



SLIGHT WEAKNESS IN NIM AND COSTS, BUT STILL A VERY DEFENSIVE STOCK

Nordea's Q4 09 results were slightly worse than we had expected. However, in time, we believe that the modest miss against estimates will be considered a decent result relative to other banks. We also believe that the higher than expected costs, which were a key reason for the weak earnings, will be considered a one-off and that the NIM should stabilise.

We maintain our Buy rating on the stock. Compared to the weak underlying Q4 earnings seen at BBVA and Santander (the latter adjusted for the exceptional capital gains that were booked to provisions), we believe these results are not overly negative. Nordea's Nordic footprint is attractive given that GDP growth rates in the region are projected by consensus to be the strongest in developed Europe in 2010, and the fact that there is minimal sovereign CDS risk. However, we prefer DNB NOR (which we believe has greater valuation upside) and Handelsbanken (which should not have the same pressure on margins, in our view, given its ability to accumulate cheap deposits).

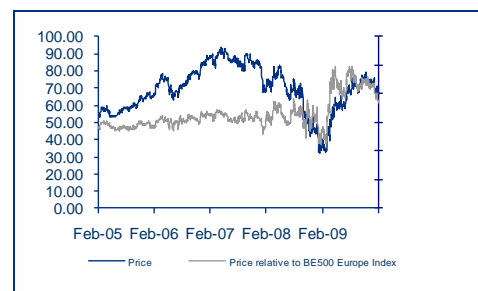
- Revenues in Q4 were slightly weak, a miss of 4% against our expectations and 2% against consensus. They were characterised by missing net interest income forecasts (with a slightly worse deterioration in net interest margin than expected) but offset to an extent by a beat on fees and commissions.
- Trading income was weaker than in the previous quarter, as expected given recent trends seen at other banks and in the fixed income markets generally (although it was still a 10% miss versus consensus).
- High operating costs were the other surprise. A large part of this was due to unexpected restructuring costs of €64m. We believe these will be considered one-off, with the market taking into account the revenue benefits in future quarters.
- Loan losses were much lower than anticipated, in keeping with results seen at SEB and Swedbank. The loan loss ratio fell slightly to 0.46% (Matrix basis) from 0.48% in Q3 09. It is reassuring to see this positive momentum against deteriorating trends in some other regions, notably Spain. We are also reassured by the increase in the coverage ratio to 53% from 51% QoQ, which is building on the increase in provisioning seen in the last quarter. On the negative side, our view is tempered somewhat by the continued increase in the NPL ratio to 1.35% from 1.28% in Q3 09, and against our 1.30% expectation.

Rating	BUY
Target price (SEK)	86.60
Yesterday's closing price (SEK)	66.80
Upside/Downside	30%
Sector	Pan-Euro Banks
Market Cap (€m)	27.0-

€/(€m)	2009A	2010E	2011E
Net interest income	5,281	5,299	5,582
Net fees & commissions	1,693	1,903	1,999
Trading profits/losses	1,743	1,928	1,957
Other revenue	356	293	305
Total operating revenues	9,073	9,424	9,843
Operating costs	-4,512	-4,609	-4,818
Operating profit	4,561	4,815	5,026
Total provisions	-1,486	-1,335	-848
Pre-tax profit	3,075	3,480	4,177
ROA	0.47%	0.50%	0.57%
ROE	11.26%	10.78%	12.01%
ROTNV	13.00%	12.28%	13.55%
Cost/income ratio	-49.73%	-48.91%	-48.94%
Payout ratio	43.49%	37.68%	40.09%
Net interest margin	1.46%	1.35%	1.33%
LLC % gross loans	-0.50%	-0.43%	-0.26%
NPL ratio	1.35%	1.10%	0.80%
NPL coverage ratio	52.56%	52.00%	58.00%
Loans % deposits	184%	179%	173%
Core tier 1 ratio	10.35%	10.99%	11.53%
EPS	0.57	0.64	0.77
DPS	0.25	0.24	0.31
P/TNAV	1.35	1.25	1.14
Div yield	3.73%	3.86%	4.63%

Research

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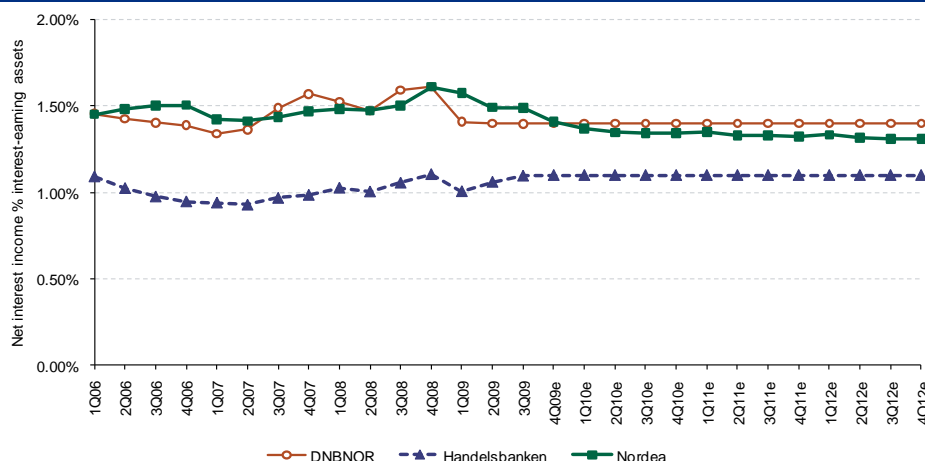
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Net interest income

Net interest income was in line with our estimates but slightly weak (~2%) against consensus. The NIM was 1.41% against our expectation of 1.43% and down from the 1.49% achieved in Q3 09. The weakness in NIM is attributed by management to continued pressure on deposit margins, slightly lower household lending margins and lower net interest income in Group Treasury by EUR 21m, due to a lower return on the liquidity buffer. The negative mix effect from the sharp fall in base rates on liability spreads is obviously still an ongoing issue. The company noted stabilising retail and corporate margins. From the conference call, it would appear that management is committing to a stable net interest margin going forward (in the absence of a rise in the base rate which would help deposit spreads expand).

Note the development of the NIM with respect to the expected development for the other Nordic banks. The chart below shows the deterioration in NIM for Nordea in Q4 09, against the expectation of flat NIMs for DNB NOR (given that the Norwegian base rate has increased since the end of October 2009), and Handelsbanken (given that it is a superior deposit franchise, with a fall in its loan-to-deposit ratio by some 30 percentage points over the course of the crisis). The relative development in the NIM is one of the key reasons why we prefer DNB NOR and Handelsbanken to Nordea (although we rate all Buy).

Figure 1: Development in NIM For The Large Cap Nordic Banks



Source: Matrix Corporate Capital Research

Asset Quality

Loan losses in Q4 were much lower than anticipated, in keeping with the results seen at SEB and Swedbank. The loan loss ratio fell slightly to 0.46% (Matrix basis) from 0.48% in Q3 09. It is reassuring in our view to see this positive momentum against the deteriorating trends in some other regions, notably Spain. We are also reassured by the increase in the coverage ratio to 53% from 51% QoQ, which builds on the increase in provisioning seen in Q3.

On the negative side, our view is tempered a little by the continued increase in the NPL ratio to 1.35% from 1.28% last quarter, and against our 1.30% expectation. However, the rate of increase in the NPL ratio is indeed slowing, having been 1.18% in Q2 09, 1.00% in Q1 09 and 0.77% in Q4 08.

Costs

Nordea surprised the market somewhat by initiating a restructuring programme which it expects will yield revenue benefits in 2010, 2011 and 2012. The impact on

Q4 09 earnings was €64m, with the initial restructuring costs yielding no revenue benefits. However, the net impact (including revenue benefits) is expected to be net neutral in 2010 and positive for 2011 and 2012. As such, we believe the market will consider the elevated expenses this quarter to be a one-off and necessary for better earnings growth going forward. The restructuring costs included the integration of Fionia Bank, a growth plan in Finland and IT costs.

Dividend

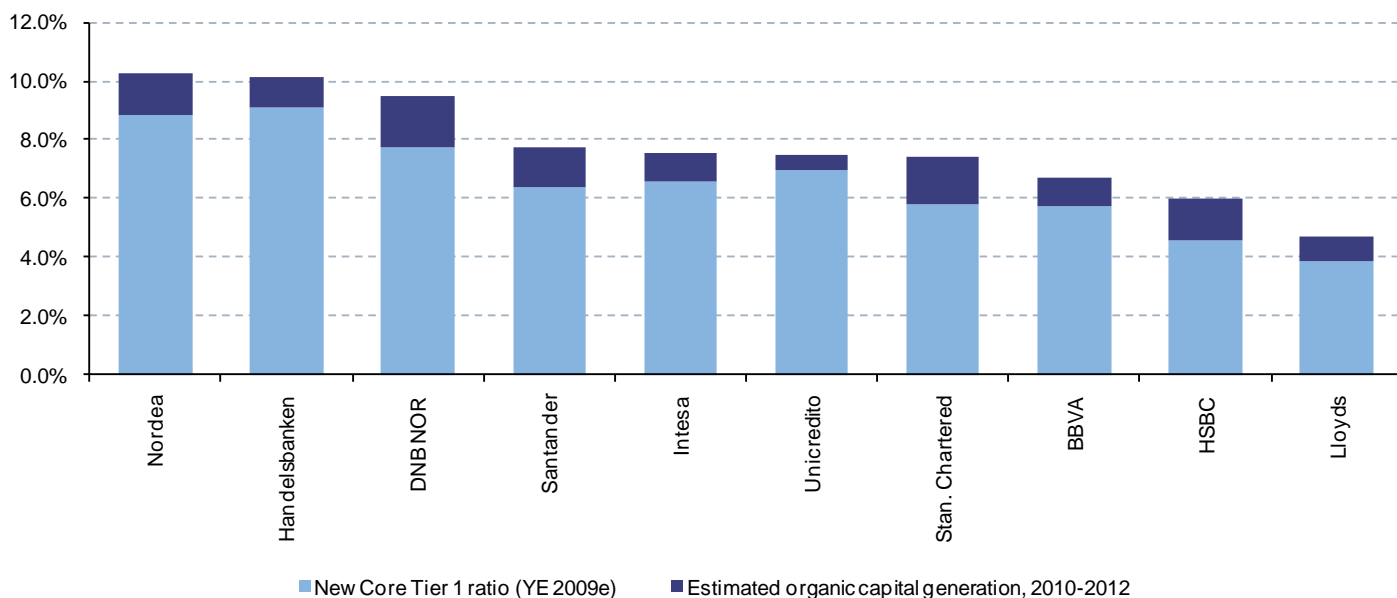
Management proposed a better than expected dividend of €0.25 per share, equivalent to a payout ratio of 43% and a yield of 3.7%.

Capital

The Core Tier 1 ratio (on a full Basel II basis) for Nordea disappointed against our expectations, falling 34bps QoQ to 10.35%. We had expected an increase to 10.77%. RWA increased very modestly QoQ. However, Core Tier 1 capital fell 1.4% QoQ despite positive earnings in the quarter. This appears to be due to an increase in deductions against common equity of about €400m, which appears related to the acquisition of Fionia Bank.

The capital adequacy of Nordea nevertheless remains very robust. We have re-run our Basel III capital analysis and project a Core Tier 1 ratio of 10.3% at the end of 2012, including organic capital generation. This places it as one of the best capitalised banks in the group of lending banks, together with DNB NOR (note that we should add ~200bps to DNB NOR's Core Tier 1 ratio since it only discloses Basel II capital ratios on a transitional basis) and Handelsbanken.

Figure 2: Banks Ranked By Core Tier 1 Ratios At The End Of 2012



Source: Matrix Corporate Capital Research

Figure 3: Nordea Earnings Table

NORDEA BANK AB	FY2008	Q4 09E	Q4 09	FY2009	FY2010E	FY2011E	FY2012E
INCOME STATEMENT (€m)							
Net interest income	5,093	1,283	1,299	5,281	5,299	5,582	5,898
Net fees & commissions	1,883	436	463	1,693	1,903	1,999	2,099
Trading profits/losses	833	355	351	1,743	1,928	1,957	2,023
Other revenue	391	166	45	356	293	305	318
Total operating revenues	8,200	2,240	2,158	9,073	9,424	9,843	10,338
Operating costs	-4,338	-1,165	-1,219	-4,512	-4,609	-4,818	-5,062
Operating profit	3,862	1,075	939	4,561	4,815	5,026	5,276
Total provisions	-466	-397	-347	-1,486	-1,335	-848	-493
Impairments on other assets	0	0	0	0	0	0	0
Goodwill impairment	0	0	0	0	0	0	0
Other income	0	0	0	0	0	0	0
Pre-tax profit	3,396	679	592	3,075	3,480	4,177	4,782
Taxes	-724	-197	-145	-757	-870	-1,044	-1,196
Minorities	-1	-2	0	-5	-7	-8	-10
Other non-operating items	0	0	0	0	0	0	0
Net profit	2,671	481	447	2,313	2,603	3,125	3,577
ASSETS (€m)							
Loans to customers	265,100	285,548	282,411	282,411	297,802	316,877	336,962
Interbank loans	23,903	16,587	18,555	18,555	19,537	20,764	22,096
Total securities	63,436	72,844	69,099	69,099	74,795	80,960	87,634
Intangible assets	2,535	2,714	2,947	2,947	2,947	2,947	2,947
Total assets	474,074	491,612	507,494	507,494	531,476	569,118	606,376
Net interest-earning assets	340,047	360,814	381,565	381,565	404,582	432,612	463,082
LIABILITIES (€m)							
Interbank borrowings	51,932	55,045	52,190	52,190	56,492	61,149	66,190
Customer deposits	257,580	264,577	284,096	284,096	307,515	336,418	364,150
Total shareholders' equity	17,725	22,368	23,346	23,346	24,943	27,087	29,411
Tangible net asset value	15,190	19,654	20,399	20,399	21,996	24,140	26,464
IMPORTANT FINANCIAL RATIOS							
ROA	0.62%	0.48%	0.36%	0.47%	0.50%	0.57%	0.61%
ROE	15.35%	11.15%	7.91%	11.26%	10.78%	12.01%	12.66%
ROTNV	18.08%	12.79%	9.05%	13.00%	12.28%	13.55%	14.14%
Cost/income	-52.90%	-47.19%	-56.49%	-49.73%	-48.91%	-48.94%	-48.97%
Tax rate	-21.32%	-25.00%	-24.49%	-24.62%	-25.00%	-25.00%	-25.00%
Payout	19.43%	170.00%	225.06%	43.49%	37.68%	40.09%	40.20%
Net interest margin	1.56%	1.43%	1.41%	1.46%	1.35%	1.33%	1.32%
LLC % gross loans	-0.17%	-0.52%	-0.46%	-0.50%	-0.43%	-0.26%	-0.14%
Non-performing loans % gross loans	0.77%	1.30%	1.35%	1.35%	1.10%	0.80%	0.80%
NPL coverage ratio	52.61%	51.00%	52.56%	52.56%	52.00%	58.00%	66.00%
Loans % deposits	178.41%	190.19%	183.89%	183.89%	179.14%	172.69%	169.65%
Tier 1 ratio	9.35%	12.01%	11.40%	11.40%	12.03%	12.53%	12.85%
Core tier 1 ratio	8.49%	10.77%	10.35%	10.35%	10.99%	11.53%	11.91%
Equity % total assets	3.74%	4.14%	4.60%	4.60%	4.69%	4.76%	4.85%
RWA % total assets	44.99%	39.78%	37.80%	37.80%	36.64%	35.79%	35.65%

Source: Matrix Corporate Capital Research

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