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Research

Summary: Realkredit Danmark A/S

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■ Rationale

The 'AAA' senior secured debt rating on the covered bonds (realkreditobligationer) issued by the General Capital Center of Realkredit Danmark A/S covers 86% of the bonds issued by Realkredit Danmark, and applies to all new bonds issued. The rating primarily reflects the realkreditobligationer collateral, coupled with protections afforded by Danish insolvency and banking laws. Realkredit Danmark maintains a segregated, revolving pool of high-quality mortgage assets, on which the holders of realkreditobligationer have a preferential claim. The amount of collateral is sufficient to absorb potential credit losses and pay interest on and repay principal of the realkreditobligationer as they become due, even in the unlikely case of Realkredit Danmark becoming unable to meet its obligations. The quality of the collateral pool and the adequacy of the underlying cash flows are subject to regular surveillance by Standard & Poor's. The rating also reflects the sound quality of Realkredit Danmark's management, control, and expertise.

Realkredit Danmark is a core subsidiary of Danske Bank A/S (AA-/Stable/A-1+), and is Danske Bank's Mortgage Finance business area. Danske Bank is the largest financial services group in Denmark and is among the leaders in the Nordic region. Realkredit Danmark's total assets represented 30% of consolidated Danske Bank group assets of Danish krone (Dkr) 1.8 trillion (€245 billion at Dkr7.45 to €1) at March 31, 2004.

Realkredit Danmark benefits from a strong and effective distribution capability, robust core capitalization, high asset quality, and the concentration of its lending in the relatively low-risk area of residential housing. Profitability has traditionally been moderate due to the low-margin nature of mortgage lending.

Realkredit Denmark's total assets amounted to Dkr561 billion (€75.5 billion at Dkr7.43 to €1) at March 31, 2004, corresponding to a 31.3% market share of gross mortgage lending and a 34.7% share of outstanding bond debt. The company is a monoline product provider, offering mortgages secured by residential, commercial, agricultural, and industrial properties. The company introduced a new interest-only mortgage product in the second half of 2003, the sales of which have exceeded expectations. Mortgages are funded back-to-back by realkreditobligationer.

Capitalization remains robust. The company's Tier 1 ratio was 10.2% at March 31, 2004. Loan quality is high: on average, the loan-to-value ratio is 61%, and the level of nonperforming loans (NPLs) remains very low. Profitability remains under pressure due to the low interest rate environment, but has held up well in the first quarter of 2004, resulting in a 0.82% annualized return on risk-weighted assets at March 31, 2004, compared with 0.75% in 2003. Preprovision core earnings at Dkr527 million in the first quarter 2004 were down by 4.7% in line with expectations, and are expected to remain flat in 2004 compared with 2003.

Standard & Poor's expects mortgage finance to remain a core strategic business area in the Danske Bank group, providing a steady income stream from low-risk assets. Standard & Poor's also expects Realkredit Danmark's credit fundamentals to remain strong, and will monitor economic risks in Denmark--particularly asset price inflation and increasing household indebtedness--which could affect the level of NPLs.

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