

# Norddeutsche Landesbank Girozentrale

## Key Rating Drivers

**SFG's Support Drives IDRs:** The Issuer Default Ratings (IDRs) of Norddeutsche Landesbank Girozentrale (NORD/LB) are driven by Fitch Ratings' view that the bank benefits from a strong likelihood of support from its owners, the German federal states of Lower Saxony and Saxony-Anhalt (both AAA/Stable) and Sparkassen-Finanzgruppe (SFG, A+/Stable), the German savings banks group. In our view, extraordinary support from SFG's institutional protection scheme (IPS) would qualify as a private-sector measure capable of preventing resolution under German law.

**Business Model Transformation on Track:** The bank's restructuring is progressing satisfactorily with regard to balance-sheet, headcount and overall cost reduction, as well as the wind-down of its shipping loan portfolios. However, the restructuring process entails high execution risk.

**Resilient Asset Quality:** The bank's risk appetite is in line with Landesbanken peers' and limited by its owners' intensive monitoring. NORD/LB's asset quality has been resilient so far through the pandemic, like its peers'. Material risks remain in the unguaranteed part of its aviation portfolio, which is equivalent to about a quarter of its common equity Tier 1 (CET1) capital.

**Weak Profit:** We expect NORD/LB to post a small pre-tax profit in 2021 after three consecutive losses to 2020, driven by reversals of loan loss allowances (LLAs) on shipping loans and positive revaluation of guarantees on aviation loans. However, we expect its operating profit to remain weak in 2022 as net interest income (NII) erodes further and loan impairment charges (LICs) could rise toward normalised levels. This will be mitigated by lower fees paid on guarantees as the loan book shrinks. We do not expect material operational losses during the restructuring.

**Adequate Capitalisation:** NORD/LB's CET1 capital ratio improved to 15.8% at end-3Q21, in line with large Landesbanken peers and well above its regulatory requirement of 8.7%. This provides a comfortable buffer to absorb larger unexpected credit losses. The bank benefits from capital reinjections from Lower Saxony during its restructuring, but its weak organic capital generation in combination with expected regulatory and business-driven risk-weighted assets inflation constrain our assessment.

**IPS Membership Underpins Funding:** In 2020 and 1H21, NORD/LB issued unsecured bonds at spreads comparable with its Landesbanken peers. Its issuance needs are low, due to its shrinking balance sheet. Its funding profile benefits from its strong owners and its membership in SFG's IPS. Liquidity is sound.

## Rating Sensitivities

**SFG's Downgrade:** A downgrade of SFG's IDRs or a change in the owners' strategic commitment to the bank or to its ownership structure could lead to a downgrade of NORD/LB's ratings. The ratings could also be downgraded if the execution of the business plan fails, threatening the bank's viability. In this case an orderly wind-down under its owners' sponsorship would be likely.

**Execution of Transformation:** We could upgrade NORD/LB's Viability Rating (VR) if we believe the bank will remain sustainably profitable and its CET1 ratio remains above 13%, while maintaining asset-quality metrics broadly in line with peers'. We could downgrade the VR upon a material negative deviation from the business plan, in particular weak execution of the cost-cutting programme or inability to generate sufficient and adequately priced new business. We could also downgrade the ratings if we expect NORD/LB's CET1 ratio to fall below 12%.

## Ratings

### Foreign Currency

Long-Term IDR	A-
Short-Term IDR	F1
Derivative Counterparty Rating	A(dcr)

Viability Rating bb

Shareholder Support Rating a-

### Sovereign Risk

Long-Term Foreign-Currency IDR	AAA
Long-Term Local-Currency IDR	AAA
Country Ceiling	AAA

### Outlooks

Long-Term Foreign-Currency IDR	Stable
Sovereign Long-Term Foreign-Currency IDR	Stable
Sovereign Long-Term Local-Currency IDR	Stable

## Applicable Criteria

[Bank Rating Criteria \(November 2021\)](#)

## Related Research

[Fitch Affirms NORD/LB at 'A-'; Stable Outlook \(December 2021\)](#)

[Fitch Revises Sparkassen-Finanzgruppe's Outlook to Stable from Negative; Affirms at 'A+' \(June 2021\)](#)

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### Debt Rating Classes

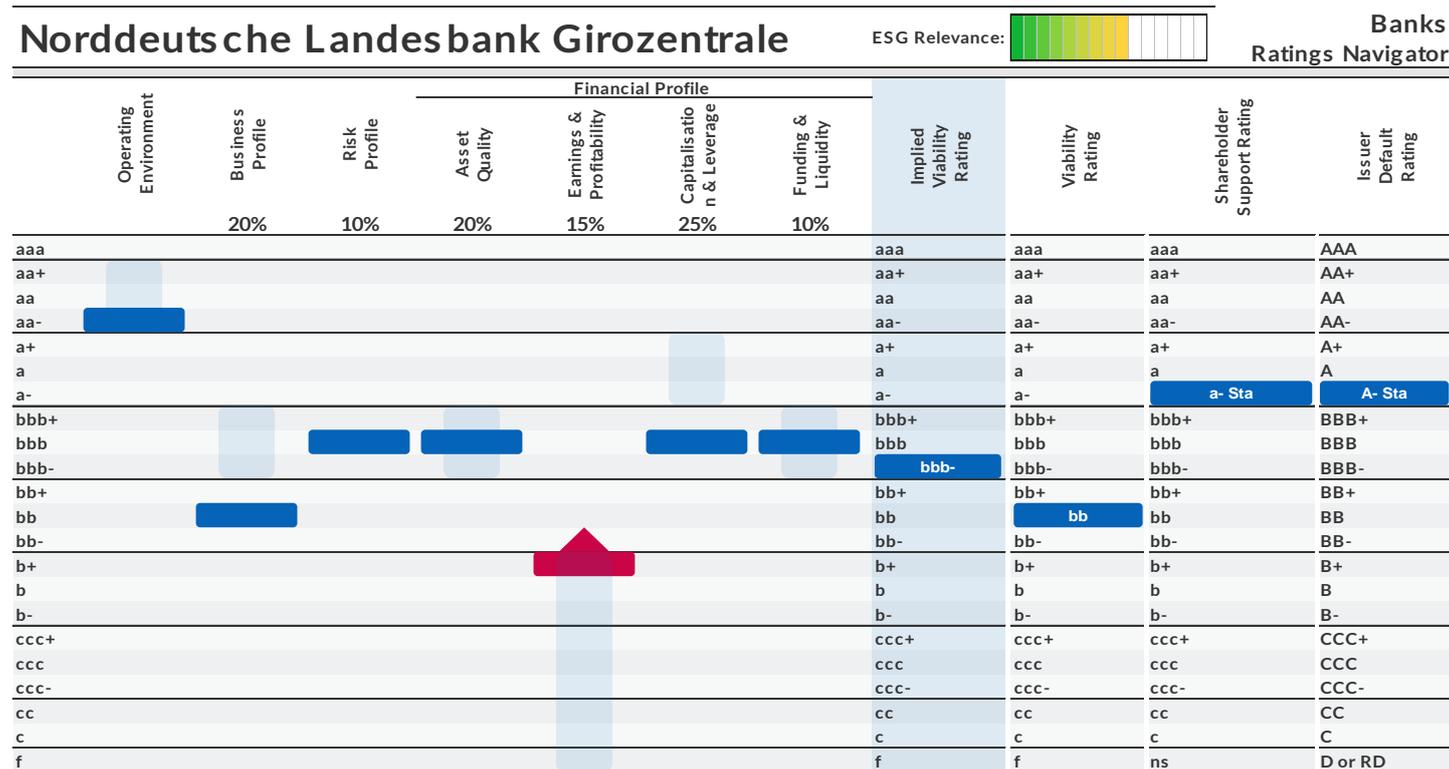
Rating Level	Rating
Deposit ratings	A/F1
Senior preferred debt	A/F1
Senior non-preferred debt	A-
Non-guaranteed Tier 2 subordinated debt	B+
State-guaranteed/grandfathered senior and subordinated debt	AAA

Source: Fitch Ratings

NORD/LB's derivative counterparty rating (DCR), long-term senior preferred (SP) debt and long-term deposit ratings are one notch above its Long-Term IDR, to reflect the protection arising from the bank's junior resolution debt buffers.

NORD/LB's short-term SP debt and deposit ratings are the lower of the two ratings that map to the long-term preferred rating of 'A'. This is because, despite the owners' very high support propensity, we believe the lengthy process required to support a Landesbank could impede the prompt flow of funds that are not commensurate with an 'F1+' short-term rating.

### Ratings Navigator



### Adjustments to Implied VR Scores

We rate NORD/LB's VR below its implied level of 'bbb-' because of the bank's poor earnings and profitability, which represents the weakest link in our rating assessment.

The business profile score is adjusted downward to reflect that NORD/LB's business model will remain in transition with weak earnings generation until its restructuring programme NORD/LB 2024 is concluded.

The capitalisation and leverage score is adjusted downward to reflect the bank's limited capital generation capacity due to its low profitability, beside the contractual reinvestment of guarantee fees by Lower-Saxony.

## Significant Changes

### Global Supply Chain Disruptions Slow Down Economic Recovery

Global supply-side shortages affected the German post-lockdown recovery in 2021. As this shock hit the country's manufacturing sector severely due to its deep integration in global trade flows, Fitch has revised down its 2021 GDP growth forecast for Germany to +2.8% from +3.6%, well below the +5.0% expected for the eurozone. The global supply chain disruptions are likely to persist in 2022 and result in weak export volumes for an extended period. There is also a risk of sharp slowdown in China, Germany's second-largest export market (EUR96 billion in 2020).

In combination with German corporates' precautionary funding activities at the start of the pandemic, we expect these developments to lead to muted corporate loan growth of about 2% in 2022, i.e. less than half the expected German GDP growth of 4.4%.

### Strong Shipping Market Recovery Drives LLA Release in 9M21

NORD/LB is close to completing the wind-down of its shipping portfolio of EUR1.1 billion, which is mostly guaranteed, and of which EUR260 million was non-performing at end-3Q21. Disposals were facilitated by a strong but volatile (and likely unsustainable) market performance for bulkers and container vessels, driven by the rapid post-lockdown recovery and resulting global supply chain shortages. As a result, NORD/LB released LLAs of EUR94 million in 9M21 in its wind-down unit. This largely compensated LICs of EUR109 million in the aviation portfolio, resulting in a net release of EUR42 million for the bank overall in 9M21.

### Pandemic-Related Management Adjustments to LLAs to be Carried Over to 2022

NORD/LB booked EUR426 million of LICs in 2020, including EUR386 million management adjustments for sectors vulnerable to the pandemic, mainly aviation, selected corporate sectors and commercial real estate (CRE), mainly hotels and retail. The bank plans to carry over to 2022 the EUR372 million management adjustments still in place at end-3Q21.

### Restructuring Programme NORD/LB 2024 on Track but Lacks Revenue Progress

Most of the restructuring programme's key performance indicators are developing as expected, primarily asset wind-down, headcount reduction and IT investments. However, NORD/LB's operating revenue remains weak as NII, its dominant revenue source, continues to decline in line with its balance sheet. The bank reduced new lending in 2020 as it expected negative rating migrations to inflate its risk-weighted assets, which eventually did not occur. New business volumes in 9M21 were also low as loan demand from German corporates remains muted. This constrains our assessment of NORD/LB's business profile.

### Management Team Partially Renewed Over Last 12 Months

NORD/LB's CEO will retire at end-2021 at his own request together with the board member in charge of the corporate business. Successors have been recruited for both roles.

### DEUTSCHE/HYPO's Merger Simplifies Organisational Structure

DEUTSCHE/HYPO, the group's specialised CRE lender, was merged into NORD/LB in 3Q21 to achieve cost synergies. CRE lending will remain a core business under the well-established DEUTSCHE/HYPO brand. NORD/LB has also simplified its organisational structure by realigning its two corporate customer divisions into a new joint unit.

## Brief Company Summary and Qualitative Assessments

### Regional German Landesbank, Business Model in Transition

NORD/LB, a public-sector wholesale bank operating primarily in northern Germany, focuses on corporate and asset-based finance with a good footprint in renewable energies and agriculture. It is also the core bank for the federal states of Lower Saxony and Saxony-Anhalt and the savings banks' central institution in both regions and in Mecklenburg-Western-Pomerania. Its modest international franchise is primarily linked to larger corporate clients. Its subsidiary Braunschweigische Landessparkasse serves retail and small business clients.

NORD/LB has been undergoing a deep restructuring agreed with its owners and the European Commission since its recapitalisation by its owners at end-2019. The programme targets a significantly leaner and more profitable bank with less than EUR100 billion total assets by 2024. However, the ability of its future business model to deliver adequate returns remains unproven.

### Moderate Risk Profile

NORD/LB's risk profile is one rating category above its business profile and close to its peers' level. The deleveraging of riskier non-strategic assets should improve its business profile and asset quality in the long term. Consequently, we expect LICs, which have been material and volatile in the past, to be increasingly manageable. NORD/LB has reviewed its credit policy through the pandemic. We believe its underwriting practices prevent onboarding of clients with weak credit profiles even if this constrains loan growth. Its commitment to preserve its capitalisation and to adhere to its restructuring plan also limit its risk appetite.

NORD/LB's market risk, mainly interest-rate and spread risk in its banking book, declined further in 6M21 and does not materially affect the bank's risk profile. Currency risk accounts for less than 5% of the total market risk following exposure reductions in shipping and aviation.

## Summary Financials and Key Ratios

	30 Jun 21 6 months - interim (EURm)	31 Dec 20 Year end (EURm)	31 Dec 19 Year end (EURm)	31 Dec 18 Year end (EURm)
<b>Summary income statement</b>				
Net interest and dividend income	427	988	1,024	1,279
Net fees and commissions	14	-38	41	52
Other operating income	-35	40	151	-109
Total operating income	406	990	1,216	1,222
Operating costs	455	916	970	1,253
Pre-impairment operating profit	-49	74	246	-31
Loan and other impairment charges	20	425	-29	1,893
Operating profit	-69	-351	275	-1,924
Other non-operating items (net)	10	338	-305	-133
Tax	-14	-38	39	297
Net income	-45	25	-69	-2,354
Other comprehensive income	55	-138	-327	-248
Fitch comprehensive income	10	-113	-396	-2,602
<b>Summary balance sheet</b>				
<b>Assets</b>				
Gross loans	71,313	75,119	82,909	91,024
- Of which impaired	1,288	1,427	2,714	2,765
Loan loss allowances	925	1,014	1,595	3,971
Net loans	70,388	74,105	81,314	87,053
Interbank	14,255	14,949	20,701	25,406
Derivatives	4,325	5,983	5,897	5,488
Other securities and earning assets	21,070	23,626	26,536	31,762
Total earning assets	110,038	118,663	134,448	149,709
Cash and due from banks	4,858	6,031	3,454	1,519
Other assets	1,853	1,797	1,717	2,784
Total assets	116,749	126,491	139,619	154,012
<b>Liabilities</b>				
Customer deposits	48,982	52,374	57,887	62,447
Interbank and other short-term funding	29,752	30,460	35,517	44,244
Other long-term funding	23,690	27,401	29,837	34,509
Trading liabilities and derivatives	4,128	6,122	6,395	6,186
Total funding and derivatives	106,552	116,357	129,636	147,386
Other liabilities	4,366	4,313	4,145	3,222
Preference shares and hybrid capital	50	50	50	50
Total equity	5,781	5,771	5,788	3,354
Total liabilities and equity	116,749	126,491	139,619	154,012
Exchange rate	USD1 = EUR0.841468	USD1 = EUR0.821963	USD1 = EUR0.89015	USD1 = EUR0.873057

Source: Fitch Ratings

## Summary Financials and Key Ratios

	30 Jun 21	31 Dec 20	31 Dec 19	31 Dec 18
<b>Ratios (annualised as appropriate)</b>				
<b>Profitability</b>				
Operating profit/risk-weighted assets	-0.4	-0.9	0.7	-4.2
Net interest income/average earning assets	0.8	0.8	0.8	0.9
Non-interest expense/gross revenue	113.8	90.3	82.3	104.4
Net income/average equity	-1.6	0.4	-1.8	-43.3
<b>Asset quality</b>				
Impaired loans ratio	1.8	1.9	3.3	3.0
Growth in gross loans	-5.1	-9.4	-8.9	-4.3
Loan loss allowances/impaired loans	71.8	71.1	58.8	143.6
Loan impairment charges/average gross loans	0.1	0.5	0.0	1.9
<b>Capitalisation</b>				
Common equity Tier 1 ratio	15.4	14.6	14.5	6.8
Tangible common equity/tangible assets	4.5	4.5	3.8	2.1
Basel leverage ratio	4.9	4.3	4.1	2.1
Net impaired loans/common equity Tier 1	6.3	7.1	19.3	-38.8
<b>Funding and liquidity</b>				
Gross loans/customer deposits	145.6	143.4	143.2	145.8
Liquidity coverage ratio	142.8	158.9	166.5	150.3
Customer deposits / total non-equity funding	47.8	47.5	46.9	44.1

Source: Fitch Ratings

## Key Financial Metrics – Latest Developments

### Asset Quality Improving as Wind-Down of Shipping Portfolio Progresses

NORD/LB's loan quality has been so far resilient to the pandemic, in line with most German banks. Its Stage 3 loans declined to EUR1.3 billion at end-1H21 from EUR1.4 billion at end-2020, mainly due to the shrinkage of the non-performing shipping portfolio. Adjusted for the guaranteed shipping portfolio, Stage 3 loans would total about EUR1 billion at end-1H21, equivalent to an impaired loans ratio of 1.4%, broadly in line with peers.

Stage 2 loans increased to 5% of gross loans at end-2020 from 3% at end-2019 and remained broadly stable in 1H21. This is well below the levels of other Landesbanken, which booked management adjustments on a broader set of asset classes than NORD/LB. As its weak pre-impairment profits constrained its ability to book precautionary provisions, NORD/LB focused on the most affected sectors, with services, shipping, aviation and manufacturing accounting for a large majority of Stage 2 loans at end-2020. We expect manageable losses from Stage 2 loans, as 29% of these were collateralised with mortgages or guaranteed. Moreover, 43% was rated investment grade at end-1H21 and only a third was classified as high or very high risk.

We expect Stage 3 loan inflows in NORD/LB's EUR3.1 billion aviation loan book, which shrunk by EUR1 billion yoy, but 46% of which is non-guaranteed and non-securitised. This portfolio is a material source of risk as 11% is non-performing and a further 23% is on the bank's watch list.

### Declining Balance Sheet Constrains Core Profitability

After a loss in 1H21, NORD/LB's pre-tax result turned positive (EUR113 million) in 9M21, driven by a pre-tax profit of EUR292 million at its wind-down unit on the back of the shipping market's exceptionally strong performance.

We include restructuring costs in NORD/LB's operating profit and adjust it for the revaluation of the guarantees on the shipping portfolios and the termination of the silent participations, which strongly supported the bank's net profit in 2020 and 9M21. Our adjustment reflects the fact that the guarantee's valuation will be offset by LICs or reversed when the guaranteed portfolios are reduced. We therefore expect net income to remain low in the coming two years.

NII continued to erode (down 15% yoy) as gross loans declined by 6% to EUR68 billion in 3Q21, while cost-cutting progresses slowly (reduction of 2% in 9M21) as the bank invests in its IT infrastructure and digitalisation. However, we expect the restructuring plan's revenue and cost measures and declining guarantee fees to increasingly support NORD/LB's performance from 2022 despite the negative pull-to-par effect from the expiry of the asset guarantees in 2024.

### Capitalisation Provides Adequate Regulatory Buffer

NORD/LB is committed to a 15% CET1 ratio by end-2024 under its restructuring plan, which we view as achievable if credit losses remain low. The ratio rose at end-3Q21, due to model changes, lower counterparty risks, lower corporate exposure and EUR122 million profit in 9M21. In 2020, the bank decided to redeem silent participations that lost their regulatory recognition as AT1 capital. The bank expects risk-weighted asset inflation from CRR II/Basel IV to be about EUR5 billion, which should be manageable in light of the long implementation timeframe of the new regime.

Lower Saxony's contractual commitment to reinvest the fees it receives for guaranteeing aviation and shipping loans (about EUR350 million in total over the guarantees' lifetime, of which the bank expects EUR111 million to be reinjected at end-2021) will support NORD/LB's capitalisation until 2024. NORD/LB's owners have contractually agreed to forego dividends until end-2021 and to make profit distribution from 2022 conditional on the achievement of specific performance indicators.

### Normalised Funding with Lower Volumes; Adequate Liquidity

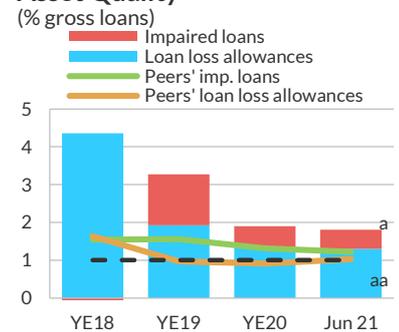
NORD/LB issued moderate unsecured bond volumes in 2020 and 1H21 (including its first 'green' covered bond in benchmark format) at spreads comparable with peers, which suggests the restoration of its wholesale funding franchise. It made only moderate use of the ECB's TLTRO III, initially drawing EUR1.1 billion. Its Liquidity Coverage Ratio remained above 130% in 2020 and 1H21 (149% at end-3Q21), underpinned by EUR20 billion of highly liquid assets.

### Note on Charts

Dashed lines: indicative ranges and implied scores for core financial metrics for banks operating in environments scored in the 'aa' category.

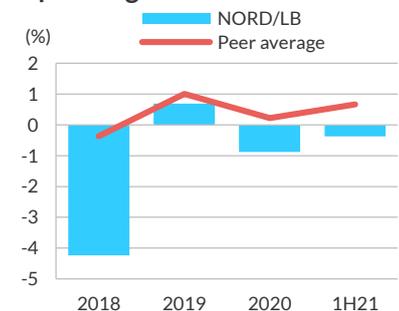
Peer averages include NORD/LB, Bayerische Landesbank (VR: bbb), Landesbank Saar (bb+), and Landesbank Baden-Wuerttemberg (bbb).

### Asset Quality



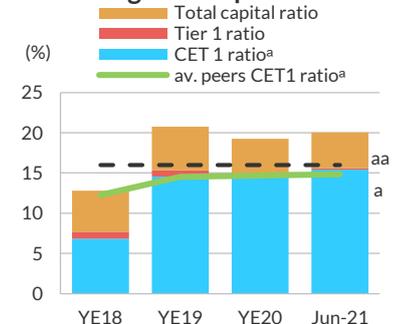
Source: Fitch Ratings, banks

### Operating Profit/RWAs



Source: Fitch Ratings, banks

### Risk-Weighted Capital Ratios



Source: Fitch Ratings, banks

## Shareholder Support Rating (SSR)

SSR Key Rating Drivers	
Shareholder IDR	A+
Total Adjustments (notches)	-2
<b>Shareholder Support Rating</b>	<b>a-</b>
<b>Shareholder ability to support</b>	
Shareholder Rating	A+/Stable
Shareholder regulation	2 Notches
Relative size	1 Notch
Country risks	Equalised
<b>Shareholder propensity to support</b>	
Role in group	1 Notch
Reputational risk	1 Notch
Integration	2 Notches
Support record	Equalised
Subsidiary performance and prospects	1 Notch
Legal commitments	1 Notch

Source: Fitch Ratings

NORD/LB's SSR reflects our view of a very high support propensity from its owners. We use the lowest rating of NORD/LB's parents, SFG's Long-Term IDR, as the anchor rating for determining the bank's SSR because, in our view, support from SFG would help avoid triggering state-aid considerations and resolution under the German Recovery and Resolution Act if NORD/LB fails. We notch down NORD/LB's Long-Term IDR twice from SFG's 'A+', to reflect regulatory restrictions to support due to the requirement for state aid examination under the EU competition rules. The two-notch difference in the ratings also reflects NORD/LB's non-integral role within SFG despite strong synergies. The Stable Outlook on NORD/LB's Long-Term IDR mirrors that on SFG.

## Environmental, Social and Governance Considerations

Unless otherwise disclosed in this section, 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 the entity, either due to their nature or the way in which they are being managed by the entity. For more information on Fitch's ESG Relevance Scores, visit [www.fitchratings.com/esg](http://www.fitchratings.com/esg).

### FitchRatings Norddeutsche Landesbank Girozentrale

Banks  
Ratings Navigator

Credit-Relevant ESG Derivation			Overall ESG Scale			
Norddeutsche Landesbank Girozentrale has 5 ESG potential rating drivers → Norddeutsche Landesbank Girozentrale has exposure to compliance risks including fair lending practices, mis-selling, repossession/foreclosure practices, consumer data protection (data security) but this has very low impact on the rating. → Governance is minimally relevant to the rating and is not currently a driver.			key driver	0	issues	5
			driver	0	issues	4
			potential driver	5	issues	3
			not a rating driver	4	issues	2
				5	issues	1

Environmental (E)				E Scale
General Issues	E Score	Sector-Specific Issues	Reference	
GHG Emissions & Air Quality	1	n.a.	n.a.	5
Energy Management	1	n.a.	n.a.	4
Water & Wastewater Management	1	n.a.	n.a.	3
Waste & Hazardous Materials Management; Ecological Impacts	1	n.a.	n.a.	2
Exposure to Environmental Impacts	2	Impact of extreme weather events on assets and/or operations and corresponding risk appetite & management; catastrophe risk; credit concentrations	Business Profile (incl. Management & governance); Risk Profile; Asset Quality	1

**How to Read This Page**  
ESG scores range from 1 to 5 based on a 15-level color gradation. Red (5) is most relevant and green (1) is least relevant.

The Environmental (E), Social (S) and Governance (G) tables break out the individual components of the scale. The right-hand box shows the aggregate E, S, or G score. General Issues are relevant across all markets with Sector-Specific Issues unique to a particular industry group. Scores are assigned to each sector-specific issue. These scores signify the credit-relevance of the sector-specific issues to the issuing entity's overall credit rating. The Reference box highlights the factor(s) within which the corresponding ESG issues are captured in Fitch's credit analysis.

The Credit-Relevant ESG Derivation table shows the overall ESG score. This score signifies the credit relevance of combined E, S and G issues to the entity's credit rating. The three columns to the left of the overall ESG score summarize the issuing entity's sub-component ESG scores. The box on the far left identifies some of the main ESG issues that are drivers or potential drivers of the issuing entity's credit rating (corresponding with scores of 3, 4 or 5) and provides a brief explanation for the score.

Social (S)				S Scale
General Issues	S Score	Sector-Specific Issues	Reference	
Human Rights, Community Relations, Access & Affordability	2	Services for underbanked and underserved communities: SME and community development programs; financial literacy programs	Business Profile (incl. Management & governance); Risk Profile	5
Customer Welfare - Fair Messaging, Privacy & Data Security	3	Compliance risks including fair lending practices, mis-selling, repossession/foreclosure practices, consumer data protection (data security)	Operating Environment; Business Profile (incl. Management & governance); Risk Profile	4
Labor Relations & Practices	2	Impact of labor negotiations, including board/employee compensation and composition	Business Profile (incl. Management & governance)	3
Employee Wellbeing	1	n.a.	n.a.	2
Exposure to Social Impacts	2	Shift in social or consumer preferences as a result of an institution's social positions, or social and/or political disapproval of core banking practices	Business Profile (incl. Management & governance); Financial Profile	1

Classification of ESG issues has been developed from Fitch's sector ratings criteria. The General Issues and Sector-Specific Issues draw on the classification standards published by the United Nations Principles for Responsible Investing (PRI) and the Sustainability Accounting Standards Board (SASB).

Sector references in the scale definitions below refer to Sector as displayed in the Sector Details box on page 1 of the navigator.

Governance (G)				G Scale	CREDIT-RELEVANT ESG SCALE	
General Issues	G Score	Sector-Specific Issues	Reference		How relevant are E, S and G issues to the overall credit rating?	
Management Strategy	3	Operational implementation of strategy	Business Profile (incl. Management & governance)	5	5	Highly relevant, a key rating driver that has a significant impact on the rating on an individual basis. Equivalent to "higher" relative importance within Navigator.
Governance Structure	3	Board independence and effectiveness; ownership concentration; protection of creditor/stakeholder rights; legal /compliance risks; business continuity; key person risk; related party transactions	Business Profile (incl. Management & governance); Earnings & Profitability; Capitalisation & Leverage	4	4	Relevant to rating, not a key rating driver but has an impact on the rating in combination with other factors. Equivalent to "moderate" relative importance within Navigator.
Group Structure	3	Organizational structure; appropriateness relative to business model; opacity; intra-group dynamics; ownership	Business Profile (incl. Management & governance)	3	3	Minimally relevant to rating, either very low impact or actively managed in a way that results in no impact on the entity rating. Equivalent to "lower" relative importance within Navigator.
Financial Transparency	3	Quality and frequency of financial reporting and auditing processes	Business Profile (incl. Management & governance)	2	2	Irrelevant to the entity rating but relevant to the sector.
				1	1	Irrelevant to the entity rating and irrelevant to the sector.

The ratings above were solicited and assigned or maintained at the request of the rated entity/issuer or a related third party. Any exceptions follow below.

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