

Rating Action: Moody's concludes reviews on 3 Austrian banking groups; takes action on another 2 institutions' ratings

Global Credit Research - 01 Jul 2015

Actions follow conclusion of methodology-related reviews and revision of government support assumptions

Frankfurt am Main, July 01, 2015 -- Moody's Investors Service has today concluded its rating reviews on three banking groups based in Austria (Aaa stable) and further extended the rating review on one bank. The rating agency first initiated -- and in some cases extended -- the reviews on 17 March 2015, following the publication of the agency's new bank rating methodology and revisions to Moody's government support assumptions for these banks.

Please refer to: https://www.moodys.com/research/--PR_321005, for the rating action published on 17 March 2015 and https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_179038, for Moody's new bank rating methodology, published on 16 March 2015.

The rating agency has now further taken actions on Heta Asset Resolution AG, whose ratings were unaffected following the publication of the new banking methodology.

In light of the new bank rating methodology, Moody's rating actions on the Austrian banking groups generally reflect the following considerations (1) the Macro Profiles applicable to each group or bank, based on the geographical breakdown of their asset bases; (2) these banks' financial profiles and related qualitative factors; (3) the protection offered to depositors and senior creditors in the event of resolution, as captured by Moody's Advanced Loss Given Failure (LGF) analysis, reflecting the benefit of instrument volume and subordination; and (4) Moody's view of a decline in the likelihood of government support for Austrian banks.

The five groups covered in this press release are:

- BAWAG P.S.K. (BAWAG)
- Erste Group Bank AG (Erste)
- Heta Asset Resolution AG (Heta)
- Kommunalkredit Austria AG (KA)
- UniCredit Bank Austria AG (UBA)

and its subsidiary card complete Service Bank AG (card complete)

Among the rating actions on the five Austrian groups and their subsidiaries that Moody's has taken are the following:

- One long-term bank deposit rating upgraded, three confirmed and one downgraded
- Three short-term bank deposit ratings affirmed, and two confirmed
- One bank senior unsecured debt rating upgraded, two confirmed and one downgraded
- Three short-term bank senior unsecured debt ratings affirmed and one confirmed
- Two baseline credit assessments (BCAs) upgraded, two affirmed and one downgraded

Moody's has also assigned Counterparty Risk (CR) Assessments to four Austrian banking groups and their branches and/or subsidiaries, in line with its new bank rating methodology.

Bank level subordinated debt ratings for the affected groups, branches and subsidiaries have either been affirmed,

confirmed or upgraded and most of the hybrid securities ratings were affirmed as part of this rating action. Moody's also affirmed the Aaa subordinated debt rating of Heta's EUR1 billion subordinated debt issued in December 2012 that the Austrian Government guarantees. Subsequently, Moody's has withdrawn the outlooks on all subordinated and junior/hybrid instrument ratings for its own business reasons. For more information, please refer to "Moody's Investors Service's Policy for Withdrawal of Credit Ratings", available at moodys.com.

Outlooks, which provide an opinion on the likely rating direction over the medium term, are now assigned only to long-term deposit and issuer/senior unsecured debt ratings.

Please click on http://www.moodys.com/viewresearchdoc.aspx?docid=PBC_182746 for the List of Affected Credit Ratings. This list is an integral part of this Press Release and identifies each affected issuer.

Moody's has also published a Special Comment entitled "Key Analytic Considerations in Our Rating Actions on Austrian banks", providing more background on today's rating action. Subscribers can access the report under the following link: http://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_1006111.

RATINGS RATIONALE

The new bank rating methodology includes a number of elements that Moody's has developed to help accurately predict bank failures and determine how each creditor class is likely to be treated when a bank fails and enters resolution. These new elements capture insights gained from the crisis and the fundamental shift in the banking industry and its regulation.

(1) MACRO PROFILES RANGING FROM "STRONG-" TO "VERY STRONG-"

The Macro Profile constitutes an assessment of the macroeconomic environment in which a bank operates. The banks' Macro Profiles derive from their asset bases. Exposures to borrowers and issuers in Austria are accounted for with a Macro Profile of "Very Strong-". In addition to their domestic exposures, the major Austrian banks pursue strategic interests in Central and Eastern Europe (CEE) which are characterized by significantly weaker operating environments that are reflected by weaker macro profiles. As a result of the differences in exposure, Macro Profiles vary between "Strong-" and "Very Strong-".

For their domestic business, banks in Austria benefit from operating in a strong economic environment with a robust institutional and legal framework, sound government finances, and very low susceptibility to adverse events. Despite rising house prices, private-sector debt is low and declining, supporting credit conditions. The banks' funding benefits from high levels of domestic and foreign customer deposits. Austria's largest banks rely on wholesale capital markets to fund parts of their CEE lending, but this dependency has reduced. The Macro Profile also incorporates the Austrian banking system's high market fragmentation, low fee-income generation and intense competition for domestic business.

(2) AUSTRIAN BANKS DISPLAY SOLID FINANCIAL RATIOS, BUT CHALLENGES REMAIN

The considerations that support Austrian banks' BCAs are the stable operating environment and the banks' generally improving financial stability.

The creditworthiness of the Austrian sovereign and the country's solid economic development as well as the country's low unemployment support Moody's view of a continued, stable operating environment for Austrian commercial banks (Moody's forecasts Austrian GDP to grow 0.5% in 2015 and 1.3% in 2016).

The banks affected by this rating action are either internationally diversified institutions (Erste, UBA) or specialised domestic lenders (BAWAG, KA, card complete). The banks' BCAs range from b3 to baa3, reflecting the varying challenges resulting from higher-risk CEE exposures or marked portfolio concentrations, as well as from more stringent capital requirements and earnings pressures. However, improving capital ratios, and defensible funding and liquidity mitigate these pressures.

(3) PROTECTION OFFERED TO CREDITORS MORE SENIOR IN THE CREDITOR HIERARCHY, AS CAPTURED BY MOODY'S ADVANCED LGF LIABILITY ANALYSIS

Austrian banks are subject to the EU's Bank Resolution and Recovery Directive (BRRD), which Moody's considers to be an Operational Resolution Regime. Accordingly, Moody's applies its Advanced LGF analysis to Austrian banks' liability structures, thereby mostly applying its standard assumptions. These assumptions include a residual tangible common equity of 3%, losses post-failure of 8% of tangible banking assets, a 25% run-off in junior wholesale deposits, a 5% run-off in preferred deposits, and a 25% probability of deposits being preferred to

senior unsecured debt. For Erste as a more retail-oriented bank, Moody's has considered a proportion of 10% of junior deposits of the banks' total deposit base, below the estimated EU-wide average of 26% applied to commercially more diversified banks.

The Advanced LGF analysis generally results in a "very low" loss-given-failure for long-term junior deposits as well as in a "very low" or "low" loss-given-failure for senior unsecured debt ratings, reflecting the banks' substantial volume of deposit funding as well as the amount of senior unsecured debt and securities more subordinated to it.

For more information on Moody's LGF analysis and a discussion of the differences in creditor hierarchies Moody's "How Resolution Frameworks Drive Our Creditor Hierarchies" at https://www.moody.com/researchdocumentcontentpage.aspx?docid=PBC_1003760 (in addition to the methodology itself).

(4) REDUCED LIKELIHOOD OF GOVERNMENT SUPPORT

Moody's has lowered its expectations about the degree of support that the government might provide to a bank in Austria. The main trigger for this reassessment is the introduction of BRRD and its recent application to Heta, as wind-down institutions are in the scope of the Austrian transposition of BRRD.

With the implementation of bank resolution legislation, Moody's has either eliminated or lowered its assumption about the probability of government support for the banks in the EU, thereby generally attributing a "moderate" probability of government support to banking groups in the EU that are considered systemically relevant. While Moody's considers Erste and UBA to be domestically systemically relevant, the rating agency now only attributes a "low" probability of Austrian government support -- from mostly "high" previously -- in light of the precedent set by triggering a resolution of Heta. Moody's believes that the wider scope of the BRRD implementation in Austria and its recent application illustrate the willingness of the Austrian government to apply burden-sharing.

The reduction of government support assumptions for KA to "low" from previously "very high" results in one notch of rating uplift from the Austrian government support versus eight previously. While not considered systemically relevant, in its revised assessment the rating agency has taken into account that KA continues to be owned by the Austrian Government which, for now, retains the discretion as to whether it will provide liquidity and capital support under KA's state-aid case decision that the European Commission took before the introduction of BRRD. Moody's expects to reconsider this assessment once the pending sales process has been completed.

Following Moody's revised support assessments, only KA continues to benefit from Austrian government support.

See also "Austrian application of BRRD to wind-down entity Heta sets precedent" at https://www.moody.com/researchdocumentcontentpage.aspx?docid=PBC_1003540.

RATIONALE FOR THE OUTLOOK ON DEBT AND DEPOSIT RATINGS

The outlooks on deposits and debt ratings for most banks affected by today's rating action principally reflect the anticipated evolution of the banks' financial fundamentals in combination with Moody's expectations regarding potential changes in the banks' liability structures. These changes may change the amount of uplift provided by Moody's LGF analysis, thereby affecting the banks' debt and/or deposit ratings.

--- BANK SPECIFIC ANALYTIC FACTORS

BAWAG P.S.K.

The one-notch upgrade of BAWAG's long-term deposit and senior unsecured debt ratings to Baa1 incorporates (1) the one-notch upgrade of the bank's BCA and adjusted BCA to baa3; (2) the results of Moody's LGF analysis providing a two-notch uplift to the bank's debt and deposit ratings; thereby together more than offsetting (3) the removal of two notches of government support uplift.

The upgrade of the BCA reflects the stronger and higher-quality capital adequacy ratios and the bank's underlying recovery in profitability that have allowed the bank to reduce on-balance sheet risks, as well as its significantly strengthened loss-absorption capacity.

BAWAG's baa3 BCA is at the low-end of Moody's scorecard range, indicating potential upside over Moody's 12-18 month outlook horizon. This reflects the rating agency's anticipation of a further improvement in the bank's financial profile, driven by (1) the further de-risking of the bank's balance sheet; (2) the continuous build-up of the bank's capital adequacy ratios; and (3) BAWAG establishing a sustainable track record of higher earnings levels.

BAWAG's BCA remains constrained by Moody's assessment of the bank's expansion into higher-risk asset classes, including international corporate and commercial real estate. In Moody's view, this adds concentration risks to BAWAG's balance sheet and may exert undue pressure on the bank's profitability and, potentially, capital ratios in a highly adverse scenario.

For BAWAG, Moody's LGF analysis indicates a very low loss-given-failure for senior unsecured debt and deposits, leading to a two-notch uplift on BAWAG's wholesale deposits as well as its senior unsecured debt from its baa3 adjusted BCA.

The outlook on the long-term debt and deposit ratings is positive.

ERSTE GROUP BANK AG

The confirmation of Erste's long-term deposit and senior unsecured debt ratings at Baa2 reflects (1) the affirmation of the bank's BCA and adjusted BCA at ba1; (2) the results of Moody's LGF analysis, providing a two-notch uplift to the bank's debt and deposit ratings; offsetting (3) the removal of two notches of government support uplift.

The affirmation of Erste's ba1 BCA reflects (1) Erste's overall satisfactory financial fundamentals; (2) its leading retail and corporate franchises throughout Austria and the more mature economies in Central and Eastern Europe (CEE); and (3) its solid and highly granular deposit funding base. However, the BCA is constrained by the bank's (1) high, albeit declining, volume of problem loans, which may exert pressure on the bank's capital generation capacity in an adverse scenario; and (2) moderate capitalisation metrics for its risk profile.

For Erste, Moody's LGF analysis indicates a very low loss-given-failure for senior unsecured debt and deposits, leading to a two-notch uplift on Erste's wholesale deposits as well as its senior unsecured debt from its ba1 adjusted BCA.

The outlook on the long-term debt and deposit ratings is stable, reflecting the stabilisation of the bank's financial profile, also a result of its improved asset-quality metrics.

KOMMUNALKREDIT AUSTRIA AG

KA's long-term deposit and senior unsecured debt ratings were downgraded by two notches to Ba3. The rating action incorporates (1) a three-notch upgrade of the bank's BCA and adjusted BCA to b3; (2) the results of Moody's LGF analysis providing a two-notch uplift to the bank's debt and deposit ratings; together not fully offsetting (3) the reduction in government support uplift.

The upgrade of KA's BCA to b3 reflects the bank's gradual progress in reducing legacy assets without needing to resort to additional capital or liquidity support from its ultimate owner, the Austrian government. KA has improved its risk-weighted capital ratios and returned to modest levels of profitability. But, the BCA remains constrained by (1) the very high single-name concentrations in the bank's public finance and infrastructure lending portfolio, which will become even more accentuated during KA's ongoing wind-down of its monoline exposure book; in combination with (2) very weak Tangible Common Equity leverage ratios (1.9% as of FYE 2014); and (3) the low visibility regarding the development of the bank's standalone financial profile as result of the agreed partial sale of the bank.

Under Moody's Advanced LGF analysis, KA's long-term deposit and senior unsecured debt ratings take into account their very low loss-given-failure because of the bank's high volume of senior unsecured debt outstanding, leading to a two-notch uplift, respectively, from the bank's b3 adjusted BCA.

KA's long-term debt and deposit ratings, as well as the bank's BCA, were placed under review with direction uncertain, reflecting (1) the lack of visibility as to the impact on the bank's standalone profile of the planned, but yet to be fully substantiated, asset and liability split; and (2) the need to re-assess government support for the future obligors of debt issued by KA or its successor entities.

UNICREDIT BANK AUSTRIA AG

The confirmation of UBA's Baa2 long-term deposit and senior unsecured debt ratings reflects (1) the one-notch downgrade of the bank's BCA to ba2; (2) the confirmation of the ba1 adjusted BCA, reflecting the offsetting effect of one notch of rating uplift for support from UBA's Italian parent bank, UniCredit SpA (deposits Baa1 stable, BCA ba1), which the rating agency expects to be available with a "very high" probability; (3) the results of Moody's LGF analysis, which support the bank's deposit and debt ratings, adding two notches to these ratings; together fully offsetting (4) the removal of two notches of government support uplift.

Because Moody's no longer recognises sub-sovereign credit enhancement for Austrian bank debt, the rating agency downgraded to Baa2 (from Baa1) with a stable outlook the long-term senior unsecured instruments backed by a deficiency guarantee of the City of Vienna (Aaa stable).

The BCA downgrade indicates deterioration in the operating environment for some of UBA's Central and Eastern European (CEE) operations, which raise risks to capital. Risks are particularly high in relation to exposures in Russia (Ba1 negative) that have been a prominent contributor to group profits in recent years. A deep and extended depression of the Russian economy would imply elevated credit and market risk for UBA. However, support from UBA's parent company will likely offset any pressure on the Austrian group's resources, should additional capital requirements add further pressure. This is reflected in the unchanged adjusted BCA of ba1, which now includes one notch of affiliate support.

Under Moody's LGF framework, UBA's long-term senior unsecured debt and deposit ratings take into account their very low loss-given-failure, owing to the group's high volume of subordinated and senior unsecured debt.

The stable outlook on UBA's senior debt and deposit ratings reflects Moody's expectations that UniCredit SpA will remain fully committed to UBA, and that UBA's liability structure will remain broadly unchanged. The latter includes the view that UBA will issue additional subordinated instruments that will offset any underwriting of subordinated debt for its subsidiaries outside Austria.

CARD COMPLETE SERVICE BANK AG

Card complete's deposit ratings were confirmed at Baa3. The rating action incorporates (1) an affirmation of the bank's ba2 BCA; (2) a downgrade of the adjusted BCA to ba2 from baa3, reflecting Moody's assessment of a reduced ability of card complete's parent, UBA, to provide affiliate support when needed and the removal of one notch of indirect government support uplift; and (3) the results of Moody's LGF analysis transferred to card complete from its parent UBA.

The affirmation of card complete's BCA at ba2 reflects (1) the bank's sound coverage of asset risks; (2) the bank's high, but declining profitability levels; (3) sound risk-weighted capitalization, even after adjusting for the zero risk-weighting of exposures to UBA; and (4) a high degree of dependence on UBA in terms of card complete's funding profile.

For its LGF analysis, Moody's assumes that card complete, as a majority owned domestic subsidiary, would be resolved together with UBA. Therefore, the same LGF notching applies to UBA as to card complete, affording two notches of uplift from the bank's ba2 adjusted BCA.

The outlook for the long-term deposit ratings of card complete is stable, in line with the rating outlook assigned to UBA's deposit ratings.

RATIONALE FOR COUNTERPARTY RISK (CR) ASSESSMENTS

Moody's has also assigned CR Assessments to four Austrian banking groups and their branches/subsidiaries. CR Assessments are opinions of how counterparty obligations are likely to be treated if a bank fails, and are distinct from debt and deposit ratings in that they (1) consider only the risk of default rather than expected loss and (2) apply to counterparty obligations and contractual commitments rather than debt or deposit instruments. The CR Assessment is an opinion of the counterparty risk related to a bank's covered bonds, contractual performance obligations (servicing), derivatives (e.g., swaps), letters of credit, guarantees and liquidity facilities.

The CR Assessment takes into account the issuer's standalone strength as well as the likelihood of affiliate and government support in the event of need, reflecting the anticipated seniority of these obligations in the liabilities hierarchy. The CR Assessment also incorporates other steps authorities can take to preserve the key operations of a bank should it enter a resolution.

For the affected Austrian banking groups, the CR Assessment, prior to government support, is in most cases positioned three notches above the adjusted BCA and therefore above senior unsecured and deposit ratings, reflecting Moody's view that its probability of default is lower than that of senior unsecured debt and deposits. Moody's believes that senior obligations represented by the CR Assessment likely be preserved in order to limit contagion, minimize losses and avoid disruption of critical functions.

In line with Moody's support assumptions on deposits and senior unsecured debt, the CR Assessments of Austrian banking groups do generally not benefit from government support.

WHAT COULD CHANGE THE RATINGS UP/DOWN

Upward rating momentum on any of the affected Austrian banks' ratings could develop from (1) a sustainable and significant improvement in the banks' profitability; (2) further improvements in the banks' and the groups' asset quality; (3) materially stronger capital positions; and/or (4) a substantial increase in the volume of the banks' liquid resources that significantly exceeds the banks' confidence-sensitive wholesale funding sources.

Downward rating pressure could emerge if (1) asset quality declines, in particular in relation to CEE and foreign-currency exposures; (2) credit underwriting standards deteriorate beyond Moody's current expectations; (3) current revenue and profitability pressures intensify, especially if the low interest-rate environment persists or even worsens; (4) the domestic and/or CEE macroeconomic environment deteriorates such that unemployment rises markedly and the Austrian real-estate markets weaken; and/or (5) the banks' liquidity profiles deteriorate significantly.

Upward (or downward) pressure on the long-term debt and deposit ratings could develop if the individual banks' subordinated instruments increase (or decrease) relative to their tangible banking assets, which could result in additional (or fewer) notches of uplift resulting from Moody's LGF analysis, thereby affecting the debt and/or deposit ratings.

PRINCIPAL METHODOLOGY

The principal methodology used in these ratings was Banks published in March 2015. Please see the Credit Policy page on www.moodys.com for a copy of this methodology.

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The below contact information is provided for information purposes only. Please see the ratings tab of the issuer page at www.moodys.com, for each of the ratings covered, Moody's disclosures on the lead analyst and the Moody's legal entity that has issued the ratings.

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