

Credit Opinion: Jyske Bank A/S

Global Credit Research - 22 Dec 2011

Silkeborg, Denmark

Ratings

Category	Moody's Rating
Outlook	Stable
Bank Deposits	A2/P-1
Bank Financial Strength	C
Baseline Credit Assessment	(A3)
Adjusted Baseline Credit Assessment	(A3)
Senior Unsecured	A2
Subordinate MTN	(P)Baa2
Jr Subordinate	Baa2 (hyb)
Pref. Stock	Baa3 (hyb)
Other Short Term	(P)P-1

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Key Indicators

Jyske Bank A/S (Consolidated Financials)[1]

	[2]9-11	[2]12-10	[2]12-09	[2]12-08	[3]12-07	Avg.
Total Assets (DKK million)	246,960.0	244,114.2	224,510.0	236,301.7	214,278.7	[4]3.6
Total Assets (EUR million)	33,188.0	32,757.9	30,172.3	31,747.3	28,737.0	[4]3.7
Total Assets (USD million)	44,528.6	43,946.1	43,289.5	44,130.2	42,015.0	[4]1.5
Tangible Common Equity (DKK million)	14,332.1	14,006.2	12,362.9	10,116.2	9,501.8	[4]10.8
Tangible Common Equity (EUR million)	1,926.0	1,879.5	1,661.5	1,359.1	1,274.3	[4]10.9
Tangible Common Equity (USD million)	2,584.2	2,521.4	2,383.8	1,889.2	1,863.1	[4]8.5
Net Interest Margin (%)	1.9	2.0	2.0	1.6	1.8	[5]1.9
PPI / Avg RWA (%)	1.9	2.8	3.3	1.5	1.9	[6]2.4
Net Income / Avg RWA (%)	0.4	0.8	0.5	0.5	1.4	[6]0.5
(Market Funds - Liquid Assets) / Total Assets (%)	-1.7	3.7	7.6	9.0	9.0	[5]5.5
Core Deposits / Average Gross Loans (%)	95.3	85.0	79.6	77.7	80.4	[5]83.6
Tier 1 Ratio (%)	14.1	13.6	13.5	9.9	8.1	[6]12.8

Tangible Common Equity / RWA (%)	13.6	13.3	12.3	8.6	7.2[6]12.0
Cost / Income Ratio (%)	68.9	58.7	51.0	67.6	59.2[5]61.1
Problem Loans / Gross Loans (%)	--	6.4	5.8	2.0	0.8 [5]3.8
Problem Loans / (Equity + Loan Loss Reserves) (%)	--	41.5	41.6	22.1	9.7[5]28.7

Source: Moody's

[1] All ratios are adjusted using Moody's standard adjustments [2] Basel II; IFRS [3] Basel I; IFRS [4] Compound Annual Growth Rate based on IFRS reporting periods [5] IFRS reporting periods have been used for average calculation [6] Basel II & IFRS reporting periods have been used for average calculation

Opinion

SUMMARY RATING RATIONALE

Moody's rates Jyske Bank A2/Prime-1/C. The C bank financial strength rating (BFSR) assigned to Jyske Bank, which translates into a baseline credit assessment (BCA) of A3, reflects the bank's good domestic franchise and relatively low risk profile. However, the rating is constrained by the bank's limited net profit and volatile earnings (due to mark-to-market adjustments), as well as the ongoing need to focus on its managing asset quality, particularly that of large single-name exposures through the economic downturn.

The A2 global local currency (GLC) rating incorporates the bank's A3 BCA, as well as one-notch uplift from systemic support.

Credit Strengths

- Good domestic franchise
- Adequate core profitability
- Satisfactory capitalisation

Credit Challenges

- Increasing core earnings in a low growth environment to offset deteriorating asset quality
- Expected pressure on funding following the implementation of Bank Package III
- Some credit concentration in the lending portfolio
- Preserving asset quality across the economic cycle in a continued challenging environment

Rating Outlook

Jyske Bank's ratings carry a stable outlook, being well positioned in their current rating category.

What Could Change the Rating - Up

A sustainable improvement in asset quality and earnings could exert upward pressure on the ratings. However, Moody's does not see this as likely in the short term.

What Could Change the Rating - Down

The BFSR could be downgraded in the event of further deterioration in the bank's asset quality, increased

funding costs, increased levels of single-borrower exposure, or pressure on earnings.

Recent Results and Company Events

RECENT RESULTS

Jyske Bank Group reported for the first nine months of 2011 a pre-provision profit of DKK 1.4 billion, down 32% year-on-year. The lower pre-provision profitability was mainly driven by a decrease in mark-to-market value adjustment on the fixed income portfolio as a result of low interest levels and volatility in the markets (a loss of DKK 70 million vs. a DKK 424 million profit in Q3 2010). Net interest & fee income was down 2% at DKK 4.4 billion compared to the same period last year. Employee and administrative expenses were up 10% compared to Q3 2010 as a result of severance costs from staff reductions that were carried out in September 2011. Loan loss provisions, decreased by 35% compared to Q3 2010, but overall pre-tax profit fell year-on-year (DKK 426 million vs. DKK 601 million in Q3 2010). The Group's Tier 1 and total capital ratios were 14.1% and 15.6% respectively at Q3 2011, compared with an individual solvency requirement of 10%.

COMPANY EVENTS

In May 2011, Moody's Investors Service concluded the review initiated in February 2011 and downgraded Jyske Bank's long-term debt and deposit ratings to A2 from A1 and the stand alone BFSR to C from C+. The review followed similar actions taken for other Danish banks and reflected a reduction of Moody's systemic support assumptions for the Danish banking market to low from high. The downgrade of Jyske Bank's BFSR to C from C+ and debt and deposit ratings to A2 from A1 reflects Moody's assessment that core profitability will be under pressure going forward due to the low-growth environment with increasing funding costs. Increased deposit competition and market concerns related to Bank Package III also increase the vulnerability of Jyske Bank's funding and liquidity positions. Following the review, Jyske bank's debt and deposit ratings continue to include one notch of systemic support uplift.

DETAILED RATING CONSIDERATIONS

Detailed considerations for Jyske Bank's currently assigned ratings are as follows:

Bank Financial Strength Rating

Moody's assigns a C BFSR to Jyske Bank, reflecting the bank's good qualitative credentials and solid regulatory practices, but constrained by factors such as its loan portfolio concentration, particularly its single-loan exposure, and the less benign Danish economy. The assigned C BFSR is in line with the outcome of Moody's bank financial strength scorecard.

Qualitative Rating Factors (50%)

Factor 1: Franchise Value

Trend: Neutral

Jyske Bank enjoys a solid franchise as one of the leading banks in Denmark, with total assets of DKK244 billion (EUR 33 billion) at YE 2010. A large proportion of mortgage loans originated by the bank are financed by Totalkredit, DLR Kredit and Nykredit Realkredit, and as such do not appear on the bank's balance sheet.

Jyske Bank had an approximate 7% market share of total deposits in Denmark at YE 2010. The bank has a nationwide presence, with its strongest franchise in Jutland, where the majority of its branches and its headquarters are located.

Furthermore, around 10% of its earnings in 2010 stem from its foreign operations, which primarily focus

on private banking and asset management. In addition to its wholly owned subsidiaries and branches, Jyske Bank has asset management operations in the Netherlands via its 60% stake in asset management firm Berben's Effectenkantoor.

Jyske Bank has cooperation agreements with mortgage and life insurance providers, which enable it to maintain cost efficiency while maintaining market share.

Moody's believes the overall score of C for franchise value adequately reflects these strengths and challenges.

Factor 2: Risk Positioning

Trend: Neutral

As of December 2010, the bank had around 238,000 shareholders. Each share carries one vote, with a maximum of 4,000 votes permitted for any one shareholder. As of YE 2010, the only two shareholders with more than 5% of total shares were Nykredit Realkredit (7.2%) and Baillie Gifford & Co. Ltd (5.1%). Given the high proportion of shareholders with a relatively low stake in Jyske Bank, and the restriction in voting rights, we consider a hostile takeover to be unlikely.

Jyske Bank largely complies with the corporate governance rules set by the Copenhagen Stock Exchange. However, those relating to voting rights are not considered to be in line with the bank's strategy and are duly not followed.

The bank's score for risk positioning is negatively influenced by high borrower concentration, as discussed in the "asset quality" section below.

The bank utilises a Value-at-Risk (VaR) model with a time frame of one day and with a 99% confidence level. Jyske's VaR for interest-rate, currency and stock-market risk amounted to DKK12 million in 2010, compared with DKK16 million in 2009. The main component of the VaR figure is interest-rate risk.

Jyske Bank scores C- for risk positioning.

Factor 3: Regulatory Environment

This factor does not address bank-specific issues; instead, it evaluates whether regulatory bodies are independent and credible, whether they demonstrate enforcement power, and whether they adhere to global standards of best practice for risk control. Please refer to Moody's most recent Banking System Outlook on Denmark for a detailed discussion of the regulatory environment.

Factor 4: Operating Environment

Trend: Neutral

This factor is common to all Danish banks. Moody's assigns an A- score for the overall operating environment. Please refer to Moody's most recent Banking System Outlook on Denmark for a detailed discussion of the operating environment.

Quantitative Rating Factors (50%)

Factor 5: Profitability

Trend: Weakening

For the the first nine months of 2011, Jyske Bank reported a pre-tax profit of DKK 426 million, down 30% from DKK 600 million in Q3 2010, which was mainly attributable to a loss on the securities portfolio, as

well as increased employee and administrative expenses.

Net interest income historically contributes the major component of operating income (close to 70%) but decreased slightly by 3% year-on-year. The increase in interest income from DKK 4.7 billion to DKK 5 billion year-on-year, in particular from trading and investment, was partly offset by higher expenses on issued bonds and deposits. Fee & commission income accounts for around 20% of operating income, and was largely unchanged compared to Q3 2010

The bank's operating expenses (excluding costs under banking package I) increased 10% following an increase in employee expenses due to severance costs for staff reductions carried out in the third quarter of 2011.

It will be important for Jyske Bank to improve its core top-line results going forward in order to mitigate any deterioration of the loan portfolio.

Jyske Bank scores C for profitability, but with a weakening trend reflecting upward pressure on funding costs, although these are somewhat mitigated by the expiry of costs associated with banking package I (costing the bank DKK506 million in 2010). Given that the economic environment remains challenging and its potential impact on asset quality, we also expect that the need for loan loss provisions will remain elevated in the near future and thereby maintain pressure on the bank's net earnings.

Factor 6: Liquidity

Trend: Neutral

Jyske Bank's deposit funding profile is improving. As of Q3 2011, deposits covered almost 95% of gross loans and accounted for approximately 50% of Jyske Bank's total funding (up from DKK 98.5 billion in Q3 2010 to DKK 112.4 billion in Q3 2011). Interbank funding decreased nearly 30% during the period (now accounting for about 11.5% of the bank's total funding), with market funding making up the remainder.

In addition, the bank continues to place its mortgage loans with Nykredit Realkredit, Totalkredit and DLR.

Moody's notes that Jyske Bank has not participated in the Danish government's funding support scheme (banking package II) and that the bank was able to issue DKK2.5 billion on a standalone basis during 2010. While the bank was able to raise a further EUR 500 million in May 2011, in Moody's opinion, funding pressure will increase going forward post Bank Package III. The political agreement "Bank Package IV", announced in August 2011 and proposed in law in December, supports banks that have liquidity problems during a takeover process. Although the package was successfully used in the resolution of Max Bank in October 2011, it remains to be seen to what extent willing acquirers can be found so that this mitigating tool can be used.

Key System Performance Measures

At Q3 2011, the bank's liquid assets stood at nearly 40% of total assets, giving it a satisfactory liquidity profile, since a majority of these assets can be used for repos with the central bank.

Jyske Bank increased its asset-backed portfolio to DKK3.4 billion at the end of 2010 (DKK2.6 billion at the end of 2009). Moody's notes that ECB-repo eligible Aaa rated European RMBSs make up the bulk of the asset backed portfolio.

We believe a score of C is appropriate for the bank's liquidity.

Factor 7: Capital Adequacy

Trend: Neutral

Jyske Bank reports strong capitalisation ratios. At end-September 2011, Jyske Bank's Tier 1 ratio stood at 14.1%, with a total capital adequacy ratio of 15.6%, as calculated under transitional rules towards full Basel II. The corresponding figures at Q3 2010 were 13.9% and 15.6%, respectively. The individual solvency requirement for the bank is 10%, which as of end-September 2011 meant the bank had a capital cushion exceeding its individual requirement of DKK 5.8 billion (equivalent to 6.8% of total loans to customers). Moody's notes that hybrid capital accounts for close to 11% of total Tier 1 capital.

The bank scores A for capital adequacy.

Factor 8: Efficiency

Trend: Weakening

Jyske Bank's cost-to-income ratio weakened to 68% at end-September 2011 from 58% at end-September 2010, mainly due to the higher employee and administration costs, partly one-off severance costs.

In September 2010, the bank announced a strategic cooperation agreement with Bankdata, a provider of IT solutions. The bank expects that the cooperation will lead to efficiency savings for the bank's IT department of around DKK 200 million as of 2013.

We believe a score of C for efficiency is appropriate, but include a weakening trend signalling further pressure on cost management in the still challenging macroeconomic environment.

Factor 9: Asset Quality

Trend: Weakening

At end-September 2011, loan impairments accounted for around 70% of pre-provision income. Loans for which an objective indication for impairment occurred almost tripled from DKK2.7 billion (2.0% of gross loans) in 2008 to DKK7.5 billion (6.4% of gross loans) in 2010. Jyske Bank reports that, after haircuts, almost half of total credit exposure was unsecured as of year-end 2010.

Only around 35% of total lending and guarantees were to private individuals at YE2010, as the mortgage loans financed via Totalkredit, Nykredit and DLR do not appear on Jyske Bank's balance sheet.

Jyske Bank's largest industry exposures include credit, finance and insurance at around 20%, property administration & services at around 10%, and manufacturing, mining, electricity and gas at almost 10%. The loan book is mainly focused on Denmark (almost 90%).

When looking at top 20 limits for single-name exposures, not taking collateral into consideration, in relation to Tier 1 capital, Jyske Bank's borrower concentration is high when compared with that of other European banks and placed in the "E" bucket, but this is in line with many Nordic banking peers.

Based on our expectations of a decline in asset quality indicators, we have assigned a weakening trend to this factor, with Jyske Bank scoring D+ on 2008-10 average asset quality ratios.

Global Local Currency Deposit Rating (Joint Default Analysis)

Moody's assigns a global local currency deposit rating of A2 to Jyske Bank. In view of the bank's position in Denmark and strength in its local area of Jutland and despite its only moderate nationwide coverage, the A2 global local currency deposit rating receives a one-notch uplift from the A3 BCA.

Notching Considerations

The ratings for the Bank's hybrid obligations are notched off the BCA according to "Moody's Guidelines

for Rating Bank Hybrid Securities and Subordinated Debt" released on 17 November 2009.

Foreign Currency Deposit Rating

The A2 foreign currency deposit ratings of Jyske Bank are unconstrained given that Denmark, in common with other EU members, has a country ceiling of Aaa.

Foreign Currency Debt Rating

The A2 foreign currency debt ratings of Jyske Bank are unconstrained given that Denmark, in common with other EU members, has a country ceiling of Aaa.

ABOUT MOODY'S BANK RATINGS

Bank Financial Strength Rating

Moody's Bank Financial Strength Ratings (BFSRs) represent Moody's opinion of a bank's intrinsic safety and soundness and, as such, exclude certain external credit risks and credit support elements that are addressed by Moody's Bank Deposit Ratings. Bank Financial Strength Ratings do not take into account the probability that the bank will receive such external support, nor do they address risks arising from sovereign actions that may interfere with a bank's ability to honor its domestic or foreign currency obligations. Factors considered in the assignment of Bank Financial Strength Ratings include bank-specific elements such as financial fundamentals, franchise value, and business and asset diversification. Although Bank Financial Strength Ratings exclude the external factors specified above, they do take into account other risk factors in the bank's operating environment, including the strength and prospective performance of the economy, as well as the structure and relative fragility of the financial system, and the quality of banking regulation and supervision.

Moody's uses the Baseline Credit Assessment (BCA) to map BFSRs onto the 21-point Aaa-C rating scale and like the BFSR, it reflects a bank stand-alone default risk. Each point on the Aaa-C scale represents a specific probability of default and therefore allows Moody's to use the BCA as an input to Moody's Joint Default Analysis (JDA), described below. The baseline credit assessment reflects what the local currency deposit rating of the bank with the given BFSR would be without any assumed external support from a government or third party

Global Local Currency Deposit Rating

A deposit rating, as an opinion of relative credit risk, incorporates the Bank Financial Strength Rating as well as Moody's opinion of any external support. Specifically, Moody's Bank Deposit Ratings are opinions of a bank's ability to repay punctually its deposit obligations. As such, Moody's Bank Deposit Ratings are intended to incorporate those aspects of credit risk relevant to the prospective payment performance of rated banks with respect to deposit obligations, and includes: intrinsic financial strength, sovereign transfer risk (in the case of foreign currency deposit ratings), and both implicit and explicit external support elements. Moody's Bank Deposit Ratings do not take into account the benefit of deposit insurance schemes which make payments to depositors, but they do recognize the potential support from schemes that may provide assistance to banks directly.

According to Moody's joint default analysis (JDA) methodology, the global local currency deposit rating of a bank is determined by the incorporation of any external elements of support into the bank's Baseline Credit Assessment. In assigning the local currency deposit rating to a bank, the JDA methodology also factors in the rating of the various potential support providers (parent company, cooperative group, regional or national governments), as well as the degree of dependence that may exist between each one of them and the bank. Moody's assessment of the probability of systemic support (by a national government) is derived from the analysis of the capacity of a government and its central bank to provide support on a system-wide basis. The systemic support indicator is determined for a particular country and

serves as an input for all bank ratings in that country. The support indicator can be set at, above or, in rare cases, below the government's local currency bond rating for that country.

Foreign Currency Deposit Rating

Moody's ratings on foreign currency bank obligations derive from the bank's local currency rating for the same class of obligation. The implementation of JDA for banks can lead to high local currency ratings for certain banks, which could also produce high foreign currency ratings. Nevertheless, it should be noted that foreign currency deposit ratings are in all cases constrained by the country ceiling for foreign currency bank deposits. This may result in the assignment of a different, and typically lower, rating for the foreign currency deposits relative to the bank's rating for local currency obligations.

Foreign Currency Debt Rating

Foreign currency debt ratings are derived from the bank's local currency debt rating. In a similar way to foreign currency deposit ratings, foreign currency debt ratings may also be constrained by the country ceiling for foreign currency bonds and notes; however, in some cases the ratings on foreign currency debt obligations may be allowed to pierce the foreign currency ceiling. A particular mix of rating factors are taken into consideration in order to assess whether a foreign currency bond rating pierces the country ceiling. They include the issuer's global local currency rating, the foreign currency government bond rating, the country ceiling for bonds and the debt's eligibility to pierce that ceiling.

About Moody's bank financial strength scorecard

Moody's bank financial strength model (see scorecard below) is a strategic input in the assessment of the financial strength of a bank, used as a key tool by Moody's analysts to ensure consistency of approach across banks and regions. The model output and the individual scores are discussed in rating committees and may be adjusted up or down to reflect conditions specific to each rated entity.

Rating Factors

Jyske Bank A/S

Rating Factors [1]	A	B	C	D	E	Total Score	Trend
Qualitative Factors (50%)						C+	
Factor: Franchise Value						C	Neutral
Market Share and Sustainability		x					
Geographical Diversification			x				
Earnings Stability				x			
Earnings Diversification [2]							
Factor: Risk Positioning						C-	Neutral
Corporate Governance [2]	--	--	--	--	--		
- Ownership and Organizational Complexity	--	--	--	--	--		
- Key Man Risk	--	--	--	--	--		
- Insider and Related-Party Risks	--	--	--	--	--		
Controls and Risk Management		x					
- Risk Management			x				
- Controls	x						

Financial Reporting Transparency		x					
- Global Comparability	x						
- Frequency and Timeliness	x						
- Quality of Financial Information		x					
Credit Risk Concentration	--	--	--	--	--		
- Borrower Concentration	--	--	--	--	--		
- Industry Concentration	--	--	--	--	--		
Liquidity Management			x				
Market Risk Appetite	x						
Factor: Operating Environment						A-	Neutral
Economic Stability		x					
Integrity and Corruption	x						
Legal System	x						
Financial Factors (50%)						C	
Factor: Profitability						C	Weakening
PPI / Average RWA - Basel II		2.53%					
Net Income / Average RWA - Basel II				0.57%			
Factor: Liquidity						C	Neutral
(Mkt funds-Liquid Assets) / Total Assets			6.76%				
Liquidity Management			x				
Factor: Capital Adequacy						A	Neutral
Tier 1 Ratio - Basel II	12.34%						
Tangible Common Equity / RWA - Basel II	11.43%						
Factor: Efficiency						C	Weakening
Cost / Income Ratio			59.12%				
Factor: Asset Quality						D+	Weakening
Problem Loans / Gross Loans			4.75%				
Problem Loans / (Equity + LLR)				35.06%			
Lowest Combined Score (15%)						D+	
Economic Insolvency Override						Neutral	
Aggregate Score						C	
Assigned BFSR						C	

[1] - Where dashes are shown for a particular factor (or sub-factor), the score is based on non public information [2] - A blank score under Earnings diversification or Corporate Governance indicates the risk is neutral



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