MOODY'S
RATINGS

Rating Action: Moody's Ratings downgrades Volkswagen's ratings to Baa1, outlook stable

17 Mar 2025

Frankfurt am Main, March 17, 2025 -- Moody's Ratings (Moody's) has today downgraded the long-term issuer rating of Volkswagen Aktiengesellschaft (Volkswagen, VW or the company) to Baa1 from A3. The company's short-term ratings are affirmed at Prime-2 (P-2). The outlook was changed to stable from negative.

The downgrade to Baa1 reflects the recent contraction in operating margin and free cash flow generation, with limited expectation of a material recovery over the next quarters. Volkswagen had already been weakly positioned in the previous A3 rating category since July 21, 2023, when we expected a sustained recovery of Moody's adjusted EBITA margin to a level of 6.5-7%.

Volkswagen's operating performance will remain pressured in the next 12-18 months by a combination of:

1. Sector headwinds, such as low volume growth and sustained high price pressure globally, intensified by geopolitical uncertainties, especially trade tensions.

2. Structural challenges from the transition to zero-emissions vehicles, constraining profitability levels.

3. Fierce competition in China, resulting in reduced market share and weakening profit contributions.

4. Ongoing need for investments and successful execution in software to stay competitive, an area that encompasses high execution risk in our view.

While we positively acknowledge management's recently implemented efficiency improvement measures, the significant market challenges make it unlikely that the Moody's adjusted EBITA margin will recover sustainably towards 7% in the next 12-18 months. While Volkswagen's credit profile benefits from its scale, diversification and strong balance sheet with very good liquidity profile, the profitability gap compared to its single A-rated peers has recently widened.

A full list of all affected ratings can be found at the end of this press release.

RATINGS RATIONALE

Last year, Volkswagen's automotive division's revenue decreased by 1%, and profitability dropped to 5.7% (Moody's adjusted EBITA). The company's operating performance in Q4 2024 largely met our expectations set last October, which were based on VW's revised guidance issued in September 2024. Considering the more challenging market environment, we expect a Moody's adjusted EBITA margin of around 5.5-6.0% over the next 12-18 months, including €2 billion of restructuring expenses per year for 2025 and 2026 (€2.5 billion in 2024).

In 2024, Moody's adjusted free cash flow (FCF) turned negative at -€1.3 billion due to the weakening operating profit and high capex. We expect FCF to improve with reduced capex, but it will likely remain relatively weak, below mid-single digits as a percentage of debt in the next 12-18 months. This forecast includes 30 product launches this year, mainly at Audi and VW. While these launches constrain FCF generation, they are a key basis for Volkswagen's medium term performance improvements.

Volkswagen's management, which took over in 2022, has initiated strategic changes to stay competitive. These measures, provided a successful execution could support an improvement in profitability by 2026/27. One element is a new software strategy with XPeng and Rivian. The partnership with Rivian aims to improve software development and marks a shift away from the costly in-house subsidiary CARIAD, which faced operational issues and continued losses. The first car on the Rivian platform, the ID1, is expected in 2027. Another key initiative are planned fixed cost reductions. The restructuring agreement in December 2024 aims to reduce fixed costs in Germany, which have weighed on VW brand's profitability. We forecast €1 billion in cost savings from this agreement in 2025, mainly from canceled bonuses and planned wage increases. Larger cost savings towards the mid-term targeted €4 billion per year are expected by 2027/28 through workforce and production capacity reductions.

Volkswagen generates its profits in China from locally produced vehicles within the local joint-ventures (€1.7 billion proportionate profit accounted at equity in 2024, down from €2.6 billion in 2023) and imported cars mainly from Audi and Porsche. Volkswagen's market share in China has dropped from 17.2% in 2019 to 11.1% due to the rapid adoption of New Energy Vehicles (NEVs) and the rise of local brands. NEVs now account for 40% of the market, up from 5% in 2019, while local brands' sales have surged to 65% of total passenger vehicle sales in 2024. We expect NEV adoption to continue rising, with local brands leading the market. Consequently, Volkswagen and other foreign automakers, which still rely on the declining internal combustion engine (ICE) segment, face ongoing challenges. Fierce price competition from local brands is also hurting their profits. Volkswagen's new strategy for China aims to launch more competitive BEV and ICE models by 2026 through its local joint venture partners.

The transition to electric vehicles has been slower and more costly than expected, constraining Volkswagen's profitability, as electric vehicles relative profitability is still lower compared to combustion vehicles. The company has invested significantly in electrification, including in-house battery production under its subsidiary PowerCo, increasing its BEV share to 8.3% in 2024. The European Commission's proposal to relax CO2 emissions regulation could give Volkswagen more time to achieve CO2 compliance in Europe, positively impacting its 2025 operating profit.

Volkswagen's strong business profile as the second-largest global auto manufacturer, with good geographic and brand diversification and good progress towards zero-emissions vehicles, supports its Baa1 rating. Volkswagen's balance sheet is robust, with low leverage (1.7x Moody's adjusted debt/EBITDA in 2024) and very good liquidity. This gives the company time to implement strategic shifts and manage industry challenges.

OUTLOOK

The stable outlook reflects our expectations that despite the challenging market environment, Volkswagen will maintain a Moody's adjusted EBITA margin (after restructuring expenses) of around 5.5-6.0%, a Moody's adjusted debt/EBITDA well below 2.5x and very good liquidity. Consequently, Volkswagen is solidly positioned in the Baa1 rating category.

FACTORS THAT COULD LEAD TO AN UPGRADE OR DOWNGRADE OF THE RATINGS

Upward rating pressure could develop in case (1) Moody's adjusted EBITA margin (after restructuring) increases above 7% sustainably, (2) Moody's adjusted debt/EBITDA stays below 2x sustainably, (3) Moody's adjusted FCF/debt improves well above mid-single-digit percentages sustainably and (4) the company global market share trend stabilizes supported by a successful execution of BEV transition.

Downward rating pressure could develop in case (1) Moody's adjusted EBITA margin (after restructuring) decreases below 5% for a prolonged period of time, (2) Moody's adjusted debt/EBITDA increases above 2.5x for a prolonged period of time, (3) Moody's adjusted FCF remains negative and/or liquidity weakens. Loss of global market share could add to the downward rating pressure.

LIST OF AFFECTED RATINGS

Issuer: Volkswagen Aktiengesellschaft

..Downgrades:

.... LT Issuer Rating, Downgraded to Baa1 from A3

.... Senior Unsecured Bank Credit Facility (Local Currency), Downgraded to Baa1 from A3

.... Senior Unsecured Medium-Term Note Program (Local Currency), Downgraded to (P)Baa1 from (P)A3

..Affirmations:

.... Commercial Paper (Local Currency), Affirmed P-2

..Outlook Actions:

....Outlook, Changed To Stable From Negative

Issuer: Porsche Holding Gesellschaft m.b.H.

..Affirmations:

.... Backed Commercial Paper (Local Currency), Affirmed P-2

..Outlook Actions:

.... Outlook, No Outlook

Issuer: Volkswagen Group Canada, Inc.

..Affirmations:

.... Backed Commercial Paper (Local Currency), Affirmed P-2

..Outlook Actions:

.... Outlook, No Outlook

Issuer: Volkswagen Group of America Finance, LLC

..Downgrades:

.... Backed Senior Unsecured Medium-Term Note Program (Foreign Currency), Downgraded to (P)Baa1 from (P)A3

.... Backed Senior Unsecured (Local Currency), Downgraded to Baa1 from A3

..Affirmations:

.... Backed Commercial Paper (Local Currency), Affirmed P-2

.... Backed Commercial Paper (Foreign Currency), Affirmed P-2

..Outlook Actions:

....Outlook, Changed To Stable From Negative

Issuer: Volkswagen Group of America, Inc.

..Affirmations:

.... Backed Commercial Paper (Local Currency), Affirmed P-2

..Outlook Actions:

.... Outlook, No Outlook

Issuer: Volkswagen International Belgium S.A.

.... Commercial Paper (Local Currency), Affirmed P-2

..Outlook Actions:

.... Outlook, No Outlook

Issuer: Volkswagen International Finance N.V.

..Downgrades:

.... Backed Junior Subordinated (Local Currency), Downgraded to Baa3 from Baa2

.... Backed Senior Unsecured Medium-Term Note Program (Local Currency), Downgraded to (P)Baa1 from (P)A3

.... Backed Senior Unsecured (Foreign Currency), Downgraded to Baa1 from A3

.... Backed Senior Unsecured (Local Currency), Downgraded to Baa1 from A3

..Affirmations:

.... Backed Commercial Paper (Local Currency), Affirmed P-2

.... Backed Other Short Term (Local Currency), Affirmed (P)P-2

..Outlook Actions:

....Outlook, Changed To Stable From Negative

Issuer: Volkswagen International Luxemburg S.A

..Affirmations:

.... Backed Commercial Paper (Local Currency), Affirmed P-2

..Outlook Actions:

.... Outlook, No Outlook

Issuer: VW Credit Canada, Inc.

..Downgrades:

.... Backed Senior Unsecured Medium-Term Note Program (Foreign Currency), Downgraded to (P)Baa1 from (P)A3

.... Backed Senior Unsecured (Local Currency), Downgraded to Baa1 from A3

..Affirmations:

.... Backed Commercial Paper (Local Currency), Affirmed P-2

.... Backed Other Short Term (Foreign Currency), Affirmed (P)P-2

..Outlook Actions:

....Outlook, Changed To Stable From Negative

Issuer: VW Credit, Inc.

..Affirmations:

.... Backed Commercial Paper (Local Currency), Affirmed P-2

.... Backed Other Short Term (Foreign Currency), Affirmed (P)P-2

..Outlook Actions:

....Outlook, Changed To Stable From Negative

The principal methodology used in these ratings was Automobile Manufacturers published in May 2021 and available at https://ratings.moodys.com/rmc-documents/72240. Alternatively, please see the Rating Methodologies page on https://ratings.moodys.com for a copy of this methodology.

REGULATORY DISCLOSURES

For further specification of Moody's key rating assumptions and sensitivity analysis, see the sections Methodology Assumptions and Sensitivity to Assumptions in the disclosure form. Moody's Rating Symbols and Definitions can be found on https://ratings.moodys.com/rating-definitions .

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