Press Release

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Insight beyond the rating.

DBRS Assigns BBB (low) Rating to Veneto Banca Scpa, Trend Negative

Industry: Fin.Svc.--Banks & Trusts

DBRS Ratings Limited (DBRS) has today assigned new ratings to Veneto Banca Scpa (Veneto Banca, the Bank or the Group). These ratings include a Senior Long-Term Debt and Deposit Rating of BBB (low) and a Short-Term Debt and Deposit Rating of R-2 (low). The Trend on both ratings is Negative. At the same time, DBRS assigned an Intrinsic Assessment (IA) to the Group of BBB (low) and a support assessment of SA-3.

The IA of BBB (low) reflects Veneto Banca's stable franchise in its home region of Veneto and its largely satisfactory financials. However, DBRS also notes the challenges faced by management to further streamline costs, effectively control asset quality, and also to strengthen Veneto Banca's capital position. Given the fragmented nature of banking in Italy and Veneto Banca's ranking as 12th largest bank by assets in Italy (EUR 40 billion), the ratings do not incorporate the expectation of timely support for the Group in the event of a highly stressed scenario. As such, DBRS has assigned an SA-3 support designation which does not provide upward rating support for the IA. The final rating for Veneto Banca of BBB (low) is thus equal to the IA. Although DBRS would view successful execution of Veneto Banca's plans to consolidate its prior acquisitions as a credit positive, at present DBRS does not foresee any immediate positive rating dynamic for Veneto Banca. The Negative Trend reflects the difficult economic condition in Italy and the direct challenges this environment poses for the Bank.

Veneto Banca has a stable market position in key retail markets, as well as a solid franchise across some of the key industrial and commercial districts in the wealthy regions of Northern Italy. The Bank's historically close knit relationships with retail and SME businesses across these regions are central to supporting the earnings generation capacity of the Bank. The Bank is active in 15 of Italy's 20 regions and holds a 1.5% national share of both deposits and loans. Outside of Italy, Veneto Banca has a small presence in Eastern Europe which is primarily focused on serving the needs of Italian customers abroad.

Veneto Banca's margins have deteriorated in recent years due to higher funding costs and this has been compounded by pressure to maintain competitive lending terms for its shareholder clients. In addition, the Bank has faced incremental costs for the ongoing consolidation and simplification of the Group structure following past acquisitions. Nonetheless, compared to the Italian banking system as whole, Veneto Banca has had an acceptable track record of pre-provision earnings during the extended economic downturn. Indeed, Income Before Provisioning and Taxes (IBPT) for 2012 improved to EUR 398 million, helped by carry trade earnings on Italian sovereign bonds and cost controls.

In 2012, Veneto Banca reported its first loss in many years of EUR 40 million. The result was triggered by provisioning costs which more than doubled in 2012 to EUR 467 million from EUR 177 million the prior year. The jump was a full EUR 200 million more than anticipated and reflected the recent on-site asset quality inspection by Bank of Italy. This inspection involved nearly all of Italy's largest institutions and recommended a more prudent approach in assessing collateral values for real estate for both retail and SME lending. The result for many banks, such as Veneto Banca, was a significant increase in required provisions in order to improve cash coverage as an offset to the lower collateral values. For DBRS, this additional caution is likely to translate into a higher level of future coverage requirements reflecting the worsening economic condition. This may put further pressure on Veneto Banca to deliver cost savings through its ongoing consolidation process so that IBPT can be improved and help to absorb what are expected to be higher credit costs.

DBRS notes that Veneto Banca has a stable and growing deposit base that is generally aligned with lending activity. Deposit levels have continued to increase over and above levels linked to former acquisitions, and there has also been a significant shift from demand to time deposits. Customer retention has also been solid, aided by both competitive pricing, as well as the shareholder/client status of many key customers. Competition for deposits has remained high in Italy which has added to Veneto Banca's funding costs. The growth in deposits combined with ECB borrowings has reduced Veneto Banca's reliance on the wholesale funding market, thus limiting the impact of the refinancing risk for the medium term. DBRS notes that the Bank does have sizeable LTRO borrowings of EUR 4 billion, but this funding has been largely invested in government and other securities that can be used to pay down this borrowing at maturity. Nevertheless, absent a normalization of bank funding markets in Italy, Veneto Banca will likely face the challenge of reduced earnings when this ECB funding is replaced.

Veneto Banca's relatively simple risk profile reflects the nature of the Bank's franchise as a cooperative, predominantly retail, bank with related activities. Within the group, the total lending portfolio is 95% domestic and mainly concentrated within the Parent Company "Veneto Banca Scpa" which is the central entity into which the Bank's core acquisitions will be merged. Lending to households and SMEs dominate the portfolio and are largely represented by mortgages. In recent years the Bank has experienced a significant deterioration in asset quality. This development has been system-wide and Veneto Banca's impaired lending has increased steadily since the beginning of the current economic downturn. Impaired lending to total loans was 6.5% in 2008 but rose to roughly 10% for 2011, before stepping up to more than 13% by end 2012. The latest increase was also impacted by stricter regulatory definitions on past due loans, as well as further deterioration in the economy. Credit quality concerns remain concentrated in commercial real estate and corporate lending, particularly domestic oriented SMEs. Although there has been only limited deterioration in residential mortgage quality, DBRS notes that the Bank has a significant overall exposure to real estate including EUR 6.7 billion in residential and EUR 5.1 billion in SME and commercial real estate. Together, these comprise 42% of the total gross loan book in 2012.

DBRS notes that Veneto Banca faces challenges regarding capital levels. In 2012, Veneto Banca reported a Basel II Core Tier 1 capital ratio of 7.3%, up from 7.0% in 2011, mainly as result of the EUR 210 million capital increase which more than offset EUR 40 million loss reported for the year. DBRS also notes that Veneto Banca's regulatory capital ratios are calculated using standardized models for risk weightings and this results in lower ratios relative to banks using advanced models. DBRS notes that Veneto Banca's Core Tier 1 remains below the system average, and the Bank may face challenges in strengthening capital in preparation for Basel III in the current economic environment. DBRS views Veneto Banca's shareholder support as critical, particularly given the mutual structure and the inability of the Bank to raise capital in wholesale markets.

Notes:
All figures are in EUR unless otherwise noted.

The principal applicable methodology is the Global Methodology for Rating Banks and Banking Organisations. Other methodologies used include the DBRS Criteria – Intrinsic and Support Assessments. Both can be found on the DBRS website under Methodologies.

The sources of information used for this rating include company documents, Bank of Italy and SNL Financial. DBRS considers the information available to it for the purposes of providing this rating was of satisfactory quality.

Ratings assigned by DBRS Ratings Limited are subject to EU regulations only.

Lead Analyst: Peter Burbank
Rating Committee Chair: Alan G. Reid
Initial Rating Date: 13 May 2013
Most Recent Rating Update: 13 May 2013

For additional information on this rating, please refer to the linking document under Related Research.

Issuer	Debt Rated	Rating Action	Rating	Trend	Latest Event
Veneto Banca Scpa	Senior Long-Term Debt and Deposits	New Rating	BBB (low)	Neg	May 13, 2013
Veneto Banca Scpa	Short-Term Debt and Deposits	New Rating	R-2 (low)	Neg	May 13, 2013

For more information on this credit or on this industry, visit www.dbrs.com or contact us at info@dbrs.com.

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