FitchRatings

RATING ACTION COMMENTARY

Fitch Revises Outlook on Rabobank to Stable; Affirms at 'A+'

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Fitch Ratings - Paris - 26 Nov 2021: Fitch Ratings has revised the Outlook on Cooperatieve Rabobank U.A.'s Long-Term Issuer Default Rating (IDR) to Stable from Negative and affirmed the Long-Term IDR at 'A+'. Fitch has also affirmed Rabobank's Viability Rating (VR) at 'a+'.

The revision of the Outlook reflects better than anticipated financial performance of the bank during the pandemic and the stabilisation of the Dutch operating environment. Fitch's updated economic assumptions for the Netherlands indicate a strong economic recovery, despite some remaining risks related to the pandemic, supply chain disruptions and rising energy prices. Consequently, we believe that downside risks to Rabobank's profitability, asset quality and capitalisation have receded.

Fitch has withdrawn Rabobank's Support Rating and Support Rating Floor as they are no longer relevant to the agency's coverage following the publication of its updated Bank Rating Criteria on 12 November 2021. In line with the updated criteria, we have assigned Rabobank a Government Support Rating (GSR) of 'No Support' ('ns').

KEY RATING DRIVERS

IDRS, VR AND SENIOR NON-PREFERRED DEBT (SNP)

Rabobank's IDRs and VR are underpinned by its modest risk profile. This includes the bank's more conservative capital management, which we believe will remain central to the bank's strategy. The ratings are also supported by Rabobank's leading market position in Dutch retail banking, complemented by a solid franchise in the global food and agriculture (F&A) sectors, and its sound funding and liquidity profile. Adequate asset quality and profitability are relative rating weakness. Rabobank's VR is one notch above the 'a' implied rating, driven by a risk profile adjustment assessed by Fitch at 'a+'.

Rabobank's impaired loans/gross loans ratio (as calculated by Fitch, where impaired loans are defined as Stage 3 loans under IFRS, and loans include exposures to the public sector but exclude reverse repos), continued to improve despite the pandemic and decreased to 2.8% at end-June 2021 from 3.2% at end-2020. The improvement in asset quality was driven by limited inflows in impaired loans and the bank's active problem loan work-out management.

We believe the bank's definition of non-performance is conservative relative to peers, as highlighted by the low share of past due loans in total impaired loans (19% at end-2020). Rabobank's stock of impaired loans has been consistently declining for the last few years, and the pace of reduction has accelerated since 2018, as the bank has taken a more active approach to work-outs in anticipation of provisioning backstop regulation and supervisory expectations on impaired loan coverage.

We expect this improving trend to reverse in the near term from higher inflows in impaired loans from the SME and corporate exposures as government support measures are discontinued. However, we expect deterioration to be manageable and not push Rabobank's four-year average impaired loans ratio above the current 3.7% average in the next two years, given the sound starting point.

Rabobank's high exposure to low-risk and well-performing Dutch residential mortgage loans and small aggregate exposure to sectors most affected by lockdowns and social distancing rules should help contain the expected weakening of asset quality metrics. At end-June 2021, Rabobank's exposure to sectors vulnerable to the pandemic was EUR12.6 billion or about 3% of total loans. Rabobank's focus on the F&A industry, accounting for about a quarter of total loans, may also lead to a lower than average impact on its asset quality, as companies in the food supply chain appear less affected by the current pandemic because of strong demand and rising soft commodity prices.

Specific coverage of Stage 3 loans (23% at end-June 2021) is low relative to European peers. This reflects the highly secured nature of the loan book and availability of collateral and low historical credit losses, but exposes Rabobank's earnings to fluctuations in collateral values.

Rabobank's operating profit/risk-weighted assets (RWA) rebounded strongly in 1H21 to an unsustainable 2.7% from about 0.9% in 2020, supported by healthy fee income growth from market activities, positive revaluation of the bank's equity participations, and a EUR298 million net release of loan loss allowances (-14bp of gross loans on an annualised basis). We expect operating profit to decrease in 2022 from a strong 2021 level as solid revenue growth will most likely not be replicated and loan impairment charges will start to normalise. However, the operating profit/RWA ratio should remain around 1.5% of RWA. At the same time, we expect revenue pressure from low interest rates to be partly offset by structural cost savings from the ongoing efficiency programmes.

Capitalisation is a rating strength. Rabobank's common equity Tier 1 (CET1) ratio increased to a solid 17.2% at end-June 2021, up from 16.8% at end-2020. We expect Rabobank's CET1 ratio will remain above 15% in the next 12-24 months, despite the expected RWA inflation from the introduction by the Dutch central bank of a floor for the risk-weighting of residential mortgages from 1 January 2022 and the increase in credit risk RWAs due to negative internal rating migration. The Basel III leverage ratio (7.1% at end-June 2021) is also solid and compares well with peers.

Rabobank's funding mix is diversified and benefits from the bank's strong deposit franchise in the Netherlands and sound access to the wholesale market. The liquidity buffer is ample and has increased to account for 22% of total assets at end-June 2021.

The 'F1' Short-Term IDR is the baseline option mapping to a Long-Term IDR of 'A+' under Fitch's criteria and in line with Rabobank's funding and liquidity score of 'a+'.

Rabobank plans to meet its minimum requirements for own funds and eligible liabilities (MREL), set at 27.6% of RWAs (and binding starting 1 January 2022), through the issuance of SNP and more junior debt. This drives the equalisation of the SNP debt rating with the Long-Term IDR.

DERIVATIVE COUNTERPARTY RATING (DCR), SP DEBT AND DEPOSITS

Rabobank's DCR and long-term SP debt ratings have been affirmed and are one notch above the bank's Long-Term IDR. This reflects the protection offered to preferred creditors by the resolution buffers of equity and more junior debt. Rabobank has publicly stated that it intends to meet its MREL using subordinated and SNP instruments only. Rabobank's long-term deposit rating is 'AA-' because deposits benefit from the same protection as other preferred creditors. Short-term SP debt and the short-term deposit rating of 'F1+' are the only short-term rating options mapping to the long-term ratings of 'AA-'.

SUBORDINATED DEBT

Rabobank's subordinated Tier 2 debt is rated two notches below its VR. This is in line with Fitch's baseline notching for loss severity as we expect recoveries to be poor for this type of debt in case of default/non-performance of the bank.

Additional Tier 1 instruments with fully discretionary coupons and legacy hybrid debt with partly discretionary coupons are rated four notches below the VR, in line with the baseline notching for this type of debt. This comprises two notches each for loss-severity and for non-performance risk. Our assessment is based on the fact that there is a significant distance between the bank's CET1 ratio and mandatory coupon omission triggers.

GSR

Rabobank's GSR of 'no support' reflects Fitch's view that senior creditors cannot rely on receiving full extraordinary support from the sovereign in the event that the bank becomes nonviable. The EU's Bank Recovery and Resolution Directive (BRRD) and the Single Resolution Mechanism (SRM) for eurozone banks provide a framework for resolving banks that requires senior creditors participating in losses, if necessary, instead of, or ahead of, a bank receiving sovereign support.

RATING SENSITIVITIES

Factors that could, individually or collectively, lead to negative rating action/downgrade:

We would likely downgrade Rabobank's Long-Term IDR and VR if its CET1 ratio falls materially below 14% together with a deterioration in leverage without a credible plan to restore them. A sharper-than-expected weakening of asset quality, meaning that Rabobank's impaired loans ratio would increase above 4% on a sustained basis, or the bank's operating profit/RWA declines below 1.5% due to structural challenges, would also likely lead to a downgrade.

The DCR, SP debt and deposit ratings could be downgraded to the level of the IDRs if we expect Rabobank to fulfil part of its MREL requirement with SP debt and the buffer of qualifying junior debt and SNP debt to fall below 10% of RWA.

Subordinated debt ratings would be downgraded if Rabobank's VR was downgraded. The ratings of the additional Tier 1 instruments could also be downgraded if we see a heightened risk that capital cushions above the mandatory coupon omission triggers will fall below 100bp.

Factors that could, individually or collectively, lead to positive rating action/upgrade:

Upgrade potential of the VR and the Long-Term IDR is limited and would require a significant and structural improvement in profitability and asset quality.

Rabobank's Short-Term IDR would be upgraded if its Long-Term IDR is upgraded or if its funding and liquidity score is upgraded to 'aa-' or above.

The subordinated debt ratings would be upgraded if Rabobank's VR was upgraded.

VR ADJUSTMENTS

The Asset Quality score of 'a-' has been assigned above the 'bbb' category implied score due to the following adjustment reason: Loan classification policies (positive).

The Capitalisation & Leverage score of 'a+' has been assigned below the 'aa' implied score due to the following adjustment reason: Historical and Future Metrics (negative).

BEST/WORST CASE RATING SCENARIO

International scale credit ratings of Financial Institutions and Covered Bond issuers have a best-case rating upgrade scenario (defined as the 99th percentile of rating transitions, measured in a positive direction) of three notches over a three-year rating horizon; and a worst-case rating downgrade scenario (defined as the 99th percentile of rating transitions, measured in a negative direction) of four notches over three years. The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Best- and worst-case scenario credit ratings are based on historical performance. For more information about the methodology used to determine sector-specific best- and worst-case scenario credit ratings, visit https://www.fitchratings.com/site/re/10111579

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

ESG CONSIDERATIONS

Unless otherwise disclosed in this section, 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 the entity, either due to their nature or the way in which they are being managed by the entity. For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg

RATING ACTIONS

ENTITY / DEBT	RATING			PRIOR
Cooperatieve Rabobank U.A.	LT IDR	A+ Rating Outlook Stable	Affirmed	A+ Rating Outlook Negative
	ST IDR	F1	Affirmed	F1
	Viability	a+	Affirmed	a+
	Support	WD	Withdrawn	5
	Support Floor	WD	Withdrawn	NF
	DCR	AA-(dcr)	Affirmed	AA-(dcr)
	Government Support	ns	New Rating	
subordinated	LT	BBB	Affirmed	BBB
Senior preferred	LT	AA-	Affirmed	AA-
long-term deposits	LT	AA-	Affirmed	AA-
Senior non-preferred	LT	A+	Affirmed	A+
subordinated	LT	A-	Affirmed	A-
Senior preferred	ST	F1+	Affirmed	F1+

short-term deposits	ST	F1+	Affirmed	F1+

VIEW ADDITIONAL RATING DETAILS

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APPLICABLE CRITERIA

Bank Rating Criteria (pub. 12 Nov 2021) (including rating assumption sensitivity)

ADDITIONAL DISCLOSURES

Dodd-Frank Rating Information Disclosure Form

Solicitation Status

Endorsement Policy

ENDORSEMENT STATUS

Cooperatieve Rabobank U.A.	EU Issued, UK Endorsed

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