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Basler Kantonalbank

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Major Rating Factors

Strengths:

- Statutory guarantee of the Canton of Basel-City
- Sound asset quality and very strong capitalization
- Strong profitability and cost efficiency at group level despite investments into new IT infrastructure

Counterparty Credit Rating

AA+/Positive/A-1+

Weaknesses:

- Remaining profitability gap between parent bank and subsidiary, Bank Coop, unlikely to narrow fully
- Comparably higher concentration risk (single name, regional, and industry (real estate))

Rationale

The ratings on Switzerland-based Basler Kantonalbank (BKB) are based on the statutory guarantee provided by the sole owner, the Swiss canton (state) of Basel-City (Basel-City; AA+/Positive/A-1+), which legally obliges the canton to guarantee all liabilities incurred by the bank--excluding the bank's capital participation certificates (Partizipationsscheine) and liabilities of its subsidiaries, specifically Bank Coop (BC; not rated). Although this guarantee does not stipulate a timely repayment, Standard & Poor's Ratings Services believes that, to maintain investor and creditor confidence, the cantonal government would respond quickly to preserve the solvency of the bank in the unlikely event BKB were to suffer losses. Since fiscal year 2003, BKB has paid compensation on the guarantee.

With total consolidated assets of Swiss franc (CHF) 31 billion (\$27 billion) and adjusted common equity (ACE) of CHF2.6 billion at Dec. 31, 2008, the BKB group is the third-largest Swiss Cantonal Bank and one of the largest Swiss banking groups. Through the nationwide retail network of its subsidiary, BC, the BKB group has a better geographic diversification of its customer base and loan portfolio compared with most cantonal bank peers. BC represented 43% and 38% of BKB's consolidated assets and pretax income, respectively, with business focused on residential real estate and small and midsize enterprise (SME) lending. The parent's bank business is mainly focused on the wealthy Basel region, where it has a strong market share in retail banking, mortgage lending, and lending to SMEs.

BKB is expected to maintain its two-brand strategy, leveraging on both its strong brand recognition in the Canton of Basel-City and on Bank Coop on a national basis. BKB intends to raise revenues in line with cautious business growth targets and to maintain a stable stream of income by better exploiting its customer base, while maintaining sound asset quality. Mass-affluent banking and asset management is expected to continue to grow organically via acquiring expert teams rather than sizable takeovers of competitors' franchises, but could face higher earnings volatility due to the weaker capital market environment.

Although the lending business dominates BKB group's risk profile, mitigated by diversification and sufficient collateralization of exposures, market risk in both banking and trading book is prudently limited. Asset quality is strong and is dominated by granular and low-risk residential mortgages. However, BKB has a comparably higher

sensitivity to general swings in the Swiss economy through a loan portfolio, which comprises a comparably high level of single name and industry concentration (real estate--mainly residential mortgages). Funding has benefited from strong new money inflow of deposits during the global financial crisis. Liquidity remains strong, supported by a portfolio of low-risk and actively traded securities, whereas a high standardization of processes within the group addresses operational risks.

Profitability is expected to remain dominated by interest income while fee income from private banking activities may grow just slightly from the current low level. In 2008, bottom line profitability was impacted by a variety of extraordinary factors: valuations on its assets, including exposure to Lehmans; an adjustment in the value of one of its strategic holdings (National Swiss); as well as the implementation of a new IT infrastructure. We expect BKB to continue to focus on profitable growth in its core business segments while maintaining a conservative lending profile. However, during the expected more challenging economic environment going forward, we expect loan-loss provisions to customer loans to return to a level of around 30 basis points (bps) in 2009/2010 driven by a slightly higher--although still very low--provision in mortgage business and more corporate/SME defaults.

Capitalization remains a key positive rating factor as we expect further strengthening of the bank's capital position--BKB targets a capital quota of around 200% (currently 169%) versus the national requirements--and no movement toward a more aggressive dividend pay-out. With a Tier 1 capital ratio of 13.6%, BKB group's capitalization is considered very strong and continues to compare favorably by international standards. The currently outstanding volume (CHF50.1 million) of nonvoting participation certificates, which account for around 20% of the share capital ("Dotationskapital"), are expected to remain unchanged in volume.

Outlook

The positive outlook on BKB reflects that on the canton, as rating actions on the guarantor affect the ratings on BKB.

BKB is expected to maintain its sound financial and risk profile. Furthermore, we believe that neither the current guarantee mechanism and creditor protection, nor BKB's legal status and ownership structure will alter materially in the short to medium term. In the event of changes to the cantonal law that would lead to a privatization of the bank, BKB's existing obligations would be grandfathered under the cantonal guarantee. Any fundamental changes to the status quo with respect to either BKB's ownership structure or the cantonal guarantee could pressure the ratings. We do not expect BKB to materially increase its stake in BC going forward.

Basler Kantonalbank Financial Statistics					
	--Year ended Dec. 31--				
(Mil. CHF)	2008	2007	2006	2005	2004
KEY DATA					
Adjusted assets	31,219	27,832	25,629	24,621	23,749
Risk adjusted assets (regulatory definition)	N.A.	17,704	16,472	16,109	15,957
Customer loans (net)	21,006	19,868	18,680	18,019	17,316
Core/customer deposits	18,231	15,878	14,869	14,324	13,878
Adjusted common equity	2,582	2,504	2,380	2,177	1,943
Operating revenues	666	737	709	671	638

Basler Kantonalbank Financial Statistics (cont.)					
Noninterest expenses	413	354	326	308	299
Net income after extraordinary	146	244	253	234	248
BALANCE SHEET COMPOSITION (% of Adj. Assets)					
Cash and money market instruments/assets(adj.)	0.98	0.7	0.78	0.76	0.96
Securities/assets(adj.)	10.46	9.29	10.15	8.66	9.68
Loans (net)/assets(adj.)	67.29	71.39	72.89	73.19	72.91
P&L COMPOSITION (% of revenues)					
Net interest income/revenues	61.73	56.12	55.47	55.97	56.38
Fee income/revenues	27.08	29.17	29.39	29.17	26.6
Market-sensitive income/revenues	8.95	10.78	12.58	11.72	11.67
Noninterest expense/revenues	62.09	48.01	46.01	45.91	46.83
New loan loss provisions/revenues	4.42	4.12	4.33	7.54	8.73
Net income/revenues	25.94	38.05	40.18	39.17	43.53
PROFITABILITY (%)					
Net interest income (taxable equiv.)/avg. earning assets	1.52	N.A.	1.67	1.66	1.67
Noninterest expenses /assets(avg. adj.)	1.4	1.32	1.3	1.27	1.29
Net operating income before loss provisions/avg. risk assets (%)	N.A.	2.24	2.35	2.26	2.14
Net operating income after loss provisions/avg. risk assets (%)	N.A.	2.06	2.16	1.95	1.79
Net income/avg. risk assets (%)	N.A.	1.64	1.75	1.64	1.75
Core earnings/avg. tang. common equity (ROE) (%)	7.59	12.61	13.86	13.71	13.98
Funding and Liquidity					
Customer deposits/funding base	69.91	67.02	67.73	68.56	69.16
Total loans/customer deposits	138.81	144.02	144.59	146.48	143.19
Customer loans (net)/assets (adj.)	67.29	71.39	72.89	73.19	72.91
CAPITALIZATION (%)					
Adjusted common equity/adjusted assets	8.27	9	9.29	8.84	8.18
Adjusted common equity/customer loans (net)	12.29	12.6	12.74	12.08	11.22
Adjusted common equity/risk assets	N.A.	14.14	14.45	13.51	12.18
Adjusted total equity/risk assets	N.A.	13.54	13.87	12.96	11.65
ASSET QUALITY (%)					
New loan loss provisions/avg. customer loans (net)	0.14	0.16	0.17	0.29	0.33
Net charge-offs/avg. customer loans (net)	0.18	0.07	0.21	0.3	0.33
Loan loss reserves/customer loans (gross)	2.23	2.39	2.46	2.52	2.39
NPA (excl. delinquencies)/customer loans + ORE	1.56	1.92	1.95	2.31	2.43
Net NPA/customer loans (net) + ORE	(0.69)	(0.48)	(0.53)	(0.21)	0.04
Loan loss reserves/NPA (gross)	143.23	124.53	126.31	109	98.33

CHF--Swiss franc.N.A.--Not available.

Ratings Detail (As Of April 23, 2009)***Basler Kantonalbank**

Counterparty Credit Rating

AA+/Positive/A-1+

Certificate Of Deposit

AA+/A-1+

Ratings Detail (As Of April 23, 2009)* (cont.)	
Senior Unsecured (5 Issues)	AA+
Counterparty Credit Ratings History	
30-May-2008	AA+/Positive/A-1+
17-Jan-2006	AA+/Stable/A-1+
20-Oct-2003	AA+/Negative/A-1+
Sovereign Rating	
Swiss Confederation	AAA/Stable/A-1+
Related Entities	
Basel-City (Canton of)	
Issuer Credit Rating	AA+/Positive/A-1+
Senior Unsecured (2 Issues)	AA+

*Unless otherwise noted, all ratings in this report are global scale ratings. Standard & Poor's credit ratings on the global scale are comparable across countries. Standard & Poor's credit ratings on a national scale are relative to obligors or obligations within that specific country.

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