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UniCredit SpA

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UniCredit SpA

SACP	BBB
Anchor	bbb	
Business Position	Strong	+1
Capital and Earnings	Adequate	0
Risk Position	Moderate	-1
Funding	Average	0
Liquidity	Adequate	

+

Support	0
ALAC Support	0
GRE Support	0
Group Support	0
Sovereign Support	0

+

Additional Factors	0

Issuer Credit Rating
BBB/Negative/A-2

Resolution Counterparty Rating
BBB+/--/A-2

Major Rating Factors

Strengths:	Weaknesses:
• Strong franchise in Italy, Germany, Austria, and Central and Eastern Europe (CEE). • High level of geographic diversification. • Sound and well-balanced funding base.	• Significant business and credit exposure in higher economic risk countries than international peers. • Likely rise in non-performing exposures and credit losses amid COVID-19-driven recession. • Modest profitability prospects.

Outlook: Negative

The negative outlook on UniCredit primarily reflects increased pressure on revenue and asset quality and significant downside risks we see to our base-case expectations over the next two years.

Downside scenario

We could lower the rating if we see that economic and operating conditions have materially deteriorated, implying far more negative effects on UniCredit's credit metrics compared with our current expectations. In particular, a downgrade could follow if we saw the bank's projected risk-adjusted capital (RAC) falling below 7% and its asset-quality metrics deteriorating much more than we currently expect, over the next two years.

A negative action on the Italian sovereign would not necessarily lead to a downgrade on UniCredit. We could affirm the ratings on UniCredit in such circumstances, and potentially rate it above the sovereign, provided that we continue to believe that it will maintain sufficient loss-absorbing buffers to protect senior bondholders, reduces its exposures in Italy, and nonperforming exposures (NPEs) do not increase too much--thereby improving the chance that it could withstand a sovereign default.

Upside scenario

We could revise the outlook back to stable if we were to see easing economic conditions, particularly in Italy, or we were to conclude that there are reduced downside risks to UniCredit's creditworthiness.

Hybrids

We do not assign outlooks to bank issue ratings. However, we will continue to notch the ratings on the hybrids--namely senior non-preferred, subordinated, and junior subordinated notes--down from the lower of two potential starting points: the stand-alone credit profile (SACP) and the issuer credit rating (ICR). Still, in the event of a downgrade of Italy, we might lower our issue ratings on the hybrid instruments by widening the notching, even if we were to affirm the ICR on UniCredit. At this stage, we conclude that our hypothetical sovereign default scenario would trigger the resolution of UniCredit relatively quickly, given its direct sovereign exposures, with a bail-in of the subordinated instruments to recapitalize the bank.

Rationale

The starting point for our ratings on UniCredit group is its 'bbb' anchor, which we base on our view of economic risks across the countries in which the group operates and industry risks in its home market of Italy.

Our ratings on UniCredit SpA reflect our opinion that the bank will continue to build on its strengths--its strong franchises and leading positions in commercial banking in its core markets of Italy, Germany, Austria, and most of the countries in Eastern Europe, in continuity with the business strategy it launched in 2016 and reiterated in the recently-presented 2020-2023 business plan. We also believe the efforts the bank made to shed their legacy NPEs in Italy, improved quality of credit underwriting, and build-up capital could put them in a better position to cope with the challenging economic conditions, compared with most Italian banks.

Still, we expect the COVID-19 pandemic to cause a severe recession in Italy and most European countries where UniCredit operates in 2020. Although we expect a recovery in 2021, we anticipate it will not immediately and entirely offset the damage caused to the economy, household wealth, and various corporate sectors.

Even under our base-case scenario, we expect a meaningful deterioration of UniCredit's asset quality, revenue, and profitability through the course of 2020 and into 2021.

More specifically, we expect operating income to sharply decline in 2020, as a result of falling revenue--by 5%-10% compared with 2019--and almost doubling credit losses from €3.3 billion. We anticipate this trend will only partially reverse in 2021 to then restate a pre-COVID-19 earnings in 2022.

Despite pressure on its earnings, we forecast UniCredit's RAC will remain sustainably above 7% over the next two years, compared with an estimated 7.5%-8.0% as of year-end 2019. On this point, we think that management's commitment to confirm its target of common equity Tier 1 (CET 1) maximum distributable amount (MDA) buffers of 200-250 basis points (bps) would likely result into prudent capital management over the next couple of years, supporting our existing expectations.

We assess UniCredit group's creditworthiness, including its capital position, on a consolidated basis. In this context, we assume fungibility of resources among UniCredit group entities within regulatory limits. Our assessment takes into account management's public stance on managing capital allocations on a consolidated basis, including excess regulatory capital in certain operations, and the group's track record in this respect.

Anchor: 'bbb', based on the average economic risk score of countries where UniCredit operates, and industry risk in Italy.

Our bank criteria use our Banking Industry Country Risk Assessment economic risk and industry risk scores to determine a bank's anchor, the starting point in assigning an ICR. We assess the economic risk for UniCredit based on our view of the weighted-average economic risk in the countries in which UniCredit operates--Italy, Germany, Austria, and CEE countries. Italy's share is the largest in our assessment of UniCredit's weighted economic risk. The economic risk score we apply to determine UniCredit's anchor is '4' (on a scale of 1 to 10). By contrast, UniCredit's anchor takes into account our industry risk score for Italy, the bank's country of domicile, which is '5' (on a scale of 1 to 10). Our anchor for UniCredit is 'bbb'. This anchor compares favorably with those of other Italian banks operating almost exclusively in Italy. The anchor benefits from the bank's high degree of diversification in countries with comparatively lower economic risk than that of UniCredit's domestic market, in our view.

We believe that Italian banks continue to face higher economic risk than most European peers. While most Italian banks had largely absorbed the effect of past recessions and tightened their underwriting standards, some still have meaningful legacy NPEs, an additional burden in a deteriorating economic environment. Moreover, the substantial amount of time needed for creditors in Italy to recover collateral and settle lawsuits--due to the less effective insolvency and foreclosure procedures and judicial system--remains a weakness compared with most advanced economies. In such a context, the sharp contraction in economic activity in 2020 amid the coronavirus outbreak is likely to impact a large number of small and midsize enterprises to which the Italian banks are particularly exposed, in our opinion. We anticipate Italian banks' credit losses will double in 2020 and 2021, versus roughly 70bps reported in 2019, before then normalizing again only in 2022 when we expect Italy's GDP to return to near 2019 levels.

The bank's German and Austrian operations also account for a significant portion of its total assets. Our economic risk assessment for Germany reflects its highly diversified and competitive economy and lack of major economic imbalances. Our economic risk assessment for Austria reflects its highly competitive and diverse economy and its strong economic fundamentals.

Industry risks for Italian banks are also higher than for banks in peer countries, in our opinion. Italian banks' access to affordable unsecured wholesale funding remains constrained from time to time by uncertainties about the sovereign's creditworthiness and economic prospects. Clearly, near- to medium-term refinancing risk has abated, given the abundant liquidity provided the European Central Bank (ECB), the large deposit funding base, and the banking sector's very low external position, with only 5% of reliance on wholesale funding. Failing business volume and margins combined with structural problems, such as high cost bases and fragmentation, will constrain the banks' capacity to absorb the likely rise in credit losses over the next couple of years.

Table 1

UniCredit SpA--Key Figures

	--Year ended Dec. 31--				
Mil. €	**2019**	**2018**	**2017**	**2016**	**2015**
Adjusted assets	852,847	827,961	833,404	856,341	854,675
Customer loans (gross)	442,493	466,990	451,275	467,741	489,503
Adjusted common equity	48,260	44,200	45,842	30,747	41,719
Operating revenues	17,995	20,086	19,208	18,165	22,398
Noninterest expenses	10,030	10,703	11,356	12,237	13,400
Core earnings	3,258	6,150	4,478	(6,992)	4,577

Business position: One of the largest pan-European banking groups.

The stability of the group's revenue stream will continue to stem from its higher degree of geographic diversification compared with most of its domestic and international peers, in our opinion. UniCredit is the second-largest bank in Italy after Intesa Sanpaolo SpA, with a market share of about 12% of domestic loans. Germany's UniCredit Bank AG has a strong domestic footprint, while Austria's UniCredit Bank Austria AG has a domestic market share of about 14% of total lending. The group also has successful franchises in several CEE countries, particularly Croatia, Bulgaria, and Russia. UniCredit's subsidiaries in these countries have sound market shares in most of the segments in which they operate. This translates into well-balanced revenue diversification, with approximately 50% from Italy, 20% from Germany, and the remainder from Austria and other countries in Central and Eastern Europe, as of December 2019.

Table 2

Unicredit Group: Achievements Versus Targets Since 2015

	2015	**2019 Target**	**2019 A**	**Q1 2020 A**
Gross NPE (Bil. €)	78	44.3	25.3	24.9
CET 1 ratio	10.40%	>12.5%	13.22%	13.44%
Cost to income ratio	>60%	<52%	52.70%	N.M.
Net NPE/TAC	82.70%	N/A	12%	<12%
RAC ratio before diversification	5.70%	N/A	8%	N/A

Note: N.M.--Not meaningful. N/A--Not applicable. E--Estimate. TAC--Total adjusted capital. RAC--Risk-adjusted capital. A--Actual. NPE--Nonperforming exposure. Source: S&P Global Ratings calculations based on bank's annual and interim diclosures.

In a deteriorating economic environment, we expect UniCredit to benefit from its successful efforts in recent years in making the group simpler, more cost efficient, better capitalized, and less risky. As such, we consider the group's past decision to dispose of some of its most valuable assets to be coherent with its capital optimization plan and focus on core businesses. Most recently, the decision to exit from Turkey, while costly, appeared effective.

Given current context, such decisions will likely pay-off and the accumulated capital buffers and enhanced efficiency and risk management put Unicredit in a better position today than before the prior recessions.

More structurally, though, we think the sale of valuable assets such as Fineco Bank, Pioneer, or Pekao reduced UniCredit's business diversification, compared with most large international peers. We anticipate that Unicredit will continue to accurately allocate its capital to countries, businesses, or segments that could provide adequate return.

Table 3

UniCredit SpA--Business Position

	--Year ended Dec. 31--				
(%)	**2019**	**2018**	**2017**	**2016**	**2015**
Loan market share in country of domicile	N/A	N/A	N/A	N/A	12.5
Total revenues from business line (currency in millions)	19,250.0	20,973.0	19,452.0	19,068.0	22,398.0
Commercial & retail banking/total revenues from business line	96.7	93.3	95.5	98.7	99.0
Trading and sales income/total revenues from business line	5.3	4.7	5.4	5.8	4.4
Asset management/total revenues from business line	N/A	3.0	3.0	2.9	2.4
Other revenues/total revenues from business line	(1.9)	(1.0)	(3.9)	(7.4)	(5.8)
Investment banking/total revenues from business line	5.3	4.7	5.4	5.8	4.4
Return on average common equity	6.7	7.8	12.8	(29.8)	3.8

N/A--Not applicable.

Capital and earnings: Management committed to maintaining sound capital buffers.

We appreciate Unicredit reiterated its goal to maintain at least a 200bps-250bps common equity Tier 1 MDA buffer over the next three years, amid a significantly tougher economic and operating context. After progress in recent years, UniCredit is starting from a strong base, and the bank's CET 1 MDA buffers stood at 436bps in Q12020. Over time, we anticipate achieving this target will require UniCredit to maintain a prudent dividend policy and likely to hold off on its plan to materially increase shareholders remuneration.

In our base-case scenario, we estimate the bank's RAC to remain comfortably at 7% in the next two years, in line with 7.5%-8% we estimate as of December 2019.

In the above forecast, we are factoring in our view that:

- The group will be loss-making in 2020, mainly as a result of the €2.9 billion net one-offs related to the deconsolidation of Yapi in Turkey and restructuring charges in Italy the bank had already communicated to the market prior to the emergence of COVID-19;
- Revenue contracting by around 10%; and
- Credit losses likely doubling compared with 2019 figures.

In 2021, we expect profitability to recover to a relatively modest level, with underlying earnings between €2.5 billion–€3 billion. We assume no dividends in 2020 and roughly 50% pay-out in 2021.

We also assume corporate loans will increase over the next two years, to support the near term liquidity needs triggered by the COVID-19 crisis. The bank communicated that it is targeting to grant around €15 billion of new loans, with the guarantee provided by the government. This would reduce the capital absorption.

Our RAC calculation, however, is sensitive to potential changes of economic risks we could see in Italy, Germany, and Austria for which we currently see negative trends, and eventually to the rating of the Republic of Italy (BBB/Negative/A-2). We calculate the overall sensitivity to all those factors would reach up to 70bps-80bps of the projected RAC ratio.

Table 4

UniCredit SpA--Capital And Earnings

	--Year ended Dec. 31--				
(%)	**2019**	**2018**	**2017**	**2016**	**2015**
Tier 1 capital ratio	14.9	13.6	15.4	9.0	11.5
S&P Global Ratings' RAC ratio before diversification	N/A	7.2	7.5	4.4	5.8
S&P Global Ratings' RAC ratio after diversification	N/A	8.0	8.2	4.8	6.9
Adjusted common equity/total adjusted capital	84.7	85.1	85.5	84.8	89.2
Net interest income/operating revenues	56.7	54.0	53.1	56.7	53.2
Fee income/operating revenues	35.0	33.6	34.9	30.0	35.0
Market-sensitive income/operating revenues	8.5	6.2	8.7	9.9	7.3
Noninterest expenses/operating revenues	55.7	53.3	59.1	67.4	59.8
Preprovision operating income/average assets	0.9	1.1	0.9	0.7	1.1
Core earnings/average managed assets	0.4	0.7	0.5	(0.8)	0.5

N/A--Not applicable. RAC--Risk-adjusted capital.

Table 5

UniCredit SpA--Risk-Adjusted Capital Framework Data

(Mil. €)	**Exposure***	**Basel III RWA**	**Average Basel III RW(%)**	**S&P Global Ratings RWA**	**Average S&P Global Ratings RW (%)**
Credit risk					
Government & central banks	223,630.2	25,562.8	11.4	61,716.9	27.6
Of which regional governments and local authorities	26,481.0	737.2	2.8	10,038.0	37.9
Institutions and CCPs	62,812.5	13,856.5	22.1	27,144.0	43.2
Corporate	317,239.2	177,902.7	56.1	339,103.0	106.9
Retail	160,061.5	62,609.2	39.1	107,958.2	67.4
Of which mortgage	90,954.7	26,089.4	28.7	40,099.3	44.1
Securitization§	18,325.0	4,109.6	22.4	8,069.4	44.0
Other assets†	36,662.3	35,706.8	97.4	65,490.7	178.6
Total credit risk	818,730.7	319,747.6	39.1	609,482.1	74.4

Table 5

UniCredit SpA--Risk-Adjusted Capital Framework Data (cont.)

	Exposure	Basel III RWA	Average Basel II RW (%)	S&P Global Ratings RWA	% of S&P Global Ratings RWA
Credit valuation adjustment					
Total credit valuation adjustment	--	1,971.1	--	0.0	--
Market risk					
Equity in the banking book	5,876.7	0.0	0.0	50,611.5	861.2
Trading book market risk	--	10,068.8	--	15,159.5	--
Total market risk	--	10,068.8	--	65,771.0	--
Operational risk					
Total operational risk	--	29,505.9	--	45,316.3	--

	Exposure	Basel III RWA	Average Basel II RW (%)	S&P Global Ratings RWA	% of S&P Global Ratings RWA
Diversification adjustments					
RWA before diversification	--	370,180.1	--	720,569.5	100.0
Total Diversification/ Concentration Adjustments	--	--	--	(73,778.4)	(10.2)
RWA after diversification	--	370,180.1	--	646,791.0	89.8

	Tier 1 capital	Tier 1 ratio (%)	Total adjusted capital	S&P Global Ratings RAC ratio (%)
Capital ratio				
Capital ratio before adjustments	50,487.9	13.6	51,955.0	7.2
Capital ratio after adjustments‡	50,487.9	13.6	51,955.0	8.0

*Exposure at default. §Securitization Exposure includes the securitization tranches deducted from capital in the regulatory framework. †Exposure and S&P Global Ratings' risk-weighted assets for equity in the banking book include minority equity holdings in financial institutions. ‡Adjustments to Tier 1 ratio are additional regulatory requirements (e.g. transitional floor or Pillar 2 add-ons). RWA--Risk-weighted assets. RW--Risk weight. RAC--Risk-adjusted capital. Sources: Company data as of Dec. 31, 2018, S&P Global Ratings.

Risk position: The bank is better prepared to cope with economic recession.

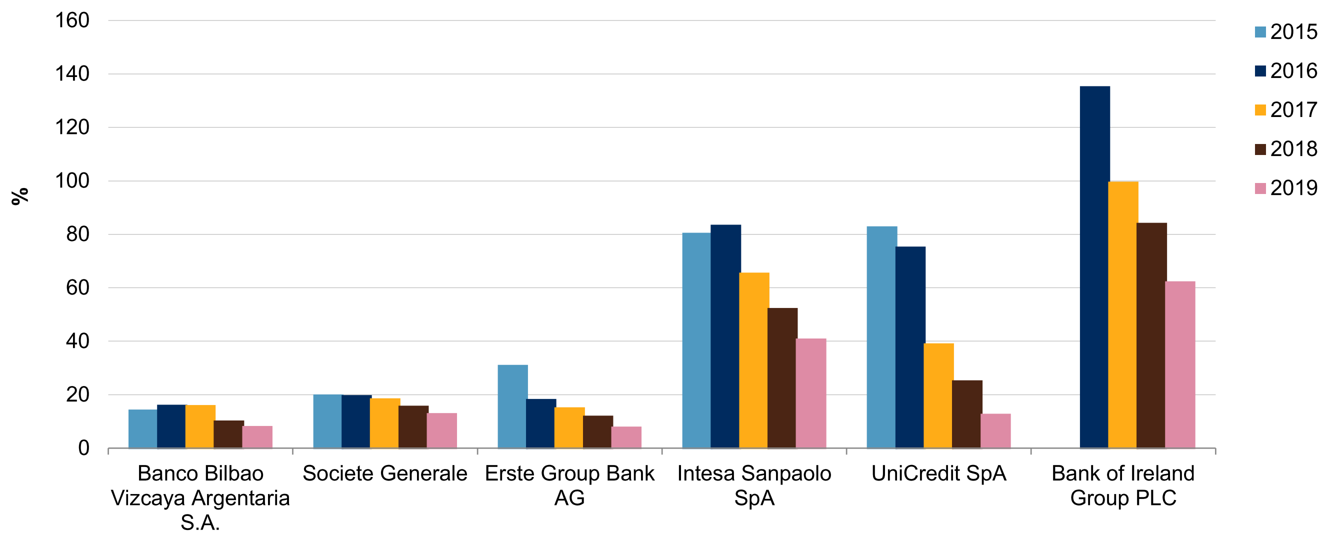
The sharp contraction we now see in Italy and in most EU countries the group operates in, will eventually test the resilience of UniCredit's credit quality, in our opinion.

We think the bank will definitely benefit from the effective efforts made in recent years to strengthen its risk management, improve the quality of new loans, and get rid of large legacy NPEs that emerged during the past recession. As of December 2019, the gross stock of NPEs amounted to €25 billion, or around 5% of customer loans, compared with €78 billion in 2014 (18% of loans).

Chart 1

Unicredit's Coverage Has Improved Over The Years

Net nonperforming exposures/total adjusted capital

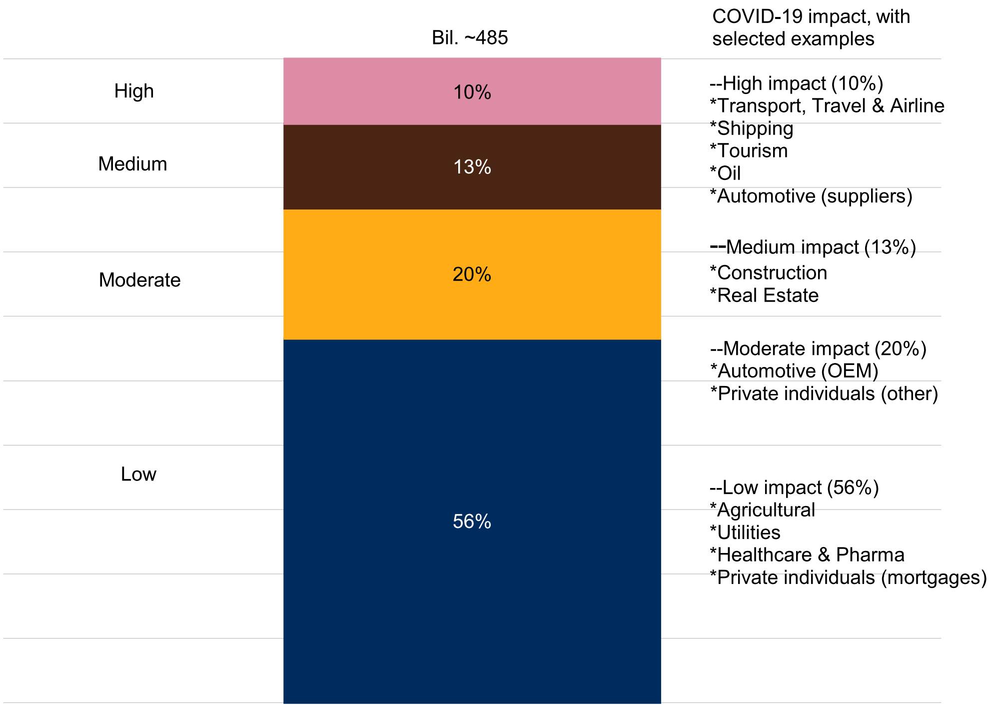


Source: S&P Global Ratings.

Despite the abovementioned progress, we expect NPEs to start rising at the end of 2020, and to continue in the first quarters of 2021. During its first quarter results presentation, Unicredit communicated it has already granted moratorium to loans corresponding to €28 billion (5% of total loans) and that about 10% of its loans are to sectors highly affected by the COVID-19 pandemic (Oil, Gas, shipping tourism).

Chart 2

Unicredit Group's Loan Book Breakdown
As of March 2020



Source: Unicredit Group presentation for the quarter ended March 31, 2020. S&P Global Ratings.

In our base-case scenario, we assume the deterioration will eventually be manageable for Unicredit and materially lower than the one experienced in the past downturn.

In our forecast, we anticipate cumulative credit losses in 2020 and 2021 of around 220bps-240bps, just above the initial guidance provided by the management of 100bps-120bps in 2020, and 70bps-90bps in 2021.

Downside risks remains, though, if the economic contraction were to become deeper and longer than we anticipate or the economic recovery delayed. While we expect UniCredit to be overall more resilient in this downturn than most Italian banks, we think that its larger presence in Italy makes the bank's asset quality more vulnerable compared with most other international peers.

Compared with recent times, UniCredit's decision to reduce its stake in Yapi Kredi to 20% from 45% in Turkey will pay-off in the current environment, as it reduced further downside risks to the group risk position.

Other meaningful exposures to high economic risk countries include Russia and Croatia. The bank's total exposure to Russia remains contained and accounts for less than 3% of the group's consolidated loan book. We also believe that the Russian unit, UniCredit ZAO, will remain one of the best performing banks in Russia.

Table 6

UniCredit SpA--Risk Position

	--Year ended Dec. 31--				
(%)	**2019**	**2018**	**2017**	**2016**	**2015**
Growth in customer loans	(5.2)	3.5	(3.5)	(4.4)	(0.0)
Total diversification adjustment/S&P Global Ratings' RWA before diversification	N/A	(10.2)	(9.1)	(9.1)	(16.5)
Total managed assets/adjusted common equity (x)	17.7	18.8	18.3	28.0	20.6
New loan loss provisions/average customer loans	0.7	0.6	0.6	2.6	0.8
Net charge-offs/average customer loans	(0.1)	(0.5)	3.0	(0.7)	1.0
Gross nonperforming assets/customer loans + other real estate owned	6.4	8.6	11.1	16.5	16.9
Loan loss reserves/gross nonperforming assets	74.7	67.6	58.6	64.7	53.4

N/A--Not applicable. RWA--Risk-weighted assets.

Funding and liquidity: Well positioned to withstand the effect of market turbulence on Italian banks' access to funding sources.

We expect UniCredit to maintain a well-balanced funding profile, broadly in line with its domestic and international peers. This stems from its sizable core customer deposits, covering over 60% of UniCredit's total funding as of December 2019. Retail funding growth and asset deleveraging support UniCredit's efforts to progressively reduce its reliance on wholesale funding, in our view.

We also think that UniCredit's funding is mainly oriented toward long-term financing instruments, thereby reducing refinancing risk. We estimate the bank's stable funding ratio was about 111% as of Dec. 31, 2019. This is in line with most of its international peers. Moreover, UniCredit has been able to issue covered bonds and senior unsecured notes through group entities in Italy, Germany, and Austria, even when such market access was unavailable to many of its peers. It was the first Italian bank to issue senior non-preferred bonds in January 2018, and managed to issue subordinated bonds in the wholesale market even during the most turbulent period in 2018.

In our view, this ability constitutes a strong element of UniCredit's superior market access compared with other Italian banks. That said, persistent market turbulence linked to concerns about the Republic of Italy's creditworthiness could have repercussions for UniCredit's funding strategy and most likely on its cost of financing. Still, we observe that Unicredit has already completed most of its funding plan for the year 2020.

In order to optimize its cost of funding and reduce the interconnection with Italy's perceived creditworthiness, UniCredit announced that it will materially reduce intragroup funding exposures.

The group's reliance on short-term wholesale financing will remain generally manageable, and we expect it to maintain sufficient liquidity if needed. UniCredit's unencumbered eligible assets with central banks, plus cash and deposits, net of regulatory deductions, stood at about €181 billion at February 2020, providing the bank with a significant cushion. We estimate broad liquid assets to short-term wholesale funding was about 1.4x as of Dec. 31, 2019.

In addition, UniCredit took advantage of the attractive pricing conditions offered by the ECB's targeted long-term refinancing operations (TLTRO II), and increased its use up to €51.2 billion as of December 2019. We do not consider the use of ECB funding TLTRO II as structural and we expect that such reliance will generally remain manageable, and that the bank will manage it carefully in the future to avoid a large maturity concentration.

Table 7

UniCredit SpA--Funding And Liquidity					
	--Year ended Dec. 31--				
(%)	2019	2018	2017	2016	2015
Core deposits/funding base	60.4	61.7	60.6	60.8	60.7
Customer loans (net)/customer deposits	96.0	100.2	97.9	98.3	102.2
Long-term funding ratio	74.6	76.2	76.4	73.1	72.4
Stable funding ratio	105.6	106.9	111.7	93.5	98.2
Short-term wholesale funding/funding base	27.4	25.6	25.5	28.4	29.5
Broad liquid assets/short-term wholesale funding (x)	1.3	1.4	1.5	1.2	1.1
Net broad liquid assets/short-term customer deposits	16.9	19.4	23.5	8.6	8.0
Short-term wholesale funding/total wholesale funding	67.2	65.1	62.8	71.2	73.7
Narrow liquid assets/3-month wholesale funding (x)	N/A	1.6	2.2	1.7	1.5

N/A--Not applicable.

Environmental, Social, and Governance (ESG)

We believe ESG factors influence UniCredit's credit quality similarly to its industry and local peers. As a large commercial bank operating in multiple jurisdictions, UniCredit has robust control practices, unified risk culture, adequate underwriting, and know-your-customer practices in all those countries. Since the appointment of Jean-Pierre Mustier as CEO in 2016, management has focused on making the bank's structure simpler, less risky, better capitalized, and more transparent. We believe UniCredit follows a clearer strategy and vision among the different group entities. The bank's well-balanced board composition and diversity looks to all the stakeholders' interest. Nevertheless, like other large and diversified banks, UniCredit has been, and remains, exposed to a wide range of legal and non-financial risks, as evidenced by UniCredit and its German and Austrian subsidiaries paying a $1.3 billion fine to U.S. authorities related to the violation of U.S. sanctions on Iran, for prohibited operations concluded from 2002-2011. We are not aware of any large-scale pending litigation or compliance-related issues, though. Environment and social factors do not affect credit quality differently from industry peers. The group is exposed to transition risks, in particular through its exposure to the car industry (in Italy and Germany). Regarding social risk, we note UniCredit has undertaken sizable staff reduction in recent years, and this is likely to continue over the next years as part of its efficiency enhancment plan. We believe the layoffs have been handled carefully in UniCredit's main countries of operations, primarily in agreement with local unions and predominantly through participation to voluntary early retirement scheme.

Support: No uplift for additional loss-absorbing capital (ALAC).

In our ALAC calculation, we include capital instruments issued by UniCredit that have the capacity to absorb losses without triggering a default on senior obligations; namely, subordinated debt and hybrid instruments with minimal equity content, which we exclude from our calculation of total adjusted capital (TAC). ALAC also includes hybrids and common equity that are already counted in TAC up to an amount whereby together they exceed the minimum needed to maintain a RAC ratio consistent with our assessment of a bank's capital and earnings (which for UniCredit is 7%).

Our ALAC estimate is likely to remain between 200bps-300bps over the next three years, which is well below the 500bps threshold we set for a higher potential ICR.

Government support: High systemic importance in a country where we assess government support for banks as uncertain.

We view UniCredit as having high systemic importance for Italy. This is combined with our assessment of the Italian government's tendency to support its banking system as uncertain. As a result, systemic banks including UniCredit are no longer eligible for uplift for possible future extraordinary support from the Italian government.

Additional rating factors: UniCredit could withstand a hypothetical sovereign stress scenario.

We consider that the bank's €18 billion of subordinated instruments (excluding AT1), combined with the clean-up of its domestic balance sheet, enhanced its ability to potentially withstand a sovereign distress scenario. In addition, UniCredit has largely reduced its Italian Government securities to €42 billion in 2019, compared with €58 billion the year before, and remains committed to the market and to lowering the proportion of Italian govies on tangible equity in the quarters to come, primarily through rolling over some of its exposures. We anticipate that the exposure to Italian government bonds will decline further in the coming years.

As one of the global systemically important financial institutions (SIFIs), UniCredit is geographically diversified outside of Italy--which accounts for about 45% of its total exposures--and is subject to more advanced resolution planning than many of its peers, in our view. As a global SIFI, UniCredit has been building up buffers of subordinated liabilities to comply with TLAC. These issuances, as well as the bank's enhanced capital base, provide more cushion to cover the potential high losses from a hypothetical scenario of sovereign default.

In our base-case scenario, a sovereign default would most likely trigger the resolution of UniCredit, the Italian parent company. We expect that the conversion of the loss-absorbing subordinated instruments to equity would be sufficient to adequately recapitalize UniCredit. Still, we expect that the authorities would require the group to restore its consolidated minimum capital requirement as well.

Hybrid instruments

We currently rate UniCredit's hybrid instruments by applying our standard notching from the group's SACP. This means we currently rate the bank's senior non-preferred notes 'BBB-', by applying one-notch of subordination compared to the preferred senior unsecured liabilities. As we currently do for all the senior non-preferred notes issued by banks operating in the eurozone, we assume that a write-down of those instruments would apply only in a bail-in scenario.

This differs from other subordinated liabilities such as non-deferrable Tier II notes issued by UniCredit. We rate them 'BB+' as we also apply one additional notch to reflect the risk that regulators may force the write-down/conversion to equity of those instruments even outside a resolution/liquidation scenario.

In addition, we rate UniCredit's Upper Tier II instrument 'BB' to reflect an additional notch for subordination risk.

Resolution counterparty ratings (RCRs)

We set the RCR on Unicredit one notch above our long-term issuer credit rating on the entity. Our RCR on Unicredit SpA is currently one-notch above the Republic of Italy Sovereign Rating reflecting the large buffer of instruments, including senior obligation, that would protect the RCRs liabiblities in the hypothetical scenario of stress linked to a Sovereign default.

Related Criteria

- Criteria | Financial Institutions | Banks: Commercial Paper I: Banks, March 23, 2004.
- Criteria | Financial Institutions | Banks: Bank Rating Methodology And Assumptions: Additional Loss-Absorbing Capacity, April 27, 2015.
- General Criteria: Guarantee Criteria, October 21, 2016.
- Criteria | Financial Institutions | General: Risk-Adjusted Capital Framework Methodology, July 20, 2017.
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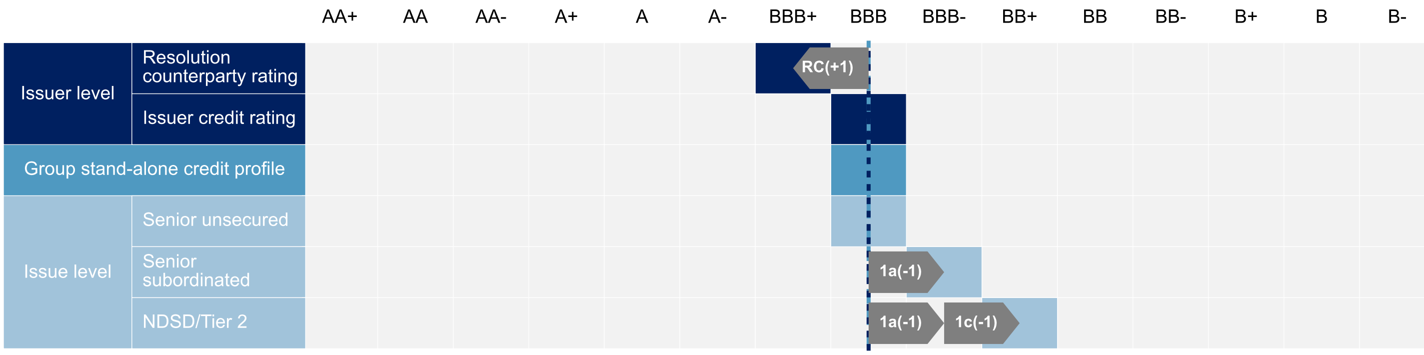
UniCredit SpA: Notching



Key to notching

----- Group stand-alone credit profile

------ Issuer credit rating

RC Resolution counterpartyliabilities (senior secured debt)

1a Contractual subordination

1c Mandatory contingent capital clause or equivalent

Note: The number-letter labels in the table above are in reference to the notching steps we apply to hybrid capital instruments, as detailed in table 3 of our "Hybrid Capital: Methodology And Assumptions" criteria, published on July 1, 2019.
NDSD--Non-deferrable subordinated debt.

Anchor Matrix

Industry Risk	Economic Risk									
	1	2	3	**4**	5	6	7	8	9	10
1	a	a	a-	bbb+	bbb+	bbb	-	-	-	-
2	a	a-	a-	bbb+	bbb	bbb	bbb-	-	-	-
3	a-	a-	bbb+	bbb+	bbb	bbb-	bbb-	bb+	-	-
4	bbb+	bbb+	bbb+	bbb	bbb	bbb-	bb+	bb	bb	-
5	bbb+	bbb	bbb	**bbb**	bbb-	bbb-	bb+	bb	bb-	b+
6	bbb	bbb	bbb-	bbb-	bbb-	bb+	bb	bb	bb-	b+
7	-	bbb-	bbb-	bb+	bb+	bb	bb	bb-	b+	b+
8	-	-	bb+	bb	bb	bb	bb-	bb-	b+	b
9	-	-	-	bb	bb-	bb-	b+	b+	b+	b
10	-	-	-	-	b+	b+	b+	b	b	b-

Ratings Detail (As Of June 10, 2020)*

UniCredit SpA	
Issuer Credit Rating	BBB/Negative/A-2
Resolution Counterparty Rating	BBB+/--/A-2
Certificate Of Deposit	
Foreign Currency	A-2

Ratings Detail (As Of June 10, 2020)*(cont.)	
Commercial Paper	
Local Currency	A-2
Junior Subordinated	BB
Junior Subordinated	BB-
Senior Secured	AA-/Negative
Senior Subordinated	BBB-
Senior Unsecured	BBB
Subordinated	BB+
Issuer Credit Ratings History	
29-Apr-2020	BBB/Negative/A-2
15-Jul-2019	BBB/Stable/A-2
30-Oct-2018	BBB/Negative/A-2
31-Oct-2017	BBB/Stable/A-2
Sovereign Rating	
Italy	BBB/Negative/A-2
Related Entities	
BA-CA Finance (Cayman) (2) Ltd.	
Issuer Credit Rating	BBB+/Negative/A-2
Junior Subordinated	BB
BA-CA Finance (Cayman) Ltd.	
Issuer Credit Rating	BBB+/Negative/A-2
Junior Subordinated	BB
HVB Capital LLC I	
Junior Subordinated	BB
HVB Capital LLC II	
Junior Subordinated	BB
HVB Capital LLC III	
Junior Subordinated	BB
HVB Funding Trust I	
Junior Subordinated	BB
HVB Funding Trust II	
Junior Subordinated	BB
HVB Funding Trust III	
Junior Subordinated	BB
UniCredit Bank AG	
Issuer Credit Rating	BBB+/Negative/A-2
Resolution Counterparty Rating	A-/--/A-2
Senior Subordinated	BBB
Senior Unsecured	BBB+
UniCredit Bank AO	
Issuer Credit Rating	BBB-/Negative/A-3
UniCredit Bank Austria AG	
Issuer Credit Rating	BBB+/Negative/A-2

Ratings Detail (As Of June 10, 2020)*(cont.)	
Resolution Counterparty Rating	A-/--/A-2
Senior Unsecured	BBB+
Short-Term Debt	A-2
Subordinated	BBB-
Zagrebacka banka dd	
Issuer Credit Rating	BBB-/Negative/--
Resolution Counterparty Rating	BBB-/--/--

*Unless otherwise noted, all ratings in this report are global scale ratings. S&P Global Ratings' credit ratings on the global scale are comparable across countries. S&P Global Ratings' credit ratings on a national scale are relative to obligors or obligations within that specific country. Issue and debt ratings could include debt guaranteed by another entity, and rated debt that an entity guarantees.