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DBRS Assigns BBB (low) Senior Ratings to Kommunalkredit Austria AG, Stable Trend

Industry: Fin.Svc.--Banks & Trusts

DBRS has today assigned first-time ratings to Kommunalkredit Austria AG (KA or the Bank). These include a Long Term Debt and Deposit Rating of BBB (low) and a Short Term Debt and Deposit Rating of R-2 (mid). The Trend on both ratings is Stable. Underpinning these ratings, DBRS has assigned an Intrinsic Assessment (IA) of BBB (low) and a Support Assessment (SA) of SA-3. This follows the establishment of KA as of 26 September 2015, and confirmation of the Bank's financial position at initiation.

The BBB (low) rating reflects the quality, profitability and self-funding dynamic of the legacy portfolio demerged into KA in the course of the partial sale process of the former Kommunalkredit. This portfolio will allow the new Bank some cushion in terms of time, capital and earnings in order to fully establish KA's planned business model. However the rating also takes into account the challenges faced by the Bank, including its narrow business model, lack of track record, and dependence on wholesale funding.

Once the business platform is fully-established over the medium term, there could be scope for rating improvement if the Bank is able to meet the targets it has set for profitability, credit quality, liquidity and capitalisation. However, near term upside for the ratings is limited. Any deterioration or variance from targeted levels of new business, profitability, capital and/or expected leverage, or the quality of assets or earnings from the legacy portfolio, would contribute towards negative rating pressure. These incorporate DBRS' expectation that, if necessary to maintain capital levels, planned dividends will not be distributed.

DBRS notes the Bank inherits a well-recognised banking platform and that the new entity will benefit from important project finance relationships established by its predecessor Kommunalkredit, in Austria, and to a lesser extent, more widely in Europe. KA is controlled by Private Equity investors Interritus Limited and Attestor Capital LLP. The new bank benefits from a good quality, fully-funded loan portfolio which generates carry income which in part will fund the future business model. Focusing on recognised areas of expertise inherited from Kommunalkredit, such as energy & environment, social infrastructure and transport, KA will generate new business based on project cash flows and plans to sell the major portion of future risk to market investors.

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DBRS views the new business model positively as the emphasis is on capital-light generation of project risks which will then be largely targeted for sale. Market dynamics have led to a perceived deficit of project finance supply, which combined with insurance and pension investor interest for quality assets, are likely to support the planned business model. Nonetheless, KA will need to establish the Bank's new business generation following several years of European Commission imposed moratoriums. The Bank's ability to leverage its ongoing project finance consulting, management and advisory roles will be central for success, as will its ability to build on relationships with investors to establish ongoing distribution capability.

New business is expected to grow slowly but is then planned to increase at a faster rate from 2017, once the new model is fully established. These earnings are planned to offset the expected decline in cash flow from the legacy portfolio as these assets mature. The planned improvement in earnings is expected to fund a future dividend stream. DBRS expects that these dividends are non-binding and that foregoing payment could provide a further cushion for establishing the Bank's strategy, if required.

KA targets a 13% common equity tier 1 (CET1) ratio over the long-term which DBRS understands should correspond to an improved leverage ratio approaching double digits by 2025. At inception the Bank had a CET1 ratio of 19% and a leverage ratio of 3.8%, reflecting the retroactive establishment of the Bank under Austrian HGB (GAAP) accountancy rules, to January 1, 2015. The initial capital ratio reflects the good quality of the Bank's legacy portfolio which is mostly exposed to Austrian municipalities which enjoy low risk weightings. Although the ratios are solid, DBRS notes that RWAs amount to only 20% of assets. As a result the absolute levels of CET1 (EUR 170 million under Austrian HGB (GAAP)) are relatively low.

Notes:

All figures are in EUR unless otherwise noted.

The principal applicable methodology is the Global Methodology for Rating Banks and Banking Organisations (June 2015). Other applicable methodologies include the DBRS Criteria: Support Assessments for Banks and Banking Organisations (March 2015) and DBRS Criteria: Rating Bank Capital Securities – Subordinated, Hybrid, Preferred & Contingent Capital Securities (February 2015). These can be found can be found at: <http://www.dbrs.com/about/methodologies>

DBRS considers the information available to it for the purposes of providing this rating was of

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satisfactory quality.

This rating concerns a newly issued financial instrument.

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Issuer	Debt Rated	Rating Action	Rating	Trend	Latest Event
Kommunalkredit Austria New AG	Long Term Debt and Deposit	New Rating	BBB (low)	Stb	Sep 30, 2015
Kommunalkredit Austria New AG	Short-Term Debt and Deposit	New Rating	R-2 (middle)	Stb	Sep 30, 2015

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