

**Austria
Credit Update**

KA Finanz AG

Ratings

Long-Term IDR	A+
Short-Term IDR	F1+
Support Rating	1
Support Rating Floor	A+
Sovereign Risk	
Foreign-Currency Long-Term IDR	AAA
Local-Currency Long-Term IDR	AAA

Outlooks

Foreign-Currency Long-Term IDR	Stable
Sovereign Foreign-Currency Long-Term IDR	Stable
Sovereign Local-Currency Long-Term IDR	Stable

Financial Data

KA Finanz AG	
	30 Jun 09 ^a
Total assets (USDm)	24,627.1
Total assets (EURm)	17,423.7
Total equity local GAAP (EURm)	781.4
Total equity IFRS (EURm)	-191.1
Operating profit 2009 (EURm) ^b	35.1
Published pre-tax income 2009 (EURm) ^b	-81.5
Operating ROA 2009 (%) ^b	0.20
Operating return on Austrian GAAP equity 2009 (%) ^b	5.40
Pre-tax return on Austrian GAAP equity 2009 (%) ^b	-12.53
IFRS equity/assets (%)	-1.17
Austrian GAAP equity/assets (%)	3.73
Tier 1 ratio (%)	7.30

^a Unaudited pro forma financials under Austrian GAAP;
^b management forecast, end-H109 P&L not available; once Kommunalkredit International Bank Ltd. has been merged with KA Finanz, KA Finanz will solely report under Austrian GAAP.

Analysts

Christian Kuendig, London
+44 20 7682 7541
christian.kuendig@fitchratings.com

Michael Steinbarth, London
+44 20 7682 7468
michael.steinbarth@fitchratings.com

Related Research

- *Fitch Rates Newly-Formed Kommunalkredit Austria 'A'; Outlook Stable (30 November 2009)*
- *Global Financial Institutions Rating Criteria (29 December 2009)*

Rating Rationale

- KA Finanz AG's (KA Finanz) ratings are based on its 99.78% ownership by the Republic of Austria and Fitch Ratings' assumption that there will be no change to the ultimate ownership and the willingness of Austria to support KA Finanz AG. Given that KA Finanz's sole purpose is to ensure an orderly run-off of its asset base, Fitch no longer assigns an Individual Rating.
- KA Finanz, established 28 November 2009, is the legal successor of Kommunalkredit Austria (KA Old), which was nationalised in late 2008 after severe liquidity and funding problems. KA Finanz holds KA Old's non-core assets, essentially its credit default swap (CDS) book and non-core public-sector credit exposure. KA Old's core business was transferred to newly established Kommunalkredit Austria AG (KA New; 'A'/Stable; see *Related Research*).
- Given that KA Finanz will not undertake any new business, the bank's profitability largely depends on the performance of its current asset base. Assuming a recovery in asset values, management expects KA Finanz's underlying revenue to be adequate. However, due to annual guarantee payments to the owner (around EUR110m-EUR130m net for funding and asset guarantees), Fitch expects KA Finanz to report pre-tax losses in 2009-2012.
- KA Finanz is mostly exposed to credit risk in its large CDS and public sector loan/bond books and corresponding funding and liquidity risks. At end-H109, its total credit exposure amounted to EUR27.4bn with two-fifths each relating to its CDS and bond books respectively. Most of its exposure is to public-sector entities in the EU (67%, excl. Austria), non-EU European states (6%), Austria (5%) and non-European countries (22%). The average rating at end-H109 was 'A+'.
- Due to a high proportion of long-term assets (around 50% of assets mature after 2014) and a large share of short-term funding, KA Finanz is running a significant funding gap. At end-H109, state-guaranteed funding made up 31% of non-equity funding, ECB funding 17% and money market funding 35%. Despite recovering asset values, KA Finanz's IFRS equity remained negative at end-H109. Its Tier 1 ratio, under Austrian GAAP, amounted to 7.3%. The Republic of Austria has committed to maintaining a Tier 1 ratio of 7% as long as the bank's former owners remain invested in KA Finanz's participation capital.

Support

- Given KA Finanz's ownership, Fitch considers there to be an extremely high propensity of support from the public authorities.

Key Rating Drivers

- The Stable Outlook on KA Finanz's Long-Term IDR mirrors the Outlook on the sovereign. An unexpected change in KA Finanz's ownership, i.e. after a European Commission ruling, or a downgrade of Austria would lead to a reassessment of KA Finanz's ratings.

Profile

KA Finanz is running off its assets. It retains a banking licence but its operations are conducted via service-level agreements with KA New. KA Finanz's subsidiary, Cyprus-based Kommunalkredit International Bank Ltd ('A+'/Stable), will be merged into KA Finanz in H110.