

Research Update:

Kommunalkredit Austria AG Assigned 'BBB-/A-3' Ratings; Outlook Stable

February 24, 2021

Overview

- Kommunalkredit Austria AG has demonstrated superior business and earnings resilience to very difficult operating conditions since the outbreak of the COVID-19 pandemic.
- We anticipate that Kommunalkredit will continue to attract new business at attractive risk-adjusted margins, particularly in the sustainable finance-related areas of green energy or social infrastructure.
- We are assigning our 'BBB-/A-3' long- and short-term issuer credit ratings to Kommunalkredit.
- The stable outlook reflects our expectation that Kommunalkredit will continue to report strong profits and a high degree of business resilience to the pandemic-induced adverse economic environment over the next 24 months.

Rating Action

On Feb. 24, 2021, S&P Global Ratings assigned its 'BBB-/A-3' long- and short-term issuer credit ratings on Austria-based Kommunalkredit Austria AG. The outlook is stable.

Rationale

Our ratings reflect Kommunalkredit's robust niche business model, solid risk management, and earnings resilience to very difficult operating conditions amid the COVID-19 pandemic. For example, Kommunalkredit reported a preliminary 15.4% return on equity (RoE) for the full-year 2020, after 10.3% in 2019, aided by strong business growth and robust asset quality.

We also believe that Kommunalkredit has made good progress in building both its reputation and its franchise for arranging infrastructure finance, underwriting, and leading syndications; diversifying into new businesses; and improving its transaction granularity and cost efficiency. We anticipate that Kommunalkredit benefits particularly from its expertise and strong business inflow at attractive margins in the sustainable finance-related areas of green energy or social infrastructure such as hospitals. In our view, this is supported by the global trend and political

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support for a green economy and renewed political interest in strengthening social and health care infrastructure in a post-pandemic environment.

We balance the material progress Kommunalkredit has made in building its business position in its niche area and its transaction-driven revenue base that relies heavily on syndications. We note improving governance measures, including an increase in the number of members on the management board to three. Although it has much improved in recent years, we remain mindful that Kommunalkredit remains more dependent on key personnel for business generation and organization than many of its similarly and higher-rated peers in Austria and elsewhere in Europe.

We expect that capitalization will remain Kommunalkredit's particular strength, as indicated by our forecast of the bank's risk-adjusted capital ratio of 11%-14% over the next two years. We anticipate that Kommunalkredit's asset-light business model, whereby it syndicates about 50% of new business, above-average earnings buffer, and committed owner provide sufficient funds for significant planned business growth. This ties in with Kommunalkredit's announcement of ambitious targets to deliver 10% and above RoE before tax, with a common equity tier 1 ratio above 15% from 2021-2023. Kommunalkredit's credit-risk record is excellent, considering it had no credit-risk costs or nonperforming loans at year-end 2020 or in recent years, but we remain mindful of its more concentrated portfolio than we see at most other European banks.

We anticipate that Kommunalkredit's combined funding and liquidity assessment will remain weaker than that of many global peers considering its high share of wholesale funding. Its increasing share of online marketed deposits is positive, but these are more price-sensitive, confidence-driven, and less sticky compared to large diversified retail banks.

Outlook

The stable outlook reflects our expectation that Kommunalkredit will continue to report strong profits and that its business will remain highly resilient to the pandemic-induced adverse economic environment over the next 24 months. Moreover, we anticipate that Kommunalkredit will gradually build its franchise and originate-to-collaborate business model in the infrastructure and energy financing markets while maintaining high capitalization. As the bank grows, we will look in particular for enhancements in governance and the broader control environment to keep pace with growth.

Downside scenario

We could lower our ratings on Kommunalkredit if the bank experiences material setbacks in its risk-adjusted profitability or asset quality, or if we see a delayed economic recovery adversely affecting Kommunalkredit's most important markets. Similarly, we could lower the ratings if Kommunalkredit fails to professionalize its organizational and business setup in line with strong business growth, if it shifts unexpectedly to an overly aggressive growth strategy beyond its core competencies, or if material risks from a high level of syndication emerge.

Upside scenario

We consider a positive rating action on Kommunalkredit as a remote prospect over the medium term. This reflects some persistent downside risks from the economic environment. More importantly, an upgrade would likely require a much broader franchise and a more diversified earnings profile, with concurrent improvements in controls in order to improve the bank's alignment with higher-rated peers.

Ratings Score Snapshot

Issuer Credit Rating	BBB-/Stable/A-3
SACP	bbb-
Anchor	bbb+
Business Position	Weak (-2)
Capital and Earnings	Strong (+1)
Risk Position	Adequate (0)
Funding and Liquidity	Below Average and Adequate (-1)
Support	0
ALAC Support	0
GRE Support	0
Group Support	0
Sovereign Support	0
Additional Factors	0

Related Criteria

- 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
- Criteria | Financial Institutions | Banks: Bank Rating Methodology And Assumptions: Additional Loss-Absorbing Capacity, April 27, 2015
- Criteria | Financial Institutions | Banks: Quantitative Metrics For Rating Banks Globally: Methodology And Assumptions, July 17, 2013
- Criteria | Financial Institutions | Banks: Banks: Rating Methodology And Assumptions, Nov. 9, 2011
- Criteria | Financial Institutions | Banks: Banking Industry Country Risk Assessment Methodology And Assumptions, Nov. 9, 2011
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Related Research

- Banking Industry Country Risk Assessment Update: January 2021, Jan. 28, 2021
- Banking Industry Country Risk Assessment: Austria, June 17, 2020
- Full Analysis: Austria, March 13, 2020

Ratings List

New Rating; Outlook Action

Kommunalkredit Austria AG

Issuer Credit Rating	BBB-/Stable/A-3
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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/sourceId/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; Stockholm (46) 8-440-5914; or Moscow 7 (495) 783-4009.

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