FitchRatings

Banks
Retail & Consumer Banks
Germany

Santander Consumer Bank AG

Update

Key Rating Drivers

Support and VR Drive IDRs: Santander Consumer Bank AG's (SCB AG) Issuer Default Ratings (IDRs) are driven by its Viability Rating (VR) and by Fitch Ratings' view of the strong support available from its ultimate parent Banco Santander, S.A. (Santander; A-/Stable), potentially channelled via SCB AG's intermediate parent Santander Consumer Finance SA (SCF; A-/Stable). We revised the Outlook on SCB AG's IDR in June 2021 to mirror the revision of Santander's Outlook and our view that SCB AG's VR offers sufficient headroom to navigate the pandemic.

Solid Standalone Profile: SCB AG's VR reflects the bank's leading German car and consumer financing franchise, which dominates its business model, earnings and risk profile. The VR also factors in modest diversification into mortgage and SME lending. In June 2021, we revised to stable from negative the outlooks on the profitability and asset-quality scores, which we now expect to be resilient to plausible downside scenarios in light of the economic recovery.

Deep Integration Underpins Support: We view Santander's propensity and ability to support SCB AG as high, due to SCB AG's deep integration, shared brand name and small size relative to the group. Car financing and unsecured consumer finance are core business lines for the group. We expect Santander to increase SCB AG's capital to support organic growth and acquisitions whenever needed, as in the past.

Profit Resilient to Pandemic: Sound consumer finance margins and cost efficiency underpinned SCB AG's solid operating profit/risk-weighted assets (RWAs) in 2020. This was despite loan impairment charges (LICs) rising by 270%, largely driven by actual defaults rather than management overlays. We expect moderately stronger profits but still material LICs in 2021 despite subdued demand in the overall German consumer finance market due to the pandemic.

Robust Asset Quality: Ample support from the German government has mitigated the impact of the pandemic on SCB AG's loan quality, as at peers. We expect non-performing loans (NPLs) to rise moderately in the short term as state support measures recede and the effects of the crisis become more apparent. However, we believe SCB AG's four-year-average NPL ratio (1.8% at end-2020 based on our calculation) will remain close to 2% in the medium term.

Adequate Capitalisation: Our assessment of SCB AG's capitalisation includes ordinary group support as the bank relies on capital injections from the group to back significant loan growth or acquisitions. The bank usually does not generate capital as it upstreams its full annual profits to its German intermediate parent based on a control-and-profit transfer agreement. However, SCB AG has some flexibility to retain some of its profits as part of the group's capital planning.

Increasingly Diverse Funding: Granular retail deposits will remain SCB AG's main funding source despite its increasing use of bond and ECB financing. Its large stock of auto and consumer loans enables flexible management of liquid assets, which consist of ECB-eligible retained ABS.

Rating Sensitivities

Weaker Group Support: SCB AG's IDRs are primarily sensitive to changes in Santander's ability to support, as reflected in its IDRs. A downgrade of Santander's IDRs would be likely to trigger a downgrade of SCB AG's VR, which benefits from ordinary group support. The sale of a large stake in SCB AG, or a decline in its strategic importance for Santander could reduce the group's propensity to support its subsidiary. However, we view these scenarios as highly unlikely.

Unexpectedly High Credit Losses: We could downgrade the VR if the economic disruption caused by the pandemic intensifies, making a swift economic recovery less likely, potentially weakening revenues and driving credit losses significantly above our base-case expectations.

Ratings

Foreign Currency	
Long-Term IDR	A-
Short-Term IDR	F2
Derivative Counterparty Rating	A(dcr)
Viability Rating	a-
Support Rating	1
Sovereign Risk	
Long-Term Foreign-Currency IDR	AAA
Long-Term Local-Currency IDR	AAA
Country Ceiling	AAA

Outlooks

Long-Term Foreign-Currency IDR	Stable
Sovereign Long-Term Foreign-Currency IDR	Stable
Sovereign Long-Term Local-Currency IDR	Stable

Applicable Criteria

Bank Rating Criteria (February 2020)

Related Research

Fitch Revises Santander's Outlook to Stable; Affirms IDR at 'A-' (June 2021)

Santander Consumer Bank AG (June 2021)

Global Economic Outlook (June 2021)

German Banks' Profits to Be Hit by Customer Fee Reimbursement (June 2021)

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Debt Rating Classes

Rating Level	Rating
Deposit ratings	A/F1
Senior preferred (SP)	A/F1
Senior non-preferred (SNP)	A-

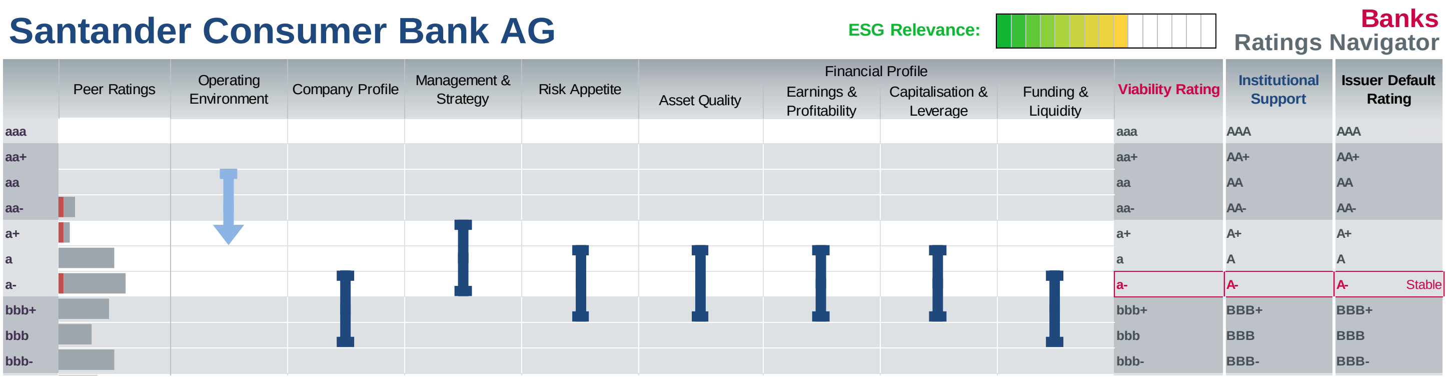
Source: Fitch Ratings

SCB AG's SNP debt rating is aligned with its Long-Term IDR, as we expect the bank to continue to meet its resolution buffer requirements with SNP and more junior debt only.

The DCR, long-term SP debt and deposit ratings are one notch above the Long-Term IDR to reflect the protection accruing to preferred creditors from the SNP and junior debt buffers. SCB AG is issuing its resolution debt buffers internally to SCF/Santander, with which it shares a resolution group. The short-term SP debt and deposit ratings of 'F1' are the lower of the two options, mapping to the respective long-term ratings of 'A', because the liquidity and funding score of 'bbb+' prevents higher short-term ratings.

The Short-Term IDR of 'F2' is aligned with that of Santander. It is also the lower of the two options mapping to SCB AG's Long-Term IDR of 'A-', because the bank's liquidity and funding score of 'bbb+' prevents a higher Short-Term IDR.

Ratings Navigator



Institutional Support Assessment

Institutional Support			Value
Parent IDR			A-
Total Adjustments (notches)			+0
Institutional Support:			**A-**
Support Factors (negative)	**Equalised**	**1 Notch**	**2+ Notches**
Parent ability to support and subsidiary ability to use support			
Parent/group regulation	✓		
Relative size	✓		
Country risks	✓		
Parent Propensity to Support			
Role in group	✓		
Potential for disposal		✓	
Implication of subsidiary default	✓		
Integration	✓		
Size of ownership stake	✓		
Support track record		✓	
Subsidiary performance and prospects	✓		
Branding	✓		
Legal commitments			✓
Cross-default clauses			✓

Bar Chart Legend

Vertical bars – VR range of Rating Factor

Bar Colors – Influence on final VR

- Higher influence
- Moderate influence
- Lower influence

Bar Arrows – Rating Factor Outlook

⇧	Positive	⇩	Negative
⇳	Evolving	▫	Stable

Significant Changes

Improved Economic Prospects Since Last Rating Review

We expect SCB AG's operating environment to further improve in 2H21 and 2022. The German authorities' large-scale response to the pandemic has ensured a supportive operating framework, reducing the risk of significant deterioration in loan quality more effectively than in most EU countries. With a 4.8% decline, Germany's GDP was more resilient than most large European economies in 2020, and Fitch expects it to recover close to its pre-pandemic level by end-2021. German banks front-loaded less provisions for expected credit losses in 2020 and LICs were generally low in 1H21 despite less significant releases than at many European peers.

Structural Weaknesses Will Continue to Weigh on German Banks' Profitability

German banks' profits have been remarkably low for years despite steady economic growth before thepandemic. Profitability is likely to remain under pressure in the coming years due to stubbornly high fragmentation, intense competition, vulnerable business models and untested strategic directions at some large banks.

German banks have largely missed out on strong trading revenue opportunities from the exceptional market volatility prevailing since 2Q20, which other European banking sectors were better positioned to seize. Truly universal banking models are rare, and the lack of revenue diversification has constrained the adaptability of most German banks during the crisis. A short-lived increase in corporate lending margins in 2Q20 quickly gave way to deep-rooted excessive price competition among German banks, especially in corporate lending, despite the need to compensate for rising LICs.

We expect German banks to recover to more adequate profits in 2021 given the economic recovery, the increasing penetration of negative rates on deposits and progress on restructuring at several large banks. However, a more disciplined and sustainable focus on risk-adjusted pricing, instead of following pre-crisis strategies of low-margin lending to gain market shares, is necessary for the sector to close its wide profitability gap relative to the European average.

Summary Financials and Key Ratios

	31 Dec 20 (EURm)	31 Dec 19 (EURm)	31 Dec 18 (EURm)	31 Dec 17 (EURm)
Summary income statement				
Net interest and dividend income	1,010	1,055	1,148	1,149
Net fees and commissions	158	155	110	150
Other operating income	130	111	90	127
Operating costs	780	833	815	933
Pre-impairment operating profit	518	488	533	493
Loan and other impairment charges	124	33	65	101
Operating profit	394	454	468	393
Summary balance sheet				
Gross loans	29,749	30,497	30,402	31,421
- Of which impaired	528	537	566	663
Loan loss allowances	532	536	548	622
Interbank	2,860	2,152	1,531	1,025
Other securities and earning assets	12,196	10,019	8,337	8,706
Cash and due from banks	5,348	3,496	2,954	1,538
Total assets	**50,127**	**46,102**	**43,048**	**42,421**
Customer deposits	22,774	23,170	22,719	22,474
Interbank and other short-term funding	7,254	4,999	5,374	5,943
Other long-term funding	15,217	13,298	10,475	9,527
Other liabilities	1,161	1,238	1,194	1,190
Preference shares and hybrid capital	408	333	223	223
Total equity	3,313	3,063	3,063	3,063
Total liabilities and equity	**50,127**	**46,102**	**43,048**	**42,421**
Ratios (annualised as appropriate)				
Profitability				
Operating profit/risk-weighted assets	2.0	2.3	2.5	1.9
Non-interest expense/gross revenue	60.1	63.1	60.5	65.4
Net income/average equity	12.4	14.8	15.1	12.8
Asset quality				
Impaired loans ratio	1.8	1.8	1.9	2.1
Growth in gross loans	-2.5	0.3	-3.2	-0.4
Loan loss allowances/impaired loans	100.8	99.8	96.8	93.8
Loan impairment charges/average gross loans	0.4	0.1	0.2	0.3
Capitalisation				
Common equity Tier 1 ratio	14.4	13.0	13.9	12.5
Tangible common equity/tangible assets	6.2	6.2	6.7	6.8
Basel leverage ratio	7.5	7.0	7.4	7.4
Funding and liquidity				
Loans/customer deposits	130.6	131.6	133.8	139.8
Liquidity coverage ratio	236.6	187.8	169.1	133.6
Customer deposits/funding	49.9	55.4	58.6	58.9

Source: Fitch Ratings, Fitch Solutions, SCB AG

Environmental, Social and Governance Considerations

SCB AG's highest level of ESG credit relevance is a score of '3'. This means ESG issues are credit neutral or have only a minimal credit impact, either due to their nature or the way in which they are being managed by the bank.

FitchRatings **Santander Consumer Bank AG**

Banks
Ratings Navigator

Credit-Relevant ESG Derivation

Santander Consumer Bank AG has 5 ESG potential rating drivers

- Santander Consumer Bank AG has exposure to compliance risks including fair lending practices, mis-selling, repossession/foreclosure practices, consumer data protection (data security) but this has very low impact on the rating.
- Governance is minimally relevant to the rating and is not currently a driver.

Overall ESG Scale

key driver	0	issues	5
driver	0	issues	4
potential driver	5	issues	3
not a rating driver	4	issues	2
	5	issues	1

Environmental (E)

General Issues	E Score	Sector-Specific Issues	Reference	E Scale
GHG Emissions & Air Quality	1	n.a.	n.a.	5
Energy Management	1	n.a.	n.a.	4
Water & Wastewater Management	1	n.a.	n.a.	3
Waste & Hazardous Materials Management; Ecological Impacts	1	n.a.	n.a.	2
Exposure to Environmental Impacts	2	Impact of extreme weather events on assets and/or operations and corresponding risk appetite & management; catastrophe risk; credit concentrations	Company Profile; Management & Strategy; Risk Appetite; Asset Quality	1

Social (S)

General Issues	S Score	Sector-Specific Issues	Reference	S Scale
Human Rights, Community Relations, Access & Affordability	2	Services for underbanked and underserved communities: SME and community development programs; financial literacy programs	Company Profile; Management & Strategy; Risk Appetite	5
Customer Welfare - Fair Messaging, Privacy & Data Security	3	Compliance risks including fair lending practices, mis-selling, repossession/foreclosure practices, consumer data protection (data security)	Operating Environment; Company Profile; Management & Strategy; Risk Appetite	4
Labor Relations & Practices	2	Impact of labor negotiations, including board/employee compensation and composition	Company Profile; Management & Strategy	3
Employee Wellbeing	1	n.a.	n.a.	2
Exposure to Social Impacts	2	Shift in social or consumer preferences as a result of an institution's social positions, or social and/or political disapproval of core banking practices	Company Profile; Financial Profile	1

Governance (G)

General Issues	G Score	Sector-Specific Issues	Reference	G Scale
Management Strategy	3	Operational implementation of strategy	Management & Strategy	5
Governance Structure	3	Board independence and effectiveness; ownership concentration; protection of creditor/stakeholder rights; legal /compliance risks; business continuity; key person risk; related party transactions	Management & Strategy; Earnings & Profitability; Capitalisation & Leverage	4
Group Structure	3	Organizational structure; appropriateness relative to business model; opacity; intra-group dynamics; ownership	Company Profile	3
Financial Transparency	3	Quality and frequency of financial reporting and auditing processes	Management & Strategy	2
				1

How to Read This Page
ESG scores range from 1 to 5 based on a 15-level color gradation. Red (5) is most relevant and green (1) is least relevant.

The Environmental (E), Social (S) and Governance (G) tables break out the individual components of the scale. The right-hand box shows the aggregate E, S, or G score. General Issues are relevant across all markets with Sector-Specific Issues unique to a particular industry group. Scores are assigned to each sector-specific issue. These scores signify the credit-relevance of the sector-specific issues to the issuing entity's overall credit rating. The Reference box highlights the factor(s) within which the corresponding ESG issues are captured in Fitch's credit analysis.

The Credit-Relevant ESG Derivation table shows the overall ESG score. This score signifies the credit relevance of combined E, S and G issues to the entity's credit rating. The three columns to the left of the overall ESG score summarize the issuing entity's sub-component ESG scores. The box on the far left identifies some of the main ESG issues that are drivers or potential drivers of the issuing entity's credit rating (corresponding with scores of 3, 4 or 5) and provides a brief explanation for the score.

Classification of ESG issues has been developed from Fitch's sector ratings criteria. The General Issues and Sector-Specific Issues draw on the classification standards published by the United Nations Principles for Responsible Investing (PRI) and the Sustainability Accounting Standards Board (SASB).

Sector references in the scale definitions below refer to Sector as displayed in the Sector Details box on page 1 of the navigator.

CREDIT-RELEVANT ESG SCALE

How relevant are E, S and G issues to the overall credit rating?

5	Highly relevant, a key rating driver that has a significant impact on the rating on an individual basis. Equivalent to "higher" relative importance within Navigator.
4	Relevant to rating, not a key rating driver but has an impact on the rating in combination with other factors. Equivalent to "moderate" relative importance within Navigator.
3	Minimally relevant to rating, either very low impact or actively managed in a way that results in no impact on the entity rating. Equivalent to "lower" relative importance within Navigator.
2	Irrelevant to the entity rating but relevant to the sector.
1	Irrelevant to the entity rating and irrelevant to the sector.

The ratings above were solicited and assigned or maintained at the request of the rated entity/issuer or a related third party. Any exceptions follow below.

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