



Ministerie van Financiën

KORTE

> Retouradres Postbus 20201 2500 EE Den Haag

SNS REAAL N.V.  
t.a.v. de heer Latenstein van Voorst  
Croeselaan 1  
Postbus 8444  
3503 RK Utrecht

Directie Financieringen

Korte Voorhout 7  
2511 CW Den Haag  
Postbus 20201  
2500 EE Den Haag  
[www.rijksoverheid.nl](http://www.rijksoverheid.nl)

Inlichtingen  
dhr. V. Hülzr

Ons kenmerk  
FIN/ U

Uw brief (Kenmerk)  
Bijlagen

Date 28th of January 2013  
Subject Cushman & Wakefield Report

Dear Mr Latenstein van Voorst, Dear Mr Lamp,

The Ministry of Finance has received your letter dated 13 January 2013 in which you state that both the procedure followed and the methodology used in the creation of the Cushman & Wakefield (C&W) report are seriously flawed. We have relayed your arguments to our advisers C&W, Morgan Stanley and to professor Tom Berkhout, chairman of the Competence Center Real Estate of the Dutch Tax Authorities. This letter serves to share their views and arguments with you and to enable you to reconsider your views.

In your letter you raise several concerns with respect to the use of information, applied methodology, calculated discount rate, potential double counting of risk factors and the estimation of probability of default (PD) and loss given default (LGD) figures. We have critically assessed your points of attention and think it would prove insightful to give additional information on the aforementioned concerns. This elaboration is included as an annex to this letter and shows that C&W has made a thorough analysis of the Property Finance portfolio (PF portfolio). We hope that this explanation also clarifies your concerns.

Besides comments on the applied methodology by C&W, you also raise several concerns regarding the process of the C&W valuation in your letter. Therefore we believe that a clarification on the part of the Ministry of Finance could be useful. Due to the losses on SNS REAAL's PF portfolio, the capital position of SNS BANK has increasingly become a concern. As a consequence the Ministry of Finance and DNB have investigated potential stabilizing solutions for SNS REAAL in the event that the situation would continue to worsen. An important step in this process was to assess the impact of the potential PF losses on SNS REAAL's capital position. This has led the Ministry of Finance to hire C&W as a renowned and independent expert on real estate loans and objects for an assessment of the Real Economic Value (REV) of the aforementioned portfolio in line with the requirements of the European Commission. The aim of this analysis was to make an independent assessment and not to validate any (internal) review of the same portfolio by yourself, Ernst & Young (E&Y) or any other party. Such an undertaking would not be meaningful due to differences in scope and methodology applied by for example the research done by C&W and E&Y; the former has focused on calculating a REV

value of the loan portfolio. By contrast, E&Y has focused on estimating the potential (provisioning) shortfall which in itself gives insufficient information on the potential transfer price that is warranted for such a portfolio. Understandably these discrepancies can lead to differences between outcomes. Any difference in fees paid to E&Y and C&W is irrelevant in this respect as the scope of both researches is different.

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C&W informs us that it has made a thorough analysis on the basis of the available information provided by SNS REAAL, meetings with management and your employees, and an expert meeting with E&Y on the interpretation of their research results. Parts of the dataset constructed by E&Y proved useful for the analysis of C&W, particularly the information on the collateral value of specific real estate loans. These parts are therefore also used in the C&W research.

Currently C&W is working on an update of the findings in which the value of the PF portfolio will be calculated using the most recent data tape provided by SNS REAAL and the most recent forecasts for macro-economic parameters by DNB's macro-economic department and other independent organizations. It is worth mentioning that an extrapolation of the applied discount rates and expected losses in the PF portfolio to other Dutch market parties is not valid; these parties each have specific loan portfolios with different risk characteristics which makes a projection of implied losses on a larger scale meaningless.

The Ministry of Finance has been as transparent as possible during the process in terms of the applied methodology by C&W and the aim of the conducted research. C&W has given a presentation on the methodology and also on the outcomes of their report and carefully assessed your concerns. In addition you have also received a copy for your own assessment as did the European Commission on the same day. The report is prepared for the Ministry of Finance and we see no added value of distributing the report to other parties than the ones to whom the report already has been disclosed.

We hope that this letter has given you additional insight in the background of the followed procedures and outcomes of the C&W report.

Yours sincerely,



Wouter Raab

Director Financing Directorate

## Addendum

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Please find in this addendum further explanation and background to the points of concern raised in your letter dated 13 January 2013. This addendum deals with five topics:

1. Use of information
2. Applied methodology
3. Calculated discount rate
4. Potential double counting of risk factors
5. Estimation of PD and LGD figures

### 1. Use of Information

C&W reviewed information provided by E&Y as well as documents that were made available on the Merrill Data Site, making extensive use of this information, in particular the collateral data reports. The data provided formed part of the inputs for C&W's financial models. The E&Y information was helpful and provided insights that C&W would normally have sought to extract from credit and collateral files. This has been an important reason why the start of the C&W trajectory was timed to take place shortly after E&Y had prepared their analysis.

E&Y provided C&W access to collateral information that it had put into Excel format for their analysis which made the processing of this material more time efficient. However C&W raised several written questions with E&Y and SNS REAAL that remained unanswered or not met in a timely manner.

### 2. Applied methodology

C&W was invited to provide an assessment of the REV-value of SNS REAAL's PF portfolio under a base and an adverse scenario. Our advisor was not engaged to provide a loan loss provision analysis or to validate the work of another party. We understand that E&Y was engaged to provide advice on loss provisions (shortfall) for the top relationship complexes only. In your letter it is inferred that E&Y has valued the loan portfolio and that therefore its results might be comparable to those produced by C&W. The objective of E&Y's reports was to estimate the potential shortfall of the selected RCs. The comparison of results of E&Y's analysis with those of C&W's analysis is therefore flawed. With reference to the macroeconomic estimates used by C&W it is worth mentioning that C&W based their projections on EC forecasts where they are available and a consensus view where they are not.

### 3. Calculated discount rate

C&W based their estimation of the discount rate on their extensive professional experience in the valuation of bank loans. They used a discount rate which is derived from several components to reflect the specific risk which is attributable to individual loans (examples of such specific risk components are the riskfree rate and the location of the real estate collateral). These estimates are based on observable market parameters and C&W's professional experience. The different riskprofiles of the loans result in an appropriate average discount rate of (■■■■)%. C&W would have calculated a lower discount rate if the portfolio contained mainly good quality real estate investment loans and less development loans. The collateral of the portfolio is however of relatively poor quality; an analysis of C&W shows that the percentage of development loans is very substantial and the average loan to value (LTV) of the loans is high. In addition the portfolio contains a

large amount of non-performing commercial real estate loans (approximately 7%).

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#### **4. Potential Double counting of risk factors**

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C&W calculated a discount rate which is used in both the base and adverse case. The mentioned scenarios however lead to different expected cashflows. C&W prevented double counting of risk factors by differentiating between the estimation of the discount rate (which is unaffected by expected cashflows), and the projection of cashflows (which are based on different macro-economic assumptions).

#### **5. Estimation of PD and LGD figures**

LGD is calculated for the entire portfolio based on the individual and thorough analysis of the non-performing loans. Our adviser derived the PD-rates from a qualitative and quantitative analysis of the available data in relation to a representative sample of loans from each bucket. These PD figures have been estimated on the basis of interest coverage ratios (ICRs) and debt service coverage ratios. C&W applied the same expected default rates in both the base and adverse case. The LGDs however are substantially higher in the adverse case due to the economic scenario.