

Rating Action: Moody's downgrades DZ BANK AG's junior senior unsecured debt ratings to A2 from A1

12 Aug 2020

Senior unsecured debt and deposit ratings affirmed at Aa1, outlook remains negative

Frankfurt am Main, August 12, 2020 -- Moody's Investors Service, (Moody's) today downgraded the junior senior unsecured debt ratings of DZ BANK AG (DZ BANK) to A2 from A1. At the same time, the rating agency affirmed the bank's long-term deposit and senior unsecured debt ratings at Aa1; the outlook for these ratings remains negative. Concurrently, Moody's affirmed DZ BANK's baa2 Baseline Credit Assessment (BCA) and a2 Adjusted BCA.

Moody's has also corrected the rating class for the Tier I Perpetual Limited Recourse Securities issued by DZ Bank Perpetual Funding Issuer (Jersey) Limited to Preferred Stock Non-cumulative. Due to an internal administrative error, these hybrid securities were previously mislabelled as Junior Subordinate. This correction has no impact on the current Baa3 (hyb) ratings or the ratings history.

For a list of all affected ratings, please refer to the end of this press release.

RATINGS RATIONALE

-- DOWNGRADE OF THE JUNIOR SENIOR UNSECURED DEBT RATINGS REFLECTS INCREASE IN LOSS SEVERITY EXPECTATION

Today's one-notch downgrade of DZ BANK's junior senior unsecured debt ratings to A2 from A1 was prompted by a meaningful reduction in the outstanding volume of this loss-absorbing instrument, in combination with strong balance sheet growth. These developments result in a higher loss severity for junior senior debt under Moody's Advanced Loss Given Failure (LGF) analysis. Moody's LGF analysis now indicates a moderate loss-given-failure for junior senior unsecured debt, while the previous LGF analysis resulted in a low loss-given-failure.

Moody's assumes an unchanged low probability of government support and zero notches of rating uplift for junior senior unsecured debt instruments issued by DZ BANK, which is subject to an operational resolution regime, because these are designed to absorb losses in the case of bank failure.

-- AFFIRMATION OF THE BASELINE CREDIT ASSESSMENT AND ADJUSTED BCA REFLECTS RESILIENT FINANCIAL PROFILE

The affirmation of DZ BANK's baa2 BCA reflects the resilience of the bank's intrinsic financial strength, even in an adverse operating environment further weakened by the coronavirus outbreak. While this increases pressure on solvency, Moody's views DZ BANK as sufficiently robust to absorb the likely shock to asset quality without a meaningful decline in its standalone creditworthiness. Moody's regards the coronavirus outbreak as a social risk under its ESG framework, given the substantial implications for public health and safety.

DZ BANK's baa2 BCA considers its overall sound solvency profile, based on adequate asset quality; a strong capitalization and moderate profitability; and its overall sound liquidity profile, with a high share of liquid assets mitigating some dependence on market funding. DZ BANK benefits from a degree of diversification across businesses that are only partly correlated, such as banking, asset management and insurance, but also shows some risk concentrations that could result in a more rapid deterioration of asset quality in an adverse scenario.

DZ BANK's a2 Adjusted BCA incorporates three notches of rating uplift from affiliate support to DZ BANK's baa2 BCA. DZ BANK is the central institution of the banking group that forms the German cooperative banking association, Bundesverband der Deutschen Volksbanken und Raiffeisenbanken (BVR). BVR and its member banks operate a regulated and supervised institutional protection scheme and Moody's assesses the likelihood that member banks support each other as very high, resulting in an Adjusted BCA that benefits from the overall financial creditworthiness of the group.

-- AFFIRMATION OF DEBT AND DEPOSIT RATINGS REFLECTS UNCHANGED LOSS-ABSORPTION CAPACITY AND GOVERNMENT SUPPORT ASSUMPTIONS

The affirmation of the senior unsecured and deposit ratings reflects the affirmation of the bank's BCA and Adjusted BCA as well as the unchanged notching results under Moody's Advanced LGF analysis of the group's current consolidated balance sheet structure at end-2019[1] and its near-term funding plan. While the reduced volume of junior senior unsecured instruments reduces the protection for senior unsecured debt and deposits, it remains sufficient to support the previous three notches of rating uplift for these instrument classes.

Moody's considers Germany's cooperative banking sector and its central institution DZ BANK to be of domestic systemic importance and assumes a moderate probability of government support for DZ BANK's senior unsecured debt and deposits, which results in a further one-notch rating uplift, leading to long-term deposit and senior unsecured ratings of Aa1.

-- NEGATIVE OUTLOOK ON LONG-TERM RATINGS CONTINUES TO REFLECT DOWNWARD PRESSURE ON ADJUSTED BCA

The negative outlook on the long-term deposit and senior unsecured debt ratings reflects Moody's view that the weak operating environment for banks in Germany could undermine the overall strength of Germany's cooperative banking sector, resulting in reduced affiliate support for DZ BANK and a lower Adjusted BCA and ratings.

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

As indicated by the negative outlook, upward pressure on the ratings is currently unlikely. An upgrade of DZ BANK's ratings could be triggered by an improvement in the cooperative sector's financial strength which may result in a higher Adjusted BCA of DZ BANK. As long as the sector's financial strength does not improve, it would take a multi-notch upgrade of the bank's BCA which would in turn require a significant joint improvement of DZ BANK's key financial ratios, for an upgrade of DZ BANK's ratings because a single-notch upgrade of DZ BANK's BCA would likely be balanced by a reduction in affiliate support uplift. Additional rating uplift from Moody's Advanced LGF analysis could only occur for junior senior unsecured and lower ranking instruments. With three notches of rating uplift over the Adjusted BCA the bank's deposit and senior unsecured debt ratings already benefit from the highest-possible LGF result.

An upgrade of DZ BANK's BCA could be prompted by a reduction in higher-risk asset concentrations, in combination with a sustainable improvement in its profitability and a further improvement in its capitalisation and risk-weighted capital ratios.

A downgrade of DZ BANK's ratings could arise from a downgrade of its BCA, or of its Adjusted BCA in case the cooperative sector's financial strength deteriorates, or if the bank issued less debt designed to absorb losses in bail-in compared with its total banking assets than the rating agency currently anticipates.

DZ BANK's baa2 BCA could be downgraded if substantial unexpected risks were to emerge from its commercial banking activities, or if the group's loss-absorption capacity through capital and profits were to materially decrease.

LIST OF AFFECTED RATINGS

Issuer: DZ BANK AG

..Affirmations:

- ...Adjusted Baseline Credit Assessment, Affirmed a2
- ...Baseline Credit Assessment, Affirmed baa2
- ...LT Counterparty Risk Assessments, Affirmed Aa1(cr)
- ...ST Counterparty Risk Assessments, Affirmed P-1(cr)
- ...LT Counterparty Risk Ratings, Affirmed Aa1
- ...ST Counterparty Risk Ratings, Affirmed P-1

...LT Senior Unsecured Bond/Debenture, Affirmed Aa1, Outlook Remains Negative

...LT Senior Unsecured Medium-Term Note Program, Affirmed (P)Aa1

...LT Issuer Ratings, Affirmed Aa1, Outlook Remains Negative

...ST Issuer Ratings, Affirmed P-1

...LT Bank Deposit Ratings, Affirmed Aa1, Outlook Remains Negative

...ST Bank Deposit Ratings, Affirmed P-1

...Subordinate Regular Bond/Debenture, Affirmed A3

...Subordinate Medium-Term Note Program, Affirmed (P)A3

...Commercial Paper, Affirmed P-1

...Other Short Term Program, Affirmed (P)P-1

Downgrades:

...Junior Senior Unsecured Regular Bond/Debenture, Downgraded to A2 from A1

...Junior Senior Unsecured Medium-Term Note Program, Downgraded to (P)A2 from (P)A1

Outlook Action:

...Outlook, Remains Negative

..Issuer: DZ BANK AG, New York Branch

Affirmation:

.Commercial Paper, Affirmed P-1

Outlook Actions:

...No outlook assigned

PRINCIPAL METHODOLOGY

The principal methodology used in these ratings was Banks Methodology published in November 2019 and available at https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_1147865. Alternatively, please see the Rating Methodologies page on www.moodys.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.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_79004.

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Moody's general principles for assessing environmental, social and governance (ESG) risks in our credit analysis can be found at https://www.moody.com/researchdocumentcontentpage.aspx?docid=PBC_1133569.

At least one ESG consideration was material to the credit rating action(s) announced and described above.

REFERENCES/CITATIONS

[1] Company Annual Report 31-Dec-2019

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