



Fitch Affirms NORD/LB Luxembourg S.A. Covered Bond Bank's LdGPs at 'AAA'/Stable

Fitch Ratings - Milan - 09 January 2020:

Fitch Ratings has affirmed NORD/LB Luxembourg S.A. Covered Bond Bank's (NORD/LB CBB, A-/Stable/F1) legislative public sector covered bonds (Lettre de Gage Publiques, LdGPs) at 'AAA' and removed them from Rating Watch Negative (RWN). The Outlook is Stable.

The rating actions follow the periodic review of the programme and the resolution of the RWN on NORD/LB CBB's Issuer Default Rating (IDR) (see "Fitch Affirms NORD/LB's IDR at 'A-'; off RWN; Outlook Stable" dated 3 January 2020 at www.fitchratings.com). Fitch placed the LdGPs on RWN on 11 December 2018 (see Fitch Places NORD/LB Luxembourg S.A. Covered Bond Bank's LdGPs on Rating Watch Negative' dated 11 December 2018 at www.fitchratings.com).

KEY RATING DRIVERS

The covered bonds' 'AAA' rating is based on NORD/LB CBB's 'A-' IDR, the various uplifts above the IDR granted to the programme and also considers the overcollateralisation (OC) protection for covered bondholders. The Stable Outlook reflects that on the bank's IDR and the two-notch buffer against an IDR downgrade.

The covered bonds are rated six notches above the bank's IDR. This is out of a maximum achievable uplift of eight notches, consisting of an IDR uplift of one notch, a payment continuity uplift (PCU) of five notches and a recovery uplift of two notches.

Fitch relies on the lowest level of OC in the preceding 12 months of 24.6% as the bank's Short-Term IDR is 'F1' and the programme is not considered in wind-down. This provides more protection than the revised Fitch 'AAA' breakeven OC of 19.5% (from 15.5%). The increase was mostly driven by the larger interest rate mismatches in the programme.

'AAA' Breakeven OC

The 19.5% Fitch 'AAA' breakeven OC supports timely payments in a 'AA' stress scenario and a two-notch recovery uplift to 'AAA'. The credit loss of currently 11.5% remains the largest component of the breakeven OC.

As of September 2019, the cover pool remains internationally diversified with concentrations in Germany (43.7%), UK (19.9%) and the US (13.2%). The high share of German assets results in the programme's rating being credit-linked to Germany (AAA/Stable/F1+).

The cover pool's exposure to public private partnerships (PPP; 22.7%) and government-related entities (GRE; 36.4%) has increased from 19.1% and 33.9%, respectively, counterbalanced by a further reduction of the exposure towards sovereign and municipalities (30.1% from previously 32.5%), as of September 2019. Fitch's Public Finance team provided rating assumptions for GRE based on the approach outlined in the Government-Related Entities Rating Criteria. Fitch assumes superior recoveries (45% in a AAA scenario) for PPP loans.

The ALM loss component of 8.2% reflects the post-swap residual FX risk and open interest rate positions between assets and liabilities. As of September 2019, 51.1% of the assets are considered fixed as opposed to 71.7% fixed rate covered bonds. The increase in interest rate mismatches (20.6% compared with 14.6% as of September 2018) drives the increase in the breakeven OC for the rating. Fitch models asset and liabilities on a post-swap basis as cross-currency and interest rate swaps are in place with an eligible counterparty.

Uplifts

The one-notch IDR uplift reflects that collateralised covered bonds in Luxembourg are exempt from bail-in, that Fitch deems the risk of under-collateralisation at the point of resolution to be sufficiently low, and that a resolution of NORD/LB CBB, should it happen, is not likely to result in the direct enforcement of the recourse against the cover pool. It also factors in the support-driven IDR of NORD/LB CBB by the German parent bank Norddeutsche Landesbank Girozentrale (A-/Stable/F1).

The five-notch PCU assessment for the programme is driven by the mandatory 180-day liquidity rule in Luxembourgian covered bonds law. Liquid assets are included in the cover pool to match the maximum negative accumulated balance of cash flows for the next 180 days, which provides effective protection for interest and principal payments on the covered bonds.

The recovery uplift for the programme is two notches as Fitch does not identify material risks to recoveries. The residual post-swap foreign-exchange (FX) risk is stressed when testing timely payments for the covered bonds.

RATING SENSITIVITIES

All else being equal, the 'AAA' rating of NORD/LB CBB's covered bonds would be vulnerable to a downgrade if any of the following occurs: (i) NORD/LB CBB's IDR was downgraded by three notches to 'BBB-' or below; (ii) the German sovereign was downgraded to 'AA+' or below; or (iii) the relied-upon OC drops below Fitch's 'AAA' breakeven OC of 19.5%.

If the OC that Fitch considers in its analysis drops to the legal minimum requirement of 2%, we would likely downgrade the rating to 'A+'.

PUBLIC RATINGS WITH CREDIT LINKAGE TO OTHER RATINGS

The covered bonds rating remains credit-linked to Germany (AAA/Stable/F1+), reflecting the 43.7% exposure to German debtors.

ESG Considerations

The highest level of ESG credit relevance is a score of 3. This means ESG issues are credit-neutral or have only a minimal credit impact on NORD/LB CBB's covered bonds, either due to their nature or to the way in which they are being managed.

For more information on our ESG Relevance Scores, visit www.fitchratings.com/esg

RATING ACTIONS

ENTITY/DEBT	RATING	PRIOR
NORD/LB Luxembourg S.A. Covered Bond Bank		
senior secured, Public Sector Covered Bonds, Lettres de Gage publiques	LT AAA ● Affirmed	AAA ◆

Additional information is available on www.fitchratings.com

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Applicable Criteria

Bank Rating Criteria (pub. 12 Oct 2018)

Structured Finance and Covered Bonds Country Risk Rating Criteria (pub. 23 Oct 2018)

Structured Finance and Covered Bonds Counterparty Rating Criteria (pub. 18 Apr 2019)

Structured Finance and Covered Bonds Counterparty Rating Criteria: Derivative Addendum (pub. 18 Apr 2019)

CLOs and Corporate CDOs Rating Criteria (pub. 03 Jul 2019)

Covered Bonds Rating Criteria (pub. 24 Jul 2019)

Fitch's Foreign-Currency Stress Assumptions for Residual Foreign-Exchange Exposures in Covered Bonds and Structured Finance (Excel) (pub. 24 Jul 2019)
U.S. Public Finance State Revolving Fund and Municipal Finance Pool Program Rating Criteria (pub. 18 Sep 2019)
Covered Bonds and CDOs Public Entities' Asset Analysis Rating Criteria (pub. 14 Oct 2019)
Government-Related Entities Rating Criteria (pub. 13 Nov 2019)
Structured Finance and Covered Bonds Interest Rate Stresses Rating Criteria (pub. 06 Dec 2019)
Fitch Ratings Interest Rate Stress Assumptions for Structured Finance and Covered Bonds (Excel) (pub. 06 Dec 2019)

Additional Disclosures

Dodd-Frank Rating Information Disclosure Form
Solicitation Status
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