MOODY'S INVESTORS SERVICE

CREDIT OPINION
26 November 2021

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.

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Caja Rural de Navarra

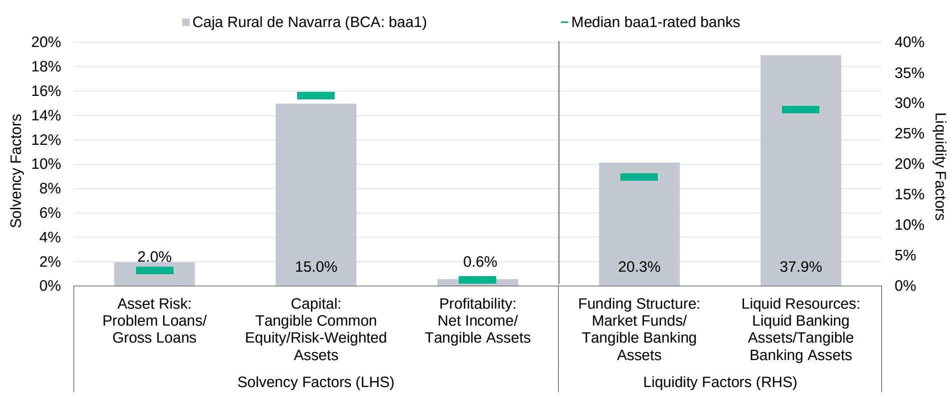
Update to credit analysis

Summary

Caja Rural de Navarra's (CRN) Baa1/Prime-2 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 and the limited geographical diversification of its franchise, which is concentrated in Navarre and its neighbouring regions.

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

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

Credit challenges

» Asset-risk profile to deteriorate because of the coronavirus pandemic

» Lower revenue and high cost of credit as a result of the coronavirus pandemic will continue to weigh on CRN's recurrent profitability

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.

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. 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.

Key indicators

Exhibit 2

Caja Rural de Navarra (Consolidated Financials) [1]

	12-20[2]	12-19[2]	12-18[2]	12-17[2]	12-16[2]	CAGR/Avg.[3]
Total Assets (EUR Million)	15,849.8	13,133.1	12,202.9	11,726.2	11,085.6	9.3[4]
Total Assets (USD Million)	19,393.1	14,741.9	13,949.6	14,080.8	11,692.5	13.5[4]
Tangible Common Equity (EUR Million)	1,303.1	1,212.0	1,110.7	1,036.9	943.8	8.4[4]
Tangible Common Equity (USD Million)	1,594.4	1,360.4	1,269.7	1,245.1	995.5	12.5[4]
Problem Loans / Gross Loans (%)	2.0	2.0	1.8	2.0	2.6	2.1[5]
Tangible Common Equity / Risk Weighted Assets (%)	15.0	14.2	14.0	13.4	13.3	14.0[6]
Problem Loans / (Tangible Common Equity + Loan Loss Reserve) (%)	11.7	12.1	11.2	12.8	16.4	12.8[5]
Net Interest Margin (%)	1.0	1.2	1.2	1.3	1.4	1.2[5]
PPI / Average RWA (%)	1.4	1.5	1.4	1.6	1.8	1.5[6]
Net Income / Tangible Assets (%)	0.5	0.8	0.8	0.8	0.6	0.7[5]
Cost / Income Ratio (%)	58.3	57.4	60.4	56.3	54.8	57.4[5]
Market Funds / Tangible Banking Assets (%)	20.3	15.7	16.2	16.9	17.4	17.3[5]
Liquid Banking Assets / Tangible Banking Assets (%)	37.9	29.6	26.9	31.7	31.7	31.6[5]
Gross Loans / Due to Customers (%)	88.1	95.1	99.1	99.6	99.8	96.3[5]

[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 €15.8 billion as of year-end 2020, 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 market shares of 29.4% in lending and 25.6% in deposits as of the end of June 2020 (latest available data), the bank is ranked second in Navarre, behind CaixaBank, S.A. (CaixaBank, A3/Baa1 stable, baa3)[1]. 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

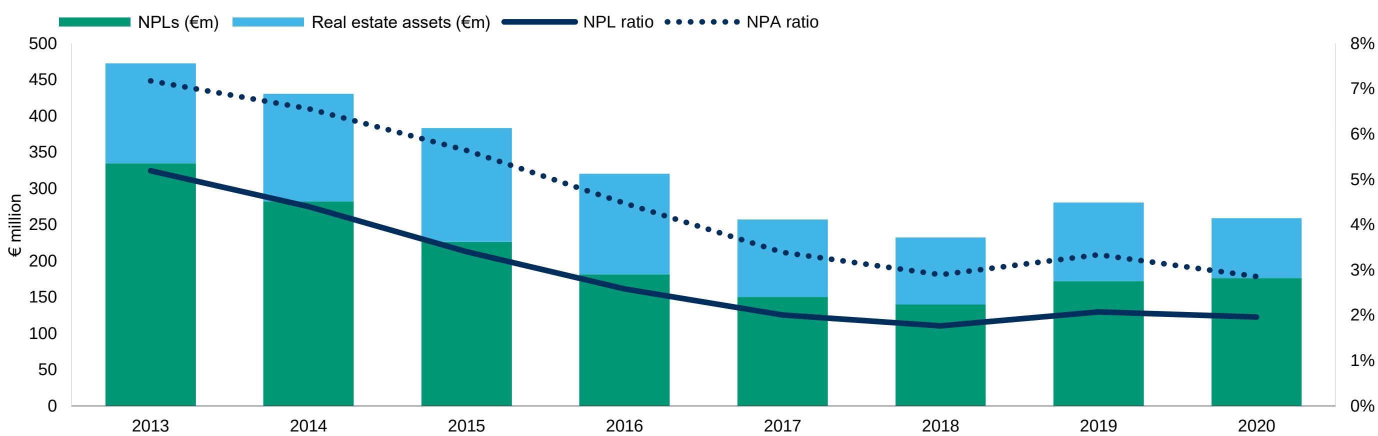
CRN's assigned Asset Risk score of baa1 incorporates the bank's very low level of nonperforming assets (NPA; defined as nonperforming loans (NPLs) plus real estate assets) relative to the banking system, as well as our expectation that asset quality will deteriorate as the public support measures that the Spanish authorities put in place in view of the coronavirus pandemic are progressively withdrawn. The assigned score also incorporates a one notch negative adjustment to reflect the limited geographical diversification of the bank's franchise that makes the bank more vulnerable to economic shocks in the region.

As of the end of 2020, CRN reported an outstanding volume of loans under moratoria of €60 million and of loans granted under public guarantee schemes of €1.0 billion (0.6% and 10.6% of the bank's loan book respectively).

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 year-end 2020, the bank reported an NPL ratio of 2.0%, broadly in line with the 2.1% reported a year earlier, while the ratio for the banking system was 4.3% as of the same date. In addition to NPLs, CRN has a low amount of real estate assets repossessed over the past few years. If these assets are added to the bank's NPLs, the NPA ratio would be 2.9% as of year-end 2020, below the 3.3% reported a year earlier and still comparing very favourably with the 6.5% average for its domestic peers as of the same date (see Exhibit 3).

Exhibit 3

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



Sources: CRN and Moody's Investors Service

CRN booked loan-loss provisions amounting to €79 million in 2020 in anticipation of higher expected credit losses that will be triggered by the pandemic-induced economic downturn. As a result, the bank's cost of risk stood at a high 88 basis points (bps) for the year. This extraordinary provisioning effort resulted in an increase of the bank's coverage ratio (measured as loan-loss reserves as a percentage of NPLs) to 116% as of the end of December 2020, up from 80% a year earlier and above the system average of 69% for the same period. The coverage of NPA was 88% as of the same date.

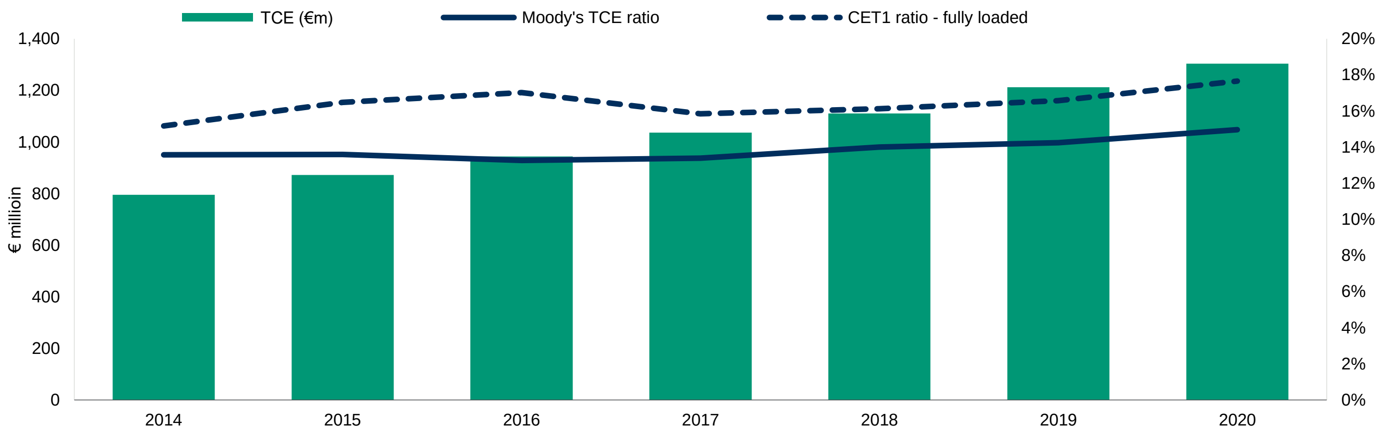
CRN displays sound solvency levels

CRN's assigned Capital score of a3 reflects our assessment that capitalisation is a relative strength for the bank. As of year-end 2020, CRN's tangible common equity/risk-weighted assets was 15.0%, up from 14.2% a year earlier. CRN's capital is mainly composed of retained earnings and contributions (the so-called aportaciones) on which it pays interest.

The bank's capital ratio as of year-end 2020 improved mainly because of the application of the capital requirement regulation "quick fix" (CRR 2.5)[2] measures, as well as the high share of profit retention of CRN. 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 17.7% as of year-end 2020. 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%[3].

Exhibit 4
CRN's capital levels have improved over recent years



Sources: CRN and Moody's Investors Service

CRN's bottom-line profitability is strained by the challenging operating environment

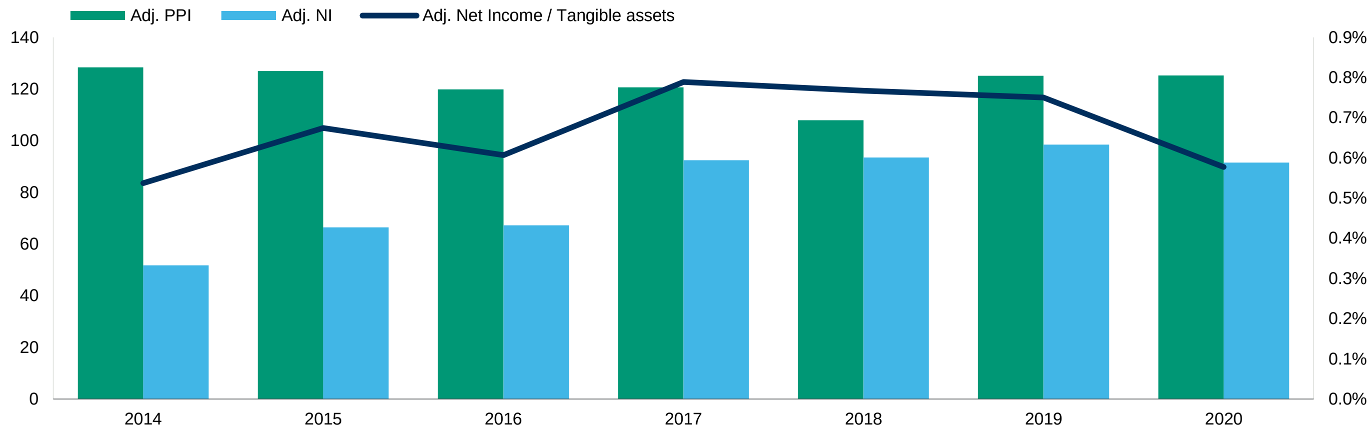
We assign a Profitability score of ba1 to CRN. Our assessment of the bank's profitability factors in our expectation that the challenging operating environment will continue to result in lower operating revenue and high cost of credit risk. CRN reported a net income/ tangible assets of 0.6% as of year-end 2020.

CRN's top-line earnings have been relatively stable over the past few years, as opposed to system trends (see Exhibit 5). For 2020, the bank reported an operating income of €293 million, broadly in line with the €292 million reported for 2019. The bank's net interest income increased by 2%, while its fee and commission income and operating expenses showed no variation and remained at the same level than the previous year. This led to a broadly unchanged pre-provision income (PPI) year over year amounting to €125 million.

Despite the broadly stable PPI, CRN's net income reduced by 7% year over year in 2020, reflecting the higher provisioning efforts as a result of the challenging operating environment.

CRN's cost-to-income ratio was maintained broadly stable at 57% as of year-end 2020, weaker than the system average of 52%, reflecting the bank's modest efficiency levels.

Exhibit 5
CRN's top-line earnings have been fairly resilient over recent years



Sources: CRN and Moody's Investors Service

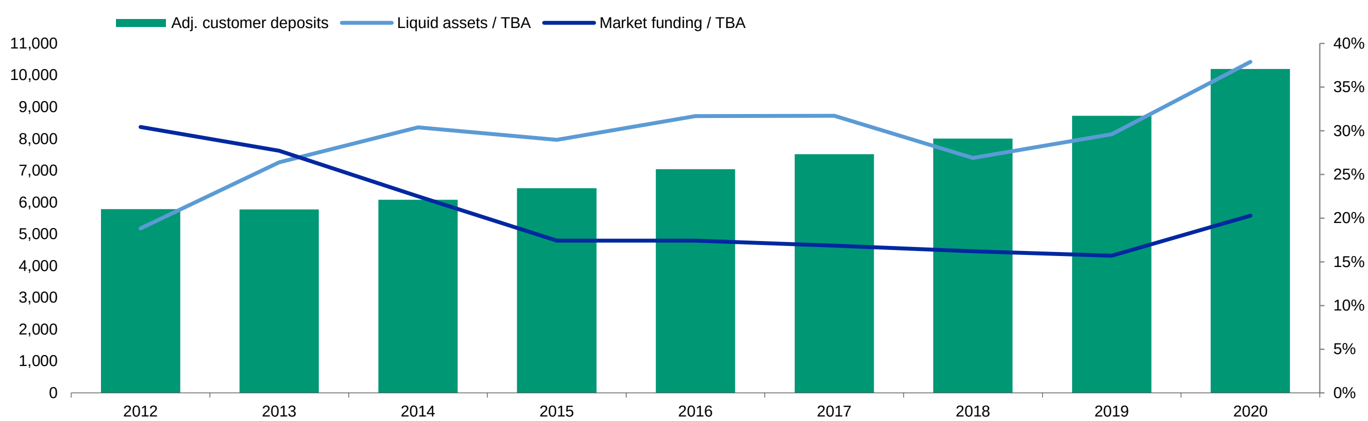
Low reliance on market funding, most of which is secured

We assign a Funding Structure score of baa2 to CRN, in line with its Macro-Adjusted score, to reflect the bank's limited reliance on market funding. CRN is predominantly retail funded. As of year-end 2020, deposits accounted for around 72% of the bank's total funding, representing 88% of its gross loans. The bank's regional identity adds a component of stability to its retail funding base, which has consistently grown over the years (see Exhibit 6).

Most of CRN's wholesale funding is composed of covered bonds (€1.7 billion) and ECB funding (€1.9 billion), all secured funding sources. ECB funding is primarily used to take advantage of its attractive terms, especially following the TLTRO[4] III. In addition, CRN has tapped wholesale markets through a number of sustainable financing instruments, which form part of its sustainability framework (two €500 million sustainable mortgage covered bonds [November 2016 and May 2018] and a €100 million senior sustainable bond in June 2017).

CRN's liquid banking assets accounted for 37.9% of its tangible banking assets as of year-end 2020. We assign a Liquid Resources score of baa3 to the bank, in line with its Macro-Adjusted score, to reflect the level of encumbrance.

Exhibit 6
Growing deposit base and low reliance on wholesale funding



Sources: CRN and Moody's Investors Service

Environmental, social and governance considerations

In line with our general view on the banking sector, CRN has a low exposure to environmental risks. See our Environmental risk heat map for further information.

Overall, we expect banks to face moderate social risks. This includes considerations in relation to the rapid and widening spread of the coronavirus pandemic, given the substantial implications for public health and safety, and the deteriorating global economic outlook, creating a severe and extensive credit shock across many sectors, regions and markets. See our Social risk heat map for further information.

For Spanish banks, we have identified the potential litigation around the IRPH (Mortgage Loan Reference Index, Índice de Referencia de Préstamos Hipotecarios) index reference rate as a key social risk. The bank has not publicly disclosed its exposure to IRPH loans.

Governance is highly relevant for CRN, as it is to all banks in the industry. Corporate governance weaknesses can lead to a deterioration in a bank's credit quality, while governance strengths can benefit its credit profile. We do not have any particular concern around CRN's governance, and we believe that the bank displays an appropriate risk management framework commensurate with its risk appetite. Nonetheless, corporate governance remains a key credit consideration and requires ongoing monitoring.

Support and structural considerations

Affiliate support

We assign a high probability of affiliate support for CRN from the entities integrated into the IPS, which are the 30 rural cooperatives under the AECR and BCE. This support assessment 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 7
Caja Rural de Navarra

Macro Factors							
Weighted Macro Profile	**Strong -**	**100%**					
Factor		**Historic Ratio**	**Initial Score**	**Expected Trend**	**Assigned Score**	**Key driver #1**	**Key driver #2**
Solvency							
Asset Risk							
Problem Loans / Gross Loans		2.0%	a3	↓	baa1	Expected trend	Geographical concentration
Capital							
Tangible Common Equity / Risk Weighted Assets (Basel III - transitional phase-in)		15.0%	a3	↔	a3	Expected trend	
Profitability							
Net Income / Tangible Assets		0.5%	ba1	↔	ba1	Expected trend	
Combined Solvency Score			baa1		baa1		
Liquidity							
Funding Structure							
Market Funds / Tangible Banking Assets		20.3%	baa3	↑	baa2	Extent of market funding reliance	
Liquid Resources							
Liquid Banking Assets / Tangible Banking Assets		37.9%	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		

Balance Sheet	**in-scope (EUR Million)**	**% in-scope**	**at-failure (EUR Million)**	**% at-failure**
Other liabilities	4,099	25.9%	4,881	30.8%
Preferred deposits	10,048	63.4%	9,546	60.3%
Junior deposits	1,116	7.0%	837	5.3%
Senior unsecured bank debt	100	0.6%	100	0.6%
Equity	475	3.0%	475	3.0%
Total Tangible Banking Assets	4,675	100.0%	5,456	34.4%

Debt Class	De Jure waterfall		De Facto waterfall		Notching		LGF Notching Guidance vs. Adjusted BCA	Assigned LGF notching	Additional Notching	Preliminary Rating Assessment
	Instrument volume + subordination	Sub-ordination	Instrument volume + subordination	Sub-ordination	De Jure	De Facto				
Counterparty Risk Rating	8.9%	8.9%	8.9%	8.9%	1	1	1	1	0	a3
Counterparty Risk Assessment	8.9%	8.9%	8.9%	8.9%	2	2	2	2	0	a3 (cr)
Deposits	8.9%	3.0%	8.9%	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 8

Category	Moody's Rating
CAJA RURAL DE NAVARRA	
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 deposit ratings, senior long-term debt ratings when available and BCA.

2 The aforementioned quick fix to the capital requirement regulation resulted in a reduction in risk weighting factors for loans to SMEs. It was approved in the European Parliament in June 2020, aimed at supporting the credit flow to SMEs and households, and mitigating the impact of the lockdown because of the coronavirus pandemic on capital.

3 See Moody's Adjustment to Increase the Risk Weightings of Sovereign Debt Securities in the Analysis of Banks: Frequently Asked Questions.

4 Targeted long-term refinancing operations.

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