FITCH AFFIRMS DE VOLKSBANK AT 'A-'; STABLE OUTLOOK

Fitch Ratings-London-13 November 2018: Fitch Ratings has affirmed de Volksbank N.V.'s Long-Term Issuer Default Rating (IDR) at 'A-'. The Outlook is Stable. A full list of rating actions is at the end of this rating action commentary.

The rating actions are part of a portfolio review of major Dutch banking groups rated by Fitch.

KEY RATING DRIVERS
IDRS, VR, DERIVATIVE COUNTERPARTY RATING AND SENIOR DEBT
De Volksbank's ratings reflect the bank's sound asset quality and overall moderate risk appetite, with a focus on low-risk residential mortgage lending. The ratings also reflect the bank's high risk-weighted capital ratios and sound leverage. The ratings are constrained by the bank's concentrated business model and franchise that lacks the breadth of the three larger Dutch banks.

De Volksbank's impaired loans are low (1.5% of gross loans at end-June 2018, 1.4% in mortgage lending) despite a one-off increase on 1 January 2018 due to the first-time adoption of IFRS 9. On a like-for-like basis, de Volksbank's asset quality has been improving, helped by a benign operating environment in the Netherlands and the bank's reasonably conservative underwriting. We do not expect de Volksbank to deviate from its narrow but fairly low-risk business model or to materially increase its risk appetite.

We expect de Volksbank's revenues to remain under pressure due to the subdued loan growth, the current low rate environment, intense competition in the Dutch mortgage lending market and the necessary accumulation of MREL-eligible liabilities, which will weigh on the bank's funding costs. Despite these challenges, de Volksbank maintained healthy operating profitability with operating profit/risk weighted assets (RWA) of 4.2% and an 8.4% return on average equity in 1H18. In our view, the successful implementation of the bank's cost-efficiency programme will be instrumental in safeguarding profitability in the medium term as loan impairment charges (LICs) eventually normalise.

De Volksbank's Fitch Core Capital (FCC; 36.5% of RWAs at end-June 2018) and common equity Tier 1 (CET1; 34.3% at end-June 2018) ratios compare favourably with Dutch banking peers, partly as a consequence of the low risk-weighting of residential mortgage loans. The introduction of a risk-weight floor under Basel III end-game rules is likely to dent the bank's risk-weighted capital ratios, although amendments to the regulation still need to be adopted by the European authorities and will be subject to a long phase-in period. We believe the bank's minimum 4.25% leverage ratio target will help it preserve ample buffers over its regulatory capital requirements despite the RWA inflation. The bank's leverage ratio at end-June 2018 (5.2%) is sound and commensurate with its retail banking profile.

De Volksbank is predominantly deposit-funded, with a loan-to-deposits ratio of 104% at end-June 2018. The bank's funding mix is stable but wholesale funding may be more confidence-sensitive than larger banks with a more established presence in debt capital markets, in our view. De Volksbank's liquidity is sound with a liquidity coverage ratio of 156% at end-June 2018 and is underpinned by a large buffer of high-quality liquid assets well in excess of wholesale funding maturities in the next two years.

De Volksbank's Derivative Counterparty Rating (DCR) is at the same level as the Long-Term IDR because under Dutch legislation, derivative counterparties have no preferential status over other senior obligations in a resolution scenario.

The Short-Term IDR of 'F2' is the baseline option mapping to a 'A-' Long-Term IDR. De Volksbank's liquidity metrics are sound and compare well with peers, but we believe they are warranted given the potentially more confidence-sensitive funding in light of the bank's overall moderate franchise and less certain than larger peers' market access.

SUPPORT RATING AND SUPPORT RATING FLOOR
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.

SUBORDINATED DEBT
Subordinated debt is rated one notch below de Volksbank's VR, 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.

RATING SENSITIVITIES
IDRS, VR, DERIVATIVE COUNTERPARTY RATING AND SENIOR DEBT
An upgrade is unlikely within the constraints of de Volksbank's franchise and business model. While currently not Fitch's base case, de Volksbank's ratings could come under pressure if risk appetite increases, for example through a loosening of underwriting standards or a significant and rapid shift in the business model, particularly if that would worsen asset quality and capitalisation in the longer term.

SUPPORT RATING AND SUPPORT RATING FLOOR
An upgrade of the Support Rating or upward revision of the Support Rating Floor would be contingent on a positive change in the Dutch sovereign's propensity to support its banks. This is highly unlikely, in Fitch's view.

SUBORDINATED DEBT
Subordinated debt is sensitive to changes in de Volksbank's VR. It is also sensitive to a change in Fitch's assessment of loss severity or non-performance risk.

The rating actions are as follows:

Long-Term IDR affirmed at 'A-'; Outlook Stable
Short-Term IDR affirmed at 'F2'
Support Rating: affirmed at '5'
Support Rating Floor: affirmed at 'No Floor'
Viability Rating: affirmed at 'a-'
Derivative Counterparty Rating: affirmed at 'A-(dcr)'
Long-term senior debt rating: affirmed at 'A-'
Short-term senior debt rating: affirmed at 'F2'
Commercial paper: affirmed at 'F2'
Subordinated (Tier 2) debt: affirmed at 'BBB+'

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Additional information is available on www.fitchratings.com

Applicable Criteria
Bank Rating Criteria (pub. 12 Oct 2018)
https://www.fitchratings.com/site/re/10044408