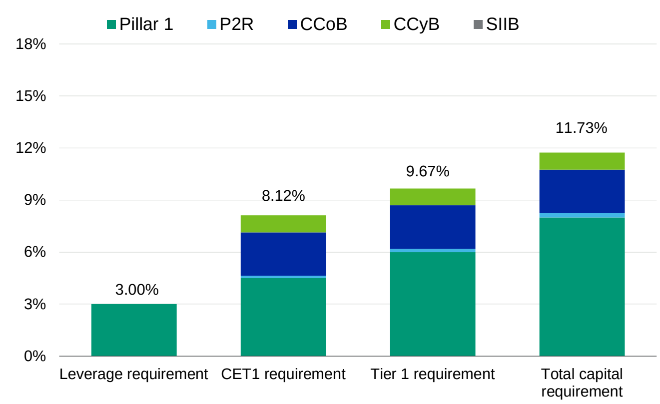
We assign an a2 Capital score to LB GmbH, three notches below the aa2 initial score. The negative adjustment reflects the limited buffers to regulatory minima because of the bank's sustained high, but only gradually improving, balance-sheet leverage as well as an expected decrease in strong risk-weighted capitalisation due to further loan growth and the upcoming implementation of risk floors under the finalised Basel III accord.

Exhibit 5
LB GmbH's capitalisation is strong, but leverage is very high



TCE = Tangible common equity; CET1 = Common Equity Tier 1 capital. The TCE leverage ratio compares TCE to tangible banking assets.
Sources: Company reports, Moody's Ratings

Exhibit 6
LB GmbH regulatory capital requirements
As of 31 December 2023



Sources: Company reports, Moody's Ratings

LB GmbH's tangible common equity (TCE) leverage is high, displaying a TCE leverage ratio of 3.5% as of the end of 2023. The bank's regulatory Tier 1 leverage ratio stood at 3.6% as of the same date, supported by €60 million of Additional Tier 1 (AT1) instruments held by the parent. This resulting buffer to the 3.0% regulatory leverage ratio requirement is lower than for many peers, exposing the bank to potentially nearing its regulatory minimum if future growth is not supported by an almost full retention of earnings. If sustained, this could exert strain on the bank's solvency profile, in particular if upcoming regulation or asset quality deterioration coupled with continued strong balance growth leads to higher-than-anticipated growth in risk-weighted assets and/or leverage exposures.

As of 31 December 2023, LB GmbH's TCE capital ratio stood at 18.3%, up from 17.8% as of year-end 2022. These ratios were close to the regulatory Common Equity Tier 1 (CET1) capital ratio of 17.6% as of the same date and remained well above the bank's respective capital requirements. Regarding the latter, LB GmbH originally carried a relatively high Pillar 2 buffer requirement (P2R) of 4.00% as part of its 2022 Supervisory Review and Evaluation Process (SREP) requirements because of its 'start-up' status following its founding in 2019. This buffer was reduced meaningfully following LB GmbH's strong ICAAP results and external reviews, including for sound management of interest-rate risks in the banking book (IRRBB).

On 3 July 2024, German regulator BaFin has increased the bank's minimum capital requirements. The capital add-on – which we estimate to be around 200 basis points – will be in place until the findings have been remediated. In any case, we expect LB GmbH to continue to display strong buffers over and above the now higher minimum.

Strong efficiency and stable return on assets despite reliance on interest income

We assign a ba1 Profitability score to LB GmbH, in line with the initial score. The assigned score reflects the bank's net income to tangible assets ratio of around 58 bps as of year-end 2023 as well as our expectation of a stable return on assets of 40-50 bps over the next foreseeable time frame.

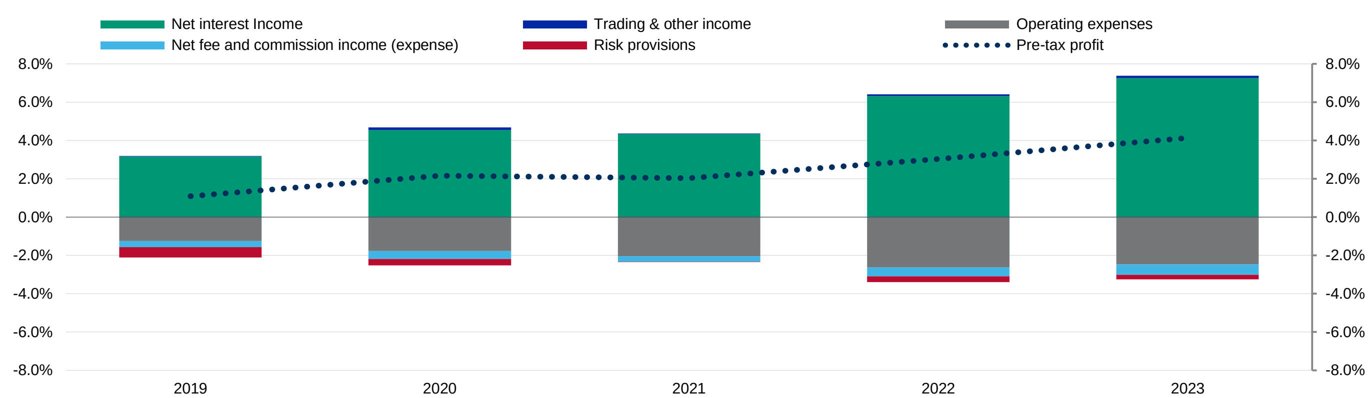
LB GmbH's main source of income is net interest income (NII) generated from its mortgage lending activities in the Netherlands while interest expenses largely relate to its deposits franchise in Germany. The bank further holds interest rate swaps with the parent group to manage its interest rate risk from maturity mismatches. Over the next 12 months and likely beyond, we expect net interest income to be strained by higher deposit funding costs in a highly competitive market, in part offset by continued high loan growth.

In 2023, LB GmbH's Moody's-adjusted net income of €119 million (2022: €72 million) was largely driven by growth in net interest income to €289 million (2022: €213 million), in part offset by growth in operating expenses to €97 million (2022: €87 million). Given LB GmbH's business model as direct bank with no expensive branch network, its profitability benefits from a low fixed cost base as reflected by a cost-to-income ratio of around 36% in 2023 (2022: 44%), which is favourable compared to peers.

Exhibit 7

LB GmbH's earnings are heavily reliant on net interest income

Data in % of RWA



Sources: Company reports, Moody's Ratings

Growing market funding dependence besides its strong online deposit franchise

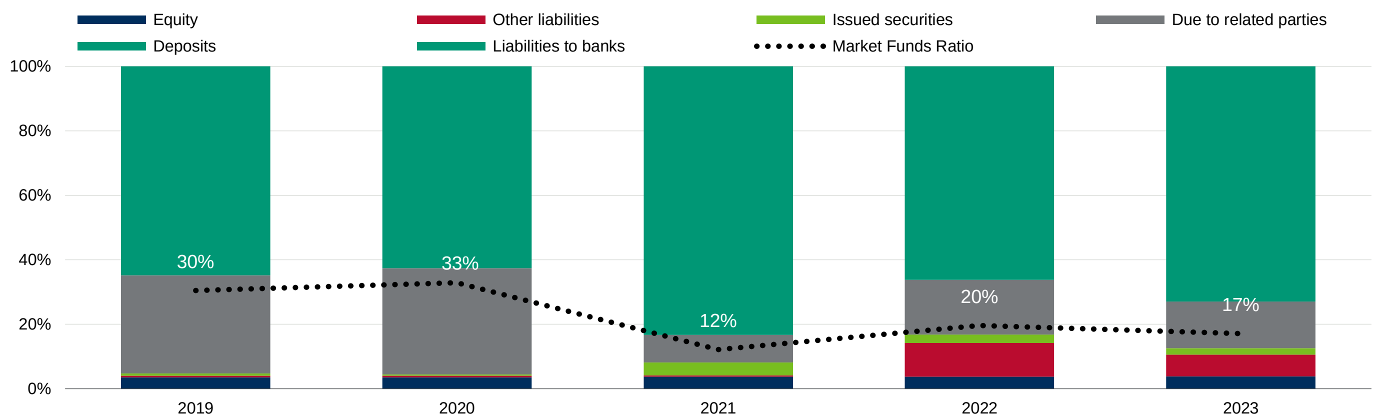
We assign a baa2 Funding Structure score to LB GmbH, two notches below the initial score of a3. The assigned score incorporates an expected moderate increase in market funding over the next two years following the planned issuance of covered bonds and additional RMBS as well as the bank's deposit franchise in Germany being exposed to more price-sensitive online deposits and being decoupled from the bank's Dutch lending client base.

LB GmbH's funding largely stems from retail deposits sourced through its online distribution channels under the “Bank of Scotland” brand. We consider online deposits less sticky compared to branch-based accounts and much more price sensitive than current accounts. As of year-end 2023, the bank held €15.0 billion of customer deposits (2022: €11.7 billion), representing 73% of total assets. The remaining funding consisted of €0.4 billion of RMBS as well as interbank funding of €3.1 billion, the latter almost exclusively provided by the parent.

The issuance of longer-term funding like covered bonds will help diversify the bank's funding mix and extend its funding tenors, as well as reduce funding from (and interest hedging with) the parent.

As of year-end 2023, LB GmbH's net stable funding ratio stood at 153% and its loan-to-deposit ratio was 116%.

Exhibit 8
LB GmbH's deposits dominate the current funding mix, supported by intragroup funding



Market Funds Ratio = Market funds/tangible banking assets
Sources: Company reports, Moody's Ratings

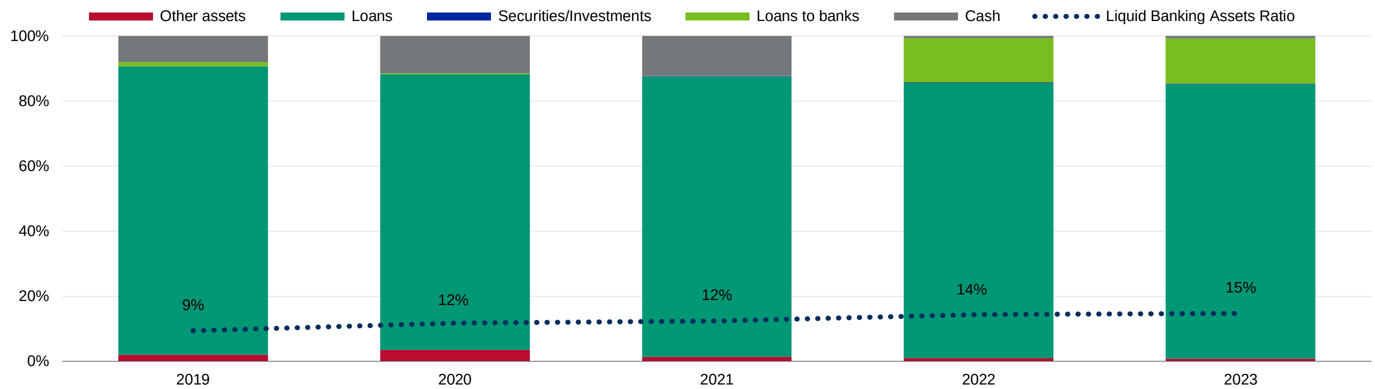
Adequate liquid resources

We assign a ba1 Liquid resources score to LB GmbH, in-line with the initial score. The adjustment reflects our expectation that the volume of liquid resources will slightly decline in relation to tangible assets as the bank continues to grow its lending activities.

Further, and considering its loan-to-deposit ratio of well above 100% as of the end of 2023, the bank has limited flexibility to manage larger and unexpected deposit outflows as long as it has not established a proven access to other sources of (market) funding. This exposes it to higher funding costs to retain or grow deposits in a highly competitive market to fund its lending operations, a credit negative. In case of stress, however, we would expect the parent to provide the necessary funding, limiting overall refinancing risks.

As of year-end 2023, LB GmbH held €0.15 billion in cash and interbank claims with central banks of €2.9 billion that we reflect in our liquid resources ratio of 14.7%, which is at the lower end of LB GmbH's peers. Over the next 12 to 18 months, we expect cash reserves to slightly decline, mainly driven by deposit growth contributing to the bank's cash reserves, the latter being reduced again as and when loans grow further.

Exhibit 9
LB GmbH's liquid resources remain only adequate



Liquid Banking Asset Ratio = Liquid assets/tangible banking assets
Sources: Company reports, Moody's Ratings

Strong business focus results in lack of income diversification constraining the bank's BCA

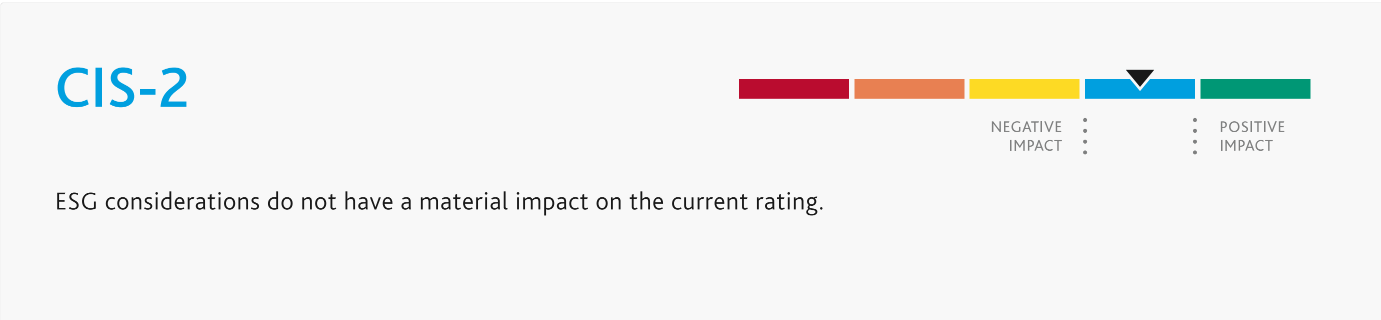
We reduce LB GmbH's Financial Profile by one notch to reflect the bank's lack of income diversification outside of its narrowly distributed largely Dutch real estate lending business. LB GmbH's revenue depend almost exclusively on this business line generating a very high share of the bank's net interest income and revenue. Therefore, we consider LB GmbH to operate a monoline business model, evidencing a lack of business diversification compared to more typical business models in banking.

Business diversification is an important gauge of a bank's sensitivity to stress in a single business line. It is related to earnings stability in the sense that earnings diversification across distinct and relatively uncorrelated lines of business increases the reliability of a bank's earnings streams and its potential to absorb shocks affecting a business line.

ESG considerations

Lloyds Bank GmbH's ESG credit impact score is CIS-2

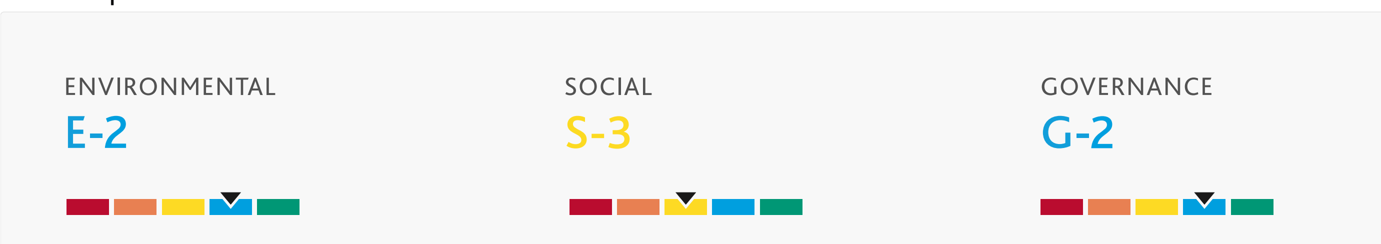
Exhibit 10
ESG credit impact score



Source: Moody's Ratings

LB GmbH's **CIS-2** indicates that ESG considerations have no material impact on the current ratings. This reflects the limited credit impact of environmental and social risk factors on the ratings to date, and low governance risks.

Exhibit 11
ESG issuer profile scores



Source: Moody's Ratings

Environmental

LB GmbH faces low exposure to environmental risks, which is lower than the average of its industry. The group has limited exposure to carbon transition risks because its loan book is highly concentrated in Dutch residential mortgages.

Social

LB GmbH faces moderate social risks related to customer relations and associated regulatory risks and to litigation exposure and is required to meet high compliance standards. The bank's strong conduct track record demonstrates the effective management of related product distribution risks by developed policies and procedures - in conjunction with Lloyds Banking Group plc - and is supported by LB GmbH's focus on plain-vanilla, transparent financial products and services for its clientele. Further, the bank's track record of handling sensitive customer data as well as technology solutions and organizational measures to prevent data breaches and business disruption help to manage high cyber and personal data risks. The bank is further exposed to demographic and societal trends. Banks in Germany and in the Netherlands face long-term economic and fiscal pressures arising from adverse demographic trends impacting demand for certain products and/or lowering economic growth prospects. Product diversity as well as ability to adapt to changing customer preferences, regulatory changes and societal trends would help mitigate these risks.

Governance

LB GmbH's governance risk is low. LB GmbH faces low governance risks, despite concentration risks inherent in its business model as a regionally focused mortgage lender. The bank's risk management, policies and procedures are embedded within those of the parent banking group and in line with industry practices. LB GmbH embeds conservative, risk-focused and risk-aware financial policies, and up-to-date corporate governance practices. The bank has a clear and simple organizational structure with no identified concerns regarding ownership and control. Because LB GmbH is fully controlled by Lloyds Banking Group plc, and despite its relatively small size, we have aligned the subsidiary's board structure, policies and procedures as well as the organizational structure score with that of its parent, given the bank's strategic importance and public affiliation with the group.

ESG Issuer Profile Scores and Credit Impact Scores for the rated entity/transaction are available on Moodys.com. In order to view the latest scores, please click here to go to the landing page for the entity/transaction on MDC and view the ESG Scores section.

Support and structural considerations

Affiliate support

Our considerations of a very high affiliate support from LB GmbH's direct parent Lloyds Bank plc results in two notches of rating uplift and an Adjusted BCA of a3. The very high support assumption is based on the strategic fit and the close operational integration of LB GmbH into Lloyds Banking Group plc (LBG, senior unsecured debt A3 stable, BCA a3). We also incorporates the 100% ownership by Lloyds Bank; additional financial interlinkages with its parent; and the brand similarity in its support assumption.

Loss Given Failure analysis

Domiciled in Germany, LB GmbH is subject to the EU's Bank Recovery and Resolution Directive (BRRD), which we consider an operational resolution regime. We assume the proportion of deposits considered junior at 10%, below our standard assumption of 26%, because of the bank's largely retail-oriented depositor base. All other assumptions are in line with our standard assumptions.

Our Advanced LGF analysis indicates a moderate loss given failure for LB GmbH's bank deposit ratings, leading to no rating uplift.

Government support considerations

We do not incorporate any rating uplift from government support to LB GmbH because of its small size in the context of the German banking sector.

Rating methodology and scorecard factors

The principal methodology we use in rating Lloyds Bank GmbH is the Banks Methodology, published in March 2024.

About Moody's Bank Scorecard

Our Scorecard is designed to capture, express and explain in summary form our Rating Committee's judgement. When read in conjunction with our research, a fulsome presentation of our judgement is expressed. As a result, the output of our Scorecard may materially differ from that suggested by raw data alone (though it has been calibrated to avoid the frequent need for strong divergence). The Scorecard output and the individual scores are discussed in rating committees and may be adjusted up or down to reflect conditions specific to each rated entity.

Rating methodology and scorecard factors

Exhibit 12

Rating Factors

Macro Factors		
Weighted Macro Profile	**Strong +**	**100%**

Factor	Historic Ratio	Initial Score	Expected Trend	Assigned Score	Key driver #1	Key driver #2
Solvency						
Asset Risk						
Problem Loans / Gross Loans	0.5%	aa1	↔	a2	Loan growth	Sector concentration
Capital						
Tangible Common Equity / Risk Weighted Assets (Basel III - transitional phase-in)	18.3%	aa2	↔	a2	Nominal leverage	Expected trend
Profitability						
Net Income / Tangible Assets	0.5%	ba1	↔	ba1	Return on assets	Expected trend
Combined Solvency Score		aa3		a3		
Liquidity						
Funding Structure						
Market Funds / Tangible Banking Assets	17.1%	a3	↔	baa2	Expected trend	Market funding quality
Liquid Resources						
Liquid Banking Assets / Tangible Banking Assets	14.7%	ba1	↔	ba1	Stock of liquid assets	Expected trend
Combined Liquidity Score		baa2		baa3		
Financial Profile				baa1		
Qualitative Adjustments				Adjustment		
Business Diversification				-1		
Opacity and Complexity				0		
Corporate Behavior				0		
Total Qualitative Adjustments				-1		
Sovereign or Affiliate constraint				Aaa		
BCA Scorecard-indicated Outcome - Range				baa1 - baa3		
Assigned BCA				baa2		
Affiliate Support notching				2		
Adjusted BCA				a3		

Balance Sheet	in-scope (EUR Million)	% in-scope	at-failure (EUR Million)	% at-failure
Other liabilities	4,912	23.8%	5,966	28.9%
Deposits	15,064	72.9%	14,009	67.8%
Preferred deposits	13,557	65.6%	12,880	62.4%
Junior deposits	1,506	7.3%	1,130	5.5%
Preference shares (bank)	60	0.3%	60	0.3%
Equity	620	3.0%	620	3.0%
Total Tangible Banking Assets	20,655	100.0%	20,655	100.0%

Debt Class	De Jure waterfall		De Facto waterfall		Notching		LGF Notching Guidance vs. Adjusted BCA	Assigned LGF notching	Additional Notching	Preliminary Rating Assessment
	Instrument volume + subordination	Sub-ordination	Instrument volume + subordination	Sub-ordination	De Jure	De Facto				
Counterparty Risk Rating	8.8%	8.8%	8.8%	8.8%	1	1	1	1	0	a2
Counterparty Risk Assessment	8.8%	8.8%	8.8%	8.8%	2	2	2	2	0	a1 (cr)
Deposits	8.8%	3.3%	8.8%	3.3%	0	0	0	0	0	a3

Instrument Class	Loss Given Failure notching	Additional notching	Preliminary Rating Assessment	Government Support notching	Local Currency Rating	Foreign Currency Rating
Counterparty Risk Rating	1	0	a2	0	A2	A2
Counterparty Risk Assessment	2	0	a1 (cr)	0	A1(cr)	
Deposits	0	0	a3	0	A3	A3

[1] Where dashes are shown for a particular factor (or sub-factor), the score is based on non-public information.
Source: Moody's Ratings

Ratings

Exhibit 13

Category	Moody's Rating
LLOYDS BANK GMBH	
Outlook	Stable
Counterparty Risk Rating	A2/P-1
Bank Deposits	A3/P-2
Baseline Credit Assessment	baa2
Adjusted Baseline Credit Assessment	a3
Counterparty Risk Assessment	A1(cr)/P-1(cr)

Source: Moody's Ratings

Endnotes

1 The ratings shown are Lloyds Bank's deposit and senior unsecured debt ratings together with their corresponding outlooks as well as its BCA.

2 The ratings shown are Bank of Scotland's deposit and backed senior unsecured debt ratings together with their corresponding outlooks as well as its BCA.

REPORT NUMBER 1409921

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