

Rating Action: Moody's downgrades Banco de Valencia's standalone ratings to E+/B2; confirms debt ratings at Ba2, outlook developing

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Madrid, December 02, 2011 – Moody's Investors Service has today downgraded Banco de Valencia's standalone bank financial strength rating (BFSR) to E+ from D-. The E+ standalone BFSR maps to B2 on the long-term scale. Moody's has also downgraded the bank's preference shares to Caa3 from Caa1. At the same time, Moody's has confirmed Banco de Valencia's senior debt and deposit ratings at Ba2. The short term rating remains at Not Prime. All of Banco de Valencia's ratings have a developing outlook, except the dated subordinated debt rated Ba3 which remains on review for downgrade.

Today's action concludes the rating review initiated on 28 October 2011. For further details please see "Moody's downgrades Banco de Valencia to Ba2; all ratings on review for downgrade".

RATINGS RATIONALE

DOWNGRADE OF BANCO DE VALENCIA'S BFSR

Moody's decision to downgrade Banco de Valencia's standalone BFSR to E+ from D-, reflects the material deterioration on the bank's credit profile due to (i) its fragile liquidity position with a continuously increasing funding deficit that is only covered by ECB and domestic public debt Repo funding and the EUR2 billion credit facility provided by the state-owned fund ("FROB", Fund for the Orderly Restructuring of the Banking System) and (ii) weak solvency indicators when compared to Moody's calculation of embedded expected losses in Banco de Valencia's balance sheet, despite the EUR1 billion capital injection committed by the FROB.

On 21 November 2011, Bank of Spain intervened in Banco de Valencia and instructed the FROB to take control of the bank, after having committed a capital injection into the bank up to EUR1 billion and a credit facility of EUR2 billion. The Bank of Spain's decision to intervene in Banco de Valencia was based on the bank's inability to immediately adopt a viable plan to raise needed capital. The capital shortfall was revealed after the Bank of Spain concluded an inspection on 17 November 2011 that resulted in additional provisioning requirements of at least EUR562 million.

Moody's believes that without the support provided by the Spanish government via the FROB, Banco de Valencia would not be able to face its sizable refinancing requirements over the next 12 months given its very weak liquidity position and lack of access to wholesale market financing. In addition, Moody's is concerned by the bank's very weak risk absorption capacity, with very weak solvency and profitability indicators, which has been severely affected by the rapid deterioration of its asset portfolio.

The FROB and Bank of Spain have announced their intention to recapitalise and stabilise Banco de Valencia with the ultimate aim of selling it through a competitive tender.

Moody's has assigned a developing outlook to the bank's BFSR to reflect the different rating implications for Banco de Valencia in case the sale process is completed or if the FROB fails to conclude it. By placing a developing outlook on Banco de Valencia's BFSR the rating agency notes the possibility (i) for the bank's rating to be upgraded if it is acquired by a stronger peer; (ii) of negative rating actions (including the potential for a multi-notch downgrade), if the resulting entity after the sale displays a weaker credit profile than Banco de Valencia's standalone financial strength; and (iii) of Banco de Valencia's standalone rating being downgraded if the sale process fails to succeed and the government weakens its current support for the bank.

DOWNGRADE OF THE PREFERENCE SHARES

At the same time, Moody's has also downgraded the preference shares to Caa3 from Caa1. The downgrade follows the downgrade of the bank's BFSR; these instruments continue to be rated four notches below the adjusted standalone rating as per Moody's methodology for Spanish hybrids.

CONFIRMATION OF BANCO DE VALENCIA'S SENIOR DEBT AND DEPOSIT RATINGS

In today's action Moody's has also confirmed Banco de Valencia's debt and deposit ratings at Ba2. Following the downgrade of the bank's BFSR, Moody's has broadened the uplift from its standalone rating to three notches, to reflect a high likelihood of the FROB to continue providing support to Banco de Valencia in terms of liquidity and capital until the sale process is completed.

Moody's does not incorporate any probability of parental support into its debt and deposit ratings from its parent Banco Financiero y de Ahorro (BFA; Ba2 negative outlook). Despite being the majority shareholder of Banco de Valencia with 38.6% of its capital, BFA has not provided any type of support to its subsidiary when this was now needed. Thus, Moody's also does not expect the entity to receive any future support from its legal owner nor from BFA's operating company Bankia (Baa2/D+ (mapping to Ba1 on the long-term scale)/Prime-2, negative).

The bank's debt and deposits ratings have a developing outlook reflecting the developing outlook of its standalone rating. In addition, Moody's notes that Banco de Valencia's debt ratings could be aligned with its standalone BFSR and therefore downgraded by several notches in case the government (via FROB) will provide any signal that it may weaken the support that is currently expected to be forthcoming for the bank in case of need.

BANCO DE VALENCIA'S DATED SUBORDINATED DEBT RATINGS

The ratings of Banco de Valencia's dated subordinated debt instruments remain at Ba3. These dated subordinated debt instruments continue to be rated one notch lower than the senior debt instruments, based on subordination in the case of liquidation. The ratings are on review for possible downgrade since 29 November 2011. For further details please see "Moody's reviews European banks' subordinated, junior and Tier 3 debt for downgrade".

POTENTIAL TRIGGERS OF A DOWNGRADE/UPGRADE

Downward pressure would be exerted on Banco de Valencia's standalone credit strength following (i) a further weakening of its liquidity position; (ii) greater-than-expected deterioration in its risk-absorption capacity and a depletion of its capital levels; and/or (iii) weakening of the bank's franchise.

The bank's debt and deposit ratings are linked to the standalone BFSR, and any change to the BFSR would likely also affect these ratings. In addition, downward pressure on Banco de Valencia's debt and deposit ratings could be exerted if the FROB fails to provide sufficient support to the bank in terms of liquidity and capital.

An improvement of Banco de Valencia's standalone rating could be driven by (i) its acquisition by a stronger peer; (ii) an improved liquidity position, with normalised access to wholesale funding and broader diversification of its funding sources; (iii) reduction of its real-estate and related assets; and (iv) enhanced access to capital.

METHODOLOGY

The methodologies used in this rating were Bank Financial Strength Ratings: Global Methodology published in February 2007, Incorporation of Joint-Default Analysis into Moody's Bank Ratings: A Refined Methodology published in March 2007, and Moody's Guidelines for Rating Bank Hybrid Securities and Subordinated Debt published in November 2009. Please see the Credit Policy page on www.moody.com for a copy of these methodologies.

Headquartered in Valencia (Spain), Banco de Valencia had EUR24 billion assets at end-June 2011.

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