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Analysis

SWITZERLAND
Europe/M.East/Africa

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NLB InterFinanz AG

NLB InterFinanz AG's A3 issuer rating is based on the company's good position in the forfaiting market in South-Eastern and Central & Eastern Europe, its good risk management capabilities and overall satisfactory financial profile.

Ownership, Regulation and Financial Reporting

NLB InterFinanz AG is the wholly owned subsidiary of Slovenian banking group Nova Ljubljanska banka d.d. (NLB, rated A2/Prime-1/C) and was established in 1989.¹ NLB is the dominant force in the Slovenian banking market and claims the largest share of the market with around one-third of total banking assets. It is mainly owned by the Slovenian government (35.4%) and by Belgian financial services group KBC (34%). The NLB group has expanded into other countries in the region through various subsidiaries – both banks and specialised finance companies. Moody's views NLB InterFinanz as a key part of NLB's strategy to increase its presence in the fast-growing countries of Central and Eastern Europe.

In our opinion, this ownership structure is a positive element in the assessment of NLB InterFinanz's credit quality as it provides stability, access to a broad customer base and expertise in international banking, and corporate governance structures that adequately take account of the interests of outside investors. Furthermore, we expect that NLB would provide financial assistance to NLB InterFinanz, whether to fund its growth or if an event of financial stress were to occur.

NLB InterFinanz is domiciled in Zürich, Switzerland. As a forfaiting company, it does not hold a banking licence, nor is it regulated or supervised by Eidgenössische Bankenkommission (EBK), the Swiss banking regulator.

The company prepares its financial statements pursuant to Swiss GAAP. The financial information it provides publicly offers limited insight into its financial performance and risk profile. Since 2003, PricewaterhouseCoopers AG has acted as external auditor and has not expressed any qualifications on NLB InterFinanz's accounts.

1. See Moody's Analysis on Nova Ljubljanska banka d.d., October 2006.

Franchise and Strategy

NLB InterFinanz specialises in providing non-recourse forfaiting and other forms of trade financing to customers in both South-Eastern and Central & Eastern Europe (CEE). In order to achieve a more balanced product offering and better diversification, the company also increasingly offers collateralised lending products in several CEE markets.

Non-recourse forfaiting – Typical transactions in which NLB InterFinanz would become involved include an exporter who intends to sell goods to an importer who needs a trade credit to finance the purchase. The exporter and importer agree on a deferred payment, secured by promissory notes corresponding to the future instalment dates. The exporter benefits from this structure because NLB InterFinanz takes over the credit risk, interest rate and exchange rate risks, and any possible political or transfer risks inherent in the transaction. NLB InterFinanz mitigates its own credit risk by a guarantee on the promissory notes from a bank residing in the importer's country. The exporter retains the risks associated with the legality of the claim, the authenticity of the forfeited documents and the performance risk of the underlying trade agreement.

Geographically, NLB InterFinanz's franchise builds on NLB's core market in Slovenia and, through a number of smaller subsidiaries, extends across South-Eastern Europe and CEE, with a particular focus on the Czech Republic, Serbia, Macedonia and, more recently, Italy. Moody's acknowledges that the political and economic structures in many of NLB InterFinanz's markets are less firmly entrenched than in more mature countries and that the sharp growth still entails some potentially significant risks. Notwithstanding the caution this merits, we also recognise the considerable progress that has been achieved to date in CEE and the positive effects that increasingly close links with the European Union should produce over time.

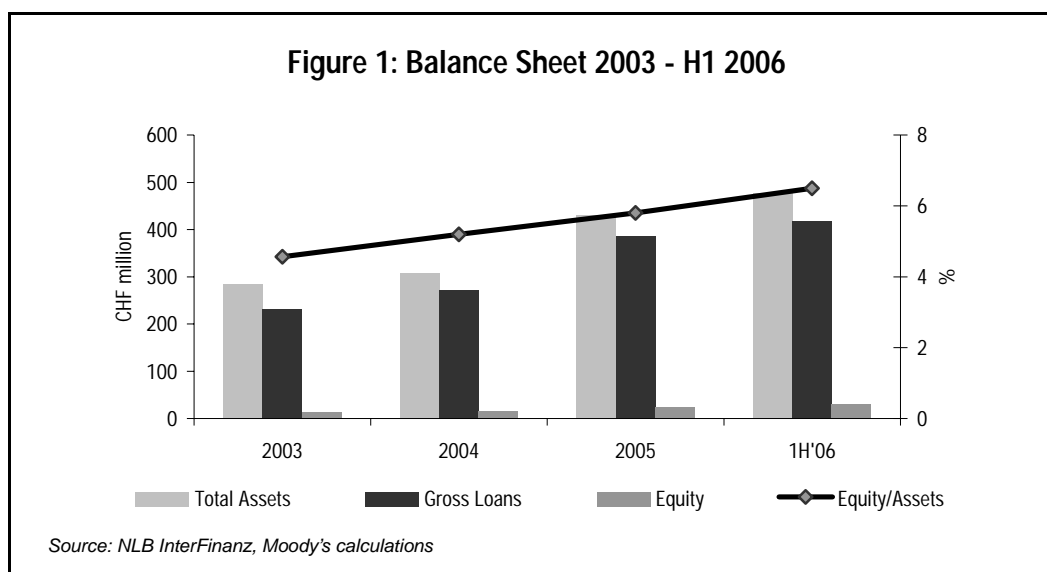
Although the company's single-country exposures are skewed towards sub-investment grade countries, Moody's takes into account the fact that states in financial distress have historically tended to default last on their trade finance obligations as the ongoing supply of vital goods is a critical economic concern for them. Consequently, we believe that NLB InterFinanz's franchise and financial performance should not unduly suffer from macro-economic shocks or country-specific event risks. In fact, Moody's concurs with management's view that the geographic, product- and client-specific diversification should effectively mitigate the risks typical for such developing markets.

Bearing in mind the current cyclical low in the forfaiting market in CEE and in South-Eastern Europe, NLB InterFinanz has geared its business model to a high degree of flexibility in order to allow it to grow and adjust quickly in the fast-changing environment. Given its narrow product range and niche strategy, NLB InterFinanz must excel as much through its quality of execution as through competitive pricing if it is not to lose customer relationships to banks with broader product expertise, stronger pricing power and greater risk-bearing capacity. Moody's believes, however, that the company has succeeded in building a good and defensible, albeit limited, franchise, positioning it well to exploit selectively the expected strong growth in many of the markets in which it is present. Nevertheless, it is worth bearing in mind that as markets mature, demand for forfaiting may fall in the longer run, challenging any competitor in the forfaiting business to expand its product range or geographic focus.

We currently do not expect NLB InterFinanz to change its business model materially, notably with regard to its core activities and geographic focus, but we do expect it to continue to expand. Any significant deviations from this strategic course, especially if they depart from the company's comparative advantages and established area of expertise, could have a detrimental impact on NLB InterFinanz's credit quality.

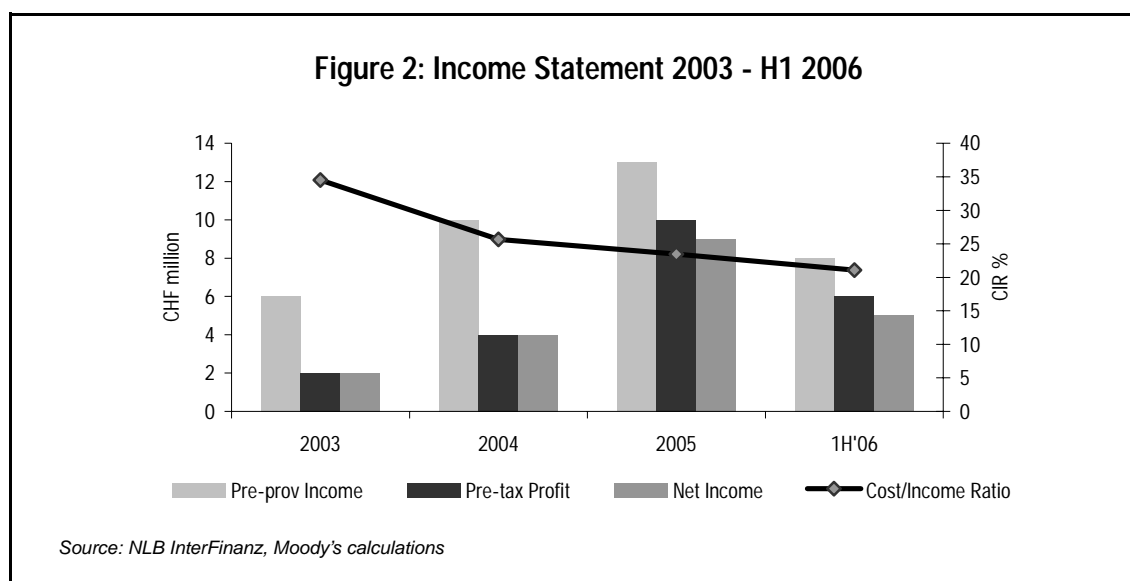
Financial Fundamentals

NLB InterFinanz has recorded rapid growth in its business volumes in recent years. After recording total assets of CHF431 million (equivalent to approximately €277 million or US\$327 million) and equity of CHF25 million at the end of 2005, the balance sheet grew to CHF477 million at the end of June 2006, underpinned by equity of CHF31 million. Moody's is aware of the challenges such expansion poses for a company's operating infrastructure and for maintaining appropriate underwriting standards and control and monitoring procedures; and understands that NLB InterFinanz has continuously adapted its Management Information System to its growing business needs. The current rating is therefore also based upon our expectation that NLB InterFinanz will continue to invest in these areas in order to protect its financial health.



The company's earnings quality is somewhat constrained by its limited-product business focus and is skewed towards net interest revenues. Although their relative importance has decreased, these are likely to remain the principal source of revenues. In this context, we note too that about half of NLB InterFinanz's portfolio consists of loans secured against mortgage collateral. Regardless of the recent progress, we see limited room for greater diversification and believe that net commission revenues are likely to remain of minor significance. NLB InterFinanz seldom engages in trading activities relating to its forfeiting portfolio and is perceived by the market as a final investor.

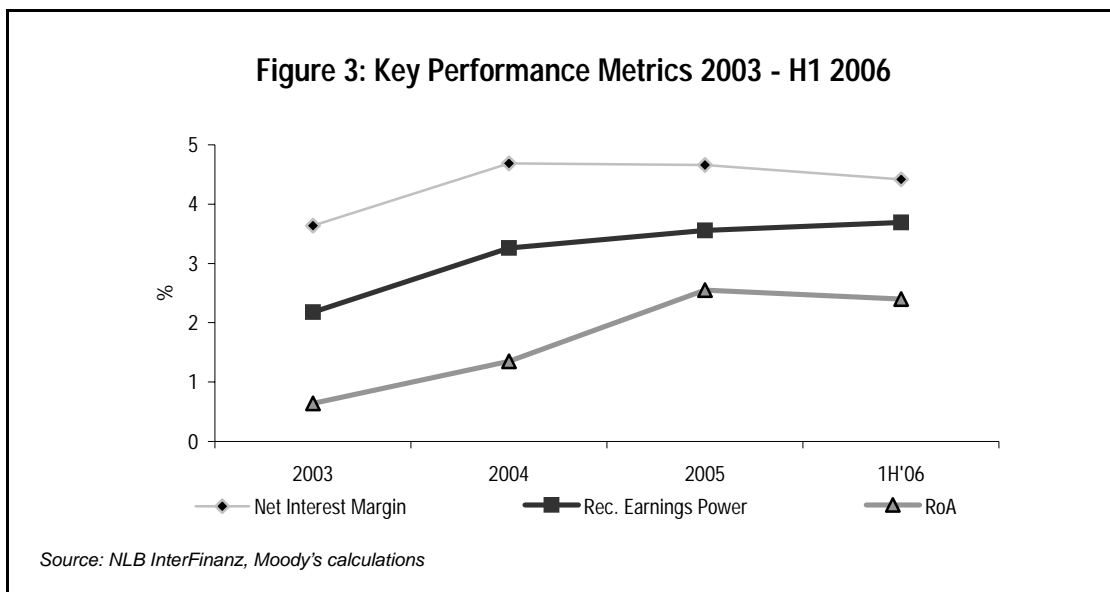
In line with the company's overall limited size, the level of pre-provision income, operating profits and net income have developed positively, albeit at low levels. For 2005, NLB InterFinanz reported pre-provision income of CHF13 million and a net income of CHF9 million. First-half results for 2006 suggest that NLB InterFinanz should be able to extend its upward trend, in both absolute and relative terms, with pre-provision income of CHF8 million and net income of CHF5 million.



Historically, asset quality, the cost of credit risk and provisioning levels have been satisfactory, reflecting the institution's good risk management capabilities and the high degree of collateralisation of its loan portfolio. Apart from geographic concentrations to some sub-investment-grade countries, we note that in terms of individual transactions and exposures NLB InterFinanz may occasionally show more meaningful risk concentrations when measured against its pre-provision income. The proportion of un-guaranteed lending is limited to counterparties known for their solid creditworthiness, such as government-owned companies, and is in most cases secured by mortgage or other types of collateral. Bank counterparties are carefully selected and constantly monitored in close liaison with NLB. Loan loss

provisions have generally been negligible, except for a manageable charge of CHF2 million in 2004. In Moody's view, NLB InterFinanz has built sufficient provisions to protect itself from political and transfer risks.

Key performance indicators show that the growth in volume has not come at the cost of lower profitability. For the first six months of 2006, NLB InterFinanz achieved a high net interest margin of 4.42%, a good recurring earnings power of 3.69% and a solid return on assets of 2.40%. While the company's expansion may trigger investment requirements for its back- and middle-office operations and infrastructure, we do not foresee a material weakening in profitability measures in the medium term.



Roughly 50% of NLB InterFinanz's wholesale funding is provided through NLB Group and, the remaining portion by the interbank market. For the time being, the acceptable strain on its liquidity and funding is sufficiently mitigated by the highly fungible and short-term nature of its receivables, the support from NLB and access to the interbank market. In light of the anticipated growth, it will be one of the company's challenges to continue to strengthen its funding base and liquidity, by broadening the range of products and investors and by moderately lengthening the duration of its liabilities.

With regard to the business and financial risks inherent in its niche franchise and certain asset concentrations, the company's capitalisation is relatively weak when measured by banking standards. Bearing in mind the relatively prudent accounting practices and the meaningful provisions – often of a general nature – which NLB InterFinanz has accumulated over time, capitalisation appears more satisfactory. We note favourably that the good profitability and internal capital generation have led to higher retained earnings and to a stronger equity/assets ratio of 6.5% at the end of June 2006. However, we believe that NLB InterFinanz's financial leverage will rise again in the future.

Issuer Profile

HISTORY

NLB InterFinanz AG (NLBIF) is a specialised trade finance provider established in 1989 in Zurich (Switzerland) as a wholly owned subsidiary of the largest Slovenian bank, Nova Ljubljanska banka d.d. (NLB, rated A2/P-1/C). In March 2006, NLBIF changed its name to NLB InterFinanz AG from LB InterFinanz AG in order to underline its membership of the NLB banking group.

OWNERSHIP

NLBIF is 100% owned by Nova Ljubljanska banka d.d. Slovenia (rated A2/P-1/C).

BUSINESS ACTIVITIES

NLBIF's has a niche strategy and narrow product range, with its main activities being forfaiting (without recourse) and the provision of other forms of financing for international trade-related transactions. Financing is almost entirely provided in major currencies, mainly euros. Complementary activities include direct financing, risk participation and financial consulting.

Geographically, the bank is active in South-Eastern and Eastern Europe. While the six countries of former Yugoslavia (Slovenia, Serbia, Montenegro, Macedonia, Bosnia and Herzegovina, and Croatia) form NLBIF's core market, the portfolio is now diversified into over 20 countries.

More specifically, NLBIF offers the following products and services:

- Forfaiting: NLBIF purchases receivables from exporters on a non-recourse basis. In this context, NLBIF assumes all risks associated with the underlying transaction from the exporter or the selling party, including political, commercial, interest rate, currency and transfer risk.
- Loans: NLBIF offers, on a case-by-case basis, structured import, export and pre-export financing, as well as project-related commercial loans and buyer's credits.
- Unfunded risk acceptance, typically through confirmations of Letters of Credit (L/C) and Letters of Guarantee (L/G). This represents an irrevocable undertaking by NLBIF to settle amounts owed at maturity of the L/C or L/G in case the other parties involved do not effect payment in accordance with the underlying transaction's terms. On a case-by-case basis, NLBIF also enters into risk participation agreements, providing its clients with full or partial coverage of risks embedded in the underlying export transaction.
- Others, including financial consulting and project-related financing.

NUMBER OF EMPLOYEES

At 31 December 2005, NLBIF employed 19 staff.

DISTRIBUTION CAPACITY

NLBIF maintains two branches, one in Zurich and the other in Ljubljana (Slovenia). The institution also benefits from a number of subsidiaries and foreign representatives in its target countries (see below).

INTERNATIONAL REPRESENTATION

NLBIF maintains subsidiaries in Prague (Czech Republic), Belgrade (Serbia) and Skopje (Macedonia). The institution also has two foreign representatives, one in Frankfurt (Germany) and one in Gorizia (Italy). The business units in Prague, Gorizia, Belgrade and Frankfurt have business promotion and representation functions. The entity in Skopje (NLB Lizing d.o.o.e.l. Skopje) is a leasing subsidiary, which holds a majority share of the Macedonian leasing market. The leasing subsidiary is in the process of being sold to NLBIF's parent, Nova Ljubljanska banka.

SUBSIDIARIES RATED BY MOODY'S

None.

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	12/31/05	12/31/04	12/31/03	12/31/02	12/31/01
Summary Balance Sheet (CHF million)					
Cash & central bank	4	3	1	1	1
Due from banks	3	1	6	6	7
Securities	0	0	0	0	0
Gross loans	387	272	231	196	157
Loan loss reserves (LLR)	0	0	0	0	0
Insurance assets	0	0	0	0	0
Fixed assets	0	0	0	0	0
Other assets	37	32	47	21	23
Total assets	431	308	285	223	188
Total assets (USD million) [1]	327	271	231	161	113
Total assets (EUR million)	277	199	183	154	127
Demand deposits	0	0	0	0	0
Savings deposits [2]	0	0	0	0	0
Due to banks	0	0	0	0	0
Market funds	0	0	0	0	0
Insurance liabilities	0	0	0	0	0
Other liabilities	405	292	273	212	178
Total liabilities	406	292	273	212	178
Subordinated debt	0	0	0	0	0
Shareholders' equity	25	16	13	11	10
Total capital funds	25	16	13	11	10
Total liabilities & capital funds	431	308	285	223	188
Derivatives - notional amount	2	—	—	—	—
Derivatives - replacement value	—	—	—	—	—
Contingent liabilities	10	8	—	—	—
Risk weighted assets (RWA)	—	—	—	—	—
Assets under management (CHF million) [3]	—	—	—	—	—
Number of employees	19	19	18	—	—
Summary Income Statement					
+Interest income	23	19	15	13	11
-Interest expense	8	6	6	6	7
=Net interest income	15	12	9	6	4
+Trading income	0	0	0	0	-1
+Fee & commission income	1	0	0	1	1
+Insurance income (net)	0	0	0	0	0
+Dividend income and other operating income	1	0	0	0	0
=Operating income	17	13	9	7	4
-Personnel expenses	3	2	2	1	1
-Other operating expenses	1	1	1	1	1
= Operating funds flow	13	10	6	5	1
-Amortisation/depreciation	0	0	0	0	0
(Total operating expenses)	4	3	3	3	2
=Preprovision income (PPI)	13	10	6	5	1
-Loan loss provisions	0	2	0	0	0
+Impairment of goodwill, fixed assets and investments [4]	-4	-3	-4	-3	-1
+Result of subsidiaries and associates	0	0	0	0	0
+Non-recurring items	1	-1	0	0	0
=Pretax income	10	4	2	2	1
-Taxes	1	0	0	0	0
=Net income	9	4	2	1	0
-Minority interests	0	0	0	0	0
=Net income (group share)	9	4	2	1	0
Growth Rates (%)					
Gross loans	42.28	17.48	18.12	24.56	—
Total assets	39.76	7.98	27.88	18.56	—
Customer deposits (demand and savings)	-35.07	52.34	22.67	-26.00	—
Net interest income	18.04	36.75	41.47	61.95	—
Fee and commission income	188.28	10.18	-59.22	33.99	—
Operating expenses	20.80	1.80	27.49	10.90	—
Preprovision income	35.95	55.56	36.42	212.88	—
Net income	136.13	117.41	26.15	247.74	—
Income Statement in % Average Risk Weighted Assets					
Net interest income	—	—	—	—	—
Trading income	—	—	—	—	—
Fee and commission income	—	—	—	—	—
Insurance income	—	—	—	—	—
Operating income	—	—	—	—	—
Operating expenses	—	—	—	—	—
Preprovision income	—	—	—	—	—
Loan loss provisions	—	—	—	—	—
Extraordinary profit	—	—	—	—	—
Net income	—	—	—	—	—

	12/31/05	12/31/04	12/31/03	12/31/02	12/31/01
Liquidity, Funding (including sub debt) & Balance Sheet Composition					
Avg. liquid assets % avg. total assets	1.55	1.87	2.58	3.45	4.13
Avg. gross loans % avg. total assets	89.14	84.79	84.02	85.85	83.55
Avg. customer deposits % avg. total funding	100.00	100.00	100.00	100.00	100.00
Avg. interbank funds % avg. total funding	0.00	0.00	0.00	0.00	0.00
Avg. market funds (excl. interbank) % avg. total funding	—	—	—	—	—
Avg. sub debt % avg. total funding	—	—	—	—	—
Avg. liquid assets % avg. customer deposits	3083.19	2980.09	4890.97	5018.19	4776.52
Avg. gross loans % avg. customer deposits	177455.21	135009.44	159360.61	124736.98	96651.94
Avg. market funds reliance [5]	-1.74	-2.27	-3.10	-4.13	—
Avg. RWA % avg. total assets	—	—	—	—	—
Breakdown of Operating Income in %					
Net interest income % operating income	85.45	95.60	95.77	90.17	105.13
Trading income % operating income	1.17	0.00	0.00	0.00	-16.94
Fee & commission income % operating income	5.28	2.42	3.01	9.83	13.85
Insurance income % operating income	0.00	0.00	0.00	0.00	0.00
Other operating income % operating income	8.10	1.98	1.22	0.00	-2.04
Profitability					
Yield on avg. earning assets (%)	7.12	6.96	6.60	6.94	6.70
Cost of interest bearing liabilities (%)	4556.78	3284.95	4416.56	4587.78	4410.82
Net interest margin (%) [6]	4.66	4.69	4.01	3.45	2.40
Recurring earning power (Pre-prov. inc. % avg. assets)	3.56	3.26	2.45	2.22	0.77
Risk-weighted recurring earning power (PPI % avg. RWA)	—	—	—	—	—
Post-provision income % avg. assets	3.56	2.51	2.45	2.21	0.77
Post-provision income % avg. risk weighted assets	—	—	—	—	—
Return on average assets (%)	2.55	1.35	0.72	0.71	0.22
Return on avg. RWA (%)	—	—	—	—	—
Post-provision income % tier 1 capital	—	—	—	—	—
Return on equity (period end) (%)	37.51	24.64	14.50	12.97	4.24
Net interest income coverage of loan loss provisions	—	5.61	—	434.41	—
Loan loss provisions % preprovision income	—	22.93	—	0.32	—
Pre-tax income % operating income	60.15	33.68	21.23	24.52	13.33
Internal capital growth (%)	58.17	31.53	16.36	14.75	4.24
Dividend payout ratio (%)	0.00	0.00	0.00	0.00	0.00
Efficiency					
Cost/income ratio (op. expenses % op. income) [7]	23.47	25.66	34.53	36.07	61.42
Adjusted cost/income ratio (incl. non-operating items)	39.85	49.28	78.77	75.27	86.67
Operating expenses % average assets	1.09	1.12	1.29	1.25	1.23
Operating income / employee (CHF thousand)	904.29	684.76	527.62	—	—
Operating expenses / employee (CHF thousand)	212.23	175.69	182.18	—	—
PPI / employee (CHF thousand)	692.06	509.07	345.44	—	—
Asset Quality and Risk Measurement					
Problem loans % gross loans	—	—	—	—	—
LLR % problem loans	—	—	—	—	—
LLR % gross loans	—	—	—	—	—
Loan loss provisions % gross loans	—	0.82	—	0.01	—
Problem loans % (shareholders' equity + LLR)	—	—	—	—	—
Replacement value % shareholder's equity	—	—	—	—	—
Capital Adequacy (Period End)					
Tier 1 ratio (%)	—	—	—	—	—
Total capital ratio (%)	—	—	—	—	—
Shareholders' equity % total assets	5.83	5.26	4.44	5.03	5.24
Equity participations % shareholders' equity	48.74	91.16	128.33	38.22	22.88

[1] Historical exchange rates are applied accordingly for USD and EUR figures.

[2] Full disclosure may not be available for all years. The amount is then included in demand deposits.

[3] As reported by the bank.

[4] Includes goodwill amortisation (pre-IFRS).

[5] Avg. [(market funds-liquid assets) % (earning assets-liquid assets)].

[6] Although not part of net interest income calculation, the NIM includes dividend income.

[7] Cost/income ratio excludes goodwill amortisation, which is included together with net non-operating income in the adjusted cost/income ratio.

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