

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-/Negative
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 (%)	24.0
AAA breakeven OC (%)	14.5

Key Data

	Sep 17
Asset type	Public sector
Cover assets (EURbn)	5.0
LdGP (EURbn)	4.0
WAL of cover assets (years)	7.1
WAL of LdGP (years)	7.0
Stressed WAL of cover assets (years)	5.4
Stressed WAL of LdGP (years) ^a	5.2

^a Including exercise of callable LdGP

Key Rating Drivers

One-Notch Buffer against IDR Downgrade: The 'AAA' rating of the covered bonds is based on NORD/LB Luxembourg S.A. Covered Bond Bank's (NORD/LB CBB) Long-Term Issuer Default Rating (IDR) of 'A-', an IDR uplift of one notch, a Payment Continuity Uplift (PCU) of four notches, a two-notch recovery uplift and the overcollateralisation (OC) Fitch Ratings relies upon of 24%, which provides more protection than the 'AAA' breakeven OC of 14.5%.

The Outlook on the Lettres de Gage Publiques (LdGP) is Stable despite the Negative Outlook on NORD/LB CBB's IDR, reflecting the one-notch buffer against a downgrade of the bank.

Credit Loss Drives Breakeven OC: Fitch has increased the breakeven OC to 14.5% from 14%. It is now driven by the 'AAA' credit loss component of 14.7%. This reflects a 6% exposure to countries rated in the 'Acat' or below and the pool's high concentration, with 343 assets assigned to 152 final guarantors. The programme's rating remains credit-linked to Germany (AAA/Stable/F1+) given the high share of German assets (42%).

Fitch applied a 100% loss rate for the Hungarian exposure (1.6%) to account for extreme macroeconomic or event risks in Hungary. We applied a 0% recovery rate for NORD/LB CBB's United Arab Emirates (UAE; 2%) exposure, reflecting uncertainty about governmental support should the obligor default. Additionally, the UAE's legal environment limits recovery prospects.

One-Notch IDR Uplift: An IDR uplift of one notch has been assigned to NORD/LB CBB's public-sector programme, as the issuer's Long-Term IDR is support-driven and LdGP are exempt from bail-in in a resolution scenario. Fitch does not expect resolution of the issuer to result in the direct enforcement of recourse against the cover pool and the risk of undercollateralisation at the point of resolution is assessed as low.

PCU of Four Notches: The PCU of four notches reflects the voluntary inclusion of liquid assets in the cover pool, matching the maximum negative accumulated balance of cash flows for the next 180 days. This provides effective protection for interest and principal payments for NORD/LB CBB's LdGP.

Programme Highlights

Cash Flow Risk Minimal: Cash Flow risks, captured by Fitch's asset disposal loss and cash flow valuation component, are only a secondary driver for NORD/LB CBB's LdGP reflecting the programmes well-matched maturity profile and the generated excess spread. The issuer hedges interest-rate and foreign-currency risks with intra-group swaps. The calculated post-swap open foreign-currency position is within Fitch's 10% limit and considered residual.

Cover Pool Composition: NORD/LB CBB's cover pool mirrors the wider definition of eligible assets under Luxembourgian covered bond legislation. This is reflected in the 45.5% exposure to unguaranteed public-sector companies and subnational entities from outside the European Economic Area. The share of public-private partnership (PPP) loans has further increased to about 17% of the cover pool (up from 13% as of end-2016), for which Fitch assumes superior recoveries (45% in a 'AAA' scenario).

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

Related Research

Fitch Affirms NORD/LB Luxembourg S.A. Covered Bond Bank's Lettres de Gages Publiques at 'AAA' (January 2018)

Norddeutsche Landesbank Girozentrale (August 2017)

Fitch 2018 Outlook: Covered Bonds (December 2017)

Covered Bonds Surveillance Snapshot (January 2018)

'B' Portfolio Loss Rates for Covered Bonds (September 2017)

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Cover Pool Characteristics: Sep 17

General	
Number of assets	343
Number of final guarantors	152

Cover assets by country (%)	
Germany	41.8
United States	17.0
United Kingdom	14.3
Canada	4.1
Suprationals	3.8
Netherlands	3.3
United Arab Emirates	2.0
Finland	1.9
Poland	1.8
Hungary	1.6
Sweden	1.6
Italy	1.4
France	1.3
Austria	1.2
Denmark	1.0
Czech Republic	0.8
Luxembourg	0.4
Belgium	0.4
Japan	0.3

Instrument type (%)	
Bonds	57.1
Loans	39.2
Promissory notes	3.7

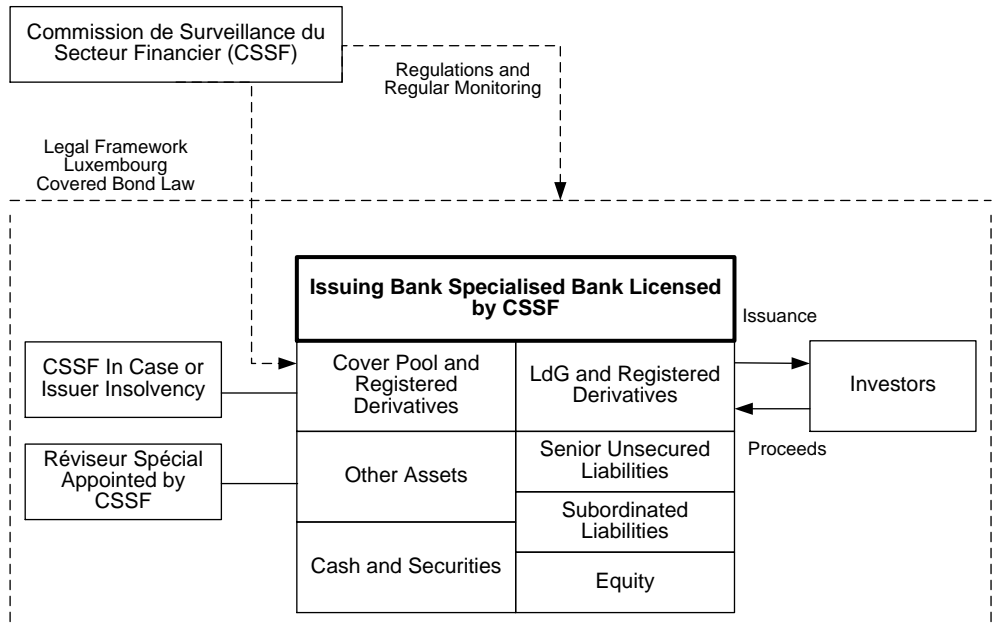
Repayment type (%)	
Bullet	59.5
Amortising	40.5

Interest type after swaps (%)		
	Assets	Liabilities
Fixed	58.9	74.4
Floating	41.1	25.6

Denomination after swaps (EURm)		
	Assets	Liabilities
EUR	3,968.1	3,371.0
USD	987.2	627.6
GBP	38.3	0.0
CHF	17.5	0.0
JPY	15.1	0.0
NOK	0.0	10.6

Source: Fitch/NORD/LB CBB

Simplified Lettres de Gage Issuance Diagram



Source: Fitch, Transactional document

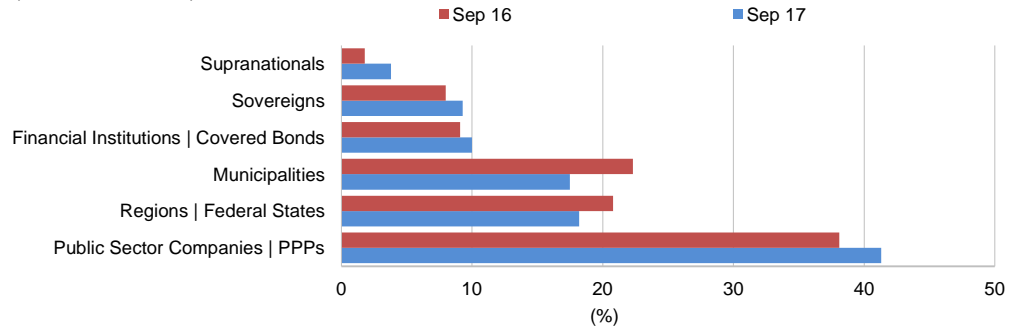
Fitch Default Model Output (%)

Rating level	AAA	AA+	AA
Rating Default Rate (RDR)	19.5	18.2	17.6
Rating Recovery Rate (RRR)	34.2	40.9	42.0

Source: Fitch

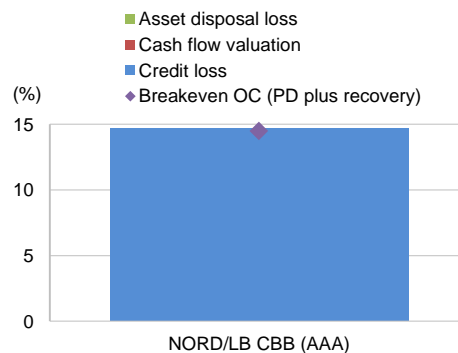
Classification of Cover Assets by Guarantor

(% of cover assets)



Source: Fitch/NORD/LB CBB

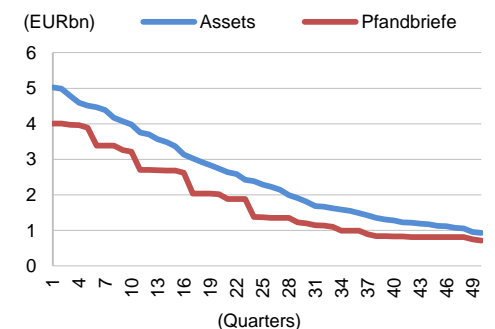
Breakeven OC Components



Source: Fitch

Amortisation Profile

(As of Sep 17)



Source: Fitch/NORD/LB CBB

Outstanding Lettres de Gage (Benchmarks Only)

ISIN	Currency	(Size m)	Coupon rate (%)	Interest type	Maturity
XS1199018398	EUR	500	0.250	Fixed	10 Mar 20
XS1316421137	EUR	500	0.125	Fixed	06 Nov 18
XS1432510631	EUR	500	0.375	Fixed	15 Jun 23
XS1569741884	EUR	500	0.250	Fixed	23 Aug 21

Source: NORD/LB CBB

Variations from Criteria

Fitch applied a variation from “Counterparty Criteria for Structured Finance and Covered Bonds – Derivatives Addendum”, published on 23 May 2017. 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.

Fitch applied a variation from “Covered Bonds and CDOs Public Entities’ Asset Analysis Rating Criteria”, published on 21 December 2017 by applying a 0% recovery rate for subnational entities from the UAE. NORD/LB CBB’s cover pool now also includes exposure to companies owned by public entities from the UAE, for which the criteria do not specify recovery rate assumptions.

Related Criteria

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

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