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**Research Update:**

# Deutsche Bank 'A+/A-1' Ratings Affirmed Following 2008 Loss; Outlook Remains Stable

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## Research Update:

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## Rationale

On Jan. 15, 2009, Standard & Poor's Ratings Services affirmed its 'A+/A-1' counterparty credit ratings on Deutsche Bank AG. The outlook remains stable.

This follows yesterday's announcement that Deutsche Bank suffered a net loss of €4.8 billion in the fourth quarter of 2008. According to the bank, this was mainly attributable to the combination of a substantial deleveraging and reduction in the trading books during a period of extreme volatility, correlation, and basis risk in the capital markets. This had a severe effect on revenues in the global markets activity, particularly in credit trading, equity derivatives, and equity proprietary trading. Outside the global markets business, there were further markdowns on exposures to monoline insurers, injections into money market funds, and a write-down on intangible assets. The net loss also comes despite significant write-backs on cancelled leveraged loan transactions.

The very difficult environment in the fourth quarter was widely known, and some competitors had already reported losses. These exceptionally poor trading conditions were considered an important factor in the recent downgrade of Deutsche Bank on Dec. 19, 2008, along with a number of other major financial institutions. (For more information, see "Deutsche Bank AG Ratings Lowered To 'A+/A-1' On Industry Review; Outlook Stable," published on Dec. 19, 2008, on RatingsDirect.)

Nevertheless, the reported loss was greater than we expected at the time of our downgrade. Although Deutsche Bank has succeeded in meeting its targeted 10% Tier 1 ratio at year end, we believe that the fourth-quarter loss has reduced the quality of capital. According to Standard & Poor's measures, capitalization is likely to have declined from a level we consider adequate. Set against this, however, we understand that Deutsche Bank continued to reduce the risk inherent in its trading activities during the quarter, and exposures to certain risky assets such as leveraged loans have been cut materially. In addition, the restructured acquisition of a stake in Deutsche Postbank AG (A-/Positive/A-2) reduces the future regulatory capital requirement of the transaction by about €1.2 billion.

## Outlook

The outlook remains stable. We believe that the massive deleveraging in late 2008 is unlikely to be repeated and do not expect further losses on this scale. However, the weaker capital position does, in our opinion, leave Deutsche Bank more vulnerable to further potential adverse shocks, for example, more trading losses and a potentially very sharp increase in impairments as economies contract. We consider that a further decline in

capitalization would likely lead to a dilution in Deutsche Bank's stand-alone credit profile, and that this could have repercussions for the confidence-sensitive capital markets business in particular.

Nevertheless, given Deutsche Bank's high systemic importance, we believe government support would be forthcoming, limiting the impact on the counterparty credit rating. For this reason, the outlook remains stable--although a downgrade could occur if we perceive that external support may not be forthcoming. A downgrade could also occur, in particular, if material additional charges from trading, credit, or litigation risks affected capital, or if a material and persistent slowdown in operating revenues were to jeopardize Deutsche Bank's medium-term earnings potential. An upgrade is considered highly unlikely in the current environment.

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