

Research Update:

# MedioCredito Centrale Affirmed; Outlook Still Negative On Risk Of Weak Recovery And Banca Popolare di Bari Integration

October 29, 2020

## Overview

- On Oct. 23, S&P Global Ratings affirmed its 'BBB/A-2' ratings on Italy and revised the outlook to stable from negative.
- While this removes a key risk to the ratings on MedioCredito Centrale (MCC), we continue to see potential constraints to its earnings, capital, and asset quality if the economic recovery is significantly delayed. Additional risks might also relate to the integration of recently acquired Banca Popolare di Bari (BPB).
- We are affirming our ratings on MCC.
- The outlook remains negative, primarily reflecting our view that the cyclical economic recovery could be substantially weaker or delayed compared with our current expectations, which would imply a far more negative effect on MCC's creditworthiness.

## Rating Action

On Oct. 29, 2020, S&P Global Ratings affirmed its 'BBB-/A-3' long- and short-term issuer credit ratings on Italy-based government-related bank MedioCredito Centrale SpA (MCC). The outlook remains negative.

## Rationale

The affirmation follows the recent rating action on Italy (see "Italy Outlook Revised To Stable From Negative; Ratings Affirmed At 'BBB/A-2'"), as well as our updated macroeconomic view of Italy. We consider that the revision of the outlook on Italy to stable removes a key risk for the ratings on MCC as they incorporate two notches of government support. Conversely, further evolution of the pandemic in Italy and the potential introduction of new restrictive measures could heighten pressure on Italy's ongoing recovery in the coming months and may constrain our existing

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forecast. This would be particularly detrimental for the recovery of Italian banks' asset quality. We currently project that Italian GDP will fall by 8.9% in 2020, gradually bouncing back from 2021 and 2022 and returning to 2019 levels in 2023.

We affirmed the ratings on MCC because we continue to believe that its profitability and capital buffer would be sufficient to absorb the rising credit losses we project over 2020-2021. Positively, we expect 2020 to be an exceptional year for MCC's profitability, owing to unprecedented fee income related to the management of the public "Fondo di Garanzia" (FdG). The fund, which the Italian government strengthened as part of its measures to support the economy, experienced a significant increase in applications in 2020. As of October 2020, MCC received (and granted) slightly over a million guarantee applications. This equates to the total number of guarantees granted cumulatively over the previous 20 years.

We believe that MCC will likely remain susceptible to the deteriorating economic conditions in Italy, largely due to its high exposure to small and midsize enterprises, which we consider to be particularly vulnerable to coronavirus-related stress. As of June 2020, about 55% of its customer loans are to corporate borrowers concentrated in Southern Italy.

The government's €430 million capital injection into MCC to support the acquisition of troubled Southern Italian bank BPB represented a significant capital enhancement from its equity base of about €300 million as of end-2019. However, we understand that MCC will use these funds to support the restructuring of BPB. There is still some uncertainty regarding the overall impact of the BPB integration on MCC's creditworthiness. Once we have more visibility on the combined entity's financials and strategic plan, we will reassess whether the government's capital injection will sufficiently offset the potential negative effect of the integration on MCC's financial profile.

## **Outlook**

The negative outlook on MCC reflects the increased pressure on the bank's revenue and asset quality amid the pandemic, as well as significant risks we see to our base-case expectations over the next two years. It also reflects our view that the acquisition and integration of BPB could have negative repercussions for MCC's stand-alone creditworthiness.

## **Downside scenario**

We could lower the ratings on MCC by up to two notches over the next 12-24 months if we concluded that the bank's financial profile had meaningfully deteriorated following a weaker economic recovery or a deeper and more prolonged downturn than we currently expect, or if we believed that the integration with BPB was likely to substantially erode the bank's capitalization or tarnish its risk profile.

## **Upside scenario**

Alternatively, we could revise our outlook on MCC to stable over the next 12-24 months if we believed that the economic fallout of the pandemic would not affect its creditworthiness, providing that the risks and uncertainties related to the acquisition and integration of BPB had materially abated.

## Ratings Score Snapshot

Issuer Credit Rating	BBB-/Negative/A-3
SACP	bb
Anchor	bbb-
Business Position	Moderate (-1)
Capital and Earnings	Strong (+1)
Risk Position	Moderate (-1)
Funding and Liquidity	Below Average and (-1) Adequate
<b>Support</b>	<b>(+2)</b>
ALAC Support	(0)
GRE Support	(+2)
Group Support	(0)
Sovereign Support	(0)
Additional Factors	(0)

## Related Criteria

- General Criteria: Group Rating Methodology, July 1, 2019
- Criteria | Financial Institutions | General: Risk-Adjusted Capital Framework Methodology, July 20, 2017
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- General Criteria: Rating Government-Related Entities: Methodology And Assumptions, March 25, 2015
- Criteria | Financial Institutions | Banks: Quantitative Metrics For Rating Banks Globally: Methodology And Assumptions, July 17, 2013
- Criteria | Financial Institutions | Banks: Banking Industry Country Risk Assessment Methodology And Assumptions, Nov. 9, 2011
- Criteria | Financial Institutions | Banks: Banks: Rating Methodology And Assumptions, Nov. 9, 2011
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

## Related Research

- Italy Outlook Revised To Stable From Negative; Ratings Affirmed At 'BBB/A-2', Oct. 23, 2020
- EMEA Financial Institutions Monitor 4Q2020: Banks Prepare As Winter Is Coming, Oct. 23, 2020
- How COVID-19 Is Affecting Bank Ratings: October 2020 Update, Oct. 22, 2020

- Economic Research: European Economic Snapshots: A Second COVID-19 Wave Is Dampening The Recovery, Oct. 14, 2020
- COVID-19 Puts The Brakes On Capital Strengthening For The 50 Largest European Banks, Oct. 14, 2020
- Banking Horizons Europe 2020: COVID-19 As A Catalyst For Change, Oct. 13, 2020
- European Bank Asset Quality: Half Year Results Tell Only Half The Story, Sept. 28, 2020
- The Impact Of MedioCredito Centrale's Acquisition Of Banca Popolare di Bari Is Still Uncertain, Jul. 2, 2020
- Outlooks On Most Italian Banks Now Negative On Deepening COVID-19 Downside Risks, April 29, 2020
- MedioCredito Centrale SpA, Feb. 4, 2020

## Ratings List

### Ratings Affirmed

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#### MedioCredito Centrale SpA

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Issuer Credit Rating BBB-/Negative/A-3

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#### MedioCredito Centrale SpA

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Senior Unsecured BBB-

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