

# Zuercher Kantonalbank

## Key Rating Drivers

Zuercher Kantonalbank's (ZKB) Issuer Default Ratings (IDRs) are driven by support from its guarantor and sole owner, the Canton of Zurich (AAA/Stable/F1+), and ZKB's Shareholder Support Rating (SSR) is equalised with the canton's Long-Term IDR. ZKB's Viability Rating (VR) reflects the bank's stable and resilient business model, conservative risk appetite, strong asset quality, funding and capitalisation and adequate profitability.

**Manageable Recapitalisation:** The canton guarantees all of ZKB's non-subordinated liabilities according to a specific cantonal law (ZKB Law). ZKB's balance sheet is large relative to the canton's budgetary resources, but Fitch Ratings believes the bank's stable and resilient business model, funding, and capital buffers mean that recapitalisation or liquidity support needs would be manageable in a realistic stress scenario.

**Timely Support Expected:** The canton's guarantee does not explicitly address the timeliness of support, but Fitch believes that, if necessary, support would be provided in a timely fashion, given ZKB's high importance for the canton and the potential repercussions of a failure for the Swiss financial sector. The canton's constitution also requires it to have a cantonal bank, making the institutional owner more likely to support the bank in financial distress.

**Strong Regional Franchise:** ZKB's leading franchise in deposit-taking and residential mortgage lending in the Canton of Zurich, where the bank's operations are concentrated, supports the VR. Geographic concentration is mitigated by Zurich's economic strength and the bank's diversified business activities covering retail and commercial banking. ZKB is also the third-largest fund provider and one of the largest asset managers in Switzerland.

**Material Real Estate Exposure:** ZKB's impaired loans ratio is very low compared with international peers. ZKB's main risk stems from a large real-estate exposure in Zurich, with 74% of end-2022 gross customer loans in residential mortgages. Fitch believes loan quality would be resilient to a significant decline in property values due to the bank's strict credit standards and moderate overall loan-to-value ratios.

**Improving Earnings:** Our assessment of ZKB's profitability reflects its long record of adequate, stable, and fairly diversified earnings despite a material share of trading income in the bank's revenue. Operating profitability (1.4% of risk-weighted assets (RWAs) in 2022) is benefitting from rising interest rates and we expect it to increase further this year.

**Strong Capitalisation:** ZKB's common equity Tier 1 (CET1) ratio remained strong at 16.8% at end-2022, despite strong loan growth. The canton's guarantee covers half of ZKB's gone-concern capital requirement, which will be fully phased in at 7.86% in 2026. The remaining gap will be covered with bail-in debt the bank started issuing this year.

**Very Stable Funding:** ZKB's funding is underpinned by a large, and mostly granular, deposit base despite some more concentrated corporate and institutional deposits. Customer deposits account for over half of non-equity funding and almost cover the full volume of loans. Wholesale funding needs are moderate and benefit from the bank's cantonal guarantee, due to which investors perceive ZKB as a safe haven in times of increased market uncertainty.

**Recovery and Resolution Plan:** As a domestic systemically important bank, ZKB has a recovery and resolution plan to be approved by the Swiss banking supervisor (FINMA), according to which, to recapitalise ZKB the canton could be required to provide CHF3 billion of capital, which is large relative to its own resources. We believe the provision of this capital would be manageable for the canton given its strong financial position, and would not on its own drive negative action on the canton's ratings, or trigger a reassessment of our support assumptions.

## Ratings

Foreign Currency	
Long-Term IDR	AAA
Short-Term IDR	F1+
Viability Rating	a+
Shareholder Support Rating	aaa

## Sovereign Risk (Switzerland)

Long-Term Foreign-Currency IDR	AAA
Long-Term Local-Currency IDR	AAA
Country Ceiling	AAA

## Outlooks

Long-Term Foreign-Currency IDR	Stable
Sovereign Long-Term Foreign-Currency IDR	Stable
Sovereign Long-Term Local-Currency IDR	Stable

## Applicable Criteria

[Bank Rating Criteria \(September 2022\)](#)

## Related Research

[Fitch Affirms Zuercher Kantonalbank at 'AAA'; Outlook Stable \(April 2022\)](#)

[Fitch Affirms Switzerland at 'AAA'; Outlook Stable \(November 2022\)](#)

[Global Economic Outlook \(March 2023\)](#)

[Fitch Affirms Canton of Zurich at 'AAA'; Outlook Stable \(November 2022\)](#)

## Analysts

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## Rating Sensitivities

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

A downgrade of the Canton of Zurich's IDRs would result in a downgrade of ZKB's IDRs and SSR. A material increase in the canton's contingent liabilities, which are dominated by ZKB, could put pressure on the canton's and ZKB's IDRs and SSR. Contingent liabilities could increase, for instance because of sustained growth in the bank's balance sheet in excess of the canton's GDP growth, or due to a material delay by the canton in promptly addressing a potential capital shortfall at ZKB.

ZKB's IDRs and SSR are also sensitive to changes to the bank's relationship with the canton, especially if the ZKB Law is amended in a way that would weaken the guarantee's effectiveness or cast doubt on the timeliness of support. However, we view this scenario as unlikely.


The VR would likely be downgraded if large real estate-related losses, which could arise from a sharp drop in residential property prices in Zurich, led to a CET1 materially below 16%, or an impaired loans ratio durably above 2%. The rating would also come under pressure if profitability deteriorated durably, or if the bank increased its risk appetite, which could be indicated by higher loan growth or by greater exposure to interest-rate risk in the loan book.

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

As the Long-Term IDR is already at the highest level on Fitch's scale, it cannot be upgraded.

An upgrade of the VR is unlikely given the concentration of ZKB's business model on the Canton of Zurich, resulting in a large exposure to the local property market. An upgrade would also require an improvement in the bank's profitability.

**Ratings Navigator**

Zuercher Kantonalbank							ESG Relevance: 	Banks Ratings Navigator		
Operating Environment	Business Profile	Risk Profile	Financial Profile				Implied Viability Rating	Viability Rating	Shareholder Support Rating	Issuer Default Rating
			Asset Quality	Earnings & Profitability	Capitalisation & Leverage	Funding & Liquidity				
	20%	10%	20%	15%	25%	10%	aaa	aaa	aaa	AAA Sta
aaa							aaa	aaa	aaa	AAA Sta
aa+							aa+	aa+	aa+	AA+
aa							aa	aa	aa	AA
aa-							aa-	aa-	aa-	AA-
a+							a+	a+	a+	A+
a							a	a	a	A
a-							a-	a-	a-	A-
bbb+							bbb+	bbb+	bbb+	BBB+
bbb							bbb	bbb	bbb	BBB
bbb-							bbb-	bbb-	bbb-	BBB-
bb+							bb+	bb+	bb+	BB+
bb							bb	bb	bb	BB
bb-							bb-	bb-	bb-	BB-
b+							b+	b+	b+	B+
b							b	b	b	B
b-							b-	b-	b-	B-
ccc+							ccc+	ccc+	ccc+	CCC+
ccc							ccc	ccc	ccc	CCC
ccc-							ccc-	ccc-	ccc-	CCC-
cc							cc	cc	cc	CC
c							c	c	c	C
f							f	f	ns	D or RD

The Key Rating Driver (KRD) weightings used to determine the implied VR are shown as percentages at the top. In cases where the implied VR is adjusted upwards or downwards to arrive at the VR, the KRD associated with the adjustment reason is highlighted in red. The shaded areas indicate the benchmark-implied scores for each KRD.

Note: Since our latest review of ZKB, Switzerland's operating environment score was downgraded to 'aa-/stable' from 'aa/stable' in March 2023.

**VR - Adjustments to Key Rating Drivers**

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).

The funding and liquidity score of 'aa' has been assigned above the 'a' category implied score, due to the following adjustment reasons: deposit structure (positive) and liquidity access and ordinary support (positive).

## Company Summary and Key Qualitative Factors

### Business Profile

ZKB is the largest cantonal bank in Switzerland. It will become the third-largest banking group by assets in the country if the acquisition of Credit Suisse Group AG (CS; BBB/RWE) by UBS Group AG (UBS; A+/RWN) is completed as planned. ZKB's public mandate, set out in the ZKB Law, governs its focus on the Zurich region. The law prescribes the bank's activities, focused on providing full banking services to local households and SMEs, as well as helping the canton's economic and social development by supporting access to residential property. Accordingly, ZKB operates the densest branch network in the Canton of Zurich and has a leading regional franchise, with market shares between 30% and 40% in retail deposits and mortgage lending.

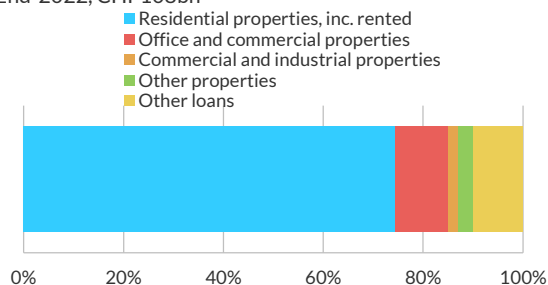
Beyond Zurich, ZKB mostly lends to Swiss SMEs and export-focused companies, but the bank's national-level market shares are modest. ZKB is also the third-largest fund provider in the country and one of the largest asset managers in Switzerland, with CHF335 billion of assets under management at end-2022. The bank's domestic and international private-banking franchise remains niche.

While we believe the acquisition of CS by UBS will offer growth opportunities for ZKB, particularly in investment and asset management and corporate banking with larger companies, this would not fundamentally change our assessment of ZKB's business profile given the regional mandate of the bank, high market shares locally and already reasonably diversified business model factored into our assessment.

The bank's cantonal owners maintain good oversight of ZKB's activities, including through board representation, and the bank is ultimately supervised by the canton's parliament. In combination with the ZKB Law, this helps to support the stability of ZKB's business model and strategy, also constraining the bank's ability to expand its business activities. This has delivered a stable through-the-cycle performance record. At the same time, we estimate that ZKB's management is independent and not subject to undue political influence.

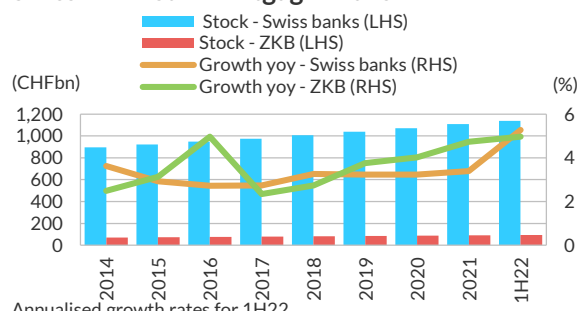
### Loan Portfolio Split

End-2022, CHF108bn



Source: Fitch Ratings, ZKB

### Swiss Domestic Mortgage Loans



Source: Fitch Ratings, ZKB, SNB

### Risk Profile

ZKB's public mandate drives the bank's conservative risk appetite. We consider ZKB's underwriting standards to be low-risk and conservative, to the benefit of its stable and sound loan quality. The bank is proactive in tightening its lending policies based on market changes. ZKB also bases its loan-to-value calculations on indexed property values, providing an extra buffer in the event of a significant market price correction. ZKB has limited risk appetite for commercial real estate lending outside the residential sector.

ZKB pursues organic growth in its investment and asset-management business to further strengthen its income diversification and to reduce the share of net interest income (NII) to less than 50% of total operating income. We believe the bank's expertise is sufficiently advanced to cope with volume increases. Although the ZKB Law allows for bank operations outside its home region (subject to not taking any excessive risks or negatively affecting the bank's provision of services locally), we do not expect ZKB to significantly grow its balance sheet outside the canton. Locally it has been growing above market – a trend that we expect to continue.

ZKB's interest-rate risk in the banking book (IRRBB) is higher than international peers', driven by the bank's strategic interest rate position, which allowed it to offset the impact of negative CHF interest rates on its interest income in the past. Unrealised losses in its held-to-maturity debt portfolio are low (2% of CET 1 capital at end-2022). The bank has been able to manage IRRBB well to date, but an increased appetite for this risk could put the VR under pressure. Trading is client-driven and focuses on foreign exchange (mainly francs to euros), interest-rate and credit derivatives, commodities, and Swiss franc- and euro-denominated bonds, as well as other securities.

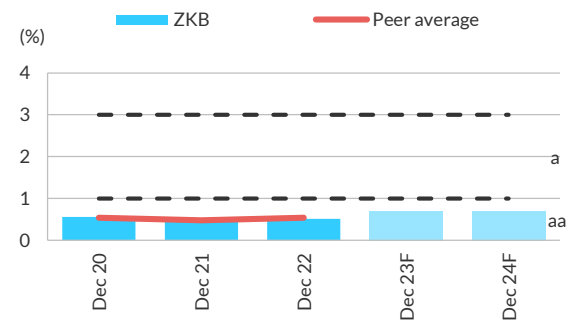
## Financial Profile

### Asset Quality

ZKB's main risk stems from its large real-estate exposure in Zurich, with about three quarters of end-2022 gross customer loans consisting of residential mortgages, including rental properties. We believe this concentration on real estate is adequately mitigated by the Canton of Zurich's strong economic fundamentals and the stability of ZKB's asset quality metrics. Close to 70% of mortgage loans was to private individuals, with a median loan-to-value of 47% at end-2022, about two thirds of which are for owner-occupied homes. Loan quality would therefore be resilient to a significant decline in residential property values, but a severe price correction would put pressure on the VR.

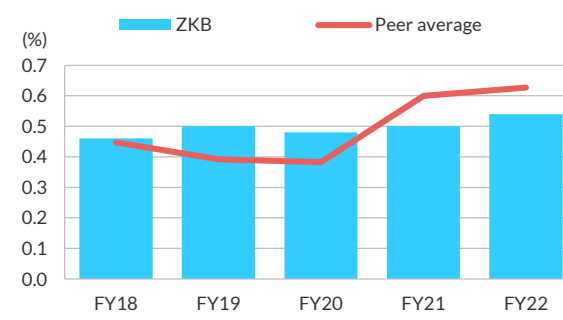
An increase in specific loan impairment charges (LICs) in 2022 was more than compensated by lower expected credit losses, driven by customer preference for variable mortgages with shorter duration. This resulted in risk costs for the year totalling less than a half of their 2021 level. Impaired loans made up 0.4% of gross loans at end-2022. However, we believe Switzerland is heading into a more challenging macroeconomic environment. We therefore expect LICs and impaired loans to increase moderately in 2023, driven by higher interest rates, but for the impaired loans ratio to remain under 1% in the coming years. Fitch still expects GDP to grow by 0.8% in 2023 and unemployment to increase only marginally to 2.4%.

### Impaired Loans/Gross Loans



Source: Fitch Ratings, banks

### Operating Profit/Average Assets



Source: Fitch Ratings, banks

### Earnings and Profitability

ZKB's universal banking model provides good earnings diversification. The bank posted a record profit of CHF1.1 billion in 2022, helped by the return of interest rates into positive territory. Mortgage lending grew by 5.4% yoy, above the market average and slightly above the previous year's growth rate. This, combined with rising interest rates, led to NII growth of 10% in 2022. The net interest margin has only improved marginally so far but we expect it to benefit from rising policy rates and limited pass-through to depositors, and to peak in late 2023. The composition of the mortgage growth has changed, with buy-to-let financing to institutional clients being the dominant mortgage growth driver in 2022.

Net fees and commissions is an important revenue source for ZKB, accounting for more than one third of the bank's revenues. It remained stable in 2022 despite negative market performance. We expect fees and commission income in 2023 to be supported by ZKB's new and existing clients, making use of its expanding investment product offering. Trading activities continue to contribute a material, though more volatile, proportion of operating income (15% in 2022) as the bank has well-established franchises in some trading segments and in structured products.

Personnel expenses went up by 6% in 2022 as the number of employees and variable compensation component increased. Other operating expenses also went up (8%), including on the back of higher marketing and representation costs as well as IT investments. As a result of a higher increase in revenues than in costs, however, the Fitch-calculated cost-income ratio improved marginally to 61% in 2022 (2021: 62%). The bank's management is working on reducing costs, but we believe ZKB's cost base will remain heavier and less flexible than that of many peers given the cantonal mandate, which limits the bank's ability to reduce headcount and close branches.

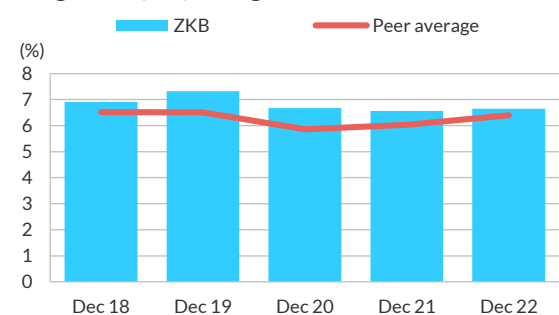
**Capital and Leverage**

ZKB's CET1 ratio remained strong at 16.8% at end-2022, well above the going-concern capital requirement of 13.8% (including the countercyclical capital buffer). We expect the CET1 ratio to increase in the next two years as we do not expect RWA growth to outpace earnings retention. We expect the dividend pay-out ratio to remain below 50% of net profits, in line with ZKB's pre-pandemic distribution level.

Together with the dividends, ZKB also pays the Canton a financial compensation of CHF20 million–30 million a year for its guarantee. The Canton's guarantee covers half of ZKB's gone-concern capital requirement, which will be fully phased in at 7.86% of RWAs in 2026, corresponding to CHF6 billion at 2022 RWAs.

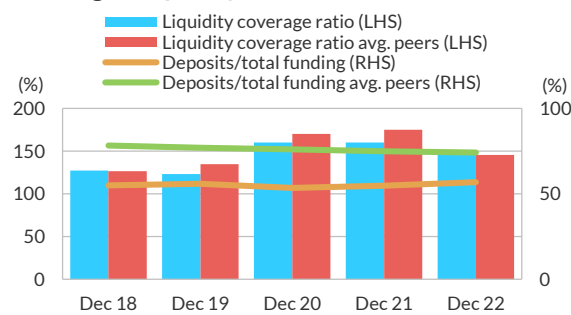
ZKB's undrawn endowment capital of CHF1 billion was reserved entirely for the bank's recovery and resolution planning and, as such, qualifies as gone-concern capital. The remaining gap, which we estimate at around CHF1.1 billion at end-2026, will be covered with bail-in bonds, which ZKB started issuing in 2023 as detailed regulation governing the issuance of bail-in bonds by cantonal banks has been put in place.

**Tangible Equity/Tangible Assets**



Source: Fitch Ratings, banks

**Funding & Liquidity vs Peers**



Source: Fitch Ratings, banks

**Funding and Liquidity**

ZKB's wholesale funding needs are moderate and diversified and benefit from ordinary support via the bank's cantonal guarantee and investor perception of ZKB as a safe haven. ZKB's funding profile is underpinned by a large and mostly granular deposit base despite some concentrated corporate deposits. Customer deposits account for over half of non-equity funding. The bank's loan-to-deposit ratio (104%, as calculated by Fitch at end-2022) has improved since its pre-pandemic levels and we expect it to improve further. The less interest-rate sensitive deposits are favourable in terms of funding costs, that are on the rise for ZKB following the interest rate increases. Since mid-2021 ZKB has been required to report its net stable funding ratio, which, at 124% at end-2022, comfortably exceeded regulatory requirements.

As a domestic systemically important bank (D-SIB), ZKB is subject to a minimum 135% average liquidity coverage ratio requirement. The bank meets this requirement through high-quality liquid assets, which increased to CHF59 billion at end-2022 (end-2019: CHF44 billion), the significant proportion of which is in the form of the central bank deposits. Liquidity coverage ratio stood at an average of 146% in the fourth quarter of 2022. The Swiss government is imposing stricter liquidity requirements for D-SIBs from 2024.

**Note on Charts**

**Dashed lines:** indicative ranges and implied scores for core financial metrics for banks operating in environments scored in the 'aa' category.

Peer averages include ZKB, UBS Switzerland AG (VR: a+/RWN), Credit Suisse (Schweiz) AG (bb/RWE), Raiffeisen Group (a+), and Basler Kantonalbank (a).

## Financials

### Financial Statements

	31 Dec 22		31 Dec 21	31 Dec 20	31 Dec 19
	(USDm) Audited - unqualified	(CHFm) Audited - unqualified	(CHFm) Audited - unqualified	(CHFm) Audited - unqualified	(CHFm) Audited - unqualified
<b>Summary income statement</b>					
Net interest and dividend income	1,527	1,421	1,287	1,258	1,210
Net fees and commissions	995	926	926	806	777
Other operating income	455	423	371	488	421
Total operating income	2,978	2,770	2,584	2,552	2,408
Operating costs	1,820	1,693	1,594	1,665	1,568
Pre-impairment operating profit	1,158	1,077	990	887	840
Loan and other impairment charges	19	18	39	39	-6
Operating profit	1,138	1,059	951	848	846
Other non-operating items (net)	9	8	0	25	4
Tax	9	8	9	8	5
Net income	1,138	1,059	942	865	845
Other comprehensive income	n.a.	n.a.	n.a.	n.a.	n.a.
Fitch comprehensive income	1,138	1,059	942	865	845
<b>Summary balance sheet</b>					
<b>Assets</b>					
Gross loans	116,110	108,017	102,365	97,120	93,375
- Of which impaired	457	425	418	500	435
Loan loss allowances	658	612	627	188	159
Net loans	115,452	107,405	101,738	96,932	93,216
Interbank	3,157	2,937	3,173	3,396	4,917
Derivatives	1,279	1,190	1,272	1,593	1,486
Other securities and earning assets	50,005	46,520	43,645	33,032	29,316
Total earning assets	169,894	158,052	149,828	134,953	128,935
Cash and due from banks	43,322	40,302	40,883	52,154	36,786
Other assets	1,545	1,437	1,394	1,257	1,333
Total assets	214,760	199,791	192,105	188,364	167,054
<b>Liabilities</b>					
Customer deposits	111,094	103,351	96,777	92,609	85,089
Interbank and other short-term funding	53,521	49,791	39,300	39,661	39,051
Other long-term funding	27,381	25,473	38,608	36,286	23,250
Trading liabilities and derivatives	6,129	5,702	3,059	5,721	6,205
Total funding and derivatives	198,126	184,317	177,744	174,277	153,595
Other liabilities	2,338	2,175	1,687	1,437	1,122
Preference shares and hybrid capital	n.a.	n.a.	n.a.	n.a.	n.a.
Total equity	14,295	13,299	12,674	12,650	12,337
Total liabilities and equity	214,760	199,791	192,105	188,364	167,054
Exchange rate		USD1 = CHF0.9303	USD1 = CHF0.9202	USD1 = CHF0.88985	USD1 = CHF0.97165

Source: Fitch Ratings, Fitch Solutions, Zuercher Kantonalbank

**Key Ratios**

	31 Dec 22	31 Dec 21	31 Dec 20	31 Dec 19
<b>Profitability</b>				
Operating profit/risk-weighted assets	1.4	1.3	1.2	1.3
Net interest income/average earning assets	0.9	0.9	0.9	1.0
Non-interest expense/gross revenue	61.4	62.0	65.6	65.8
Net income/average equity	8.2	7.5	7.0	7.0
<b>Asset quality</b>				
Impaired loans ratio	0.4	0.4	0.5	0.5
Growth in gross loans	5.5	5.4	4.0	3.9
Loan loss allowances/impaired loans	144.0	150.0	37.6	36.6
Loan impairment charges/average gross loans	0.0	0.0	0.0	0.0
<b>Capitalisation</b>				
Common equity Tier 1 ratio	16.8	17.0	17.4	17.7
Fully loaded common equity Tier 1 ratio	n.a.	n.a.	n.a.	n.a.
Fitch Core Capital ratio	n.a.	n.a.	n.a.	18.8
Tangible common equity/tangible assets	6.7	6.6	6.7	7.3
Basel leverage ratio	6.2	6.2	6.2	6.6
Net impaired loans/common equity Tier 1	-1.5	-1.7	2.6	2.4
Net impaired loans/Fitch Core Capital	n.a.	n.a.	n.a.	2.3
<b>Funding and liquidity</b>				
Gross loans/customer deposits	104.5	105.8	104.9	109.7
Liquidity coverage ratio	146.0	160.0	160.0	123.0
Customer deposits/total non-equity funding	56.7	54.8	53.4	55.9
Net stable funding ratio	124.0	118.0	n.a.	n.a.

Source: Fitch Ratings, Fitch Solutions, Zuercher Kantonalbank



## Support Assessment

Shareholder Support	
Parent IDR	AAA
Total Adjustments (notches)	0
Shareholder Support Rating	aaa
<b>Shareholder ability to support</b>	
Shareholder Rating	AAA/ Stable
Shareholder regulation	Equalised
Relative size	1 Notch
Country risks	Equalised
<b>Shareholder propensity to support</b>	
Role in group	Equalised
Reputational risk	Equalised
Integration	1 Notch
Support record	Equalised
Subsidiary performance and prospects	Equalised
Legal commitments	Equalised

The colours indicate the weighting of each KRD in the assessment.  
■ Higher influence ■ Moderate influence ■ Lower influence

ZKB's Shareholder Support Rating is based on support from the Canton of Zurich, the bank's guarantor and sole owner, and is equalised with the canton's IDRs. The canton guarantees all of ZKB's non-subordinated liabilities according to the ZKB Law. ZKB's balance sheet is large relative to the canton's budgetary resources, but Fitch believes the bank's stable and resilient business model, funding and capital buffers would mean manageable recapitalisation or liquidity support needs in a realistic stress scenario.

The canton's guarantee does not explicitly address the timeliness of support, but Fitch believes that support, if necessary, would be provided in a timely fashion, given ZKB's high importance for the canton and the potential repercussions of a failure for the Swiss financial sector.

ZKB's strategic importance is underpinned by the bank's mandate to provide financial services to individuals and companies in the canton. The bank's nationwide and international activities are limited. The Canton of Zurich's constitution also requires the canton to have a cantonal bank, making the institutional owner more likely to support the bank in financial distress.

As a D-SIB, ZKB has a Swiss emergency plan, to be approved by FINMA. The plan requires the canton to commit a large volume of contingent capital relative to its own resources. We believe that the provision of this contingent capital, if needed, would be manageable for the canton given its strong financial position, and would not on its own drive a negative action on the canton's ratings, or trigger a reassessment of our support assumptions underpinning ZKB's IDRs.

## Environmental, Social and Governance Considerations

### FitchRatings Zuercher Kantonalbank

Banks  
Ratings Navigator

#### Credit-Relevant ESG Derivation

Credit-Relevant ESG Derivation		Overall ESG Scale			
Zuercher Kantonalbank has 5 ESG potential rating drivers		key driver	0	issues	5
<ul style="list-style-type: none"> <li>Zuercher Kantonalbank has exposure to compliance risks including fair lending practices, mis-selling, repossession/foreclosure practices, consumer data protection (data security) but this has very low impact on the rating.</li> <li>Governance is minimally relevant to the rating and is not currently a driver.</li> </ul>		driver	0	issues	4
		potential driver	5	issues	3
		not a rating driver	4	issues	2
			5	issues	1

#### Environmental (E)

General Issues	E Score	Sector-Specific Issues	Reference	E Scale	How to Read This Page
GHG Emissions & Air Quality	1	n.a.	n.a.	5	<p>ESG scores range from 1 to 5 based on a 15-level color gradation. Red (5) is most relevant and green (1) is least relevant.</p> <p>The Environmental (E), Social (S) and Governance (G) tables break out the individual components of the scale. The right-hand box shows the aggregate E, S, or G score. General Issues are relevant across all markets with Sector-Specific Issues unique to a particular industry group. Scores are assigned to each sector-specific issue. These scores signify the credit-relevance of the sector-specific issue to the issuing entity's overall credit rating. The Reference box highlights the factor(s) within which the corresponding ESG issues are captured in Fitch's credit analysis.</p> <p>The Credit-Relevant ESG Derivation table shows the overall ESG score. This score signifies the credit relevance of combined E, S and G issues to the entity's credit rating. The three columns to the left of the overall ESG score summarize the issuing entity's sub-component ESG scores. The box on the far left identifies some of the main ESG issues that are drivers or potential drivers of the issuing entity's credit rating (corresponding with scores of 3, 4 or 5) and provides a brief explanation for the score.</p>
Energy Management	1	n.a.	n.a.	4	
Water & Wastewater Management	1	n.a.	n.a.	3	
Waste & Hazardous Materials Management; Ecological Impacts	1	n.a.	n.a.	2	
Exposure to Environmental Impacts	2	Impact of extreme weather events on assets and/or operations and corresponding risk appetite & management; catastrophe risk; credit concentrations	Business Profile (incl. Management & governance); Risk Profile; Asset Quality	1	

#### Social (S)

General Issues	S Score	Sector-Specific Issues	Reference	S Scale	Classification of ESG issues has been developed from Fitch's sector ratings criteria. The General Issues and Sector-Specific Issues draw on the classification standards published by the United Nations Principles for Responsible Investing (PRI) and the Sustainability Accounting Standards Board (SASB).
Human Rights, Community Relations, Access & Affordability	2	Services for underbanked and underserved communities; SME and community development programs; financial literacy programs	Business Profile (incl. Management & governance); Risk Profile	5	<p>Sector references in the scale definitions below refer to Sector as displayed in the Sector Details box on page 1 of the navigator.</p>
Customer Welfare - Fair Messaging, Privacy & Data Security	3	Compliance risks including fair lending practices, mis-selling, repossession/foreclosure practices, consumer data protection (data security)	Operating Environment; Business Profile (incl. Management & governance); Risk Profile	4	
Labor Relations & Practices	2	Impact of labor negotiations, including board/employee compensation and composition	Business Profile (incl. Management & governance)	3	
Employee Wellbeing	1	n.a.	n.a.	2	
Exposure to Social Impacts	2	Shift in social or consumer preferences as a result of an institution's social positions, or social and/or political disapproval of core banking practices	Business Profile (incl. Management & governance); Financial Profile	1	

#### Governance (G)

General Issues	G Score	Sector-Specific Issues	Reference	G Scale	CREDIT-RELEVANT ESG SCALE
Management Strategy	3	Operational implementation of strategy	Business Profile (incl. Management & governance)	5	How relevant are E, S and G issues to the overall credit rating?
Governance Structure	3	Board independence and effectiveness; ownership concentration; protection of creditor/stakeholder rights; legal /compliance risks; business continuity; key person risk; related party transactions	Business Profile (incl. Management & governance); Earnings & Profitability; Capitalisation & Leverage	4	5 Highly relevant, a key rating driver that has a significant impact on the rating on an individual basis. Equivalent to "higher" relative importance within Navigator.
Group Structure	3	Organizational structure: appropriateness relative to business model; opacity; intra-group dynamics; ownership	Business Profile (incl. Management & governance)	3	4 Relevant to rating, not a key rating driver but has an impact on the rating in combination with other factors. Equivalent to "moderate" relative importance within Navigator.
Financial Transparency	3	Quality and frequency of financial reporting and auditing processes	Business Profile (incl. Management & governance)	2	3 Minimally relevant to rating, either very low impact or actively managed in a way that results in no impact on the entity rating. Equivalent to "lower" relative importance within Navigator.
				1	2 Irrelevant to the entity rating but relevant to the sector.
				1	1 Irrelevant to the entity rating and irrelevant to the sector.

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](http://www.fitchratings.com/esg).

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