

13 JUL 2021

## Fitch Affirms Standard Chartered PLC's 'A' IDR; Negative Outlook

Fitch Ratings - London - 13 Jul 2021: Fitch Ratings has affirmed Standard Chartered PLC's (Standard Chartered) and Standard Chartered Bank's (SCB) Long-Term Issuer Default Rating (IDR) at 'A' and 'A+', respectively, with Negative Outlooks. Their Viability Ratings (VRs) have been affirmed at 'a'. A full list of rating actions can be found below.

### Key Rating Drivers

#### IDRs, VRs AND SENIOR DEBT

The IDR of Standard Chartered is driven by its VR, which balances strong funding and liquidity, resilient capitalisation, and fairly conservative risk appetite, against its weaker earnings and asset quality relative to most similarly-rated peers'. We see the group's company profile under pressure from challenges in generating adequate profitability on a sustained basis, particularly in a lower interest-rate environment, broadly in line with global peers.

Standard Chartered has been refining its strategy in response to the challenging revenue environment, although the operating environment has broadly stabilised, in our opinion, and risks to its asset quality and capitalisation have eased. Challenges to its business model, management and strategy and earnings and profitability contribute to the Negative Outlook on the IDRs.

Fitch sees pandemic-related economic risks subsiding across much of Standard Chartered's footprint, particularly in Hong Kong, China, Singapore, the US and the UK, where economies have been more resilient than we expected due to pandemic-containment measures (particularly in Asia) and effective support measures put in place by authorities. We have therefore revised the outlook on the group's 'a' operating environment to stable, which reflects a blended view on the markets it operates in.

The improved economic backdrop, as well as the group's risk appetite and risk-provisioning policies mean that pressure has also subsided for Standard Chartered's asset quality, for which we have also revised the outlook to stable. We expect the impaired loans ratio to increase from 3% at end-1Q21, considering the magnitude of early-alert exposures of about USD10 billion at end-1Q21 and the group's USD48 billion exposure to more cyclical and vulnerable sectors such as aviation, commodity traders, metals and mining, commercial real estate, hotels, tourism and oil& gas. Nevertheless, loans impairment charges (LICs) should decline in 2021 and beyond, despite downside risk to the 35bp-40bp LICs guidance given economic uncertainties and the group's presence in markets, particularly in southeast Asia, which are experiencing a resurgence in infections.

A drop in LICs should support an improvement in operating return on risk weighted assets (RWAs) to 1.2%-1.4% over 2021-2022 from 0.8% in 2020, as per our estimates, with further medium-term upside if interest rates rise and if the group's strategies to drive 5%-7% revenue growth through a combination of volume, asset mix, funding optimisation and better fee generation bear fruit from 2022 onwards. Profitability remains a weakness for the rating, and if sustained we would revise downward our assessment for this factor, with potential implications for the VR. This could be the case if our assumed recovery and the path to at least 7% return on tangible equity (RoTE) by 2023 and 10% over the medium term are disrupted again by weaker than-expected revenue or higher provisioning needs.

This would also have implications for our assessment of company profile, and management and strategy which at this level are contingent on the business model and strategies having reached a degree of stability. The group's 2021 strategic update puts additional emphasis on mass-market retail opportunities, sustainable finance business and expanding financial markets originate-to-distribute capabilities. This is on top of longer-standing strategies to derive value from a very extensive network, capturing trade flows, investment flows in and out of China, and banking with affluent retail customers.

Capitalisation has been resilient since the onset of the pandemic due to a combination of controlled RWA expansion, including business disposals, positive profitability and pay-out restrictions. We have revised the outlook on this factor to stable from negative because we believe that management's targeted 13%-14% common equity Tier 1 (CET1) will be adhered to under our baseline expectation of sufficient profit retention and moderate RWA growth.

Our funding and liquidity assessment is underpinned by Standard Chartered's deposit-led funding profile, low loans/deposits ratio, strong liquidity, and manageable refinancing needs. The group is mainly funded by deposits, which grew reasonably strongly in 2020 (by 8%), driven by operating account balances in cash management and retail current and savings accounts. The liquidity coverage ratio improved to 150% at end-1Q21 from 143% at end-2020.

The ratings of Standard Chartered reflect its consolidated risk profile, which mainly consists of UK-based SCB and Hong Kong-based Standard Chartered Bank (Hong Kong) Limited. We reflect the group's consolidated profile in SCB's ratings as well, as we believe that its risk profile is highly correlated with the group's, reflecting its deep integration.

The IDR of SCB is one notch above its and the group's VRs as we believe that its senior creditors are protected by internal minimum requirement for own funds and eligible liabilities (MREL) buffers, given its role as a material legal entity in the group's resolution planning.

Standard Chartered's VR also considers moderate common equity double leverage (109% at end-2020) at the holding company level.

Senior debt ratings are aligned with the respective issuers' IDRs.

#### SUBORDINATED & HYBRID DEBT

Subordinated Tier 2 debt is rated two notches below the respective issuers' VRs, which is Fitch's

baseline notching for loss severity for this type of debt given our expectations of poor recoveries. Upper Tier 2 debt is rated three notches below SCB's VR, including one notch for non-performance given cumulative coupon deferral features.

Additional Tier 1 (AT1) instruments and preference shares are rated four notches below the VR, as we expect that the group will maintain a buffer over capital requirements of at least 100bp of RWAs.

#### SUPPORT RATING AND SUPPORT RATING FLOOR

Standard Chartered's and SCB's Support Rating of '5' and Support Rating Floor of 'No Floor' reflect Fitch's opinion that senior creditors cannot rely on extraordinary support from the UK government.

#### RATING SENSITIVITIES

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

Standard Chartered's and SCB's Long- and Short-Term IDRs are mainly sensitive to the factors driving the VRs. The VRs are most sensitive to progress with the group's strategic objectives aimed at improving profitability, and Fitch's assessment of the group's business model and company profile strength linked to these. Our assessment could also be negatively affected by a meaningful increase in the group's risk appetite in a response to medium-term pressures on profitability, as well as by any geopolitical tensions between China and the West, should they have more binding negative implications for the group's company profile, strategy and financial position.

We would likely downgrade the VR if the expected trajectory of operating profitability drops significantly below 1.2% of RWAs and the prospects of achieving over 7% RoTE by 2023 and 10% over the medium term are disrupted again. This could happen in conjunction with weaker-than-expected revenue growth relative to management's guidance or higher provisioning needs, for instance due to setbacks in the economic recovery, and if the group's assets quality deteriorates beyond an assumed four-year average impaired loans ratio of 3%-4%. A decline in capitalisation below the 13%-14% targeted range, without a credible plan to restore it, is also a negative sensitivity.

SCB's IDR would be downgraded to the level of the bank's VR if we no longer believe that creditors will be protected in a resolution by internal MREL.

Senior debt ratings are primarily sensitive to the respective issuers' IDRs.

AT1 and Tier 2 subordinated notes are primarily sensitive to changes in the respective issuers' VRs. The AT1 notes' ratings are also sensitive to Fitch's assessment of their non-performance risk relative to the risk captured in the VR. They could be downgraded to five or more levels below the VRs of Standard Chartered and SCB if non-performance risk is assessed to have increased, for instance, due to a shift in capital requirements, lower capital targets, or heightened likelihood that the buffer over maximum distributable amount (MDA) thresholds will decrease below 100bp.

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

The Outlook could be revised to Stable if our view of the company profile and associated pressures improves, which could happen in conjunction with a better-than-expected earnings trajectory, and once risks to the revenue and LIC guidance subside. An upgrade of the IDR and VR is unlikely in the medium term as it would require sustained improvement in the group's company profile, earnings and evidence of robust asset quality through the cycle, with no meaningful increase in risk appetite.

Tier 2 debt could be upgraded if the group's tier 2 and AT1 debt increase sustainably to over 10% of RWAs as this would lead to better recovery prospects.

An upgrade of the banks' Support Ratings and upward revision of their Support Rating Floors would be contingent on a positive change in the sovereign's propensity to support the banks, which we see as highly improbable.

### **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 entity, either due to their nature or the way in which they are being managed by the entity. For more information on Fitch's ESG Relevance Scores, visit [www.fitchratings.com/esg](http://www.fitchratings.com/esg)

### **Fitch Ratings Analysts**

**Ioana Sima**

Director

Primary Rating Analyst  
+44 20 3530 1736  
Fitch Ratings Ltd 30 North Colonnade, Canary Wharf London E14 5GN

**Tania Gold**

Senior Director  
Secondary Rating Analyst  
+65 6796 7224

**David Wong**

Senior Director  
Committee Chairperson  
+852 2263 9927



**Media Contacts**

**Louisa Williams**

London  
+44 20 3530 2452  
louisa.williams@thefitchgroup.com

**Rating Actions**

ENTITY/DEBT	RATING		RECOVERY	PRIOR
Standard Chartered Bank	LT IDR	A+	Affirmed	A+
	ST IDR	F1	Affirmed	F1
	Viability	a	Affirmed	a
	Support	5	Affirmed	5
	Support Floor	NF	Affirmed	NF
• senior unsecured	LT	A+	Affirmed	A+

ENTITY/DEBT	RATING		RECOVERY	PRIOR
• subordinated	BBB+		Affirmed	BBB+
• subordinated	BBB		Affirmed	BBB
• senior unsecured <sup>ST</sup>	F1		Affirmed	F1
Standard Chartered PLC	LT IDR	A 	Affirmed	A 
	ST IDR	F1	Affirmed	F1
	Viability	a	Affirmed	a
	Support	5	Affirmed	5
	Support Floor	NF	Affirmed	NF
• subordinated	BBB-		Affirmed	BBB-
• preferred <sup>T</sup>	BBB-		Affirmed	BBB-
• senior unsecured <sup>LT</sup>	A		Affirmed	A
• subordinated	BBB+		Affirmed	BBB+

ENTITY/DEBT	RATING	RECOVERY	PRIOR
• senior unsecured <sup>ST</sup>	F1	Affirmed	F1

## RATINGS KEY OUTLOOK WATCH

POSITIVE	⊕	◊
NEGATIVE	⊖	◊
EVOLVING	◊	◆
STABLE	◐	

## Applicable Criteria

[Bank Rating Criteria \(pub.28 Feb 2020\) \(including rating assumption sensitivity\)](#)

## Additional Disclosures

[Solicitation Status](#)

## Endorsement Status

Standard Chartered Bank UK Issued, EU Endorsed

Standard Chartered PLC UK Issued, EU Endorsed

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