10 Jul 2020 | Affirmation

Fitch Affirms Van Lanschot Kempen Wealth Management N.V. at 'BBB+'; Outlook Negative

Fitch Ratings-Paris-10 July 2020:

Fitch Ratings has affirmed Van Lanschot Kempen Wealth Management N.V.'s Long--Term Issuer Default Ratings (IDR) at 'BBB+' with a Negative Outlook and Viability Rating (VR) at 'bbb+'. A full list of rating actions is below.

Key Rating Drivers

IDRS AND VR

The ratings are underpinned by adequate franchises in private banking, asset management and merchant banking, and by an asset-light and fairly diverse business model. The ratings also reflect the bank's average asset quality, sound capitalisation and good funding and liquidity profile. They also factor in the inherent market risk embedded in the structured products placed by the bank with its clients, which leads to some earnings volatility.

The Negative Outlook reflects our view that the coronavirus crisis continues to create additional risks to the bank under our updated assessment of various possible downside scenarios to our baseline economic forecast. This primarily reflects our assessment of the group's asset quality (bbb+/Negative) and earnings and profitability (bbb/Negative).

Van Lanschot is a well-established mid-size private bank operating principally in the Netherlands with EUR24.7 billion assets under management (AuM) at end-2019. The bank also has an adequate asset management franchise (EUR62 billion AuM at-end 2019) with a large share of AuM in low margin fiduciary business that results in limited pricing power. Its merchant banking operations mainly provide M&A advisory, equity capital markets and brokerage in the Netherlands, UK, the Nordics, Spain and the US in niche sectors.

The stressed operating environment may challenge the execution of Van Lanschot's strategy focused on AuM growth, and its medium-term profitability targets may be more difficult to achieve. The strategy focuses on strengthening its wealth management franchise through organic and inorganic growth. The bank has demonstrated its ability to expand AuM through a combination of acquisitions and recurrent net new money inflows in both private banking and asset management in recent years.

Management's risk appetite appears moderate. Van Lanschot recorded a material loss related to structured products placed with its clients during 1Q20. The sharp increase in market volatility in March 2020 led to a surge in hedging costs as the bank struggled to timely adjust its hedging positions. Van Lanschot took corrective measures to avoid further losses on structured products, but we believe the bank is still exposed, albeit on a lower scale to one-off losses in case of extreme market volatility.

Van Lanschot's asset quality has gradually improved over the years. However, it is still below that of diversified Dutch commercial banks due to its weak legacy corporate book. The impaired loans ratio reached a 10-year low of 2.8% at end-2019 as a result of the benign operating environment in the Netherlands and continued de-risking of the corporate book. We believe the trend in asset quality will soon turn negative due to the economic fallout from the coronavirus pandemic, with an expected increase in impaired loans, especially from the bank's core SME and legacy corporate exposures.

The bank's profitability is average compared with other private banks and we expect some pressure on revenue. Revenue is mainly fee-based and will remain sensitive to capital market volatility. Net interest income accounted for about 36% of operating income in 2019. It will come under pressure from the lower interest rates and as a result of the wind-down of the higher-margin legacy corporate book. The stabilisation of costs following the completion of the IT investment programme will only partly counterbalance the negative revenue outlook.

Van Lanschot's risk-weighted capitalisation is sound, with a CET1 ratio of 22.8% at end-March 2020. This compares well with peers and larger Dutch banks. The bank has strengthened its capital position over the years, benefiting from the continued deleveraging of its corporate loan book. Our assessment of capital continues to factor in above-average exposure to unreserved impaired loans in relation to capital.

The bank benefits from a large amount of customer deposits that now fully funds its loan book and reflects Van Lanschot's asset light private banking model. The bank's wholesale funding needs have declined in line with the legacy corporate loan book. Liquidity is sound, underpinned by a large buffer of highly liquid assets well in excess of wholesale funding maturities through end-2020.

Van Lanschot's Short-Term IDR of 'F2' is the lower of the two options mapping to a 'BBB+' Long-Term IDR. This is because our 'a-' assessment of the bank's funding and liquidity is below the minimum 'a' expected for a Short-Term IDR of 'F1'.

DEBT RATING

Van Lanschot's long- and short-term senior unsecured debt ratings are at the same level as the bank's IDRs. Fitch believes the default risk of the bank's senior unsecured debt is equivalent to the default risk implied by the IDR since senior unsecured obligations are viewed as having average recovery prospects.

The Tier 2 subordinated debt securities issued by Van Lanschot are rated two notches lower than its VR, reflecting Fitch's baseline notching for loss severity.

SUPPORT RATING AND SUPPORT RATING FLOOR

The Support Rating (SR) and Support Rating Floor (SRF) reflect Fitch's view that Van Lanschot's senior creditors cannot rely on receiving full extraordinary support from the Dutch sovereign if the bank becomes non-viable. This reflects the bank's lack of systemic importance in the Netherlands, as well as the EU's Bank Recovery and Resolution Directive and Single Resolution Mechanism. These provide a framework for resolving banks that is likely to require senior creditors participating in losses, if necessary, instead of or ahead of a bank receiving sovereign support.

RATING SENSITIVITIES

IDRS AND VR

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

The ratings remain sensitive to the ultimate depth and duration of the coronavirus shock to the international economy and financial markets, and the pace of the economic recovery. The ratings could be downgraded if the economic and financial market disruption arising from the pandemic places severe and sustained pressure on the group's asset quality and earnings. We would also downgrade Van Lanschot's ratings if capitalisation weakens significantly due to higher than expected loan impairment charges or large losses on structured products.

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

In the event Van Lanschot withstands ratings pressure arising from the coronavirus outbreak, the most likely trigger for an upgrade would arise from successful implementation of the private banking and asset management strategy. We would expect in particular a sustainable strengthening of the bank's profitability from a track record of steady and sizeable inflows of assets under management. A rating upgrade would also hinge on continued progress in reducing the bank's stock of non-performing corporate loans.

DEBT RATING

The senior unsecured debt ratings are sensitive to changes in the IDRs. The senior unsecured debt may receive a one-notch uplift from the Long-Term IDR if the bank builds up a significant combined buffer of qualifying junior debt and senior non-preferred notes to comply with its future minimum requirement for own funds and eligible liabilities.

The Tier 2 subordinated debt rating is primarily sensitive to the same factors as the VR, from which it is notched.

SR AND SRF

An upgrade of the SR and an upward revision of the SRF are contingent on a positive change in the Netherlands' propensity to support its banks, as well as a significant increase in Van Lanschot's systemic importance. While not impossible, this is highly unlikely in light of the resolution regime in place, in Fitch's view.

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
The highest level of ESG credit relevance, if present, is a score of 3. This means ESG issues are credit-neutral or have only a minimal credit impact on the entity(ies), either due to their nature or to the way in which they are being managed by the entity(ies). For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg.

Van Lanschot Kempen Wealth Management N.V.; Long Term Issuer Default Rating; Affirmed; BBB+; RO:Neg
; Short Term Issuer Default Rating; Affirmed; F2
; Viability Rating; Affirmed; bbb+
; Support Rating; Affirmed; 5
; Support Rating Floor; Affirmed; NF
----senior unsecured; Long Term Rating; Affirmed; BBB+
----subordinated; Long Term Rating; Affirmed; BBB-
----senior unsecured; Short Term Rating; Affirmed; F2

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Additional information is available on www.fitchratings.com

Applicable Criteria

Bank Rating Criteria (pub. 28 Feb 2020) (including rating assumption sensitivity)

Additional Disclosures

Dodd-Frank Rating Information Disclosure Form
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