FitchRatings

Banks
Universal Commercial Banks
Germany

Sparkassen-Finanzgruppe Hessen-Thueringen

Update

Key Rating Drivers

Regional retail and commercial banking group Sparkassen-Finanzgruppe Hessen-Thueringen's (SFG-HT) Issuer Default Ratings (IDRs) are underpinned by the strong local retail franchises of the savings banks members of the group, which are complemented by the wholesale activities of Landesbank Hessen-Thueringen Girozentrale (Helaba; A+/Stable), the group's central institution. The ratings also reflect the close integration of SFG-HT's members, and the group's sound asset quality, strong capitalisation and moderate recurring profitability.

Strong Mutual Support: SFG-HT is not a legal entity but a network that comprises 49 savings banks in Hessen and Thuringia, as well as Helaba, and that forms a common economic unit whose cohesion is supported by a mutual support scheme. SFG-HT's IDRs apply to each individual member bank (including Helaba) and are aligned with the group's Viability Rating (VR).

Conservative Risk Profile: SFG-HT's asset quality has been historically sound, including through the pandemic, reflecting prudent underwriting standards, a high share of collateralised lending and a fairly standardised product offering. The savings banks' granularity, long-standing client relationships and their limited complexity also underpin the group's sound risk profile. SFG-HT's large exposure to commercial real estate, mainly through Helaba, leaves it vulnerable to a real-estate crisis. Strong collateralisation based on conservative valuation mitigates risks.

Robust Asset Quality: Fitch Ratings expects SFG-HT's impaired loans ratio will remain below 2% in the medium term. However, we expect SFG-HT's asset quality to modestly deteriorate in 2022 and 2023, due to an expected economic deterioration, rising interest rates and inflationary pressure.

Profitability Under Pressure: We expect that SFG-HT will continue to generate a moderate operating profit of 0.8%–1% of its risk-weighted assets (RWA) on a sustained basis. In the coming quarters the ratio could temporarily fall below that level as a challenging domestic operating environment, due to a Russian gas cut-off, would weaken loan demand and lead to higher loan impairment charges. In addition, write-downs in the savings banks' securities portfolios, driven by rising interest rates are likely to significantly lower SFG-HT's 2022 profit.

Well Capitalised: SFG-HT's capitalisation is a rating strength and we expect its common equity Tier 1 (CET1) capital ratio to remain above 16% in the medium term.

Strong Funding and Liquidity: The savings banks' large and granular retail deposit base underpins the group's strong funding and liquidity profile. The 'F1+' Short-Term IDR is the higher of two options mapping to the 'A+' Long-Term IDR and reflects the group's 'aa-' score for funding and liquidity. Helaba diversifies the group's funding profile by providing access to the international unsecured and secured funding markets.

Ratings

Foreign Currency	
Long-Term IDR	A+
Short-Term IDR	F1+
Viability Rating	a+
Government Support Rating	ns
Sovereign Risk (Germany)	
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 2022)

Related Research

Fitch Affirms Sparkassen-Finanzgruppe Hessen-Thueringen at 'A+'; Outlook Stable (June 2022)

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Rating Sensitivities

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

SFG-HT's, the savings banks' and Helaba's ratings are sensitive to changes in the group's VR. We could downgrade the VR if we expect the group's operating profit/RWA ratio to durably fall below 0.5% and its impaired loans ratio to durably exceed 3%. This could result from large single losses in Helaba's concentrated loan portfolio, notably in its large commercial real estate exposure. SFG-HT's Short-Term IDR is sensitive to changes in the Long-Term IDR and to a revision of the funding and liquidity score to below 'aa-'.

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

An upgrade of the VR would require materially improved earnings and cost efficiency sustainably lifting the group's operating profit/RWA ratio above 1.5%, while maintaining a low impaired loans ratio and strong capitalisation.

Other Debt and Issuer Ratings

Debt Rating Classes

Rating level	Helaba	Savings banks
Deposit ratings	AA-/F1+	A+/F1+
Senior preferred – long-term	AA-	-
Senior non-preferred	A+	-
Guaranteed debt	AAA	-
Tier 2 debt	A-	-

Source: Fitch Ratings

Deposit Ratings and Helaba's Derivative Counterparty Rating and Senior Debt Ratings

Helaba's Deposit Counterparty Rating, deposit ratings and preferred debt ratings are one notch above the bank's Long-Term IDR because of the protection provided by Helaba's sustainable resolution buffers to these preferred creditors. Helaba forms a resolution group that does not include SFG-HT's savings banks (except for Frankfurter Sparkasse, of which Helaba owns 100%). Helaba is subject to minimum requirements for own funds and eligible liabilities, and we expect that the bank's junior and senior non-preferred debt buffer will continue to sustainably exceed 10% of its RWA. Helaba's senior unsecured and senior non-preferred debt ratings are aligned with its IDRs for the same reason.

The deposit ratings of SFG-HT's savings banks are in line with their IDRs because each savings bank's junior and senior non-preferred debt buffers, when available, are insufficient to warrant a rating uplift. We do not expect the savings banks to build up significant buffers because SFG-HT is not regulated as a single resolution group. This means that, in a highly unlikely scenario where the mutual support mechanism would fail to protect its members' viability, the preferred resolution strategy for each savings bank would be insolvency procedures.

Helaba's State-Guaranteed Senior Unsecured and Subordinated Notes

The 'AAA' on Helaba's guaranteed senior unsecured and subordinated Tier 2 debt are based on Fitch Ratings' view of the State of Hesse and the Free State of Thuringia's extremely high ability and propensity to honour their grandfathered statutory guarantor's liability (Gewaehrtraegerhaftung). Fitch believes that the senior and subordinated instruments are similarly protected because the guarantee does not differentiate between seniorities. In our view, the regulatory and EU state aid frameworks do not constrain support for grandfathered debt.

Helaba's Non-Guaranteed Subordinated Debt

Helaba's subordinated Tier 2 notes that do not benefit from the state guarantee are notched down twice from SFG-HT's VR to reflect Fitch's baseline notching for loss severity and the assumption that extraordinary support from SFG-HT would be forthcoming to support these junior instruments, if needed, even though junior instruments are not formally covered by the group's mutual support scheme.

Significant Changes from Last Review

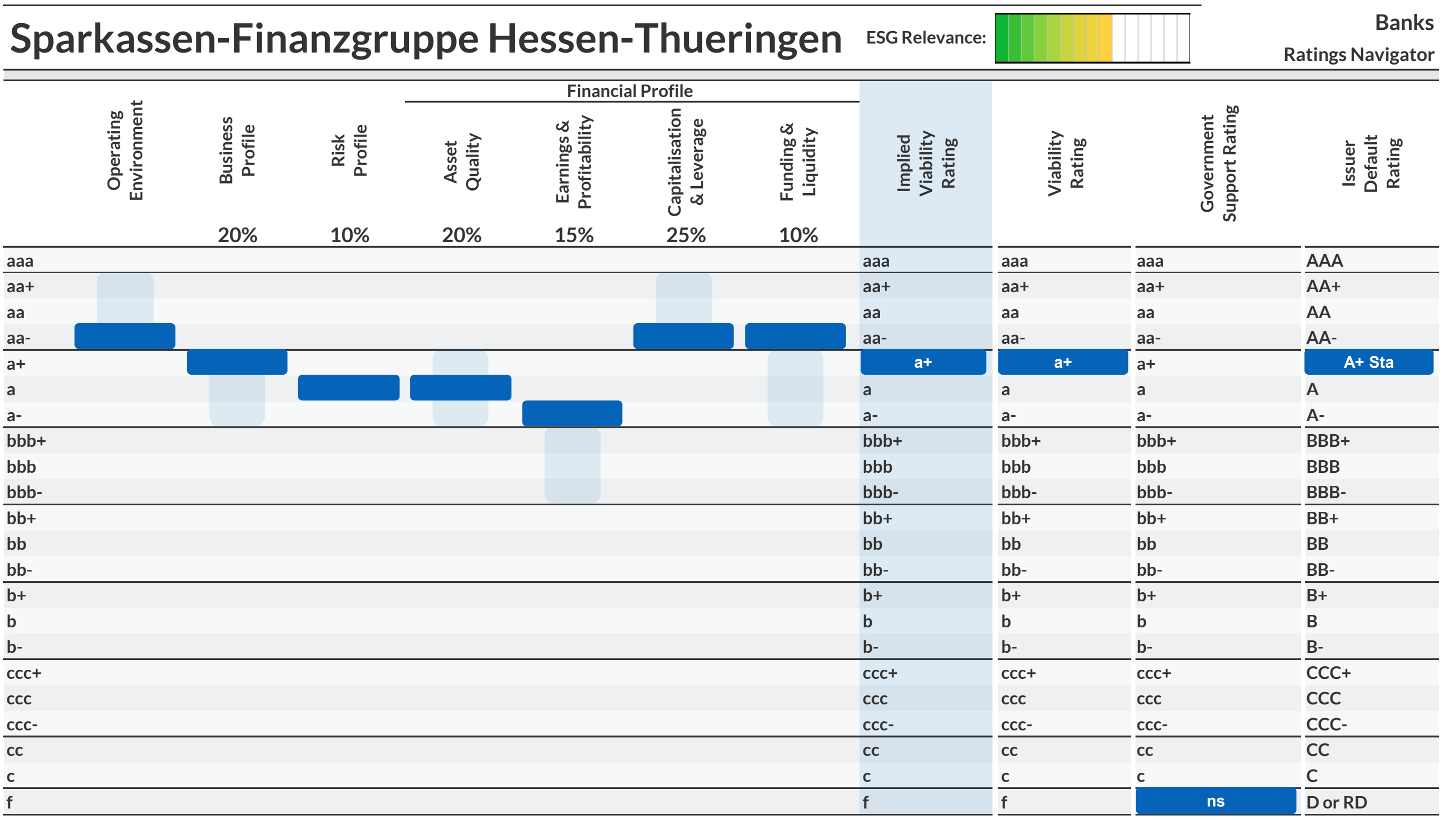
Resilient Pre-Impairment Profit; Elevated Impairment Charges on Securities Portfolio

In 1H22 SFG-HT's pre-impairment profit was broadly stable, supported by a resilient performance at Helaba and the savings banks. Helaba's pre-tax income increased by 12% (yoy), due to a good operating performance based on profitable new business, despite rising interest rates causing lower valuation gains on fair-value instruments. Helaba continued to strengthen its stock of loan loss allowances, the reported loan impairment charges of EUR85 million in 1H22 (1H21: EUR141 million) were mainly driven by post-model-adjustments, referring to performing Stage 2 loans rather than actual defaults. Helaba's asset quality remained strong, reflected in a reported impaired loans ratio of 0.7% at end-1H22. Helaba expects to report a 2022 pre-tax profit of above EUR500 million (2021: EUR569 million), which appears reasonable despite the expected challenges triggered by a Russian gas cut-off, which is likely to have a more severe impact on 2023 results.

The savings banks reported stable 1H22 pre-impairment profits, based on their solid regional business model and sound new business, while significant write-downs in the securities portfolios (not further quantified), driven by rising interest rates rather than credit spread widening, weigh on the group's operating profit. New business remained strong in 1H22, reflected in loan growth of 3% (yoy) driven by all segments. While retail mortgage business dominated the new lending in recent years, in 1H22 SME lending likewise had a strong growth rate of 3.3%. Fitch expects that a large part of new business was driven by clients hedging and securing low rates in a rising rate environment, likely leading to lower activity in 2H22.

We expect SFG-HT's capital ratios to remain strong. Helaba's CET1-ratio was stable at 13.9% at end-1H22, providing a reasonable buffer over requirements. Fitch believes that the savings banks' capital ratios are likely to decline due to further RWA increases, driven by loan growth, which is unlikely to be offset by profit retention. However, the savings banks have some flexibility to manage their capital ratios, as the banks have built up Art.340f reserves in recent years, which could be released to support regulatory capital ratios.

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 earnings & profitability score of 'a-' has been assigned above the category implied score of 'bbb' due to the following adjustment reason: risk-weight calculation (positive).

The funding & liquidity score of 'aa-' has been assigned above the category implied score of 'a' due to the following adjustment reason: deposit structure (positive).

Financials

Financial Statements

	31 Dec 21		31 Dec 20	31 Dec 19	31 Dec 18
	(USDm)	(EURm)	(EURm)	(EURm)	(EURm)
Summary income statement					
Net interest and dividend income	3,359	2,970	2,895	2,935	2,954
Net fees and commissions	1,453	1,285	1,177	1,114	1,029
Other operating income	918	812	294	782	229
Total operating income	5,731	5,067	4,366	4,831	4,212
Operating costs	3,727	3,295	3,339	3,302	3,258
Pre-impairment operating profit	2,004	1,772	1,027	1,529	954
Loan and other impairment charges	414	366	400	188	-4
Operating profit	1,590	1,406	627	1,341	958
Other non-operating items (net)	5	4	97	130	0
Tax	308	272	169	323	306
Net income	1,287	1,138	555	1,148	652
Summary balance sheet					
Assets					
Gross loans	215,444	190,490	187,006	183,935	162,203
- Of which impaired	2,601	2,300	2,000	1,653	1,900
Loan loss allowances	1,490	1,317	1,124	824	803
Net loans	213,955	189,173	185,882	183,111	161,400
Interbank	15,675	13,859	17,053	15,558	9,929
Derivatives	18,232	16,120	23,467	19,417	11,738
Other securities and earning assets	69,082	61,080	64,292	66,303	60,670
Total earning assets	316,942	280,232	290,694	284,389	243,737
Cash and due from banks	53,527	47,327	37,307	20,051	11,683
Other assets	5,005	4,425	4,232	4,525	3,356
Total assets	375,474	331,984	332,233	308,965	258,776
Liabilities					
Customer deposits	189,544	167,590	163,859	152,595	134,405
Interbank and other short-term funding	79,400	70,203	63,880	51,052	36,609
Other long-term funding	51,299	45,357	49,012	49,914	46,066
Trading liabilities and derivatives	22,433	19,835	26,342	26,959	14,956
Total funding and derivatives	342,676	302,985	303,093	280,520	232,036
Other liabilities	5,084	4,495	5,016	4,878	4,210
Preference shares and hybrid capital	28	25	543	591	543
Total equity	27,686	24,479	23,581	22,976	21,987
Total liabilities and equity	375,474	331,984	332,233	308,965	258,776
Exchange rate		USD1 = EUR0.884173	USD1 = EUR0.821963	USD1 = EUR0.89015	USD1 = EUR0.873057

Source: Fitch Ratings, Fitch Solutions, SFG-HT

Key Ratios

	31 Dec 21	31 Dec 20	31 Dec 19	31 Dec 18
Ratios (annualised as appropriate)				
Profitability				
Operating profit/risk-weighted assets	1.0	0.5	1.1	0.9
Net interest income/average earning assets	1.0	1.0	1.1	1.2
Non-interest expense/gross revenue	65.8	76.9	68.9	77.9
Net income/average equity	4.7	2.4	5.1	3.0
Asset quality				
Impaired loans ratio	1.2	1.1	0.9	1.2
Growth in gross loans	1.9	1.7	13.4	4.3
Loan loss allowances/impaired loans	57.3	56.2	49.9	42.3
Loan impairment charges/average gross loans	0.2	0.2	0.1	0.0
Capitalisation				
Common equity Tier 1 ratio	17.8	18.6	18.6	19.3
Tangible common equity/tangible assets	7.1	6.9	7.2	8.5
Total Capital Ratio	20.4	21.4	21.6	22.6
Funding and liquidity				
Gross loans/customer deposits	113.7	114.1	120.5	120.7
Liquidity coverage ratio	176.8	194.3	204.0	n.a.
Customer deposits/total non-equity funding	58.3	58.1	58.2	60.4
Net stable funding ratio	120.1	n.a.	n.a.	n.a.

Source: Fitch Ratings, Fitch Solutions, SFG-HT

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

The Government Support Rating of 'ns' reflects Fitch's view that senior creditors of the bank cannot rely on full extraordinary support from the sovereign if the bank becomes non-viable, due to the EU's Bank Recovery and Resolution Directive.

Environmental, Social and Governance Considerations

FitchRatings **Sparkassen-Finanzgruppe Hessen-Thueringen** Banks Ratings Navigator

Credit-Relevant ESG Derivation

Sparkassen-Finanzgruppe Hessen-Thueringen has 5 ESG potential rating drivers

- Sparkassen-Finanzgruppe Hessen-Thueringen 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
not a rating driver	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.

Unless otherwise disclosed in this section, the highest level of ESG credit relevance is a score of '3'. This 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. For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg.

The ratings for Sparkasse Vogelsbergkreis were unsolicited and have been provided by Fitch as a service to investors. All other entities' ratings were solicited and assigned or maintained at the request of the rated entity/issuer or a related third party.