FitchRatings

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Fitch Affirms Mediobanca at 'BBB-'/Stable

Fitch Ratings - Milan - 04 Feb 2021: Fitch Ratings has affirmed Mediobanca S.p.A.'s (Mediobanca) Long-Term Issuer Default Rating (IDR) at 'BBB-' with a Stable Outlook and Viability Rating (VR) at bbb-'.

The affirmation of Mediobanca reflects Fitch's view that its ratings have sufficient headroom at the current level, due mainly to its solid capitalisation being able to absorb the pressures on asset quality and profitability stemming from the economic fallout from the coronavirus pandemic.

Key Rating Drivers

IDRS, VR, DERIVATIVE COUNTERPARTY RATING (DCR) AND SENIOR DEBT

Mediobanca's ratings reflect a specialised business model with strong competitive positions in selected businesses and a moderate risk appetite, which underpin the bank's better operating profitability and asset quality relative to domestic peers' through the cycle. The ratings are supported by strong capitalisation relative to its VR and our expectation that it will remain resilient under various possible downside scenarios to our baseline.

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 EUR40 billion of assets under management and administration. The bank is also successfully expanding its customer deposits base in Italy through CheBanca!, although its national market share remains small. The acquisition of advisory firm Messier Maris & Associés (MMA) has enhanced international footprint of the bank's corporate and investment banking (CIB) activities, but it remains small relative to Mediobanca's domestic operations. The Italian economy and Italian sovereign risk have therefore a significant influence on Mediobanca's credit profile.

Mediobanca's capitalisation is a rating strength. Its common equity tier 1 (CET1) ratio of 16.2% at end-September 2020 was one of the highest among domestic rated banks' and has ample buffers over its Supervisory Review and Evaluation Process (SREP) requirement. Its fully loaded ratio of 14.6% at the same date is also satisfactory and provides comfortable loss absorption capacity, in our view, also considering the bank's low encumbrance by unreserved impaired loans. Unlike the majority of domestic peers, holdings of Italian government bonds are modest and therefore do not impact our assessment of capitalisation.

Asset quality slightly deteriorated in 2020 with moderate inflows of new impaired loans, mainly from its consumer business. Mediobanca's impaired loans ratio (excluding purchased loans) increased by about 30bp since end-December 2019 to 4.2% at end-September 2020, which compares well domestically. Asset-quality trends observed since then, including the positive evolution of moratoriums and some reclassifications of non-performing loans to performing status, may lead to a lower year-end impaired loans ratio.

Coverage by loan loss allowances was satisfactory at above 70%. Corporate lending exposes the bank to some idiosyncratic risk but Mediobanca's conservative underwriting, which has been tightened in response to the pandemic, has so far resulted in stable, low levels of impaired loans, despite a challenging operating environment.

Under our baseline scenario, we expect modest deterioration of Mediobanca's impaired loan ratio in the coming quarters. Our expectation considers the bank's tight control over credit risk and contained risk from outstanding loan moratoriums, which represented less than 3% of its gross loans at end-September 2020, well below domestic averages. However, the bank remains exposed to downside risks arising from persisting uncertainty over the economic environment in Italy, should it prove worse than our expectation.

Profitability is exposed to similar downside risks, in Fitch's opinion, as a weaker-than-expected economic recovery could put pressure on earnings generation and inflate loan impairment charges (LICs). Mediobanca's operating profitability proved more resilient to the low interest-rate environment than other domestic banks, due to a diverse business model with strong pricing power in consumer lending and increased fee generation from wealth management operations as well as operating cost restraint. We expect profitability to remain moderately below pre-crisis levels in the near-to-medium term given the still challenging economic environment.

We view Mediobanca's funding and liquidity as stable and diversified due to established market access, which allowed the bank to regularly issue debt also during 2020 and early 2021 with no additional burden on its funding costs. Its customer deposit base is smaller and less established than the largest domestic banks'. During 2020 central bank funding increased for Mediobanca, which we deem as more opportunistically motivated than for liquidity needs. Medium-term funding needs are manageable and liquidity is underpinned by adequate buffers of unencumbered eligible assets.

Mediobanca's Short-Term IDR and short-term senior debt ratings of 'F3' are in line with our rating correspondence table for banks with 'BBB-' Long-Term IDRs.

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.

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 more senior debt to meet resolution buffer requirements and the combined buffer of AT1, Tier 2 and SNP debt being unlikely to exceed 10% of risk-weighted assets (RWAs). For the same reason, the rating of senior preferred debt is in line with the Long-Term IDR.

SUBSIDIARY AND AFFILIATED COMPANIES

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

SUPPORT RATING AND SUPPORT RATING FLOOR

The Support Rating and Support Rating Floor reflect Fitch's 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 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.

DEPOSIT RATING

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

The 'F3' Short-Term Deposit Rating is the baseline option for a 'BBB' Long-Term Deposit Rating because the funding and liquidity score is not high enough to achieve the higher equivalent short-term rating corresponding to a 'BBB' Long-Term Deposit Rating.

SUBORDINATED DEBT AND OTHER HYBRID SECURITIES

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 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.

RATING SENSITIVITIES

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

Rating upgrades for Mediobanca are reliant on an Italian sovereign upgrade and easing pressures on asset quality and profitability resulting from the pandemic.

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

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

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

The ratings are also sensitive to the depth and duration of the economic crisis caused by the pandemic and its impact on the bank's financial profile and 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 currently 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 due to a delay in the recovery of Italy's economy.

SUBSIDIARY AND AFFILIATED COMPANIES

The ratings of the senior preferred debt issued by Mediobanca International (Luxembourg) SA are sensitive to the same factors that affect the senior preferred debt issued by the parent and would move in line with the parent's.

SUPPORT RATING AND SUPPORT RATING FLOOR

An upgrade of the Support Rating and upward revision of the Support Rating Floor 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 Rating is primarily sensitive to changes in the bank's IDR. 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.

SUBORDINATED DEBT AND OTHER HYBRID SECURITIES

The rating of T2 debt is primarily sensitive to changes in the bank's 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 risk relative to that 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/

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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.

Public Ratings with Credit Linkage to other ratings

The ratings of debt issued by Mediobanca International (Luxembourg) SA are driven by the ratings of the guarantor Mediobanca.

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

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Rating Actions

ENTITY/DEBT	RATING			RECOVERY	PRIOR
Mediobanca - Banca di Credito Finanziario SPA	LT IDR	BBB-	Affirmed		BBB-
	ST IDR	F3	Affirmed		F3
	Viability	bbb-	Affirmed		bbb-
	Support	5	Affirmed		5
	Support Floor	NF	Affirmed		NF
	DCR	BBB-(dcr)	Affirmed		BBB-(dcr)
• subordinated	LT	BB	Affirmed		BB
• long-term deposits	LT	BBB	Affirmed		BBB
• Senior preferred	LT	BBB-	Affirmed		BBB-

ENTITY/DEBT	RATING			RECOVERY	PRIOR
• Senior non-preferred	LT	BB+	Affirmed		BB+
• Senior preferred	ST	F3	Affirmed		F3
• short-term deposits	ST	F3	Affirmed		F3
Mediobanca International (Luxembourg) SA					
• Senior preferred	LT	BBB-	Affirmed		BBB-
• Senior preferred	ST	F3	Affirmed		F3

RATINGS KEY	OUTLOOK	WATCH
POSITIVE		
NEGATIVE		
EVOLVING		
STABLE		

Applicable Criteria

Bank Rating Criteria (pub.28 Feb 2020) (including rating assumption sensitivity)

Additional Disclosures

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Endorsement Status

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