

**CREDIT OPINION**

22 October 2024

Update



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**RATINGS**

**Volkswagen Financial Services AG**

Domicile	Braunschweig, Germany
Long Term Rating	A3
Type	LT Issuer Rating
Outlook	Negative

Please see the [ratings section](#) at the end of this report for more information. The ratings and outlook shown reflect information as of the publication date.

**Contacts**

Michael Rohr +49.69.70730.901  
Senior Vice President  
michael.rohr@moodys.com

Ibrahim Kara +49.69.86790.2181  
Sr Ratings Associate  
ibrahim.kara@moodys.com

Carola Schuler +49.69.70730.766  
MD-Banking  
carola.schuler@moodys.com

# Volkswagen Financial Services AG

Update following rating affirmation and outlook change to negative

**Summary**

Volkswagen Financial Services AG's (VW FS AG) A3 long-term issuer ratings carry a negative outlook and are aligned with Volkswagen Aktiengesellschaft (Volkswagen, A3 negative <sup>1</sup>) ratings and outlook, based on the captive's strategic significance to its carmaking parent, our expectation that Volkswagen would support VW FS AG if required, as well as the domination and profit and loss transfer agreement in place between the two companies. VW FS AG's credit profile, therefore, reflects its ba1 standalone assessment and the uplift derived from affiliate support from Volkswagen.

VW FS AG's standalone assessment of ba1 reflects its elevated exposure to residual value risks – particularly in Germany and in the UK – which is mitigated by its anticipated solid capitalisation under the new setup and its geographically diversified funding profile, displaying access to a wide range of funding sources. It also includes a one-notch negative qualitative adjustment for Opacity & Complexity, reflecting execution risks under the new construct as well as the entity's limited financial track record.

Its funding profile benefits from Volkswagen Bank's (VW Bank, A1/A1 negative<sup>2</sup>) strong, diversified and granular deposit franchise which has proven to be a reliable and sufficiently flexible funding source, despite strong competition. This partly mitigates VW FS AG's dependence on more confidence-sensitive funding sources such as asset-backed securities and medium-term wholesale funding.

**Credit strengths**

- » Implicit and explicit support from the parent protects creditors
- » Low historical losses on the loan portfolio indicate sound underwriting standards
- » Strong deposit franchise mitigates refinancing risks and asset-liability mismatches
- » Solid profitability and good leverage ratio will likely be maintained under the new setup

**Credit challenges**

- » The continued reshaping of the automobile industry towards low-emission, alternative-fuel vehicles could eventually hurt VW FS AG's sound asset quality and profitability in the current volatile economic and geopolitical environment.
- » In particular, elevated residual value (RV) risks due to the large lease portfolio may impact earnings volatility, further elevated by the ongoing and uncertain transition to alternative-fuel or battery-electric vehicles.
- » Moderate reliance on confidence-sensitive wholesale funding carries refinancing risks

## Outlook

- » The negative outlook reflects the negative outlook on the parent Volkswagen and reflects our assessment of the very strong contractual and economic rationale for Volkswagen to support its financial services entities.
- » The strategic importance of VW FS AG for the distribution of Volkswagen vehicles and the formal commitment of Volkswagen through a long-term control and profit-and-loss transfer agreement effectively leads to an alignment of the issuer's long-term ratings and outlook with that of Volkswagen.

## Factors that could lead to an upgrade

- » VW FS AG's and its guaranteed subsidiaries' ratings could be upgraded following an upgrade of Volkswagen's rating.
- » VW FS AG's ba1 standalone assessment could be upgraded if VW FS AG manages to sustain asset risks and keep contained loan loss charges or residual value impairments through the cycle, if it improves its capitalisation to levels well above our current expectations, or if it meaningfully lowers its dependence on confidence-sensitive wholesale funding. The standalone assessment could also be upgraded if the reorganisation gets implemented as planned and within the entity's financial targets.
- » However, a change in VW FS AG's standalone assessment without a change in our assessment of Volkswagen's willingness and ability to support VW FS AG would not affect the captive's ratings.

## Factors that could lead to a downgrade

- » VW FS AG's ratings and its guaranteed subsidiaries' ratings could be downgraded if Volkswagen's ratings were downgraded.
- » A downgrade of VW FS AG's and its guaranteed subsidiaries' ratings could also be triggered if Volkswagen were to loosen its ties with its financial services subsidiaries. This loosening could lead to a lowering of our support assumption for VW FS AG and a downgrade of the associated ratings to a level below the parent's issuer ratings.
- » VW FS AG's ba1 standalone assessment could be downgraded following an unexpected erosion of the company's capital base or if its asset quality declines significantly, particularly if associated with residual value losses on lease assets leading to meaningfully higher lease asset depreciation. The standalone assessment could also be downgraded if there is a higher-than-expected increase in the volume of confidence-sensitive wholesale funding or an extended mismatch with the company's lease and lending assets.
- » However, a change in VW FS AG's standalone assessment without a change in our assessment of Volkswagen's willingness and ability to support VW FS AG would not affect the captive's ratings.

## Profile

Effective 1 July 2024, Volkswagen has reorganised its financial services operations to streamline its regulatory and organisational structure, with its European and UK banking and leasing operations, which also include insurance and mobility services, now consolidated under the umbrella of VW FS AG (previously named Volkswagen Financial Services Europe AG). This new EU parent financial holding company holds total assets of approximately €180 billion and was formed by the transfer of ownership of VW Bank to VW FS AG. Also, as of 1 July 2024, all shares of VW Leasing GmbH (VW Leasing, A1 stable<sup>3</sup>) have been taken up by VW Bank. The majority of the holding's total assets are, therefore, held by VW Bank. For a detailed assessment of VW Bank's rating drivers, please see the Credit Opinion on [the bank's Moody's homepage](#).

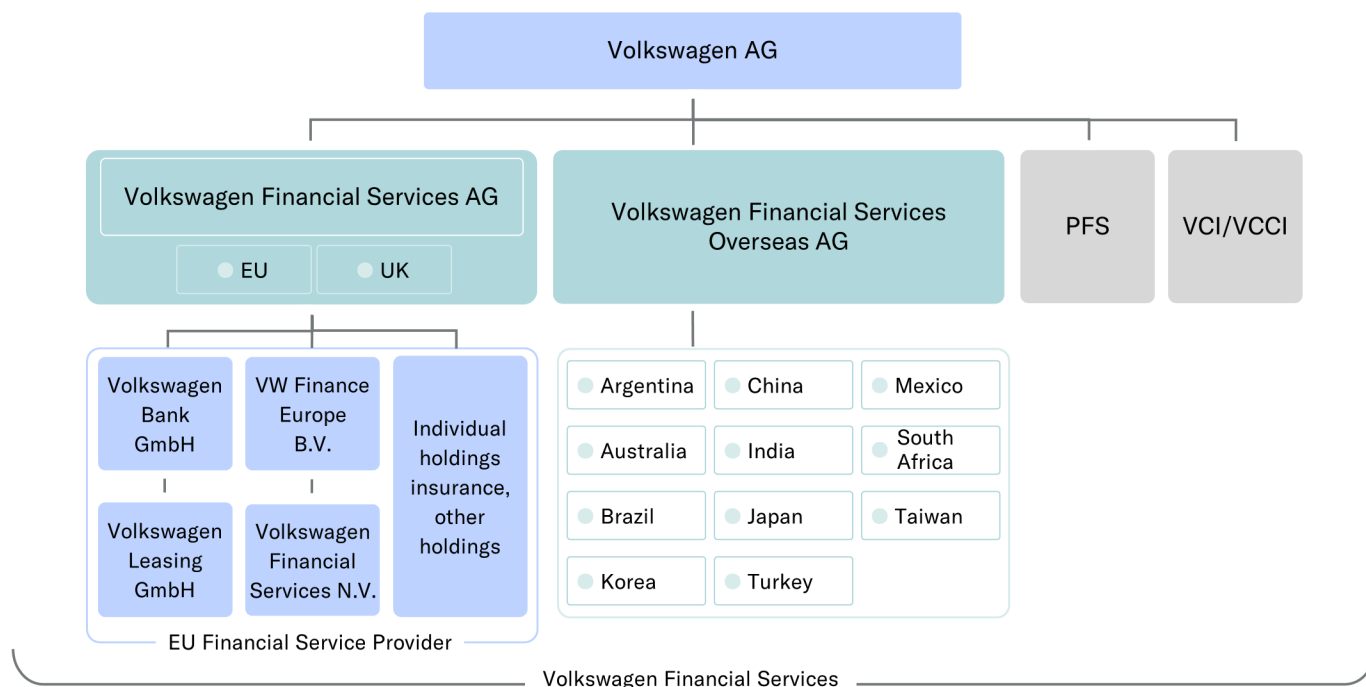
In addition, a newly formed subholding under VW FS AG, Volkswagen Finance Europe B.V., will consolidate most of the carmaker's captive finance operations in the UK, Scandinavia as well as Central and Eastern Europe (CEE), in addition to the existing guaranteed refinancing vehicles Volkswagen Financial Services N.V. and SkoFIN s.r.o., both of which have been moved under VW FS AG.

This publication does not announce a credit rating action. For any credit ratings referenced in this publication, please see the issuer/deal page on <https://ratings.moody's.com> for the most updated credit rating action information and rating history.

Under the new setup, VW FS AG will benefit from a direct domination and profit and loss transfer agreement with Volkswagen and will become subject to ECB supervision as the superordinate EU parent financial holding company, which is responsible for compliance with the provisions of the CRR for the financial holding group.

Exhibit 1

### New organisational structure of Volkswagen's financial services operations



Abbreviations: PFS = Porsche Financial Services GmbH; VCI = VW Credit Inc.; VCCI = VW Credit Canada Inc.

Sources: Moody's Ratings and company filings

## Detailed credit considerations

### Parental support from Volkswagen affords greater protection to creditors

VW FS AG has strategic importance to Volkswagen as it controls most of the group's banking and non-banking financial and leasing operations in the EU and the UK, the most important sales markets for Volkswagen and its associated brands. The importance is illustrated by a control and profit and loss transfer agreement: According to the agreement, Volkswagen is obliged to absorb any net losses of VW FS AG and to provide security to its creditors in accordance with section 303 of German AktG. Although the agreement does not constitute a full guarantee of VW FS AG's obligations by Volkswagen, the carmaker has a strong economic incentive to support its captive because of the latter's important role as the key leasing and financing provider supporting group sales.

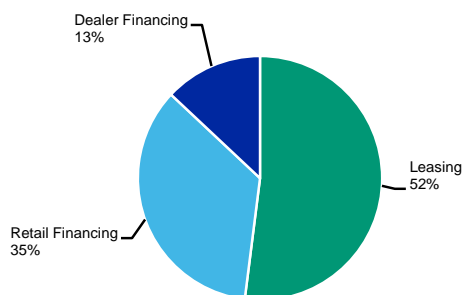
As such, VW FS AG's default probability and expected loss are closely linked with those of its parent Volkswagen. We also believe that there is a strong willingness of the parent to provide support due to the reasons mentioned above and, thus, the senior unsecured rating of VW FS AG is aligned with the A3 issuer rating of Volkswagen AG.

### Asset quality remains exposed to car market cyclicality

We assign a weighted average Asset Risk score of Baa3 to VW FS AG, taking account of lower economic growth forecasts straining the group's asset quality and leading to potentially higher loan losses in its lending operations or heightened lease asset depreciation or net charge-offs on customer leases arising from its leasing operations. The assigned score further captures residual value (RV) risks residing within its leasing operations. Within VW Leasing, the portfolio also includes operating lease assets, in particular personal contract purchases (PCP) in the UK, which makes VW FS AG's results potentially more sensitive to lease car return rates and value fluctuations in the used car markets.

VW FS AG's asset quality performance is influenced by its significant car financing concentrations arising from dealers' inventories of Volkswagen group vehicles and retail loan collateral and lease residual exposures. VW FS AG's risk profile is, therefore, affected by trends in new and used car values and macroeconomic conditions in the markets in which the carmaker and its captive operate. Moreover, the future sales performance of cars in general appears significantly less certain and predictable as a result of shifting consumer preferences, higher inflation tightening disposable incomes and the effects of carbon transition on the captive's stock of leased vehicles. Regarding the latter, the EU's zero emission targets and volatile policy response add to RV risks because of the unpredictable speed and magnitude of vehicle depreciation in light of the uncertainty surrounding future technology development and related government policies.

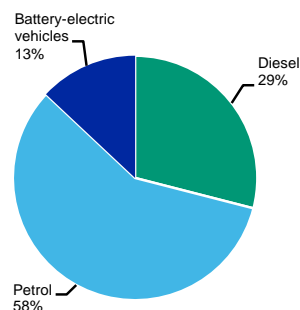
Exhibit 2  
**VW FS AG's business model split Q1 2024E**  
 Based on pro-forma Moody's Ratings' estimates



Based on receivables and leased assets. Based on data after reorganisation for year-end 2023.

Sources: Moody's Ratings estimates and company filings

Exhibit 3  
**VW FS AG's estimated portfolio by fuel type**  
 Battery-electric vehicles' rising share of overall financed stock bears residual value risks



Based on data after reorganisation.

Sources: Moody's Ratings estimates

To mitigate these risks, VW FS AG has started to increase its penetration into the used cars market through various channels, supported by attractive financing or lease packages, all with the aim of safeguarding affordability and, therefore, the asset quality of its customer base. At the same time, because Volkswagen plans to involve its captive operations even more intensely in its vehicle distribution approach by raising its used car penetration rate, we expect the resulting asset growth to further expose VW FS AG to RV risks for each newly leased or financed vehicle.

In addition, another risk factor for VW FS AG is the potentially deteriorating creditworthiness of car dealers because Volkswagen's financial services arms also provide day-to-day financing to Volkswagen's vehicle dealers. However, because of the importance of the dealer network to the broader group's value chain, the carmaker has supported car dealers in the past and will likely continue to provide support in case of need, thereby alleviating potential asset-quality and RV risks at the level of its captive finance subsidiary.

### Solid capital ratio expected

We assign a Capital score of Baa2 to VW FS AG, capturing our expectation that VW FS AG will display a tangible common equity/tangible managed assets (TCE/TMA, our equivalent of the leverage ratio for finance companies) of around 14% going forward. Considering VW FS AG's asset composition, with approximately 50% of assets in leases, we believe the company's current capital is well aligned with its peers, although its sizeable lease portfolio makes it vulnerable to variations in new and used car prices and resulting RV risk. However, the profit and loss agreement with Volkswagen serves as a mitigating factor to its overall sound capitalisation.

### Profitability will match those of its closest peers

We assign a Ba2 Profitability score to VW FS AG, reflecting our expectation that VW FS AG's net income/average managed assets ratio will reside within a narrow range of around 0.8%-0.9% in 2024 and potentially beyond.

Strong demand momentum and recovering supply should help maintain profitability margins, but will increasingly be strained by falling used car values. In particular, the high uncertainty regarding alternative fuel or battery electric vehicles, now commanding a higher share of the captive's lending and lease portfolio assets, may exert undue strain, or at least volatility, on its profitability. In addition, disposable household incomes remain suppressed by higher inflation and persistently higher interest rates, which is likely to increase earnings volatility driven by cyclical variances in consumer financial health and the demand for used vehicles. At the same time, the recovery in global car markets and the resulting new vehicle growth (at often higher sales prices) will support VW FS AG's lending and leasing asset volumes.

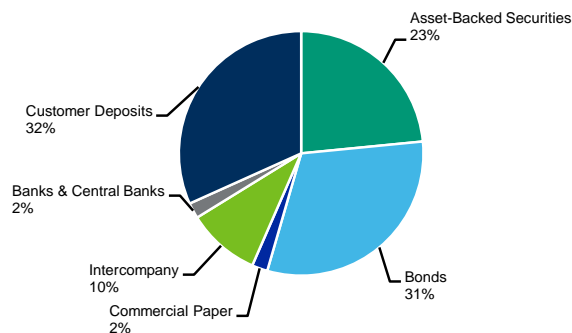
### Moderate reliance on wholesale and secured funding mitigated by strong and granular deposit franchise

We assign a weighted average Cash Flow and Liquidity Score of Ba1 to VW FS AG. The assigned score captures VW FS AG's meaningful reliance on secured and wholesale funding, which renders the company vulnerable to market disruptions and illiquidity. However, market funding dependence is mitigated by VW Bank's strong, diversified and granular deposit franchise which has proven to be a reliable and sufficiently flexible funding source, despite strong competition.

VW FS AG's funding mix represents a solid mix of various funding instruments with varying tenors and spreads. In addition to €31.9 billion of deposits held at VW Bank as of the end of 2023, it included senior unsecured debt (€45.7 billion), asset-backed securities (€28.4 billion), intragroup funding (€14.2 billion), and liabilities to banks and through commercial paper issuance (€14.5 billion). In the asset-backed securities category, the company benefits from the established market presence, for example, of its VCL Master Netherlands B.V. lease asset-backed security programme and the non-EU driver auto loan programmes, which can help fill liquidity or funding gaps in local markets.

Exhibit 4

#### VW FS AG's expected funding mix for year-end 2024



Sources: Moody's Ratings estimates and company filings

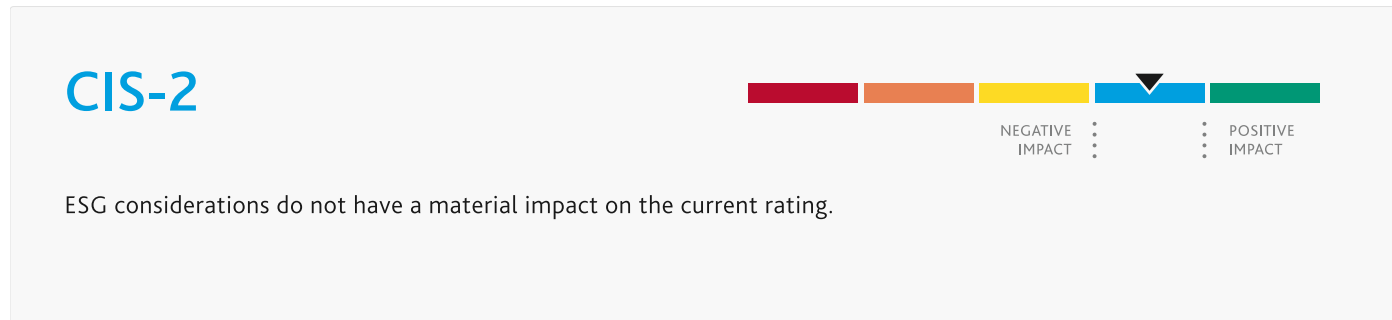
VW FS AG further operates with adequate liquid resources in the form of cash largely held within its banking subsidiary and securities holdings, supported by high short-term cash inflows under its lease and loan contracts. Moreover, in case of need, the company has access to additional funding sources, including a multibillion euro committed standby liquidity facility from its parent as well as interbank facilities.

## ESG considerations

### Volkswagen Financial Services AG's ESG credit impact score is CIS-2

Exhibit 5

#### ESG credit impact score



Source: Moody's Ratings

VW Financial Services AG's (VW FS AG) ESG Credit Impact Score is **CIS-2** and reflects the mitigating rating impact of support from its automotive parent. VW FS AG is exposed to material environmental and social risks, reflecting the high risk exposure of its automotive parent and the bank's role as facilitator of sales. The entity's governance risks are low.

Exhibit 6

#### ESG issuer profile scores



Source: Moody's Ratings

### Environmental

VW FS AG faces high environmental risks, primarily related to carbon transition. As a facilitator of sales for its automotive parent, its exposure to carbon transition risk is consistent with that of its ultimate parent Volkswagen AG and the global auto manufacturing sector because of stricter environmental regulation and the trend towards low and zero emission vehicles. In response, VW FS AG supports Volkswagen AG's electric mobility strategy targeting to provide financing solutions for 80% of Volkswagen AG's electric vehicles in the medium term. VW FS AG's exposure to other environmental risks is low.

### Social

VW FS AG faces high social risks from societal trends. VW FS AG's key product is auto lending and leasing, the demand for which is subject to societal trends like higher adoption of mass transportation and heightened environmental awareness and is highly correlated to the ability of its parent to meet consumers' demand. In line with other retail consumer-focused banks and leasing companies, VW FS AG is also exposed to fines and reputational damage due to product mis-selling or other types of misconduct. High cyber and personal data risks are also key considerations as more applications are submitted online.

### Governance

VW FS AG's governance risks are low. VW FS AG has well-developed risk management and governance practices in place, in line with industry practices. Our governance assessment also takes account of execution risks under the new construct as well as the entity's limited financial track record post reorganisation. VW FS AG's score for board structure, policies and procedures is aligned with that of its parent, given the captive's strategic importance to its parent and brand sharing.

ESG Issuer Profile Scores and Credit Impact Scores for the rated entity/transaction are available on Moody's.com. In order to view the latest scores, please click [here](#) to go to the landing page for the entity/transaction on MDC and view the ESG Scores section.

## Support and structural considerations

### Affiliate support

Based on the application of Moody's Methodology of Captive Finance Subsidiaries of Nonfinancial Corporations, the ratings of VW FS AG are aligned with its ultimate parent, Volkswagen. This is based on VW FS AG's strategic significance to its parent, our expectation that Volkswagen would support VW FS AG if required, as well as the explicit support agreement between the captive and its carmaking parent.

### Operating environment and industry-risk indicators

We assign a Baa2 weighted Operating Environment score to VW FS AG, based on the industry and macro-level risks at its EU and UK car financing and leasing operations. The score benefits from VW FS AG's activities in Germany, where the company has most of its total lending and leasing exposures, and to which we assign a Baa2 Operating Environment score.

The operating environment score has no impact on VW FS AG's financial profile. Overall, and including a one-notch negative qualitative adjustment for Opacity & Complexity reflecting execution risks under the new construct as well as the entity's limited financial track record, this results in a Ba1 adjusted financial profile.

### Home market macro-level and industry-risk indicators

VW FS AG's exposures primarily relate to the German car financing and leasing markets. The Aa2 German Macro-Level Indicator score reflects the country's very high degree of economic and institutional financial strength, with a low susceptibility to event risk.

We assign a Baa Industry Risk score for German car finance and leasing companies. Companies in this sector benefit from relatively high barriers to entry and pricing power. A growing proportion of leases is underwritten at the point of sale, as reflected by rising new and used car penetration rates. Banks in Germany have been slowly building competitive leasing offers, hence competition remains limited.

VW FS AG further benefits from exclusive subvention programs from Volkswagen, which provide access to loan and lease origination volumes bolstering the captive's franchise.

### Industry risk

We assign a Baa industry risk score for diversified auto-finance lenders operating in German and core Western European markets. Firms in this sector provide retail loans and leases to consumers and commercial lending to dealerships. The sector has limited barriers to entry along with manageable compliance requirements and costs. Pricing power is limited since different types of financial institutions (finance companies, banks and credit unions) participate in the sector and increase their presence quickly.

Cyclicality is normal since there is a steady demand for loans, moderate underwriting variability and limited tolerance for weakening asset quality. Vehicles are becoming more expensive, heightening the need for financing.

Retail loan loss rates are generally low. Loan yields are low as well resulting in profit volatility if asset quality weakens. Leases have higher yields but also greater volatility which is tied to residual values and related used vehicles values.

## Rating methodology and scorecard factors

The methodologies we use in rating VW FS AG are the [Finance Companies Methodology](#), published in July 2024, and the [Captive Finance Subsidiaries of Nonfinancial Corporations Methodology](#), published in August 2024.

## Ratings

Exhibit 7

Category	Moody's Rating
<b>VOLKSWAGEN FINANCIAL SERVICES AG</b>	
Outlook	Negative
Issuer Rating	A3
Senior Unsecured -Dom Curr	A3
Commercial Paper	P-2
Other Short Term	(P)P-2
<b>PARENT: VOLKSWAGEN AKTIENGESELLSCHAFT</b>	
Outlook	Negative
Issuer Rating	A3
Sr Unsec Bank Credit Facility -Dom Curr	A3
Senior Unsecured MTN -Dom Curr	(P)A3
Commercial Paper -Dom Curr	P-2
<b>VOLKSWAGEN LEASING GMBH</b>	
Outlook	Negative
Bkd Senior Unsecured -Dom Curr	A1
<b>VOLKSWAGEN BANK GMBH</b>	
Outlook	Negative
Counterparty Risk Rating	Aa3/P-1
Bank Deposits	A1/P-1
Baseline Credit Assessment	baa3
Adjusted Baseline Credit Assessment	a3
Counterparty Risk Assessment	Aa3(cr)/P-1(cr)
Issuer Rating	A1
Senior Unsecured MTN	(P)A1
Junior Senior Unsecured -Dom Curr	A3
Junior Senior Unsecured MTN	(P)A3
Subordinate MTN	(P)Baa1
Commercial Paper -Dom Curr	P-1
Other Short Term -Dom Curr	(P)P-1
<b>VOLKSWAGEN FINANCIAL SERVICES N.V.</b>	
Outlook	Negative
Bkd Senior Unsecured	A3
Bkd Commercial Paper	P-2
Bkd Other Short Term	(P)P-2
<b>SKOFIN S.R.O.</b>	
Bkd Commercial Paper	P-2

Source: Moody's Ratings

## Endnotes

- <sup>1</sup> The rating shown here is Volkswagen's long-term issuer rating and outlook.
- <sup>2</sup> The ratings shows are VW Bank's long-term deposit and issuer ratings together with their corresponding outlook(s).
- <sup>3</sup> The rating shown is VW Leasing's long-term backed senior unsecured debt rating together with its corresponding outlook.



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