FitchRatings

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# Fitch Revises Barclays plc's Outlook to Stable; Affirms at 'A'

Fitch Ratings - London - 21 Jul 2021: Fitch Ratings has revised the Outlook on Barclays plc's (Barclays) Long-Term Issuer Default Rating (IDR) to Stable from Negative and affirmed the Long-Term IDR at 'A' and Viability Rating (VR) at 'a'.

Fitch has also affirmed the Long-Term IDRs of Barclays' subsidiaries, including Barclays Bank plc (BBplc) and Barclays Bank UK PLC (BBUK) at 'A+' and their VRs at 'a'. Their Outlooks have also been revised to Stable from Negative.

The revision of the Outlooks is primarily driven by the revision of the outlook on Fitch's 'aa-' operating environment score for Barclays to stable from negative, following the recent revision of the Outlook on the UK's 'AA-' Long-Term IDR to Stable, and Fitch's improved expectations for the economic recovery in Barclays' key markets.

The Outlook revision also considers Fitch's view that Barclays' performance through the pandemic and its expected performance has increased rating headroom for the group to absorb pressure that may arise from remaining uncertainties caused by the pandemic. The group's diversified business model, which combines retail and corporate banking with investment banking, has enabled it to report resilient earnings since the onset of the health crisis and maintain healthy capital ratios.

## Key Rating Drivers

BARCLAYS

Barclays' VR and IDRs are based on the group's consolidated financial profile, which reflects the group's strong franchises in UK retail, cards and corporate & investment banking (CIB) and a diversified revenue mix by product and geography, all of which have supported resilient earnings despite the economic shock from the pandemic. This is counterbalanced by the group's reliance on capital markets businesses, which are inherently volatile and competitive. This constrains the company profile and risk appetite scores at 'a' and 'a-', respectively. The ratings are also supported by solid capitalisation and a strong funding and liquidity profile.

The VR considers Barclays' role as a holding company and the low level of common equity double leverage (110% at end-2020) and prudent liquidity management at the holding company.

We believe that the challenges to the UK and US economies from the coronavirus pandemic have subsided sufficiently to remove the negative outlook on Barclays' 'aa-' operating environment score.

Better adaptation of businesses to working with the economic restrictions and greater resilience of private consumption and investment have resulted in an upward revision of Fitch's UK real GDP growth estimate and forecast for 2020-2021 to -9.8% and 6.6%, respectively, with growth moderating to 5.0% in 2022. We expect the unemployment rate to average just 5.4% in 2021, supported by the extension of income- and job-support schemes and the continuation of fiscal and pandemic-related loan support to businesses.

The US economic outlook has also improved substantially over recent months, aided by the strong rollout of vaccines and additional fiscal stimulus and means that the operating environment for banks operating in the US has stabilised. Fitch recently revised up its US GDP growth for 2021 by 1.7pp to 6.2% on the back of the USD1.9 trillion coronavirus relief package and stronger than expected data for 1Q21.

Barclays remained profitable in 2020, despite exceptionally high impairments, lower interest rates and weaker lending revenue. Pre-tax profit of GBP3.1 billion was down 30% y-o-y but operating profit/risk-weighted assets (RWA) of 1.0% was a reasonable outcome amid significant disruptions to economic activity, driven by a strong performance by CIB and resilient banking fees (notably debt capital markets). This helped the group remain profitable, despite a 2.1x yoy increase in loan impairment charges to GBP3.9 billion and lower revenue from other activities (such as credit cards).

We expect profitability to recover in 2021, helped by conducive market conditions (including still high corporate capital and financing needs and continued economic uncertainty) for the CIB and lower provisioning, and despite pressure from the low interest rate environment and fragile corporate borrower confidence. We have revised the outlook on Barclays' 'a-' earnings mid-point to stable as we expect the group to report operating profit profit/RWA of between 1.5%-2.0% over the next two years as the customer segments most affected by the pandemic (credit cards and payments) begin to recover as economic conditions normalise.

Barclays' asset quality metrics have held up well so far, with an end-1Q21 impaired (Stage 3) loan ratio of 2.4%. As government support for borrowers in the UK and US is unwound, Stage 3 inflows are likely to pick up in 2H21, particularly from Barclays' exposure to unsecured consumer credit (12% of end-1Q21 customer balances) and certain more vulnerable sectors (such as oil & gas, leisure and hospitality, transportation).

However, we believe the deterioration will be manageable, reflecting the improved economic outlook and the group's conservative underwriting standards in domestic mortgages and corporate lending, including the routine use of risk transfer deals to help mitigate losses. Consequently, we have revised the outlook on the asset quality mid-point of 'a' to stable as the increase in Stage 3 loans is likely to be more modest than we previously expected.

Barclays' end-1Q21 common equity Tier 1 (CET1) ratio of 14.6% (14.0% excluding IFRS9 transitional arrangements) remains comparable with global trading and universal bank peers. We expect organic capital generation to remain strong and sufficient for the CET1 ratio to remain within the bank's 13%-14% target range. Challenges that could arise during 2021 include RWA inflation from rating migrations and a reduced benefit from IFRS9 transitional relief as more loans start to migrate to Stage 3. However, the timing of this is uncertain and depends partly on how government support measures and borrower activity develops. Regulatory changes appear manageable based on management guidance.

The group's funding profile is stable and diversified, underpinned by a strong UK retail franchise to fund retail assets and good market access to fund wholesale operations. The group's Fitch-calculated loan/deposit ratio of 71% at end-1Q21 is unusually strong and reflects crisis-driven deposit inflow rates, although in line with peers, the ratio should return to the mean (2016-19 average: 84%) as savings rates normalise and loan growth picks up. Liquidity is conservatively managed, with a liquidity coverage ratio of 161% (2018-2020 average: 164%) and an eligible liquidity pool of GBP290 billion, which are well above regulatory requirements.

The 'F1' Short-Term IDR is the lower of two possible options mapping to a Long-Term IDR of 'A' since the group's funding and liquidity score of 'a' is not sufficient to achieve a higher Short-Term IDR.

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. We consider the VRs of BBplc and BBUK to be very closely correlated as capital and funding remains highly fungible between the two entities, subject to each meeting their respective regulatory requirements. Additionally, integration between the two entities and the group is underpinned by common group management and strategy, and access to group knowledge and systems through the group's service company.

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 size and houses CIB and the international cards and payments businesses.

The revision of the Outlooks on BBplc's and BBUK's Long-Term IDRs to Stable reflects the same drivers as Barclays. BBplc's business model is structurally more volatile because of the nature of the bank's businesses, but underlying profitability has remained resilient to the pandemic. This is due to conducive markets for investment banking and capital markets but also developments that pre-date the pandemic, such as growth in key CIB segments, including debt capital markets activities and in the payments business.

BBplc's funding profile is not as strong as BBUK's, which is a function of its heavy reliance on wholesale funding, but we believe that the availability of ordinary support (BBplc already benefits from significant debt (including hybrid) downstreamed from the holding company) mitigates this risk. 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 one notch above their respective VRs, and one notch above Barclays' 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 Derivative Counterparty Ratings (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 a 'A+' Long-Term IDR as their funding and liquidity scores are not sufficient to achieve a higher Short-Term IDR.

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 to date 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 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. The SR indicates a 'A' long-term rating floor based on institutional support.

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) and was set up in advance of the UK's departure from the EU on 31 January 2021. The activities that are housed in BBI give the group 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 we expect senior creditors of both entities to benefit from the parent's resolution debt buffers, reflecting regulatory requirements to pre-place junior debt or equity (in the case of BCI, at the level of the US intermediate holding company).

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 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:

Barclays' VR and other ratings linked to it are sensitive to an unexpected severe setback in the economic recovery (for example, due to further lockdowns or new Covid-19 variants) in the group's two key markets, the UK and US, or if the financial repercussions of rising unemployment and economic disruptions due to the pandemic are worse than Fitch's current base case.

Negative rating action could be triggered if we expect asset quality deterioration to be more severe than expected, if capitalisation weakens significantly with the CET1 ratio (excluding the IFRS 9 transitional relief) looking set to fall towards 12% without a clear path to restore it within 18-24 months to within the bank's current target, or if profitability challenges arising from the pandemic shock to the economy persist and we no longer expect the group's operating profit/RWA to rise above 1.5% on a sustained basis.

The 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 RWA allocated to investment-banking activities or towards higher-risk credit exposures.

Barclays' VR is also sensitive to an increase in common equity double leverage above 120%, which we do not expect.

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 could 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 BBI could be downgraded if BBplc was downgraded or if they are no longer expected to be protected by resolution plan buffers of junior debt/equity from BBplc.

The Short-Term IDRs could be downgraded if Long-Term IDRs were 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 trigger points will fall below 100bp.

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

Under more normalised economic conditions, the most likely trigger for an upgrade of Barclays' ratings would be evidence that on a sustained basis the group can meet its cost-to-income targets and maintain operating/profit comfortably above 1.5%, resulting in a stronger capacity to generate capital organically. This would be in the context of the group ensuring sufficiently robust risk appetite and controls in light of its focus on more volatile investment banking activities, while maintaining healthy capital metrics and consistently strong asset quality performance.

Barclays' IDR could be rated above the VR if AT1 and Tier 2 debt increase sustainably above 10% of RWAs, but we view this as unlikely.

The Short-Term IDRs of Barclays, BBplc and BBUK could be upgraded if our assessment of their respective funding & liquidity improves to 'aa-' or above. The Short-Term IDRs of BBI and BCI could be upgraded if BBplc's Short-Term IDR was upgraded.

## 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.

## ESG Considerations

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

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## Rating Actions

| ENTITY/DEBT | RATING | | | RECOVERY | PRIOR |
|---|---|---|---|---|---|
| Barclays Bank UK PLC | LT IDR | A+ | Affirmed | | A+ |
| | ST IDR | F1 | Affirmed | | F1 |
| | Viability | a | Affirmed | | a |
| | Support | 1 | Affirmed | | 1 |
| | DCR | A+(dcr) | Affirmed | | A+(dcr) |
| • senior unsecured | LT | A+ | Affirmed | | A+ |
| • senior unsecured | ST | F1 | Affirmed | | F1 |
| Barclays plc | LT IDR | A | Affirmed | | A |
| | ST IDR | F1 | Affirmed | | F1 |
| | Viability | a | Affirmed | | a |
| | Support | 5 | Affirmed | | 5 |
| | Support Floor | NF | Affirmed | | NF |

| ENTITY/DEBT | RATING | | | RECOVERY | PRIOR |
|---|---|---|---|---|---|
| • senior unsecured | LT | A | Affirmed | | A |
| • senior unsecured | LT | A | Affirmed | | A |
| • subordinated | LT | BBB+ | Affirmed | | BBB+ |
| • subordinated | LT | BBB- | Affirmed | | BBB- |
| • subordinated | LT | BBB+ | Affirmed | | BBB+ |
| • senior unsecured | ST | F1 | Affirmed | | F1 |
| Barclays Bank plc | LT IDR | A+ | Affirmed | | A+ |
| | ST IDR | F1 | Affirmed | | F1 |
| | Viability | a | Affirmed | | a |
| | Support | 5 | Affirmed | | 5 |
| | Support Floor | NF | Affirmed | | NF |
| | DCR | A+(dcr) | Affirmed | | A+(dcr) |

| ENTITY/DEBT | RATING | | | RECOVERY | PRIOR |
|---|---|---|---|---|---|
| • senior unsecured | LT | A+ | Affirmed | | A+ |
| • senior secured | LT | A+ | Affirmed | | A+ |
| • senior secured | LT | A+ | Affirmed | | A+ |
| • senior unsecured | LT | A+ | Affirmed | | A+ |
| • subordinated | LT | BBB+ | Affirmed | | BBB+ |
| • subordinated | LT | BBB- | Affirmed | | BBB- |
| • subordinated | LT | BBB | Affirmed | | BBB |
| • senior unsecured | ST | F1 | Affirmed | | F1 |
| • senior secured | ST | F1 | Affirmed | | F1 |
| Barclays Capital Inc. | LT IDR | A+ | Affirmed | | A+ |

| ENTITY/DEBT | RATING | | | RECOVERY | PRIOR |
|---|---|---|---|---|---|
| | ST IDR | F1 | Affirmed | | F1 |
| | Support | 1 | Affirmed | | 1 |
| | DCR | A+(dcr) | Affirmed | | A+(dcr) |
| • senior unsecured | ST | F1 | Affirmed | | F1 |
| Barclays Bank Ireland Plc | LT IDR | A+ | Affirmed | | A+ |
| | ST IDR | F1 | Affirmed | | F1 |
| | Support | 1 | Affirmed | | 1 |
| | DCR | A+(dcr) | Affirmed | | A+(dcr) |

| RATINGS KEY | OUTLOOK | WATCH |
|---|---|---|
| **POSITIVE** | | |
| **NEGATIVE** | | |
| **EVOLVING** | | |
| **STABLE** | | |

## 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

Solicitation Status

## Endorsement Status

| | |
|---|---|
| Barclays Bank Ireland Plc | UK Issued, EU Endorsed |
| Barclays Capital Inc. | UK Issued, EU Endorsed |
| Barclays plc | UK Issued, EU Endorsed |

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