



RATING ACTION COMMENTARY

Fitch Affirms Berlin Hyp's Long-Term IDR at 'A-'/Stable; VR at 'bbb+'

Tue 08 Nov, 2022 - 11:24 AM ET

Fitch Ratings - Frankfurt am Main - 08 Nov 2022: Fitch Ratings has affirmed Berlin Hyp AG's Long-Term Issuer Default Rating (IDR) at 'A-' with a Stable Outlook and Viability Rating (VR) at 'bbb+'. A full list of rating actions is below.

KEY RATING DRIVERS

Support Drives IDR: We align Berlin Hyp's IDRs and 'a-' Shareholder Support Rating (SSR) with the IDRs of its owner, Landesbank Baden-Wuerttemberg (LBBW, A-/Stable/F1), reflecting our view that LBBW would have a very high propensity to support Berlin Hyp. We believe LBBW's reputation would be greatly damaged if, as Berlin Hyp's owner, it failed to provide support if needed. The Stable Outlook on Berlin Hyp's Long-Term IDR mirrors that on its parent.

LBBW recently acquired 100% of Berlin Hyp, which has been defined as a central pillar to LBBW's commercial real estate (CRE) strategy. We expect integration to intensify over time, although Berlin Hyp currently retains some management independence.

German CRE Lender: Berlin Hyp's VR reflects its role as a specialised CRE lender, which dominates its business model, earnings and risk profile, resulting in good asset quality, adequate profitability and capitalisation. The VR also factors in its integration into the savings banks organisation (Sparkassen-Finanzgruppe; SFG; A+/Stable/F1+), which enhances its loan origination potential and supports its liquidity and funding profile.

Focus on Core Domestic CRE: Berlin Hyp's lending mix is focussed on investment and development financings mainly in metropolitan areas and larger cities, where it has expertise. The risk/return profile of the loans originated in recent years appears reasonable and consistent over time, despite the intense competition.

Robust Asset Quality: We expect Berlin Hyp's impaired loans ratio to deteriorate modestly in 2023, as a result of an economic downturn, rising interest rates and inflation, but to stay below 2% in the medium term. The bank's focus on CRE lending with inherently high loan concentration constrains our asset quality assessment.

Resilient Profitability: We expect the bank's four-year average operating profit/risk-weighted assets (RWAs) to remain at about 1.0-1.5% through the cycle. In the coming quarters, profitability could temporarily fall below this level as a challenging operating environment in Germany is likely to weaken loan demand and could lead to higher loan impairment charges (LICs), which might only partially offset by higher revenue from rising rates.

Adequate Capital: Berlin Hyp's common equity Tier 1 (CET1) ratio stood at 14% at end-1H22, which is adequate for the bank's risk profile and provides a reasonable buffer over regulatory requirements. Berlin Hyp is likely to continue to retain parts of its profits to match long-term RWA inflation that will result from the implementation of the Basel III end-game output floor.

Sound Funding and Liquidity Profile: Berlin Hyp is wholesale-funded, mostly through mortgage Pfandbriefe and unsecured debt. Due to Berlin Hyp's membership in SFG's institutional protection scheme, investments by SFG's members in the bank's unsecured debt benefit from a 0% regulatory risk weight. This ensures privileged access to SFG's vast excess liquidity. The issuance of green bonds and sustainability-linked bonds further diversifies its institutional investor base.

RATING SENSITIVITIES

Factors that could, individually or collectively, lead to negative rating action/downgrade:

A downgrade of LBBW's IDRs, or a change in the ownership structure or the owner's strategic commitment to Berlin Hyp could lead to a downgrade of its IDRs and SSR.

Berlin Hyp's VR has moderate headroom in the event of downside risks to our baseline forecast. We could downgrade the VR if we expect severe and sustained pressure on the performance of the CRE market to durably weaken the bank's impaired loans and operating profit/RWAs ratios above 3.0% and below 0.8%, respectively.

Factors that could, individually or collectively, lead to positive rating action/upgrade:

An upgrade of the IDRs and SSR would require an upgrade of LBBW's ratings.

An upgrade of the VR is likely to require an upgrade of LBBW's VR (bbb), as Fitch would usually limit the VR of Berlin Hyp to one notch above its parent's VR, because we view both banks' credit profiles as highly correlated. Additionally, an upgrade of Berlin Hyp's VR would require a record of substantially stronger lending margins and a more diversified business model with significant revenue sources independent from CRE lending.

OTHER DEBT AND ISSUER RATINGS: KEY RATING DRIVERS

Senior Debt and Deposit Ratings: Berlin Hyp's long-term senior preferred debt and deposit ratings are one notch above its Long-Term IDR due to its large buffer of senior non-preferred (SNP) debt equivalent to about 40% of the bank's RWAs at end-2021. We expect Berlin Hyp to become part of LBBW's single-point-of-entry resolution perimeter.

Berlin Hyp's short-term senior preferred debt and deposit ratings are the baseline options that map to the 'A' long-term ratings and in line with LBBW's ratings.

OTHER DEBT AND ISSUER RATINGS: RATING SENSITIVITIES

Berlin Hyp's senior debt and deposit ratings are sensitive to a change in its IDRs or if the sum of SNP and more junior debt falls below 10% of RWAs.

An upgrade of Berlin Hyp's IDRs would trigger an upgrade of the senior debt and deposit ratings, unless its resolution buffers decrease below 10% of its RWAs.

VR ADJUSTMENTS

The Asset Quality score of 'bbb+' has been assigned below the 'aa' category implied score due to the following adjustment reason(s): Concentrations (negative).

The Earnings & Profitability score of 'bbb' has been assigned below the 'a' category implied score due to the following adjustment reason(s): Revenue Diversification (negative).

The Capitalisation & Leverage score of 'bbb+' has been assigned below the 'a' category implied score due to the following adjustment reason(s): Risk Appetite and Business Model (negative).

The Funding & Liquidity score of 'bbb+' has been assigned above the 'b and below' category implied score due to the following adjustment reason(s): Liquidity Support and Ordinary Support (positive).

BEST/WORST CASE RATING SCENARIO

International scale credit ratings of Financial Institutions and Covered Bond issuers have a best-case rating upgrade scenario (defined as the 99th percentile of rating transitions, measured in a positive direction) of three notches over a three-year rating horizon; and a worst-case rating downgrade scenario (defined as the 99th percentile of rating transitions, measured in a negative direction) of four notches over three years. The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Best- and worst-case scenario credit ratings are based on historical performance. For more information about the methodology used to determine sector-specific best- and worst-case scenario credit ratings, visit <https://www.fitchratings.com/site/re/10111579>

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

PUBLIC RATINGS WITH CREDIT LINKAGE TO OTHER RATINGS

Berlin Hyp's ratings are driven by shareholder support from LBBW.

ESG CONSIDERATIONS

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

RATING ACTIONS

ENTITY / DEBT ⇅	RATING ⇅	PRIOR ⇅
Berlin Hyp AG	LT IDR A- Rating Outlook Stable Affirmed	A- Rating Outlook Stable

	ST IDR	F1	Affirmed	F1
	Viability	bbb+	Affirmed	bbb+
	Shareholder Support	a-	Affirmed	a-
long-term deposits	LT	A	Affirmed	A
Senior preferred	LT	A	Affirmed	A
Senior non-preferred	LT	A-	Affirmed	A-
short-term deposits	ST	F1	Affirmed	F1
Senior preferred	ST	F1	Affirmed	F1

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APPLICABLE CRITERIA[Bank Rating Criteria \(pub. 07 Sep 2022\) \(including rating assumption sensitivity\)](#)**ADDITIONAL DISCLOSURES**[Dodd-Frank Rating Information Disclosure Form](#)[Solicitation Status](#)[Endorsement Policy](#)**ENDORSEMENT STATUS**

Berlin Hyp AG

EU Issued, UK Endorsed

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