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Analysis

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Jyske Bank A/S

STRONG JUTLAND FRANCHISE SUPPORTED BY NATIONWIDE PRESENCE UNDERPINS THE RATING

Jyske Bank (A1/P-1/B-, stable outlook) is the third largest banking group in Denmark with total assets of DKK153 billion. It has a nationwide franchise with a market share of around 6%, although it is strongest in the Jutland area where 70 out of its 122 branches, as well as its headquarters, are situated. The bank's core customer base comprises of retail clients and small-and medium-sized Danish businesses. It distributes its own products and also products from third parties, for example it distributes mortgages for Nykredit, Totalkredit and DLR.

CONSISTENT STRATEGY FOCUSED ON THE DOMESTIC MARKET WITH SOME SMALL FOREIGN DIVERSIFICATION

The bank's strategy is primarily domestically focused although the bank does have some operations abroad, including banking subsidiaries in Switzerland and Gibraltar, and branches in London, Hamburg and Fuengirola (Spain). The implementation of the RAROC project across the bank in recent years has increased the focus on the earnings of, and the allocation of capital, to the nine business units. The generation of fee and commission income is an integral part of the bank's strategy and we view this aim to diversify its earnings streams positively. As part of this the bank has positioned itself in the market as a bank which offers strong advisory services from which it hopes to generate increasing levels of fees and commissions. This also means that the branch network remains vital for the necessary face to face interaction with the customer base and as part of this the internet and other direct channels are seen primarily as a method of completing simple transactions, rather than as a sales channel. We see this as a sensible strategy for a small bank such as Jyske Bank as it differentiates them from some other players in the market.

The non-Danish operations are primarily aimed at developing private banking and asset management business, including some lending activities. These include mortgage lending on Spanish and Portuguese properties, Lombard lending to high net worth individuals with appropriate haircuts, and also some commercial lending in Gibraltar. Jyske Bank has a long and successful track record in lending in these geographies and we therefore feel comfortable with this activity.

LINK WITH NYKREDIT EXPANDS MORTGAGE OFFERING...

Since 2002 Jyske has had a co-operation agreement with Nykredit, Denmark's largest mortgage institution. This link benefits Jyske as its mortgage offering to its retail customers is expanded as customers can now choose products from Nykredit, Totalkredit or DLR.

...AND PROVIDES A PARTNER FOR JOINT VENTURES

In addition to the widening of its mortgage offering there is the scope for Jyske Bank to participate in joint ventures with Nykredit and they have already established a joint IT company based in Silkeborg. It is hoped that this will reduce annual IT costs for Jyske Bank by approximately DKK50 million over the coming years.

THE PROPOSED ACQUISITION OF TOTALKREDIT BY NYKREDIT WILL LEAD TO A SIGNIFICANT ONE-OFF GAIN FOR JYSKE BANK

If Nykredit's proposed acquisition of Totalkredit (20.46% owned by Jyske Bank) is successful then Jyske Bank would record a significant one-off gain from the sale of its stake. Although Jyske Bank continues to see organic growth as the way forward, we believe that in the longer term a deepening of the relationship between the bank and the strengthened Nykredit is not beyond the bounds of possibility, and with the inclusion of Totalkredit this would provide a third significant force in financial services in Denmark.

PROTECTED FROM HOSTILE TAKEOVER

Jyske Bank's legal status protects the bank from unwanted takeovers. Although each of the 37.5 million shares carries one voting right, the maximum number of votes allowed per shareholder is restricted to just 2,000 and 41% of the share capital is owned by entities holding less than 1,000 shares. This makes a hostile takeover highly unlikely or at least extremely expensive. We note positively that this protection has not led to any relaxation on the part of Jyske Bank's management, who continue to focus on delivering satisfactory financial results.

Financial Fundamentals

PRE-PROVISION PROFITABILITY REMAINS GOOD...

Jyske Bank's risk-weighted recurring earning power was 2.0% in 2002 up from 1.7% in 2001. Excluding the marked-to-market revaluation imposed by Danish accounting and disclosure guidelines, the results show a recurring earning power of 1.5% on a risk-weighted basis which is unchanged on last year. This performance compares well with Danish peers and reflects its strong retail franchise where returns have proved to be consistently strong in Denmark.

...AND FEE AND COMMISSION INCOME SHOULD INCREASE

Jyske Bank continues to place emphasis on fee and commission-generating services, such as investment fund management, to help further diversify its income stream (currently around 20% of total revenues when the mark-to-market revaluation is excluded). Fees and commissions are also generated through the distributing of mortgage products, and the link with Nykredit should enable these to continue to perform well. Looking ahead, we expect limited margin pressure in Denmark due to the pricing discipline put in place by the major banks, nevertheless, some pressure remains and Moody's thus views Jyske Bank's efforts to enhance fee and commission generating income positively.

ADEQUATE EFFICIENCY GIVEN THE BANKS ADVISORY STRATEGY

The bank's cost income ratio improved slightly in 2002 driven by the increased in income, however the actual cost base of the bank rose slightly. Although this increase reflects the continuing investment in branch refurbishment and organisational change (to support the RAROC project), personnel costs rose by almost 9%. The increase in the personnel costs are driven by the strategy of the bank to offer advisory services as the main thrust of its offering and this means that we would expect the cost income ratio to remain higher than some peers, nevertheless we believe that cost efficiency remains an important and ongoing challenge for Jyske if it is to continue to contend effectively in the highly competitive Danish market, and we therefore view positively the IT joint venture with Nykredit which should lead to some efficiency gains. The current rating will be strengthened if current capital investment helps deliver a narrower cost base.

SOLID ASSET QUALITY

Jyske Bank demonstrates solid asset quality with a well diversified credit exposure by sector and a relatively small average exposure. Problem loans as a percentage of gross loans were only 0.36% at the end of 2002, and loan loss reserves as a percentage of problem loans was very strong at nearly 600%. Credit exposure is overwhelmingly (80% plus) to Danish customers with the balance primarily made up of lending out of its Gibraltar subsidiary. We regard Jyske Bank's solid asset quality as a key rating driver.

DIVERSIFIED FUNDING BASE AND GOOD LIQUIDITY

Jyske Bank's funding sources are well diversified, with almost 50% of funding coming from customer deposits and around 30% from medium and long term market funding. We see the relatively low level of interbank funding as a positive given the more volatile nature of these deposits. From a liquidity standpoint the group holds a portfolio of marketable securities, which at the end of 2002 stood at approximately DKK24 billion, and this more than covers the bank's interbank funds.

STRONG CAPITAL BASE

The Tier 1 ratio was 8.2% at the end of 2002, up from 7.9% at the end of 2001, and we also believe economic capital levels to be good in view of the bank's risk profile.

Issuer Profile

HISTORY

Jyske Bank was established in July 1967, following the merger of four banks in the mid-Jutland area of Denmark. The four banks, Silkeborg Bank, Kjellerup Bank, Kjellerup Handels- og Landbobank and the Handels- og Landbrugsbank, based in the towns of Kjellerup and Silkeborg, could trace their roots back to the mid-1850s. Three other local banks subsequently joined Jyske Bank: Banken for Brødstrup og Omegn in 1968, Samsø Bank in 1970 and Odder Landbobank in 1971. With the takeover of Copenhagen-based Finansbanken in 1981, Jyske Bank achieved a nationwide franchise. It expanded further by merging with Vendelbobanken in 1983 and with Holstebro Bank in 1989.

OWNERSHIP

Jyske Bank is owned by over 210,000 share holders, of which the most important are currently Nykredit, PFA and Fidelity, the only three holders with more than 5% of the shares.

BUSINESS ACTIVITIES

Jyske Bank is a commercial bank, which provides its clients with a widely diversified range of products, both its own and those of third-party providers. The products range from general banking services to life insurance, brokerage and asset management products. With almost half a million clients, Jyske Bank continues to grow organically with an increasing number of both individual and corporate clients.

MARKET SHARES

Jyske Bank has a stable national retail market share of about 6%.

DISTRIBUTION CAPACITY

Jyske Bank operates through a network of over 100 branches with nationwide coverage. The bank also provides comprehensive Internet services to both private and corporate clients. The corporate Internet service is used for servicing all government payments, for which Jyske Bank won the contract in 2000.

NUMBER OF EMPLOYEES

At the end of 2002 the bank had over 3,300 employees.

INTERNATIONAL REPRESENTATION

Jyske Bank operates subsidiaries in Switzerland and Gibraltar and branches in London, Hamburg and Fuengirola (Spain). These are primarily aimed at developing private banking and asset management business.

Related Research

Banking Statistical Supplement:

[Denmark, June 2003 \(Doc ID# 78596\)](#)

Banking System Outlook:

[Denmark, September 2002 \(Doc ID# 76155\)](#)

Rating Methodology:

[Bank Credit Risk \(An Analytical Framework for Banks in Developed Markets\), April 1999 \(Doc ID# 44246\)](#)

To access any of these reports, click on the entry above. Note that these references are current as of the date of publication of this report and that more recent reports may be available. All research may not be available to all clients.

	12/31/02	12/31/01	12/31/00	12/31/99	12/31/98
Summary Balance Sheet (DKK million)					
Cash & central bank	708	646	788	1,030	1,124
Due from banks	12,054	10,475	13,169	11,065	6,308
Securities	24,785	25,647	22,102	19,877	20,479
Gross loans	97,359	84,457	77,204	51,508	41,334
Loan loss reserves (LLR)	-2,058	-1,920	-1,842	-1,780	-1,624
Insurance assets	0	0	0	0	0
Fixed assets	1,522	1,482	1,376	1,280	1,421
Other assets	18,800	12,368	14,562	9,515	7,844
Total assets	153,169	133,156	127,359	92,495	76,886
Total assets (USD million) [1]	21,621	15,786	16,066	12,482	12,016
Total assets (EUR million)	20,629	17,831	17,053	12,423	10,293
Demand deposits	33,284	29,284	24,390	23,223	21,794
Savings deposits [2]	25,679	25,109	27,877	26,590	22,021
Due to banks	17,210	17,484	22,380	25,124	17,452
Market funds	43,362	36,964	26,902	192	623
Insurance liabilities	0	0	0	0	0
Other liabilities	24,378	15,442	17,781	10,550	9,389
Total liabilities	143,912	124,283	119,331	85,678	71,279
Subordinated debt	2,600	2,663	2,110	1,395	434
Shareholders' equity	6,658	6,174	5,887	5,391	5,108
Total capital funds	9,258	8,873	8,028	6,816	5,607
Total liabilities & capital funds	153,169	133,156	127,359	92,495	76,886
Derivatives - notional amount	1,010,697	1,692,781	1,574,989	1,153,852	897,420
Derivatives - replacement value	13,500	7,347	—	—	—
Contingent liabilities	17,247	17,310	15,404	14,426	12,723
Risk weighted assets (RWA)	84,186	79,798	74,216	62,137	52,800
Assets under management (DKK million) [3]	19,900	20,000	16,000	—	—
Number of employees	3,359	3,418	3,190	3,013	2,856
Summary Income Statement					
+Interest income	6,394	6,796	5,847	3,913	4,083
-Interest expense	3,748	4,346	3,712	1,888	2,047
=Net interest income	2,646	2,450	2,135	2,025	2,037
+Trading income	565	303	594	683	-264
+Fee & commission income	758	668	760	646	594
+Insurance income (net)	0	0	0	0	0
+Other operating income	267	311	231	227	253
=Operating income	4,237	3,731	3,719	3,582	2,619
-Personnel expenses	1,507	1,385	1,234	1,130	1,019
-Other operating expenses	941	908	789	706	593
= Operating funds flow	1,789	1,437	1,696	1,746	1,007
-Amortisation/depreciation	150	149	119	168	101
(Total operating expenses)	2,598	2,442	2,142	2,004	1,712
=Preprovision income (PPI)	1,639	1,288	1,577	1,577	907
-Loan loss provisions	408	286	318	258	249
+Other non operating adjustments [4]	-148	-112	-5	-44	52
+Extraordinary profit / loss	0	0	0	0	0
=Pretax income	1,083	890	1,255	1,276	710
-Taxes	572	267	172	379	198
=Net income	511	624	1,083	897	511
-Minority interests	0	4	0	-1	7
=Net income (group share)	511	619	1,083	898	505
Growth Rates (%)					
Gross loans	15.28	9.39	49.89	24.61	8.68
Total assets	15.03	4.55	37.69	20.30	21.89
Customer deposits (demand and savings)	8.40	4.07	4.93	13.69	5.69
Net interest income	8.03	14.74	5.43	-0.57	10.16
Fee and commission income	13.59	-12.10	17.63	8.70	8.75
Operating expenses	6.39	14.00	6.90	17.04	-4.75
Preprovision income	27.20	-18.31	-0.03	74.02	-2.09
Net Income	-17.48	-42.82	20.59	77.96	15.87

	12/31/02	12/31/01	12/31/00	12/31/99	12/31/98
Income Statement in % Average Risk Weighted Assets					
Net interest income	3.23	3.18	3.13	3.52	4.03
Trading income	0.69	0.39	0.87	1.19	-0.52
Fee and commission income	0.93	0.87	1.11	1.12	1.18
Insurance income	0.00	0.00	0.00	0.00	0.00
Operating income	5.17	4.84	5.46	6.23	5.19
Operating expenses	3.17	3.17	3.14	3.49	3.39
Preprovision income	2.00	1.67	2.31	2.74	1.79
Loan loss provisions	0.50	0.37	0.47	0.45	0.49
Extraordinary profit	0.00	0.00	0.00	0.00	0.00
Net income	0.62	0.81	1.59	1.56	1.01
Liquidity, Funding (including sub debt) & Balance Sheet Composition					
Avg. liquid assets % avg. total assets	25.95	27.95	30.94	35.35	36.19
Avg. gross loans % avg. total assets	63.50	62.05	58.54	54.81	56.71
Avg. customer deposits % avg. total funding	48.52	49.57	56.65	67.43	75.01
Avg. interbank funds % avg. total funding	14.85	18.53	26.36	30.66	23.68
Avg. market funds (excl. interbank) % avg. total funding	34.38	29.68	15.04	0.59	0.55
Avg. sub debt % avg. total funding	2.25	2.22	1.95	1.32	0.76
Avg. liquid assets % avg. customer deposits	65.56	68.28	66.64	63.96	59.40
Avg. gross loans % avg. customer deposits	160.39	151.57	126.09	99.16	93.08
Avg. market funds reliance [5]	3.11	-5.83	-37.36	-65.21	—
Avg. RWA % avg. total assets	57.27	59.12	62.02	67.86	72.17
Breakdown of Operating Income in %					
Net interest income % operating income	62.46	65.66	57.40	56.54	77.77
Trading income % operating income	13.34	8.11	15.98	19.08	-10.10
Fee & commission income % operating income	17.90	17.90	20.42	18.03	22.68
Insurance income % operating income	0.00	0.00	0.00	0.00	0.00
Other operating income % operating income	6.30	8.33	6.20	6.35	9.65
Profitability					
Yield on avg. earning assets (%)	5.05	5.89	6.05	5.26	6.44
Cost of interest bearing liabilities (%)	3.21	4.04	4.12	2.72	3.60
Net interest margin (%)	2.12	2.18	2.25	2.75	3.24
Recurring earning power (PPI % avg. assets)	1.14	0.99	1.43	1.86	1.30
Risk-weighted recurring earning power (PPI % avg. RWA)	2.00	1.67	2.31	2.74	1.79
Return on average assets (%)	0.36	0.48	0.99	1.06	0.73
Return on avg. RWA (%)	0.62	0.81	1.59	1.56	1.01
Return on equity (period end) (%)	7.68	10.03	18.40	16.66	9.88
Net interest income coverage of loan loss provisions	6.49	8.56	6.72	7.85	8.18
Loan loss provisions % preprovision income	24.88	22.20	20.15	16.36	27.45
Internal capital growth (%)	8.28	10.52	20.09	15.00	8.03
Dividend payout ratio (%)	0.00	0.00	0.00	14.70	24.96
Efficiency					
Cost/income ratio (operating expenses % operating income)	61.32	65.47	57.60	55.96	65.38
Operating expenses % average assets	1.81	1.87	1.95	2.37	2.45
Operating income / employee (DKK thousand)	1261.40	1091.47	1165.94	1188.68	916.95
Operating expenses / employee (DKK thousand)	773.53	714.54	671.58	665.13	599.54
PPI / employee (DKK thousand)	487.87	376.93	494.37	523.55	317.40
Total assets / employee (DKK million)	45.60	38.96	39.92	30.70	26.92
Asset Quality and Risk Measurement					
Problem loans % gross loans	0.36	0.46	0.35	0.63	0.77
LLR % problem loans	594.76	494.28	679.38	552.21	507.12
LLR % gross loans	2.11	2.27	2.39	3.46	3.93
Loan loss provisions % gross loans	0.42	0.34	0.41	0.50	0.60
Problem loans % (shareholders' equity + LLR)	3.97	4.80	3.51	4.50	4.76
Replacement value % shareholder's equity	202.77	119.00	—	—	—
Capital Adequacy (Period End)					
Tier 1 ratio (%)	8.20	7.90	8.00	8.20	9.50
Total capital ratio (%)	11.30	11.40	11.00	10.50	10.40
Shareholders' equity % total assets	4.35	4.64	4.62	5.83	6.64
Equity participations % shareholders' equity	5.47	7.79	9.52	2.15	3.13

[1] USD figure uses historical exchange rate against the DKK.

[2] Full disclosure may not be available for all years. The amount is then included in demand deposits.

[3] As reported by the bank

[4] This may include value adjustments of securities.

[5] Avg. [(market funds-liquid assets) % (earning assets-liquid assets)]

Coupon	Type of Debt	Maturity	Moody's Rating
Jyske Bank A/S			
—	Euro MTN Program	—	A2
—	Euro MTN Program	—	A1
6.725%	Sub. Euro Medium Term Notes	2026	A2
7.000%	Sub. Fix/Flt Rt. Euro Medium Term Notes	2024	A2
5.650%	Sub. Euro Medium Term Notes	2023	A2
—	Sub. Flt Rt Euro Medium Term Notes	2023	A2
—	Sub. Flt Rt Euro Medium Term Notes	2008	A2
4.800%	Euro Medium Term Notes	2018	A1
—	Flt Rt Euro Medium Term Notes	2011	A1
—	Flt Rt Euro Medium Term Notes	2010	A1
—	Flt Rt Euro Medium Term Notes	2010	A1
—	Flt Rt Euro Medium Term Notes	2008	A1
—	Flt Rt Euro Medium Term Notes	2007	A1
—	Flt Rt Euro Medium Term Notes	2007	A1
—	Flt Rt Euro Medium Term Notes	2006	A1
—	Flt Rt Euro Medium Term Notes	2005	A1
—	Flt Rt Euro Medium Term Notes	2005	A1
—	Flt Rt Euro Medium Term Notes	2005	A1
—	Flt Rt Euro Medium Term Notes	2003	A1
—	Medium-Term Note Program	—	P-1
—	Bank Financial Strength Rating	—	B-
—	Long-Term Bank Deposit Rating	—	A1
—	Short-Term Bank Deposit Rating	—	P-1

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