

**Rating Action: Moody's changes outlook on Erste Group Bank's Baa2 senior ratings to positive**

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**Outlook change reflects expected improvement in the bank's sustained credit metrics**

Frankfurt am Main, September 01, 2015 -- Moody's Investors Service (Moody's) today affirmed Erste Group Bank AG's Baa2 long-term senior debt and deposit ratings and assigned a positive outlook. The rating affirmation is supported by the recent strengthening of Erste's credit metrics. The positive outlook reflects Moody's expectation that Erste will be able to sustain and further improve its credit metrics.

At the same time the agency affirmed Erste's baseline credit assessment (BCA) at ba1, its counterparty risk assessment (CRA) at Baa1(cr)/Prime-2(cr) and all other ratings of the bank.

A full list of affected ratings can be found at the end of this press release.

**RATING RATIONALE**

**AFFIRMATION OF THE BANK'S LONG-TERM SENIOR RATINGS**

Erste's affirmed Baa2 long-term senior ratings reflect (1) the bank's affirmed ba1 BCA and adjusted BCA; and (2) the unchanged results of Moody's Advanced loss-given-failure (LGF) analysis, which provide a two-notch uplift. The ratings do not benefit from any government support as Moody's attributes a "low" probability of support from the Austrian government (Aaa, stable) in light of the precedent set by triggering a resolution of Heta Asset Resolution AG (Carinthian-state-guaranteed senior unsecured debt Ca, developing outlook), which illustrates the Austrian government's willingness to apply burden sharing.

**-- IMPROVEMENT IN ERSTE'S CREDIT METRICS**

The BCA affirmation is supported by the recent strengthening of Erste's credit metrics, which is underpinned by a Common Equity Tier 1 (CET1) ratio of 11.3% under Basel 3 on a fully-loaded basis and the bank's non-performing loan (NPL) ratio of 7.7% as of end-of June 2015.

Moody's considers the improved capitalisation to be more adequate for the intrinsic risks of the bank's operating model, which is geared towards Central and Eastern Europe (CEE). At the achieved capital levels, the agency also considers the bank to be better prepared to comply with upcoming regulatory requirements. Moody's expects the Austrian regulator to implement a systemic risk buffer over the next 12-24 months.

As of end-June 2015, NPLs were at EUR10.1 billion, down from EUR12.6 billion at its peak in June 2013, helped by portfolio sales, particularly in Romania and Hungary. As a result, the bank's NPL ratio stood at 7.7% at end-of June 2015, down from 9.7% at end-of June 2013. Moody's expects the NPL ratio to drop further if the bank is able to continue with its portfolio sales and maintains tight control of new NPL formation.

Overall, Moody's considers Erste to be on track toward regaining its full earnings generation capacity after significant risk charges and write-downs in previous years. This will allow the bank to buffer for potential additional charges, such as the bank levy and contributions to the deposit guarantee scheme as well as building further capital from retained earnings.

**-- CLOSE CONTROL OF RISKS KEY FOR FURTHER STRENGTHENING OF CREDIT PROFILE**

A close control of the risks in the CEE region remains key for a further strengthening of the bank's credit profile. Erste remains vulnerable to idiosyncratic developments in single countries, as experienced in Hungary in recent years. For Croatia, additional downside risks result from a potential forced conversion of Swiss-franc loans to retail clients. Given the size of Erste's portfolio in the country, the agency considers this risk to be manageable. The bank is subject to concentration risks as profit contributions in recent years were concentrated in Czech Republic and Slovakia.

## RATIONALE FOR THE POSITIVE OUTLOOK ON SENIOR DEBT AND DEPOSIT RATINGS

The positive outlook on Erste's long-term senior deposit and debt ratings reflects Moody's expectation that Erste is on track to resume its full earnings generation capacity in the medium term, in line with its announced target of a return on tangible equity of 8-10% in 2015, which should result in a further strengthening of the banks' financial fundamentals in the next 12 - 18 months. An upgrade could be prompted should Erste sustain and further improve its current credit metrics.

## AFFIRMATION OF THE BANK'S HYBRID CAPITAL INSTRUMENTS

The rating agency affirmed the ratings of Erste's supplementary capital and hybrid debt instruments at their current levels which had resulted from the rating downgrade as of 18 December 2014, and reflect the coupon skip earlier this year. The instruments are currently rated at the lower of normal notching or on an expected loss basis. The agency would move these ratings back to normal notching according to Moody's bank methodology once the 2015 accounts become available and allow the bank to resume coupon payments in 2016, which is Moody's expectation.

## WHAT WOULD MOVE THE RATING UP / DOWN

Upward pressure could be exerted on Erste's long-term ratings as a result of (1) an increase of its standalone ba1 BCA; or (2) a significant increase in the bank's bail-inable debt.

Upward pressure on Erste's ba1 standalone BCA would be prompted by (1) a further significant and sustained reduction in the volume of NPLs; (2) a sustained capitalisation above 11%; and (3) sustained improvement in the bank's operating performance and capital generation capacity. In addition, an upgrade would require the bank to maintain a solid risk management and corporate governance track record. Upward rating pressure on the bank's senior debt ratings would also develop if the bank significantly increased the amount of subordinated debt which could be bailed-in ahead of senior unsecured debt, thereby allowing for an extremely low loss-given-failure for the senior debt classes.

If Erste were to resume payments on its supplementary capital and hybrid capital instruments on a sustained basis, upward pressure would develop on these instruments' ratings to the extent that ratings would return to normal notching, for some of these instruments entailing several notches of upgrade potential.

Downward pressure could be exerted on Erste's long-term ratings as a result of (1) a lowering of its standalone ba1 BCA; or (2) a significant decrease in the bank's bail-inable debt cushion.

Downward pressure could be exerted on Erste's ba1 standalone BCA following (1) additional credit charges, in particular related to the bank's operations in CEE; (2) a weakening in earnings that results in lower internal capital generation; and (3) weakened capitalisation levels.

## LIST OF AFFECTED RATINGS

The following ratings of Erste Group Bank AG were affirmed with a change in outlook:

- Long-term senior debt and deposit ratings at Baa2 positive.

The following ratings of Erste Bank, New York, were affirmed with a change in outlook:

- Bank deposit ratings at Baa2 positive.

The following ratings and risk assessments of Erste Group Bank AG were affirmed at their current levels:

- Short-term debt and deposit rating at Prime-2;
- Counterparty Risk Assessment at Baa1(cr) / Prime-2(cr);
- Baseline Credit Assessment (BCA) of ba1;
- Adjusted Baseline Credit Assessment of ba1;
- Subordinated and senior subordinated debt ratings at Ba2;
- Certain junior subordinate debt ratings at B1(hyb) (ISIN: XS0303559115);

- Certain junior subordinate debt ratings at B2(hyb) (ISIN: XS0143383148; ISIN: AT000B000450, ISIN: AT000B000518, ISIN: AT000B001078);

- Certain junior subordinate debt ratings at Caa1(hyb) (ISIN: AT000B000062).

The following risk assessments of Erste Bank, New York, were affirmed at their current levels:

- Counterparty Risk Assessment at Baa1(cr) / Prime-2(cr).

The following ratings of Erste Capital Finance (Jersey) Tier I PC were affirmed:

- Non-cumulative preferred securities at Caa1(hyb).

The following ratings of Erste Finance (Jersey) (4) Limited were affirmed:

- Backed non-cumulative preferred securities at B2(hyb).

The following ratings of Erste Finance (Jersey) (6) Limited were affirmed:

- Backed non-cumulative preferred securities at Caa1(hyb).

The following ratings of Erste Finance (Delaware) LLC were affirmed:

- Backed Commercial Paper at Prime-2.

#### PRINCIPAL METHODOLOGY

The principal methodology used in these ratings was Banks published in March 2015. Please see the Credit Policy page on [www.moodys.com](http://www.moodys.com) for a copy of this methodology.

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