Research Update:

DRAFT: Grenke AG Outlook Revised To Negative On Heightened Macroeconomic COVID-19 Risks; 'BBB+/A-2' Ratings Affirmed

April 20, 2020

Vendor: S&PGR Revises Grenke AG Outlook To Neg; Afrms 'BBB+/A-2' Rtgs

Overview

- Despite governments' measures to contain the COVID-19 pandemic, it provides an unprecedented challenge to the key economies in Grenke's countries of operation, including Germany and France.
- Under our base case, economic recovery will only start in the third quarter of 2020, so we expect the bank's earnings, asset quality, and capitalization will be lower this year than we previously envisaged.
- We are revising our outlook on Grenke to negative from stable and affirming our 'BBB+/A-2' issuer credit ratings on the bank.
- The negative outlook reflects our view that Grenke faces tougher economic conditions in its main European markets over the next 18-24 months.

Rating Action

On April 23, 2020, S&P Global Ratings revised its outlook on Grenke AG to negative from stable. At the same time, we affirmed our 'BBB+/A-2' long- and short-term issuer credit ratings on the bank, as well as the issue ratings on the bank's debt.

Rationale

The outlook revision reflects our view that Grenke's creditworthiness could be vulnerable to the rapid deterioration of economic conditions that has taken place in recent weeks. The bank is a specialist lender, focusing mainly on small ticket information technology-leasing across many European countries. The COVID-19 pandemic and sudden stop of the global economy have led us
to sharply revise our GDP forecasts. We now expect a global recession in 2020, which will materially harm the economies to which Grenke is heavily exposed—particularly Germany, Italy, and France. Furthermore, despite ample fiscal stimulus, credit losses for banks in these markets will likely start to rise through 2020.

We have affirmed our ratings on Grenke because we think it will enter the anticipated recession with solid profitability compared to peers, superior capitalization, and sound asset quality. Although we anticipate much worsened operating credit conditions in Grenke’s main markets, we expect a manageable increase in the bank’s cost of risk, nonperforming loan levels, and similar risk metrics. We view positively the high granularity and collateralization of Grenke’s portfolios, and comparably high risk-adjusted margins that provide a substantial buffer to absorb a rise in credit losses. Accordingly, we continue to anticipate that Grenke will maintain its very strong capitalization—we forecast the bank’s S&P Global Ratings risk-adjusted capital (RAC) ratio to remain at 15%-16% over the coming 12 to 24 months.

S&P Global Ratings acknowledges a high degree of uncertainty about the rate of spread and peak of the coronavirus outbreak. Some government authorities estimate the pandemic will peak between June and August, and we are using this assumption in assessing the economic and credit implications. We believe the measures adopted to contain COVID-19 have pushed the global economy into recession (see our macroeconomic and credit updates here: www.spglobal.com/ratings). As the situation evolves, we will update our assumptions and estimates accordingly.

**Outlook**

The negative outlook reflects our view that Grenke faces tougher economic conditions in its main European markets over the next 18-24 months, as well as the broader negative industry risk trend that we see for the German banking industry.

**Downside scenario**

We would likely lower the ratings on Grenke if we considered its operating environment to have further deteriorated, leading to a material weakening of its asset quality or earnings. We could reflect such pressures through a revision of our assessment of German bank economic or industry risks, for example. Although less likely, we could also lower our rating on Grenke if the bank's RAC ratio dropped below our forecasted 15% threshold.

**Upside scenario**

We could revise our outlook back to stable if we saw a sustainable and material improvement in the macroeconomic market environment in the main regions where Grenke operates. An outlook revision to stable would also depend on the bank demonstrating ongoing superior profitability compared with peers. A positive rating action is very unlikely given Grenke is smaller than its peers and it has a niche business model with a material reliance on wholesale funding.

**Ratings Score Snapshot**
Grenke AG -- Ratings Score Snapshot

**Issuer Credit Rating**: BBB+/Negative/A-2

<table>
<thead>
<tr>
<th>Component</th>
<th>Rating</th>
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<tbody>
<tr>
<td>SACP</td>
<td>bbb</td>
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<tr>
<td>Anchor</td>
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<td>Sovereign Support</td>
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<tr>
<td>Additional Factors</td>
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</tr>
</tbody>
</table>

ALAC—Additional loss-absorbing capacity. GRE—Government-related entity. SACP—Stand-alone credit profile.

**Related Criteria**

- General Criteria: Hybrid Capital: Methodology And Assumptions, July 1, 2019
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- Criteria | Financial Institutions | Banks: Quantitative Metrics For Rating Banks Globally: Methodology And Assumptions, July 17, 2013
- Criteria | Financial Institutions | Banks: Banking Industry Country Risk Assessment Methodology And Assumptions, Nov. 9, 2011
- Criteria | Financial Institutions | Banks: Rating Methodology And Assumptions, Nov. 9, 2011
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009

**Related Research**

- European Banks' First-Quarter Results: Many COVID-19 Questions, Few Conclusive Answers, April 1, 2020
- COVID-19: The Steepening Cost To The Eurozone And U.K. Economies, March 26, 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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