

## **CORRECTION: FITCH PLACES FIVE GERMAN LANDESBANKEN IDRS ON RWN**

Fitch Ratings-London/Frankfurt-14 September 2009: This announcement corrects the version issued earlier today. The Support Rating of Landesbank Baden-Wuerttemberg is affirmed at '1', and not placed on RWN.

Fitch Ratings today placed the Long-term Issuer Default Ratings (IDRs) of Bayerische Landesbank (BayernLB), HSH Nordbank (HSH), Landesbank Baden-Wuerttemberg (LBBW), Landesbank Saar (SaarLB) and WestLB AG (WestLB) on Rating Watch Negative (RWN). In addition, the Short-term IDRs of BayernLB, WestLB, LBBW and SaarLB were placed on RWN as well as the Support Rating Floors of all five banks. A full rating breakdown is provided at the end of this comment.

The five banks' IDRs remain at their Support Rating Floors and are based on Fitch's view of the extent to which the respective German regional governments would provide support in case of need. Any ownership change could reduce the likelihood of state support for the banks, compounding the effects of the gradual expiration of the vast majority of grandfathered guaranteed debt up until 2015. However, Fitch anticipates that state support will still remain strong enough for all of the Landesbanks, with the possible exception of WestLB, to remain within the single 'A' range ('A-', 'A' or 'A+') in the foreseeable future.

The RWN reflect the possibility of ownership change and a related diminution in the importance of these banks to their regional state owners. BayernLB, HSH, LBBW and WestLB have received substantial support from their owners in the form of capital injections and guarantees after they suffered a material impact from the financial crisis. For the first three banks, these support measures are currently subject to a review and approval process by the European Commission (EC), which is expected to communicate its decision in the coming months. A downgrade of these banks' IDRs is likely if the EC's conditions include a change in ownership. WestLB's state aid has already been approved by the EC with conditions imposed, specifically the change of ownership until the end of 2011. While the RWN on BayernLB, HSH, LBBW and SaarLB will be reviewed by Fitch, as the EC's decisions on each of HSH, BayernLB and LBBW are announced, WestLB's RWN will remain pending until details of its future ownership structure become clear - in 2011 at the latest. The RWN on SaarLB's IDRs reflects the pressures on its 75.1% parent BayernLB to restructure.

Fitch believes that the sustainability of all Landesbanken's business models will continue to rely on direct or indirect state ownership and/or institutional support from the savings banks in the medium term, as the agency will outline in an upcoming report.

Even in a stabilised economic environment, the combination of the Landesbanken's weak stand-alone quality and reliance on wholesale funding sources will likely prevent them from funding their (even reduced) balance sheets on competitive terms on their own merits, depending on their various sources of funding. Therefore, developments in the restructuring processes of BayernLB, HSH and LBBW may result in negative rating actions for each bank over a longer period of time after the EC's decisions on the respective banks. However, Fitch notes that the pressure on these Landesbanken's IDRs could ease if there are clear signs that a change of ownership structure is neither given as a condition of approving state aid by the EC nor likely to arise willingly by the owners. More certainty in this respect is unlikely before there are more tangible signs that the economic crisis, and accompanying deterioration of asset quality, is nearing its end.

HSH has suffered most from the global financial and economic crisis. It has received comprehensive support measures from its state owners and has initiated an ambitious restructuring process. This increases the uncertainty about the bank's ability to manage the restoration of a viable business model post-restructuring. HSH's majority owners, the relatively small regional states of

Hamburg (HH) and Schleswig-Holstein (SH), went to great lengths to rescue their Landesbank, constraining their own financial flexibility as a result. The local savings banks, HSH's minority owners, largely disengaged themselves by not participating in the latest capital increase. Fitch remains confident of the ability of both states to provide support if needed, as underlined by their 'AAA' ratings. However, if the EC were to order the sale of HSH, the regional public sector may not insist on retaining a substantial stake in HSH.

WestLB had required state support even prior to the current crisis. As such its restructuring process is ahead of its peers. It was the first to ring-fence a considerable volume of troubled and non-core assets into a segregated run-off portfolio. It is also the only Landesbank that has announced its intention to use the bad bank scheme recently adopted by the federal parliament. The EC has completed its review of the state aid received and imposed an ownership change by end-2011. Fitch believes that, in view of the enduring recessionary environment and protracted sale endeavours, uncertainty will continue, potentially further unsettling potential clients and long-term debt investors. This may reduce the bank's chances of emerging as a strong going concern, making it unlikely that WestLB's owners will manage to attract interest from a majority private investor.

BayernLB and, to a lesser extent, LBBW, might also face stringent restructuring requirements and ownership changes. Even if pressure for these does not come from the EC this time around, a renewed need for capital injections, although currently not expected, from the owner states cannot be fully excluded, due to the two banks' considerable loan portfolios and potential for mounting credit losses. This, or the potential implementation of a bad bank model, would in turn trigger a new review by the EC, increasing the risk of ownership change. However, the stronger franchises held by the two south German banks may enable them to achieve faster recoveries, reducing the probability that they would need renewed support. Fitch also expects BayernLB's and LBBW's core franchises to remain important to their respective regional governments even after any potential sale or merger (full or partial) with another Landesbank. Bayern LB and LBBW's IDR's are unlikely to fall below 'A-' in the foreseeable future, due to the superior financial flexibility of their regional governments, Bavaria and Baden-Wuerttemberg, as well as the strategic relevance of these banks for their states.

SaarLB has not received any state support and therefore is not undergoing any restructuring or compensatory demands from the EC although it may be indirectly affected by the EC approval of state aid for BayernLB. In addition, a change in its ownership structure is possible in the near term, with the state of Saarland planning to take up some of BayernLB's stake.

The rating actions follow a comprehensive review of the German Landesbank sector, in which Fitch has investigated the key parameters that will influence the strength of external support in the foreseeable future. These include the severity of shortcomings exposed by the current adverse economic conditions; the amount of external support needed and received since the outbreak of the crisis; the suitability of the restructuring processes to address the key issues faced by the banks; the sustainability of their resulting business models; and (in most cases still awaited) compensatory measures imposed by the EC in return for the state help received. The conclusions of the review will be published in an upcoming report.

The rating actions taken today are as follows:

Bayerische Landesbank

Long-term IDR 'A+' placed on RWN

Short-term IDR 'F1+' placed on RWN

Individual rating: affirmed at 'D/E'

Support rating: affirmed at '1'

Support Rating Floor 'A+' placed on RWN

HSH Nordbank AG

Long-term IDR 'A' placed on RWN

Short-term IDR affirmed at 'F1'

Individual rating: affirmed at 'D/E'

Support rating: affirmed at '1'

Support Rating Floor 'A' placed on RWN

Landesbank Baden-Wuerttemberg  
Long-term IDR 'A+' placed on RWN  
Short-term IDR 'F1+' placed on RWN  
Individual rating: affirmed at 'C/D'  
Support rating: affirmed at '1'  
Support Rating Floor 'A+' placed on RWN

Landesbank Saar  
Long-term IDR 'A+' placed on RWN  
Short-term IDR 'F1+' placed on RWN  
Individual rating: 'C'; RWN  
Support rating: affirmed at '1'  
Support Rating Floor 'A+' placed on RWN

WestLB AG  
Long-term IDR 'A-' placed on RWN  
Short-term IDR 'F1' placed on RWN  
Individual rating: affirmed at 'E'  
Support rating '1' placed on RWN  
Support Rating Floor 'A-' placed on RWN

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