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Research Update:

Dutch Development Finance Institution FMO 'AA+/A-1+' Ratings Affirmed; Outlook Stable

Primary Credit Analyst:
Marko Mrsnik, Madrid (34) 91-389-6953; marko.mrsnik@standardandpoors.com

Secondary Contact:
Frank Gill, London (44) 20-7176-7129; frank.gill@standardandpoors.com

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Overview

- We believe there is an almost certain likelihood that the Dutch government would provide development finance institution FMO with timely and sufficient extraordinary support if needed.
- Consequently, we are affirming our 'AA+/A-1+' ratings on FMO.
- The stable outlook on FMO reflects that on The Netherlands and our expectation that the support from the Dutch government will continue.

Rating Action

On Nov. 5, 2014, Standard & Poor's Ratings Services affirmed its 'AA+/A-1+' long- and short-term issuer credit ratings on Dutch development finance institution and government-related entity Nederlandse Financierings-Maatschappij voor Ontwikkelingslanden (FMO). The outlook is stable.

Rationale

We equalize our ratings on FMO with those on The Netherlands (unsolicited ratings, AA+/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, 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 sovereign support for FMO, based on the government's maintenance obligation on FMO's operations, its liquidity injections, and its commitment to preserve FMO's solvency, as well as a track record of such support.

The 1998 agreement between FMO and the government formally codified sovereign support to FMO. Under Article 8 of the agreement, the government is legally required to enable FMO to meet its obligations on time by providing liquidity. The duration of the agreement is indefinite and its termination requires 12 years' notice by either party. 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). 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. FMO's creditors have no direct recourse to the Dutch government. Rather, the government's obligation is to FMO.

FMO supports businesses and financial institutions in developing countries by providing capital and skills. It does so by arranging loans (€3.2 billion net loans outstanding on June 30, 2014), equity investments (€996 million), 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: these represented approximately 10% of FMO's total assets at the end of June 2014.

FMO manages the following government funds: financing of Dutch small and midsize enterprises (SMEs) that invest in developing countries; a local currency fund reaching out to SMEs via financial institutions (MASSIF); earmarked funds for infrastructure projects in low-income countries (IDF); a fund financing energy projects (AEF); and capacity development (CD). The latter enables targeted access to know-how, bundled to meet a company's full organizational needs, is financed by the Dutch Minister for Development Cooperation, and stimulates technical cooperation between developing country companies and enterprises in industrialized nations.

The Dutch government allocated an additional €110 million to FMO in 2013, highlighting FMO's importance in achieving government development policy.

FMO's dividend policy has also changed slightly over time. We understand 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. Between 2007 and 2013, FMO retained on average over 97% of its annual profits as capital. At 32%, FMO's leverage ratio is very strong, reflecting high levels of equity on the balance sheet, which illustrates the government's commitment to the organization, as well as FMO's consistent profitability.

FMO's 2013 net profitability declined slightly versus 2012's, to €133 million, mainly due to lower equity investment results because of the complex financial market environment. Net interest income, the most significant component of FMO's revenues--just over 60%--grew slightly in 2013, compared with one year earlier. Nevertheless, in 2014, we expect FMO's operating environment, particularly with regard to income on equity investments, to improve, as reflected in first-half 2014 results standing at €42.9 million for the six months, against €43.4 million in full-year 2013. We expect that FMO's loan growth will remain steady, at about 5%-7% per year, in line with management's expectations, tempered slightly by some deterioration in asset quality (nonperforming loans amount to roughly 4% of total loans).

Given the nature of its business and the high level of equity and mezzanine financing, FMO's financial results are fairly volatile, in our opinion, especially in an uncertain world growth environment. Based on FMO's track record of managing emerging market risks, we expect that the company will remain profitable despite what we consider to be a weakening of current global economic growth conditions. Moreover, in March this year FMO received the full banking license it had applied for from the Dutch Central Bank (DNB), further improving its access to the international capital markets and widening its financing options. FMO can now fully benefit from emergency monetary policy measures that the European Central Bank adopts.

Outlook

The stable outlook on FMO mirrors that on The Netherlands and also reflects our expectation that the 1998 agreement with the Dutch state will remain in force for the foreseeable future.

If we receive new information that would lead us to reassess FMO's integral link with and critical role for the Dutch government, we could lower the long-term rating to below that on The Netherlands.

If we took a positive rating action on The Netherlands, we would take a similar action on FMO, assuming that FMO continues to enjoy an unchanged role and link with the government.

Related Criteria And Research

- Rating Government-Related Entities: Methodology And Assumptions, Dec. 9, 2010

Ratings List

Ratings Affirmed

Nederlandse Financierings-Maatschappij voor Ontwikkelingslanden N.V.

Sovereign Credit Rating	AA+/Stable/A-1+
Senior Unsecured	AA+

Additional Contact:
SovereignAmericas; sovereignamericas@standardandpoors.com

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