

NORD/LB Luxembourg S.A. Covered Bond Bank

Public-Sector Covered Bonds

Update

Ratings

Lettres de Gage Publiques	AAA/Stable
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Rating Rationale

IDR/Outlook	A-/Stable
IDR uplift	1 notch
Payment continuity uplift	4 notches
Tested rating on a PD basis	AA
Recovery given default uplift	2 notches
Covered bond rating	AAA
OC Fitch considers in analysis (%)	24.6
AAA breakeven OC (%)	14.0

Key Data

	Sep 16
Asset type	Public sector
Cover assets (EURbn)	4.5
Lettres de Gage (EURbn)	3.6
WAL of cover assets (years)	7.9
Stressed WAL of cover assets (years)	7.1
WAL of Lettres de Gage (years)	7.1
Modelled WAL of Lettres de Gage (years) ^a	6.6

^a Including exercise of Callable LdGP

Related Research

[Covered Bond Criteria Implementation Report - October 2016 Criteria Update \(January 2017\)](#)

[Covered Bonds Surveillance Snapshot \(January 2017\)](#)

[Fitch Affirms NORD/LB CBB's Lettres de Gages Publiques at 'AAA'; Outlook Stable \(December 2016\)](#)

[Nord/LB Luxembourg CBB's Public Sector Lettres de Gage - Rating Action Report \(December 2016\)](#)

[2017 Outlook: Covered Bonds \(December 2016\)](#)

[NORD/LB Luxembourg S.A. Covered Bond Bank - Full Rating Report \(May 2016\)](#)

[Fitch Affirms NORD/LB's IDR at 'A-'; Outlook Stable \(May 2016\) \(December 2015\)](#)

Analysts

Alexander Etdzaev
+49 69 7680 76 171
alexander.etsdzaev@fitchratings.com

Timo Dums
+49 69 7680 76 132
timo.dums@fitchratings.com

Key Rating Drivers

Rating Rationale: The 'AAA' rating of NORD/LB Luxembourg S.A. Covered Bond Bank's (NORD/LB CBB) Lettres de Gage Publiques (LdGPs) is based on NORD/LB CBB's Long-Term Issuer Default Rating (IDR) of 'A-', an unchanged IDR uplift of one notch, an unchanged Payment Continuity Uplift of four notches and the 24.6% overcollateralisation (OC) that Fitch Ratings takes into account. The latter provides more protection than the 14% 'AAA' breakeven OC.

Stable Outlook Mirrors Issuer's IDR: The Outlook on the LdGPs' rating is Stable, mirroring that on the issuer's IDR. It further reflects a one-notch cushion against an IDR downgrade that LdGPs' 'AAA' rating could sustain.

Credit Loss Drives Breakeven OC: The main constituent of the breakeven OC remains the credit loss component of 10.0%. A higher share of assets credit-linked to the German sovereign (AAA/Stable/F1+) and first-time individual rating assessments for all loans to public-private partnerships (PPP; 13% of cover assets) are the main drivers of the improved weighted average credit quality of NORD/LB CBB's pool, which is mirrored in the decreased credit loss.

Programme Highlights

Maturity Mismatches Minimal: The relatively low asset disposal loss and cash flow valuation components (1.6% and 2.4%) reflect the well-matched maturity profiles of assets and liabilities supported by flexibility provided by callable LdGPs. As a result, only limited forced assets sales are required to ensure timely payment on outstanding LdGPs. A slight increase in the cash flow valuation component is due to a higher share of fixed liabilities, which reduced the excess spread generated by the programme under the modelled low-interest-rate stress.

Privileged Derivatives in Place: NORD/LB CBB hedges interest-rate and foreign-currency risks with intra-group swaps, which Fitch considered in its analysis. The calculated post-swap open foreign-currency position is within Fitch's 10% limit. The agency applied in its cash flow modelling, along with appropriate stresses for post-swap open-interest-rate positions, criteria-defined foreign-exchange stresses for the residual foreign-currency exposure.

Internationally Diversified Pool: NORD/LB CBB's LdGPs is the most geographically diversified public sector covered bonds programme rated by Fitch. Whereas the US assets, largely represented by the subnational debt, are a legacy sub-portfolio that has been gradually decreasing over recent years, the issuer's focus is on Germany and other core European countries. The sharp growth of UK assets to almost 10% of the cover pool from just 1% two years ago has been fuelled by the rapid increase in loans to UK's PPPs.

The issuer actively manages the programme and taps the capital markets at least once a year to issue LdGPs in a benchmark format. The cover pool volume, which has remained fairly stable at about EUR4.0bn over recent years, showed some signs of growth in the past year, reaching EUR4.5bn at end-September 2016.

Criteria Variation: Please see Page 3 for a detailed explanation on the criteria variation applied in the analysis for NORD/LB CBB's covered bonds programme.

Cover Pool Characteristics: Sep 16

General	
Number of assets	303
Number of final obligors	131

Cover assets by country (%)	
Germany	44.5
United States	20.9
United Kingdom	9.7
Canada	5.6
Netherlands	3.7
Poland	2.5
Italy	2.4
Austria	2.0
Suprationals	1.8
France	1.4
Finland	1.0
Luxembourg	1.0
Sweden	1.0
Denmark	0.9
Czech Republic	0.7
Norway	0.6
Japan	0.4

Instrument type (%)	
Bonds	51
Loans	36
Promissory notes	8
Covered bonds	5

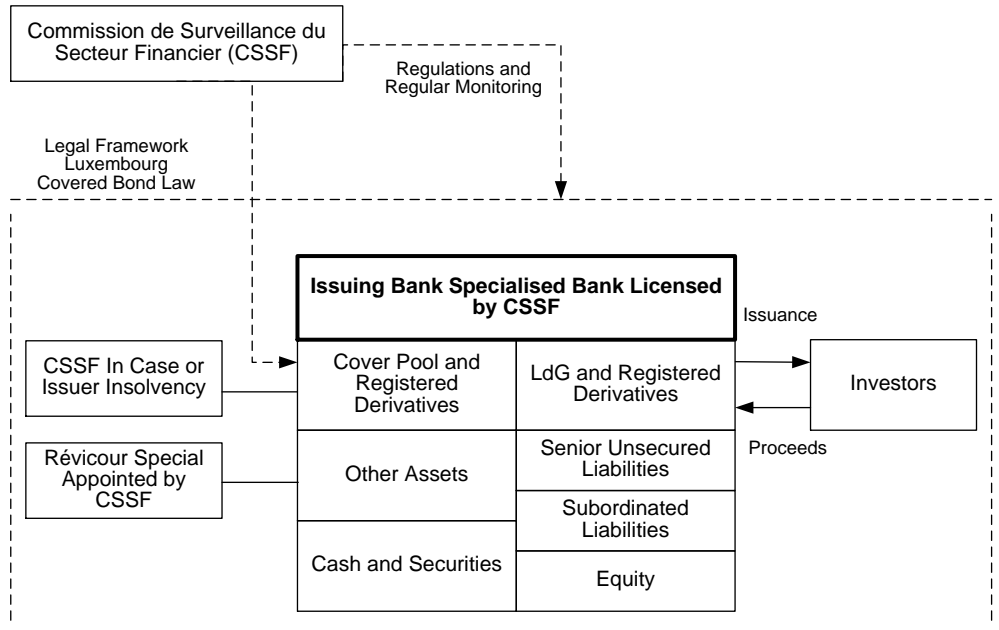
Repayment type (%)	
Bullet	65
Instalments	33
Annuity	2

Interest type after swaps (%)		
	Assets	Liabilities
Fixed	59	73.5
Floating	41	26.5

Denomination after swaps (%)		
	Assets	Liabilities
EUR	73.2	76.3
USD	23.2	23.4
GBP	0.5	0
CHF	2.7	0
JPY	0.4	0
NOK	0	0.3

Source: Fitch/CBB

Simplified Lettres de Gage Issuance Diagram



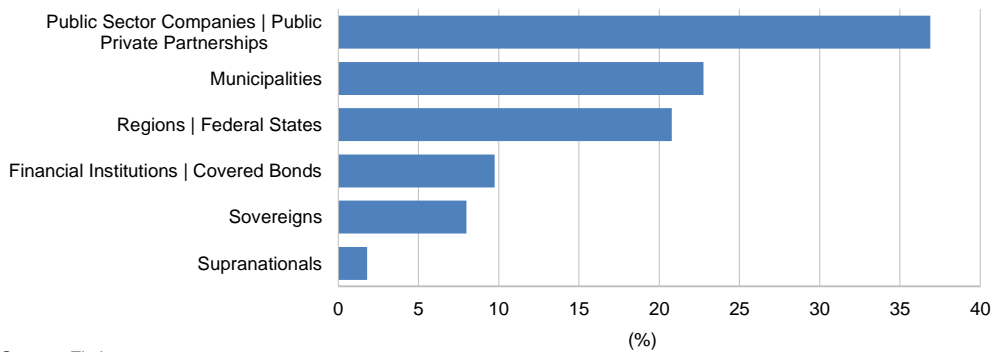
Source: Fitch, Transactional document

Fitch Default Model Output (%)

Rating level	AAA	AA+	AA
Rating default rate (RDR)	17.1	15.6	14.8
Rating recovery rate (RRR)	30.6	37.8	38.5
Rating loss rate (RLR)	11.9	9.7	9.1

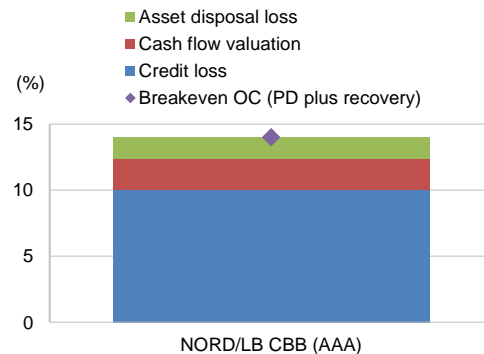
Source: Fitch

Classification of Cover Assets by Guarantor



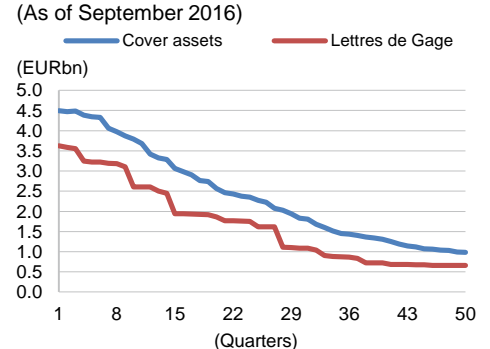
Source: Fitch

Breakeven OC Components



Source: Fitch

Amortisation Profile (After Swaps)



Source: Fitch/NORDB/LB CBB

Related Criteria

- [Asset Analysis Criteria for Covered Bonds and CDOs of Public Entities \(January 2017\)](#)
- [Counterparty Criteria for Structured Finance and Covered Bonds \(September 2016\)](#)
- [Counterparty Criteria for Structured Finance and Covered Bonds: Derivative Addendum \(July 2016\)](#)
- [Covered Bonds Rating Criteria \(October 2016\)](#)
- [Criteria for Interest Rate Stresses in Structured Finance Transactions and Covered Bonds \(October 2016\)](#)
- [Fitch's Interest Rate Stress Assumptions for Structured Finance and Covered Bonds - Excel File \(May 2016\)](#)
- [Fitch's Cover Assets Refinancing Spread Level \(RSL\) Assumptions - Excel file \(January 2017\)](#)
- [Fitch's Foreign-Currency Stress Assumptions for Residual Foreign-Exchange Exposures in Covered Bonds and Structured Finance – Excel File \(October 2016\)](#)
- [Rating of Public-Sector Entities - Outside the United States \(February 2016\)](#)
- [State Revolving Fund and Leveraged Municipal Loan Pool Criteria \(October 2016\)](#)
- [Criteria for Country Risk in Global Structured Finance and Covered Bonds \(September 2016\)](#)
- [Global Bank Rating Criteria \(November 2016\)](#)

Outstanding Lettres de Gage (Benchmarks Only)

ISIN	Currency	(Size m)	Coupon rate (%)	Interest type	Maturity
XS1199018398	EUR	500	0.25	Fixed	10 Mar 20
XS1316421137	EUR	500	0.13	Fixed	06 Nov 18
XS1432510631	EUR	500	0.38	Fixed	15 Jun 23
XS1569741884	EUR	500	0.25	Fixed	23 Aug 21
XS0303324585	USD	500	5.38	Fixed	05 Jun 17

Source: NORD/LB CBB

Variations from Criteria

Fitch applied a variation from “Counterparty Criteria for Structured Finance and Covered Bonds - Derivatives Addendum” published on 8 July 2016. Although the collateral formula is different to the calculation as per Fitch’s criteria, no adjustment has been made as the calculated amounts meet the expectation outlined in Fitch’s counterparty criteria. Accordingly, there is no rating impact from this variation.

The ratings above were solicited by, or on behalf of, the issuer, and therefore, Fitch has been compensated for the provision of the ratings.

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