

## Equity Research

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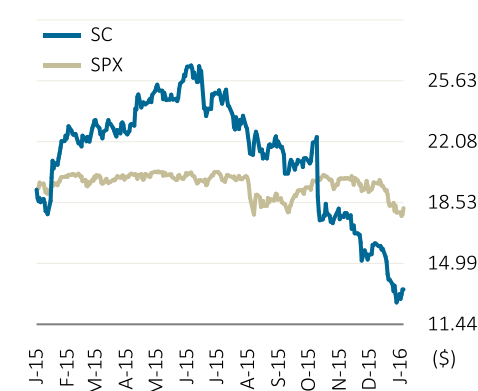
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**SC** **\$13.47**  
12 month target \$21.00

## BUY

52 week range \$12.71 - \$26.52  
Market Cap (m) \$4,800

### Price Performance



Source: IDC

## Financials

## Santander Consumer USA Holdings

### Will SC's 4Q15 Results Help to Begin Reversal of Six-Month Stock Slump? Reducing PT to \$21 (from \$30)

It is probably difficult for many investors in Santander Consumer USA to recall that just over six months ago the company's shares reached an all-time high of \$26.52. Since then, SC has seen its stock lose almost half of its value as its long-time CEO stepped down on July 2, concerns about the resiliency of subprime lending gained traction during 2H15, and the overhang associated with its two-time failure of the Comprehensive Capital Analysis and Review (CCAR) have weighed on it.

- While it may be a coincidence, SC's swoon began nine days before Tom Dundon resigned as the company's CEO and was replaced by Jason Kulas. It was also right around that time that investors began to really focus on their perception that the credit cycle has entered a later stage to the particular detriment of those firms focused on the subprime sector, even though SC's credit metrics had been so solid to that point that some investors had been asking whether auto lending had entered the early stages of a new credit cycle, skipping over the negative effects of the prior one.
- SC delivered a couple of earnings beats during 2H15, but the path was not without bumps that intensified lurking qualms. In particular, the company for 3Q15 reported a net charge-off rate of 14.4%. Even though that figure was 8.7% after adjusting for the lower of cost or market adjustments on loans sold or held for sale, the headline figure fed into the narrative of credit deterioration promoted by SC's detractors.
- Given that it will take some time for SC to overcome such concerns, combined with increased competition in its core business, **we are reducing our price target to \$21 (from \$30) based on 8x our revised FY16E earnings per share of \$2.67.** (Our previous multiple and FY16E EPS were 10x and \$2.98.)
- Valuation:** Our price target of \$21 is based on 8x our 2016E earnings per share of \$2.67.

## Estimates

	1Q14 A	2Q14 A	3Q14 A	4Q14 A	FY14 A	1Q15 A	2Q15 A	3Q15 A	4Q15 E	FY15 E	FY16 E
Net Income (Adj.)	81	246	191	247	767	289	285	224	208	1,007	977
Diluted EPS (Adj.)	0.23	0.69	0.54	0.69	2.15	0.81	0.79	0.62	0.57	2.80	2.67
Operating Income	130	390	282	409	1,210	431	447	353	331	1,561	1,527

Source: BTIG Research Estimates and Company Documents (\$ in millions, except per share amount)

*Please Read: Important disclosures and analyst's certification appear in Appendix*

- ▶ So as SC approaches its 4Q15 report and the recent weakness of the equity market has elevated concerns about the economy, the expectations bar has been lowered. The company is scheduled to report its 4Q15 results on Wednesday, January 27 before the market open with a conference call scheduled for 9am ET on that day. We estimate that SC will report 4Q15 EPS of \$0.57, which is in line with the consensus estimate.

Among the questions that we believe SC management should address during the conference call are the following:

- ▶ Kulas during SC's 3Q15 conference call said the company had recently seen more competition emerge in portions of the subprime market it targets. He added that the company had adopted a more cautious approach to the segment as a result. **Almost three months later, what is management's take on the state of competition in the subprime auto lending market? How has management's more cautious approach impacted its loan origination performance?**
- ▶ SC announced on its 3Q15 conference call that it was in the process of engaging investment banks to assist it in the sale of all of the company's personal lending assets after it announced that it had issued a notice of termination to a peer-to-peer personal lending platform – LendingClub Corporation (LC, Buy, \$21 PT) – would exit that space. **What is the status of SC's effort to engage assistance to divest its personal lending holdings? What is the company's timeframe for the divestiture?**
- ▶ Kulas during the 3Q15 call highlighted SC's serviced for others platform of loans, a category that it has emphasized due to its positive impact on the company's capital efficiency and ROE, which had grown by 13% thanks to \$3.1bn in asset sales during the quarter. **What is SC's outlook for its serviced for other platform? How should investors think about modeling the upside associated with this category?**
- ▶ SC has failed its CCAR test twice for qualitative reasons with a particular focus on internal controls, governance and risk identification. In particular, the Federal Reserve appears to be demanding that the company creates a robust risk management infrastructure. **What is the status of the company's efforts to achieve a CCAR non-objection from the Fed?**
- ▶ Wholesale used vehicle prices as measured by the Manheim Used Vehicle Index improved modestly during 4Q15 with the index reading 125.3 in October, 125.1 in November and 125.7 in December. SC management last year stated that in anticipation of lower used-car recovery values due to lower prices it was using lower recovery assumptions in its models than the actuals. **What is SC management's current thinking on the outlook for the used car market? Asked differently, what is the company currently modeling for depreciation expense on its operating leases as well as remarketing gains going forward?**

- ▶ The average national gasoline price has declined by more than 30% since SC shares achieved their all-time high on June 23. Insofar as the difference between a marginal subprime borrower making or missing a payment can hinge on a relatively small amount of money, the lower price of gas can be a significant factor for lenders. **To what extent does management believe lower gas prices are a mitigant to other factors with regard to its credit metrics?**

## Income Statement

Santander Consumer USA Operating Model \$ millions	Dec-11 2011A	Dec-12 2012A	Dec-13 2013A	Dec-14 2014A	Mar-15 1Q15A	Jun-15 2Q15A	Sep-15 3Q15A	Dec-15 4Q15E	Dec-15 2015E	Mar-16 1Q16E	Jun-16 2Q16E	Sep-16 3Q16E	Dec-16 4Q16E	Dec-16 2016E
<b>Total finance and other interest income</b>	<b>2,594.51</b>	<b>2,948.50</b>	<b>3,934.02</b>	<b>5,569.66</b>	<b>1,570.29</b>	<b>1,683.12</b>	<b>1,733.53</b>	<b>1,741.33</b>	<b>6,728.26</b>	<b>1,697.50</b>	<b>1,788.77</b>	<b>1,853.87</b>	<b>1,868.84</b>	<b>7,208.98</b>
Interest expense	418.53	374.03	408.79	523.20	148.86	150.62	171.42	176.56	647.46	182.74	188.22	193.87	199.69	764.53
Leased vehicle expense	-	-	121.54	740.24	273.06	281.12	296.35	299.32	1,149.85	302.31	300.80	299.29	297.80	1,200.20
<b>Net interest margin</b>	<b>2,175.99</b>	<b>2,574.48</b>	<b>3,403.69</b>	<b>4,306.22</b>	<b>1,148.37</b>	<b>1,251.38</b>	<b>1,265.75</b>	<b>1,265.45</b>	<b>4,930.95</b>	<b>1,212.45</b>	<b>1,299.75</b>	<b>1,360.71</b>	<b>1,371.35</b>	<b>5,244.26</b>
Provision for loan losses	819.22	1,122.45	1,852.97	2,616.66	605.98	738.74	744.14	811.59	2,900.44	785.71	804.96	820.84	877.83	3,289.34
Profit sharing	-	-	78.25	74.93	13.52	21.50	11.82	11.94	58.77	12.29	12.42	12.54	12.67	49.92
<b>Net interest margin after provisions &amp; profit sharing</b>	<b>1,356.77</b>	<b>1,452.02</b>	<b>1,472.48</b>	<b>1,614.64</b>	<b>528.87</b>	<b>491.14</b>	<b>509.80</b>	<b>441.93</b>	<b>1,971.74</b>	<b>414.45</b>	<b>482.38</b>	<b>527.33</b>	<b>480.85</b>	<b>1,905.00</b>
Gain on sale of receivables	-	-	40.69	116.77	21.25	86.67	1.57	25.00	134.48	35.00	35.35	35.70	36.06	142.11
Servicing fee income	251.39	34.14	25.46	72.63	24.80	28.04	35.91	36.63	125.38	40.29	41.30	42.33	43.39	167.31
Fees, commissions and other	201.14	261.55	245.41	368.28	101.13	94.27	93.08	95.87	384.35	98.74	100.72	102.73	104.79	406.99
<b>Total other income</b>	<b>452.53</b>	<b>295.69</b>	<b>311.57</b>	<b>557.67</b>	<b>147.18</b>	<b>208.98</b>	<b>130.55</b>	<b>157.50</b>	<b>644.21</b>	<b>174.04</b>	<b>177.37</b>	<b>180.77</b>	<b>184.24</b>	<b>716.41</b>
Salary and benefit expense	213.69	225.16	305.06	482.64	100.54	110.97	136.29	116.37	464.18	117.54	118.71	119.90	121.10	477.25
Servicing and repossession expense	155.86	136.55	147.54	201.02	58.83	55.47	60.77	61.38	236.44	61.99	62.61	63.24	63.87	251.71
Other operating costs	187.54	197.45	246.36	278.38	86.01	86.99	90.28	90.73	354.01	90.73	91.19	91.64	92.10	365.66
<b>Total costs and expenses</b>	<b>557.08</b>	<b>559.16</b>	<b>698.96</b>	<b>962.04</b>	<b>245.38</b>	<b>253.43</b>	<b>287.34</b>	<b>268.48</b>	<b>1,054.63</b>	<b>270.26</b>	<b>272.51</b>	<b>274.78</b>	<b>277.07</b>	<b>1,094.62</b>
<b>Income before taxes</b>	<b>1,252.21</b>	<b>1,188.55</b>	<b>1,085.09</b>	<b>1,210.27</b>	<b>430.68</b>	<b>446.69</b>	<b>353.01</b>	<b>330.94</b>	<b>1,561.31</b>	<b>318.22</b>	<b>387.23</b>	<b>433.32</b>	<b>388.02</b>	<b>1,526.79</b>
Income taxes	464.03	453.62	389.42	443.64	141.43	161.23	129.11	122.45	554.21	114.56	139.40	155.99	139.69	549.64
<b>Net income</b>	<b>788.18</b>	<b>734.93</b>	<b>695.67</b>	<b>766.63</b>	<b>289.25</b>	<b>285.46</b>	<b>223.90</b>	<b>208.49</b>	<b>1,007.11</b>	<b>203.66</b>	<b>247.83</b>	<b>277.32</b>	<b>248.33</b>	<b>977.15</b>
Noncontrolling interests	(19.98)	(19.93)	1.82	-	-	-	-	-	-	-	-	-	-	-
<b>Net income attributable to Santander Consumer USA</b>	<b>768.20</b>	<b>715.00</b>	<b>697.49</b>	<b>766.63</b>	<b>289.25</b>	<b>285.46</b>	<b>223.90</b>	<b>208.49</b>	<b>1,007.11</b>	<b>203.66</b>	<b>247.83</b>	<b>277.32</b>	<b>248.33</b>	<b>977.15</b>
Change in unrealized gains (losses) on cash flow hedges	(5.68)	7.27	9.56	-	-	-	-	-	-	-	-	-	-	-
Change in unrealized gains (losses) on investments	(6.34)	(4.94)	(3.25)	-	-	-	-	-	-	-	-	-	-	-
<b>Other comprehensive income</b>	<b>(12.02)</b>	<b>2.33</b>	<b>6.31</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>
<b>Comprehensive income</b>	<b>776.16</b>	<b>737.27</b>	<b>701.98</b>	<b>766.63</b>	<b>289.25</b>	<b>285.46</b>	<b>223.90</b>	<b>208.49</b>	<b>1,007.11</b>	<b>203.66</b>	<b>247.83</b>	<b>277.32</b>	<b>248.33</b>	<b>977.15</b>
<b>Earnings per share</b>	<b>\$3.13</b>	<b>\$2.07</b>	<b>\$2.01</b>	<b>\$2.15</b>	<b>\$0.81</b>	<b>\$0.79</b>	<b>\$0.62</b>	<b>\$0.57</b>	<b>\$2.80</b>	<b>\$0.56</b>	<b>\$0.68</b>	<b>\$0.76</b>	<b>\$0.68</b>	<b>\$2.67</b>
<b>Dividends per share</b>	<b>\$0.00</b>	<b>\$0.00</b>	<b>\$0.84</b>	<b>\$0.30</b>	<b>\$0.00</b>	<b>\$0.00</b>	<b>\$0.00</b>	<b>\$0.00</b>	<b>\$0.00</b>	<b>\$0.00</b>	<b>\$0.00</b>	<b>\$0.00</b>	<b>\$0.00</b>	<b>\$0.00</b>
<b>Shares outstanding</b>	<b>245.78</b>	<b>346.16</b>	<b>346.18</b>	<b>355.86</b>	<b>356.65</b>	<b>359.19</b>	<b>362.22</b>	<b>363.22</b>	<b>360.32</b>	<b>361.82</b>	<b>363.32</b>	<b>364.82</b>	<b>366.32</b>	<b>366.32</b>

Source: BTIG Research Estimates and Company Documents

## Appendix: Analyst Certification and Other Important Disclosures

### Analyst Certification

I, Mark Palmer, hereby certify that the views about the companies and securities discussed in this report are accurately expressed and that I have not received and will not receive direct or indirect compensation in exchange for expressing specific recommendations or views in this report.

I, Giuliano Bologna, hereby certify that the views about the companies and securities discussed in this report are accurately expressed and that I have not received and will not receive direct or indirect compensation in exchange for expressing specific recommendations or views in this report.

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**SELL** – A stock that is expected at initiation to produce a negative total return of 15% or greater over the next 12 months following the initial recommendation. The SELL rating may be maintained following initiation as long as it is deemed appropriate, notwithstanding price fluctuations that would cause the target to fall outside of the 15% return.

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### Company Valuation and Risk Disclosures

#### Santander Consumer USA Holdings (SC, Buy)

**Valuation:** Our price target of \$21 is based on 8x our 2016E earnings per share of \$2.67

**Risks:** Primary risks to our recommendation include reduced access to funding; higher-than-expected default rates, particularly on nonprime receivables; poor portfolio performance that triggers credit enhancement provisions on the company's revolving credit facilities or secured structured financings; inability to meet certain milestones and metrics that could result in the termination of the company's agreement with Chrysler; adverse changes in interest rates; adverse economic conditions; and regulatory risks.

### Santander Consumer USA Holdings (SC)



*Note: Closing Price and Target Price have been adjusted for corporate actions.*

Date	Closing Price (\$)	Target Price (\$)	Analyst	Rating
22-Jan-14	25.25	31	Mark Palmer	Buy
04-Nov-14	17.29	26	Mark Palmer	Buy
28-Apr-15	24	28	Mark Palmer	Buy
30-Jul-15	24.18	30	Mark Palmer	Buy

### LendingClub Corporation (LC, Buy)

**Valuation:** Our price target of \$21 for LC is based on 18x the company's FY19E adjusted EBITDA of \$549 discounted back at 10%.

**Risks:** Increase in defaults on loans facilitated through LC's marketplace could negatively impact return on investment for investors in those loans, which could result in a decline in investment in the marketplace. Additionally, changes in the regulatory environment surrounding peer to peer loans could negatively impact Lending Club's ability to originate new peer to peer loans.

## LendingClub Corporation (LC)



*Note: Closing Price and Target Price have been adjusted for corporate actions.*

Date	Closing Price (\$)	Target Price (\$)	Analyst	Rating
11-Dec-14	23.43	19	Mark Palmer	Buy
15-Dec-14	24.97	31	Mark Palmer	Buy
29-Oct-15	14.18	21	Mark Palmer	Buy

## Company-Specific Regulatory Disclosures

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Additional Information Available Upon Request

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