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Summary:

UniCredit Bank Austria AG

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Summary:

UniCredit Bank Austria AG

Credit Rating: A/Stable/A-1

Rationale

The ratings on UniCredit Bank Austria AG (BA) reflect the bank's group status as a core subsidiary of its 99.995% owner, UniCredit SpA (A/Stable/A-1), owing to its role in developing business in Central and Eastern Europe (CEE) and, to a lesser degree, in Austria. Over the past few years, BA's business and financial profiles have improved substantially, mainly as a result of domestic restructuring measures and profitable growth in CEE. However, the bank's performance (like that of its major Austrian peers) has become increasingly sensitive to the developments in CEE countries, many of which are facing a sharp reversal of the favorable growth trend seen until 2008. Although BA's CEE network is geographically well diversified, the weight of economically weaker countries has increased and exposes the bank to higher economic risk.

In 2008, BA's operating profitability remained satisfactory. However, this did not reflect the full impact of global recession. Consequently, Standard & Poor's Ratings Services believes that rising risk costs in riskier markets may materially hamper BA's performance and could lead to losses in 2009. The contribution of CEE to BA's operating profit has constantly increased and, as a result of trading losses at its investment banking division, rose to about 75% in 2008. Although we consider BA's track record and well-diversified CEE network a key strength, rapid credit growth, particularly in the least developed countries, leading to rising risk costs, are primary risk factors, in our view.

The ratings are based on what we consider to be BA's core status within the UniCredit group, and we now factor in two notches of parental support. We consider BA a highly systemically important institution in Austria, but we do not factor government support into the ratings over and above the parental support.

In our view, future capital ratios will depend on capital allocation within the UniCredit group following completion of the squeeze-out of BA's minority shareholders. However, we expect that, as a core group member, BA will maintain what we view as prudent capitalization relative to its business risk in potentially more volatile markets. We understand that BA will apply for support from the national support plan provided by the Republic of Austria (AAA/Stable/A-1+) to maintain capitalization consistent with our ratings. During the second quarter of 2009, we expect more clarity on the size of the capital injections and the features of the instruments used, which are likely to be in line with those of BA's Austrian peers. However, we believe the expected capital measures might not be sufficient to absorb rising risk costs if credit quality were to deteriorate further and the economic downturn turns out to be deeper and more prolonged than currently expected.

Outlook

The stable outlook on BA solely reflects that on BA's parent, therefore any rating changes on UniCredit would likely trigger rating actions on BA.

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