

6. Counterparty credit risk

The counterparty credit risk translates the risk of counterparties being unable to meet their liabilities resulting from securities contracts such as derivatives for instance.

The Bank gives preference to the definition of exposure limits to counterparty credit risk, bilateral contracts to guarantee exposures resulting from derivatives and the creation of collaterals within the scope of these agreements as preferred tools to mitigate counterparty credit risk.

The manual Credit Regulations for Sovereigns and Financial Institutions defines the way in which the consumptions of the counterparty credit risk limits are determined. This calculation is regularly made based on the market value of the operations, to which a factor arising from the future potential variation of that same value is added, adjusting for the volatility and deadline of each operation.

The Bank has a policy of closing bilateral contracts to guarantee exposures resulting from OTC derivatives contracted with Banks under the ISDA Master Agreement (ISDA - International Swaps and Derivatives Association).

In addition, an ISDA Master Agreement may frame the creation of collateral using an annex or ISDA Credit Support Document. As a template for the Credit Support Document, the Bank chose the Credit Support Annexes (CSA) contracts to guarantee the constitution, by the entity with net values payable in the future, of financial collaterals from the other party to guarantee the payment of these contractual obligations. In these contracts, the Bank (almost exclusively) accepts deposits in Euros as collateral.

The Bank does not use netting as a technique for credit risk mitigation/reduction under RWA/capital requirements calculation; only in accounting, non-prudential terms, netting is used for interest rate swaps, per operation. The exception to this is the approved ISDA Master Netting Agreements (MNA) celebrated with 5 entities from the "Institutions" risk class that effectively provide prudential credit risk mitigation.

The total exposure limits for counterparties that are not financial institutions, in contracts subject to this type of risk, are generally divided into two components: one for traditional credit operations (financial and / or subscription) and another for treasury products.

Finally, the Bank uses a framework agreement model of TBMA/ISMA (The Bond Market Association/International Securities Market Association) within the scope of the repo operations it carries out. This framework agreement, the Global Master Repurchase Agreement (GMRA), defines the repo transactions between the parties and regulates the creation of the collateral that guarantees the exposure.

Both in 2020 and in 2019, for the purposes of measuring counterparty credit risk, the Group used the financial collateral comprehensive method, as established in article 223, Section 4, Chapter 4, Title II, Part III of the CRR, and the mark-to-market method to calculate the future exposure in the relevant positions with credit risk, as defined in article 274, Section 3, Chapter 6, Title II, Part III of the CRR.

After estimating the exposures as at 2020 and 2019, the own funds requirements were computed, on one hand, according to Chapter 2, Title II, Part III of the CRR, for risk scores and portfolios that followed the standardised approach, and, on the other hand, according to Chapter 3, Title II, Part III of the CRR, for the portfolios for which the Supervisor has authorised the IRB Approach.

According to the mark-to-market method, the necessary values to calculate the exposure in the relevant positions have two components: (i) the market value of each operation and (ii) the percentage of the nominal to be applied as an add-on to that market value.

The market values of the operations are directly collected from the Bank's front-end application (namely Kondor+), in which the management and evaluation of the operations is carried out, whilst the add-on values to be applied are directly identifiable in table I of paragraph c) of article 274, Section 3, Chapter 6, Title II, Part III of the CRR.

Regulation (EU) No. 648/2012 of the European Parliament and of the Council, of 4 July 2012, on OTC derivatives, central counterparties and trade repositories - commonly referred to as EMIR (European Markets Infrastructure Regulation) - has introduced legal obligations with the aim of improving post-trade transparency and reducing the risks associated with the derivatives market, in particular through the need to bring in a central counterparty or the adoption of risk mitigation techniques for derivatives not centrally cleared.

Considering the regulations applicable to its category, the Group became obliged to carry out the clearing of the OTC derivatives portfolio within the criteria defined by the EMIR, with a qualified CCP. This clearing obligation is, in a first stage, applicable to the simpler derivatives, namely, those relating to interest rate (IRS and FRA) and in the most common currencies (EUR, GBP, JPY, USD). Afterwards, there will be a phased extension of these obligations to a broader set of derivatives.

The Bank's negotiating policy for ISDA CSA clauses privileges bilateral conditions, without any terms associated with the counterparties' ratings. Moreover, after the implementation of the last phase of EMIR, the conditions defined for OTC collateral contracts cannot be linked to credit ratings. In this context, there is currently no relation between the collateral requirements for OTC derivatives and the rating of the Bank.

As at December 2020, the Group did not have any formal counterparty credit risk coverage operation in force.

The next tables present further details on the exposures to counterparty credit risk.

TABLE 55 – TEMPLATE 25 / EU CCR1 – ANALYSIS OF CCR EXPOSURE BY APPROACH

31/12/2020

(Thousand euros)

	Notional	Replacement cost / Current market value	Potential future credit exposure	EEPE	Multiplier	EAD post CRM	RWA
Mark to market		245,744	112,683			327,102	253,210
Original exposure							
Standardised approach							
Internal Model Method - IMM (for derivatives and SFTs)							
Of which: securities financing transactions							
Of which: derivatives and long settlements transactions							
Of which: from contractual cross-product netting							
Financial collateral simple method (for SFTs)							
Financial collateral comprehensive method (for SFTs)							
VaR (Value at risk) for SFTs							
TOTAL							253,210

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(Thousand euros)

	Notional	Replacement cost / Current market value	Potential future credit exposure	EEPE	Multiplier	EAD post CRM	RWA
Mark to market		299,953	189,675			451,859	294,679
Original exposure							
Standardised approach							
Internal Model Method - IMM (for derivatives and SFTs)							
Of which: securities financing transactions							
Of which: derivatives and long settlements transactions							
Of which: from contractual cross-product netting							
Financial collateral simple method (for SFTs)							
Financial collateral comprehensive method (for SFTs)							
VaR (Value at risk) for SFTs							
TOTAL							294,679

TABLE 56 – TEMPLATE 26 / EU CCR2 – CVA CAPITAL CHARGE

(Thousand euros)

	31 Dec 2020		30 Jun 2019	
	Exposure value	RWA	Exposure value	RWA
Total portfolios subject to the advanced method				
(i) VaR component (including the 3x multiplier)				
(ii) SVaR component (including the 3x multiplier)				
All portfolios subject to the standardised method	142,112	73,141	236,008	95,337
Based on the original exposure method				
TOTAL SUBJECT TO THE CVA CAPITAL CHARGE	142,112	73,141	236,008	95,337

TABLE 57 – TEMPLATE 27 / EU CCR8 – EXPOSURES TO CCP

(Thousand euros)

	EAD post CRM	RWA
EXPOSURES TO QCCP (TOTAL)		5,716
Exposures for trades at QCCP (excluding initial margin and default fund contributions); of which:		
(i) OTC derivatives	285,803	5,716
(ii) Exchange-traded derivatives		
(iii) SFT		
(iv) Netting sets where cross-product netting has been approved		
Segregated initial margin	286,532	
Non-segregated initial margin		
Prefunded default fund contributions		
Alternative calculation of own funds requirements for exposures		
EXPOSURES TO NON-QCCP (TOTAL)		
Exposures for trades at non-QCCP (excluding initial margin and default fund contributions); of which:		
(i) OTC derivatives	-	-
(ii) Exchange-traded derivatives		
(iii) SFT		
(iv) Netting sets where cross-product netting has been approved		
Segregated initial margin		
Non-segregated initial margin		
Prefunded default fund contributions		
Unfunded default fund contributions		

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(Thousand euros)

	EAD post CRM	RWA
EXPOSURES TO QCCP (TOTAL)		
Exposures for trades at QCCP (excluding initial margin and default fund contributions); of which:		
(i) OTC derivatives	351,972	7,039
(ii) Exchange-traded derivatives		
(iii) SFT		
(iv) Netting sets where cross-product netting has been approved		
Segregated initial margin	286,368	
Non-segregated initial margin		
Prefunded default fund contributions		
Alternative calculation of own funds requirements for exposures		
EXPOSURES TO NON-QCCP (TOTAL)		
Exposures for trades at non-QCCP (excluding initial margin and default fund contributions); of which:		
(i) OTC derivatives	31,540	15,640
(ii) Exchange-traded derivatives		
(iii) SFT		
(iv) Netting sets where cross-product netting has been approved		
Segregated initial margin	225	
Non-segregated initial margin		
Prefunded default fund contributions		
Unfunded default fund contributions		

TABLE 58 – TEMPLATE 28 / EU CCR3 – STANDARDISED APPROACH – CCR EXPOSURES BY REGULATORY PORTFOLIO AND RISK

(Thousand euros)

	Dec 2020													
Exposure classes	Risk weight											Total	Of which unrated	
	0%	2%	4%	10%	20%	50%	70%	75%	100%	150%	Others			
Central governments or central banks	5 900												5 900	
Regional government or local authorities														
Public sector entities					0								0	
Multilateral development banks														
International organizations														
Institutions					82 632	18 510			116		285 803		387 060	65 817
Corporates									82 901				82 901	82 901
Retail								57					57	
Institutions and corporates with a short-term credit assessment														
Other elements														
TOTAL	5 900				82 632	18 510		57	83 017		285 803		475 919	148 718

	Jun 2020													
Exposure classes	Risk weight											Total	Of which unrated	
	0%	2%	4%	10%	20%	50%	70%	75%	100%	150%	Others			
Central governments or central banks	7 168												7 168	
Regional government or local authorities														
Public sector entities					1								1	
Multilateral development banks														
International organizations														
Institutions		351 972			152 347	86 654			1 530				592 503	141 091
Corporates									82 349				82 349	82 349
Retail								35					35	
Institutions and corporates with a short-term credit assessment														
Other elements														
TOTAL	7 168	351 972			152 347	86 654		35	83 879				682 056	223 440

TABLE 59 – TEMPLATE 29 / EU CCR4 (I) – IRB APPROACH – CCR EXPOSURES BY PORTFOLIO AND PD SCALE - CORPORATES

31/12/2020		(Thousand euros)						
	PD scale	EAD post CRM	Average PD	Number of obligors	Average LGD	Average maturity	RWA	RWA density
CORPORATE	0.01% to 0.05%							
	0.05% to 0.07%							
	0.07% to 0.14%	18	0.10%	1	42.26%	365	3	18.6%
	0.14% to 0.28%	479	0.20%	2	42.26%	1,181	241	50.4%
	0.28% to 0.53%							
	0.53% to 0.95%	8,646	0.70%	4	42.26%	1,685	9,160	105.9%
	0.95% to 1.73%	25	1.30%	1	42.26%	365	20	81.3%
	1.73% to 2.92%	3,977	2.30%	5	42.26%	825	4,605	115.8%
	2.92% to 4.67%	891	3.70%	4	42.26%	365	1,047	117.5%
	4.67% to 7.00%	2,155	5.90%	4	42.26%	545	3,146	146.0%
	7.00% to 9.77%							
	9.77% to 13.61%							
	13.61% to 100.00%							
	100.00% (default)							
	SUBTOTAL	16,190	1.94%	21	42.26%	1,231	18,224	112.6%
SME	0.01% to 0.05%							
	0.05% to 0.07%							
	0.07% to 0.14%							
	0.14% to 0.28%	23	0.20%	3	41.38%	365	4	18.6%
	0.28% to 0.53%	15	0.40%	2	43.74%	365	4	29.5%
	0.53% to 0.95%	81	0.70%	2	44.36%	365	37	46.5%
	0.95% to 1.73%	87	1.30%	6	39.85%	404	41	47.0%
	1.73% to 2.92%	99	2.30%	4	38.66%	428	61	61.2%
	2.92% to 4.67%	224	3.70%	6	43.96%	365	164	73.1%
	4.67% to 7.00%	11	5.90%	3	40.96%	365	9	86.7%
	7.00% to 9.77%	94	8.30%	2	44.40%	490	105	111.2%
	9.77% to 13.61%	287	11.50%	7	43.02%	365	356	124.0%
	13.61% to 100.00%							
	100.00% (default)							
	SUBTOTAL	921	11.50%	35	43.02%	365	782	84.91%
TOTAL		17,110	-	56	-	-	19,005	111.1%

NOTE: This data does not include the Specialised Lending exposures.

30/06/2020		(Thousand euros)						
	PD scale	EAD post CRM	Average PD	Number of obligors	Average LGD	Average maturity	RWA	RWA density
CORPORATE	0.01% to 0.05%							
	0.05% to 0.07%							
	0.07% to 0.14%							
	0.14% to 0.28%	311	0.20%	2	42.26%	1,379	173	55.4%
	0.28% to 0.53%							
	0.53% to 0.95%	134	0.70%	3	42.26%	365	83	61.8%
	0.95% to 1.73%	1,263	1.30%	2	42.26%	365	1,028	81.3%
	1.73% to 2.92%	3,936	2.30%	4	42.26%	1,050	4,863	123.5%
	2.92% to 4.67%	161	3.70%	4	42.26%	365	189	117.5%
	4.67% to 7.00%	1,724	5.90%	2	42.26%	767	2,642	153.2%
	7.00% to 9.77%	126	8.30%	1	42.26%	365	204	161.8%
	9.77% to 13.61%							
	13.61% to 100.00%							
	100.00% (default)							
	SUBTOTAL	7,656	2.96%	18	42.26%	849	9,181	119.9%

SME	0.01% to 0.05%							
	0.05% to 0.07%							
	0.07% to 0.14%							
	0.14% to 0.28%	29	0.20%	6	42.46%	365	6	19.3%
	0.28% to 0.53%	29	0.40%	2	39.05%	365	11	36.4%
	0.53% to 0.95%	5	0.70%	3	38.66%	365	3	55.4%
	0.95% to 1.73%	41	1.30%	7	38.69%	586	20	50.3%
	1.73% to 2.92%	174	2.30%	6	39.58%	365	142	81.7%
	2.92% to 4.67%	39	3.70%	4	43.18%	372	27	69.9%
	4.67% to 7.00%	16	5.90%	2	43.68%	365	15	89.4%
	7.00% to 9.77%	135	8.30%	4	44.40%	589	177	131.1%
	9.77% to 13.61%	89	11.50%	8	42.85%	365	113	126.3%
	13.61% to 100.00%							
	100.00% (default)							
SUBTOTAL		557	11.50%	42	42.85%	365	514	92.13%
TOTAL		8,214	-	60	-	-	9,695	118.0%

NOTE: This data does not include the Specialised Lending exposures.

TABLE 60 – TEMPLATE 29 / EU CCR4 (II) – IRB APPROACH – CCR EXPOSURES BY PORTFOLIO AND PD SCALE - RETAIL

31/12/2020

(Thousand euros)

	PD scale	EAD post CRM	Average PD	Number of obligors	Average LGD	Average maturity	RWA	RWA density
OTHER RETAIL - SME	0.01% to 0.05%							
	0.05% to 0.07%							
	0.07% to 0.14%							
	0.14% to 0.28%	2	0.20%	1	45.18%		0	14.8%
	0.28% to 0.53%	43	0.40%	4	32.18%		7	16.4%
	0.53% to 0.95%	4	0.70%	1	22.44%		1	15.6%
	0.95% to 1.73%							
	1.73% to 2.92%							
	2.92% to 4.67%							
	4.67% to 7.00%							
	7.00% to 9.77%							
	9.77% to 13.61%	403	11.50%	3	61.65%		354	87.8%
	13.61% to 100.00%							
	100.00% (default)							
SUBTOTAL		453	10.29%	9	58.39%		362	79.98%
OTHER RETAIL - NON SME	0.01% to 0.05%							
	0.05% to 0.07%							
	0.07% to 0.14%							
	0.14% to 0.28%							
	0.28% to 0.53%							
	0.53% to 0.95%							
	0.95% to 1.73%							
	1.73% to 2.92%							
	2.92% to 4.67%							
	4.67% to 7.00%							
	7.00% to 9.77%							
	9.77% to 13.61%	423	11.50%	1	44.05%		348	82.3%
	13.61% to 100.00%							
	100.00% (default)							
SUBTOTAL		423	10.29%	1			348	82.3%
TOTAL		453	10.29%	9	58.39%		362	80.0%

NOTE: This data does not include the Specialised Lending exposures.

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(Thousand euros))

	PD scale	EAD post CRM	Average PD	Number of obligors	Average LGD	Average maturity	RWA	RWA density
OTHER RETAIL - SME	0.01% to 0.05%							
	0.05% to 0.07%							
	0.07% to 0.14%							
	0.14% to 0.28%	7	0.20%	3	43.10%		1	14.1%
	0.28% to 0.53%							
	0.53% to 0.95%			1				
	0.95% to 1.73%	2	1.30%	3	85.66%		2	78.1%
	1.73% to 2.92%							
	2.92% to 4.67%	1	3.70%	1	43.17%		0	50.0%
	4.67% to 7.00%							
	7.00% to 9.77%	0	8.30%	2	21.75%		0	28.0%
	9.77% to 13.61%	443	11.50%	3	61.81%		390	88.0%
	13.61% to 100.00%							
	100.00% (default)							
	SUBTOTAL	454		13			394	86.79%
OTHER RETAIL - NON SME	0.01% to 0.05%							
	0.05% to 0.07%							
	0.07% to 0.14%							
	0.14% to 0.28%							
	0.28% to 0.53%							
	0.53% to 0.95%							
	0.95% to 1.73%							
	1.73% to 2.92%							
	2.92% to 4.67%							
	4.67% to 7.00%							
	7.00% to 9.77%							
	9.77% to 13.61%							
	13.61% to 100.00%							
	100.00% (default)							
	SUBTOTAL							
TOTAL		454		13			394	86.8%

NOTE: This data does not include the Specialised Lending exposures,

TABLE 61 – TEMPLATE 31 / EU CCR5-A – IMPACT OF NETTING AND COLLATERAL HELD ON EXPOSURE VALUES

31/12/2020

(Thousand euros)

	Gross positive fair value or net carrying amount	Netting benefits	Netted current credit exposure	Collateral held	Net credit exposure
Derivatives	389,965	29,592	360,373	39,704	322,801
Value of collateral held without impact				2,131	
SFT					
Cross-product netting					
TOTAL	389,965	29,592	360,373	39,704	322,801

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(Thousand euros)

	Gross positive fair value or net carrying amount	Netting benefits	Netted current credit exposure	Collateral held	Net credit exposure
Derivatives	453,205	47,243	405,962	66,121	368,372
Value of collateral held without impact				28,530	
SFT					
Cross-product netting					
TOTAL	453,205	47,243	405,962	66,121	368,372

TABLE 62 – TEMPLATE 32 / EU CCR5-B – COMPOSITION OF COLLATERAL FOR EXPOSURES TO CCR

31/12/2020

(Thousand euros)

	Collateral used in derivatives transactions				Collateral used in SFTs	
	Fair value of collateral received		Fair value of posted collateral		Fair value of collateral received	Fair value of posted collateral
	Segregated	Unsegregated	Segregated	Unsegregated		
Cash	0	25,049	286,532	288,449	0	0
Other assets			0			
TOTAL	0	25,049	286,532	288,449	0	0

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(Thousand euros)

	Collateral used in derivatives transactions				Collateral used in SFTs	
	Fair value of collateral received		Fair value of posted collateral		Fair value of collateral received	Fair value of posted collateral
	Segregated	Unsegregated	Segregated	Unsegregated		
Cash	0	18,303	286,593	285,338	0	0
Other assets			0			
TOTAL	0	18,303	286,593	285,338	0	0

TABLE 63 – TEMPLATE 33 / EU CCR6 – CREDIT DERIVATIVES EXPOSURES

31/12/2020	(Thousand euros)		
	Credit derivative hedges		Other credit derivatives
	Protection bought	Protection sold	
NOTIONAL			
Credit default swaps		275,720	
Total return swaps			
Credit linked notes			
Other credit derivatives			
TOTAL NOTIONAL		275,720	
FAIR VALUES			
Positive fair value (asset)		261,729	
Negative fair value (liability)			

30/06/2020	(Thousand euros)		
	Credit derivative hedges		Other credit derivatives
	Protection bought	Protection sold	
NOTIONAL			
Credit default swaps		278,624	
Total return swaps			
Credit linked notes			
Other credit derivatives			
TOTAL NOTIONAL		278,624	
FAIR VALUES			
Positive fair value (asset)		266,366	
Negative fair value (liability)			

6.1. Wrong way risk

The Wrong Way risk corresponds to the risk of a given exposure being negatively correlated with the counterparty's credit risk. Within credit granting this risk stems from the correlation between the collateral value and the credit worthiness of the borrower, i.e., when the deterioration of the credit risk of the latter leads to a devaluation of the collateral.

Similarly, in the case of derivative and repo transactions, this translates to the risk associated with the fact that the exposure at risk is adversely impacted by the credit quality of the counterparty.

Overall, the Bank considers this risk as immaterial, considering the composition of financial collateral. In terms of credit granted, the borrower's own securities (shares or bonds) represents a very small percentage of the total amount of credit, corresponding mainly to structured finance, including Project Finance, where the usual pledge of shares from the companies or vehicles is part of a comprehensive guarantees' package. Indeed, almost all the credits that have a securities' pledge have additional collateral to secure the exposure.

In the case of derivative and repo operations, in which the Bank mitigates counterparty credit risk through ISDA contracts with CSA, the coverage of market receivables is exclusively made through deposits at the Group itself; hence, wrong-way risk does not apply. In terms of credit default derivatives (CDS or TRS) or other guarantees provided by counterparties, the Bank is also not subject to material wrong-way risk, as the risk covered is not positively correlated with the protection provider.

It should also be noted that, in the ICAAP 2020, this risk was not considered material, within the scope of the assessment carried out.