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Research Update:

Dutch Development Bank FMO 'AAA/A-1+' Ratings Affirmed; Outlook Remains Stable

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Table Of Contents

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Overview

- We equalize our ratings on Nederlandse Financierings-Maatschappij voor Ontwikkelingslanden N.V. (FMO) with the sovereign ratings on The Netherlands, reflecting our opinion that there is an almost certain likelihood that the Dutch government would provide FMO with timely and sufficient extraordinary support in the event of financial distress.
- Consequently, we are affirming our 'AAA/A-1+' ratings on FMO.
- The stable outlook on FMO reflects that on The Netherlands and our expectation that the 1998 agreement with the Dutch state regarding its relationship with FMO will remain in force.

Rating Action

On Nov. 28, 2018, S&P Global Ratings affirmed its 'AAA/A-1+' long- and short-term issuer credit ratings on Dutch development finance institution and government related entity Nederlandse Financierings-Maatschappij voor Ontwikkelingslanden N.V. (FMO). The outlook is stable.

Rationale

We equalize our ratings on FMO with those on The Netherlands (unsolicited, AAA/Stable/A-1+), reflecting our opinion that there is an almost certain likelihood that the Dutch government would provide timely and sufficient extraordinary support to FMO in the event of financial distress.

In accordance with our criteria for government-related entities (GREs), our rating approach factors in our view of FMO's:

- Critical role as the key government vehicle for promoting private-sector growth in developing countries, an important public policy goal in The Netherlands; and
- Integral link with the Dutch government. The ratings reflect the 51% government ownership of and strong support for FMO, based on the government's obligation to maintain FMO's operations, its liquidity injections, and its commitment to preserve FMO's solvency, as well as a track record of such support.

Established in 1970, FMO is a public-private development bank. Its majority shareholder is the Dutch government (51%). The rest of the shares are held by large Dutch banks (42%) and employers' associations, trade unions, and individual investors (7%).

The 1998 agreement between FMO and the government formally codified sovereign support to FMO. The duration of the agreement is indefinite and its termination requires 12 years notice by either party. Under Article 8 (financial security obligation) of the agreement, the government is legally required to enable FMO to meet its obligations, including funding raised in capital markets, on time. The agreement aims to provide financial support so that no situations arise in which FMO is unable to meet certain of its commitments on time. FMO's creditors have no direct recourse to the Dutch government. Instead, the government has an obligation to FMO.

The Netherlands' long-term commitment to, and support of FMO is also demonstrated by the sovereign's obligation in most circumstances to safeguard the company's solvency (Article 7 of the agreement--maintenance obligation). Article 7 states that the Dutch government is committed to covering all losses from operations that cannot be covered by general or specific provisioning and reserves. We understand that although the government does not explicitly guarantee FMO's individual obligations, it views its maintenance guarantee on FMO's operations as equivalent to an explicit guarantee. Discussions are ongoing between the Dutch state and its related entities regarding payment for guarantees. If FMO has to pay for its guarantee from the state, we think it would strengthen the explicit character of the guarantee.

FMO supports business and financial institutions in developing countries by providing capital and skills, which is part of the general policy of The Netherlands' Ministry of Development Cooperation, and therefore qualifies as a strategically important activity. It does so by arranging loans (€4.3 billion outstanding as of June 30, 2018), equity investments (€1.5 billion), guarantees, and other investment promotion activities.

In addition, it manages several off-balance-sheet development funds on behalf of, and at the risk of, the Dutch government. Government funds represented about 15% of FMO's total assets as of end-2017. FMO manages the following government funds that finance high-risk projects in developing countries:

- MASSIF: a fund aiding the development of micro-, small-, and midsized enterprises via financial institutions;
- IDF: long-term financing of funds earmarked for infrastructure projects in low income countries; and
- AEF: a fund financing energy projects.

In 2017, FMO established NedLinx B.V., a 100% subsidiary focusing on financing activities for Dutch small and midsize enterprises investing abroad. NedLinx B.V. integrates FMO's Dutch business activities. In our view, the creation of

NedLinx B.V. strengthens FMO's economic policy role for the Dutch government by supporting Dutch business activities in emerging markets. There are ongoing discussions regarding the transfer of NedLinx B.V.'s activities to a joint venture between FMO and Invest-NL, a new financing institution created by the Dutch government that will become operational in 2019. The institution will consist of a project development arm and an investment arm, and invest in companies and projects that are unable to attract sufficient financing from the market because of the unsecure risk-return or long payback time nature of the investments.

Under FMO's revised dividend policy, the shareholders, including the government, may now take an increased dividend of up to 100% of distributable profit (about 5% of total profit), compared with 40%-60% previously. FMO's 2017 net profits increased significantly to €255 million, from €176 million in 2016, supported by exits from several private equity investments and the loan business' robust performance, despite a decrease in net interest income (€200 million in 2017, down 8% from 2016) as a result of a weaker U.S. dollar. In the first half of 2018, net interest income (€99 million) fell slightly compared with the first half of 2017 (€102 million). Net profit declined to €124 million compared with €156 million in June 2017, still reflecting a rise in the euro-dollar exchange rate. However, 2018 is not fully comparable with previous years due to the implementation of International Financial Reporting Standards 9, because fair value changes in FMO's private equity portfolio must be recorded in the profit and loss account, while previously they were recognized in the available for sale reserve.

In 2014, FMO received its full banking license from De Nederlandsche Bank, the Dutch central bank, further improving its access to the international capital markets and widening its financing options. FMO can now fully benefit from any emergency monetary policy measures that the European Central Bank (ECB) adopts. Moreover, within the ECB's Public Sector Purchase program (PSPP), launched in March 2015, securities issued by FMO became eligible for the Eurosystem's expanded asset purchase at an early stage of the program's implementation. In our view, the inclusion of FMO's securities did not have a significant impact on its already favorable borrowing conditions, partly because only slightly more than a third of the funding portfolio is denominated in euros. Nevertheless, we think that including FMO's securities into the ECB's PSPP benefits its funding options. FMO is subject to the Bank Recovery and Resolution Directive, as implemented under Dutch law, with the competent resolution authority being the Dutch central bank.

We assess FMO's creditworthiness as being linked to that of the sovereign. We do not assess FMO's stand-alone credit profile because we view the likelihood of extraordinary government support as almost certain. As such, we consider that the likelihood of government support is not subject to transition risk.

Outlook

The stable outlook on FMO mirrors that on The Netherlands and reflects our expectation that the 1998 agreement with the Dutch state regarding its support of FMO will remain in force.

In the unlikely case that we were to reassess our view of FMO's integral link with and critical role for the Dutch government, in turn prompting us to adopt a view of a lower probability of extraordinary government support, we could lower our long-term rating on FMO to below that on The Netherlands.

Related Criteria

- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings , April 7, 2017
- General Criteria: Rating Government-Related Entities: Methodology And Assumptions, March 25, 2015
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009

Related Research

- The Netherlands Ratings Affirmed At 'AAA/A-1+'; Outlook Stable, Nov. 16, 2018

Ratings List

Ratings Affirmed

Nederlandse Financierings-Maatschappij voor Ontwikkelingslanden N.V.

Issuer Credit Rating	AAA/Stable/A-1+
Senior Unsecured	AAA

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. Complete ratings information is available to subscribers of RatingsDirect at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column. Alternatively, call one of the following S&P Global Ratings numbers: Client Support Europe (44) 20-7176-7176; London Press Office (44) 20-7176-3605; Paris (33) 1-4420-6708; Frankfurt (49) 69-33-999-225; Stockholm (46) 8-440-5914; or Moscow 7 (495) 783-4009.