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## Research Update:

# Austrian Bank KA Finanz Affirmed At 'A/A-1'; Off Watch; Outlook Stable

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## Research Update:

# Austrian Bank KA Finanz Affirmed At 'A/A-1'; Off Watch; Outlook Stable

## Overview

- Austria has recently enacted legislation to bail in holders of Hypo Group Alpe Adria's subordinated debt, despite Carinthia's grandfathered guarantee of this debt.
- In our view, the new law indicates reduced predictability of extraordinary government support for systemically important banks, and for banks' hybrid capital instruments and grandfathered debt, than we previously envisaged.
- However, we still see a very high likelihood of extraordinary government support for government-related entity KA Finanz AG.
- We are therefore affirming our ratings on KA Finanz at 'A/A-1' and removing them from CreditWatch negative.
- The stable outlook reflects our expectation that the probability of state support for KA Finanz will remain very high.

## Rating Action

On Aug. 13, 2014, Standard & Poor's Ratings Services affirmed its 'A/A-1' long- and short-term counterparty credit ratings on Austria-based KA Finanz AG. The outlook is stable.

We removed the ratings from CreditWatch with negative implications, where we had placed them on June 10, 2014.

## Rationale

The ratings reflect our view that the likelihood of KA Finanz receiving timely and sufficient extraordinary support from its owner, the Austrian government, remains very high, despite less predictable government support for systemically important banks in Austria.

The affirmation follows the Austrian government's enactment of special legislation to bail in Hypo Group Alpe Adria's (HGAA's) subordinated debtholders, despite a grandfathered guarantee from the State of Carinthia for the debt. The legislation, passed in July, forms part of the law to transform HGAA into a wind-down unit from a bank, and it has been ratified by Austria's federal president. The Austrian government's decision to impose losses on HGAA's subordinated debtholders, despite the grandfathered guarantee, and public statements from government officials, in our view, indicate that the authorities' stance toward supporting systemically important banks is

wavering. We consider, therefore, that extraordinary government support for a systemically important bank, or from the federal states for a bank's grandfathered instruments, is now less predictable than before.

Generally, however, we consider that in the absence of a legal framework for bank resolution in Austria, extraordinary future government support could remain available. Consequently, we continue to classify the Austrian government as supportive of the banking sector.

We understand that, in the coming months, the Austrian constitutional court will examine whether the new legislation complies with national and European statutes. There will therefore be a period of uncertainty for market participants until the court makes its ruling.

We regard KA Finanz as a government-related entity (GRE), under our criteria, with a very high likelihood of receiving timely and sufficient extraordinary support from the Austrian government in the event of financial difficulties. We expect the likelihood of state support to KA Finanz to remain unchanged over the medium term, even though we consider extraordinary government support for systemically important banks in Austria to be less predictable than before.

In accordance with our criteria for GREs, our view of a very high likelihood of timely and sufficient extraordinary government support is based on our assessment of KA Finanz's:

- Very important role for the Austrian government. KA Finanz's default could destabilize the Austrian banking system and tarnish Austria's reputation. In addition, the bank is meeting a key political objective; and
- Very strong link with the government. The bank plays an important public policy role as the work-out entity of the former Kommunalkredit Austria. The government has displayed a track record of support for KA Finanz and has stated its commitment to supporting the bank in the future.

## **Outlook**

The stable outlook reflects our view that KA Finanz's ownership structure and Austria's strong commitment are unlikely to change in the medium term. We think that Austria will continue to support its GRE, KA Finanz, in terms of funding, liquidity, and capital. However, we note that Austria has no legal obligation to support KA Finanz indefinitely. We currently believe resolution frameworks are unlikely to impede the states' willingness to provide extraordinary support to banks that we view as GREs.

We expect that KA Finanz will maintain its current financial profile determined by its run-off status. Deterioration of the bank's stand-alone financial profile would likely trigger a negative rating action on the bank unless the government provided timely support. As such, our expectation of government support to KA Finanz 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%. Its failure to sustain the ratio above this threshold would indicate a deterioration of capital and lead us to reassess our view of the likelihood of state support. We would also lower the ratings if the bank proved unable to sustain its current funding and liquidity profile.

We consider a positive rating action to be unlikely. We could raise the ratings if the legal support framework for KA Finanz's outstanding unsecured debt strengthened.

## Ratings Score Snapshot

	To	From
Counterparty Credit Rating	A/Stable/A-1	A/Watch Neg/A-1
SACP	bbb-	bbb-
Anchor	bbb+	bbb+
Business Position	Adequate (0)	Adequate (0)
Capital and Earnings	Moderate (-1)	Moderate (-1)
Risk Position	Moderate (-1)	Moderate (-1)
Funding and Liquidity	Average and Adequate (0)	Average and Adequate (0)
Support	+4	+4
GRE Support	+4	+4
Group Support	0	0
Sovereign Support	0	0
Additional Factors	0	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
- Use Of CreditWatch And Outlooks, Sept. 14, 2009

### Related Research

- Various Rating Actions Taken On Six Austrian Banks On Legislation To Bail In State-Guaranteed Debt, Aug. 13, 2014
- Seven Austrian Banks Placed On CreditWatch Negative On Planned Bail-In Of State-Guaranteed Debt Of Hypo Group Alpe Adria, June 10, 2014
- Austrian Bank KA Finanz 'A/A-1' Ratings On CreditWatch Negative On Risks

Of Diminishing State Support, June 10, 2014

- Banking Industry Country Risk Assessment: Austria, 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
- Austria (Republic of), April 25, 2014
- Austria Ratings Affirmed At 'AA+/A-1+' On Continuing Fiscal Consolidation And Resilient Economy; Outlook Stable, March 28, 2014

## Ratings List

Ratings Affirmed; CreditWatch/Outlook Action

	To	From
KA Finanz AG		
Counterparty Credit Rating	A/Stable/A-1	A/Watch Neg/A-1
Senior Unsecured	A	A/Watch Neg
Certificate Of Deposit	A/A-1	A/Watch Neg/A-1
Commercial Paper	A-1	A-1/Watch Neg

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