FITCH AFFIRMS 6 GERMAN DEVELOPMENT BANKS AT 'AAA'; OUTLOOK STABLE

Fitch Ratings-Frankfurt/London-31 January 2018: Fitch Ratings has affirmed the Long- and Short-Term Issuer Default Ratings (IDRs) of six German development banks at 'AAA' and 'F1+' respectively. The Outlooks on the Long-Term IDRs are Stable. The Support Ratings (SRs) have been affirmed at '1'. A full list of rating actions is at the end of this rating action commentary.

The peer review includes KfW, Landwirtschaftliche Rentenbank (Rentenbank), NRW.BANK, Investitionsbank Berlin (IBB), Investitionsbank Schleswig-Holstein (IB.SH), and Landeskreditbank Baden-Wuerttemberg - Foerderbank (L-Bank).

KfW and Rentenbank both benefit from an explicit guarantee from the Federal Republic of Germany (AAA/Stable). Consequently, Fitch has also affirmed their Support Rating Floors (SRF) at 'AAA'.

NRW.BANK, IBB, IB.SH and L-Bank are owned by the respective German federal states where they are located and operate. The banks benefit from guarantees from the federal states. The ratings and Fitch's view of the creditworthiness of the German federal states reflect the stability and sustainability of the solidarity system for German federal states.

KEY RATING DRIVERS
IDRs, SENIOR DEBT, SRs AND SRFs
The banks' IDRs, senior debt ratings, SRs and for KfW and Rentenbank, SRFs, are based on Fitch's view of an extremely high likelihood of support from the entities' respective owners. The banks' policy roles as well as the formal support arrangements in place between the banks and their ultimate owners or guaranteeing federal states have a high influence on our assessment of support.

Fitch does not assign Viability Ratings to these banks as their business models are entirely dependent on the support of their state guarantors. The key rating drivers below also apply to the KfW's, Rentenbank's and NRW.BANK's market-linked securities' ratings.

KfW
KfW is 80%-owned by Germany, with the remainder of shares held by the German federal states. The institution was established in 1948 and is the largest development bank in Europe. Its obligations are backed by a direct and unlimited statutory guarantee from Germany. Based on the maintenance obligation (Anstaltslast), Germany is committed to safeguarding the economic basis of KfW and ensuring that its operations can continue in the event of financial difficulty. The bank undertakes a broad range of activities including SME lending via commercial banks, retail, housing, municipal and social infrastructure lending, as well as certain capital market activities and lending in developing countries. Commercial activities in the area of export and project financing are carried out through KfW's wholly-owned subsidiary KfW IPEX-Bank GmbH, which is legally independent and excluded from the state guarantees.

KfW increased its promotional activities by 2% to a record EUR81 billion in 2016, reflecting its broad policy role. Despite this growth, rising risk costs led to lower net profit of around EUR2 billion in 2016 and we expect the bank's profitability to have declined in 2017. The transition to an IRB approach in 2017 has resulted in strengthened capital ratios, as evidenced by a common equity Tier 1 (CET1) ratio of 20.3% at end-3Q17.

Rentenbank

Rentenbank was established by federal law in 1949 and has the mandate to support the development of the agricultural sector and rural areas. The bank benefits from the Anstaltslast from Germany. In addition, all of the bank's liabilities are fully covered by the state through a direct and unlimited statutory guarantee that came into effect on 1 January 2014. As stipulated in its law, Rentenbank is insolvency remote and can only be dissolved by law.

In 2016, Rentenbank's new lending volume for special promotional loans amounted to EUR7.7 billion. This is still at historically high levels but slightly lower than in the previous year, reflecting challenging market conditions in the agricultural sector. Rentenbank's CET1 ratio had risen to 26.7% at end-1H17 (23.2% at end-2016), which compares well among its peers considering its inherent risks.

NRW.BANK

NRW.BANK provides funding for economic, social, environmentally friendly, municipal, infrastructure and housing promotion projects in North Rhine-Westphalia. The state wholly owns the bank and provides it with an explicit, irrevocable, unlimited and unconditional statutory first demand guarantee covering all liabilities. Moreover the bank benefits from Anstaltslast and a statutory guarantor's liability (Gewaehrtraegerhaftung).

NRW.BANK's total business volume has decreased significantly from its peak in 2009, but remained high at around EUR162 billion at end-2016. Nonetheless, net lending has been increasing steadily, reaching EUR11.2 billion in 2016. The bank reported a CET1 ratio of 41.8% at end-2016, one of the highest among its peers.

IBB

IBB benefits from an explicit unconditional statutory guarantee obligation covering all liabilities and Anstaltslast from Berlin. IBB focuses on a narrower range of development activities than peers as Berlin is a "city state" and therefore IBB is not active in financing municipalities' budgets or renewable energy projects, two areas of growth for other regional development banks in recent years. Fitch believes that the narrower range of promotional activities allows IBB to better focus its resources than other development banks. As a public law institution IBB is insolvency remote in accordance with state legislation.

Like its peers, IBB has benefited from increased demand for its promotional loans particularly in the housing and urban development segment. New financing commitments amounted to EUR1.7 billion in 2016 (EUR1.2 billion in 2015) but about one-third was attributable to the refinancing of the state-guaranteed Berlin Brandenburg airport project. Margins remain relatively low as the bank's beneficial wholesale funding costs, driven by its state support, are largely passed on to customers. IBB's regulatory capital and leverage ratios are adequate in view of the moderate risk in its balance sheet.

IB.SH

IB.SH provides funding for social, infrastructure and environmental projects, as well as for corporates, municipalities, affordable housing and energy-efficient real estate lending in SH. It also takes on special tasks on behalf of SH, which provides it with an explicit unconditional statutory guarantee obligation covering all liabilities, Anstaltslast and Gewaehrtraegerhaftung. In July 2016, the local legislation (Landesverwaltungsgesetz) was amended to ensure that IB.SH cannot be subject to insolvency procedures and can only be dissolved by law.

IB.SH's moderate but steady business growth over recent years reflects demand for long-term financing given low interest rates. Strong demand resulted in new lending of EUR2.4 billion in 2016. IB.SH's operating profit has been stable over the past three years. Interest income, IB.SH's main revenue source, and the level of its expected new promotional business are the key drivers of its profits, which currently benefit from low impairments and good cost discipline. IB-SH's capitalisation improved in 2016 as the bank increased its capital base by converting hidden reserves under German GAAP ("340f" reserves) into "340g" reserves (fund for general banking risks) that are part of CET1 capital. Its end-2016 leverage ratio rose to about 8% and its CET1 ratio to 17.3%.

L-Bank
L-Bank endorses home ownership, supports families and promotes small- and medium-sized companies through the provision of low interest rate loans in its operating region Baden-Wuerttemberg. The state wholly owns L-Bank and provides it with an explicit unconditional and irrevocable statutory guarantee obligation covering all liabilities, Anstaltslast and Gewaehrtraegerhaftung. BW is not rated by Fitch, but its creditworthiness is underpinned by the strength of the German solidarity system, which links BW's creditworthiness closely to that of Germany. As a public law institution L-Bank is insolvency remote as laid out in BW legislation.

L-Bank further strengthened its capital in 2016 and reported a CET1 ratio of 18% at the end of the year after increasing its new promotional lending volume to EUR10.6 billion in 2016 from EUR8.5 billion in the previous year. In 2016, L-Bank introduced a new development contribution system, which intends to channel accumulated earnings in a separate fund to subsidise future promotional activities. This led to a significant provision resulting in lower reported net interest income. A substantial profit from the reversal of a prior write-down of receivables helped the bank deliver a pre-tax profit in line with that of the previous year.

DERIVATIVE COUNTERPARTY RATINGS
We regard KfW, Rentenbank and NRW.BANK as notable derivative counterparties and assign them Derivative Counterparty Ratings (DCRs). The DCRs are in line with the banks' IDRs.

We do not believe that these state-guaranteed non-banks or institutions protected from insolvency proceedings by law could become subject to bail-in measures. Therefore, we consider it highly unlikely that they could become eligible for DCR uplifts even if their Long-Term IDRs were downgraded below 'AAA'.

SUBORDINATED DEBT AND OTHER HYBRID SECURITIES
Fitch rates the subordinated debt instruments of NRW.BANK and Rentenbank at the same level as their senior debt, as the agency believes that the support mechanisms for both banks provide the same degree of protection to both senior and subordinated debt instruments.

RATING SENSITIVITIES
IDRs, SENIOR DEBT, SRs AND SRFs
The banks' IDRs, senior debt ratings, SRs and SRFs ratings are sensitive to a change in Fitch's assumptions regarding support from their owners, specifically a downgrade of Germany, or a change in the terms of the state guarantees. The Stable Outlook on the banks' ratings mirrors that of Germany and reflects Fitch's view that neither of these scenarios is likely in the foreseeable future.

Fitch believes that the nature of the state support for German development banks is unlikely to change significantly in the medium term due to the strategic importance of these banks to the German economy and their entrenchment in the domestic financial system. The support structure was approved by the EU in 2002, although under competition law the banks may only engage in non-competitive activity. This also makes significant changes to the banks' business models unlikely in the medium term.

Following an amendment to the "Law concerning KfW" in 2013, KfW has been subject to key banking supervision standards under the German Banking Act and is supervised by the German Federal Financial Supervisory Authority in cooperation with the German central bank. However, this has not resulted in a change of KfW's special role as a promotional bank or a change in support for KfW.

Fitch views state support for development banks as unaffected by the German implementation of the BRRD or the Single Resolution Mechanism (SRM). Furthermore, we do not expect the debt brake established for the Bund and the Laender, which will require Laender to run their budgets from 2020 without taking on new debt, to constrain the ability of the states to provide support to their development banks if needed.

KfW's, Rentenbank's and NRW.BANK's market-linked securities' ratings are subject to the same sensitivities as the banks' IDR.

DCR
KfW, Landwirtschaftliche Rentenbank and NRW.BANK's DCRs are primarily sensitive to changes in the respective bank's Long Term IDR, which is driven by their support structures.

SUBORDINATED DEBT AND OTHER HYBRID SECURITIES
Rentenbank's and NRW.BANK's subordinated debt ratings are primarily sensitive to changes in the level of support provided to the bank by its owner.

The rating actions are as follows:

KfW
Long-Term IDR affirmed at 'AAA'; Outlook Stable
Short-Term IDR affirmed at 'F1+'
Senior unsecured and programme ratings affirmed at 'AAA'/'F1+'
Support Rating affirmed at '1'
Support Rating Floor affirmed at 'AAA'
Derivative Counterparty Rating affirmed at 'AAA(dcr)'
Market-linked securities affirmed at 'AAAemr'
Commercial paper affirmed at 'F1+'

Landwirtschaftliche Rentenbank
Long-Term IDR: affirmed at 'AAA'; Stable Outlook
Short-Term IDR: affirmed at 'F1+'
Senior unsecured ratings including programme ratings: affirmed at 'AAA' and 'F1+'
Support Rating: affirmed at '1'
Support Rating Floor: affirmed at 'AAA'
Derivative Counterparty Rating: affirmed at 'AAA(dcr)'
Market-linked securities: affirmed at 'AAAemr'
Commercial paper: affirmed at 'F1+'
Subordinated notes: affirmed at 'AAA'

NRW.BANK
Long-Term IDR: affirmed at 'AAA'; Stable Outlook
Short-Term IDR: affirmed at 'F1+'
Senior unsecured ratings including programme ratings: affirmed at 'AAA' and 'F1+'
Support Rating: affirmed at '1'
Derivative Counterparty Rating: affirmed at 'AAA(dcr)'
Market-linked securities: affirmed at 'AAAemr'
Commercial paper: affirmed at 'F1+'
Short-term certificates of deposit: affirmed at 'F1+'
Subordinated notes: affirmed at 'AAA'

Investitionsbank Berlin
Long-Term IDR: affirmed at 'AAA'; Stable Outlook
Short-Term IDR: affirmed at 'F1+'
Senior unsecured ratings: affirmed at 'AAA'
Support Rating: affirmed at '1'

Investitionsbank Schleswig-Holstein
Long-Term IDR: affirmed at 'AAA'; Stable Outlook
Short-Term IDR: affirmed at 'F1+'
Support Rating: affirmed at '1'
Senior unsecured rating: affirmed at 'AAA'

L-Bank
Long-Term IDR: affirmed at 'AAA'; Stable Outlook
Short-Term IDR: affirmed at 'F1+'
Support Rating: affirmed at '1'
Senior unsecured rating: affirmed at 'AAA'

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Applicable Criteria
Global Bank Rating Criteria (pub. 25 Nov 2016)
https://www.fitchratings.com/site/re/891051