de Volksbank N.V.

Key Rating Drivers

Sound Metrics, Concentrated Franchise: The ratings of de Volksbank N.V. reflect its sound asset quality and moderate risk appetite, with a focus on low-risk residential mortgage lending, high risk-weighted capital ratios and sound leverage. The bank's undiversified business model and its franchise lacking the breadth of the larger Dutch banks are rating weaknesses.

Resilient Asset Quality: The bank's asset quality is mainly driven by a large and low-risk residential mortgage loan portfolio. Fitch Ratings expects asset quality will remain largely unaffected by the pandemic and the bank's impaired loans/gross loans ratio should stay below 1.5% in 2021. We do not expect de Volksbank to deviate from its narrow but fairly low-risk business model or to materially increase its risk appetite.

Structural Profitability Challenges Persist: The bank's revenues were eroding even before the coronavirus pandemic due to a lack of diversification and intense competition in mortgage lending, which is virtually the bank's only product. We expect these revenue challenges will persist in the next few years and believe 2021 results will be lower than in the previous year. This is because the decrease in loan impairment charges will likely not fully offset increasing operating and regulatory costs.

Strong Capital Ratios and Leverage: The bank's risk-weighted capital ratios are very strong and compare well with peers'. The bank's common equity Tier 1 (CET1) ratio of 31.2% at end-2020 provides strong buffers above the revised regulatory requirements and will allow the bank to withstand asset quality deterioration.

Manageable Capital Requirement Inflation: The bank's capital ratios greatly benefit from the low risk-weighting of mortgage loans, but remain robust when accounting for the expected inflation of risk-weighted assets (RWAs) from Basel III end-game rules. Factoring in 30% inflation in RWAs from end-2020 levels, the pro-forma CET1 ratio would be about 24%, still well above the bank's target of at least 19%.

Granular Funding, Sound Liquidity: Stable household and SME deposits form the bulk of de Volksbank's funding. Wholesale funding is limited and the bank is a less frequent issuer in debt capital markets than its larger Dutch peers. Liquidity has remained strong since the onset of the pandemic and its buffer of liquid asset comfortably covers upcoming wholesale funding maturities.

Rating Sensitivities

Stable Outlook: The ratings have sufficient headroom to absorb significant shocks under our updated assessment of various downside scenarios to our baseline economic forecast. This primarily reflects our assessment of the bank's asset quality (a-/stable) and capitalisation (a-/stable). We expect de Volksbank's robust capital buffers would uphold the bank's current ratings even in a downside scenario.

Severe Economic Stress: The bank's ratings could be downgraded if the pandemic places severe and sustained pressure on the bank's asset quality, earnings and capitalisation. This could be due to a materially weaker economic recovery in the Netherlands than Fitch forecasts together with a substantial fall in property prices and a sustained rise in unemployment.

Ratings

de Volksbank N.V.	
Long-Term IDR	A-
Short-Term IDR	F1
Derivative Counterparty Rating	A(dcr)
Viability Rating	a-
Support Rating	5
Support Rating Floor	NF
Sovereign Risk	
Long-Term Foreign and Local-Currency IDRs	AAA
Country Ceiling	AAA

Outlooks

Long-Term Foreign-Currency IDR	Stable
Sovereign Long-Term Foreign- and Local-Currency IDRs	Stable

Applicable Criteria

Bank Rating Criteria (February 2020)

Related Research

Global Economic Outlook – June 2021 (June 2021)

Benelux Banks: Recovery to Pre-Pandemic Profitability Levels Unlikely Before 2022 (April 2021)

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Debt Rating Classes

Rating level	Rating
Deposits	A/F1
Senior preferred	A/F1
Senior non-preferred	A-
Tier 2 subordinated debt	BBB

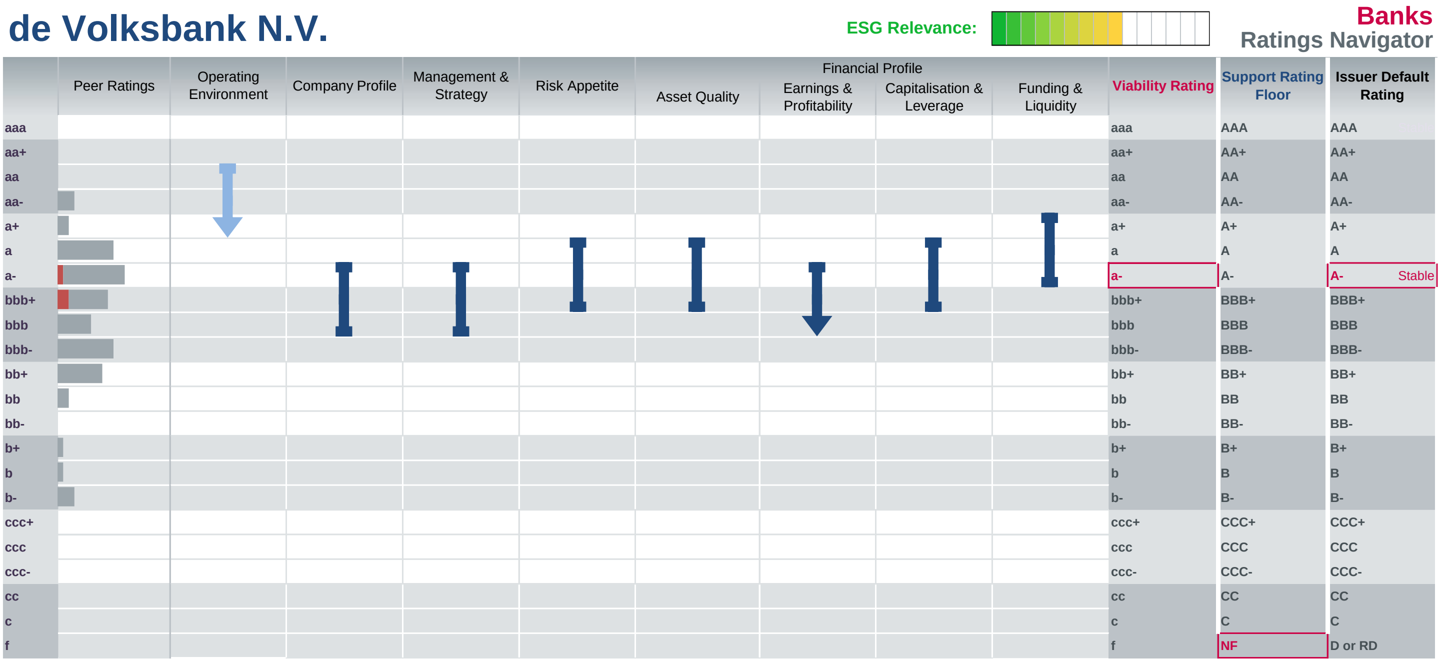
Source: Fitch Ratings

The bank's long-term senior preferred debt and deposit ratings are one notch above its Long-Term Issuer Default Rating (IDR), reflecting Fitch's expectation that the bank will meet its resolution buffer requirement only with senior non-preferred (SNP) and junior debt and equity instruments. This also drives the equalisation of de Volksbank's long-term senior non-preferred debt with the bank's Long-Term IDR.

The bank's short-term senior preferred debt and deposit ratings are mapped to their respective long-term ratings and also reflect our assessment of the bank's funding and liquidity at 'a'.

The bank's subordinated debt is rated two notches below its Viability Rating, reflecting the higher-than-average loss severity of this type of debt. Fitch does not apply additional notching for incremental non-performance risk relative to the VR given that any loss absorption would only occur once the bank reaches the point of non-viability.

Ratings Navigator



Significant Changes

Negative Rates Charged on Customer Deposits

de Volksbank will charge negative interest rates on retail customer deposits above EUR100,000 from July 2021. The bank had already introduced negative rates on retail accounts over EUR250,000 in March 2021 and has been selectively charging business customers since 3Q20. The positive earnings impact from negative rates on liabilities was negligible in 2020 but may become material as negative rates are levied on a larger share of deposits.

Similar to Dutch and Belgian banking peers, de Volksbank is trying to limit the negative impact on its net interest income from maintaining non-remunerated customer accounts while banks' deposits with central banks and highest quality assets pay negative interest rates. The bank is more sensitive to pressure from negative interest rates as net interest income represents about 90% of its revenues, making deposit pricing a critical issue for the bank. It has not experienced large deposit outflows after it took these measures.

Bar Chart Legend

Vertical bars – VR range of Rating Factor

Bar Colors – Influence on final VR

- Higher influence
- Moderate influence
- Lower influence

Bar Arrows – Rating Factor Outlook

⇧	Positive	⇩	Negative
⇳	Evolving	▫	Stable

Company Summary and Key Qualitative Assessment Factors

Domestic Retail Banking Business Model

The bank operates four separate brands under a single banking licence: SNS, RegioBank, BLG Wonen and ASN Bank. The four brands serve about 3.3 million customers and have strong social recognition.

The bank's market share in the mortgage market (6.2% at end-2020) has eroded in recent years. Historically low rates have encouraged borrowers to favour loans with long fixed-rate periods, which are particularly attractive assets for insurance companies that need to match the long tenor of their policies. These structures are less favourable for de Volksbank due to higher interest rate risk.

Delayed Privatisation, Management Turnover

The bank's monoline business profile and depressed valuations across the European banking sector have so far discouraged the efforts of its state-owned shareholder to privatise the bank. We expect the pandemic to defer privatisation further.

de Volksbank's management team has a good degree of depth and experience but the bank had increased turnover among top executives starting 2018, which we believe may affect strategic execution. The bank has appointed an interim chief financial officer in April 2021 as the position had been vacant since 3Q20 and in 1Q21, the chairman of its supervisory board announced that he would step down ahead of the end of his term.

Underwriting Consistent with Industry Standards

We view the bank's underwriting standards for residential mortgage loans as prudent and consistent with industry standards. Dutch mortgage lending is mainly prime and owner-occupied, with a very limited buy-to-let segment due to a small and inflexible private rental market. The bank's mortgage lending has been conducted at high loan-to-value (LTV) ratios by international standards, as at its Dutch peers, and driven by past tax incentives to borrow. Regulatory changes adopted since 2011 have reduced the LTV cap at loan origination to 100%, which is still high, and require new mortgage loans to be fully amortising for interest expenses to be tax-deductible.

Loans with high LTVs and interest-only structures will remain a feature of Dutch banks' loan portfolios in the foreseeable future given the long maturity of the asset class. Fully interest-only loans made up about a fifth of de Volksbank's mortgage loans at end-2020. Fitch believes mortgage lending risks are mitigated by Dutch banks' focus on debt affordability, including under-stressed interest rates. The use of centralised credit bureau data and fraud registers is widespread. The legal system is creditor-friendly and banks have full recourse to the borrowers.

Moderate Interest Rate Risk Exposure

The bank's exposure to market risk is moderate. It is mainly affected by structural interest rate risk arising from its portfolio of mortgage loans with fixed-rate periods of longer than one year. These represent nearly 95% of the bank's mortgage loan book. The bank calculates that a 100bp parallel downward shift in the yield curve would cause a EUR55million decrease in trailing 12-month net interest income at end-2020.

Credit spread risk in de Volksbank's securities portfolio is low and underpinned by the high quality of its investments. Nearly all of its investment portfolio consists in bonds issued by sovereign governments of core European countries and financial institutions with a credit rating of 'A' or above.

Summary Financials and Key Ratios

	31 Dec 20		31 Dec 19	31 Dec 18	31 Dec 17
	Year end (USDm) Audited - unqualified	Year end (EURm) Audited - unqualified	Year end (EURm) Audited - unqualified	Year end (EURm) Audited - unqualified	Year end (EURm) Audited - unqualified
Summary income statement					
Net interest and dividend income	1,034	850	875	908	929
Net fees and commissions	56	46	51	44	49
Other operating income	33	27	3	6	50
Total operating income	1,123	923	929	958	1,028
Operating costs	793	652	574	609	603
Pre-impairment operating profit	330	271	355	349	425
Loan and other impairment charges	46	38	-7	-12	-24
Operating profit	283	233	362	361	449
Other non-operating items (net)	n.a.	n.a.	n.a.	n.a.	n.a.
Tax	72	59	87	93	120
Net income	212	174	275	268	329
Other comprehensive income	7	6	2	-7	-41
Fitch comprehensive income	219	180	277	261	288
Summary balance sheet					
Assets					
Gross loans	61,691	50,708	50,580	50,662	49,471
- Of which impaired	825	678	645	657	415
Loan loss allowances	202	166	119	126	149
Net loans	61,489	50,542	50,461	50,536	49,322
Interbank	6,724	5,527	3,368	3,185	2,226
Derivatives	1,051	864	718	732	1,075
Other securities and earning assets	6,220	5,113	5,350	4,782	5,117
Total earning assets	75,485	62,046	59,897	59,235	57,740
Cash and due from banks	6,247	5,135	2,449	1,219	2,574
Other assets	369	303	495	494	578
Total assets	82,101	67,484	62,841	60,948	60,892
Liabilities					
Customer deposits	64,580	53,082	48,142	47,265	45,848
Interbank and other short-term funding	1,442	1,185	830	1,307	3,118
Other long-term funding	8,454	6,949	8,022	7,085	5,968
Trading liabilities and derivatives	2,632	2,163	1,841	1,120	1,252
Total funding	77,107	63,379	58,835	56,777	56,186
Other liabilities	797	655	571	600	992
Preference shares and hybrid capital	n.a.	n.a.	n.a.	n.a.	n.a.
Total equity	4,197	3,450	3,435	3,571	3,714
Total liabilities and equity	82,101	67,484	62,841	60,948	60,892
Exchange rate		USD1 = EUR0.821963	USD1 = EUR0.89015	USD1 = EUR0.873057	USD1 = EUR0.83382

Source: Fitch Ratings, Fitch Solutions, de Volksbank

Summary Financials and Key Ratios

	31 Dec 20	31 Dec 19	31 Dec 18	31 Dec 17
Ratios (annualised as appropriate)				
Profitability				
Operating profit/risk-weighted assets	2.3	3.7	3.9	4.6
Net interest income/average earning assets	1.4	1.5	1.6	1.6
Non-interest expense/gross revenue	70.6	61.8	63.6	58.7
Net income/average equity	5.1	7.8	7.5	9.1
Asset quality				
Impaired loans ratio	1.3	1.3	1.3	0.8
Growth in gross loans	0.3	-0.2	2.4	1.4
Loan loss allowances/impaired loans	24.5	18.5	19.2	35.9
Loan impairment charges/average gross loans	0.1	0.0	0.0	-0.1
Capitalisation				
Common equity Tier 1 ratio	31.2	32.6	35.5	34.1
Fully loaded common equity Tier 1 ratio	n.a.	n.a.	35.5	34.3
Tangible common equity/tangible assets	5.1	5.5	5.9	6.1
Basel leverage ratio	5.2	5.1	5.5	5.5
Net impaired loans/common equity Tier 1	15.9	16.7	16.0	8.0
Funding and liquidity				
Loans/customer deposits	95.5	105.1	107.2	107.9
Liquidity coverage ratio	233.0	182.0	177.0	177.0
Customer deposits/funding	86.7	84.5	84.9	83.5
Net stable funding ratio	n.a.	n.a.	n.a.	n.a.

Source: Fitch Ratings, Fitch Solutions, de Volksbank

Key Financial Metrics – Latest Developments

Resilient Asset Quality

The bank's asset quality metrics compare well with similarly rated peers due to its product concentration in residential mortgage lending in a stable economy. We expect the impact of the pandemic will be more visible by end-2021 but the bank entered the economic downturn with sound asset quality, which we expect to hold up in a more challenging operating environment.

de Volksbank's impaired loans/gross loans ratio remained broadly stable at 1.3% at end-2020 and the increase in the bank's early arrears was limited. Stage 2 loans were 5.5% of gross loans and increased slightly from end-2019 as the bank reclassified some of its performing interest-only loans as Stage 2.

The bank's low coverage of impaired loans by loan-loss allowances equalled about 12% on average for defaulted exposures at end-2020. The bank's expectation of high recoveries can be explained by the national mortgage guarantee scheme, swift collateral repossession, and full recourse to the borrower in the Netherlands. Credit losses will decrease in 2021 and will comfortably remain below European averages due to resilience of the mortgage loan book.

The bank has increased portfolio monitoring during the pandemic and has sought to support its more vulnerable borrowers. However, only few debtors have taken advantage of Covid-19-related payment deferrals. At end-2020, the bank had granted payment deferrals on less than 1% of its loan portfolio. Payment behaviour on expiry has been largely positive.

High Interest Income Reliance Penalising in Low Rate Environment

de Volksbank has healthy operating profitability considering its business model concentration. With the exception of 2020, the bank has consistently delivered a return on equity near or above its 8% target over the past years, offsetting margin pressures with cost cutting. However, the bank's weak income diversification and high reliance on net interest income are rating weaknesses. The bank's modest drawings of targeted long-term refinancing operations have a negligible impact on its net interest income.

We expect the bank's profitability will be increasingly challenged in the medium to long term due to low interest rates, intense competition in mortgage lending and reduced opportunities for cost-cutting.

Sound Capitalisation

At end-2020, de Volksbank had a comfortable buffer above its Tier 1 capital requirement of 19.8pp of RWAs, or EUR2.0 billion, which it met entirely using CET1 capital. The bank's use of internal models to gauge credit risk exposes it to RWA inflation from the finalisation of the Basel III capital framework. The bank estimates that these regulatory changes would lower its CET1 ratio by about 7pp from a very high 31.2% at end-2020. This negative impact will be gradual and phased-in from 2023 to 2028.

We view the bank's capital planning as conservative as it targets a CET1 ratio of at least 19% and a minimum leverage ratio of 4.5%. We expect dividends will resume at the higher end of the bank's pay-out range of 40%–60% of net profits in coming years, considering the bank's sizeable buffer above regulatory requirements.

de Volksbank will need to meet a minimum requirement for own funds and eligible liabilities (MREL) equating to 8% of its total liabilities and own funds by 2024, which it intends on doing entirely with CET1 capital, subordinated-and SNP debt. The bank issued its first SNP bond of EUR500 million in 1Q21 towards this objective and will need to issue an additional EUR1 billion–1.5 billion over 2021–2023, which we consider is manageable.

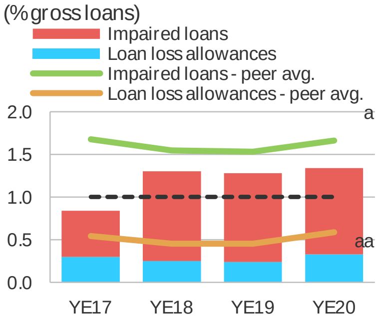
Stable Deposit Funding, Sound Liquidity

de Volksbank mainly funds its operations with retail customer deposits (85% of total funding at end-2020) and these have remained stable despite the introduction of negative rates above certain thresholds. Reliance on wholesale funding is low and mainly consists of covered bonds and senior preferred debt. In the future the bank will mainly issue SNP debt to observe its MREL requirement. The bank maintains a large buffer of high-quality liquid assets, which was about EUR6.4 billion at end-2020 and comfortably covered short- and medium-term funding.

Note on Charts:

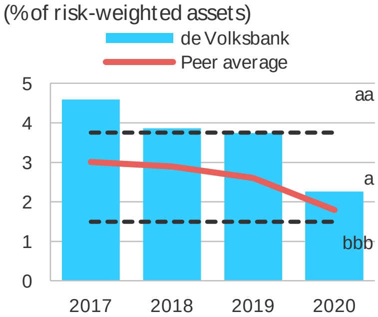
Black dashed lines in the charts represent indicative quantitative ranges and corresponding implied scores for Fitch's core financial metrics for banks operating in the environments that Fitch scores in the 'aa' category.
Peer average includes de Volksbank N.V. (VR: 'a-'), Realkredit Danmark A/S (a), Nykredit Realkredit A/S (a), Cooperatieve Rabobank U.A. (a+), Landshypotek Bank AB (a), Leeds Building Society (a-), Skipton Building Society (a-), ING Groep N.V. (a+) and ABN AMRO Bank N.V. (a)

Asset Quality
(% gross loans)



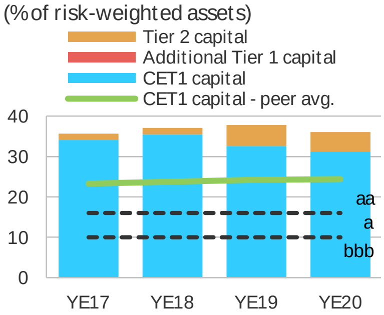
Source: Fitch Ratings, banks

Operating Profit
(% of risk-weighted assets)



Source: Fitch Ratings, banks

Regulatory Capital
(% of risk-weighted assets)



Source: Fitch Ratings, banks

Sovereign Support Assessment

Support Rating Floor	Value
Typical D-SIB SRF for sovereign's rating level (assuming high propensity)	A or A-
Actual country D-SIB SRF	NF
Support Rating Floor:	**NF**

Support Factors	Positive	Neutral	Negative
Sovereign ability to support system			
Size of banking system relative to economy			✓
Size of potential problem	✓		
Structure of banking system			✓
Liability structure of banking system		✓	
Sovereign financial flexibility (for rating level)		✓	
Sovereign propensity to support system			
Resolution legislation with senior debt bail-in			✓
Track record of banking sector support		✓	
Government statements of support			✓
Sovereign propensity to support bank			
Systemic importance		✓	
Liability structure of bank		✓	
Ownership		✓	
Specifics of bank failure		✓	
Policy banks			
Policy role			
Funding guarantees and legal status			
Government ownership			

The Support Rating of '5' and Support Rating Floor of 'No Floor' reflect Fitch's view that senior creditors cannot rely on receiving full extraordinary support from the sovereign if de Volksbank becomes non-viable. The EU's Bank Recovery and Resolution Directive and the Single Resolution Mechanism for eurozone banks provide a framework for resolving banks that is likely to require senior creditors participating in losses, if necessary, instead of or ahead of a bank receiving sovereign support.

Environmental, Social and Governance Considerations

FitchRatings **de Volksbank N.V.**

Banks
Ratings Navigator

Credit-Relevant ESG Derivation

de Volksbank N.V. has 5 ESG potential rating drivers

- de Volksbank N.V. has exposure to compliance risks including fair lending practices, mis-selling, repossession/foreclosure practices, consumer data protection (data security) but this has very low impact on the rating.
- Governance is minimally relevant to the rating and is not currently a driver.

			Overall ESG Scale
key driver	0	issues	5
driver	0	issues	4
potential driver	5	issues	3
not a rating driver	4	issues	2
	5	issues	1

Environmental (E)

General Issues	E Score	Sector-Specific Issues	Reference	E Scale
GHG Emissions & Air Quality	1	n.a.	n.a.	5
Energy Management	1	n.a.	n.a.	4
Water & Wastewater Management	1	n.a.	n.a.	3
Waste & Hazardous Materials Management; Ecological Impacts	1	n.a.	n.a.	2
Exposure to Environmental Impacts	2	Impact of extreme weather events on assets and/or operations and corresponding risk appetite & management; catastrophe risk; credit concentrations	Company Profile; Management & Strategy; Risk Appetite; Asset Quality	1

Social (S)

General Issues	S Score	Sector-Specific Issues	Reference	S Scale
Human Rights, Community Relations, Access & Affordability	2	Services for underbanked and underserved communities: SME and community development programs; financial literacy programs	Company Profile; Management & Strategy; Risk Appetite	5
Customer Welfare - Fair Messaging, Privacy & Data Security	3	Compliance risks including fair lending practices, mis-selling, repossession/foreclosure practices, consumer data protection (data security)	Operating Environment; Company Profile; Management & Strategy; Risk Appetite	4
Labor Relations & Practices	2	Impact of labor negotiations, including board/employee compensation and composition	Company Profile; Management & Strategy	3
Employee Wellbeing	1	n.a.	n.a.	2
Exposure to Social Impacts	2	Shift in social or consumer preferences as a result of an institution's social positions, or social and/or political disapproval of core banking practices	Company Profile; Financial Profile	1

Governance (G)

General Issues	G Score	Sector-Specific Issues	Reference	G Scale
Management Strategy	3	Operational implementation of strategy	Management & Strategy	5
Governance Structure	3	Board independence and effectiveness; ownership concentration; protection of creditor/stakeholder rights; legal /compliance risks; business continuity; key person risk; related party transactions	Management & Strategy; Earnings & Profitability; Capitalisation & Leverage	4
Group Structure	3	Organizational structure; appropriateness relative to business model; opacity; intra-group dynamics; ownership	Company Profile	3
Financial Transparency	3	Quality and frequency of financial reporting and auditing processes	Management & Strategy	2
				1

How to Read This Page
ESG scores range from 1 to 5 based on a 15-level color gradation. Red (5) is most relevant and green (1) is least relevant.

The Environmental (E), Social (S) and Governance (G) tables break out the individual components of the scale. The right-hand box shows the aggregate E, S, or G score. General Issues are relevant across all markets with Sector-Specific Issues unique to a particular industry group. Scores are assigned to each sector-specific issue. These scores signify the credit-relevance of the sector-specific issues to the issuing entity's overall credit rating. The Reference box highlights the factor(s) within which the corresponding ESG issues are captured in Fitch's credit analysis.

The Credit-Relevant ESG Derivation table shows the overall ESG score. This score signifies the credit relevance of combined E, S and G issues to the entity's credit rating. The three columns to the left of the overall ESG score summarize the issuing entity's sub-component ESG scores. The box on the far left identifies some of the main ESG issues that are drivers or potential drivers of the issuing entity's credit rating (corresponding with scores of 3, 4 or 5) and provides a brief explanation for the score.

Classification of ESG issues has been developed from Fitch's sector ratings criteria. The General Issues and Sector-Specific Issues draw on the classification standards published by the United Nations Principles for Responsible Investing (PRI) and the Sustainability Accounting Standards Board (SASB).

Sector references in the scale definitions below refer to Sector as displayed in the Sector Details box on page 1 of the navigator.

CREDIT-RELEVANT ESG SCALE	
How relevant are E, S and G issues to the overall credit rating?	
5	Highly relevant, a key rating driver that has a significant impact on the rating on an individual basis. Equivalent to "higher" relative importance within Navigator.
4	Relevant to rating, not a key rating driver but has an impact on the rating in combination with other factors. Equivalent to "moderate" relative importance within Navigator.
3	Minimally relevant to rating, either very low impact or actively managed in a way that results in no impact on the entity rating. Equivalent to "lower" relative importance within Navigator.
2	Irrelevant to the entity rating but relevant to the sector.
1	Irrelevant to the entity rating and irrelevant to the sector.

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 de Volksbank, either due to their nature or to the way in which they are being managed by the bank. For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg.

The ratings above were solicited and assigned or maintained at the request of the rated entity/issuer or a related third party. Any exceptions follow below.