

## Equity Research

October 29, 2015

### Mark Palmer

(212) 588-6582  
mpalmer@btig.com

### Giuliano Bologna

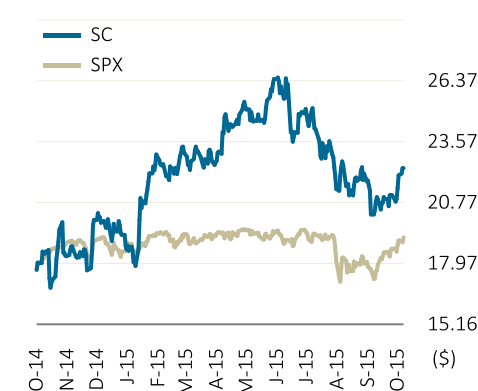
(212) 588-6583  
gbologna@btig.com

**SC** **\$22.35**  
12 month target \$30.00

## BUY

52 week range \$16.85 - \$26.52  
Market Cap (m) \$7,965

### Price Performance



Source: IDC

## Financials

### Santander Consumer USA Holdings

#### Noisy 3Q15 Earnings Beat as SC Exits Personal Lending Space to Focus on Core Auto Lending Business

The 3Q15 earnings beat that Santander Consumer USA (SC) posted this morning was aided by a refinement in the company's loan-loss provision model that reduced the impact of seasonality and resulted in a one-time, \$134mm reduction in provision and higher earnings for the quarter. That change also should remove from 4Q15 the seasonal provision benefit that SC typically experiences during the fourth quarter. Adding back the \$134mm provision adjustment would result in a 3Q15 provision of \$878mm, higher than our estimate of \$828mm.

- The adjustments required to understand how SC actually performed during 3Q15 didn't end with provisions. The company also reported a net charge-off ratio of 14.4%, up 9.1% sequentially and 6% year-over-year. However, that figure was elevated by a non-recurring lower of cost or market adjustment on loans sold and held for sale. On an adjusted basis, SC's net charge-off ratio during the quarter was 8.7%, which while still higher both sequentially and versus the prior year period was relatively benign given the expectation, based on historical patterns, that the company's credit performance will seasonally weaken during 2H15.
- Meanwhile, in the first significant shift in SC's direction under CEO Jason Kulas, who was appointed chief executive on July 2 following the resignation of Tom Dundon, the company announced that it would exit the personal lending space and focus on its core auto-lending business. As such, SC designated its personal lending portfolio as held for sale. Kulas explained the decision during the 3Q15 conference call as part of an effort by management to "get back to basics."
- **We are reiterating our Buy recommendation on SC and price target of \$30** based on 10x our 2016E earnings per share of \$2.98. We are *(continued on page 2)*
- **Valuation:** Our price target of \$30 for SC is based on 10x our 2016E earnings per share of \$2.98.

## 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	226	1,024	1,091
Diluted EPS (Adj.)	0.23	0.69	0.54	0.69	2.15	0.81	0.79	0.62	0.62	2.84	2.98
Operating Income	130	390	282	409	1,210	431	447	353	358	1,588	1,704

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

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

*(continued from page 1)*

also reducing our estimate of SC's 4Q15 earnings per share to \$0.62 (from \$0.64) based on our increased estimate of the company's 4Q15 provision to \$798mm (from \$784mm) to reflect the shift created by the change to its provision model. Despite a noisy 3Q15, we believe SC remains well positioned for sustained profitable growth.

- ▶ SC reported 3Q15 adjusted EPS of \$0.62 versus the consensus estimate of \$0.53 and our estimate of \$0.54. Despite the headline beat, the 3Q15 report had the feeling of a delayed "kitchen sink" quarter for Kulas as CEO as the company not only changed its provision accounting to remove volatility and moved to focus the company on its core business, but also announced an expected increase in its cost of debt in 2016.
- ▶ The increased funding costs would be driven by issuance of unsecured debt as well as contingent liquidity committed by its holding company. The latter change is aimed at aligning SC's liquidity risk management practices with regulators' expectations of bank holding companies, which appears to be part of its ongoing effort to receive a Comprehensive Capital Analysis and Review (CCAR) non-objection from the Federal Reserve after the company twice failed the CCAR test for qualitative reasons.
- ▶ SC reported loan originations of \$7.6bn during 3Q15, which was flat on a sequential basis. Kulas noted during the conference call that the company has recently seen an increase in competition in the market. At the same time, SC's serviced for others portfolio of loans it originated and sold – an approach aimed at achieving both increased capital efficiency and a higher ROE – increased 13% versus the prior quarter due to \$3.1bn in asset sales during the quarter.

## Income Statement

Santander Consumer USA Operating Model	Dec-11	Dec-12	Dec-13	Dec-14	Mar-15	Jun-15	Sep-15	Dec-15	Dec-15	Mar-16	Jun-16	Sep-16	Dec-16	Dec-16
\$ millions	2011A	2012A	2013A	2014A	1Q15A	2Q15A	3Q15A	4Q15E	2015E	1Q16E	2Q16E	3Q16E	4Q16E	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>1,754.85</b>	<b>6,741.79</b>	<b>1,705.20</b>	<b>1,811.14</b>	<b>1,888.72</b>	<b>1,928.31</b>	<b>7,333.36</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>1,278.98</b>	<b>4,944.48</b>	<b>1,220.15</b>	<b>1,322.11</b>	<b>1,395.55</b>	<b>1,430.82</b>	<b>5,368.64</b>
Provision for loan losses	819.22	1,122.45	1,852.97	2,616.66	605.98	738.74	744.14	798.06	2,886.92	775.42	800.72	821.60	838.82	3,236.56
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>468.98</b>	<b>1,998.79</b>	<b>432.43</b>	<b>508.97</b>	<b>561.42</b>	<b>579.34</b>	<b>2,082.16</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>357.99</b>	<b>1,588.37</b>	<b>336.20</b>	<b>413.83</b>	<b>467.40</b>	<b>486.51</b>	<b>1,703.94</b>
Income taxes	464.03	453.62	389.42	443.64	141.43	161.23	129.11	132.46	564.22	121.03	148.98	168.27	175.14	613.42
<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>225.53</b>	<b>1,024.15</b>	<b>215.17</b>	<b>264.85</b>	<b>299.14</b>	<b>311.36</b>	<b>1,090.52</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>225.53</b>	<b>1,024.15</b>	<b>215.17</b>	<b>264.85</b>	<b>299.14</b>	<b>311.36</b>	<b>1,090.52</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>225.53</b>	<b>1,024.15</b>	<b>215.17</b>	<b>264.85</b>	<b>299.14</b>	<b>311.36</b>	<b>1,090.52</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>\$0.62</b>	<b>\$2.84</b>	<b>\$0.59</b>	<b>\$0.73</b>	<b>\$0.82</b>	<b>\$0.85</b>	<b>\$2.98</b>
<b>Dividends per share</b>			<b>\$0.84</b>	<b>\$0.30</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.

### Regulatory Disclosures

#### Analyst Stock Ratings Definitions

**BTIG LLC's ("BTIG") ratings, effective May 10, 2010, are defined as follows:**

**BUY** – A stock that is expected at initiation to produce a positive total return of 15% or greater over the 12 months following the initial recommendation. The BUY 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.

**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.

**NEUTRAL** – A stock that is not expected to appreciate or depreciate meaningfully over the next 12 months.

**NOT RATED** – A stock that is not rated but that is covered by BTIG.

#### Distribution of Ratings and Investment Banking Clients

BTIG must disclose in each research report the percentage of all securities rated by the member to which the member would assign a "buy", "neutral" or "sell" rating. The said ratings are updated on a quarterly basis. BTIG must also disclose the percentage of subject companies within each of these three categories for whom the member has provided investment banking services within the previous twelve months. **Stocks under coverage as of the end of the most recent calendar quarter (September 30, 2015): 175**

**Distribution of BTIG's Research Recommendations (as of September 30, 2015):**

**BUY: 66.3% NEUTRAL: 30.3% SELL: 3.4%**

**Distribution of BTIG's Investment Banking Services (as of September 30, 2015):**

**BUY: 88% NEUTRAL: 6% SELL: 6%**

For purposes of FINRA ratings distribution rules, BTIG's stock ratings of Buy, Neutral and Sell fall into Buy, Hold and Sell categories, respectively.

### Company Valuation and Risk Disclosures

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

**Valuation:** Our price target of \$30 is based on 10x our 2016E earnings per share of \$2.98

**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

## Other Disclosures

Additional Information Available Upon Request

### General Disclosures

Research reports produced by BTIG LLC ("BTIG") are published for and intended to be distributed solely to BTIG institutional and corporate clients. Recipients of BTIG reports will not be considered clients of BTIG solely because they may have received such BTIG report.

The equity research analyst(s) responsible for the preparation of this report receives compensation based upon a variety of factors, including the quality and accuracy of research, internal/client feedback, and overall Firm revenues.

BTIG reports are based on public information and BTIG considers the same to be reliable, comprehensive information, but makes no representation or warranty that the reports are accurate or complete. BTIG opinions and information provided in this report are as of the date of the report and may change without notice.

This research report is not an offer to buy or sell or solicitation of an offer to buy or sell any security in any jurisdiction where such an offer or solicitation would be illegal. This research report was not drafted specifically for any particular individual or entity and is not a personal recommendation to participate in any particular trading strategy or transaction. Any recipient of this research report should obtain independent advice specific to their personal circumstances before undertaking any investment activity and must make their own independent evaluation of any securities or financial instruments.

Facts, views or opinions presented in this report have not been reviewed by, and may not reflect information known to, employees or other professionals in the "BTIG Group" (BTIG Group includes, but is not limited to, BTIG and its parents, subsidiaries and/or affiliates). BTIG Group employees, including Sales Representatives and Traders, may provide oral or written commentary or advice that may be inconsistent with the opinions and/or views expressed in this research report. BTIG Group employees and/or its affiliates not involved in the preparation of this research report may have investments in securities or derivatives of securities of companies mentioned in this report that are inconsistent with the views discussed in this report.

Investors in securities products bear certain risks in conjunction with those investments. The value of, and income from, any investments may vary because of changes in interest rates or foreign exchange rates, securities prices or market indexes, operational or financial conditions of companies or other factors within or beyond the companies control. Recipient of the research reports should be aware that investments in equity securities may pose significant risks due to the inherent uncertainty associated with relying on forecasts of various factors that can affect the earnings, cash flow and overall valuation of a company. Any investment in equity securities should be undertaken only upon consideration of issues relating to the recipient's overall investment portfolio and objectives (such as diversification by asset class, industry or company) as well as time horizon and liquidity needs. Further, past performance should not be taken as an indication or guarantee of future performance, and no representation or warranty, express or implied, is made regarding future performance. There may be time limitations on the exercise of options or other rights in any securities transactions.

Investing in foreign markets and securities, including ADRs, is subject to additional risks such as currency fluctuation, limited information, political instability, economic risk, and the potential for illiquid markets. Investing in emerging markets may accentuate these risks. Non-U.S. reporting issuers of foreign securities, however, may not make regular or complete public disclosure relating to their financial condition or the securities that they issue.

The trademarks and service marks contained herein are the property of their respective owners. Third-party data providers make no warranties or representations of any kind relating to the accuracy, completeness, or timeliness of the data they provide and shall not have liability of any damages of any kind relating to such data. The report or any portion hereof may not be reprinted, sold or redistributed without the written consent of BTIG. This report is intended only for use by the recipient. The recipient acknowledges that all research and analysis in this report are the property of BTIG and agrees to limit the use of all publications received from BTIG within his, or her or its, own company or organization. No rights are given for passing on, transmitting, re transmitting or reselling the information provided.

## **Jurisdiction and Dissemination**

BTIG is a U.S. broker-dealer and member of FINRA and SIPC.

BTIG Australia Limited ACN 128 554 601, member of ASIC and ASX; BTIG Hong Kong Limited, an Exchange Participant of SEHK and licensed and regulated by the SFC; BTIG Ltd, member of the LSE, authorized and regulated by the FSA; and BTIG Singapore Pte Ltd, registered and licensed with MAS; are all separate but affiliated entities of BTIG. Unless governing law permits otherwise, you must contact a BTIG entity in your home jurisdiction for further information, or if you want to use our services in effecting a transaction.

Issues and approved for distribution in the UK and EEA by BTIG Ltd. to eligible counterparties and professional clients only. Issued and distributed in Australia to "wholesale clients" only by BTIG Australia Limited. In Singapore and Hong Kong, further information may be obtained from BTIG Singapore Pte Ltd and BTIG Hong Kong Limited, respectively.