



ABNANV 4.75% 04/01/26 (ABNANV)

Intermediate-Term Carry

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Company Background: ABN Amro is a modern, full-service bank serving retail, private and corporate banking clients with a primary focus on the Netherlands and selective operations internationally. The group has presence in countries including France, Germany, Belgium, Luxembourg and the United Kingdom with total assets exceeding EUR 392bn as of September 2018.

Credit Considerations:

Net interest income remained strong. The group's operating income before tax rose 8% YoY to EUR 985mn, driven by net interest income, which grew 4% YoY on the back of a strong Dutch economy while cost-saving programmes and lower impairments improved the cost/income ratio to 52.9% from 56.9% in 3Q17.

For 9M18, the group's operating income before tax declined 10% YoY to EUR 2.6bn due to higher impairment charges and cost of risk (23bps). Excluding impairment charges, operating income grew 6% YoY to EUR 3.1bn, driven by growth in net interest income, which benefitted from corporate loan growth and higher mortgage penalty fees. For FY18, management has reconfirmed the impairment outlook and expects the cost of risk to remain below 25 – 30 bps.

9M18 results on track to meet financial targets. With 9M18 cost/income ratio at 55.3%, the group is on track to meet the 56%-58% target by 2020 and <55% by 2022. Further restructuring charges are expected in 4Q18 with ~50m EUR for existing programmes in Commercial Banking, Retail Banking and I&T. For the next 2 years, interest rates are expected to remain low, which will affect deposit margins and growth prospects. Loan volumes are expected to normalize and grow again after 2020.

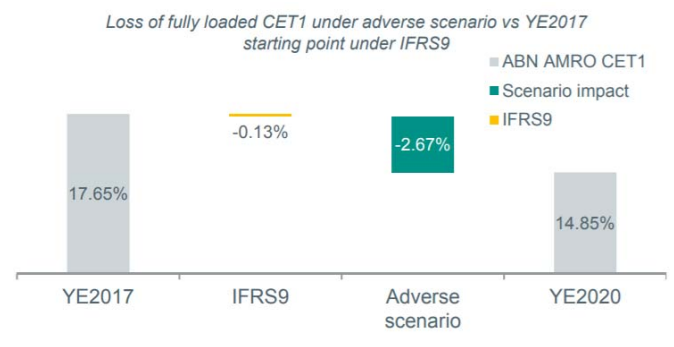
Figure 1: 9M18 Performance vs. Financial Targets

	2017	YTD 2018	Q3 2018	Targets
Return on Equity	14.5% ¹⁾	13.1%	14.4%	10-13%
Cost/Income ratio	60.1% ¹⁾	55.3%	52.9%	56-58% (By 2020)
CET1 ratio (FL)	17.7%	18.6%	18.6%	17.5-18.5% ²⁾ (2018)
Dividend - per share (EUR) - pay-out ratio	1.45 50%	0.65 interest	-	<ul style="list-style-type: none"> 50% of sustainable profit ³⁾ Additional distributions will be considered ³⁾ Combined at least 50%

Source: Company Data, KGI Research

Ample capital adequacy increases the probability of higher dividends for FY18. For 9M18, the group raised its dividend accrual for 2018 to 60% (2017 Target: 50%) after its fully loaded CET1 ratio increased to 18.6% from 17.7% in FY17, higher than management's target range between 17.5% to 18.5% and well in excess of the group's estimates of the 2019 European Central Bank's SREP CET1 requirement of 11.78% (2018: 10.4%), which could be reviewed lower given that the group outperformed its peers with a CET1 impact of -2.67% (Peers -3.6%) in the 2018 European Banking Authority's (EBA) stress test.

Figure 2: Resilience under EBA stress test



Source: Company Data, KGI Research

Credit Recommendations: While ABNANV's 2026 have been rated investment grade by S&P (BBB), Moody's (Baa2) and Fitch (A-), the bond is a subordinated issue which may be subject to mandatory write-down or conversion to equity if the issuer becomes subject to a resolution procedure.

Given the group's solid fundamentals, ample capital adequacy and strong performance in the EBA stress test, we expect ABN Amro's credit outlook to be well supported going forward and we add ABNANV 4.75% 2026 to our defensive portfolio. The bond is currently trading at 102.58 with a YTW of 3.37%.

Additionally, the issue has an optional redemption date on 1 April 2021 and a coupon reset at the 5-year SGD Swap Offer Rate + 271bps on 1 April 2021, which can help to mitigate interest rate risks.

Financials

FYE 31 December

INCOME STATEMENT (EUR mn)	2016A	2017A	9M18A
Net Interest Income	6,267	6,456	4,951
Net Fee and Commission Income	1,810	1,747	1,273
Other Operating Income	150	1,086	711
Operating expenses	(5,657)	(5,581)	(3,837)
Operating Income	2,570	3,708	3,098
Provisions	114	(63)	447
Profit Before Tax	2,456	3,771	2,651
Net Income	1,806	2,791	2,008
BALANCE SHEET (EUR mn)	2016A	2017A	9M18A
Total Assets	394,482	393,171	392,419
Total Customer Loans	266,551	273,666	651,306
Total Allowances	3,666	2,460	2,270
Total NPLs	8,912	6,909	6,059
Total Liabilities	364,848	371,841	371,121
Total Deposits	228,758	236,699	237,518
Total Equity	18,937	21,330	21,298
KEY RATIOS	2016A	2017A	9M18A
Net Interest Margin (%)	1.52	1.57	1.63
Cost/Income Ratio (%)	65.9	60.1	52.9
Loan/Deposit Ratio (%)	117.0	116.1	116.7
Non Performing Loans (%)	3.33	2.51	2.19
Equity/Assets (%)	4.80	5.43	5.43
CET1 (%)	17.00	17.70	18.60
CAR (%)	24.60	21.30	22.30
ROE (%)	11.8	14.5	13.1

Source: Company Data, KGI Research

KGI's Ratings

Rating	Definition
	KGI Securities Research's recommendations are based on an Absolute Return rating system.
BUY	>10% total return over the next 12 months
HOLD	-10% to +10% total return over the next 12 months
SELL	<-10% total return over the next 12 months

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