

Research Update:

# Santander Financial Services PLC Assigned 'A-/A-2' Ratings; Outlook Negative

May 12, 2021

## Overview

- We have assigned our 'A-/A-2' ratings to Santander Financial Services PLC (SFS) as we consider it to be a highly strategic operating subsidiary of Santander UK Group Holdings PLC (Santander UK).
- SFS is the non-ring-fenced bank of Santander UK, and conducts a limited range of activities--most of which cannot be conducted by Santander UK's ring-fenced bank, Santander UK PLC--serving customers in the U.K., the Crown dependencies, and internationally.
- The outlook on SFS is negative, mirroring that on Santander UK, reflecting the economic and market effects of the COVID-19 pandemic.

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## Rating Action

On May 12, 2021, S&P Global Ratings assigned its 'A-' long- and 'A-2' short-term issuer credit ratings to Santander Financial Services PLC (SFS)--the bank subsidiary that sits outside the ring-fenced operations of Santander UK Group Holdings PLC (Santander UK). The outlook on SFS is negative.

At the same time, we assigned our resolution counterparty rating of 'A/A-1' to SFS.

## Rationale

The ratings on SFS reflect our view that it is a highly strategic subsidiary of Santander UK. We consider SFS' materiality, important role in the parent's strategy, and close link to the group's brand and reputation. In our view, these factors increase its strategic importance to the group and the likelihood of receiving financial support in case of need. We assess SFS as highly strategic rather than core (a stronger assessment) because we consider it to be tactically important rather than integral to the group, in the context of the U.K.'s ring-fencing regime. It is also less diversified with relatively modest operations compared with the group's ring-fenced activities, which we consider to be core to the group. SFS' highly strategic status leads us to rate the entity one notch below the 'a' group credit profile, which includes a two-notch uplift for additional loss-absorbing

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capacity (ALAC). We do not maintain a stand-alone credit profile on SFS.

SFS is Santander UK's non-ring-fenced bank (NRFB). Historically its principle activities have included retail banking and wealth management services for customers in the U.K., Jersey, and the Isle of Man. SFS' balance sheet was repositioned in 2020 following the purchase of a £3.2 billion portfolio of U.K. residential mortgages from Santander UK to support group profitability by more efficiently deploying excess liquidity.

In our view, SFS' reported and underlying earnings are modest relative to the parent's but are set to improve after repositioning. Although SFS reported a £27 million pre-tax loss from continuing operations in full-year 2020, we forecast a return to statutory profitability in 2021. While modest balance sheet growth is likely within our two-year outlook horizon, we do not anticipate transformational development of business activity, diversification, or profitability beyond the initial redeployment of excess deposits into U.K. mortgages.

The U.K. government rolled out the ring-fencing regime to protect critical banking functions. We think parental support for non-ring-fenced entities might be marginally weaker in a stress scenario than for ring-fenced banks (see "Rearranged And Ready: U.K. Banks Are On Track For Ring-Fencing," published on Aug. 15, 2018). SFS is notable versus other U.K. peer NRFBs for its small size, in both absolute terms and relative to the group. We assess Barclays and HSBC NRFBs to have core group status on account of their scale and alignment to their respective groups' core business activities. Lloyds and NatWest NRFBs meanwhile carry highly strategic group status assessments given their exposure to higher business risk activities, which are typically less diversified than the groups' ring-fenced activities.

We include ALAC uplift in the ratings on SFS because, through internal downstreaming, we believe senior creditors will benefit from the ALAC buffer amassed by Santander UK.

### Outlook

S&P Global Ratings' negative outlook on SFS mirrors that on parent Santander UK. The negative outlook on Santander UK reflects our expectation that, despite its good market position, the bank will endure weakened asset quality and earnings over our two-year outlook horizon as a result of the economic and market effects of the COVID-19 pandemic. It also reflects our expectation that the bank will steadily expand its market position in U.K. retail banking, while maintaining its supportive risk appetite and capitalization. We assume the ultimate parent, Banco Santander, will continue to provide ongoing group support, despite the uncertainty for extraordinary group support in a severe stress scenario, given the group's multiple point of entry approach to resolution.

### Downside scenario

We could lower the ratings on SFS if we lowered the ratings on its parent, or if our view of its group status weakened, for example due to evidence of a less integral role to the group.

### Upside scenario

An outlook revision to stable would follow a similar action on Santander UK. Over time, we could raise the ratings if we revised upward SFS' group status to that of a core subsidiary. However, this appears unlikely absent a significant change in its materiality and strategic significance to the group.

## Related Criteria

- General Criteria: Group Rating Methodology, July 1, 2019
- Criteria | Financial Institutions | General: Methodology For Assigning Financial Institution Resolution Counterparty Ratings, April 19, 2018
- 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
- General Criteria: Guarantee Criteria, Oct. 21, 2016
- Criteria | Financial Institutions | Banks: Bank Rating Methodology And Assumptions: Additional Loss-Absorbing Capacity, April 27, 2015
- Criteria | Financial Institutions | Banks: Assessing Bank Branch Creditworthiness, Oct. 14, 2013
- 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: Banks: Rating Methodology And Assumptions, Nov. 9, 2011
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011
- Criteria | Financial Institutions | Banks: Commercial Paper I: Banks, March 23, 2004

## Related Research

- U.K. Bank Credit Losses Could Fall 40% in 2021, March 29, 2021
- Bulletin: U.K. Bank Rating Actions Won't Wait For The Bank Of England's 2021 Stress Test Results, Jan. 20, 2021
- Banco Santander S.A., Dec. 22, 2020
- Santander UK Group Holdings PLC, Dec. 9, 2020
- Rearranged And Ready: U.K. Banks Are On Track For Ring-Fencing, Aug. 15, 2018

## Ratings List

### New Rating

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**Santander Financial Services PLC**

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Resolution Counterparty Rating A/--/A-1

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### New Rating; Outlook

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**Santander Financial Services PLC**

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Issuer Credit Rating A-/Negative/A-2

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