Research Update:

RCI Banque 'BBB/A-2' Ratings Affirmed Despite Renault Downgrade; Outlook Remains Negative

April 10, 2020

PRIMARY CREDIT ANALYST

Mathieu Plait
Paris
(33) 1-4420-7364
mathieu.plait@spglobal.com

SECONDARY CONTACT

Nicolas Malaterre
Paris
(33) 1-4420-7324
nicolas.malaterre@spglobal.com

Overview

- We lowered our long-term rating on carmaker Renault S.A. to 'BB+/B' from 'BBB-/A-3' on April 9, 2020.
- Renault's captive finance bank, RCI Banque, has strong financial performance and capitalization, with less cyclical revenue than its parent. We expect it will maintain a robust financial profile as it navigates the COVID-19 pandemic.
- We are therefore affirming our 'BBB/A-2' long- and short-term issuer credit ratings on RCI Banque.
- The negative outlook indicates that we could lower the ratings on RCI in 2020-2021 if we take a similar action on Renault. It also continues to reflect the risk that the mixed financial performance of Renault's industrial activities and other group challenges could have negative contagion effects on RCI, notably regarding funding costs, access to capital markets, and operating performance.

Rating Action

On April 10, 2020, S&P Global Ratings affirmed its 'BBB/A-2' long- and short-term issuer credit ratings on France-based RCI Banque (RCI) and its core subsidiary DIAC S.A. The outlooks on both entities remain negative. We also affirmed the issue ratings on all rated debt.

Rationale

The affirmation follows a review of RCI after the downgrade of its sole parent, Renault S.A. (BB+/Negative/B). We believe that Renault and other global automakers will face intense credit pressures resulting from the COVID-19 pandemic and drastic measured to contain it. As stated in our previous outlooks, we now rate RCI two notches above its parent, due to the bank's more predictable and stable revenues than its more-cyclical parent.

The 'BBB' rating on RCI reflects the bank's financial strength. We include one notch of uplift above the 'bbb-' stand-alone credit profile (SACP) to reflect RCI's outperformance of similarly rated peers over a long cycle, particularly capital generation capabilities and risk-adjusted operating performance. We view RCI's earnings buffer--defined as the capacity for operating earnings to cover normalized losses--as strong, exceeding 2% of our risk-weighted assets over time. We expect this buffer to remain firmly above 2% in the next two years despite challenges from the COVID-19 pandemic; this is strong for a bank operating in relatively low-risk countries. While we do not expect RCI to be immune to the impacts of COVID-19, we note that it is entering this uncertain environment on a strong footing. It has solid earning capacity, a low cost-to-income ratio at about 30%, and strong capitalization, with an expected S&P Global Ratings risk-adjusted capital (RAC) ratio above 11% at year-end 2019. Refinancing needs are lower in 2020 than in recent years at about €1.5 billion-€2 billion, of which €750 million was already issued in January, compared with an average of €3 billion-€4 billion for previous years. Return on equity was about 18% in 2019. Nevertheless, we note that RCI has significant exposure to the car dealers, mostly in France, which could be materially affected by the pandemic. They represented about 23.3% of the loan book at end 2019 and we expect this proportion will increase over the coming months. We will closely monitor such exposures and any rise in risks. We expect many dealers to benefit, if needed, from the French government's measures to ease pressure on local businesses during the pandemic, which could alleviate the pressure on their creditworthiness.

In our view, RCI's overall creditworthiness is commensurate with a 'BBB' long-term issuer credit rating when compared with peers. In recent years, it has continued to improve its market penetration (42.2% as of year-end 2019, up from 35.2% as of 2014). The bank is also gradually broadening its business mix toward fees and services, which along with its increased penetration rate, supports revenue resilience and customer loyalty, and ultimately strong profitability. Over the past decade, the bank has shown extremely modest revenue volatility, despite auto market depressions, and benefitted from a lean cost structure, with no branches and good pricing power. These features help RCI weather auto cycles well. In particular, it enjoys annuity-like revenue spread across a loan's term, and generates predictable and strong profits, despite its concentration in auto finance. We also note that part of its funding comprises retail deposits, which are less price sensitive to any deterioration of Renault's creditworthiness than debt issuances.

However, RCI's business model and name affiliation do not fully shield the bank from developments in the auto sector and Renault-specific challenges. Amid a tough market environment for carmakers, with fierce competition, tightening carbon dioxide regulations in Europe, and lower dividends from Nissan, Renault has identified a set of initiatives to improve its operational performance. These include the optimization of its industrial footprint and outsourcing activities, a review of noncore assets, and the new leader-follower strategy with alliance partners Nissan and Mitsubishi. We expect the company to publish a detailed plan in May 2020. Last but not least, we now project the impact of the COVID-19 pandemic will lead to a decline in global auto sales of about 15% in 2020, followed by a recovery in sales volumes of 6%-8% in 2021, adding further challenges for the group. Although they mostly relate to Renault's industrial activities, these challenges could affect RCI, especially its funding costs. RCI is primarily wholesale funded and the success of its business model depends on its capacity to access debt markets regularly and at nonprohibitive costs. Therefore, we believe the bank can smooth the effects of the lower car sales expected in 2020 and flat auto sales over time, but it is not immune to Renault's potential difficulties. We believe the bank may struggle to sustain above-average profitability metrics in 2020-2021 if pressures on the auto market intensify and if gradual changes in investor sentiment lead to rising funding costs. The negative outlook also reflects this risk.

We believe RCI is insulated from its 100% owner, Renault, due to France's favorable insolvency laws and its regulated status as a bank, supervised by the European Central Bank and the French regulator. This means there is limited capacity for the parent to repatriate cash flows outside the regulatory perimeter, a high degree of operational independence, and total funding independence. Therefore, we rate the bank above its parent and allow a rating differential of up to two notches, a level that is now reached.

Outlook

The negative outlook indicates that we could lower the ratings on RCI in 2020-2021 if we take a similar action on Renault. This is because we maintain our view that RCI cannot be rated more than two notches above its parent. We could also lower the ratings if the bank's earnings capacity stopped outperforming similarly rated peers. This could be due to intensifying pressures on the auto market resulting from COVID-19 containment measures, or rising funding costs and difficult access to capital markets as a result of contagion risk from Renault.

Downside scenario

A downgrade of Renault would entail a similar downgrade of RCI.

Irrespective of our rating on Renault, we could remove the notch of flexibility and lower the long- and short-term issuer credit ratings on RCI to 'BBB-/A-3' if contagion risks start to crystallize and affect RCI's access to debt markets, or cost of funding. This could be the case if the challenges faced by Renault or tensions within the alliance negatively affect RCI's operations and activities, notably regarding funding costs and strategic focus, or if the intense pressure we see in the auto market partly resulting from the COVID-19 pandemic, reduces RCI's profitability and new business volumes beyond our expectations.

Upside scenario

We would revise the outlook to stable in 2020-2021 if we took a similar action on Renault and if our view of RCI's stand-alone creditworthiness remained unchanged and resilient to COVID-19 impacts and to challenges faced by the parent and the auto sector as a whole.

Ratings Score Snapshot

Issuer Credit Rating	BBB/Negative/A-2
SACP	bbb-
Anchor	bbb+
Business Position	Weak (-2)
Capital & Earnings	Strong (+1)
Risk Position	Adequate (0)
Funding and Liquidity	Below Average and Adequate (-1)
Support	0
ALAC Support	0
GRE Support	0

Group Support	0
Sovereign Support	0
Additional factors	+1

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
- Criteria | Financial Institutions | Banks: Bank Rating Methodology And Assumptions: Additional Loss-Absorbing Capacity, April 27, 2015
- 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
- Criteria | Financial Institutions | Banks: Commercial Paper I: Banks, March 23, 2004

Related Research

- French Automaker Renault Downgraded To 'BB+/B' On Weaker Metrics Due To COVID-19; Outlook Negative, April 9, 2020
- COVID-19 Will Batter Global Auto Sales And Credit Quality, March 23, 2020
- RCI Banque 'BBB/A-2' Ratings Affirmed Despite Renault CreditWatch Negative Placement; Outlook Negative, Feb. 20, 2020
- RCI Banque, Aug. 22, 2019

Ratings List

Ratings Affirmed	
RCI Banque	
Issuer Credit Rating	BBB/Negative/A-2
Senior Unsecured	BBB
Subordinated	BB

Ratings Affirmed	
DIAC S.A.	
Issuer Credit Rating	BBB/Negative/A-2