

Research Update:

Dutch Social Housing Guarantee Fund WSW Outlook Revised To Stable; 'AAA' Rating Affirmed

July 25, 2019

Overview

- Waarborgfonds Sociale Woningbouw (WSW) has negotiated and received clarity on the financial impact stemming from its guarantee obligations related to the restructuring of two failing housing associations
- WSW has increased its minimal capital requirement level to enhance the resilience of the guarantee system and to reduce its likelihood of calling on government support.
- The risk profile of the Dutch housing sector has improved, decreasing the risk of guarantee calls.
- We are therefore revising our outlook on WSW to stable from negative and affirming our 'AAA' rating.

Rating Action

On July 25, 2019, S&P Global Ratings revised its outlook on Dutch social housing guarantee fund Waarborgfonds Sociale Woningbouw (WSW) to stable from negative. At the same time, we affirmed the 'AAA' long-term issuer credit rating on WSW.

Rationale

We revised the outlook to stable because the guarantee resolution procedures related to restructuring housing associations Humanitas Housing Foundation (SHH) and Woningstichting Geertruidenberg (WSG) have provided some clarity and predictability for WSW's operations.

WSW signed an agreement in January 2019 with SHH and Stichting Woonbron, another housing association, stipulating the transfer of all assets and some liabilities from SHH to Woonbron. Similarly, WSG was split up in the beginning of 2019, and its assets were transferred to other regional housing associations. As part of the resolution process, WSW was able to choose which loans to take over and service for the two entities. To limit the pressure on liquidity, WSW prioritized selecting loan contracts with maturities spread over 30-40 years.

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The total cash flow arising from the guarantee claims related to both housing associations will amount to around €15 million annually in the next five years. WSW does not foresee any additional guarantee calls in the near future, partly owing to the improvement in the overall risk profile of the Dutch housing sector and the effects of the Housing Act changes now being finalized.

To enhance the resilience and financial strength of the guarantee system, WSW has reached an agreement with its key stakeholders to increase the minimal capital requirement to 0.65% of outstanding guaranteed debt from 0.25%. Currently, the capital level is at 0.67%. Since WSW forecasts a decrease in risk capital because of guarantee claims in the coming years, the capital needed to reach and maintain the 0.65% level requires contributions by the participants from 2020. To date, WSW has received no formal objections from any participating housing associations and no indication of unwillingness or inability to pay additional contributions. WSW initiated the decision to increase the minimal risk capital but it is also supported by the government and other stakeholders.

We also expect WSW to establish a credit facility with BNG and NWB, two promotional banks, to further strengthen the support from its participants. The arrangement is structured so that the housing associations can borrow in their own names but the funds are earmarked to be used by WSW to fulfill any potential capital requirements. For WSW, having access to additional back-up funds reduces the liquidity risk by not having to rely solely on liquidating parts of its investment portfolio if guarantees are called upon.

The objective of the investment portfolio, currently amounting to €529 million, is to sustain WSW's capital, accounting for inflation, by investing in highly rated bonds. WSW's investment policies strictly regulate which assets the organization can invest in, along with maximum holding caps based on asset risks. The maximum holding per issuer is 10%, except for sovereign debt issued by eurozone countries. As of mid-2019, the portfolio comprises AAA-rated bonds (44%) and AA-rated bonds (56%). The investment portfolio is currently valued at 0.66% of total guaranteed debt.

The ambition to increase the robustness of the guarantee system primarily stems from the revised Housing Act implemented in 2015. Rather than providing financial backing to housing association entities, the central government resolution fund will, under the revised law, provide support only to activities considered vital to the general economic interests. As a result of the amendment, WSG was only granted partial resolution support in the restructuring process. This decision implied that the residual support had to come from WSW, since it guarantees the loans of the housing association, resulting in the first ever guarantee calls in the history of WSW.

WSW continues to engage in vertical supervision in collaboration with the Dutch Authority for Housing Associations. The framework is structured to uphold uniform and transparent oversight of the housing associations to ensure satisfactory sector standards. The agreement signed with the authority in 2018 specifies that WSW should be concerned primarily with the business model of the housing associations, whereas the authority should oversee their governance. A new assessment framework was introduced in January of 2019, and the criteria will be finalized during the year. The arrangement will increase the strength of the risk framework by ensuring that the supervision process is more robust and that communication between WSW and the authority is efficient.

Vestia, the housing association to which WSW has the largest exposure, underwent restructuring in 2018. However, WSW's has so far not needed to provide any support, and the current view is that Vestia's financial position is sufficiently resilient to service its debt obligations in the coming years. The analysis is supported by Vestia's forecast on cash flow from operations, which points to sufficient cash flow generation to cover ongoing debt repayments.

Our current assessment of WSW's creditworthiness incorporates the three layers of support to

withstand guarantee claims from the participating housing associations.

The first line of support comprises WSW's own risk capital, which is intended to cover any guarantee claims under normal circumstances.

The next layer constitutes the participants' committed capital. Currently, each housing association is obliged to pay up to 3.85% of the value of outstanding guaranteed debt if WSW's capital is insufficient to pay guarantee claims. In December 2018, this sum amounted to €3 billion. WSW and key stakeholders have also agreed in principle to secure the callable capital with a committed loan from one of the Dutch promotional banks, and have the scope to call for additional capital, subject to a maximum annual amount.

As a last resort, WSW has a backstop agreement with the central government and local authorities. This support materializes if the risk capital falls below 0.25% of guaranteed debt, in which case the arrangement gives WSW unlimited access to interest-free loans. Under the terms of the backstop agreement, there can be at most a 75-day delay between a request to the central government and municipalities for capital, and the funds becoming available. However, we understand from the government that these funds will be made available in a timely manner. WSW's decision to increase the minimal risk capital to 0.65% for its participants reduces the risk of WSW's risk capital falling below 0.25% and thereby also reduces the likelihood of the backstop mechanism being triggered.

The last tier of support is a key factor behind our view of an almost certain likelihood of WSW receiving extraordinary support from the government of Netherlands. We do not consider the financial issues experienced by SHH and WSG as systematic, and we believe that WSW's risk capital and participant contributions will be enough to cover any potential guarantee calls in the next few years.

Our opinion of an almost certain likelihood of government support reflects our assessment of WSW's:

- Critical public policy role for the government, based on our view that its main purpose is to indirectly provide a key public service by keeping the funding costs of social housing associations at a minimum. WSW is a not-for-profit private foundation that guarantees loans provided by lenders to Dutch social housing associations; and
- Integral link with the Dutch government. We view WSW as having a special public status, given the government's ultimate responsibility for ensuring that WSW can meet its obligations. While we believe a default of WSW would not necessarily impair market access for the Dutch government, it could have a detrimental effect on the reputation and market access of housing associations, sector banks and entities similar to WSW (Waarborgfondsen voor de Zorgsector for instance), and their access to public-sector funding in general.

Outlook

The stable outlook reflects that on Netherlands and our expectations that recently established and enhanced mechanisms will ensure sufficient buffers in WSW's operations. The outlook further assumes we see no weakening in WSW's importance or relationship with the Dutch government.

Downside scenario

We could lower the rating by one or several notches if we observe a delay in the support from WSW's members or the government, leading us to conclude that WSW's role for or link with the

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central government had weakened. Significant further losses or systematic stress in the Dutch social housing sector could also put pressure on our rating if WSW's callable capital appeared insufficient, and no additional support from the state were forthcoming.

Related Criteria

- General Criteria: Rating Government-Related Entities: Methodology And Assumptions, March 25, 2015
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009

Related Research

- Summary: Netherlands, May 17, 2019

Ratings List

Ratings Affirmed; CreditWatch/Outlook Action

	To	From
Waarborgfonds Sociale Woningbouw		
Issuer Credit Rating	AAA/Stable/--	AAA/Negative/--

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. Complete ratings information is available to subscribers of RatingsDirect at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column. Alternatively, call one of the following S&P Global Ratings numbers: Client Support Europe (44) 20-7176-7176; London Press Office (44) 20-7176-3605; Paris (33) 1-4420-6708; Frankfurt (49) 69-33-999-225; Stockholm (46) 8-440-5914; or Moscow 7 (495) 783-4009.

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