FitchRatings

RATING ACTION COMMENTARY

Fitch Revises Volkswagen's Outlook to Negative; Affirms IDR at 'A-'

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Fitch Ratings - Barcelona - 07 Apr 2025: Fitch Ratings has revised Volkswagen AG's (VW) Outlook to Negative from Stable, while affirming its Long-Term Issuer Default Rating (IDR) at 'A-'. A full list of rating actions is below.

The Negative Outlook reflects worsening market conditions in the US and increasing cost pressures driven by tariffs imposed on the automotive sector. Fitch expects VW's EBIT margins to fall 100bp-150bp, to around 5%, and free cash flow (FCF) margins to remain negative over the next 12 months, putting them below their rating sensitivities. Although we expect medium-term recovery as restructuring charges subside and new model launches ramp up, we see limited rating headroom for execution risk and additional economic stress from our revised expectations for much of Europe.

The affirmation reflects the company's robust capital structure and solid business profile with good geographic diversification and a product range covering almost all car and commercial-vehicle subsectors.

KEY RATING DRIVERS

Tariffs to Hit Operating Profit: We estimate the 25% tariff targeting US-bound EU cars to cause EBIT margin to drop by 100bp-150bp in 2025, on top of recent restructuring costs in Europe. The tariffs affect one third of VW's US sales and less than 4% of its total sales, affecting mostly its lucrative Audi and Porsche brands. Fitch expects the levies to be largely absorbed by VW.

The company can pass on the additional price increase to customers, although this would erode its market share in the US. Fitch forecasts the operating margin will recover to 7% by 2026. Nevertheless, prolonged trade talks between the political parties for a resolution and tariff-induced inflation could dampen new car demand and pose further downside to operating margins.

Mitigation Measures: We estimate that VW manufactures around 40% of its US sales in its Mexico plants, where some of the produced output is not United States-Mexico-Canada Agreement (USMCA)-compliant. Although like its US peers, the company should be able to certify its USMCA-compliant parts and production, it will not be able to fully mitigate the tariff effect. Inventory in hand can provide temporary buffer, but, if decided, moving production lines to the Chattanooga plant or increasing capacity in Blythewood for its Scout brand will take time and may increase capex.

Temporarily Negative FCF Margin: We forecast VW's FCF margin will remain negative for the second year in 2025, breaching the downgrade sensitivity of 2%, before recovering to close to that in 2026. This considers its squeezed operating margins, the restructuring cash expense, lower cash flow contributions from Chinese joint ventures (which we expect to stabilise at a lower level) and VW Financial Services, but does not incorporate additional capex needs stemming from localising production capacity for the affected vehicle models. Fitch expects capex to be reshuffled within the company's existing EUR165 billion programme. The temporarily negative FCF is offset by its net cash position, which we forecast will be sustainable across 2025-2028.

Robust Capital Structure: We expect VW's capital structure to remain in line with those of higher-rated peers and commensurate with the 'a' rating category median in our criteria for the industry. This is a key pillar for the company's rating, despite historical swings in FCF generation. Profitability from 2026 should benefit from restructuring programmes. Nonetheless, CO2 emission fines, although delayed for the short term, and the push for a higher electric vehicle portfolio share with more affordable models can disrupt the profitability recovery trajectory.

Strong Business Profile: VW's ratings are supported by its unparalleled product portfolio in the auto and heavy-truck segments. The ratings also reflect the company's broad diversification, leading market share and unrivalled potential for cost savings and economies of scale. Its size enables an industrial strategy of platform consolidation and yields sizable economies of scale and synergies across its broad brand portfolio. However, its complex structure has hindered the full reflection of these synergies in operating profit.

Chinese Competition: Fitch does not expect a major shift in the competitive landscape in China, as demand continues to fluctuate on the back of macroeconomic trends and government subsidies. Luxury brands are aligned with overall demand and we expect them to take time to fully recover. The local automotive market continues to face intense competition, leading to steep price discounts, and an increasing number of domestic electric vehicle producers, except BYD, are becoming financially distressed. The timing of a turnaround is uncertain and we do not expect European original equipment manufacturers, including VW, to regain market shares lost over the past four years.

Porsche Strategy Untested: The tariffs could weigh on Porsche's 2025 US sales, but Fitch believes the luxury subsector is less price sensitive, and US competitors would take time to develop comparable models. Porsche's 'value over volume' strategy in China, together with the Taycan 4 tailored for local consumers, remains untested. Competition at the higher end of the luxury subsector is intensifying since 2024, as domestic automakers seek to gain market share. Fitch assumes Porsche's profit margins will be 14% towards 2028, below management's medium-term guidance of 15%-17%.

PEER ANALYSIS

VW is the largest car manufacturer by deliveries in Europe and is among the top global manufacturers, like Toyota Motor Corporation (A+/Stable), Hyundai Motor Company (A-/Stable), General Motors Company (BBB/Positive) and the global alliance between Renault SA (NR), Nissan Motor Co., Ltd. (BB+/Negative) and Mitsubishi Motors Corporation.

VW is the most diversified auto manufacturer in the world, in line with Toyota, with substantial product and geographic exposure as well as production diversification. Its individual brands have a lower value than other premium manufacturers, such as BMW and Mercedes-Benz Group AG (A/Stable), as well as other large global manufacturers, including Honda Motor Co., Ltd (A/Stable) and Toyota, but VW owns several brands with a strong image and value.

The company's Fitch-adjusted industrial operating margin of 7%-8% exceeds 6%, which is the midpoint for 'a' rating category in our criteria for auto producers, but lags that of other German car manufacturers. Its profitability benefits from the high operating margins of its premium and sports brands, Audi and Porsche. FCF generation is robust (except for 2024-2025), aided by dividends from its Chinese joint ventures and reduced settlement payments related to diesel emissions scandal disputes.

KEY ASSUMPTIONS

Revenue growth at low-to mid-single digits over 2025-2028.

EBIT margin declining to around 5% in 2025 caused by tariffs, before recovering to around 7% in 2026.

Neutral to negative net working capital (NWC) development to 2028.

Capex averaging around 9% of revenue (Fitch definition, does not include R&D costs and investments into JVs)

Dividends to common shareholders and preferred shareholders at about 30% of net income.

Fitch has a blanket assumption of EUR4 billion restructuring costs, captured in 2025 and 2026.

RATING SENSITIVITIES

Factors that Could, Individually or Collectively, Lead to Negative Rating Action/Downgrade

FCF margins below 2.0% for a sustained period.

Industrial operating margin remaining below 6%.

Sharp deterioration in key credit metrics, including net debt/EBITDA of 1x.

Factors that Could, Individually or Collectively, Lead to Positive Rating Action/Upgrade

Tighter corporate governance.

FCF margins sustained above 3%.

LIQUIDITY AND DEBT STRUCTURE

VW's industrial business has a consistent record of strong liquidity and a net cash position. Its industrial operations reported EUR24.1 billion in cash and equivalents and EUR23.1 billion in marketable securities at end-2024. Fitch restricts around EUR6.6 billion, or about 2.5% of annual sales, for working capital and operational purposes. We project negative FCF generation in 2025, resulting from restructuring programme cash payout and a challenging operating environment. The company has sufficient internal liquidity to absorb the FCF volatility.

VW's liquidity profile is supported by its renewed and increased EUR12.5 billion syndicated credit line with a five-year maturity and two extension options. At the group level, the company had EUR32.4 billion in bilateral and syndicated credit lines, with only EUR2 billion drawn at end-2024. It has a solid record of capital market access, even under stress conditions, and benefits from diversified funding sources.

ISSUER PROFILE

VW is among the largest global car and commercial vehicle manufacturers, with group sales of EUR324.7 billion and around 9 million vehicles delivered in 2024.

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.

MACROECONOMIC ASSUMPTIONS AND SECTOR FORECASTS

Click here to access Fitch's latest quarterly Global Corporates Macro and Sector Forecasts data file which aggregates key data points used in our credit analysis. Fitch's macroeconomic forecasts, commodity price assumptions, default rate forecasts, sector key performance indicators and sector-level forecasts are among the data items included.

ESG CONSIDERATIONS

VW has an ESG Relevance Score of '4' for Governance Structure due to a lack of independence and diversity at the supervisory board level, potential conflicts of interest with board members and a 20% blocking minority in voting resolutions. The Porsche AG (PAG) IPO is likely to further increase VW's governance structure complexity given the creation of ordinary and non-voting preferred shares in PAG. VW's governance structure and limited board independence is embedded in Fitch's rating assessment of VW. This has a negative impact on the credit profile and is relevant to the rating in conjunction with other factors.

VW has an ESG Relevance Score of '4' for GHG Emissions and Air Quality due to stringent emission regulations, notably in Europe and China, which are its main markets. Investments in lower emissions are a key driver of the group's strategy and cash generation, which has a negative impact on the credit profile and is relevant to the rating in conjunction with other factors.

The highest level of ESG credit relevance is a score of '3', unless otherwise disclosed in this section. A score of '3' 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. Fitch's ESG Relevance Scores are not inputs in the rating process; they are an observation on the relevance and materiality of ESG factors in the rating decision. For more information on Fitch's ESG Relevance Scores, visit https://www.fitchratings.com/topics/esg/products#esg-relevance-scores.

RATING ACTIONS

ENTITY / DEBT	RATING			PRIOR
VW Credit Canada, Inc.				
senior unsecured	LT	A-	Affirmed	A-
Volkswagen Group of America Finance, LLC				
senior unsecured	LT	A-	Affirmed	A-
Volkswagen International Finance NV				
senior unsecured	LT	A-	Affirmed	A-
subordinated	LT	BBB	Affirmed	BBB
Volkswagen AG	LT IDR	A-	Affirmed	A-

ST IDR	F1	Affirmed	F1

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VIEW ADDITIONAL RATING DETAILS

Additional information is available on www.fitchratings.com

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APPLICABLE CRITERIA

Corporate Hybrids Treatment and Notching Criteria (pub. 12 Nov 2020)

Corporates Recovery Ratings and Instrument Ratings Criteria (pub. 02 Aug 2024) (including rating assumption sensitivity)

Corporate Rating Criteria (pub. 06 Dec 2024) (including rating assumption sensitivity)

Sector Navigators – Addendum to the Corporate Rating Criteria (pub. 06 Dec 2024)

APPLICABLE MODELS

Numbers in parentheses accompanying applicable model(s) contain hyperlinks to criteria providing description of model(s).

Corporate Monitoring & Forecasting Model (COMFORT Model), v8.1.0 (1)

ADDITIONAL DISCLOSURES

Dodd-Frank Rating Information Disclosure Form

Solicitation Status

Endorsement Policy

ENDORSEMENT STATUS

Volkswagen AG	EU Issued, UK Endorsed

Volkswagen Group of America Finance, LLC	EU Issued, UK Endorsed
Volkswagen International Finance NV	EU Issued, UK Endorsed
VW Credit Canada, Inc.	EU Issued, UK Endorsed

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