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Research Update:

Ratings On Austria-Based KA Finanz Affirmed At 'A/A-1'; Outlook Remains Stable

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Overview

- We consider that Austria-Based KA Finanz AG is operating in a more favorable domestic environment.
- This is in line with our view that the trend for economic risk in Austria is now stable, due to the improving overall economic climate in Europe.
- We are consequently affirming our 'A/A-1' ratings on KA Finanz.
- The stable outlook reflects our view that the bank's ownership structure and its parent's strong commitment are unlikely to change in the foreseeable future.

Rating Action

On June 3, 2014, Standard & Poor's Ratings Services affirmed its 'A' long-term and 'A-1' short-term counterparty credit ratings on Austria-based KA Finanz AG. The outlook is stable.

Rationale

The affirmations follow the completion of our review of risks to Austria's banking industry and potential implications for KA Finanz. We have revised our view of the economic risk trend to stable from negative, according to our banking industry country risk assessment methodology (see "Ratings On Seven Austrian Banks Affirmed, With Various Outlooks, On Stabilizing Economic Risks," published June 3, 2014, on RatingsDirect). We believe that the improving economic environment in Europe, stabilization of house prices in Austria, and a further reduction of foreign currency lending to households will stabilize economic risks for Austrian banks over the next two years. Although we do not believe the fragile economic recovery will support a strong rebound in the banking sector, domestic risks have reduced materially, in our view. We expect that Austria's GDP growth will outpace that of most peers in the eurozone (European Economic and Monetary Union) over the coming years.

In our opinion, overcapacity in the Austrian banking sector, which results in low bank earnings through aggressive pricing, increasingly poses a risk to the stability of the banking system. We furthermore see risks to the banking sector stemming from the government's comparably high levy on banks. If this levy remains in place over the longer term, it will further diminish domestic banks' chances of improving their modest domestic earnings.

Our ratings on KA Finanz are based on its 'bbb+' anchor. We factor in our view

of the bank's "adequate" business position, "moderate" capital and earnings, "moderate" risk position, "average" funding, and "adequate" liquidity, as our criteria define these terms. The bank's stand-alone credit profile (SACP) therefore stands at 'bbb-'.

We regard KA Finanz as a government-related entity (GRE) under our criteria, with a "very high" likelihood of timely and sufficient extraordinary government support in the event of financial distress. We expect support to come from KA Finanz's 100% owner, the Republic of Austria. This is based on our view of KA Finanz's "very important" role for and "very strong" link with the Austrian government. The bank plays an important public policy role as the work-out entity of the former Kommunalkredit Austria. We expect KA Finanz's role for the government and its link to the government to remain unchanged, at least in the medium term.

Outlook

The stable outlook on KA Finanz reflects our view that the bank's ownership structure and its parent's strong commitment are unlikely to change in the foreseeable future. We think that Austria's ability and willingness to support KA Finanz in terms of funding, liquidity, and capital will remain unchanged over the next two years. However, we note that Austria has no legal obligation to support KA Finanz indefinitely.

We expect that KA Finanz will maintain its current financial profile determined by its "run-off" status. Deterioration would likely prompt us to take a negative rating action on the bank unless the government provided timely and sufficient support. Our assumption of government support is a key component of our ratings.

We would lower the ratings if the government did not deliver on its commitment to sustain the bank's regulatory Tier 1 capital ratio at more than 7%. Failure to sustain the ratio above this threshold would cause a deterioration of capital and lead us to reassess our view of the likelihood of government support. We would also lower the ratings if the bank proved unable to sustain its current funding and liquidity profile.

We could raise the ratings if the legal support framework for KA Finanz's outstanding unsecured debt were to strengthen. We don't anticipate that this will happen in the foreseeable future and consider a positive rating action unlikely.

Ratings Score Snapshot

Issuer Credit Rating	A/Stable/A-1
SACP	bbb-

Anchor	bbb+
Business Position	Adequate (0)
Capital and Earnings	Moderate (-1)
Risk Position	Moderate (-1)
Funding	Average (0)
Liquidity	Adequate
Support	+4
GRE Support	+4
Group Support	0
Sovereign Support	0
Additional Factors	0

Related Criteria And Research

Related Criteria

- 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
- Rating Government-Related Entities: Methodology And Assumptions, Dec. 9, 2010

Related Research

- Ratings On Seven Austrian Banks Affirmed, With Various Outlooks, On Stabilizing Economic Risks, June 3, 2014
- Standard & Poor's Takes Various Rating Actions On European Banks Following Government Support Review, April 29, 2014
- Credit FAQ: The Rating Impact Of Resolution Regimes For European Banks, April 29, 2014
- Banking Industry Country Risk Assessment Update: May 2014, May 13, 2014
- Austria (Republic of), April 25, 2014
- KA Finanz AG, June 28, 2013

Ratings List

Ratings Affirmed

KA Finanz AG

Counterparty Credit Rating	A/Stable/A-1
Certificate Of Deposit	A/A-1

KA Finanz AG

Senior Unsecured	A
Certificate Of Deposit	A-1
Commercial Paper*	A-1+
Commercial Paper	A-1

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