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## KA Finanz AG

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# KA Finanz AG

## Major Rating Factors

### Issuer Credit Rating

AA+/Stable/A-1+

Strengths:	Weaknesses:
<ul style="list-style-type: none"><li>• Almost certain likelihood of extraordinary government support from Austria, KA Finanz AG's sole owner.</li><li>• A direct €8.2 billion refinancing agreement with government-owned Abbaumanagementgesellschaft des Bundes (ABBAG), with €4.4 billion drawn as of June 30, 2019.</li><li>• Critical public policy role for the wind-down of the former Kommunalkredit Austria AG's nonstrategic assets.</li></ul>	<ul style="list-style-type: none"><li>• No internal capital generation capacity and, since December 2018, reliance on government support to offset negative equity from accelerated portfolio runoff measures.</li><li>• Reliance on the government to close any funding or liquidity gaps.</li><li>• No new business as a pure wind-down company.</li></ul>

### Outlook

S&P Global Ratings' stable outlook on KA Finanz reflects that on Austria. As a result, any rating action on Austria will prompt a similar rating action on KA Finanz.

Any weakening of KA Finanz's role for and link to Austria could cause us to take a negative rating action on the company. However, we currently do not anticipate any adverse changes. We believe that the almost certain likelihood of government support will remain unchanged over the next two years.

## Rationale

We equalize our ratings on KA Finanz with the ratings on its sole owner and support provider, Austria. The equalization reflects our opinion that there is an almost certain likelihood that the Austrian government would provide timely and sufficient extraordinary support to KA Finanz in the event of financial distress.

KA Finanz was set up following the restructuring of the troubled former Kommunalkredit Austria through a demerger that took place in 2009, with the aim of avoiding disturbance in the financial markets. As part of its restructuring, the

former Kommunalkredit Austria was split into two independent entities: Kommunalkredit Austria and KA Finanz. The European Commission approved the restructuring plan on March 31, 2011, with KA Finanz not being allowed to take on any new lending business. The new Kommunalkredit Austria was reprivatized in September 2015 via its sale to a private equity investor.

Since the lapse of its banking license on Sept. 6, 2017, KA Finanz has been operating as a nonbank wind-down entity according to section 162 of the Austrian Bank Recovery and Resolution Act. In its relations with KA Finanz, the Austrian government acts through a fully owned state company, ABBAG, which has replaced KA Finanz's market refinancing structure by providing a funding framework of up to €8.2 billion. The entity continues to be supervised by the Austrian Financial Market Authority.

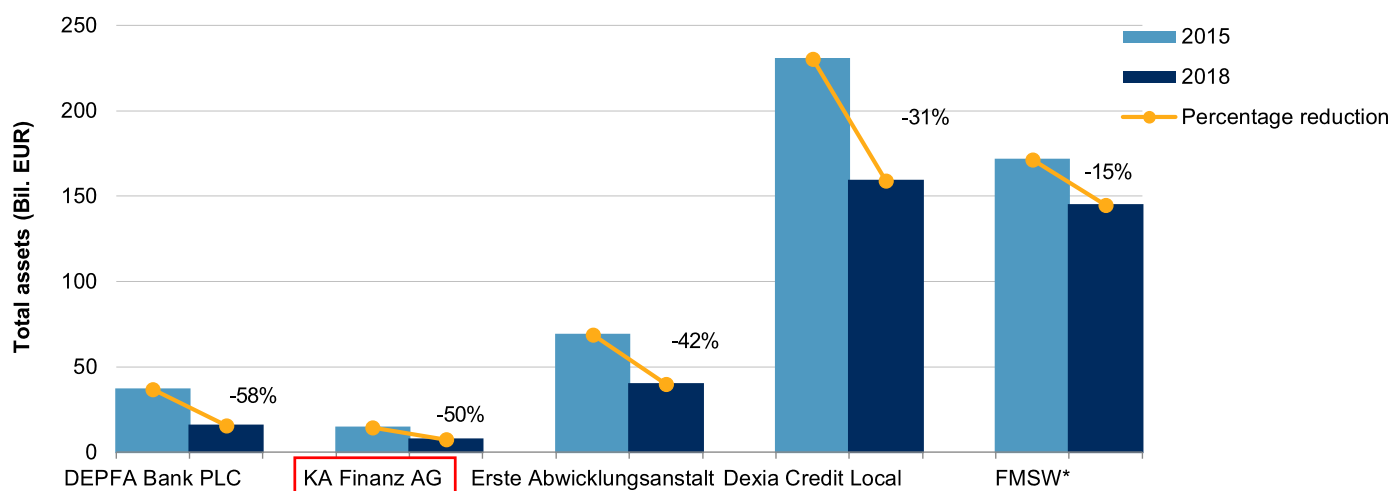
KA Finanz's nonbank status allows for an accelerated 10-year wind-down plan, since it is not subject to regulatory capital requirements and only has to comply with a reduced scope of the banking regulatory framework. Also, the institution no longer contributes to the Bank Resolution Fund, compared with €3.7 million paid for the last time in 2018.

We expect KA Finanz will continue to receive government support over the accelerated runoff term to compensate for losses that have already exceeded KA Finanz's equity base for the full-year 2018. Respectively, the €216.1 million reduction of the repayment obligation to ABBAG, recognized as extraordinary income, brought KA Finanz's equity level back to zero as of year-end 2018. We expect further obligation reductions will cover any negative equity for 2019 and the following years.

#### Chart 1

#### KA Finanz Wound Down Assets Quickly (2015 Versus 2018)

KA Finanz compared with runoff peers



\*Germany-based FMS Wertmanagement AöR. Source: S&P Global Ratings.

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As of December 2018, KA Finanz's gross exposure at default was mainly split between eurozone countries (67%)

including Austria(45%), the U.S. and Canada (19%), and the U.K. (6%), with other European countries, including in Central Europe, accounting for the rest. KA Finanz plans to continue proactively winding down its remaining exposure outside Austria, Germany, and Switzerland throughout 2019, as it has already reduced total balance sheet to €6.2 billion as of June 30, 2019 (versus €7.2 billion as of year-end 2018). The main measure of the balance sheet reduction remains asset sales, with €20.7 billion positions sold in total over the last 11.5 years, followed by accelerated redemptions amounting to €8.8 billion.

There were no nonperforming loans KA Finanz's portfolio as of June 30, 2019, and we expect the nonperforming loan ratio will remain negligible over the coming years, given that the pace of the accelerated wind-down prioritizes assets in riskier geographical regions.

The operating income remained negative for the full-year 2018, at €244 million loss. This results predominantly from the net valuation adjustments and realizations from the market values of the receivables or securities that are being wound down. We expect KA Finanz will post structural losses for the full-year 2019 and the years ahead.

As of June 30, 2019, KA Finanz's capital markets legacy funding amounted to €1.8 billion, including €0.6 billion in covered bonds and a government-guaranteed bond of €1.0 billion that is to mature in 2020. Outstanding funding from ABBAG amounted to €4.4 billion. The liquidity guarantee for the commercial paper program was terminated together with the program itself in January 2018. KA Finanz's outstanding covered bonds, loans, and private placements continue to be honored and redeemed at their full nominal value on the relevant due dates. We assume that about €120 million of subordinated debt and private placements maturing after the 10-year wind-down period will eventually be redeemed.

KA Finanz has only a very limited back-office structure. In May 2018, the institution approved a service agreement with a new general outsourcing contractor Ithuba Capital AG, which replaced Kommunalkredit in April 2019. Moreover, as a result of a project that ABBAG is pursuing aimed at generating possible operational synergies, KA Finanz signed a framework agreement with another government controlled wind-down entity, HETA Asset Resolution AG. The latter provides internal audit services or legal support, for example.

### **External support:**

We base our view of an almost certain likelihood that the Austrian government would provide timely and sufficient extraordinary support to KA Finanz in the event of financial difficulties on KA Finanz's:

- Critical role as a key government policy tool to stabilize the banking system and minimize potential long-term losses to taxpayers through the orderly wind-down of the noncore assets of the former Kommunalkredit Austria; and
- Integral link with the Austrian government, since we think the government not only fully owns KA Finanz but also supports the company's management, which should enable effective governance, monitoring, and control during the envisaged 10-year wind-down period.

We have no doubts regarding the Austrian government's propensity to support KA Finanz. We believe the government has sufficient financial resources to do so and, as such, we do not consider government support to be subject to transition risk.

We do not expect KA Finanz's ownership status or the state-support mechanism will weaken. We expect KA Finanz's public policy role as a wind-down entity will continue until this task is complete, since we believe an accelerated wind-down could not be easily undertaken by a private entity given its advanced and accelerated stage.

We expect Austria will remain supportive of KA Finanz and that the implemented EU Bank Recovery and Resolution Directive does not affect its willingness or ability to support KA Finanz as a wind-down entity, in our opinion.

### Additional rating factors:None

No additional factors affect the rating.

**Table 1**

<b>KA Finanz AG--Key Figures</b>					
	<b>--Year ended Dec. 31--</b>				
<b>(Mil. €)</b>	<b>2019*</b>	<b>2018</b>	<b>2017</b>	<b>2016</b>	<b>2015</b>
Adjusted assets	6,700.1	7,222.0	9,843.8	11,949.6	14,391.1
Customer loans (gross)	4,102.3	4,802.1	5,894.3	6,784.7	7,163.1
Adjusted common equity	(24.9)	0.0	29.1	453.0	481.0
Operating revenues	0.8	(1.0)	(22.4)	(42.8)	(46.6)
Noninterest expenses	14.4	23.7	34.9	22.5	21.5
Core earnings	(7.2)	(245.3)	(423.9)	(28.0)	(63.6)

\*Data as of June 30.

**Table 2**

<b>KA Finanz AG--Capital And Earnings</b>					
	<b>--Year ended Dec. 31--</b>				
<b>(%)</b>	<b>2019*</b>	<b>2018</b>	<b>2017</b>	<b>2016</b>	<b>2015</b>
Tier 1 capital ratio	N/A	N/A	N/A	17.2	15.3
Adjusted common equity/total adjusted capital	100.0	N.M.	100.0	100.0	100.0
Net interest income/operating revenues	477.9	(1,649.8)	(6.6)	9.2	43.0
Fee income/operating revenues	(1,059.3)	1,769.9	109.5	94.8	59.4
Market-sensitive income/operating revenues	(30.2)	(1.5)	0.2	(0.1)	(0.4)
Noninterest expenses/operating revenues	1,867.0	(2,342.8)	(155.7)	(52.5)	(46.1)
Preprovision operating income/average assets	(0.4)	(0.3)	(0.5)	(0.5)	(0.6)
Core earnings/average managed assets	(0.2)	(2.9)	(3.9)	(0.2)	(0.6)

\*Data as of June 30. N/A--Not applicable. N.M.--Not meaningful.

**Table 3**

<b>KA Finanz AG--Risk Position</b>					
	<b>--Year ended Dec. 31--</b>				
<b>(%)</b>	<b>2019*</b>	<b>2018</b>	<b>2017</b>	<b>2016</b>	<b>2015</b>
Growth in customer loans	(29.1)	(18.5)	(13.1)	(5.3)	218.4
Total managed assets/adjusted common equity (x)	(268.6)	N.M.	337.8	26.4	29.9
New loan loss provisions/average customer loans	(0.3)	4.1	5.7	(0.5)	(0.1)
Gross nonperforming assets/customer loans + other real estate owned	0.0	0.0	0.1	0.1	1.7

\*Data as of June 30. N.M.--Not meaningful.

**Table 4**

<b>KA Finanz AG--Funding And Liquidity</b>					
	<b>--Year-ended Dec. 31--</b>				
<b>(%)</b>	<b>2019*</b>	<b>2018</b>	<b>2017</b>	<b>2016</b>	<b>2015</b>
Core deposits/funding base	72.0	73.8	67.3	9.3	7.8
Customer loans (net)/customer deposits	88.1	93.4	92.8	653.9	681.9
Long-term funding ratio	90.8	91.5	86.0	33.4	35.3
Stable funding ratio	121.8	115.2	117.1	49.1	52.7
Short-term wholesale funding/funding base	9.1	8.5	14.0	69.3	67.1
Broad liquid assets/short-term wholesale funding (x)	3.1	2.8	2.0	0.5	0.6
Net broad liquid assets/short-term customer deposits	2,384.0	1,808.9	254.3	(380.7)	(421.7)
Short-term wholesale funding/total wholesale funding	32.5	32.5	42.8	76.4	72.7

\*Data as of June 30.

## Related Criteria

- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- General Criteria: Guarantee Criteria, Oct. 21, 2016
- General Criteria: Rating Government-Related Entities: Methodology And Assumptions, March 25, 2015
- Criteria - Financial Institutions - Banks: Banks: Rating Methodology And Assumptions, Nov. 9, 2011
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009

## Related Research

- Summary: Austria, Sept. 13, 2019
- Austria-Based KA Finanz Upgraded To 'AA+/A-1+' On Almost Certain Likelihood Of Government Support; Outlook Stable, Sept. 11, 2017

### Ratings Detail (As Of October 29, 2019)\*

#### KA Finanz AG

Issuer Credit Rating AA+/Stable/A-1+

Senior Secured AA+/Stable

#### Issuer Credit Ratings History

11-Sep-2017 AA+/Stable/A-1+

27-Apr-2017 A-/Watch Pos/A-2

13-Mar-2015 A-/Stable/A-2

#### Sovereign Rating

Austria AA+/Stable/A-1+

\*Unless otherwise noted, all ratings in this report are global scale ratings. S&P Global Ratings' credit ratings on the global scale are comparable across countries. S&P Global Ratings' credit ratings on a national scale are relative to obligors or obligations within that specific country. Issue and debt ratings could include debt guaranteed by another entity, and rated debt that an entity guarantees.



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