Sparkassen-Finanzgruppe Hessen-Thueringen

Ratings

Foreign Currency	
Long-Term IDR	A+
Short-Term IDR	F1+
Viability Rating	a+
Support Rating	5
Support Rating Floor	NF
Derivative Counterparty Rating	AA- (dcr)
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 (February 2020)

Related Research

Fitch Revises Outlook on Sparkassen-Finanzgruppe Hessen Thueringen to Stable; Affirms at 'A+' (June 2021)

Global Economic Outlook (June 2021)

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Key Rating Drivers

Mutual Support Drives Group Ratings: Sparkassen-Finanzgruppe Hessen-Thueringen's (SFG-HT) ratings are based on a mutual support scheme shared by SFG-HT's 49 savings banks and their central institution Landesbank Hessen-Thueringen Girozentrale (Helaba). These members form an economic unit whose cohesion is ensured by a common business and risk strategy.

SFG-HT's Issuer Default Ratings (IDRs) apply to each member bank, but the Viability Rating (VR) applies only to SFG-HT, not to the individual member banks, based on Annex 4 of Fitch's Bank Rating Criteria, which applies to banking structures backed by mutual support schemes.

Outlook Revision: The Outlook revision on SFG-HT's Long-Term IDR to stable from negative in July 2021 reflects our expectation that SFG-HT's financial profile will remain commensurate with its VR of 'a+', driven by its strong capitalisation, funding and liquidity, despite weaker profitability. Consequently, we have revised to stable from negative our outlooks on the group's asset quality ('a') and earnings (lowered to 'bbb+' from 'a-').

Well Capitalised: SFG-HT's capitalisation is much stronger than the German sector average. We believe SFG-HT's common equity Tier 1 (CET1) ratio remained stable in 2020 (18.6% at end-2019), as profit retention is likely to offset risk-weighted assets (RWAs) inflation from strong loan growth.

Robust Asset Quality: We believe SFG-HT's non-performing loans (NPLs) ratio remained stable at end-2020 and will rise moderately this year (driven by the constrained ability of weak corporates/SMEs to recover after the pandemic) but to remain within the 1%-2% range by end-2022, well below the European average.

Lower Profitability: SFG-HT's profitability weakened in 2020, mainly driven by Helaba's below-average performance which suffered from strongly increased loan impairment charges (LICs) including a substantial Covid-19 related management buffer. Helaba's wholesale activities are unlikely to deliver sufficiently robust margins to enhance the savings banks' robust financial performance. Consequently SFG-HT's earnings potential is structurally weaker than that of Sparkassen-Finanzgruppe (SFG, A+/Stable), the nationwide savings banks group.

Strong Funding and Liquidity: The savings banks' large, stable and growing retail deposit base underpins SFG-HT's funding and liquidity profile. Helaba has a strategy of matched-funding new business, and its wholesale funding benefits from its established international investor base.

Rating Sensitivities

Weak Financial Performance: We could downgrade SFG-HT's ratings if intensifying economic disruptions reduce the chances of a swift recovery in 2021 and 2022. In this scenario, SFG-HT's profitability would come under pressure from elevated credit losses and weaker revenues.

Upgrade Unlikely: An upgrade of SFG-HT's ratings is unlikely in light of the lasting adverse interest-rate environment and margin pressure in the German banking sector. An upgrade would also require greater cost efficiency and a durable decline in LICs to lift the group's operating profit/RWAs ratio sustainably above 1.5%.

Debt Rating Classes

Debt level	Helaba	Individual savings banks
Deposit ratings	AA-/F1+	A+/F1+
Senior preferred (SP) debt	AA-	
Senior non-preferred (SNP) debt	A+	
Guaranteed senior and subordinated debt	AAA	
Tier 2 subordinated debt	A-	

Source: Fitch Ratings

Helaba's Derivative Counterparty Rating and its long-term SP debt and deposit ratings are one notch above its Long-Term IDR to reflect the protection of preferred creditors by the bank's large resolution buffers. Helaba's SNP debt rating is aligned with its Long-Term IDR.

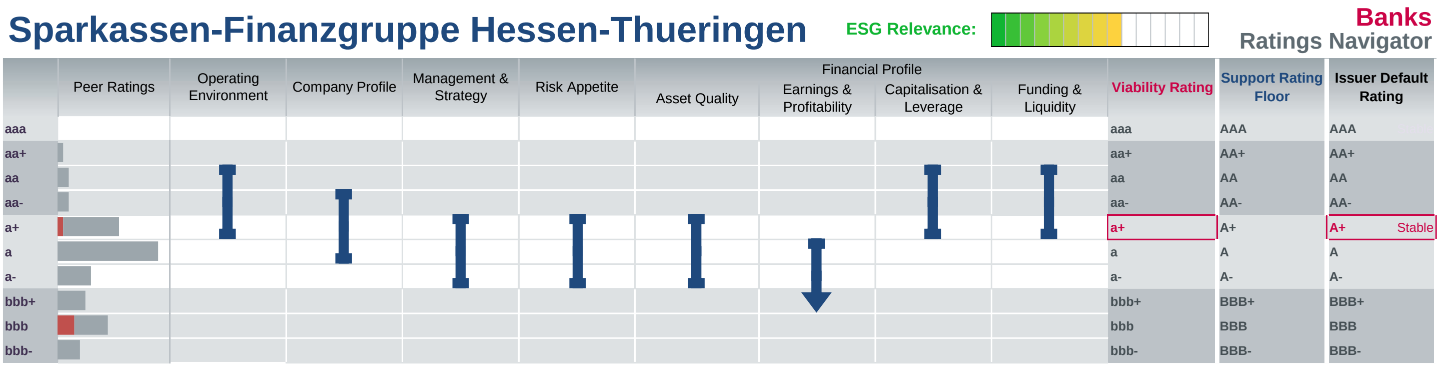
The 'AAA' of Helaba's guaranteed senior unsecured and subordinated Tier 2 debt reflect the extremely high ability and propensity of the states of Hesse and Thuringia to honour their grandfathered statutory guarantees. We believe the guarantees similarly protect senior and subordinated debt because the statutory guarantor's liability (Gewaehrtraegerhaftung) does not differentiate between the seniority of debt classes. In our view, regulatory and EU state aid frameworks do not constrain the level of support for grandfathered debt.

Helaba's non-guaranteed subordinated Tier 2 notes 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.

The savings banks' long-term deposit ratings are one notch below those of Helaba to reflect their lower protection in a resolution scenario. We believe savings banks' depositors are less likely than Helaba's depositors to benefit from the protection of Helaba's large layer of SNP and subordinated debt if SFG-HT fails. The authorities favour a single-point-of-entry resolution strategy with a bail-in for Helaba-Group. As long as SFG-HT is not recognised as a regulatory resolution group including the savings banks, the likeliest resolution approach for savings banks will remain standard insolvency procedures. As a result, savings banks' depositors would not benefit from a bail-in of Helaba's junior and SNP buffers.

SFG-HT and the savings banks' Short-Term IDR of 'F1+' is the higher of two options mapping to their Long-Term IDRs of 'A+'. This reflects the savings banks' large retail deposit base and leading collective market share in the regional retail deposit market, which underpins SFG-HT's strong funding and liquidity profile and drives the group's 'aa-' score for funding & liquidity.

Ratings Navigator



Significant Changes

Risk from Pandemic has Subsided

SFG-HT regional business model proved resilient in 2020. This was despite a substantial decline in GDP and repeated (partial) lockdowns in both regional states and the group's broader operating area as the pandemic failed to subside.

Large state programmes to support companies and households affected by the pandemic have averted material negative spill-over effects into the German banking sector. Government payments compensated for a sharp deterioration in cash flows in the most affected corporate sectors and contained credit losses. In addition, regulatory forbearance for the classification of loan payment holidays and NPLs have strongly mitigated German banks' negative rating migration, RWAs inflation, and provisioning needs since 2Q20.

The extensive use of furlough schemes since 2Q20 has protected household income and contained the rise in the unemployment rate to 4.2% at end-2020. This has strongly supported borrowers' ability to service their loans. The use of loan moratoriums has been much lower than in most European countries since the start of the crisis. Consequently consumer spending declined less in Germany than in other European economies in 2020, and contracted by 6.1% in 2020, compared with 11% in the UK and 8% on average in the Eurozone.

The government also suspended the legal obligation for companies that qualify for state support to file for bankruptcy until end-April 2021. This has kept the number of corporate insolvencies very low until end-1Q21, and we expect them to peak between 2H21 and 1H22. Fitch's June 2021 Global Economic Outlook forecasts the German GDP to grow by 4.2% both this year and in 2022. Although we expect the positive effect of these measures to gradually diminish and the full effect of the pandemic to affect banks' credit profiles in 2021 and 2022, we believe that SFG-HT can sustain this pressure as the economic recovery gathers pace.

We have consequently revised to stable from negative the outlooks on the group's asset quality ('a') and earnings & profitability (lowered to bbb+). We expect the VR of 'a+' to show sufficient resilience to plausible downside scenarios. We also believe that SFG-HT will be able to navigate through the pandemic without materially revising its strategy.

Operating Environment Score for German Banks Stabilised

The outlook revision reflects our view that the economic fall-out from the coronavirus crisis no longer represents a near-term risk to the operating environment, which was our base case when we downgraded the score to ‘aa-’/Negative from ‘aa’/Stable as part of the Covid-19-driven banking sector review in March 2020.

The German banking sector’s high fragmentation, intense competition, as well as vulnerable business models including limited foreign diversification and untested strategic orientations at most large banks, have kept the sector’s profits remarkably low. This is despite years of strong economic environment before the pandemic. We expect this unfavourable market structure to persist after the pandemic, ruling out a higher score within the ‘aa’ range.

Bar Chart Legend

Vertical bars – VR range of Rating Factor

Bar Colors – Influence on final VR

- Higher influence
- Moderate influence
- Lower influence

Bar Arrows – Rating Factor Outlook

⇧	Positive	⇩	Negative
⇳	Evolving	▫	Stable

Sovereign / Institutional Support Assessment

SFG-HT's Support Rating and Support Rating Floor reflect our view that, due to the EU's resolution framework, senior creditors cannot rely on full extraordinary state support.

Support Factors	Positive	Neutral	Negative
Sovereign ability to support system			
Size of banking system relative to economy			✓
Size of potential problem	✓		
Structure of banking system		✓	
Liability structure of banking system		✓	
Sovereign financial flexibility (for rating level)	✓		
Sovereign propensity to support system			
Resolution legislation with senior debt bail-in			✓
Track record of banking sector support		✓	
Government statements of support			✓
Sovereign propensity to support bank			
Systemic importance		✓	
Liability structure of bank		✓	
Ownership		✓	
Specifics of bank failure		✓	

Summary Financials and Key Ratios

	31 Dec 19 (EURm)	31 Dec 18 (EURm)	31 Dec 17 (EURm)	31 Dec 16 (EURm)
Summary income statement				
Net interest and dividend income	2,935	2,954	3,001	3,172
Net fees and commissions	1,114	1,029	1,025	968
Other operating income	782	229	926	1,099
Total operating income	4,831	4,212	4,952	5,239
Operating costs	3,302	3,258	3,601	3,544
Pre-impairment operating profit	1,529	954	1,351	1,695
Loan and other impairment charges	188	-4	-100	97
Operating profit	1,341	958	1,451	1,598
Other non-operating items (net)	130	0	-10	-2
Tax	323	306	439	446
Net income	1,148	652	1,002	1,150
Summary balance sheet				
Gross loans	183,616	162,203	155,474	156,472
- Of which impaired	1,653	1,900	2,200	2,800
Loan loss allowances	824	803	922	1,365
Net loans	182,792	161,400	154,552	155,107
Interbank	15,558	9,929	9,603	13,876
Derivatives	19,417	11,738	12,341	16,440
Other securities and earning assets	66,637	60,670	58,737	62,415
Total earning assets	284,404	243,737	235,233	247,838
Cash and due from banks	20,051	11,683	13,293	5,412
Other assets	4,520	3,356	3,323	3,378
Total assets	**308,975**	**258,776**	**251,849**	**256,628**
Customer deposits	152,816	134,405	128,825	123,954
Interbank and other short-term funding	51,052	36,609	32,470	32,185
Other long-term funding	49,914	46,066	48,883	51,549
Trading liabilities and derivatives	26,959	14,956	14,488	22,407
Total funding	280,741	232,036	224,666	230,095
Other liabilities	4,657	4,210	4,292	4,418
Preference shares and hybrid capital	591	543	916	977
Total equity	22,986	21,987	21,975	21,138
Total liabilities and equity	**308,975**	**258,776**	**251,849**	**256,628**
Ratios (annualised as appropriate)				
Profitability				
Operating profit/risk-weighted assets	1.1	0.9	1.4	1.5
Net interest income/average earning assets	1.1	1.2	1.2	1.3
Non-interest expense/gross revenue	68.9	77.9	74.4	68.3
Net income/average equity	5.1	3.0	4.7	5.6

Source: Fitch Ratings, Fitch Solutions, SFG-HT

Summary Financials and Key Ratios (Cont.)

	31 Dec 19 (EURm)	31 Dec 18 (EURm)	31 Dec 17 (EURm)	31 Dec 16 (EURm)
Asset quality				
Impaired loans ratio	0.9	1.2	1.4	1.8
Growth in gross loans	13.2	4.3	-0.6	1.5
Loan loss allowances/impaired loans	49.9	42.3	41.9	48.8
Loan impairment charges/average gross loans	0.1	0.0	-0.1	0.1
Capitalisation				
Common equity tier 1 ratio	18.6	19.3	20.6	19.6
Total capital ratio	21.6	22.6	24.1	23.6
Tangible common equity/tangible assets	7.2	8.5	8.7	8.2
Net impaired loans/ equity	3.6	5.0	5.8	6.8
Funding and liquidity				
Loans/customer deposits	120.2	120.7	120.7	126.2
Liquidity coverage ratio	204	139	n.a.	n.a.
Customer deposits/funding	58.3	60.4	59.8	57.3

Source: Fitch Ratings, Fitch Solutions, SFG-HT

Brief Company Summary

Regional German Banking Group with Retail and Commercial Franchise

SFG-HT is not a legal entity but a group of regional German savings banks with a large branch network interlinked with Helaba as their central institution. It comprises 33 savings banks in Hesse (EUR117 billion total assets at end-2020), 16 in Thuringia (EUR29 billion) and Helaba, which consolidates a building society and an insurer. We rated a further 318 savings banks outside Hesse/Thuringia separately as part of SFG at end-June 2021.

The savings banks are owned and controlled by their respective municipalities and operate within a local area delimited by law. This ensures performance-enhancing knowledge of their local environment and high client loyalty within their local communities, where the banks are socially engaged. Helaba, by a wide margin SFG-HT's largest member, is the central institution and prime cooperation partner for the savings banks in Hesse and Thuringia, as well as those in North Rhine-Westphalia and Brandenburg, although the latter are not members of SFG-HT.

Tighter Cohesion Positively Differentiates SFG-HT from SFG

SFG-HT's members are part of SFG's nationwide network of interlinked regional mutual support schemes, which is designed as an institutional protection scheme and recognised as such by the regulators. In addition, SFG-HT has its own regional reserve fund to emphasise its members' solidarity. The fund's volume was EUR514 million at end-2020 (EUR509 million at end-2019) with a target to reach 0.5% of the affiliated institutions' total risk exposure amount.

Loan Growth Despite Pandemic

In 2020 SFG-HT experienced strong overnight deposits inflows, due to its clients' high savings rate during the pandemic. Traditional loan growth moderated, but the group played an important role in passing on to corporates EUR850 million of state-guaranteed pandemic loans and grants from KfW, Germany's government-owned development bank, and WI Bank, Hesse's regional development bank. The group (mainly Helaba) has made use of the ECB's TLTRO III facility, which inflated SFG-HT's balance sheet by 7.5% in 2020 (total assets of EUR 332 billion at end-2020).

Key Financial Metrics – Latest Developments

Asset Quality Risks Set to Subside in the Medium Term

In 2020, SFG-HT's asset quality was more resilient than our initial expectations. Its NPL ratio stabilised at a very low level compared with the European peer average. Despite concentration risk, larger single exposures and a large (largely collateralised) commercial real estate portfolio, Helaba contributed positively to SFG-HT's loan quality. Helaba's Stage 3/gross loans ratio rose only from 0.4% to 0.6% in 2020 and remained below SFG-HT's level owing to the bank's conservative risk appetite and focus on public sector and real estate lending, which both still perform well. However, we perceive the group's large property portfolio as a key source of risk.

SFG-HT's LICs, including a management adjustment of EUR123 million at Helaba, suggest that more risks could crystallise this year, when support measures are phased out. We expect a further moderate increase in SFG-HT's NPLs, primarily in the corporate/SME segment as weaker borrowers' ability to recover after the pandemic will be constrained. However, we have stabilised our outlook on SFG-HT's asset quality as we expect the group's NPL ratio to be contained within the 1%-2% range, well below the European average.

Fair Value Swings and LICs Weigh on 2020 Pre-Tax Profit

Stable operating revenues from strong regional market positions support SFG-HT's core profitability. However, Helaba's below average performance will likely drag the group's operating profit/RWAs ratio towards the lower end of the range commensurate with an earnings & profitability score in the 'bbb' category. Helaba incurred market-volatility driven, negative fair value swing and strongly increased LICs, including a substantial management buffer, through the pandemic last year. The savings banks' performance was much more resilient despite increased LICs.

We have lowered SFG-HT's earnings & profitability score to 'bbb+' as we believe 2021 will be another challenging year before further cost discipline and a smaller need for LICs stabilise profitability at a level more commensurate with the 'bbb+' range.

Earnings Retention Stabilise Capitalisation

Because it is not regulated as a group, SFG-HT is not subject to the Supervisory Review and Evaluation Process (SREP), Minimum Requirements for own funds and Eligible Liabilities or resolution planning at group level, neither does it manage its capital centrally. Each savings bank has its own SREP requirement, which ignore the mutual support benefits. Capitalisation varies by bank, but the group's risk monitoring function tightly oversees their solvency levels.

SFG-HT voluntarily discloses a pro-forma CET1 ratio of 18.6%, stable yoy and well above most German and European peers. Capital predominantly consists of retained earnings owing to the savings banks' strong profit retention discipline. In addition, the group could convert into CET1 capital at its own discretion undisclosed German GAAP reserves built up from profit retention.

Helaba's CET1 ratio moderately improved to 14.7% at end-2020 despite the pandemic (14.2% at end-2019), broadly in line with the EBA's average. This provides a comfortable buffer over regulatory requirements, but moderately dilute SFG-HT's CET1 ratio.

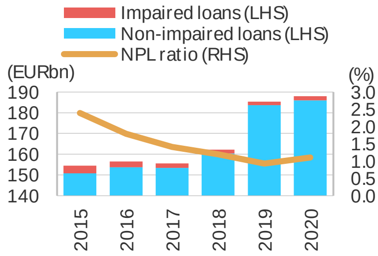
Lower Need for Debt Issuance due to Strong Deposit Inflows

The strong increase in households' savings rate in Germany during the pandemic boosted SFG-HT's customer deposits by 8% in 2020. In line with SFG, SFG-HT's savings bank typically fund their complete loan books with deposits. Helaba's sizeable unsecured debt and covered bond funding franchise inflates SFG-HT's loan-to-deposit ratio, but it also enhances SFG-HT's funding & liquidity profile by adding major diversification (especially compared with the predominantly deposit-funded SFG). Helaba pursues a strategy of matched funding of new business, and its wholesale funding benefits from an established investor base and wholesale market access.

SFG-HT's liquidity benefits from Helaba's large central-bank eligible securities portfolio of EUR34 billion. Helaba could also significantly increase covered bond issuance to generate liquidity if needed.

NPL Development[a]

2014-2018



[a] NPL includes 90 days overdue; 2020 expected
Source: Fitch Ratings, SFG-HT

Environmental, Social and Governance Considerations

The highest level of ESG credit relevance for SFG-HT is a score of '3' in line with most German banks. SFG-HT's governance structure is not a rating driver and is not constrained by SFG's score of '4' for group structure, even though SFG-HT's savings banks are also part of the nationwide savings banks' organisation. This is because SFG-HT statutorily operates as one economic unit, which is a key pillar of its corporate culture. This commitment makes its decision-making processes more effective and fosters a materially stronger cohesion than within SFG. The score of '3' means ESG issues are credit-neutral or have only a minimal credit impact on SFG-HT, either due to their nature or to the way in which they are being managed. For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg.

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
	5	issues	1

Environmental (E)

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

E Scale: 5, 4, 3, 2, 1

Social (S)

General Issues	S Score	Sector-Specific Issues	Reference
Human Rights, Community Relations, Access & Affordability	2	Services for underbanked and underserved communities: SME and community development programs; financial literacy programs	Company Profile; Management & Strategy; Risk Appetite
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; Company Profile; Management & Strategy; Risk Appetite
Labor Relations & Practices	2	Impact of labor negotiations, including board/employee compensation and composition	Company Profile; Management & Strategy
Employee Wellbeing	1	n.a.	n.a.
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	Company Profile; Financial Profile

S Scale: 5, 4, 3, 2, 1

Governance (G)

General Issues	G Score	Sector-Specific Issues	Reference
Management Strategy	3	Operational implementation of strategy	Management & Strategy
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	Management & Strategy; Earnings & Profitability; Capitalisation & Leverage
Group Structure	3	Organizational structure; appropriateness relative to business model; opacity; intra-group dynamics; ownership	Company Profile
Financial Transparency	3	Quality and frequency of financial reporting and auditing processes	Management & Strategy

G Scale: 5, 4, 3, 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 Priniciples 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 ratings above were solicited and assigned or maintained at the request of the rated entity/issuer or a related third party. Any exceptions follow below.