NORD/LB Covered Bond Bank Luxembourg

Detailed information to the press statement
of October 1st, 2015

„Downgrade by reason of S&Ps methodological change”

On October 1st, 2015, the rating agency Standard & Poor’s (hereafter S&P) lowered NORD/LB Luxembourg Covered Bond Banks (hereafter NORD/LB CBB or the Bank) rating from AA+ outlook negative to AA- outlook stable.

Key trigger of this rating action is a methodological change of bank ratings to meet the requirements of BRRD. The ratings of counterparties of derivative transactions in the cover pool were amended subsequently. The quality of the cover pool has not been changed.

The current bank ratings are as follows:

	FITCH RATINGS	STANDARD&POOR‘S
NORD/LB Luxembourg Covered Bond Bank		
Langfristig / Ausblick / kurzfristig	A- / stable / F1	BBB / negative / A-2
Lettres de Gage publiques / Ausblick	AAA / stable	AA- / stable

In order to hedge interest rate and currency risks in the cover pool, the bank has been using rating criteria compliant derivatives for years, which are collateralised according to the much stricter security standards demanded by the rating agencies. In this context, the following requirements relating to the level of collateral provisions extend far beyond those of bilateral swap contracts outside of the cover pool:

- Unilateral collateralisation in favour of the cover pool
- Determination of market values taking into account currency stress (CARs)
- Supplementary add-ons per derivative for market volatility (volatility buffers)

This means that as of 30.06.2015, collaterals for derivatives was available to the cover pool, which exceeded the market induced value many times. The breakdown of the collateral into market induced values and add-on amounts emphasises the fact that the cover pool has a more than adequate volume of collateral available to replace the derivative in the event of a default by a derivative counterparty.

Despite the substantially higher provision of collateral in favour of the cover pool, the cover pool is directly dependent to the rating of the derivative counterparties. According to S&P ratings methodology a derivative counterparty of an AA+ rated cover pool has to have at least a BBB+ counterparty rating, even though he is willing to provide increased collateral. If the counterparty’s rating sinks one notch to BBB this leads to a downgrade of the cover pool by two notches to AA-.

Since the derivatives in the cover pool at NORD/LB CBB constitute an elementary part of the pool in order to keep the interest rate and currency risks at the accustomed moderate level, it would not be in the interests of the bank or the covered bond creditor to remove derivatives without replacement. The assignment of derivatives to other counterparties does not currently constitute an economic alternative.

The unilateral provision of collateral by the derivative counterparties and the high level of add-ons will also more than adequately hedge the cover pool against the derivative exposures in the future. The derivatives, which are used exclusively for hedging purposes, make a major contribution to the continuity and risk balance of the cover pool and its credit rating by other rating agencies.

NORD/LB CBB has long pursued the policy of continuity and stability in the structural organisation of its lettres de gage publiques cover pool. In the practical implementation of this policy, hedging derivatives have been a major component of the risk management of the cover pool for quite some time. For this reason, the Board of Directors of NORD/LB CBB has decided to pursue the hedging strategy of the cover pool unchanged, including the retention of the existing derivatives. With respect to covered bond creditors, this constitutes the retention of the accustomed and sustained cover pool management by the bank

In addition to the statutory provisions of the Luxembourg Covered Bond Act of 5 April 1993, we have publicly committed to meet the following extra criteria. Firstly, the hedging of 180 days liquidity will be ensured; in addition to this, NORD/LB CBB has undertaken to comply with the transparency provisions under Section 129 (7) of Regulation No. (EU) 575/2013 of the European Parliament. NORD/LB CBB complies with the transparency provisions of the German and Luxembourg covered bond laws and regularly publishes them on its website at www.nordlb.lu. NORD/LB CBB holds surplus cover of at least 22 percent and has committed to comply with the institute ratio. By complying with the institute ratio, NORD/LB CBB is creating the conditions for lettres de gage to meet the quality criteria of the LCR eligible assets according to the regulations that currently apply as of 01.10.2015.