FitchRatings

RATING ACTION COMMENTARY

Fitch Upgrades Credit Europe Bank to 'BB-'; Outlook Positive

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Fitch Ratings - Milan - 21 Sep 2023: Fitch Ratings has upgraded Credit Europe Bank N.V.'s (CEB) Long-Term Issuer Default Rating (IDR) to 'BB-' from 'B+' and Viability Rating (VR) to 'bb-' from 'b+'. The Outlook on the Long-Term IDR is Positive. A full list of rating actions is below.

The upgrades reflect Fitch's improved assessment of CEB's operating environment due to reduced exposure to emerging markets, which together with tightened underwriting standards has contributed to a gradual de-risking of the bank's balance sheet. The rating actions also consider the bank's improved operating performance and capitalisation.

KEY RATING DRIVERS

Balance Sheet De-risking; Improved Profitability: CEB's niche franchise in commodity trade finance remains a rating strength, despite its business model's limited diversification. Since 2018, CEB has been de-risking its balance sheet by reducing its volume of impaired loans and exposure to some emerging countries, which contributed to improving the bank's profitability. We expect this will feed through to increased internal capital generation, ultimately supporting CEB's capitalisation.

Global Growth Slowing: Fitch expects global growth to decelerate in 2023 to 2.5%, from 2.7% a year earlier. Stubborn inflation, high interest rates, risks from credit tightening, trade restrictions and regulatory challenges will affect both advanced and emerging economies. We expect these factors to result in subdued investments, weak productivity and decreasing international trade, leading to a reduction in merchandise trade.

Niche Trade Finance Bank: CEB has a niche commodity-trade-finance and corporate franchise with diversification into the retail segment in Romania. We expect the bank to continue benefiting from the higher interest rate environment, while the revenue's volatility decreases alongside its exposure to volatile countries, notably Turkiye.

Reduced Risk Appetite: Over the past five years, the bank has adopted a more conservative risk approach by reducing its exposure to cyclical sectors, countries affected by high volatility (e.g. Turkiye), or significant geopolitical developments (e.g. Russia and Ukraine). These measures led to a significant decline in non-performing assets (NPA, which include on and off-balance sheet risks), which we expect to continue in the coming years.

Lower NPA; Improved Coverage: CEB has recently demonstrated satisfactory balance sheet management, although exposure to emerging markets make asset quality potentially volatile. The NPA ratio declined to 4% at end-2022 (from 7.2% at end-2020), helped by tightened underwriting policies and increased lending in developed markets. We expect this ratio to drop further in the next two years. Additionally, the bank materially improved its coverage of NPA.

Improving Medium-term Profitability: CEB's core profitability has been modest in recent years, but improved in 2022 thanks to the increase in net interest income, taking advantage of rising interest rates and lower loan impairment charges. We expect the bank to maintain an operating profit to risk-weighted assets (RWA) of around 2% in 2023 due to persisting high interest rates, steady business flows, good control over costs and NPA, despite the global economic slowdown.

Capital Buffers Improving: Over the past four years, CEB's common equity Tier 1 ratio has consistently exceeded 15% and capital encumbrance materially has decreased, falling below 20%. Although the bank's capital size remains modest in nominal terms, CEB's capital buffers materially increased in July 2023, following the bank's local regulator's decision to reduce its capital requirements.

Moderately Stable Deposit Franchise: CEB is mainly funded through granular retail deposits, which are collected online mostly in Germany, and to a lesser extent the Netherlands and Romania. Almost all household deposits benefit from deposit-guarantee schemes in all three countries, contributing to funding stability. Corporate and interbank deposits are originated from CEB's trade-finance and corporate-banking operations. Wholesale borrowings are limited to one subordinated bond placement.

RATING SENSITIVITIES

Factors that Could, Individually or Collectively, Lead to Negative Rating Action/Downgrade

The ratings would be downgraded if the macroeconomic environment weakens more than we expect, leading to a material asset-quality deterioration (with an NPA ratio increasing over 6%) and weaker operating profitability (operating profit falling below 1% of RWA on a sustained basis).

Factors that Could, Individually or Collectively, Lead to Positive Rating Action/Upgrade

The ratings could be upgraded on broader business diversification, leading to improved internal capital generation by means of a longer record of operating profit at around 1.5% of RWA. In addition, an upgrade would require stable asset quality and capitalisation maintained at current levels.

OTHER DEBT AND ISSUER RATINGS: KEY RATING DRIVERS

CEB's Tier 2 subordinated debt is rated two notches below the bank's VR, reflecting poor recovery prospects for this type of debt.

No Government Support: CEB's Government Support Rating (GSR) of 'ns' reflects Fitch's view that although external extraordinary sovereign support is possible, it cannot be relied on. Senior creditors can no longer expect to receive full extraordinary support from the sovereign in the event that the bank becomes non-viable. This is because the EU's Bank Recovery and Resolution Directive and the Single Resolution Mechanism for eurozone banks provide a framework for resolving banks that requires senior creditors participating in losses, if necessary, instead of or ahead of a bank receiving sovereign support

OTHER DEBT AND ISSUER RATINGS: RATING SENSITIVITIES

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

The subordinated debt rating is primarily sensitive to a downgrade of the VR, from which it is notched. The rating is also sensitive to an adverse change in the notes' notching, which could arise if Fitch changes its assessment of their non-performance relative to the risk captured in the VR.

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

The subordinated debt rating is primarily sensitive to an upgrade of the VR.

An upgrade of the GSR would be contingent on a positive change in the sovereign's propensity to support the bank. In Fitch's view, this is highly unlikely.

VR ADJUSTMENTS

The operating environment score of 'bbb' is below the category-implied score of 'aa' due to the following adjustment reason: international operations (negative).

The capitalisation & leverage score of 'bb' is below the category-implied score of 'bbb' due to the following adjustment reason: size of the capital base (negative).

The funding & liquidity score of 'bb' is below the category-implied score of 'bbb' due to the following adjustment reason: non-deposit funding (negative).

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

Unless otherwise disclosed in this section, the highest level of ESG credit relevance is a score of '3'. This means ESG issues are credit neutral or have only a minimal credit impact on the entity, neither due to their nature or the way in which they are being managed by the entity. For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg.

RATING ACTIONS

ENTITY / DEBT	RATING			PRIOR
Credit Europe Bank N.V.	LT IDR	BB- Rating Outlook Positive	Upgrade	B+ Rating Outlook Stable
	ST IDR	B	Affirmed	B
	Viability	bb-	Upgrade	b+
	Government Support	ns	Affirmed	ns
subordinated	LT	B	Upgrade	B-

VIEW ADDITIONAL RATING DETAILS

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APPLICABLE CRITERIA

Bank Rating Criteria (pub. 01 Sep 2023) (including rating assumption sensitivity)

ADDITIONAL DISCLOSURES

Dodd-Frank Rating Information Disclosure Form

Solicitation Status

Endorsement Policy

ENDORSEMENT STATUS

Credit Europe Bank N.V.	EU Issued, UK Endorsed

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The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Fitch also provides information on best-case rating upgrade scenarios and worst-case rating downgrade scenarios (defined as the 99th percentile of rating transitions, measured in each direction) for international credit ratings, based on historical performance. A simple average across asset classes presents best-case upgrades of 4 notches and worst-case downgrades of 8 notches at the 99th percentile. Sector-specific best- and worst-case scenario credit ratings are listed in more detail at https://www.fitchratings.com/site/re/10238496

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