

Research Update:

Kommunalkredit Austria Outlook Revised To Positive On Sound Performance And Asset Quality Trajectory; Affirmed At 'BBB-'

March 10, 2023

Overview

- Kommunalkredit Austria AG (Kommunalkredit) continues to demonstrate sound risk-adjusted performance and strong asset quality amid very difficult market conditions.
- We anticipate that the bank's proposed new majority shareholder, Altor Funds (Altor), will fully support the continuance of management's sound business, risk, and capital strategy.
- We expect that the bank's capitalization will remain a strength, with a risk-adjusted capital ratio of 12%-14% over the next two years.
- As a result, we revised our outlook on Kommunalkredit to positive from stable and affirmed our 'BBB-/A-3' issuer credit ratings.
- The positive outlook reflects our expectation within the next 12-24 months that the bank will continue to demonstrate healthy risk-adjusted earnings, sound asset quality, and robust capitalization, thanks to full support from its expected new owner.

PRIMARY CREDIT ANALYST

Harm Semder
Frankfurt
+ 49 693 399 9158
harm.semder
@spglobal.com

SECONDARY CONTACTS

Cihan Duran, CFA
Frankfurt
+ 49 69 3399 9177
cihan.duran
@spglobal.com

Karim Kroll
Frankfurt
6933999169
karim.kroll
@spglobal.com

Rating Action

On March 10, 2023, S&P Global Ratings revised its outlook on Kommunalkredit Austria AG to positive from stable and affirmed its 'BBB-/A-3' long- and short-term issuer credit ratings.

Rationale

The outlook revision reflects our view of Kommunalkredit's ongoing solid risk-adjusted earnings amid very difficult market conditions. We expect under our base-case scenario that Kommunalkredit's niche business model will continue generating relatively high earnings and strong asset-quality indicators, despite tough operating conditions amid global uncertainties from the Russia-Ukraine conflict. Based on its healthy margins, sound underwriting, and very high

growth opportunities in infrastructure, energy, and sustainable finance projects, over 2023-2025 we forecast Kommunalkredit's return on average common equity at 10%-13% (after 20% in 2022 and 13% in 2021) and a cost-to-income ratio below 50%.

We expect Kommunalkredit's risk-adjusted capitalization will remain a rating strength, despite the bank's very ambitious business plans, thanks to support from its proposed new financial owner Altor. We forecast the bank's risk-adjusted capital ratio at 12%-14% over the next two years, after 13.5% at year-end 2022. We understand Altor will fully support the continuance of Kommunalkredit management's business strategy, risk appetite, and capital needs, and this is part of our base-case scenario. Under its asset-light strategy, Kommunalkredit syndicates 30%-50% of its yearly new business. In addition to the announced proposal of a €100 million capital increase in 2023, we expect that the new owner will also fund any further capital needs to match Kommunalkredit's ambitious plan to increase customer loans by roughly 50% through 2025.

We anticipate Kommunalkredit will maintain solid asset-quality metrics. Supported by its solid risk management and expected further governance improvements, we anticipate Kommunalkredit will continue to post a very good credit-risk record, after incurring almost no credit-risk costs and no nonperforming loans in recent years. We note, however, that its more concentrated portfolio than we see at most other European banks and higher dependence on key personnel could make it more sensitive to potential adverse economic scenarios or single events than peers.

Outlook

The positive outlook reflects our expectation that within the next 12-24 months Kommunalkredit's proposed new owner will fully support the continuance of the bank's existing business and risk strategy. In particular, we expect that Kommunalkredit will maintain its double-digit risk-adjusted profitability, sound risk appetite and asset quality, and robust capitalization. Similarly, we anticipate that Kommunalkredit will continue to further improve its management and control capabilities consistent with its growth trajectory.

We could raise our rating on Kommunalkredit over the next 24 months, if the bank shows similar or higher-than-anticipated earnings performance and sound asset quality demonstrating outperformance of higher rated, more diversified banking peers. In addition, we would also need more confidence that Altor will fully fund and support Kommunalkredit's business expansion strategies in the medium-to-long term.

Downside scenario

We would revise the outlook to stable over the next 24 months, if the bank or its owner were to adversely change Kommunalkredit's business and risk strategies, or unexpectedly we were to see meaningful deterioration in its earnings or asset quality, or if delayed economic recovery adversely affected Kommunalkredit's key markets.

Similarly, we could revise the outlook to stable if Kommunalkredit failed to improve its organizational and business settings in line with its strong growth path, or if it shifted unexpectedly to a more aggressive growth strategy beyond its core competencies.

Ratings Score Snapshot

	To	From
Issuer Credit Rating	BBB-/Positive/A-3	BBB-/Stable/A-3
SACP	bbb-	bbb-
Anchor	bbb+	bbb+
Business position	Constrained (-2)	Constrained (-2)
Capital and earnings	Strong (+1)	Strong (+1)
Risk position	Adequate (0)	Adequate (0)
Funding and liquidity	Moderate and Adequate (-1)	Moderate and Adequate (-1)
Comparable ratings analysis	0	0
Support	0	0
ALAC support	0	0
GRE support	0	0
Group support	0	0
Sovereign support	0	0
Additional factors	0	0

SACP--Stand-alone credit profile. ALAC—Additional loss-absorbing capacity. GRE--Government-related entity.

ESG credit indicators: E-2, S-2, G-3

Related Criteria

- General Criteria: Hybrid Capital: Methodology And Assumptions, March 2, 2022
- Criteria | Financial Institutions | General: Financial Institutions Rating Methodology, Dec. 9, 2021
- Criteria | Financial Institutions | Banks: Banking Industry Country Risk Assessment Methodology And Assumptions, Dec. 9, 2021
- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- General Criteria: Group Rating Methodology, July 1, 2019
- Criteria | Financial Institutions | General: Risk-Adjusted Capital Framework Methodology, July 20, 2017
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Related Research

- Kommunalkredit Austria Planned Majority Ownership Change Is Consistent With Its Growth Strategy, Feb. 8, 2023
- Various Rating Actions Taken On Austrian Banks On Stabilization Of Operating Performance, Feb. 24, 2023
- Global Macro Update: Post-Davos, We Reaffirm Our View, Jan. 26, 2023
- Kommunalkredit Austria AG, July 5, 2022

Ratings List

Ratings Affirmed

Kommunalkredit Austria AG

Senior Unsecured	BBB-
------------------	------

Ratings Affirmed; Outlook Action

	To	From
--	----	------

Kommunalkredit Austria AG

Issuer Credit Rating	BBB-/Positive/A-3	BBB-/Stable/A-3
----------------------	-------------------	-----------------

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. A description of each of S&P Global Ratings' rating categories is contained in "S&P Global Ratings Definitions" at https://www.standardandpoors.com/en_US/web/guest/article/-/view/sourceld/504352 Complete ratings information is available to subscribers of RatingsDirect at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column. Alternatively, call one of the following S&P Global Ratings numbers: Client Support Europe (44) 20-7176-7176; London Press Office (44) 20-7176-3605; Paris (33) 1-4420-6708; Frankfurt (49) 69-33-999-225; or Stockholm (46) 8-440-5914

Copyright © 2023 by Standard & Poor's Financial Services LLC. All rights reserved.

No content (including ratings, credit-related analyses and data, valuations, model, software or other application or output therefrom) or any part thereof (Content) may be modified, reverse engineered, reproduced or distributed in any form by any means, or stored in a database or retrieval system, without the prior written permission of Standard & Poor's Financial Services LLC or its affiliates (collectively, S&P). The Content shall not be used for any unlawful or unauthorized purposes. S&P and any third-party providers, as well as their directors, officers, shareholders, employees or agents (collectively S&P Parties) do not guarantee the accuracy, completeness, timeliness or availability of the Content. S&P Parties are not responsible for any errors or omissions (negligent or otherwise), regardless of the cause, for the results obtained from the use of the Content, or for the security or maintenance of any data input by the user. The Content is provided on an "as is" basis. S&P PARTIES DISCLAIM ANY AND ALL EXPRESS OR IMPLIED WARRANTIES, INCLUDING, BUT NOT LIMITED TO, ANY WARRANTIES OF MERCHANTABILITY OR FITNESS FOR A PARTICULAR PURPOSE OR USE, FREEDOM FROM BUGS, SOFTWARE ERRORS OR DEFECTS, THAT THE CONTENT'S FUNCTIONING WILL BE UNINTERRUPTED OR THAT THE CONTENT WILL OPERATE WITH ANY SOFTWARE OR HARDWARE CONFIGURATION. In no event shall S&P Parties be liable to any party for any direct, indirect, incidental, exemplary, compensatory, punitive, special or consequential damages, costs, expenses, legal fees, or losses (including, without limitation, lost income or lost profits and opportunity costs or losses caused by negligence) in connection with any use of the Content even if advised of the possibility of such damages.

Credit-related and other analyses, including ratings, and statements in the Content are statements of opinion as of the date they are expressed and not statements of fact. S&P's opinions, analyses and rating acknowledgment decisions (described below) are not recommendations to purchase, hold, or sell any securities or to make any investment decisions, and do not address the suitability of any security. S&P assumes no obligation to update the Content following publication in any form or format. The Content should not be relied on and is not a substitute for the skill, judgment and experience of the user, its management, employees, advisors and/or clients when making investment and other business decisions. S&P does not act as a fiduciary or an investment advisor except where registered as such. While S&P has obtained information from sources it believes to be reliable, S&P does not perform an audit and undertakes no duty of due diligence or independent verification of any information it receives. Rating-related publications may be published for a variety of reasons that are not necessarily dependent on action by rating committees, including, but not limited to, the publication of a periodic update on a credit rating and related analyses.

To the extent that regulatory authorities allow a rating agency to acknowledge in one jurisdiction a rating issued in another jurisdiction for certain regulatory purposes, S&P reserves the right to assign, withdraw or suspend such acknowledgment at any time and in its sole discretion. S&P Parties disclaim any duty whatsoever arising out of the assignment, withdrawal or suspension of an acknowledgment as well as any liability for any damage alleged to have been suffered on account thereof.

S&P keeps certain activities of its business units separate from each other in order to preserve the independence and objectivity of their respective activities. As a result, certain business units of S&P may have information that is not available to other S&P business units. S&P has established policies and procedures to maintain the confidentiality of certain non-public information received in connection with each analytical process.

S&P may receive compensation for its ratings and certain analyses, normally from issuers or underwriters of securities or from obligors. S&P reserves the right to disseminate its opinions and analyses. S&P's public ratings and analyses are made available on its Web sites, www.standardandpoors.com (free of charge), and www.ratingsdirect.com and www.globalcreditportal.com (subscription), and may be distributed through other means, including via S&P publications and third-party redistributors. Additional information about our ratings fees is available at www.standardandpoors.com/usratingsfees.

STANDARD & POOR'S, S&P and RATINGSDIRECT are registered trademarks of Standard & Poor's Financial Services LLC.