FitchRatings

RATING ACTION COMMENTARY

Fitch Affirms Swiss Raiffeisen Group and Raiffeisen Schweiz 'A+'; Outlook Stable

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Fitch Ratings - London - 03 Jul 2024: Fitch Ratings has affirmed the Long-Term Issuer Default Ratings (IDR) of Swiss Raiffeisen Group and the members of its mutual-support mechanism, including Raiffeisen Schweiz Genossenschaft and the 218 local cooperative banks, at 'A+' with Stable Outlooks and Short-Term IDRs at 'F1'. Raiffeisen Group's Viability Rating (VR) has been affirmed at 'a+'. A full list of rating actions is below.

Fitch has also withdrawn the ratings of one local cooperative bank following its merger with one other member of the group.

KEY RATING DRIVERS

Swiss Retail Cooperative Group: Raiffeisen Group comprises 218 local banks and Raiffeisen Schweiz, the group's central institution. Its ratings are underpinned by the group's strong domestic franchise in retail and SME banking. They also reflect the group's conservative risk appetite with a loan portfolio dominated by Swiss residential mortgage loans, resulting in much better asset quality metrics than most international peers. The ratings also factor in the group's improved profitability, strong capitalisation and stable funding profile.

Mutual Support Underpins Ratings: The IDRs of Raiffeisen Schweiz and the local banks are group ratings and in line with Raiffeisen Group's IDRs. This is because Raiffeisen Group is a banking network, not a legal entity. The network's cohesion is underpinned by its mutual-support mechanism, which includes a solidarity fund to support failing banks and a cross-guarantee between the local banks and Raiffeisen Schweiz, to which the local banks are liable for up to the amount of their equity.

No creditor of any member bank has suffered losses since the establishment of the group. Raiffeisen Group is supervised as a group by the Swiss regulator, which does not set individual capital requirements for the local banks, and under its resolution plan the group will be resolved as one. Local banks operate predominantly in their geographic

region, focusing on retail and SME clients, whereas Raiffeisen Schweiz is responsible for the group's strategy and oversight of the local banks' risk profiles and acts as the group's central bank.

Large Swiss Housing Exposure: Raiffeisen Group has a strong record in managing credit risks, but the group is highly exposed to the residential real estate sector, as mortgage loans account for about 95% of gross loans. Over half of Raiffeisen Group's credit exposure is to owner-occupied homes, but exposure to real estate investments, including buy-to-let mortgages, is material. Switzerland's strong economic fundamentals and Raiffeisen Group's conservative underwriting standards mitigate risks from this concentrated exposure. The group's asset quality remained strong in 2023 and we expect its gross impaired loan ratio to stay well below 1% in the next two years.

Stable Profitability: We expect Raiffeisen Group's operating profit/risk-weighted assets (RWAs) ratio to stabilise at around 1.5% in the next two years, supported by predictable revenue streams and costs and low loan impairment charges. Profitability has improved in the past five years but remains moderate and less diversified than international peers. Net interest income accounts for about three-quarters of its revenue on average and is sustained by the low elasticity of the local banks' deposit base. The group has been expanding its fee-generating businesses, including the sale of investment products, and plans to increase the proportion of non-interest income to over 30% of revenue.

Strong Capitalisation: The group's common equity Tier 1 (CET1) ratio of 22.5% at end-March 2023 is higher than that of most peers. Internal capital generation is underpinned by low payout ratios to its cooperative members, which averaged 8% over the past five years. At the same time, the group's cooperative structure results in a weaker ability to raise core equity in the capital markets, in case of need, compared with listed peers.

Sound Deposit Franchise: The group benefits from a large and stable granular customer deposit base, which represented just over 80% of funding at end-2023. The group regularly refinances mortgage loans through the issuance of covered bonds via the Swiss central mortgage institution Pfandbriefbank schweizerischer Hypothekarinstitute AG, and Raiffeisen Schweiz regularly issues unsecured bonds, including bail-in bonds.

RATING SENSITIVITIES

Factors that Could, Individually or Collectively, Lead to Negative Rating Action/Downgrade

The most likely trigger of a downgrade of Raiffeisen Group's VR and IDRs would be a material deterioration of the group's asset quality in conjunction with weakening capitalisation, which could arise from a sharp and prolonged downturn in the Swiss housing market. A persistent increase in the group's gross impaired loan ratio to above

2% or a material decline of the group's CET1 capital ratio below 16% without any action taken to restore it to this level within 12 months would put Raiffeisen Group's ratings under pressure.

A downgrade of Raiffeisen Group's IDRs would result in a downgrade of Raiffeisen Schweiz's and the local banks' IDRs.

Factors that Could, Individually or Collectively, Lead to Positive Rating Action/Upgrade

An upgrade of Raiffeisen Group's VR and Long-Term IDR would require a material and sustained improvement in operating profitability, with the four-year average operating profit/risk-weighted assets ratio above 3% and successful execution of the group's strategic plan to increase the proportion of non-interest revenue.

An upgrade of Raiffeisen Group's IDRs would result in an upgrade of Raiffeisen Schweiz's and the local banks' IDRs.

OTHER DEBT AND ISSUER RATINGS: KEY RATING DRIVERS

Raiffeisen Group's 'F1' Short-Term IDR is the lower of the two ratings that maps to a 'A+' Long-Term IDR. This reflects our assessment of the group's funding and liquidity, to which we assign an 'a+' score.

Raiffeisen Schweiz is the sole issuer of capital-market instruments in the cooperative banking group.

The senior preferred bonds are rated one notch above Raiffeisen Schweiz's Long-Term IDR because Fitch expects creditors to be protected by Raiffeisen Group's buffer of 'bail-in bonds' and additional Tier 1 (AT1) instruments. As Switzerland's second-largest banking group, Raiffeisen Group is required to maintain a buffer of gone-concern capital, excluding senior preferred debt, which will protect senior preferred creditors in a resolution.

The 'F1+' rating on Raiffeisen Schweiz's certificates of deposits (CD) issuance programme reflects the protection provided to preferred creditors by the group's resolution buffers.

Raiffeisen Schweiz's senior non-preferred debt (bail-in bonds) are rated in line with the Long-Term IDR. Fitch views these bonds as senior non-preferred liabilities of the issuer, which under their terms rank behind senior obligations.

Raiffeisen Schweiz's AT1 notes are notched down four times from Raiffeisen Group's VR, twice each for loss severity and for incremental non-performance risk, in line with Fitch's baseline notching for AT1 instruments. We use Raiffeisen Group's VR as the anchor rating because we believe that the group will protect Raiffeisen Schweiz's viability, including by ensuring that regulatory capital requirements are met at all times. The AT1 notes are also protected by Raiffeisen Group's cross-guarantee scheme.

Raiffeisen Schweiz's distributable reserves of CHF230.4 million at end-2023 provide a sufficient buffer to cover the coupon payment of the bank's outstanding and new AT1 notes. With a going-concern capital ratio of 19.1% at end-1Q24, Raiffeisen Group has also a comfortable buffer over its regulatory requirement (14.6%) and over the notes' 7% CET1 loss absorption trigger, which could trigger the notes' full or partial write-down. Raiffeisen Group has a strong retail deposit franchise, and liquidity is fungible within the group. Because of this, we view the likelihood of the group requesting state support to fill a funding or liquidity gap as minimal.

The Government Support Rating (GSR) of 'ns' reflects our view that senior creditors cannot rely on receiving full extraordinary sovereign support in the event that RG becomes non-viable. This is because Swiss legislation and regulation to address the 'too-big-to-fail' problem for large Swiss banks is in place, and would require senior creditors to bear losses ahead of any potential extraordinary sovereign support. The country's large banking system relative to GDP has provided strong incentives to implement legislation in this respect. We are therefore of the view that resolution legislation in Switzerland is sufficiently progressed to resolve even a large Swiss group, and resolution legislation becomes the overriding factor and all other factors are therefore scored as 'low importance'.

OTHER DEBT AND ISSUER RATINGS: RATING SENSITIVITIES

Raiffeisen Group's Short-Term IDR would be upgraded if the group's funding and liquidity score was upgraded to 'aa-' or if Raiffeisen Group's Long-Term IDR was upgraded.

The senior preferred and senior non-preferred debt ratings are sensitive to a change in Raiffeisen Schweiz's Long-Term IDR and ultimately to a change in Raiffeisen Group's Long-Term IDR. The senior preferred, senior non-preferred debt and CD issuance programme ratings could also be downgraded if Fitch concludes that recovery prospects for senior non-preferred creditors weaken, or if the buffer is no longer sufficient to protect senior preferred creditors.

The AT1 notes' rating is sensitive to a change in Raiffeisen Group's VR. In addition, the notes could be downgraded if non-performance risk increases relative to the risk

captured in Raiffeisen Group's VR, for example if Raiffeisen Group's capitalisation or leverage decline close to its transitional regulatory requirements or if Raiffeisen Schweiz's available distributable items, including the full year profit, decline below CHF100 million.

We would only upgrade RG's GSR if we believe the sovereign has a rising propensity to support systemically important banks, which is highly unlikely in the current regulatory environment.

VR ADJUSTMENTS

The earnings and profitability score of 'a-' has been assigned above the 'bbb' category implied score due to the following adjustment reason: earnings stability (positive).

The capitalisation and leverage score of 'a+' has been assigned below the 'aa' category implied score due to the following adjustment reason: capital flexibility and ordinary support (negative).

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.

ESG CONSIDERATIONS

The highest level of ESG credit relevance is a score of '3', unless otherwise disclosed in this section. A score of '3' 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. Fitch's ESG Relevance Scores are not inputs in the rating process; they are an observation on the relevance and materiality of ESG factors in the rating decision. For more information on Fitch's ESG Relevance Scores, visit https://www.fitchratings.com/topics/esg/products#esg-relevance-scores.

VIEW ADDITIONAL RATING DETAILS

FITCH RATINGS ANALYSTS

Maria Shishkina
Director
Primary Rating Analyst
+44 20 3530 1379
maria.shishkina@fitchratings.com

Fitch Ratings Ltd
30 North Colonnade, Canary Wharf London E14 5GN

Marco Diamantini
Director
Secondary Rating Analyst
+49 69 768076 114
marco.diamantini@fitchratings.com

Christian Kuendig
Managing Director
Committee Chairperson
+44 20 3530 1399
christian.kuendig@fitchratings.com

MEDIA CONTACTS

Peter Fitzpatrick
London
+44 20 3530 1103
peter.fitzpatrick@thefitchgroup.com

Additional information is available on www.fitchratings.com

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APPLICABLE CRITERIA

Bank Rating Criteria (pub. 15 Mar 2024) (including rating assumption sensitivity)

ADDITIONAL DISCLOSURES

Dodd-Frank Rating Information Disclosure Form

Solicitation Status

Endorsement Policy

ENDORSEMENT STATUS

Banca Raiffeisen Basso Ceresio societa cooperativa	UK Issued, EU I
Banca Raiffeisen Bellinzonese e Visagno societa cooperativa	UK Issued, EU I
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Banca Raiffeisen Losone Pedemonte Vallemaggia societa cooperativa	UK Issued, EU I
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Banca Raiffeisen Mendrisio e Valle di Muggio societa cooperativa	UK Issued, EU I
Banca Raiffeisen Morbio-Vacallo societa cooperativa	UK Issued, EU I
Banca Raiffeisen Piano di Magadino societa cooperativa	UK Issued, EU I
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