

## CREDIT OPINION

12 December 2016

Update

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### RATINGS

#### Banca Sella Holding

Domicile	Italy
Long Term Deposit	Baa3
Type	LT Bank Deposits - Fgn Curr
Outlook	Negative

Please see the [ratings section](#) at the end of this report for more information. The ratings and outlook shown reflect information as of the publication date.

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## Banca Sella Holding

### Update Following Rating Action

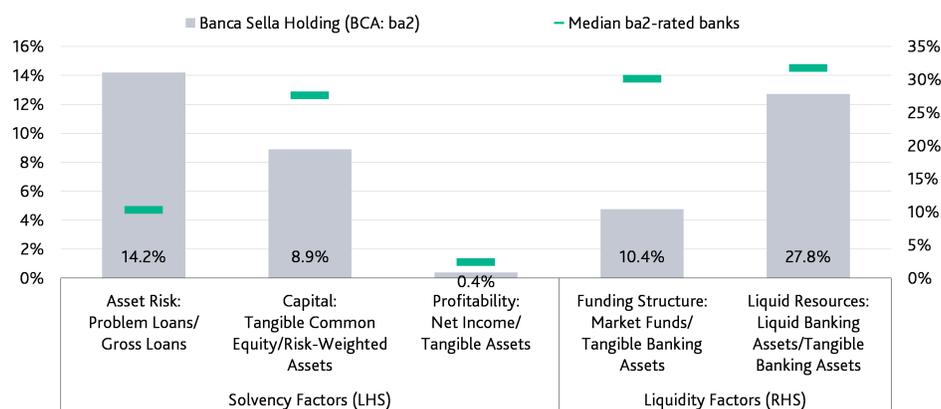
#### Summary Rating Rationale

Banca Sella Holding's Baa3 deposit rating is underpinned by the bank's ba2 standalone baseline credit assessment (BCA), very low loss-given-failure under our Loss Given Failure (LGF) analysis, and our assessment of a low probability of government support.

Banca Sella Holding's BCA reflects the bank's modest capital, large stock of problem loans, and weak profitability.

Exhibit 1

#### Rating Scorecard - Key Financial Ratios



Source: Moody's Financial Metrics

#### Credit Strengths

- » Retail funding profile
- » Large stock of liquid assets

#### Credit Challenges

- » Modest capital
- » Large stock of problem loans
- » Weak profitability

## Rating Outlook

The outlook on Banca Sella Holding's long-term deposit ratings is negative, reflecting the probability that the outstanding bail-in-able liabilities will continue to reduce over time, thereby increasing the loss-given-failure.

## Factors that Could Lead to an Upgrade

Banca Sella Holding's BCA could be upgraded following further improvements in capital, larger than-expected reduction in the stock of problem loans, and an improvement in the profits coming from the commercial banking activities.

The deposit rating would be upgraded following an upgrade in the BCA, combined with a material improvement in the bank's stock of bail-in-able debt and volume of junior deposits.

## Factors that Could Lead to a Downgrade

Banca Sella Holding's BCA could be downgraded following a material increase in the stock of problem loans, net losses, or a capital reduction.

The deposit ratings would be downgraded following a downgrade of the BCA, or a continuous reduction in the stock of bail-in-able debt or volume of junior deposits.

## Key Indicators

Exhibit 2

### Banca Sella Holding (Consolidated Financials) [1]

	6-16 <sup>2</sup>	12-15 <sup>2</sup>	12-14 <sup>2</sup>	12-13 <sup>3</sup>	12-12 <sup>3</sup>	Avg.
Total Assets (EUR million)	13,272.6	12,450.9	14,257.8	13,360.5	13,135.7	0.3 <sup>4</sup>
Total Assets (USD million)	14,745.2	13,525.3	17,252.7	18,410.0	17,318.0	-3.9 <sup>4</sup>
Tangible Common Equity (EUR million)	778.1	699.9	674.5	615.9	487.5	12.4 <sup>4</sup>
Tangible Common Equity (USD million)	864.4	760.3	816.2	848.6	642.7	7.7 <sup>4</sup>
Problem Loans / Gross Loans (%)	14.2	14.3	12.0	10.8	9.5	12.2 <sup>5</sup>
Tangible Common Equity / Risk Weighted Assets (%)	8.9	8.1	7.4	6.7	5.4	8.2 <sup>6</sup>
Problem Loans / (Tangible Common Equity + Loan Loss Reserve) (%)	85.6	92.8	76.6	81.9	86.7	84.7 <sup>5</sup>
Net Interest Margin (%)	1.9	1.9	2.2	2.3	2.4	2.1 <sup>5</sup>
PPI / Average RWA (%)	1.6	1.9	3.3	2.4	2.2	2.3 <sup>6</sup>
Net Income / Tangible Assets (%)	0.4	0.2	0.5	0.3	0.2	0.3 <sup>5</sup>
Cost / Income Ratio (%)	76.8	73.0	58.2	65.7	68.4	68.4 <sup>5</sup>
Market Funds / Tangible Banking Assets (%)	12.0	10.4	18.9	18.8	17.2	15.5 <sup>5</sup>
Liquid Banking Assets / Tangible Banking Assets (%)	31.9	27.8	30.3	24.7	19.6	26.9 <sup>5</sup>
Gross loans / Due to customers (%)	87.6	92.7	100.0	108.8	114.0	100.6 <sup>5</sup>

[1] All figures and ratios are adjusted using Moody's standard adjustments [2] Basel III - fully-loaded or transitional phase-in; IFRS [3] Basel II; IFRS [4] Compound Annual Growth Rate based on IFRS reporting periods [5] IFRS reporting periods have been used for average calculation [6] Basel III - fully-loaded or transitional phase-in & IFRS reporting periods have been used for average calculation

Source: Moody's Financial Metrics

## Detailed Rating Considerations

### Modest capital

We view Banca Sella Holding's capital as modest, both in terms of risk-adjusted and absolute levels (leverage). Our score for capital is ba3, is positioned one notch above the macro-adjusted score of b1, as we expect a moderate improvement of the bank's capital ratios.

This publication does not announce a credit rating action. For any credit ratings referenced in this publication, please see the ratings tab on the issuer/entity page on [www.moody's.com](http://www.moody's.com) for the most updated credit rating action information and rating history.

In June 2016 the bank reported a Common Equity Tier 1 (CET1) ratio of 12%, which is equivalent to our Tangible Common Equity over adjusted risk-weighted assets of 8.9%<sup>1</sup>; the difference mostly derives from our adjustment that we apply to some government bonds of European countries<sup>2</sup>. In September 2016 the bank reported a slightly improved CET1 ratio to 12.2%, thanks to its 3Q profit.

In 2015 Banca Sella Holding activated a series of measures aimed at improving its Common Equity Tier 1 (CET1) ratio, which rose to 12.2% in September 2016 from 9.0% in December 2014. In particular, the group executed a €120 million capital increase of its commercial banking subsidiary Banca Sella SpA (unrated), the sale of insurance subsidiary CBA Vita (unrated), and the sale of a stake in Istituto Centrale delle Banche Popolari Italiane (corporate family rating Ba2 with stable outlook).

### Large stock of problem loans

We view Banca Sella Holding's asset risk as a key weakness, and we score it b2, in line with the bank's macro-adjusted score.

In June 2016 Banca Sella Holding reported problem loans<sup>3</sup> of 14.2% of gross loans, a reduction from the 15.5% reported in 2014; the decrease largely derived from the disposal of a portfolio of non-performing consumer loans. Banca Sella Holding's stock of problem loans, although high, compares favourably with the 17.7% system average as of June 2016 (source: Bank of Italy).

Coverage is just adequate at 52%, which is however higher than the 46% average for Italian banks.

### Weak profitability

Banca Sella Holding's profitability is weak; our score for Banca Sella Holding's profitability is b3, two notches below our b1 macro-adjusted score. The adjustment is driven by our expectations that the bank's net profitability will be affected by an environment still characterised by very low interest rates, high competition amongst banks, and volatile financial markets, which will only be partially offset by lower loan loss charges/provisions going forward.

Compared with banks of similar size, Banca Sella Holding's revenues are better diversified; in 2014 and in 2015 Banca Sella Holding's net profits have been sustained by the group's trading activity, and wealth management business.

Despite the higher revenue diversification, substantial trading gains, and average efficiency (around 70% cost-income ratio as reported by the bank), net profit was modest relative to tangible assets, with an average of 0.3% between 2012 and 2015. This was largely attributable to the bank's high loan loss provisions, which on average represented around two-thirds of Banca Sella Holding's pre-provision profit.

In September 2016 Banca Sella Holding reported a net profit of €103 million, up from the €14 million reported in September 2015. The improvement was however mostly driven by extraordinary gains reported in 2016, and a substantially reduced cost of credit. In 2016 Banca Sella Holding reported a €50 million gain from the sale of its insurance subsidiary CBA Vita and the investment VISA Europe. Furthermore, the bank reported a 50% reduction in loan loss charges, to €58 million from €117 million.

### Retail funding profile and large stock of liquid assets

Banca Sella Holding's funding profile is mostly retail, with wholesale funding representing 10.4% of the bank's tangible banking assets. We assign an a3 score for funding structure, one notch above the baa1 macro-adjusted score, to reflect the fact that the majority of outstanding bonds have been sold to retail clients and represents a stable source of funding. Thanks to its large stock of retail funding, currently Banca Sella Holding's wholesale funding is limited to ECB funding which has been used to purchase government bonds and improve profitability.

Our score for liquid resources is baa2, in line with the macro-adjusted score, reflecting a large stock of liquid assets, mostly Italian government bonds.

### Family ownership is neutral for Banca Sella Holding's ratings

Banca Sella Holding is almost entirely owned by the Sella family, which designates all board members. Although the family ownership could potentially affect the independence of risk management and controls, we view it as neutral for the bank's ratings, considering the following mitigating factors: (1) there is sufficient transparency of the ownership structure, which includes holdings incorporated in Italy; (2) related parties exposures are limited and publicly disclosed according to international best practices; and (3) other businesses of the Sella family are limited, reducing potential conflict of interests between the bank and other activities.

## Notching Considerations

### Loss Given Failure

Banca Sella Holding is subject to the EU Bank Recovery and Resolution Directive (BRRD), which we consider to be an Operational Resolution Regime. Our analysis assumes residual tangible common equity of 3% and losses post-failure of 8% of tangible banking assets, a 25% run-off in "junior" wholesale deposits, a 5% run-off in preferred deposits and 26% of junior deposits over total deposits. These are in line with our standard assumptions. Furthermore, we take into account the full 'depositor preference' whereby junior deposits are preferred over senior debt creditors in accordance with a law decree introducing full depositor preference in Italy starting from 2019.

We believe that Banca Sella Holding's deposits are likely to face very low loss-given-failure, due to the loss absorption provided by the residual equity that we expect in resolution, subordinated debt and senior unsecured debt, as well as the volume of deposits themselves. This is supported by the combination of deposit volume and subordination. This results in an uplift of two notches from the bank's BCA.

### Government Support

We believe that there is a low likelihood of government support for Banca Sella Holding's debt and rated wholesale deposits in the event of its failure, which does not result in any uplift; this probability reflects the bank's position in the Italian market, with Banca Sella Holding being significantly smaller than the country's two largest banks. As such, we do not believe Banca Sella Holding to be a sufficiently systemically important bank to give any uplift to the ratings.

### Counterparty Risk Assessment

Banca Sella Holding's Baa2(cr)/P-2(cr) Counterparty Risk Assessment (CR Assessment) is three notches above the bank's BCA. Banca Sella Holding's CR Assessment is driven by the bank's ba2 BCA, and by substantial bail-in-able debt and deposits likely to support the operating obligations; low probability of government support does not result in any further uplift.

The CR Assessment, which is not a rating, reflects an issuer's probability of defaulting on certain bank operating liabilities, such as covered bonds, derivatives, letters of credit and other contractual commitments. In assigning the CR Assessment, we evaluate the issuer's standalone strength and the likelihood, should the need arise, of affiliate and government support, as well as the anticipated seniority of counterparty obligations under our advanced Loss Given Failure framework. The CR Assessment also assumes that authorities will likely take steps to preserve the continuity of a bank's key operations, maintain payment flows, and avoid contagion should the bank enter a resolution.

## Rating Methodology and Scorecard Factors

Exhibit 3

### Banca Sella Holding

#### Macro Factors

Weighted Macro Profile	Moderate	100%
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#### Financial Profile

Factor	Historic Ratio	Macro Adjusted Score	Credit Trend	Assigned Score	Key driver #1	Key driver #2
Solvency						
Asset Risk						
Problem Loans / Gross Loans	14.2%	b2	← →	b2	Quality of assets	
Capital						
TCE / RWA	8.9%	b1	↑	ba3	Expected trend	
Profitability						
Net Income / Tangible Assets	0.4%	b1	↓↓	b3	Expected trend	
Combined Solvency Score		b1		b1		
Liquidity						
Funding Structure						
Market Funds / Tangible Banking Assets	10.4%	baa1	← →	a3	Market funding quality	
Liquid Resources						
Liquid Banking Assets / Tangible Banking Assets	27.8%	baa2	← →	baa2	Stock of liquid assets	
Combined Liquidity Score		baa1		baa1		
Financial Profile						
Business Diversification				0		
Opacity and Complexity				0		
Corporate Behavior				0		
Total Qualitative Adjustments				0		
Sovereign or Affiliate constraint:				Baa2		
Scorecard Calculated BCA range				ba1-ba3		
Assigned BCA				ba2		
Affiliate Support notching				0		
Adjusted BCA				ba2		

#### Balance Sheet

	in-scope (EUR million)	% in-scope	at-failure (EUR million)	% at-failure
Other liabilities	2,328	17.7%	3,352	25.4%
Deposits	10,037	76.1%	9,013	68.3%
Preferred deposits	7,427	56.3%	7,056	53.5%
Junior Deposits	2,610	19.8%	1,957	14.8%
Senior unsecured bank debt	104	0.8%	104	0.8%
Dated subordinated bank debt	375	2.8%	375	2.8%
Junior subordinated bank debt				
Preference shares (bank)				
Senior unsecured holding company debt				
Dated subordinated holding company debt	-50	-0.4%	-50	-0.4%
Junior subordinated holding company debt				
Preference shares (holding company)				
Equity	396	3.0%	396	3.0%
Total Tangible Banking Assets	13,190	100%	13,190	100%

Debt class	De jure waterfall		De facto waterfall		Notching		LGF notching guidance versus BCA	Assigned LGF notching	Additional notching	Preliminary Rating Assessment
	Instrument volume + subordination	Sub-ordination	Instrument volume + subordination	Sub-ordination	De jure	De facto				
Counterparty Risk Assessment	21.1%	21.1%	21.1%	21.1%	3	3	3	3	0	baa2 (cr)
Deposits	21.1%	5.5%	21.1%	6.3%	2	2	2	2	0	baa3

Instrument Class	Loss Given Failure notching	Additional notching	Preliminary Rating Assessment	Government Support notching	Local Currency rating	Foreign Currency rating
Deposits	2	0	baa3	0	Baa3	Baa3

Source: Moody's Financial Metrics

## Ratings

Exhibit 4

Category	Moody's Rating
<b>BANCA SELLA HOLDING</b>	
Outlook	Negative
Bank Deposits	Baa3/P-3
Baseline Credit Assessment	ba2
Adjusted Baseline Credit Assessment	ba2
Counterparty Risk Assessment	Baa2(cr)/P-2(cr)

Source: Moody's Investors Service

## Endnotes

- <sup>1</sup> Unless noted otherwise, data in this report is sourced from company reports and Moody's Banking Financial Metric.
- <sup>2</sup> See [Moody's Adjustment to Increase the Risk Weightings of Sovereign Debt Securities in the Analysis of Banks: Frequently Asked Questions](#), published in September 2013.
- <sup>3</sup> Problem loans is the sum of three categories (from worst to best): (1) Bad loans (in Italian, "sofferenze"; (2) Unlikely to pay (in Italian, "inadempienze probabili"); (3) Past Due - by more than 90 days (in Italian, "esposizioni scadute e/o sconfinanti". For further details please refer to our Sector In-Depth entitled "[Italian Banks Implement New Problem Loan Definition; Our View on Asset Risk Is Unchanged](#)", published in October 2015

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