

RATING ACTION COMMENTARY

Fitch Affirms KBC Group NV at 'A'; Outlook Stable

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Fitch Ratings - Warsaw - 27 Jun 2024: Fitch Ratings has affirmed the Long-Term Issuer Default Ratings (IDR) of KBC Group NV (KBC) at 'A' and KBC Bank NV (KBC Bank) at 'A+'. The Outlooks are Stable. Fitch has also affirmed KBC's and KBC Bank's Viability Ratings (VRs) at 'a'. A full list of rating actions is below.

KEY RATING DRIVERS

Sound Business Profile: KBC's ratings are underpinned by its leading franchises in commercial banking and insurance in Belgium and the Czech Republic, strong and diversified earnings, solid capitalisation, and sound funding and liquidity. The ratings also incorporate KBC's operations in less developed and more volatile operating environments in central and eastern Europe (CEE), despite its conservative risk appetite and sound risk-adjusted profitability.

Ratings Reflect Consolidated Group: We believe that the failure risk of KBC and its main subsidiary KBC Bank (90% of group assets) is substantially the same, given the high integration of insurance and banking operations. KBC is the group's holding company and its VR is equalised with KBC Bank's VR. The group is regulated on a consolidated basis and holding company double leverage is generally maintained at below 120%. Liquidity is managed centrally and the fungibility of capital is high.

Strong Franchise in Core Countries: KBC is one of the largest banking groups in Belgium, market leader in the Czech Republic and has a well-established market footprint in Slovakia, Bulgaria and Hungary. KBC's stable business model is underpinned by insurance and asset management franchises, which provide good cross-selling opportunities and revenue diversification, contributing to the group's strong profitability.

Moderate Risk Appetite: The group's generally conservative risk appetite is supported by the dominance of its fairly low-risk Belgian operations and stability in its Czech operations. Exposure to some CEE countries could lead to potential earnings and asset-

quality volatility but these risks should be contained, given the strong integration of risk controls and credit standards within the group. Prudent management of insurance risks leads to low risk of potential losses in this business segment.

Stable Asset Quality: We expect KBC's impaired loans ratio to be modestly above 2% at end-2024 and end-2025, which compares favourably with those of Belgian peers, in light of material exposure to CEE countries. The bank's ratio has improved materially in the last couple of years due to the sale of its Irish impaired loans and tightened underwriting. The group's large SME and corporate lending poses moderate asset-quality risks.

Robust Earnings Generation: KBC's profitability is a rating strength and compares favourably with that of peers. The group's earnings generation has been resilient even in low interest rate environment due to its sound business and geographic diversification, more moderate reliance on net interest income than Western European peers, integrated bancassurance business model, and sound pricing power in home markets. We expect KBC's operating profit/risk-weighted assets (RWA) to modestly weaken to about 3% in 2024 from 3.4% in 2023 and remain at this level in 2025.

Strong Capital, Solid Buffers: Capitalisation is strong, reflecting robust internal capital generation, and is in line with similarly-rated peers. We expect KBC's fully-loaded common equity Tier 1 (CET1) ratio will remain above 15% in 2024 and 2025, which provides comfortable buffers above its regulatory minimum capital requirements.

Sound Funding and Liquidity: KBC's funding and liquidity profile is a rating strength, underpinned by a stable and diversified retail and SME deposit franchise base that is the main source of funding. We expect the bank's consolidated loans/deposit ratio to remain below 90% in 2024 and 2025. All subsidiaries, except for Slovakia, are self-funded. KBC has good access to wholesale funding markets, upcoming maturities are reasonably balanced and an ample liquidity buffer adequately mitigates refinancing risk.

RATING SENSITIVITIES

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

KBC's and KBC Bank's ratings are mainly sensitive to a substantial and durable deterioration in asset quality, translating into erosion of the bank's profitability and capital generation. This could be signalled by a potential increase in the impaired loans ratio to above 3%, operating profit durably below 3% of RWAs and our expectation that the group's fully-loaded CET1 ratio falls below 14% without prospects of a swift recovery.

An adverse change in KBC's risk appetite could be negative for the ratings, for example, if the contribution of more volatile CEE countries to KBC's earnings grows rapidly, as this could imply an increase in exposure to weaker operating environments.

A potential lowering of the Belgian banks' 'aa-/negative operating environment score would most likely lead to a revision of KBC's own operating environment by one notch to 'a', but the bank's ratings would be unaffected, all else equal.

KBC's ratings could also be downgraded should the holding company's double leverage sustainably rises above 120% without a clear path to reduction, although this is not Fitch's expectation.

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

Upside for KBC's and KBC Bank's ratings would require a stabilisation of the operating environment assessment for Belgian banks and for the group. In this scenario, an upgrade would be contingent on a stronger business profile and a structural improvement in asset-quality and capitalisation metrics while maintaining risk appetite and strong profitability.

OTHER DEBT AND ISSUER RATINGS: KEY RATING DRIVERS

KBC Group and KBC Bank

KBC Bank's Long-Term IDR and long-term senior unsecured debt are rated 'A+', which is one notch above the bank's VR, because Fitch believes the risk of default on senior obligations, as measured by the Long-Term IDR, is lower than the risk of the bank failing, as measured by its VR. The group adopts a single-point-of-entry resolution strategy with bail-in as the preferred resolution tool. KBC is the resolution entity, which meets the group's minimum requirements for own funds and eligible liabilities (MREL). MREL instruments issued by KBC and channelled to KBC Bank rank junior to third-party senior creditors.

KBC's and KBC Bank's Short-Term IDR and short term senior unsecured debt rating of 'F1' is the lower of two options that map to their respective long-term ratings, reflecting our 'a+' assessment of funding and liquidity.

KBC Bank's Derivative Counterparty Rating (DCR) is aligned with its Long-Term IDR because under Belgian legislation, derivative counterparties have no preferential status over other senior obligations in a resolution.

The subordinated Tier 2 debt securities issued by KBC are notched down twice from its VR, reflecting baseline notching for this type of debt under Fitch's criteria.

KBC's additional Tier 1 (AT1) notes are rated four notches below its VR, reflecting poor recoveries of these securities given their deep subordination (two notches) as well as incremental risk of non-performance relative to the VR due to fully discretionary coupons (two notches). Our assessment is based on the bank operating with a CET1 ratio that is comfortably above maximum distributable amount thresholds, and our expectation that this will continue.

KBC IFIMA S.A.

KBC IFIMA S.A.'s senior debt is aligned with KBC Bank's IDRs, as the debt is guaranteed by KBC Bank and we believe that KBC Bank will ensure these obligations are met. Subordinated debt issued by KBC IFIMA S.A. and guaranteed by KBC Bank on a subordinated basis is rated two notches below KBC Bank's VR to reflect poor recovery expectations.

No Government Support: KBC's and KBC Bank's Government Support Ratings (GSRs) of 'no support' reflect Fitch's view that sovereign support for senior creditors of KBC and KBC Bank cannot be relied on given the implementation of the Bank Resolution and Recovery Directive in Belgium.

OTHER DEBT AND ISSUER RATINGS: RATING SENSITIVITIES

KBC Group and KBC Bank

KBC Bank's Long-Term IDR, DCR and debt ratings are sensitive to changes in KBC's VR. In addition, they could be downgraded to the same level as KBC's if Fitch views that resolution buffers channelled into the bank no longer provide protection to creditors in the event of the bank's failure.

KBC's and KBC Bank's short-term senior unsecured debt ratings would be upgraded if their Long-Term IDRs are upgraded to 'AA-' or if their funding and liquidity score is revised up to 'aa-' or above, which is unlikely.

KBC Bank's DCR could also be upgraded in case of a change in legislation giving preference to derivative counterparties over senior obligation in a resolution scenario.

The ratings of KBC's subordinated Tier 2 debt and AT1 notes are sensitive to changes in the VR. The ratings of the additional Tier 1 notes are also sensitive to Fitch's assessment

of their incremental non-performance risk relative to the risk captured in KBC's VR, for instance if capital buffers above requirements become thin.

KBC IFIMA S.A.

The senior debt ratings issued by KBC IFIMA are sensitive to a change in KBC Bank's IDRs. The subordinated Tier 2 notes issued by KBC IFIMA are sensitive to changes to the VR of KBC Bank, which guarantees the notes.

An upgrade of KBC's and KBC Bank's GSRs 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.

VR ADJUSTMENTS

The operating environment score of 'a+' is below the 'aa' implied category score and below the 'aa-' score of domestic Belgian banks due to the following adjustment reason: international operations (negative).

The asset quality score of 'a-' is above the 'bbb' implied category score due to the following adjustment reason: impaired loan formation (positive).

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.

PUBLIC RATINGS WITH CREDIT LINKAGE TO OTHER RATINGS

The ratings of the senior and subordinated debt issued by KBC IFIMA are driven by the ratings of KBC Bank, which guarantees the notes.

ESG CONSIDERATIONS

The highest level of ESG credit relevance is a score of '3', unless otherwise disclosed in this section. A score of '3' means ESG issues are credit-neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. Fitch's ESG Relevance Scores are not inputs in the rating process; they are an observation on the relevance and materiality of ESG factors in the rating decision. For more information on Fitch's ESG Relevance Scores, visit

<https://www.fitchratings.com/topics/esg/products#esg-relevance-scores>.

RATING ACTIONS



ENTITY / DEBT ↕	RATING ↕			PRIOR ↕
KBC Group NV	LT IDR	A Rating Outlook Stable		A Rating Outlook Stable
	Affirmed			
	ST IDR	F1	Affirmed	F1
	Viability	a	Affirmed	a
	Government Support	ns	Affirmed	ns
subordinated	LT	BBB+	Affirmed	BBB+
senior unsecured	LT	A	Affirmed	A
subordinated	LT	BBB-	Affirmed	BBB-
senior unsecured	ST	F1	Affirmed	F1
KBC IFIMA S.A.				
subordinated	LT	BBB+	Affirmed	BBB+

[VIEW ADDITIONAL RATING DETAILS](#)

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APPLICABLE CRITERIA

[Bank Rating Criteria \(pub. 15 Mar 2024\) \(including rating assumption sensitivity\)](#)

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