FitchRatings

Banks
Wholesale Commercial Banks
Germany

Aareal Bank AG

Update

Key Rating Drivers

Concentrated CRE Business: Aareal Bank AG's ratings reflect the bank's concentrated core business as a medium-sized international commercial real estate (CRE) lender, which exposes the bank to sector risks despite geographical diversification. The ratings also reflect cyclical asset quality, adequate operating profitability that provides a sufficient buffer to absorb above-average loan impairment charges (LICs) in the coming quarters, and sound capitalisation and adequate funding and liquidity.

Tested Underwriting Standards: Aareal mainly finances properties in prime locations. The underwriting standards and collateralisation of its loan book are broadly in line with market practice. The bank's risk profile is also underpinned by its centralised, sophisticated risk-control framework and good record of impaired loan workouts, which Fitch Ratings views as crucial for weathering the current challenging conditions in some real-estate markets.

Asset Quality Stabilising: Asset quality has varied, reflecting the bank's strategic sector concentrations. It has come under pressure in the past year, mostly in Aareal's sizeable US office portfolio, which is by far the biggest contributor to the bank's 3.2% impaired loans ratio at end-2024.

Aareal demonstrated good capacity to actively manage its non-performing loan portfolio through workouts and sales in 2024. We expect these to continue offsetting further moderate inflows of impaired loans in 2025, which drives our expectation of stable asset quality.

Adequate Profitability: Aareal's housing industry deposits lower the sensitivity of the bank's profits to downturns of the CRE market when interest rates rise. The bank's net interest margin also benefits from Aareal's greater international diversification than more domestic-focused German peers. Both elements sustained profitability in 2024 and will also have a positive effect in 2025, mitigating above-average LICs. The sale of IT subsidiary Aareon is neutral to our assessment of Aareal's profitability given its limited contribution.

Sound Capitalisation: The bank's common equity Tier 1 ratio of 20.2% at end-2024 comfortably exceeds regulatory requirements and benefits from a partial retention of the gain on the sale of Aareon. We view the bank's capitalisation as adequate, considering its property finance business model with high single-borrower and sector concentrations. However, continuing risk on CRE markets drives our negative outlook on the score.

Diversified Funding: Aareal's funding profile is sound and benefits from its established covered bond franchise, which is its main funding source, and stable deposits from the institutional housing sector, supplemented by retail term deposits collected through independent online platforms. This reduces the bank's reliance on unsecured debt market funding.

Ratings

Foreign Currency	
Long-Term IDR	BBB
Short-Term IDR	F2
Derivative Counterparty Rating	BBB+(dcr)
Viability Rating	bbb
Government Support Rating	ns
Sovereign Risk (Germany)	
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

Highest ESG Relevance Scores

Environmental	2
Social	3
Governance	3

Applicable Criteria

Bank Rating Criteria (March 2025)

Related Research

Fitch Affirms Aareal at 'BBB'; Outlook Stable (October 2024)

Western European Banks Outlook 2025 (December 2024)

Aareal Bank AG (October 2024)

German Banks' Commercial Real Estate: Credit Losses to Stay High (February 2024)

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Rating Sensitivities

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

Aareal's ratings would be likely to be downgraded if the bank's impaired loans ratio increases above 6% for an extended period with no credible reduction plan, or if heightened LICs weigh on its operating profitability, lowering its operating profit/RWAs ratio to below 0.5% in the longer term. This could result from further severe stress in the US office property market and a spillover to European property markets.

Significantly higher funding costs triggered by a material loss of deposits in the housing sector or signs of challenges to access the wholesale funding market could also impair Aareal's profitability and funding and result in a downgrade.

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

An upgrade of Aareal's ratings would be contingent on a sustainable recovery of US office property markets and resilient asset quality in the bank's other property segments and regions. An upgrade would also be contingent on the bank further strengthening its profitability, with an operating profit/RWAs ratio sustainably above 2%, combined with an impaired loans ratio of around 3%, while maintaining sound capitalisation.

Other Debt and Issuer Ratings

Rating Level	Rating
Long-term/short-term deposits	BBB+/F2
Long-term/short-term senior preferred	BBB+/F2
Senior non-preferred	BBB
Subordinated Tier 2 debt	BB+
Additional Tier 1 notes	BB-

Source: Fitch Ratings

Aareal's Derivative Counterparty Rating, long-term deposit and senior preferred debt ratings are one notch above its Long-Term IDR, while the long-term senior non-preferred debt rating is aligned with the Long-Term IDR. This reflects the large and sustainable layer of non-preferred and junior debt that provides preferred creditors and counterparties with additional protection in a resolution. The short-term senior preferred and deposit ratings are the lower of the two options mapping to the respective long-term ratings.

The Tier 2 debt rating is two notches below the VR to reflect higher loss severity relative to senior creditors in a resolution. The Additional Tier 1 notes are rated four notches below the VR (two notches for loss severity and two notches for non-performance risk) to reflect our expectation that Aareal will maintain large capital buffers above the notes' mandatory coupon omission triggers.

Aareal's Short-Term IDR is the higher of the two short-term ratings that map to its Long-Term IDR and reflects our assessment of its funding and liquidity.

Significant Changes from Last Review

Improved Performance in 2024

Aareal's 2024 operating profit rose by 33% to EUR294 million, which is the bank's strongest result since 2018. The result was also at the top end of its target range for 2024, despite a one-off charge for efficiency measures of EUR34 million. Net interest income increased by 5% to EUR1.1 billion, driven in part by good margins and credit portfolio growth, while administrative expenses (excluding the one-off charge) remained broadly stable. Operating profit/RWAs increased to 2.1%, in line with our expectations.

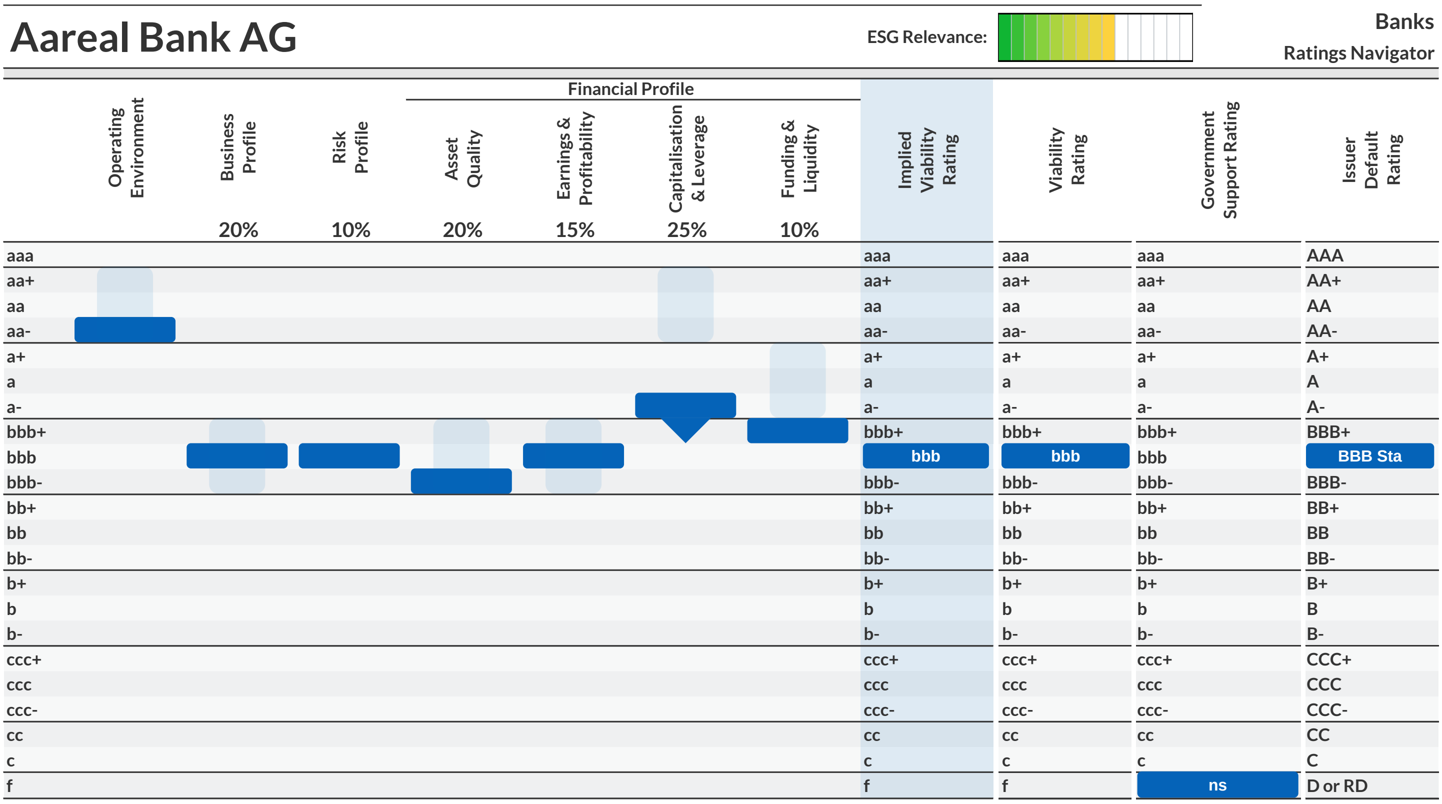
LICs declined by 16% to EUR370 million at end-2024, but these remain at a heightened 1.1% of gross loans, reflecting continued stress on the US office properties market. The bank also increased its management overlays by EUR60 million to EUR85 million at end-2024 and reduced its impaired loans ratio to 3.2% (end-2023: 4.4%), broadly in line with our expectations. We expect LICs to gradually decline in 2025 and 2026 as property markets recover, but the positive effect on earnings should be mostly offset by lower deposit margins. For 2025, the bank expects to achieve an operating profit of EUR375 million–EUR425 million and increase its return on equity to 7%–8%, which is only slightly above our forecast.

The sale of the bank's IT subsidiary Aareon closed in October 2024 and led to a net gain on sale of EUR2.1 billion. The bank paid a dividend of EUR1.9 billion out of its consolidated net income (including Aareon) of EUR2.3 billion.

New Strategy for Growth

Aareal's new three-year strategy focuses on growth and efficiency measures. The bank plans to increase the size of its CRE loan book by 12% by end-2027, expand its balance-sheet-light business by close to 30%, while maintaining its institutional housing deposits above EUR13 billion. From the efficiency measures, the bank aims to achieve cost savings of EUR40 million a year in 2027. The main objectives are to increase return on equity to at least 13% by 2027 (post-tax, based on a standardised 13.5% CET1 ratio Basel IV fully phased-in, excluding one-offs; 2024: 6.7%, excluding the sale of Aareon), to have a cost/income ratio below 30%, and to maintain a common equity Tier 1 ratio above 13.5% on a Basel IV fully phased-in basis (end-2024: 15.2%). The bank also aims to maintain a non-performing exposure ratio below 3% and to normalise its cost of risk to around 45bp by 2027. We believe that the achievement of these targets is conditional on a recovery of the US CRE market.

Ratings Navigator



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.

VR - Adjustments to Key Rating Drivers

The capitalisation and leverage score of 'a-' has been assigned below the 'aa' implied category score due to the following adjustment reason: risk profile and business model (negative).

The funding and liquidity score of 'bbb+' has been assigned below the 'a' implied category score due to the following adjustment reason: non-deposit funding (negative).

Financials

Financial Statements

	31 Dec 24		31 Dec 23	31 Dec 22	31 Dec 21
	12 months	12 months	12 months	12 months	12 months
	(USDm)	(EURm)	(EURm)	(EURm)	(EURm)
	Audited – unqualified	Audited – unqualified	Audited – unqualified	Audited – unqualified	Audited – unqualified
Summary income statement					
Net interest and dividend income	1,102	1,060	1,014	702	597
Net fees and commissions	-4	-4	39	277	245
Other operating income	-19	-18	-62	23	-38
Total operating income	1,079	1,038	991	1,002	804
Operating costs	389	374	329	571	516
Pre-impairment operating profit	690	664	662	431	288
Loan and other impairment charges	385	370	441	192	133
Operating profit	306	294	221	239	155
Other non-operating items (net)	2,143	2,062	-79	–	–
Tax	85	82	94	86	87
Net income	2,363	2,274	48	153	68
Summary balance sheet					
Assets					
Gross loans	35,443	34,103	33,698	31,720	31,723
– Of which impaired	1,138	1,095	1,470	985	1,505
Loan loss allowances	414	398	424	487	489
Net loans	35,030	33,705	33,274	31,233	31,234
Interbank	1,582	1,522	2,976	1,914	1,264
Derivatives	1,189	1,144	1,538	1,825	1,132
Other securities and earning assets	7,702	7,411	6,084	5,329	6,705
Total earning assets	45,503	43,782	43,872	40,301	40,335
Cash and due from banks	2,707	2,605	977	5,424	6,942
Other assets	1,483	1,427	1,984	1,606	1,451
Total assets	49,693	47,814	46,833	47,331	48,728
Liabilities					
Customer deposits	17,111	16,464	17,181	16,895	15,109
Interbank and other short-term funding	1,238	1,191	1,622	1,981	6,109
Other long-term funding	22,613	21,758	20,898	21,050	21,705
Trading liabilities and derivatives	2,667	2,566	2,683	3,514	1,882
Total funding and derivatives	43,629	41,979	42,384	43,440	44,805
Other liabilities	390	375	1,149	633	862
Preference shares and hybrid capital	312	300	300	300	300
Total equity	5,363	5,160	3,000	2,958	2,761
Total liabilities and equity	49,693	47,814	46,833	47,331	48,728
Exchange rate		USD1 = EUR0.962186	USD1 = EUR0.912742	USD1 = EUR0.937559	USD1 = EUR0.884173

Source: Fitch Ratings, Fitch Solutions, Aareal Bank AG

Key Ratios

(%)	31 Dec 24	31 Dec 23	31 Dec 22	31 Dec 21
Profitability				
Operating profit/risk-weighted assets	2.1	1.6	1.9	1.2
Net interest income/average earning assets	2.5	2.4	1.7	1.5
Non-interest expense/gross revenue	36.1	33.3	56.9	64.0
Net income/average equity	66.0	1.6	5.3	2.5
Asset quality				
Impaired loans ratio	3.2	4.4	3.1	4.7
Growth in gross loans	1.2	6.2	0.0	6.3
Loan loss allowances/impaired loans	36.4	28.8	49.4	32.5
Loan impairment charges/average gross loans	1.1	1.4	0.6	0.4
Capitalisation				
Common equity Tier 1 ratio	20.2	19.4	19.3	18.2
Fully loaded common equity Tier 1 ratio	15.2	13.4	–	–
Tangible common equity/tangible assets	10.5	4.8	4.9	4.9
Basel leverage ratio	6.8	6.4	6.0	5.5
Net impaired loans/common equity Tier 1	24.2	39.3	20.2	43.7
Funding and liquidity				
Gross loans/customer deposits	207.1	196.1	187.8	210.0
Gross loans/customer deposits + covered bonds	114.2	112.1	109.3	115.5
Liquidity coverage ratio	230.0	203.7	207.4	255.4
Customer deposits/total non-equity funding	41.5	43.0	42.0	35.0
Net stable funding ratio	117.0	115.1	–	–

Source: Fitch Ratings, Fitch Solutions, Aareal Bank AG

Support Assessment

Commercial Banks: Government Support	
Typical D-SIB GSR for sovereign's rating level (assuming high propensity)	A+ to A-
Actual jurisdiction D-SIB GSR	ns
Government Support Rating	ns
Government ability to support D-SIBs	
Sovereign Rating	AAA/ Stable
Size of banking system	Negative
Structure of banking system	Neutral
Sovereign financial flexibility (for rating level)	Positive
Government propensity to support D-SIBs	
Resolution legislation	Negative
Support stance	Negative
Government propensity to support bank	
Systemic importance	Negative
Liability structure	Neutral
Ownership	Neutral

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

Aareal's Government Support Rating of 'no support' (ns) reflects Fitch's view that senior creditors cannot rely on full extraordinary state support. This is driven by the EU's resolution framework that is likely to require senior creditors participating in losses, if necessary, instead of, or ahead of, a bank receiving government support.

Environmental, Social and Governance Considerations

FitchRatings **Aareal Bank AG**

Banks
Ratings Navigator

Credit-Relevant ESG Derivation

Aareal Bank AG has 5 ESG potential rating drivers

- Aareal Bank AG 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.
- Governance is minimally relevant to the rating and is not currently a driver.

			Overall ESG Scale
key driver	0	issues	5
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
GHG Emissions & Air Quality	1	n.a.	n.a.	5
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
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
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
Management Strategy	3	Operational implementation of strategy	Business Profile (incl. Management & governance)	5
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
Group Structure	3	Organizational structure; appropriateness relative to business model; opacity; intra-group dynamics; ownership	Business Profile (incl. Management & governance)	3
Financial Transparency	3	Quality and frequency of financial reporting and auditing processes	Business Profile (incl. Management & governance)	2
				1

How to Read This Page
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.

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 issues 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.

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.

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).

Sector references in the scale definitions below refer to Sector as displayed in the Sector Details box on page 1 of the navigator.

CREDIT-RELEVANT ESG SCALE

How relevant are E, S and G issues to the overall credit rating?	
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.
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.
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.
2	Irrelevant to the entity rating but relevant to the sector.
1	Irrelevant to the entity rating and irrelevant to the sector.

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.

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