Covered Bond & SSA View

NORD/LB Markets Strategy & Floor Research

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Investment strategy recommendation and marketing communication
(see disclaimer on the last pages)

Agenda

Our latest publications:

Issuer Guide Covered Bonds 2020

Issuer Guide German Bundeslaender 2020

Canadian Provinces & Territories 2020

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Covered Bonds
Market overview

Analyst: Henning Walten, CIIA

Brisk issuance activity continues

Numerous issuers again approached their investors with covered bonds in the EUR benchmark segment over the past five trading days. Three separate issuers each placed covered bonds on the market last Wednesday and Thursday. Firstly, BAWAG issued a 10y bond at ms +7bp. With a final order book of EUR 2.8bn, the deal was substantially oversubscribed in comparison with the issuance volume of EUR 750m. Secondly, Eika Boligkreditt also made an appearance in the market last Wednesday, having previously issued its first benchmark of the current year back at the beginning of March. This latest bond has a term of 7.5 years and a volume of EUR 500m. Following initial guidance in the area of ms +12bp, the transaction was ultimately placed five basis points tighter at ms +7bp on account of high demand (final order book: EUR 1.5bn). Thirdly and finally, the trio of issuers was rounded off by NN Bank, which is now responsible for both the last deal from the Netherlands before the summer break and the first Dutch transaction after the resumption of covered bond activities on the market. As was the case with the deal placed on 30 June, this latest deal features a soft bullet structure issued under the bank's recently established soft bullet programme. In addition, NN Bank has a total of five outstanding EUR benchmarks in CPT format. The most recent transaction for EUR 500m and with a term to maturity of 15y was issued on the market at ms +12bp and was 5x oversubscribed. Moreover, this was the only deal seen in the past five trading days to offer investors a positive yield at issue (0.081%). On Thursday, Desjardins from Canada, CFF from France and Sparebanken Vest from Norway then also launched deals on the market. At 5.2 years and 5 years respectively, the deals from Sparebanken Vest and Desjardins therefore rank among the shortest-dated transactions since the end of the summer break. While the bond issued by Sparebanken Vest (EUR 500m; ms +6bp) already marked the third deal from Norway after the end of the summer break, Desjardins was the first Canadian issuer in the market for EUR benchmarks since 20 March. At that time, the primary market exclusively contained issuances from Canada and France between 11 March and 28 April. In contrast to the demand seen for primary market transactions back then, the most recent Canadian deal generated substantial interest. With an oversubscription ratio of 4.2x and an issuance volume of EUR 500m, the bond ranks among the most heavily oversubscribed transactions seen in recent times. Last Thursday, an additional French bank, namely CFF, approached its investors to place the second-largest deal after CAFFIL (EUR 1.5bn) since the end of the summer break. This bond had a volume of EUR 1.25bn with a term to maturity of 10y and was placed at ms +7bp.

Issuer	Country	Timing	ISIN	Maturity	Volume	Spread	Rating
Sparebanken Vest	NO	17:09.	XS2237321190	5.2y	0.50bn	ms +6bp	- / Aaa / -
Desjardins	CA	17:09.	XS2148051621	5.0y	0.50bn	ms +9bp	AAA / Aaa / -
CFF	FR	17:09.	FR0013536950	10.0y	1.25bn	ms +7bp	- / Aaa / AAA
Eika Boligkreditt	NO	16:09.	XS2234711294	7.5y	0.50bn	ms +7bp	- / Aaa / -
NN Bank	NL	16:09.	NL0015614611	15.0y	0.50bn	ms +12bp	-/ - /AAA
BAWAG	AT	16:09.	XS2234573710	10.0y	0.75bn	ms +7bp	- / Aaa / -

Source: Bloomberg, NORD/LB Markets Strategy & Floor Research (Rating: Fitch / Moody's / S&P)

NORD/LB

Public sector Pfandbrief marks sub-benchmark debut from SaarLB

In addition to the brisk issuance activity in the EUR benchmark segment, one issuer was also active in the sub-benchmark segment in the form of SaarLB. For the Saarbrücken-based bank, in which the Bundesland of Saarland holds a stake of around 75% and the Sparkassenverband Saar (Association of Savings Banks in Saarland) owns approximately 25%, this was its inaugural sub-benchmark transaction. The public sector Pfandbrief worth EUR 250m featured a term to maturity of 10 years and was eventually placed at ms +8bp, with initial guidance having been in the area of ms +12bp. This deal primarily generated domestic interest (89% of the transaction allocation was attributable to Germany) in the amount of EUR 575m. You can find comprehensive information on the underlying cover pool totalling EUR 3.4bn (Q2 2020) and the cover pool for mortgage-backed Pfandbriefe in our quarterly publication "NORD/LB Covered Bond Special - Transparency requirements §28 PfandBG".

Nationwide Building Society buys back around EUR 2.2bn in covered bonds

After we reported on the buy-back offer presented by Nationwide Building Society in last week's edition of this publication, the results of this transaction have now been published. Accordingly, the bank has bought back covered bonds worth the equivalent of around EUR 2.2bn overall spread across seven of the eleven ISINs on offer. Looking at the EUR benchmarks offered for buy-backs, for which the buy-back volume was limited to EUR 3.0bn, a total of EUR 1.58bn was accepted. This resulted in a ratio of 52.8%. This value is therefore well above that attributable to the three German banks (approx. 25%) to have already bought back EUR-denominated benchmarks so far in 2020. Of the five GBP benchmarks offered for buy-backs, deals were closed under just two ISINs (XS1806359714 and XS2100384853). The converted volume for these deals is equivalent to EUR 655.2m.

Nationwide Building Society: Buy-back volume of the EUR benchmarks on offer

ISIN	Bond	Amount outstanding (EUR)	Accepted amount (EUR)	Remaining volume (EUR)	Fixed spread	Purchase price
XS1130066175	NWIDE 0 3/4 10/29/21	1,000m	128.5m	871.5m	-1bp	101.383
XS1308693867	NWIDE 0 3/4 10/26/22	1,000m	0m	1,000m	+3bp	Not applicable
XS1569896498	NWIDE 0 1/2 02/23/24	1,000m	341.4m	658.6m	-6bp	103.590
XS2004366287	NWIDE 0.05 06/03/24	1,250m	709.1m	540.9m	-3bp	102.061
XS1207683522	NWIDE 0 5/8 03/25/27	750m	250m	500m	-3bp	106.857
XS1638816089	NWIDE 1 3/8 06/29/32	1,000m	154.6m	845.4m	+9bp	117.067

Source: Issuer, NORD/LB Markets Strategy & Floor Research

SSA/Public Issuers
Market overview

Analyst: Dr Norman Rudschuck, CIIA

Funding of E-supras in Q4

For the fourth quarter of the year, all Luxembourg E-supras will reassemble in the primary market. The EFSF is planning funding of a further EUR 5bn from October onwards, while the ESM has revised its figure upwards to a considerable EUR 2.0bn. At present, the EIB is at more than EUR 60bn and has authorisation up to EUR 65bn, although the actual funding target is always lower than the authorisation. We expect that a further EUR 2bn could be possible. If the EIB were to exceed this figure, prefunding for 2021 would then commence.

Results of the 158th tax revenue estimate

The results of the 158th tax revenue estimate indicate that Germany is financially well positioned, despite the coronavirus crisis. Based on the forecast, tax revenue this year will be steady compared with the May estimate. According to the press release, any shortfall in revenue during the remaining forecast period (2021-2024), compared with the May estimate, is mainly attributable to a lowering of the tax burden. This is a measure intended to safeguard the liquidity of both citizens and companies. It should be noted that this year, the temporary VAT reduction alone will result in a shortfall in tax receipts of around EUR 20bn and the child bonus in a further shortfall in revenue of EUR 4bn. Both of these measures were implemented after the last tax revenue estimate and were not therefore taken into account in the May tax revenue estimate. The trend in tax revenue for the entire forecast period is determined by the unprecedented support measures to help manage the economic impact of the coronavirus pandemic. For the Bund, the federal government, the shortfall in revenue amounts to EUR 9.2bn. In contrast, the Laender and municipalities are recording surplus revenue of EUR 9.3bn and EUR 1.4bn respectively. The Working Party on Tax Revenue Estimates revised its forecast for 2021 by EUR -19.6bn (Bund: EUR -10.6bn), for 2022 by EUR -5.5bn (Bund: EUR -1.1bn), for 2023 by EUR -4.4bn (Bund: EUR -1.2bn) and for 2024 by EUR 0.0bn (Bund: EUR +3.0bn). The surplus revenue expected for the federal government in 2024 essentially results from lower EU payments, as explained in the press release. In addition, Finance Minister Olaf Scholz announced last week that the planning for the coming year included new borrowing of EUR 96.2bn. For this purpose, the debt brake will need to be suspended again at federal level, as has also been the case this year. Otherwise, the maximum possible new debt in 2021 would be EUR 10bn, which is far too low. From 2022 onwards, the debt brake is then to be re-activated under the current planning.

"Bremen Fonds" fund and tablets for schools

The economic policy programme and money from the European Union are just some of the instruments which Bremen intends to use. Bremen's own share has a name: "Bremen-Fonds". This fund is worth a total of EUR 1.2bn. To fill the fund, the Land of Bremen is raising loans worth EUR 900m. The municipality of Bremen is contributing EUR 300m and the city of Bremerhaven EUR 70m. To make this possible, the Bremen parliament suspended the restrictive regulations of the debt brake in Bremen's state constitution before the summer recess. The loans for the Bremen-Fonds will need to be serviced from the budget, starting in 2024 over a 30-year period, with an annual amount of EUR 40m to EUR 50m. The programme is to have an economic stabilising effect, for example, on public sector companies (e.g. Bremer Straßenbahn AG trams, Bremen Airport etc.). The Mayor mentioned the development of hydrogen business, sustainable air travel, e-mobility and the establishment of Bremerhaven, in particular, as a centre of government shipbuilding. With regard to hydrogen production, Bremen already took action with a project in January this year, H2B – roadmap project for the gradual defossilisation of the steel industry and urban infrastructure by means of hydrogen electrolysis in Bremen. An amount of EUR 10m is to be invested in developing Bremen's city centre as well as in support for the hotel and hospitality industry. Bremen's economy has been hard hit by the coronavirus crisis, as it is heavily dependent on exports and in view of its major focus on industry. Major players from industrial circles are hoping to strengthen research and development at Airbus in Bremen, the automotive industry, investment in the digitisation of care and a new structure for retail. Furthermore, all school pupils in Bremen are to be equipped with 100,000 tablets, free of charge, to be rolled out in two stages (EUR 51m). Stage 1 comprises 30,000 tablets for low-income families and 7,680 teaching staff including trainee teachers. In the second phase, all other children and young people attending state schools are then to receive tablets on loan free of charge.

Primary market

Last Wednesday, NRW Bank placed a bond worth EUR 1.0bn with a 10y maturity in the market. With a final order book of EUR 1.9bn, the deal was met with a good level of demand. Consequently, the bond was issued one basis point tighter than the guidance (ms +4bp area) at ms +3bp. The issuing yield amounted to -0.198%. At 57%, investors from the German-speaking DACH region dominated in terms of the geographical allocation. With regard to investor type, bank treasuries (61%) were predominant. Berlin was present last Thursday with a tap issue (BERGER 0.01 07/02/30), raising EUR 250m at ms -1bp and increasing the original bond volume of EUR 500m. Another tap issue of EUR 250m was implemented on the same day by the EIB. Based on demand of more than EUR 950m, the increase was completed at ms -11bp, with the volume of EIB 0 05/15/28 now amounting to EUR 1.25bn. With only one new benchmark bond issue and two tap issues in the past five trading days, the primary market was more or less on a break, following the previous five trading days during which eight deals were placed in the market.

Issuer	Country	Timing	ISIN	Maturity	Volume	Spread	Rating
NRWBK	DE	16.09.	DE000NWB9056	10.0y	1.00bn	ms +3bp	AAA / - / AA

Source: Bloomberg, NORD/LB Markets Strategy & Floor Research (Rating: Fitch / Moody's / S&P)

Covered Bonds
Bausparkasse Schwäbisch Hall plans inaugural EUR benchmark

Analyst: Henning Walten, CIIA

Investor calls to pave the way for inaugural EUR benchmark bond issue

Last week, Bausparkasse Schwäbisch Hall AG issued a mandate for conducting investor calls, which are to start today, Wednesday. The aim is to approach investors with a benchmark transaction as early as the fourth quarter of this year, although no concrete details are to be announced regarding the possible maturity. This will mark Schwäbsich Halls first time the EUR benchmark segment is to be used to place Pfandbriefe. The issue forms part of the building society's long-term strategic direction. Following its first Pfandbrief issue last year, the strategy encompasses a stronger focus on including mortgage Pfandbriefe in its funding strategy. For this reason and in view of the imminent debut from Bausparkasse Schwäbisch Hall in the EUR benchmark segment, we take a closer look at both the issuer and the mortgage cover pool as well as the market for Pfandbriefe from German building societies in the following.

Schwäbisch Hall with a focus on building society savings and housing finance

Bausparkasse Schwäbisch Hall has a market share of 29.7%, making it the biggest building society in Germany according to its own information. Its activities are mainly based in the business divisions of building society saving ("Bausparen") and housing finance. In financial year 2019, new business in the building savings segment amounted to EUR 28.5bn based on around 524,000 new contracts. Both figures represented a slight decrease on the previous year. The volume of building society deposits totalled EUR 63.7bn as at the end of the financial year. The volume of building savings deposits amounted to EUR 63.7 billion at the end of the financial year, whereas the target contract sums of the contract portfolio amounted to EUR 313.4 billion. In the segment of housing finance, the building society posted a new record in 2019 with a volume of new business of EUR 16.7bn (incl. intermediary activities). In addition to domestic business, the building society also has activities outside Germany in Hungary, Slovakia and China. Overall, Bausparkasse Schwäbisch Hall has around 9 million customers, of which more than 7 million are based in Germany, indicating a clear domestic focus on the part of the institution. As a member of the Genossenschaftliche FinanzGruppe (cooperative financial group), the building society relies on this network for its sales and additionally employs a field sales force of around 3,300 workers. The majority shareholder is DZ BANK, with a 96.8% stake. The remaining 3.2% is held by 600 cooperative banks. As at 31 December 2019, the Schwäbisch Hall Group, which mainly comprises the parent company Bausparkasse Schwäbisch Hall AG and, in addition, subsidiaries and affiliated companies in Germany and abroad, had total assets of EUR 77.5bn and a CET1 ratio of 31.4%. Pre-tax profit amounted to EUR 189m. A profit transfer agreement is in place between DZ BANK and the building society. The cost-income ratio was 71.6% and the LCR ratio 249.4%.

Four German building societies currently have a Pfandbrief licence

As part of the amendment of the Bausparkassengesetz (BausparG, Building Society Act) and the Bausparkassen-Verordnung (BausparV, Building Society Directive) implemented in 2015, it became possible for German building societies to issue mortgage Pfandbriefe for specific purposes. Wüstenrot Bausparkasse (mortgage Pfandbrief licence since 12 April 2017), Bausparkasse Mainz (13 June 2018), Alte Leipziger Bauspar (28 November 2018) and Bausparkasse Schwäbisch Hall (2 January 2019) are currently the four building societies with such a licence. At the end of the second quarter of 2020, Wüstenrot Bausparkasse had Pfandbriefe outstanding worth EUR 1,777m, Bausparkasse Schwäbisch Hall a volume of EUR 6m, Bausparkasse Mainz EUR 10m and Alte Leipziger Bauspar had not yet issued any Pfandbriefe at the time. Wüstenrot Bausparkasse additionally had placed two issues in the EUR sub-benchmark segment (EUR 250m ≤ X < EUR 500m) and placed EUR 300m for 8.1 years at ms -10bp in 2017 and EUR 250m in 2018 for eight years at ms -4bp. Bausparkasse Schwäbisch Hall would be the first German building society to have an EUR benchmark bond outstanding in the covered bond segment.

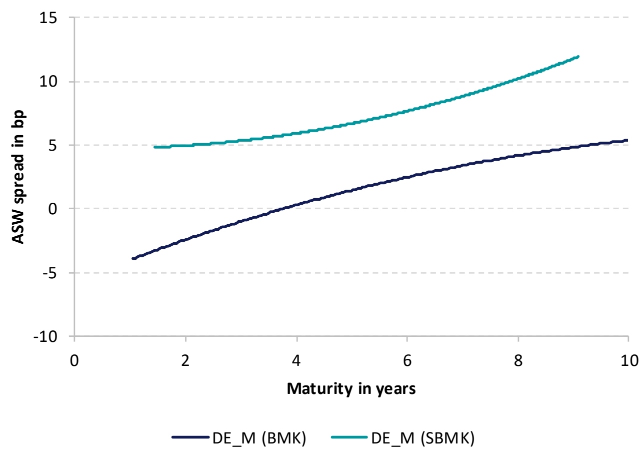
Cover pool not yet sufficient for benchmark bond issue

As at 30 June 2020, the cover pool volume of Bausparkasse Schwäbisch Hall amounted to EUR 373.2m. At the same time, it had mortgage Pfandbriefe outstanding of a volume of only EUR 6m, producing an overcollateralisation ratio of more than 6,000%. Assuming the imminent issue would amount to EUR 500m, it is evident that such an issue would first require the cover pool to be increased. The extent to which such an increase would change the features and characteristics of the cover pool in its current form, as shown below, cannot be predicted at this stage. However, we assume that at its core, the nature of the cover pool would be maintained in view of the focused housing finance activities of Bausparkasse Schwäbisch Hall.

Programme data

30 June 2020	Mortgage
Covered bonds outstanding	EUR 6.0m
Cover pool volume	EUR 373.2m
Current OC (nominal / legal)	6,119.7% / 2.0%
Type	99.5% Residential
Main country	100.0% Germany
Main region	32.1% Bavaria
Number of borrowers	4,565
Average exposure size	EUR 129,500
Share of largest 10 exposures	1.8%
Fixed interest (Cover Pool / CBs)	100.0% / 100.0%
WAL (Cover Pool / CBs)	10.3y / 3.9y
CB Rating (Fitch / Moody's / S&P)	- / Aaa / -

Spread overview – Germany

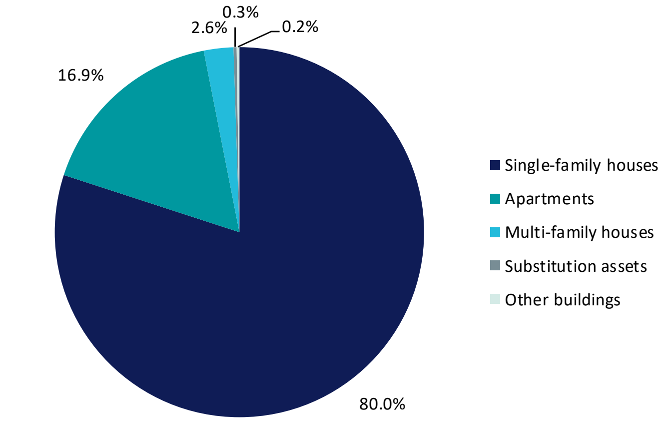


Source: issuer, rating agencies, Bloomberg, NORD/LB Markets Strategy & Floor Research

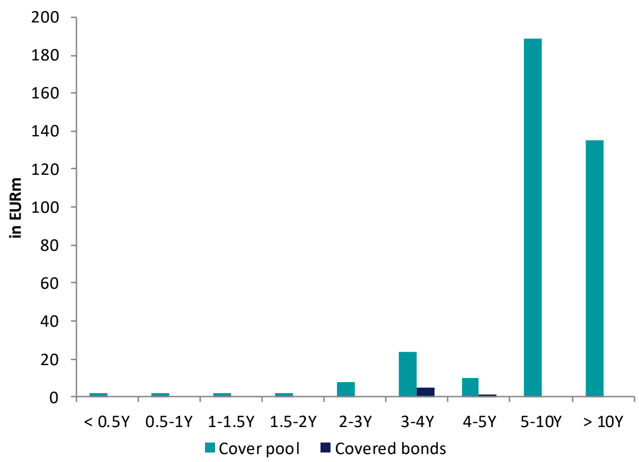
Geographical focus on southern Germany

The mortgage cover pool of Bausparkasse Schwäbisch Hall comprises 99.5% residential property assets. Commercial property assets account for a further 0.2%, in the form of other commercially used buildings, and assets serving as substitute cover for 0.3%. As illustrated in the chart below, the majority of cover assets are loans to finance single-family homes (80.0%) and apartments (16.9%). Multi-family dwellings, which are also included in the residential property segment, account for 2.6% of cover assets. At 91.0%, the share of owner-occupied homes is high. All cover assets are located in Germany and denominated in EUR. The ten largest exposures account for a share of 1.8% and have an average loan amount of EUR 129,500. The cover pool can therefore be described as granular. As part of the necessary increase in cover assets ahead of the planned new bond issue, the cover pool is likely to benefit in terms of its granularity, since the current number of loans and/or borrowers (2,867 and 4,565 respectively) will increase. From a geographical point of view, the loans granted are focused on Bavaria (32.1%) and Baden-Württemberg (21.7%). This means than more than half of the loans relate to the two Bundeslaender in southern Germany. With North Rhine-Westphalia also represented in the cover pool with a share of 14.0%, the cover pool also includes the most densely populated federal state.

Cover pool by type and use



Maturity pattern of the cover pool



Source: issuers, vdp, NORD/LB Markets Strategy & Floor Research

Ratings & regulatory aspects

The bond issues of Bausparkasse Schwäbisch Hall currently have Aaa ratings from Moody's. We therefore assume that Moody's will also rate the planned bond issue at Aaa. The rating agency assigned a low collateral score of 5.0% based on the data as at the end of the second quarter of the year. Cover pool losses were also assessed as low at 15.7%. In addition, the TPI is "high" and the TPI leeway is seven notches, meaning that the covered bonds of the building society feature a significant rating buffer (cf. NORD/LB Covered Bond & SSA of 16 September 2020). Based on an amount issued of (minimum) EUR 500m, the imminent EUR benchmark bond issue would be regarded as a Level 1 asset for the purposes of LCR management, in our opinion. It would also benefit from a privileged risk weighting as per the CRR of 10%. Furthermore, the transaction would be eligible for purchasing by the Eurosystem under both CBPP3 and the PEPP.

Conclusion

With the latest announcement regarding investor calls, Germany's biggest building society is getting ever closer to its first EUR benchmark bond issue. The planned debut in the fourth quarter of this year forms part of the financial institution's funding strategy and was made possible by an amendment of the Bausparkassengesetz (Building Society Act) in 2015, which has enabled building societies to issue mortgage Pfandbriefe for specific purposes since then. While currently four German building societies have a licence to issue Pfandbriefe, to date only Wüstenrot Bausparkasse has been present in the market for publicly placed deals in form of two sub-benchmark bond issues. The imminent EUR benchmark debut of Bausparkasse Schwäbisch Hall therefore marks a further milestone in Germany's Pfandbrief history and may pave the way for other building societies to gain access to the segment of publicly placed (sub-) benchmark bond issues.

SSA/Public Issuers
Update: Auckland Council – Investment alternative in Down Under

Analyst: Dr Norman Rudschuck, CIIA

New Zealand – Australia's smaller neighbour

With regard to the economy in this part of the world, Australia and New Zealand are often mentioned in the same breath. They maintain a close cooperation on numerous levels. The CER (Closer Economic Relations) agreement has guaranteed tariff-free trading between Australia and New Zealand since 1990. Moreover, negotiations have been underway since 2004 to introduce a joint domestic market. Due to their historical status as colonies of the British Empire, both countries also share Western cultural values and as a result are to be regarded as Western economies, despite their isolated location. Even though New Zealand is significantly smaller than Australia both in terms of area and population, it is nevertheless one of the most developed industrial countries in the world. As at 2019 (GDP PPP), it ranked just behind the UK but ahead of countries such as France and Japan in terms of GDP per capita. Over the past few years, New Zealand has attracted the attention of the global financial markets due to its positive economic growth as well as a supportive investment climate, which arose not least as a result of high demand for alternative investment opportunities outside of the eurozone. It is therefore worth taking another look at New Zealand and providing an update on this country.

Covid-19 in the South Pacific – between eradication and renewed lockdown

For months, New Zealand was regarded by the international community as the role model for successfully combatting the coronavirus. Once the first case of coronavirus was discovered in New Zealand at the end of February and infections were reported from all areas of the country a month later, the Prime Minister Jacinda Ardern imposed a strict lockdown. In addition to closing all public institutions, citizens were only allowed to leave their homes to purchase essential supplies. Breaches of the rules were punished strictly. The government's rigorous approach had an immediate impact, with the result that the Ministry of Health was able to declare New Zealand officially "free of coronavirus" on 8 June. Consequently, social life rapidly reverted to normal; masks disappeared from public view and sporting events were once again held in front of terraces packed with spectators. New cases of coronavirus were solely attributable to returning travellers, who were sent directly to quarantine upon arrival in the country. After 102 days without any new infections, four members of a family based in Auckland tested positive for coronavirus in mid-August. To date, the authorities are unaware of the source of the infection. The immediate imposition of a lockdown for the entire region surrounding New Zealand's largest city succeeded in preventing the virus from spreading further. Currently, there are 61 active cases in New Zealand and no more new infections, which is why the restrictions have been eased once more. As a consequence of the pandemic, the parliamentary elections scheduled for 19 September were postponed by four weeks until 17 October. This measure is expected to ensure that the elections and election campaign can be carried out smoothly, according to Prime Minister Ardern.

Organisation as a "federal centralised state"

Originally part of the colony of New South Wales, New Zealand did not become a colony of the British Empire in its own right until 1841. Administrative autonomy was then granted in 1852, when its own parliament was formed. In 1907, the country was given the title Dominion of New Zealand and was granted independence from British rule. The statute of Westminster, which the British government passed in 1931 and which was accepted by the New Zealand government in 1947, granted full legal independence to all Commonwealth dominions. Today, as opposed to countries such as Australia, New Zealand is not organised in a federal structure. Instead, the central government has created different administrative areas. In 1974, 2002 and 2010, reforms were introduced that affected these administrative areas. The regional administration of New Zealand is currently divided into eleven regional councils and 67 territorial authorities, with further differentiations within these categories.

Division of powers as defined in the New Zealand constitution (examples)

Central government	Regions	Territories
Defence	Natural disaster management	Waste disposal/sewage
Foreign policy	Port security and marine pollution	Local road construction
Finance	Public transport	Water supply
International trade and industry	Environmental protection and management	Healthcare
Family law	Civil defence	Maintenance of parks and reserves
Social security system		

Source: Department of Internal Affairs, NORD/LB Markets Strategy & Floor Research

Status of the territories

Compared with the regions, New Zealand's 67 territorial authorities are smaller administrative units which are found within a particular region. However, some territorial authorities can span more than one region (unitary authorities). There are 13 city councils and 54 district councils. The difference between the two lies solely in the population size. A territorial authority is classified as a city council when the population size reaches 50,000 or more. Moreover, six of the territories are also classified as regions and, as a result, they perform a dual function. This variant is known as a unitary authority. Regardless of the term under which it is classified, each territory has the same responsibilities. As opposed to the regions, these responsibilities are less environmentally-orientated and more focused on providing the population with the necessary infrastructure (water, sewage, roads, healthcare, etc.). However, they also carry out control functions such as construction supervision and inspection activities. On account of the largely centrally organised state system, there is little to no political representation or participation at regional level. The territories cover funding costs by raising fees, payments and taxes on property, specific services or fuel. They also receive funding from the central government for the maintenance and expansion of their road networks and other public transport routes. As a result, they are also obligated to develop appropriate long-term and annual plans and budgets, to audit these in order to verify whether and how successfully their aims have been met and to report on their results.

Status of the regions

As a unitary authority, Auckland is one of the few regions of New Zealand which may autonomously use the capital market for funding purposes. Moreover, the council has successfully placed several EUR-denominated bonds since March 2014; three of these issuances have even been in benchmark format. As a result, there are now four bonds outstanding; three of these are actually benchmarks, with a total cumulative volume of EUR 1,685m. As a result, Auckland is of increasing interest to European investors. The EUR supply from New Zealand has, thanks to AUCKCN, therefore already outstripped the total raised by all Australian sub-sovereigns.

Regions as an equivalent to federal states

The fact that New Zealand is organised as a central state with different administrative levels makes it difficult to draw a comparison with nations such as Australia and Germany that are organised along federal lines. Nevertheless, the regions of New Zealand correspond the most to a sub-sovereign of a federal state. The smaller size of the individual regions and the comparatively smaller funding requirement that this entails makes Auckland Council a particular focal point.

Brief regulatory classification

We will not expand upon the regulatory framework conditions in New Zealand and its sub-sovereigns in full at this point. Instead, we refer to the corresponding section in our Issuer Guides and shall briefly list what we believe to be the likely classifications.

Risk weighting	0% (based on New Zealand's current ratings: AA / Aaa / AA)
LCR classification	Level 1
NSFR classification	5%
Solvency II classification	Non-preferred

The issuer: Auckland Council (NZ)

As detailed above, Auckland Council is a unitary authority. It was created in 2010 as part of the amalgamation of the seven territories in the region and the region of Auckland. This amalgamation created New Zealand's largest local administrative entity, with a population of over 1.7 million (approximately one third of the total population of New Zealand). Overall, 1.5 million people live in the city of Auckland alone. It is also the largest city in the country. Historically, Auckland began to develop as the new capital of New Zealand from 1841. However, it lost this title to Wellington in 1865. Nevertheless, the city grew quickly as a military base and was also the gateway to New Zealand for immigrants from Europe. Even today, the majority of international visitors to New Zealand arrive at Auckland airport. Additionally, the port is an important trading centre for goods, with a greater volume of containers handled here than anywhere else in the country. During the 1980s, many businesses relocated their headquarters from Wellington to Auckland. In addition, many international firms operate their New Zealand headquarters out of Auckland. The city’s economy is predominantly shaped by the tertiary sector, with Auckland generating approximately 38% of the total GDP of New Zealand. Auckland boasts a wealth of institutes of higher education. In the Mercer rankings for quality of living, Auckland regularly occupies the top positions. It was ranked third in the most recent edition of this study. Population growth is also above average: indeed, this is already at a high level in New Zealand as a whole, with the country’s population having grown by 7.2% over the past five years. However, global urbanisation and the city's high level of attractiveness have caused Auckland's population to rocket by 11.5% across the same time frame.

Special features of AUCKCN bonds

When considering Auckland Council, a special feature only becomes apparent at second glance: the outstanding bonds are "secured notes" and are repaid from future taxes or levies. Should bonds default, creditors are treated preferentially ahead of other claimants to property. There is also a green bond framework under which an inaugural issuance (NZD 200m) was placed in June 2018.

General information

Outstanding bond volume

EUR 3.8bn (EUR equivalent)

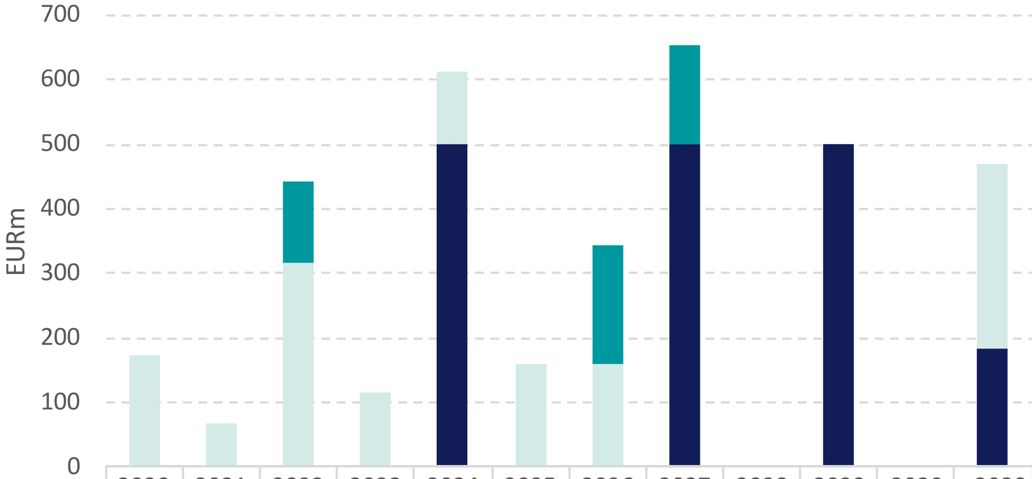
Of which EUR bonds

EUR 1.7bn

Bloomberg ticker

AUCKCN

Auckland Council – outstanding bonds



	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	>2030
AUD	0	0	127	0	0	0	185	154	0	0	0	0
NZD	175	66	315	115	115	158	160	0	0	0	0	285
EUR	0	0	0	0	500	0	0	500	0	500	0	185

Foreign currencies are converted into EUR at rates as at 18 September 2020.
Source: Bloomberg, NORD/LB Markets Strategy & Floor Research

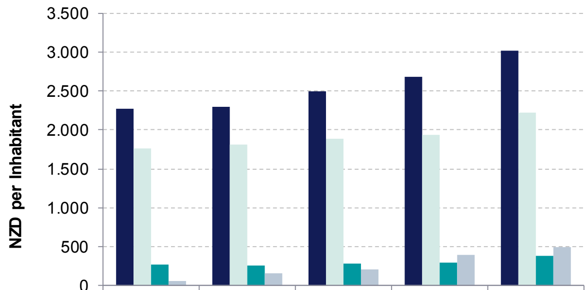
Outstanding bonds

Auckland Council has the equivalent of approximately EUR 3.8bn outstanding, with the majority of the bond volume (44.0%) actually denominated in EUR, followed by the domestic currency NZD (28.8%). It is then followed by the AUD and CHF. There are 26 bonds outstanding in total. Maturities for the rest of 2020 amount to the equivalent of EUR 175m. Given the issuer's openness to currency diversification, we see further EUR potential here. The longest outstanding bond is "green" (2050) and denominated in NZD. This is also always worth looking at for international, sustainable investors. The longest EUR bond is currently due in 2034 (EUR 185m). The three EUR benchmarks are due to be refinanced in 2024, 2027 and 2029.

Assessment of the ratings

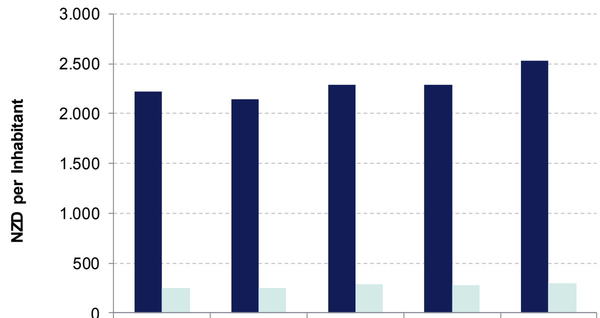
The two rating agencies Moody's (Aa2) and S&P (AA) both rate Auckland Council two notches below the top rating AAA (stable outlook). This assessment in both ratings reflects the well-diversified economy, which also offers further potential for growth in future due to the expanding population. Auckland's financial management also operates in New Zealand's exceptionally reliable and professional environment. At the same time, as a unitary authority, Auckland has stable revenues plus flexibility in its spending policy. Substantial investment – a necessity given the comparatively rapid population growth – in infrastructure measures (City Rail Link, Watercare and road construction) is fundamentally to be seen as positive for the opportunities for growth, but is resulting in a significant debt burden for the council. At the same time, the trend in debt is the critical factor driving future expectations for the rating. Accordingly, a reversal in the trend towards higher debts would probably lead to a positive outlook and to the rating being upgraded in future.

Development of revenue in NZD per capita



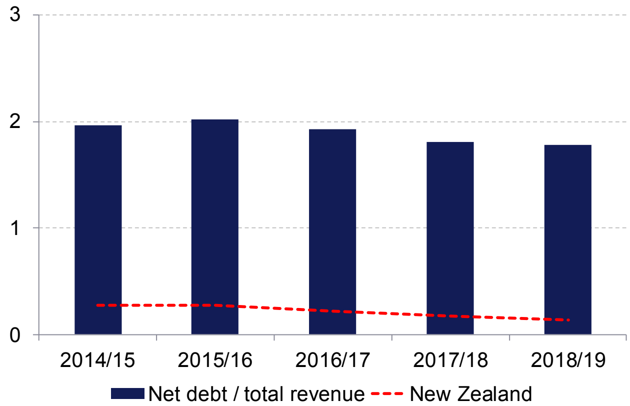
	2014/15	2015/16	2016/17	2017/18	2018/19
Total revenue	2.266	2.295	2.492	2.679	3.014
Own-source-revenue	1.757	1.811	1.890	1.941	2.226
Transfers	271	250	277	293	378
Balance	51	155	205	389	488

Development of expenditure in NZD per capita

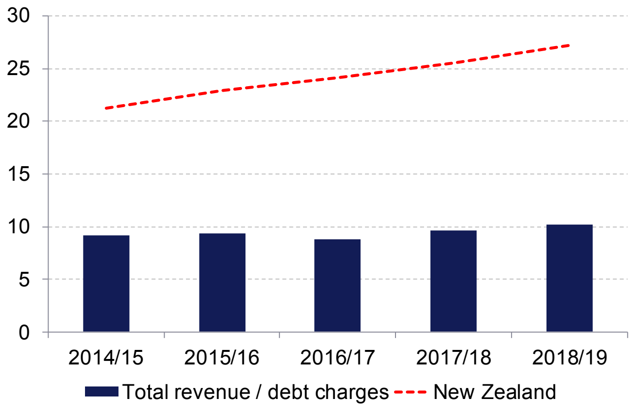


	2014/15	2015/16	2016/17	2017/18	2018/19
Total expenditure	2.215	2.140	2.286	2.290	2.526
Interest expenditure	247	247	284	278	295

Trend in debt sustainability

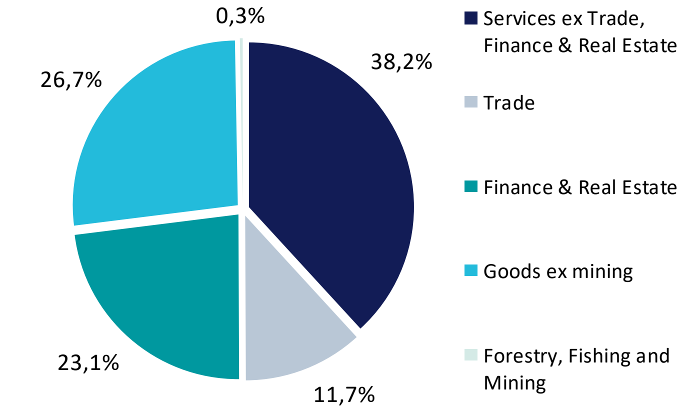


Trend in interest cover

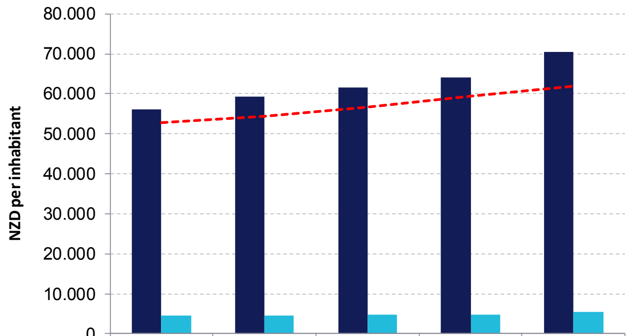


Source: Statistics New Zealand, Auckland Regional Council, NORD/LB Markets Strategy & Floor Research

Gross value added by economic sector



Trend in GDP and total debt



	2014/15	2015/16	2016/17	2017/18	2018/19
GDP	56.218	59.306	61.520	64.104	70.531
Net debt	4.457	4.635	4.809	4.848	5.355
GDP (New Zealand)	52.882	54.425	56.608	59.345	61.859

Source: Statistics New Zealand, NORD/LB Markets Strategy & Floor Research

(Values in NZD)

Balance (vs. 2017/18)

790m (659m)

Balance/GDP (2017/18)

0.7% (0.6%)

Adjusted income*
(vs. 2017/18)

4.9bn (+0.3bn)

Adjusted income*/
interest expenditure (2017/18)

8.9x (8.6x)

Net debt
(vs. 2017/18)

8.7bn (+0.4bn)

Net debt/GDP (2017/18)

7.6% (7.6%)

Net debt/adjusted income*
(2017/18)

1.8x (1.8x)

* Revenue excluding equalisation payments.

Key budget indicators – July 2018 to June 2019

At the end of the budget year in June 2019 (data for 2019/20 is not yet available), Auckland was able to report a positive balance of around NZD 790m and was therefore able to increase this metric for the fourth time in succession (2018: NZD 659m). Once again, this is driven by the increase in absolute revenue (NZD +335m Y/Y) and a comparatively modest increase in expenditure (NZD +204m Y/Y). Having been close to a zero budget in 2013/14 and 2014/15, there has been a significant improvement in the budget position over the last four years. Aside from increased revenue from grants and subsidies, Auckland benefited from increases in local taxes and further assistance from the New Zealand government. Expenditure only rose minimally thanks to marginally higher personnel and pension costs as well as depreciation and amortisation. In addition to Auckland Council, the past budget year also went well for the nation as a whole, with New Zealand reporting the highest surplus revenue in recent years (2018/19: NZD 10.9bn). Despite the population growth recorded by Auckland Council, revenue per capita also rose to NZD 3,014. Adjusted revenue grew by 5.4% while interest expense only rose slightly by 1.3% to NZD 478m. The ratio therefore improved to 8.9x (2017/18: 8.6x). Net debt increased year on year, reaching around NZD 8.7bn, which equates to an increase of 5.4%. Having stagnated for years, net debt as a proportion of GDP also rose in the last budget year. Auckland's debt sustainability – measured by net debt in relation to adjusted income – remained constant compared with the previous year, with a value of 1.8x recorded here.

GDP (vs. 2017/18)
NZD 114.1bn
(NZD +5.4bn)

GDP per capita (vs. 2017/18)
NZD 70,531 (NZD +6,427)

GDP growth (2017/18)
5.0% (6.6%)

Unemployment (2018)
4.1% (4.2%)

Economic data 2018/19

Auckland's economic output has risen continuously since the start of the period under review in 2011 and reached a nominal GDP of NZD 114.1bn in 2018/19, which would imply a value of NZD 70,531 on a per capita basis. In 2018, annual growth, at 5.0%, was on a par with national growth. The significant dependence on the financial and property sector (23.1%) and retail sector (11.7%) is striking. In total, approximately 73% of GDP is attributable to the tertiary sector. In the last three years, the economy grew by just under 20% in total. In the last two budget years, in particular, unemployment has been cut significantly, falling from 5.3% in 2016 to the current figure of 4.1%. Auckland accounted for approximately 37.6% of New Zealand's gross domestic product in the 2018/19 budget year.

Outlook

Due to years of significant immigration from overseas and other regions of New Zealand, combined with the significance of Auckland for the economy as a whole, further economic growth is also expected over the next few years. Substantial investment means that Auckland Council's debt level is still relatively high, which could restrict its financial leeway to a certain extent in future. However, the figures for debt sustainability and interest coverage have improved in recent years, meaning that Auckland City Council is well placed in terms of fiscal policy. New Zealand has largely been spared from the most severe effects of the global coronavirus pandemic, meaning that the economic impact can largely be described as manageable and overly dramatic financial cutbacks are not expected. To comply with funding targets, we expect that additional EUR bonds and green bonds will be issued in future, meaning that Auckland City Council bonds will continue to provide an attractive alternative investment in the current investment environment.

Strengths

+ Highest share of New Zealand's total economic output
+ Steady improvement in key budget figures
+ Good capital market access and trading environment
+ Issuance of secured notes

Weaknesses

– Significant debt compared locally (Down Under)

Comment

Significant infrastructure expenditure in recent years means that Auckland Council still has higher than average debts, which has resulted in the classification (Aa2/AA) from Moody's and S&P. Compared with many industrialised countries, demographic change will have a positive impact on the labour supply in the next few years. Due to Auckland's strong position as a financial centre, the council often issues its bonds in foreign currencies. We are therefore confident that the authority will issue additional EUR benchmark bonds in future. The special feature of the outstanding bonds is that they were issued as "secured notes". AUCKCN has also established a green bond framework under which it has issued several bonds (first bond: NZD 200m in June 2018).

Appendix

The ECB tracker and Charts & Figures chapters will be included here again soon.

Appendix
Publication overview

Publication	Topics
35/2020 ♦ 16 September	▪ Moody's covered bond universe: an overview ▪ Update Down Under: Victoria (TCV)
34/2020 ♦ 26 August	▪ Covered bonds as central bank-eligible collateral – European Central Bank presents Q2 2020 figures ▪ Update: New South Wales (NSWTC)
33/2020 ♦ 19 August	▪ German Pfandbrief savings banks in Q2 2020 ▪ ECBC publishes annual statistics for 2019
32/2020 ♦ 12 August	▪ Transparency requirements §28 PfandBG in Q2 2020 ▪ Development of the German property market ▪ European Atomic Energy Community (Euratom)
31/2020 ♦ 05 August	▪ PEPP: Second round of reporting again provides valuable insights
30/2020 ♦ 29 July	▪ LCR levels and risk weights of EUR benchmarks ▪ Update: Funding of German Bundeslaender (ytd)
29/2020 ♦ 22 July	▪ iBoxx Covered indices: current status and criteria ▪ Update: Joint Laender jumbos (LANDER)
28/2020 ♦ 15 July	▪ Repayment structures on the covered bond market ▪ 21st meeting of the Stability Council
27/2020 ♦ 08 July	▪ Sparebanken Vest issues first EUR benchmark in ESG format ▪ Second issuer from South Korea: Kookmin Bank to shortly make its debut in the EUR benchmark segment ▪ KfW reduces 2020 funding target to EUR 65bn
26/2020 ♦ 01 July	▪ Half-year review and outlook for the second half of 2020 ▪ The German debt brake in 2020
25/2020 ♦ 24 June	▪ EUR benchmark covered bonds in ESG format – an overview ▪ BULABO falling due – R.I.P.
24/2020 ♦ 17 June	▪ TLTRO-III.4 vs. covered bonds: are bond repurchases worth it? ▪ TLTRO-III now of increased interest for promotional banks too?
23/2020 ♦ 10 June	▪ The adjustment follows the reporting: insights into the PEPP
22/2020 ♦ 03 June	▪ Moody's covered bond universe – an overview
21/2020 ♦ 27 May	▪ BPCE issues inaugural green covered bond ▪ France: retained issuances and benchmark deals ▪ The federal financial equalisation system (LFA)
20/2020 ♦ 20 May	▪ German Pfandbrief savings banks in Q1 2020 ▪ EIOPA and BaFin see insurers as prepared for the coronavirus crisis: SCR calculation for covered bonds under Solvency II

NORD/LB: Markets Strategy & Floor Research

NORD/LB: Covered Bond Research

NORD/LB: SSA Research

Bloomberg: RESP NRDR <GO>

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Sales MM/FX	+49 511 9818-9460
Sales Europe	+352 452211-515

Origination & Syndicate	
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Origination Corporates	+49 511 361-2911

Treasury	
Collat. Management/Repos	+49 511 9818-9200
Liquidity Management	+49 511 9818-9620 +49 511 9818-9650

Trading	
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Financials	+49 511 9818-9490
Governments	+49 511 9818-9660
Länder/Regionen	+49 511 9818-9550
Frequent Issuers	+49 511 9818-9640

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Additional information
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None

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Issuer / security	Date	Recommendation	Bond type	Cause