

Research Update:

# De Volksbank Outlook Revised To Stable On Impaired Earnings In COVID-19 Fallout; 'A-/A-2' Ratings Affirmed

April 23, 2020

## Overview

- Despite the government's measures to contain the COVID-19 pandemic, the Dutch economy and its domestic banks face an unprecedented challenge. Even under our base case of an economic recovery starting in third-quarter 2020, we expect Dutch banks' earnings and asset quality to be meaningfully impaired through end-2020 and into 2021.
- This weaker operating environment, alongside low interest rates for an extended period, and sustained price competition in the Dutch mortgage market are weighing on De Volksbank N.V.'s (DVB's) earnings capacity.
- Still, DVB continues to adhere to much stronger capitalization principles than peers, leading to high additional loss-absorbing capacity (ALAC) buffers.
- We have therefore revised the outlook on DVB to stable from positive and affirmed the ratings at 'A-/A-2'.
- The stable outlook reflects our view that DVB's capitalization will remain very strong and will therefore contribute to the protection for its debtholders.

### PRIMARY CREDIT ANALYST

**Sylvie Dalmaz, PhD**  
Paris  
(33) 1-4420-6682  
sylvie.dalmaz  
@spglobal.com

### SECONDARY CONTACT

**Nicolas Hardy**  
Paris  
(33) 1-4420-7318  
nicolas.hardy  
@spglobal.com

## Rating Action

On April 23, 2020, S&P Global Ratings revised to stable from positive its outlook on De Volksbank N.V. (DVB). We affirmed the issuer credit ratings at 'A-/A-2'.

## Rationale

Today's rating action follows a review of several Western European banking sectors, including the Netherlands-based one. We revised our trend to negative from stable on our economic risk for the Dutch Bank Industry Country Risk Assessment (BICRA). The anchor for a domestic bank in the Netherlands remains 'bbb+'. The Netherlands remains in group '3', like the U.S., the U.K.,

Australia, France, or Denmark.

Until the start of March, Dutch banks, like their European counterparts, were fully engaged with the same two key themes that have been paramount in recent years--stabilizing balance sheet strength with solid investor returns, and identifying how to refine operating models in the face of the looming risks and opportunities of the digital era. For the short term at least, the COVID-19 pandemic has changed (almost) everything. We now are expecting a 6.7% GDP contraction in the Netherlands, and 7.3% in the eurozone, and a recovery of about 6.0% in 2021. Even under this base case, the effects of COVID-19 will be evident for long after the crisis subsides.

Dutch and European authorities have delivered unprecedented policy responses in the form of monetary, fiscal, and regulatory support to their economies. However, while we expect banks in the Netherlands to remain broadly resilient in the face of this short-term cyclical shock, we expect that it will encounter in 2020 a meaningful impact on asset quality, revenues, profitability, liquidity, and, potentially, capitalization. We expect very few of these negative trends to be strongly evident in Dutch banks' first-quarter results, but consider that they would become increasingly evident through the course of 2020 and persist into 2021.

The outlook revision to stable captures the potential risks from this weaker environment. The rating affirmation balances our view of DVB's high loss-absorbing capacity buffers with the additional pressures we see on the bank's profitability. Although we believe that DVB's credit quality is bolstered by the bank's loss-absorbing capacity, the anticipated decline in the bank's net income over the coming two years constrains the ratings.

DVB remains a monoline Dutch bank. Its stand-alone credit profile (SACP), which excludes ALAC uplift, is unchanged at 'bbb+'. DVB's stand-alone credit quality is most notably supported by the bank's stable franchise, limited income streams outside its mortgage portfolio, a low-risk lending book, concentrated in a single asset class, and very strong capital buffers. As of end-2019, DVB's risk-adjusted capital (RAC) ratio stood at an estimated 22.6% and its ALAC buffers at more than 10% of S&P Global Ratings' risk-weighted assets. We anticipate the latter ratio will remain at or above this level over the coming two years. This is on the back of DVB's ongoing policy to adhere to very strong capital and potential issuance of senior nonpreferred notes in order to meet its requirements of minimum own funds and eligible liabilities.

At the same time, under our base-case scenario, DVB's net income will face a double-digit drop in 2020. The deteriorated operating environment because of the COVID-19 pandemic and prolonged low interest rates will be detrimental to DVB's revenue. This comes at a time when continuous investments are necessary. In 2020-2021, we believe that declining margins will continue to constrain the bank's efforts to improve efficiency, while cost of credit risk will increase as the bank's asset quality remains sensitive to potentially rising unemployment and declining houses prices. DVB is currently exploring ways to optimize its business model, to diversify income, and cut costs. We assume these considerations will yield a new strategic plan that the bank will announce before end-2020.

## **Outlook**

The stable outlook on DVB reflects our view that the bank's capitalization will remain very strong and therefore offer protection to its debtholders, including its senior preferred bondholders through its loss-absorbing capacity. Our central scenario also incorporates that DVB will eventually issue senior nonpreferred notes. Furthermore, we consider that, despite recovery in the bank's franchise, privatization is unlikely over our outlook horizon given the persistently low interest rate environment, which makes it challenging for the bank to optimize its business model.

We would revise the outlook to negative if a less conservative capital policy weakened DVB's financial profile, including its loss-absorbing capacity. Also, a downgrade could happen if we believed economic risks of the Dutch banking market intensified as a result of COVID-19, leading us to reassess the bank's currently favorably risk-adjusted ALAC buffers.

## Ratings Score Snapshot

	To	From
Issuer Credit Rating	A-/Stable/A-2	A-/Positive/A-2
SACP	bbb+	bbb+
Anchor	bbb+	bbb+
Business Position	Moderate (-1)	Moderate (-1)
Capital and Earnings	Very strong (+2)	Very strong (+2)
Risk Position	Moderate (-1)	Moderate (-1)
Funding and Liquidity	Average and Adequate (0)	Average and Adequate (0)
Support	+2	+1
ALAC Support	+2	+1
GRE Support	0	0
Group Support	0	0
Sovereign Support	0	0
Additional Factor	-1	0

## Related Criteria

- General Criteria: Hybrid Capital: Methodology And Assumptions, July 1, 2019
- General Criteria: Group Rating Methodology, July 1, 2019
- Criteria | Financial Institutions | General: Methodology For Assigning Financial Institution Resolution Counterparty Ratings, April 19, 2018
- Criteria | Financial Institutions | General: Risk-Adjusted Capital Framework Methodology, July 20, 2017
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- Criteria | Financial Institutions | Banks: Bank Rating Methodology And Assumptions: Additional Loss-Absorbing Capacity, April 27, 2015
- Criteria | Financial Institutions | Banks: Quantitative Metrics For Rating Banks Globally: Methodology And Assumptions, July 17, 2013
- Criteria | Financial Institutions | Banks: Banking Industry Country Risk Assessment Methodology And Assumptions, Nov. 9, 2011
- Criteria | Financial Institutions | Banks: Banks: Rating Methodology And Assumptions, Nov. 9, 2011
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009

## Related Research

- Negative Rating Actions Taken On Multiple Benelux Banks On Deepening COVID-19 Downside Risks, April 23, 2020
- Negative Rating Actions Taken On Various French Banks On Deepening COVID-19 Downside Risks, April 23, 2020
- How COVID-19 Risks Prompted European Bank Rating Actions, April 23, 2020
- Europe's AT1 Market Faces The COVID-19 Test: Bend, Not Break, April 22, 2020
- How COVID-19 Is Affecting Bank Ratings, April 22, 2020
- Europe Braces For A Deeper Recession In 2020, April 20, 2020
- European Banks' First-Quarter Results: Many COVID-19 Questions, Few Conclusive Answers, April 1, 2020
- COVID-19: The Steepening Cost To The Eurozone And U.K. Economies, March 26, 2020
- COVID-19 Countermeasures May Contain Damage To Europe's Financial Institutions For Now, March 13, 2020
- The Coronavirus Will Shave 50 Basis Points Off Eurozone Growth, March 4, 2020
- Full Analysis: ING Groep N.V., March 23, 2020

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at [www.standardandpoors.com](http://www.standardandpoors.com) for further information. A description of each of S&P Global Ratings' rating categories is contained in "S&P Global Ratings Definitions" at [https://www.standardandpoors.com/en\\_US/web/guest/article/-/view/sourceId/504352](https://www.standardandpoors.com/en_US/web/guest/article/-/view/sourceId/504352) Complete ratings information is available to subscribers of RatingsDirect at [www.capitaliq.com](http://www.capitaliq.com). All ratings affected by this rating action can be found on S&P Global Ratings' public website at [www.standardandpoors.com](http://www.standardandpoors.com). Use the Ratings search box located in the left column. Alternatively, call one of the following S&P Global Ratings numbers: Client Support Europe (44) 20-7176-7176; London Press Office (44) 20-7176-3605; Paris (33) 1-4420-6708; Frankfurt (49) 69-33-999-225; Stockholm (46) 8-440-5914; or Moscow 7 (495) 783-4009.

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