MOODY'S
INVESTORS SERVICE

Rating Action: Moody's downgrades Canadian banks

Global Credit Research - 28 Jan 2013

Toronto, January 28, 2013 -- Moody's Investors Service today downgraded the long-term ratings of six Canadian banks concluding the review initiated on 26 October 2012. The long-term senior debt ratings of the banks were all downgraded by 1 notch. We also removed systemic support from the ratings of all rated Canadian banks' subordinated debt instruments, including those issued by Royal Bank of Canada (RBC). RBC's other ratings were affirmed. The short term Prime-1 ratings of the Canadian banks were affirmed. All ratings for these banks now have a stable outlook. Moody's special comment "Key drivers of Canadian bank rating actions" (http://www.moodys.com/viewresearchdoc.aspx?docid=PBC_149485) provides additional commentary on the rationale behind today's actions. "Today's downgrade of the Canadian banks reflects our ongoing concerns that Canadian banks' exposure to the increasingly indebted Canadian consumer and elevated housing prices leaves them more vulnerable to unpredictable downside risks facing the Canadian economy than in the past." said David Beattie, a Moody's Vice President. "Following today's actions, the Canadian banks still rank amongst the highest rated banks in our global rating universe."

OVERVIEW OF TODAY'S ACTIONS

Bank of Montreal (BMO; downgraded to Aa3 stable from Aa2 for long-term deposits)

Bank of Nova Scotia (BNS; downgraded to Aa2 stable from Aa1 for long-term deposits)

Caisse centrale Desjardins (CcD; downgraded to Aa2 stable from Aa1 for long-term deposits)

Canadian Imperial Bank of Commerce (CIBC; downgraded to Aa3 stable from Aa2 for long-term deposits)

National Bank of Canada (NBC; downgraded to Aa3 stable from Aa2 for long-term deposits)

Toronto-Dominion Bank (TD; downgraded to Aa1 stable from Aaa for long-term deposits)

Please click on the following link to access the full list of affected credit ratings. This list is an integral part of this press release and identifies each affected issuer: http://www.moodys.com/viewresearchdoc.aspx?docid=PBC_149548

SUMMARY RATINGS RATIONALE

High levels of consumer indebtedness and elevated housing prices leave Canadian banks more vulnerable than in the past to downside risks the Canadian economy faces:

By 30 September 2012, Canadian household debt to personal disposable income reached a record 165%, up from 137% as of 30 June 2007, as debt grew faster than personal incomes. Growth in consumer debt has been driven by rising house prices, which have increased by approximately 20% since November 2007.

Downside risks to the Canadian economy have increased:

Moody's central scenario for Canada's gross domestic product (GDP) is for it to grow between 2% and 3% in 2013, but downside risks have increased. The open, commodity-oriented economy is exposed to external macro-economic risks, which if they arise would have significant ramifications for the Canadian economy, and consequently its banks.

NBC, BMO and BNS have sizeable exposure to volatile capital markets businesses:

Moody's believes that trading and investment banking activities expose financial firms to the risk of outsized losses and risk management and controls challenges, and leave them highly dependent on the confidence of investors, customers and counterparties.

Canadian banks' have noteworthy reliance on wholesale funding:

The Canadian bank's noteworthy reliance on confidence-sensitive wholesale funding, which is obscured by limited public disclosure, increases their vulnerability to financial markets turmoil.

Moody's has removed systemic support from the ratings of all Canadian banks' subordinated debt instruments that had benefited from support "uplift":

The rating agency believes the global trend towards imposing losses on junior creditors in the context of future bank resolutions reduces the predictability of such support being provided to the sub-debt holders of the large Canadian banks given the Canadian regulators' broad legislated resolution powers. The removal of support for subordinated debt is consistent with recent actions we've taken elsewhere, including in many European countries, reflecting the increased likelihood that sub-debt holders would be subject to burden sharing in the event support was required.

SUMMARY OF BANK SPECIFIC RATING RATIONALE (listed alphabetically)

Bank of Montreal (BMO; Aa3 stable; C+/a2 stable)

Reflecting the smaller size of its Canadian residential mortgage business relative to peers, BMO has a high proportionate exposure to unsecured and non-real estate secured consumer loans, (20% of total Canadian consumer loans at 31 October 2012) which Moody's views as the debt category most likely to give rise to sizeable incremental loss experience in the event of a sharp system-wide economic shock. In addition, BMO's capital markets earnings contribution is the second highest in the peer group (25% at 31 October 2012) and BMO has significant growth aspirations for its US mid-cap corporate and investment banking initiative which may increase its reliance on inherently less stable capital markets earnings going forward.

The downgrade of BMO also resulted in a downgrade of its rated US subsidiaries, whose ratings benefit from Moody's expectation of support for them from BMO. Specifically, BMO Financial Corp.'s issuer rating was lowered to A3 from A2 and the long-term deposit rating of BMO Harris Bank, N.A., was lowered to A2 from A1. Moody's standalone bank financial strength rating/baseline credit assessment of C/a3 on BMO Harris Bank, N.A., as well as its Prime-1 short-term rating, were affirmed.

Bank of Nova Scotia (BNS; Aa2 stable; B-/a1 stable)

BNS has the most diversified earnings profile of the peer group at the business segment level and arguably the most line of business diversification within those segments, given the numerous geographies in its international division and its diversified capital markets lines of business. BNS has low historical earnings volatility evidencing the consistent quality of execution against its diversification strategies. That being said, it has mid-peer group levels of proportionate exposure to less well secured Canadian consumer debt relative to peers. BNS is also more reliant upon confidence sensitive wholesale funding than its peers, a consideration which weighs on its credit profile.

The downgrade of BNS also resulted in a downgrade of ING Bank of Canada, a domestic subsidiary that BNS acquired in November 2012, as a result of the parental support incorporated in ING Bank of Canada's ratings. Specifically, ING Bank of Canada's long-term deposit rating was lowered to Aa3 from Aa2 and the subordinated debt rating was lowered to A2 from Aa3. Moody's standalone bank financial strength rating/baseline credit assessment of C-/baa1 (negative outlook) on ING Bank of Canada, as well as its Prime-1 short-term rating, were affirmed.

Canadian Imperial Bank of Commerce (CIBC; Aa3 stable; C+/a2 stable)

CIBC is the most reliant of the Canadian banks on domestic P&C earnings, which generated 71% of earnings in 2012. In the event of a sharp system-wide economic shock, or a prolonged period of low growth and low interest rates, CIBC has only modest "shock absorbers" in the form of diversified earnings to offset earnings erosion and/or capital charges attributable to increased Canadian consumer loan losses. Our review of CIBC's capital markets growth aspirations has left us less concerned that the bank might return to its previous high reliance on inherently less stable capital markets earnings.

Caisse Centrale Desjardins (CcD; Aa2 stable; C/a3 stable)

Among the peer group, Desjardins has the second highest exposure to Canadian consumer credit after CIBC. At December 31, 2011, loans to individuals represented 78% of gross loans. This is offset in part by the group's bias towards residential mortgage lending (82% of total consumer loans) and the diversification benefit from insurance operations. While unsecured consumer credit is a relatively small proportion of total consumer assets, Desjardins' retail concentration means that non-real estate secured consumer credit exposure is still relatively high as a proportion of Tier 1 capital at 146%. We highlight that Desjardins' concentration in Québec is in this instance an advantage because it means that the group's exposure to the riskiest property markets (Vancouver and Toronto) is very low. While household debt to income is lower in Québec than the rest of Canada (partly because the province has a lower level of home ownership), leverage has increased, leaving consumers exposed to external macro-economic shocks. As an export-oriented economy, Québec shares similar exposures to external economic events as Canada as a whole.

National Bank of Canada (NBC; Aa3 stable; C/a3 stable)

NBC is the Canadian bank most reliant upon inherently less stable capital markets earnings, which generated 32% of total earnings in 2012. Within capital markets, NBC's franchise is heavily oriented towards three concentrations; (1) equity derivatives, (2) fixed income (NBC is the leading underwriter of Canadian government debt despite its limited size) and, (3) Quebec investment banking. Reflecting this exposure, NBC also has the highest pre-tax earnings volatility among peers (excepting only CIBC), measured over a five year period since 2007. NBC maintains a relatively large trading inventory ($44.5 billion) which is required to support a trading business concentrated in fixed income. In addition, NBC is also at the high end of the peer group in terms of concentrations in unsecured and non-real estate secured Canadian consumer loans as a proportion of their Canadian consumer loans, at approximately 20% at 31 October 2012, which will give rise to the highest levels of incremental loan losses in a stress scenario.

Toronto Dominion Bank (TD; Aa1 stable; B/ aa3 stable)

TD has the lowest exposure to the capital markets earnings of the peer group (other than CcD), only medium reliance upon Canadian P&C earnings (50% in full-year 2012) and a low concentration in less well secured consumer loans. However, the increasing proportion of earnings contributed by its less well positioned US subsidiary to the group's overall earnings and risk profile is the overriding driver behind today's rating actions for this bank.

With regard to its US subsidiary, Moody's downgraded the standalone bank financial strength rating/baseline credit assessment of TD Bank, N.A. to C+/a2 from B-/a1. The downgrade reflects the challenges that stem from parent TD's growth ambitions in US commercial and retail banking. To achieve its parent's objectives, TD Bank, N.A. continues to expand its business at an above-average rate, which poses risks for creditors. Moreover, as a frequent acquirer in the US, TD has displayed a willingness to reintroduce integration risk on a periodic basis.

Nonetheless, Moody's acknowledges that TD has been successful in creating a diverse US banking franchise. However, that franchise is less profitable than those of many higher-rated US regional banks and the expenses associated with its continued growth, including ongoing de novo branch expansion, will remain significant going forward.

TD Bank, N.A.'s long-term deposit rating, which continues to benefit from Moody's expectation of support from parent TD, was downgraded to Aa3 from Aa2. However, the A1 issuer rating of TD Bank, N.A.'s immediate parent, TD Bank US Holding Company, was confirmed. This reflects its growing capital base and declining double leverage, trends that the rating agency expects will continue.

The principal methodology used in these ratings was Moody's Consolidated Global Bank Rating Methodology published in June 2012. Please see the Credit Policy page on www.moodys.com for a copy of this methodology.

REGULATORY DISCLOSURES

For ratings issued on a program, series or category/class of debt, this announcement provides certain regulatory disclosures in relation to each rating of a subsequently issued bond or note of the same series or category/class of debt or pursuant to a program for which the ratings are derived exclusively from existing ratings in accordance with Moody's rating practices. For ratings issued on a support provider, this announcement provides certain regulatory disclosures in relation to the rating action on the support provider and in relation to each particular rating action for securities that derive their credit ratings from the support provider's credit rating. For provisional ratings, this announcement provides certain regulatory disclosures in relation to the provisional rating assigned, and in relation to a definitive rating that may be assigned subsequent to the final issuance of the debt, in each case where the transaction structure and terms have not changed prior to the assignment of the definitive rating in a manner that would have affected the rating. For further information please see the ratings tab on the issuer/entity page for the respective issuer on www.moodys.com.

For any affected securities or rated entities receiving direct credit support from the primary entity(ies) of this rating action, and whose ratings may change as a result of this rating action, the associated regulatory disclosures will be those of the guarantor entity. Exceptions to this approach exist for the following disclosures, if applicable to jurisdiction: Ancillary Services, Disclosure to rated entity, Disclosure from rated entity.

The below contact information is provided for information purposes only. Please see the ratings tab of the issuer page at www.moodys.com, for each of the ratings covered, Moody's disclosures on the lead analyst and the Moody's legal entity that has issued the ratings.

Please see www.moodys.com for any updates on changes to the lead rating analyst and to the Moody's legal entity that has issued the rating.

Please see the ratings tab on the issuer/entity page on www.moodys.com for additional regulatory disclosures for each credit rating.

David Beattie
VP - Senior Credit Officer
Financial Institutions Group
Moody's Canada Inc.
70 York Street
Suite 1400
Toronto, ON M5J 1S9
Canada
(416) 214-1635

Robert Franklyn Young
MD - Financial Institutions
Financial Institutions Group
JOURNALISTS: 212-553-0376
SUBSCRIBERS: 212-553-1653

Releasing Office:
Moody's Canada Inc.
70 York Street
Suite 1400
Toronto, ON M5J 1S9
Canada
(416) 214-1635