

Rating Action: Moody's affirms Volvofinans Bank's A3 deposit ratings, changes outlook to stable from negative

06 Apr 2021

Stockholm, April 06, 2021 -- Moody's Investors Service ("Moody's") today affirmed Volvofinans Bank AB's long-term and short-term, foreign and local currency A3/P-2 bank deposit ratings and its subordinated debt rating at Baa3. The Baseline Credit Assessment (BCA) and the Adjusted BCA were affirmed at baa2. Furthermore, the long-term and short-term, foreign and local currency Counterparty Risk Ratings (CRR) of A2/P-1, and the long-term and short-term Counterparty Risk Assessments (CR Assessment) of A2(cr)/P-1(cr) were affirmed. The outlook on the long-term deposit rating was changed to stable from negative.

The affirmation of Volvofinans Bank AB's (Volvofinans) long-term deposit rating of A3 incorporates (1) the affirmation of the bank's baa2 BCA, reflecting Moody's expectation of a moderate deterioration in asset risk, balanced against the protection afforded to the bank by its recourse agreements with Volvo dealers and Volvofinans' very strong capitalisation; and (2) the results from Moody's Advanced Loss Given Failure (LGF) analysis, which takes into account the sizable volumes of liabilities that would cushion depositors in case of failure, leading to two notches of uplift.

The stable outlook on Volvofinans' long-term deposit ratings reflects the continued recovery in global light vehicle sales during the next 12 to 18 months, which reduced Moody's concerns of downside risks materializing. Accordingly, the stable outlook also factors in the bank's links with the car maker, Volvo Car AB (Ba1, Stable), whose ratings outlook changed to stable, from negative, on 30 March.

A full list of affected ratings can be found at the end of this press release.

RATINGS RATIONALE

BASELINE CREDIT ASSESSMENT

The affirmation of Volvofinans' BCA at baa2 reflects Moody's view that the expected moderate deterioration in the bank's asset risk, due to weaker borrowers not being able to meet timely repayments as the pandemic continues into 2021, is mitigated by its very strong capitalisation, as well as the additional protection the bank has against loan losses from the recourse agreements it has with Swedish Volvo dealers. While reported non-performing loans and leases to gross exposures has remained low at 0.6% in 2020 compared to 0.2% in 2019.

While, demand for new vehicles fell sharply in 2020, the used car market remained strong, and Moody's expects a growth of new car sales in 2021. Profitability during 2020 was stronger than Moody's previously expected, with reported operating results increasing to SEK 568 million compared to SEK 516 million in 2019 as loans and leases were upheld and loan loss provisions remained manageable at SEK 21.7 million compared to SEK 16 million in 2019. The rating agency expects continued strong performance during 2021 with net income to tangible assets of 0.8%.

Continued internal capital generation and low loan loss provisions support the bank's strong capitalisation, a material credit strength, with tangible common equity to risk weighted assets to remain above 21% excluding dividends for 2019 and 2020.

Volvofinans funding position remains stable, with a larger share of deposits compared to other auto lenders. During 2020, Volvofinans was designated as a temporary monetary policy counterpart, ensuring that it could access additional liquidity made available by the Swedish central bank. The continued monetary stimulus has ensured excellent access to capital market with lower cost of funding as a result.

LONG-TERM RATINGS

Volvofinans long-term deposit and subordinated debt ratings reflect the bank's BCA and Adjusted BCA of baa2 and the application of Moody's Advanced Loss Given Failure (LGF) analysis to its liabilities, reflecting the volumes of loss absorbing obligations protecting creditors and depositors in case of failure. The A3 deposit rating incorporates two notches of uplift from the bank's Adjusted BCA due to the large volumes of more junior

obligations protecting depositors in case of failure. The Baa3 rating on Volvofinans subordinated debt incorporates a negative notch due to the higher loss severity, given this instrument's limited protection from losses.

Volvofinans's long-term CRRs incorporates three notches of LGF uplift above the bank's Adjusted BCA of baa2. Volvofinans long-term CR Assessment incorporates three notches of LGF uplift above the bank's Adjusted BCA of baa2.

OUTLOOK

The stable outlook on Volvofinans' long-term deposit ratings reflects the continued recovery in global light vehicle sales during the next 12 to 18 months. This trend has reduced Moody's concerns of downside risks materializing. During 2021, the rating agency expects Volvofinans's problem loans ratio to remain below 2%, and tangible common equity to risk weighted assets to remain above 21%, while profitability remains overall stable. The stable outlook also factors in the bank's links with the car maker, Volvo Car AB, whose ratings changed to stable outlook on 30 March, 2021. The press release regarding Volvo Car AB can be found here: https://www.moodys.com/research/--PR_442994.

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

Volvofinans' ratings and assessments could be upgraded if the bank strengthens its profitability without accumulating more credit risk and further reduces its reliance on market funding while simultaneously maintaining solid capitalisation.

We could downgrade Volvofinans' BCA and long-term deposit ratings if: i) its profitability and asset quality significantly deteriorate; ii) the bank is constrained by a lack of access to wholesale funding; iii) or a substantial reduction in its volume of deposits compared with its tangible banking assets, resulting in higher loss severity for deposits in the event of the bank's failure.

Furthermore, notwithstanding the fact that Volvofinans is more effectively ring-fenced from its industrial parent than certain peers, a downgrade of Volvo Car AB's ratings could cause a downgrade of Volvofinans' ratings.

LIST OF AFFECTED RATINGS

..Issuer: Volvofinans Bank AB

Affirmations:

...Adjusted Baseline Credit Assessment, Affirmed baa2

...Baseline Credit Assessment, Affirmed baa2

...Long-term Counterparty Risk Assessment, Affirmed A2(cr)

...Short-term Counterparty Risk Assessment, Affirmed P-1(cr)

...Long-term Counterparty Risk Ratings, Affirmed A2

...Short-term Counterparty Risk Ratings, Affirmed P-1

...Short-term Bank Deposit Ratings, Affirmed P-2

...Subordinate Regular Bond/Debenture, Affirmed Baa3

...Long-term Bank Deposit Ratings, Affirmed A3, Outlook Changed To Stable From Negative

Outlook Action:

...Outlook, Changed To Stable From Negative

PRINCIPAL METHODOLOGY

The principal methodology used in these ratings was Banks Methodology published in March 2021 and available at https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_1261354. 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.moody.com/researchdocumentcontentpage.aspx?docid=PBC_79004.

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