FitchRatings

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Fitch Maintains Barclays' 'A' Long-Term IDR on Negative Watch

Fitch Ratings-London-29 May 2020:

Fitch Ratings is maintaining Barclays plc's (Barclays) 'A' Long-Term Issuer Default Rating (IDR) and 'a' Viability Rating on Rating Watch Negative (RWN).

Barclays Bank plc's (BBplc) 'A+' Long-Term IDR and 'a' VR have also been maintained on RWN, while Fitch has affirmed Barclays Bank UK plc's (BBUK) Long-Term IDR at 'A+'/Negative and VR at 'a'.

Barclays' solid balance sheet entering the crisis and its performance in 1Q20 suggest the bank's ratings have the potential to withstand the economic fallout of the coronavirus pandemic. However, rating headroom at 'A'/'a' levels is low, in view of the heightened risk from the pandemic, as reflected by further downward revisions to our global economic forecasts on 26 May. These factors are underlined by the RWN. BBUK has more rating headroom due to its more stable company profile, lower risk appetite and superior funding profile to BBplc. Nevertheless, the Negative Outlook reflects the pandemic's longer-term risks to asset quality, earnings and execution.

Our assessment of Barclays' company profile and risk appetite (both a-) are constrained by the bank's exposure to volatile and competitive capital markets and trading activities and need to be offset by stronger and resilient financial metrics to maintain the current rating level. The pandemic creates pressure on three of these financial metrics: asset quality (assessed at a/negative), earnings & profitability (a-/negative) and capitalisation & leverage (a/negative).

We expect to resolve the RWN in mid-2H20, by which time 2Q20 results should give more visibility on the pandemic's impact on several factors that are important to the group's ratings, notably i) the resilience of Barclays' capital to further risk-weighted asset (RWA) inflation (10% in 1Q20) and profitability challenges; ii) the resilience of Barclays' revenues after a strong 1Q20 (20%), albeit a quarter that included less than a month of lockdown in the UK and US and late cuts to key interest rates; and iii) prospects for asset quality after a worsening of expected credit losses in 1Q20 and in light of the group's high exposure to some more vulnerable asset classes, including consumer loans in both BBplc and BBUK and leveraged lending in BBplc, and rising UK and US unemployment levels. In the UK, these are being supported by the UK government's furlough scheme.

Key Rating Drivers

BARCLAYS

Barclays' VR and IDR are based on the consolidated analysis of the group, and reflect strengthened earnings prior to the economic downturn, benefitting from progress made with the group's legacy conduct issues. The group's sound capitalisation, funding, liquidity and asset quality going into the economic crisis also support the ratings.

Earnings had been improving prior to the onset of the pandemic, supported by lower restructuring and legacy conduct costs, and by a focus on reducing operating costs. Its 2019 return on tangible equity (RoTE) improved to 9%, in line with its target for the year, and management continues to target a RoTE of greater than 10% over time despite likely short-term earnings deterioration due to the economic crisis.

Earnings for 2020 will be burdened by higher loan impairment charges, and by revenue pressure from lower interest rates and subdued lending volumes. Reflecting these challenges 1Q20 pre-tax profit was GBP0.9 billion (-38% yoy), including impairment charges of GBP2.1 billion (higher than the charge for the whole of 2019), which translated into an operating profit/RWA ratio of 1.1% (2019: 1.5%). The 1Q20 result benefitted from increased market volatility, which supported trading income. Volatility will likely aid Barclays' trading results in the near term, although issuance activity may be subdued for the full year. We expect weak profitability for 2Q20 as the effects of the pandemic feed through. The bank expects to remain profitable for the full year, with a recovery starting from 2H20, although the economic assumptions underpinning this guidance are highly sensitive to how the crisis develops.

Barclays' asset quality was sound going into the crisis. Deterioration is likely over 2020 although this should be partly mitigated by the group's conservative underwriting standards in domestic mortgages and corporate lending, and by government measures to support borrowers in the crisis. Actual impairment cases have remained low to date with reported end-1Q20 stage 3 loans broadly stable quarter-on-quarter at 2.2% of loans at amortised cost. However, the bank's more negative economic guidance following the onset of the pandemic drove an increase in loan impairment charges equivalent to 223bp of gross loans for the quarter, compared with 55bp for 2019.

Pressure on asset quality could arise from Barclays' exposure to leveraged finance, and to industries that are vulnerable to the economic disruption, most notably oil and gas, high street retail and hospitality and leisure, although we expect Barclays' conservative risk appetite to partially mitigate losses. Barclays' consumer loan exposures, mainly in the US and UK, are at risk if government measures do not fully compensate borrowers' falling income and rising unemployment, especially if the disruptions extend beyond 2H20.

The end-1Q20 CET1 ratio of 13.1% (-70bp quarter-on-quarter) was sound and comfortably above the minimum regulatory requirement of 11.5% (including a 0% countercyclical buffer, with a further reduction in Pillar 2a requirement expected). The CET1 ratio may fall below 13% over 2020 due to earnings pressure and RWA growth from credit-risk migrations, and capitalisation could also come under pressure from material one-off credit risk or valuation losses. We expect management to maintain adequate buffers above minimum capital requirements but a sharp fall in capitalisation may not be commensurate with an 'a' VR given mounting credit risks.

Barclays' funding profile remains well-matched and diversified. It benefits from the group's UK retail franchise to fund retail assets and good capital-market access to fund wholesale operations. Its gross loans/customer deposits ratio of 81% at end-1Q20 is healthy. Liquidity is comfortable, with a liquidity coverage ratio (LCR) of 155% and an eligible liquidity pool of GBP237 billion at end-1Q20, which are well above regulatory requirements.

The group is well-positioned to meet its minimum requirement for own funds and eligible liabilities (MREL) and at end-1Q20 holding-company MREL instruments were equivalent to 29.3% of RWAs, compared with a 30.6% indicative requirement for 1 January 2022. The group issued GBP2 billion in MREL-eligible debt in 1Q20 and plans to issue a further GBP5 billion-GBP6 billion over 2020; we expect issuance needs to be manageable despite market volatility given Barclays' established wholesale funding franchise.

Barclays' VR and IDR also reflect reasonably low levels of common equity double leverage (107% at end-2019) and prudent liquidity management at the holding company.

The 'F1' Short-Term IDR is the lower of two possible options mapping to a Long-Term IDR of 'A'. This reflects Fitch's view that the group's liquidity is sound but not sufficiently strong to warrant a 'F1+'

BBplc and BBUK

The VRs of the two main operating banks, BBplc and BBUK, reflect their Standalone Credit Profiles, which include the benefit of ordinary support from the group. BBUK operates a simple, domestically focused, retail and SME banking business model, and has stable funding dominated by granular deposits. BBplc is the larger operating bank by balance sheet and houses the corporate and investment bank (CIB) and the international cards and payments businesses.

The Negative Outlook on BBUK's Long-Term IDR reflects our view that BBUK has more headroom than BBplc, whose ratings are on RWN, to absorb the current challenges given its simple retail- and business-banking business model and strong deposit franchise. BBplc's business model is structurally more volatile because of the nature of the businesses included here and higher reliance on wholesale funding. Fitch is unlikely to rate Barclays' VR higher than BBplc's because of the latter's significant weight in the group.

The Long-Term IDRs and senior debt ratings of BBplc and BBUK are rated one notch above their respective VRs, and one notch above the holdco's IDR. This reflects our expectation that external senior creditors will benefit from resolution funds ultimately raised by Barclays, which are designed to protect BBplc's and BBUK's senior creditors if the group fails.

The DCRs of BBUK and BBplc are at the same level as their Long-Term IDRs because derivative counterparties in the UK have no definitive preferential status over other senior obligations in a resolution.

The Short-Term IDRs of 'F1' of BBplc and BBUK are the lower of two options mapping to an 'A+' Long-Term IDR. This reflects Fitch's view that the banks' liquidity is sound but not sufficiently strong to warrant an 'F1+' rating.

The long- and short-term debt ratings on BBplc's global collateralised medium-term note (GCMTN) programme and notes are at the same level as BBplc's senior unsecured debt because the terms of the notes issued do not allow for a one-notch uplift of the rating under Fitch's criteria. The notes are rated under our Bank Rating Criteria, which allow rating of secured senior debt that is not complex.

SUPPORT RATING (SR) AND SUPPORT RATING FLOOR (SRF)

Barclays' and BBplc's SRs and SRFs reflect Fitch's view that senior creditors of the bank and the holding company cannot rely on extraordinary support from the sovereign in the event that Barclays or BBplc become non-viable. In our opinion, the UK has implemented legislation and regulations to provide a framework that is likely to require senior creditors to participate in losses for resolving even large banking groups. BBplc's SR is based on sovereign support because we believe that its role as the non-ring-fenced bank and its size mean that institutional support from Barclays and, indirectly from BBUK, is unlikely.

BBUK's SR of '1' reflects our view of an extremely high probability of institutional support being made available from Barclays and, indirectly, from BBplc, given the ring-fenced bank's strategic role in the group and reputational considerations. Despite its size we believe that support would be manageable.

BARCLAYS BANK IRELAND (BBI), BARCLAYS CAPITAL INC (BCI)

The Long- and Short-Term IDRs of BBI and BCI are equalised with the IDRs of their parent BBplc, which along with their SRs of '1', reflect our view of an extremely high likelihood that BBI and BCI would be supported by BBplc if needed.

BBI houses BBplc's EU operations (mainly CIB, credit cards, private banking and legacy Italian mortgages), with the aim of avoiding business disruption following the UK's departure from the EU. The activities that are housed in BBI give the group uninterrupted access to European clients and financial markets and we therefore view this entity as core to the parent and the wider group's business.

BCI is the broker dealer and futures commission merchant that services BBplc's US-domiciled CIB clients, and a material operating entity of Barclays in the US. Fitch views the businesses conducted out of BCI as core to the group and vital for CIB's client relationships and strategy, which provides a strong incentive for BBplc to support it.

A potential sale of the entities is hard to conceive given BBI's and BCI's business models and high degree of integration with the group, and also because a sale would also alter the group's ability to service international clients. Moreover, potentially allowing these entities to default would give rise to material reputational implications for BBplc, given common business relationships and branding.

Fitch equalises BBI's and BCI's Long-Term IDRs with BBplc's IDR rather than the VR because both entities benefit from a significant buffer of junior debt, which is likely to be sufficient to recapitalise BBI and BCI in case of need without imposing losses on external senior creditors.

The DCRs are equalised with the respective entities' Long-Term IDRs. The Short-Term IDRs of 'F1' are at the same level as BBplc's.

SUBORDINATED DEBT

Subordinated debt and other hybrid capital issued by Barclays and BBplc are all notched down from their respective VRs, in accordance with Fitch's assessment of each instrument's respective non-performance and relative loss severity risk profiles, which vary considerably.

Barclays' and BBplc's subordinated lower Tier 2 debt is rated two notches below the VRs for loss severity, reflecting below-average recoveries. This includes contingent convertible Tier 2 notes for which we see no incremental non-performance risk. BBplc's legacy Upper Tier 2 instruments are rated lower, at three notches below the VR, due to incremental non-performance risk.

Additional tier 1 instruments and preference shares with no constraints on coupon omission are rated four notches below the relevant VRs. The issues are notched down twice for loss severity, reflecting their deep subordination and poor recoveries as the instruments can be converted into equity or written down well ahead of resolution. In addition, they are notched down twice for high non-performance risk due to fully discretionary coupon omission. The rating of these instruments is supported by our expectation that the group will maintain at least a 100bp buffer over capital requirements that would trigger coupon omission on the bonds.

RATING SENSITIVITIES

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

The most immediate downside rating sensitivity for Barclays and its subsidiaries relates to the economic and financial market fallout arising from the pandemic as this represents a clear risk to our assessment of asset quality, earnings and capitalisation, and to management's ability to execute on strategic objectives.

The Long-Term IDRs, VRs and debt ratings would likely be downgraded if it becomes less likely that the pandemic will abate in 2H20, resulting in further revisions to our economic forecasts for 2020. A delay to recovery - which we currently expect in 2021 - would likely result in more permanent damage to the bank's asset quality, earnings and capitalisation, which would be difficult to restore within 18-24 months. Beyond 2020, ratings also remain sensitive to the economic repercussions of Brexit trade negotiations between the UK and European Union.

We would likely downgrade Barclays' and subsidiaries' Long-Term IDRs, VRs and debt ratings if the group's CET1 ratio looks set to fall towards 12% without a clear path for it to return above the 13% target within 18-24 months, or if operating profit/RWA is unlikely to rise above 1.5% by end-2021.

The ratings are also sensitive to a sustained weakening of asset quality that materially increases the level of capital that is encumbered by unreserved impaired loans or may mean weaker solvency than implied by reported capital ratios for example due to IFRS9 transitional relief.

Ratings could also be downgraded if the group increases its risk appetite to boost profitability in the near term. Evidence of this could be a significant increase in RWAs allocated to investment-banking activities or towards higher-risk credit exposure.

BBUK's and BBplc's VRs could be downgraded if the banks' competitive positions or financial profiles weaken and if we believe that ordinary support from the group is not available to offset this weakness. BBUK's ratings may withstand a one-notch downgrade of Barclays' ratings provided that BBUK's financial profile at that point is significantly stronger than that of the rest of the group. The one-notch uplift applied to the IDRs and senior debt ratings of BBplc and BBUK are also sensitive to Barclays maintaining a clear and credible role as the resolution entity for the group.

BBplc's DCR is primarily sensitive to changes in the bank's Long-Term IDR.

The ratings of BCI and BB could be downgraded if BBplc is downgraded or if they are no longer expected to be protected by resolution plan buffers of junior debt/equity from BBplc.

Short-Term IDRs could be downgraded if Long-Term IDRs are downgraded to 'A-' and our assessment of funding & liquidity falls to 'a-' or below.

The ratings of AT1s could be downgraded if we see a heightened risk that capital cushions above maximum distributable amount (MDA) trigger points will fall below 100bp.

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

The ratings could be affirmed and removed from RWN if a sharp deterioration in credit losses beyond our current expectations becomes less likely and if the group's revenues continue to demonstrate resilience in a challenging environment.

In the event Barclays is able to withstand rating pressure arising from the pandemic, an upgrade would require a sustained improvement in earnings through the cycle, resulting in a materially stronger capacity to generate capital internally, which we do not expect in the near term. Barclays' IDR could be rated above the VR if AT1 and Tier 2 debt increase sustainably above 10% of RWAs, but this is unlikely.

Best/Worst Case Rating Scenario

International scale credit ratings of Financial Institutions 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

The IDRs of BBI and BCI are based on BBplc.

ESG Considerations
The highest level of ESG credit relevance, if present, is a score of 3. This means ESG issues are credit-neutral or have only a minimal credit impact on the entity(ies), either due to their nature or to the way in which they are being managed by the entity(ies). For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg.

Barclays Bank UK PLC; Long Term Issuer Default Rating; Affirmed; A+; RO:Neg
; Short Term Issuer Default Rating; Affirmed; F1
; Viability Rating; Affirmed; a
; Support Rating; Affirmed; 1
; Derivative Counterparty Rating; Affirmed; A+(dcr)
----senior unsecured; Long Term Rating; Affirmed; A+
----senior unsecured; Short Term Rating; Affirmed; F1
Barclays plc; Long Term Issuer Default Rating; Rating Watch Maintained; A; RW: Neg
; Short Term Issuer Default Rating; Affirmed; F1
; Viability Rating; Rating Watch Maintained; a; RW: Neg
; Support Rating; Affirmed; 5
; Support Rating Floor; Affirmed; NF
----senior unsecured; Long Term Rating; Rating Watch Maintained; A; RW: Neg
----subordinated; Long Term Rating; Rating Watch Maintained; BBB-; RW: Neg
----subordinated; Long Term Rating; Rating Watch Maintained; BBB+; RW: Neg
----senior unsecured; Short Term Rating; Affirmed; F1
Barclays Bank plc; Long Term Issuer Default Rating; Rating Watch Maintained; A+; RW: Neg
; Short Term Issuer Default Rating; Affirmed; F1
; Viability Rating; Rating Watch Maintained; a; RW: Neg
; Support Rating; Affirmed; 5
; Support Rating Floor; Affirmed; NF
; Derivative Counterparty Rating; Rating Watch Maintained; A+(dcr); RW: Neg

----senior unsecured; Long Term Rating; Rating Watch Maintained; A+; RW: Neg

----subordinated; Long Term Rating; Rating Watch Maintained; BBB; RW: Neg

----subordinated; Long Term Rating; Rating Watch Maintained; BBB+; RW: Neg

----subordinated; Long Term Rating; Rating Watch Maintained; BBB-; RW: Neg

----senior secured; Long Term Rating; Rating Watch Maintained; A+; RW: Neg

----senior unsecured; Short Term Rating; Affirmed; F1

----senior secured; Short Term Rating; Affirmed; F1

Barclays Capital Inc.; Long Term Issuer Default Rating; Rating Watch Maintained; A+; RW: Neg

; Short Term Issuer Default Rating; Affirmed; F1

; Support Rating; Affirmed; 1

; Derivative Counterparty Rating; Rating Watch Maintained; A+(dcr); RW: Neg

Barclays Bank Ireland Plc; Long Term Issuer Default Rating; Rating Watch Maintained; A+; RW: Neg

; Short Term Issuer Default Rating; Affirmed; F1

; Support Rating; Affirmed; 1

; Derivative Counterparty Rating; Rating Watch Maintained; A+(dcr); RW: Neg

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Additional information is available on www.fitchratings.com

Applicable Criteria

Bank Rating Criteria (pub. 28 Feb 2020) (including rating assumption sensitivity)

Non-Bank Financial Institutions Rating Criteria (pub. 28 Feb 2020) (including rating assumption sensitivity)

Additional Disclosures

Dodd-Frank Rating Information Disclosure Form

Solicitation Status

Endorsement Status

Endorsement Policy

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