Santander Consumer Bank AG (/gws/en/esp/issr/88386330)

Fitch Affirms Santander Consumer Bank AG at 'A-'; Outlook Stable

Fitch Ratings-London-28 July 2017: Fitch Ratings has affirmed Santander Consumer Bank AG's (SCB AG) Long-Term Issuer Default Rating (IDR) at 'A-' and Short-Term IDR at 'F2'. The Outlook is Stable. Fitch has also affirmed SCB AG's Viability Rating (VR) at 'a-'. A full list of rating actions is at the end of this rating action commentary.

KEY RATING DRIVERS
IDRS, VR AND SUPPORT RATING
The IDRs are driven by the standalone strength of SCB AG as captured in its Viability Rating (VR), and by institutional support.

We believe that, if needed, SCB AG would benefit from strong support from its ultimate parent, Banco Santander, S.A. (Santander, A-/Stable/F2/a-). As Santander's main operating subsidiary in Germany, SCB AG is deeply integrated within the operations of its intermediate parent Santander Consumer Finance, S.A. (SCF, A-/Stable/F2/bbb+). The VR reflects SCB AG's solid business model and franchise in Germany, which result in strong pricing power and adequate risk pricing, and considerable flexibility to mitigate the earnings pressure arising from a low interest-rate environment.

Our assessment of SCB AG's business model also reflects our expectation that the bank's mortgage and SME lending businesses will continue to grow gradually, in turn increasing revenue diversification, but eroding the bank's return on assets. We expect that consumer finance will continue to dominate the bank's business and drive the bank's strong performance and resilient financial profile. As a result, we expect profitability to remain strong in the foreseeable future, even if Germany's operating environment starts to deteriorate slightly, which is not our base case.

SCB AG's funding consists primarily of retail deposits, and liquidity is robust. Funding is independent of Santander and has been significantly diversified since 2014 by scaling up origination of retained auto and consumer ABS, which the bank used as collateral to access the European Central Bank's (ECB) targeted longer-term refinancing operations (TLTRO) in 2016. Its large pool of unencumbered ECB-eligible secured loans provides funding flexibility. Further moderate diversification will be achieved in the medium term by issuing mortgage Pfandbriefe. We believe the high asset margins and established franchise of SCB AG in the large German retail deposit market, despite its low market share, would enable the bank to collect sufficient deposits by raising deposit remuneration should additional liquidity needs arise.

SCB AG's capitalisation is robust but should be assessed in the context of a control and profit transfer agreement (CPTA) that obliges SCB AG to transfer its entire net income to its immediate parent, Santander Consumer Holding GmbH (SCH), a German-based holding company. This could create a reliance on capital injections from Santander, should SCB AG resume significant loan growth.

SCB AG's IDRs also reflect our view that Santander has a high propensity to provide both ordinary and extraordinary support if needed, given the shared brand name and SCB AG's deep integration within SCF and, ultimately, Santander's organisation and systems. SCB AG accounts for the largest share (about 40%) of SCF's consolidated loan portfolio, and Santander has publicly defined consumer finance as one of its 10 core markets. In addition, several capital injections from Santander in recent years to support SCB AG's organic and external growth support our view that Santander's willingness to support its subsidiary is strong.

SCB AG's Support Rating reflects Santander's strong ability to provide support directly or via SCF if needed. We assess this ability through Santander's and SCF's Long-Term IDRs as well as SCB AG's modest size relative to Santander's. Therefore, we equalise SCB AG's IDRs with those of Santander and SCF.

The CPTA prevents SCB AG from generating internal capital despite its strong performance. In light of SCH's limited resources, this is likely to make SCB AG reliant on capital re-injections from Santander/SCF to compensate it for any potential large annual losses or to support significant loan growth. Therefore, SCB AG's IDRs are likely to be capped by those of Santander.

SCB AG's 'F2' Short-Term IDR is the lower of two possible Short-Term IDRs for an 'A-' rated bank because we do not consider funding and liquidity a particular strength for the bank.

SENIOR NON-PREFERRED DEBT RATINGS
The programme ratings are driven by and equalised with SCB AG's IDRs. Fitch views that the likelihood of default on senior unsecured notes under this programme would reflect the likelihood of default of the bank.

DCR AND DEPOSIT RATINGS
Due to its retail deposits and ABS-driven funding mix, the buffer of junior and vanilla senior debt at SCB AG is very small at about 2% of risk-weighted assets and does not provide material incremental probability of default protection to derivative counterparties or depositors or provide comfort that recoveries in a default scenario would be above average. Therefore, the bank's DCR and Deposit Ratings are equalised with the bank's IDRs.

RATING SENSITIVITIES
IDRS, VR AND SUPPORT RATING
SCB AG's IDRs are primarily sensitive to a change of Santander's or SCF's IDRs or to a weaker propensity of institutional support from the parent. The latter could be signalled, for example, by the sale of a significant stake in SCB AG or if we otherwise believe that Santander no longer views SCB AG as a core entity. SCB AG's IDRs would only be downgraded if the VR is also downgraded. Our assessment of SCB AG's capitalisation incorporates strong ordinary support from the parent because of the presence of the CPTA, which means that a downgrade of its parents' IDRs would likely lead to a downgrade of SCB AG's VR.

An upgrade of SCB AG's VR would require major revenue diversification and sustainable strengthening of the bank's standalone capital and liquidity buffers. A downgrade of the VR could result from excessive growth, a failure to maintain an adequate risk-return profile in mortgage and SME lending, strong margin pressure in consumer finance, severe deterioration of German households' creditworthiness triggering significant asset quality pressure or sharp capital erosion due to insufficient re-injections from Santander, or if we conclude that Santander's ability to provide capital has weakened.

SENIOR NON-PREFERRED DEBT RATINGS
The ratings are primarily sensitive to changes in SCB AG's IDRs.

DCR AND DEPOSIT RATINGS
SCB AG's DCR and Deposit Ratings are primarily sensitive to changes in the bank's IDRs. In addition, we could notch the DCR and Deposit Ratings above the IDRs if the bank increases its qualifying junior and vanilla senior debt buffers to an extent sufficient to restore viability and prevent a default on its derivative obligations and deposits after a failure of the bank.

The DCR and Deposit Ratings are also sensitive to future changes to Germany's resolution regime, which may alter the hierarchy of the various instruments in resolution, although this is not our expectation.

The rating actions are as follows:

Long-Term IDR affirmed at 'A-'; Outlook Stable
Short-Term IDR affirmed at 'F2'
Viability Rating affirmed at 'a-'
Support Rating affirmed at '1'
Derivative Counterparty Rating affirmed at 'A-(dcr)'
Deposit Ratings affirmed at 'A-'/'F2'
Senior unsecured debt issuance programme affirmed at 'A-'/'F2'

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Applicable Criteria
Global Bank Rating Criteria (pub. 25 Nov 2016) (https://www.fitchratings.com/site/re/891051)

Additional Disclosures
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