



EUROPEAN Commission

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**Subject: State Aid N 412/2009, Germany
Prolongation of State Aid N 655/2008
"Secured guaranteed medium-term note programme" of Norddeutsche
Landesbank**

Sir,

1. PROCEDURE

- (1) With decision C (2008) 8985 fin of 22 December 2008¹ the Commission approved the initial aid measure N 655/2008 'Secured guaranteed medium-term note programme' (hereinafter 'programme') for Norddeutsche Landesbank for the duration of six months.
- (2) With notification of 10 July 2009, Germany requested a prolongation of this aid measure for an additional period of six months from 15 August 2009 until 15 February 2010.

¹ Commission Decision of 22 December 2008, N 655/2008, Secured guaranteed medium-term note programme, OJ C 63, 18.03.2009, p. 16. http://ec.europa.eu/community_law/state_aids/comp-2008/n655-08.pdf

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2. DESCRIPTION OF THE AID MEASURE

2.1. The beneficiary

- (3) The beneficiary is the 'Norddeutsche Landesbank' (hereinafter 'NORD/LB'). With its consolidated balance-sheet total of EUR 244.3 billion, NORD/LB is a major commercial bank in Northern Germany which concentrates its business policy on Northern and North-East Europe. The bank has its main headquarters in Hannover. Furthermore, NORD/LB operates as the Landesbank for Lower Saxony and Saxony-Anhalt and acts as central savings bank in Lower Saxony, Saxony-Anhalt and Mecklenburg-Western Pomerania.
- (4) The main areas of specialisation of NORD/LB are investment, agricultural and real estate banking, corporate finance, ship and aircraft financing and private banking.
- (5) Additionally, NORD/LB maintains a presence in major financial and trading centres, including London, Singapore and New York.
- (6) The bank's rating has been downgraded by the rating agency Standard & Poors from A to A-/A-2 with negative outlook on 6 May 2009². The reasons for the down-grading are explained by NORD/LB's considerable exposure to cyclical asset classes in corporate finance, such as ship finance, commercial real estate, and large corporate lending which is expected to suffer materially from a weak economic outlook and ongoing market dislocations. The decision on the bank's down-grade was taken despite the anticipation of the aid measures provided to NORD/LB through the programme.

2.2. Initial measure (programme for issuance of guarantees in favour of NORLD/LB secured by the German Länder Lower Saxony and Saxony-Anhalt)

- (7) In autumn 2008, NORD/LB was confronted with funding shortfalls especially in the medium-term segment due to the increased issuances of State-guaranteed securities by competing credit institutions. For this reason, it became difficult for NORD/LB to place non-guaranteed securities on the market. The placement of non-guaranteed, but secured instruments (hereinafter 'Pfandbriefe'³) was also severely impaired.
- (8) In order to cover part of NORD/LB's medium-term refinancing needs a 'Secured guaranteed medium-term note programme' was established. This programme consists of medium-term securities (with a maximum maturity of five years), which are issued by a special purpose vehicle (hereinafter: 'SPV'), set up by NORD/LB. Guarantees for these securities are provided by the Länder of Lower Saxony and Saxony-Anhalt (hereinafter 'the guarantors'). For each issuance of securities the SPV provides NORD/LB with financing in the same amount. Potential claims of the SPV against NORD/LB are secured by an insolvency-proof guarantee pool (similar to Pfandbriefe).

² This information is taken from Standards and Poor's website and is dated 6 May 2009. At present, this is the only available up-to-date rating for Nord/LB.

³ The Pfandbrief is a specific type of covered bond under German law of a very high credit quality.

- (9) The measure is granted outside the German rescue scheme for credit institutions, but in line with the conditions provided for in the German rescue scheme, approved by the Commission on 12 December 2008⁴.
- (10) The above-mentioned guarantee pool is provided with a portfolio of assets which are recorded in the NORD/LB refinancing register. The outstanding nominal value of the assets of the guarantee pool must at all time amount to at least 150% of the nominal amount of the guarantees extended by the guarantors. This results in excess collateral. There is an examination of the compliance with the excess collateral on a quarterly basis as well as the obligation to provide subsequent collateral in case of a reduction.
- (11) In consideration of the high level of protection of the guarantee pool, each guarantor claims from the SPV a remuneration for the guarantee amounting to 20 basis points plus the NORD/LB 5-year CDS spread (to be determined in accordance with the European Central Bank recommendations⁵), in each case calculated on the outstanding amount of the guarantees provided.
- (12) In the event of calls on the guarantees, the guarantors have a claim for reimbursement of expenses. To secure their claims, the guarantors are granted, directly or through a security trustee, liens of equal ranking to the claim of the SPV to transfer of the securities belonging to the guarantee pool. After redemption in full of the securities it has issued, the SPV is to transfer any remaining assets to NORD/LB. Likewise, the guarantors must refund any surplus proceeds from realisation of the guarantee pool to the SPV.
- (13) The term of the guarantees amounts to a maximum of five years. In this respect, the SPV will have the possibility to issue up to 75% of the securities guaranteed under the programme (i.e. a maximum of EUR 7.5 billion per year) with a maturity of five years. The remaining at least 25% can be issued with a maturity of only up to three years.
- (14) In principle, the programme provides that State-guaranteed issues of a maximum of EUR 10 billion per year can be floated in 2009 and 2010. However, the programme has been approved for 6 months and a prolongation requires the authorisation of the Commission.

2.3. The notified measure (prolongation of the programme for a period of six months)

- (15) At this time, funding conditions for banks in general have eased. Rescue packages and individual state aid granted to banks and the extended funding provided by the ECB have prevented a further deterioration and helped re-establish market confidence to a certain extent. The 'Pfandbrief' market in Germany reopened. Credit spreads for banks have come down significantly and several banks have tested the capital markets' willingness to procure funding, albeit to a limited extent. The interbank market shows signs of revival and even unsecured lending is provided again.

⁴ Commission Decision of 12 December 2008, N 625/2008, Rescue package for financial institutions in Germany , OJ C 143, 24.06.2009, p.1.-http://ec.europa.eu/community_law/state_aids/comp-2008/n625-08.pdf

⁵ Recommendations of the Governing Council of the European Central Bank on Government Guarantees for Bank Debt of 20 October 2008.

- (16) Nord/LB, however, has only to some extent been able to profit from this more benevolent environment. NORD/LB has also access to the retail business. Furthermore, the bank has, though to a limited extent, again the possibility to issue 'Pfandbriefe'.
- (17) It is still difficult for NORD/LB to place non-guaranteed securities on the market. As a result, the refinancing of the credit business needs to be extended and the current supply of credit from NORD/LB is still in jeopardy. NORD/LB's refinancing requirements in the medium-term at least partly still depend on the guarantees provided by Lower Saxony and Saxony-Anhalt within the scope of the programme. For this reason, Germany notified a prolongation of the programme for an additional period of six months.
- (18) Since the initial approval of the programme on 22 December 2008, guarantees in the amount of EUR 3.55 billion have been granted for the issuance of fixed bonds by Lower Saxony: EUR 2 billion on 13 February 2009, EUR 50 million on 9 April 2009 and EUR 1.5 billion on 15 May 2009. Saxony-Anhalt has not granted any guarantees so far.
- (19) Until the end of 2009, NORD/LB intends to issue additional bonds in the amount of EUR 4 billion with duration above 3 years and bonds in the amount of EUR 0.5 billion with duration below 3 years. Thereof, an amount of EUR 2 billion should be placed at short notice during the third quarter of 2009. Within the scope of the programme an amount of EUR 6.45 billion could still be used within this year. For 2010, the granting of guarantees will be similar; in particular in January 2010 NORD/LB plans to issue a further bond in the amount of EUR 2 billion.

3. COMMENTS FROM GERMANY

- (20) The German authorities have notified the measure as aid to remedy a serious disturbance in the economy of a Member State within the meaning of Article 87 (3) (b) of the EC Treaty. Due to the risk that NORD/LB could become illiquid and thus may face insolvency and the serious consequences this would entail for Germany's financial system leading to a serious disturbance in the German economy, Germany argues that the measures are compatible with the common market under Article 87(3) (b) of the Treaty.

4. ASSESSMENT

4.1. Existence of State aid

- (21) Article 87(1) of the EC Treaty provides that, save as otherwise provided in the Treaty, 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.
- (22) The Commission considers that the notified guarantee for liabilities in favour of NORD/LB constitutes state aid within the meaning of Article 87(1) EC Treaty. It should be noted in particular that no market investor would grant NORD/LB such guarantees at the same conditions under the current circumstances.

4.2. Application of Article 87(3)(b) of the EC Treaty

- (23) Article 87(3)(b) allows the Commission to find state aid compatible with the common market if it remedies "a serious disturbance in the economy of a Member State". The Commission has acknowledged in its approval of the prolongation of the German Rescue package⁶ that the threat of a serious disturbance in the German economy continues and that measures supporting banks are suitable to remedy such potential disturbance.
- (24) In particular, given the systemic importance of NORD/LB the volume of funding it received from other German banks and the significance of its lending activities in particular for specific markets, the Commission accepts that its failure would entail serious consequences for the German financial sector and the real economy. The aid must therefore be assessed under Article 87(3)(b) of the EC Treaty.
- (25) In line with the Banking Communication⁷ in order for the aid to be compatible, any aid or aid scheme must comply with the general criteria for compatibility under Article 87(3) of the Treaty. Viewed in the light of the general objectives of the Treaty and in particular Articles 3(1)(a) and 4(2) thereof, this implies that the measures have to be appropriate, necessary and proportionate.

4.3. Assessment of the compatibility of the measure

- (26) Section three of the Banking Communication stipulates criteria for the compatibility of guarantees with state aid rules. First, it confirms that such aid needs to be appropriate, necessary and proportionate. Furthermore, the Banking Communication defines the range and maturities of instruments eligible for guarantees.
- (27) In its initial decision C (2008) 8985 fin of 22 December 2008 on the programme⁸, the Commission assessed the appropriateness, necessity and proportionality of the programme and concluded that the measure was compatible with the Common market under Article 87 (3)(b) of the EC Treaty. The notified measure is a prolongation of this programme and is basically identical.
- (28) In its decision C(2008) 8629 of 12 December 2008 on the German Rescue package to financial institutions⁹, the Commission established that a guarantee scheme can help to revive interbank lending and is therefore an appropriate means to overcome the present difficulties in the financial markets. In its initial decision on the programme¹⁰ the Commission indicated that it sees no reason to judge a guarantee provided by a Land

⁶ Commission Decision of 22 June 2009, N 330/2009, Prolongation of the German rescue package for financial institutions in Germany, OJ C 143, 24.06.2009, p.1.

⁷ Communication from the Commission - Application of the State Aid rules to measures taken in relation to financial institutions in the context of the current global financial crisis, OJ C 270, 25.10.2008, p. 8.

⁸ Commission Decision of 22 December 2008, N 655/2008, 'Secured guaranteed medium-term note programme', OJ C 63, 18.03.2009, p. 16..

⁹ See point 71 of Commission Decision of 12 December 2008 in case N 625/2008 Rescue package for financial institutions in Germany - OJ C 143, 24.06.2009, p.1.

¹⁰ See point 38 of Commission Decision of 22 December 2008, N 655/2008, ' Secured guaranteed medium-term note programme'.

differently from a guarantee granted by the Federal State via SoFFin, if it complies with the same criteria.

- (29) The Commission states that NORD/LB is still a suitable recipient as it meets the solvency criteria laid down in the German Rescue package to financial institutions.
- (30) As regards the material and temporary scope of instruments covered by the measure, the Commission notes that the programme provides for guarantees for bonds to be issued by NORD/LB with a maximal maturity of five years. This is valid for an issue up to 75 % of the securities guaranteed under the programme. The remaining securities (accounting for at least 25 %) can be issued for instruments with the maturity of up to three years.
- (31) Bonds are included in the eligible instruments identified in paragraph 20 of the Banking Communication. The Banking Communication focuses on short and medium term instruments and expresses the Commission's view that guarantees should be as short as possible. However, the Banking Communication allows for exceptions to this principle subject to closer scrutiny as to its justification in paragraph 24. Accordingly, the Commission had approved such longer terms in its decision authorising the programme¹¹ since it was considered adequate. However, the guarantees with a term beyond three years were limited in volume. As these conditions have not changed in relation to the prolongation of the measure, the Commission sees no reason for changing its view.
- (32) As regards necessity, the Commission notes that NORD/LB still faces difficulties to place non-guaranteed securities on the market and, therefore, its refinancing requirements continue to depend in the medium-term on the guarantee programme. For this reason, the Commission considers the prolongation of the measure as necessary to cover the bank's refinancing demands and to enable it to continue extending loans to the real economy.
- (33) Limiting aid to the minimum is further ensured by appropriate pricing of the guarantees. To achieve proportionality, the provision of liquidity guarantees requires a premium which is in line with the Recommendations of the ECB on government guarantees for bank debt¹². In its decision authorising the programme, the Commission considered the premium to be paid by NORD/LB to be appropriate¹³. The conditions which formed the basis of the calculation have not changed: NORD/LB is still an A-rated bank and the guarantee pool is sufficiently collateralised as its assets have a fair value which, irrespective the nominal value, will ensure excess collateral of 150 %. Consequently, the Commission deems the amount of the fee to be proportionate.

¹¹ Commission Decision of 22 December 2008, N 655/2008, 'Secured guaranteed medium-term note programme', see point 42 subsequent

¹² Recommendations of the Governing Council of the European Central Bank on government guarantees for bank debt of 20 October 2008.

¹³ See Points 26 and 45, 46 of Commission Decision of 22 December 2008, N 655/2008, 'Secured guaranteed medium-term note programme'.

- (34) Finally, the Commission recalls that NORD/LB has given a commitment to provide biannually a report on the guarantees and, in the event of a call on the guarantee, to present a restructuring plan within six months¹⁴.
- (35) On the basis of the above, the Commission considers the notified prolongation of the programme for further six months as in line with the criteria laid down in the Banking Communication and as compatible with the Common market under Article 87(3)(b) EC Treaty.
- (36) Under present conditions the Commission raises no objections against the prolongation of the guarantee programme. However, the Commission would like to stress that the guarantee programme in question cannot be considered as a permanent refinancing measure. Thus, a possible further request for prolongation of the guarantee programme would have to be assessed carefully, taking into account the situation of the bank and the economic environment prevailing at the time of the potential request.

5. DECISION

The Commission concludes that the measure notified by Germany on 10 July 2009 concerning the prolongation of the 'Secured guaranteed medium-term note programme' for the NORD/LB constitutes state aid according to Article 87(1) EC Treaty which has to be individually notified.

The Commission finds the aid measure to be compatible with the common market pursuant to Article 87(3)(b) of the EC Treaty and raises no objection for its prolongation for further six months.

The German authorities have indicated that the notification does not contain any confidential information. The Commission will therefore disclose this letter to third parties publishing its full text on the Internet site http://ec.europa.eu/community_law/state_aids/state_aids_texts_en.htm

Yours faithfully,

For the Commission

Neelie KROES
Member of the Commission

¹⁴ See Point 47 of Commission Decision of 22 December 2008, N 655/2008, 'Secured guaranteed medium-term note programme'.