

Research Update:

RCI Banque 'BBB/A-2' Ratings Affirmed Despite Renault CreditWatch Negative Placement; Outlook Negative

February 20, 2020

Overview

- On Feb. 19, 2020, S&P Global Ratings placed the 'BBB-/A-3' long- and short-term issuer credit ratings on French carmaker Renault on CreditWatch with negative implications.
- However, we are affirming our 'BBB/A-2' long- and short-term issuer credit ratings on Renault's captive finance bank RCI Banque (RCI).
- The affirmation is supported by RCI's strong financial performance in 2019 and our expectation that it will continue to maintain a stable and solid financial profile, with less cyclical revenue than its parent.
- The negative outlook continues to reflect the risk that the mixed financial performance of Renault's industrial activities and other group challenges--such as tightening carbon dioxide regulations and its strategy with alliance partners Nissan and Mitsubishi--could have negative contagion effects on RCI, notably regarding funding costs and operating performance.

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Rating Action

On Feb. 20, 2019, 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. 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 its sole parent Renault S.A. (BBB-/Watch Neg/A-3) was placed on CreditWatch with negative implications. We currently rate RCI one notch above its parent, due to the bank's more predictable and stable revenue than its more-cyclical parent.

The 'BBB' rating on RCI reflects the bank's stand-alone 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. This particularly includes 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 it to remain firmly above 2% in the next two years, which is strong for a bank operating in low-risk countries.

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% as of 2014). The bank is also gradually broadening its business mix toward fees and services, which along with its increased penetration rate, positively supports revenue resilience and customer loyalty, and ultimately strong profitability. Over the past decade, the bank has shown extremely modest revenue volatility, even during a depressed auto market, 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. Although they mostly relate to Renault's industrial activities, these challenges could affect RCI, especially regarding 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 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 the next 18-24 months if pressures on the auto market intensify, with repercussions on new business volumes, and if gradual changes in investor sentiment lead to rising funding costs.

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 already rate the bank above its parent and could allow a rating differential of up to two notches.

Outlook

The negative outlook indicates that we could lower the ratings on RCI in the coming 18-24 months if the bank's earnings capacity stopped outperforming similarly rated peers. This could be due to intensifying pressures on the auto market, or if we see contagion risk from Renault's difficulties on RCI's funding costs. However, we maintain our view that RCI can be rated above its parent by up to two notches. A downgrade of Renault by one notch would also not automatically entail a downgrade of RCI, but would certainly trigger a deeper review on the bank's capacity to sustain its financial performance and funding profile in this context.

Downside scenario

Specifically, and irrespective of Renault, we may remove one notch of flexibility and lower the long- and short-term issuer credit ratings to 'BBB-/A-3' if those contagion risks start to crystallize and affect RCI's access to, or cost of, funding. This could be the case if tensions within the alliance negatively affect RCI's operations and activities, notably regarding funding costs and strategic focus, or if the pressure we see in the auto market negatively affects its profitability and new business volumes. Although less likely, we may also lower the long- and short-term issuer credit ratings to 'BBB-/A-3' if we downgrade Renault by more than one notch.

Upside scenario

We would revise the outlook to stable in the next 12-24 months if our view of RCI's stand-alone creditworthiness remains unchanged and resilient to parent and sector challenges.

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

- Renault S.A. Ratings Placed on CreditWatch Negative On Expected Further Depressed Free Cash Flow Generation, Feb. 19, 2020
- RCI Banque 'BBB/A-2' Ratings Affirmed On High Operating Performance Despite Renault Downgrade; Outlook Remains Negative, Oct. 28, 2019
- RCI Banque, Aug. 22, 2019

Ratings List

Ratings Affirmed

RCI Banque

Issuer Credit Rating	BBB/Negative/A-2
Senior Unsecured	BBB
Subordinated	BB

DIAC S.A.

Issuer Credit Rating	BBB/Negative/A-2
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