

# Kommunalkredit Austria AG

## Update

### Key Rating Drivers

**Business Model Constrains Ratings:** Kommunalkredit Austria AG's (KA) Viability Rating (VR) reflects its established niche franchise in infrastructure and energy (I&E) finance, experienced management team, improving profitability and strong asset quality record. It is underpinned by a robust risk-management framework and adequate funding and liquidity. The bank's Viability Rating (VR) is constrained by Fitch Ratings' assessment of its business profile given its small equity base relative to concentration risks in its I&E portfolio.

**Well-Executed Business:** The bank's concentrated but robust business model focuses on its niche franchise in European I&E financing and on municipal finance (mainly in Austria). KA's highly experienced management team has a successful, but short, record in operating these businesses, keeping above-average returns while maintaining strong asset-quality metrics. We believe that the expected change in KA's ownership – agreed in February and likely to be closed in 1H24 – will not result in a fundamental change of its strategy.

**Uneven Risk Profile:** Our assessment of the bank's risk profile incorporates its appetite for sub-investment-grade-rated, opportunistic infrastructure and project-finance transactions and declining low-risk municipal financing as a share of its total loans. KA's underwriting standards and risk-control framework have so far mitigated inherent project risks in infrastructure assets, as demonstrated by an impaired loan ratio close to 0% since end-2015.

**Strong Asset-Quality Metrics:** KA's asset quality benefits from its low-risk public-sector portfolio. The bank has not reported any substantial impaired loans, despite higher-risk exposures in its I&E segment. However, given its concentrated loan book, single NPLs could sharply inflate its impaired loans ratio as its infrastructure loan book seasons. This is, however, mitigated by above-average historical recovery rates in the I&E segment and low correlation between the financed asset classes.

**Above-Average Profitability:** KA's profitability is a rating strength – and is rising – due to the expansion of its new business volume in combination with limited credit losses and a competitive cost base. Our assessment also reflects concentration of revenue in the I&E segment. We believe KA can maintain healthy profitability above peers' in 2023 and 2024, but the bank's concentrated credit exposures mean that loan losses on a small number of counterparties would affect earnings materially.

**Small Capital Base:** KA maintains capital ratios with adequate buffers over its minimum capital requirements, and the bank has a targeted capital increase of EUR100 million from its new owner. Despite the planned injection and internal capital generation, the size of its equity base is still small relative to the concentration and business risks inherent in its I&E portfolio.

**Stable Funding and Sound Liquidity:** The bank's funding profile is stable, which we expect to remain intact as rates rise given KA's recourse to retail and wholesale deposits. This is supplemented by KA's capital-market activities, including covered bond and senior debt issuance. KA's liquidity is sound, prudently managed, and underpinned by the bank's solid liquidity buffers.

### Ratings

<b>Foreign Currency</b>	
Long-Term IDR	BBB-
Short-Term IDR	F3
Viability Rating	bbb-
Government Support Rating	ns

### Sovereign Risk (Austria)

Long-Term Foreign-Currency IDR	AA+
Long-Term Local-Currency IDR	AA+
Country Ceiling	AAA

### Outlooks

Long-Term Foreign-Currency IDR	Stable
Sovereign Long-Term Foreign-Currency IDR	Stable
Sovereign Long-Term Local-Currency IDR	Stable

### Applicable Criteria

[Bank Rating Criteria \(September 2023\)](#)

### Related Research

[Fitch Affirms Kommunalkredit Austria at 'BBB-'; Outlook Stable \(February 2023\)](#)

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## Rating Sensitivities

### Factors that Could, Individually or Collectively, Lead to Negative Rating Action/Downgrade

We could downgrade the ratings if the bank incurs multiple sizeable defaults in its project-finance portfolio, leading to weaker capitalisation, or if it relaxes its limits and underwriting standards to enable further opportunistic lending to higher-risk projects, more aggressive project-financing structures or junior financing.

We could also downgrade the ratings if aggressive risk-weighted assets (RWAs) growth without matching capital increases results in an increasing use of KA's large exposure limit. A downgrade could also result from significant deterioration in the bank's ability to syndicate its lending commitments to a sizeable pool of external investors.

### Factors that Could, Individually or Collectively, Lead to Positive Rating Action/Upgrade

An upgrade of the IDR and the VR would require a materially larger and more diversified franchise and a major reduction in single-name concentration, in combination with further and material strengthening of its capital base, beyond the planned capital injection from its owners .

## Other Debt and Issuer Ratings

Rating level	Rating
Senior preferred: Long term	BBB-

Source: Fitch Ratings

KA's 'F3' Short-Term IDR is the only option mapping to a 'BBB-' Long-Term IDR.

KA's long-term senior preferred (SP) debt rating is aligned with the bank's Long-Term IDR. This reflects Fitch's expectation that KA will not be subject to a minimum requirement for own funds and eligible liabilities, and that the bank will not build and maintain buffers of junior and senior non-preferred debt sustainably in excess of 10% of its RWAs.

## Significant Changes from Last Review

### Ownership Change Not Yet Approved

In February 2023, Altor Equity Partners, a long-term-oriented Nordic financial investor with EUR11 billion assets under management, announced its intention to acquire an 80% stake in KA. The current owners, private investor firm Interritus Limited, and Trinity Investments Designated Activity Company, will remain shareholders of KA, with each holding a 9.9% stake. The remaining 0.2% share is held by the Austrian Association of Municipalities.

The closing of the transaction is still pending as necessary regulatory approvals have not yet been granted. This is now expected at latest in 1H24. We perceive no negative impact for KA's business from this delay as Altor's strategic commitment remains unchanged, including a targeted EUR100 million capital increase. Altor could also supplement KA's services, for example by extending the footprint of KA's infrastructure debt funds to Nordic investors.

### Solid Business Performance in 1H23 Despite Challenges

KA continued its growth strategy in 1H23, benefitting from the resilience of the I&E markets despite economic and geopolitical difficulties. However, higher interest rates are increasing the refinancing risks of related projects and therefore could negatively affect future volume growth in these markets. We believe KA is well positioned to participate on the decarbonisation and energy transmission in Europe based on its sound expertise and agile business approach also in the years ahead.

### Stronger Margins Drive Profitability

KA's total operating income improved significantly at end 1H23, driven by a 52% yoy rise in net interest income (NII), to EUR81.8 million, based on higher volumes and better-than-expected margins. Net fee and commission income comprising placement and origination fees, servicing and asset management fees through the Fidelio debt platform and advisory fees from its consulting business Kommunalkredit Public Consulting (KPC) increased 18% yoy to EUR14.5 million. KA's overall cost base remained competitive, with a reported IFRS cost/income ratio of 41% (bank stand-alone) despite a 27 % yoy increase in administrative expenses, well above that of most peers. Ongoing investments in staff and IT serve to support the bank's capacity growth and strategic expansion in the long-term. KA's annualised operating profit/RWAs ratio (1H23: 3.9%) is well above our expectations and significantly outperforms that of peers. We expect KA's operating profitability to moderate due to increasing funding costs over the next two years, but to remain well above 2%.

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### **Strong Asset Quality Maintained**

KA's asset quality is supported by low default and high recovery rates in the I&E segment, and a gradual reduction in its concentration risks. Following seven years of full performance, an Export Credit Agency-covered international public finance counterparty defaulted on an obligation (with an exposure of EUR12.5 million) as of end-1H23. However, accounting for the Export Credit Agency collateral, the net non-performing exposure is immaterial. We expect KA's risk cost to remain well below 10 bp in 2023 but borrowers' higher refinancing costs could put moderate pressure on KA's asset quality.

### **Further Strengthening of Capitalisation Planned**

KA's common equity Tier 1 ratio (end-1H23: 15.2%, on a solo basis) comfortably exceeded its minimum regulatory requirements and remained above its targeted level of 15%. We expect KA to make use of counterbalancing measures in case the ratio drops below that level, such as profit retention to compensate for RWA consumption until the planned capital increase of EUR100 million is injected. KA has additionally available authorised capital at its discretion, which it could also use to strengthen its capital in the meantime.

### **Focus on Deposit Funding**

KA's funding activities in 1H23 shifted from capital market funding to customer deposits (both retail and institutional) with a focus on term-deposit extension. The increase of EUR220 million in deposits in 1H23 adds to the bank's diversification and further improved KA's loans-to-deposits ratio, but, at the same time, its reliance on online deposits means that its funding costs are increasing. Deposits made up 55% of the bank's funding structure at end-1H23. Capital market activities were moderate, and largely referred to the issuance of senior preferred private placements.

KA has a liquid balance sheet with a solid liquidity position of EUR908 million (18% of its balance sheet). The bank held cash, cash equivalents and balances with central banks of EUR401 million and a free liquidity reserve consisting of high-quality liquid securities of EUR507 million.

Ratings Navigator

Kommunalkredit Austria AG



Banks  
Ratings Navigator

	Operating Environment	Business Profile	Risk Profile	Financial Profile			Implied Viability Rating	Viability Rating	Government Support Rating	Issuer Default Rating
				Asset Quality	Earnings & Profitability	Capitalisation & Leverage				
		20%	10%	20%	15%	25%	10%			
aaa								aaa	aaa	AAA
aa+								aa+	aa+	AA+
aa								aa	aa	AA
aa-								aa-	aa-	AA-
a+								a+	a+	A+
a								a	a	A
a-								a-	a-	A-
bbb+								bbb+	bbb+	BBB+
bbb								bbb	bbb	BBB
bbb-								bbb-	bbb-	BBB- Sta
bb+								bb+	bb+	BB+
bb								bb	bb	BB
bb-								bb-	bb-	BB-
b+								b+	b+	B+
b								b	b	B
b-								b-	b-	B-
ccc+								ccc+	ccc+	CCC+
ccc								ccc	ccc	CCC
ccc-								ccc-	ccc-	CCC-
cc								cc	cc	CC
c								c	c	C
f								f	ns	D or RD

The Key Rating Driver (KRD) weightings used to determine the implied VR are shown as percentages at the top. In cases where the implied VR is adjusted upwards or downwards to arrive at the VR, the KRD associated with the adjustment reason is highlighted in red. The shaded areas indicate the benchmark-implied scores for each KRD.

VR - Adjustments to Key Rating Drivers

The operating environment score of 'a+' is below the 'aa' category implied score due to the following adjustment reason: international operations (negative).

The business profile score of 'bbb-' is above the 'bb' category implied score due to the following adjustment reason: strategy and execution (positive)

The asset quality score of 'bbb' is below the 'aa' category implied score due to the following adjustment reason: concentrations (negative)

The earnings and profitability score of 'bbb' is below the 'a' category implied score due to the following adjustment reason: revenue diversification (negative)

The capitalisation and leverage score of 'bb+' is below the 'a' category implied score due to the following adjustment reason: size (negative); internal capital generation and growth (negative)

The funding and liquidity score of 'bbb-' is above the 'bb' category implied score due to the following adjustment reason: non-deposit funding (positive)

## Financials

### Financial Statements

	30 Jun 23		31 Dec 22	31 Dec 21	31 Dec 20
	6 months - interim (USDm)	6 months - interim (EURm)	Year end (EURm)	Year end (EURm)	Year end (EURm)
<b>Summary income statement</b>					
Net interest and dividend income	89	81.8	125.8	79.0	77.1
Net fees and commissions	16	14.5	29.9	29.4	28.5
Other operating income	3	3.0	23.3	24.3	1.8
Total operating income	108	99.3	179.0	132.7	107.4
Operating costs	47	43.7	78.1	65.4	59.2
Pre-impairment operating profit	60	55.6	100.9	67.3	48.2
Loan and other impairment charges	0	0.3	1.6	0.2	0.2
Operating profit	60	55.3	99.3	67.1	48.0
Tax	15	13.6	21.1	18.2	11.6
Net income	45	41.7	78.2	48.9	36.4
Other comprehensive income	7	6.6	-26.9	-10.0	-20.2
Fitch comprehensive income	52	48.3	51.3	38.9	16.2
<b>Summary Balance Sheet</b>					
<b>Assets</b>					
Gross loans	3,100	2,852.6	2,789.4	2,602.9	2,427.7
- Of which impaired	14	12.5	0.0	0.0	0.0
Loan loss allowances	7	6.3	6.0	4.4	4.3
Net loans	3,093	2,846.3	2,783.4	2,598.5	2,423.4
Interbank	69	63.7	103.4	129.3	152.7
Derivatives	202	185.9	201.4	129.6	140.3
Other securities and earning assets	1,514	1,393.0	997.7	995.9	863.0
Total earning assets	4,878	4,488.9	4,085.9	3,853.3	3,579.4
Cash and due from banks	443	407.4	503.2	543.4	808.6
Other assets	42	38.2	39.2	31.2	35.2
Total assets	5,362	4,934.5	4,628.3	4,427.9	4,423.2
<b>Liabilities</b>					
Customer deposits	2,737	2,518.8	2,125.6	1,710.2	1,772.7
Interbank and other short-term funding	161	148.5	156.6	480.8	520.3
Other long-term funding	1,576	1,450.6	1,572.1	1,581.8	1,509.2
Trading liabilities and derivatives	219	201.9	199.3	168.9	222.9
Total funding and derivatives	4,694	4,319.8	4,053.6	3,941.7	4,025.1
Other liabilities	105	96.6	102.8	48.5	38.7
Preference shares and hybrid capital	68	62.2	62.2	62.2	n.a.
Total equity	495	455.9	409.7	375.5	359.4
Total liabilities and equity	5,362	4,934.5	4,628.3	4,427.9	4,423.2
Exchange rate		USD1 = EUR0.920302	USD1 = EUR0.937559	USD1 = EUR0.884173	USD1 = EUR0.821963

Source: Fitch Ratings, Fitch Solution. KA

## Key Ratios

	30 Jun 23	31 Dec 22	31 Dec 21	31 Dec 20
<b>Ratios (%; annualised as appropriate)</b>				
<b>Profitability</b>				
Operating profit/risk-weighted assets	3.9	3.9	3.3	2.8
Net interest income/average earning assets	3.9	3.2	2.1	2.1
Non-interest expense/gross revenue	44.0	43.6	50.0	55.1
Net income/average equity	19.4	20.3	13.3	10.4
<b>Asset quality</b>				
Impaired loans ratio	0.4	0.0	0.0	0.0
Growth in gross loans	2.3	7.2	7.2	-9.7
Loan loss allowances/impaired loans	50.4	0.0	0.0	0.0
Loan impairment charges/average gross loans	0.0	0.1	0.0	0.0
<b>Capitalisation</b>				
Common equity Tier 1 ratio	15.2	15.9	17.0	20.0
Tangible common equity/tangible assets	9.1	8.7	8.5	8.0
Net impaired loans/common equity Tier <sup>1</sup>	1.4	-1.5	-1.3	-1.3
<b>Funding and liquidity</b>				
Gross loans/customer deposits	113.3	131.2	152.2	137.0
Gross loans/customer deposits + covered bonds	n.a.	91.4	101.4	91.2
Liquidity coverage ratio	387.0	348.0	735.0	420.6
Customer deposits/total non-equity funding	60.3	54.3	44.6	46.6
Net stable funding ratio	115.0	129.0	122.0	117.5

Source: Fitch Ratings, Fitch Solutions, KA

## Support Assessment

Commercial Banks: Government Support	
Typical D-SIB GSR for sovereign's rating level (assuming high propensity)	a+ to a-
Actual jurisdiction D-SIB GSR	ns
Government Support Rating	ns
<b>Government ability to support D-SIBs</b>	
Sovereign Rating	AA+/ Stable
Size of banking system	Neutral
Structure of banking system	Neutral
Sovereign financial flexibility (for rating level)	Neutral
<b>Government propensity to support D-SIBs</b>	
Resolution legislation	Negative
Support stance	Neutral
<b>Government propensity to support bank</b>	
Systemic importance	Negative
Liability structure	Negative
Ownership	Negative

The colours indicate the weighting of each KRD in the assessment.  
■ Higher influence ■ Moderate influence ■ Lower influence

The government support rating reflects KA's lack of systemic importance, and our view that the EU's resolution framework is likely to require senior creditors participating in losses, if necessary, instead or ahead of a bank receiving sovereign support. The IDRs do not factor in any support from KA's owners either, because Fitch generally considers that support from financial investors, while possible, cannot be relied upon.

## Environmental, Social and Governance Considerations

### Credit-Relevant ESG Derivation

Kommunalkredit Austria AG has 5 ESG potential rating drivers

- Kommunalkredit Austria AG has exposure to compliance risks including fair lending practices, mis-selling, repossession/foreclosure practices, consumer data protection (data security) but this has very low impact on the rating.
- Governance is minimally relevant to the rating and is not currently a driver.

			ESG Relevance to Credit Rating	
key driver	0	issues	5	
driver	0	issues	4	
potential driver	5	issues	3	
not a rating driver	4	issues	2	
	5	issues	1	

### Environmental (E) Relevance Scores

General Issues	E Score	Sector-Specific Issues	Reference	E Relevance	
GHG Emissions & Air Quality	1	n.a.	n.a.	5	
Energy Management	1	n.a.	n.a.	4	
Water & Wastewater Management	1	n.a.	n.a.	3	
Waste & Hazardous Materials Management; Ecological Impacts	1	n.a.	n.a.	2	
Exposure to Environmental Impacts	2	Impact of extreme weather events on assets and/or operations and corresponding risk appetite & management; catastrophe risk; credit concentrations	Business Profile (incl. Management & governance); Risk Profile; Asset Quality	1	

**How to Read This Page**  
ESG relevance scores range from 1 to 5 based on a 15-level color gradation. Red (5) is most relevant to the credit rating and green (1) is least relevant.

**The Environmental (E), Social (S) and Governance (G) tables** break out the ESG general issues and the sector-specific issues that are most relevant to each industry group. Relevance scores are assigned to each sector-specific issue, signaling the credit-relevance of the sector-specific issues to the issuer's overall credit rating. The Criteria Reference column highlights the factor(s) within which the corresponding ESG issues are captured in Fitch's credit analysis. The vertical color bars are visualizations of the frequency of occurrence of the highest constituent relevance scores. They do not represent an aggregate of the relevance scores or aggregate ESG credit relevance.

**The Credit-Relevant ESG Derivation table's** far right column is a visualization of the frequency of occurrence of the highest ESG relevance scores across the combined E, S and G categories. The three columns to the left of ESG Relevance to Credit Rating summarize rating relevance and impact to credit from ESG issues. The box on the far left identifies any ESG Relevance Sub-factor issues that are drivers or potential drivers of the issuer's credit rating (corresponding with scores of 3, 4 or 5) and provides a brief explanation for the relevance score. All scores of '4' and '5' are assumed to result in a negative impact unless indicated with a '+' sign for positive impact. Scores of 3, 4 or 5) and provides a brief explanation for the score.

### Social (S) Relevance Scores

General Issues	S Score	Sector-Specific Issues	Reference	S Relevance	
Human Rights, Community Relations, Access & Affordability	2	Services for underbanked and underserved communities; SME and community development programs; financial literacy programs	Business Profile (incl. Management & governance); Risk Profile	5	
Customer Welfare - Fair Messaging, Privacy & Data Security	3	Compliance risks including fair lending practices, mis-selling, repossession/foreclosure practices, consumer data protection (data security)	Operating Environment; Business Profile (incl. Management & governance); Risk Profile	4	
Labor Relations & Practices	2	Impact of labor negotiations, including board/employee compensation and composition	Business Profile (incl. Management & governance)	3	
Employee Wellbeing	1	n.a.	n.a.	2	
Exposure to Social Impacts	2	Shift in social or consumer preferences as a result of an institution's social positions, or social and/or political disapproval of core banking practices	Business Profile (incl. Management & governance); Financial Profile	1	

### Governance (G) Relevance Scores

General Issues	G Score	Sector-Specific Issues	Reference	G Relevance	CREDIT-RELEVANT ESG SCALE
Management Strategy	3	Operational implementation of strategy	Business Profile (incl. Management & governance)	5	5 Highly relevant, a key rating driver that has a significant impact on the rating on an individual basis. Equivalent to "higher" relative importance within Navigator.
Governance Structure	3	Board independence and effectiveness; ownership concentration; protection of creditor/stakeholder rights; legal/compliance risks; business continuity; key person risk; related party transactions	Business Profile (incl. Management & governance); Earnings & Profitability; Capitalisation & Leverage	4	4 Relevant to rating, not a key rating driver but has an impact on the rating in combination with other factors. Equivalent to "moderate" relative importance within Navigator.
Group Structure	3	Organizational structure; appropriateness relative to business model; opacity; intra-group dynamics; ownership	Business Profile (incl. Management & governance)	3	3 Minimally relevant to rating, either very low impact or actively managed in a way that results in no impact on the entity rating. Equivalent to "lower" relative importance within Navigator.
Financial Transparency	3	Quality and frequency of financial reporting and auditing processes	Business Profile (incl. Management & governance)	2	2 Irrelevant to the entity rating but relevant to the sector.
				1	1 Irrelevant to the entity rating and irrelevant to the sector.

The highest level of ESG credit relevance is a score of '3', unless otherwise disclosed in this section. A score of '3' means ESG issues are credit neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. Fitch's ESG Relevance Scores are not inputs in the rating process; they are an observation on the relevance and materiality of ESG factors in the rating decision. For more information on Fitch's ESG Relevance Scores, visit <https://www.fitchratings.com/topics/esg/products#esg-relevance-scores>.



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