

**RATING ACTION COMMENTARY**

# Fitch Revises Banca Popolare di Sondrio's Outlook to Stable; Affirms at 'BB+'

Wed 01 Sep, 2021 - 12:11 ET

Fitch Ratings - Milan - 01 Sep 2021: Fitch Ratings has revised the Outlook on Banca Popolare di Sondrio's (Sondrio) Long-Term Issuer Default Rating (IDR) to Stable from Negative and affirmed the IDR at 'BB+' and Viability Rating (VR) at 'bb+'. A full list of rating actions is below.

The revision of the Outlook reflects our view that the pandemic-related downside risks for the bank's asset quality and profitability have eased. Sondrio's performance in 1H21 and our medium-term expectations for its performance should provide some headroom to absorb moderate deterioration of its profitability and asset quality that may arise from the remaining pandemic-related risks to the economic recovery in Italy.

**KEY RATING DRIVERS****IDRS, VR AND SENIOR PREFERRED DEBT**

Sondrio's ratings reflect its still weak asset quality and modest profitability. However, we expect that the bank's average risk appetite and its credible impaired loan strategy should mitigate asset quality pressure from the pandemic, and that profitability should benefit from loan impairment charges (LICs) remaining under control and strategic initiatives aimed at improving earnings generation.

The ratings also reflect the bank's satisfactory regulatory capitalisation and our expectation that it will maintain capital ratios with ample buffers over requirements.

Sondrio benefits from adequate franchises in its regions of operations, which results in a stable customer deposit base, underpinning a sound funding and liquidity profile.

Sondrio's asset quality is a rating weakness, with an impaired loan ratio of around 7% at end-June 2021, which is higher than the domestic industry average of around 6% and weak compared with international peers. The impaired loans reserve coverage ratio of over 62% at end-June 2021 is adequate for the bank's credit risks.

We expect Sondrio's impaired loan ratio to remain under control, even in case of a weaker-than-expected economic recovery in Italy, as the bank should be able to compensate possible asset quality deterioration once the government support measures gradually unwind through a combination of sales and effective workout. Furthermore, the bank's contained amount of loan moratoria at end-June 2021, at below 4% of gross performing loans, and better-than-expected performance of loan moratoria with limited default rates to date should mitigate near- to medium-term risks.

Sondrio's operating profitability is modest by international standards and compared with stronger domestic rated banks, despite good cost efficiency. Its operating profit/risk-weighted assets (RWA) recovered to around 2.0% in 1H21 from 0.7% in 2020, due to re-established business activities, increased core revenue and the positive contribution of securities investments. In 1H21, LICs decreased by over 40% yoy (including 1H20 losses from the doubtful loans disposal). The benign impaired loan inflows and improving macroeconomic scenario allowed for some releases of provisions in 1H21, which could continue in the coming quarters and sustain the bank's profits.

The improved 1H21 performance suggests that the bank is in a position to benefit from the economic recovery in Italy. We expect profitability to stabilise at around 1% of RWA in the medium term, benefiting from higher business volumes if the economy rebounds in line with our current expectations, continuing use of the Targeted-Longer Term Refinancing Operations (TLTRO) facilities to mitigate pressure on the interest margin, a strategy aimed at expanding wealth management activities and ongoing cost efficiency.

Sondrio's capitalisation is satisfactory, with a common equity Tier 1 (CET1) ratio of 16.7% at end-June 2021, sustained by acceptable earning generation and historically prudent dividend payouts, which allowed to maintain ample buffers over regulatory requirements. Capital encumbrance by unreserved impaired loans improved to below 28% at end-June 2021 from its peak of 74% at end-2016, and we expect it to remain under control, in line with our expectations on asset quality. However, capitalisation remains at risk from large exposure to Italian government bond holdings at about 240% of CET1 capital at end-June 2021.

The bank's funding and liquidity profile is sound. Customer deposits are a stable source of funding, benefiting from the bank's adequate franchise in its home regions and strong client relationships. Funding sources are increasingly diversified through the bank's access to both secured and unsecured wholesale funding markets. Liquidity remains sound, thanks to adequate buffers of unencumbered eligible assets and access to ECB financing.

Sondrio's 'B' Short-Term IDR is the only option mapping to a 'BB+' Long-Term IDR.

Sondrio's long-term senior preferred notes are rated in line with the bank's Long-Term IDR. We expect the bank to use senior preferred debt to meet its minimum requirement for own funds and eligible liabilities. We also do not expect the bank to build up buffers of subordinated and senior non-preferred debt in excess of 10% of RWA, which is required under our criteria to rate senior preferred debt above the Long-Term IDR.

## DEPOSIT RATINGS

Sondrio's 'BBB-' long-term deposit rating is one-notch above the bank's Long-Term IDR to reflect protection from lower-ranking senior preferred and Tier 2 debt buffer, as full depositor preference is in force in Italy. The one-notch uplift also reflects our expectation that the bank will maintain these buffers, given the need to comply with minimum requirement for own funds and eligible liabilities. The short-term deposit rating of 'F3' is in line with our rating correspondence table for banks with 'BBB-' long-term deposit ratings.

## SUBORDINATED DEBT

Tier 2 debt is rated two notches below Sondrio's VR to reflect poor recovery prospects. No notching is applied for incremental non-performance risk because 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.

## SUPPORT RATING AND SUPPORT RATING FLOOR

The Support Rating (SR) of '5' and Support Rating Floor (SRF) of 'No Floor' reflect Fitch's view that although external support is possible, it cannot be relied upon. Senior creditors can no longer expect to receive full extraordinary support from the sovereign in the event that the bank becomes non-viable. The EU's Bank Recovery and Resolution Directive and the Single Resolution Mechanism for eurozone banks provide a framework for the resolution of banks that requires senior creditors to participate in losses, if necessary, instead of or ahead of a bank receiving sovereign support.

## RATING SENSITIVITIES

### IDRS, VR AND SENIOR PREFERRED DEBT

Factors that could, individually or collectively, lead to positive rating action/upgrade:

While rating upside is currently limited, a stronger and more stable operating environment combined with improved asset quality could be positive for the ratings. These factors would have to be accompanied by more diversified income sources, supporting sustained profitability enhancement.

We would upgrade the long-term senior preferred debt by one notch if resolution buffers were to be met with senior non-preferred debt and more junior instruments or if the size of the combined buffer of junior and senior non-preferred debt is expected to exceed 10% of RWAs on a sustained basis.

Factors that could, individually or collectively, lead to negative rating action/downgrade:

Sondrio's ratings remain sensitive to a significant weakening of the operating environment in Italy, which would result in a prolonged and substantial damage to the bank's asset quality and earnings causing significant capital erosion, including from higher-than-expected capital encumbrance from unreserved impaired loans. The bank's ratings could be downgraded if we expect its CET1 ratio to edge closer to 13% and its impaired loan ratio deteriorates to above 10%, especially if these result in capital encumbrance by impaired loans to increase close to or above 50%, without the prospect of recovery in the short term.

### SR AND SRF

An upgrade of the SR and upward revision of the SRF 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.

### DEPOSIT RATINGS

The deposit ratings would likely be downgraded if the bank's Long-Term IDR was downgraded. The deposit ratings are also sensitive to a reduction in the size of the senior and junior debt buffers to below 10% of RWAs.

### SUBORDINATED DEBT

The subordinated debt rating is primarily sensitive to changes in the VR, from which it is notched. The rating is also sensitive to a 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.

## BEST/WORST CASE RATING SCENARIO

International scale credit ratings of Financial Institutions and Covered Bond issuers have a best-case rating upgrade scenario (defined as the 99th percentile of rating transitions, measured in a positive direction) of three notches over a three-year rating horizon; and a worst-case rating downgrade scenario (defined as the 99th percentile of rating transitions, measured in a negative direction) of four notches over three years. The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Best- and worst-case scenario credit ratings are based on historical performance. For more information about the methodology used to determine sector-specific best- and worst-case scenario credit ratings, visit <https://www.fitchratings.com/site/re/10111579>

## 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

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)

## RATING ACTIONS

ENTITY/DEBT	RATING		PRIOR	
Banca Popolare di Sondrio-Societa' Cooperativa per Azioni	LT IDR	BB+ Rating Outlook Stable	Affirmed	BB+ Rating Outlook Negative
	ST IDR	B	Affirmed	B

ENTITY/DEBT	RATING			PRIOR
	Viability	bb+	Affirmed	bb+
	Support	5	Affirmed	5
	Support	NF	Affirmed	NF

[VIEW ADDITIONAL RATING DETAILS](#)

## FITCH RATINGS ANALYSTS

### Valeria Pasto

Director

Primary Rating Analyst

International

+39 02 879087 298

valeria.pasto@fitchratings.com

Fitch Ratings Ireland Limited Sede Secondaria Italiana

Via Morigi, 6 Ingresso Via Privata Maria Teresa, 8 Milan 20123

### Manuela Banfi

Associate Director

Secondary Rating Analyst

+39 02 879087 202

manuela.banfi@fitchratings.com

### Olivia Perney

Managing Director

Committee Chairperson

+33 1 44 29 91 74

olivia.perney@fitchratings.com

## MEDIA CONTACTS

### Louisa Williams

London

+44 20 3530 2452

louisa.williams@thefitgroup.com

Additional information is available on [www.fitchratings.com](http://www.fitchratings.com)

## PARTICIPATION STATUS

The rated entity (and/or its agents) or, in the case of structured finance, one or more of the transaction parties participated in the rating process except that the following issuer(s), if any, did not participate in the rating process, or provide additional information, beyond the issuer's available public disclosure.

## APPLICABLE CRITERIA

[Bank Rating Criteria \(pub. 28 Feb 2020\) \(including rating assumption sensitivity\)](#)

## ADDITIONAL DISCLOSURES

[Dodd-Frank Rating Information Disclosure Form](#)

[Solicitation Status](#)

[Endorsement Policy](#)

## ENDORSEMENT STATUS

Banca Popolare di Sondrio-Societa' Cooperativa per Azioni

EU,UK Endorsed

## DISCLAIMER

ALL FITCH CREDIT RATINGS ARE SUBJECT TO CERTAIN LIMITATIONS AND DISCLAIMERS. PLEASE READ THESE LIMITATIONS AND DISCLAIMERS BY FOLLOWING THIS LINK:

[HTTPS://WWW.FITCHRATINGS.COM/UNDERSTANDINGCREDITRATINGS](https://www.fitchratings.com/understandingcreditratings). IN ADDITION, THE FOLLOWING [HTTPS://WWW.FITCHRATINGS.COM/RATING-DEFINITIONS-DOCUMENT](https://www.fitchratings.com/rating-definitions-document) DETAILS FITCH'S RATING DEFINITIONS FOR EACH RATING SCALE AND RATING CATEGORIES, INCLUDING DEFINITIONS RELATING TO DEFAULT. PUBLISHED RATINGS, CRITERIA, AND METHODOLOGIES ARE AVAILABLE FROM THIS SITE AT ALL TIMES. FITCH'S CODE OF CONDUCT, CONFIDENTIALITY, CONFLICTS OF INTEREST, AFFILIATE FIREWALL, COMPLIANCE, AND OTHER RELEVANT POLICIES AND PROCEDURES ARE ALSO AVAILABLE FROM THE CODE OF CONDUCT SECTION OF THIS SITE. DIRECTORS AND SHAREHOLDERS RELEVANT INTERESTS ARE AVAILABLE AT [HTTPS://WWW.FITCHRATINGS.COM/SITE/REGULATORY](https://www.fitchratings.com/site/regulatory). FITCH MAY HAVE PROVIDED ANOTHER PERMISSIBLE SERVICE OR ANCILLARY SERVICE TO THE RATED ENTITY OR ITS RELATED THIRD PARTIES. DETAILS OF PERMISSIBLE SERVICE(S) FOR WHICH THE LEAD ANALYST IS BASED IN AN ESMA- OR FCA- REGISTERED FITCH RATINGS COMPANY (OR BRANCH OF SUCH A COMPANY) OR ANCILLARY SERVICE(S) CAN BE FOUND ON THE ENTITY SUMMARY PAGE FOR THIS ISSUER ON THE FITCH RATINGS WEBSITE.

## READ LESS

**COPYRIGHT**

Copyright © 2021 by Fitch Ratings, Inc., Fitch Ratings Ltd. and its subsidiaries. 33 Whitehall Street, NY, NY 10004. Telephone: 1-800-753-4824, (212) 908-0500. Fax: (212) 480-4435. Reproduction or retransmission in whole or in part is prohibited except by permission. All rights reserved. In issuing and maintaining its ratings and in making other reports (including forecast information), Fitch relies on factual information it receives from issuers and underwriters and from other sources Fitch believes to be credible. Fitch conducts a reasonable investigation of the factual information relied upon by it in accordance with its ratings methodology, and obtains reasonable verification of that information from independent sources, to the extent such sources are available for a given security or in a given jurisdiction. The manner of Fitch's factual investigation and the scope of the third-party verification it obtains will vary depending on the nature of the rated security and its issuer, the requirements and practices in the jurisdiction in which the rated security is offered and sold and/or the issuer is located, the availability and nature of relevant public information, access to the management of the issuer and its advisers, the availability of pre-existing third-party verifications such as audit reports, agreed-upon procedures letters, appraisals, actuarial reports, engineering reports, legal opinions and other reports provided by third parties, the availability of independent and competent third-party verification sources with respect to the particular security or in the particular jurisdiction of the issuer, and a variety of other factors. Users of Fitch's ratings and reports should understand that neither an enhanced factual investigation nor any third-party verification can ensure that all of the information Fitch relies on in connection with a rating or a report will be accurate and complete. Ultimately, the issuer and its advisers are responsible for the accuracy of the information they provide to Fitch and to the market in offering documents and other reports. In issuing its ratings and its reports, Fitch must rely on the work of experts, including independent auditors with respect to financial statements and attorneys with respect to legal and tax matters. Further, ratings and forecasts of financial and other information are inherently forward-looking and embody assumptions and predictions about future events that by their nature cannot be verified as facts. As a result, despite any verification of current facts, ratings and forecasts can be affected by future events or conditions that were not anticipated at the time a rating or forecast was issued or affirmed.

The information in this report is provided "as is" without any representation or warranty of any kind, and Fitch does not represent or warrant that the report or any of its contents will meet any of the requirements of a recipient of the report. A Fitch rating is an opinion as to the creditworthiness of a security. This opinion and reports made by Fitch are based on established criteria and methodologies that Fitch is continuously evaluating and updating. Therefore, ratings and reports are the collective work product of Fitch and no individual, or group of individuals, is solely responsible for a rating or a report. The rating does not address the risk of loss due to risks other than credit risk,



unless such risk is specifically mentioned. Fitch is not engaged in the offer or sale of any security. All Fitch reports have shared authorship. Individuals identified in a Fitch report were involved in, but are not solely responsible for, the opinions stated therein. The individuals are named for contact purposes only. A report providing a Fitch rating is neither a prospectus nor a substitute for the information assembled, verified and presented to investors by the issuer and its agents in connection with the sale of the securities. Ratings may be changed or withdrawn at any time for any reason in the sole discretion of Fitch. Fitch does not provide investment advice of any sort. Ratings are not a recommendation to buy, sell, or hold any security. Ratings do not comment on the adequacy of market price, the suitability of any security for a particular investor, or the tax-exempt nature or taxability of payments made in respect to any security. Fitch receives fees from issuers, insurers, guarantors, other obligors, and underwriters for rating securities. Such fees generally vary from US\$1,000 to US\$750,000 (or the applicable currency equivalent) per issue. In certain cases, Fitch will rate all or a number of issues issued by a particular issuer, or insured or guaranteed by a particular insurer or guarantor, for a single annual fee. Such fees are expected to vary from US\$10,000 to US\$1,500,000 (or the applicable currency equivalent). The assignment, publication, or dissemination of a rating by Fitch shall not constitute a consent by Fitch to use its name as an expert in connection with any registration statement filed under the United States securities laws, the Financial Services and Markets Act of 2000 of the United Kingdom, or the securities laws of any particular jurisdiction. Due to the relative efficiency of electronic publishing and distribution, Fitch research may be available to electronic subscribers up to three days earlier than to print subscribers.

For Australia, New Zealand, Taiwan and South Korea only: Fitch Australia Pty Ltd holds an Australian financial services license (AFS license no. 337123) which authorizes it to provide credit ratings to wholesale clients only. Credit ratings information published by Fitch is not intended to be used by persons who are retail clients within the meaning of the Corporations Act 2001

Fitch Ratings, Inc. is registered with the U.S. Securities and Exchange Commission as a Nationally Recognized Statistical Rating Organization (the "NRSRO"). While certain of the NRSRO's credit rating subsidiaries are listed on Item 3 of Form NRSRO and as such are authorized to issue credit ratings on behalf of the NRSRO (see <https://www.fitchratings.com/site/regulatory>), other credit rating subsidiaries are not listed on Form NRSRO (the "non-NRSROs") and therefore credit ratings issued by those subsidiaries are not issued on behalf of the NRSRO. However, non-NRSRO personnel may participate in determining credit ratings issued by or on behalf of the NRSRO.

[READ LESS](#)

## SOLICITATION STATUS

The ratings above were solicited and assigned or maintained by Fitch at the request of the rated entity/issuer or a related third party. Any exceptions follow below.

## ENDORSEMENT POLICY

Fitch's international credit ratings produced outside the EU or the UK, as the case may be, are endorsed for use by regulated entities within the EU or the UK, respectively, for regulatory purposes, pursuant to the terms of the EU CRA Regulation or the UK Credit Rating Agencies (Amendment etc.) (EU Exit) Regulations 2019, as the case may be.

Fitch's approach to endorsement in the EU and the UK can be found on Fitch's [Regulatory Affairs](#) page on Fitch's website. The endorsement status of international credit ratings is provided within the entity summary page for each rated entity and in the transaction detail pages for structured finance transactions on the Fitch website. These disclosures are updated on a daily basis.

---

[Structured Finance: Covered Bonds](#)   [Structured Finance](#)   [Banks](#)   [Europe](#)   [Italy](#)

---