

Announcement: Moody's extends review of Norddeutsche Landesbank GZ's ratings

30 Aug 2019

Frankfurt am Main, August 30, 2019 -- Moody's Investors Service said today that it has extended its review for upgrade of Norddeutsche Landesbank GZ's (NORD/LB), its New York Branch's and its rated subsidiaries' long-term ratings and rating inputs that are currently under review for upgrade, including its Baa2 deposit, senior unsecured debt and issuer ratings, and its review with direction uncertain for hybrid debt instruments issued by various funding vehicles (Fuerstenberg Capital Erste GmbH and Fuerstenberg Capital II GmbH), rated Caa1(hyb).

The review extension follows an announcement by NORD/LB which updates on the expected timeframe of the completion of its recapitalisation; the bank now expects the recapitalization measures to be executed only in the fourth quarter of 2019, due to the complexity of the process.

RATINGS RATIONALE

NORD/LB's ratings reflect (1) its b2 Baseline Credit Assessment (BCA); (2) its ba3 Adjusted BCA, because our assessment of a high probability of affiliate support from Sparkassen-Finanzgruppe (S-Group, corporate family rating Aa2 stable; BCA a2) adds two notches of rating uplift; (3) the results of our Advanced Loss Given Failure (LGF) analysis, which provide three notches of uplift to the deposit and senior unsecured debt ratings; and (4) our moderate government support assumption, resulting in one notch of uplift for the senior debt and deposit ratings.

The review for upgrade on NORD/LB reflects that the bank's poor asset quality, inadequate provisioning of distressed assets and weak capital ratios will be addressed through a €2.835 billion capital injection, along with other capital measures and a gradual balance-sheet clean-up in 2019. The measures remain subject to necessary regulatory and stakeholder approvals.

Moody's initiated the review on NORD/LB's long-term ratings with direction uncertain on 18 December 2018 following an announcement made by NORD/LB that a sizeable reduction of its impaired shipping loans may lead to a balance sheet loss and a temporary decline in its capital ratios.

The rating agency changed the review direction to a review for upgrade on 14 February 2019 following an announcement by NORD/LB that a general decision of its owners to focus on a capital strengthening and a realignment of the bank jointly with S-Group was reached. This general decision has almost eliminated the downside risk that a targeted capital injection could derail. Moreover, the proposed measures entail significant financial benefits for NORD/LB.

Moody's said that decision for a "sector solution" for the bank include not only the positive effects in the form of financial benefits but also promises long-term ownership by S-Group members and the public sector and the resulting continued membership of NORD/LB in the mutual support mechanism of Germany's largest institutional protection scheme. Both are strong positive factors for NORD/LB's ratings.

While the use of funds from S-Group's Institutional Protection Scheme and from its public sector shareholders will require a favourable decision from the anti-trust department of the EU Commission (DG Comp) before the transaction can proceed, Moody's believes that, ultimately, an agreement with DG Comp will be found that is in keeping with Europe's anti-trust legislation. The rating agency believes that NORD/LB can emerge as a viable franchise, once restructured.

The review with direction uncertain on NORD/LB's preference shares was triggered by ad-hoc announcements of the two Fuerstenberg funding vehicles, stating that the instruments will be affected by a large loss of NORD/LB for the financial year 2018. The rating agency said that, on the one hand, announcements of the two issuing vehicles that followed NORD/LB announcement on 2 February clarified that investors in the non-cumulative preference shares will have to suffer a coupon loss and principal write-down. On the other hand, Moody's said that several important aspects still remain opaque, including (1) to what extent NORD/LB may report further (local GAAP) losses during 2019-20; (2) whether management plans to implement measures

which limit the eventual loss that investors face, and (3) the risk from NORD/LB's possible decision to call these instruments for reasons relating to their regulatory or tax treatment during the time of their impairment.

WHAT COULD MOVE THE RATINGS UP/DOWN

A rating upgrade for NORD/LB's and its rated subsidiaries' deposit and senior unsecured debt ratings, where applicable, depends on an upgrade of the banks' BCA.

A BCA upgrade will likely be prompted as and when (1) the bank and its current and future owners successfully execute the measures that have been agreed upon, specifically the recapitalisation and the sale of nonperforming loans relating to ship finance, and (2) the most important regulatory approvals have been obtained.

Moody's may downgrade NORD/LB's and its rated subsidiaries' ratings if NORD/LB's BCA and Adjusted BCA are downgraded.

NORD/LB's BCA could be downgraded if the planned de-risking and recapitalisation measures were to face major obstacles from one or several authorities which need to approve the transactions. Specifically, failure to obtain DG Comp's approval could lead to NORD/LB's unwinding, with adverse implications for the bank's BCA.

The impact of a BCA downgrade on the long-term and short-term ratings could be reduced or even offset by Moody's re-assessment of affiliate support, e.g. if higher support assumptions were justified by credible support measures undertaken by S-Group, specifically in an unwinding scenario.

PRINCIPAL METHODOLOGY

The methodology used in these ratings/analysis was Banks published in August 2018. Please see the Rating Methodologies page on www.moodys.com for a copy of this methodology.

Please see www.moodys.com for any updates on changes to the lead rating analyst and to the Moody's legal entity that has issued the rating.

This publication does not announce a credit rating action. For any credit ratings referenced in this publication, please see the ratings tab on the issuer/entity page on www.moodys.com for the most updated credit rating action information and rating history.

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