



Fitch Affirms Belfius at 'A-'; Outlook Stable

Fitch Ratings-Paris-23 November 2018: Fitch Ratings has affirmed Belfius Bank SA/NV's (Belfius) Long-Term Issuer Default Rating (IDR) at 'A-' and Short-Term IDR at 'F2'. The Outlook on the Long-Term IDR is Stable. Belfius's Viability Rating (VR) has also been affirmed at 'a-'. A full list of rating actions is at the end of this rating action commentary.

KEY RATING DRIVERS

IDRS, VR, DCR AND SENIOR DEBT

Belfius's IDRs and debt ratings reflect sound risk-weighted capital ratios and asset quality, combined with a sound retail funding franchise and satisfactory liquidity profile. Belfius is the third-largest bank in Belgium, with a sound domestic public sector and retail banking franchise, but it remains a challenger in corporate banking. However, the company profile is a rating constraint as its franchise and business model is less diversified than more highly rated regional peers'.

Lending is weighted towards mortgage and public-sector loans, benefiting asset quality overall, although the bank continues to expand its business with corporates. The gross impaired loans ratio was 2.2% at end-June 2018, reflecting the low-risk nature of the retail and public sector loans. Its reserve coverage of slightly below 80% at end-June 2018 compares well with regional peers'. Legacy exposures have been materially reduced and the related credit risk is now in line with Belfius's risk appetite.

The bank still has large derivative exposures outstanding with Dexia, and although fully hedged externally, these will represent an operational burden until fully run down, and the bank might have to amend clearing arrangements if the UK's exit from the European Union results in changed access to clearing houses based in the UK.

Belfius reported a fully loaded common equity Tier 1 (CET1) ratio of 16.3% at end-June 2018, in line with its Fitch Core Capital ratio, a satisfactory level with solid buffer above regulatory requirements. Management has stated a targeted CET1 ratio of 15.5%, which supports our long-term view on capitalisation. Its fully loaded Basel III leverage ratio of 5.9% at end-June 2018 was also satisfactory.

The strategy of Belfius is clear, with a strong focus on leveraging on its banking and insurance model, with further material scope to cross-sell insurance products to its banking customers. Profitability has been improving on good cost controls and revenue initiatives, but remains a rating weakness. We expect the low-risk low-income public sector lending to continue to weigh on earnings, but the improvement in the quality of revenue and stronger contribution from the insurance than in the past should provide resilient earnings generation and offset lower returns than at peers.

Belfius's deposit-driven funding is healthy, with an adjusted loans/deposits ratio at 92% at end-June 2018 as calculated by the bank, if retail bonds are included. Belfius has accessed the capital markets with various types of issuance, including additional Tier 1 notes (AT1) and non-preferred senior notes, in the past year. Liquid assets that are encumbered by their use as collateral for the bank's large derivative book have been reduced partly due to lower notional amounts but also favourable interest rate development. Nevertheless, liquidity is not outstanding for the rating level, resulting in the Short-Term IDR of 'F2', the lower of the two options for an 'A-' Long-Term IDR.

Belfius's Derivative Counterparty Rating (DCR) has been affirmed at the same level as the bank's Long-Term IDR because under Belgian legislation derivative counterparties have no preferential status over other senior obligations in a resolution scenario.

SUPPORT RATING AND SUPPORT RATING FLOOR

The '5' Support Rating and 'No Floor' Support Rating Floor reflect Fitch's view that senior creditors can no longer rely on receiving full extraordinary support from the Belgian sovereign in the event that Belfius becomes non-viable. The EU's Bank Recovery and Resolution Directive (BRRD) and the Single Resolution Mechanism (SRM) for eurozone 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

SUBORDINATED DEBT AND OTHER HYBRID SECURITIES

Subordinated debt and other hybrid capital are all notched down from the bank's VR in accordance with Fitch's assessment of each instrument's respective non-performance and relative loss severity risk profiles, which vary considerably.

Belfius's junior subordinated notes rank below the bank's other subordinated obligations but above Tier 1 debt, and are notched down twice for loss severity.

SUBSIDIARY'S DEBT

Belfius Financing Company is a wholly-owned financing subsidiary of Belfius and its debt ratings are aligned with those of its parent. This is based on Fitch's expectation that Belfius will honour the unconditional and irrevocable guarantee provided to holders of the notes issued by Belfius Funding Company.

RATING SENSITIVITIES

IDRS, VR, DCR AND SENIOR DEBT

Belfius's ratings are primarily sensitive to a deterioration of capitalisation or profitability. A setback to the scaling back of the bank's derivative positions, although not expected, would create negative rating pressure. An upgrade is unlikely given the limited scope of the franchise and business model improvement.

SUPPORT RATING AND SUPPORT RATING FLOOR

An upgrade of Belfius's Support Rating and upward revision of Belfius's Support Rating Floor would be contingent on a positive change in the Belgian sovereign's propensity to support its banks. While not impossible, this is highly unlikely in Fitch's view.

SUBORDINATED DEBT AND OTHER HYBRID SECURITIES

The junior subordinated notes issued by Belfius are sensitive to the same considerations that might affect Belfius's VR.

SUBSIDIARY'S DEBT

As all the debt ratings of Belfius Financing Company are aligned with Belfius's ratings they are sensitive to the same factors that might drive a change in the bank's senior debt ratings.

The rating actions are as follows:

Belfius Bank:

- Long-Term IDR affirmed at 'A-' Outlook Stable
- Short-Term IDR affirmed at 'F2'
- Viability Rating affirmed at 'a-'
- Senior unsecured debt affirmed at 'A-/'F2'
- Junior subordinated notes affirmed at 'BBB'
- Support Rating affirmed at '5'

- Support Rating Floor affirmed at 'No Floor'
- Derivative counterparty rating: affirmed at 'A-(dcr)'

Belfius Financing Company:

- Senior debt affirmed at 'A-'
- Commercial paper affirmed at 'F2'

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Applicable Criteria

Bank Rating Criteria (pub. 12 Oct 2018) (<https://www.fitchratings.com/site/re/10044408>)

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