Creditreform Bank Rating

KBC Group NV

Creditreform Rating

Rating Object	Rating Information
KBC Group NV	Long Term Issuer Rating / Outlook: **A+ / stable** — Short Term: **L2**
Creditreform ID: 0403227515 Management: Johan Thijs (CEO), Luc Popelier (CFO)	Type: Update / Unsolicited
Rating Date: **01 October 2021** Monitoring until: withdrawal of the rating Rating Methodology: CRA "Bank Ratings v.3.0" CRA "Rating of Bank Capital and Unsecured Debt Instruments v.2.0" CRA "Environmental, Social and Governance Score for Banks v.1.0" CRA "Rating Criteria and Definitions v.1.3" Rating History: www.creditreform-rating.de	Rating of Bank Capital and Unsecured Debt Instruments: Preferred Senior Unsecured: - Non-Preferred Senior Unsecured: A Tier 2: BBB+ Additional Tier 1: BBB-

Contents

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Key Rating Driver

+ Diversified business model, by business activities and by geography
+ One of largest financial institutions in Belgium
+ Strong capitalization
+ Sound and stable earnings figures, despite significant impairment charges, which are likely lead to reversals in 2021
+ Continued growth and business expansion in East ern Europe

+/- Digital transformation of the banking business

+/- High proportion of operating income in Belgium

- High dependency on Interest income amid a low interest environment, which puts significant pressure on profitability
- Significant stage 2 exposure and exposure affected to loan payment deferrals

Executive Summary

Creditreform Rating upgrades the unsolicited long-term issuer rating of KBC Group NV to "A+" from "A" and increases the outlook to stable from negative. The upgrade of the outlook is the result of the only minor impact of the Corona crisis on KBC's business, contrary to our expectations of last year. In addition, we expect KBC already in 2021 to regain its convincing pre-Corona level of profitability. The upgrade of the credit rating is among others a result of our change in methodology. Moreover, KBC benefits from its strong bank insurance business and its significant market shares in developed and developing countries. Furthermore, KBC increased its capitalization further, but risks may arise from the significant potential problem loans (stage 2) exposure. Uncertainties exist due to the withdrawal from Ireland, whereby the withdrawal will likely have a positive impact on the banks asset quality.

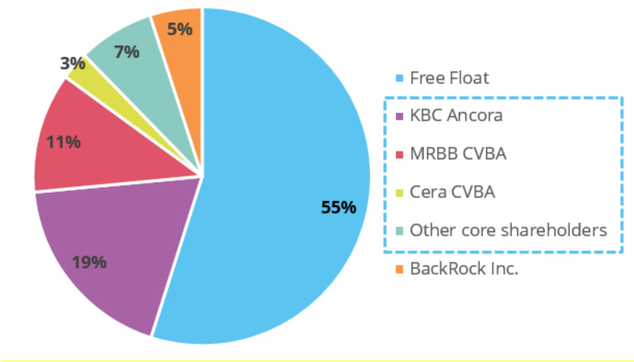
Company Overview

KBC Group NV (hereafter: KBC) is an integrated bank insurance group created in 1998 by the merger of two Belgian banks (Kredietbank and CERA Bank) and a Belgian insurance company (ABB Insurance) with headquarters in Brussels. The Group is a non-operating holding company of its insurance and banking activities and is the single point of entry in a resolution case for the Group. KBC's most significant asset is its bank KBC Bank NV (€284bn assets). With 37.696 employees (FTE's in 2020) and about 1,265 bank branches, KBC serves approximately 12 million customers and had total assets of €320 billion in 2020.

KBC acts as a bank insurance group in its core markets Belgium, Bulgaria, the Czech Republic, Hungary, Ireland and Slovakia. In addition, KBC is represented to a limited extent in several other countries in order to support its corporate clients. The focus of the Group is the retail and private banking business, as well as business activities with small and medium sized enterprises and mid-cap clients. The Group is divided into three business units and the *Group Centre*. The Group's *Belgium Business Unit* includes all activities such as banking business, insurance business and the asset management business in Belgium, whereas the *Czech Republic Business Unit* includes all of the Group's activities in the Czech Republic. By contrast, the *International Markets Business Unit* comprises the Group's activities in Ireland, Hungary, Slovakia and Bulgaria. KBC's *Group Centre*, however, comprises the Group's capital and liquidity management, as well as the funding of the Group and other administrative and holding activities.

The shareholder structure of KBC is as follows:

Chart 1: Shareholder structure of KBC as of half-year 2021. | Source: Own presentation based on data of Half-year report 2021 of KBC

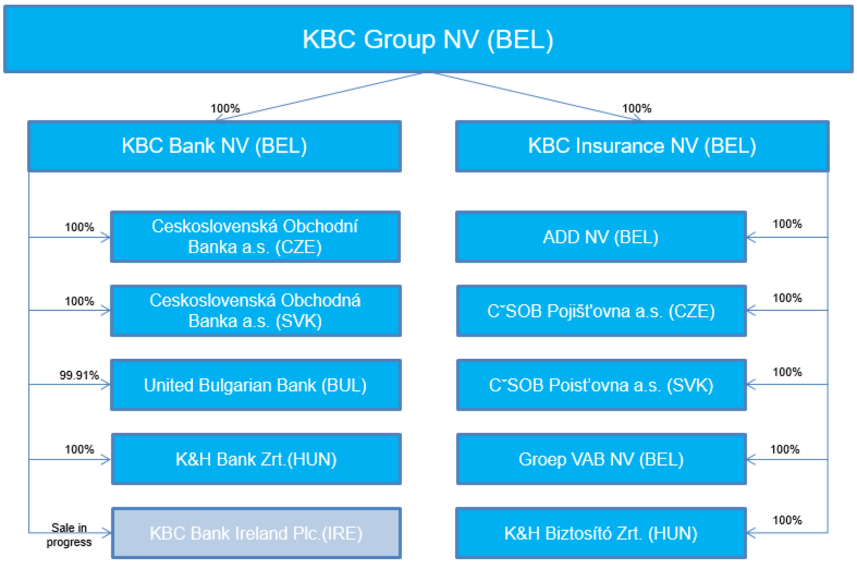


The shareholders of KBC are composed of 40% core shareholders (KBC Ancora, MRBB, Cera and other core shareholders) and 60% free float, whereby BlackRock Inc. is the most significant shareholder among the non-core shareholders. KBC concluded a shareholder agreement between these core shareholders in order to ensure shareholder stability and guarantee continuity within the Group, as well as to support and coordinate its general policy. KBC's core shareholders act in concert at the General Meeting of the Group and are represented on its Board.

Recent changes in the Group structure are as follows: KBC acquired 99.44% of the shares of OTP Banka Slovensko (SVK) at the end of 2020 (fully consolidated from 1 January 2021) and all of the shares of NN's Bulgarian pension and life insurance businesses at the beginning of 2021. Moreover, KBC Bank Ireland entered into a Memorandum of Understanding (MoU) with Bank of Ireland Group in April 2021 already. Thereby Bank of Ireland Group intends to acquire substantially all of KBC Bank Ireland's performing assets and liabilities. The remaining non-performing mortgage loan portfolio of KBC Ireland, which are not part of the MoU, are sold to funds managed by US private equity company CarVal as announced in August 2021. The execution of these two transactions would ultimately result in KBC Group's withdrawal from the Irish market. Moreover, KBC intends to develop to a so-called "Clean HoldCo" until 2024 in order to ensure that KBC's HoldCo senior debt is eligible for the subordinated MREL target. Moreover, at the end of May 2019, CSOB Bank (KBC subsidiary in Czech Republic) closed the acquisition of the remaining 45% stake in the Czech building savings bank CMSS (total assets of about €5.5bn) and owns now 100% of the bank. Since then, CMSS has been fully consolidated in the financial statements of KBC.

The main subsidiaries and investments of KBC can be found in the following Chart 2:

Chart 2: Main subsidiaries and investments of KBC at year-end 2020| Source: Own presentation based on data of Annual Report 2020 of KBC



Business Development

Profitability

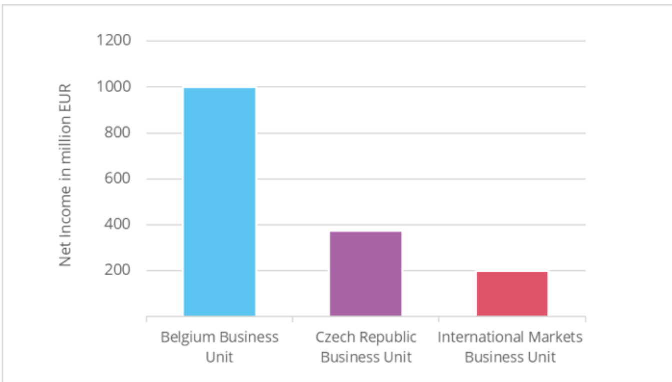
KBC's operating income amounted to €7.2 billion in 2020, reaching the lowest result in the past 5 years. Net interest income was the main driver of decrease in KBC's operating income (€-151 million YOY) but represents still KBC's major source of income. This decrease is primarily attributed to the Czech Republic business unit (€-265mn) and is mostly a result of interest-rate cuts by the Czech Central Bank and the depreciation of the Czech Koruna against the Euro in addition to overall lower reinvestment yields of KBC. This development could only be partially compensated by the positive effect of a larger loan and bond portfolio, higher margins on new home loans and the effect of TLTRO III in 2020. As of June 2021, KBC records a further decline of its net interest income, which indicates the strong pressure of the low interest rate environment on the bank's margins. However, KBC intensifies the charging of negative interest rates at its customers to counteract this development and benefits from the appreciation of the Czech Koruna. Net fee and commission income accounted for 22.4% of operating income, decreasing by about 7.2% YOY. The decrease was primarily attributable to a decline in fees for asset management services, a reduction in fees for banking services (incl. payments, which were down due to the lockdowns, and for loans, the effect of which was only partly offset by higher securities fees) as well as due to the depreciation of the Czech Koruna against the Euro. As of June 2021, KBC was able to counteract the negative development of 2020. Net insurance income (technical) contributed the lowest share of the three main drivers to the operating income, but increased significantly year-over-year due to lower claims during lockdowns in 2020. In this regard, KBC's non-life insurance division is generating almost the entire insurance income with about €847mn. As of June 2021, KBC is able to increase its insurance result, but the flood disaster in Belgium will have a negative impact (approximately about €41mn). Net trading income contributed an insignificant amount to the operating income with about €45mn, and even decreased strongly YOY. The decrease is mainly a result of lower fair values of derivatives used for asset/liability management purposes and a lower result from shares, which is expected to rebound in 2021 already.

Operating expenses amounted to €4.2 billion in 2020, decreasing slightly by 2% in a year-over-year comparison (€83 million). Personnel expenses accounted for 55% of operating expenses, decreasing slightly mainly due to the reduction in workforce. In general, the slight decrease in operating expense is reflected in a number of items directly affected by the Corona pandemic, including lower expenses for facility services, marketing, events, travel and professional fees, in addition to reduced software expenses (owing to the changed rules for software depreciation) and the depreciation of the Czech Koruna and Hungarian Forint against the Euro. These items more than offset the negative impact of increased wages, higher IT costs and the changes in the scope of consolidation, among other things. In addition, KBC faced higher bank taxes in 2020 (€501mn vs €491mn in 2019). As of June 2021, KBC reported stable operating expenses leaving out one-offs as the Covid-attributed bonus awarded to staff and the consolidation of OTP Banka Slovensko. Overall, KBC's development of its operating expenses indicate a sound cost management.

KBC's pre-impairment profit decreased to about €3 billion in 2020. However, significant cost of risk burdened the result. Following large loan loss impairments of about €1.074bn (of which €783mn collective impairment; stage 1: €44mn, stage 2: €724mn, stage 3: €302mn; €654mn in Belgium, €210mn in Czech Republic) due to the Corona pandemic, KBC's net result decreased YOY significantly to only €1.4bn. However, this development is in line with other large European banks. In addition, due to the fast, worldwide recovery of the economies in 2021, a significant reversal of impairments is expected, which will likely boost the net profit in 2021. As of June 2021, KBC already reported net reversals of €206mn but expects to reach cost of risk of zero bp. Moreover, we expect KBC to reverse back to its natural, low level of impairment charges from 2022 on.

Chart 3 shows the contribution of each business unit of KBC to the Group's net profit in 2020.

Chart 3: Net profit of each operating business unit of KBC in 2020| Source: Own presentation based on data of Annual Report 2020 of KBC



A detailed group income statement for the years of 2017 through 2020 can be found in Figure 1 below:

Figure 1: Group income statement | Source: eValueRate / CRA

Income Statement (EUR m)	2020	%	2019	2018	2017
Income					
Net Interest Income	4.467	-3,3	4.618	4.543	4.121
Net Fee & Commission Income	1.610	-7,2	1.735	1.719	1.707
Net Insurance Income	855	+18,1	724	701	640
Net Trading Income	45	-78,6	210	254	1.055
Equity Accounted Results	-11	< -100	7	16	11
Dividends from Equity Instruments	52	-36,6	82	82	63
Other Income	167	-35,8	260	213	116
Operating Income	**7.185**	**-5,9**	**7.636**	**7.528**	**7.713**
Expense					
Depreciation and Amortisation	382	+6,1	360	325	311
Personnel Expense	2.329	-1,2	2.357	2.343	2.303
Tech & Communications Expense	-	-	-	-	-
Marketing and Promotion Expense	-	-	-	-	-
Other Provisions	-	-	-	-	-
Other Expense	1.518	-4,8	1.595	1.612	1.505
Operating Expense	**4.229**	**-1,9**	**4.312**	**4.280**	**4.119**
Operating Profit & Impairment					
Pre-impairment Operating Profit	**2.956**	**-11,1**	**3.324**	**3.248**	**3.594**
Asset Writedowns	1.109	> +100	208	-62	-74
Net Income					
Non-Recurring Income	-	-	-	-	-
Non-Recurring Expense	-	-	-	-	-
Pre-tax Profit	**1.847**	**-40,7**	**3.116**	**3.310**	**3.668**
Income Tax Expense	407	-35,1	627	740	1.093
Discontinued Operations	-	-	-	-	-
Net Profit	**1.440**	**-42,1**	**2.489**	**2.570**	**2.575**
Attributable to minority interest (non-controlling interest)	-	-	-	-	-
Attributable to owners of the parent	1.440	-42,1	2.489	2.570	2.575

Due to the decrease of KBC's net profit in 2020, almost all of the Group's earnings figures worsened but still reached a satisfying level.

KBC's figures of ROA, RORWA and ROE before and after taxes lowered from an outstanding level to an average level YOY. However, as the Corona pandemic impact did not materialize as expected and significant reversals of impairments are likely, we are confident that the bank will reach its outstanding level of profitability in 2021 already. The Group's distinctly benefits from its diversified business model with its profitable activities in Eastern Europe, despite the negative impact of depreciations against the Euro. In particular, the negative impact of the depreciation of the Czech Koruna is already almost compensated. KBC's intrinsic profitability, which is indicated by the cost to income ratios, remained at a convincing level despite the reduction in operating income. In this regard, KBC is clearly ahead of other large European banks. KBC's net interest margin affirms the bank's sound level of profitability. Overall, despite the Corona impact and the significant impairment charges, KBC's earnings figures are still the best performers in any of the areas analyzed.

A detailed overview of the income ratios for the years of 2017 through 2020 can be found in Figure 2 below:

Figure 2: Group key earnings figures| Source: eValueRate / CRA

Income Ratios (%)	2020	%	2019	2018	2017
Cost Income Ratio (CIR)	58,86	+2,39	56,47	56,85	53,40
Cost Income Ratio ex. Trading (CIRex)	59,23	+1,16	58,07	58,84	61,87
Return on Assets (ROA)	0,45	-0,41	0,86	0,91	0,88
Return on Equity (ROE)	6,69	-5,62	12,31	13,09	13,69
Return on Assets before Taxes (ROAbT)	0,58	-0,50	1,07	1,17	1,25
Return on Equity before Taxes (ROEbT)	8,58	-6,83	15,41	16,86	19,51
Return on Risk-Weighted Assets (RORWA)	1,41	-1,10	2,51	2,71	2,79
Return on Risk-Weighted Assets before Taxes (RORWAbT)	1,81	-1,34	3,15	3,49	3,97
Net Interest Margin (NIM)	1,84	-0,11	1,95	2,00	1,85
Pre-Impairment Operating Profit / Assets	0,92	-0,22	1,14	1,14	1,23
Cost of Funds (COF)	0,68	-0,44	1,12	1,07	0,88
Change in %- Points					

Asset Situation and Asset Quality

Net loans to customers represent the largest share of KBC's financial assets, accounting for 53.5%, and increasing by €3.8 billion YOY. The growth in customer loans is primarily attributed to the Belgium Business Unit and the International Markets Unit (with growth in all countries). The growth is mainly attributable to increased mortgage loans. The growth in customer loans in 2019 is primarily attributed to the full consolidation of CMSS in Czech Republic (€4.5 billion). Overall, the main lending products of KBC are term loans (€69.5 billion) and mortgage loans (€71.9 billion). As of June 2021, KBC recorded a total of €12.7 billion in loans under granted payment holidays.
Total securities, as the second largest asset, increased YOY following KBC's increased holding of public sector debt securities (2020: €57.2bn vs 2019: €50.5bn). Investments in public sector debt securities represent a prudent risk approach but are also accompanied by low yields. Most significant government debt securities are attributed to Belgium (€15.6bn), the Czech Republic (€11bn) and Hungary (€3.4bn). The bank's strong increase in its cash position is attributed to KBC's participation in the ECB's TLTRO III program with about €19.5bn in 2020 and a lack of investment opportunities. However, cash balances at the ECB burdens KBC's interest income, due to the negative rates. As of June 2021, KBC even increased its TLTRO III amount to about €24.5bn but could also increase its customer lending volume to about €164.3bn. Other financial assets of the bank are primarily reverse repurchase loans with credit institutions.

A detailed look at the development of the asset side of the balance sheet for the years of 2017 through 2020 can be taken in Figure 3 below:

Figure 3: Development of assets| Source: eValueRate / CRA

Assets (EUR m)	2020	%	2019	2018	2017
Cash and Balances with Central Banks	24.583	> +100	8.356	18.691	29.727
Net Loans to Banks	6.343	+17,5	5.399	5.069	4.878
Net Loans to Customers	159.621	+2,4	155.816	147.052	140.999
Total Securities	71.783	+9,4	65.633	62.707	68.370
Total Derivative Assets	7.179	+23,8	5.799	5.189	5.932
Other Financial Assets	28.990	+8,8	26.645	23.126	20.076
Financial Assets	**298.499**	**+11,5**	**267.648**	**261.834**	**269.982**
Equity Accounted Investments	24	-4,0	25	215	240
Other Investments	555	-2,6	570	561	485
Insurance Assets	14.399	-4,9	15.144	14.340	14.552
Non-current Assets & Discontinued Ops	19	-34,5	29	14	21
Tangible and Intangible Assets	4.687	-0,4	4.705	4.068	3.926
Tax Assets	1.624	+13,3	1.433	1.549	1.625
Total Other Assets	936	-9,7	1.037	1.227	1.511
Total Assets	**320.743**	**+10,4**	**290.591**	**283.808**	**292.342**

KBC was able to lower its NPL ratio despite the Corona pandemic to 3.39% and reached an adequate level. In particular, the write-offs and disposals of NPL portfolios in Ireland helped KBC to reduce its non-performing exposure in recent years. The withdrawal from the business in Ireland as announced in 2021 will lead to a further improvement in this regard. It is noteworthy that as of year-end 2020, about 24% of KBC's stage 3 loans are attributable to the Business Unit in Ireland despite their low share of total customer loans, while only 45% are attributed to the business unit in Belgium and 12% are attributable to the Czech Republic business unit. As a result of the strong increase in impairment charges in 2020, KBC's asset-write-downs to risk-weighted assets as well as in relation to its total assets worsened clearly and reached a substandard level. However, due to the expected significant reversal of the impairment charges, we expect KBC to regain its previously sound asset write-down figures in 2021 already. The bank's potential problem loan ratio (measured as stage 2 loans) increased YOY slightly to about 12.1%. Despite the only little increase in the stage 2 ratio, KBCs records a relatively high level with its potential problem loans, which indicates potential risk. Most of KBC's stage 2 exposure is attributable to the Belgium business unit with about 79%. Moreover, KBC's reserves to NPL ratio of about 68% reached an adequate level and indicates an increasing prudent approach in 2020. The RWA ratio of 31.8% shows a relatively low amount of risk weighted assets in relation to its competitors, which are in this regard more risk seeking. Overall, we consider the bank's risk profile as adequate.

According to KBC's Q2-2021 report, the Group reports widely stable asset quality figures and a small decrease of the NPL ratio. However, with the run out of all public guarantees as well as the end of all moratorium measures we expect a negative impact on the banks asset quality figures in the upcoming periods.

A detailed overview of the asset quality for the years of 2017 through 2020 can be found in Figure 4 below:

Figure 4: Development of asset quality | Source: eValueRate / CRA

Asset Ratios (%)	2020	%	2019	2018	2017
Net Loans/ Assets	49,77	-3,85	53,62	51,81	48,23
Risk-weighted Assets/ Assets	31,84	-2,26	34,09	33,43	31,61
NPLs*/ Net Loans to Customers	3,39	-0,18	3,57	4,50	6,51
NPLs*/ Risk-weighted Assets	5,31	-0,31	5,62	6,97	9,94
Potential Problem Loans**/ Net Loans to Customers	12,17	+0,26	11,91	11,55	2,39
Reserves/ NPLs*	68,21	+16,89	51,32	53,26	44,18
Reserves/ Net Loans	2,31	+0,48	1,83	2,40	2,88
Net Write-offs/ Net Loans	0,69	+0,56	0,13	-0,04	-0,05
Net Write-offs/ Risk-weighted Assets	1,09	+0,88	0,21	-0,07	-0,08
Net Write-offs/ Total Assets	0,35	+0,27	0,07	-0,02	-0,03
Level 3 Assets/ Total Assets	0,51	-0,10	0,61	0,53	0,99
Change in %Points					

* NPLs are represented from 2017 onwards by Stage 3 Loans.
** Potential Problem Loans are Stage 2 Loans where available.

Refinancing, Capital Quality and Liquidity

Total deposits from customers represent the largest share of the Group's liabilities with 64% and show the Group's major refinancing source. KBC recorded a strong growth in customer deposits over all of its business units mostly as a result of increasing customer liquidity due to the Corona pandemic and several lockdowns. This development continues in 2021 and can be observed across the whole banking sector. In 2019, the growth in customer deposits is primarily attributed to the full consolidation of CMSS in Czech Republic. The main deposit products at group level were again demand deposits (€101bn) and savings accounts (€75bn). To counteract the negative effects of the excess liquidity (negative interest rates at the ECB) KBC started to intensify charging negative interest rates to its customers. The strong increase of the banks liabilities to banks is a result of KBC's participation at the ECB's TLTRO III program with about €19.5bn in 2020 (increased to €24.5bn as of June 2021), which enables KBC to reach very favorable refinancing conditions at even negative interest rate if conditions are met. By contrast, total debt of KBC decreased YOY (crowding out of TLTRO III refinancing) following a further reduction of certificates of deposits, accounting for only 8.3% of KBC's liabilities. Moreover, KBC issued its second green bond (each €0.5 billion) in 2020. The bank's line item of insurance liabilities is attributed to the technical provisions and liabilities under the insurer's investment contracts. Moreover, KBC increased its total equity item by about €1.3bn through its retained earnings and followed thereby the ECB recommendation to waive dividend payments. However, with the run out of the ECB recommendation at the end of the year 2021, KBC will continue to pay dividends in line with its general dividend policy, which is acceptable considering the good capitalization of the bank.

A detailed overview of the development of liabilities for the years of 2017 through 2020 can be found in Figure 5 below:

Figure 5: Development of refinancing and capital adequacy| Source: eValueRate / CRA

Liabilities (EUR m)	2020	%	2019	2018	2017
Total Deposits from Banks	34.605	+84,7	18.731	23.684	27.761
Total Deposits from Customers	190.553	+10,0	173.184	159.644	152.479
Total Debt	24.877	-17,6	30.184	32.245	41.227
Derivative Liabilities	6.780	+11,0	6.106	5.705	7.066
Securities Sold, not yet Purchased	-	-	-	-	-
Other Financial Liabilities	7.341	+13,6	6.463	8.320	22.639
Total Financial Liabilities	**264.156**	**+12,6**	**234.668**	**229.598**	**251.172**
Insurance Liabilities	31.520	-2,2	32.241	31.352	18.711
Non-current Liabilities & Discontinued Ops	-	-	-	-	-
Tax Liabilities	498	+4,6	476	380	582
Provisions	744	+6,6	698	865	1.024
Total Other Liabilities	2.295	+0,4	2.286	1.980	2.050
Total Liabilities	**299.213**	**+10,7**	**270.369**	**264.175**	**273.539**
Total Equity	**21.530**	**+6,5**	**20.222**	**19.633**	**18.803**
Total Liabilities and Equity	**320.743**	**+10,4**	**290.591**	**283.808**	**292.342**

KBC Group was able to increase its fully loaded regulatory capital figures significantly due to retained earnings, but no changes of the Group's additional tier 1 and tier 2 capital was recorded. With a CET1 ratio of 17.6% and a Total Capital ratio of about 21.2%, KBC shows a quite strong capitalization and outperforms other large European banks. In addition, the Group comfortably meets the required CET1 ratio of 10.4% and exceeds its own targeted CET1 ratio of 14.5% (+1% management buffer) clearly. The Leverage ratio and the total capital to total assets ratio confirm the Group's sound capitalization. However, as of June 2021 KBC records increasing risk weighted assets, which has a slightly negative impact on the banks regulatory capital ratios. In addition, the strong increase of the banks total assets (TLTRO III and customer deposits) leads to a reduction of the Group's total capital ratio. Nevertheless, KBC's reports a sound capitalization and displays sufficient capital for the absorption of adverse developments.

The Group's LCR of 147% and the NSFR of 146% are in line with other large European banks and show sufficient liquidity. KBC clearly exceeds the regulatory requirements with both ratios. The regulatory requirement regarding the NSFR ratio comes into force in 2021. The customer deposits to total funding ratio of KBC with 65% shows the Group's stable and favorable source of funding - the deposits of its customers. However, the decreasing loan to deposit ratio, which is now at 83.7% shows a decreasing demand for the Group's loans.

Up to now, we do not perceive any liquidity issues at KBC and the whole banking sector.

A detailed overview of the development of capital and liquidity ratios for the years of 2017 through 2020 can be found in Figure 6 below:

Figure 6: Development of capital and liquidity ratios | Source: eValueRate / CRA

Capital Ratios and Liquidity (%)	2020	%	2019	2018	2017
Total Equity/ Total Assets	6,71	-0,25	6,96	6,92	6,43
Leverage Ratio	6,60	-0,20	6,80	6,10	6,10
Common Equity Tier 1 Ratio (CET1)*	17,60	+0,50	17,10	16,00	16,30
Tier 1 Ratio (CET1 + AT1)*	19,00	+0,30	18,70	17,00	17,90
Total Capital Ratio (CET1 + AT1 + T2)*	21,20	+0,60	20,60	19,20	20,20
SREP Capital Requirements	10,42	-0,26	10,68	10,32	10,60
MREL / TLAC Ratio	10,10	-0,30	10,40	9,60	8,90
Net Loans/ Deposits (LTD)	83,77	-6,20	89,97	92,11	92,47
Interbank Ratio	18,33	-10,49	28,82	21,40	17,57
Liquidity Coverage Ratio	147,00	+9,00	138,00	139,00	139,00
Customer Deposits / Total Funding (excl. Derivates)	65,16	-0,37	65,53	61,77	57,22
Net Stable Funding Ratio (NSFR)	146,00	+10,00	136,00	136,00	134,00
Change in %Points					

*Fully loaded whenever available.

Due to KBC's bank capital and debt structure, KBC Bank's preferred senior unsecured debt instruments have not been notched down in comparison to the long-term issuer rating. Moreover, the rating for preferred senior unsecured debt is only assigned to the issuing entity of these debt class KBC Bank NV. Due to the seniority structure, KBC Group's non-preferred senior unsecured debt has been notched down by one notch, which is only assigned to the issuing entity of these debt instrument KBC Group NV. However, the KBC's Tier 2 capital rating is three notches below the long-term issuer rating based on the bank's capital structure and seniority in accordance with our rating methodology. Additional Tier 1 capital is rated five notches below the long-term issuer rating, reflecting a high bail-in risk in the event of resolution. All of the Group's and the Bank's capital and debt instruments received an up notch by one notch due to the upgrade of KBC's long-term credit rating by one notch.

Environmental, Social and Governance (ESG) Score Card

KBC has one significant and two moderate ESG rating drivers

• Corporate Governance is identified as a highly significant rating driver. The relevance for the credit rating results from the impact of the corporate governance factor on all other ESG factors and the overall well-being of the bank. This sub-factor is rated positive due to KBC's strong and stable economic track record, the implemented ESG policies and its diversified business model.

• Corporate Behaviour and Green Financing / Promoting are identified as moderate rating driver. While Green Financing / Promoting is rated neutral due to the relatively low amount of green bonds, Corporate Behaviour is rated positive due to the bank's business activities in accordance with the ideas and beliefs of the society.

ESG Score

3,8 / 5

ESG Score Guidance	
> 4,25	Outstanding
>3,5 - 4,25	Above-average
>2,5 - 3,5	Average
>1,75 - 2,5	Substandard
< = 1,75	Poor

Factor	Sub-Factor	Consideration	Relevance Scale 2021	Eval.
Environmental	1.1 Green Financing / Promoting	The sub-factor "Green Financing/Promoting" has a moderate relevance for the credit rating, and is rated neutral in terms of the CRA ESG criteria.	3	( )
	1.2 Exposure to Environ-mental Factors	The sub-factor "Exposure to Environmental Factors" has a low relevance for the credit rating, and is rated positive in terms of the CRA ESG criteria.	2	(+)
	1.3 Resource Efficiency	The sub-factor "Resource Efficiency" has no significant relevance for the credit rating, and is rated positive in terms of the CRA ESG criteria.	1	(+)
Social	2.1 Human Capital	The sub-factor "Human Capital" has low relevance for the credit rating, and is rated positive in terms of the CRA ESG criteria.	2	(+)
	2.2 Social Responsibility	The sub-factor "Social Responsibility" has no significant relevance for the credit rating, and is rated neutral in terms of the CRA ESG criteria.	1	( )
Governance	3.1 Corporate Governance	The sub-factor "Corporate Governance" is highly relevant for the credit rating, and is rated positive in terms of the CRA ESG criteria.	4	(+)
	3.2 Corporate Behaviour	The sub-factor "Corporate Behaviour" has a moderate relevance for the credit rating, and is rated positive in terms of the CRA ESG criteria.	3	(+)
	3.3 Corporate Transparency	The sub-factor "Corporate Transparency" has no significant relevance for the credit rating, and is rated very positive in terms of the CRA ESG criteria.	1	(+ +)

ESG Relevance Scale	
5	Highest Relevance
4	High Relevance
3	Moderate Relevance
2	Low Relevance
1	No significant Relevance

ESG Evaluation Guidance	
(+ +)	Strong positive
(+)	Positive
( )	Neutral
(-)	Negative
(- -)	Strong negativ

The ESG Score is based on the Methodology "Environmental, Social and Governance Score of Banken (Version 1.0)" of Creditreform Rating AG, which is available on our homepage https://creditreform-rating.de/en/about-us/regulatory-requirements.html. In addition, we refer to CRA's position paper "Consodering the Impact of ESG Factors".

Conclusion

Creditreform Rating upgrades the rating of KBC Group N.V. to 'A+' from A and sets the outlook to stable.

Overall, KBC showed a resilient performance in 2020 despite the Corona pandemic impact. The Group recorded significant impairment charges in 2020, but will benefit from reversals of impairments, as the Corona pandemic did not materialize as previously expected, which was the main reason for the negative outlook. KBC is likely to regain its pre-Corona level of profitability in 2021 already. In addition, the withdrawal from the business operations in Ireland will likely lead to a higher profitability as well. However, KBC is highly dependent on its interest income and struggles with the ongoing low interest rate environment, which imposes a severe challenge for the bank. This issue is mitigated by the banks business operations in Eastern Europe with higher yields. In addition, KBC benefits from its early-imposed digitization strategy. However, a further diversification of KBC's income sources would serve the Group well.

KBC benefited amid the Corona pandemic from its leading position with its bank-insurance products in widely economic strong countries, which were able to counteract the negative development by large stimulus measures of the governments. The Group even recorded a decrease in the NPL ratio. However, the Group reports significant potential problem loans exposure (stage 2), which might bear significant credit risk in the bank's loan portfolio. In addition, KBC reports a significant amount of exposure attributed to memorandum and guarantee measures. Notwithstanding the above, KBC announced the intention of withdrawal from the banks business operations from Ireland, which would likely improve the bank's asset quality. The capitalization of KBC remained strong and even improved due to the waiver of dividend payments. However, a decline in this regard is likely, as KBC exceeds its own target CET1 ratio of about 15.5% (incl. management buffer) and will thus likely increase its dividend payments. The Group complies with and exceeds all regulatory capital requirements comfortably. On the liabilities side, the Group recorded large inflows of customer deposits, but started to intensify charging negative interest rates to its customers to counteract the negative effects. In addition, KBC benefits from the favorable conditions of the TLTRO III program, which pushes the bank's net interest income as well. Furthermore, the liquidity situation of the Group and the banking sector in general remains satisfactory. Even though the final impact of the Corona pandemic remains unclear, we assume KBC will overcome this challenging environment with its diversified business model and the already implemented digitization strategy.

Outlook

We raised the outlook of KBC's long-term issuer rating and its bank capital and debt instruments from negative to stable. This reflects our view that the economic downturn due to the Corona pandemic with a strong negative impact on KBC did not materialize as expected. Thus, the reason for the negative outlook no longer exists. Instead, we expect KBC to regain its pre-Corona level of profitability and benefit from reversal of its loan loss provisions. This expectation is underpinned by the Group's half-year 2021 report, which showed a strong improvement. Moreover, the withdrawal from the business operations in Ireland will likely improve the asset quality and profitability of the Group. In addition, various government measures are in place, which will help KBC to overcome the remaining Corona crisis impact. In addition, we assume no significant economic worsening due to the Corona pandemic and stable political environment in the banks markets of operations.

Scenario Analysis

Best-case scenario: AA-

Worst-case scenario: A-

Please note:

The scenarios are based on information available at the time of the rating. Within the forecast horizon, circumstances may occur that could lead to a change of the rating out of the indicated range.

In a scenario analysis, the bank is able to reach an "AA-" rating in the "best case" scenario and an "A-" rating in the "worst case" scenario. The ratings of bank capital and senior unsecured debt would behave similarly based on our rating mechanism. These ratings are especially sensitive to changes in total equity and to the bank capital and debt structure in general.

We might upgrade KBC's long-term issuer credit rating and its bank capital and debt instruments if we see that KBC is able improve its quality of assets in particular by reducing its potential problem loans in addition to higher earnings figures. In addition, a significant improvement of KBC capital ratios might lead to an upgrade as well.

By contrast, a downgrade of the Group`s long-term issuer credit rating and its bank capital and debt instruments is likely if we see a lasting decline of KBC's profitability and / or a reduction of the banks' capital ratios. In particular, we will observe the ongoing Corona pandemic impact on KBC's asset quality and its business activities in general.

Appendix

Bank ratings

The bank ratings are dependent on a host of quantitative and qualitative factors. An improvement in either sub-category may result in a higher rating score.

LT Issuer / Outlook / Short-Term **A+ / stable / L2**

Bank Capital and Debt Instruments Ratings

The ratings for bank capital and debt instruments are inter alia dependent on subordination and relative size of the instrument class, based on the long-term issuer rating of the bank.

Preferred Senior Unsecured Debt (PSU): **A+** (only KBC Bank)
Non-Preferred Senior Unsecured Debt (NPS): **A** (only KBC Group)
Tier 2 (T2): **BBB+**
Additional Tier 1 (AT1): **BBB-**

Rating History

Please consult our website www.creditreform-rating.de for additional information regarding the dates of publication.

Figure 7: Rating History

Bank Issuer Rating	Rating Date	Result
Initialrating	12.06.2018	A / stable / L2
Rating Update	15.07.2019	A / stable / L2
Monitoring	29.11.2019	A / stable / L2
Monitoring	28.03.2020	A / watch negative / L2
Rating Update	25.11.2020	A / negative / L2
Rating Update	01.10.2021	A+ / stable / L2
Bank Capital and Debt Instruments	**Rating Date**	**Result**
Senior Unsecured / T2 / AT1 (Initial)	12.06.2018	A- / BBB- / BB+
PSU / NPS / T2 / AT1	15.07.2019	n.r. / BBB+ / BBB- / BB+
PSU / NPS / T2 / AT1	29.11.2019	- / A- / BBB- / BB+
PSU / NPS / T2 / AT1 (watch negative)	28.03.2020	- / A- / BBB- / BB+
PSU / NPS / T2 / AT1	25.11.2020	- / A- / BBB / BB+
PSU / NPS / T2 / AT1	01.10.2021	- / A / BBB+ / BBB-
Subsidiaries of the Bank	**Rating Date**	**Result**
KBC Bank NV		
Initialrating	04.12.2018	A / stable / L2
Rating Update	15.07.2019	A / stable / L2

Monitoring	29.11.2019	A / stable / L2
Monitoring	28.03.2020	A / watch negative / L2
Rating Update	25.11.2020	A / negative / L2
Rating Update	01.10.2021	A+ / stable / L2
Bank Capital and Debt Instruments of KBC Bank NV		
Senior Unsecured / T2 / AT1 (Initial)	04.12.2018	A- / BBB- / BB+
PSU / NPS / T2 / AT1	15.07.2019	A- / - / BBB- / BB+
PSU / NPS / T2 / AT1	29.11.2019	A / - / BBB- / BB+
PSU / NPS / T2 / AT1 (watch negative)	28.03.2020	A / - / BBB- / BB+
PSU / NPS / T2 / AT1	25.11.2020	A / - / BBB / BB+
PSU / NPS / T2 / AT1	01.10.2021	A+ / - / BBB+ / BBB-

Regulatory

Creditreform Rating AG was neither commissioned by the rating object nor by any other third party for the rating. The analysis took place on a voluntary basis by Creditreform Rating AG and is to be described in the regulatory sense as an unsolicited rating. The following scheme clarifies the level of participation of the rated entity (rating object):

Unsolicited Credit Rating	
With Rated Entity or Related Third Party Participation	No
With Access to Internal Documents	No
With Access to Management	No

The rating is based on publicly available information and internal evaluation methods for the rated bank. The quantitative analysis is based mainly on the latest annual accounts, interim reports, other investor relations information of the bank, and calculated key figures by eValueRate / CRA.

The information and documents processed met the requirements of the rating system of Creditreform Rating AG as published on the website www.creditreform-rating.de. The rating was carried out on the basis of the rating methodology for bank ratings as (v3.0), the methodology for the rating of bank capital and unsecured debt instruments (v2.0) as well as the rating methodology for Environmental, Social and Governance Score for Banks (v1.0) in conjunction with Creditreform's basic document Rating Criteria and Definitions (v1.3).

The complete presentation of the rating methodologies used by Creditreform Rating AG and the basic document Rating Criteria and Definitions (v1.3) are published on our homepage:

https://www.creditreform-rating.de/en/about-us/regulatory-requirements.html

On 01 October 2021, the rating was presented by the analysts to the rating committee and adopted in a resolution.

The rating result was communicated to KBC Group NV (Group) and the relevant subsidiary, and the preliminary rating report was made available to the bank. There was no change in the rating score.

The rating is valid until withdrawal and is subject to monitoring from the rating date (see cover page). The rating will be comprehensively reviewed at least once every year. Within this period, the rating can be updated.

In 2011 Creditreform Rating AG was registered within the European Union according to EU Regulation 1060/2009 (CRA-Regulation). Based on the registration Creditreform Rating AG (CRA) is allowed to issue credit ratings within the EU and is bound to comply with the provisions of the CRA-Regulation.

Rating Endorsement Status: The rating of KBC Group NV (Group) and the relevant subsidairy was not endorsed by Creditreform Rating AG from a third country as defined in Article 4 (3) of the CRA-Regulation.

Conflict of Interests

No conflicts of interest were identified during the rating process that might influence the analyses and judgements of the rating analysts involved or any other natural person whose services are placed at the disposal or under the control of Creditreform Rating AG and who are directly involved in credit rating activities or approving credit ratings and rating outlooks.

In case of providing ancillary services to the rated entity, CRA will disclose all ancillary services in the credit rating report.

Rules on the Presentation of Credit Ratings and Rating Outlooks

The approval of credit ratings and rating outlooks follows our internal policies and procedures. In line with our policy "Rating Committee," all credit ratings and rating outlooks are approved by a rating committee based on the principle of unanimity.

To prepare this credit rating, CRA has used following substantially material sources:

1. Aggregated data base by eValueRate

2. Annual Report and interim reports

3. Investors relations information and other publications

4. Website of the rated bank

5. Public and internal market analyses

6. Internet research

There are no other attributes and limitations of the credit rating or rating outlook other than displayed on the CRA website. Furthermore CRA considers satisfactory the quality and extent of information available on the rated entity. In regard to the rated entity Creditreform Rating AG regarded available historical data as sufficient.

Between the disclosure of the credit rating to the rated entity and the public disclosure no amendments were made to the credit rating.

The "Basic data" information card indicates the principal methodology or version of methodology that was used in determining the rating, with a reference to its comprehensive description.

In case where the credit rating is based on more than one methodology or where reference only to the principal methodology might cause investors to overlook other important aspects of the credit rating, including any significant adjustments and deviations, Creditreform Rating AG explains this fact in the credit rating and indicates how the different methodologies or these other aspects are taken into account in the credit rating. This information is integrated in the credit rating report.

The meaning of each rating category, the definition of default or recovery and any appropriate risk warning, including a sensitivity analysis of the relevant key rating assumptions, such as mathematical or correlation assumptions, accompanied by worst-case scenario credit ratings as well as best-case scenario credit ratings are explained in mentioned methodologies and / or in the credit rating report.

The date at which the credit rating was released for distribution for the first time and when it was last updated including any rating outlooks is indicated clearly and prominently in the "Basic data" card as a "Rating action"; first release is indicated as "initial rating", other updates are indicated as an "update", "upgrade or downgrade", "not rated", "confirmed", "selective default" or "default".

In the case of a rating outlook, the time horizon is provided during which a change in the credit rating is expected. This information is available within „Basic data" information card.

In accordance to Article 11 (2) EU-Regulation (EC) No 1060/2009 registered or certified credit rating agency shall make available in a central repository established by ESMA information on its historical performance data, including the ratings transition frequency, and information about credit ratings issued in the past and on their changes. Requested data are available at the ESMA website: https://cerep.esma.europa.eu/cerep-web/statistics/defaults.xhtml.

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