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Summary:
Eurofidi Scpa

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Summary:

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Credit Rating: BBB+/Negative/A-2

Rationale

The counterparty credit ratings on Eurofidi Scpa--an Italian mutual credit guarantee company or "confidi"--balance its extensive use of credit risk mitigation instruments, adequate capital position, and strong business ties with major Italian banks against the deteriorating quality of its guarantee portfolio, uncapped loss exposure on certain guarantees, and modest financial performance.

The ratings also reflect the ownership of and recurring support that Eurofidi receives from the Italian Region of Piedmont (not rated) through holding company Finpiemonte Partecipazioni SpA--Eurofidi's main shareholder--given its role in implementing regional economic plans and supporting local small and midsize enterprises (SMEs). Because of its strong links with and importance to the Piedmont region, the ratings on Eurofidi incorporate one notch of uplift above the company's stand-alone creditworthiness.

With €4.7 billion in guarantees outstanding at year-end 2008, Eurofidi is the largest Italian confidi, and offers mutual guarantees to SMEs to facilitate bank lending to them. Eurofidi's home base is in Piedmont, where it maintains a close relationship with the regional government and taps SME development funds, though the company has also significantly expanded its guarantee business in neighboring regions, reducing geographic concentration. Although Standard & Poor's Ratings Services feels that continued growth outside of Piedmont could, over the longer term, potentially weaken the rationale for regional support, we consider this highly unlikely at present, especially given Eurofidi's role in supporting local enterprises during the current economic downturn.

Apart from Finpiemonte, Eurofidi's other major shareholders include leading domestic financial institutions--namely UniCredit SpA (A/Stable/A-1), Intesa Sanpaolo SpA (AA-/Negative/A-1+), and Banco Popolare Societa Cooperativa SCRL (A-/Negative/A-2)--which collectively own 25% of capital and to which the company extended over 80% of its guarantee stock on Sept. 30, 2008. Ties with these major banks represent fundamental business channels for Eurofidi, which also benefits from their credit management capabilities.

Eurofidi extensively employs risk mitigation instruments, such as counterguarantees and maximum loss caps, which significantly reduce its exposure to credit risks. Actual losses are covered annually by shareholder and regional funds, part of Eurofidi's capital base. Deterioration in asset quality indicators, paired with Eurofidi's uncapped exposure on certain guarantees, nevertheless raises the risk of higher losses in the coming year, potentially eroding available reserves and the company's now adequate capital position.

Financial performance remains modest, reflecting Eurofidi's nonprofit business mission and sustained cost growth. Capital metrics are currently adequate, having been supported through the completion of a shareholder-sponsored capital increase in 2007. Funding is based on equity and loan-loss-reserve-type liabilities.

Outlook

The negative outlook reflects the possibility that Standard & Poor's could lower the ratings in the event of a significant deterioration in Eurofidi's risk profile, namely a material increase in credit losses due to worsening guarantee quality, eroding, in turn, the company's capital base.

Eurofidi's maintenance of a close relationship with Piedmont remains important for the ratings. We are closely following the region's efforts to support Eurofidi during the current downturn, and understand that these measures include a capital injection by 2010. Piedmont has also established a regional counterguarantee fund, to which Eurofidi should be a main beneficiary. Any weakening of Eurofidi's relationship with the region, which we do not expect at this time, would place downward pressure on the ratings.

Standard & Poor's could revise the outlook on Eurofidi back to stable if the company proves able to adequately weather the worsening economic environment and related deterioration in its guarantee portfolio, limiting the financial impact of likely higher guarantee losses through risk mitigation instruments and shareholder and regional contributions, while maintaining an adequate capital base.

We continue to monitor Eurofidi's planned transition into a regulated financial intermediary, as well as the ongoing adaptation of its guarantee business to Basel II.

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