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Fitch Downgrades Santander BP's VR to 'bbb'; Affirms IDR at 'BBB+'; Outlook Stable

Fitch Ratings - Warsaw - 14 Sep 2022: Fitch Rating has downgraded Santander Bank Polska S.A.'s (Santander BP) Viability Rating (VR) to 'bbb' from 'bbb+' and removed it from Rating Watch Negative (RWN). At the same time we have affirmed the bank's Long-Term Issuer Default Rating (IDR) at 'BBB+' with a Stable Outlook. A full list of rating actions is below.

The downgrade of the VR and removal from RWN reflects the increased pressure on Santander BP's credit profile from the Polish operating environment, which has been downgraded to 'bbb' from 'bbb+' due to the rise in the risk of government intervention in the Polish banking sector (see 'Fitch Places 5 Polish Banks' VRs and 3 IDRs on RWN' published on 5 August 2022 on www.fitchratings.com).

Fitch has withdrawn Santander BP's Support Rating of '2' as it is no longer relevant to the agency's coverage following the publication of its updated Bank Rating Criteria on 12 November 2021. In line with the updated criteria, we have assigned Santander BP a Shareholder Support Rating (SSR) of 'bbb+'.

Key Rating Drivers

Santander BP's IDR and SSR are driven by a high probability of support from its parent, Banco Santander S.A. (A-/Stable/a-). The Stable Outlook reflects that on the parent. The bank's Short-Term IDR of 'F2' is the lower of two options for a Long-Term IDR of 'BBB+' and is in line with Banco Santander's Short-Term IDR. The National Ratings reflect the bank's creditworthiness relative to Polish peers and are driven by potential support from Banco Santander.

Santander BP's VR balances the bank's solid capital position, healthy funding and liquidity, recovering earnings and reasonable asset quality against the risks from the operating environment, which impact the bank's business and risk profiles. Additionally, the need to set aside legal risk provisions related to the bank's foreign-currency (FC) mortgage portfolio weigh on the bottom line.

Parent Support: Santander BP's IDR is driven by a high probability of support from its parent, Banco Santander, in case of need. The support consideration reflects the strategic importance of the Polish market to the parent and Santander BP's role in the group. The bank's synergies with its parent are strong and underpinned by a solid record of supporting its parent's objectives, which is likely to continue. In our opinion, any required support for the bank would be immaterial relative to its parent's ability to provide it.

Intervention Risk Weighs on Operating Environment: Fitch has downgraded the Polish banks' operating environment score. This reflected its view that the recently introduced payment holidays on

local-currency mortgages are further evidence of the willingness of the Polish authorities to intervene in the banking sector and impose large additional costs on banks. This most recent measure comes in addition to the sizeable bank tax and as banks need to make substantial provisions for legal risks relating to Swiss franc mortgage loans. The authorities have been also putting pressure on banks to increase deposit rates.

Solid Capitalisation: Capitalisation is strong, underpinned by high regulatory capital ratios, solid capital buffers above minimum requirements, low leverage and a robust recovery in internal capital generation. We expect the bank's capital ratios to remain resilient, underpinned by a healthy recovery in profitability, even accounting for the significant one-off charges.

Diversified Business Profile: Santander BP is the third-largest bank in Poland with about 11% market shares and diversified loan portfolio serving a broad range of retail and non-retail, where the bank maintains solid market shares. Its business mix allowed it to significantly benefit from rising interest rates.

Moderate Risk Profile: Santander BP's risk profile reflects the operating environment risks and its somewhat higher appetite for riskier segments, compared with peers, such as mass-market consumer lending. The bank's risk profile is additionally weighed by moderate exposure to legal risks from its FC mortgage portfolio.

Reasonable Asset Quality: The bank's asset quality has remained fairly resilient, underpinned by robust loan growth and low generation of problem loans. However, we expect the bank's asset quality will weaken gradually as energy prices, inflationary pressures and higher borrowing costs weigh on borrowers' repayment capacity, especially among business clients.

Recovering Earnings: Profitability has showed a robust recovery underpinned by widening net interest margins as market rates have increased but profit in 2H22 will be weighed down by the significant charges related to payment holidays and the contribution to the borrower support fund. We expect profitability to remain solid in 2023 but cost inflation, rising loan impairment charges and low lending growth will start to weigh on underlying profits.

Robust Funding and Liquidity: Robust funding and liquidity reflect high self-financing capacity, funding based on granular customer deposits, strong coverage of short-term liabilities by liquid assets and potential ordinary parental support. At end-1H22, the gross loans-to-customer deposits ratio remained stable at 87%. Liquidity is strong and covers moderate refinancing needs over the next 12 months. Regulatory liquidity ratios remain well above requirements.

Rating Sensitivities

Factors that could, individually or collectively, lead to negative rating action/ downgrade:

A downgrade of Banco Santander's IDR would drive a downgrade of Santander BP's IDR and SSR.

Santander BP's VR has sizeable rating headroom. The ratings could be downgraded if the operating

environment was downgraded or if the negative impact of the weakening economic environment results in deterioration of key financial metrics materially beyond our expectations, or if further government interventions lead to high additional costs for the sector, including Santander BP. In particular this could happen if the impaired loans ratio rises above 8% on a sustained basis or if the common equity Tier 1 ratio falls below 13% without prospects for improvement.

Santander BP's National Ratings are sensitive to a downgrade of the bank's IDR.

Factors that could, individually or collectively, lead to positive rating action/upgrade:

An upgrade of Banco Santander's IDR would drive an upgrade of Santander BP's IDR and SSR.

An upgrade of the bank's VR would require an upgrade of the operating environment score for Polish banks coupled with Santander BP maintaining its robust financial profile.

Santander BP's National Ratings are sensitive to an upgrade of the bank's IDR.

OTHER DEBT AND ISSUER RATINGS: KEY RATING DRIVERS

Santander BP's senior preferred debt is rated in line with the bank's Long-Term IDR, because we do not expect the bank to meet its resolution buffer with the level of senior non-preferred debt and more junior debt that would sustainably exceed 10% of Santander BP's risk weighted assets (RWAs). This predominantly reflect the bank's high levels of common equity Tier 1 capital relative to its resolution requirements as well as sizable allowance to meet resolution requirements with senior preferred debt.

Santander BP must comply with resolution buffers set under both total loss-absorbing capacity (TLAC) and minimum requirements for own funds and eligible liabilities (MREL). The bank's TLAC requirement stands at 21.25%, excluding combined buffer requirement, of which 3.5pp can be met with senior preferred debt, while the bank's fully loaded MREL requirement valid from end-2023 will be 15.41%, excluding the combined buffer requirement, which currently stands at 3.25% of RWAs.

OTHER DEBT AND ISSUER RATINGS: RATING SENSITIVITIES

Senior preferred debt ratings are primarily sensitive to changes in the bank's IDR. If we expect Santander BP to meet its resolution requirements with SNP and more junior instruments only, or if we expect Santander BP's SNP and more junior debt buffers to sustainably exceed 10% of RWAs, we would likely upgrade the bank's SP debt ratings and rate them one notch above the bank's IDR.

VR ADJUSTMENTS

The Asset Quality score of 'bbb' has been assigned above the implied score of 'bb' due to the following adjustment reason(s): Underwriting Standards and Growth (positive).

Best/Worst Case Rating Scenario

International scale credit ratings of Financial Institutions and Covered Bond issuers have a best-case rating upgrade scenario (defined as the 99th percentile of rating transitions, measured in a positive

direction) of three notches over a three-year rating horizon; and a worst-case rating downgrade scenario (defined as the 99th percentile of rating transitions, measured in a negative direction) of four notches over three years. The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Best- and worst-case scenario credit ratings are based on historical performance. For more information about the methodology used to determine sector-specific best- and worst-case scenario credit ratings, visit <https://www.fitchratings.com/site/re/10111579>

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

Public Ratings with Credit Linkage to other ratings

Santander BP's IDRs and SSR are linked to the IDRs of its parent, Banco Santander.

ESG Considerations

Santander BP's ESG Relevance Scores for Management Strategy is '4', reflecting our view of high government intervention risk in the Polish banking sector, which affects the bank's operating environment, its business profile and ability to define and execute on its strategy. This has a negative impact on its credit profile and is relevant to ratings in combination with other factors.

Unless otherwise disclosed in this section, the highest level of ESG credit relevance is a score of '3'. This means ESG issues are credit-neutral or have only a minimal credit impact on the entities, either due to their nature or the way in which they are being managed by the entities. For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg

Fitch Ratings Analysts

Jakub Kopiec, CFA

Director

Primary Rating Analyst

+48 22 103 3020

Fitch Ratings Ireland Limited spolka z ograniczona odpowiedzialnoscia oddzial w Polsce Krolewska 16, 00-103 Warsaw

Monika Panasiuk

Associate Director

Secondary Rating Analyst

+48 22 103 3028

Eric Dupont

Senior Director

Committee Chairperson

+33 1 44 29 91 31

Media Contacts






Peter Fitzpatrick

London

+44 20 3530 1103

peter.fitzpatrick@thefitchgroup.com

Rating Actions

ENTITY/DEBT	RATING		RECOVERY	PRIOR
Santander Bank Polska S.A.	LT IDR	BBB+ 	Affirmed	BBB+ 
	ST IDR	F2	Affirmed	F2
	Natl LT	AA(pol) 	Affirmed	AA(pol) 
	Natl ST	F1+(pol)	Affirmed	F1+(pol)
	Viability	bbb	Downgrade	bbb+ 
	Support	WD	Withdrawn	2
	Shareholder Support	bbb+	New Rating	
• Senior preferred	LT	BBB+	Affirmed	BBB+
• Senior preferred	ST	F2	Affirmed	F2

RATINGS KEY OUTLOOK WATCH

POSITIVE



NEGATIVE



RATINGS KEY OUTLOOK WATCH

EVOLVING



STABLE



Applicable Criteria

[Bank Rating Criteria \(pub.07 Sep 2022\) \(including rating assumption sensitivity\)](#)

[National Scale Rating Criteria \(pub.22 Dec 2020\)](#)

Additional Disclosures

[Solicitation Status](#)

Endorsement Status

Santander Bank Polska S.A. EU Issued, UK Endorsed

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