S&P Global
Ratings

Research

Bank Nederlandse Gemeenten N.V.

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Bank Nederlandse Gemeenten N.V.

SACP	a+

\+

Support	+4

\+

Additional Factors	0

Anchor	bbb+	
Business Position	Adequate	0
Capital and Earnings	Very Strong	+2
Risk Position	Strong	+1
Funding	Average	0
Liquidity	Adequate	

ALAC Support	0
GRE Support	+4
Group Support	0
Sovereign Support	0

Issuer Credit Rating
AAA/Stable/A-1+

Major Rating Factors

Strengths:	Weaknesses:
• Almost certain likelihood of extraordinary government support. • Leading lender to Dutch public authorities, supporting very strong asset quality. • Sound capitalization.	• Sector and geographic concentration with limited diversification of income sources. • Moderate capital generation due to low lending margins. • Mostly wholesale funded.

Outlook: Stable

S&P Global Ratings' stable outlook on Bank Nederlandse Gemeenten N.V. (BNG Bank) reflects that on The Netherlands (AAA/Stable/A-1+). As long as we consider support from the Dutch government to be almost certain, any reassessment of the bank's stand-alone creditworthiness would not directly affect the long-term issuer credit rating on BNG Bank. In addition, any rating action on The Netherlands would likely result in a similar rating action on BNG Bank. That said, we expect the financial profile to remain strong in the next two years.

We could therefore downgrade BNG Bank by one notch if we were to take a similar action on The Netherlands. We could also lower the ratings over the next two years if we see a reduced likelihood of support from the Dutch government. This could happen if the bank's role for the Dutch government diminished following a sharp increase in competition, or if we viewed that the link with the government had weakened.

Rationale

We base our ratings on our classification of BNG Bank as a government-related entity (GRE) with an almost certain likelihood of extraordinary government support.

We view the stand-alone credit profile (SACP) at 'a+', which is one of the strongest we have in The Netherlands.

BNG Bank benefits from a stable franchise as one of the principal lenders to the Dutch public sector through economic cycles and a very predictably strategy. However, this is offset by its business and geographic concentration.

Typical for banks with a large balance sheet made of very low-risk assets, BNG Bank displays very strong capital ratios but modest leverage metrics. We expect some future dividend policy to be primarily determined by its leverage ratio.

Low-risk lending to, or guaranteed by, public authorities and our expectation of limited loan book growth and high quality securities dominate the asset base. This makes BNG Bank an entity with an extremely low credit risk profile. But we recognize that its business model is based on its continued capacity to access funding at very low costs, given the structurally low asset margins.

BNG Bank remains wholesale funded, as in line with other public sector-focused peers, and funding sources are well diversified by source and maturity.

We equalize the long-term issuer credit rating on BNG Bank with that on The Netherlands, reflecting the implicit support the bank receives from the Dutch Ministry of Finance because of the bank's public sector mandate and combined ownership by The Netherlands (50%) and other Dutch public authorities.

Anchor: 'bbb+' for a bank operating only in The Netherlands

We use our Banking Industry Country Risk Assessment (BICRA) economic and industry risk scores to determine a bank's anchor--the starting point in assigning an issuer credit rating. The anchor for a bank operating only in The Netherlands is 'bbb+'.

We base our assessment of economic risk on our view that the Dutch economy is wealthy, diversified, open, and competitive, as seen in its high income per capita, its net external asset position, recurrent and elevated current account surpluses, and a long track record of prudent and flexible macroeconomic policies. Following real GDP growth of 2.1% in 2016, we think that The Netherlands' real GDP will post 2.2% growth this year before lowering to a 1.9% average during 2017-2019. The ongoing recovery continues to be fuelled by strong domestic demand. We think that supportive macro-economic developments, the dynamics of the real estate markets--both residential and commercial--and, last but not least, the legal reforms introduced since 2013 and the banks' own restructuring efforts in this context, are gradually leading to receding economic imbalances in the country. In our view, the trend on economic risk is positive.

Our assessment of industry risks for Dutch banks incorporates high domestic concentration and our view of a stable competitive environment. We consider that the prospective profitability of domestic banking activities is adequate. Some of the large banks have completed large restructuring efforts in exchange for state aid. Cost optimization programs continue in the context of the persistently low-interest-rate environment and cost of risk has also improved, mitigating asset repricing. The system's relatively large reliance on wholesale funding is partly attributable to households' propensity to save in life insurance and pension products, rather than in bank deposits. We consider that Dutch systemwide funding benefits from, among other things, the depth of the domestic capital market and the Dutch authorities' good track record in providing liquidity support.

Table 1

Bank Nederlandse Gemeenten N.V. Key Figures					
		--Year-ended Dec. 31--			
(Mil. €)	**2017***	**2016**	**2015**	**2014**	**2013**
Adjusted assets	146,340	154,000	149,511	153,505	131,183
Customer loans (gross)	85,921	87,346	88,605	89,705	90,997
Adjusted common equity	3,608	3,384	3,111	2,941	2,847
Operating revenues	368	554	499	291	579
Noninterest expenses	43	117	113	97	97
Core earnings	242	349	232	131	328

*Estimates as of June 30.

Business position: A stable public sector financing franchise offset by business and geographic concentration

Our assessment of BNG Bank's business position as adequate reflects the sound market position of the franchise and its stable activities. BNG Bank enjoys a 57% market share dominance in the Dutch public sector, followed by NWB Bank (30%). In 2016, BNG Bank registered stable market shares on new loan production compared to 2015; 66% on public entities, 49% on social housing, and 34% on healthcare. We do not expect any substantial change in the next two years.

BNG bank's new loan production for 2016 stood at €10.2 billion, which compares to €11.2 billion in 2015, supported by high refinancing volumes. Negative trends affecting the bank's main asset classes include municipal and provincial budgets that are under pressure, a narrowing of Waarborgfonds Sociale Woningbouw's guarantee scheme (WSW; Netherlands's social housing guarantee fund) causing social housing loan production to decline, and budget cuts compounded by regulatory uncertainties with respect to the care sector.

BNG Bank's focus on low-risk loans is offset by concentration risks as the whole loan portfolio is exclusively invested in The Netherlands on a nearly one-sided government-risk asset class.

BNG Bank has an unchanged strategy centered on its exclusive Dutch public financing mandate. BNG Bank aims at minimizing the cost of financing to the public sector while achieving a reasonable return for shareholders and complying with regulatory requirements. In our view, the stability and predictability of the business model support stable underlying earnings generation capacities and prevents excessive risk taking by maintaining business in areas of long-standing expertise.

Table 2

Bank Nederlandse Gemeenten N.V. Business Position

		--Year-ended Dec. 31--			
(%)	**2017***	**2016**	**2015**	**2014**	**2013**
Return on equity	12.4	9.9	6.2	3.6	9.2

*Data as of June 30.

Capital and earnings: Continued capital strengthening toward Basel III leverage ratio requirement

Our assessment of BNG Bank's very strong capital and earnings mainly reflects our expectation that BNG Bank's RAC ratio before diversification and concentration adjustments will remain very comfortably above the 15% mark. We calculate BNG Bank's to be 24.3% at year-end 2016, and expect the ratio to rise above 25% over the next 24 months.

We base our RAC ratio projections on steady retained earnings, about €350 million, and stable S&P Global Ratings' risk-weighted assets (RWAs). We include in our forecasts for the next two years a stable outstanding loan book, net interest margins in the 35-40 basis point (bp) range, and rising cost-to-income ratio of 20%-25% due to regulatory pressure. IFRS 9 implementation should lead to a slight increase in credit losses provisioning but cost of risk should remain inferior to 5 bps.

Interest risk and foreign exchange risk are fully hedged through derivatives and most of the counterparties are large financial institutions in Europe. We note that the volatility of the balance sheet due to interest rates and foreign exchange rate fluctuations has a direct impact on our capital metric, but we anticipate that this volatility will not move the RAC ratio below our 15% threshold for the very strong assessment.

Net interest income stood at €222 million as of June 2017 and the bank booked €11 million of income from commissions, and a €132 million gain on financial transactions. The latter remain volatile since they include the unrealized gains or losses on financial assets at fair value through the income statement. For instance, the bank registered a €22 million loss in 2016 due to value adjustments based on interest rate and base currency spreads. BNG Bank booked a €242 million net profit in June 2017.

Typical for banks with a large balance sheet made of low-risk assets, meeting leverage ratios is more of constraint for BNG Bank than meeting capital ratios, which are based on risk-weighted assets. As of June 2017, BNG Bank registered a Basel III leverage ratio of 3.3%, which is modest when compared to commercial banks but in line with the business model, and therefore complies with the expected future regulatory requirement. Now that the bank's migration plan to achieve 3% is complete, we understand BNG Bank could increase its dividend payout in 2018 and 2019 as long as its leverage ratio remains above the minimum regulatory requirement.

Table 3

Bank Nederlandse Gemeenten N.V. Capital And Earnings

		--Year-ended Dec. 31--			
(%)	**2017***	**2016**	**2015**	**2014**	**2013**
Criteria reflected in RAC ratios	N/A	2017 RAC Criteria	2010 RAC Criteria	2010 RAC Criteria	2010 RAC Criteria
Tier 1 capital ratio	36.0	32.7	28.0	26.0	25.0
S&P RAC ratio before diversification	N/A	24.7	23.4	17.8	18.0
S&P RAC ratio after diversification	N/A	19.7	20.4	15.8	16.7

Table 3

Bank Nederlandse Gemeenten N.V. Capital And Earnings (cont.)					
		--Year-ended Dec. 31--			
(%)	**2017***	**2016**	**2015**	**2014**	**2013**
Adjusted common equity/total adjusted capital	83.1	82.2	88.0	100.0	100.0
Net interest income/operating revenues	60.3	73.1	90.2	152.6	91.5
Fee income/operating revenues	3.0	4.3	5.6	10.0	4.3
Market-sensitive income/operating revenues	35.9	21.3	3.2	(64.3)	3.8
Noninterest expenses/operating revenues	11.7	21.1	22.6	33.3	16.8
Preprovision operating income/average assets	0.4	0.3	0.3	0.1	0.4
Core earnings/average managed assets	0.3	0.2	0.2	0.1	0.2

*Data as of June 30. N/A--Not applicable.

Risk position: The bank is likely to maintain its conservative risk profile

Our assessment of BNG Bank's strong risk position reflects our view of its continued focus on low-risk lending to, or guaranteed by, public authorities. The portfolio is dominated by largely government risk and was broken down as follows as of Dec. 31, 2016: 49% social housing, 36.6% public sector, 9% healthcare, and 5% other sectors. Longer-term lending to social housing corporations and healthcare institutions is guaranteed by WSW and Waarborgfonds voor de Zorgsector, respectively. The central bank considers these exposures to be equivalent to risk arising from the Dutch state, resulting in a 0% risk weight. In terms of loss experience, BNG Bank booked one exceptional impairment over the last few years following the restructuring of a €125 million bond issued by the former Austrian bank Hype Alpe Adria but the NPL ratio should remain below 0.5%.

Credit risk in BNG Bank's securities portfolio is tempered by means of a large share of highly rated instruments: 56% of the portfolio was invested in 'AAA' rated securities on June 30, 2017 (27% and 10% in 'AA' and 'A' rated securities, respectively). Inevitably, this creates some concentration risk for highest quality sovereigns. At mid-year 2017, BNG Bank reported €1.9 billion of total exposures to peripheral eurozone countries, down from €2.5 billion one year earlier. BNG Bank has indicated that it does not intend to increase its long-term exposure in these countries in the future. Most of the nonsovereign exposures to peripheral eurozone countries are in asset-backed securities.

The bank undertakes no trading activities and interest rate risk is controlled within a framework of limits approved by the board. BNG Bank's policy is to fully hedge the exposure from all foreign currency debt issuance.

We note the bank is dependent on continued access to low-cost liabilities given the structurally low yields on most of its assets. This creates a structural sensitivity to any negative market sentiment, essentially around Dutch risk.

Table 4

Bank Nederlandse Gemeenten N.V. Risk Position					
		--Year-ended Dec. 31--			
(%)	**2017***	**2016**	**2015**	**2014**	**2013**
Growth in customer loans	(3.3)§	(1.4)	(1.2)	(1.4)	0.8
Total diversification adjustment / S&P RWA before diversification	N/A	25.4	14.8	12.9	7.6
Total managed assets/adjusted common equity (x)	40.6	45.5	48.1	52.2	46.1
New loan loss provisions/average customer loans	0.0	(0.0)	0.1	0.0	0.0

Table 4

Bank Nederlandse Gemeenten N.V. Risk Position (cont.)					
		--Year-ended Dec. 31--			
(%)	**2017***	**2016**	**2015**	**2014**	**2013**
Gross nonperforming assets/customer loans + other real estate owned	0.2	0.1	0.1	0.1	0.0
Loan loss reserves/gross nonperforming assets	20.7	32.6	38.3	45.3	N.M.

*Data as of June 30. §Annualized rate. N/A--Not applicable. N.M.--Not meaningful.

Funding and liquidity: Wholesale funded with well-diversified sources

We view funding as average and liquidity as adequate, despite BNG Bank's main funding and liquidity metrics being weaker than Dutch peers'. We particularly have a negative view of the large share of short-term wholesale funding in BNG Bank's funding base--which has decreased slightly below 30% over the past three years--because this funding resource is more confidence-sensitive by nature. However, we understand this short-term funding is mostly used to fuel short-term highly rated securities that act as a liquidity buffer, ECB accounts and cash collateral for hedging operations. This recourse to short-term funding supports low cost of liabilities, which is a sine qua non condition for the good functioning of the business model.

In line with public sector-focused peers, BNG Bank is almost entirely wholesale funded as it does not take deposits, which deprives it of a stable funding source. Under our own metrics, we estimate BNG Bank's stable funding ratio to be improving to 90.88% and broad liquid assets to short-term wholesale funding to be 0.66x as of mid-2017. We nevertheless do not incorporate any negative rating adjustment regarding BNG Bank's funding profile and liquidity position because we also take into account many qualitative factors. BNG Bank enjoys a large and diversified investor base, demonstrated in its currency funding mix (44% euros, 38% U.S. dollars, and 12% pounds sterling), its geographic funding mix (24% Americas, 18% Asia, 9% U.K., and 41% Europe not including the U.K.) and its investor type funding base (29% banks, 23% central banks, and 20% asset managers). The bank's liquidity position is also more resilient than our metrics show, thanks to its €9 billion untapped ECB facility and its large investment portfolio composed of highly liquid securities. Lastly, in contrast with most banks we rate, a large majority of BNG Bank's loan book is solvency free and could be pledged as collateral at De Nederlandsche Bank in case of liquidity stress.

Table 5

Bank Nederlandse Gemeenten N.V. Funding And Liquidity					
		--Year-ended Dec. 31--			
(%)	**2017***	**2016**	**2015**	**2014**	**2013**
Long term funding ratio	76.6	70.0	68.1	65.5	67.7
Stable funding ratio	90.9	82.5	78.6	75.9	70.8
Short-term wholesale funding/funding base	24.3	28.4	31.0	32.3	30.4
Broad liquid assets/short-term wholesale funding (x)	0.7	0.6	0.5	0.4	0.4
Short-term wholesale funding/total wholesale funding	24.2	28.2	30.8	32.3	30.4
Narrow liquid assets/3-month wholesale funding (x)	1.0	1.1	1.1	0.9	0.6

*Estimates as of June 30.

External support: Almost certain likelihood of support from the Dutch government

We equalize the long-term rating on BNG Bank with that on The Netherlands, reflecting the implicit support the bank receives from the Dutch Ministry of Finance because of its public sector mandate and combined ownership by the Dutch state (50%) and other Dutch public authorities. For this reason, we view BNG Bank as a GRE with an almost certain likelihood of extraordinary government support. In accordance with our GRE criteria, our rating approach is based on our view of BNG Bank's:

- Critical role as one of two public sector banks with a public policy role. In our view, BNG Bank plays a vital role in providing low-cost and stable/constant financing to the Dutch public sector. Private sector commercial banks are typically willing to finance only a small part of the public sector's financing needs and are not able to provide financing at the same low cost as BNG Bank. In the absence of public sector banks, the government would likely have to finance the public sector directly. BNG Bank's links with other entities, such as WSW, that benefit from government guarantees, increase the government's incentive to provide extraordinary support, in our view.
- Integral link with the government as we consider the bank to be an extension of the government. The bank's articles of association limit BNG Bank's ownership and lending activities to the public sector, which supports our view of the link between BNG Bank and the government. We note that although the government is not involved in the day-to-day running of BNG Bank, it maintains close oversight over the bank's strategy and capital policy.

Our assessment also factors in our view that the EU's Bank Recovery and Resolution Directive (BRRD) could reduce the predictability of government support for systemically important banks in the region. When it comes to Dutch-domiciled GREs, even when they are subject to the BRRD, our longstanding view is that the BRRD by itself does not appear to restrict the possibility of a government in its capacity as existing shareholder of a bank to grant support in a going-concern situation.

Nevertheless, in a going concern scenario, the BRRD could well prevent the government from injecting capital into some GREs to correct an acute solvency problem without first bailing in senior liabilities.

Related Criteria

- 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
- General Criteria: Rating Government-Related Entities: Methodology And Assumptions, March 25, 2015
- Criteria - Financial Institutions - Banks: Bank Hybrid Capital And Nondeferrable Subordinated Debt Methodology And Assumptions, Jan. 29, 2015
- General Criteria: Group Rating Methodology, Nov. 19, 2013
- Criteria - Financial Institutions - Banks: Quantitative Metrics For Rating Banks Globally: Methodology And Assumptions, July 17, 2013
- Criteria - Financial Institutions - Banks: Banks: Rating Methodology And Assumptions, Nov. 9, 2011
- Criteria - Financial Institutions - Banks: Banking Industry Country Risk Assessment Methodology And Assumptions, Nov. 9, 2011
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009
- Criteria - Financial Institutions - Banks: Commercial Paper I: Banks, March 23, 2004

Related Research

- State of The Netherlands Ratings Affirmed At 'AAA/A-1+'; Outlook Stable, Nov. 17, 2017
- Various Dutch Bank Outlooks To Positive On Receding Economic Imbalances In The Netherlands, Sept. 15, 2017
- Banking Industry Country Risk Assessment: The Netherlands, March 30, 2016

Anchor Matrix

Industry Risk	Economic Risk									
	1	2	**3**	4	5	6	7	8	9	10
1	a	a	a-	bbb+	bbb+	bbb	-	-	-	-
2	a	a-	a-	bbb+	bbb	bbb	bbb-	-	-	-
3	a-	a-	**bbb+**	bbb+	bbb	bbb-	bbb-	bb+	-	-
4	bbb+	bbb+	bbb+	bbb	bbb	bbb-	bb+	bb	bb	-
5	bbb+	bbb	bbb	bbb	bbb-	bbb-	bb+	bb	bb-	b+
6	bbb	bbb	bbb-	bbb-	bbb-	bb+	bb	bb	bb-	b+
7	-	bbb-	bbb-	bb+	bb+	bb	bb	bb-	b+	b+
8	-	-	bb+	bb	bb	bb	bb-	bb-	b+	b
9	-	-	-	bb	bb-	bb-	b+	b+	b+	b
10	-	-	-	-	b+	b+	b+	b	b	b-

Ratings Detail (As Of December 22, 2017)

Bank Nederlandse Gemeenten N.V.	
Counterparty Credit Rating	AAA/Stable/A-1+
Commercial Paper	A-1+
Senior Unsecured	AAA
Short-Term Debt	A-1+
Counterparty Credit Ratings History	
24-Nov-2015	AAA/Stable/A-1+
27-May-2015	AA+/Positive/A-1+
02-Dec-2013	AA+/Stable/A-1+
Sovereign Rating	
Netherlands (State of The)	AAA/Stable/A-1+
Related Entities	
Waarborgfonds Sociale Woningbouw	
Issuer Credit Rating	AAA/Stable/--
Waarborgfonds voor de Zorgsector	
Issuer Credit Rating	AAA/Stable/--

*Unless otherwise noted, all ratings in this report are global scale ratings. S&P Global Ratings' credit ratings on the global scale are comparable across countries. S&P Global Ratings' credit ratings on a national scale are relative to obligors or obligations within that specific country. Issue and debt ratings could include debt guaranteed by another entity, and rated debt that an entity guarantees.

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