

ISSUER COMMENT

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Rabobank

Full-Year 2016 Results: Pressure On Revenues, Sizeable Exceptional Items But Low Credit Costs

All figures in this report relate to full year 2016 and comparisons are made to full year 2015, unless otherwise indicated.

Summary Opinion

On 16 February, Rabobank (Aa2/Aa2 negative, a2)¹ reported full year 2016 net income of €2,024 million, down 9% from 2015. Net banking revenues declined because of pressure on net interest income (-4%) and the bank incurred significant negative exceptional items (€1,372 million). Nevertheless net income was resilient thanks to a strong decline in the cost of risk. The cost of risk was only €310 million in 2016 (2015: €1,033 million, 2014: €2,633 million), or 7 basis points (bps) of the average loan book. Rabobank reported a pro forma fully loaded common equity tier 1 (CET1) ratio of 14.3%, post January issuance of Rabobank Certificates, which is slightly above the bank 2020's target (at least 14%).

Rabobank's net banking income decreased to €12,805 million (-2%) due to weaker net interest income generation (-4%), which was only partially compensated by higher fees and commissions (+1%). The sale of parts of the residential mortgage and commercial real estate portfolios, as well as early repayments on mortgages, contributed to a 0.3% reduction of the private sector loan portfolio. Coupled with a decrease in average net interest margins, the reduction of the loan book weighed on the net interest income, which stood at €8,743 million (-4%) in 2016. Although the bank endeavored to reprice new lending both in the retail and commercial segments, the net interest margin decreased by 4 bps², in part due to the higher cost of maintaining the liquidity buffer. Although Rabobank has room for further loan book repricing, we expect pressures on net interest margins to continue in 2017 as the cost of customer deposits can only go marginally lower than is currently the case (Rabobank currently pays 0.25% on its most popular retail savings account).

Rabobank reported - €1,372 million of exceptional items in 2016, which is almost twice the amount of exceptional items recorded in 2015 (€723 million). Exceptional items include a €251 million book profit on the sale of Athlon, a profit of €106 million on the fair value of own debt and hedge accounting, €515 million of restructuring costs, €514 million of provisions for interest rate derivatives compensation and impairment worth €700 million on the stake in Achmea.

Exhibit 1

Impact of exceptional items on operating profit before tax

Source: Rabobank

These exceptional items had an impact of 6 percentage points on Rabobank's cost-to-income ratio at 71% as of year-end 2016³. Excluding these exceptional items, the cost-to-income ratio deteriorated by 1 percentage point year-over-year. The reduction of staff costs (-€265 million) was not sufficient to compensate for weaker net interest income (-€396 million) and higher contribution to bank tax, to the resolution fund and to the deposit guarantee scheme (+€141 million). The current cost-to-income ratio (65%), which excludes exceptional items, is largely above the bank's 2020 internal target of 53%-54%.

Loan impairment charges continued to decrease to a very low level of €310 million (or 7 bps of average loan portfolio) from the already low €1,033 million in 2015 (or 24 bps). Except for leasing activities, all segments reported improvements in the cost of risk. The bank also reported reversals of provisions related to Dutch commercial real estate exposures.

The transitional CET1 ratio stood at 14% at year-end 2016, well above the Supervisory Review and Evaluation Process' minimum CET1 capital requirement of 9% for 2017. The 9% CET1 requirement is the sum of the Pillar 1 requirement of 4.5%, a Pillar 2 requirement of 1.75%, a capital conservation buffer of 1.25% and a systemic risk buffer of 1.5% imposed by the Dutch Central Bank for 2017. On 11 January 2017, Rabobank issued a nominal amount of €1.5 billion Rabobank Certificates, which improved the fully loaded CET1 ratio by 80 bps to 14.3%, above the 2020 target of at least 14%. The total capital ratio already reached the 2020 internal target of at least 25%.

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Endnotes

- [1](#) The ratings shown are the long-term deposit and senior unsecured debt ratings, their outlook and the bank's baseline credit assessment (BCA).
- [2](#) The average net interest margin was 1.29% in 2016, compared to 1.33% in 2015 and 1.35% in 2014.
- [3](#) For consistency reasons, in this report we will only refer to the cost-to-income ratio that includes regulatory levies.

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