

07 May 2019 | Affirmation

## Fitch Affirms Credit Union Baywide at 'BB' After Merger; Outlook Stable

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Fitch Ratings-Sydney-07 May 2019: Fitch Ratings has affirmed the ratings of Credit Union Baywide (CUB) following its merger with three smaller New Zealand credit unions. A full list of rating actions is at the end of this rating action commentary.

The affirmation reflects Fitch's view that the merger process will not significantly impact CUB's credit profile in the short term. The merger should provide greater economies of scale and geographic diversification over the longer term, which in turn should support CUB's financial profile. CUB is the largest of the four merger partners (the others being Credit Union South, Aotearoa Credit Union, and Credit Union Central), accounting for 65% of the combined entity's NZD550 million asset base at 31 March 2019.

### KEY RATING DRIVERS

#### IDRS AND VIABILITY RATING

CUB's Issuer Default Ratings (IDR) and Viability Rating reflect its greater risk appetite relative to New Zealand banks and building societies, with a focus on growth and riskier target markets in higher loan/value mortgages and consumer lending. Fitch believes these loan classes are more susceptible to higher losses through an economic cycle relative to more traditional residential mortgages, which are the focus of larger domestic peers. CUB's risk controls are adequate for its size and consistent with its similarly sized peers.

The combined entity still has a modest franchise, reflected in a small system market share, meaning it is generally a price taker, which is unlikely to change. The merger is likely to weigh on profitability in 2019 due to integration and one-off costs but should support CUB's longer-term earnings and profitability through significant cost synergies.

CUB has experienced strong loan growth in recent years, which has resulted in a weakening of capitalisation. However, Fitch believes growth is likely to moderate as management focuses on the integration of multiple entities. CUB's capitalisation levels are above regulatory minimums but buffers are moderate. The credit union has limited sources of new capital beyond retained earnings due to its mutual structure.

Customer deposits are likely to remain the main source of funding for CUB, despite the merger providing access to a modest warehouse facility previously utilised by Credit Union South.

#### SUPPORT RATING AND SUPPORT RATING FLOOR

The Support Rating and Support Rating Floor of CUB reflect our view that while support from the New Zealand sovereign (AA/Stable) is possible, it cannot be relied on. The institutions are not part of the open bank resolution scheme (OBR), which allows for the imposition of losses on depositors and senior debt holders to recapitalise failed institutions. However, Fitch believes the existence of the OBR, in conjunction with the institution's low systemic importance, will make sovereign support unlikely.

#### RATING SENSITIVITIES

##### IDRS AND VIABILITY RATING

CUB's IDRs and Viability Rating would be sensitive to a change in its risk appetite. Ratings may be upgraded if there is a sustained improvement in risk appetite, possibly through improved underwriting standards, or a stronger control framework. A negative rating action would result from an increase in risk appetite. Ratings may also be downgraded if management focus is significantly diverted from the ongoing operations of the business during the integration process, leading to a sustained negative impact on CUB's financial profile.

#### SUPPORT RATING AND SUPPORT RATING FLOOR

The Support Rating and Support Rating Floor are sensitive to any change in assumptions around the propensity of the New Zealand government to provide timely support.

The rating actions are as follows:

Credit Union Baywide

Long-Term Foreign-Currency IDR affirmed at 'BB'; Outlook Stable

Short-Term Foreign-Currency IDR affirmed at 'B'

Long-Term Local-Currency IDR affirmed at 'BB'; Outlook Stable

Short-Term Local-Currency IDR affirmed at 'B'

Viability Rating affirmed at 'bb'

Support Rating affirmed at '5'

Support Rating Floor affirmed at 'No Floor'

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### **Applicable Criteria**

[Bank Rating Criteria \(pub. 12 Oct 2018\)](#)

[Short-Term Ratings Criteria \(pub. 02 May 2019\)](#)

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