



# Banca Popolare di Sondrio

## PRESS RELEASE

### FITCH RATINGS UPGRADES BANCA POPOLARE DI SONDRIO

### THE BANK'S ISSUER RATING IS AT INVESTMENT GRADE 'BBB-' WITH 'STABLE' OUTLOOK

Banca Popolare di Sondrio informs that, today, the agency Fitch Ratings, at the end of its annual rating review process, has improved the Bank's credit rating.

In particular, the Long-term Issuer Default Rating ('IDR') now stands at *investment grade* 'BBB-', with a 'stable' *outlook*.

Below are the details of the ratings assigned to the bank:

- Long-term Issuer Default Rating ('IDR'): 'BBB-
- Short-term Issuer Default Rating ('IDR'): 'F3'.
- Viability Rating: "bbb-"
- Government Support Rating: 'ns'
- Long-term Deposit Rating: 'BBB'
- Short-term Deposit Rating: 'F3'
- Senior Preferred Debt: 'BBB-'
- Subordinated Tier 2 Debt: 'BB'.

*"With today's improved rating by Fitch, the creditworthiness of Banca Popolare di Sondrio is now considered investment grade by all the rating agencies that assess us, with full recognition of the intense work carried out in recent years both on the derisking front and on that of structural strengthening in various strategic areas. This is a reason for particular satisfaction, because we believe that corporate solidity is the fundamental requirement to continue - in line with our statutory mission - to effectively support the territories and communities in which we*

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*operate, opening up to new markets. Leveraging the operational efficiency that has always distinguished us, we will continue to work to strengthen our business model, aiming to diversify on the one hand, and consolidate on the other, our spheres of action. The objective is to create value in the medium to long term for all stakeholders, giving particular impetus to economic sectors that favour growth,' commented **Mario Alberto Pedranzini, CEO and General Manager of Banca Popolare di Sondrio.***

Please find attached the press release issued by Fitch Ratings.

Sondrio, 24 April 2024

BANCA POPOLARE DI SONDRIO Spa

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*The English translation is provided solely for the benefit of the reader and in the case of discrepancies the Italian shall prevail.*

## RATING ACTION COMMENTARY

# Fitch Upgrades Banca Popolare di Sondrio to 'BBB-'; Outlook Stable

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Fitch Ratings - Milan - 24 Apr 2024: Fitch Ratings has upgraded Banca Popolare di Sondrio - Societa per Azioni's (Sondrio) Long-Term Issuer Default Rating (IDR) at 'BBB-' from 'BB+'. The Outlook is Stable. Fitch has also upgraded the Viability Rating (VR) to 'bbb-' from 'bb+'. A full list of rating actions is below.

The upgrades primarily reflect Sondrio's improved business profile, which benefits from the bank's strengthened credit profile and growing fee-generating business. The latter leverages on Sondrio's presence in the wealthy Lombardy region and product diversification. This should support a durable improvement in Sondrio's core profitability metrics.

The upgrades also consider faster-than expected progress on de-risking, which together with a tighter risk appetite has brought the impaired loan ratio close to industry levels.

## KEY RATING DRIVERS

**Sound Business and Financial Profile:** Sondrio's ratings reflect its second-tier franchise as a regional bank with small national market shares but well-established position in the wealthy Lombardy region, and traditional commercial banking business model. They also consider satisfactory capitalisation and a sound funding and liquidity profile. Asset quality and profitability have improved to levels we expect to be sustainable and more in line with the industry average.

**Small Franchise, Moderate Diversification:** Sondrio lacks pricing power in its home region of Lombardy due to fierce competition from large domestic banks. However, the bank's business and revenue generation benefit from the economic strength of its home market, as well as Sondrio's business diversification in well-performing factoring, in Switzerland and in treasury and foreign services, in which the bank has recognised expertise. Its cost-efficiency is better than similarly sized domestic peers, which has also contributed to the bank's adequate profitability record.

**Moderate Risk Profile:** Sondrio's footprint in regions with strong economic features, a fairly high share of state guarantees and the bank's tightened loan underwriting and risk monitoring should mitigate inflows of new impaired loans from high interest rates and muted economic growth. In addition, Sondrio's continued active management of impaired loans should help its asset quality metrics to gradually converge to the sector average. Our assessment also considers the bank's high exposure to the Italian sovereign debt, which we expect to only moderately decrease in 2024.

**Asset Quality Converging to Average:** Sondrio's asset quality outperformed expectations with the impaired loans ratio improving to 3.8% at end-2023 (end-2022: 4.3%), which remains above the Italian average of around 3%. Fitch forecasts the bank will maintain its impaired loans ratio comfortably below 4% in 2024 and 2025 as planned disposals and write-offs should help offset inflows of impaired loans from the expected pick-up in default rates. Sondrio's loan loss allowance coverage of above 75%, slightly below the domestic average, provides the bank with an adequate buffer to absorb the expected asset quality weakening.

**Adequate Profitability, Sound Cost-Efficiency:** Sondrio's operating profitability peaked at 2.9% of risk-weighted assets (RWAs) in 2023, which was close to European average and materially above the bank's four-year average of 1.8%. This was mainly due to high interest rates and growing business.

We forecast the operating profit/RWAs ratio will remain well above 2% for 2024 and 2025, despite Fitch's expectation of rate cuts from 2H24. This will be supported by interest rates remaining well in positive territory and growing fee income, leveraging on partnerships with specialised players in wealth management and insurance. This should help absorb loan impairment charges of around 60bp, and continued IT investments to support the bank's modernisation.

**Adequate Capitalisation, Average Encumbrance:** Sondrio's common equity Tier 1 (CET1) ratio was stable yoy at 15.4% at end-2023, with good earnings generation offsetting RWA growth. The bank's de-risking has reduced capital encumbrance by unreserved impaired loans to 9% of CET1 capital (end-2022: 14%), which is in line with higher-rated peers. Exposure to Italian government bonds remains high, at 1.9x of end-2023 CET1 capital, despite a marked decline since 2018. We expect it to moderately reduce further as targeted long-term refinancing operations (T-LTRO) facilities mature in 2H24.

**Stable Funding, Good Liquidity Buffer:** Sondrio's funding and liquidity profile benefits from its large and stable customer deposit base, leveraging on its strong long-term client relationships. Sondrio has adequate access to the wholesale funding markets, although

less established than some higher rated domestic peers. Liquidity is sound, thanks to adequate buffers of unencumbered eligible assets, which represent about 30% of end-2023 total assets.

## **RATING SENSITIVITIES**

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

Sondrio's ratings are sensitive to a significant weakening of the operating environment in Italy. This could be due to much slower economic growth than our forecasts, which could result in higher default rates and lead to deterioration in asset quality, earnings and capital metrics, for example.

The ratings would likely be downgraded if the impaired loans ratio sustainably increased above 4% and the bank failed to maintain operating profit at around 2% of RWAs on a sustained basis, especially if this translated into weakening internal capital generation with the CET1 ratio falling below 14%, without the prospect of recovery in the short term.

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

An upgrade would require a higher assessment of Italy's operating environment, unless Sondrio materially improves the diversification of its business model and has significant franchise growth within a conservative risk appetite. For this to be rating positive, it would have to result in operating profit/RWAs reaching at least 3% on a sustained basis, while reducing its impaired loans ratio to below 2% and maintaining a prudent CET1 ratio of at least 16%, or materially reducing capital encumbrance by Italian government bonds.

## **OTHER DEBT AND ISSUER RATINGS: KEY RATING DRIVERS**

The upgrade of Sondrio's Short-Term IDR follows that of the Long-Term IDR and maps to a 'BBB-' Long-Term IDR.

The upgrade of Sondrio's long-term deposit ratings follows that of the Long-Term IDR. The 'BBB' long-term deposit rating is one-notch above the Long-Term IDR, reflecting full depositor preference in Italy and our belief that the bank has sufficient combined buffers of junior and senior debt, to protect depositors in a resolution. The one-notch uplift also reflects our expectation that the bank will maintain sufficient buffers to comply with minimum requirement for own funds and eligible liabilities (MREL).

The short-term deposit rating of 'F3' maps to a 'BBB' long-term deposit rating.

The upgrade of Sondrio's senior preferred debt follows that of the Long-Term IDR, with which it is equalised, because the bank uses senior preferred debt to meet its MREL.

The upgrade of Sondrio's subordinated (Tier 2) debt follows that of the VR, from which it is notched. Sondrio's Tier 2 debt is rated two notches below the VR for loss severity to reflect poor recovery prospects. No notching is applied for incremental non-performance risk because a write-down of the notes will only occur once the point of non-viability is reached, and there is no coupon flexibility before non-viability.

**No Government Support:** Sondrio's Government Support Rating (GSR) of 'no support' (ns) reflects Fitch's view that although external extraordinary sovereign support is possible, it cannot be relied on. Senior creditors can no longer expect to receive full extraordinary support from the sovereign in the event that the bank becomes nonviable. This is because the EU's Bank Recovery and Resolution Directive and the Single Resolution Mechanism for eurozone banks provide a framework for resolving banks that requires senior creditors participating in losses, if necessary, instead of or ahead of a bank receiving sovereign support.

## **OTHER DEBT AND ISSUER RATINGS: RATING SENSITIVITIES**

Sondrio's long- and short-term senior preferred debt and deposit ratings are primarily sensitive to changes in the Long-Term IDR and will move in tandem. In addition, the senior debt ratings could also be upgraded by one notch if at some point the bank is expected to meet its resolution buffer requirements with senior non-preferred or more junior instruments.

The deposit ratings could be downgraded by one notch and be aligned with the IDRs in the event of a reduction in the size of the senior and junior debt buffers, although we view this as unlikely in light of Sondrio's current and future MREL.

Sondrio's subordinated Tier 2 notes are primarily sensitive to changes in the bank's VR. We could also downgrade the notes in case of an unfavourable change in the notes' notching, which could arise if Fitch changes its assessment of their non-performance relative to the risk captured in the VR.

An upgrade of the GSR would be contingent on a positive change in the sovereign's propensity to support the bank. In Fitch's view, this is highly unlikely, although not impossible.

## **VR ADJUSTMENTS**

The 'bbb' operating environment score is below the 'a' implied category score due to the following adjustment reason: sovereign rating (negative).

## REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

## ESG CONSIDERATIONS

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>.

## RATING ACTIONS

ENTITY / DEBT ↕	RATING ↕			PRIOR ↕
Banca Popolare di Sondrio - Societa per Azioni	LT IDR	BBB- Rating Outlook Stable		BB+ Rating Outlook Stable
		Upgrade		
	ST IDR	F3	Upgrade	B
	Viability	bbb-	Upgrade	bb+
	Government Support	ns	Affirmed	ns
long-term deposits	LT	BBB	Upgrade	BBB-
Senior preferred	LT	BBB-	Upgrade	BB+
subordinated	LT	BB	Upgrade	BB-

short-term deposits

ST F3 Affirmed

F3

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[VIEW ADDITIONAL RATING DETAILS](#)**FITCH RATINGS ANALYSTS****Valeria Pasto**

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## APPLICABLE CRITERIA

[Bank Rating Criteria \(pub. 15 Mar 2024\) \(including rating assumption sensitivity\)](#)

## ADDITIONAL DISCLOSURES

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Banca Popolare di Sondrio - Societa per Azioni

EU Issued, UK Endorsed

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