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## Ratings On Some Austrian Banks Lowered On Less Predictable State Support And Increasing Industry Risks

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- We believe the prospect of extraordinary government support for Austrian banks is now uncertain and we therefore include no uplift in the ratings on systemic commercial banking groups domiciled in Austria.
- We nevertheless recognize that the Austrian bank resolution framework is well advanced, and therefore can include notches of uplift for systemic banks that we expect will build sizable bail-in capital volumes over the coming years.
- Significant overcapacity in Austrian banks' domestic operations results in very low earnings and, in our view, may threaten the stability of the Austrian banking system.
- We have resolved the CreditWatch placements on highly systemically important banks and their subsidiaries and reviewed three government-related entities in Austria, lowering the long-term ratings on five banks and affirming the ratings on another three.
- The outlook on four Austrian banks is negative because we see residual doubts about the development of their financial profiles over the next two years.

FRANKFURT (Standard & Poor's) June 9, 2015--Standard & Poor's Ratings Services today took various rating actions on certain Austrian banks. This follows the introduction of a well-formed bank resolution framework in Austria, the ongoing regulatory impetus to have systemic banks hold sizable buffers of bail-in capital that authorities could use to recapitalize them, and our view

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that increasing industry risks in Austria's banking system have weakened their operating environment.

As a result of various combinations of these factors, we have lowered the long-term counterparty credit ratings on highly systemically important banks Erste Group Bank AG, Raiffeissen Zentralbank Oesterreich AG and its subsidiary Raiffeisenbank International AG, UniCredit Bank Austria AG, and one government-related entity (GRE) Oberoesterreichische Landesbank AG.

We have affirmed the ratings on Erste's Czech subsidiary Ceska Sporitelna A.S. as well as on two Austrian GREs: HYPO NOE Gruppe Bank AG and KA Finanz AG.

We removed the ratings on highly systemically important banks from CreditWatch with negative implications, where we had placed them on Feb. 3, 2015.

For a full list of the counterparty credit ratings and outlooks on all banks see "RATINGS LIST" below.

We have today taken similar rating actions on certain U.K. and German banks. For more details, see: "S&P Takes Various Rating Actions On Certain U.K. And German Banks Following Government Support And ALAC Review," published today on RatingsDirect.

### RATIONALE

Further to this announcement, within the next 24 hours we will publish a research update on each banking group to explain in more detail the rating action we have taken, the reasons behind it, and our view of the likely future ratings drivers.

However, to summarize these actions, we believe that the prospect of extraordinary government support for Austrian banks is now uncertain, following the full implementation of the EU Bank Recovery and Resolution Directive, including bail-in powers, in January 2015. We have therefore reclassified Austria's tendency to support private sector commercial banks as "uncertain" under our criteria, and removed the two notches of uplift for government support that we previously included in the long-term counterparty credit ratings on highly systemically important banks.

We have also removed the one-notch negative adjustment that we introduced into the ratings on these banks on Aug. 13, 2014, to reflect lower predictability of state support following the enactment of the legislation to bail in holders of Hypo Group Alpe Adria's subordinated debt, despite Carinthia's grandfathered guarantee of this debt.

Following our review of Austrian banks' additional loss-absorbing capacity (ALAC), we currently do not add any uplift to the ratings on the banks. However, we view the Austrian resolution regime as "effective" under our ALAC criteria because, among other factors, we believe it contains a well-defined bail-in process under which authorities would permit nonviable systemically important banks to continue critical functions as going concerns following a

bail-in of eligible liabilities.

We also see that ALAC could contribute to a one-notch uplift to the long-term rating on Erste in the next two years. If Erste's management delivers on its plan to issue a sufficient amount of hybrid instruments, this could increase ALAC above our 5% threshold.

Our rating actions also reflect our opinion that industry risk for the Austrian banking system has increased. We consider that the significant overcapacity in the banking sector's domestic operations results in very low bank earnings and may pose a threat to the stability of the Austrian banking system. The economic slowdown and low interest rate environment aggravates this risk. Because we expect margins to remain compressed over a prolonged period, we see a risk that some banks may struggle to generate a risk-adjusted return that is adequate to meet their cost of capital.

The competitive landscape for Austrian banks is becoming additionally challenging as the largest banks scale down their foreign operations in higher risk regions, which leads to increasing pressure to generate earnings in their domestic markets. Furthermore, the government's comparably high levy on banks is further diminishing domestic banks' chances of generating internal capital.

Our stable trend for industry risk in the sector takes into account our expectation that the significant overcapacity in the banking sector and compressed margins will prevail at least over the medium term. We expect that structural implications of the competitive landscape faced by Austrian banks in the domestic market will continue to weigh on our industry risk assessment, but we don't anticipate further deterioration.

#### Erste Group Bank AG

We lowered the long-term issuer credit rating (ICR) on Erste to 'BBB+' from 'A-'. We lowered the stand-alone credit profile (SACP) by one notch due to increasing industry risk and removed two notches of government support uplift. However, we also removed the negative adjustment notch we had introduced on Aug. 13, 2014, reflecting lower predictability of state support. We also now include a one-notch upward adjustment into the ratings on Erste, as we anticipate positive momentum in the bank's earnings after the clean-up of its portfolio in 2014 and management's plans to issue hybrid capital to strengthen Erste's profile over the medium term. The negative outlook on Erste reflects the risk that its internal capital generation proves to be slower than we currently anticipate, with a risk-adjusted capital ratio remaining below 7% over the next two years. It also reflects the risk that the bank does not accumulate a hybrid capital buffer to provide sufficient protection for senior unsecured creditors as reflected in an ALAC proportion of risk-weighted assets, as calculated by Standard & Poor's, above 5%. We may furthermore take a negative rating action if unexpected material risks arise from the bank's Central and Eastern European operations, leading to a deterioration of the bank's asset quality.

Ceska Sporitelna A.S.

The affirmation of the ratings on Ceska Sporitelna (Ceska) reflects our opinion that the bank is likely to benefit from extraordinary government support from the Czech Republic. This provides a one-notch uplift to Ceska's stand-alone credit profile (SACP) of 'bbb+', resulting in a 'A-' long-term ICR. We view Ceska as a core subsidiary of Erste under our criteria, but we now replace group support with extraordinary government support from the Czech Republic in the ratings. The negative outlook on Ceska reflects our view that potential extraordinary government support for systemically important banks in the Czech Republic will likely decrease when the resolution framework is put in place.

Raiffeisen Zentralbank Oesterreich AG (RZB) and Raiffeisen Bank International (RBI)

For RZB, we anticipate that cohesiveness in and benefits from the aggregate franchise and creditworthiness of the wider Raiffeisen Banking Group (RBG) have intensified, for which reason we now base our ratings on RZB entirely on RBG's group credit profile (GCP). On this basis, as well as the removal of two notches of government support and one negative adjustment notch, the net effect on the long-term ICR on RZB is a one-notch downgrade to 'BBB+' from 'A-'. As a result of the rating action on RZB, we lowered the long-term rating on RBI by two notches. We regard RBI as a highly strategic subsidiary to RBG. The negative outlook on RZB reflects the wider RBG's vulnerabilities to the impact of a potential worsening of geopolitical and economic risk conditions in its extended home market in Central and Eastern Europe (CEE), especially in Russia and Ukraine, over the next 12-24 months. This is the case particularly if higher credit losses and weaker earnings for RZB in these regions cannot be offset by solid domestic earnings and more benign developments in other parts of its diversified CEE and Southeastern Europe (SEE) operations. The outlook on RBI mirrors that on its parent RZB.

UniCredit Bank Austria AG

We believe UniCredit Bank Austria (Bank Austria) is generally eligible for consideration of ALAC because we consider the bank a prudentially regulated subsidiary that we expect to be subject to a separate resolution process. We think it will be able to continue operating without defaulting on its senior unsecured obligations in the event of a resolution of the parent. Moreover, the subsidiary is not able to recapitalize another part of the group in line with our ALAC criteria. Accordingly, we rate Bank Austria at the same level as its 'bbb' SACP, higher than the 'bbb-' GCP of UniCredit SpA. On this basis, as well as the removal of two notches of government support and one negative adjustment notch, the net effect on the rating on Bank Austria is a one-notch downgrade of the long-term ICR. The negative outlook on Bank Austria reflects our view of a one-in-three risk that--in contrast to our current expectations--the likely BRRD application and intent by the European Single Resolution Board, which starts only in 2016, develops in favor of a more unified single-resolution process for all cross-border members of nationwide groups such as UniCredit SpA. This would be detrimental to Bank Austria being rated higher than its parent. Moreover, the negative outlook reflects Bank Austria's vulnerabilities to the impact of a potential worsening of geopolitical and economic risk conditions in Russia, as well as possible

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contagion in CEE and SEE over the next 12-24 months. This holds particularly if higher credit losses and weaker earnings for Bank Austria in these regions cannot be offset from solid domestic earnings and more benign developments in other of its diversified CEE and SEE operations, or Bank Austria's RAC ratio were to fall below 5%.

### KA Finanz AG

We affirmed the ratings on the GRE, KA Finanz AG, at 'A-' and our outlook on the rating is stable because we expect KA Finanz will continue its wind-down with the benefit of extraordinary government support. We anticipate that the forthcoming merger with the non-privatized part of Kommunalkredit Austria AG will not materially alter the bank's SACP.

### HYPO NOE Gruppe Bank AG (HYPO NOE)

The rating affirmation and stable outlook on HYPO NOE is also supported by its status as GRE. We have revised down the stand-alone credit profile (SACP) of HYPO NOE to 'bbb' from 'bbb+', to reflect our view that the increased risks in the domestic banking industry will likely result in additional pressure for the bank's domestic operations, but the overall rating is supported by its status as a GRE. We have factored into the ratings our base-case assumption that HYPO NOE will not suffer credit losses from its guarantees to Pfandbriefbank (Österreich) AG (Pfandbriefbank), as a result of the latter's exposure to HETA Asset Resolution AG (HETA). Our forecasts for HYPO NOE are underpinned by the State of Lower Austria's commitment to cover HYPO NOE's potential cost under its guarantee to Pfandbriefbank with regard to HETA related losses. For HYPO NOE's €225 million direct HETA exposure, we incorporate in our forecast up to a maximum loss of 50%. The stable outlook reflects our expectation that Lower Austria will remain highly supportive of HYPO NOE and that the bank will preserve its strong capitalization over the next two years.

### Oberoesterreichische Landesbank AG (HYPO OÖ)

We lowered the long-term ICR on HYPO OÖ to 'A' from 'A+' to reflect our view that the increased risks in the domestic banking industry results in additional pressure for the bank's domestic operations. The stable outlook reflects our expectation that Upper Austria will remain highly supportive of HYPO OÖ and that the bank will preserve its strong capitalization over the next two years. Our outlook reflects our base-case expectation that Hypo OÖ will not suffer further credit losses from its guarantees to Pfandbriefbank, with regard to HETA-related losses.

### BICRA SCORE SNAPSHOT\*

Austria

	To	From
BICRA Group	3	2
Economic risk	2	2
Economic resilience	Very Low risk	Very Low risk
Economic imbalances	Low risk	Low risk

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Credit risk in the economy	Intermediate risk	Intermediate risk
Industry risk	4	3
Institutional framework	Intermediate risk	Intermediate risk
Competitive dynamics	High risk	Intermediate risk
Systemwide funding	Low risk	Low risk
Trends		
Economic risk trend	Stable	Stable
Industry risk trend	Stable	Negative

\*Banking Industry Country Risk Assessment (BICRA) economic risk and industry risk scores are on a scale from 1 (lowest risk) to 10 (highest risk). For more details on our BICRA scores on banking industries across the globe, please see "Banking Industry Country Risk Assessment Update," published monthly on RatingsDirect.

### RELATED CRITERIA AND RESEARCH

#### Related criteria

- Rating Government-Related Entities: Methodology And Assumptions, March 25, 2015
- Bank Rating Methodology And Assumptions: Additional Loss-Absorbing Capacity, April 27, 2015
- Bank Hybrid Capital And Nondeferrable Subordinated Debt Methodology And Assumptions, Jan. 29, 2015
- Group Rating Methodology, Nov. 19, 2013
- Assessing Bank Branch Creditworthiness, Oct. 14, 2013
- Criteria For Assigning 'CCC+', 'CCC', 'CCC-', And 'CC' Ratings, Oct. 1, 2012
- Revised Market Risk Charges For Banks In Our Risk-Adjusted Capital Framework, June 22, 2012
- Banks: Rating Methodology And Assumptions, Nov. 9, 2011
- Banking Industry Country Risk Assessment Methodology And Assumptions, Nov. 9, 2011
- Bank Capital Methodology And Assumptions, Dec. 6, 2010
- Use Of CreditWatch And Outlooks, Sept. 14, 2009

#### Related research

- S&P Takes Various Rating Actions On Certain U.K. And German Banks Following Government Support And ALAC Review, June 9, 2015
- Credit FAQ: How Standard & Poor's Applied Its Government Support And ALAC Criteria To U.K., German, Austrian, And Swiss Banks, June 9, 2015
- Watch Placements For Systemic Austrian, German, And U.K. Bank Operating Companies To Be Reviewed Around End May 2015, April 16, 2015
- S&P Takes Various Rating Actions On Certain U.K., German, Austrian, And Swiss Banks Following Government Support Review, Feb. 3, 2015
- The Rating Implications Of The Emerging Bank Resolution Frameworks In The U.K., Germany, Austria, And Switzerland, Feb. 3, 2015
- Austria, Germany, And The U.K. Are Set To Fast Track EU Bank Bail-In Rules, Sept. 29, 2014

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- How The Regulatory Reform Process Could Reshape Banks' Business Models And Affect Issuer Ratings, Aug. 18, 2014
- Standard & Poor's Takes Various Rating Actions On European Banks Following Government Support Review, April 29, 2014
- The Rating Impact Of Resolution Regimes For European Banks, April 29, 2014

RATINGS LIST

Ratings Downgraded; CreditWatch Action; Affirmed

	To	From
Erste Group Bank AG	BBB+/Negative/A-2	A-/Watch Neg/A-2
Ceska Sporitelna A.S.	A-/Negative/A-2	A-/Watch Neg/A-2
Raiffeisen Zentralbank Oesterreich AG	BBB+/Negative/A-2	A-/Watch Neg/A-2
Raiffeisen Bank International AG	BBB/Negative/A-2	A-/Watch Neg/A-2
UniCredit Bank Austria AG	BBB/Negative/A-2	BBB+/Watch Neg/A-2
Oberoesterreichische Landesbank AG	A/Stable/A-1	A+/Stable/A-1

Ratings Affirmed

HYPO NOE Gruppe Bank AG	A/Stable/A-1
KA Finanz AG	A-/Stable/A-2

NB. This list does not include all ratings affected.

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