

Research Update:

Ratings On Macquarie Group And Bank Raised On Strengthening Risk Management; Outlook Stable

December 11, 2019

Overview

- The Macquarie group and bank's risk management capabilities have strengthened over time in the context of a wide and complex range of credit and noncredit risk exposures across various businesses and geographies.
- We are raising our long-term issuer credit rating on MGL to 'BBB+' from 'BBB' and on MBL to 'A+' from 'A'. We are also raising our long-term issuer credit rating on MBL's hybrid debt instruments by one notch reflecting the improvement in the bank's stand-alone credit quality.
- The stable outlook reflects our expectation that our ratings on the Macquarie group and MBL will remain unchanged over the next two years.

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Rating Action

On Dec. 11, 2019, S&P Global Ratings raised its long-term issuer credit ratings on Australia-based Macquarie Group Ltd. (MGL)--the nonoperating holding company of the Macquarie group--and Macquarie Financial Holdings Pty Ltd. (MFHPL), an intermediate nonoperating holding company of the investment banking subgroup, to 'BBB+' from 'BBB'. We affirmed the short-term issuer credit ratings on both MGL and MFHPL at 'A-2'. We also raised our long-term issuer credit rating on Macquarie Bank Ltd. (MBL) to 'A+' from 'A' and affirmed the short-term rating at 'A-1'. At the same time, we raised the long- and short-term issuer credit ratings on Macquarie International Finance Ltd. (MIFL), a highly strategic subsidiary of MBL to 'A/A-1' from 'A-/A-2'. We have also raised our ratings on MBL's hybrid debt instrument ratings by one notch reflecting the improvement in the bank's stand-alone credit profile (SACP). The outlook on the long-term issuer credit ratings on MGL, MFHPL, MBL, and MIFL is stable.

Rationale

The strengthening in the credit profile of Macquarie group and the bank reflects our view that the group's risk management capabilities have improved in the context of a wide and complex range of credit and noncredit risk exposures across various businesses and geographies. The group's

recent streamlining of its operating activities has resulted in some moderation of its complexity, which in our view supports management's ability to oversee and manage associated risks across different business lines. In addition, we are of the view that the Macquarie group has sustained its good risk management outcomes over a period of time and that there are no signs of it increasing its risk appetite.

Our ratings on the Macquarie group entities have the headroom to absorb a modest downturn in the credit cycle.

In our assessment of the Macquarie group's risk management capabilities we take into account:

- The Macquarie group and MBL's performance and risk management outcomes pre and post the global financial crisis. Compared with a peer group of international banks, the volatility of the Macquarie group's earnings has been lower for a sustained period and the group was able to deal with global credit headwinds.
- The Macquarie group's internal reorganization is substantially complete. In our view, the internal reorganization will improve the transparency of the group's business activities. The reorganization will also simplify the group's business activities and lead to divisions being organized along business lines with similar risk profiles and customer needs.
- The reorientation of the Macquarie group and the bank's earnings toward repeatable and sustainable income sources, which will benefit the group and bank's future earnings profile as well as risk management outcomes relative to international peer banks', which are more focused on capital market related activities.
- The significant diversity of the Macquarie group's activities in terms of geography and product.
- The resourcing of the Macquarie group's risk management team, with staff levels having nearly doubled post the global financial crisis.

We view the risk management capability of the Macquarie group as commensurate with the unique, complex nature and the broad range of the group's business activities. In our opinion, the Macquarie group's risk appetite framework is well developed. We understand that the Macquarie group delegates the ownership of risk at the business unit level, and focuses on understanding worst-case outcomes. Also, the risk management team performs an independent review, as needed. In addition, the activities of the Macquarie group are well diversified in terms of geography and products.

The Macquarie group's governance framework is sound, in our view. The final report of the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry was released in February 2019, and no significant adverse conduct issues emerged that affected MBL and the Macquarie group's brand or reputation.

Macquarie Group Ltd. Outlook

Our outlook on MGL is stable reflecting the group's well-diversified business across different asset classes and geographies, stable and repeatable income sources from the group's asset management and banking activities, which strengthens the business profile, a strongly capitalized bank that represents the majority of the group's exposures, and strong risk management capabilities to manage the group's more complex nature of credit, market, and operational risk exposures relative to local and international peers.

Downside scenario

We believe that a downside scenario could emerge over the next two years if contrary to our expectations an unexpected lapse in the Macquarie group's risk management occurred--for example, resulting in a large trading or operational risk loss--or if its credit quality deteriorated sharply. A downside scenario could also emerge if 1) the Macquarie group's risk profile shifted materially toward the lower credit quality nonbank part of the group, or 2) MBL's risk-adjusted capital (RAC) ratio deteriorated to below 10%, or 3) leverage within the nonbank part of the group increased significantly.

Upside scenario

We see very limited upside to our issuer credit rating on MGL in the next two years.

Macquarie Bank Ltd. Outlook

Our outlook on MBL is stable, reflecting our expectation that the bank will maintain solid operating performance, strong capital levels, low credit losses, and good risk management outcomes in the next two years.

Downside scenario

We believe that a downside scenario could emerge over the next two years if contrary to our expectations an unexpected lapse in risk management occurred--for example, resulting in a large trading or operational risk loss--or if its credit quality deteriorated sharply. A downside scenario could also emerge if the bank's RAC ratio deteriorated to below 10%.

Upside scenario

We see very limited upside to our issuer credit rating on MBL in the next two years.

Ratings Score Snapshot

Ratings Score Snapshot--Macquarie Bank Ltd.	To	From
Issuer Credit Rating	A+/Stable/A-1	A/Positive/A-1
SACP	a-	bbb+
Anchor	bbb+	bbb+
Business Position	Adequate (0)	Adequate (0)
Capital and Earnings	Strong (1)	Strong (1)
Risk Position	Adequate (0)	Moderate (-1)
Funding and Liquidity	Average and Adequate (0)	Average and Adequate (0)
Support	2	2
ALAC Support	0	0
GRE Support	0	0

Ratings Score Snapshot--Macquarie Bank Ltd.	To	From
Group Support	0	0
Sovereign Support	2	2
Additional Factors	0	0

Related Criteria

- General Criteria: Group Rating Methodology, July 1, 2019
- General Criteria: Hybrid Capital: Methodology And Assumptions, July 1, 2019
- Criteria | Corporates | General: Corporate Methodology: Ratios And Adjustments, April 1, 2019
- Criteria | Financial Institutions | General: Risk-Adjusted Capital Framework Methodology, July 20, 2017
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- General Criteria: Guarantee Criteria, Oct. 21, 2016
- Criteria | Corporates | General: Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- Criteria | Financial Institutions | General: Key Credit Factors For Asset Managers, Dec. 9, 2014
- Criteria | Corporates | General: The Treatment Of Non-Common Equity Financing In Nonfinancial Corporate Entities, April 29, 2014
- General Criteria: Ratings Above The Sovereign--Corporate And Government Ratings: Methodology And Assumptions, Nov. 19, 2013
- Criteria | Corporates | General: Corporate Methodology, Nov. 19, 2013
- Criteria | Financial Institutions | Banks: Assessing Bank Branch Creditworthiness, Oct. 14, 2013
- Criteria | Financial Institutions | Banks: Quantitative Metrics For Rating Banks Globally: Methodology And Assumptions, July 17, 2013
- Criteria | Financial Institutions | Banks: Banks: Rating Methodology And Assumptions, Nov. 9, 2011
- Criteria | Financial Institutions | Banks: Banking Industry Country Risk Assessment Methodology And Assumptions, Nov. 9, 2011
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009
- Criteria | Financial Institutions | Banks: Commercial Paper I: Banks, March 23, 2004

Ratings List

***** Macquarie Group Ltd. *****

Ratings Affirmed

Macquarie Bank Ltd.

Short-Term Debt	A-1
Commercial Paper	A-1

Macquarie Securities South Africa Ltd.

Senior Unsecured	zaAAA
Short-Term Debt	A-2
Short-Term Debt	zaA-1+

Upgraded

	To	From
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Macquarie Bank Ltd.

Senior Unsecured	A+	A
Subordinated	BBB+	BBB
Subordinated	BBB	BBB-
Junior Subordinated	BB+	BB
Preference Stock	BBB-	BB+
Commercial Paper	A+	A

Macquarie Group Ltd.

Senior Unsecured	BBB+	BBB
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Macquarie Securities South Africa Ltd.

Senior Unsecured	BBB+	BBB
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Upgraded; CreditWatch/Outlook Action

	To	From
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Macquarie International Finance Ltd.

Issuer Credit Rating	A/Stable/A-1	A-/Positive/A-2
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Upgraded; CreditWatch/Outlook Action; Ratings Affirmed

	To	From
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Macquarie Bank Ltd.

Issuer Credit Rating	A+/Stable/A-1	A/Positive/A-1
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Macquarie Group Ltd.

Macquarie Financial Holdings Pty Ltd

Issuer Credit Rating	BBB+/Stable/A-2	BBB/Positive/A-2
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