IBL Banca S.p.A.
Issuer Rating Report

SCOPE BBB STABLE

Overview

Scope Ratings has assigned an issuer rating of BBB to IBL Banca S.p.A., with a Stable Outlook. The rating was affirmed on 21 July 2020.

Highlights

- The rating is based on the low-risk business model of IBL, a leader in the Italian market for payroll and pension deducted loans (PDLs), which is a high-margin, low-risk personal loan product with a long history in Italy. These loans have a complex structure, involving several players and a long origination process. IBL seems to have mastered the vertical value chain entirely, evidenced by the bank's negligible credit-loss levels and high profitability across the credit cycle.
- The Outlook is Stable, reflecting our view that risks to the current rating level are balanced. The Covid-19 lockdown, which is likely to drive a very deep economic downturn in Italy, will in our view not materially alter IBL's risk profile. This is due to the bank's low asset risk and strong lines of defence, which include high profitability and strong capital. IBL's capital position is adequate, and will materially improve due to a reduction in the risk weight intensity of PDLs under CRD5.
- The ratings also account for the large exposure to Italian government bonds, mostly financed via short-term repos. This represents a large risk concentration. As most of the bonds are in the Held to Collect portfolio, they do not pose a short-term risk to the group's regulatory capital. They could, however, become a drain on liquidity under stressed scenarios.
- Aside from repo funding for the government bond portfolio, IBL funds itself through deposits and securitisations of its loan book, which have historically been retained and used as collateral for repo operations. TLTRO3 eligibility will structurally change the funding of the bank, allowing it to lower its cost of funding.
- We also highlight the key person risk regarding Mario Giordano, who has been the bank's CEO since 1998.

Rating drivers (summary)

The rating drivers, in decreasing order of importance in the rating assignment, are:

- Market leader in Italian payroll and pension deducted loans
- Very low asset risk due to the intrinsic characteristics of the products
- Strategic targeting of market share consolidation and business diversification
- Very strong financial fundamentals, including capital, asset quality and profitability
- Material exposure to Italian sovereign risk
- TLTRO3 eligibility provides funding surplus and flexibility
- Owned and closely controlled by management

Ratings & Outlook

Issuer rating	BBB
Outlook	Stable

Lead Analyst

Marco Troiano
m.troiano@scoperatings.com

Team Leader

Dierk Brandenburg
d.brandenburg@scoperatings.com

Scope Ratings GmbH

3rd Floor
111 Buckingham Palace Road
UK-London SW1W OSR

Phone +44 20 3457 0444

Headquarters

Lennéstraße 5
10785 Berlin

Phone +49 30 27891-0
Fax +49 30 27891-100

info@scoperatings.com
www.scoperatings.com

Bloomberg: SCOP

Rating-change drivers

A material reduction in the large carry trade in government securities. The bank's Italian sovereign exposure represents a material risk against which almost no capital is retained. IBL's carry trade on government bonds, while adding to profitability, does not belong to its core business, in our view, and detracts from its credit.

Volatility in value of government bond portfolio. Even a temporary decline in the value of government bonds could erode the group's liquidity: selling the bonds would translate into permanent losses, while financing the position could require higher margins.

A material increase in business model risk as a result of diversification efforts. One of IBL's key strengths is its focus on a relatively high-margin, low-risk market niche. In recent years, the group has initiated a measured diversification strategy, adding non-performing loan (NPL) investments to its activities. However, this activity has so far remained marginal. Downside risks could arise if very fast growth in these new activities materially change the group's risk DNA.

Any indication that Italy's eurozone membership is at risk. Italy's departure from the euro remains extremely unlikely. At the same time, some politicians, including in governing parties, have advocated such an outcome. A change in the currency regime would not only be extremely difficult to execute, but would also pose a material risk for financial institutions, with likely effects being a material disruption to activities and a risk of funding runs. Such an event could result in a multiple-notch downgrade for Italian banks, including IBL.

Rating drivers (details)

Market leader in Italian payroll and pension deducted loans

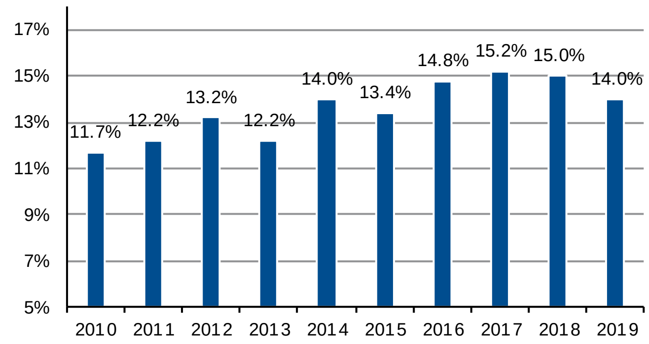
IBL Banca S.p.A. is the parent company of the IBL banking group, whose fully owned subsidiaries manage the services, real estate and the distribution of insurance for the entire group.

Market leader in payroll deducted loans in Italy

IBL is essentially a specialised lender that offers personal loans to Italian individuals, particularly Italian PDLs, including 'cessioni del quinto dello stipendio' (CQS), 'cessioni del quinto della pensione' (CQP), 'deleghe di pagamento' (DP), and 'anticipo del trattamento di fine servizio' (TFS). The group is a market leader in Italy for PDLs, with a solid 14% market share in PDL origination.

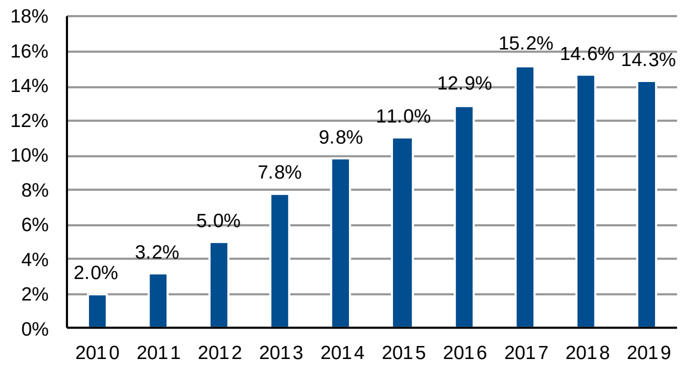
IBL also offers saving and insurance products, as well as payment cards.

Figure 1: IBL's market share, new business



Source: Company data, Assofin, Scope Ratings.

Figure 2: IBL's market share, stock

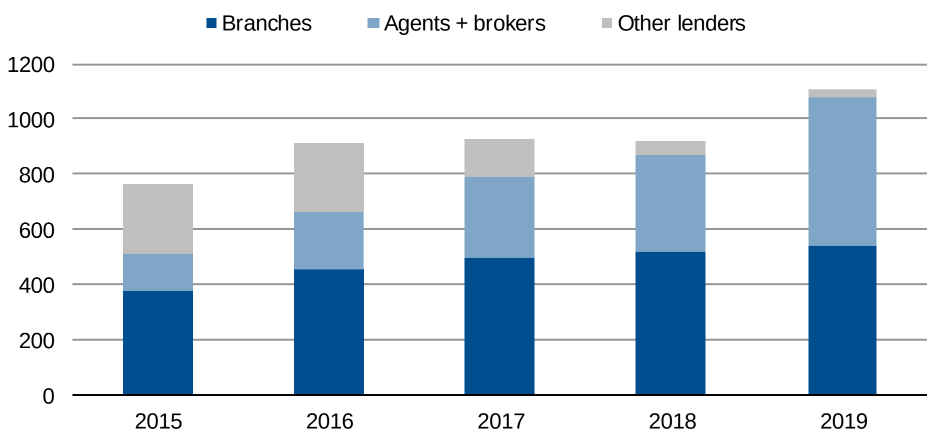


Source: Company data, Assofin, Scope Ratings.

Good diversification in distribution channels

As at the end of 2019, IBL's commercial model involves direct distribution through its own brand (54 branches), as well as indirect distribution via agents, promoters and bank distribution agreements. In the last five years, growth has been fuelled by the work of third-party agents and brokers, as well as via branches, which have usually represented 50% of annual origination. In contrast, distribution via lenders (in partnership) has shrunk.

Figure 3: Loan origination by type of distribution channel, historical (EUR m)



Source: Company data, Scope Ratings

Historically, IBL had operated an originate-to-distribute business model, largely due to limited financial resources. After obtaining a banking licence in 2004 and acquiring 30 Citifinancial branches in 2009, IBL started to accumulate deposits. Since 2012, it has undertaken several capital increases totalling EUR 62.5m. This has allowed the bank to transition to a more balance sheet-intensive model, also helped by readily available liquidity in wholesale markets and by the central bank. Today, the bank's business model aims to retain loans on the balance sheet, funding them through a mix of retail deposits and repo funding.

Very low asset risk due to the intrinsic characteristics of products

CDQs are a well established product in Italy, with low credit risk

CDQ and CDP loans are inherently low risk: historically rooted in post-unification Italy to help public-sector employees gain access to credit, CDQ was more formally regulated in 1950 by Italy's Law 180/1950 together with a wider reform of personal credit. However, it remained reserved for public-sector employees. In 2004, the product was extended to private-sector employees. In the process, several limitations were removed, such as a minimum job tenure, while more flexibility was provided on loan duration.

Today, the main characteristics of this product are:

- A target population of public- or private-sector employees and pensioners
- A duration of 24-120 months
- No maximum amount – it depends on the borrower's salary, with the average ticket at around EUR 20,000; for IBL, the maximum amount is EUR 75,000
- Monthly repayments – up to 20% of the salary or pension, including capital, interest and all fees
- Direct deductions from payroll
- Compulsory insurance for loss of employment and death
- Easy to obtain – no need for a specific purpose; credit decision made in the branch (or by an agent, or online); even available to individuals with poor credit records

These loans are essentially consumer credit products with an extremely low credit risk (the actual credit risk stems from the employer, or the insurance company in the event of job loss or the employee's death).

Also known as 'doppio quinto', a DP loan is similar to a CQS loan (only for employees) but can be up to 40% of the salary amount, in some cases even 50%, and requires the employer to accept a framework agreement (making it unavailable to some employees and to all pensioners). Government agencies typically have a framework agreement in place.

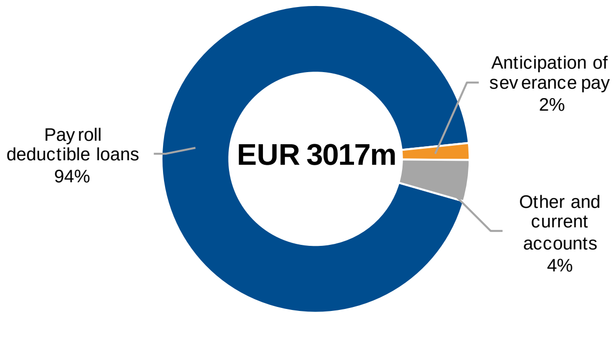
The small average tickets ensure that the bank's portfolio is very granular, with no large concentrations at individual borrower level. However, concentration risk can be present in terms of the employer or the insurance counterparty.

IBL's loan book stood at EUR 3bn at the end of 2019. PDLs made up 94% of the total, with the balance divided into the anticipation of severance pay (2%) and other loans (4%). The anticipation of severance pay is a new product, launched in 2019.

Loans to public sector employees and pensioners represent the bulk of IBL's book

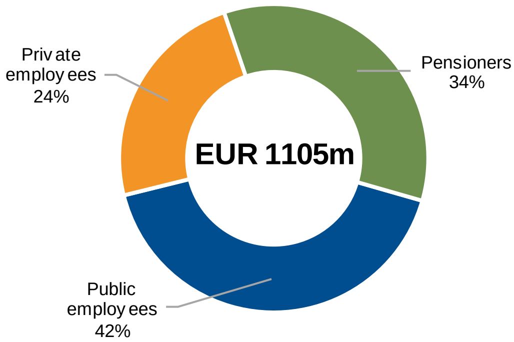
In 2019, loan origination increased by around 20%, thanks also to the contribution from new subsidiary, IBL Family, a joint venture with real estate agency network Tecnocasa. IBL Family originates PDLs in the context of house purchase processes. More than two-thirds of new loans have been granted to public employees and pensioners, for whom the risk of income loss is particularly limited. The share represented by private employees was material, at 24%, and has been growing markedly in the past few years.

Figure 4: Loan book composition, YE 2019



Source: Company data, Scope Ratings.

Figure 5: Loan origination in 2019 – breakdown by type of customer



Source: Company data, Scope Ratings.

Strategic targeting of market share consolidation and business diversification

IBL's strategy targets consolidation of the leadership in PDL and measured diversification into NPLs

At the beginning of 2019, IBL's board of directors approved the new strategic guidelines for 2019-21. Going forward, the bank aims to consolidate its position in the PDL market, targeting a market share of 18%-20%, while cautiously diversifying into other product segments. Among these, we highlight:

1) TFS loans, namely an anticipation of the severance pay to which public-sector employees are entitled at the end of their career
2) IBL Family, a joint venture with real estate agent network Tecnocasa, which originates PDL loans in conjunction with home buying processes allowing customers to get better mortgage terms (on account of lower loan-to-value ratios).
3) Unsecured retail NPLs: in 2018, IBL and EuropaFactor founded Credit Factor, a joint venture with a focus on purchasing and managing small-ticket unsecured NPLs originated by banks. Given the low market price for these portfolios, IBL is aiming at maximising recovery values, including via restructurings.
4) Secured NPLs: in June 2019, IBL bought a 9.9% stake in Frontis NPL and entered into a partnership for co-investment in secured NPL securitisations for up to EUR 50m.
5) Bancassurance: IBL has bought a 19.75% stake in Net Insurance, a key player in PDL insurance, and agreed to distribute their insurance products for individuals and households via its branch network.

Our understanding is that IBL's investment in potentially riskier markets will proceed at a highly controlled pace. We do not expect the group's business risk profile to shift materially in the next few years.

Limited financial impact from the Covid-19 recession, with the bank expected to maintain good asset quality, capital and profitability

We forecast negative GDP growth of 10% under our baseline scenario, and 12.8% GDP decline under our stressed scenario

The sudden onset of the Covid-19 pandemic, and related lockdown in H1 2020, is bound to leave scars on the Italian economy.

At this stage, it is difficult to estimate the full extent of the economic blow from the health crisis, which will depend, among other things, on the likelihood of a second lockdown, the effectiveness of public support measures and, last but not least, the international economic scenario.

At present, we forecast negative GDP growth of 10% under our baseline scenario, and 12.8% GDP decline under our stressed scenario.

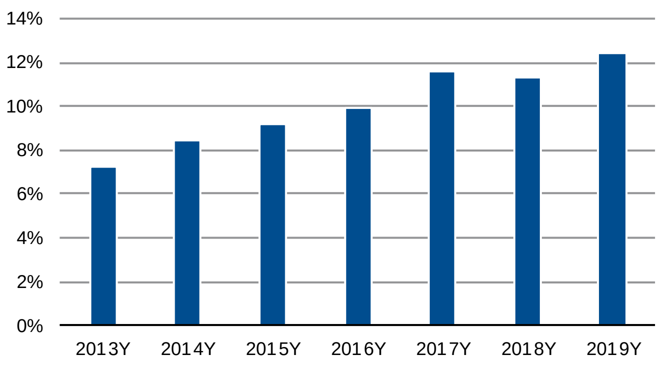
Coupled with the likely decline in tax revenues from the growth slowdown and the equally likely need to increase healthcare-related expenditures in the short term, it is already clear that government finances are set to deteriorate sharply.

We believe IBL's business model should allow it to weather the storm relatively well.

While some deterioration in IBL's performance can be expected, we believe its business model should allow it to weather the storm relatively well. Inherently low asset risk, with the majority of borrowers public-sector employees and pensioners, will in our view limit the need for credit provision, at least relative to commercial banks.

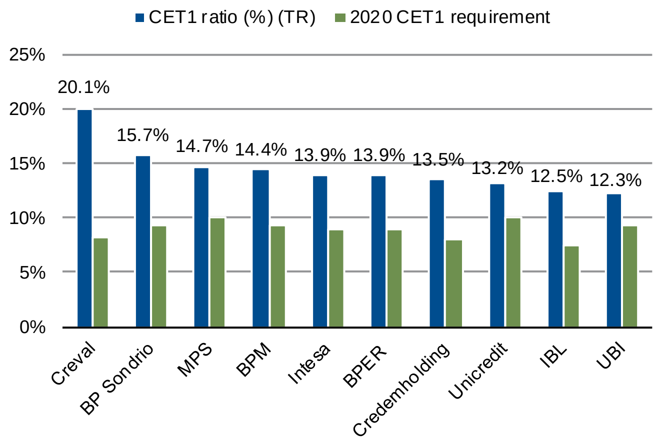
IBL's profitability is high, providing the bank with a strong first line of defense in credit downturns. With a CET1 ratio on a transitional basis of 12.5% at the end of 2019, IBL is well capitalised. From June 2020, the risk weighting of PDL under standardised models should drop from 75% to 35%, which would release significant capital for IBL and also boost reported capital ratios and the return on allocated capital.

Figure 6: IBL's historical CET1 ratio



Source: SNL Scope Ratings

Figure 7: IBL's capital position compared to that of selected Italian banks – YE 2019



Source: Company data, SNL, Scope Ratings.

Material exposure to Italian sovereign risk

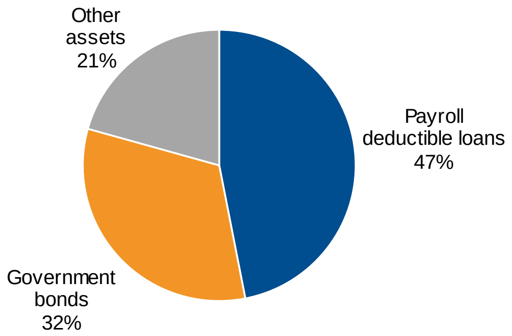
IBL's exposure to domestic sovereign risk is very material

While almost all loans are either CQS, CQP or DP, a large component of IBL's balance sheet comprises Italian government bonds, which boost profitability but represent a potential risk. Over the past five years, government bonds have been a significant source of carry trade income and trading gains for IBL, helping it to recapitalise and to finance business growth. As of Q4 2019, the Italian government bond portfolio stood at approx. EUR 2.1bn, decreased by EUR 0.4bn year-on-year and almost six times the group's CET1 capital, which we deem very high.

We still consider Italian government bonds to be safe assets (Scope rates Italian debt at BBB+, Negative Outlook). However, such a large, concentrated exposure to any borrower would pose a non-negligible risk. Moreover, Italian sovereign bond yields have in recent years been volatile as a result of the previous government's ambivalent attitude to previous fiscal commitments.

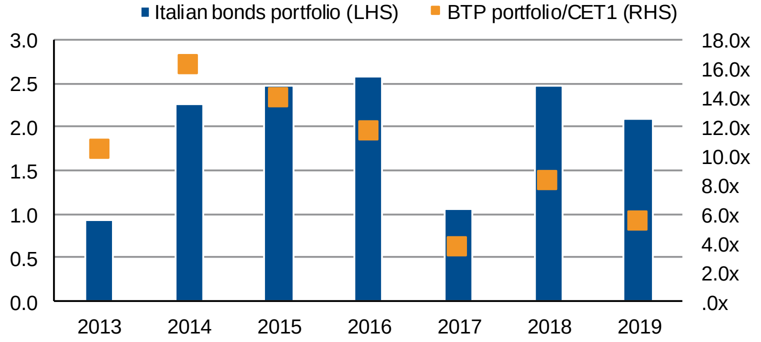
Most of the portfolio is Held to Collect (at cost), which poses little risk to regulatory capital, though it may result in a drain on liquidity if repo haircuts rise. The government bond portfolio is for the most part self-funded via repos, though IBL maintains a buffer of unencumbered bonds as a liquidity reserve.

Figure 8: Total asset split, YE 2019



Source: Company data, Scope Ratings.

Figure 9: Total exposure to Italian debt in absolute terms and as % of transitional CET1, historical



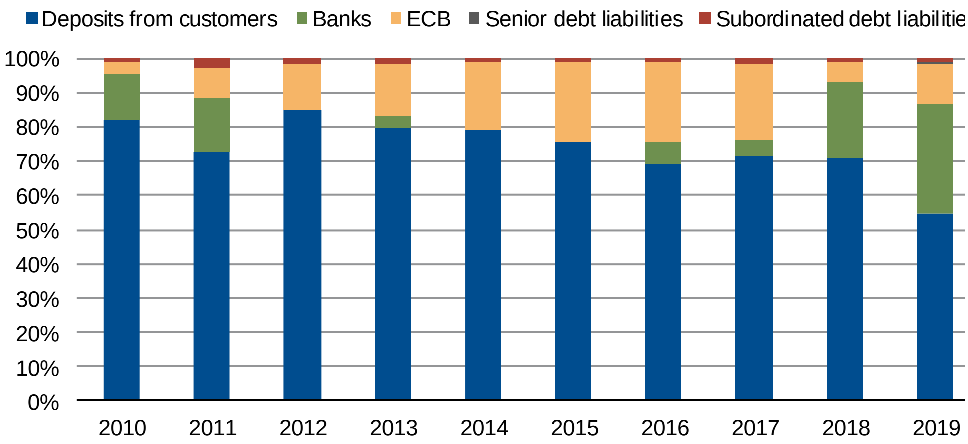
Source: Company data, Scope Ratings.

TLTRO3 eligibility provides funding surplus and flexibility

Going forward, IBL will benefit from central bank funding eligibility at favourable terms

The core PDL business has historically been primarily funded via a mix of deposits, central bank funding and private repos (Figure 10). In recent years, use of central bank funding has declined, resulting in increased activity on the secured interbank market (securitised PDL portfolios were used as collateral for these transactions). Going forward, we expect the bank to make increased use of central bank funding, given the eligibility and very advantageous terms of the TLTRO3 facility, for which IBL is eligible.

Figure 10: IBL's historical funding breakdown



Source: SNL, Scope Rating

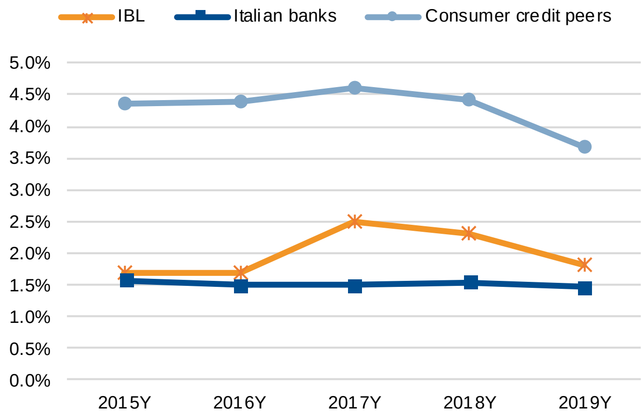
Owned and closely controlled by management

Mario Giordano, the bank's CEO since 1998 (when it was called Istituto Finanziario del Lavoro), controls 50% of the shares through holding company Delta 6. Giordano has led the group through several transformation cycles, including the acquisition of a banking license in 2004 and the recent move from an 'originate to distribute' model to a balance sheet model. His partners, the D'Amelio family, control the other 50% through holding company Sant'anna srl and sit on the board of directors.

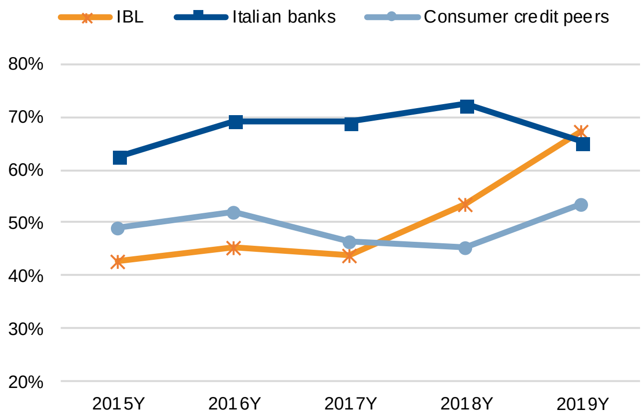
We believe Giordano represents a key person risk for the bank. His departure would add significant uncertainty in terms of both governance and strategy.

I. Appendix: Peer comparison

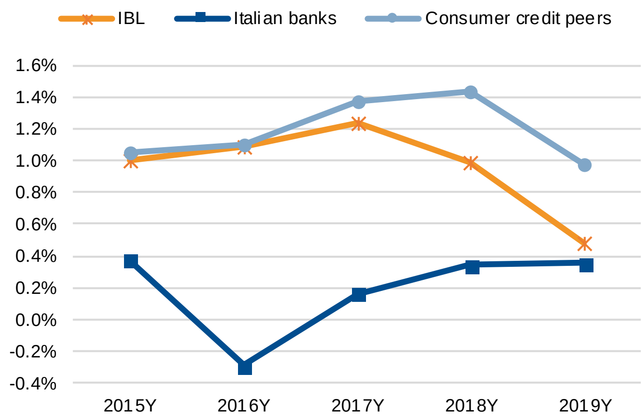
Net interest margin



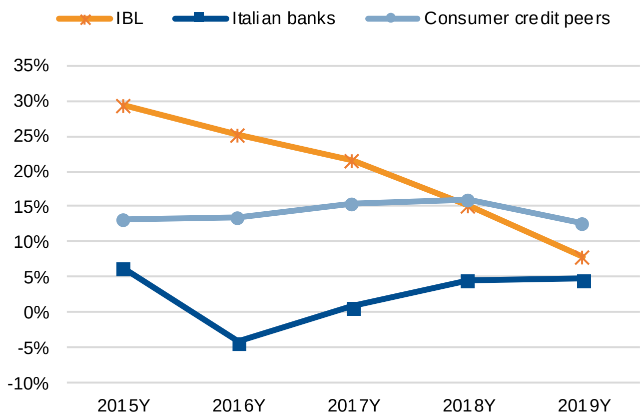
Cost-income ratio



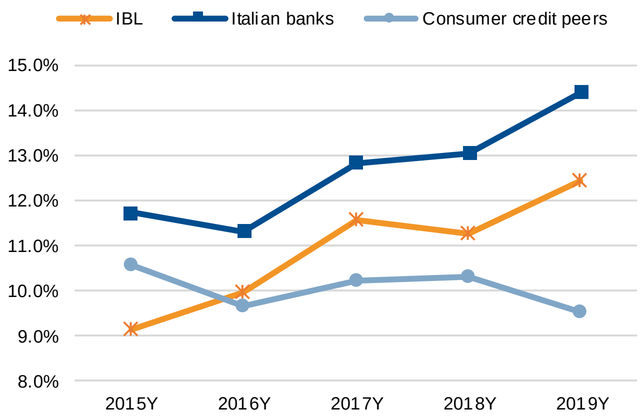
Return on average assets



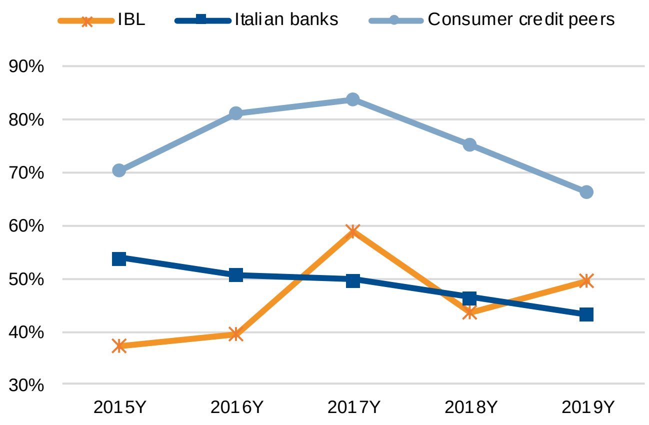
Return on average equity



CET1 ratio (transitional basis)



Asset risk intensity (RWAs as % of total assets)



Source: SNL
Italian banks: Unicredit, Intesa, Banca MPS, Banca Carige, BP Sondrio, Banco BPM; BPER, Credem, Creval, Mediobanca, UBI.
Credit consumer peers: Agos Ducato SpA, BCC Credito Consumo, Consel SpA, Creditis Servizi finanziari, Fiditalia SpA, Findomestic Banca, PrestiNuova, Prestitalia, Compass

II. Appendix: Selected Financial Information – IBL Banca S.p.A.

	2015Y	2016Y	2017Y	2018Y	2019Y
Balance sheet summary (EUR m)					
Assets					
Cash and interbank assets	372	376	285	424	459
Total securities	2,508	2,619	495	81	205
of which, derivatives	28	32	17	22	26
Net loans to customers	2,031	2,316	3,180	5,243	4,988
Other assets	252	248	248	276	383
Total assets	**5,162**	**5,559**	**4,207**	**6,023**	**6,036**
Liabilities					
Interbank liabilities	1,100	1,534	1,008	1,527	2,382
Senior debt	1	1	1	1	23
Derivatives	28	45	26	54	78
Deposits from customers	3,619	3,545	2,654	3,914	2,950
Subordinated debt	65	60	60	60	60
Other liabilities	129	132	144	123	142
Total liabilities	**4,942**	**5,316**	**3,892**	**5,678**	**5,635**
Ordinary equity	220	242	315	345	394
Equity hybrids	0	0	0	0	0
Minority interests	0	0	0	0	8
Total liabilities and equity	**5,162**	**5,559**	**4,207**	**6,023**	**6,036**
Core tier 1/ common equity tier 1 capital	*175*	*219*	*286*	*297*	*371*
Income statement summary (EUR m)					
Net interest income	80	87	115	112	104
Net fee & commission income	31	30	14	7	11
Net trading income	25	48	36	34	18
Other income	0	1	1	3	4
Operating income	**136**	**166**	**167**	**155**	**137**
Operating expenses	58	75	74	83	92
Pre-provision income	**78**	**91**	**94**	**72**	**45**
Credit and other financial impairments	2	2	4	-2	4
Other impairments	0	0	0	0	0
Non-recurring income	NA	NA	NA	NA	NA
Non-recurring expense	NA	NA	NA	NA	NA
Pre-tax profit	**76**	**89**	**89**	**74**	**41**
Income from discontinued operations	0	0	0	0	0
Income tax expense	24	28	29	24	11
Other after-tax Items	0	0	0	0	0
Net profit attributable to minority interests	0	0	0	0	0
Net profit attributable to parent	**52**	**61**	**60**	**50**	**29**

Source: SNL, Scope Ratings

III. Appendix: Selected Financial Information – IBL Banca S.p.A.

	2015Y	2016Y	2017Y	2018Y	2019Y
Funding and liquidity					
Net loans/ deposits (%)	56%	65%	120%	134%	169%
Liquidity coverage ratio (%)*	140%	NA	NA	NA	158%
Net stable funding ratio (%)	NA	NA	NA	NA	NA
Asset mix, quality and growth					
Net loans/ assets (%)	39.3%	41.7%	75.6%	87.0%	82.6%
Problem loans/ gross customer loans (%)	1.9%	1.9%	NA	1.6%	2.1%
Loan loss reserves/ problem loans (%)	23.2%	24.0%	NA	26.9%	24.7%
Net loan growth (%)	25.5%	14.0%	37.3%	64.9%	-4.9%
Problem loans/ tangible equity & reserves (%)	17.0%	17.9%	NA	22.5%	24.8%
Asset growth (%)	10.6%	7.7%	-24.3%	43.2%	0.2%
Earnings and profitability					
Net interest margin (%)	1.7%	1.7%	2.5%	2.3%	1.8%
Net interest income/ average RWAs (%)	4.5%	4.2%	4.9%	4.4%	3.7%
Net interest income/ operating income (%)	58.8%	52.3%	69.1%	72.2%	75.6%
Net fees & commissions/ operating income (%)	23.0%	18.2%	8.5%	4.4%	7.8%
Cost/ income ratio (%)	42.8%	45.1%	44.0%	53.4%	67.2%
Operating expenses/ average RWAs (%)	3.3%	3.6%	3.2%	3.3%	3.3%
Pre-impairment operating profit/ average RWAs (%)	4.4%	4.4%	4.0%	2.8%	1.6%
Impairment on financial assets / pre-impairment income (%)	2.3%	2.3%	4.6%	-2.3%	8.9%
Loan loss provision/ average gross loans (%)	0.1%	0.1%	NA	NA	0.1%
Pre-tax profit/ average RWAs (%)	4.3%	4.3%	3.8%	2.9%	1.4%
Return on average assets (%)	1.0%	1.1%	1.2%	1.0%	0.5%
Return on average RWAs (%)	2.9%	3.0%	2.6%	2.0%	1.0%
Return on average equity (%)	29.4%	25.2%	21.6%	15.3%	7.8%
Capital and risk protection					
Common equity tier 1 ratio (%, fully loaded)	NA	NA	NA	NA	12.5%
Common equity tier 1 ratio (%, transitional)	9.1%	10.0%	11.6%	11.3%	12.5%
Tier 1 capital ratio (%, transitional)	10.2%	10.9%	12.4%	12.1%	13.2%
Total capital ratio (%, transitional)	13.1%	12.8%	13.8%	13.0%	13.7%
Leverage ratio (%)	3.8%	4.4%	7.3%	5.1%	6.4%
Asset risk intensity (RWAs/ total assets, %)	37.1%	39.6%	58.7%	43.7%	49.4%
Market indicators					
Price/ book (x)	NA	NA	NA	NA	NA
Price/ tangible book (x)	NA	NA	NA	NA	NA
Dividend payout ratio (%)	NA	NA	NA	NA	NA

Source: SNL, Scope Ratings
*Average in 2019

Scope Ratings GmbH

Headquarters Berlin

Lennéstraße 5
D-10785 Berlin

Phone +49 30 27891-0

Frankfurt am Main

Neue Mainzer Straße 66-68
D-60311 Frankfurt am Main

Phone +49 69 66 77 389-0

Paris

1 Cour du Havre
F-75008 Paris

Phone +33 1 8288 5557

London

3rd Floor
111 Buckingham Palace Road
UK-London SW1W 0SR

Phone +44 20 3457 0444

Madrid

Edificio Torre Europa
Paseo de la Castellana 95
E-28046 Madrid

Phone +34 914 186 973

Milan

Via Paleocapa 7
IT-20121 Milan

Phone +39 02 30315 814

Oslo

Haakon VII's gate 6
N-0161 Oslo

Phone +47 21 623142

info@scoperatings.com
www.scoperatings.com

Disclaimer