

Scope affirms BBB- issuer rating on Banca Popolare di Sondrio

The affirmation reflects the group's derisking of NPEs in 2020, which offsets the increased uncertainty over credit losses from performing loans due to the Covid-19 pandemic.

Rating action

Scope Ratings GmbH (Scope) has today affirmed its issuer rating of BBB- to Banca Popolare di Sondrio SCpA (BPS), with a Stable Outlook.

Rating rationale

BPS' established retail and commercial banking franchise with solid market shares in the wealthy Italian region of Lombardy produces a moderately stable and predictable revenue and earnings stream. BPS has immaterial market shares in Italy but a dominant position in its home province of Sondrio and relevant market positions in the Lecco and Como provinces. BPS is also the parent company of the BPS group, which includes a small bank in Switzerland (BPS Suisse), Factorit (a factoring joint venture with Banco BPM) and BNT Banca, which specialises in agricultural business loans and payroll deductible loans.

While low by international standard, BPS' profitability track record is better than the average Italian bank. Stable revenues, good cost efficiency, a moderate level of loan losses and the lack of large one-off restructuring costs have helped the issuer maintain a positive bottom line for the past decade. This sets it apart from many peers, which have required material capital injections.

Asset quality continued to improve in 2020 thanks to sizeable disposals of NPEs and is now more aligned with the level of other former Popolari banks. At the same time, asset quality still compares unfavourably with larger Italian and international peers, a factor Scope sees as a rating constraint. Uncertainty around the final losses from the Covid-19 crisis adds to asset quality concerns.

Under Scope's bank rating methodology, the 'long-term sustainability' assessment (ESG factor) captures how relevant environmental, social and governance (ESG) factors and preparedness for digital transition (D) may impact an issuer's creditworthiness. As part of the first-time implementation of this methodology, Scope assesses Banca Popolare di Sondrio as 'Lagging'. This reflects Scope's view that while the group has been prudently managed over the years, there is material room for improvement in its governance and preparedness for digital competition. Partly offsetting these concerns, the group's cooperative roots, and its attention to the territories where it operates, indicate a strong social responsibility, and good balancing of the interests of the different stakeholders. Scope acknowledges the bank's recent efforts to improve its

governance and views favourably the bank's likely transformation into a joint stock company by the end of the year.

At the end of December 2020, BPS had a CET1 ratio of 16.3% on a transitional basis, which is higher than peers and well ahead of requirements. Scope notes that the bank could further optimise its capital structure via the issuance of capital securities, which are currently underutilised. The healthy buffers to capital requirements, alongside comfortable liquidity and funding regulatory ratios, are a key support to the rating. BPS is primarily funded by deposits, though it also uses the ECB's TLTRO lines.

Outlook and rating-change drivers

The Outlook is Stable, reflecting Scope's expectation that the issuer's credit profile will remain stable over the next 12-18 months. Scope expects the transformation of the issuer into a joint stock company to positively affect long-term sustainability. However, Scope does not expect the business model of Banca Popolare di Sondrio to change materially in the near term. At this stage, the key rating-change drivers are linked to the bank's financial performance.

What could move the credit rating up:

- Evidence that BPS' asset quality can remain resilient even in the current stressed environment
- A continued decline in NPEs and cost of risk, leading to stronger earnings

What could move the credit rating down:

- Material credit or trading losses leading to the erosion of capital buffers
- Potential disruption from the transformation into a joint stock company, which Scope expects to be completed in 2021

Overview of the rating construct

Operating environment: Supportive

Business model: Consistent

Initial mapping refinement: Low

Initial mapping: bbb-/bbb

Long-term sustainability: Lagging

Adjusted anchor: bbb-

Earnings capacity and risk exposures: Constraining

Financial viability management: Comfortable

Additional rating factors: Neutral factor

Standalone assessment: bbb-

External support: Not applicable

Issuer rating: BBB-

Outlook: Stable

One or more key drivers of the credit rating action are considered an ESG factor.

Stress testing & cash flow analysis

No stress testing was performed. No cash flow analysis was performed.

Methodology

The methodology used for this Credit Rating and Outlook, (Bank Rating Methodology, 26 January 2021), is available on <https://www.scooperatings.com/#!/methodology/list>.

Information on the meaning of each Credit Rating category, including definitions of default, recoveries, Outlooks and Under Review, can be viewed in 'Rating Definitions – Credit Ratings, Ancillary and Other Services', published on <https://www.scooperatings.com/#!/governance-and-policies/rating-scale>. Historical default rates of the entities rated by Scope Ratings can be viewed in the Credit Rating performance report at <https://www.scooperatings.com/#!/governance-and-policies/regulatory-ESMA>. Also refer to the central platform (CEREP) of the European Securities and Markets Authority (ESMA): <http://cerp.esma.europa.eu/cerp-web/statistics/defaults.xhtml>. A comprehensive clarification of Scope Ratings' definitions of default and Credit Rating notations can be found at <https://www.scooperatings.com/#!/governance-and-policies/rating-scale>. Guidance and information on how environmental, social or governance factors (ESG factors) are incorporated into the Credit Rating can be found in the respective sections of the methodologies or guidance documents provided on <https://www.scooperatings.com/#!/methodology/list>.

The Outlook indicates the most likely direction of the Credit Rating if the Credit Rating were to change within the next 12 to 18 months.

Solicitation, key sources and quality of information

The Rated Entity and/or its Related Third Parties participated in the Credit Rating process.

The following substantially material sources of information were used to prepare the Credit Rating: public domain, the Rated Entity and Scope Ratings' internal sources.

Scope Ratings considers the quality of information available to Scope Ratings on the Rated Entity or instrument to be satisfactory. The information and data supporting the Credit Rating originate from sources Scope Ratings considers to be reliable and accurate. Scope Ratings does not, however, independently verify the reliability and accuracy of the information and data.

Prior to the issuance of the Credit Rating action, the Rated Entity was given the opportunity to review the Credit Rating and Outlook and the principal grounds on which the Credit Rating and Outlook are based. Following that review, the Credit Rating was not amended before being issued.

Regulatory disclosures

This Credit Rating and Outlook is issued by Scope Ratings GmbH, Lennéstraße 5, D-10785 Berlin, Tel +49 30 27891-0. The Credit Rating and/or Outlook is UK endorsed.

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The Credit Rating/Outlook were first released by Scope Ratings on 10 September 2018. The Credit Rating/Outlook was last updated on 8 April 2020.

Potential conflicts

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