ABN AMRO’s Nine-Month 2016 Results

Lower impairment charges and resilient margins

Summary opinion
On 16 November 2016, ABN AMRO Bank (ABN AMRO, A1 stable, baa1)¹ reported a net profit of EUR 1,472 million in the first nine months of 2016 (9M-2016), down 11% compared to the same period in 2015 mainly due to a provision of EUR 271 million (net of tax)² for SME interest rate derivatives³.

Excluding the aforementioned provision, the underlying net result was EUR 1,743 million in 9M-2016, up 5% from the same period in 2015. The bank’s net interest income was up 3% to EUR 4,703 million thanks to resilient interest margins. Net fee and commission income and other income were down to EUR 1,303 million (-5%) and EUR 388 million (-13%) respectively. Operating expenses were up 7% to EUR 3,951 million due to regulatory levies of EUR 134 million and a restructuring charge of EUR 144 million which was booked in Q3 2016. However, these charges were offset by a further decrease of impairment charges in 9M-2016, which were down by 79% to EUR 79 million (or 4 basis points of gross loans), as a result of better economic conditions in the Netherlands.

Overall, we view 9M-2016 results as credit neutral for bondholders.

ABN AMRO’s CET1 fully-loaded ratio continued to improve and stood at 16.6% at end-September 2016 (versus 16.2% as of end-June 2016).

The reduction of the Dutch state’s stakes - announced on 16 November 2016 - in ABN AMRO to 70% from 77% has no credit implication.

The bank’s net interest income was resilient while fee and interest income and other operating income decreased

Net interest income rose 3% to EUR 4,703 million in 9M-2016 compared to 9M-2015. Despite the continued low interest environment, net interest margins remained robust over the period at 151 basis points (146 basis points in 9M-2015), offsetting the negative impact of lower volumes of client loans. Margins on loans (notably mortgages⁴ and corporate loans) and deposits (as the bank continued to reduce interests paid on deposits) have continued to improve in Q3 2016. We nevertheless consider that the room for further improvement in margins will be challenging in view of the competition on both deposits and lending activities.

Net fee and commission income was down to EUR 1,303 million (-5%) in 9M-2016 compared to 9M-2015 as the Private Banking business was negatively affected by volatility in the financial markets. Other income was primarily affected by lower value adjustments.
results as well as lower hedge accounting results and stood at EUR 388 million (-13% compared to 9M-2015).

As a result, operating income was stable at EUR 6,393 million (-0.15%).

**Operating expenses increased due to regulatory levies and restructuring charges**

Operating expenses stood at EUR 3,951 million, up 7% compared to 9M-2015 owing to regulatory levies of EUR 134 million and a restructuring provision of EUR 144 million (booked in Q3 2016) in relation to cost savings measures announced at the end of Q2 2016. The cost-to-income ratio was 61.8% in 9M-2016 versus 57.8% in 9M-2015.

In addition to the cost-savings initiatives announced previously (totaling EUR 0.5 billion) and which are being implemented, the bank has announced further measures this quarter which consist of cost saving action worth EUR 0.4 billion which will help offset the additional EUR 0.9 billion expected increase in costs during 2015-2020. The internal and external staff will be reduced by 13% over the plan horizon (2020). An additional provision of around EUR 150 to EUR 175 million is expected to be booked in Q4 2016.

**Cost of risk decreased substantially**

During 9M-2016, impairment charges decreased significantly, down 79% to EUR 79 million and the cost of risk declined to just 4 basis points of gross loans against 19 basis points in 9M-2015. Indeed, the continued improved domestic economy and housing market led to lower impairment charges and further IBNI (incurred but not identified) provision releases. As of end-September 2016, the impaired ratio slightly increased but remained low at 3.5% (3.4% at end-June 2016).

**Capital position of the bank further improved**

ABN AMRO’s fully-loaded CET1 ratio stood at 16.6% as of end-September 2016 compared to 16.2% as of end-June 2016, well above the current regulatory minimum requirement of 10.25% for 2016 (made up of the bank’s 9.5% SREP requirement and a phased in 0.75% systemic risk buffer). The increase was driven by the increase of the bank’s fully-loaded CET1 capital to EUR 17.5 billion (from EUR 17.2 billion in June 2016) coupled with the decrease in risk-weighted assets to EUR 105.3 billion (from 106.1 billion in June 2016).

The bank also disclosed the preliminary outcome of the Supervisory Review and Evaluation Process (SREP) for 2017. The minimum CET1 regulatory requirement is set at 9%. For 2019, other things being equal, the fully-loaded CET1 requirement is expected to be set at 11.75% which factors in 100% of the buffers (systemic and conservation) while ABN AMRO targets a CET1 ratio of 13.5%.
Moody's Related Research

» Dutch Banks Will Pay for Alleged Derivative Product Mis-selling, a Credit Negative

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Endnotes

1. The bank ratings shown in this report are the bank’s senior unsecured rating and outlook, and baseline credit assessment.


3. This provision was recorded under the caption “special items”. Please also refer to our research on this issue Dutch Banks Will Pay for Alleged Derivative Product Mis-selling, a Credit Negative.

4. As has been the case in previous quarters, the repricing of the mortgage book still results in improved margins, although the impact is expected to level off.

5. Out of which EUR 0.4 billion coming from investments in digitalization, innovation and growth initiatives, and EUR 0.5 billion coming from price inflation and regulatory levies.

6. Subject to change and regulatory approval, ABN AMRO will be required to fulfill in 2017 a CET1 ratio of 9% (4.50% of Pillar 1, 1.75% of Pillar 2 requirement, 1.25% of phased-in Capital Conversation Buffer and 1.50% of phased-in Systemic Risk Buffer). This amount differs from the 10.25% requirement previously imposed to ABN AMRO, due to the new approach adopted by the ECB to determine the SREP level, in particular the distinction between SREP requirement (disclosed) and SREP guidance (undisclosed).
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