

Research Update:

# Switzerland-Based Bank Raiffeisen Schweiz Genossenschaft Rated 'A+/A-1'; Outlook Stable

September 21, 2020

## Overview

- Raiffeisen Schweiz Genossenschaft (RCH) is a core group member of Swiss Cooperative Raiffeisen Group (Swiss Raiffeisen Group), benefiting from mutual solidarity support and joint risk management, with a solid No.3 market position in Swiss retail markets.
- Swiss Raiffeisen Group has a sound financial profile, supported by high collateralizations and prudent underwriting standards, and underpinned by superior capitalization due to stable earnings retention.
- However, Swiss Raiffeisen Group's subpar profitability and efficiency by international standards is further pressured by COVID-19 and a lower-for-longer interest rate environment.
- Moreover, the group has a high cost base, mainly attributable to a decentralized network, and the need to further invest in digitalization, as well as high concentration risks from exposures in domestic residential real estate, which would make the group sensitive to potential deterioration of the Swiss housing market.
- We are assigning our 'A+/A-1' ratings to RCH with a stable outlook.

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## Rating Action

On Sept. 21, 2020, S&P Global Ratings assigned its 'A+/A-1' issuer credit ratings to Raiffeisen Schweiz Genossenschaft (RCH). The outlook is stable.

## Outlook

The outlook reflects our expectation that RCH will remain a core group member of Swiss Cooperative Raiffeisen Group (Swiss Raiffeisen Group) over the next two years and that Swiss Raiffeisen Group will preserve its robust financial position, despite the weakened operating conditions and Swiss recession amid the COVID-19 pandemic. We forecast that Swiss Raiffeisen Group will remain sufficiently profitable to maintain its superior capitalization as indicated by our 20%-21% risk-adjusted capital (RAC) ratio through 2022 and despite strong pressure on interest

margins and risk cost increases.

## **Downside scenario**

We could lower our rating on RCH if the operating environment, particularly for the Swiss housing market, deteriorates materially further or if the expected start to market recovery is delayed beyond 2021, leading to a more pronounced setback to Swiss Raiffeisen Group's profitability and asset quality, as indicated by the level of nonperforming loans (NPLs) and risk costs. We would also consider a downgrade if Swiss Raiffeisen Group's targeted efficiency and digitalization improvements program prove unsuccessful, while interest rates and competitive pressure rise.

## **Upside scenario**

An upgrade is unlikely, reflecting the high level of the current rating and the bank's material concentration in the housing market.

An upgrade would require sustainable and substantial improvements in addressing Swiss Raiffeisen Group's structural weaknesses, such as cost efficiency and earnings diversification compared with similarly rated Swiss or international peers.

We could review our assessment of the remoteness of raising the ratings on the bank and the preferred senior obligations once regulatory authorities consider Swiss Raiffeisen Group's resolution plan effective. If we conclude that Swiss Raiffeisen Group has sufficient amounts of bail-in-able instruments, such as Tier 1, Tier 2, and subordinated instruments, the group can qualify for additional loss absorbing capital (ALAC) uplift. At the same time, we would most likely offset such an uplift with a negative rating adjustment factor, given the stronger rating fundamentals of higher-rated peers.

## **Rationale**

We derive our rating on RCH from our view of its core group status to the Swiss Raiffeisen Group and our assessment of the latter's leading retail market position with an 17.6% market share in residential real estate financing throughout Switzerland. We expect Swiss Raiffeisen Group to successfully defend its franchise against increasing competition based on growth initiatives under its "Raiffeisen 2025" strategy, and consider its digitalization "follower" strategy, spurred by the entire group, as a positive factor.

Swiss Raiffeisen Group enters the current recession from a position of strength after having bolstered its financial and liquidity profile with stable core business performance, improving risk metrics, and increased retail deposits. In particular, we consider substantial improvements in corporate governance, joint risk management, and groupwide business initiatives in recent years.

As its central institution, we expect RCH will remain core for Swiss Raiffeisen Group's strategy, whose consolidated creditworthiness (group credit profile; GCP) draws on the strong domestic retail positions of local Raiffeisen banks. We regard the group as a cohesive economic entity and expect solidarity support among member banks--if ever needed--in a crisis, which also takes into account regulators' group-based oversight, a groupwide mutual guarantee scheme, as well as a strong track record of more than a century of support for group members.

In our view, Swiss Raiffeisen Group's main weaknesses remain its subpar profitability and high cost base compared with international peer groups. Efficiency is a weakness, as indicated by a 67% cost-to-income ratio at midyear 2020, which is materially weaker than that of most

international peers. Return on average common equity was 4.9% at year-end 2019, which is relatively low by international standards, but, this also owes to Swiss Raiffeisen Group's superior capitalization. Our 20.6% RAC ratio was well above that of many international banks at year-end 2019, and facilitated by Swiss Raiffeisen Group's policy of very high earnings retention.

Despite Swiss Raiffeisen Group's intensified strategic efficiency measures and digitalization efforts, we forecast only gradual medium-term improvements, reflecting the complexities of its decentralized network, as well as elevated regulatory and information technology investment requirements. What is more, we continue to see severe earnings pressure from Swiss Raiffeisen Group's dominance in low-risk, but also low-margin, residential real estate business, which we project will suffer from a lower-for-longer interest rate environment until at least 2023, as well as hefty competition. Although we acknowledge Swiss Raiffeisen Group's recent efforts to diversify its income stream, such as boosting by 13% its client assets under management, this will take time given it is starting from underdeveloped low levels. Compared with peers, the group has by far the highest concentration on interest income, and we do not expect this to change in the medium term.

Swiss Raiffeisen Group reported solid midyear 2020 results, posting Swiss franc (CHF) 444 million pretax profits only mildly below its midyear 2019 results, and despite prudently allocating CHF75 million into capital reserves for pandemic-related potential risk-cost increases later this year. The abruptly worsened economic environments across Europe in the wake of the COVID-19 pandemic is the main cause of our weaker medium-term forecasts for Swiss Raiffeisen Group, specifically in terms of its temporary negative fallout on earnings, NPLs, and asset quality through 2021 and into early 2022.

At the same time, relative to many international peers, we expect Swiss Raiffeisen Group's profitability to be more resilient and that a potential rise in risk costs will be more contained. This owes to our view on the group's domicile and lending focus, Switzerland, and our forecast that Switzerland and its residential real estate market will perform relatively well through the crisis (see "Government Job Support Will Stem European Housing Market Price Falls," published on May 15, 2020, and "COVID-19: Swiss Banking Sector To Remain Resilient," published on June 17, 2020, both published on RatingsDirect).

We see Swiss Raiffeisen Group's risk profile in line with that of peers operating in Switzerland and other countries with similar economic risks, benefitting from the current robustness of the Swiss real estate sector, strong collateralization of the bank's lending, and prudent underwriting standards that currently mitigate our concerns on Swiss Raiffeisen Group's substantial tail risk from massive concentration in Switzerland's residential mortgage markets.

We expect Swiss Raiffeisen Group's funding and its liquidity profile to remain sound, materially benefitting from the Raiffeisen banks' dominant share of granular retail deposits generated under its robust, well-established franchise. Orchestrated by the central institution RCH, we expect the stability of the group's retail deposits and the diversification of the funding tools will remain well balanced relative to the typically long-term nature of the member banks' loan books. For example, Swiss Raiffeisen Group's main indicators of 103% loan-to-deposit ratio and 106% stable funding ratio at year-end 2019 are close to the sound median for Swiss banks. We note that core customer deposits grew by 6% in the first half of 2020, indicating customer confidence in the difficult COVID-19 environment.

RCH's prudent management and level of liquidity, represented by its 1.6x ratio of broad liquid assets to short-term wholesale funding is another positive factor. However, although such a ratio can be indicative of superior strength, we think that Swiss Raiffeisen Group's low diversification of funding sources with very high reliance on customer deposits, most of which are short term, prevents a better assessment of liquidity for the group. Although we acknowledge that customers

have historically maintained their deposits in the bank, a potential outflow could quickly deplete the group's superior buffer, given relatively low coverage of short-term customer deposits by liquid assets, as indicated by our net broad liquid assets-to-short-term customer deposits ratio of just 12% at year-end 2019.

## Ratings Score Snapshot

Issuer Credit Rating	A+/Stable/A-1
SACP	a+
Anchor	a-
Business Position	Adequate (0)
Capital and Earnings	Very Strong (+2)
Risk Position	Adequate (0)
Funding	Average
and Liquidity	Adequate (0)
Support	(0)
ALAC Support	(0)
GRE Support	(0)
Group Support	(0)
Government Support	(0)
Additional Factors	(0)

SACP--Stand-alone credit profile.

## Related Criteria

- General Criteria: Hybrid Capital: Methodology And Assumptions, July 1, 2019
- General Criteria: Group Rating Methodology, July 1, 2019
- Criteria | Financial Institutions | General: Risk-Adjusted Capital Framework Methodology, July 20, 2017
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- Criteria | Financial Institutions | Banks: Bank Rating Methodology And Assumptions: Additional Loss-Absorbing Capacity, April 27, 2015
- Criteria | Financial Institutions | Banks: Quantitative Metrics For Rating Banks Globally: Methodology And Assumptions, July 17, 2013
- Criteria | Financial Institutions | Banks: Banking Industry Country Risk Assessment Methodology And Assumptions, Nov. 9, 2011
- Criteria | Financial Institutions | Banks: Banks: Rating Methodology And Assumptions, Nov. 9, 2011

## Related Research

- Banking Industry Country Risk Assessment: Switzerland, Nov. 20, 2019
- Tech Disruption In Retail Banking: Swiss Banks Are In No Rush To Become Digital Frontrunners; Feb. 13, 2020

## Ratings List

### New Rating;

#### **Raiffeisen Schweiz Genossenschaft**

Issuer Credit Rating A+/Stable/A-1

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at [www.standardandpoors.com](http://www.standardandpoors.com) for further information. A description of each of S&P Global Ratings' rating categories is contained in "S&P Global Ratings Definitions" at [https://www.standardandpoors.com/en\\_US/web/guest/article/-/view/sourceId/504352](https://www.standardandpoors.com/en_US/web/guest/article/-/view/sourceId/504352) Complete ratings information is available to subscribers of RatingsDirect at [www.capitaliq.com](http://www.capitaliq.com). All ratings affected by this rating action can be found on S&P Global Ratings' public website at [www.standardandpoors.com](http://www.standardandpoors.com). Use the Ratings search box located in the left column. Alternatively, call one of the following S&P Global Ratings numbers: Client Support Europe (44) 20-7176-7176; London Press Office (44) 20-7176-3605; Paris (33) 1-4420-6708; Frankfurt (49) 69-33-999-225; Stockholm (46) 8-440-5914; or Moscow 7 (495) 783-4009.

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