Fitch Ratings

Banks
Retail & Consumer Banks
Germany

Genossenschaftliche FinanzGruppe

Key Rating Drivers

High Influence of Strong Capitalisation: Genossenschaftliche FinanzGruppe (GFG) is the German cooperative banking group. GFG's strong risk-adjusted capitalisation and low leverage have a high influence on its ratings. The ratings also reflect GFG's leading domestic franchise in retail and small SME banking, sound asset quality and strong funding and liquidity. The group's resilient pre-impairment earnings represent a robust first line of defence against an expected rise in loan impairment charges (LICs) in 2021.

Strong Mutual Support Record: GFG is not a legal entity but a cooperative banking network whose cohesion is ensured by a mutual support scheme. GFG's Issuer Default Ratings (IDRs) apply to each member bank. The ratings are underpinned by the scheme's high effectiveness given its long and successful record of ensuring GFG's cohesion, monitoring members' risks and enforcing corrective measures when needed. The scheme has protected its members' viability very effectively and averted losses by their creditors since its inception.

Pandemic, Interest Rates: The Outlook reflects downside risk to the group's profitability and asset quality if the economic recovery from the Covid-19 pandemic proves significantly weaker than expected in Fitch Ratings' baseline economic scenario for Germany. In the longer term, we also expect ultra-low interest rates to further erode GFG's around 800 local bank members' net interest margins, and increase pressure on the group's revenues.

Asset Quality under Pressure: We expect a material increase in defaults in the local banks' SME books in 2021. The historical cyclicality of GFG's asset quality has been moderate and strongly correlates with the number of corporate insolvencies in Germany, which has decreased at the start of the crisis due to extensive state-support to the economy. However, insolvencies will likely rise significantly when the legal suspension of the obligation to file for bankruptcy ends.

Rating Sensitivities

Upgrade Unlikely: We could revise the Outlook to Stable if the economic disruptions turn out to be short-lived, if the group maintains its superior ability to navigate this severe external shock, or if government intervention effectively neutralises the impact on GFG's financial strength. An upgrade is unlikely in light of the already high ratings and the lasting adverse interest-rate environment. 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.

Lasting Economic Downturn: GFG's ratings may be downgraded if the economic disruptions caused by the pandemic intensify, making a swift economic recovery in 2021 and 2022 less likely. This would weaken GFG's relative resilience, and increase the risk that the group may not be able to maintain financial metrics commensurate with its high Viability Rating (VR). A downgrade of our operating environment score for Germany (currently 'aa-'/Negative) would trigger a downgrade of GFG's Long-Term IDR and VR.

Decreasing Margins and Capitalisation: The likely persistence of very low interest rates could eventually cause a downgrade of GFG's ratings. Low interest rates could erode GFG's profits below levels we view as commensurate with its VR. In addition, the VR remains sensitive to weakening capital ratios due to the combination of eroding net interest margins and continued strong balance sheet growth or credit losses. The latter would need to be exceptionally large and well above our expectations to exceed GFG's robust pre-impairment profits.

Ratings

Foreign Currency	
Long-Term IDR	AA-
Short-Term IDR	F1+
Viability Rating	aa-
Support Rating	5
Support Rating Floor	NF
Sovereign Risk	
Long-Term Foreign-Currency IDR	AAA
Long-Term Local-Currency IDR	AAA
Country Ceiling	AAA

Outlooks

Long-Term Foreign-Currency IDR	Negative
Sovereign Long-Term Foreign-Currency IDR	Stable
Sovereign Long-Term Local-Currency IDR	Stable

Applicable Criteria

Bank Rating Criteria (February 2020)

Related Research

Fitch Ratings 2021 Outlook: Western European Banks (December 2020)

Fitch Affirms German Cooperative Banks and DZ BANK at 'AA-'; Outlook Negative (August 2020)

Fitch Revises German Coop Banks' Outlook to Negative on Deteriorating Environment (March 2020)

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Debt Rating Classes

Rating level	Rating
DZ BANK AG Deutsche Zentral-Genossenschaftsbank	
Long-term deposit rating[a, c]	AA
Short-term deposit rating[a,c]	F1+
Long-term senior preferred debt[b,c]	AA
Short-term senior preferred debt[b,c]	F1+
Long-term senior non-preferred debt[a,c]	AA-
Tier 2 subordinated debt[a,c]	A
Legacy hybrid capital notes issued by DZ Bank Capital Funding Trust I	BBB+
Legacy hybrid capital notes issued by DZ BANK Capital Funding Trust II and III and by DZ BANK Perpetual Funding Issuer (Jersey) Limited	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+
815 local cooperative banks (end-2020)	
Long-term deposit ratings	AA-
Short-term deposit ratings	F1+

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

The long-term Deposit Ratings and long-term senior preferred debt ratings of DZ BANK AG Deutsche Zentral-Genossenschaftsbank (DZ BANK) and its banking subsidiaries, and the long-term deposit ratings of GFG's members Deutsche Apotheker- und Aerztebank eG (apoBank) and Muenchener Hypothekenbank eG (Muenchener Hyp) are one notch above their respective Long-Term IDRs. This is because of the protection provided by resolution buffers to preferred creditors. In our view, resolution would only occur in the extremely unlikely event that GFG's mutual support scheme would fail to protect group members' viability. A downgrade of the preferred ratings could result from a downgrade of GFG's IDRs, or if we believed the sum of senior non-preferred and more junior debt buffers at DZ BANK, apoBank or Muenchener Hyp, respectively, could fall below 10% of the banks' risk-weighted assets (RWAs).

The deposit ratings of the local cooperative banks are aligned with GFG's IDRs due to the absence of significant resolution debt buffers at these entities. Each local bank is regulated individually as a less significant institution (LSI).

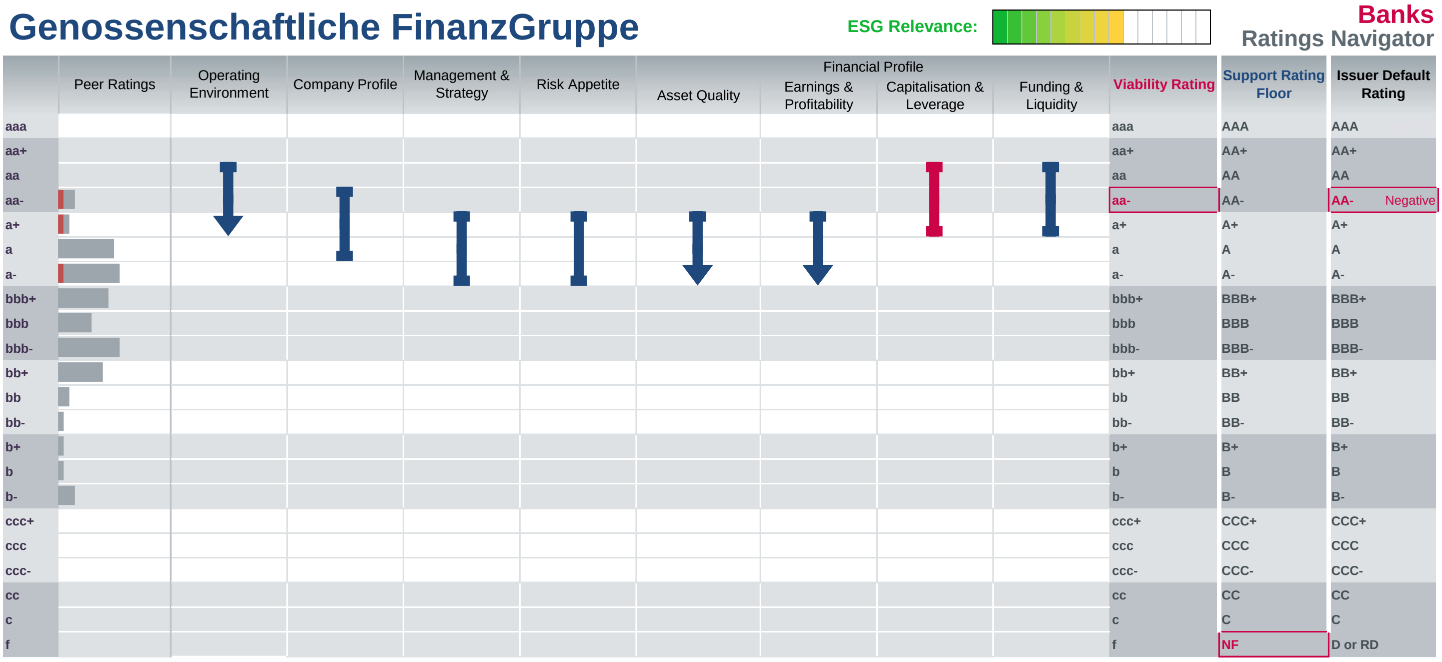
Consequently, the German regulator's preferred resolution strategy for these banks consists of standard insolvency procedures. This contrasts with the preferred resolution strategy via bail-in for the DZ BANK group as well as for apoBank and Muenchener Hyp, each of which is directly supervised by the European Single Resolution Board and follows a single-point-of-entry approach. Therefore, the predominantly deposit-funded local banks have no incentive to build up resolution debt buffers.

The ratings of the subordinated Tier 2 debt issued by DZ BANK and its banking subsidiaries are notched down twice from GFG's VR. We use the VR as anchor rating as 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. The two notches reflect our expectation that DZ BANK will not maintain buffers of Tier 2 and AT1 debt exceeding 10% of its RWAs.

The legacy, non-CRR compliant hybrid capital notes issued by DZ Bank Capital Funding Trust I are rated four notches below GFG's VR, twice each for loss severity and for incremental non-performance risk. The legacy, non-CRR compliant hybrid capital notes issued by DZ BANK Capital Funding Trust II and III and by DZ BANK Perpetual Funding Issuer (Jersey) Limited are rated six notches below GFG's VR, twice for loss severity and four times for incremental non-performance risk. This is because DZ BANK's annual consolidated IFRS profit is a distribution trigger for these instruments, i.e. a loss would prevent DZ BANK from paying coupons on the notes.

In January 2021, DZ BANK announced it will redeem throughout 1H21 all outstanding legacy, non-CRR compliant hybrid capital notes (EUR1.4 billion in total) ahead of the end of the regulatory grandfathering period on 31 December 2021. This does not affect our assessment of GFG's capitalisation.

Ratings Navigator



Significant Changes

Uncertain Economic Outlook

We revised our sector outlook for German banks to negative in December 2019 to reflect, at the peak of the credit cycle, the domestic banking sector's inability to generate adequate returns during periods of strong economic growth due to structural weaknesses, in particular intense competitive pressure preventing adequate profit generation. We revised the outlook to stable in December 2020 to balance our expectation that Germany's 2021 GDP will be only slightly short of the 2019 level with the fact that most banks' structurally weak revenue will further erode marginally and prevent adequate earnings.

In addition, we lowered the operating environment score for German banks to 'aa-'/Negative from 'aa'/Stable in March 2020 as the pandemic exposes the banking sector to a rapid and severe deterioration in earnings and asset quality. The negative outlook signals we could lower the operating environment score further if there are signs the economy will suffer in the longer term from the crisis, or if the sector does not restore its profitability, which is likely to require greater pricing discipline and consolidation to remove excess capacity.

Germany's economy has come so far through the pandemic crisis better than its large European peers. This results from the early adoption of comparatively mild lockdowns, the implementation of a large-scale fiscal programme to sustain companies and households, and a strong recovery in the manufacturing sector in 3Q20. However, the ultimate implications of the pandemic on the German economy and financial market remain unclear, as the second wave of infections threatens to slow down the recovery in the short term. Fitch therefore considers the risks to German banks' credit profiles to remain skewed to the downside.

The operating environment score has a moderate importance for GFG's ratings, unlike most other German banking groups, whose Operating Environment scores are of low importance for the ratings. This is because GFG's score is close to its high VR. A downgrade of the operating environment score would put immediate pressure on the VR, which is not the case with the other German banks, which are rated significantly lower.

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

Company Summary

GFG is the German Cooperative Banking Group

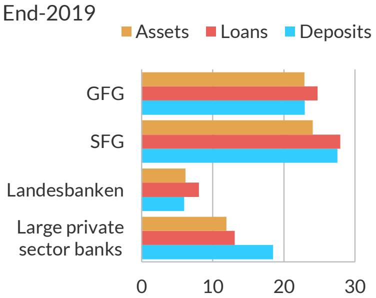
GFG comprises 815 local cooperative banks (as of end-2020), which focus on retail and small SME banking, and their central institution DZ BANK, which also consolidates GFG's banking product suppliers. DZ BANK is large (35% of GFG's aggregated assets at end-2019) and more exposed to riskier wholesale asset classes such as shipping and commercial real estate (CRE). However, stable and low-risk retail businesses dominate its revenue mix, similar to the local banks.

GFG's domestic market shares are close to 20% in most deposit and loan segments, second only to the savings banks (Sparkassen-Finanzgruppe, SFG). Like SFG, GFG is particularly strong in retail and small business banking. More than 60% of the group's 30 million clients are also the local banks' owners. This significantly enhances the stability of GFG's client base, as does the local banks' strong commitment to their home regions.

GFG has steadily increased its market shares in most core products over the last decade, gradually reducing the gap with SFG, and still has some potential to improve its penetration of the vast German mid-sized SME market. The local banks and DZ BANK's product suppliers have also intensified their cooperation and cross-selling, strengthening GFG's cohesion.

Domestic Market Shares

End-2019



Source: Fitch Ratings, Bundesbank, DZ BANK

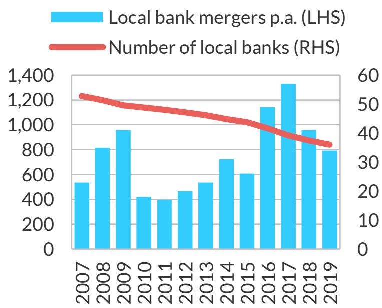
Decentralised Structure Strengthens Franchise but Complicates Regulation

GFG's local banks collectively own DZ BANK, control its supervisory board and define its strategic orientations in cooperation with DZ BANK's management. The local banks' management teams operate much more autonomously than in most European cooperative banking groups. This is because each local bank is legally independent.

We believe that this autonomy and the fact that DZ BANK has no authority over the local banks explain the absence of regulatory requirements at GFG's level, with the exception of consolidated COREP and FINREP reporting. The ECB's formal direct supervision applies only to the domestically systemically important DZ BANK, apoBank and Muenchener Hyp, while the Bundesbank and BaFin supervise each local bank individually. In our view, this regulatory fragmentation prevents considerable efficiency gains, as each local bank must maintain extensive regulatory reporting and back office functions.

We consider that the absence of comprehensive direct group supervision also fails to fully accommodate GFG's operational cohesion. Each local bank must fulfil regulatory requirements such as SREP and liquidity coverage ratios individually, although the mutual support scheme and DZ BANK's central liquidity pooling ensure intragroup fungibility of capital and funding.

Ongoing Consolidation



Source: Fitch Ratings, BVR

Similarly, this fragmented supervision has so far prevented the implementation of a group-wide regulatory recovery and resolution planning, but GFG's mutual support scheme drafts standard requirements for the recovery plans, which will be adopted by nearly all local banks. However, we believe a recovery or resolution could only occur if a particularly severe and protracted systemic crisis exhausts GFG's ability to protect its members' viability via its mutual support scheme. GFG's VR reflects the very low probability of the occurrence of this scenario.

The ECB has been increasingly turning its supervisory attention to European LSIs (of which GFG and SFG's local banks account for the vast majority) over the past two years. In the long term, we believe this could eventually result in GFG being increasingly subject to supervisory provisions at consolidated level.

Despite these regulatory peculiarities, we expect GFG to remain strongly committed to its decentralised structure, wide-ranging autonomy of local management and large (but rapidly decreasing) branch network, as long as the benefits from the strong local franchises outweigh the onerous regulatory costs of the strict decentralised set-up. However, mergers among local banks driven by cost-cutting are likely to continue at a sustained pace, as the low interest rates add to the pressure. The local banks and DZ BANK also continue to align their strategic goals to maximise revenue generation by increasing product penetration.

GFG's decentralised setup also has positive risk implications as it limits risk correlations, drives granularity and promotes a cautious risk culture locally. BVR, GFG's umbrella organisation, ensures the compatibility of GFG's decentralised setup with its common identity and strategic coherence. The continuous development of BVR's monitoring tools enables increasingly effective checks and balances. BVR's responsibilities notably include GFG's risk monitoring, the coordination of product development by the group's specialised product providers, and the management of the dual mutual support scheme.

The publication of consolidated accounts at GFG's level attests its commitment to be perceived as a cohesive group by key stakeholders. In our view, the group's market share gains relative to SFG in recent years partly reflect its higher cohesion, whereas SFG is (despite some progress) still far from having a single central institution and unified product suppliers.

Common Strategic Goals Despite Local Banks' Independent Management

The highly decentralised structure results in fairly loose corporate governance at GFG's level, in our view. BVR has limited powers to influence the governance of DZ BANK and the local banks, each of which has its own management and supervisory boards.

BVR's former president became DZ BANK's co-chief executive in 2019. This unprecedented move evidences the deepening cooperation and strategic alignment of DZ BANK, BVR and the local banks. A current illustration of this alignment is the ongoing wind-down of DZ BANK's ship financing business after heavy losses in the past five years at its transportation finance unit DVB BANK. The volatile, wholesale, bulky, global and largely dollar-denominated ship lending was the last remaining sizeable business that did not serve the local banks' business models.

Increasingly Acting in Concert on Digitalisation and IT Harmonisation

In our view, GFG is well equipped to manage the transition of its clients' banking behaviour (notably toward rising acceptance and more extensive use of digital services) while maintaining the local proximity that underpins its franchise. In doing so, the group is helped by the marked inertia that characterises German retail clients, including a fairly slow adoption of digitisation trends and a high degree of loyalty to long-standing main banking relationships.

Successfully combining its traditional and innovative banking channels is crucial as we believe GFG's set-up will prevent the creation of a common pure online bank in the foreseeable future. In the long term, we view as plausible GFG's aim to diversify its revenues by leveraging the primary banks' strong ties to their local communities to create local digital platforms offering services beyond traditional banking.

Decentralised Risk Management but Adequate Risk Controls

Each local bank defines its risk appetite, and underwriting decisions are not subject to GFG-wide centralised approvals or limits. However, BVR's monitoring system indirectly influences the banks' risk-taking as 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. The local banks also use a shared internal credit rating system for retail and SME loans (the VR Rating System) and a synthetic risk diversification tool, both managed by BVR and DZ BANK.

The local banks' low risk appetite and their diversified and granular exposures adequately mitigate GFG's credit risk. The banks' strong focus on owner-occupied housing loans, which account for over one third of GFG's total loans, as well as their good knowledge of their local areas of operation and close proximity to their clients, are also important risk mitigating factors.

High Structural Interest-Rate Risk in the Banking Books

The banking books of GFG's local banks are exposed to high structural interest-rate risk, which is predominantly unhedged. Local banks' large portion of price inelastic retail deposits would mitigate the negative impact of rising interest rates. However, interest rates are likely to remain low for long. We expect most banks to react by increasingly passing on negative rates to retail depositors, and not only to institutional and corporate clients. However, we believe this will not prevent ultra-low interest rates from further eroding the local banks' net interest margins and, consequently, increase pressure on the group's profitability in the long term.

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	18,185	18,368	18,638	18,826
Net fees and commissions	7,092	6,816	6,491	5,963
Other operating income	3,665	817	2,247	1,985
Total operating income	28,942	26,001	27,376	26,774
Operating costs	18,142	18,079	17,884	17,944
Pre-impairment operating profit	10,800	7,922	9,492	8,830
Loan and other impairment charges	832	151	576	522
Operating profit	9,968	7,771	8,916	8,308
Tax	3,133	2,369	2,843	2,410
Net income	7,046	5,402	6,073	5,898
Summary balance sheet				
Gross loans	844,552	794,916	761,880	733,155
Loan loss allowances	9,119	8,988	7,363	7,520
Net loans	835,433	785,928	754,517	725,635
Interbank	22,439	18,800	51,042	41,433
Derivatives	25,232	20,530	22,325	34,234
Other securities and earning assets	390,104	371,554	363,597	370,237
Total earning assets	1,273,208	1,196,812	1,191,481	1,171,539
Cash and due from banks	87,421	75,169	32,594	25,421
Other assets	23,459	21,196	19,241	18,820
Total assets	**1,384,088**	**1,293,177**	**1,243,316**	**1,215,780**
Customer deposits	880,398	842,420	801,031	774,302
Interbank and other short-term funding	156,316	119,300	113,065	103,282
Other long-term funding	46,793	58,677	68,581	75,922
Trading liabilities and derivatives	54,896	48,742	44,181	57,526
Total funding	1,138,403	1,069,139	1,026,858	1,011,032
Other liabilities	129,525	116,160	111,608	105,999
Preference shares and hybrid capital	204	243	492	265
Total equity	115,956	107,635	104,358	98,484
Total liabilities and equity	**1,384,088**	**1,293,177**	**1,243,316**	**1,215,780**
Ratios (annualised as appropriate)				
Profitability				
Operating profit/risk-weighted assets	1.5	1.2	1.5	1.5
Net interest income/average earning assets	1.5	1.5	1.6	1.6
Non-interest expense/gross revenue	63.2	69.9	65.6	67.3
Net income/average equity	6.3	5.1	6.0	6.2
Asset quality				
Growth in gross loans	6.2	4.3	3.9	4.7
Loan impairment charges/average gross loans	0.1	0.0	0.1	0.1

Source: Fitch Ratings, Fitch Solutions, GFG

Summary Financials and Key Ratios (Cont.)

	31 Dec 19	31 Dec 18	31 Dec 17	31 Dec 16
Capitalisation				
Common equity Tier 1 ratio	13.6	13.5	13.3	13.0
Tangible common equity/tangible assets	8.2	8.3	8.4	8.1
Basel leverage ratio	7.0	6.9	6.8	6.3
Funding and liquidity				
Loans/customer deposits	95.9	94.4	95.1	94.7
Liquidity coverage ratio	174.3	166.0	161.0	156.0
Customer deposits/funding	79.0	80.5	79.9	79.6

Source: Fitch Ratings, Fitch Solutions, GFG

Key Financial Metrics – Latest Developments

Asset Quality Deterioration Likely in 2021

Strong economic conditions in Germany before the outbreak of the pandemic, a dominant focus on granular retail housing, small SMEs and professionals, high collateralisation levels in secured lending as well as low single-name and sector concentrations, have driven a steady improvement in GFG's asset quality over the past decade. The group's international diversification is limited. But its focus on domestic lending is rating-positive on balance given the strength and the size of the domestic economy, and Fitch's expectation that Germany will continue to fare better than other large European economies through the crisis.

The German government put in place, at the beginning of the pandemic, large programmes to support companies and households affected by the crisis. It has also suspended until end-3Q20 the legal obligation for illiquid companies to file for bankruptcy (the suspension has been extended until end-April 2021 for companies that qualify for state support but have yet to receive it). This has contained the number of corporate insolvencies at a low level until end-2020 and impaired loan volumes close to their end-2019 level. However, we expect impaired loans to significantly rise from early 2021, when support measures for SMEs are successively phased out.

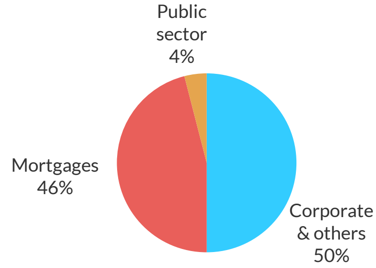
The local banks' coverage of impaired loans is lower than international peers' but has remained stable in recent years and should be assessed in the context of the local banks' large proportion of mortgage loans. Including collateral, the total coverage is reasonably close to 100%. We also expect the extension of furlough schemes (Kurzarbeit) until end-2021, and stable real estate prices, to support asset quality in the retail mortgage loan books.

DZ BANK's asset quality benefits from years of run-down of the bank's most vulnerable asset classes, including southern European public-sector bonds. In 2019 and 2020, the bank made significant progress with the wind-down of its troubled transportation lender DVB BANK, whose maritime lending portfolio has been responsible for the majority of GFG's LICs in recent years. Despite the particularly weak quality of loans to the offshore oil services sector and their vulnerability to the challenging global oil market, the modest size of the residual maritime lending portfolio no longer represents a significant risk for DZ BANK's profitability.

DZ BANK and Muenchner Hyp are two of the largest German CRE lenders, with a combined loan volume of close to EUR80 billion. CRE is a cyclical asset class, but GFG's focus on the still resilient domestic market should mitigate its vulnerability to the consequences of the pandemic.

GFG's Loan Breakdown

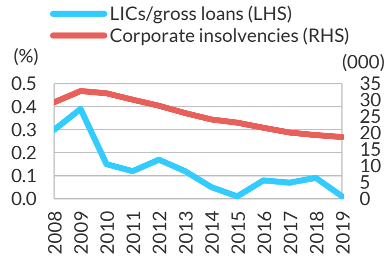
End-2019; total EUR844bn



Source: Fitch Ratings, BVR

Costs of Risk

Driven by corporate insolvencies



Source: Fitch Ratings,BVR, Federal Statistical Office

Higher LICs and Margin Pressure Likely to Weigh on Profitability

We expect LICs to rise along with impaired loans at the local banks, in addition to continued provisioning needs for DZ BANK's weak shipping and offshore financing portfolios. LICs should substantially weaken GFG's profitability in 2020, and even more so in 2021, compared with the EUR10.2 billion earned before tax in 2019, its second-highest result ever. The EUR2.4 billion increase in the group's pre-tax profit in 2019 yoy was mainly driven by valuation gains in the securities portfolios of DZ BANK and its insurance subsidiary R+V. This was owing to strong capital markets developments, which we believe unlikely to recur in 2020 and 2021 due to the pandemic.

We also expect GFG's profitability to gradually decline in the medium term as the Covid-19 crisis is unlikely to end the intense pricing pressure prevailing in the German banking sector. This will increasingly constrain the ability of GFG's local banks to sustainably counter the erosion of their net interest margins. So far, the strong growth of their loan books and net fee income has largely offset this erosion, but further fee increases will be increasingly challenging to impose on clients. Despite about 500 branch closures a year in recent years, GFG's cost savings have failed to keep pace with the attrition of net interest income. However, we expect the local banks to increasingly use their ample cost-cutting potential (they still operated 9,300 branches at end-2019) if charging negative interest rates on depositors proves challenging.

Strong Capitalisation is of High Importance for the Rating

We expect GFG's loan growth to continue to exceed the German sector average - though at a slower pace than in previous years - as the group continues to gain market share from weaker competitors. The combination of moderating organic capital generation, higher defaults and growing balance sheet will exert pressure on GFG's CET1 ratio in the medium-term.

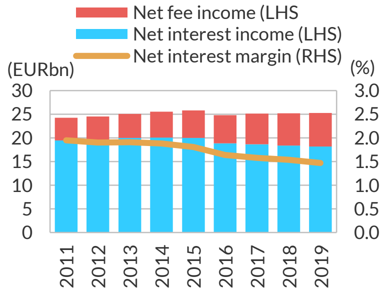
These effects should have been largely mitigated in 2020 by the favourable revision of the regulatory supporting factor applied to the calculation of RWAs on SME lending exposures.

In our assessment of GFG's capitalisation we include the undisclosed German GAAP reserves (section 340f, which count as regulatory Tier 2 capital) in GFG's CET1. This is because these reserves are fully loss-absorbing on a going-concern basis and the member banks can convert them into their funds for general banking risk (German GAAP section 340g, which count as regulatory CET1 capital) at the management's discretion. This results into a pro-forma CET1 ratio of 15.5% at end-2019, well above the regulatory CET1 ratio of 13.6% and close to the disclosed regulatory total capital ratio. We also positively adjust our implied capitalisation score to reflect the standardised approach used by GFG's local banks to measure credit risk for all asset classes. We believe the use of the standardised approach considerably overstates the riskiness of GFG's balance sheet compared with similar European peers which use the internal-rating based approach.

Very Stable and Diversified Retail-Focused Funding Remains a Key Rating Strength

The local banks are predominantly funded by granular domestic retail deposits, and their structurally large excess liquidity covers about a third of DZ BANK's short-term funding needs. As a frequent issuer of unsecured debt and the largest German issuer of covered bonds to an established and geographically diversified investor base, DZ BANK provides GFG with reliable access to wholesale markets (including with short-term instruments) and has proven the adaptability of its funding sources at the height of the COVID-19 market dislocations. The group's Short-Term IDR of 'F1+' is the only option mapping to the Long-Term IDR of 'AA-' and is also commensurate with the group's Funding & Liquidity score of 'aa-'.

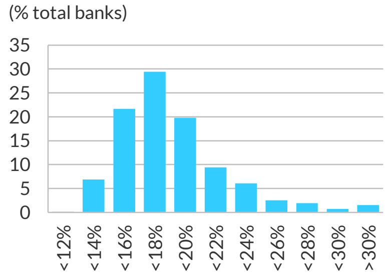
Fee Income and Loan Growth Stabilise Revenues



Source: Fitch Ratings, BVR

Distribution of Capital Ratios

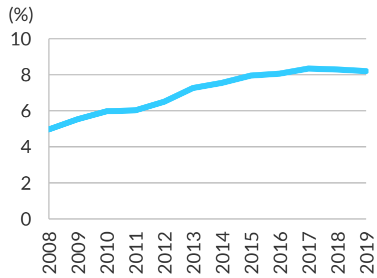
Local banks' FYE19 total capital ratios



Source: Fitch Ratings, BVR

Flattening Capitalisation

Tang.common equity/tang.assets



Source: Fitch Ratings, BVR

Sovereign Support Assessment

The Support Rating and Support Rating Floor reflect our view that, due to the EU's Bank Recovery and Resolution Directive, GFG's senior creditors can no longer rely on full extraordinary support from the German sovereign if the bank becomes non-viable.

Support Rating Floor:			NF
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		✓	

Environmental, Social and Governance Considerations

ESG issues are credit neutral or have only a minimal credit impact on GFG, either due to their nature or the way in which they are being managed by the group. For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg.

FitchRatings **Genossenschaftliche FinanzGruppe** **Banks** Ratings Navigator

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	Company Profile; Management & Strategy; Risk Appetite; 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	Company Profile; Management & Strategy; Risk Appetite	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; Company Profile; Management & Strategy; Risk Appetite	4
Labor Relations & Practices	2	Impact of labor negotiations, including board/employee compensation and composition	Company Profile; Management & Strategy	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	Company Profile; Financial Profile	1

Governance (G)

General Issues	G Score	Sector-Specific Issues	Reference	G Scale
Management Strategy	3	Operational implementation of strategy	Management & Strategy	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	Management & Strategy; Earnings & Profitability; Capitalisation & Leverage	4
Group Structure	3	Organizational structure; appropriateness relative to business model; opacity; intra-group dynamics; ownership	Company Profile	3
Financial Transparency	3	Quality and frequency of financial reporting and auditing processes	Management & Strategy	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).

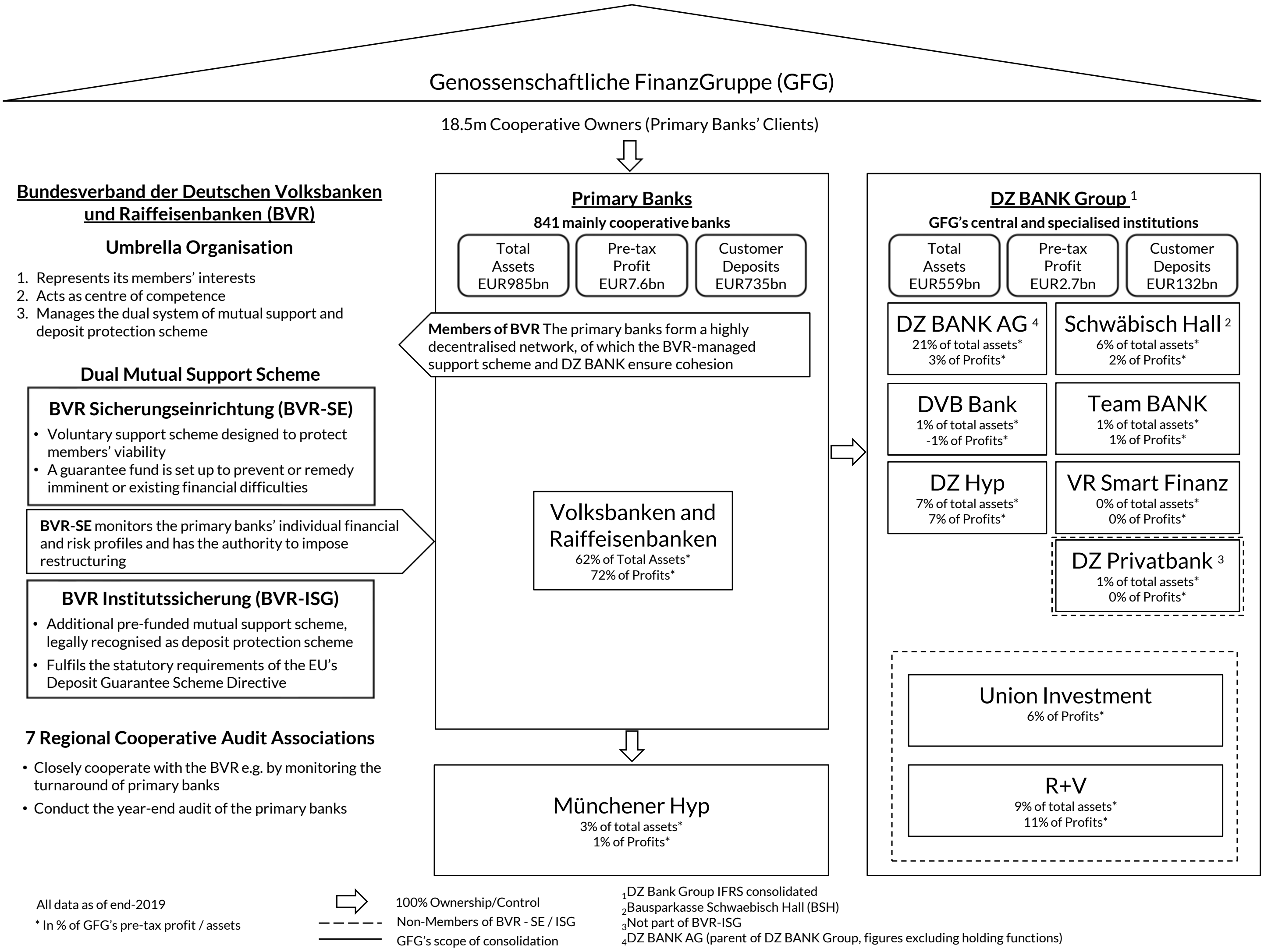
Sector references in the scale definitions below refer to Sector as displayed in the Sector Details box on page 1 of the navigator.

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.

Appendix 1: Simplified Organisational Structure



Source: Fitch Ratings

Appendix 2: BVR-Run Dual System of Mutual Support and Deposit Guarantee Scheme

The banks' membership in the mutual support scheme allows a 0% regulatory risk-weighting of GFG's intragroup receivables (standardised approach) under Art. 113 (7), Capital Requirements Regulation (CRR). This is an important element of the group's cohesiveness as it ensures funding fungibility and facilitates intragroup risk transfers. In addition, group members do not have to deduct their equity stakes in other members from their regulatory capital under Art. 49 (3) 3 CRR, and only 50% of their intragroup receivables counts toward their regulatory large exposure limits.

BVR-SE

BVR-SE is a legally segregated trust governed by BVR's bye-laws. GFG's group ratings do not apply to BVR, which manages the mutual support scheme but is not a member itself. In theory, GFG's members are allowed to exit the scheme, and BVR can exclude any bank that fails to monitor its risks adequately. However, exits and exclusions are very rare occurrences.

The fund is at the core of the institutional protection scheme that protects the viability of all bank members, and covers all of their obligations, not only their deposits. Since BVR-SE's creation in 1934, no member has ever defaulted on any of its obligations.

Each deposit-taking member of GFG is affiliated to the fund and makes mandatory annual cash contributions ("Garantiefonds") based on its RWAs and adjusted for BVR's assessment of its individual risk profile. The fund retains the net interest income accrued on the accumulated cash contributions. If the Garantiefonds' endowment is insufficient to provide support when the need arises, BVR is entitled to call guarantees ("Garantieverbund"), based on irrevocable letters of credit from the members and proportional to their individual risk profiles.

In theory, timeliness of payment could become an issue if the combined Garantiefonds and Garantieverbund are insufficient to cover the failure of sizeable members (of which DZ BANK is by far the largest) and need replenishment. However, should this unlikely scenario occur, we would expect the fund to borrow against future cash flows to ensure timely payment or arrange timely support from another source (e.g. members might provide the troubled entity with subordinated debt directly or set up an asset guarantee structure, similar to the one put in place to cover some of DZ BANK's non-core securitisation assets at end-2008).

BVR-ISG

GFG established in 2015 a second support scheme, BVR Institutssicherungs GmbH (BVR-ISG), in addition to its long-standing mutual support scheme BVR-SE. BVR-ISG is the group's legally recognised deposit protection fund, pursuant to the EU's Deposit Guarantee Scheme Directive (DGSD). The two schemes constitute the BVR's dual system and are linked by an indemnity declaration of BVR-SE in favour of BVR-ISG.

Centralised Monitoring Tools

BVR calculates a set of capital, profitability and asset-quality ratios for each local bank based on annual reports, which are typically audited by GFG's regional audit associations. These metrics feed into an internal classification system to determine preventative or curative measures and, if needed, the turnaround management of distressed banks.

This classification is validated by regular back-testing. Lowly-rated banks are subject to extended reporting requirements. Banks in these categories may also be subject to special audits or recommendations from BVR on actions needed. They may also have to present a turnaround plan, which, if accepted, will be closely monitored by GFG's auditors and BVR and may include a management reshuffle. The number of local banks subject to preventive measures or restructuring procedures has fallen materially since the mid-2000s, reflecting the efficiency of BVR's monitoring processes and Germany's benign operating environment.

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.