

Rating Action: Moody's upgrades BAWAG's ratings to A2; outlook positive

Global Credit Research - 20 Apr 2017

Baseline credit assessment upgraded to baa1 from baa2

Frankfurt am Main, April 20, 2017 -- Moody's Investors Service has today upgraded BAWAG P.S.K.'s (BAWAG) long-term senior unsecured debt, issuer and deposit ratings by one notch to A2 from A3; the outlook on these long-term ratings remains positive. Concurrently, Moody's upgraded BAWAG's subordinated debt ratings to Baa2 from Baa3 as well as the bank's short-term issuer and deposit ratings to P-1 from P-2.

The rating agency further upgraded the bank's baseline credit assessment (BCA) and adjusted BCA by one notch to baa1 from baa2, as well as the bank's long-term Counterparty Risk Assessment to A1(cr) from A2(cr), and affirmed the bank's short-term CR Assessment at P-1(cr).

The rating upgrade reflects the continued strengthening of the bank's financial fundamentals, in particular the improvement of its capitalisation and asset quality, as well as its sustained strong profitability. The positive outlook reflects Moody's expectation that BAWAG will be able to sustain current solvency and liquidity ratios going forward while developing a more stable loan book composition track record.

A full list of affected ratings can be found at the end of this press release.

RATINGS RATIONALE

-- UPGRADE OF THE BCA

The upgrade of the BCA to baa1 from baa2 reflects BAWAG's sustained high profitability levels above the Austrian industry average, which was underscored by a reported net profit of €484 million in 2016 and the continued build-up of the bank's capital adequacy ratios (fully-loaded common equity Tier 1 ratio of 15.1% as of year-end 2016, up more than 200 basis points year-over-year) that compare favorably to similarly-rated peers across Europe. In assessing the bank's capital strength, Moody's has also considered some potential dilution of the capital ratios reflecting the expectation that capital buffers will be partly used to expand the bank's domestic and international presence at least within the bank's declared capital targets of a sustained 12% fully-loaded CET1 ratio.

The baa1 BCA also takes into account that Moody's expects BAWAG's future net income growth to be constrained by the industry-wide interest margin pressures driven by the low interest rate environment and an intense competitive landscape in many banking business areas in the Austrian and German target markets of BAWAG. In addition, the currently still beneficial effects of the booking and usage of tax loss carry-forwards will gradually diminish for BAWAG and result in higher effective tax rates and therefore lower capital retention capabilities over the medium-term.

-- UPGRADE OF LONG-TERM RATINGS TO A2

The one-notch upgrade of BAWAG's long-term deposit, issuer and senior unsecured debt ratings to A2 incorporates: (1) the one-notch upgrade of the bank's BCA to baa1 from baa2; (2) the result of Moody's Advanced Loss Given Failure (LGF) analysis, which takes into account the severity of loss faced by the different liability classes in resolution and which continues to provide two notches of rating uplift to BAWAG's long-term ratings; and (3) a low likelihood of BAWAG receiving government support, resulting in no additional rating uplift.

BAWAG's A2 long-term senior unsecured debt, issuer and deposit ratings reflect the likely reduction in expected loss resulting from the substantial volume of wholesale deposits and senior unsecured debt at failure, leading to a two-notch rating uplift from the bank's baa1 adjusted BCA.

Moody's LGF analysis further indicates a high loss-given-failure for subordinated debt classes, leading to a rating positioning one notch below the adjusted BCA, at Baa2.

-- POSITIVE OUTLOOK ON BAWAG'S LONG-TERM RATINGS

The positive outlook on the long-term senior unsecured debt, issuer and deposit ratings of BAWAG incorporates Moody's expectation that BAWAG's BCA may be further upgraded over the 12-18 months outlook horizon depending on: (1) the compatibility of the bank's capital employment choices with the maintenance of a strong capitalisation level; and (2) the bank's continued progress in profitably strengthening its presence as a retail bank foremost in Austria and Germany, supplemented with measured and low-risk loan portfolio investments.

-- WHAT COULD MOVE THE RATINGS UP/DOWN

Upward pressure on BAWAG's BCA and long-term ratings could result from: (1) sustaining the achieved solvency, in particular because of the improvement in retained earnings; (2) continued strong risk control and sound risk metrics in relation to BAWAG's portfolio acquisition-driven diversification and international expansion strategy; and (3) the absence of unduly aggressive or transformative M&A activity over the outlook horizon of 12-18 months.

BAWAG's ratings could be downgraded if the bank's financial strength significantly deteriorates following: (1) large acquisitive activities that would significantly reduce BAWAG's capital ratios and result in material execution risks; and/or (2) currently unexpected losses from acquired international portfolios driving up significantly the risk costs of BAWAG.

A downgrade of the long-term issuer and senior unsecured debt ratings could develop if BAWAG's volume of debt instruments decreases relative to the bank's tangible banking assets, which could result in fewer notches of rating uplift resulting from our LGF analysis.

LIST OF AFFECTED RATINGS

Issuer: BAWAG P.S.K.

Upgrades:

-LT Issuer Rating (Local & Foreign Currency), Upgraded to A2 from A3, Outlook Remains Positive
-ST Issuer Rating (Local & Foreign Currency), Upgraded to P-1 from P-2
-LT Bank Deposits (Local & Foreign Currency), Upgraded to A2 from A3, Outlook Remains Positive
-ST Bank Deposits (Local & Foreign Currency), Upgraded to P-1 from P-2
-Senior Unsecured Regular Bond/Debenture, Upgraded to A2 from A3, Outlook Remains Positive
-Subordinate, Upgraded to Baa2 from Baa3
-Senior Unsecured MTN, Upgraded to (P)A2 from (P)A3
-Subordinate MTN, Upgraded to (P)Baa2 from (P)Baa3
-Adjusted Baseline Credit Assessment, Upgraded to baa1 from baa2
-Baseline Credit Assessment, Upgraded to baa1 from baa2
-LT Counterparty Risk Assessment, Upgraded to A1(cr) from A2(cr)

Affirmations:

-ST Counterparty Risk Assessment, Affirmed P-1(cr)

Outlook Actions:

-Outlook, Remains Positive

PRINCIPAL METHODOLOGY

The principal methodology used in these ratings was Banks published in January 2016. Please see the Rating Methodologies page on www.moodys.com for a copy of this methodology.

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