

**Rating Action: Moody's affirms BAWAG P.S.K.'s Baa2 ratings; outlook changed to positive**

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Global Credit Research - 16 Apr 2014

**Standalone bank financial strength rating raised to D+/ba1; outlook stable**

Frankfurt am Main, April 16, 2014 -- Moody's Investors Service has today affirmed Bank fuer Arbeit und Wirtschaft und Oesterreichische Postsparkasse AG's (BAWAG P.S.K.) Baa2 long-term debt and deposit ratings, reflecting the rating agency's assessment of a continued high probability of government (systemic) support for BAWAG P.S.K. in the event of need from the Republic of Austria (Aaa stable).

Concurrently, the rating agency raised the bank's standalone bank financial strength rating (BFSR) to D+ with a stable outlook, equivalent to a baseline credit assessment (BCA) of ba1, from D/ba2. The higher BFSR reflects (1) the continued de-risking of BAWAG P.S.K.'s balance sheet; (2) the bank's significantly strengthened capital adequacy ratios; and (3) BAWAG P.S.K.'s recovery in profitability.

The long-term debt and deposit ratings carry a positive outlook, indicating the potential for a further improvement of the bank's standalone credit strength, which could result in a remapping of the BCA to the upper end of the D+ BFSR category.

The bank's Prime-2 short-term ratings have also been affirmed.

Furthermore, Moody's upgraded BAWAG P.S.K.'s subordinated debt ratings to Ba2 with a positive outlook and upgraded the bank's hybrid ratings to B1(hyb) with a positive outlook.

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

**RATINGS RATIONALE**

**-- AFFIRMATION OF LONG-TERM RATINGS WITH A POSITIVE OUTLOOK**

The affirmation of BAWAG P.S.K.'s long-term debt and deposit ratings reflects the rating agency's assessment of a continued high probability of systemic support for BAWAG P.S.K. in the event of need. This reflects the bank's sizeable national deposit market share and its importance to the country's payment system.

Following the full payback of participation capital to the Republic of Austria in March 2014 and the raising of the bank's BCA by one notch to ba1, BAWAG P.S.K.'s long-term ratings now benefit from a two-notch uplift from the bank's BCA to Baa2 versus three previously, which still included one notch of extraordinary uplift during the period when BAWAG benefitted from government participation capital.

The positive outlook on BAWAG P.S.K.'s long-term ratings reflects the potential for a further strengthening of the bank's standalone credit profile over time which could result in a remapping of the BCA to the upper end of the D+ BFSR category. If Moody's support assumptions remain unchanged, a higher BCA could exert upward pressure on the bank's long-term debt and deposit ratings over time.

**-- RAISING OF THE BFSR**

The rating agency says that the raising of BAWAG P.S.K.'s BFSR/BCA to D+/ba1 reflects:

(1) the continued de-risking of BAWAG P.S.K.'s balance sheet, as evidenced by the full sale of its previously large structured credit securities book as well as non-performing loan sales during 2013;

(2) the bank's significantly strengthened capital adequacy ratios (fully-loaded common equity Tier 1 ratio reported at 9.4% as of year-end 2013) accompanied by the full payback of EUR550 million of participation capital held by the Republic of Austria during March 2014; and

(3) BAWAG P.S.K.'s recovery in profitability, displaying a reported net profit of EUR229 million as of 31 December 2013 following several years in which write-offs, impairments and restructuring charges subdued the bank's

earnings.

The BFSR remains constrained by (1) Moody's cautious assessment of the bank's increased exposures to peripheral euro-area and higher-rated structured credit assets that replaced higher-risk legacy investments in the bank's structured credit book; and (2) uncertainties arising from the expansion of BAWAG P.S.K.'s international corporate and commercial real-estate (CRE) portfolios. The expansion in these portfolios could exert undue pressure on the bank's profitability and, potentially, capital ratios in a highly adverse scenario.

The rating agency believes that there is potential for a further strengthening of BAWAG P.S.K.'s standalone credit profile and therefore a re-mapping of the bank's BCA to the upper end of the D+ BFSR category. However, this would be contingent on the bank continuing to (1) carefully execute on its re-sizing and de-risking strategy while minimising potential negative effects on its profitability; (2) build a sizeable high-quality capital buffer over and above the regulatory minimum as determined by the Basel III capital regime; and (3) further improve the quality and quantity of recurring earnings from core businesses and sustain this structural improvement in retained earnings. The latter would foster sound internal capital generation and thus loss-absorption capacity.

Furthermore, Moody's will assess business risks potentially resulting from an unfavourable court ruling or settlement agreement (City of Linz case) that -- albeit considered manageable -- may delay the further build-up of high-quality capital elements.

#### -- UPGRADE OF THE BANK'S SUBORDINATED AND HYBRID DEBT RATINGS

The upgrade of the bank's subordinated debt ratings to Ba3 from Ba2 as well as the upgrade of the bank's hybrid ratings to B1(hyb) from B2(hyb) follows the raising of the bank's BCA, as these instruments are notched off the bank's adjusted BCA.

#### -- WHAT COULD MOVE THE RATINGS UP/DOWN

Upward pressure on BAWAG P.S.K.'s standalone BFSR and long-term ratings could result from (1) a faster and more pronounced than anticipated implementation of the bank's strategy to focus on its core Austrian market and better exploitation of its retail footprint; (2) markedly stronger performance in client-facing businesses; and (3) strong and further improving financial fundamentals coupled with a sustainable de-risking of its business profile.

Downward pressure could be exerted on the bank's BFSR if (1) the bank's financial strength or franchise strength were to deteriorate; (2) the expansion of the domestic branch network does not lead to a meaningful improvement in underlying revenues and earnings; (3) the bank's risk profile does not improve or even weakens; and (4) BAWAG P.S.K. is unable to continue building a high-quality capital buffer in-line with upcoming stricter capital requirements under the Basel III regime and/or as set by the Austrian regulator.

BAWAG P.S.K.'s long-term ratings could be downgraded if Moody's were to lower its assessment of the high probability of systemic support factored into the bank's long-term ratings.

#### LIST OF AFFECTED RATINGS

BAWAG P.S.K.:

The following ratings were upgraded with a stable outlook:

- BFSR to D+ from D

The following ratings were upgraded with a positive outlook:

- Subordinated debt ratings to Ba2 from Ba3
- Hybrid ratings of BAWAG Capital Finance (Jersey) I and II Limited to B1(hyb) from B2(hyb)

The following ratings were affirmed with a positive outlook:

- Long-term bank debt and deposit ratings (local and foreign currency) at Baa2

The following ratings were affirmed:

- Short-term bank deposit ratings (local and foreign currency) at Prime-2

## PRINCIPAL METHODOLOGY

The principal methodology used in these ratings was Global Banks published in May 2013. Please see the Credit Policy page on [www.moody's.com](http://www.moody's.com) for a copy of this methodology.

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