FitchRatings

Banks
Retail & Consumer Banks
Germany

Genossenschaftliche FinanzGruppe

Update

Key Rating Drivers

Leading German Retail and Commercial Group: Genossenschaftliche FinanzGruppe's (GFG) ratings reflect the group's leading and highly diversified business profile, strong risk-adjusted capitalisation and low leverage, sound asset quality, a record of profitability that is considerably better than most German peers, as well as its outstanding funding profile, by international standards. GFG's Viability Rating (VR) is one notch above the implied VR, reflecting the high importance for GFG's ratings of its strong business profile.

Mutual Support Mechanism: GFG is not a legal entity, but a cooperative banking network whose cohesion is ensured by an institutional protection scheme (IPS) managed by the Bundesverband der Deutschen Volksbanken und Raiffeisenbanken e. V. (BVR). GFG's Issuer Default Ratings (IDRs) are group ratings that apply to each member bank, including its central institution DZ BANK AG Deutsche Zentral-Genossenschaftsbank and its subsidiaries.

Diversified Business Model: GFG's domestically focused, stable universal banking business model has delivered stable profits over several economic cycles. It is based on its local banks' strong domestic retail and small SME banking franchise, supported by DZ BANK's product suppliers. These include domestic market leaders in the insurance, asset-management and real-estate businesses. The business model benefits from a strong strategic alignment of DZ BANK and the local banks with intensified cooperation and cross-selling across GFG.

Sound Asset Quality: Fitch Ratings expects GFG's asset quality to have remained resilient in 2023, despite macroeconomic and geopolitical risks. We expect impaired loans to increase modestly in the next two years, to about 2% of gross loans due to higher interest rates and inflation, which are likely to drive rising insolvencies in the group's SME and commercial real estate (CRE) portfolios.

Improved Profitability: We expect profitability to have recovered in 2023, driven by strong net interest income (NII) and low loan impairment charges (LICs). Operating profit had declined significantly in 2022 due to temporary write-downs in the local banks' securities portfolios and DZ BANK's insurance subsidiary, driven by the sharp increase of interest rates during 2022. Historically, GFG's profits have been more stable than the German banking sector's.

Strong Capitalisation: The local banks and DZ BANK are both well-capitalised, and GFG's leverage ratio is high by international standards. We expect GFG's common equity Tier 1 (CET1) ratio to remain close to the current 15% in the medium term, supported by slower loan growth than in previous years.

Very Stable Funding: The local banks are predominantly funded by granular, mostly price-inelastic domestic retail deposits, and their structurally large excess liquidity covers most of DZ BANK's short-term funding needs. DZ BANK, as a frequent issuer of unsecured debt and the largest German covered bond issuer to an established and geographically diversified investor base, provides GFG with reliable access to the wholesale markets.

Ratings

Foreign Currency	
Long-Term IDR	AA-
Short-Term IDR	F1+
Viability Rating	aa-
Government Support Rating	ns
Sovereign Risk	
Long-Term Foreign-Currency IDR	AAA
Long-Term Local-Currency IDR	AAA
Country Ceiling	AAA
Outlooks	
Long-Term Foreign-Currency IDR	Stable
Sovereign Long-Term Foreign-Currency IDR	Stable
Sovereign Long-Term Local-Currency IDR	Stable

Applicable Criteria

Bank Rating Criteria (September 2023)

Related Research

Global Economic Outlook (December 2023)

Western European Banks Outlook 2024 (December 2023)

Fitch Affirms German Cooperative Banks and DZ BANK at 'AA-'; Outlook Stable (April 2023)

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Rating Sensitivities

Factors that Could, Individually or Collectively, Lead to Negative Rating Action/Downgrade

We could downgrade GFG's and its members' ratings if GFG's impaired loan ratio durably rises above 3%, its average operating profit/risk-weighted assets (RWAs) ratio declines below 1%, or its regulatory CET1 ratio falls durably below 13%. A downgrade of our operating environment score for GFG (aa-/stable) would also put pressure on its ratings.

Factors that Could, Individually or Collectively, Lead to Positive Rating Action/Upgrade

An upgrade of GFG's and of its members' ratings is unlikely, given the already high ratings and in light of the increased economic and financial uncertainties. In addition to a domestic environment that would allow higher lending margins, an upgrade would also require greater cost efficiency, which is likely to necessitate a protracted streamlining of the group's structure, especially at the local banks.

Other Debt and Issuer Ratings

	Rating
DZ BANK AG Deutsche Zentral-Genossenschaftsbank[a]	
Long-term deposit rating[a]	AA
Short-term deposit rating[a]	F1+
Long-term senior preferred debt[a, b]	AA
Short-term senior preferred debt[a, b]	F1+
Long-term senior non-preferred debt[a]	AA-
Tier 2 subordinated debt	A
AT1 Notes	BBB+
Deutsche Apotheker- und Aerztebank eG	
Long-term deposit rating	AA-
Short-term deposit rating	F1+
Muenchener Hypothekenbank eG	
Long-term deposit rating	AA
Short-term deposit rating	F1+
Local cooperative banks	
Long-term deposit ratings	AA-
Short-term deposit ratings	F1+

[a] Also applies to DZ BANK's subsidiary DZ HYP AG
[b] Also applies to DZ BANK's subsidiary DZ PRIVATBANK S.A.
Source: Fitch Ratings

The long-term deposit ratings and long-term senior preferred debt ratings of DZ BANK and its banking subsidiaries, DZ BANK's Derivative Counterparty Rating (DCR), and the long-term deposit rating of Muenchener Hypothekenbank are one notch above their respective Long-Term IDRs because of the protection provided by senior non-preferred and more junior debt buffers to preferred creditors. The deposit ratings of Deutsche Apotheker- und Aerztebank and of the local cooperative banks are aligned with GFG's IDRs due to the absence of sustainable significant senior non-preferred and more junior debt buffers at these entities.

A preferred bail-in resolution strategy with a single-point-of-entry approach is applicable for DZ BANK group, which is directly under the authority of the European Single Resolution Board.

Each local bank is regulated individually as a less significant institution. Consequently, the German regulator's preferred resolution strategy for these banks consists of standard insolvency procedures, and the predominantly deposit-funded local banks have no incentive to build up resolution buffers. Deutsche Apotheker- und Aerztebank and Muenchener Hypothekenbank's preferred resolution strategy also consists of standard insolvency procedures, but Muenchener Hypothekenbank has a very large stock of legacy senior non-preferred debt outstanding, which we expect to remain well in excess of 10% of RWAs.

The ratings of the subordinated Tier 2 and additional Tier 1 notes issued by DZ BANK and its subsidiaries are two and four notches, respectively, below GFG's VR. This is the standard notching for this type of instruments under Fitch's criteria. We use the VR as the anchor rating because we believe that GFG, by protecting the viability of DZ BANK and its subsidiaries, increases the likelihood that all due payments on these notes will continue to be met.

Significant Changes from Last Review

GFG Most Likely Returned to Long-Term Profitability Levels in 2023

We expect higher net income for GFG in 2023 than in 2022 and a return to the group's long-term average pretax profit level of about EUR8.7 billion over the past 10 years. This is due to further rising in NII on higher interest rates, a slow repricing of retail deposits and less impact from the fair value result, which is partly offset by cost increase, given the inflationary environment.

Fitch expects GFG's profitability to remain strong and GFG to generate stable profitability in 2024. We believe GFG's net interest margins will benefit from higher new lending margins and rising treasury income due to higher reinvestment yields, which are likely to offset the expected moderate deposit repricing in 2024. Deposit costs have already increased throughout 2023 and Fitch expects them to further rise in 2024 because of changes in the deposit composition, in particular at the primary banks, in favour of higher-interest term deposits.

Strong Contribution from DZ BANK Group

DZ BANK group raised its 2023 financial guidance, expecting a result above EUR2.5 billion after reporting a pretax profit of EUR1.9 billion in 1H23 (1H22: EUR938 million). DZ BANK group is by far GFG's largest member (accounting for almost 40% of GFG's assets at end-2022), which is driving our expectation of GFG's profitability rebound for 2023 income.

Improved profitability was mainly driven by higher NII (up 26% to EUR1.8 billion in 1H23), low loan impairment charges and adequate cost discipline. Moreover, a significantly higher income from its asset management and insurance activities underpinned the group's financial performance. The latter benefitted from the strong investment result at the insurance subsidiary R+V, reversing last year's first half loss of EUR30 million due to the temporary valuation losses in the securities portfolio.

Resilient Asset Quality to Weaken Moderately

Loan defaults in GFG remained benign throughout 2023 both at the level of the primary banks and at DZ BANK group. Fitch expects a moderate increase of impaired loans in 2024, which will push LICs upward given the weak macroeconomic environment, as Fitch expects Germany's GDP to expand by only 0.4% in 2024. Default rates could increase, in particular for vulnerable corporate sectors sensitive to energy prices and for retailers, as consumer spending remains under pressure because of the high inflation.

GFG's exposure to CRE lending, which is mainly concentrated in DZ BANK's subsidiary DZ HYP and in Muenchner Hypothekenbank, leaves it vulnerable to refinancing risk in combination with falling real estate valuations. Fitch expects new impaired loan inflows, particularly in CRE developments, office and retail property portfolios, to materialise in 2H23 and 2024 as construction costs surged, valuations are adjusted downwards and loans come up for refinancing. LICs are likely to be significantly above the historical average in these segments, but they should not lead to outsized losses in the next two years, due to portfolio collateralisation.

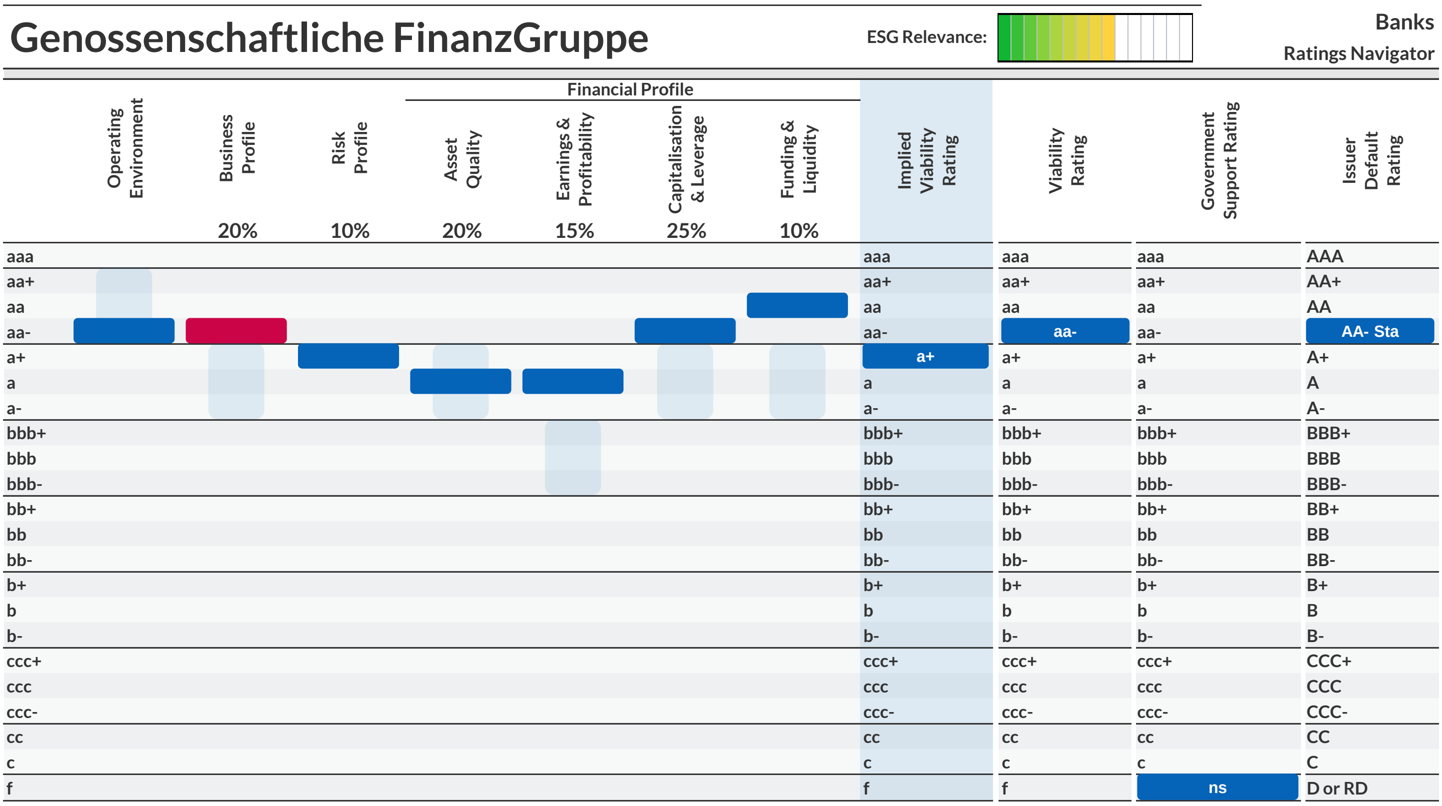
Fair Value Losses in Security Portfolios Decline Significantly

The sizeable fair value loss in the primary banks' bond portfolios following the steep interest rate rises in 2022 was the main driver of GFG's 2022 net profit decline, which we do not expect to recur in 2023, as a further rise in interest rates during 1H23 has mainly been reversed since autumn and the pull-to-par effect will gradually mitigate further losses. We also believe that primary banks will have further lowered their interest rate risk in the banking book since rates began rising in 2022 to lower earnings volatility.

Reform of Institutional Protection Scheme Strengthens Cohesion

Moderate changes to the statute of GFG's IPS were approved by GFG's members in June 2023. The changes aim to increase the scope of IPS's tools such as early information rights and the speed of intervention should it become necessary. The modifications support the alignment of members' risk appetite with their risk bearing capacity and aims to improve members' discipline. This is because the local banks define their risk appetite independently and underwriting decisions are not subject to GFG-wide centralised approvals or limits. However, BVR's monitoring systems were also strengthened. This indirectly influences the banks' risk-taking because their individual contributions to GFG's mutual support fund, BVR-Sicherungseinrichtung (BVR-SE), depend on BVR-SE's assessment of each bank's risk profile.

Ratings Navigator



The Key Rating Driver (KRD) weightings used to determine the implied VR are shown as percentages at the top. In cases where the implied VR is adjusted upwards or downwards to arrive at the VR, the KRD associated with the adjustment reason is highlighted in red. The shaded areas indicate the benchmark-implied scores for each KRD.

VR - Adjustments to Key Rating Drivers

The business profile score of 'aa-' is above the 'a' category implied score for the following adjustment reason: business model (positive).

The earnings and profitability score of 'a' is above the 'bbb' category implied score for the following adjustment reason: earnings stability (positive).

The capitalisation and leverage score of 'aa-' is above the 'a' category implied score for the following adjustment reason: leverage and risk-weight calculation (positive).

The funding and liquidity score of 'aa' is above the 'a' category implied score for the following adjustment reason: deposit structure (positive).

Financials

Financial Statements

	31 Dec 22		31 Dec 21	31 Dec 20	31 Dec 19
	Year end (USDm)	Year end (EURm)	Year end (EURm)	Year end (EURm)	year end (EURm)
Summary income statement					
Net interest and dividend income	21,914	20,546	18,232	18,272	18,185
Net fees and commissions	9,222	8,646	8,675	7,439	7,092
Other operating income	-5,182	-4,858	1,610	1,709	3,665
Total operating income	25,955	24,334	28,517	27,420	28,942
Operating costs	20,350	19,079	18,577	18,036	18,142
Pre-impairment operating profit	5,605	5,255	9,940	9,384	10,800
Loan and other impairment charges	1,454	1,363	-337	2,327	832
Operating profit	4,151	3,892	10,277	7,057	9,968
Other non-operating items (net)	n.a.	n.a.	245	159	211
Tax	1,909	1,790	3,017	2,189	3,133
Net income	2,242	2,102	7,505	5,027	7,046
Other comprehensive income	-5,494	-5,151	133	377	1,055
Fitch comprehensive income	-3,252	-3,049	7,638	5,404	8,101
Summary balance sheet					
Assets					
Gross loans	1,066,532	999,937	944,028	890,576	844,552
Loan loss allowances	10,517	9,860	9,170	9,830	9,119
Net loans	1,056,016	990,077	934,858	880,746	835,433
Interbank	48,100	45,097	15,794	19,651	22,439
Derivatives	20,137	18,880	19,695	29,443	25,232
Other securities and earning assets	401,981	376,881	411,846	399,375	390,104
Total earning assets	1,526,235	1,430,935	1,382,193	1,329,215	1,273,208
Cash and due from banks	125,820	117,964	156,973	120,961	87,421
Other assets	34,350	32,205	27,285	25,715	23,459
Total assets	1,686,405	1,581,104	1,566,451	1,475,891	1,384,088
Liabilities					
Customer deposits	1,101,649	1,032,861	984,926	937,876	880,398
Interbank and other short-term funding	192,434	180,418	207,032	170,802	156,316
Other long-term funding	88,377	82,859	77,280	75,071	46,793
Trading liabilities and derivatives	30,069	28,191	21,932	32,589	54,896
Total funding and derivatives	1,412,529	1,324,329	1,291,170	1,216,338	1,138,403
Other liabilities	137,794	129,190	145,720	137,725	129,525
Preference shares and hybrid capital	249	233	176	246	204
Total equity	135,834	127,352	129,385	121,582	115,956
Total liabilities and equity	1,686,405	1,581,104	1,566,451	1,475,891	1,384,088
Exchange rate		USD1 = EUR0.937559	USD1 = EUR0.884173	USD1 = EUR0.821963	USD1 = EUR0.89015

Source: Fitch Ratings Fitch Solutions, Genossenschaftliche FinanzGruppe

Key Ratios

	31 Dec 22	31 Dec 21	31 Dec 20	31 Dec 19
Ratios (annualised as appropriate)				
Profitability				
Operating profit/risk-weighted assets	0.5	1.4	1.0	1.5
Net interest income/average earning assets	1.5	1.3	1.4	1.5
Non-interest expense/gross revenue	78.7	65.1	65.8	63.2
Net income/average equity	1.6	6.0	4.2	6.3
Asset quality				
Growth in gross loans	5.9	6.0	5.5	6.2
Loan impairment charges/average gross loans	0.1	-0.1	0.3	0.1
Capitalisation				
Common equity Tier 1 ratio	15.1	15.1	15.3	13.6
Tangible common equity/tangible assets	8.0	8.2	8.2	8.2
Basel leverage ratio	7.4	8.0	8.0	7.0
Funding and liquidity				
Gross loans/customer deposits	96.8	95.9	95.0	95.9
Gross loans/customer deposits + covered bonds	92.2	91.2	90.5	91.7
Liquidity coverage ratio	158.5	160.1	177.6	174.3
Customer deposits/total non-equity funding	79.5	77.4	78.9	79.0

Source: Fitch Ratings Fitch Solutions, Genossenschaftliche FinanzGruppe

Support Assessment

Commercial Banks: Government Support	
Typical D-SIB GSR for sovereign's rating level (assuming high propensity)	A+ to A-
Actual jurisdiction D-SIB GSR	ns
Government Support Rating	**ns**
Government ability to support D-SIBs	
Sovereign Rating	AAA/ Stable
Size of banking system	Negative
Structure of banking system	Neutral
Sovereign financial flexibility (for rating level)	Positive
Government propensity to support D-SIBs	
Resolution legislation	Negative
Support stance	Negative
Government propensity to support bank	
Systemic importance	Neutral
Liability structure	Neutral
Ownership	Neutral

The colours indicate the weighting of each KRD in the assessment.
Higher influence Moderate influence Lower influence

GFG's Government Support Rating (GSR) of 'no support' reflects our view that extraordinary sovereign support for EU banks is possible but cannot be relied on because of the Bank Recovery and Resolution Directive and the Single Resolution Mechanism's resolution tools and mechanisms. It is likely that senior creditors will be required to participate in losses, if necessary, instead of, or ahead of, the group receiving sovereign support.

Subsidiaries and Affiliates

DZ BANK's subsidiaries' issuer and debt ratings are sensitive to a change in DZ BANK's issuer or debt ratings.

Environmental, Social and Governance Considerations

FitchRatings **Genossenschaftliche FinanzGruppe**

Banks
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Credit-Relevant ESG Derivation

Genossenschaftliche FinanzGruppe has 5 ESG potential rating drivers

- Genossenschaftliche FinanzGruppe has exposure to compliance risks including fair lending practices, mis-selling, repossession/foreclosure practices, consumer data protection (data security) but this has very low impact on the rating.
- Governance is minimally relevant to the rating and is not currently a driver.

			Overall ESG Scale
key driver	0	issues	5
driver	0	issues	4
potential driver	5	issues	3
not a rating driver	4	issues	2
	5	issues	1

Environmental (E)

General Issues	E Score	Sector-Specific Issues	Reference	E Scale
GHG Emissions & Air Quality	1	n.a.	n.a.	5
Energy Management	1	n.a.	n.a.	4
Water & Wastewater Management	1	n.a.	n.a.	3
Waste & Hazardous Materials Management; Ecological Impacts	1	n.a.	n.a.	2
Exposure to Environmental Impacts	2	Impact of extreme weather events on assets and/or operations and corresponding risk appetite & management; catastrophe risk; credit concentrations	Business Profile (incl. Management & governance); Risk Profile; Asset Quality	1

Social (S)

General Issues	S Score	Sector-Specific Issues	Reference	S Scale
Human Rights, Community Relations, Access & Affordability	2	Services for underbanked and underserved communities: SME and community development programs; financial literacy programs	Business Profile (incl. Management & governance); Risk Profile	5
Customer Welfare - Fair Messaging, Privacy & Data Security	3	Compliance risks including fair lending practices, mis-selling, repossession/foreclosure practices, consumer data protection (data security)	Operating Environment; Business Profile (incl. Management & governance); Risk Profile	4
Labor Relations & Practices	2	Impact of labor negotiations, including board/employee compensation and composition	Business Profile (incl. Management & governance)	3
Employee Wellbeing	1	n.a.	n.a.	2
Exposure to Social Impacts	2	Shift in social or consumer preferences as a result of an institution's social positions, or social and/or political disapproval of core banking practices	Business Profile (incl. Management & governance); Financial Profile	1

Governance (G)

General Issues	G Score	Sector-Specific Issues	Reference	G Scale
Management Strategy	3	Operational implementation of strategy	Business Profile (incl. Management & governance)	5
Governance Structure	3	Board independence and effectiveness; ownership concentration; protection of creditor/stakeholder rights; legal /compliance risks; business continuity; key person risk; related party transactions	Business Profile (incl. Management & governance); Earnings & Profitability; Capitalisation & Leverage	4
Group Structure	3	Organizational structure; appropriateness relative to business model; opacity; intra-group dynamics; ownership	Business Profile (incl. Management & governance)	3
Financial Transparency	3	Quality and frequency of financial reporting and auditing processes	Business Profile (incl. Management & governance)	2
				1

How to Read This Page
ESG scores range from 1 to 5 based on a 15-level color gradation. Red (5) is most relevant and green (1) is least relevant.

The Environmental (E), Social (S) and Governance (G) tables break out the individual components of the scale. The right-hand box shows the aggregate E, S, or G score. General Issues are relevant across all markets with Sector-Specific Issues unique to a particular industry group. Scores are assigned to each sector-specific issue. These scores signify the credit-relevance of the sector-specific issues to the issuing entity's overall credit rating. The Reference box highlights the factor(s) within which the corresponding ESG issues are captured in Fitch's credit analysis.

The Credit-Relevant ESG Derivation table shows the overall ESG score. This score signifies the credit relevance of combined E, S and G issues to the entity's credit rating. The three columns to the left of the overall ESG score summarize the issuing entity's sub-component ESG scores. The box on the far left identifies some of the main ESG issues that are drivers or potential drivers of the issuing entity's credit rating (corresponding with scores of 3, 4 or 5) and provides a brief explanation for the score.

Classification of ESG issues has been developed from Fitch's sector ratings criteria. The General Issues and Sector-Specific Issues draw on the classification standards published by the United Nations Principles for Responsible Investing (PRI) and the Sustainability Accounting Standards Board (SASB).

Sector references in the scale definitions below refer to Sector as displayed in the Sector Details box on page 1 of the navigator.

CREDIT-RELEVANT ESG SCALE

How relevant are E, S and G issues to the overall credit rating?

5	Highly relevant, a key rating driver that has a significant impact on the rating on an individual basis. Equivalent to "higher" relative importance within Navigator.
4	Relevant to rating, not a key rating driver but has an impact on the rating in combination with other factors. Equivalent to "moderate" relative importance within Navigator.
3	Minimally relevant to rating, either very low impact or actively managed in a way that results in no impact on the entity rating. Equivalent to "lower" relative importance within Navigator.
2	Irrelevant to the entity rating but relevant to the sector.
1	Irrelevant to the entity rating and irrelevant to the sector.

The highest level of ESG credit relevance is a score of '3', unless otherwise disclosed in this section. A score of '3' means ESG issues are credit neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. Fitch's ESG Relevance Scores are not inputs in the rating process; they are an observation on the relevance and materiality of ESG factors in the rating decision. For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/topics/esg/products#esg-relevance-scores.

SOLICITATION & PARTICIPATION STATUS

For information on the solicitation status of the ratings included within this report, please refer to the solicitation status shown in the relevant entity's summary page of the Fitch Ratings website.

For information on the participation status in the rating process of an issuer listed in this report, please refer to the most recent rating action commentary for the relevant issuer, available on the Fitch Ratings website.

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