

Fitch Ratings

Fitch Downgrades Caixa Galicia to 'BBB+'; Outlook Stable
13 Mar 2009

Fitch Ratings-London/Barcelona-13 March 2009: Fitch Ratings has today downgraded Caja de Ahorros de Galicia's (Caixa Galicia) Long-term Issuer Default rating (IDR) to 'BBB+' from 'A'. The Outlook on the IDR is Stable. The Short-term IDR was downgraded to 'F2' from 'F1' and the Individual rating to 'C' from 'B/C'.

At the same time, Fitch has affirmed Caixa Galicia's Support rating at '3' and Support Rating Floor at 'BB+'. Fitch has also downgraded Caixa Galicia's senior debt to 'BBB+' from 'A' and undated subordinated debt (upper tier 2) to 'BBB-' (BBB minus) from 'A-' (A minus). For Caixa Galicia's hybrid capital issues, the agency has also downgraded the outstanding preference shares to 'BB' from 'BBB+', in line with Fitch's criteria for rating capital instruments. Fitch's downgrade of preference shares reflects the agency's view that the risk of coupon deferral has increased.

The rating actions reflect the negative impact of the sharp ongoing adjustment in the Spanish economy and property sector on Caixa Galicia's asset quality and profitability, in the context of a tight capital base. Fitch recognises management's efforts to reduce risk concentration and manage liquidity, asset quality and capital levels, which have shown some tangible results. However, further improvement will prove challenging as a result of the deepening global financial crisis.

Caixa Galicia has been transforming its risk profile by selling equity stakes and has significantly reduced its risk concentration to single names since 2006. Its lending portfolio grew by a strong 35% annually in 2004-2007 and the exposure to the real estate and construction sectors continued to be high at end-2008 (28% of lending). The sharp deterioration in the Spanish economy and real estate sector will make it more difficult to transform these exposures into mortgages to individuals. In addition, unemployment and the number of real estate companies filing for creditor protection rose in 2008. As a result, the caja's impaired/total loans ratio weakened to 3.8% at end-2008 (55% loan loss coverage) and is expected to deteriorate further in 2009, although the caja's EUR171m generic reserves provide a buffer.

Caixa Galicia's 2008 net income declined 44% due to higher loan impairment charges, some of which were built in advance of requirements, and the impairment from some equity stakes. However, this was partly compensated at the bottom-line level through capital gains. Its cost/income ratio of 67% in 2008 was affected by higher costs from recent branch expansion, although management is addressing this issue.

Caixa Galicia is rebalancing its funding sources and reducing its reliance on short-term wholesale funds. At end-2008, customer deposits remained the caja's main source of funding (58% of total loans) and grew by a strong 16%, reflecting higher commercial efforts and its good franchise in its home region. While improving, its Tier 1 capital of 6.7% at end-2008 remained tight for its risk profile.

Caixa Galicia was Spain's 6th-largest savings bank by assets at end-2008, with a strong market share in the region of Galicia, although it also has a national franchise. Its activities are mostly retail/commercial banking.

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