

## CREDIT OPINION

23 December 2022

Update



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### RATINGS

#### Caja Rural de Navarra

Domicile	Pamplona, Spain
Long Term CRR	A3
Type	LT Counterparty Risk Rating - Dom Curr
Outlook	Not Assigned
Long Term Debt	Not Assigned
Long Term Deposit	Baa1
Type	LT Bank Deposits - Dom Curr
Outlook	Stable

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.

### Contacts

Maria Vinuela +34.91.768.8237  
VP-Senior Analyst  
maria.vinuela@moodys.com

Alberto Postigo +34.91.768.8230  
VP-Sr Credit Officer  
alberto.postigoperez@moodys.com

Maria Cabanyes +34.91.768.8214  
Senior Vice President  
maria.cabanyes@moodys.com

### CLIENT SERVICES

Americas 1-212-553-1653  
Asia Pacific 852-3551-3077  
Japan 81-3-5408-4100  
EMEA 44-20-7772-5454

## Caja Rural de Navarra

Update following rating update

### Summary

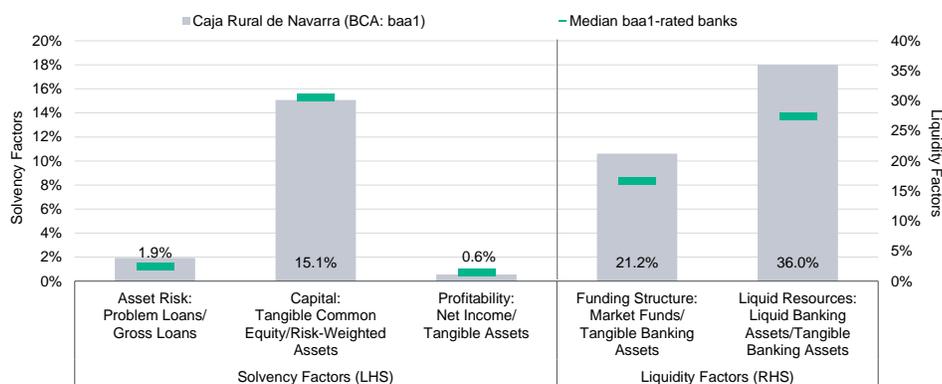
On 21 December 2022, we affirmed [Caja Rural de Navarra's \(CRN\)](#) deposit ratings at Baa1/Prime-2.

CRN's deposit ratings reflect the bank's Baseline Credit Assessment (BCA) of baa1; a high probability of affiliate support from the entities integrated into the Institutional Protection Scheme (IPS), which, nevertheless, translates into no uplift from CRN's BCA and consequently into an Adjusted BCA of baa1; and the result of our Advanced Loss Given Failure (LGF) analysis, which does not translate into any rating uplift. CRN's Counterparty Risk (CR) Assessment is A3(cr)/Prime-2(cr) and its Counterparty Risk Ratings (CRRs) are A3/Prime-2.

CRN's BCA of baa1 reflects the bank's sound financial fundamentals, namely, its strong asset-quality performance, sound capitalisation, stable retail deposit base and low reliance on wholesale funding. The bank's BCA also reflects its modest profitability levels, albeit stronger than that of its domestic peers.

Exhibit 1

### Rating Scorecard - Key financial ratios



Source: Moody's Financial Metrics

## Credit strengths

- » Stronger asset-quality indicators than the system average
- » Sound solvency levels
- » Higher revenue as a result of the increasing interest rates will improve bottom-line profitability
- » Low reliance on market funding, most of which is secured

## Credit challenges

- » Moderate increase in the inflow of new nonperforming loans (NPLs) because of more difficult macroeconomic conditions
- » Lower business levels and higher operating expenses will partially offset ample benefits from higher interest rates
- » Modest efficiency levels.

## Outlook

The stable outlook on CRN's long-term deposit ratings reflects our view that the expected performance of the bank's financial fundamentals over the next 12-18 months is already captured in the bank's current ratings. Moody's anticipates a moderate increase in problem loans amid the current unsettled operating environment and inflationary pressures on households' purchasing power and corporate margins. However, under Moody's base case scenario, such deterioration is unlikely to materially weaken CRN's credit profile.

## Factors that could lead to an upgrade

CRN's BCA could be upgraded if the bank's asset quality indicators improve further, along with a sustainable improvement in the bank's recurring earnings. However, any upward pressure on CRN's BCA is unlikely to materialise as long as the Spanish government bond rating remains at Baa1, as a bank's BCA will not typically exceed the sovereign rating under our methodology without any factor that reduces the dependency between the creditworthiness of the bank and the sovereign. Upward pressure on CRN's BCA and Adjusted BCA is also dependent on a strengthening of the creditworthiness of the IPS group.

CRN's deposit ratings could be upgraded as a result of changes in its liability structure, which indicate a lower loss given failure to be faced by deposits.

## Factors that could lead to a downgrade

The bank's BCA could be downgraded if the bank's asset quality and profitability worsen beyond our current expectations. Negative pressure on the bank's BCA could also result from a downgrade of the Spanish sovereign rating.

Any change in the BCA would also likely affect the deposit ratings because they are linked to the standalone BCA. CRN's deposit ratings could also change as a result of alterations to the bank's liability structure, which would indicate a higher loss given failure to be faced by deposits.

This publication does not announce a credit rating action. For any credit ratings referenced in this publication, please see the issuer/deal page on <https://ratings.moody's.com> for the most updated credit rating action information and rating history.

## Key indicators

Exhibit 2

### Caja Rural de Navarra (Consolidated Financials) [1]

	12-21 <sup>2</sup>	12-20 <sup>2</sup>	12-19 <sup>2</sup>	12-18 <sup>2</sup>	12-17 <sup>2</sup>	CAGR/Avg. <sup>3</sup>
Total Assets (EUR Million)	16,333.1	15,849.8	13,133.1	12,202.9	11,726.2	8.6 <sup>4</sup>
Total Assets (USD Million)	18,507.2	19,393.1	14,741.9	13,949.6	14,080.8	7.1 <sup>4</sup>
Tangible Common Equity (EUR Million)	1,399.3	1,303.1	1,212.0	1,110.7	1,036.9	7.8 <sup>4</sup>
Tangible Common Equity (USD Million)	1,585.5	1,594.4	1,360.4	1,269.7	1,245.1	6.2 <sup>4</sup>
Problem Loans / Gross Loans (%)	1.9	2.0	2.0	1.8	2.0	1.9 <sup>5</sup>
Tangible Common Equity / Risk Weighted Assets (%)	15.1	15.0	14.2	14.0	13.4	14.3 <sup>6</sup>
Problem Loans / (Tangible Common Equity + Loan Loss Reserve) (%)	11.1	11.7	12.1	11.2	12.8	11.8 <sup>5</sup>
Net Interest Margin (%)	0.9	1.0	1.2	1.2	1.3	1.1 <sup>5</sup>
PPI / Average RWA (%)	1.4	1.4	1.5	1.4	1.6	1.5 <sup>6</sup>
Net Income / Tangible Assets (%)	0.6	0.5	0.8	0.8	0.8	0.7 <sup>5</sup>
Cost / Income Ratio (%)	57.4	58.3	57.4	60.4	56.3	58.0 <sup>5</sup>
Market Funds / Tangible Banking Assets (%)	21.2	20.3	15.7	16.2	16.9	18.1 <sup>5</sup>
Liquid Banking Assets / Tangible Banking Assets (%)	36.0	37.9	29.6	26.9	31.7	32.4 <sup>5</sup>
Gross Loans / Due to Customers (%)	94.1	88.1	95.1	99.1	99.6	95.2 <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] May include rounding differences because of the scale of reported amounts. [4] Compound annual growth rate (%) based on the periods for the latest accounting regime. [5] Simple average of periods for the latest accounting regime. [6] Simple average of Basel III periods.

Sources: Moody's Investors Service and company filings

## Profile

With total assets of €16.7 billion as of end-June 2022, Caja Rural de Navarra (CRN) is the second-largest rural cooperative bank in Spain and the first of the Spanish Rural Cooperatives Association (Asociacion Espanola de Cajas Rurales, AECR), composed of CRN and 29 other rural cooperatives.

CRN is primarily based in Navarre. The bank also operates as the only rural credit cooperative in the neighbouring regions of the Basque Country and La Rioja. With a reported market shares of 28.1% in lending and 29.9% in deposits as of the end of December 2021 (latest available data), the bank is ranked second in Navarre, behind [CaixaBank, S.A.](#) (CaixaBank, A3/Baa1 stable, baa3)<sup>1</sup>. Despite its small size, CRN has a strong brand recognition and market position in its home region.

In March 2018, CRN integrated into an IPS, together with the 28 other Spanish rural cooperatives under the AECR and Banco Cooperativo Español, S.A. This IPS is a contractual scheme that ensures support through recourse to a private-sector fund, to which members have to contribute according to the terms and conditions established by a contractual agreement. This private fund will be an effective resource to assist IPS members in times of difficulty and before any resolution or liquidation, with the objective of preserving the financial stability of the IPS members and improving their risk profile.

Members of the IPS, including CRN, continue to be regulated on an individual basis, although they are required to publish consolidated accounts for the group.

This IPS entails some regulatory privileges for these entities, in particular capital relief on cross-sector lending and stakeholdings; higher permissible single-borrower exposures, if these exposures are to fellow members of the group; and lower contributions to the Deposit Guarantee Fund.

## Detailed credit considerations

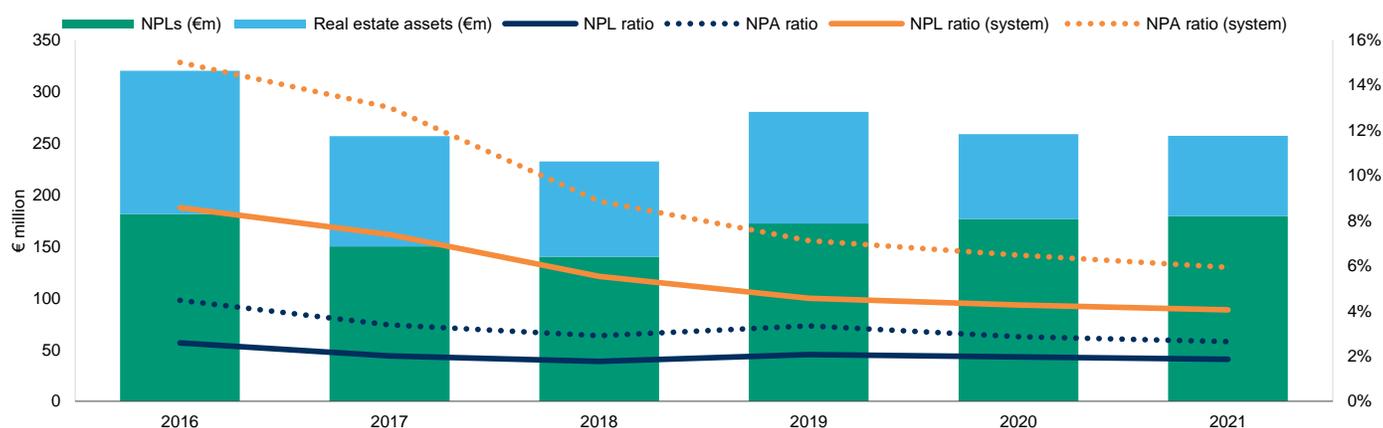
### Stronger asset-quality indicators than the system average

CRN's assigned Asset Risk score of a3 incorporates the bank's very low level of nonperforming assets (NPA; defined as nonperforming loans (NPLs) plus real estate assets) relative to the banking system, as well as our expectation that asset quality will deteriorate moderately as rising interest rates will make loans more costly, which combined with soaring inflation will undermine the repayment capacity of domestic businesses and households.

CRN's asset-quality indicators have historically performed better than the Spanish banking system average because of the bank's more prudent risk management, with a relatively low exposure to the real estate sector and its activities being limited to its home territories. As of end-June 2022, the bank reported an NPL ratio of 2.0%, broadly in line with the 1.9% reported by year-end 2021, while the ratio for the banking system was 3.6%<sup>2</sup> as of the same date. In addition to NPLs, CRN has a low amount of real estate assets repossessed. If these assets are added to the bank's NPLs, the NPA ratio would be 2.6% as of year-end 2021 (latest available data), below the 2.9% reported a year earlier and still comparing very favorably with the 5.9%<sup>3</sup> average for its domestic peers as of the same date.

Exhibit 3

### CRN's asset-risk indicators have historically outperformed system average



Source: CRN and Moody's Investors Service

CRN booked loan-loss provisions amounting to €14 million in 2021. As a result, the bank's cost of risk stood at 15 basis points (bps). This resulted in a mild increase of the bank's coverage ratio (measured as loan-loss reserves as a percentage of NPLs) to 119% as of the end of December 2021, up from 116% a year earlier and above the system average of 70% for the same period.

### CRN displays sound solvency levels

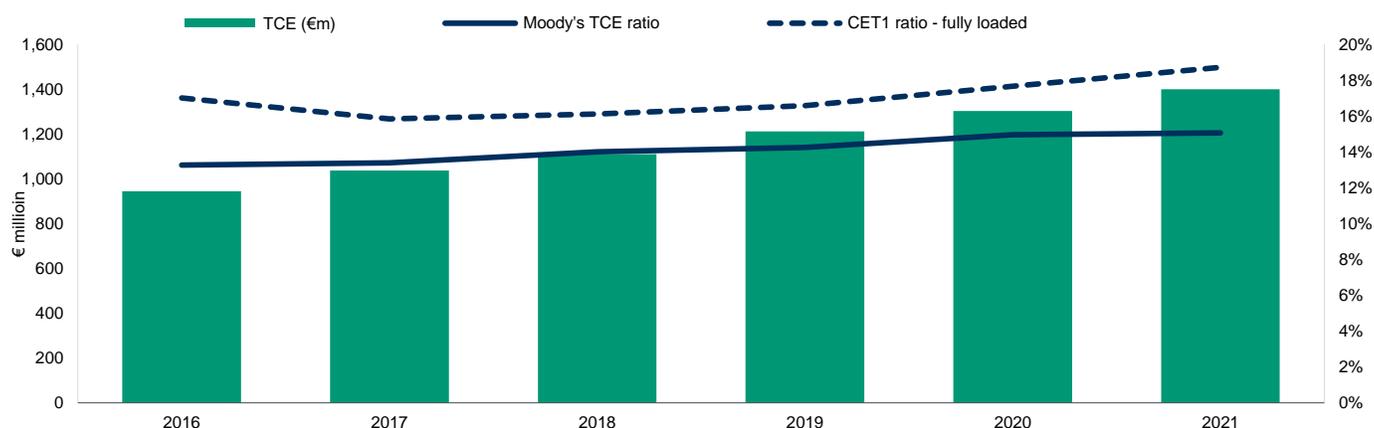
CRN's assigned Capital score of a2 reflects our assessment that capitalisation is a relative strength for the bank. As of year-end 2021, CRN's tangible common equity/risk-weighted assets was 15.1%, broadly in line with a year earlier (latest available data). The bank's TCE ratio was broadly unchanged in 2021, as the increase in capital resulting from the profit retention was offset by the increase in risk weighted assets as adjusted by Moody's.

CRN's capital is mainly composed of retained earnings and contributions from cooperative members on which it pays dividends. In line with the Spanish legislation, CRN allocates a part of its net profit to a welfare fund, although it retains most of the profit to support capital generation and fund future growth, which translates into the bank's higher-than-average capital ratios.

In terms of regulatory capital ratios, CRN reported a fully loaded Common Equity Tier 1 capital ratio of 18.7% as of year-end 2021, compared to 18.3% a year earlier and above the European Union (EU) average of 15.8%<sup>4</sup> as of the same date. Our more conservative capital assessment relative to regulators' capital ratios is primarily explained by the more conservative risk weighting that we apply to the sovereign exposures (at 50% for Spain's sovereign bonds) compared with regulators' risk weighting of 0%.<sup>5</sup>

Exhibit 4

## CRN's capital levels have improved over recent years from already very high levels



Source: CRN and Moody's Investors Service

## Higher revenues as a result of rising interest rates will improve profitability

We assign a Profitability score of baa3 to CRN. This reflects our assessment that the bank's profitability will benefit from the repricing of the loan book (the bulk of it at variable rates) to the ECB's higher interest rates against the profitability headwinds it will be facing in 2023, mainly stemming from lower activity levels and increased operating costs. CRN reported a net income/tangible assets of 0.8% at end-June 2022.

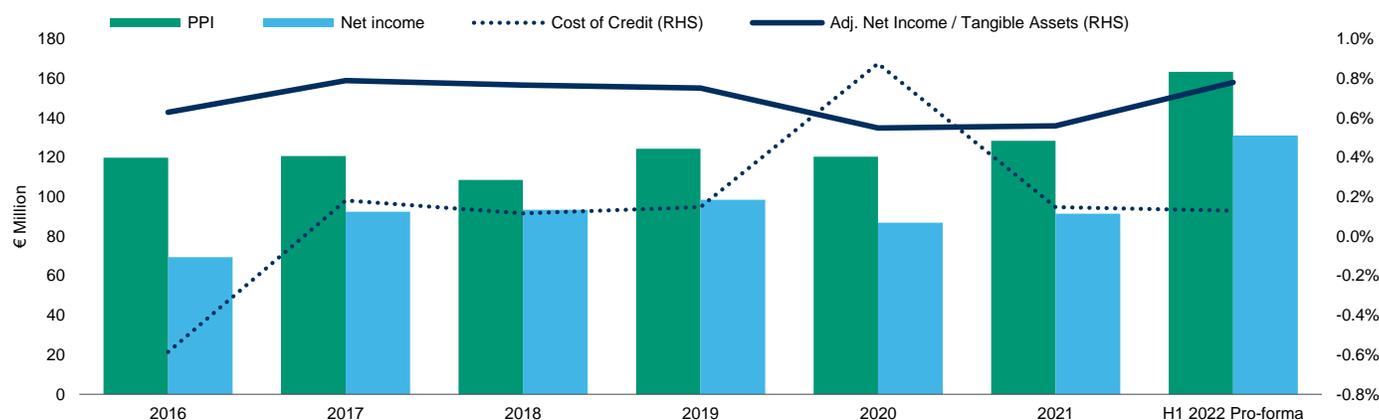
CRN's reported a net income of €66 million at end-June 2022, up from €49 million a year earlier. This was mainly the result of a significant 23% increase in pre-provision income (PPI), while provisions stood at similar levels.

In June 2022 the bank reported a PPI of €82 million, up from €66 million a year earlier. This was due to 15% higher operating income that more than offset the 10% increase in operating expenses. The bank's net interest income decreased by 2%, while its fee and commission income increased 17% and other results by 40%, which mainly explained the significant increase in operating income.

CRN's cost-to-income ratio improved to 54% at end-June 2022, from 57% a year earlier, weaker than the system average of 51%<sup>6</sup>, reflecting the bank's modest efficiency levels.

Exhibit 5

## CRN's top-line earnings have been fairly resilient over recent years



Source: CRN and Moody's Investors Service

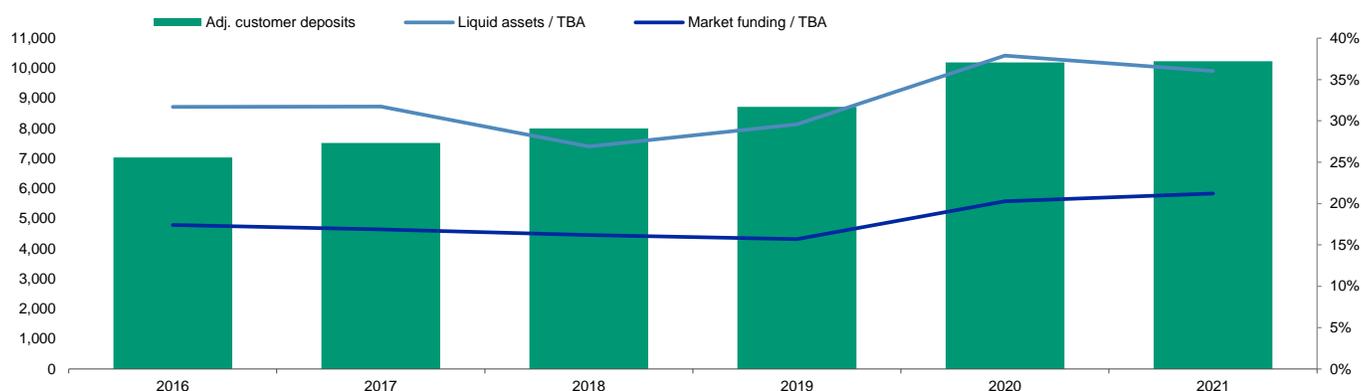
### Low reliance on market funding, most of which is secured

CRN's market funds ratio stood at 21.2% as of the end of December 2021 (latest available data), equivalent to a score of baa3. We assess CRN's Funding structure score at baa2, one notch above the Macro-adjusted score, as we make a positive adjustment to CRN's market funds/tangible assets ratio by deducting a portion of the ECB's targeted longer-term refinancing operations (TLTRO) III funds from market funds. These funds were solely used to take advantage of the favourable terms offered by the ECB and the part of those are deposited back at the central bank rather than being used for lending or investment purposes, thereby temporarily inflating CRN's market funds.

CRN is predominantly retail funded. As of year-end 2021, deposits accounted for around 70% of the bank's total funding, representing 94% of its gross loans (latest available data). The bank's regional identity adds a component of stability to its retail funding base, which has consistently grown over the years.

Most of CRN's wholesale funding is composed of covered bonds (€1.7 billion) and ECB funding (€2.1 billion), all secured funding sources. In addition, CRN has tapped wholesale markets through a number of sustainable financing instruments, which form part of its sustainability framework (three €500 million sustainable mortgage covered bonds [November 2016, May 2018, February 2022] and a €100 million senior sustainable bond in June 2017).

Exhibit 6  
**Growing deposit base and low reliance on wholesale funding**



Source: CRN and Moody's Investors Service

## ESG considerations

### Caja Rural de Navarra's ESG Credit Impact Score is Neutral-to-Low CIS-2

Exhibit 7  
**ESG Credit Impact Score**

**CIS-2**

**Neutral-to-Low**



For an issuer scored CIS-2 (Neutral-to-Low), its ESG attributes are overall considered as having a neutral-to-low impact on the current rating; i.e., the overall influence of these attributes on the rating is non-material.

Source: Moody's Investors Service

Caja Rural de Navarra's ESG Credit Impact Score is neutral-to-low (**CIS-2**), reflecting the limited credit impact of environmental and social factors on the rating to date, and neutral-to-low governance risks.

Exhibit 8

#### ESG Issuer Profile Scores



Source: Moody's Investors Service

#### Environmental

Caja Rural de Navarra faces moderate environmental risks primarily because of its portfolio exposure to carbon transition risk as a diversified bank. In line with its peers, the bank is exposed to mounting business risks and stakeholder pressure to meet broader carbon transition goals. In response, Caja Rural de Navarra is developing its climate risk and portfolio management capabilities and is actively transitioning its lending portfolios to achieve carbon neutrality targets.

#### Social

Caja Rural de Navarra is exposed to high industrywide social risks particularly related to customer relations risk and associated regulatory and litigation risks, requiring high compliance standards. These risks are mitigated by Caja Rural de Navarra's developed policies and procedures. Caja Rural de Navarra's high cyber and personal data risks are mitigated by the bank's sound IT framework.

#### Governance

Caja Rural de Navarra faces neutral-to-low governance risks, with a corporate governance framework in line with industry best practices. The bank applies conservative financial policies and has a strong track record of achieving its strategic and financial targets, supported by an outstanding risk management function. As a rural cooperative, the bank's capital is composed of retained earnings and contributions from customers which show no concentration.

ESG Issuer Profile Scores and Credit Impact Scores for the rated entity/transaction are available on Moody's.com. In order to view the latest scores, please click [here](#) to go to the landing page for the entity/transaction on MDC and view the ESG Scores section.

### Support and structural considerations

#### Affiliate support

Our cross-sector support assessment is based on CRN's integration into the IPS, which includes the 30 rural cooperatives associated under the AEER and BCE, and results in a contractually binding support arrangement among member banks. Cross-sector support materially reduces default risk, as it would be available to stabilize a distressed member bank, and not just compensate for losses in resolution/liquidation.

We consider the readiness of the group to support its members to be high. Under our methodology, this high support translates into no uplift from CRN's BCA of baa1.

#### Loss Given Failure (LGF) analysis

CRN is subject to the EU Bank Recovery and Resolution Directive, which we consider an operational resolution regime. Accordingly, we apply most of its standard assumptions. These assumptions include a residual tangible common equity of 3%, post-failure losses of 8% of tangible banking assets, a 25% runoff in junior wholesale deposits and a 5% runoff in preferred deposits, and assign a 25% probability to deposits being preferred over senior unsecured debt. Because we assume that CRN's deposit base is essentially retail in nature, we consider a proportion of 10% of junior deposits, below the estimated EU-wide average of 26%.

For CRN's deposits, our LGF analysis takes into consideration the likely impact on loss given failure of the combination of its own volume and subordination. Our LGF analysis indicates a moderate loss given failure for deposits, which leads us to position the bank's Preliminary Rating Assessment at the same level as its Adjusted BCA. Please refer to the Loss Given Failure and Government Support table at the bottom of the scorecard.

### Counterparty Risk (CR) Assessment

#### CRN's CR Assessment is positioned at A3(cr)/Prime-2(cr)

CRN's CR Assessment is constrained by Spain's sovereign rating of Baa1. Under our "Banks" methodology, a bank's CR Assessment will typically not exceed the sovereign rating by more than one notch.

Before the government cap, the CR Assessment is positioned two notches above the bank's Adjusted BCA of baa1, based on the buffer against default provided to the senior obligations represented by the CR Assessment by subordinated instruments, amounting to 8.7% of tangible banking assets. The main difference in our Advanced LGF approach used to determine instrument ratings is that the CR Assessment captures the probability of default on certain senior obligations, rather than expected loss, thereby focusing purely on subordination and taking no account of the volume of the instrument class.

### Counterparty Risk Ratings (CRRs)

#### CRN's CRRs are positioned at A3/Prime-2

The CRRs are positioned one notch above the Adjusted BCA of baa1, reflecting the low loss given failure from the high volume of instruments that are subordinated to CRR liabilities. According to our methodology, a bank's CRR will typically not exceed the sovereign rating by more than two notches. Therefore, Spanish banks' maximum achievable CRRs are A2/Prime-1.

### Government support

We assign a low probability of government support for CRN's deposits, which does not translate into any uplift. Likewise, the CR Assessment does not benefit from any rating uplift from government support.

## Methodology and scorecard

### About Moody's Bank Scorecard

Our scorecard is designed to capture, express and explain in summary form our rating committee's judgement. When read in conjunction with our research, a fulsome presentation of our judgement is expressed. As a result, the output of our scorecard may materially differ from that suggested by raw data alone (though it has been calibrated to avoid the frequent need for strong divergence). The scorecard output and the individual scores are discussed in rating committees and may be adjusted up or down to reflect conditions specific to each rated entity.

## Rating methodology and scorecard factors

Exhibit 9

### Caja Rural de Navarra

<b>Macro Factors</b>							
<b>Weighted Macro Profile</b>		<b>Strong - 100%</b>					
<b>Factor</b>	<b>Historic Ratio</b>	<b>Initial Score</b>	<b>Expected Trend</b>	<b>Assigned Score</b>	<b>Key driver #1</b>	<b>Key driver #2</b>	
Solvency							
Asset Risk							
Problem Loans / Gross Loans	1.9%	a3	↓	a3	Expected trend		
Capital							
Tangible Common Equity / Risk Weighted Assets (Basel III - transitional phase-in)	15.1%	a2	↔	a2	Expected trend		
Profitability							
Net Income / Tangible Assets	0.6%	ba1	↑	baa3	Expected trend		
Combined Solvency Score		baa1		a3			
Liquidity							
Funding Structure							
Market Funds / Tangible Banking Assets	21.2%	baa3	↑	baa2	Extent of market funding reliance		
Liquid Resources							
Liquid Banking Assets / Tangible Banking Assets	36.0%	a3	↓	baa3	Asset encumbrance		
Combined Liquidity Score		baa2		baa2			
Financial Profile							
				baa1			
Qualitative Adjustments				Adjustment			
Business Diversification				0			
Opacity and Complexity				0			
Corporate Behavior				0			
Total Qualitative Adjustments				0			
Sovereign or Affiliate constraint				Baa1			
BCA Scorecard-indicated Outcome - Range				a3 - baa2			
Assigned BCA				baa1			
Affiliate Support notching				0			
Adjusted BCA				baa1			
<b>Balance Sheet</b>							
		<b>in-scope (EUR Million)</b>		<b>% in-scope</b>	<b>at-failure (EUR Million)</b>	<b>% at-failure</b>	
Other liabilities		3,871		24.8%	4,652	29.8%	
Preferred deposits		10,040		64.4%	9,538	61.2%	
Junior deposits		1,116		7.2%	837	5.4%	
Senior unsecured bank debt		100		0.6%	100	0.6%	
Equity		468		3.0%	468	3.0%	
Total Tangible Banking Assets		4,439		100.0%	5,219	33.5%	

Debt Class	De Jure waterfall		De Facto waterfall		Notching		LGF	Assigned LGF	Additional Notching	Preliminary Rating Assessment
	Instrument volume + subordination	Sub-ordination	Instrument volume + subordination	Sub-ordination	De Jure	De Facto				
Counterparty Risk Rating	9.0%	9.0%	9.0%	9.0%	1	1	1	1	0	a3
Counterparty Risk Assessment	9.0%	9.0%	9.0%	9.0%	2	2	2	2	0	a3 (cr)
Deposits	9.0%	3.0%	9.0%	3.6%	0	0	0	0	0	baa1

Instrument Class	Loss Given Failure notching	Additional notching	Preliminary Rating Assessment	Government Support notching	Local Currency Rating	Foreign Currency Rating
Counterparty Risk Rating	1	0	a3	0	A3	
Counterparty Risk Assessment	2	0	a3 (cr)	0	A3(cr)	
Deposits	0	0	baa1	0	Baa1	

[1] Where dashes are shown for a particular factor (or sub-factor), the score is based on non-public information.

Source: Moody's Investors Service

## Ratings

Exhibit 10

Category	Moody's Rating
<b>CAJA RURAL DE NAVARRA</b>	
Outlook	Stable
Counterparty Risk Rating -Dom Curr	A3/P-2
Bank Deposits -Dom Curr	Baa1/P-2
Baseline Credit Assessment	baa1
Adjusted Baseline Credit Assessment	baa1
Counterparty Risk Assessment	A3(cr)/P-2(cr)

Source: Moody's Investors Service

## Endnotes

- 1 The ratings shown in this report are deposits ratings, senior long-term debt ratings when available and BCA.
- 2 Moody's calculations
- 3 Moody's estimated
- 4 As per the European Banking Authority (EBA) risk dashboard
- 5 See Moody's Adjustment to Increase the Risk Weightings of Sovereign Debt Securities in the Analysis of Banks: Frequently Asked Questions.
- 6 According to data disclosed by EBA

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