

Banco Cooperativo Espanol, S.A.

Key Rating Drivers

Moderate Risk Appetite: The ratings of Banco Cooperativo Español, S.A. (BCE) reflect its moderate risk appetite, its strategic importance to the members of the Asociación Española de Cajas Rurales (AECR; the Spanish rural cooperatives association), and stable but low profitability due to its low-margin business model. The ratings also incorporate BCE's adequate risk management, sound capital ratios and stable liquidity profile.

Support Underpins Strategic Role: The ratings also take into account the set-up of a cross-support mechanism between member entities and BCE to achieve a unified cooperative banking group by pooling strategic goals, common services and IT/risk management systems. The mechanism includes a private guarantee fund to address liquidity or solvency problems within the banking group's member banks, including BCE.

Challenging Operating Environment: Spain's deteriorating economic environment poses challenges to the bank's financial profile and the prospects of the members of AECR, which are BCE's main shareholders and counterparties. BCE's business volumes are largely dependent on those of the Spanish rural cooperatives, and its treasury activities bear counterparty risks with weakening sovereigns as a result of the pandemic.

Central Treasurer of AECR: Channelling liquidity from/to AECR members is BCE's main function. Consequently, the structure and size of the bank's balance sheet depend to a large extent on the liquidity and financing needs of AECR members. At end-2019, the AECR consisted of 29 members, with aggregate equity of around EUR5.0 billion.

Modest but Stable Profitability: Profit maximisation is not BCE's main goal and profitability, despite being modest, has been stable over economic and interest-rate cycles. BCE aims to offer competitive services to AECR members and to achieve a stable performance to support internal capital generation.

Sound Liquidity and Risk Management: BCE's risk management systems and procedures are sound. BCE benefits from a highly liquid balance sheet, underpinned by its role as the central treasurer for the AECR member credit cooperatives. This is primarily invested in Spanish public debt, which results in some counterparty risk concentration and, to a lesser extent, in securities issued by financial institutions.

Sound Risk-Weighted Ratios: Risk-weighted capital ratios are sound for its risk profile with a fully loaded Common Equity Tier 1 (CET) ratio of 35.6% and a Basel leverage ratio of 7.9% at end-2019. High capital ratios compensate for high counterparty risk concentration to Spanish sovereign debt (about 5x CET1 capital at end-2019).

Rating Sensitivities

Downside Risks: BCE's ratings would likely be downgraded if prospects that the health crisis is resolved globally in 2H20 become less likely, making a sharp recovery in global growth in 2021 more remote. A delay to this sharp recovery could reduce both BCE's importance within the group and business volumes, putting sustained pressure on profitability.

Stabilisation of the Operating Environment: The Outlook could be revised to Stable if the bank's operating environment stabilised and if BCE successfully managed the challenges arising from the economic downturn, limiting downside risks to its asset quality and profitability, while keeping current capital levels.

Ratings

Foreign Currency	
Long-Term IDR	BBB
Short-Term IDR	F2

Local Currency

Viability Rating	bbb
Support Rating	5
Support Rating Floor	NF

Sovereign Risk

Long-Term Foreign- and Local-Currency IDR	A-
Country Ceiling	AAA

Outlooks

Long-Term Foreign-Currency IDR	Negative
Sovereign Long-Term Foreign- and Local-Currency IDR	Stable

Applicable Criteria

[Bank Rating Criteria \(February 2020\)](#)

Related Research

[Global Economic Outlook: September 2020 - Recovery Underway](#)

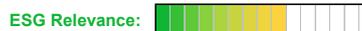
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Ratings Navigator

Banco Cooperativo Espanol, S.A.



Banks
Ratings Navigator

	Peer Ratings	Operating Environment	Company Profile	Management & Strategy	Risk Appetite	Asset Quality	Earnings & Profitability	Capitalisation & Leverage	Funding & Liquidity	Viability Rating	Support Rating Floor	Issuer Default Rating
aaa										aaa	AAA	AAA
aa+										aa+	AA+	AA+
aa										aa	AA	AA
aa-										aa-	AA-	AA-
a+										a+	A+	A+
a										a	A	A
a-										a-	A-	A-
bbb+		↓	↓	↓	↓	↓	↓	↓	↓	bbb+	BBB+	BBB+
bbb		↓	↓	↓	↓	↓	↓	↓	↓	bbb	BBB	BBB Negative
bbb-			↓	↓	↓	↓	↓	↓	↓	bbb-	BBB-	BBB-
bb+							↓			bb+	BB+	BB+
bb										bb	BB	BB
bb-										bb-	BB-	BB-
b+										b+	B+	B+
b										b	B	B
b-										b-	B-	B-
ccc+										ccc+	CCC+	CCC+
ccc										ccc	CCC	CCC
ccc-										ccc-	CCC-	CCC-
cc										cc	CC	CC
c										c	C	C
f										f	NF	D or RD

Significant Changes

Spain Highly Affected by the Coronavirus Crisis

Spain is one of the countries most affected by the coronavirus pandemic in Europe. Under Fitch's forecasts, which are based on an extended lockdown to halt the spread of the virus, Spain's GDP is expected to contract by 13.2% in 2020 before seeing a partial recovery of 6.2% in 2021.

The unprecedented scale and scope of policy responses should help to limit the extent of the collapse in activity through the lockdown and will support economic recovery. However, job losses and great pressure on SMEs and the self-employed, which are key parts of the Spanish economy, will heavily weigh on post-crisis activity levels. As a result of these challenges, Fitch changed the outlook of the operating environment for banks operating in Spain to Negative from Stable in March 2020.

Government and Regulatory Support Measures

A number of measures introduced by Spain's government should be beneficial to the banks' financial profiles by reducing near-term credit risks. These include the introduction of a sector-wide debt moratorium suspending interest and principal repayment for at least three months for residential mortgage and consumer loans, and the provision of up to EUR100 billion of state loan guarantees (of which EUR74 billion had already been disbursed at mid-August 2020) for the self-employed, SMEs and corporates. The Spanish government also announced on 3 July a new line of loan guarantees of up to EUR40 billion to support new investment in businesses in the areas of environmental sustainability and digitalisation.

Although we expect some regulatory flexibility on the recognition of problem assets, this may only delay credit losses and protection will only be limited in an adverse durable stress scenario extending throughout 2021.

The ECB's response to the coronavirus pandemic includes capital-relief measures and extensive monetary-policy support facilities intended to alleviate the economic difficulties for European banks. While all these measures should support the flow of funds to the economy, we expect credit demand to be hit.

Bar Chart Legend

Vertical bars - VR range of Rating Factor
 Bar Colors - Influence on final VR
 ■ Higher influence
 ■ Moderate influence
 ■ Lower influence
 Bar Arrows - Rating Factor Outlook
 ↑ Positive ↓ Negative
 ⇅ Evolving □ Stable

Brief Company Summary

Treasurer for AEER Members

BCE is the central treasurer for the credit cooperatives that are members of the Spanish rural AEER. The latter's credit cooperatives generally have sound retail franchises in their home regions or provinces, particularly in rural areas of Spain but their national presence is small. The 29 credit cooperatives have similar business models and share common cooperative values.

BCE offers a range of wholesale banking services to other institutions and corporations but is mostly focused on servicing credit cooperatives, which are also its main shareholders. About 24% of BCE's total balance sheet relates to activities conducted on behalf of AEER members, which benefits from the treasury agreement, whereby AEER members bear the credit risk. Its functions entail acting as a representative body for AEER members and coordinating IT systems.

In December 2017, the AEER members strengthened their cross-support mechanism, which includes a private guarantee fund to deal with any liquidity or solvency problems within the banking group's member banks. Although the targeted amount is insufficient to provide support to the entire group, it strengthens both AEER's existing cross-support mechanism to support members undergoing severe liquidity or solvency problems and BCE's role within the group. From a regulatory standpoint, each credit cooperative will remain supervised on an individual basis. However, they benefit from a 0% risk-weighting for exposures between AEER members and lower contribution to the Spanish Deposit Guarantee Fund.

Experienced Management and Prudent Strategy

BCE's executive team is stable and has good depth and extensive experience in the financial services industry, and in particular in the cooperative sector. The bank's strategic objectives are stable, and oriented towards serving AEER member credit cooperatives by offering central treasurer services, channelling liquidity to the cooperatives and helping members to achieve economies of scale and improving their operating efficiency. Its financial targets are conservative. BCE has been consistent in executing its strategy, included the setting-up of the cross-support mechanism.

In our view, BCE's corporate governance is effective in implementing the strategic objectives set by the board of directors, where AEER members are well represented. BCE's main strategic objectives are linked to the quality and efficiency of services offered while maintaining reasonable earnings. However, the deteriorating operating environment challenges the execution of its strategy, and in particular the bank will be sensitive to the performance of the AEER banks.

Low Risk Appetite

BCE's risk management systems and procedures are sound. BCE's activities are generally low risk, and it has well-developed risk management systems to minimise its exposure to credit, market, liquidity and foreign-exchange risks. Counterparty risk is limited to leading European, OECD and US banks, and mainly in the form of short-term exposures. At end-2019, about 90% of BCE's counterparty exposures were rated investment-grade. Non-bank lending accounts for a small part of the balance sheet and often relates to clients operating with various Cajas Rurales. The size and equity of the AEER banks limit their ability to extend large loans; consequently, BCE arranges loan syndications or assists its members by providing this service.

BCE's exposure to structural interest-rate mismatches and price volatility in the trading portfolio is average for the industry and the bank has appropriate techniques to mitigate risks. BCE measures market risk using value at risk (VaR), based on a 99% confidence level, an observation period of 525 days and a holding period of 10 days, backed by stress testing. The average VaR for 2019 was about EUR1.0 million, with a maximum exposure of EUR1.5 million.

Exposure to structural balance-sheet mismatches (interest rate and liquidity) is minimised by the short-term nature of assets and liabilities, which are closely matched in terms of interest rates and maturities. At end-2019 BCE calculated that a 100bp upward (downward) parallel shift in the interest-rate curve would result in a 3.8% decrease (1.9% decrease) in the bank's net interest income in the following 12 months.

Summary Financials and Key Ratios

	30 Jun 20 6 months - interim (EURm) Unaudited	31 Dec 19 Year end (EURm) Audited - unqualified	31 Dec 18 Year end (EURm) Audited - unqualified	31 Dec 17 Year end (EURm) Audited - unqualified
Summary income statement				
Net interest and dividend income	30.3	51.6	83.7	55.1
Net fees and commissions	5.6	12.0	12.0	15.8
Other operating income	4.6	4.2	5.1	8.3
Total operating income	40.5	67.8	100.8	79.2
Operating costs	15.2	28.1	26.5	26.8
Pre-impairment operating profit	25.3	39.7	74.3	52.4
Loan and other impairment charges	0.0	-4.3	-3.7	0.9
Operating profit	25.3	44.0	78.0	51.5
Other non-operating items (net)	n.a.	-0.2	-0.3	0.0
Tax	6.8	11.8	13.8	14.2
Net income	18.5	32.0	63.9	37.3
Summary balance sheet				
Assets				
Gross loans	1,876.0	1,369.3	639.5	1,277.2
- Of which impaired	n.a.	1.7	2.1	5.9
Loan loss allowances	21.5	22.4	28.2	36.1
Net loans	1,854.5	1,346.9	611.3	1,241.1
Interbank	861.3	270.1	255.9	401.2
Derivatives	1,128.4	937.7	804.9	509.0
Other securities and earning assets	8,093.6	4,964.9	5,327.5	3,782.0
Total earning assets	11,937.8	7,519.6	6,999.6	5,933.3
Cash and due from banks	1,091.9	1,558.3	1,471.9	1,360.7
Other assets	52.7	44.1	59.0	47.9
Total assets	13,082.4	9,122.0	8,530.5	7,341.9
Liabilities				
Customer deposits	1,409.9	1,026.5	795.7	660.8
Interbank and other short-term funding	7,671.3	5,388.0	6,079.3	4,856.7
Other long-term funding	1,419.9	417.5	50.3	370.8
Trading liabilities and derivatives	1,969.4	1,664.7	1,054.0	762.6
Total funding	12,470.5	8,496.7	7,979.3	6,650.9
Other liabilities	53.2	53.7	45.2	155.8
Preference shares and hybrid capital	n.a.	n.a.	n.a.	n.a.
Total equity	558.7	571.6	506.0	535.2
Total liabilities and equity	13,082.4	9,122.0	8,530.5	7,341.9
Exchange rate	USD1 = EUR0.893017	USD1 = EUR0.89015	USD1 = EUR0.873057	USD1 = EUR0.83382

Source: Fitch Ratings, Fitch Solutions, Bank

Summary Financials and Key Ratios

	30 Jun 20	31 Dec 19	31 Dec 18	31 Dec 17
Ratios (annualised as appropriate)				
Profitability				
Operating profit/risk-weighted assets	2.4	2.8	4.8	2.6
Net interest income/average earning assets	0.6	0.6	1.2	0.6
Non-interest expense/gross revenue	37.5	41.5	26.3	33.8
Net income/average equity	9.0	4.7	10.8	7.3
Asset quality				
Impaired loans ratio	n.a.	0.1	0.3	0.5
Growth in gross loans	37.0	114.1	-49.9	11.4
Loan loss allowances/impaired loans	n.a.	1,317.7	1,342.9	611.9
Loan impairment charges/average gross loans	0.0	-0.5	-0.3	0.1
Capitalisation				
Common equity Tier 1 ratio	25.5	35.6	30.5	25.2
Fully loaded common equity Tier 1 ratio	n.a.	n.a.	n.a.	n.a.
Tangible common equity/tangible assets	4.3	6.2	5.8	7.2
Basel leverage ratio	n.a.	7.9	8.6	n.a.
Net impaired loans/common equity Tier 1	n.a.	-3.7	-5.2	-6.1
Net impaired loans/Fitch Core Capital	n.a.	n.a.	-5.4	-5.7
Funding and liquidity				
Loans/customer deposits	133.1	133.4	80.4	193.3
Liquidity coverage ratio	n.a.	n.a.	281.9	648.3
Customer deposits/funding	13.4	15.0	11.5	11.2
Net stable funding ratio	n.a.	n.a.	307.1	172.3

Source: Fitch Ratings, Fitch Solutions, Bank

Key Financial Metrics – Latest Developments

Small Loan Book

Due to its role as the central treasurer for credit cooperatives BCE's interbank and securities portfolios are large and account for the bulk of assets. BCE's non-bank loan book was small (14% of total assets at end-June 2020) and mainly comprised loans to large corporates, SMEs and individuals. The stock of impaired loans was small and was fully covered by reserves. We expect asset quality pressures in the current economic environment to be contained at BCE given its small risk appetite for loans and the well collateralised profile of its operations. However, there is high exposure to Spanish public debt, which brings high counterparty risk concentration and exposes the bank to some market risk, given that a large part of its sovereign debt portfolio is fairvalued.

AECR Treasury Agreement Covers Part of the Credit Risk

The process of investing AECR members' liquidity through BCE is governed by a treasury agreement, through which AECR members guarantee any losses or commitments that could arise from interbank placements made by BCE on their behalf. Any claim under the guarantee is split between the AECR members in proportion to their equity shares in BCE, regardless of the volumes of their activity under the agreement. On account of this guarantee, BCE is exempt from complying with large exposure limits under the Spanish interpretation of EU capital adequacy requirements.

At end-2019, BCE managed EUR3.7 billion liquidity on behalf of the AECR members under the treasury agreement. The funds under the treasury agreement are mostly invested in debt securities (EUR2.1 billion), mainly Spanish sovereign bonds, and reverse repos (EUR1.1 billion). Interbank loans and reverse repos outside the treasury agreement are small at about EURO.4 billion and short term.

Modest but Stable Profitability

BCE's profitability is modest but has remained broadly stable over the cycle. BCE's revenue mix is dominated by net interest income, reflecting BCE's role as an intermediary for AECR members charging a fixed margin on the volume of funding and liquidity channelled to and from them. The operating profit/risk-weighted assets ratio has been at acceptable levels for the past few years, helped by the high business volumes and the bank's sound cost efficiency. BCE's ability to sustain profitability partly depends on business volumes from Spanish rural cooperatives, which are expected to slightly decline moderately as a result of the pandemic.

Robust Risk-Weighted Capital Ratios

The bank maintains risk-weighted capital ratios with satisfactory buffers above regulatory minimums, although its overall equity base is small. At end-2019, the fully-loaded Common Equity Tier 1 ratio was 35.6%, well above the bank's minimum requirements. Fitch expects the bank to maintain these ample buffers based on earnings retention and the bank's conservative capital management. The regulatory leverage ratio was also sound at 7.9% at end-2019.

The liquid nature of its own investments (excluding assets related to AECR members) means BCE has some flexibility to deleverage its balance sheet quickly, if needed. Apart from deleveraging, the main levers for BCE to improve its capital position are through earnings retention and to raise capital from AECR members. According to the AECR's statutes, all member banks are obliged to subscribe to BCE's capital increases, as they did in 2009 -2010. This illustrates their commitment and the importance of BCE for the group.

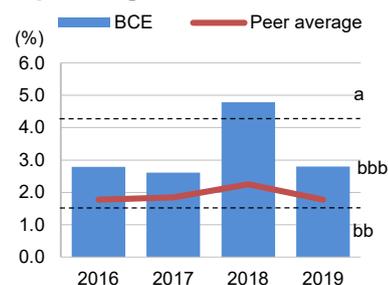
Stable Funding and Liquidity

BCE is the central treasurer for the AECR member credit cooperatives. In this capacity, BCE's main function is to provide them with access to funding from the ECB and the wholesale markets, and to manage their liquidity. The bank had a comfortable liquidity position at end-2019, with EUR2.9 billion of unencumbered ECB-eligible assets (32% of total assets), largely in the form of Spanish sovereign bonds. At end-March 2020 BCE reported good regulatory liquidity coverage and net stable funding ratios of 260% and 225% respectively.

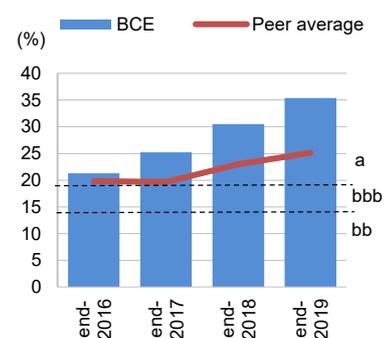
Notes on charts: Black dashed lines represent indicative quantitative ranges for core financial metrics given an operating environment score of 'bbb'. Peers include: BCE (Long-term IDR/VR: BBB/bbb) DZ BANK AG Deutsche Zentral-Genossenschaftsbank (AA-/); Cecabank SA (BBB-/bbb-); Iccrea Banca S.P.A. (BB-/)

From 2018 on, Fitch based its analysis on BCE's individual and audited results following the group's reorganization in 2017 and to ease comparison.

Operating Profit/RWAs

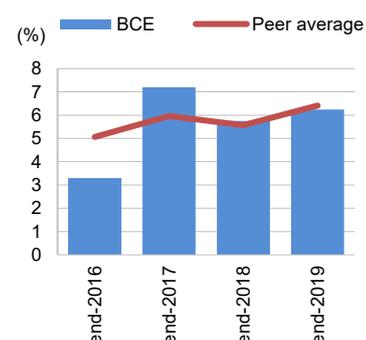


CET 1 Ratio (%)



Source: Banks, Fitch

Tangible Leverage



Source: Banks, Fitch

Sovereign Support Assessment

Support Rating Floor		Value	
Typical D-SIB SRF for sovereign's rating level (assuming high propensity)		BBB+ or BBB	
Actual country D-SIB SRF		NF	
Support Rating Floor:		NF	
Support Factors	Positive	Neutral	Negative
Sovereign ability to support system			
Size of banking system relative to economy			✓
Size of potential problem		✓	
Structure of banking system		✓	
Liability structure of banking system		✓	
Sovereign financial flexibility (for rating level)		✓	
Sovereign propensity to support system			
Resolution legislation with senior debt bail-in			✓
Track record of banking sector support		✓	
Government statements of support		✓	
Sovereign propensity to support bank			
Systemic importance			✓
Liability structure of bank		✓	
Ownership		✓	
Specifics of bank failure		✓	
Policy banks			
Policy role			
Funding guarantees and legal status			
Government ownership			

BCE's Support Rating (SR) of '5' and Support Rating Floor (SRF) of 'No floor' reflect Fitch's belief that senior creditors can no longer rely on receiving full extraordinary support from the sovereign in the event that BCE becomes non-viable. The EU's Bank Recovery and Resolution Directive and the Single Resolution Mechanism for eurozone banks provide a framework for resolving banks that is likely to require senior creditors to participate in losses, instead of or ahead of a bank receiving sovereign support.

Environmental, Social and Governance Considerations

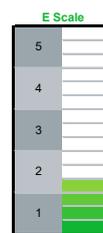
FitchRatings **Banco Cooperativo Espanol, S.A.**

Credit-Relevant ESG Derivation

			Overall ESG Scale	
Banco Cooperativo Espanol, S.A. has 5 ESG potential rating drivers				
<ul style="list-style-type: none"> ▶ Banco Cooperativo Espanol, S.A. has exposure to compliance risks including fair lending practices, mis-selling, repossession/foreclosure practices, consumer data protection (data security) but this has very low impact on the rating. ▶ Governance is minimally relevant to the rating and is not currently a driver. 	key driver	0	issues	5
	driver	0	issues	4
	potential driver	5	issues	3
	not a rating driver	4	issues	2
		5	issues	1

Environmental (E)

General Issues	E Score	Sector-Specific Issues	Reference
GHG Emissions & Air Quality	1	n.a.	n.a.
Energy Management	1	n.a.	n.a.
Water & Wastewater Management	1	n.a.	n.a.
Waste & Hazardous Materials Management; Ecological Impacts	1	n.a.	n.a.
Exposure to Environmental Impacts	2	Impact of extreme weather events on assets and/or operations and corresponding risk appetite & management; catastrophe risk; credit concentrations	Company Profile; Management & Strategy; Risk Appetite; Asset Quality



How to Read This Page

ESG scores range from 1 to 5 based on a 15-level color gradation. Red (5) is most relevant and green (1) is least relevant.

The Environmental (E), Social (S) and Governance (G) tables break out the individual components of the scale. The right-hand box shows the aggregate E, S, or G score. General Issues are relevant across all markets with Sector-Specific Issues unique to a particular industry group. Scores are assigned to each sector-specific issue. These scores signify the credit-relevance of the sector-specific issues to the issuing entity's overall credit rating. The Reference box highlights the factor(s) within which the corresponding ESG issues are captured in Fitch's credit analysis.

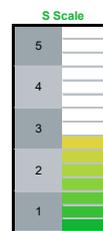
The Credit-Relevant ESG Derivation table shows the overall ESG score. This score signifies the credit relevance of combined E, S and G issues to the entity's credit rating. The three columns to the left of the overall ESG score summarize the issuing entity's sub-component ESG scores. The box on the far left identifies some of the main ESG issues that are drivers or potential drivers of the issuing entity's credit rating (corresponding with scores of 3, 4 or 5) and provides a brief explanation for the score.

Classification of ESG issues has been developed from Fitch's sector ratings criteria. The General Issues and Sector-Specific Issues draw on the classification standards published by the United Nations Principles for Responsible Investing (PRI) and the Sustainability Accounting Standards Board (SASB).

Sector references in the scale definitions below refer to Sector as displayed in the Sector Details box on page 1 of the Navigator.

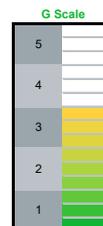
Social (S)

General Issues	S Score	Sector-Specific Issues	Reference
Human Rights, Community Relations, Access & Affordability	2	Services for underbanked and underserved communities: SME and community development programs; financial literacy programs	Company Profile; Management & Strategy; Risk Appetite
Customer Welfare - Fair Messaging, Privacy & Data Security	3	Compliance risks including fair lending practices, mis-selling, repossession/foreclosure practices, consumer data protection (data security)	Operating Environment; Company Profile; Management & Strategy; Risk Appetite
Labor Relations & Practices	2	Impact of labor negotiations, including board/employee compensation and composition	Company Profile; Management & Strategy
Employee Wellbeing	1	n.a.	n.a.
Exposure to Social Impacts	2	Shift in social or consumer preferences as a result of an institution's social positions, or social and/or political disapproval of core banking practices	Company Profile; Financial Profile



Governance (G)

General Issues	G Score	Sector-Specific Issues	Reference
Management Strategy	3	Operational implementation of strategy	Management & Strategy
Governance Structure	3	Board independence and effectiveness; ownership concentration; protection of creditor/stakeholder rights; legal /compliance risks; business continuity; key person risk; related party transactions	Management & Strategy; Earnings & Profitability; Capitalisation & Leverage
Group Structure	3	Organizational structure; appropriateness relative to business model; opacity, intra-group dynamics; ownership	Company Profile
Financial Transparency	3	Quality and frequency of financial reporting and auditing processes	Management & Strategy



CREDIT-RELEVANT ESG SCALE	
How relevant are E, S and G issues to the overall credit rating?	
5	Highly relevant, a key rating driver that has a significant impact on the rating on an individual basis. Equivalent to "higher" relative importance within Navigator.
4	Relevant to rating, not a key rating driver but has an impact on the rating in combination with other factors. Equivalent to "moderate" relative importance within Navigator.
3	Minimally relevant to rating, either very low impact or actively managed in a way that results in no impact on the entity rating. Equivalent to "lower" relative importance within Navigator.
2	Irrelevant to the entity rating but relevant to the sector.
1	Irrelevant to the entity rating and irrelevant to the sector.

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 to 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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