

Research Update:

# Spain-Based Ibercaja Banco S.A. Upgraded To 'BBB-/A-3' On Profitability Converging With Peers'; Outlook Stable

November 25, 2022

## Overview

- Ibercaja is successfully executing its business plan and has achieved most of its stated targets, including a significant reduction of its operating costs, one year ahead of schedule.
- Recent interest rate increases will significantly boost Ibercaja's earnings, and they are accelerating the convergence of its profitability with that of its peers.
- We raised our long- and short-term issuer credit ratings on Ibercaja to 'BBB-/A-3'.
- We also assigned our 'BBB/A-2' long- and short-term resolution counterparty ratings (RCRs) to the bank.
- The stable outlook reflects our expectation that Ibercaja will continue improving its operating profitability and efficiency in line with peers, and that asset quality deterioration in the now less favorable environment will be modest.

### PRIMARY CREDIT ANALYST

**Miriam Fernandez, CFA**  
Madrid  
+ 34917887232  
Miriam.Fernandez@spglobal.com

### SECONDARY CONTACT

**Elena Iparraguirre**  
Madrid  
+ 34 91 389 6963  
elena.iparraguirre@spglobal.com

## Rating Action

MADRID (S&P Global Ratings) Nov. 25, 2022--S&P Global Ratings today raised its long- and short-term issuer credit ratings on Ibercaja Banco S.A. to 'BBB-/A-3' from 'BB+/B'. The outlook is stable.

## Rationale

### The upgrade reflects our view that Ibercaja has delivered the execution of its business plan.

We think management's efforts to restructure, streamline, and digitize its business are effective. The completion of a 15% headcount reduction over 2017-2021 was particularly pertinent in addressing the bank's high-cost base and it prepares the bank well to deal with ongoing inflationary pressures. Furthermore, Ibercaja fulfilled its business plan without impairing

business generation capacity. Additionally, focus on fee income growth, leveraging on its relevant market shares in mutual and pension funds management, also supported earnings in the interest rate environment, which was negative until recently. Assets under management and insurance products grew by about 8% cumulatively between 2019 and the first nine months of 2022 and fee income represented about 43% of operating income as of end-September 2022.

**Higher interest rates will strongly boost Ibercaja's net interest income (NII), causing its underlying profitability to converge with peers' more rapidly than we previously anticipated.**

Ibercaja's largely floating loan book and large share of loyal deposits mean it is particularly likely to benefit from the recent rise in Euribor rates, with a stronger NII complementing its already solid fee generation. At the same time, the bank's focus on residential mortgages (which account for 60% of its loan book versus 42% for the Spanish system) will also protect it against potentially significant asset quality deterioration and credit losses in the now more difficult economic environment. We now expect Ibercaja will achieve return on equity of about 6.5% in 2022, further increasing to 7.0%-7.5% by 2023 and to 7.7%-8.3% by 2024, despite having to accommodate the new windfall tax (very much aligned with our average expectation for its peers). The bank should also close the gap with peers in terms of efficiency, with its cost-to-income ratio reducing to 60% by 2023 and further to 57% in 2024, compared with 67% at end-2021.

**Ibercaja's improving capitalization and our expectation of modest asset quality deterioration further support the rating.**

Although we anticipate some credit quality deterioration from the slowing economic growth environment and high inflation, we think this should be more manageable for Ibercaja compared with other peers that are more exposed to potentially vulnerable small and midsize enterprises and consumer lending. Under our base case, we expect cost of risk (including loans and foreclosed assets) to rise to 45 basis points (bps) in 2023 from 40 bps in 2022 (see "European Banks' Residential Mortgage Losses Should Remain Contained Even As Economies Slow," published Nov. 15, 2022). Moreover, Ibercaja's starting point is solid. Its nonperforming asset (NPA) ratio stood at 3.5% of gross loans at end-September 2022, while its loans classified as stage 2 represented 4.6% of gross loans and coverage of NPAs was 73%. We also expect its capitalization will continue to strengthen, with its risk-adjusted capital (RAC) ratio at about 9.0%-9.5% over the next 18-24 months.

**Ibercaja's buffer of subordinated bail-inable debt is not large enough to protect senior debt creditors in a resolution scenario.**

Therefore, the ratings on the bank do not benefit from additional loss-absorbing capacity (ALAC) uplift. According to Ibercaja's funding plans to fulfil its minimum requirement for own funds and eligible liabilities (MREL), we expect its ALAC buffer will approach the 400 bp minimum threshold that we require for the bank to benefit from a one-notch ratings uplift, but it will still fall short. We forecast it will stand at about 3.7%-3.9% of S&P Global Ratings-adjusted risk-weighted assets by end-2024. We also note that the bank is not subject to issuing any subordinated MREL, and therefore it could well complete its pending MREL gap with more affordable senior preferred instruments, which we will not include in our ALAC buffer.

**We assigned our RCR to Ibercaja, reflecting that we view its sale of whole business resolution strategy as likely to ensure the full and timely payment of some or all of these banks' senior liabilities.**

We base this view on the presence of a number of domestic players that could have the financial capacity and willingness to acquire the bank, and because Ibercaja is taking the necessary steps to be operationally prepared to ensure a sale could be executed. Recognizing the resolution strategy as effective implies that certain senior liabilities, namely those not legally bail-inable, may be protected from default during the resolution process. An RCR is a

forward-looking opinion of the relative default risk of certain liabilities, notably insured deposits and secured claims. The long-term RCR generally stands one notch above the long-term issuer credit rating for investment-grade issuers.

## Outlook

The stable outlook reflects that we expect Ibercaja will continue improving its earnings capacity and efficiency over the next 18-24 months, with its NII benefitting from the rising interest rate environment. It also indicates that we expect asset quality deterioration to be more modest than for other Spanish players, and capitalization to remain sound, with the RAC ratio at about 9.0%-9.5% by end-2024.

## Downside scenario

We could lower the rating if Ibercaja's performance deviated from our expectations, increasing the gap with peers again. We could also lower the ratings if the bank's internal capital generation were much weaker than we expect or if asset quality deteriorated substantially.

## Upside scenario

Although an upgrade is currently unlikely, we could consider it if the bank progressed in building bail-in-able buffers with subordinated instruments. An upgrade could also take place if its capital strengthened to the point that, when compared to the risks facing the bank, we thought it represented a ratings strength, provided that the bank's higher creditworthiness aligned with similarly rated peers'.

## Ratings Score Snapshot

|  | To              | From         |
|--|-----------------|--------------|
| Issuer Credit Rating                       | BBB-/Stable/A-3 | BB+/Stable/B |
| Stand-alone credit profile                 | bbb-            | bb+          |
| Anchor                                     | bbb             | bbb          |
| Business position                          | Moderate        | Constrained  |
| Capital and earnings                       | Adequate        | Adequate     |
| Risk position                              | Adequate        | Adequate     |
| Funding                                    | Adequate        | Adequate     |
| Liquidity                                  | Adequate        | Adequate     |
| Comparable ratings analysis                | 0               | 0            |
| Support                                    | 0               | 0            |
| Additional loss-absorbing capacity support | 0               | 0            |
| Government-related entity support          | 0               | 0            |
| Group support                              | 0               | 0            |
| Sovereign support                          | 0               | 0            |

|                                | To         | From |
|--------------------------------|------------|------|
| Additional factors             | 0          | 0    |
| Resolution Counterparty Rating | BBB/--/A-2 | NR   |

NR--Not rated.

## ESG credit indicators: E-2, S-2, G-2

### Related Criteria

- General Criteria: Hybrid Capital: Methodology And Assumptions, March 2, 2022
- Criteria | Financial Institutions | General: Financial Institutions Rating Methodology, Dec. 9, 2021
- Criteria | Financial Institutions | Banks: Banking Industry Country Risk Assessment Methodology And Assumptions, Dec. 9, 2021
- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- General Criteria: Group Rating Methodology, July 1, 2019
- Criteria | Financial Institutions | General: Risk-Adjusted Capital Framework Methodology, July 20, 2017
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

### Related Research

- European Banks' Residential Mortgage Losses Should Remain Contained Even As Economies Slow, Nov. 15, 2022
- Ibercaja Banco S.A., July 11, 2022
- Global Bank Country-By-Country Outlook 2023. Greater Divergence Ahead, Nov. 17, 2022
- European Banks: The Agile Will Come Out Stronger, Nov. 11, 2022

### Ratings List

#### New Rating

#### Ibercaja Banco S.A.

Resolution Counterparty Rating BBB/--/A-2

**Upgraded**

|                            | To              | From         |
|----------------------------|-----------------|--------------|
| <b>Ibercaja Banco S.A.</b> |                 |              |
| Issuer Credit Rating       | BBB-/Stable/A-3 | BB+/Stable/B |
| Senior Unsecured           | BBB-            | BB+          |
| Subordinated               | BB              | B+           |
| Preferred Stock            | B+              | B-           |

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at [www.standardandpoors.com](http://www.standardandpoors.com) for further information. A description of each of S&P Global Ratings' rating categories is contained in "S&P Global Ratings Definitions" at [https://www.standardandpoors.com/en\\_US/web/guest/article/-/view/sourceld/504352](https://www.standardandpoors.com/en_US/web/guest/article/-/view/sourceld/504352) Complete ratings information is available to subscribers of RatingsDirect at [www.capitaliq.com](http://www.capitaliq.com). All ratings affected by this rating action can be found on S&P Global Ratings' public website at [www.standardandpoors.com](http://www.standardandpoors.com). Use the Ratings search box located in the left column. Alternatively, call one of the following S&P Global Ratings numbers: Client Support Europe (44) 20-7176-7176; London Press Office (44) 20-7176-3605; Paris (33) 1-4420-6708; Frankfurt (49) 69-33-999-225; or Stockholm (46) 8-440-5914

Copyright © 2022 by Standard & Poor's Financial Services LLC. All rights reserved.

No content (including ratings, credit-related analyses and data, valuations, model, software or other application or output therefrom) or any part thereof (Content) may be modified, reverse engineered, reproduced or distributed in any form by any means, or stored in a database or retrieval system, without the prior written permission of Standard & Poor's Financial Services LLC or its affiliates (collectively, S&P). The Content shall not be used for any unlawful or unauthorized purposes. S&P and any third-party providers, as well as their directors, officers, shareholders, employees or agents (collectively S&P Parties) do not guarantee the accuracy, completeness, timeliness or availability of the Content. S&P Parties are not responsible for any errors or omissions (negligent or otherwise), regardless of the cause, for the results obtained from the use of the Content, or for the security or maintenance of any data input by the user. The Content is provided on an "as is" basis. S&P PARTIES DISCLAIM ANY AND ALL EXPRESS OR IMPLIED WARRANTIES, INCLUDING, BUT NOT LIMITED TO, ANY WARRANTIES OF MERCHANTABILITY OR FITNESS FOR A PARTICULAR PURPOSE OR USE, FREEDOM FROM BUGS, SOFTWARE ERRORS OR DEFECTS, THAT THE CONTENT'S FUNCTIONING WILL BE UNINTERRUPTED OR THAT THE CONTENT WILL OPERATE WITH ANY SOFTWARE OR HARDWARE CONFIGURATION. In no event shall S&P Parties be liable to any party for any direct, indirect, incidental, exemplary, compensatory, punitive, special or consequential damages, costs, expenses, legal fees, or losses (including, without limitation, lost income or lost profits and opportunity costs or losses caused by negligence) in connection with any use of the Content even if advised of the possibility of such damages.

Credit-related and other analyses, including ratings, and statements in the Content are statements of opinion as of the date they are expressed and not statements of fact. S&P's opinions, analyses and rating acknowledgment decisions (described below) are not recommendations to purchase, hold, or sell any securities or to make any investment decisions, and do not address the suitability of any security. S&P assumes no obligation to update the Content following publication in any form or format. The Content should not be relied on and is not a substitute for the skill, judgment and experience of the user, its management, employees, advisors and/or clients when making investment and other business decisions. S&P does not act as a fiduciary or an investment advisor except where registered as such. While S&P has obtained information from sources it believes to be reliable, S&P does not perform an audit and undertakes no duty of due diligence or independent verification of any information it receives. Rating-related publications may be published for a variety of reasons that are not necessarily dependent on action by rating committees, including, but not limited to, the publication of a periodic update on a credit rating and related analyses.

To the extent that regulatory authorities allow a rating agency to acknowledge in one jurisdiction a rating issued in another jurisdiction for certain regulatory purposes, S&P reserves the right to assign, withdraw or suspend such acknowledgment at any time and in its sole discretion. S&P Parties disclaim any duty whatsoever arising out of the assignment, withdrawal or suspension of an acknowledgment as well as any liability for any damage alleged to have been suffered on account thereof.

S&P keeps certain activities of its business units separate from each other in order to preserve the independence and objectivity of their respective activities. As a result, certain business units of S&P may have information that is not available to other S&P business units. S&P has established policies and procedures to maintain the confidentiality of certain non-public information received in connection with each analytical process.

S&P may receive compensation for its ratings and certain analyses, normally from issuers or underwriters of securities or from obligors. S&P reserves the right to disseminate its opinions and analyses. S&P's public ratings and analyses are made available on its Web sites, [www.standardandpoors.com](http://www.standardandpoors.com) (free of charge), and [www.ratingsdirect.com](http://www.ratingsdirect.com) (subscription), and may be distributed through other means, including via S&P publications and third-party redistributors. Additional information about our ratings fees is available at [www.standardandpoors.com/usratingsfees](http://www.standardandpoors.com/usratingsfees).

STANDARD & POOR'S, S&P and RATINGSDIRECT are registered trademarks of Standard & Poor's Financial Services LLC.