

Rating Action: Moody's affirms Bausparkasse Schwaebisch Hall's Aa2 deposit and issuer ratings, outlook remains stable

18 Jan 2022

Frankfurt am Main, January 18, 2022 -- Moody's Investors Service (Moody's) today affirmed Bausparkasse Schwaebisch Hall AG's (BSH) Aa2/P-1 deposit and issuer ratings. At the same time, the rating agency affirmed all other ratings of BSH, including the bank's baa2 Baseline Credit Assessment (BCA), its a3 Adjusted BCA, the Aa2/P-1 Counterparty Risk Rating as well as the bank's Aa2(cr)/P-1(cr) Counterparty Risk Assessment. The outlook on BSH's long-term deposit and issuer ratings remains stable.

A full list of affected ratings and assessments can be found at the end of this press release.

RATINGS RATIONALE

BCA AFFIRMATION REFLECTS BSH'S ABILITY TO STABILIZE RESULTS DESPITE BUSINESS MODEL CHALLENGES

The affirmation of BSH's baa2 BCA reflects its very strong capitalization, conservative funding and liquidity profile and sound asset quality, despite a concentration of BSH's monoline business model on residential mortgage lending. The baa2 BCA also incorporates Moody's expectation that BSH will be able to absorb ongoing pressure on its building and loan association (Bausparkasse) business model through growth of its residential mortgage loan book, accompanied by a gradual shift in its funding profile towards covered bonds. BSH's BCA remains capped at the baa2 level of its parent DZ BANK AG (DZ BANK, deposits Aa2 stable/senior unsecured debt Aa2 stable, BCA baa2) because of the tight strategic and financial integration of BSH into the cooperative banking sector and with its parent.

The pandemic has had a very limited negative effect on the credit quality of BSH's retail customers, which also provide highly stable fixed rate Bauspar deposits as the backbone of BSH's funding profile. BSH provides predominantly fixed rate residential mortgage loans, in most cases with loan-to-value ratios below 80%, conservatively calculated based on German lending values that typically are below house market values.

The extended low rates environment has compressed the spread BSH and its peers can derive between their deposit funding and mortgage lending and it has triggered repeated adjustments to reserve levels designed to absorb future interest bonus payments to depositors.

AFFIRMATION OF LONG-TERM RATINGS REFLECTS UNCHANGED STRUCTURAL SUPPORT ASSESSMENT

The affirmation of BSH's Aa2/P-1 deposit and issuer ratings reflects Moody's unchanged assumption of very high affiliate support and moderate government support as well as unchanged results under the rating agency's Advanced Loss Given Failure (LGF) analysis.

Genossenschaftliche FinanzGruppe (G-Finanzgruppe) and its member banks, including BSH, operate a regulated and supervised institutional protection scheme and Moody's considers the likelihood of member banks supporting each other to be very high, resulting in an Adjusted BCA that benefits from the overall financial creditworthiness of the group.

Moody's expects BSH as a domestic banking subsidiary to form a joint resolution perimeter in case of failure with its parent group DZ BANK. Moody's therefore applies the results of DZ BANK's LGF analysis to the rated instruments of BSH, considering the risks faced by the different debt and deposit classes across the group's liability structure at failure.

For BSH's deposit and issuer ratings, Moody's Advanced LGF analysis continues to indicate an extremely low loss given failure, which translates into three notches of rating uplift from the bank's a3 Adjusted BCA. The assumption of a moderate probability of government support adds one notch to BSH's Aa2 long-term deposit and issuer ratings.

RATIONALE FOR THE STABLE OUTLOOK

Moody's expects the intrinsic strength of DZ BANK, which caps the BCA of BSH at baa2, to remain broadly unchanged over the 12 to 18 months outlook horizon. Similarly, the rating agency does not anticipate a change in its affiliate support or in the liability structure of DZ BANK uplift during this timeframe.

FACTORS THAT COULD LEAD TO AN UPGRADE OR DOWNGRADE OF THE RATINGS

An upgrade of BSH's ratings could be triggered by an upgrade of the bank's BCA, or by an improvement in the cooperative sector's financial strength. BSH's ratings already benefit from the highest possible uplift under Moody's Advanced LGF analysis.

An upgrade of BSH's BCA would require an upgrade of DZ BANK's BCA which caps BSH's BCA at baa2 and at the same time to BSH at least maintaining its own financial profile. An upgrade of BSH's unconstrained BCA could be prompted by a sustained improvement in the bank's profitability, particularly by successfully stabilising its net interest income against downward pressures in the current low interest rate environment.

A downgrade of BSH's ratings could result from a joint weakening of the financial strength of G-Finanzgruppe and DZ BANK, or if DZ BANK significantly reduced its liabilities designed to absorb losses in bail-in compared with its tangible banking assets.

BSH's BCA could be downgraded in the case of a downgrade of DZ BANK's BCA, because it caps BSH's BCA. BSH's unconstrained BCA could be downgraded if the bank's gradual funding structure transformation resulted in a significantly higher dependence on market funding or if BSH fails to overcome the pressure exerted by the low interest rate environment on its business model.

LIST OF AFFECTED RATINGS

Issuer: Bausparkasse Schwaebisch Hall AG

..Affirmations:

-Adjusted Baseline Credit Assessment, affirmed a3
-Baseline Credit Assessment, affirmed baa2
-Long-term Counterparty Risk Ratings, affirmed Aa2
-Short-term Counterparty Risk Ratings, affirmed P-1
-Long-term Counterparty Risk Assessment, affirmed Aa2(cr)
-Short-term Counterparty Risk Assessment, affirmed P-1(cr)
-Long-term Bank Deposits, affirmed Aa2, outlook remains Stable
-Short-term Bank Deposits, affirmed P-1
-Long-term Issuer Ratings, affirmed Aa2, outlook remains Stable
-Short-term Issuer Ratings, affirmed P-1

..Outlook Action:

-Outlook remains Stable

PRINCIPAL METHODOLOGY

The principal methodology used in these ratings was Banks Methodology published in July 2021 and available at https://www.moody.com/researchdocumentcontentpage.aspx?docid=PBC_1269625. Alternatively, please see the Rating Methodologies page on www.moody.com for a copy of this methodology.

REGULATORY DISCLOSURES

For further specification of Moody's key rating assumptions and sensitivity analysis, see the sections

Methodology Assumptions and Sensitivity to Assumptions in the disclosure form. Moody's Rating Symbols and Definitions can be found at: https://www.moody.com/researchdocumentcontentpage.aspx?docid=PBC_79004.

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