

Research Update:

Italy-Based FCA Bank 'BBB/A-2' Ratings Affirmed On Strong Capital Base And Group Support; Outlook Remains Negative

April 29, 2020

Overview

- Despite governments' measures to contain the COVID-19 pandemic, and the unprecedented support that governments have committed to provide to their corporate and household sectors, European economies, including Italy, face an unprecedented challenge ahead.
- Even under our base case of an economic recovery starting in third-quarter 2020, we expect FCA Bank's earnings and asset quality to weaken through end-2020 and into 2021; we note, however, the bank's sufficient capital buffer to mitigate the impact.
- We are therefore affirming our 'BBB/A-2' ratings on FCA Bank.
- The outlook remains negative mirroring that on the Italian sovereign. We think that the support available from FCA Bank's parent, CASA, remains substantial and sufficient to compensate for the downside risks FCA Bank is facing.

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Rating Action

S&P Global Ratings today affirmed its 'BBB/A-2' issuer credit ratings on FCA Bank. The outlook remains negative.

Rationale

Today's rating action follows our review of several Western European banking sectors. We expect this pandemic to cause a severe recession in Europe and in Italy in particular in 2020. While we see a recovery in 2021, we anticipate it will not immediately and entirely offset the damage caused to the economy, household wealth, and various corporate sectors.

COVID-19 will also severely affect the automotive sector. We expect a material decline of light vehicle demand globally, particularly in the second quarter of the year (see "COVID-19 Will Batter Global Auto Sales And Credit Quality," published March 23, 2020). This is particularly relevant for

FCA Bank due to its business focus on car sales financing, which means its revenues are highly correlated with the dynamics of automotive sector sales.

The outlook remains negative, reflecting the outlook on the Republic of Italy.

Under our economic base case, we expect a meaningful deterioration of FCA Bank's asset quality, revenues, and profitability through 2020 and into 2021. More specifically, we forecast revenues to decline by about 10%-12% in 2020 and cost of risk to peak at 70-80 basis points (bps) from 17 bps as of end-2019. Despite pressure on its earnings, we forecast FCA Bank's risk-adjusted capital (RAC) to remain above 10% by end-2022 compared to the 11.0%-11.5% we estimate for year-end 2019.

We have affirmed our ratings on FCA Bank. This reflects the resilience that we expect the bank to demonstrate in the face of this short-term cyclical event, supported by better-than-peers capital buffers able to absorb the expected earnings decline. Our affirmation also factors in the funding support we expect from French banking group Crédit Agricole SA (CASA), its 50% owner, over the upcoming quarters in line with the terms of the joint-venture (JV) agreement. Considering that funding and liquidity are the main risks for the bank's predominantly wholesale-funded business model, having a strong and creditworthy owner is a clear strength that supports our 'BBB' rating on the bank.

As FCA Bank is an important pillar in CASA's business strategy in consumer finance, we continue to consider FCA Bank as a strategically important subsidiary. We think that CASA will provide support, if needed, to preserve the value of an otherwise profitable subsidiary.

We consider the merger between Fiat Chrysler Automotive and Peugeot S.A. in 2021 more crucial than ever. We think that following the merger, FCA and Peugeot might reconsider their respective long-term strategies for their captive finance subsidiaries. We will therefore monitor how the new group's JV agreements develop, and how this might affect FCA Bank.

Outlook

The negative outlook on FCA Bank SpA mirrors that on Italy and reflects that we could lower the rating over the next 18-24 months. We consider FCA Bank to be a strategically important subsidiary of CASA. Despite its strategically important status, we incorporate only one notch of group support into the ratings because we consider that the uplift for group support for strategically important subsidiaries cannot lead to the subsidiary being rated above its sovereign. In FCA Bank's case, this reflects our opinion that potential extraordinary support from CASA would not be sufficient to allow FCA Bank to withstand a sovereign default stress scenario.

Absent a sovereign downgrade, a downward revision of FCA Bank's stand-alone credit profile--for example due to a deterioration in the economies in which FCA Bank operates (particularly Italy, France, U.K., and Spain) that hits the bank's profitability and capitalization--would not lead us to lower the ratings on FCA Bank. This is because we would incorporate an additional notch of support from CASA, given our view of FCA Bank's importance for the French group.

We would revise the outlook to stable if we revised our outlook on Italy to stable.

Ratings Score Snapshot

Issuer Credit Rating	BBB/Negative/A-2
SACP	bbb-

Anchor	bbb
Business Position	Weak (-2)
Capital and Earnings	Strong (+1)
Risk Position	Adequate (0)
Funding and Liquidity	Average and adequate (0)
Support	1
ALAC Support	0
GRE Support	0
Group Support	1
Sovereign Support	0
Additional Factors	0

Related Criteria

- 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: Ratings Above The Sovereign--Corporate And Government Ratings: Methodology And Assumptions, Nov. 19, 2013
- Criteria | Financial Institutions | Banks: Assessing Bank Branch Creditworthiness, Oct. 14, 2013
- Criteria | Financial Institutions | Banks: Quantitative Metrics For Rating Banks Globally: Methodology And Assumptions, July 17, 2013
- Criteria | Financial Institutions | Banks: Banks: Rating Methodology And Assumptions, Nov. 9, 2011
- Criteria | Financial Institutions | Banks: Banking Industry Country Risk Assessment Methodology And Assumptions, Nov. 9, 2011
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009

Related Research

- Outlooks On Most Italian Banks Now Negative On Deepening COVID-19 Downside Risks, April 29, 2020
- How COVID-19 Risks Prompted European Bank Rating Actions, April 2020
- Italy 'BBB/A-2' Ratings Affirmed; Outlook Negative, April 24, 2020
- Europe Braces For A Deeper Recession In 2020, April 20, 2020
- European Banks' First-Quarter Results: Many COVID-19 Questions, Few Conclusive Answers, April 1, 2020
- COVID-19 Countermeasures May Contain Damage To Europe's Financial Institutions For Now,

March 13, 2020

- Italian Banks Not Adapting To The Digital World Quickly Will Be Left Behind, Feb. 17, 2020
- The Coronavirus Pandemic Is Set To Test The Resiliency Of Italy's Banks, March 13, 2020

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. A description of each of S&P Global Ratings' rating categories is contained in "S&P Global Ratings Definitions" at https://www.standardandpoors.com/en_US/web/guest/article/-/view/sourceId/504352 Complete ratings information is available to subscribers of RatingsDirect at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column. Alternatively, call one of the following S&P Global Ratings numbers: Client Support Europe (44) 20-7176-7176; London Press Office (44) 20-7176-3605; Paris (33) 1-4420-6708; Frankfurt (49) 69-33-999-225; Stockholm (46) 8-440-5914; or Moscow 7 (495) 783-4009.

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