KINGDOM OF THE NETHERLANDS
Rating Analysis - 7/9/12
Debt: EUR453.4B

EJR Sen Rating(Curr/Prj) A/ BBB+
EJR CP Rating: A1
EJR's 1 yr. Default Probability: 1.8%

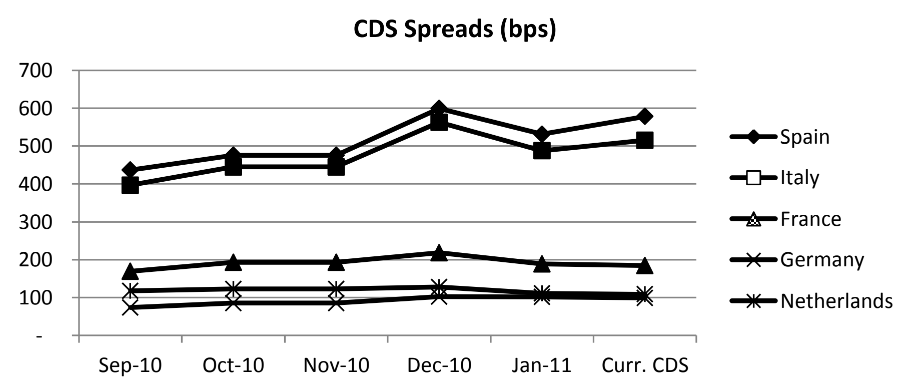
The Netherlands is among the European Union's top economies. However, the Netherlands has been shouldering the burdens of other EU countries and their banks via its exposure to the EFSF and indirectly via the ECB. The country's debt to GDP of 75% as of 2011 (expect near 82% for 2012) and a deficit to GDP of 4.7% is weak and is understated due to exposures to the EU periphery and the Netherland's financial institutions. On the positive side, unemployment was only 5.8% but will probably increase as many EU countries implement austerity measures. Other positives were the EUR48B balance of trade surplus and the EUR67B current account surplus as of the end of 2011. Inflation is near 2.5% currently (per the the Dutch Statistics Office) but is up from 0% in 2009 and will probably rise with monetization.

The markets have cheered the decision to provide EUR100B directly to Spain's banks and to forego seniority for bailout funds. However, the market provides few gifts; the northern European countries will absorb the cost of providing support. Furthermore, with Spain's and probably Italy's seeking support from the EFSF and ESM, two major economies will switch from providers to users of funds. Our view is that the longer the euro crisis continues, the lower the ultimate recoveries. We are downgrading to "A" with a negative watch.

	Annual Ratios (source for past results: IMF)					
INDICATIVE CREDIT RATIOS	2009	2010	2011	P2012	P2013	P2014
Debt/ GDP (%)	67.4	70.6	75.1	81.9	88.8	96.7
Govt. Sur/Def to GDP (%)	-5.6	-5.1	-4.7	-6.3	-6.3	-7.3
Adjusted Debt/GDP (%)	67.4	94.5	98.4	105.1	111.8	119.5
Interest Expense/ Taxes (%)	9.0	7.9	8.5	8.4	9.2	9.6
GDP Growth (%)	-2.3	2.0	-0.4	0.7	0.7	0.6
Foreign Reserves/Debt (%)	1.7	1.4	1.5	1.3	1.2	1.1
Implied Sen. Rating	A	BBB+	A-	BBB+	BBB+	BBB

INDICATIVE CREDIT RATIOS	AA	A	BBB	BB	B	CCC
Debt/ GDP (%)	45.0	55.0	75.0	85.0	95.0	145.0
Govt. Sur/Def to GDP (%)	4.0	1.0	-2.0	-5.0	-8.0	-10.0
Adjusted Debt/GDP (%)	40.0	50.0	60.0	80.0	120.0	150.0
Interest Expense/ Taxes (%)	7.0	9.0	12.0	15.0	22.0	26.0
GDP Growth (%)	4.0	3.0	2.0	1.0	-1.0	-5.0
Foreign Reserves/Debt (%)	25.0	20.0	15.0	12.0	9.0	7.0

PEER RATIOS	S&P Sen.	Debt as a % GDP	Govt. Surp. Def to GDP (%)	Adjusted Debt/ GDP	Interest Expense/ Taxes %	GDP Growth (%)	Ratio-Implied Rating*
Government Of Canada	AAA	33.0	-4.5	34.0	14.1	1.9	A+
Federal Republic Of Germany	AAA	78.3	-5.2	88.7	11.4	2.0	BB+
French Republic	AA+	82.5	-5.2	106.6	9.5	1.2	BB
Republic Of Italy	BBB+	113.2	-3.9	124.4	16.7	-0.5	B
Kingdom Of Spain	BBB+	64.2	-8.5	77.8	12.3	0.3	BB+



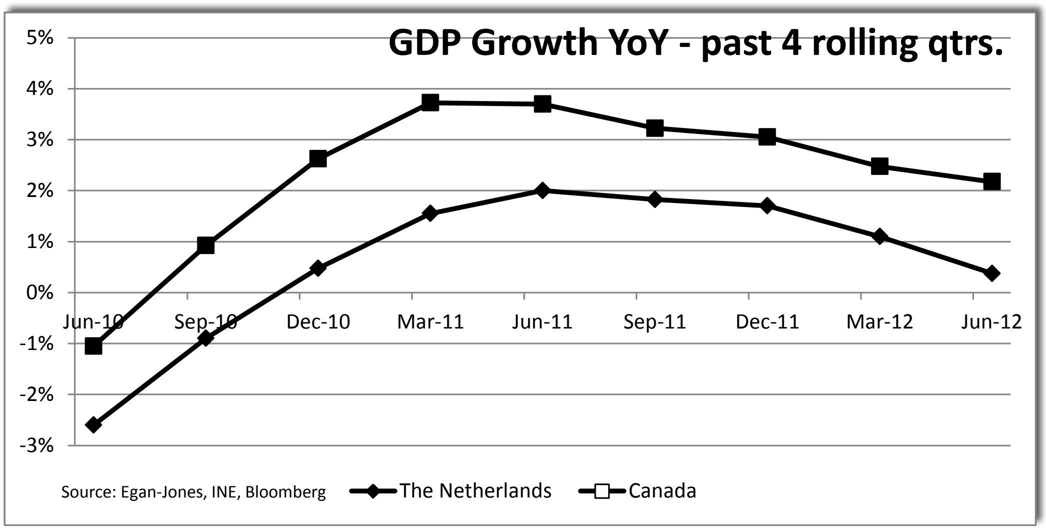
Country (EJR Rtg*)	Current CDS	Targeted CDS
Spain (CC)	578	3,000
Italy (B)	515	1,200
France (BBB-)	185	400
Germany (A-)	99	120
Netherlands (A+)	109	80

* Projected Rating
* EJR's targeted CDS based on rating

Economic Growth

From an economic perspective, the Netherlands has historically been among the stronger EU countries with growth near 2% for the June 2012 period, which is respectable in moribund Europe. The recent decline in the euro will help the major exporters in the Netherlands such as the manufacturers, chemical and pharmaceutical firms. However, imports will cost more and the economies of other EU countries are likely to remain weak and the Netherlands will be expected to contribute support.

As can be seen from the below chart, the Netherland's recent GDP growth has been nearly 2% below Canada's although as of the end of 2009 and beginning of 2010 growth was negative and below Canada's. We expect the GDP growth for 2012 to be positive but slower than 2011. Perhaps the more relevant factor is the growth of the weaker EU countries.



Fiscal Policy

The Netherland's deficit to GDP of 4.7% is not particularly comforting for a top tier country. Over the last several fiscal years (that is from 2008 through 2011), total sovereign revenues declined a total of 1.3% while expenses rose a total 11.3%; the country had to spend to support citizens as a result of the 2008 slowdown. As can be seen from the chart at right, the Netherland's debt to GDP was 75% which is reasonable but is understated due to its indirect support to Greece, Spain and other weak countries.

	Deficit-to-GDP (%)	Debt-to-GDP (%)	5 Yr CDS Spreads
The Nether	4.7	75.1	111
Canada	4.5	33.0	N/A
Germany	5.2	78.3	102
France	5.2	82.5	189
Italy	3.9	113.2	488
Spain	8.5	64.2	531

Sources: Bloomberg and IFS

Unemployment

The Netherland's unemployment rate has long been among the lowest in the Euro zone. Regarding peers, per the chart at right, Belgium is at the lowest rate of the peer countries and declined by 50 basis points from 2010 to 2011. For the more recent periods, the Netherland's unemployment rate was 5.9% as of the end of 2011 which was up from 5.1% for the prior year, a disconcerting rise of 80bps. We expect unemployment will continue to rise with the fiscal problems.

Unemployment (%)

	2010	2011
The Nether	5.1	5.8
Canada	7.6	7.5
Germany	7.4	6.8
France	9.6	9.8
Italy	8.3	9.1
Spain	20.3	22.9

Source: Intl. Finance Statistics

Banking Sector

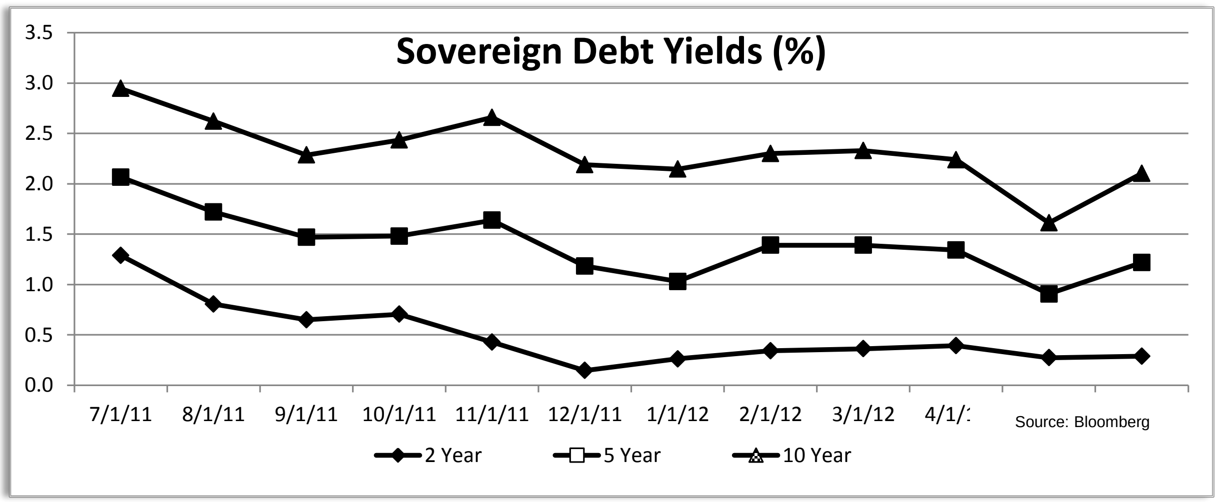
History has shown that country and bank obligations are linked during times of economic distress. The Netherlands has significant exposure to its banking sector because the bank's large aggregate size measured in assets The top five banks have assets equal to 295% of GDP, vs. 124% for Germany, and 477% for the UK, which is at the high end. Our concern is the Netherlands will provide financial support to weaker EU banks over the next couple of years to ameliorate asset quality problems.

Bank Assets (billions of local currency)

	Assets	Cap/ Assets %
ING GROEP NV-CVA	1,279	3.9
AEGON NV	346	7.4
SNS REAAL	132	4.1
VAN LANSCHOT-CVA	18	8.5
CORIO NV	8	53.4
Total	1,783	
EJR's est. of cap shortfall at 10% of assets less market cap		139
The Netherlands's GDP		604

Funding Costs

A Flight to Supposed Quality - with the problems of the periphery EU countries, capital has migrated to the supposed safe havens. As can be seen in the below graph, the bond yields have plunged particularly since Nov. 2011 but have risen recently. A major issue is whether the Netherlands belongs in the top-tier of credit quality given its exposure via the ECB.



Ease of Doing Business

Major factors for growing the economy are the ease of doing business and the economic freedom; although not the sole factor for determining economic growth, a country which makes it easy for businesses to operate and provides a reasonably free environment to conduct business has a good chance for growth. The chart on the right indicates that with an overall rank of 31 (1 is best) the Netherlands is strong.

The World Bank's Doing Business Survey*

	2012 Rank	2011 Rank	Change in Rank
Overall Country Rank:	**31**	**29**	**-2**
Scores:			
Starting a Business	79	68	-11
Construction Permits	99	92	-7
Getting Electricity	67	68	1
Registering Property	48	47	-1
Getting Credit	48	45	-3
Protecting Investors	111	108	-3
Paying Taxes	43	41	-2
Trading Across Borders	13	12	-1
Enforcing Contracts	28	28	0
Resolving Insolvency	7	11	4

* Based on a scale of 1 to 183 with 1 being the highest ranking.

Economic Freedom

As can be seen below, The Netherlands is above average in its overall rank of 73.3 for Economic Freedom with 100 being best.

Heritage Foundation 2012 Index of Economic Freedom
World Rank 73*

	Rank**	2011 Rank	Change in Rank	World Avg.
Business Freedom	**81.9**	81.9	0.0	64.3
Trade Freedom	**87.1**	87.6	-0.5	74.8
Fiscal Freedom	**51.2**	50.6	0.6	76.3
Government Spending	**20.9**	36.8	-15.9	63.9
Monetary Freedom	**83.6**	82.7	0.9	73.4
Investment Freedom	**90.0**	90.0	0.0	50.2
Financial Freedom	**80.0**	80.0	0.0	48.5
Property Rights	**90.0**	90.0	0.0	43.5
Freedom from Corruption	**88.0**	89.0	-1.0	40.5
Labor Freedom	**60.0**	58.3	1.7	61.5

*Based on a scale of 1-100 with 100 being the highest ranking.
**The ten economic freedoms are based on a scale of 0 (least free) to 100 (most free).
Source: The Heritage Foundation & Wall Street Journal

Assumptions for Projections

	Peer	Issuer	Base Case	
Income Statement	**Median**	**Average**	**Yr 1&2**	**Yr 3,4,5**
Taxes Growth%	1.7	(2.6)	**1.0**	**1.0**
Social Contributions Growth %	1.4	7.3	**2.0**	**2.0**
Grant Revenue Growth %	0.0	0.0		
Other Revenue Growth %	5.0	(1.2)	**0.4**	**0.4**
Other Operating Income Growth%	0.0	0.0		
Total Revenue Growth%	2.0	0.8	**1**	**0.6**
Compensation of Employees Growth%	2.0	(0.4)	**1.0**	**1.0**
Use of Goods & Services Growth%	5.3	(2.6)	**1.5**	**1.5**
Social Benefits Growth%	1.6	3.6	**3.0**	**3.0**
Subsidies Growth%	(3.8)	0.2		
Other Expenses Growth%	(10.9)	(10.9)	**1.0**	**1.0**
Interest Expense	0.0	2.6	**3**	
Balance Sheet				
Currency and Deposits (asset) Growth%	(36.0)	0.0		
Securities other than Shares LT (asset) Growth%	(7.2)	(4.4)	**0.5**	**0.5**
Loans (asset) Growth%	7.5	3.2	**1.0**	**1.0**
Shares and Other Equity (asset) Growth%	(2.0)	(6.2)	**2.0**	**2.0**
Insurance Technical Reserves (asset) Growth%	3.0	0.0		
Financial Derivatives (asset) Growth%	0.0	354.4	**1.0**	**1.0**
Other Accounts Receivable LT Growth%	3.0	4.8	**1.0**	**1.0**
Monetary Gold and SDR's Growth %	0.0	0.0	**1.0**	**1.0**
Other Accounts Payable Growth%	(2.9)			
Currency & Deposits (liability) Growth%	2.5	9.2	**4.0**	**4.0**
Securities Other than Shares (liability) Growth%	7.6	9.3	**2.0**	**2.0**
Loans (liability) Growth%	3.1	9.1	**3.0**	**3.0**
Insurance Technical Reserves (liability) Growth%	0.0	0.0		
Financial Derivatives (liability) Growth%	0.0	0.0		
Addl debt. (1st Year) million EUR	0.0	0.0		

Base Case
ANNUAL REVENUE AND EXPENSE STATEMENT (MILLIONS EUR)

	Dec-09	Dec-10	Dec-11	PDec-12	PDec-13	PDec-14
Taxes	137,576	143,100	139,448	140,842	142,251	143,673
Social Contributions	83,466	86,901	93,278	95,144	97,046	98,987
Grant Revenue	0	0	0	0	0	0
Other Revenue	41,679	41,826	41,319	41,484	41,650	41,817
Other Operating Income	0	0	0	0	0	0
Total Revenue	262,721	271,827	274,045	277,470	280,948	284,478
Compensation of Employees	57,670	59,088	58,866	59,455	60,049	60,650
Use of Goods & Services	47,636	47,684	46,450	47,147	47,854	48,572
Social Benefits	129,148	135,331	140,204	144,410	148,742	153,205
Subsidies	8,891	8,853	8,867	8,868	8,869	8,870
Other Expenses	25,294	26,993	24,062	27,263	24,303	27,536
Grant Expense	0	0	0	0	0	0
Depreciation	15,697	16,224	16,772	16,772	16,772	16,772
Total Expenses excluding interest	275,445	285,320	286,354	303,914	306,589	315,603
Operating Surplus/Shortfall	-12,724	-13,493	-12,309	-26,444	-25,641	-31,126
Interest Expense	12,416	11,256	11,887	11,887	13,069	13,723
Net Operating Balance	-25,140	-24,749	-24,196	-38,331	-38,711	-44,848

Base Case
ANNUAL BALANCE SHEETS (MILLIONS EUR)

ASSETS	Dec-09	Dec-10	Dec-11	PDec-12	PDec-13	PDec-14
Currency and Deposits (asset)	17,088	13,224				
Securities other than Shares LT (asset)	19,511	18,166	17,372	17,459	17,546	17,634
Loans (asset)	49,371	48,359	49,905	50,404	50,908	51,417
Shares and Other Equity (asset)	88,290	87,044	81,639	83,272	84,937	86,636
Insurance Technical Reserves (asset)				0	0	0
Other Accounts Receivable LT	41,471	44,218	46,347	46,810	47,279	47,751
Monetary Gold and SDR's						
Additional Assets			13,668			
Total Financial Assets	215,511	213,049	218,191	207,298	210,116	212,979
LIABILITIES						
Other Accounts Payable						
Currency & Deposits (liability)	505	435	475	475	475	475
Securities Other than Shares (liability)	279,198	308,951	337,552	344,303	351,189	358,213
Loans (liability)	78,798	77,926	85,055	123,386	162,097	206,945
Insurance Technical Reserves (liability)						
Financial Derivatives (liability)						
Other Liabilities	26,935	28,034	30,271	12,627	12,627	12,627
Liabilities	385,436	415,346	453,353	480,791	522,320	570,031
Net Financial Worth	(169,925)	(202,297)	(235,162)	(273,493)	(312,204)	(357,052)
Total Liabilities & Equity	215,511	213,049	218,191	207,298	210,116	212,979

Sovereign Rating Methodology

Egan-Jones takes the perspective of the investor as its primary point of view when developing the ratings it issues for sovereigns. Therefore, in the case of sovereign ratings, we attempt to take a more holistic view of credit quality to include not only analytic comparisons of various sovereign issuers but also the impact on our quantitative and qualitative analyses by current global, sovereign, governmental and market events, including the effects of government investments in speculative, volatile or other high risk investment products. For example, many sovereign issuers have taken on significant exposures of major financial institutions over the past several years. Hence, we calculate the under-funding of financial institutions and include this amount in the total indebtedness of sovereigns. (We use a base assumption that no country can afford to allow its major banks to fail and therefore we believe that there will almost always be an intervention by either a host or allied nation should financial institutions or markets require support at some measurable level.)

Generally we devise modeling calculators and do an analysis that examines the debt load of a country with respect to its GDP and other economic indicators. The analysis is then adjusted to reflect the outlook on a myriad of factors that reflect the firm's overall view of the sovereign debt and the quality of the country's ability to meet and thrive under such load. Some of the qualitative factors that impact our ultimate assessment of credit quality such as the flexibility, stability and overall strength of the economy, ease of tax collection, acceptance of contract law, ease of doing business, and prospects for future growth and health. The non quant issues are generally subjective and a moving target, so each rating of a sovereign may differ because of the non-quantitative nuances being addressed. Note, debt levels for many sovereign issuers have increased over the past decade and has accelerated recently, effecting the implied ratings.

Nota Bene

History has proven that defaults on domestic public debt do occur. In fact, seventy out of three hundred twenty defaults since 1800 have been on domestic public debt (1). Egan-Jones does not view a country's ability to print its own currency as a guarantee against default. Additionally, Egan-Jones generally views cases of excessive currency devaluation as a de facto default.

1. "This Time Is Different: Eight Centuries of Financial Folly", Reinhart & Rogoff, p.111, 126