

Rating Action: Erste Group Bank AG

Moody's reviews Erste Group Bank for downgrade

Prime-1 short-term rating unaffected

London, 11 December 2008 -- Moody's Investors Service has today placed on review for possible downgrade the Aa3 long-term debt and deposit ratings and C bank financial strength rating (BFSR) of Erste Group Bank AG. The Prime-1 short-term deposit rating was affirmed. The ratings of Erste Group Bank's subordinated debt and hybrid capital securities, as well as those of certain subsidiaries, were also placed on review for possible downgrade.

"The review for downgrade reflects Moody's concern that the bank's financial flexibility -- most notably its capitalisation levels, but also its profitability -- may not be sufficiently strong to withstand the expected weakening in most of its markets in Central & Eastern Europe (CEE) and may require further capital strengthening measures over the course of the next couple of years," explains Guido Versoedert, Vice President -- Senior Analyst in Moody's Financial Institutions group and lead analyst for Erste Bank. This already takes into account the temporary benefits of the government's EUR2.7 billion capital contribution, which is earmarked for early 2009, as well as the completion of the sale in Q4 2008 of Erste Bank's insurance operations resulting in a EUR600 million capital strengthening.

Moody's says that the increasing visibility of a significant economic slowdown in Erste Group's core markets in CEE will exert pressure on asset quality, capital ratios, revenues and earnings because the bank's performance is heavily dependent on the rapidly growing retail banking franchises which the bank has successfully established in the region. As at 30 September 2008, around 36% of Erste Group's risk-weighted assets (RWA) and 62% of its pre-tax profits were generated within CEE, with the Czech Republic and Romania being the most important markets.

"Erste Group Bank has built well-performing retail banks in CEE with attractive long-term prospects. Nonetheless, the economic and political uncertainty and the instability still inherent in many of these markets is considerable. The looming economic downturn may reduce revenue and earnings streams, affect asset quality and erode capital ratios," Mr. Versoedert adds. The rating agency also points to the funding and capital gaps that Moody expects will arise at the level of the local banks in CEE, even in scenarios of comparatively moderate growth, as well as Erste Group Bank's historically weak capital ratios and quality.

As a result, Moody's is concerned that -- across a broad range of stress scenarios that factor in a weakening in these markets -- earnings may decrease and loan loss provisioning requirements may substantially increase, which may result in significantly weaker financial results for 2009, and possibly 2010, than those typically required for a C BFSR.

Moody's rating review will therefore focus on the bank's (i) performance trends in Q4 2008 and early indicators for the economic situation in its core CEE markets in 2009, which may already give an indication about the resilience of these markets; (ii) the expected development of problem loans and provisioning requirements in 2009 and 2010, and (iii) most importantly, Erste Group Bank's longer-term capitalisation plans beyond the measures already indicated so far this year.

With regard to the review for possible downgrade on the bank's ratings for subordinated debt and, in particular, hybrid capital securities, Moody's notes that Erste Group Bank makes extensive use of this form of low-quality regulatory capital. In line with Moody's approach to differentiate more clearly among banks and their intrinsic creditworthiness, the varying legal frameworks and the characteristics of individual instruments, the review will focus on the extent to which a weaker BFSR may have negative implications for rating transition risk and the severity of loss of these hybrid capital instruments. As a result, Moody's may potentially take a more negative rating view on these securities than in the past.

Moody's will be issuing separate announcements about the impact of today's rating action for Erste Bank on its subsidiaries.

Moody's previous rating action on Erste Group Bank AG was implemented on 20 April 2007, when the rating agency applied the revised methodologies (see below) and assigned Aa3/P-1/C ratings to Erste Group Bank AG.

The principal methodologies used in rating Erste Group Bank are "Bank Financial Strength Ratings: Global Methodology" and "Incorporation of Joint-Default Analysis into Moody's Bank Ratings: A Refined Methodology", which can be found on www.moody.com in the Credit Policy & Methodologies directory, in the Ratings Methodologies subdirectory. Other methodologies and factors that may have been considered in the process of rating Erste Group Bank AG can also be found in the Credit Policy & Methodologies directory.

Erste Group Bank AG is domiciled in Vienna, Austria. At the end of September 2008, it reported total consolidated assets of EUR209.4 billion and equity of EUR12.9 billion pursuant to IFRS. The group's Tier 1 ratio reached 5.8% according to BIS standards. For the first nine months of 2008, Erste Group Bank reported consolidated pre-tax profits of EUR1.3 billion and a net income of EUR1.5 billion.

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