

PRESS RELEASE

NOVEMBER 13, 2020

DBRS Morningstar Revises Trend on Banco Cooperativo to Negative; Confirms BBB (high) Long-Term Issuer Rating

BANKING ORGANIZATIONS

DBRS Ratings GmbH (DBRS Morningstar) confirmed the ratings of Banco Cooperativo Español S.A (BCE or the Bank), including the Long-Term Issuer Rating of BBB (high) and the Short-Term Issuer Rating of R-1 (low). The Trend has been revised to Negative from Stable. The Intrinsic Assessment (IA) for the Bank is BBB (high), while its Support Assessment remains SA3. A full list of rating actions is included at the end of this press release. The support Assessment is SA1 to reflect that BCE is part of the larger consolidated entity, GrucajRural Inversiones S.L. (the Group). A full list of rating actions is included at the end of this press release.

KEY RATING CONSIDERATIONS

The change of the trend to Negative reflects DBRS Morningstar's view that the wide and evolving scale of economic and market disruption resulting from the coronavirus (COVID-19) pandemic will have a negative effect on the operating environment for banks in Spain, including BCE and the members of the Asociación Española de Cajas Rurales (AECR). BCE performs an important role as the central clearing bank and liquidity provider for the members of the AECR. The COVID-19 crisis is likely to reverse some of the positive developments seen in recent years, and we expect BCE and AECR's revenues, asset quality and cost of risk to be negatively affected. The COVID-19 impact will likely emerge in the coming quarters. Downward rating pressure would intensify should the crisis be prolonged.

The ratings also reflect the Bank's low risk profile, its stable profitability, which allows it to build up capital through retained earnings, and the benefit it receives from its funding relationship with AECR members, who provide a stable deposit base. BCE's ratings also take into account the Bank's relatively small size and scope, its moderate business diversification and its sizeable risk concentration.

RATING DRIVERS

An upgrade of the Long-Term Issuer Rating is unlikely given the change in trend and the negative economic implications from the global pandemic. The trend on the Long-Term ratings could revert to Stable if the Bank's profitability metrics are not affected by the pandemic while maintaining capital ratios near to current levels.

A downgrade of the Long-Term Issuer Rating would also arise from a weakening in the Bank's profitability, which could arise from a prolonged deterioration in the AECR's earnings or material asset quality weakening of the members of the AECRs. Given its large exposure to Spanish sovereign bonds, a downgrade of Spain's sovereign rating could also have negative rating implications.

RATING RATIONALE

BCE acts as the central treasurer and liquidity provider for the members of the Asociación Española de Cajas Rurales (AECR), the largest cooperative Group in Spain by asset size. Moreover BCE's role within the AECR has been strengthened with the creation of

an Institutional Protection Scheme (IPS) between the members of the AECR, BCE and the Holding Company “GrucajRural Inversiones S.L.” in 2018. The IPS had a market share in Spain of around 3.3% of loans (EUR 40 billion) and around 3.4% of deposits (EUR 48 billion) at end-June 2020. Following the creation of the IPS, the members of the AECR sold their stake in BCE to the Holding Company “GrucajRural” (or consolidated Group). As result, the Holding Company is now the entity at the highest level of prudential consolidation, which includes Banco Cooperativo SA and Grupo Seguros RGA. BCE’s assets account for approximately 75% of the consolidated balance sheet. The structure of this new IPS does not create a consolidated banking group, as the IPS members remain autonomous institutions. Members created an ex-ante fund to provide support in the event of a member institution facing severe financial difficulties. The goal of the IPS is to increase the size of this fund to around EUR 300 million or 1% of the AECR’s combined Risk Weighted Assets by 2024. As of end-September, the total available amount in the ex-ante fund was EUR 200 million.

DBRS Morningstar considers that the Bank’s core profitability has been fairly resilient during the first months of the COVID-19 crisis. The Bank has generated stable profits over recent years, with similar net results each year since 2013. BCE has limited revenue diversification, as most of its revenues arise from a small loan book and a relatively large fixed income portfolio. However, since 2018, the consolidated Group includes insurance revenues from Grupo Seguros RGA, its insurance arm. In 9M 2020, the insurance revenues represented around 31% of the consolidated Group’s earnings. BCE’s individual net income (excluding Grupo Seguros RGA) was EUR 27 million in 9M 2020, up 21.6% Year-on-Year (YoY), with the Bank’s net interest income (7.5% YoY) positively affected by a larger fixed income book. Net fees & commissions dragged on profits in 9M 2020 down 7% YoY but this was compensated for by larger trading gains. Despite the current resiliency of the bank’s earnings profile, DBRS Morningstar considers that the AECR’s core profitability evolution during 2020 and 2021 will be materially affected by the crisis.

DBRS Morningstar considers BCE to have a generally low risk profile, driven by its low-risk business mix and specialised franchise. At end-2019, the consolidated Group had a material exposure to financial securities, mainly Sovereign bonds (44% of total assets) due to its business model as part of its intermediary role for the AECR CRs, and its fixed income portfolio related to its insurance business. At end-2019, the consolidated Group’s sovereign exposures (including debt bonds and loans) totaled EUR 6 billion, 89% of which related to Spain and 9% to Italy. Apart from its securities portfolio, the consolidated Group’s main exposures are lending to financial institutions (around 13.3% of total assets) and direct client lending (10% of total assets at end-September 2020). Given its limited exposure to lending, the Bank’s non-performing loans (NPLs) stood at only EUR 2.9 million, with an NPL ratio of 0.2% at end-September 2020. Nevertheless, DBRS Morningstar expects that, given the unprecedented economic shock, BCE and ACER’s asset quality will deteriorate in coming quarters.

BCE’s funding and liquidity position is underpinned by a large and stable deposit base from credit institutions representing most of total funding at end-2019, a large part of which is backed by the members of the AECR, who deposit their excess liquidity at BCE in the form of bank deposits. At end-2019, the consolidated Group had a solid liquidity position with strong LCR and NSFR ratios of 260% and 244% respectively. Overall, DBRS Morningstar considers BCE’s liquidity position as solid, although the diversification of funding sources is limited.

DBRS Morningstar views BCE as having robust regulatory capital ratios given its low risk profile. Moreover BCE’s sustainable profits have supported the organic build-up of capital in recent years. The Group’s consolidated Common Equity Tier 1 (CET1) phased-in ratio was 43.4% at end-2019 or 35.6% on an individual basis. This compares to a minimum Overall Capital Requirement (OCR) for total capital of 11.63% in 2020 according to the Supervisory Review and Evaluation Process (SREP). DBRS Morningstar views BCE’s membership within the IPS positively as it provides potential support from the ex-ante fund should BCE face severe financial difficulties.

ESG CONSIDERATIONS

A description of how DBRS Morningstar considers ESG factors within the DBRS Morningstar analytical framework and its

methodologies can be found at: <https://www.dbrsmorningstar.com/research/357792>.

The Grid Summary Grades for Banco Cooperativo Español are as follows: Franchise Strength – Good/ Moderate; Earnings – Good/ Moderate; Risk Profile – Good; Funding & Liquidity – Good; Capitalisation – Moderate.

Notes:

All figures are in Euros unless otherwise noted.

The principal methodology is the Global Methodology for Rating Banks and Banking Organisations (8 June 2020).

<https://www.dbrsmorningstar.com/research/362170/global-methodology-for-rating-banks-and-banking-organisations>

For more information regarding rating methodologies and Coronavirus Disease (COVID-19), please see the following DBRS Morningstar press release: <https://www.dbrsmorningstar.com/research/357883>

The sources of information used for this rating include Company Documents, BCES Annual Accounts (2015 – 2019), Bank of Spain, European Banking Authority and S&P Global Market Intelligence. DBRS Morningstar considers the information available to it for the purposes of providing this rating to be of satisfactory quality.

DBRS Morningstar does not audit the information it receives in connection with the rating process, and it does not and cannot independently verify that information in every instance.

Generally, the conditions that lead to the assignment of a Negative or Positive trend are resolved within a 12-month period. DBRS Morningstar's outlooks and ratings are under regular surveillance.

For further information on DBRS Morningstar historical default rates published by the European Securities and Markets Authority (ESMA) in a central repository, see: <http://cerep.esma.europa.eu/cerep-web/statistics/defaults.xhtml>.

The sensitivity analysis of the relevant key rating assumptions can be found at: <https://www.dbrsmorningstar.com/research/369944>

Ratings assigned by DBRS Ratings GmbH are subject to EU and U.S. regulations only.

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Initial Rating Date: 16 December 2013

Last Rating Date: 13 November 2019

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