

## RESULTS REINFORCE OUR STRONG BULLISHNESS. NIM WEAKNESS NOT AN ISSUE

DNBNOR's Q4 09 results were exactly in line with our top-of-the-range expectations for net income and pre-tax income (representing a 30% beat against consensus for the pre-tax profit line). The quality of the results is perhaps not quite as good as had been expected, but we still believe they will be received well by the market. They are characterised by a revenue miss (driven by weak net interest income), but much better than expected loan losses, underpinned by the better credit quality seen in the strong domestic Norwegian market.

**DNBNOR is our favoured Nordic bank (with Handelsbanken). We believe it is cheap, has good earnings robustness, an attractive Nordic footprint and low exposure to sovereign risk.**

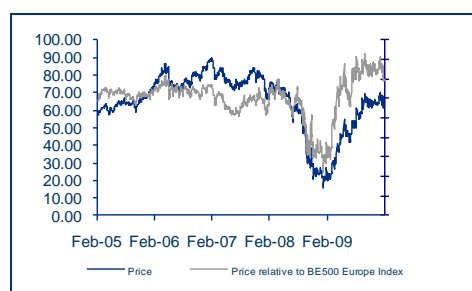
- DNB NOR's Q4 09 results were characterised by weak net interest income, similar to the other Nordic banks that have reported so far. However, this miss is only slight. The main driver is a slight compression in net interest margin (with a modest fall in total loans the other driver). However, we believe the compression is temporary and will soon be followed by an increasing NIM. The differentiating factor between DNB NOR and the other Nordic banks is that in its domestic Norwegian market, the base rate is already on an uptrend. We believe this should aid liability and overall margins going forward.
- The slight miss in NII was considerably outweighed by much lower loan losses. This is the other differentiating factor with the other Nordic banks, which reported better than expected loan losses, but not sufficient to offset the lower than expected NII. It is clear to us that the more concentrated Norwegian footprint is driving the more pronounced improvement in credit quality.
- The reinstatement of a large dividend per share of NOK1.75 was slightly more than we had anticipated and well ahead of consensus expectations. The payout ratio is 34%, leading to a dividend yield of 2.8%.
- We were also surprised by the stronger than expected Core Tier 1 ratio, which was 8.5% versus our 8.1% expectation. This was driven by a slight beat in core capital and also, more surprisingly, a 4% QoQ fall in RWA. This ratio, of course, is on a transitional Basel II basis. Management indicated on the conference call that the Core Tier 1 ratio on a full Basel II basis (to be implemented at the end of 2010) would be 10.7%. This places DNB NOR as one of the strongest capitalised banks in the sector. Our Basel III analysis also points to the bank being very well capitalised under the proposed regulations.

### Research

Andrew Lim +44 20 3206 7347 andrew.lim@matrixgroup.co.uk

Rating	BUY
Target price (NOK)	NOK86.00
Yesterday's closing price (NOK)	62.75
Upside/Downside	37%
Market Cap (€m)	12.7
Sector	Pan-Euro Banks

NOK/(NOKm)	2009A	2010E	2011E
Net interest income	22,633	23,320	24,571
Net fees & commissions	6,655	6,856	7,096
Trading profits/losses	6,285	5,161	5,264
Other revenue	2,052	3,086	3,186
Total operating revenues	37,625	38,422	40,117
Operating costs	-18,911	-18,871	-19,582
Operating profit	18,714	19,551	20,535
Total provisions	-7,710	-5,911	-4,823
Pre-tax profit	11,030	13,640	15,711
ROA	0.47%	0.53%	0.56%
ROE	9.68%	9.74%	10.14%
ROTNV	10.65%	10.53%	10.90%
Cost/Income	-50.26%	-49.12%	-48.81%
Payout	33.53%	28.44%	34.34%
Net interest margin	1.40%	1.40%	1.40%
LLC % gross loans	-0.67%	-0.52%	-0.41%
NPL ratio	1.78%	1.60%	0.80%
NPL coverage ratio	54.00%	75.00%	80.00%
Loans % deposits	189%	186%	182%
Core tier 1 ratio	8.51%	9.09%	9.49%
EPS	6.04	6.11	6.84
DPS	1.75	1.74	2.35
P/TNAV	1.12	1.04	0.96
Div Yield	2.79%	2.77%	3.74%



Matrix Corporate Capital LLP is authorised and regulated in the United Kingdom by the Financial Services Authority. This document must be treated as a marketing communication as it has not been prepared in accordance with legal requirements designed to promote the independence of investment research.

## Net interest income

As with the other Nordic banks that have reported so far, net interest income was weak: a 4% miss against our estimate and a fall of 2% QoQ. The NIM weakened 3bps QoQ to 1.36% against our expectation of a flat development. The reason was a slight contraction in both the lending spread and the deposit spread.

In our opinion, the fall in NIM is minor and should improve in the following quarters as DNB NOR benefits from the increase in the Norwegian base rate, helping the expansion in deposit spreads and overall margins. The Norwegian base rate has increased twice since the end of October 2008, from 1.25% to the current 1.75%. This should soon have a positive effect on DNB NOR's margins, which is one of the main differentiating factors with the other Nordic banks, where base rates have remained close to zero in the other Nordic countries.

As expected, the development of the NIM in Q4 09 has been more robust for DNB NOR than for Nordea (Figure 1). Aside from some positive contribution to margins from the rise in the Norwegian base rate, DNB NOR has benefitted from a slight improvement (i.e. fall) in its loan-to-deposit ratio since the end of 2008 (see Figure 2), whilst Nordea has suffered a modest deterioration, which follows through to their respective funding costs.

Figure 1: Net Interest Margin for the Nordic Banks

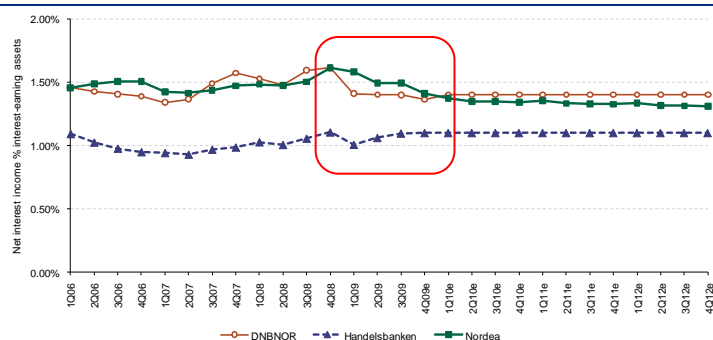
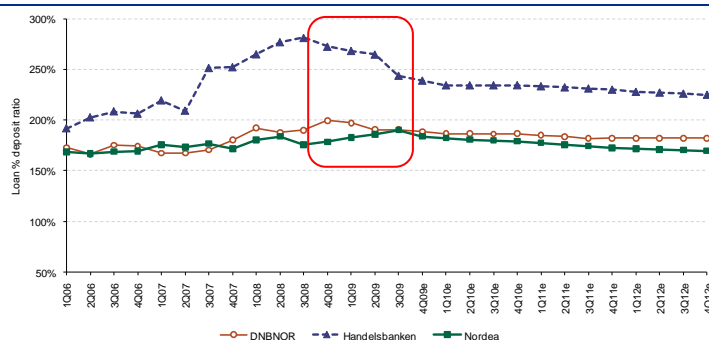


Figure 2: Loan-to-Deposit Ratio for the Nordic Banks



Source: Matrix Corporate Capital Research

Source: Matrix Corporate Capital Research

Note that Handelsbanken has enjoyed the greatest improvement in its LTD ratio since the end of 2008, underpinned by the relative improvement of its deposit franchise as the credit crisis has unfolded. This leads us to believe that the NIM for Handelsbanken in Q4 09 should be relatively stable. (Note that the absolute value of the LTD ratios for the Nordic banks is distorted by their substantial use of long term covered bond and commercial paper financing as sources of funding).

## Other aspects of operating profit

DNB NOR's weak NII in Q4 09 was offset somewhat by better than expected commission income, but total revenues were still 4% lower than what we had expected. We believe the cost/income ratio will taper down to a more normalised level in 2010 as revenues improve.

Operating costs were in line with our and consensus expectations. Because of the weakness in revenues, however, the cost/income ratio increased to 53% from 48%.

Overall operating profit (before loan losses) therefore fell short 16% against our expectations (although ‘only’ an 8% miss against consensus). Unlike the Swedish banks that have reported so far however (this excludes Handelsbanken, which reports on 18 February), the lower loan losses has more than compensated for the lower than expected operating profit, leading to pre-tax profit being 31% better than the consensus forecast.

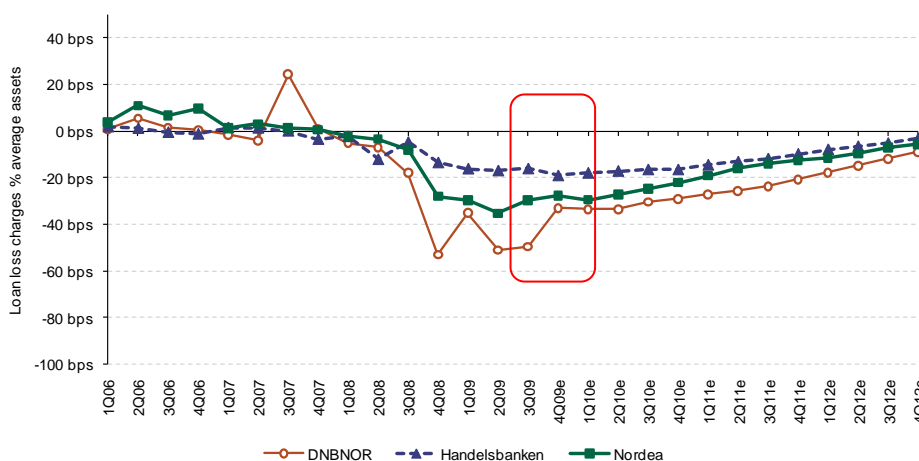
### Asset quality – substantial improvement

Loan losses were better than expected at DNB NOR, in keeping with the other Nordic banks that have reported so far, but substantially more so. The loan loss ratio improved to 0.54% from 0.71% in 3Q09. The main driver was a reduction in loan losses for the two books of business that suffered some of the greatest deterioration during the crisis: small and medium sized enterprises, and shipping. DNB NOR, the 51%-owned subsidiary which comprises DNB NOR’s Eastern European banking operations, improved QoQ but still remains at elevated levels.

We have modelled a better absolute loan loss rate for DNB NOR’s going forward. This has a direct (albeit modest) positive impact on our DCF valuation for the company. (However, for the time being, we maintain our target price of NOK86.00 which still factors in substantial upside from the current share price).

Note that the improvement in loan losses in Q4 09 versus Q3 09 is much more marked for DNB NOR than for Nordea.

Figure 3: Loan Loss Charges as a % of Average Assets for the Nordic Banks



Source: Matrix Corporate Capital Research

DNB NOR’s management also revised downwards Latvia’s non-performing loans. This was due to a reclassification to make the basis of NPL recognition the same as at peer banks. NPLs at the group level also fell as a result, causing the restated NPLs % average gross loans (the NPL ratio) to be some 7-9bps better on an historical basis. There was an increase in the NPL ratio QoQ from 1.70% to 1.78%. While this is obviously a negative, in our opinion it is outweighed by the fact that the coverage ratio has increased QoQ to 54% from 51%, building on the improvement seen in Q3 09.

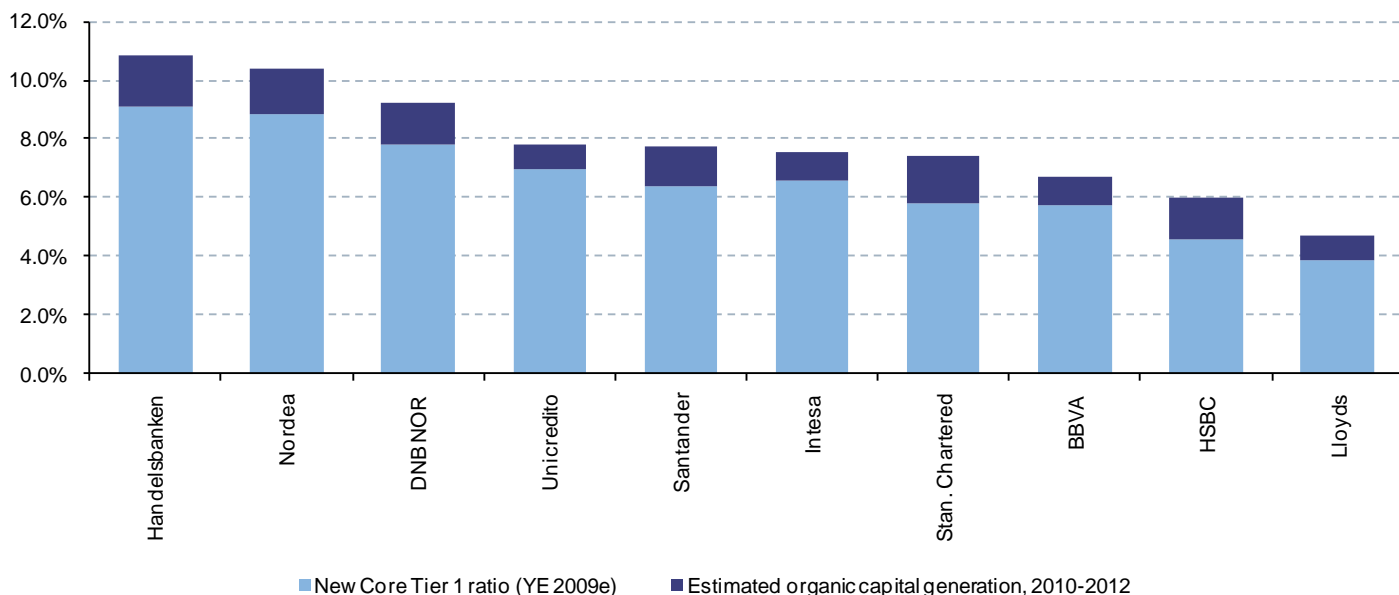
### Capital ratios – very strong on both full Basel II and Basel III

DNB NOR’s Core Tier 1 ratio jumped significantly to 8.5% from 6.5% in Q3. This is due to the NOK14bn capital raise late last year. The ratio is ahead of our own 8.1% estimate due to better than expected core capital and a 4% decrease in RWA QoQ.

DNBNOR also disclosed what its capital ratios look like under full Basel II. In the sub-sector of large cap lending banks, note that DNB NOR is the only bank that publishes its Tier 1 and Core Tier 1 ratios only on a transitional Basel II basis. Management has nevertheless provided an indicative figure for what the Tier 1 and Core Tier 1 ratios would be under full Basel II principles. The Tier 1 ratio is 11.7% (versus the published 9.3% under transitional Basel II principles) and the Core Tier 1 ratio is 10.7% (versus the published 8.5%). This is obviously a substantial improvement, making DNB NOR one of the best capitalised banks in its peer group.

We have also re-run our Basel III capital analysis for the latest published figures. DNB NOR still ranks as one of the most strongly capitalised banks in its peer group on expected Core Tier 1 ratio at the end of 2012 (including anticipated organic capital generation). Note, however, that if the full Basel II Core Tier ratio of 10.7% is used as the starting point in our analysis instead of the transitional Basel II ratio of 8.5%, then DNB NOR's Basel III Core Tier 1 ratio would be approximately 11.4% at the end of 2012, making it the best capitalised bank of all.

Figure 4: Banks Ranked by Expected Core Tier 1 Ratio at year-end 2012



Source: Matrix Corporate Capital Research

Figure 5: DNB NOR Earnings Table

DNB NOR ASA	FY2008	Q4 09E	Q4 09	FY2009	FY2010E	FY2011E	FY2012E
<b>INCOME STATEMENT (NOK m)</b>							
Net interest income	21,910	5,827	5,606	22,633	23,320	24,571	26,389
Net fees & commissions	6,895	1,554	1,616	6,655	6,856	7,096	7,380
Trading profits/losses	3,340	1,059	1,066	6,285	5,161	5,264	5,369
Other revenue	2,202	1,402	477	2,052	3,086	3,186	3,290
Total operating revenues	34,347	9,842	8,765	37,625	38,422	40,117	42,428
Operating costs	-18,719	-4,961	-4,657	-18,911	-18,871	-19,582	-20,664
Operating profit	15,628	4,880	4,108	18,714	19,551	20,535	21,765
Total provisions	-3,509	-2,221	-1,517	-7,710	-5,911	-4,823	-2,839
Impairments on other assets	0	0	0	0	0	0	0
Goodwill impairment	0	0	0	0	0	0	0
Net gains on fixed and intangible assets	52	0	19	26	0	0	0
Pre-tax profit	12,171	2,659	2,610	11,030	13,640	15,711	18,925
Taxes	-3,252	-880	-1,001	-4,086	-4,092	-4,399	-4,731
Minorities	293	343	433	1,558	407	-170	-213
Other non-operating items	0	-2	-1	0	0	0	0
Net profit	9,212	2,120	2,041	8,502	9,954	11,143	13,981
<b>ASSETS (NOK m)</b>							
Loans to customers	1,191,635	1,133,544	1,114,886	1,114,886	1,146,233	1,211,412	1,311,271
Interbank loans	59,717	71,049	62,317	62,317	64,847	67,480	70,220
Total securities	334,020	480,203	484,811	484,811	524,775	568,033	614,858
Intangible assets	8,480	8,409	7,644	7,644	7,644	7,644	7,644
Total assets	1,831,699	1,885,509	1,823,453	1,823,454	1,911,497	2,052,267	2,205,264
Net interest-earning assets	1,599,680	1,674,301	1,635,646	1,635,646	1,705,981	1,813,202	1,958,403
<b>LIABILITIES (NOK m)</b>							
Interbank borrowings	178,822	300,078	302,669	302,669	314,959	327,747	341,055
Customer deposits	1,203,464	1,126,571	1,084,477	1,084,477	1,128,511	1,221,537	1,322,231
Total shareholders' equity	77,065	99,092	98,648	98,648	105,752	114,064	124,219
Tangible net asset value	68,585	90,683	91,004	91,004	98,108	106,420	116,575
<b>IMPORTANT FINANCIAL RATIOS</b>							
ROA	0.56%	0.45%	0.46%	0.47%	0.53%	0.56%	0.66%
ROE	12.25%	9.33%	9.35%	9.68%	9.74%	10.14%	11.73%
ROTNV	13.73%	10.27%	10.25%	10.65%	10.53%	10.90%	12.54%
Cost/income	-54.50%	-50.41%	-53.13%	-50.26%	-49.12%	-48.81%	-48.70%
Tax rate	-26.72%	-33.10%	-38.35%	-37.04%	-30.00%	-28.00%	-25.00%
Payout	0.00%	130.00%	134.33%	33.53%	28.44%	34.34%	35.13%
Net interest margin	1.51%	1.40%	1.36%	1.40%	1.40%	1.40%	1.40%
LLC % gross loans	-0.33%	-0.78%	-0.54%	-0.67%	-0.52%	-0.41%	-0.22%
Non-performing loans % gross loans	1.11%	2.00%	1.78%	1.78%	1.60%	0.80%	0.80%
NPL coverage ratio	45.50%	48.00%	54.00%	54.00%	75.00%	80.00%	80.00%
Loans % deposits	199.52%	188.77%	188.73%	188.73%	186.46%	182.06%	182.06%
Tier 1 ratio	6.66%	8.88%	9.33%	9.33%	9.91%	10.27%	10.75%
Core tier 1 ratio	5.84%	8.07%	8.51%	8.51%	9.09%	9.49%	10.00%
Equity % total assets	4.21%	5.26%	5.41%	5.41%	5.53%	5.56%	5.63%
RWA % total assets	65.55%	57.44%	57.72%	57.72%	55.62%	53.90%	52.20%

Source: Matrix Corporate Capital Research

## IMPORTANT DISCLOSURES

### General Disclosures

MCC is committed to publishing accurate but non-independent research reports. MCC may provide financial advice to, and undertake corporate finance and other transactions on behalf of, companies on which it publishes research. Therefore, research reports published by MCC have not been prepared in accordance with legal requirements designed to promote the independence of investment research; nor is MCC subject to any prohibition on dealing ahead of the dissemination of investment research. Accordingly, this research report should be treated as a marketing communication.

This report was first released on 12 February 2010.

Unless otherwise noted, the securities prices noted in this report were market prices on 11 February 2010.

We seek to update our research as appropriate, but various regulations may prevent us from doing so. Our reports are published at irregular intervals as appropriate in the analyst's judgement.

MCC's price targets are based on several methodologies, which may include, but are not restricted to, analyses of market risk, growth rate, revenue stream, discounted cash flow, EBITDA, EPS, cash flow (CF), free cash flow (FCF), EV/EBITDA, P/E, PE/growth, P/CF, premium (discount)/average group EV/EBITDA, premium (discount)/average group P/E, sum of the parts, net asset value, dividend returns, and return on equity over the next 12 months.

This report has been prepared by the individual(s) whose name(s) appear(s) on the front cover. Unless it has been otherwise specified, the preparers are employed by MCC as research analysts. Research analysts are paid in part based on the profitability of MCC, which includes remuneration received from investment banking transactions.

### Specific Disclosures

Company	Disclosure
DNB NOR (DNBNOR)	None

1. Matrix Corporate Capital acts as broker
2. Matrix Corporate Capital acts as NOMAD
3. Matrix Corporate Capital acts as market maker

MCC, its partners, employees and any affiliated undertaking may have a position or holding in any of the securities mentioned in this report or in a related instrument.

### Disclaimer

This report is issued by Matrix Corporate Capital LLP ("MCC") which is authorised and regulated in the United Kingdom by the Financial Services Authority (FSA) and is a member of the London Stock Exchange.

This report is not directed to, or intended for distribution to, or use by, any person or entity who is a citizen or resident of, or located in any locality, state, country or other jurisdiction where such distribution, publication, availability or use would be contrary to law or regulation or which would subject MCC to any registration or licensing requirement within such jurisdiction.

This report is for the use of the addressees only and is intended for use only by a person or entity that qualifies as an authorised person or exempt person within the meaning of section 19 of the Financial Services and Markets Act 2000 (the "Act") or qualifies as a person to whom the financial promotion restrictions imposed by the Act do not apply by virtue of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2005, or is a person classified as an "professional client" for the purposes of the Conduct of Business Sourcebook of the FSA. Consequently, this report is intended for use only by high net worth entities or by persons having professional experience in matters relating to investments. This report is not intended for use by other persons, in particular, "retail clients" as defined by the rules of the FSA. Any such person who receives this report should not act upon the contents of this report.

The information and materials presented in this report have been obtained or derived from sources believed by MCC to be reliable. Such information and materials have not been independently verified and MCC makes no representation as to their accuracy or completeness. Neither MCC, nor any of its directors or employees accepts liability for any loss arising from the use of material presented in this report.

Any forecasts or target prices shown for companies or securities noted in this report may not be achieved due to multiple risk factors including, without limitation, market volatility, sector volatility, corporate actions, the unavailability of complete and accurate information or assumptions made by MCC or other sources relied on in the report subsequently transpiring to be inapposite.

The information and materials presented in this report are provided to you for information purposes only and are not to be used or considered as an offer, or the solicitation of an offer, to sell or buy or subscribe for securities or other financial instruments. This report was prepared for general circulation and does not give investment advice or personal recommendations specific to individual investors. As such, the companies and securities discussed in this report may not be suitable for all investors who must make their own investment decisions based on their specific investment objectives and financial situation utilising their own financial advisors as they deem necessary. MCC will not treat recipients of this report as clients by virtue of their receiving it.

Past performance should not be taken as an indication or guarantee of future performance, and no representation or warranty, express or implied, is made regarding future performance. Information, opinions and estimates contained in this report reflect the preparer's best judgement at the date of publication and are subject to change without notice. The price, value of, and income from any of the securities or financial instruments mentioned in this report can fall as well as rise. You may not get back as much as you invest. Fluctuations in exchange rates could have adverse effects on the value or price of, or income derived from, certain investments.

None of the material presented in this report, nor its content, nor any copy of it, may be altered in any way, transmitted, copied or distributed to, any other party, without the express prior written permission of MCC.

**Matrix Corporate Capital LLP**

One Vine Street

London, W1J 0AH

+44 (0) 20 3206 7000