S&P Global Ratings

RatingsDirect®

Volkswagen Bank GmbH

Primary Credit Analyst:
Heiko Verhaag, CFA, FRM, Frankfurt + 49 693 399 9215; heiko.verhaag@spglobal.com

Secondary Contact:
Harm Semder, Frankfurt + 49 693 399 9158; harm.semder@spglobal.com

Table Of Contents

Table Of Contents (cont.)

Volkswagen Bank GmbH

Ratings Score Snapshot

Issuer Credit Rating
BBB+/Stable/A-2

SACP: bbb+ → **Support: 0** → **Additional factors: 0**

Anchor	bbb+	
Business position	Constrained	-2
Capital and earnings	Very strong	+2
Risk position	Adequate	0
Funding	Adequate	0
Liquidity	Adequate	
CRA adjustment		0

ALAC support	0
GRE support	0
Group support	0
Sovereign support	0

Issuer credit rating
BBB+/Stable/A-2

ALAC--Additional loss-absorbing capacity. CRA--Comparable ratings analysis. GRE--Government-related entity. ICR--Issuer credit rating. SACP--Stand-alone credit profile.

Credit Highlights

Key strengths	Key risks
Very strong capitalization and stable revenue.	New business dependence on the parent's auto sales.
A stable retail deposit base.	Concentrated exposure and volatility in the car finance business.
Deep integration into the captive finance value chain of VW Group with clear strategic objectives.	

Volkswagen Bank GmbH's (VW Bank's) strong earnings and product offering will support VW Group's electrification strategy. As a fully owned captive finance subsidiary of German car producer Volkswagen AG (VW; BBB+/Stable/A-2), VW Bank has a core strategic business purpose of promoting the sale of products of the group, including support to VW dealers and stronger customer relationships. S&P Global Ratings does not expect this role to change in the foreseeable future, but rather be strengthened by the important role to promote the sale of electric vehicles. The expected annual transfer of local GAAP profits of about €400 million will help support the industrial transformation.

VW Bank's very strong capitalization will remain its main rating strength. We project the bank's capitalization to remain very strong, with an expected S&P Global Ratings' risk-adjusted capital (RAC) ratio of 18%-19% over 2022-2023, slightly down from an estimated 19% as of end-2021. The elevated capital level compared with that of pre-COVID-19 years is mainly from decreased financing volumes over the pandemic years. It is also supported by the reinjection of 2020 annual profits into the bank, potentially driven by European Central Bank (ECB) guidance on dividend restrictions for European banks, after the profit and loss transfer agreement triggered distributions to the parent.

VW Bank' asset quality will benefit from the economic recovery and stronger-than-expected residual values. We anticipate that the bank will maintain its sound asset quality over 2022 and 2023, after a largely nonexistent expected cost of risk in 2021. We expect cost of risk of 20-25 basis points (bps), closer to pre-pandemic levels. We expect elevated collateral values will continue to support VW Bank's asset quality over 2022.

S&P Global Ratings acknowledges a high degree of uncertainty about the extent, outcome, and consequences of the military conflict between Russia and Ukraine.

Irrespective of the duration of military hostilities, sanctions and related political risks are likely to remain in place for some time. Potential effects could include dislocated commodities markets--notably for oil and gas--supply chain disruptions, inflationary pressures, weaker growth, and capital market volatility. As the situation evolves, we will update our assumptions and estimates accordingly. See our macroeconomic and credit updates here: Russia-Ukraine Macro, Market, & Credit Risks. Note that the timing of publication for rating decisions on European issuers is subject to European regulatory requirements.

Outlook

The stable outlook indicates our expectations that VW Bank will maintain fairly steady financial performance over the next two years and very strong capitalization, while continuing to play an important role in VW's financing solutions.

Upside scenario

We would consider an upgrade if an improving credit profile for the parent would indicate stronger capacity to provide extraordinary support to VW Bank if needed. While more unlikely, we could also consider an upgrade if the bank manages to improve its business stability through further diversification or materially boost its risk-adjusted profitability through more efficient operations.

Downside scenario

We consider a downgrade a remote scenario as long as parent VW maintains its credit strengths. We would only consider downgrading VW Bank if we observed that its strategic relevance to the group, expressed in its core group status, weakened, along with its stand-alone creditworthiness. A negative rating action on the parent alone would likely not lead to a downgrade to the bank, reflecting our assessment of it as an insulated entity.

Key Metrics

Volkswagen Bank GmbH--Key Ratios And Forecasts

	--Fiscal year ended Dec. 31--				
(%)	**2019a**	**2020a**	**2021f**	**2022f**	**2023f**
Growth in operating revenue	(17.8)	2.2	3.5-4.5	(3.5)-(4.5)	3.0-4.0

Volkswagen Bank GmbH--Key Ratios And Forecasts (cont.)					
	--Fiscal year ended Dec. 31--				
(%)	2019a	2020a	2021f	2022f	2023f
Growth in customer loans	(19.2)	(6.7)	(2.5)-(3.5)	3.0-5.0	3.0-5.0
Net interest income/average earning assets (NIM)	2.3	2.5	2.7-2.9	2.7-2.9	2.7-2.9
Cost to income ratio	46.4	43.7	42.0-44.0	44.5-46.5	43.5-46.0
Return on average common equity	5.0	6.6	5.8-7.1	4.7-5.7	4.9-6.0
New loan loss provisions/average customer loans	0.2	0.4	0.0-0.1	0.2-0.3	0.2-0.3
Gross nonperforming assets/customer loans	2.3	2.6	3.1-3.4	2.4-2.7	2.3-2.6
Risk-adjusted capital ratio	17.5	17.3	18.5-19.5	18.5-19.5	18.0-19.0

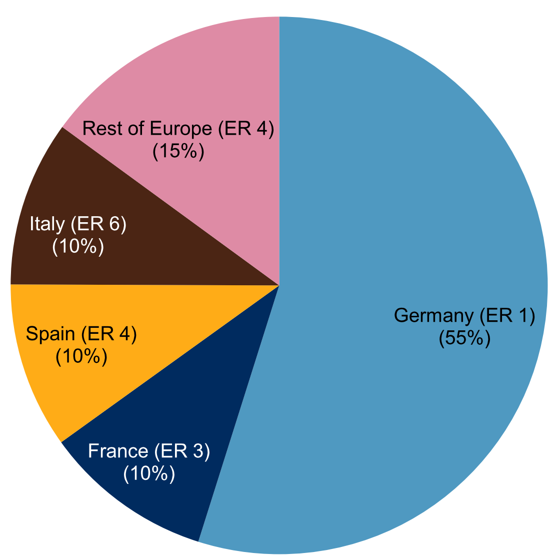
All figures are S&P Global Ratings-adjusted. a--Actual. f--Forecast. NIM--Net interest margin.

Anchor: 'bbb+' For A German Bank With European Exposure

Our anchor for VW Bank is 'bbb+' and is in line with German domestic banks, despite VW Bank's international exposure. It takes into account the German industry risk score of '4' and our view of the weighted-average economic risk across countries where VW Bank operates rounding to '2'. Since June 2021, we have assigned stable trends to both our economic risk and industry risk scores.

Chart 1

VW Bank's Loan Portfolio Contains A Majority Of German Exposure
But also large shares of higher-risk countries



ER--Economic risk. Source: S&P Global Ratings.

Our assessment of economic risk considers the strengths of Germany's highly diverse and competitive economy, with a demonstrated ability to absorb economic and financial shocks. We also anticipate that Germany's ample fiscal and monetary measures continue to mitigate the pandemic's cyclical shock to the economy, the banking system, and retail and corporate customers, as well as to limit German banks' credit losses. Nevertheless, the high degree of openness, with exports accounting for 50% of GDP, makes the trajectory of recovery also dependent on broad-based international developments. Our stable trend on economic risk signals that we have greater confidence that German households, corporates, and public finances will remain well-cushioned from the pandemic's negative effects. Similarly, despite elevated German house-price growth in recent years, we consider a rapid correction after a period of rising house prices unlikely in the next couple of years. Our assessment of industry risk considers the dual pressures from the pandemic's economic impact on banks' balance sheets, and the banking sector's profitability challenges due to poor cost efficiency, rising risks from technology disruption, and low interest rates. We believe that German banks operate in a highly competitive and structurally overbanked banking market, with low gross margin; and banks' progress in improving their structural revenue diversification, cost bases, and digitalization has widened the sector's gap with leading banking systems. Interest rates are likely to remain unsupportive for longer, putting further pressure on German banks' already-depressed interest income, and the pandemic has accelerated the move toward digital banking services, an area in which we see German banks as lagging peers. We see cost pressures from the imperative for the German banking industry to invest significantly in the core banking systems and digital customer services that are essential to avoid the risks of tech disruption and franchise damage from cyberattacks and customer data mismanagement.

Business Position: Constrained By The Bank's Role As A Monoline European Auto Finance Provider

We consider VW Bank's business position a major ratings constraint due to the bank's business model as a captive finance company and consequently its focus on one activity--car financing. This approach is in line with our assessment of most peer captive finance subsidiaries in Europe such as FCA Bank, FCE Bank, or PSA Banque France. We note, however, the sound financial prospects stemming from VW Bank's strong regional European business diversity (with material operations in nine EU countries), its sharpened focus and efficiency measures from its reorganization as the VW group's EU bank, and a groupwide growth strategy that is bolstered by VW's commitment to good capitalization.

VW Bank's strategy remains fully aligned with that of its parent, by providing banking services and supporting vehicle sales across Europe and promoting customer loyalty. This also means the bank relies on the fortunes of its parent in terms of sales and brand recognition.

The lending business comprises vehicle related loans to retail customers, business customers, and dealers; and auto loans on its HeyCar platform (a joint venture with Daimler, Allianz, and Renault Group and RCI Bank and Services) that include those for non-VW related brands. We expect this online channel also to support an increasing share of used car financing, supporting materially the growth in operating revenue.

We expect first-half 2021 to have marked the low point of lending volumes, with about €51 billion in net receivables.

The economic recovery, combined with a gradually growing share of used car financing and our expectations of steadily normalizing new car supply should benefit business growth.

VW Bank's direct banking activities in Germany, with customer deposits of 26.6 billion as of first-half 2021, in our view provide stability to the bank's business model, notably in terms of funding, but also in terms of additional fee income from brokered banking products. In cooperation with partners, the bank provides mortgage loans and investment products for retail customers among other products.

Capital And Earnings: Very Strong Capitalization Supported By Stable Earnings

We believe VW Bank will maintain its key rating strength of very strong capital and earnings, reflecting its good earnings generation and VW's commitment to maintain high capital ratios at its EU banking business. We project that the bank's RAC ratio (before diversification) will remain comfortably above 18% over 2022-2023.

In our base-case scenario for the coming two years, we expect:

- A gradual normalization of supply bottlenecks and increasing financing volumes of new and used cars.
- Loan growth of about 4% annually.
- A stable net interest margin of about 2.8%.
- Some cost inflation and a normalizing risk cost at about 25 bps.
- Annual net income under IFRS of €500 million-€600 million over 2022 and 2023.

However, local GAAP results under HGB will be distributed to the parent based on the profit and loss transfer agreement, constraining the bank's earnings retention under IFRS.

Next to very strong capital ratios, relatively high pre-provision operating income provides a sufficient buffer to cover normalized losses. We project the three-year average earnings buffer will remain solid, at 120-130 bps, indicating that VW Bank has adequate earnings to cover more than our assumed annual normalized losses, which will be about €330 million in 2022. This level compares favorably with that of many domestic and international universal banks but is weaker than that of most rated captives and consumer-finance-focused peers.

We anticipate that the bank will maintain its conservative capital management and its asset mix and growth are unlikely to change materially in the next few years. Furthermore, we expect that VW will remain committed to maintaining very strong capitalization at VW Bank, supporting the bank's business growth through capital injections, if necessary.

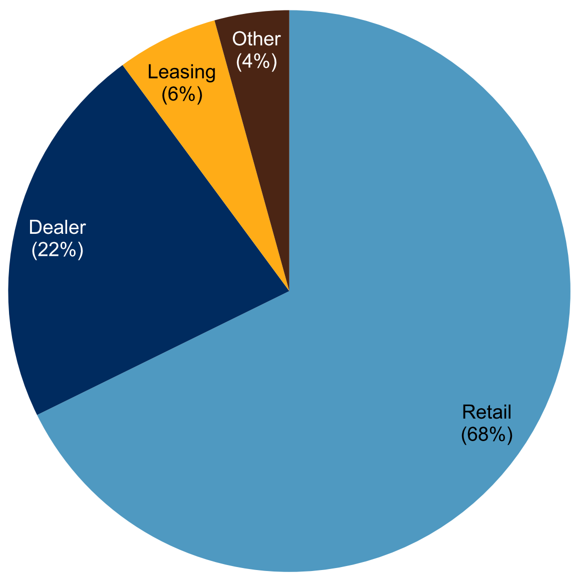
Risk Position: Sound Asset Quality And Prudent Risk Management Balance Concentration In The Auto Sector

We assess VW Bank's risk position as a neutral rating factor because we adequately capture the bank's domestic and European auto loans and dealer financings in our RAC ratio. VW Bank's auto loans are highly collateralized, and we see its loss experience in line with that of its peers.

Retail auto loan exposure (€32 billion as of midyear 2021) are granular, highly collateralized, and principally to customers in European countries with relatively lower risk. Although dealer and corporate exposure (€11 billion as of midyear 2021) inherently features single-name concentration, the 20 largest exposures represent a low proportion of the bank's total adjusted capital.

Chart 2

VW Bank's Loan Portfolio Is Dominated By Retail Customers

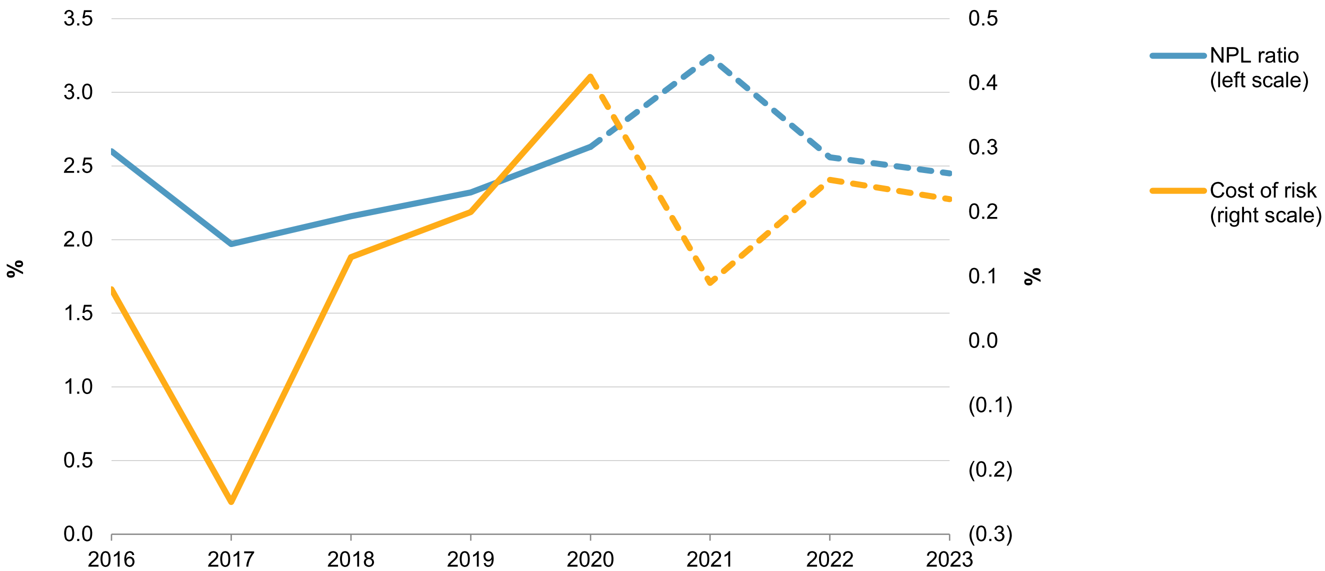


Source: S&P Global Ratings.

We recognize that VW Bank has limited interest-rate risk from a largely matched funding structure. It also has low residual-value risk because leasing business is mainly executed at VW Financial Services. Generally, we believe the risks the bank assumes show low complexity. VW Bank's asset quality is adequate and in line with that of peer captive financing subsidiaries, with nonperforming loans (NPLs) expected to have peaked at somewhat above 3% of the total loans at year-end 2021 compared with 2.6% of total loans in 2020. We also expect cost of risk to normalize at 20-25 bps in 2022 and 2023.

Chart 3

VW Bank's Credit Quality Is Expected To Normalize Over 2022



NPL--Non-performing loans. Source: S&P Global Ratings. Own Assumption And Forecasts.

Funding And Liquidity: An Adequate Funding Profile, Owing To Granular Customer Deposits

We consider VW Bank's funding and liquidity position as in line with peers'.

The bank's access to a large core deposit base, which accounted for about 66% of its funding at midyear 2021, differentiates it from its captive finance peer group. The large majority of customer deposits consist of granular retail deposits. Although we generally consider direct bank customer deposits more price sensitive and less stable than those of large retail banks, VW Bank's deposit and customer base has, in our view, proven robust, underlining its deposit franchise. This makes it less sensitive to volatile wholesale funding sources, as demonstrated by the bank's stable funding ratio of 106% as of midyear 2021. We understand VW Bank will optimize its funding sources from a cost perspective, considering the still-negative near-term rates in the eurozone, which could lead to a somewhat lower share of customer deposits. As of midyear 2021, the bank's loan-to-deposit ratio was about 115%, with wholesale funds covering the gap.

This exposes VW Bank to some refinancing risk, but the bank has access to some uncommitted lines and assets eligible for refinancing at the ECB. The bank regularly conducts liquidity stress tests to identify shortcomings in stressed environments. We also expect VW Bank to scale up its deposit funding by offering slightly more attractive terms. In our view, these liquidity buffers add to the bank's 2.4x BLAST ratio (broad liquid assets to short-term wholesale funding) as of midyear 2021. Furthermore, we expect VW Bank will have access to funding from its parent in the event of financial distress.

Support: Credit Strength, In Line With The Parent's

VW Bank remains a significant earnings contributor to its parent, and its captive finance operations are integral to the group's sales strategy. We therefore view VW Bank as having a core group status in VW's business model, indicating our expectation of group support under any foreseeable circumstances. We see the rating on VW as a floor for our rating on VW Bank, as long as the bank remains a core subsidiary.

At the same time, we consider VW Bank insulated from its corporate parent, making it potentially eligible for a rating above that of the parent if its stand-alone credit profile would justify this, which currently is not the case. This reflects VW Bank's regulatory status as a bank, an independent operational setup, and largely no funding dependence from the parent despite some intercompany funding. Regulatory restrictions regarding liquidity, capital, and funding could prevent VW Bank from supporting the group to the extent it would jeopardize the bank's own creditworthiness.

Although VW Bank is subject to requirements for own funds and eligible liabilities that it already meets, we believe it would not be targeted for meaningful recapitalization, but rather put into insolvency if it were to fail. This makes the ratings on the bank ineligible for uplift for additional loss absorbing capacity.

Environmental, Social, And Governance

ESG Credit Indicators

E-1	**E-2**	E-3	E-4	E-5	S-1	**S-2**	S-3	S-4	S-5	G-1	**G-2**	G-3	G-4	G-5

ESG credit indicators provide additional disclosure and transparency at the entity level and reflect S&P Global Ratings' opinion of the influence that environmental, social, and governance factors have on our credit rating analysis. They are not a sustainability rating or an S&P Global Ratings ESG Evaluation. The extent of the influence of these factors is reflected on an alphanumerical 1-5 scale where 1 = positive, 2 = neutral, 3 = moderately negative, 4 = negative, and 5 = very negative. For more information, see our commentary "ESG Credit Indicators: Definition And Applications," published Oct. 13, 2021.

We do not see ESG credit factors influencing VW Bank's credit quality materially different from peers and view these factors as neutral to the rating. In our view, the bank's concentrated activities in car financing exposes it to environmental risks to a somewhat larger extent than other banking peers'. In particular, we see VW Bank as more exposed than its industry peers due to carbon dioxide regulations for automakers in the EU and the secular shift to electrified vehicles. Nevertheless, the bank plays a key role in promoting the sales of electrified vehicles and, through this, reduce the environmental impact of its fleet. We consider VW Bank's exposure to governance and social risks not materially different from those of industry peers.

Key Statistics

Table 1

Volkswagen Bank GmbH--Key Figures

	--Year ended Dec. 31--				
(Mil. €)	**2021***	**2020**	**2019**	**2018**	**2017**
Adjusted assets	65,246	66,908	68,406	83,002	78,699
Customer loans (gross)	51,854	54,154	58,038	71,816	71,424
Adjusted common equity	10,649	9,116	8,976	11,580	11,232
Operating revenue	797	1,747	1,710	2,081	2,228
Noninterest expense	437	763	793	932	1,363
Core earnings	191	603	555	758	671

*Half-year results.

Table 2

Volkswagen Bank GmbH--Business Position

	--Year ended Dec. 31--				
(%)	**2021***	**2020**	**2019**	**2018**	**2017**
Total revenue from business line (currency in millions)	797.0	1,844.0	1,713.0	2,380.0	2,312.0
Commercial banking/total revenue from business line	16.3	13.1	15.8	53.0	24.3
Retail banking/total revenue from business line	83.9	69.6	75.3	42.3	51.7
Commercial and retail banking/total revenue from business line	100.3	82.7	91.1	95.3	76.0
Insurance activities/total revenue from business line	N/A	6.5	7.8	5.9	9.0
Other revenue/total revenue from business line	(0.3)	10.8	1.1	(1.2)	15.1
Return on average common equity	3.6	6.6	5.0	6.1	7.1

*Half-year results. N/A--Not applicable.

Table 3

Volkswagen Bank GmbH--Capital And Earnings

	--Year ended Dec. 31--				
(%)	**2021***	**2020**	**2019**	**2018**	**2017**
Tier 1 capital ratio	18.9	17.1	15.6	15.5	15.6
S&P Global Ratings' RAC ratio before diversification	N/A	17.3	17.5	20.1	21.4
S&P Global Ratings' RAC ratio after diversification	N/A	17.5	17.7	20.1	21.2
Adjusted common equity/total adjusted capital	100.0	100.0	100.0	100.0	100.0
Net interest income/operating revenue	100.3	87.3	91.3	108.9	98.2
Fee income/operating revenue	2.3	6.0	0.0	(8.5)	(1.7)
Market-sensitive income/operating revenue	(7.0)	0.3	(0.2)	4.1	(2.2)
Cost to income ratio	54.8	43.7	46.4	44.8	61.2
Preprovision operating income/average assets	1.1	1.5	1.2	1.4	1.3
Core earnings/average managed assets	0.6	0.9	0.7	0.9	1.0

*Half-year results. RAC--Risk-adjusted capital. N/A--Not applicable.

Table 4

Volkswagen Bank GmbH--Risk Position					
	--Year ended Dec. 31--				
(%)	**2021***	**2020**	**2019**	**2018**	**2017**
Growth in customer loans	(8.5)	(6.7)	(19.2)	0.5	49.8
Total diversification adjustment/S&P Global Ratings' RWA before diversification	N/A	(1.2)	(1.0)	0.3	1.1
Total managed assets/adjusted common equity (x)	6.1	7.3	7.6	7.2	7.0
New loan loss provisions/average customer loans	(0.2)	0.4	0.2	0.1	(0.3)
Net charge-offs/average customer loans	N.M.	0.4	0.1	0.1	0.0
Gross nonperforming assets/customer loans + other real estate owned	N/A	2.6	2.3	2.2	2.0
Loan loss reserves/gross nonperforming assets	N/A	78.4	81.6	76.3	77.2

*Half-year results. RWA--Risk-weighted assets. N/A--Not applicable. N.M.--Not meaningful.

Table 5

Volkswagen Bank GmbH--Funding And Liquidity					
	--Year ended Dec. 31--				
(%)	**2021***	**2020**	**2019**	**2018**	**2017**
Core deposits/funding base	66.1	65.7	69.0	58.7	63.9
Customer loans (net)/customer deposits	148.8	149.8	148.9	178.4	171.3
Long-term funding ratio	92.6	92.3	93.9	90.2	90.8
Stable funding ratio	106.0	105.1	99.4	92.6	92.4
Short-term wholesale funding/funding base	8.9	9.2	7.2	11.5	10.9
Broad liquid assets/short-term wholesale funding (x)	2.4	2.1	1.7	0.8	0.6
Net broad liquid assets/short-term customer deposits	20.0	17.2	7.5	(5.6)	(7.4)
Short-term wholesale funding/total wholesale funding	26.2	26.9	23.2	27.8	30.1
Narrow liquid assets/three-month wholesale funding (x)	4.5	4.4	5.4	1.3	1.3

*Half-year results.

Related Criteria

- Criteria | Financial Institutions | General: Financial Institutions Rating Methodology, Dec. 9, 2021
- Criteria | Financial Institutions | Banks: Banking Industry Country Risk Assessment Methodology And Assumptions, Dec. 9, 2021
- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- General Criteria: Hybrid Capital: Methodology And Assumptions, July 1, 2019
- General Criteria: Group Rating Methodology, July 1, 2019
- Criteria | Financial Institutions | General: Risk-Adjusted Capital Framework Methodology, July 20, 2017
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Related Research

- Volkswagen AG, Feb. 2, 2022
- German Bank Ratings Affirmed Under Revised Financial Institutions Criteria, Jan. 28, 2022
- Banking Industry Country Risk Assessment: Germany, Oct 5, 2021
- Various German Banks Downgraded On Persistent Profitability Challenges And Slow Digitalization Progress, June 24, 2021
- Research Update: VW Bank GmbH 'A-/A-2' Ratings Affirmed And Outlook Still Negative After Parent Volkswagen's Outlook Revision To Stable, April 28, 2021

Ratings Detail (As Of March 15, 2022)*	
Volkswagen Bank GmbH	
Issuer Credit Rating	BBB+/Stable/A-2
Commercial Paper	
Local Currency	A-2
Senior Subordinated	BBB
Senior Unsecured	BBB+
Short-Term Debt	A-2
Issuer Credit Ratings History	
24-Jun-2021	BBB+/Stable/A-2
12-Oct-2015	A-/Negative/A-2
24-Sep-2015	A/Watch Neg/A-1
Sovereign Rating	
Germany	AAA/Stable/A-1+
Related Entities	
Banco Volkswagen S.A.	
Issuer Credit Rating	
Brazil National Scale	brAAA/Stable/--
Navistar Financial, S.A. de C.V. SOFOM, E.R.	
Issuer Credit Rating	
CaVal (Mexico) National Scale	mxAA+/Stable/mxA-1+
Senior Unsecured *CaVal (Mexico) National Scale*	mxAA+
Short-Term Debt *CaVal (Mexico) National Scale*	mxA-1+
Scania AB (publ.)	
Issuer Credit Rating	BBB/Stable/A-2
Nordic Regional Scale	--/--/K-2
South Africa National Scale	zaAAA/--/zaA-1+
TRATON SE	
Issuer Credit Rating	BBB/Stable/--

Ratings Detail (As Of March 15, 2022)*(cont.)	
Volkswagen AG	
Issuer Credit Rating	BBB+/Stable/A-2
Volkswagen Financial Services AG	
Issuer Credit Rating	BBB+/Stable/A-2
Volkswagen Finans Sverige AB	
Issuer Credit Rating	
Nordic Regional Scale	--/--/K-1
Volkswagen International Belgium S.A.	
Issuer Credit Rating	BBB+/Stable/A-2
Commercial Paper	
Local Currency	A-2
Volkswagen Leasing, S.A. de C.V	
Senior Secured	
CaVal (Mexico) National Scale	mxAAA

*Unless otherwise noted, all ratings in this report are global scale ratings. S&P Global Ratings' credit ratings on the global scale are comparable across countries. S&P Global Ratings' credit ratings on a national scale are relative to obligors or obligations within that specific country. Issue and debt ratings could include debt guaranteed by another entity, and rated debt that an entity guarantees.