

Rating Action: Moody's confirms Volkswagen Bank GmbH's long-term debt and deposit ratings; outlook negative

03 Jun 2020

Frankfurt am Main, June 03, 2020 -- Moody's Investors Service (Moody's) has today confirmed the A1 long-term issuer and deposit ratings of Volkswagen Bank GmbH (VW Bank), as well as the bank's A3 junior senior unsecured debt ratings and its (P)A1 senior unsecured debt program rating. The outlook on the long-term issuer and deposit ratings has been changed to negative from ratings under review. Further, the rating agency affirmed the bank's baa2 Baseline Credit Assessment (BCA) and confirmed VW Bank's a3 Adjusted BCA.

The rating actions follow the confirmation -- with a negative outlook -- of Volkswagen Aktiengesellschaft's (Volkswagen; the parent company of VW Bank) A3 issuer rating. For further details, please refer to the following press release "Moody's confirms VW's A3 ratings; Outlook negative" (https://www.moody.com/research/--PR_425455), published on 2 June 2020.

The rating actions conclude the review on the bank's long-term ratings initiated on 27 March 2020.

For a full list of all affected ratings, please refer to the end of this press release.

RATINGS RATIONALE

--RATIONALE FOR THE AFFIRMATION OF THE BCA

The affirmation of VW Bank's baa2 BCA reflects the resilience of the bank's intrinsic financial strength, despite the rapid and widening spread of the coronavirus outbreak and the deteriorating global economic outlook, which are creating a severe and extensive credit shock across many sectors, regions and markets and will weigh on the bank's solvency. Moody's regards the coronavirus outbreak as a social risk under its environmental, social and governance (ESG) framework, given the substantial implications for public health and safety.

The rating agency believes VW Bank will be able to largely defend the quality of its corporate as well as retail lending books. Although Moody's anticipates the problem loan ratio to rise, also exerting strain on the bank's profitability, the baa2 BCA remains reasonably well protected by the bank's solid regulatory capital levels, as well as by its underlying sound profitability. In addition, the broad range of the bank's proven and diversified funding channels, displaying good access to capital markets despite a more volatile market environment, further underpin the bank's BCA. At the same time, the baa2 BCA remains constrained by VW Bank's undiversified business mix, resulting from its captive finance origin, and the resulting classification of the bank as a monoline business.

--RATIONALE FOR THE CONFIRMATION OF THE ADJUSTED BCA

The confirmation of VW Bank's Adjusted BCA reflects Moody's assessment of the very strong contractual and economic rationale for Volkswagen to support VW Bank, warranting the alignment of the bank's Adjusted BCA - which reflects its intrinsic financial strength after consideration of affiliate support - with the A3 issuer rating of Volkswagen, its ultimate owner.

VW Bank benefits from a direct control and profit and loss transfer agreement with Volkswagen and close strategic links with its car manufacturing parent. Moody's considers these links when assessing VW Bank's financial strength after assumed parental support.

--RATIONALE FOR THE CONFIRMATION OF VW BANK'S RATINGS

The confirmation of VW Bank's ratings reflects the confirmation of the bank's a3 Adjusted BCA as well as the application of Moody's Advanced Loss Given Failure (LGF) analysis to its liabilities, with unchanged rating uplift for individual instrument classes.

The unchanged rating uplift from Moody's Advanced LGF analysis reflects the rating agency's view that VW Bank's liability structure will only temporarily benefit from the currently greater role of junior senior debt in the

bank's liability structure relative to the bank's tangible banking assets. Over time, and considering regulatory requirements as well as likely developments in the bank's liability structure and tangible banking assets, Moody's expects the currently assigned rating uplift to the bank's various debt classes to remain stable.

--RATIONALE FOR THE NEGATIVE OUTLOOK

Because of the alignment of VW Bank's Adjusted BCA with the issuer rating of its ultimate parent Volkswagen, the outlook of VW Bank's ratings follows the negative outlook of the long-term issuer rating of Volkswagen.

FACTORS THAT COULD LEAD TO AN UPGRADE OR DOWNGRADE OF THE RATINGS

Owing to the intrinsic interlinkages of VW Bank with its automotive parent, its ratings are highly dependent on the creditworthiness of Volkswagen.

Although considered unlikely, given the negative outlook, an upgrade of VW Bank's ratings could follow an upgrade of Volkswagen's rating.

VW Bank's ratings could also be upgraded if the rating agency were to assess that the increased issuance in instruments that are designated to absorb losses at failure was likely to be sustained. This could result in additional notches of rating uplift for VW Bank's various debt classes from Moody's Advanced LGF analysis.

Upward pressure on VW Bank's baa2 BCA could only result from a combination of (1) significantly improved profitability; (2) significantly lower dependence on wholesale funding sources, coupled with a strong increase in the bank's on-balance-sheet liquidity; and (3) a further improvement in the underlying quality of VW Bank's lending assets. However, a BCA upgrade would not result in an upgrade of the bank's ratings.

VW Bank's ratings could be downgraded if Volkswagen's ratings were to be downgraded.

A downgrade of VW Bank's ratings could also be triggered if Volkswagen were to loosen its ties with its financial services subsidiary. This loosening could lead to a lowering of Moody's support assumption for VW Bank and a downgrade of the bank's Adjusted BCA to a level below the parent's issuer rating.

A downgrade of VW Bank's BCA could be triggered following (1) a sudden and more pronounced erosion of the bank's asset quality, especially considering the bank's large exposure to car dealers against an uncertain and significantly more difficult macroeconomic backdrop, and the pressure that this could exert on both the bank's profitability and capitalisation; (2) a more significant and sustained increase in the bank's dependence on wholesale funding sources, in particular if the issued instruments' terms no longer matched those of the bank's loan book; or (3) the bank losing or reducing access to committed liquidity lines from its parent or having to substantially use available assets for securitisation. However, a lower BCA would likely be offset by higher uplift from affiliate support and not result in a rating downgrade.

LIST OF AFFECTED RATINGS

Issuer: Volkswagen Bank GmbH

..Confirmations:

...Long-term Counterparty Risk Ratings, confirmed at Aa3

...Long-term Counterparty Risk Assessment, confirmed at Aa3(cr)

...Long-term Bank Deposits, confirmed at A1, outlook changed to Negative from Ratings under Review

...Long-term Issuer Ratings, confirmed at A1, outlook changed to Negative from Ratings under Review

...Senior Unsecured Medium-Term Note Program, confirmed at (P)A1

...Junior Senior Unsecured Regular Bond/Debenture, confirmed at A3

...Junior Senior Unsecured Medium-Term Note Program, confirmed at (P)A3

...Subordinate Regular Bond/Debenture, confirmed at Baa1

...Subordinate Medium-Term Note Program, confirmed at (P)Baa1

...Adjusted Baseline Credit Assessment, confirmed at a3

..Affirmation:

...Baseline Credit Assessment, affirmed baa2

..Outlook Action:

...Outlook changed to Negative from Ratings under Review

PRINCIPAL METHODOLOGY

The principal methodology used in these ratings was Banks Methodology published in November 2019 and available at https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_1147865. Alternatively, please see the Rating Methodologies page on www.moodys.com for a copy of this methodology.

REGULATORY DISCLOSURES

For further specification of Moody's key rating assumptions and sensitivity analysis, see the sections Methodology Assumptions and Sensitivity to Assumptions in the disclosure form. Moody's Rating Symbols and Definitions can be found at: https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_79004.

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Moody's general principles for assessing environmental, social and governance (ESG) risks in our credit analysis can be found at https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_1133569.

At least one ESG consideration was material to the credit rating action(s) announced and described above.

Please see www.moodys.com for any updates on changes to the lead rating analyst and to the Moody's legal entity that has issued the rating.

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Michael Rohr
Senior Vice President

Financial Institutions Group
Moody's Deutschland GmbH
An der Welle 5
Frankfurt am Main 60322
Germany
JOURNALISTS: 44 20 7772 5456
Client Service: 44 20 7772 5454

Alexander Hendricks, CFA
Associate Managing Director
Financial Institutions Group
JOURNALISTS: 44 20 7772 5456
Client Service: 44 20 7772 5454

Releasing Office:
Moody's Deutschland GmbH
An der Welle 5
Frankfurt am Main 60322
Germany
JOURNALISTS: 44 20 7772 5456
Client Service: 44 20 7772 5454



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