MOODY'S
RATINGS

Rating Action: Moody's Ratings upgrades Abanca's ratings

05 Nov 2024

Madrid, November 05, 2024 -- Moody's Ratings (Moody's) has today upgraded the long-term deposit and senior unsecured debt ratings of ABANCA Corporacion Bancaria, S.A. (Abanca) to Baa2 from Baa3. The outlook on these ratings remains stable. At the same time, we have upgraded (1) the bank's Baseline Credit Assessment (BCA) and Adjusted BCA to baa3 from ba1; (2) the subordinated debt rating to Ba1 from Ba2; (3) the short-term deposit ratings to P-2 from P-3; and (4) the long-term Counterparty Risk Assessment (CR Assessment) and Counterparty Risk Ratings (CRRs) to A3(cr) and A3 from Baa1(cr) and Baa1 respectively. We have also affirmed the bank's short-term CR Assessment and CRR at P-2(cr) and P-2 respectively.

RATINGS RATIONALE

-- RATIONALE FOR THE BCA UPGRADE

The upgrade of Abanca's BCA to baa3 from ba1 is driven by the significant improvement of the bank's profitability which, coupled with the bank's decision to lower the pay-out ratio to 25% from 40% for the net profit generated in 2023 and 2024, has led to a reinforcement of the bank's capitalization which we expect to continue during the coming months.

Abanca's profitability has substantially benefited from the increase in interest rates initiated in late 2022, which has led to a widening of its customer margin by almost 200 bps between Q2 2022 and Q2 2024. Boosted by the increase in net interest income, the bank's return on assets (ROA calculated as net income over tangible assets) grew to 1.1% in 1H2024, which stands among the highest within Spanish peers. Going forward we expect Abanca's profitability to stabilize at more moderate levels of ROA between 0.5% and 0.75% in light of the central bank's ongoing policy easing, however well above its historical levels (average ROA of 0.3% in the 2019-22 period). Margin contraction will be partly compensated by improved business dynamics from a recovery in loan demand, and by stronger operational efficiency from the materialization of synergies stemming from the bank's recent acquisition.

The retention of a large part of the net profit generated in 2023 and 2024 has led to a material improvement in the bank's capitalization according to our key capital metric, tangible common equity (TCE)/risk-weighted assets. Although the TCE ratio remains weak, weighed down by a high exposure to deferred tax assets which amounted to 82% of the bank's Common Equity Tier 1 (CET1) capital as of June 2024, the ratio improved substantially to 8.7% from 7.4% during the 12 months ended in June 2024. We expect Abanca's internal capital generation to remain strong during 2H2024, allowing the bank to absorb the capital impact from the integration of Portuguese lender Eurobic in July (which we estimate at around 50 bps) and maintain the TCE ratio above 8% over the outlook period. Our view is underpinned by the bank's stated reference level of 13% for the common equity tier 1 (CET1) ratio. Such ratio stood at 12.8% as of the end of 3Q 2024.

The rating upgrade is also underpinned by the bank's good asset quality performance, despite pressures stemming from the high cost of living and more elevated debt burden for households and corporates since 2022. Abanca's problem loan ratio was 2.6% as of September 2024 which, excluding the integration of Eurobic in July which has a worse asset quality, has remained broadly stable for several years.

-- RATIONALE FOR THE UPGRADE OF THE DEPOSIT AND SENIOR UNSECURED DEBT RATINGS

The upgrade of Abanca's long-term deposit and senior unsecured debt ratings to Baa2 from Baa3 reflects: (1) the upgrade of the bank's BCA and Adjusted BCA to baa3 from ba1; (2) the unchanged outcome of our Advanced Loss Given Failure (LGF) analysis which results in a one-notch of uplift for both instruments; and (3) our assessment of low probability of government support, which results in no further uplift.

-- RATIONALE FOR THE STABLE OUTLOOK

The stable outlook on Abanca's long-term deposit and senior unsecured debt ratings reflects our view that the bank's expected credit performance over the next 12-18 months, which assumes a moderate deterioration in profitability, is already captured in the current ratings.

FACTORS THAT COULD LEAD TO AN UPGRADE OR DOWNGRADE OF THE RATINGS

Abanca's BCA could be upgraded principally as a result of a further material improvement of Moody's-calculated capital ratio.

Because the bank's deposit and senior unsecured debt ratings are linked to its BCA, a positive change in its BCA would likely lead to a rating upgrade. The deposit and senior unsecured debt ratings could also be upgraded following a significant increase in the stock of more junior bail-in-able liabilities.

Abanca's BCA could be principally downgraded if there were an increase in problem loans significantly above our current expectations, or if the bank engages in further inorganic growth which entails an erosion of its financial position.

Abanca's ratings could also be downgraded by changes in the liability structure that indicate a higher loss given failure to be faced by deposits or debt instruments.

PRINCIPAL METHODOLOGY

The principal methodology used in these ratings was Banks Methodology published in March 2024 and available at https://ratings.moodys.com/rmc-documents/409852 . Alternatively, please see the Rating Methodologies page on https://ratings.moodys.com for a copy of this methodology.

REGULATORY DISCLOSURES

For further specification of Moody's key rating assumptions and sensitivity analysis, see the sections Methodology Assumptions and Sensitivity to Assumptions in the disclosure form. Moody's Rating Symbols and Definitions can be found on https://ratings.moodys.com/rating-definitions .

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