

**Fixed Income Research – Switzerland**

Sector: Banks  
Country: Germany  
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**ISSUER PROFILE****Bankgesellschaft Berlin***Summary*

*Bankgesellschaft Berlin AG (BGB) is the predominant banking group in the Berlin/Brandenburg area. Its three most important subsidiaries are Berlin Girozentrale, Berliner Bank AG and Berlin Hyp. With the transfer of Germany's capital to Berlin, the region's attraction and economic potential is likely to increase considerably. The Group represents a new concept in German banking by uniting private and public banking under one roof, which, in our opinion, will provide a good basis for success in a liberalised market. The Group's international bonds are issued by BGB Finance (Ireland) plc and are rated with Aa1/AAA by Moody's/IBCA due to the fact that they are guaranteed by Landesbank Berlin Girozentrale (LBB), which, in turn, benefits from the State of Berlin's guarantee (Anstaltlast, Gewährträgerhaftung).*

*One of Germany's leading banking groups*

Bankgesellschaft Berlin is one of Germany's foremost banking groups (see chart page 4) with total assets of DEM 326 bn (as of end-1996). Established in 1994, it unites the essential banking interests of the State of Berlin in the form of a holding company. The State of Berlin remains BGB's controlling stakeholder with 57% of its shares. BGB's most important participations include LBB as a public-law institute, Berliner Bank AG as a private sector bank and Berlin Hyp, which is regulated by the German Mortgage Banks Act (Hypothekenbankengesetz). In this way, BGB forms a unique combination of public- and private-sector banking institutes in Germany, offering universal services ranging from retail and commercial banking to investment banking.

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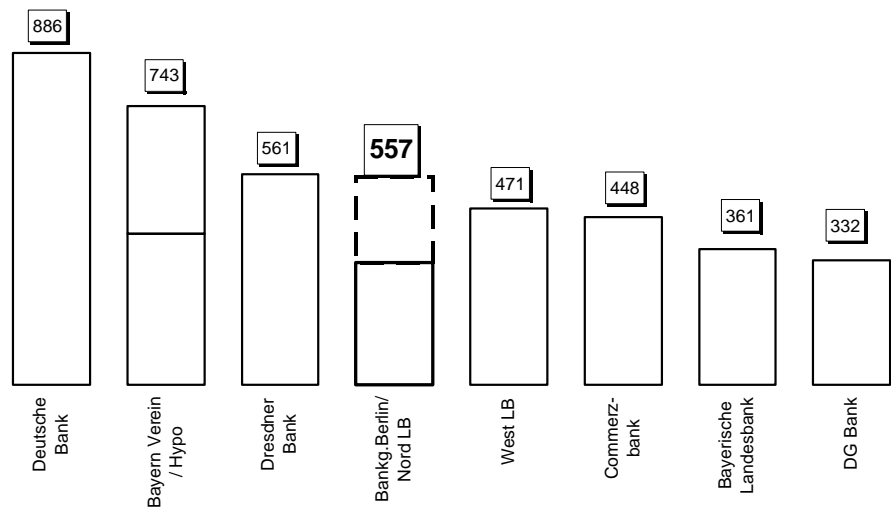
***Berlin/Brandenburg  
as a high-growth  
centre of operations***

With over 400 branch offices, of which around two-thirds are found in the Berlin/Brandenburg area, BGB's operating base encompasses one of the strongest growing regions in Germany. Eastern Germany's structural development needs represent the main source of growth. Furthermore, the transfer of the federal capital from Bonn to Berlin is providing added stimulus to the local economy. In its home territory, BGB dominates the retail banking segment and, to a lesser degree, commercial banking. Such geographical concentration of assets also involves a certain element of risk, which is why Moody's is currently reviewing its Aa3 rating for BGB (see paragraph on credit aspects for bonds).

***Potential merger with  
Nord LB***

In comparison with other European countries, the German banking sector is extremely fragmented. For this reason, the 'big three' banks (Deutsche Bank, Dresdner Bank and Commerzbank) control a mere 10% share of domestic banking<sup>1</sup>. However, a consolidation of the sector is already well under way. A merger of Bayerischen Vereinsbank and Hypobank is about to be settled, with the new entity moving up to number two in terms of total assets. The public bank Norddeutsche Landesbank Girozentrale (Nord LB) and BGB have recently agreed, in principle, to merge operations with BGB acting as a holding bank. This would result in a banking group in northern Germany with total assets comparable to those of Dresdner Bank. It is difficult to speculate about the outcome of the detailed merger talks which are still under way.

***Largest German  
banks in terms of  
total assets  
(DEM bn)***




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Data as of end-1996. As a specialised development bank, KfW was excluded from the comparison  
Source: Annual reports

<sup>1</sup> The 10% figure applies to the market share in both domestic lending and domestic deposits of clients (excluding interbank business). Source: Moody's Investor Service, January 1997.

***Mixed ownership is a good prerequisite for change***

Another characteristic of the German banking sector is its large number of public-law banks. This is because the encouragement of savings and the protection of account holders has long been viewed as a guiding principle of public policy in Germany. In the meantime, the increasing globalisation of the economy has placed new demands on modern banking. The traditional savings business, for instance, is becoming less important as new forms of investment emerge. Competitive distortions, arising from the implied and explicit federal and state guarantees for public financial institutions, are likely to disappear in the medium-term future, particularly under the pressure from EU legislation. The above-mentioned combination of private and public-sector ownership is likely to facilitate BGB's transformation and adaptation to a deregulated market.

## **CREDIT ASPECTS FOR BGB BONDS**

***State of Berlin maintenance and guarantee obligation***

BGB issues international bonds through BGB Finance (Ireland) plc, whose liabilities are jointly and severally guaranteed by BGB as the holding company as well as the LBB and Berliner Bank AG subsidiaries. This means BGB Finance benefits indirectly from the State of Berlin's maintenance and guarantee obligation to LBB. Under German law, the State of Berlin is subject to both a general obligation to maintain LBB's operating and financial base (Anstaltslast) as well as a specific guarantee obligation (Gewährträgerhaftung) vis-à-vis LBB's creditors.

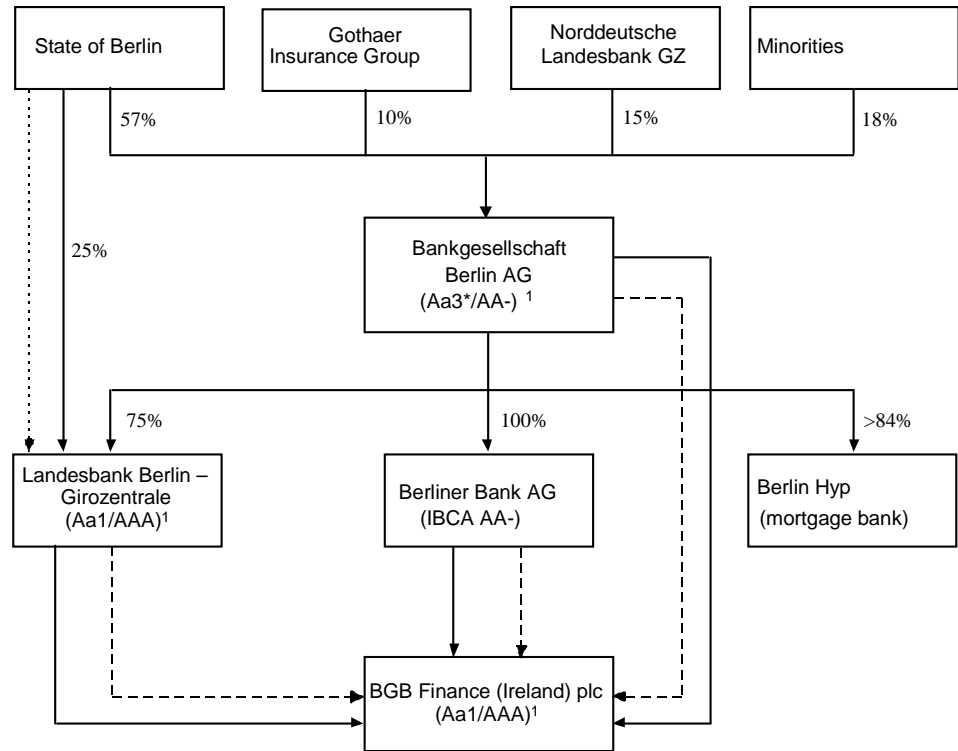
***Aa1/AAA rating for BGB Finance as an issuer of bonds***

Moody's and IBCA<sup>2</sup> take a differentiated view in their credit ratings for the BGB group companies, depending on the legal entity (see p. 4). The public-sector entity LBB, and hence BGB Finance plc, are assigned the highest ratings (Aa1/AAA). The BGB holding company is rated Aa3/AA-. The rating agencies assume that the association between BGB and the State of Berlin will continue for the foreseeable future. The State is contractually obliged to hold a controlling stake in BGB until at least the year 2023. Moody's has put its Aa3 rating for BGB on its watch list for a possible downgrade. Moody's cites quality problems in BGB Group's credit portfolio and uncertainty in connection with the future structure of the Group if Nord LB merges with BGB. However, one should note that BGB Finance plc's Aa1 rating is unaffected by Moody's rating review.

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<sup>2</sup> S&P does not currently assign credit ratings for BGB or its subsidiaries.

**BANKGESELLSCHAFT BERLIN:  
OWNERSHIP STRUCTURE AND SUPPORT FRAMEWORK**



- > Ownership link
- - - - -> Joint and several guarantee
- .....> Maintenance and guarantee obligation

<sup>1</sup> Senior long-term credit rating from Moody's Investors Service und IBCA

\* Bankgesellschaft Berlin's Aa3 rating has been on the watch list for a possible downgrade since 2 December 1996

Source: Annual reports, bond prospectuses