

**RATING ACTION COMMENTARY**

# **Fitch Upgrades Mediobanca to 'BBB'/Stable on Sovereign Upgrade**

Fri 17 Dec, 2021 - 8:51 AM ET

Fitch Ratings - Milan - 17 Dec 2021: Fitch Ratings has upgraded Mediobanca - Banca di Credito Finanziario SPA's Long-Term Issuer Default Rating (IDR) to 'BBB' from 'BBB-' and its Viability Rating (VR) to 'bbb' from 'bbb-'. The Outlook on the Long-Term IDR is Stable. A full list of rating actions is below.

The rating action follows the upgrade of Italy's sovereign rating to 'BBB'/Stable from 'BBB-'/Stable (see "Fitch Upgrades Italy to 'BBB'; Outlook Stable" dated 3 December 2021 at [www.fitchratings.com](http://www.fitchratings.com)).

Italy's sovereign upgrade and its stronger economic performance and prospects also supported the revision of the operating environment score for Italian banks to 'bbb' from 'bbb-'.

Fitch has withdrawn Mediobanca's Support Rating of '5' and Support Rating Floor of 'No Floor' as they are no longer relevant to the agency's coverage following the publication of its updated Bank Rating Criteria on 12 November 2021.

## **KEY RATING DRIVERS**

IDRS, VR and DERIVATIVE COUNTERPARTY RATING (DCR)

The ratings upgrade primarily reflects the benefits to Mediobanca's risk profile from operating in a stronger and more stable operating environment, which should result in reduced risks in combination with its conservative underwriting standards. This is because we believe the Italian economy and Italian sovereign risk have a significant influence on Mediobanca's credit profile. It also reflects the benefits to the bank's funding profile and market access as these are influenced by the improved market perception of Italian sovereign risk. Mediobanca's VR is one notch above the 'bbb-' implied rating, driven by a risk profile adjustment assessed by Fitch at 'bbb'.

The upgrade also reflects Fitch's view that pandemic-related risks on Mediobanca's asset quality and earnings have eased, and that its solid capitalisation has sufficient headroom to absorb pressure arising from the residual uncertainties caused by the pandemic. We expect the Italian economy to fully recover to pre-pandemic levels early next year and economic growth to be above recent averages thereafter throughout the rating horizon, which we consider supportive of the bank's performance and risk profile.

Mediobanca's ratings continue to reflect a specialised business model with strong competitive positions in selected businesses and a moderate risk profile, which underpin the bank's better operating profitability and asset quality than domestic peers' through the cycle.

Mediobanca is a leading corporate and investment bank and consumer lender in Italy and is expanding its wealth management franchise domestically, mainly in the affluent and private segment with around EUR50 billion of assets under management and administration. The bank is also expanding its customer deposits base in Italy through CheBanca!, although its national market share remains small.

The bank's credit profile benefits from sound capitalisation (common equity Tier 1 (CET1) ratio of 16.1% at end-September 2021, one of the highest among domestic rated banks) and our expectation that capitalisation will remain resilient. In our capital assessment, we also consider the bank's low encumbrance by unreserved impaired loans (3.7% at end-June 2021). Unlike most domestic peers, holdings of Italian government bonds are modest and therefore do not affect our assessment of capitalisation. The bank also benefits from a stable funding and liquidity profile and above-average diversification domestically due to established market access.

Corporate lending exposes the bank to some idiosyncratic risk but Mediobanca's conservative underwriting has resulted in stable, low levels of impaired loans, despite a challenging operating environment. The impaired loan ratio was 4% at end-June 2021 and

coverage levels were high at 85% relative to peers. We expect stable asset-quality dynamics in 2022, although the bank still retains large pandemic-related loan loss allowance overlays (more than EUR300 million), largely against consumer lending exposures.

Mediobanca's operating profitability has been more resilient to the low-interest-rate environment than other domestic banks, due to its diverse business model with increased fee generation from wealth management operations. Profitability has recovered ahead of initial expectations in 3Q21, thanks to growing revenues and business volumes. We expect it to remain at these levels in the coming quarters, with average operating profit/risk-weighted assets (RWAs) comfortably above the 2% threshold. Consumer loans in particular are on their way back to pre-Covid-19 levels and with a more favourable loan mix supporting margins.

Mediobanca's Short-Term IDR of 'F3' is the baseline option for a Long-Term IDR of 'BBB' because the funding and liquidity score is not high enough to achieve the higher short-term rating.

Mediobanca's DCR is at the same level as the IDRs as derivative counterparties in Italy have no preferential legal status over senior debt in liquidation.

## **RATING SENSITIVITIES**

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

IDRS, VR AND DCR

Mediobanca's largely domestic focus means ratings are sensitive to a downgrade of Italy's rating or to a downgrade of our assessment of Italy's operating environment.

The ratings could be downgraded if Mediobanca's CET1 ratio falls below 13% without the prospect of recovery in the short term and with unreserved impaired loans rising substantially above the current low levels on a sustained basis. This weakening of capitalisation could be caused by a prolonged damage to the bank's asset quality and earnings.

The ratings could also be downgraded if Mediobanca's risk profile worsened materially, for example, if the bank became more aggressive in its underwriting standards, including in riskier asset classes.

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

Rating upgrades for Mediobanca are contingent upon an Italian sovereign upgrade and on a much stronger business and risk profile (i.e. as represented by an impaired loan ratio kept consistently below 3% and operating profit/RWAs at least above 3%). The ratings could also be upgraded if stronger financial metrics were accompanied by stronger capitalisation with a CET1 ratio consistently above 17%.

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

### DEPOSIT RATINGS

The Long-Term Deposit Rating has been upgraded by one notch and is one notch above Mediobanca's Long-Term IDR to reflect protection from senior and subordinated debt and equity buffers. The 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 (MREL).

The Short-Term Deposit Rating of 'F2' is the baseline option for a Long-Term Deposit Rating of 'BBB+' because the funding and liquidity score is not high enough to achieve the higher equivalent short-term rating.

### SENIOR PREFERRED AND SENIOR NON-PREFERRED DEBT

Mediobanca's senior non-preferred (SNP) debt is rated one notch below the Long-Term IDR to reflect the risk of below-average recoveries arising from the use of senior preferred (SP) debt to meet resolution buffer requirements and the combined buffer of additional Tier 1, Tier 2 and SNP debt being unlikely to exceed 10% of RWAs. For the same reason, the rating of SP debt is in line with the Long-Term IDR. The SP and SNP debt rating have been upgraded by one notch in line with the same rating action on the bank's Long-Term IDR.

The SP short-term debt rating of 'F3' is in line with the Short-Term IDR.

### SUBORDINATED DEBT

Tier 2 subordinated 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. The Tier 2 subordinated debt has been upgraded by one notch in line with the same rating action on the VR.

## GOVERNMENT SUPPORT RATING

In line with the updated criteria, we have assigned Mediobanca a Government Support Rating (GSR) of 'No Support', which reflects its view that although external extraordinary sovereign 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 (BRRD) and the Single Resolution Mechanism (SRM) 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**

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

#### SP, SNP AND DEPOSIT RATINGS

The SP, SNP debt and Deposit Ratings are primarily sensitive to changes in the bank's Long-Term IDR, and would be downgraded if the Long-Term IDR is downgraded. The Long-Term Deposit Rating is also sensitive to a reduction in the size of the senior and junior debt buffers, although we view this unlikely in light of Mediobanca's current and future MREL requirements and the sizeable actual buffers versus regulatory requirements.

The rating of Tier 2 debt is primarily sensitive to changes in the bank's VR, from which it is notched, and would be downgraded if the VR is downgraded. The rating is also sensitive to a change in the notes' notching, which could arise if Fitch changes its assessment of their non-performance risk relative to that captured in the VR.

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

The SP, SNP debt and Deposit Ratings are primarily sensitive to changes in the bank's Long-Term IDR and would be upgraded if the Long-Term IDR were upgraded.

The SP and SNP debt ratings could also be upgraded by one notch if at some point Mediobanca is expected to meet its resolution buffer requirements with SNP and more junior instruments.

The rating of Tier 2 debt is primarily sensitive to changes in the bank's VR, from which it is notched, and would be upgraded if the VR is upgraded.

## GSR

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.

## **SUBSIDIARIES & AFFILIATES: KEY RATING DRIVERS**

The ratings of the SP debt issued by Mediobanca International (Luxembourg) SA are equalised with the parent's IDRs since the debt is unconditionally and irrevocably guaranteed by Mediobanca. Fitch expects the parent to honour this guarantee.

## **SUBSIDIARIES AND AFFILIATES: RATING SENSITIVITIES**

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

The ratings of the SP debt issued by Mediobanca International (Luxembourg) SA are sensitive to the same factors that affect the SP debt issued by the parent and would be downgraded if the parent is downgraded.

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

The ratings of the SP debt issued by Mediobanca International (Luxembourg) SA are sensitive to the same factors that affect the SP debt issued by the parent and would be upgraded if the parent is upgraded.

## **VR ADJUSTMENTS**

The 'Asset Quality' score of 'bbb-' has been assigned above the 'bb' category implied score due to the following adjustment reasons: Underwriting standards and growth (positive).

The 'Funding & Liquidity' score of 'bbb' has been assigned below the 'b' and below category implied score due to the following adjustment reason: Non-Deposit Funding (positive).

## **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 ⇅                    |
|---|-----------|---------------------------|-----------|----------------------------|
| Mediobanca - Banca di Credito Finanziario SPA | LT IDR    | BBB Rating Outlook Stable |           | BBB- Rating Outlook Stable |
|   | Upgrade   |                           |           |                            |
|   | ST IDR    | F3                        | Affirmed  | F3                         |
|   | Viability | bbb                       | Upgrade   | bbb-                       |
|   | Support   | WD                        | Withdrawn | 5                          |

|  |                    |          |            |           |
|--|--------------------|----------|------------|-----------|
|  | Support Floor      | WD       | Withdrawn  | NF        |
|  | DCR                | BBB(dcr) | Upgrade    | BBB-(dcr) |
|  | Government Support | ns       | New Rating |           |
| subordinated                             | LT                 | BB+      | Upgrade    | BB        |
| long-term deposits                       | LT                 | BBB+     | Upgrade    | BBB       |
| Senior preferred                         | LT                 | BBB      | Upgrade    | BBB-      |
| Senior non-preferred                     | LT                 | BBB-     | Upgrade    | BB+       |
| Senior preferred                         | LT                 | BBB(EXP) | Upgrade    | BBB-(EXP) |
| Senior preferred                         | ST                 | F3       | Affirmed   | F3        |
| short-term deposits                      | ST                 | F2       | Upgrade    | F3        |
| Mediobanca International (Luxembourg) SA |                    |          |            |           |
| Senior preferred                         | LT                 | BBB      | Upgrade    | BBB-      |
| Senior preferred                         | ST                 | F3       | Affirmed   | F3        |

[VIEW ADDITIONAL RATING DETAILS](#)



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any, did not participate in the rating process, or provide additional information, beyond the issuer's available public disclosure.

## **APPLICABLE CRITERIA**

[Bank Rating Criteria \(pub. 12 Nov 2021\) \(including rating assumption sensitivity\)](#)

## **ADDITIONAL DISCLOSURES**

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Mediobanca International (Luxembourg) SA

EU Issued, UK Endorsed

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