FitchRatings

Fitch Places Long-Term IDRs of 19 UK Banking Groups on RWN

Fitch Ratings-London-01 March 2019: Fitch Ratings has placed the Long-Term Issuer Default Ratings (IDR) of 19 UK banking groups on Rating Watch Negative. The banks' other ratings, including their Viability Ratings (VRs) and debt ratings are not affected by the rating action. The actions follow Fitch placing the UK's Long-Term IDR on RWN on 20 February.

The RWN reflects the heightened uncertainty over the ultimate outcome of the Brexit process and the increased risk that a disruptive 'no-deal' Brexit, where the UK leaves the EU without a withdrawal agreement in place, either in March or at the end of a short extension, could result in negative action on the UK banks, most likely with Negative Outlooks being assigned.

Fitch expects to resolve the RWN during 2Q19 in light of the modalities of the UK's scheduled exit from the EU. The RWN may be maintained for longer if Brexit negotiations are extended for a relatively short period of time and resolved after the outcome of these negotiations are known.

In the event of a disruptive 'no-deal' Brexit where the UK leaves the EU at end-March or after a short extension of Article 50, Fitch sees heightened probability that it would revise the Outlooks on the banks' Long-Term IDRs to Negative, as the impact on earnings, asset quality, liquidity and funding is likely to be negative. Banks may be able to take actions to mitigate this risk and maintain current ratings, but the level of uncertainty would likely still warrant a Negative Outlook, at least in the medium term.

Fitch believes that less diversified banks, or banks that are more exposed to highly cyclical sectors, or banks that target niche economic segments or borrowers are more vulnerable to the fall out of a disruptive 'no-deal' Brexit than the larger and more diversified banks. It is possible that in a no-deal scenario more vulnerable banks could remain on RWN for a longer period or be downgraded. However, we do not consider the risk of this to be sufficiently clear at this stage to place any bank's VR on RWN.

In the event a Brexit agreement is concluded either in March or at the end of a short extension, all else equal, the RWNs would be resolved and Outlooks likely be Stable. A longer extension of the Brexit process would also likely result in most banks' ratings reverting to Stable Outlook.

Fitch placed the UK's 'AA' Long-Term IDRs on RWN on 20 February to reflect the heightened uncertainty over the outcome of the Brexit process and an increased risk of a no-deal Brexit. The UK and EU finalised the withdrawal agreement and political declaration on future relations on 25 November. The agreement envisages a transition period lasting until the end of 2020. The UK government has so far been unable to secure parliamentary approval for the withdrawal agreement.

Political divisions in the UK have increased the likelihood of a 'no-deal' Brexit. A 'no-deal' Brexit is the default option implied by the process outlined in Article 50 of the Treaty on European Union and political divisions within the UK mean the risk of a no-deal remains heightened, even in the event of a short extension of Article 50.

Fitch believes that a 'no-deal' Brexit would lead to substantial disruption to UK economic and trade prospects, at least in the near term. The impact of a 'no-deal' Brexit on economic growth is highly uncertain, but a recession on the scale of that seen in the UK in the early 1990s, when real GDP declined by 2% over six quarters, would be a reasonable comparison for gauging the potential macroeconomic stress. At the same time, a fiscal and monetary policy response would follow a 'no-deal' Brexit, mitigating the negative impact on the macroeconomic outlook. Fitch believes that the increased risk of such economic disruption gives rise to downside risks for banks, mostly because it would put pressure on the banks' ability to execute their strategies and on their earnings, asset quality and funding profiles in a more difficult operating environment.

Fitch has placed the Long-Term IDRs of the following issuers and several of their subsidiaries on RWN. The issuers' other ratings are unaffected by the rating action.

Bank of Ireland (UK) Plc
Barclays plc
Close Brothers Group
The Co-operative Bank p.l.c
Coventry Building Society
CYBG PLC
HSBC Holdings plc
Investec Bank plc
Leeds Building Society
Lloyds Banking Group plc
Nationwide Building Society
Paragon Banking Group
Principality Building Society
The Royal Bank of Scotland Group plc
Santander UK Group Holdings plc
Skipton Building Society
Tesco Personal Finance Group Limited
Virgin Money Holdings (UK) Plc
Yorkshire Building Society

A full list of rating actions is at the end of this rating action commentary.

KEY RATING DRIVERS
Bank of Ireland (UK) Plc (BOIUK)
BOIUK's ratings reflect its modest franchise and relatively undiversified business model concentrated on the UK mortgage and savings market. Its asset quality and profitability are sound and liquidity is solid. The ratings also reflect improved capitalisation.

Barclays plc, Barclays Bank plc, Barclays Bank UK plc, Barclays Bank Ireland
Barclays plc's Long-Term IDR and VR reflect our view of the consolidated risk profile of the group and its two main operating banks, Barclays Bank plc and Barclays Bank UK plc, for which it acts as a holding company. Barclays plc's, Barclays Bank UK plc' and Barclays Bank plc's VRs are aligned because we view interlinkages as strong and that there is a high probability of ordinary support flowing between the entities, given the group oversight of the operating banks' strategy, treasury and risk management.

Barclays plc's Long-Term IDR reflects its ability to maintain capital ratios on track with targets, in particular through stronger earnings contribution as the group's earnings path has become more predictable, notwithstanding some volatility in its capital markets businesses. However, the absolute level of earnings is still weak relative to domestic and international peers. The group's sound funding and liquidity profile underpins the ratings as do the group's sound franchises in UK retail, cards and commercial banking and in select investment banking businesses in the UK and US.

The Long-Term IDRs of Barclays Bank plc and Barclays Bank UK plc are rated a notch above their respective VRs, reflecting sufficient amounts of junior debt, including from the holding company, available to protect external senior debt holders of both banks. Barclays Bank Ireland's Long-Term IDR is equalised with Barclays Bank plc's, reflecting its core strategic importance and high level of integration with the parent, as well as availability of junior debt from the parent.

Close Brothers Group PLC (CBG) and Close Brothers Limited (CBL)
The ratings of CBG and CBL reflect consistently strong earnings, which are exceptional in the context of UK peers, driven by a fairly granular and diversified business model, good franchises in its chosen niche sectors and a broadly consistent strategy. However, CBG's and its main operating subsidiary CBL's appetite for higher-risk lending, mainly concentrated in the UK, and a less resilient funding profile than larger domestic peers are rating weaknesses.

The Co-operative Bank p.l.c
The Co-operative Bank's ratings primarily reflect the bank's structural unprofitability due to its high cost base combined with pressure on its net interest margin, given stiff competition in UK retail banking, and low interest rates. We believe that its ability to return to underlying profitability over the medium term, which is largely based on its current strategy to grow its business, could be severely affected by a disruptive 'no-deal' Brexit. Although the bank's capitalisation has improved following continued risk-weighted assets reductions and the capital injection in 2017, it remains vulnerable to additional losses.

Coventry Building Society
Coventry's ratings reflect the society's conservative risk appetite, relatively stable business model, healthy asset quality, sound capitalisation, and solid funding and liquidity profile. The ratings also reflect its limited diversification and heavy reliance on net interest income in a highly competitive mortgage market. The society has recently reported very low loan loss allowances against impaired loans (Stage 3 loans under IFRS 9), a tightening net interest margin, rising costs and an increased appetite for higher LTV lending. Coventry also has higher than average exposure to the buy-to-let market, which we consider to be more vulnerable in a downturn of the economy.

CYBG PLC and Virgin Money Holdings (UK) Plc (VMH), Clydesdale Bank PLC and Virgin Money Plc
CYBG and VMH's (and their operating subsidiary banks') Long-Term IDRs reflect the combined group's overall sound asset quality, adequate capitalisation and stable funding and liquidity and a more diversified business model following the acquisition of VMH by CYBG. It also considers Fitch's view of execution risks from the acquisition of VMH, including CYBG's ability realise its targeted post-acquisition cost savings, and VMH's integration into CYBG's platforms.

HSBC Holdings plc (HSBC), HSBC Bank plc, HSBC UK Bank plc, HSBC Latin America Holdings (UK) Limited and The Hongkong and Shanghai Banking Corporation Limited
HSBC's Long-Term IDR is based on its VR and reflects Fitch's assessment of the consolidated risk profile of HSBC and its operating banks, for which it acts as the holding company. The holding company itself is driven by the financial strength of the group's operating banks. HSBC's strong franchise and solid funding and liquidity remain important rating considerations. The group's company profile has a high influence on the IDRs and VR. The ratings also reflect the group's low risk appetite, which Fitch does not expect to increase despite planned business growth, the group's solid capitalisation, very stable and robust funding and the group's strong ability to generate capital over economic cycles.

The Long-Term IDRs of HSBC Bank plc, HSBC UK Bank plc, HSBC Latin America Holdings (UK) Limited and

The Hongkong and Shanghai Banking Corporation Limited are aligned with those of their 100% ultimate parent HSBC and are based on our assessment of the likelihood that each would receive extraordinary support from HSBC, if needed. The Long-Term IDR of The Hongkong and Shanghai Banking Corporation Limited is underpinned by its VR.

Investec Bank plc (IBP)
IBP's ratings reflect the bank's strengthened business model, improving profitability, prudent liquidity management and adequate capitalisation. The ratings also reflect the bank's appetite for higher-risk asset classes, including commercial real estate loans and equity investments. The bank has strong on-balance sheet liquidity buffers and limited reliance on wholesale funding markets.

Leeds Building Society
Leeds' ratings reflect the society's sound, albeit weakening, profitability, adequate asset quality, solid capitalisation, and sound funding and liquidity. They also reflect an appetite for higher-risk segments, the society's limited franchise and the concentration of its business on the UK housing market.

Lloyds Banking Group plc (LBG), Lloyds Banking Group plc, Lloyds Bank plc, HBOS plc, Bank of Scotland Plc (BOS), Lloyds Bank International Limited (LBIL), Lloyds Bank Corporate Markets Public Limited company (LBCM), TUTP17 Management GMBH (TUTP17)
LBG's VR primarily reflects the group's strong UK franchise, solid capitalisation and funding, and low risk appetite. Activities are geographically concentrated in the UK but the group's business model is well diversified by product and by sector across retail, corporate, SME and insurance.

The Long-Term IDRs of LBG and of its subsidiaries Lloyds Bank plc and BOS are rated one notch above their respective VRs, reflecting sufficient amounts of junior debt available to protect external senior debt holders of both banks.

HBOS is an intermediate holding company and its IDRs are equalised with LBG's. This reflects our view of the high likelihood of institutional support from LBG given the deep strategic and operational integration of HBOS with its parent.

The Long-Term IDRs of the non-ring-fenced bank (NRFB) entities LBCM, LBIL and TUTP17 (expected Long-Term IDR) are equalised with LBG's VR based on our view that institutional support from LBG is highly likely. We expect that LBG would be the ultimate source of support for LBIL and TUTP17, in the event that LBCM is unable to support these entities on its own.

The Long-Term IDRs of the NRFB entities are equalised with LBG's VR as opposed to LBG's IDR to reflect insufficient certainty that the NRFB entities' senior creditors would benefit from LBG's QJD buffer in a resolution of the group. This is primarily because we believe that in a resolution of the group, the resolution authority's main objective would be the protection of senior creditors of LBG's ring-fenced bank.

Nationwide Building Society
Nationwide's Long-Term IDR reflects its leading franchise in UK mortgage lending, conservative risk appetite and sound financial profile with healthy asset quality. The ratings also consider the society's relatively undiversified business model.

Paragon Banking Group
Paragon's ratings reflect its sound franchise in buy-to-let mortgages, consistent performance track record, sound asset quality, solid capitalisation and adequate liquidity. The ratings also reflect the group's limited diversification by industry, geography and revenue streams, as well as its appetite for higher-risk business segments. We consider the group's funding profile as weaker than similarly rated peers.

Principality Building Society
Principality's ratings reflect its strong asset quality indicators, conservative underwriting standards, capitalisation and leverage commensurate with the society's risk profile, and a stable funding and liquidity profile. The ratings also consider the society's undiversified business model and its overall small size and modest market franchise.

The Royal Bank of Scotland Group plc (RBSG), The Royal Bank of Scotland plc (RBS), National Westminster Bank Plc (NatWest Bank), NatWest Markets Plc (NatWest Markets), Ulster Bank Limited, The Royal Bank of Scotland International Limited, NatWest Markets Securities Inc., NatWest Markets N.V.
RBSG's Long-Term IDR is driven by its VR, which reflects our view of the group's consolidated financial profile and the absence of double leverage. RBSG's and the main UK operating banks' VRs primarily reflect the group's strong capitalisation and funding and liquidity. The Long-Term IDR also reflects the group's still short track record of improved profitability, and somewhat weaker asset quality metrics.

NatWest Bank's and RBS's Long-Term IDRs are rated one notch above their VRs as Fitch considers that the banks' external senior creditors are protected by a sufficient buffer of qualifying junior debt and internal structurally subordinated senior debt in case of failure of the group.

The Long-Term IDRs of NatWest Markets, NatWest Markets Securities Inc., NatWest Markets N.V. and The Royal Bank of Scotland International Limited are equalised with RBSG's Long-Term IDR to reflect Fitch's view that their activities are core to the group's strategy, and that the potential support would be manageable relative to RBSG's financial resources. Ulster Bank Limited's IDRs are equalised with its direct parent's, NatWest Bank.

Santander UK Group Holdings plc (SGH), Santander UK plc (San UK) and Abbey National Treasury Services plc (ANTS)
SGH's and San UK's Long-Term IDRs are based on the VRs, which reflect our assessment of the group's consolidated financial profile, and for SGH, the modest holding company double leverage. The VR reflects a conservative risk appetite, sound asset quality, resilient profitability, adequate capitalisation and a stable funding and liquidity profile. It also considers a less diversified business model than similarly-rated peers and above average leverage. San UK's Long-Term IDR is rated one notch above its VR as Fitch considers that the banks' external senior creditors are protected by a sufficient buffer of qualifying junior debt, plus internal structurally subordinated senior debt in case of failure of the group. The Long-Term IDR of ANTS is based on institutional support from SGH and is equalised with SGH's IDR to reflect Fitch's view that SGH would have a strong ability and propensity to support ANTS, based on the entity's role within the group and our expectation that support would be manageable for SGH given ANTS's small relative size.

Skipton Building Society
Skipton's ratings reflect the society's conservative risk appetite, healthy asset quality, solid capitalisation, sound funding and strong liquidity. The ratings also reflect the limited franchise of Skipton and the concentration of its business on the UK housing market.

Tesco Personal Finance Group Limited (TPFG) and Tesco Personal Finance PLC (TPF)
TPFG and TPF's IDRs, VRs and senior debt ratings reflect its modest franchise, diversified revenue sources, sound asset quality, healthy profitability and adequate funding and capitalisation in relation to its risk profile.

Yorkshire Building Society
Yorkshire's Long-Term IDR reflects the society's conservative risk appetite, sound asset quality, strong capital ratios, and sound funding and liquidity profile. The rating also reflects limited diversification and moderate profitability, partly driven by investment in strategic initiatives.

RATING SENSITIVITIES
LONG-TERM IDRS
The Long-Term IDRs of Bank of Ireland (UK) Plc, Barclays plc, Close Brothers Group, The Co-operative Bank p.l.c., Coventry Building Society, CYBG PLC, HSBC Holdings plc, Investec Bank plc, Leeds Building Society, Lloyds Banking Group plc, Nationwide Building Society, Paragon Banking Group, Principality Building Society, The Royal Bank of Scotland Group plc, Santander UK Group Holdings plc, Skipton Building Society, Tesco Personal Finance Group Limited, Virgin Money Holdings (UK) Plc and Yorkshire Building Society and their main subsidiaries are primarily sensitive to the outcome of the Brexit negotiations.

The RWN on the Long-Term IDRs reflects the heightened probability that Fitch will revise the Outlook on the banks' Long-Term IDRs to Negative in the event of a disruptive 'no-deal' Brexit. The Negative Outlooks would reflect the likely risks to the banks' ability to execute their strategies in a more difficult operating environment, likely pressure on earnings, asset quality and funding profiles, which could put pressure on ratings if these negative trends continue for an extended period of time.

Fitch believes that less diversified banks, or banks that are more exposed to highly cyclical sectors, or banks which target niche economic segments or borrowers are more vulnerable to the fall out of a disruptive 'no-deal' Brexit than the larger and more diversified banks. It is possible that in a no-deal scenario more vulnerable banks could remain on RWN for a longer period or be downgraded. However, we do not consider the risk of this to be sufficiently heightened at this stage to place any bank's VR on RWN.

Fitch expects to resolve the RWN and affirm the banks' ratings if by end-March or a short period thereafter, a withdrawal agreement is in place that avoids a disruptive Brexit outcome. All else equal, the RWN would be resolved and Outlooks likely revert to Stable in the event a Brexit agreement is concluded either in March or at the end of a short extension. A longer extension of the Brexit process would also likely result in most banks' ratings reverting to Stable Outlook.

The Outlooks would ultimately reflect the balance of risks to ratings arising from our latest expectations for the UK economy and the banking sector and for the individual issuers, as outlined in the most recent rating action commentaries covering the IDRs and VRs of each bank, which also include additional bank-specific rating sensitivities not directly related to today's rating action. The IDRs of issuers within the following banking groups that benefit from a one-notch uplift due to the presence of sufficient junior debt remain sensitive to the level of this debt remaining sufficient under our criteria to warrant uplift: Lloyds Banking Group, The Royal Bank of Scotland Group plc, Santander UK Group Holdings and Barclays plc.

The rating actions are as follows:

Bank of Ireland (UK) Plc
Long-Term IDR: 'BBB'; placed on RWN
The issuer's other ratings are not affected by this rating action.

Barclays plc
Long-Term IDR: 'A' placed on RWN
The issuer's other ratings are not affected by this rating action.

Barclays Bank plc, Barclays Bank UK plc, Barclays Bank Ireland plc
Long-Term IDRs: 'A+' placed on RWN
The issuer's other ratings are not affected by this rating action.

Close Brothers Group plc, Close Brothers Limited
Long-Term IDRs: 'A'; placed on RWN

The issuers' other ratings are not affected by this rating action.

The Co-operative Bank p.l.c
Long-Term IDR: 'B'; placed on RWN
The issuer's other ratings are not affected by this rating action.

Coventry Building Society
Long-Term IDR: 'A'; placed on RWN
The issuer's other ratings are not affected by this rating action.

CYBG PLC and Clydesdale Bank PLC
Long-term IDRs of 'BBB+' placed on RWN
The issuers' other ratings are not affected by this rating action.

HSBC Holdings plc, HSBC Bank plc, HSBC UK Bank plc, HSBC Latin America Holdings (UK) Limited, The Hongkong and Shanghai Banking Corporation Limited:
Long-Term IDRs: 'AA-', placed on RWN
The issuers' other ratings are not affected by this rating action.

Investec Bank plc
Long-Term IDR: 'BBB+' placed on RWN
The issuer's other ratings are not affected by this rating action.

Leeds Building Society
Long-Term IDR: 'A-'; placed on RWN
The issuer's other ratings are not affected by this rating action.

Lloyds Banking Group plc; Lloyds Bank plc, HBOS plc, Bank of Scotland plc:
Long-Term IDRs: 'A+'; placed on RWN
The issuers' other ratings are not affected by this rating action.

Lloyds Bank International Limited, Lloyds Bank Corporate Markets Limited Company: Long-Term IDRs; 'A'; placed on RWN
The issuers' other ratings are not affected by this rating action.

TUTP17 Management GMBH,
Expected Long-Term IDR: 'A(EXP)'; placed on RWN
The issuer's other ratings are not affected by this rating action.

Nationwide Building Society
Long-Term IDR: 'A'; placed on RWN
The issuer's other ratings are not affected by this rating action.

Paragon Banking Group
Long-Term IDR: 'BBB'; placed on RWN
The issuer's other ratings are not affected by this rating action.

Principality Building Society
Long-Term IDR: 'BBB+'; placed on RWN
The issuer's other ratings are not affected by this rating action.

The Royal Bank of Scotland Group plc, NatWest Markets Plc, Royal Bank of Scotland International Limited, NatWest Markets Securities Inc., NatWest Markets N.V.
Long-Term IDRs: 'A'; placed on RWN
The issuers' other ratings are not affected by this rating action.

The Royal Bank of Scotland plc, National Westminster Bank Plc, Ulster Bank Limited
Long-Term IDRs: 'A+'; placed on RWN
The issuers' other ratings are not affected by this rating action.

Santander UK Group Holdings plc and Abbey National Treasury Services plc
Long-Term IDRs: 'A'; placed on RWN
The issuers' other ratings are not affected by this rating action.

Santander UK plc
Long-Term IDR: 'A+'; placed on RWN
The issuer's other ratings are not affected by this rating action.

Skipton Building Society
Long-Term IDR; 'A-'; placed on RWN
The issuers' other ratings are not affected by this rating action.

Tesco Personal Finance Group Limited and Tesco Personal Finance PLC
Long-Term IDRs of 'BBB' placed on RWN
The issuers' other ratings are not affected by this rating action.

Virgin Money Holdings (UK) Plc, Virgin Money plc
Long-Terms IDRs: 'BBB+'; placed on RWN
The issuers' other ratings are not affected by this rating action.

Yorkshire Building Society
Long-Term IDR: 'A-'; placed on RWN
The issuer's other ratings are not affected by this rating action.

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Additional information is available on www.fitchratings.com
Applicable Criteria
Bank Rating Criteria (pub. 12 Oct 2018)
Non-Bank Financial Institutions Rating Criteria (pub. 12 Oct 2018)

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