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Bankia S.A.

Primary Credit Analyst:
Lucia Gonzalez, Madrid + 34 91 788 7219; lucia.gonzalez@spglobal.com

Secondary Contact:
Elena Iparraguirre, Madrid (34) 91-389-6963; elena.iparraguirre@spglobal.com

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Bankia S.A.

SACP	bbb

Anchor	bbb	
Business Position	Adequate	0
Capital and Earnings	Adequate	0
Risk Position	Adequate	0
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/Stable/A-2

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

Major Rating Factors

Strengths:	Weaknesses:
• Large banking franchise in Spain, with more than 11% market share. • Sufficient capital buffer to absorb the effects of the current economic shock. • High share of low-risk mortgage lending. • Balanced funding structure.	• Heightened pressure on already weak profitability, given limited earnings--constrained by high weight of lower-yielding mortgage loans--amid the COVID-19-related economic shock. • More limited business and geographical diversification than some of its closest peers. • Higher than peers' stock of problematic assets at the onset of the current crisis, despite a substantial transfer to Spain's bad bank SAREB in 2012.

Outlook: Stable

The stable outlook on Bankia reflects our expectation that there will be a sharp economic contraction in 2020 associated with the COVID-19 pandemic, and only a partial rebound in 2021. Although we assume pressure will build on Bankia's earnings and asset quality over the next 18-24 months, we believe the bank will remain adequately capitalized. In particular, we anticipate Bankia's risk-adjusted capital (RAC) ratio will be about 8.75%-9.25% over the next two years, while the bank continues advancing the build-up of its additional loss-absorbing instruments. The stable outlook also incorporates our assumption that there will be an economic rebound from the second half of 2020 and throughout 2021. This, teamed with the authorities' support measures, should help limit potential credit constraints. As such, we believe that Bankia will be able to defend its solid banking franchise in Spain and maintain a balanced funding structure.

Our stable outlook also assumes Bankia will not undergo changes in management or strategic direction. The bank remains ultimately owned by the Spanish government through the Fund for Orderly Bank Resolution (FROB). The deadline for privatization is year-end 2021, although we believe it could be extended if needed, as in the past.

We could lower the ratings if we observed a further and more severe deterioration in economic and operating conditions, and greater-than-currently-anticipated pressure on Bankia's earnings or asset quality. Although not our base case, we could also lower the ratings if Bankia's capitalization erodes significantly, such that its RAC ratio falls sustainably below 7%.

Although unlikely in the current context, we could raise our ratings if Bankia builds an ALAC buffer above 5% of RWAs, while sustaining its risk profile at manageable levels.

The stable outlook on the holding company, BFA Tenedora de Acciones S.A.U., mirrors that on the group's operating entity, Bankia, as we expect the ratings on both the operating and holding company to move in tandem.

Rationale

Our ratings on Bankia factor in its large domestic franchise; its solvency, which we see as adequate for the risks it faces and ample enough to absorb the COVID-19 economic shock; and its low-risk mortgage-focused and well-seasoned portfolio, which should see lower asset quality deterioration compared to other Spanish players that have a higher exposure to companies. However, our ratings also reflect Bankia's limited business and geographical diversification compared to some of its closest peers, as well as its weak core operating profitability which is under mounting pressure in the current context. In fact, we project that its return on equity will remain below 3% this year and next, before improving somewhat in 2022.

Bankia's asset-quality metrics have improved notably since year-end 2017 on the back of organic reduction efforts and a €2.7 billion market sale announced in 2018. Still, at the onset of the COVID-19 pandemic, they remained somewhat weaker than peers', with pro forma nonperforming assets (NPAs) equaling 6.9% of gross loans at end-2019, versus an estimated 5.0% average for its closest domestic competitors on the same date, and an estimated 7.0% for the Spanish banking sector overall. The bank has also rebalanced its funding profile and liquidity position. However, even if Bankia has successfully reduced its reliance on European Central Bank (ECB) and other short-term funding, we note that it still has a large holding of less-liquid and low-yield SAREB bonds.

We analyze Bankia and BFA on a consolidated basis, at the highest level of supervisory and regulatory oversight, using BFA's consolidated financial information. Our assessment of the group credit profile (GCP) is 'bbb'. We consider Bankia to be the group's core operating entity and we rate it at the GCP level. We rate BFA one notch below the GCP. This is the standard downward adjustment we make for holding companies when the GCP is investment grade. It also reflects the structural subordination of BFA's creditors to those of Bankia.

We compare Bankia with domestic peers, namely Caixabank (stand-alone credit profile [SACP]: bbb+), Bankinter (bbb+), Banco de Sabadell (bbb), and Kutxabank (bbb). We also consider as peers foreign banks that operate in countries with relatively similar industry and economic risks that have broadly similar business models, such as Poland-based Pekao (bbb+), Ireland-based Bank of Ireland Group PLC (bbb), Italy-based UBI Banca SpA (bbb-), and Portugal-based Banco Comercial Portugues (bb). In addition, we compare Bankia with other entities in which public authorities have a majority ownership, namely AIB Group PLC (bbb), Royal Bank of Scotland (bbb+), and ABN Amro (a-).

Anchor: 'bbb' for Spanish domestic banks

The anchor for banks operating primarily in Spain is 'bbb', reflecting our economic risk assessment of '4' and our industry risk assessment of '4' (on a scale of 1-10, with '10' signifying the highest risk). We view the trend for economic risk as negative and the trend for industry risk as stable.

Spanish banks operate in a wealthy economy that, following the severe, double-dip recession of 2009-2013, managed to return to growth and correct previous imbalances, notably the persistent current account deficit and the previously high private sector indebtedness. The economy's external account has been in surplus since 2013, while private sector leverage is now adequately aligned to its debt capacity, after having declined by the equivalent of almost 70 percentage points of GDP over the past decade. Although it has taken a while, the banking system has also largely completed the provisioning of nonperforming assets (NPAs) that were left after the property bubble burst and recession ensued, and note stronger capital overall. In our view, the property market no longer shows signs of imbalances.

That said, the outbreak of COVID-19, and the lockdown measures imposed to contain its spread, represent a meaningful shock for the Spanish economy. We expect GDP to fall severely in 2020, and consider it unlikely to return to pre-COVID levels until 2022. Certain sectors will be more affected than others, such as tourism, which is particularly important for the Spanish economy. In addition, unemployment will increase from already comparatively high levels, potentially reaching 16.5% in 2021, and the government's fiscal accounts will also suffer. As a result, we also expect banks' asset quality to deteriorate and credit costs to rise, despite support measures that the government and banks have put in place to help borrowers navigate this difficult period. We estimate that credit provisions will double from 2019 levels, standing at 80 basis points (bps) of average loans in both 2020 and 2021. Existing plans to continue reducing the remaining stock of legacy NPAs from the previous downturn (7.7% at end-2019 according to our estimates) will be difficult to execute, in our view.

Our assessment of industry risk reflects Spanish banks' balanced funding profiles and ample liquidity, as well as the profitability challenges ahead. Customer deposits now fund the bulk of banks' loan books, and at historically low costs. Reliance on wholesale market funding is therefore limited and markets remain open. In addition, through the TLTRO

III program and the recently launched PELTRO facility, the European Central Bank will continue to ensure banks' access to funding, if needed, at attractive prices. The COVID-19 shock, however, will aggravate existing profitability challenges resulting from low rates, limited business growth, and intense competition. The prospect of banks achieving returns in line with their cost of capital was already remote, particularly for midsize banks, and much more so in the current environment. Banks' profitability will decline substantially in 2020, from the combination of weaker earnings and increased credit costs, and will only partially recover in 2021. However, we expect Spanish banks to remain fairly efficient compared to peers.

Table 1

Bankia S.A.--Key Figures

	--Year ended Dec. 31--				
Mil. €	**2019**	**2018**	**2017**	**2016**	**2015**
Adjusted assets	210,379.9	207,369.4	217,672.5	193,829.8	213,495.7
Customer loans (gross)	120,614.2	122,413.5	128,546.1	110,087.7	115,930.4
Adjusted common equity	10,940.1	10,970.9	11,527.6	10,511.5	10,453.7
Operating revenues	3,332.6	3,277.0	3,147.4	3,199.0	3,731.0
Noninterest expenses	2,123.2	2,174.8	1,969.3	1,795.2	1,970.7
Core earnings	322.6	406.4	575.3	608.3	851.6

Business position: Weak profitability balanced by its large domestic franchise

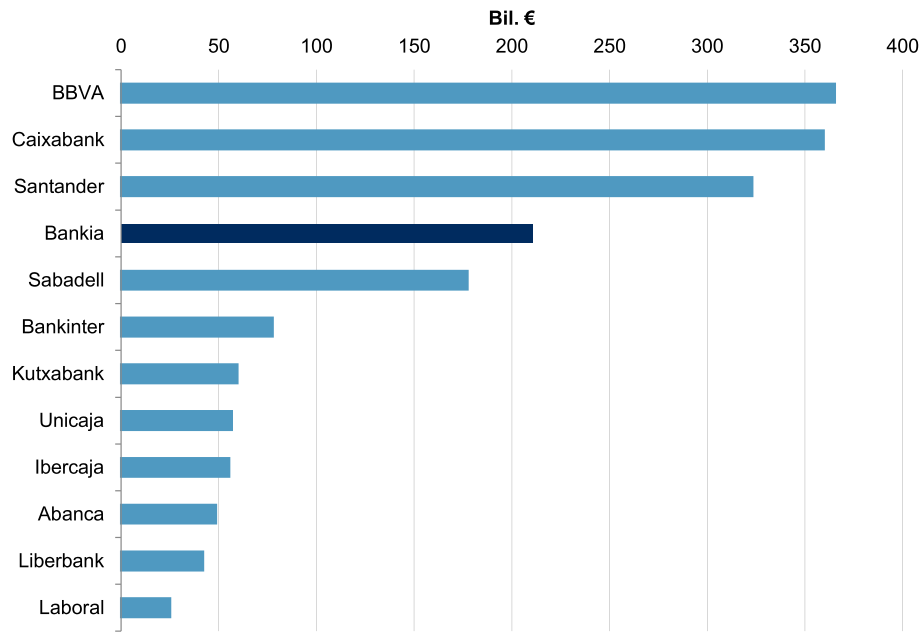
Our view of Bankia's business position factors in its large domestic franchise, which is, however, more geographically concentrated and less diversified by product than that of some peers. In addition, its already weak profitability is now under mounting pressure.

With €211 billion in assets at end-2019, Bankia is the fourth-largest financial institution in Spain by total domestic assets, with nationwide market shares of about 12% in loans and 11% in deposits. Bankia's franchise is particularly strong in mortgage lending, where it held a market share of 12.4% at end-February 2020. It is also present in all other lending segments, although much less so, holding 7.7% market share in corporate lending and 6.1% in consumer lending, on the same date, as well as mutual funds (7.3%) and pension plans (6.3%). Compared with larger domestic peers, however, its scale and market share are more limited, as is its business diversification. Bankia also lacks the international presence of some of its closest peers.

Chart 1

Bankia Is The Fourth Largest Spanish Bank By Domestic Assets, Although Largely Behind Domestic "Champions"

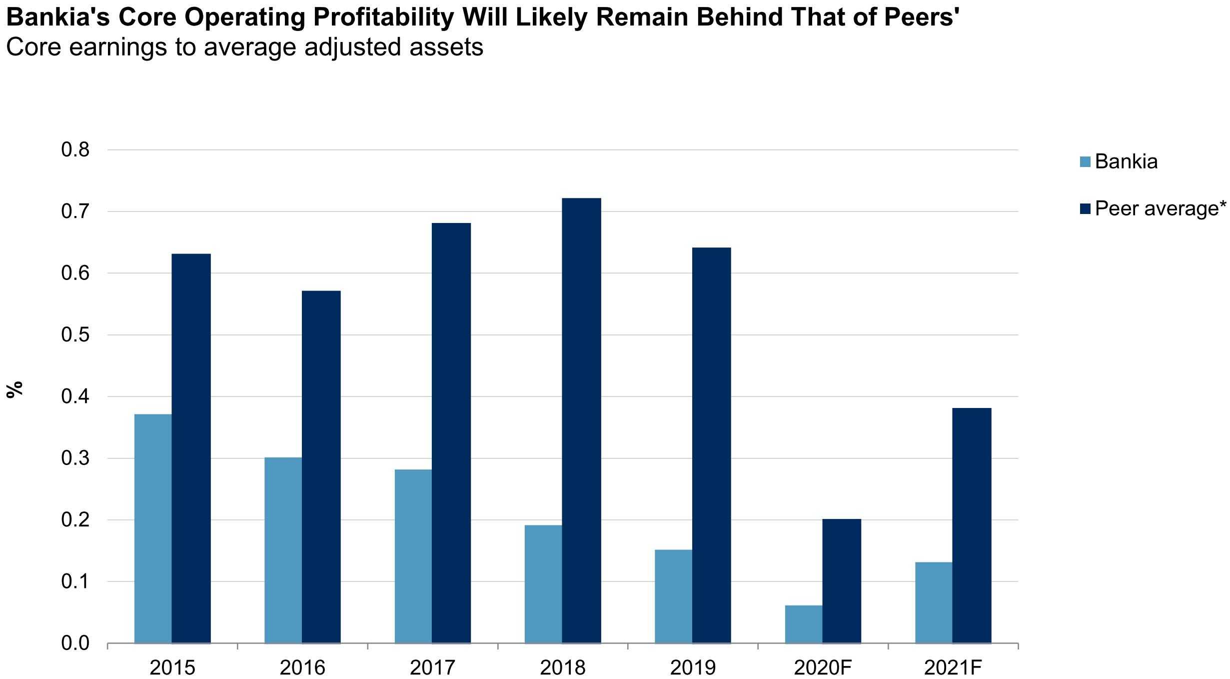
Spanish banks reported domestic assets as of YE2019



Source: S&P Global Ratings.

Bankia successfully emerged in 2017 from a deep restructuring plan agreed with the European authorities. Despite some tentative diversification improvement, Bankia remains mostly mortgage and domestic-focused. In our view, it now faces mounting pressure on its already weak profitability. Until the outbreak of COVID-19, Bankia's operating revenue was pressured by ultra-low interest rates and the significant weight of mortgages in its loan book--with a notable portion generated in the boom years, with tight spreads--and with its core operating profitability lagging that of peers. In addition, bottom-line profitability was strongly supported by a cost of risk well below the sector average and below Bankia's normalized cost of risk. We project heightened pressure on the bank's revenue stream and overall profitability amid the COVID-19-related economic shock, with ROE likely to remain below 3% this year and next before recovering somewhat in 2022. This level is below that of its closest peer group, including other government-owned banks.

Chart 2



*Peers include Caixabank, Bankinter, Banco de Sabadell, Kutxabank, Pekao, Bank of Ireland Group PLC, AIB Group PLC, UBI Banca SpA, Banco Comercial Portugues, Royal Bank of Scotland, and ABN Amro. Source: S&P Global Ratings.

The main action pending after the bank's restructuring relates to its privatization and the exit of the Fund for Orderly Bank Restructuring (FROB), which currently holds a 61.8% stake in Bankia--and ultimately of the Spanish government--from the shareholder base. Even though this has already been on the agenda for some time, the deadline has been extended more than once in the past and is now due by 2021. However, given the current context and pressure on the bank's profitability and market valuation, we believe there is a high probability that the privatization will not materialize by end-2021, and that the deadline will have to be extended again. Until its privatization, we believe that Bankia will continue to be managed independently, and we see no risks of it becoming a public bank as suggested by one of the coalition parties in the government.

Table 2

BFA Tenedora de Acciones, S.A.U.--Business Position

	--Year ended Dec. 31--				
%	**2019**	**2018**	**2017**	**2016**	**2015**
Total revenues from business line (currency in millions)	3,997.4	4,098.9	3,713.4	4,221.2	6,657.6
Commercial banking/total revenues from business line	15.3	14.3	14.7	13.5	8.4
Retail banking/total revenues from business line	50.7	46.9	43.4	43.6	35.8
Commercial & retail banking/total revenues from business line	N/A	N/A	58.1	57.1	44.2

Table 2

BFA Tenedora de Acciones, S.A.U.--Business Position (cont.)					
	--Year ended Dec. 31--				
%	2019	2018	2017	2016	2015
Other revenues/total revenues from business line	34.0	38.8	41.9	42.9	55.8
Return on average common equity	1.1	2.6	3.0	0.7	12.6

N/A--Not applicable.

Capital and earnings: Ample capital buffer to absorb the COVID-19 economic shock

Bankia's solvency has improved materially in the past few years on the back of supportive economic conditions in Spain and capital-enhancing measures including disposals of noncore assets, increasing organic capital generation, and the issuance of hybrid instruments. At end-2019, its RAC ratio stood at 9.4%, up from 6.9% at end-2015.

Amid mounting pressure on its profitability, we anticipate that Bankia's RAC ratio will decline somewhat but remain at an adequate level through the downturn. We project its RAC ratio at about 8.75%-9.25% over the next two years. If we were to reassess our view of economic risk in Spain to '5', from '4' currently, this would translate into an additional reduction of around 110 bps from Bankia's RAC.

In our forecasts we assume that Bankia's operating revenues will decline by more than 7% this year, before recovering slightly in 2021, mostly due to compressed margins but also lower other income sources. In terms of volumes, we anticipate higher loan growth of about 2%, with an important part explained by new loan origination to the corporate sector, taking advantage of government guarantees programs. In addition, we project that Bankia's cost of risk will hike to about 60 bps, versus a reported 25 bps in 2019, excluding extraordinary provisions. This is in line with Bankia's reported cost of risk for Q1 results but is lower than what we anticipate for many of its domestic peers, factoring in Bankia's mortgage-focused and well-seasoned portfolio.

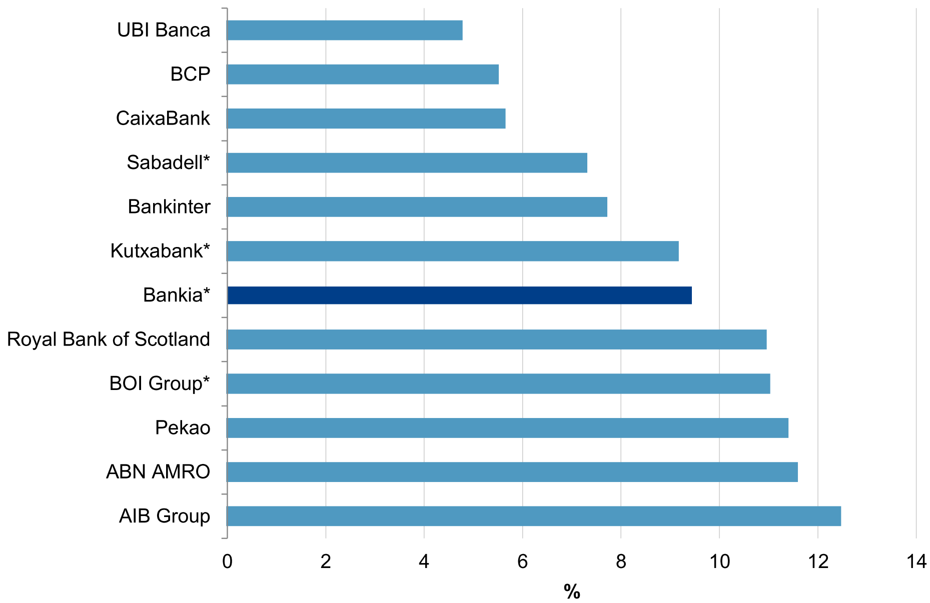
Overall, we expect Bankia's bottom-line profits to decline by more than 60% in 2020 versus 2019, before recovering somewhat next year, but still remaining below pre-pandemic levels in 2021 and 2022. Our forecasts do not contemplate future contingencies related to legacy risks (such as claims against the misselling of preference shares, and removal of mortgage floors), which we believe are now contained. Similarly, we believe that the risk of Bankia and its domestic peers facing significant claims from Indice de Referencia de Prestamos Hipotecarios (IRPH)-linked mortgage borrowers is limited (see "Contingency Risk From IRPH-Linked Mortgage Litigation Claims Is Reducing For Spanish Banks," published Sept. 13, 2019). In addition, we assume no dividends distribution for this year. Bankia has announced it will postpone any dividend decision to be charged to 2020 results until after Q1 2021. This contrasts with the 65% payout on 2019 results, relatively higher than the 44% average of the previous three years.

Our RAC forecasts do not incorporate the potential extraordinary upstreaming of capital from BFA to the state in the form of the repayment of some of the capital support that the group received during the financial crisis (€22.5 billion). At this stage, even if this repayment were made, we assume that it would not alter our current assessment of the capital position of either the group or Bankia.

At March 31, 2020, Bankia reported a regulatory phase-in CET1 ratio of 13.98%--well above its 9.25% supervisory review and evaluation process (SREP) requirement--or 12.95% on a fully loaded basis. This compares with management's targets of a fully loaded CET1 ratio of at least 12.0% by year-end 2020, roughly in line with that of other domestic peers. We note positively that Bankia's phase-in CET1 buffer versus its requirement is among the largest of the banks that we rate in Spain, equivalent to slightly more than 5% at end-2019.

Chart 3

Bankia's Large Capital Buffer Should Allow It To Better Absorb The Current Economic Shock
RAC ratios as of YE2018



*RAC ratio for Bankia, Kutxabank, Sabadell, and BOI Group as of December 2019, for all others as of December 2018. Source: S&P Global Ratings.

The difference between the reported regulatory ratios and our capital measures relates mainly to the higher-risk weightings we assign to asset classes in Spain and our more conservative treatment of deferred tax assets (DTAs). In particular, we deduct from Bankia's total adjusted capital (TAC) €2.5 billion of DTAs (including tax-loss carry forward). Bankia's convertible DTAs, which we don't deduct from the bank's TAC and which we risk weight at 250%, equaled a high 66% of its TAC at end-2019.

In our view, and despite the stock of DTAs accumulated, the quality of Bankia's capital is satisfactory and consistent with most domestic and international peers, with Additional Tier 1 (AT1) representing 10% of our TAC at end-2019. In addition, we consider Bankia's earnings profile relatively predictable, with net interest income and fees and commissions accounting for about 90% of operating revenue over the past five years.

Table 3

BFA Tenedora de Acciones, S.A.U.--Capital And Earnings					
	--Year ended Dec. 31--				
%	**2019**	**2018**	**2017**	**2016**	**2015**
Tier 1 capital ratio	14.8	14.0	14.2	14.9	14.6
S&P Global Ratings' RAC ratio before diversification	9.4	8.4	7.3	6.7	6.9
S&P Global Ratings' RAC ratio after diversification	8.8	7.8	6.8	6.3	7.4
Adjusted common equity/total adjusted capital	89.7	89.8	93.9	100.0	100.0
Net interest income/operating revenues	60.8	63.4	63.8	68.7	75.3
Fee income/operating revenues	32.3	31.7	27.2	25.1	23.4
Market-sensitive income/operating revenues	3.0	0.8	5.9	0.7	(1.6)
Noninterest expenses/operating revenues	63.7	66.4	62.6	56.1	52.8
Preprovision operating income/average assets	0.6	0.5	0.6	0.7	0.8
Core earnings/average managed assets	0.2	0.2	0.3	0.3	0.4

RAC--Risk-adjusted capital.

Table 4

BFA Tenedora de Acciones, S.A.U. RACF [Risk-Adjusted Capital Framework] Data					
(Mil. €)	**Exposure***	**Basel III RWA**	**Average Basel III RW(%)**	**S&P Global RWA**	**Average S&P Global RW (%)**
Credit risk					
Government & central banks	87,805	9,341	11	6,830	8
Of which regional governments and local authorities	3,949	11	0	444	11
Institutions and CCPs	5,954	2,210	37	1,987	33
Corporate	37,826	18,987	50	34,041	90
Retail	78,901	27,678	35	39,265	50
Of which mortgage	61,260	18,665	30	22,414	37
Securitization§	487	275	56	1,044	214
Other assets†	19,004	7,358	39	34,480	181
Total credit risk	229,978	65,849	29	117,646	51
Credit valuation adjustment					
Total credit valuation adjustment	--	175	--	228	--
Market Risk					
Equity in the banking book	371	927	250	3,246	875
Trading book market risk	--	1,088	--	1,739	--
Total market risk	--	2,015	--	4,985	--
Operational risk					
Total operational risk	--	5,600	--	6,249	--

Table 4

BFA Tenedora de Acciones, S.A.U. RACF [Risk-Adjusted Capital Framework] Data (cont.)					
(Mil. €)	Exposure	Basel III RWA	Average Basel II RW (%)	S&P Global RWA	% of S&P Global RWA
Diversification adjustments					
RWA before diversification	--	77,551	--	129,108	100
Total Diversification/ Concentration Adjustments	--	--	--	9,134	7
RWA after diversification	--	77,551	--	138,242	107
(Mil. €)		**Tier 1 capital**	**Tier 1 ratio (%)**	**Total adjusted capital**	**S&P Global RAC ratio (%)**
Capital ratio					
Capital ratio before adjustments		12,376	16.0	12,190	9.4
Capital ratio after adjustments‡		12,376	15.8	12,190	8.8

*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 2019', S&P Global Ratings.

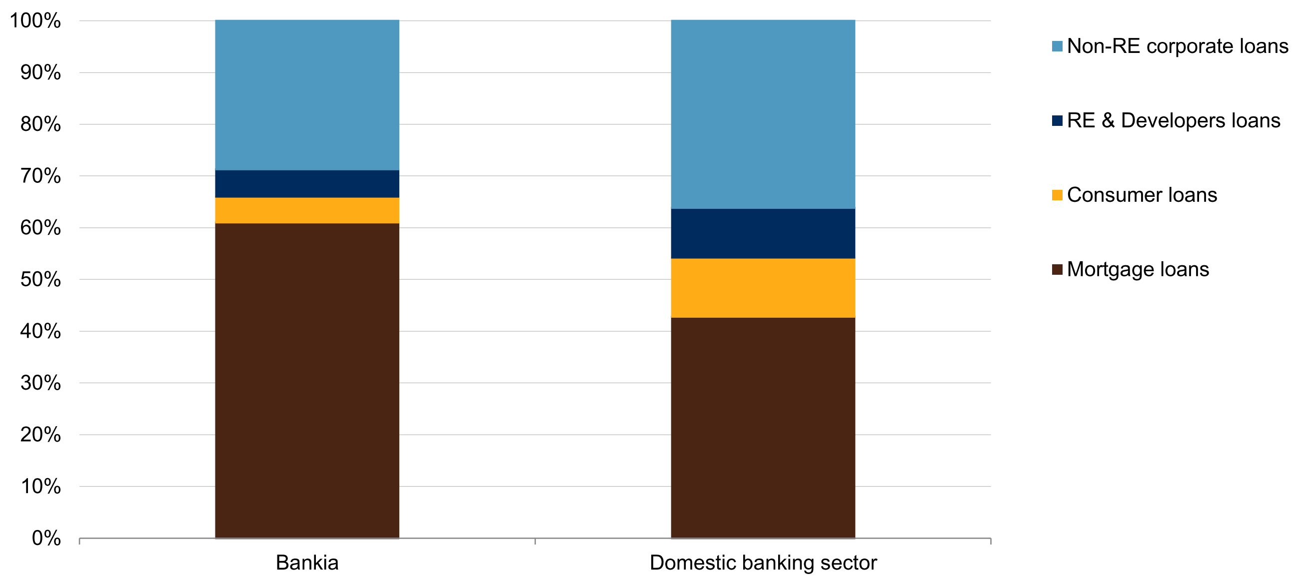
Risk position: Mortgage-focused and well-seasoned portfolio should help contain asset quality deterioration

Bankia's risk management has been completely revamped since its bail-out in 2012 and its credit risk culture has strengthened throughout the organization in what was a long and complex process. This positions the bank well to face the challenging environment ahead. In addition, we believe that the comparatively high weight of less risky mortgages in its loan book should result in lower asset quality deterioration when compared to other Spanish players that have a higher exposure to companies.

Amid the COVID-19 economic shock, we anticipate a reversal of Bankia's previously improving asset quality trend, as is the case for its peers. We forecast that its NPA ratio will increase to above 8.0% this year from an estimated 6.9% in 2019, before declining to below 7.0% by year-end 2022. We note positively that mortgage loans represent the bulk of Bankia's portfolio, accounting for 61% of total loans at end-2019, a segment that we anticipate will suffer less than corporate and consumer loans in the current environment. Bankia's exposure to sectors that we currently see as more vulnerable--such as tourism, real estate and construction, transportation, oil and gas, and services--is relevant, equivalent to about 13% of its total loan book at end-2019, but lower than our estimated average for the domestic banking sector.

Chart 4

Bankia's Exposure To Less Risky Mortgage Loans Is Well Above The Domestic Average
Loan book by segment, as of YE2019



Source: S&P Global Ratings.

On top of the relief measures established by the government to help households and businesses during the pandemic, Bankia, like many of its peers, is offering expanded solutions. These include 12-month moratoria on mortgage loans principal (compared to three-month moratoria established by the government) and six-month moratoria on consumer loans principal (versus three-month). At end-April 2020, about 3% of Bankia's mortgage loans customer base and 2% of its consumer loans customer base had requested to benefit from such moratoria. In addition, at end-April 2020, Bankia had received €7.3 billion in requests from companies (equivalent to 18% of its corporate loan book) for financing under the established government guarantee program. We anticipate an increasing amount of such requests over the coming months, which should partly mitigate the pressure on Bankia's profitability.

Despite our belief that Bankia will suffer a lower asset quality deterioration than some Spanish players, we note that it is entering this crisis with a still high stock of NPAs (€8.2 billion at the operating bank level at end-March 2020) and asset-quality metrics that are still behind those of its closest domestic competitors. Bankia has managed to derisk its balance sheet since end-2017, reducing gross NPAs by slightly more than 50% in the last two years, but it has followed a less aggressive approach than many peers so as to preserve higher value. Even if Bankia maintains satisfactory coverage ratios, with 49% coverage of NPAs at end-2019, we believe it will prove more challenging to accelerate a balance-sheet clean-up in the next two years.

As part of its current strategic plan, prior to the pandemic, Bankia was targeting to expand in the consumer segment. In fact, in January 2020, its new joint venture with Credit Agricole Consumer Finance started to operate, targeting to develop consumer credit service at points of sale, mostly with existing customers. We expect that Bankia will not loosen its underwriting standards, but we will continue to closely monitor any negative developments because we believe that the consumer finance segment is particularly vulnerable to the economic and credit distresses stemming from the COVID-19 pandemic, from both an asset-quality and a business-generation perspective.

We consider Bankia's single-name concentration to be manageable, with its top-20 largest exposures representing about 0.9x of TAC at end-2019.

Table 5

BFA Tenedora de Acciones, S.A.U.--Risk Position					
	--Year ended Dec. 31--				
%	**2019**	**2018**	**2017**	**2016**	**2015**
Growth in customer loans	(1.5)	(4.8)	16.8	(5.0)	(4.9)
Total diversification adjustment/S&P Global Ratings' RWA before diversification	7.1	7.9	7.2	6.7	(6.0)
Total managed assets/adjusted common equity (x)	19.3	18.9	18.9	18.5	20.4
New loan loss provisions/average customer loans	0.4	0.3	0.3	0.2	0.4
Net charge-offs/average customer loans	1.2	2.1	(0.0)	1.6	2.0
Gross nonperforming assets/customer loans + other real estate owned	4.9	6.3	8.8	9.8	10.7
Loan loss reserves/gross nonperforming assets	54.4	54.7	51.2	55.6	61.1

Funding and liquidity: Reduced reliance on short-term funding

Bankia benefits from an average funding profile like its domestic peers. In the past few years, the bank has successfully rebalanced its funding profile, mainly by deleveraging sharply. The bank's loan-to-deposit ratio as of end-2019 stood at 98%, down from 160% at year-end 2011, and its stable funding ratio at 99%, up from 81%.

Retail deposits remain Bankia's main funding source, representing about 65% of total funding at end-2019. Other funding sources include covered bonds, interbank deposits, and ECB funding. We note that Bankia recently started issuing senior instruments that are eligible to comply with its minimum requirement for own funds and eligible liabilities (MREL) 2024 requirement, and we expect further issuances next year. That said, we anticipate that Bankia's reliance on wholesale funding will remain within manageable levels. Upcoming wholesale maturities for this year and next amount to €2.3 billion, relating mostly to covered bonds. This represents 1.1% of total assets, which we view as manageable.

The bank's reliance on ECB funding amounted to €13.8 billion as of end-March 2020, representing 6.5% of total assets. Like its peers, Bankia has made use of this funding source for opportunistic purposes. The bank has the capacity to take additional TLTRO III funding of up to €9.2 billion, which we believe will be largely used, given its attractive terms. In addition, it has the capacity to issue a further €20 billion covered bonds, if needed.

Bankia's reliance on short-term funding has declined sharply in recent years, benefiting from a reducing commercial gap, enhanced access to longer term financing sources, and the disposal of legacy noncore assets. That said, we expect Bankia will continue financing the €18.5 billion portfolio of SAREB bonds (9% of assets) mostly with short-term sources. These bonds cannot be sold to third parties and have one-to-three-year maturities, but can be rolled over at SAREB's discretion until 2027.

We consider the level of short-term financing to be manageable, particularly as liquid assets more than fully cover potential short-term financing risks. We calculate Bankia's liquidity coverage ratio to be 1.1x, as of end-2019.

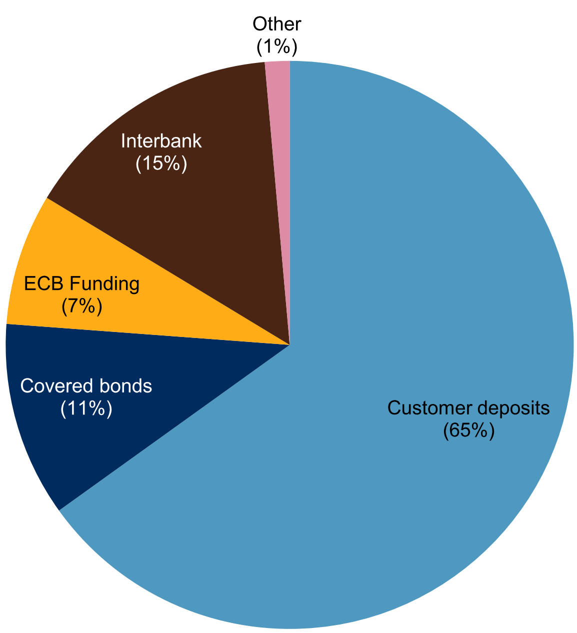
Table 6

BFA Tenedora de Acciones, S.A.U.--Funding And Liquidity

	--Year ended Dec. 31--				
%	**2019**	**2018**	**2017**	**2016**	**2015**
Core deposits/funding base	65.1	66.6	63.5	56.4	50.6
Customer loans (net)/customer deposits	98.3	98.5	102.1	110.8	119.2
Long-term funding ratio	86.7	89.7	86.8	86.5	71.0
Stable funding ratio	99.1	99.1	113.1	116.3	97.3
Short-term wholesale funding/funding base	14.5	11.2	14.3	14.6	31.3
Broad liquid assets/short-term wholesale funding (x)	1.1	1.2	1.9	2.0	1.0
Net broad liquid assets/short-term customer deposits	2.2	3.4	21.7	27.4	2.4
Short-term wholesale funding/total wholesale funding	40.6	32.9	38.8	33.4	63.4
Narrow liquid assets/3-month wholesale funding (x)	5.0	3.3	7.1	9.4	1.8

Chart 5

Retail Deposits Are Bankia's Main Funding Source
As of Dec. 2019



Source: S&P Global Ratings.

Support: No notches of uplift to the SACP.

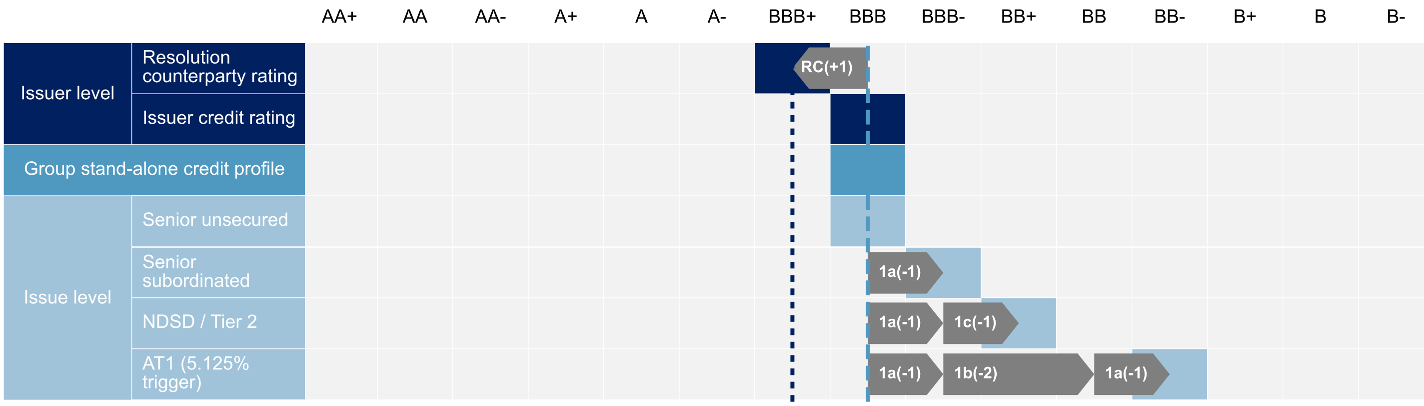
We do not include notches in the long-term rating on Bankia under our ALAC criteria because we believe that its ALAC ratio is unlikely to exceed our 5% threshold over our projection period. We consider that Bankia's ALAC ratio is likely to hover around 4.5% by year-end 2021. That said, such a buffer would decline by about 100 bps under heightened economic risks in Spain. In our calculation, we include common equity above the amount already incorporated in the SACP (which represents about 25% of our calculated ALAC for Bankia), outstanding ALAC-eligible hybrids, and other bail-in-able instruments that the bank is likely to complete in the coming years to comply with MREL regulation (in particular, outstanding AT1 instruments account for 20% of Bankia's ALAC; and senior nonpreferred and subordinated debt for slightly more than 25% each). We believe these issues have the capacity to absorb losses without triggering a default on senior obligations. As of end-March 2020, Bankia reported a 21.53% MREL ratio, compared to its required 23.66% of regulatory RWAs to be fulfilled by 2024.

Hybrid issue ratings

Our 'BB-' rating on Bankia's AT1 instruments and our 'BB+' rating on its Tier 2 subordinated instruments stand four and two notches below our 'bbb' SACP on the entity, respectively. We derive these gaps as follows:

- One notch for contractual subordination for both instruments, since Bankia is an investment-grade issuer.
- Two notches for the AT1 instrument to reflect the ability to defer coupon payments and its Tier 1 regulatory capital status.
- No notches for the Tier 2 subordinated instruments because coupon payments are nondeferrable.
- One notch for the AT1 instrument because it contains a contractual common equity conversion clause, and one notch for the Tier 2 instrument, given that it is a regulatory capital instrument and we believe that authorities could force its write down to absorb losses before the institution reaches the point of nonviability.

Bankia S.A: Notching



Key to notching

- - - - - Group stand-alone credit profile

------ Issuer credit rating

RC	Resolution counterpartyliabilities (senior secured debt)
1a	Contractual subordination
1b	Discretionary or mandatory nonpayment clause and whether the regulator classifies it as regulatory capital
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.
AT1--Additional Tier 1. NDSD--Non-deferrable subordinated debt.

Environmental, Social, And Governance (ESG)

We view exposure to ESG risks and opportunities for Bankia as broadly in line with those of the industry and Spanish peers. Management has largely rebuilt the bank's franchise and financial strength, both of which were hurt by its severe financial difficulties earlier in the decade and its subsequent nationalization. Like several banks in Europe and the U.S., Bankia has not been immune from governance problems. Its former CEO and several other directors and executives were accused of fraudulent activities by Spain's High Court. Some have received jail terms. We note that the entire board and management team were renewed in 2012 and therefore no longer affect Bankia's creditworthiness. Its governance and risk controls are now in line with the domestic peers. Although ultimately majority-owned by the Spanish government, the bank has always been managed independently. With its large retail franchise, Bankia is exposed to conduct risks. Some legacy events and legal cases have financially and reputationally affected the bank in the recent past, such as the misselling to retail customers of preference shares and subordinated debt, as well as equity shares at the time of the bank's IPO, and the inclusion of interest rate floors in some of its mortgages. Overall, we believe those cases reflect increasing consumer awareness and activism, but we do not consider Bankia to be more exposed to those risks than domestic peers' from a credit perspective. We believe the bank's exposure to environmental risk, essentially transition risks in the lending and investing activities, is manageable and in line with industry peers.

Resolution counterparty rating (RCR)

We set the resolution counterparty ratings (RCRs) on Bankia at 'BBB+/A-2', one notch above our long-term issuer credit rating on the entity. The RCR also reflects our jurisdiction assessment for Spain.

An RCR is a forward-looking opinion of the relative default risk of certain senior liabilities that may be protected from default through an effective bail-in resolution process for the issuing financial institutions. RCRs apply to issuers in jurisdictions where we assess the resolution regime to be effective and we consider the issuer likely to be subject to a resolution that entails a bail-in if it reaches nonviability.

Related Criteria

- General Criteria: Group Rating Methodology, July 1, 2019
- General Criteria: Hybrid Capital: Methodology And Assumptions, July 1, 2019
- Criteria | Financial Institutions | General: Methodology For Assigning Financial Institution Resolution Counterparty Ratings, April 19, 2018
- Criteria | Financial Institutions | General: Risk-Adjusted Capital Framework Methodology, July 20, 2017
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- Criteria | Financial Institutions | Banks: Bank Rating Methodology And Assumptions: Additional Loss-Absorbing Capacity, April 27, 2015
- Criteria | Financial Institutions | Banks: Quantitative Metrics For Rating Banks Globally: Methodology And Assumptions, July 17, 2013
- Criteria | Financial Institutions | Banks: Banking Industry Country Risk Assessment Methodology And Assumptions, Nov. 9, 2011
- Criteria | Financial Institutions | Banks: Banks: Rating Methodology And Assumptions, Nov. 9, 2011
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009
- Criteria | Financial Institutions | Banks: Commercial Paper I: Banks, March 23, 2004

Related Research

- Banking Risk Indicators: May 2020 Update, May 18, 2020
- Government Job Support Will Stem European Housing Market Price Falls, May 15, 2020
- Banking Industry Country Risk Assessment Update: April 2020, May 1, 2020
- Outlooks Revised To Negative On Several Spanish Banks On Deepening COVID-19 Downside Risks, April 29, 2020
- Spain-Based Bankia 'BBB/A-2' Ratings Affirmed Amid COVID-19 Risks; Outlook Remains Stable, April 29, 2020
- Credit Conditions In Europe Darken As Costs Of Lockdowns Add Up, April 27, 2020
- Europe's AT1 Market Faces The COVID-19 Test: Bend, Not Break, April 22, 2020

- How COVID-19 Is Affecting Bank Ratings, April 22, 2020
- Europe Braces For A Deeper Recession In 2020, April 20, 2020
- European Banks' First-Quarter Results: Many COVID-19 Questions, Few Conclusive Answers, April 1, 2020
- Full Analysis: Spain, March 20, 2020
- Spanish Banks: At A Crossroads, March 6, 2020

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 9, 2020)*

Bankia S.A.	
Issuer Credit Rating	BBB/Stable/A-2
Resolution Counterparty Rating	BBB+/--/A-2
Commercial Paper	A-2
Preferred Stock	BB-
Senior Secured	AA/Stable
Senior Subordinated	BBB-
Senior Unsecured	A-2
Short-Term Debt	A-2
Subordinated	BB+
Issuer Credit Ratings History	
06-Apr-2018	BBB/Stable/A-2
09-Feb-2017	BBB-/Positive/A-3
05-Apr-2016	BB+/Positive/B
02-Dec-2015	BB/Positive/B
Sovereign Rating	
Spain	A/Stable/A-1
Related Entities	
BFA Tenedora de Acciones, S.A.U.	
Issuer Credit Rating	BBB-/Stable/A-3

Ratings Detail (As Of June 9, 2020)*(cont.)

*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.