Press Release

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Insight beyond the rating.

DBRS Comments on ABN AMRO's 3Q12 Results; Ratings Unchanged, Bank at A (high)

Industry: Fin.Svc.--Banks & Trusts

DBRS, Inc. (DBRS) has today commented that its Issuer & Long-Term Debt Ratings for ABN AMRO Group N.V. (ABN AMRO or the Group) and ABN AMRO Bank N.V. (the Bank), "A" and A (high), respectively, with Stable trends are unchanged following the release of the Group's results for the quarter ending 30 September 2012(3Q12). The trend on all ratings remains Stable. For 3Q12, ABN AMRO reported a net profit of EUR 302 million, 4% higher than in 2Q12. The results include EUR 72 million of separation and integration-related costs. Excluding these costs, ABN AMRO reported an underlying net profit of EUR 374 million, compared to EUR 341 million in the prior quarter.

DBRS views the QoQ improvement in underlying results in the face of a notable contraction in the domestic economy as demonstrating the strength of the ABN AMRO franchise and the resilient earnings power that the Group derives from its franchise. DBRS notes that, despite the challenging conditions in the Netherlands, the loan book has grown 6% since YE11, reflecting higher securities financing volumes, good growth in commercial lending driven by Merchant Banking, while the volume of mortgage lending has remained stable. As expected, given the macroeconomic environment, credit performance weakened in the quarter, with the overall impaired portfolio increasing modestly to EUR 9.0 billion. However, impairment charges declined QoQ to EUR 208 million from EUR 367 million. The reduced impairment charge benefited from a EUR 125 million impairment release related to Greek government-guaranteed corporate exposures and the absence of the large impairment charge for construction, commercial real estate and public sector exposures that occurred in 2Q12. Excluding the impairment release, the impairment charge was EUR 34 million lower QoQ. Continuing weakness in house prices resulted in impairment charges on residential mortgages increasing to EUR 69 million from EUR 47 million in 2Q12. As a result, the cost of credit on the mortgage book increased to a still low 13 bps. Following the sale of a portion of the Greek government-guaranteed corporate exposures in October 2012, the coverage ratio stood at 58.7%, which DBRS views as acceptable given the current conditions. Given the recessionary environment in the Netherlands, DBRS expects credit costs to rise further in 4Q12 and into 2013.

For the quarter, ABN AMRO's operating result (pre-impairment income) was 4% lower QoQ at EUR 740 million, as lower revenues were only partially offset by reduced operating expenses. Importantly,

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ABN AMRO's earnings generation ability allows the Group to absorb the losses associated with the slowing economy and generate organic capital. Indeed, provisions absorbed only 28% of pre-impairment income, down from 48% in 2Q12. Operating income declined 5% on a linked quarter basis to EUR 1.8 billion on a lower release from the credit umbrella and EC remedy provisions compared to 2Q12, while net fee and commission income was broadly stable. Net interest income was rather resilient, declining only 2% QoQ to EUR 1.3 billion, primarily due to the higher cost of the recently issued subordinated notes and the higher funding costs associated with the lengthening of the maturity profile. These pressures on net interest income were partially offset by improved margins on the mortgage and consumer loan books. As a result, the net interest margin when calculated over total assets was 1.17% in 3Q12, 5bps lower than in 2Q12. While DBRS considers the quarterly performance as resilient given the slowing Dutch economy, DBRS is mindful that restoring top line revenue growth in the near-term will be a challenge.

Management's continued focus on cost containment was evident in the quarterly results. Operating expenses were 5% lower QoQ. This decline reflected lower headcount following the divestment of the Group's corporate insurance activities and reduced depreciation and amortisation. As a result, despite the modest reduction in operating income, the underlying cost/income ratio (excluding the impact of separation and integration related costs) was stable QoQ at 59%. Through its "customer excellence" programme, ABN AMRO maintains the goal of lowering its structural cost/income ratio to below 60% by 2014.

ABN AMRO continues to strengthen its balance sheet. Importantly, ABN continues to advance the lengthening of its funding profile to better match the length of loan book and improve the balance between unsecured and secured sources of funding. During the first nine months of 2012, ABN AMRO grew its deposit base by EUR 11.9 billion resulting in the loan-to-deposit ratio improving to 126% from 130%. DBRS sees this performance in a competitive domestic market as demonstrating the strength of the ABN AMRO franchise. Evidencing good access to the markets, ABN AMRO raised EUR 14.1 billion of term funding (excluding subordinated debt) in the nine months to 30 September 2012, including a benchmark transaction of 500 million Chinese Yuan. Of the term funding issued, 65% was senior unsecured notes, 25% in covered bonds, and 11% in RMBS (including LT repos). With the Group having already refinanced all long-term funding maturing in 2012 by April 2012, DBRS sees the EUR 58.1 billion liquidity buffer as conservative.

DBRS views the Group's capital as solid and prudently managed. At 30 September 2012, ABN AMRO's Core Tier 1 ratio stood at 11.4% compared to 10.7% at year-end 2011. The year-to-date increase in the Core Tier 1 ratio primarily reflects the conversion of the Mandatory Convertible Securities (MCS) liability to equity following the settlement of all outstanding litigation with Ageas.

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This benefit was partially offset by higher risk-weighted assets reflecting lending growth and application of the standardized approach to a portion of the Large Corporates portfolio. DBRS notes that 30 September 2012 capital levels exclude 40% of net reported profit, as this is the targeted payout under the Group's dividend policy. In preparation for Basel III/CRD IV, ABN AMRO strengthened its capital base issuing two subordinated notes totaling EUR 2.2 billion of Lower Tier 2 (LT2) capital in 3Q12. These issuances were followed in October with an SGD 1.0 billion LT2 subordinated note issuance.

Notes:
All figures are in EUR unless otherwise noted.

The principal applicable methodology is the Global Methodology for Rating Banks and Banking Organisations. Other methodologies used include the DBRS Criteria – Intrinsic and Support Assessments. Both can be found on the DBRS website under Methodologies.

The sources of information used for this rating include company documents and SNL Financial. DBRS considers the information available to it for the purposes of providing this rating was of satisfactory quality.

This commentary was disclosed to the issuer and no amendments were made following that disclosure.

This credit rating has been issued outside the European Union (EU) and may be used for regulatory purposes by financial institutions in the EU.

This rating is endorsed by DBRS Ratings Limited for use in the European Union.

Lead Analyst: Roger Lister
Approver: Alan G. Reid
Initial Rating Date: 25 June 2010
Most Recent Rating Update: 14 June 2012

For additional information on this rating, please refer to the linking document under Related Research.

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