EUROPEAN COMMISSION

Brussels, 18.07.2007

C(2007) 3244 final

In the published version of this decision, some information has been omitted, pursuant to articles 24 and 25 of Council Regulation (EC) No 659/1999 of 22 March 1999 laying down detailed rules for the application of Article 93 of the EC Treaty, concerning non-disclosure of information covered by professional secrecy. The omissions are shown thus […].

PUBLIC VERSION

WORKING LANGUAGE

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<u>Subject</u>: **State aid NN 34/2007 (ex CP 189/2004) — Germany**
Capital contributions NORD/LB

Sir,

The Commission wishes to inform the Federal Republic of Germany that, having examined the information supplied by your authorities on the measures referred to above, it has decided that the capital injections into Norddeutsche Landesbank - Girozentrale ("NORD/LB") as laid out in this decision do not constitute aid in the meaning of Article 87(1) of the Treaty.

I. Procedure

1. Subject of this decision are three capital measures into NORD/LB made by its public shareholders in the course of 2005.
2. On 20 October 2004 the Commission decided that the asset transfer by the Land of Lower Saxony in the end of 1991 constituted incompatible State aid and that € 472.34 million plus interest had to be recovered[1]. Including interest NORD/LB had to repay a total amount of € 712.6 million which it did on 30 December 2004. In the course of these procedures, Germany and NORD/LB informed the Commission that the bank's shareholders planned to make different capital contributions into NORD/LB the amount of which was not specified.
3. By letter of 30 November 2004 the Commission informed Germany that investments taking place after recovery raise concerns with respect to the effectiveness of the Commission's recovery policy and, therefore, established criteria relevant for the Commission's assessment of such investments, including the requirement to submit a

[1] Commission Decision C(2004)3926 fin of 20 October 2004, OJ L 307 of 7.11.2006, p. 58

robust investment calculation proving that the remuneration for capital provided would be in line with the market economy investor principle.

4. On 18 July 2005 the Commission sent a letter to Germany asking to be informed about the capital measures envisaged by NORD/LB's shareholders. By letter of 26 August 2005 Germany answered to this request for information. On 19 September 2005 the Commission sent a further request for information. Germany answered by letter of 21 October 2005 and 10 February 2006. On 16 January 2006 a meeting with representatives of Germany, the Land of Lower Saxony, NORD/LB and the Commission took place.

II. Description of the measures

1 NORD/LB

5. NORD/LB is Germany's fourth-largest Landesbank group by equity. As a public law bank it is the main bank to the governments of its state owners (Lower Saxony, Saxony Anhalt and, until 19 July 2005, Mecklenburg-Western Pomerania) and acts as the central bank for the 80 savings banks in these states.

6. NORD/LB is offering financial services to private customers, SME's, large companies and public authorities. NORD/LB concentrates on property lending, as well as shipping and aircraft financing, although it also has small, local retail operations. With a group balance sheet total of € 198 billion in 2005 it is an important player on national and also international capital markets. According to its 2005 Annual Report the Return on Equity (ROE) was 8.8% and the bank employed 5,998 employees.

7. The strengthening of NORD/LB's capital base resulted in a change in the ownership structure in the course of 2005. One component of this capital package was that the federal state of Mecklenburg-Western Pomerania decided to sell its 10% stake in NORD/LB to the Savings Banks Association of Lower Saxony and the Savings Banks Association of Saxony-Anhalt.

8. Before the capital increase of 15 July 2005 the regional state of Lower Saxony owned 40% of the shares, the Savings Banks Association of Lower Saxony 26.67%, the regional state of Saxony-Anhalt 10%, the regional state of Mecklenburg-Western Pomerania 10% and the Savings Banks Association of Saxony-Anhalt and Mecklenburg-Western Pomerania 6.67% each.

9. After the share capital increases of 15 July and 31 October 2005 and the sale of the 10% stake of Mecklenburg-Western Pomerania the shareholding structure of NORD/LB is now equally split between the savings banks and the regional states:

NORD/LB shareholder structure (%)	**End 2005**
Regional state of Lower Saxony	41.75%
Regional state of Saxony-Anhalt	8.25%
Savings Banks Association of Lower Saxony	37.25%
Savings Banks Association of Saxony-Anhalt	7.53%
Savings Banks Association of Mecklenburg-Western Pomerania	5.22%

10. NORD/LB is one of the German public banks which until 18. July 2005 still profited from the unlimited State guarantees "Anstaltslast" and "Gewährträgerhaftung", which had to be abolished following a number of Understandings between Germany and the Commission. Anstaltslast conferred rights to the financial institutions vis-à-vis its owners, whereas Gewährträgerhaftung provided for rights of the creditors of the financial institutions vis-à-vis the owners. Following the first of the Understandings (hereafter: "the Understanding") dated 17.07.2001, between a transitional period between 19.7.2001 and 18.7.2005 new liabilites could still be covered by Gewährträgerhaftung - so-called "Grandfathering" -, provided their maturity did not go beyond 31.12.2015[2].

11. After the loss of the state guarantee in July 2005 NORD/LB refocused its business profile and realigned its participation portfolio. The disposal of its 10% stake in BGB to Deutscher Sparkassen- und Giroverband (DSGV) in September 2006 is part of this ongoing re-shaping process.

2 The capital measures

12. Germany informed the Commission about three capital measures that occurred after the 20 October 2004 decision and the subsequent recovery: A silent participation of € 900 million, a share capital increase of € 850 million and another share capital increase of € 1,196.2 million by converting existing silent participations into share capital.

13. Germany informed the Commission that the foreseeable abolishment of the state guarantees Anstaltslast and Gewährträgerhaftung on 18.7.2005, the repayment of € 712.6 million of State aid in December 2004 and the envisaged withdrawal of Mecklenburg-Western Pomerania as shareholder required a comprehensive redirection of NORD/LB’s business strategy in order to ensure the future sustainability of the business model. Key areas of the transformation programme would include the strategic redirection (realignment of business areas and the interconnection with the Savings Bank in Lower Saxony, Saxony-Anhalt and Mecklenburg-Western Pomerania) and the optimisation of the capital structure.

14. The investment decisions concerning the capital contributions were made by NORD/LB’s shareholders except the federal state of Mecklenburg-Western Pomerania on 9 March 2005 on the basis of a Fairness Opinion provided by Lehman Brothers on behalf of NORD/LB. Upon request of the Commission Germany also provided a so-

[2] See E 10/2000 for details, OJ C 146, 19.6.2002, p. 6 and C 150, 22.6.2002, p.7 and http://ec.europa.eu/comm/competition/state_aid/register/ii/by_case_nr_e2000_0000.html#10

called Dividend Discount Method (DDM) analysis[3] prepared by Lehman Brothers for NORD/LB which includes different cases depending on the business development. This DDM analysis is based on the same data as the Fairness Opinion which was the basis for the investment decisions.

2.1 Silent participations of in total € 900 million

15. NORD/LB emitted silent participations in three tranches in the total amount of € 900 million in the period from April to June 2005. The regional state Lower Saxony participated via its 100% subsidiary Hannoversche Beteiligungsgesellschaft ("HB").

Description of the three tranches

Tranche	Pricing date	Amount	Coupon rate	Participation of HB
1	4 April 2005	€ 300 m	5.344% until 2015; afterwards 3month-Euribor + 150bps[4]	[…]*%
2	24 May 2005	€ 550 m	5.625%	[…]%
3	3 June 2005	€ 50 m	[…]% until 2020; afterwards 10year MidSwap + […] bps	0%

16. The first tranche was subscribed to the extent of € […] million ([…]%) by private investors and to the extent of € […] million ([…]%) by HB; the issue was priced on 4 April 2005, at par ('100'). It is noted that the instrument is perpetual, rated by Moody's (A3) and listed at the stock exchange in Amsterdam (Euronext). The instrument traded on 28 September 2005 at a bid price of 105.0. Germany has explained that 57% of the private investors were based in Germany, while the others were based in Europe (Benelux 24%, Denmark 8%, others 11%). 54% of the private investment was placed with asset management funds and the remaining 46% with banks and insurance companies.

17. The second tranche was subscribed to the extent of € […] million ([…]%) by private investors and to the extent of € […] million ([…]%) by HB; the issue was priced on 24 May 2005, at par ('100'). It is noted that the instrument is perpetual, rated by Moody's (A3) and listed at the stock exchange in Amsterdam (Euronext). The instrument traded on 28 September 2005 at a bid price of 104.90. The private investment was mainly placed with Private Banking clients based in Europe (UK 32%, Germany 24%, Switzerland 18%, Spain 11%, others 15%).

18. Germany maintained that both tranches have been placed at market conditions. The price was determined by the private investors in a book building exercise[5]. The first two tranches were oversubscribed. This allowed NORD/LB to set the coupon at the lower

[3] The DDM analysis is a variant of the DCF analysis (Discounted Cash Flow) applied for banks. It calculates the expected return of an investment in share capital by means of the companies expected value increase following the investment and is based on the business plan of the company concerned. See further explanation in paragraph 45 and following.

[4] Bps = Basis points

** Business secret*

[5] Book building refers to the collection of bids from investors, which is based on an indicative price range, the issue price being fixed after the bid closing date. The bidding can be compared to an open auction.

end of the pricing range. HB took the remaining € […] million at the same conditions as those fixed in the book building exercise with the private investors

19. Germany mentions as remunerations of comparable investments for the € 300 million emission Allied Irish Banks (Moody's rating A2) with MidSwap+97bps, Bancaja (A3) with MidSwap+93bps, Barclays (Aa3) with 4.875% until 2015 afterwards MidSwap+93bps and Barclays (Aa3) with 4.75% until 2010 afterwards MidSwap+106bps.

20. For the € 550 million silent participation Germany mentions emissions of Erste Bank (A3) 5.25% and WestLB (Baa2) of 6% as comparable.

21. The third tranche of € 50 million was fully subscribed by one private institutional investor. This investor did not ask for a rating of the emission. The price was determined by private placement. The emission was […]% oversubscribed.

22. Germany stated that as the silent participation issue was perpetual, it would not be covered by the grandfathering of the public guarantees pursuant to the Understanding; the latter would have applied only if the instrument had a maturity date before 31 December 2015.

2.2 Equity capital increase of € 850 million and conversion of silent participation into share capital of € 1.2 billion

23. On 15 July 2005 a cash capital increase in NORD/LB of a total value of € 850 million became effective. All shareholders of NORD/LB participated, except the Land Mecklenburg- Western Pomerania which ceased to be a shareholder a few days later on 19 July 2005:

Investor	Amount
Savings Banks Association of Lower Saxony	€ 405 million
Regional state of Lower Saxony	€ 280 million
Regional state of Saxony-Anhalt	€ 150 million
Savings Banks Association of Mecklenburg-Western Pomerania	€ 10 million
Savings Banks Association of Saxony-Anhalt	€ 5 million

24. On 31 October 2005 a conversion of silent partnerships of € 1.2 billion to share capital of € 1.2 billion of NORD/LB became effective. The conversion resulted in the acquisition of the following share capital:

Investor	Amount
Regional state of Lower Saxony	€ 593 million
Savings Banks Association of Lower Saxony	€ 417.5 million
Savings Banks Association of Saxony-Anhalt	€ 104 million
Savings Banks Association of Mecklenburg-Western Pomerania	€ 81 million

25. Both investment decisions were made on 9 March 2005 on the basis of the Fairness Opinion. The primary goal of the Fairness Opinion is the determination of the subscription price (fair equity value/nominal capital) at which a private market investor would underwrite the capital measures. The study is made on a likely case scenario. The valuation is based on a discounted cash flow analysis (“DCF”) with the valuation date 31 December 2004.

26. Starting from the equity value assuming that the capital measures will take place ("status quo")[6], the study establishes the equity value of the bank assuming that the capital measure would not take place ("status ante") in deducting the discounted values of the capital contributions and making discounts for increased transaction costs in case of liquidation of the investment in a non-listed bank (fungibility) and for first emission. The study valuates NORD/LB's "status quo" equity value to € […] billion. In order to determine the "status ante" equity value of Nord/LB, Lehman Brothers deduct the discounted values of the share capital increases of € 850 million (€ […] million discounted value) and € 1.2 billion (€ […] billion discounted value) and then further deduct the residual value by […]% (€ […] million) for fungibility and additional […]% (€[…] million) for first emission. The "status ante" equity value of NORD/LB amounts to € […] billion.

27. The conversion rate of […]% results from the quotient of the "status ante" equity value of € […] billion and NORD/LB's nominal share capital of € 375 million. The difference between the valuation of NORD/LB in the "status quo" and "status ante" case amounts to € […] billion and exceeds the total amounts of the investments of € 2.05 billion (€ 850 million and € 1.2 billion) by € […] million. The study therefore concludes that a market economy investor would have provided the capital to NORD/LB at the conversion rate of […]%.

28. This evaluation is based upon the business plan provided by NORD/LB's Management Board. The planning originally covered the period 2004-2008 but was extended on the request of Lehman Brothers for the years 2009/2010. The main assumption underlying the calculations are:

    - […] rating from Standard & Poors (unguaranteed long-term) from July 2005 onwards and […] rating from 2007 onwards
    - Tier I capital of […]% in 2004 up to […]% in 2010
    - ACE[7] quota of […]% in 2004 up to […]% in 2010
    - RWA[8] of € […] billion in 2004 down to € […] billion in 2010
    - Revenues of € […] billion in 2004 up to € […] billion in 2010

29. The discount rate is determined on the basis of the Capital Asset Pricing Model (CAPM)[9]. The risk free rate was assessed at 3.66% on the basis of 10-year government bonds as per 18 February 2005. The market risk premium is fixed at […]% based on a study on comparable companies of the Deutsches Aktieninstitut (DAI) and a study of Lehman Brothers. The beta-factor is determined at […] on the basis of a benchmarking with comparable banks. The resulting cost of equity for NORD/LB is […]%.

30. This evaluation was subject to a plausibility check with market trading multiples. The market or trading multiples valuation method values a company based on multiples at which similar companies ("peers") trade on the stock exchange. The value is expressed as a multiple of the net income, operation income or book value. In the case at hand,

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[6] Results from the sum of the cash flows in the period 2005-2010, the present value of the so-called terminal value, the present value of tax losses carried forward and hidden reserves.

[7] Adjusted Common Equity

[8] Risk-Weighted Assets

[9] The CAPM is a standard method to determine the cost of equity of a company. The cost of capital are the sum of the risk free rate and the market risk premium multiplied with the beta factor, which values the specific market risk for that particular company in comparison to other companies of the sector.

Lehman Brothers defined a peer group of publicly listed financial institutions (HVB, Commerzbank, Deutsche Bank, SEB Groub, BNP Paribas, Société Générale) and other Landesbanken (HSH, LB Kiel, WestLB, Landesbank Rhineland Palatinate). The fair equity value of NORD/LB's capital increases was found to be within the range determined through the market multiples approach.

31. In addition, Lehman Brothers verified the result of the DCF analysis by comparing it to the valuation based on the so-called EVA-methodology (Economic Value Added). The EVA-methodology measures a company's financial performance based on the residual wealth which is calculated by deducting costs of capital from its operating profits after taxes. The result of € […] billion before the discounts for reduced fungibility and first emission is within the range of the result of the DCF analysis (i.e. € […] billion).

32. Following a request from DG COMP, Germany further provided a DCF analysis – more precisely, DDM analysis[10] – based on detailed business plans of NORD/LB's business with the capital measures ("post-money scenario") and without the capital measures ("pre-money scenario") in different cases (worst case, likely case, best case). The DDM analysis was established by Lehman Brothers for NORD/LB on the basis on the same business information that was available at the time the business decisions were taken. Consequently, the likely "post-money scenario" was made under the same assumptions as the "status quo" scenario in the Fairness Opinion and is therefore the same as already described above. The main assumptions in the three cases are the following:

- S&P rating (unguaranteed long-term): starting from […] and […] in the year 2005 up to […],[…] and […] in 2010:

Scenario	Case	Rating
Pre-money	Pessimistic	[…],[…] from 2009 onwards
	Likely	[…],[…] from 2007 onwards
	Optimistic	[…],[…] from 2010 onwards
Post-money	Pessimistic	[…]
	Likely	[…],[…] from 2007 onwards
	Optimistic	[…],[…] from 2007 onwards

- Tier I capital: starting from 5.3% in the year 2004 in all cases to the following results in 2010:

Scenario	Case	Tier I capital ratio in 2010
Pre-money	Pessimistic	[…]%
	Likely	[…]%
	Optimistic	[…]%
Post-money	Pessimistic	[…]%
	Likely	[…]%
	Optimistic	[…]%

- ACE quota: starting from 2.2% in 2004 in all cases to the following results in 2010:

10 As stated above, the DDM analysis is a variant of the DCF analysis applied for banks. See below paragraph 45 and following for details.

Scenario	Case	ACE quota in 2010
Pre-money	Pessimistic	[…]%
	Likely	[…]%
	Optimistic	[…]%
Post-money	Pessimistic	[…]%
	Likely	[…]%
	Optimistic	[…]%

- RWA: starting from € 82.14 billion in 2004 in all cases to the following results in 2010:

Scenario	Case	RWA in 2010
Pre-money	Pessimistic	€ […] billion
	Likely	€ […] billion
	Optimistic	€ […] billion
Post-money	Pessimistic	€ […] billion
	Likely	€ […] billion
	Optimistic	€ […] billion

- Revenues: starting from € 1.74 billion in 2004 in all cases to the following results in 2010:

Scenario	Case	Revenues in 2010
Pre-money	Pessimistic	€ […] billion
	Likely	€ […] billion
	Optimistic	€ […] billion
Post-money	Pessimistic	€ […] billion
	Likely	€ […] billion
	Optimistic	€ […] billion

33. In all cases the DDM evaluation arrives at differences between the values in the "post-" and "pre-money" scenarios of NORD/LB exceeding the cumulated amounts of the capital contributions of € 850 million and € 1.2 billion, i.e. € 2.05 billion:

Case	Post money value	Pre money value	Difference Post-Pre money value
Optimistic case	€ […] billion	€ […] billion	€ 3.26 billion
Likely case	€ […] billion	€ […] billion	€ 2.43 billion
Pessimistic case	€ […] billion	€ […] million	€ 2.45 billion

III. Assessment

1 Article 87 (1) EC Treaty

34. Article 87 (1) of the EC Treaty provides that any aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods shall, in so far as it affects trade between Member States, be incompatible with the common market.

1.1. State resources

35. In so far as the first two tranches of the silent participations of in total € 900 million were subscribed by Lower Saxony's 100% subsidiary HB the investment involves State resources. The third tranche of the silent participation of € 50 million does not entail any State resources since it was fully subscribed by a private institutional investor.

36. With respect to the two capital increases, the investments were to their entirety carried out by all but one of NORD/LB´s shareholders. Only the regional state of Mecklenburg-Western Pomerania did not participate, as it sold its stake to the remaining shareholders and ceased to be a shareholder shortly afterwards. Therefore, the shareholders involved were the regional state of Lower Saxony, the regional state of Saxony-Anhalt, and the Savings Banks Associations of Saxony-Anhalt and Mecklenburg-Western Pomerania. As to the capital which was provided by the regional States, two German Länder, there is no doubt that the funds provided by those States are States resources and are imputable to the State. As regards the two Savings Banks Associations involved, the question whether the funds provided by those shareholders are State resources and whether the investment is imputable to the State, can be left open, if the measure in question is not favouring NORD/LB in the meaning of Article 87 (1) of the Treaty.

1.2 Advantage – private investor test

37. A broader capital base provides for a greater lending capacity and the associated possibility of expanding business. If additional capital is made available to the undertaking on conditions better than normal market conditions this ranks as favouring within the meaning of Article 87(1) EC Treaty. In examining this matter the Commission applies the "market economy investor principle". According to this principle no State aid is involved where funds are made available on terms which a private investor would find acceptable in providing funds to a comparable private undertaking operating under normal market conditions[11]. In contrast, a financial measure such as a capital injection is deemed unacceptable for a market economy investor if the expected return on the investment is below the return a market economy investor would expect for a comparable investment.

38. The Court of Justice and the Court of First Instance have accepted and developed this principle in a number of cases, in particular in the ruling by the Court of First Instance of 6 March 2003 in the *WestLB* case[12]. In this ruling, the Court stated: "*In order to determine whether such action is in the nature of State aid, it is necessary to assess whether, in similar circumstances, a private investor operating in normal conditions of a market economy (`a private investor') of a comparable size to that of the bodies*

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[11] Commission communication to the Members States: Application of Articles 92 and 93 of the EEC Treaty and of Article 5 of Commission Directive 80/723/EEC to public undertakings in the manufacturing sector (OJ C 307, 13.11. 1993, p.3; see paragraph 11). According to its paragraph 3, this Communication applies to all sectors of the economy.

[12] Judgment in Joined Cases T-228/99 and T 233/99 *Westdeutsche Landesbank GZ v Commission* [2003] ECR II-435 et seq.

operating in the public sector could have been prompted to make the capital contribution in question[13]*"*. The attitude of the hypothetical private investor is that of a prudent investor,[14] whose goal of profit maximisation is tempered with caution about the level of risk acceptable for a given rate of return.[15] *"… [T]he comparison between the conduct of public and private investors must be made by reference to the attitude which a private investor would have had at the time of the transaction in question, having regard to the available information and foreseeable developments at that time*[16]*"*. It follows that events subsequent to the decision to invest would be irrelevant[17]. Furthermore the Commission must *"make a complete analysis of all factors that are relevant to the transaction at issue and its context, including the situation of the beneficiary undertaking and of the relevant market, in order to verify whether that undertaking is receiving an economic advantage which it would not have obtained under normal market conditions*[18]*"*.

39. Based on this, .the key question in examining this case is therefore whether a market economy investor would have provided the capital to NORD/LB under the same conditions as the public investors.

The silent participations

40. In line with point 3.2 (iii) of the Commission's position on the application of Articles 92 and 93 of the EEC Treaty to public authorities' holdings[19], there is a strong indication that no State aid is involved where the State provides finances to a company at the same conditions as private investors operating under normal market economy conditions.

41. First, the Commission notes that the silent participations are perpetual and therefore, although they were emitted before the 18.7.2005, they are not covered by the state guarantee Gewährträgerhaftung any more. Second, the Commission recognises the considerable involvement of private investors in these silent participations, as private investors took […]% in the first tranche and […]% in the second tranche. Third, the price of the issue was determined by the private investors in a book building exercise, which is a standard procedure in financial markets to come to a market price. It follows from the choice of the instrument and the fact that there was a substantial participation of market players[20], as the silent participation was oversubscribed, that the issue has been placed at market conditions. HB as representing NORD/LB's main shareholder took the remaining € […] million at the same conditions as those fixed for the private investors. The numerous retail and institutional investors were based all over Europe.

42. Furthermore the benchmarking provided by Germany shows the remuneration for the silent participations in NORD/LB in line with those of comparable investments[21]. The companies in the benchmark like Allied Irish Banks, Bancaja, Barclays, Erste Bank and

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[13] Joined cases T-228/99 and T-233/99, cited above, paragraph 245. See also Case C-142/87 *Belgium v Commission* [1990] ECR I-959, paragraph 29, and Alfa Romeo, Case C-305/89 Italy v Commission [1991] ECR I-1603, paragraphs 18 and 19.

[14] Case C-482/99 *Francev. Commission* [2002] ECR I-4397, paragraph 71.

[15] Joined cases T-228/99 and T-233/99, already cited, paragraph 255.

[16] Joined cases T-228/99 and T-233/99, already cited, paragraph 246.

[17] Cases T-16/96, Cityflyer Express vs. Commission, paragraph 76; see also Commission communication cited above, paragraph 42.

[18] Joined cases T-228/99 and T-233/99, already cited, paragraph 251.

[19] Bulletin EC 9-1984.

[20] See paragraph 16 and following above.

[21] See above paragraphs 15, 19, 20.

WestLB are European financial institutions with comparable activities and size. The emissions were issued around the same period of time with a rating in the range of Aaa3 to Baa2, situated around the A3 rating of NORD/LB's silent participation. Given that the issuing dates, the durations and the ratings of the benchmarks do not match exactly with the NORD/LB silent participation, a direct comparison is not possible. To exemplify the comparability of the remunerations Barclay's higher rated Aa3 emission has a 0.75% lower fixed rate until 2015 compared to the first € 300 million tranche of NORD/LB. WestLB issued a lower rated Baa2 emission with a 0.375% higher fixed rate until 2015 compared to the second € 550 million tranche of NORD/LB.

43. The Commission therefore considers that the participation of HB in the first two tranches of € 300 million and € 550 million under the same terms which were acceptable to private market investors does not entail any economic advantage in the meaning of Article 87(1) EC for NORD/LB.

The capital increases of € 850 million and of € 1.2 billion

44. In order to assess the market-conformity of the investment decisions, the Commission notes that both the Fairness Opinion and the DDM analysis provided by Germany show that the investments were market-conform[22]. However, the Fairness Opinion is only analysing a likely case scenario and does not explore alternative developments.

45. The Commission takes the view that the DDM analysis applied by Germany in order to substantiate the findings of the Fairness Opinion is the appropriate study to consider when carrying out the assessment of the envisaged investments in share capital. The DDM methodology is a standard method to calculate the expected total return of an investment by means of the company’s expected value increase following the investment in question. An increase in the market value can be estimated by carrying out a valuation of the company’s business with the investment (“post-money scenario”) and a valuation of the company’s business without the investment (“pre-money scenario”). If the difference between the two (net present) values is positive and higher than the invested amount, the market value of the company increases due to the capital injection. The Commission considers that a private investor acting in a market economy would then find acceptable to provide the share capital on the same terms and that the investment could be considered to be market conform.

46. The DDM valuation methodology is a variant of the Discounted Cash Flow methodology for the valuation of financial institutions taking into account their specificities. Because of supervisory requirements and rating aspects a bank’s business can only grow to an extent that it is still underpinned by an appropriate level of own capital. The DDM thus determines a bank’s value through discounting the future distributable dividends, i.e. the annual surplus less the own capital needed. Under the DDM approach, forecasted distributable dividends are discounted back to the present date, generating a present value for the dividend stream of the bank. A terminal value at the end of the explicit forecast period is then determined and also discounted to the valuation date to give an overall value of the business

47. The same methodology was also applied in the assessments of the previous BayernLB and HSH Nordbank decisions[23].

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[22] See above paragraphs 27 and 33.

[23] Commission decisions of 6.09.2005, NN71/05 HSH Nordbank, OJ C 241 of 6.10.2006, p. 12 and NN72/05 BayernLB (Germany), OJ C 242 of 7.10.2006, p. 19.

48. The Commission notes in this context that the DDM analysis was not the basis of the investment decision, as it was only later provided by Germany upon request of the Commission. However, even though the DDM analysis was not available at the time of the shareholders´ decision, the assumptions for this analysis are taken from the existing Fairness Opinion including the complementary valuation methodologies based on market multiples and the EVA analysis which were available to the shareholders on 9 March 2005 at the time the investment decisions were made. The Commission therefore concludes that the findings would have been the same, had the study been done prior to the decision and therefore, it can be a valid basis for assessing this case.

49. Considering the DDM analysis, t Commission assessed the CAPM methodology to determine the cost of capital of NORD/LB and concludes that the approach is in line with industry standards. The Commission is of the opinion that the discount rate of […]% is reasonable. The Commission assessed the business planning including the key economic assumptions of the scenario analysis which are the rating, the Tier I capital ratio, the ACE quota and the RWA growth and thinks that they are justified in comparison to its peer groups. NORD/LB had managed over the past two years to increase its net income from € 13.9 million in 2003 to € 50.8 million in 2004.

50. In all cases the DDM analysis arrives at differences between the post- and pre-money values of NORD/LB which exceed the amount of the invested capital of € 2.05 billion[24]. Even in the pessimistic scenario the investment does not only earn the cost of capital but creates additional value for the investors.

51. As the shareholders, as noted above, were not in possession of the DDM analysis at the time the decision was made, but based their decision on the Fairness Opinion, the Commission also assessed this study including the complementary valuation methodologies based on the market multiples and the EVA analysis. These methodologies used are all standard methods which are applied elsewhere in the market. On substance, the Commission finds it reasonable The Commission considers that this document is also a valid basis on which a private investor could base his investment decision, as was done in this case.

52. The Commission has no reasons to doubt the methods and estimates used in the various assessments of the envisaged investments in share capital described above. The various investment decisions were evaluated by a qualified third party.

53. The Commission, therefore, concludes that a private investor would find acceptable providing the capital increases under the same terms and that the investment in share capital is in line with the market investor principle.

2 Effectiveness of the Commission's recovery policy

54. During its assessment, the Commission took into account the need to ensure that the capital increases concerned did not undermine the effectiveness of its recovery policy. The Commission is satisfied that the illegal aid granted to NORD/LB that was subject to the 20 October 2004 decision[25] has been entirely recovered on 30 December 2004. Furthermore, the state guarantees were abolished on 18 July 2005.

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[24] See above paragraph 33.

[25] Commission decision C(2004)3925final of 20 October 2004 on WestLB GZ.

55. The silent participations and the capital increases of July and October 2005 have been subjected to a robust analysis and found to be entirely in accordance with the market economy investor principle, and thus do not contain any element of State aid. The Commission therefore concludes that the 'effet utile' of the 20 October 2004 decision is preserved.

IV. Decision

56. The Commission has decided that the silent participations of in total € 900 million and the capital increases of € 850 million and € 1.2 billion do not constitute State aid in the meaning of Article 87(1) of the EC Treaty.

If this letter contains confidential information which should not be disclosed to third parties, please inform the Commission within fifteen working days of the date of receipt. If the Commission does not receive a reasoned request by that deadline, you will be deemed to agree to the disclosure to third parties and to the publication of the full text of the letter in the authentic language on the Internet site:

http://ec.europa.eu/community_law/state_aids/index.htm

Your request should be sent by registered letter or fax to:

European Commission
Directorate-General for Competition
State aid Greffe
B-1049 Brussels
Fax No: + 32-2-296.12.42

Yours faithfully,
For the Commission

Neelie KROES

Member of the Commission