NLFI

Report on de Volksbank

June 2021

This is a translation of the original text in Dutch. In case of divergences between the texts, the text of the Dutch version shall prevail.

Introductory summary

In 2016, NLFI issued its first advisory report on de Volksbank's future to the Minister of Finance. As per the request made by the Minister of Finance for the purpose of informing the House of Representatives, NLFI issued interim reports to the Minister in 2017 and 2018 on the points on which de Volksbank had made progress and the points that still required further progress, in which respect the usual preconditions for privatisation were assessed. In 2018, NLFI explained in its second report that it would issue an advice for privatisation or a new progress report in 2019. NLFI then opted for a new type of progress report in 2019, because – briefly summarised– de Volksbank, partly due to the market developments, was not ready yet for privatisation, while NLFI took the view that de Volksbank had opportunities to achieve a better starting position.

> *2019 progress report:*
> *"The analysis in this report shows that, partly due to market developments, de Volksbank's return and intended cost reduction are under pressure. This risk is inherent in de Volksbank's business model under these market conditions. The macroeconomic situation is not expected to improve in the next few years and it may even deteriorate. This makes it a structural challenge in de Volksbank's business model, which may put even greater pressure on the financial results in the next few years while questions also arise regarding any necessary further investments, such as in the area of IT."*

During the period 2019-2021, de Volksbank carried out a strategic reorientation. This was an intensive process within de Volksbank. NLFI explained to the Minister of Finance that a new NLFI report about the situation at de Volksbank would not be useful before the bank had completed the strategic reorientation. De Volksbank subsequently finalised its new strategy and explained it to the market in February 2021. It was de Volksbank that designed this strategy. In line with the restrictions which the Authority for Consumers and Markets (ACM) has imposed on NLFI and the State, NLFI and the Minister of Finance have no control in this area. This does not mean that NLFI was not involved: given its discretion, NLFI maintained a dialogue with de Volksbank and assessed the new strategy from its perspective of shareholder and with a view to advising the Minister of Finance on potential privatisation.

The conclusion of this progress report is that the new strategy contributes to the continuity, the stability and a stronger financial position of de Volksbank. This is why, in NLFI's opinion, it is necessary that the bank implements this new strategy. Even if the government does not opt for privatisation, the implementation of the new strategy is desirable with a view to de Volksbank's position. By improving the bank's position, the new strategy also contributes to a better starting position for privatisation. A successful strategy will give the bank greater discretion to retain its own strategy, including banking with a human touch, in a privatisation scenario. NLFI therefore takes the view that the bank must be given the discretion to implement the new strategy and subsequently demonstrate the success of this strategy to NLFI. Dynamic market conditions may impact this.

The implementation of the new strategy will not result in privatisation on a one on one basis. A multiple of factors impacts privatisation options. As usual, NLFI will continuously monitor whether privatisation is possible, applying the customary criteria.

Finally, NLFI recognises that the Minister of Finance and the House of Representatives will discuss the future of de Volksbank. This progress report will not address the exploratory study by the Ministry of Finance into "the various potential future options" and "the possibilities for safeguarding the bank's social role".[1]

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[1] https://www.rijksoverheid.nl/binaries/rijksoverheid/documenten/kamerstukken/2020/11/30/antwoorden-kamervragen-schriftelijk-overleg-ontwikkelingen-volksbank/antwoorden-kamervragen-schriftelijk-overleg-ontwikkelingen-volksbank.pdf

1. Introduction

NLFI has a statutory task to manage the shares of its participations and to advise the Minister of Finance on the strategy regarding the sale of shares held by the State, as well as to subsequently execute this strategy following a decision by the Minister.[2] The Minister of Finance will decide on de Volksbank's future at some point and, in doing so, will consider all aspects he deems desirable. Based on its statutory task and the objects included in its articles of association, NLFI helps the Minister of Finance make a decision by providing advice.

In conformity with its statutory task and the objects included in its articles of association, NLFI provides advice from a business perspective on the available possibilities for privatisation, without excluding any possibilities in advance. In this context, NLFI considers to what extent the privatisation options effectively available are in the interest of the company and of all de Volksbank's stakeholders. NLFI also considers to what extent the bank can continue executing its strategy. De Volksbank would prefer privatisation to take place in a manner that allows de Volksbank to retain as much as possible its strategic freedom in respect of its defined mission of 'banking with a human touch'. This was the ambition for 2019 at the time of NLFI's 2016 advisory report, partly in view of the options within de Volksbank itself, as translated into its targets, and the market conditions and market developments in 2016. As set out in the 2019 progress report, de Volksbank was unable to realise these objectives in all aspects.

This progress report speaks of a future privatisation and its relationship with the new strategy. This does not affect that NLFI also assesses de Volksbank's affairs separately from such privatisation in the context of its role as shareholder. After all, a future-proof strategy is essential also without looking explicitly at privatisation.

In 2016, NLFI issued its first advice on de Volksbank's future to the Minister of Finance. This advice was prepared following a comprehensive analysis by NLFI and its advisors and after market consultation. On that basis, NLFI explained in its advice that there was a widely supported need at the time for the future strategic position of SNS Bank (currently de Volksbank) to be that of a safe retail bank offering simple, transparent and fairly priced financial products, operating on the basis of an operationally excellent business model and resulting in a competitive dividend yield. In subsequent years, de Volksbank has sought to optimise its compound return by way of what de Volksbank calls the 'Shared Value' strategy, which considers the interests of customers, society, employees and shareholders as a whole. At the time, de Volksbank explained that it expected growth potential and that this would form a basis for a successful long-term strategy.

In summary, NLFI's advice in 2016 was that de Volksbank would be given two to three years to further develop and implement its strategy. Further value creation would allow de Volksbank to work towards a convincing proposition for privatisation. In the words of NLFI's progress report of October 2018: a convincing proposition for privatisation encompasses both a solid long-term view of the future and an acceptable value proposition. In that context, a number of targets or objectives were agreed that de Volksbank would focus on when pursuing its strategy. The status concerning these targets partly guides the analysis as to whether de Volksbank at some point operates with sufficient success and stability to be privatised.

As per the request made by the Minister of Finance for the purpose of informing the House of Representatives, NLFI issued interim reports to the Minister in 2017 and 2018 on the points on which progress had been made and the points that still required further progress, in which respect the preconditions for privatisation were also assessed. In 2018, NLFI explained in its second report that it would issue a recommendation for privatisation or a new progress report in 2019.

[2] As described in more detail in the Trust Office Foundation (Management Financial Institutions) Act (Wet NLFI).

1.1. A backward glance at the 2019 progress report

The 2019 progress report concluded that the results achieved showed that de Volksbank had endeavoured in recent years to reach the targets discussed in 2016 to the greatest possible extent and that its efforts had produced concrete results. De Volksbank succeeded in broadly positioning itself as a safe retail bank offering simple, transparent and fairly priced financial products. However, the market has changed significantly since NLFI's advisory report of 2016. At the time when the 2019 progress report was prepared, not only was the retail market, that is the focus of de Volksbank's business model, undergoing extensive digitisation and change, it was also assumed across the sector that the low interest rates would stay low for the time being ('low for longer'). At the time of the 2019 progress report, expectations were that the macroeconomic situation would not improve and might deteriorate in the next few years. The analysis in the 2019 progress report showed that, partly due to these market developments, de Volksbank's return and intended cost reduction were under pressure. This risk is inherent in de Volksbank's business model under these market conditions. This made it a structural challenge in de Volksbank's business model, which could put even greater pressure on the financial results in the next few years while questions also arose regarding necessary further investments, in particular in the area of IT.

Based on the benchmark at that time, NLFI saw opportunities for de Volksbank at that time to develop a better proposition for privatisation. To the extent that de Volksbank succeeded in doing so, one of the results might be that de Volksbank would have more discretion in pursuing its own strategy in a privatisation scenario.

The 2019 progress report ended with the observation that, depending on the strategic reorientation and the answer to the question whether a more favourable starting position for privatisation could be achieved, NLFI would reflect on de Volksbank's future and report on this to the Minister. This has resulted in the present progress report. Finally, the 2019 progress report contains a number of observations regarding privatisation options. Given the current situation, there is no need to update these observations. Furthermore, the Minister of Finance will give consideration to the theoretical privatisation options in his exploratory study into "the potential future directions".[3]

1.2. Developments since the 2019 progress report

After working on its strategic reorientation for 1.5 years, de Volksbank presented the resulting strategy on 12 February 2021. This strategy is to ensure that de Volksbank migrates to a business model that is future proof (regardless of the prospect of privatisation), in accordance with de Volksbank's principle of 'banking with a human touch', and ultimately provides a good starting position for privatisation. This progress report will address this strategy and discuss its impact on de Volksbank as a company and on future possibilities for privatisation.

De Volksbank sets its own commercial-strategic course on the market. This has been agreed with the ACM for reasons of merger control. However, in that context NLFI does maintain a constructive dialogue with de Volksbank about its corporate strategy, because this strategy has a major impact on the bank's privatisation options.

It must also be pointed out that in 2020 there was unrest within de Volksbank's Board of Directors and less than optimal interaction between the Board of Directors and the Supervisory Board. This was and still is an important concern for the Supervisory Board and the Board of Directors and for NLFI as the shareholder. The Supervisory Board and the Board of Directors, in consultation with NLFI, have taken measures to address the situation. In the autumn of 2020 / beginning of 2021, the external experts Paul Nobelen

[3] See footnote 1

and Gerrard Boot conducted an investigation into the dynamics within de Volksbank's Board of Directors and the interaction between the Board of Directors and the Supervisory Board in the period from January to August 2020. NLFI fulfilled a monitoring role in this investigation. Among other things, the investigators noted "*that the Board of Directors and the Supervisory Board did not always function optimally and that the relationship between the two bodies was not always healthy. Since its nationalisation, the systemic bank (which comprises SNS, Regiobank, ASN and BLG Wonen) operates in an even more complex governance context than before. Although much progress has been made since then to meet the ever-stricter requirements imposed by external regulators (including the European Central Bank) in the areas of compliance and internal operations, there is still a long way to go.*"[4] NLFI believes that de Volksbank's new strategy will help it move towards a more solid future. A more solid future is conditional on a well-functioning Board of Directors and a good relationship between the Board of Directors and the Supervisory Board. De Volksbank is in the process of finding new supervisory directors to fill the vacancies on the Supervisory Board. In addition, de Volksbank is working on an organisational restructuring of its senior management through the introduction of an Executive Committee. De Volksbank maintains dialogue about these changes with NLFI. NLFI will keep the Minister of Finance informed during the process and shall request his approval when a candidate has been selected for the position of Supervisory Board Chair and has been assessed by the regulator DNB/ECB.

Finally, NLFI would like to observe in this section that, based on its task to manage the shares in de Volksbank and based on its task to advise the Minister of Finance on the company's fitness for privatisation, it raises the subject of compliance with the Money Laundering and Terrorist Financing (Prevention) Act (Wwft) in its discussions with de Volksbank. In earlier progress reports, NLFI elaborated on the instruction and penalty which DNB imposed in this context in 2017. The instruction was lifted in 2018. De Volksbank has explained to NLFI that it has followed the public statements on the situation at ING and ABN AMRO with attention and gives express consideration at internal level to compliance with the obligations under the Wwft, on which point it maintains constructive contact with DNB/ECB.

1.3 In conclusion

In assessing whether a participation is ready for privatisation, NLFI, in line with what the Minister of Finance agreed with the House of Representatives, applies the usual conditions for privatisation which it applied in previous years. These concern questions whether: (i) the company in question is ready for privatisation; (ii) the financial sector is stable, and (iii) there is sufficient market interest in the intended transaction. In addition to these preconditions, (iv) the aim is to earn back as much as possible of the capital expenditures. [5]

NLFI would like to observe that there has been no improvement in de Volksbank's financial position in the period since the 2019 progress report, among others due to the

[4] Link (in Dutch): Onafhankelijk onderzoek naar bestuursdynamiek binnen de Volksbank afgerond

[5] Parliamentary Papers, House of Representatives, session year 2010-2011, 28165, no. 117. As the Minister summed it up at the time:
"In summary, I aim to substantially reduce the government interests in the financial sector within the next five years, provided and insofar as the following conditions are fulfilled: 1. The financial sector is stable. There are no longer any doubts about interbank transactions, the quality of the assets held by individual systemic banks and their solidity. 2. The market is ready for the intended transactions. There is adequate absorptive capacity, there is interest in investments in the financial sector and the expected proceeds are in line with that level of interest. 3. The companies concerned are ready for the intended form of sale or divestment. There is a good financial track record, the quality of reporting complies with the demands of the future, the executive board profile matches the strategy that has been determined and there are good prospects of sustained growth in value, particularly in a situation where the company continues as an independent operation. 4. The objective is to recover the total investment in the companies referred to above, plus the costs of capital incurred by the State, as much as possible.
This framework was included in the NLFI advisory report of 2016 and was also assessed every year in the reports on de Volksbank's progress. See NLFI's website for the advisory report and the subsequent reports.

impact on the real economy of the government measures to control Covid-19 and the persistently low interest rates.[6] This means that the conclusion drawn at that time, that the bank is not yet ready for privatisation, still applies today. The new strategy is intended to change this. This will be explained in more detail below.

[6] For more information on the subject of low interest rates and the impact on de Volksbank, see the 2019 progress report and the information set out below.

2. The market

Banks are currently facing a range of challenges and uncertainties. The year 2020 was characterised by Covid-19 and the associated social crisis has continued into 2021. In 2020, this had an impact on the banks through accelerated digitisation, working from home and the very high provisions created for expected credit losses. In addition, the earnings model of (retail) banks has long been under pressure, not only because of the low interest rates but also because of competition from FinTech and BigTech players and other providers in the mortgage market, including insurance companies and pension funds. Pressure is also rising where laws and regulations are concerned. Apart from the capital requirements, banks increasingly have to comply with ESG-related regulations and their gatekeeper role is again in the spotlight. These developments will be briefly explained below.

2.1. The economy

Since March 2020, the economy has been hit hard by the Covid-19 pandemic and by the contact restrictions it entailed. Thanks to financial government measures, supported by the banks, the Netherlands proved to be resilient. GDP shrank by 3.8% in 2020 (2019: 1.7% growth), unemployment among the working population increased slightly to an annual average of 3.8% (2019: 3.4%) and the number of insolvencies fell to the lowest level in 20 years. In the housing market, the number of transactions relative to 2019 rose by 7.7% to 235,511, while the average house price increased by 7.8% compared to the previous year. Despite the low savings interest rates, the Dutch private savings market grew by 6% to EUR 390 billion at year-end 2020.[7]

According to the most recent estimate of the Netherlands Bureau for Economic Policy Analysis (CPB), published on 22 June 2021, the economy is recovering rapidly now that infection numbers are falling and vaccination coverage is increasing. In 2021 and 2022, the economy will grow by more than 3% per year. In 2022, unemployment will be limited to 4.1%. The development of inflation remains an uncertain factor in all scenarios.[8]

DNB's latest Financial Stability Report (spring 2021, published on 26 May) states that the expectations regarding economic recovery remain uncertain, despite the positive outlook. According to DNB, if the virus is brought under control and the economic recovery continues, it is important that the exceptional crisis measures are phased out and that more targeted, supporting transitional measures are taken in order to prevent cliff effects.[9]

2.2. The banking sector

Digitisation

The nature of the banking sector is changing because of the digital transformation of financial services. The coronavirus crisis has speed up this digitisation process. Banks focus on customer interest and customer experience, which entails opportunities as well as risks when viewed from the perspective of digital transformation. The risks include cyber incidents, privacy issues, digital fraud and competition from FinTech and BigTech players. At the same time, digital transformation creates opportunities as well, such as product and service innovation, (better) decision-making based on data analysis, as well as collaboration with FinTechs.

The key points for banks in a digital world are a robust digital infrastructure and the right balance between innovation and consumer protection.

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[7] De Volksbank – 2020 Integrated Annual Review, p.12.
[8] Source (in Dutch): Juniraming 2021 (Centraal Economisch Plan 2021)
[9] Source (in Dutch): DNB – Overzicht Financiële Stabiliteit, voorjaar 2021

Pressure on the earnings model

The traditional earnings model of (retail) banks has long been under pressure, in particular because of the persistently low interest rates. These low interest rates have less impact on banks with a more diversified revenue model. The 'low for longer' interest rates are expected to continue in the coming years. The 2020 annual report of the Dutch Central Bank (DNB) states that, after a number of years in which the major Dutch banks recorded a fairly stable net interest margin, this margin fell by more than 0.1 percentage point in 2020 to 1.4%. The flat interest rate curve has resulted in a strong shift towards long maturities in the mortgage market. In addition, banks are losing mortgage production share to insurers and mortgage funds, which have a competitive advantage where long maturities are concerned.

Not only the income of banks is under pressure, but the costs are as well. The costs that are rising exponentially relate to IT and digitisation and cybercrime, but also to the role of banks as gatekeepers of the financial system, among others, due to the requirements of the Wwft.

In addition, the Covid-19 pandemic forced the banks to create large provisions in 2020 for expected credit losses. Because of the interventions by central banks and regulators, however, such as the provision of liquidity, the spill over effect to the financial sector has been limited until now. Nevertheless, the impact of the pandemic on the banks remains uncertain and depends on economic developments and recovery of the economy. When the government schemes will be phased out, there might be an increase in demand for bank loans, which will have a positive impact on interest income. On the other hand, in a less favourable scenario the outcome may be a greater number of insolvencies and high unemployment, resulting in an increase in credit losses.

Laws and regulations

The demands made of banks by both European and Dutch regulators are changing in several respects. For example, Basel IV imposes new rules for weighting the credit risks (and operational and marketing risks), which will have a major impact on the capital requirements of European banks. Dutch banks will be hit hard because mortgages will be assigned a higher risk weighting. Under Basel IV, Dutch banks will be required from 2028 to maintain extra capital (which will be phased in from 2023) and to further strengthen their capital position. In practice nearly all banks are already doing this and intend to comply with these regulations well before Basel IV is introduced.

ESG

When it comes to sustainability and Environmental, Social & Governance (ESG), the financial sector is impacted by various initiatives entailed by the European Green Deal and the Sustainable Finance Action Plan. The financial sector plays a key role in supporting the transition to a sustainable and climate-neutral economy. As per 10 March 2021, the Sustainable Finance Disclosure Regulation (SFDR) entered into force. This Regulation makes it mandatory to provide transparency on the sustainability of investments. Another example is the introduction of the EU Taxonomy in 2022. The Taxonomy is a classification system specifying what economic activities are sustainable. Banks, too, will have to demonstrate to what extent their portfolio is in line with the Taxonomy.[10] Apart from laws and regulations concerning ESG, also the demand from consumers and other stakeholders for corporate social impact and engagement plays an increasingly emphatic role. This is also visible in the financial sector.

2.3. In conclusion

The course of the aforementioned developments will be decisive for the long-term value creation of banks, with some developments being within the bank's own sphere of influence and others being beyond its control. All these challenges have a lowering effect

[10] See the website of the European Commission for more information about the SFDR and the EU Taxonomy.

on profitability, return on equity and staff capacity, whereby the right priorities must be set.

The above market developments were taken into account in de Volksbank's strategic reorientation and will be addressed in the next chapter.

3. New strategy

De Volksbank is a special bank in the Netherlands. As the only one of the banks classified as ‘major’ in the Netherlands, it focuses primarily on the Dutch retail market of payments, savings and mortgages and has only a small share in the market of insurance, investments and business loans. In addition, de Volksbank uses as starting point its manifest ‘banking with a human touch’.

Early in 2021, de Volksbank published its new strategic plan for 2021-2015, entitled ‘Better for Each Other – from Promise to Impact’ (hereafter: the strategy). The previous strategic plan, ‘Spot On’, covered the period up to and including 2020, and NLFI reported on the progress of this strategy in its 2017-2019 progress reports.

While drawing up the new strategy, de Volksbank identified the external challenges and opportunities and analysed the bank’s current position, with due consideration for the external developments and de Volksbank’s social character. We refer to Chapter 2, ‘The Market’, for an overview of external challenges and opportunities. The analysis of the bank’s current position revealed important strengths, such as a high Net Promoter Score (NPS), customer growth and a good capital position. In addition, the principal points of attention were identified, including low product density (the number of different products per customer), backlog of digital services and limited execution power (due to factors such as limited staff capacity and financial capacity). Based on these analyses, de Volksbank determined its strategy, including (critical) performance indicators and associated targets per stakeholder group. The realisation of these targets will require transformations in the areas of propositions, IT, digitisation and organisation. To the extent that a positive trend becomes visible towards 2025 in the implementation of the strategy and the results achieved, the possibility of de Volksbank being privatised while retaining its own strategy will increase. In this chapter, we will explain the core and the principal aspects of the 2021-2025 strategy. Chapter 4 will discuss the assessment of the strategy.

NLFI will closely monitor the implementation of the strategy and inform the Minister accordingly.

Summary of 2021-2025 strategy

The mission ‘banking with a human touch’ remains the starting point for the strategy, whereby the bank aims to create optimal overall value for customers, society, employees and the shareholder. The bank works from its characteristic and distinguishing basic premises: a strong customer relationship and making a social impact. From there, it defines growth priorities for each brand, which are supported by five transformations. These transformations are necessary in order for de Volksbank to grow into a future-proof bank.

Growth priorities per brand
Apart from bank-wide challenges, de Volksbank also faces brand-specific challenges. As each bank brand has its own service concept (own profiling and specific target groups), it has identified brand-based growth priorities. The purpose of all these brand-based growth priorities is to realise customer growth, generate extra revenue, increase product density and reinforce the customer relationship and social impact.

- **ASN Bank: accelerate as a digital, sustainable bank**

ASN Bank wants to accelerate its success by strengthening its role as a sustainable opinion leader and thereby increase its social impact.

Based on its relevant profiling, ASN expects to increase the number of customers. From the current strong customer relationship (high NPS), ASN intends to enhance product density per customer, and thereby value per customer. It will do so, for example, by offering a greater number of products and propositions and focusing on cross-sell, supported by further digitisation and personalisation towards customer groups.

The increasing by ASN of its social impact has been translated into specific sustainability targets for 2030 in respect of its climate-positive lending and investments, a positive impact on biodiversity and the category 'leadership' in promoting a living wage in the clothing industry.

- **SNS Bank: change by rejuvenating the target group and strengthening the fee-oriented business model**

The growth stategy of SNS is aimed at rejuvenating the target group, with personal growth as the central theme. At SNS, too, greater emphasis will be placed on cross-sell and personalisation of services in order to enhance product density and customer value. In addition, SNS intends to further reinforce the business model by developing and offering fee-related products and services, also from third parties.

From the theme 'personal growth', SNS intends to increase its social impact by reducing obstacles to personal growth in the areas of (1) work and business, (2) living and life, (3) money for now and later. SNS is currently developing new social KPIs which are in line with this tightened strategy.

- **RegioBank: increase commercial fitness**

RegioBank's growth strategy is aimed at extending its target group to financially strong households in villages and towns where small business services are also very relevant.

In addition, the bank will complete the transition to the full franchise formula[11] within the next two years, making the necessary improvements in online service provision for both advisors and customers. RegioBank focuses on enhancing product density and the associated customer value, supported by an extension of the product range for private customers and small businesses.

RegioBank intends to increase its social impact by promoting quality of life in the region. A KPI on this point is still being developed and is expected in the second half of 2021.

- **BLG Wonen: expand by improving distribution range and service**

BLG Wonen seeks to enhance its acquisition capability by intensifying collaboration with chains and service providers in order to realise extra annual mortgage production. It will also focus on faster and transparent service provision to advisors and on enhancing peak capacity at the service centre, with the aim of absorbing peaks in the markets and thus continuously achieving a fair share.

The bank brand wants to increase its social impact by making the housing market more accessible, its social mission statement being 'good homes for everyone'. A KPI for this is currently being developed.

Necessary transformations
In order to realise the growth priorities per bank brand, de Volksbank has formulated five transformations which are to strengthen the business and operating models and make the bank future proof. De Volksbank will invest in these five transformations in the next four years, each transformation as explained below.

1. Digital and omnichannel dialogue
The purpose is to realise a greatly improved customer experience and customer value. The omnichannel strategy has a number of key objectives, such as:

[11] RegioBank seeks to achieve a homogeneous implementation of the full franchise formula, with two aspects taking centre stage: 1) performance dialogue with advisor based on the annual plan, with explicit quantitative and qualitative targets; and 2) improving the services of the RegioBank organisation towards advisors on the basis of the advisor's and customer's expectations.

- Level up digital service provision for customers and advisors, with a seamless switch between device and channel.
- Provide digital access to all application and management processes, so that customers and advisors can easily apply for and use the products online. These processes must be automated at internal level ('Straight Through Processed').
- Offer personalised access to products and services through the use of data, while customers retain control over their data.
- Enable customers to engage in human dialogue, for example through video calls and contact with a personal advisor.
- Facilitate digital access to third-party products and services.

2. Relevant product range, new propositions, small businesses as a new target group

De Volksbank has a high net promoter score (NPS) but low product ownership per customer, because de Volksbank does not offer a full range of products. This is why de Volksbank wants to create added value for the customer and the bank by extending its current product range. Its objectives are as follows:

- Expand traditional financial services for private customers such as loans, insurance and investments.
- Develop products and services in the small business market. In doing so, the bank will concentrate on small businesses with no more than EUR 5 million in turnover and a financing need of no more than EUR 1-2 million. In this context, the focus will be on the sale of corporate mortgages and investments in digitisation of day-to-day banking affairs.
- Develop new fee-based near banking[12] propositions, including third-party products and services. The third-party product range is limited at present.
- Offer existing and new propositions in modular form, which will enable customers to tailor packages to their individual needs and create more opportunities for personalised service provision by the bank.

3. Foundation for customer bank

De Volksbank wants to realise a modular, customer-driven IT landscape with more automated processes. In this context, the bank wants to transform from a product-oriented bank into a customer-oriented bank. This customer bank will have to facilitate modular and personalised service provision in order to enable the previous two transformations. To this end, the current obsolete IT landscape will have to be converted into a modularly organised IT foundation, including automated IT processes. The use of small modular building blocks should lead to the realisation of rapid changes in IT and operational processes.

4. Customer focus

The organisation must become more versatile and customer focused by transforming into an Agile organisation. This should result in, among other things, a better overall customer experience, higher productivity and shorter time-to-market. De Volksbank wants to move towards a new way of working, where agile hubs with multidisciplinary teams form the core. In order to realise this Agile way of working, the bank has drawn up a three-year schedule involving 12 transformation design principles. A couple of design principles form a single way of working, a culture change is a must, risk control from the start and a rapid roll-out in about 12 months. The changes which de Volksbank hopes to have realised after this 12-month period include a flat organisational structure with new positions and roles with clear responsibilities, autonomous teams with facilitating leadership and a KPI-driven environment.

5. Efficient and flexible

De Volksbank aims to achieve higher efficiency through more partnerships and outsourcing (cost flexibilisation) and by using capital and balance sheet in a more targeted manner. This is expected to cut the number of jobs by approximately 400-

[12] Source: website of the Netherlands Bankers Association (NVB). In addition to bank lending, there is a large credit market. Near Banking is a form of alternative lending, with companies lending to each other. In Near Banking, large businesses or institutional investors lend their surplus funds directly to companies that need money.

500 in the coming three years. In parallel, new employees with relevant knowledge and skills will be recruited in the coming years as a result of the growth strategy. The number of jobs involved will depend on the bank's growth rate.

The bank aims to achieve a cost reduction through measures such as by implementation of the Agile way of working, as well as by outsourcing. Despite these cost savings, the projected total costs (excluding the one-off addition to the restructuring provision) will increase in 2021 relative to 2020. This increase is driven primarily by costs associated with the new strategy, such as necessary investments in digitisation.

According to de Volksbank, the future cost basis will decrease because of lower projected regulatory levies and the aforesaid cost savings. This effect will exceed the impact of increasing costs of digitisation, growth initiatives and statutory requirements such as the Wwft. The decreasing costs, in combination with projected higher revenue, will result in an expected improvement of the cost/income ratio.

De Volksbank aims to improve its return on equity through better capital utilisation by means of various actions. For instance, by determining appropriate capital targets for a risk-weighted CET1 capital ratio and an unweighted leverage ratio, or also by determining the best way of utilising or distributing potential surplus capital.

Targets and key performance indicators

For the purpose of monitoring the progress of the strategy, de Volksbank has formulated various targets in the form of key performance indicators (KPIs). Just as in the previous strategy, these are based on the shared-value principle. The KPIs will be explained below, while the table in Appendix 1 presents an overall summary of historical outcomes and targets.

Where the customer stakeholder group is concerned, the NPS remains an important KPI, with a target of +13 in 2025 (2020: +2). In addition, two new KPIs have been defined, being the number of active multi-customers and the customer relationship score. The definition of a multi-customer is 'a customer with a current account and at least one product from another product group, who has at least ten customer-initiated transactions in their current account for three months in a row'. This KPI is more in line with the new strategy, in which de Volksbank aims to increase product density, whereas the old KPI involved reporting based on the number of current account customers. The target value of the customer relationship score developed is currently being determined, although the baseline measurement has already been performed.

Where society is concerned, de Volksbank continues to measure and report in accordance with a climate-neutral balance sheet, with the target for 2025 set at at least 75% (2020: 59%). In line with the social mission of BLG Wonen, a new KPI 'contribution to accessibility of housing market' is being developed at this time.

With regard to the employee stakeholder group, the KPI 'genuine attention for employees' will remain the central point of the strategy, with the target for 2025 being ≥7.5 (2020: 7.9). This KPI is measured since 2019.

The KPIs which de Volksbank aims to achieve and which are monitored for the shareholder will remain the same.

- Where return on equity is concerned, de Volksbank has set the target for 2025 at 8% (2020: 5.1% and 6.1% excluding one-off items).
- The CET1 capital ratio has a 2025 target of ≥19.0 based on fully phased-in Basel IV (2020: 24% pro forma Basel IV).
- The cost/income ratio (operating expenses, including regulatory levies, divided by total income) has a 2025 target of 57-59% (2020: 70.6%).
- As regards the leverage ratio, the ongoing target is ≥ 4.5% (2020: 5.2%).[13]

[13] The 2025 target for the efficiency ratio is inclusive of regulatory levies, whereas the earlier target for 2020 was exclusive of regulatory levies.

- Where the dividend pay-out ratio is concerned, the 2025 target has remained unchanged relative to 2020 and equals the range of 40-60% of net profit (2020: 60%[14]).

See Appendix 1 for the performance indicators (history and targets).

[14] This concerns the proposed dividend for 2020, which will be distributed if the ECB recommendation on dividend distributions allows this.

4. Assessment of new strategy

4.1. Background

In the 2019 progress report, NLFI concluded that de Volksbank's return and intended cost reduction were under pressure. This risk is inherent in de Volksbank's business model under the market conditions at that time. Expectations were that the macroeconomic situation, and in particular the low interest rates, would not improve in the next few years and might even deteriorate. This made it a structural challenge in de Volksbank's business model, which could put even greater pressure on the financial results in the next few years while questions would also arise regarding any necessary further investments, such as in the area of IT.

As appears from Chapter 2, the market conditions have not changed materially in de Volksbank's favour since then while the bank has faced additional points of attention, including the effects on the real economy of the government measures to control Covid-19.

In the 2019 progress report, NLFI expressed the expectation that de Volksbank would have opportunities to achieve a better strategic positioning and thereby a better starting position for privatisation.

4.2. Review

NLFI has developed a financial review framework against which to assess the new strategy. The purpose of this framework is to help NLFI understand the (financial) outcomes of the bank's strategy, objectively assess these outcomes as the shareholder, and answer the question whether the strategy may result in better options in the future for the bank's privatisation. NLFI's assessment of the new strategy focuses on the medium term; it is assumed that the effects of Covid-19 will fade away before long. This assumption is based on the fact that many corona restrictions were eased at the end of June, while the government has indicated that the corona restrictions will be fully phased out in the short term (second half of 2021). However, the impact of Covid-19 was still uncertain at the time of the preparation of this report.

Below is an explanation of NLFI's assessment of de Volksbank's strategy based on the NLFI's financial review framework. Because of its confidential nature, this assessment will be explained below at aggregate level, whereby NLFI will try to be as open as possible.

Criteria applied
Ever since 2016, NLFI finds it important that the strategy considers the interests of all the stakeholders. In its analysis of the strategy, it formulated a number of objectives for 2025 in respect of each stakeholder:

1. Customers:
    a. Identify clear customer segments with a distinctive elaboration of 'banking with a human touch';
    b. Offer competitive, simple and transparent products and services at a fair price;
    c. A safe, stable and reliable bank.

2. Employees:
    a. A convincing strategy with an eye for the long-term perspective and viability of the business model, in order to retain employee commitment and motivation;

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    b. Enable employees to make a meaningful contribution to a successful bank with a clear mission.
3. Society:
    a. Define the bank's measurable impact on society, supplementary to its impact on customers and employees;
    b. Ensure compliance with legislation and prudential supervision rules.
4. Shareholder:
    a. A bank with a solid financial position, stable credit rating and sustainable business model;
    b. Ensure that the strategy does not exclude exit options for the State, and bring about a long-term value proposition for potential future shareholders;
    c. Facilitate attractive growth opportunities by investing in strategic initiatives with a positive business case.

Assessment of criteria applied
The criteria applied by NLFI in respect of **customers** are already partly enshrined in de Volksbank's social objective, such as offering simple and transparent products. Other aspects of the criteria, such as identifying clear customer segments with a distinctive elaboration of 'banking with a human touch', are part of the new strategy and will be worked out in more detail in the next few years. In addition, NLFI is positive about the rising trend in NPS in recent years.

Where **employees** are concerned, de Volksbank measures the KPI Genuine Attention for the employee. As shown in Appendix 1 (performance indicators (history and targets)), the 2020 realisation of Genuine Attention already exceeds the 2025 target. This KPI is in line with the criteria which the NLFI review framework applies in respect of employees. It is important to continue this positive trend, especially in the coming years, during which the new strategy, including the necessary transformations it entails, will trigger changes for employees.

With regard to **society**, de Volksbank already measures the climate neutrality of its balance sheet and is thus well on the way to 100% climate neutrality by 2030. The bank also wants to increase its social impact by making the housing market more accessible. A KPI for this is currently being developed. In addition, de Volksbank has formulated specific social objectives per bank brand, of which NLFI takes a positive view. NLFI's other criterion, ensuring compliance with legislation and prudential supervision rules, is regarded as a hygiene factor for banking activities. NLFI discusses this subject with de Volksbank at regular intervals.

In the area of sustainability and ESG, NLFI expects de Volksbank to improve and achieve its non-financial KPIs and thus works on its long-term value creation. Furthermore, ESG is rapidly and dynamically developing into a licence to operate, because sustainability requirements are increasing due to a growth in laws and regulations, but also because of rising expectations in society. Meeting these requirements and expectations demands an ongoing effort on the bank's part. Because of the bank's present social role, which translates among other things into a high NPS and a climate-neutral balance sheet, NLFI trusts that the bank will continue to meet these requirements and expectations.

In connection with its position as **shareholder**, NLFI has shared a number of specific – quantitative – criteria with de Volksbank concerning NLFI's expectations in respect of the financial targets[15]. The achievement of these financial targets will increase the number of privatisation options and, whereby the chance that de Volksbank will retain its strategic freedom to pursue its social objective will be higher.

[15] Because of the confidential nature of the financial targets set by NLFI and the context of its role as shareholder, these targets are not disclosed in the progress report. Instead, the progress report contains a qualitative assessment.

Although it remains to be seen whether the strategy will result in all criteria being fulfilled within the period 2021-2025, it is clear beforehand that this will pose a considerable challenge. This is due in part to Covid-19 and the low interest rates. Nevertheless, NLFI believes that the strategy is an appropriate choice and that, in pursuing this strategy, the bank will work towards the necessary transformations, such as revenue diversification, flexibilisation of its cost structure and structural improvement of data management, and be mindful of a capital position which is suitable for a bank with a size and risk profile like de Volksbank's.

Although the return on equity is not an exclusion criterion for privatisation, it will affect the proceeds of privatisation and the extent to which de Volksbank will remain able to determine its own strategy.

With regard to the other stakeholder groups (employees, customers and society), de Volksbank uses non-financial (ESG) KPIs which are largely in line with the criteria applied by NLFI.

NLFI would like to point out that the aforementioned transformations are necessary for the bank in order to make the bank's services future proof, irrespective of whether it will be privatised in the future.

4.3. Additional observations

The current strategy is the result of over 1.5 years work by the bank. The Board of Directors takes the view that it is an ambitious but also realistic plan, and that the objectives can be achieved within the period scheduled for that purpose. NLFI finds that de Volksbank, facing challenging market conditions, has drawn up an appropriate strategy with necessary transformations, and that the bank's Board of Directors and employees have embraced its implementation with enthusiasm. As shareholder, NLFI recognises the importance of the transformation which the strategy intends to achieve. By implementing this strategy successfully, de Volksbank will work towards a more solid basis for its future.

An important element of the strategy is the enhancement of product density in order to improve customer loyalty and profitability. De Volksbank is in a good position to achieve this objective because of its high NPS and low baseline of product density per customer. The strategy is not without risk, however: its success greatly depends on revenue growth from strategic initiatives and a very ambitious growth of the net interest income (NII), elements which are determined to a considerable extent by external factors. Some initiatives will have to prove themselves in the future, while other initiatives are well substantiated and promising. The plan requires several years of patience before the (financial) impact of the new strategy becomes visible. Because of the investments which de Volksbank needs to make, the total costs will first go up before they can start to go down. NLFI has discussed with de Volksbank that the bank will have to work hard on this during the next few years in order to realise the better efficiency ratio it has set itself for 2025. In addition, there are growth initiatives which do not materially contribute to a higher financial return, but which the bank regards as valuable to customers. In view of Covid-19, NLFI is sympathetic to the fact that some financial results will be achieved later.

NLFI understands the strategy chosen by de Volksbank but also has concerns about the pace and complexity of its implementation. Simultaneously carrying out a restructuring, catching-up (with regard to the underdevelopment of digital services and limited execution power referred to in Chapter 3) and realising growth plans is a challenging combination. NLFI has agreed with de Volksbank that the implementation risk will be carefully monitored, so that any adjustments required can be made in good time. NLFI supports the intention to increase the flexibility of the cost basis through new initiatives in such a way, that any disappointing revenue developments can be absorbed by cost reductions. For the next few years, de Volksbank foresees a high capital position in comparison with its peers. This decision was prompted primarily by de Volksbank's wish to give substance to its strategy of being a safe and robust bank with sufficient capital buffers that can take a hit, but also by a limited diversified earnings model and the implementation risk of the new strategy. NLFI believes that capital that is not necessary for the realisation of the plans described in the strategy should accrue to the capital provider and should be distributed as soon as this can be done. Such a distribution will also result in improvement of the financial ratios. This will be discussed with the bank in the coming years.

NLFI has agreed with de Volksbank that the bank will explain to NLFI each quarter how it monitored the progress of the implementation of the strategy. NLFI will inform the Minister of Finance.

To the extent that the implementation of this strategy shows good prospects that the envisaged results will be achieved, more concrete steps can be taken towards the (proposed) privatisation of de Volksbank. As one of these steps, de Volksbank and NLFI will together work to a strategy that forms the basis for the equity story. This may have the effect that privatisation will require a further adjustment of the strategy.

The implementation of the new strategy will not result in privatisation on a one onone basis. A multitude of factors (both company-related and market-related) impacts the privatisation options. NLFI will constantly monitor whether privatisation is possible, applying the customary criteria. If a good option for privatisation should materialise before the strategy has been implemented in full (for instance, on the initiative of third parties, such as potential strategic partners), NLFI will advise the Minister about this at that time.

5. Conclusion

In Chapter 2, NLFI concluded that the market developments outlined in this chapter would be decisive for the long-term value creation by banks and by de Volksbank. The developments which NLFI identified in 2019 as challenges for de Volksbank (such as the low interest rates and digitisation) have continued since then. Furthermore, the uncertainty about the short-term effects on the real economy of the government measures in relation to Covid-19 poses an additional challenge for de Volksbank. Like everyone else, NLFI is unable to make any predictions on that point.

Chapter 4 contains an aggregate overview of NLFI's assessment of de Volksbank's new strategy outlined in Chapter 3, based on NLFI's financial review framework. De Volksbank's new strategy has the principle of 'banking with a human touch' as an unchanged starting point. NLFI developed a financial review framework and assessed the strategy against this framework. The purpose of this framework was to help NLFI understand the (financial) outcomes of the bank's strategy, objectively assess these outcomes as the shareholder, and answer the question whether the strategy may result in better options in the future for the bank's privatisation. Based on its assessment, NLFI concludes that, although it remains to be seen whether the strategy will result in all criteria being fulfilled within the period 2021-2025, it is clear beforehand that this will pose a considerable challenge. This is due in part to Covid-19 and the low interest rates. Nevertheless, NLFI believes that the strategy is an appropriate choice and that, in pursuing this strategy, the bank will work towards the necessary transformations. The new strategy contributes to a stronger financial position of de Volksbank. This is why NLFI deems it is necessary that the bank implements this new strategy.

By improving the bank's financial position, the new strategy contributes to a better starting position for privatisation. A successful strategy will give the bank greater discretion to determine and pursue its own strategy, including banking with a human touch, in a privatisation scenario. Even if the government does not opt for privatisation, the implementation of the new strategy is desirable with a view to de Volksbank's financial position.

NLFI therefore takes the view that the bank must be given the discretion to implement this new strategy and subsequently demonstrate to NLFI that this strategy results in success. Dynamic market conditions will play a part in this. As the bank explained to NLFI, it expects that it will take several years before the effects of the implementation of its new strategy will become visible in a structural improvement of the financial results. NLFI concludes that the cost precedes the benefit.

In the coming period, NLFI will get informed on a quarterly basis of the progress in the implementation of the bank's strategy. NLFI will inform the Minister of Finance.

NLFI wants to stress that the implementation of the new strategy will not result in privatisation on a one on one basis. The privatisation options depend on a multitude of factors (both company-related and market-related). As usual, NLFI will constantly monitor whether privatisation is possible, applying the customary criteria. If, for example, a good option for privatisation should materialise before the strategy has been implemented in full (for instance, on the initiative of third parties, such as potential strategic partners), NLFI will advise the Minister about this at that time.

NLFI expects that the next progress report in 2022 will give particular consideration to the progress in the implementation of de Volksbank's strategy and the results of this implementation.

Appendix 1: Performance indicators – history and targets

Below is an overview of performance indicators, including new indicators that were formulated in the 2021-2025 strategy. The table shows the outcomes of the performance indicators over the last four years, as well as the target for 2025.

Table

		2017	2018	2019	2020	Target 2025
Customer	NPS	-3	-1	+0	2	+13
	Number (x 1,000) of current account customers (until 2020)	1,409	1,488	1,568	1,657	N/A
	Number (x 1,000) of active multi-customers (from 2020)	N/A	838	899	949	1,300
Society	Climate-neutral balance sheet	27%	37%	44%	59%	>75%[16]
	Contribution to accessible housing market	N/A	N/A	N/A	N/A	KPI in progress
Employees	eNPS (until 2018)	-2	-20	N/A	N/A	N/A
	Genuine attention (from 2019)	N/A	N/A	7.7	7.9	>7.5
Shareholder	Return on equity	9.1%	7.6%	7.7%	5.1%[17]	8.0%
	Dividend payout ratio	60%	60%	60%	60%[18]	40-60%
Other targets	CET1 capital ratio	34.1%	35.5%	32.6%	31.2%	>19%[19]
	Efficiency ratio (operating expenses, including regulatory levies, divided by total income)	58.7%	63.6%	61.7%	70.6%[20]	57-59%
	Leverage ratio	5.5%	5.5%	5.1%	5.2%	>4.5%

[16] 2030: 100%

[17] After adjustment for one-off items in 2020 (restructuring provision), the return on equity amounted to 6.1% (see, among other things, the 2020 Integrated Annual Review).

[18] This concerns the proposed dividend for 2020, which will be distributed if the ECB recommendation on dividend distributions allows this.

[19] Based on full phasing-in of Basel IV.

[20] After adjustment for one-off items in 2020 (restructuring provision), the efficiency ratio was 65.8%.