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CREDIT OPINION
1 August 2017

Update

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RATINGS

Erste Group Bank AG

Domicile	Vienna, Austria
Long Term Debt	A3
Type	Senior Unsecured - Fgn Curr
Outlook	Positive
Long Term Deposit	A3
Type	LT Bank Deposits - Fgn Curr
Outlook	Positive

Please see the ratings section at the end of this report for more information. The ratings and outlook shown reflect information as of the publication date.

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Erste Group Bank AG

Update following rating upgrade to A3/P-2

Summary rating rationale

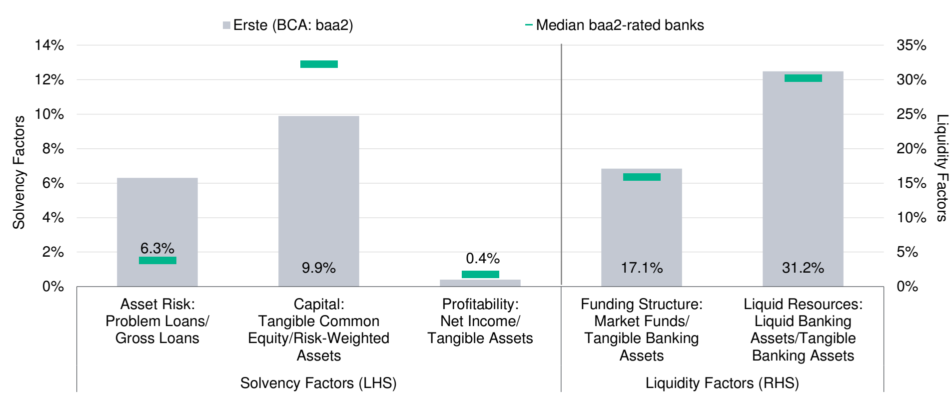
We assign A3/P-2 senior unsecured debt and deposit ratings with a positive outlook to Erste Group Bank AG (Erste). Furthermore, we assign a Baseline Credit Assessment (BCA) and Adjusted BCA of baa2, and a Counterparty Risk Assessment (CR Assessment) of A2(cr)/P-1(cr) to Erste.

Erste's ratings reflect (1) the bank's baa2 BCA and Adjusted BCA; and (2) the result of our Advanced Loss Given Failure (LGF) analysis, which takes into account the severity of loss faced by the different liability classes in resolution and results in two notches of uplift to the bank's ratings.

The recent upgrade of the bank's BCA to baa2 followed the continued strengthening of Erste's key credit metrics and incorporates the bank's sustained de-risking of its balance sheet, leading to meaningfully lower risk costs, thereby supporting the recovery of the bank's earnings-generation capacity to solid levels as well as the fostering of the bank's capital adequacy ratios.

The BCA further reflects Erste's sound funding profile largely consisting of highly granular retail deposits and very low market funding needs over the next few years as well as the bank's 'Strong' Macro Profile, reflecting gradual shifts in Erste's geographical diversification benefiting from proportionally higher exposures towards the stronger and more stable countries in its leading retail and corporate Central and Eastern European (CEE) franchises as well as its home market Austria.

Exhibit 1
Rating Scorecard Erste Group Bank AG - Key financial ratios



Source: Moody's Financial Metrics. Note: Our definition of Tangible Common Equity (TCE) excludes domestic minority shares that are recognised as part of regulatory capital. Asset Risk and Profitability show 3-year averages for Erste.

Credit strengths

» Significantly improved asset quality, following successful problem loan reduction in CEE

» Sound earnings generation capacity

» Deposit-rich funding profile with only moderate reliance on wholesale funding

» Highly liquid balance sheet mitigates potential funding market dislocations

Credit challenges

» Need to further improve capitalisation levels amid rising regulatory requirements and sustained business growth

» Defending asset quality in a more adverse market environment

» Establishing track record of strong bottom line protection once credit risk costs normalise

» Maintaining prudent lending standards in a low interest-rate environment that pressures earnings and boosts loan demand

Rating outlook

» The positive outlook on Erste's senior debt and deposit ratings reflects our expectation of further, albeit more gradual, improvements in asset quality and capital metrics over the next 12-18 months from their now higher levels.

» This assessment also takes into account Erste's ability to maintain its high earnings generation capacity in the medium term. Coupled with additional gradual improvements in the bank's asset risk metrics supporting the bank's low absolute charge-off levels on bad debts, this will likely result in a further buildup of its capital base over time, although at a pace slower than previous years.

» Moreover, a sustained increase in the volume and level of subordinated debt relative to the bank's tangible asset base may lead to a higher rating uplift for the bank's senior debt and deposit ratings as a result of our Advanced LGF analysis, currently providing two notches of rating uplift.

Factors that could lead to an upgrade

» Erste's ratings could be upgraded as a result of an upgrade of the bank's BCA or an increase in its subordinated debt volumes, or both.

» Upward rating pressure on Erste's baa2 BCA would be prompted by a combination of two or more of the following factors: (1) a further significant and sustained reduction in the volume of problem loans, specifically if this reduction leads to a problem loan ratio of below 4% through the cycle, and provided the bank maintains its solid risk management track record and strict lending criteria; (2) a sustained and further improvement in Erste's capitalisation metrics building a meaningful buffer over and above the bank's SREP[1] ratio requirements; or (3) a continuation of the bank's solid operating performance and capital-generation capacity around levels achieved in 2016.

» Upward rating pressure on the bank's debt and deposit ratings would also develop if it increases the amount of subordinated debt that could be bailed-in ahead of senior unsecured debt, providing one additional notch of rating uplift from our LGF analysis.

Factors that could lead to a downgrade

» Erste's long-term ratings could be downgraded as a result of (1) a downgrade of the bank's baa2 BCA; or (2) a significant decrease in its bail-inable debt buffer, leading to fewer notches of rating uplift from our LGF analysis.

» Downward pressure on Erste's baa2 BCA could be exerted following (1) a renewed and sustained formation of problem loans and related loan loss charges, in particular if stemming from the bank's operations in CEE or if resulting from a loosening of credit standards amid bright operating conditions; (2) a sustained weakening in the bank's earnings- and, thus, capital-generation capacity; or (3) an unexpected weakening of the bank's meanwhile solid capitalisation levels.

Key indicators

Exhibit 2

Erste Group Bank AG (Consolidated Financials) [1]

	3-17[2]	12-16[2]	12-15[2]	12-14[2]	12-13[3]	CAGR/Avg.[4]
Total Assets (EUR billion)	219	203	195	188	193	4.1[5]
Total Assets (USD billion)	234	214	212	227	265	-3.7[5]
Tangible Common Equity (EUR billion)	10	10	8.9	7.8	8.8	4.8[5]
Tangible Common Equity (USD billion)	11	10	9.6	9.5	12	-3.1[5]
Problem Loans / Gross Loans (%)	4.9	4.9	7.1	8.5	9.6	7.0[6]
Tangible Common Equity / Risk Weighted Assets (%)	9.9	9.8	9.0	7.8	9.0	9.1[7]
Problem Loans / (Tangible Common Equity + Loan Loss Reserve) (%)	45.4	45.7	62.6	71.0	74.3	59.8[6]
Net Interest Margin (%)	2.0	2.2	2.3	2.3	2.3	2.2[6]
PPI / Average RWA (%)	1.9	2.2	2.6	2.4	2.6	2.3[7]
Net Income / Tangible Assets (%)	0.6	0.7	0.6	-0.3	0.3	0.4[6]
Cost / Income Ratio (%)	69.6	67.1	61.3	65.6	62.3	65.2[6]
Market Funds / Tangible Banking Assets (%)	19.3	17.1	19.4	21.1	22.9	20.0[6]
Liquid Banking Assets / Tangible Banking Assets (%)	34.4	31.2	29.7	30.1	31.3	31.3[6]
Gross Loans / Due to Customers (%)	95.1	98.1	103.2	105.0	104.7	101.2[6]

[1] All figures and ratios are adjusted using Moody's standard adjustments [2] Basel III - fully-loaded or transitional phase-in; IFRS [3] Basel II; IFRS [4] May include rounding differences due to scale of reported amounts [5] Compound Annual Growth Rate (%) based on time period presented for the latest accounting regime [6] Simple average of periods presented for the latest accounting regime. [7] Simple average of Basel III periods presented

Source: Moody's Financial Metrics

Detailed rating considerations

Significantly improved asset quality, following successful problem loan reduction in CEE

The baa3 Asset Risk score assigned to Erste takes account of the successful reduction of problem loan exposures, particularly in CEE, and our expectation of a more gradual decline of the bank's problem loan ratio going forward. This improvement in the bank's credit risk profile was supported by pro-active portfolio sales and an underlying improvement in asset quality in Erste's CEE markets, particularly in Romania and Hungary.

Erste reported a problem loan ratio of 4.9% as of the end of 2016 and in the first quarter of 2017, significantly lower than its peak level of 9.7% as of 30 June 2013. The coverage ratio improved to 67.6% as of 31 March 2017 from 61.7% as of 30 June 2013. We view these levels as sustainable during our outlook period, yet any further improvement remains dependent on the bank maintaining tight control of its geographical concentrations as well as lending criteria amid favorable business conditions, thereby avoiding undue new problem loan formation potentially leading to higher future risk costs.

In 2016, as well as during Q1 2017, Erste's risk costs remained near historically low levels (Q1 2017: 19 basis points; 2016: 14 basis points). In the medium term, we expect the bank's loan-loss charges to increase from current levels. Additionally, Erste remains vulnerable to the risk of an overall economic slowdown in CEE (which is unlikely at present), leading to higher risk charges, as well as to idiosyncratic developments in single countries. However, as one-off charges have been booked against the profit and loss account in previous years, we believe the burden of these often politically driven consumer protection measures (for example, foreign-currency-denominated loans in Hungary, Croatia and Romania) to lie behind Erste.

Higher capital buffers position Erste well to meet regulatory requirements, but the bank needs to ensure continued scrutiny on its capital retention policy

Erste's baa1 Capital score is positioned three notches above the macro-adjusted score. Our positive adjustment captures the bank's joint liability and institutional protection scheme (IPS) with the Austrian savings banks, allowing Erste to freely access and transfer member banks' own funds in case of need[2]. Because this additional loss-absorbing capital at the level of the savings banks would be available to Erste prior to failure, we take account of these additional going-concern capital elements by positively adjusting our Capital score. Our adjustment further captures the full regulatory approval of the Austrian savings banks' IPS, allowing Erste to report its Common Equity Tier 1 (CET1) on a consolidated basis without any reduction for its domestic minority shares, i.e. the savings banks.

With a CET1 ratio of 12.8% on a fully loaded basis as of 31 March 2017 (including retained earnings), we consider the bank's improved capitalisation to be sufficient to cover the intrinsic risks of its operating model, which is geared towards CEE. In addition, balance-sheet leverage is not a constraint for Erste, with its 5.8% fully loaded Basel III leverage ratio. We believe the bank's higher earnings generation power and thus capital generation capacity will allow for a sustained build-up of Erste's fully loaded CET1 capital ratio to above 13% over the next 12-18 months, despite pressure on the bank's earnings from fierce competition, margin pressure in a persistently low interest-rate environment and regulatory costs.

At the anticipated solid capital and profitability levels, the bank is well prepared to comply with upcoming regulatory requirements, specifically with regard to the implementation of a systemic risk buffer by the Austrian regulator (50 basis points, effective since the beginning of 2017 and growing to 200 basis points by 2019) and the currently expected fully loaded CET1 ratio minimum requirement of 10.9% in 2019 (excluding Pillar 2 CET1 Guidance of 1.66% as of 2017), set by the European Central Bank as part of its Supervisory Review and Evaluation Process (SREP).

Solid earnings-generation capacity, despite earnings pressure from the persistent low interest-rate environment and regulatory contributions

The baa3 Profitability score assigned to Erste reflects the bank's fully restored earnings-generation capacity that we expect to be sustained in 2017 and potentially beyond. Over the next two to three years, Erste will primarily be subject to net interest margin and earnings pressures from the persistently low interest-rate environment, as loans and liquid financial investments reprice to lower rates. In addition, domestic and foreign bank levies, as well as contributions to various resolution funds and deposit guarantee schemes have increased the bank's regulatory expenses over the past years. Given the Government of Austria's (Aa1 stable) decision to reduce the domestic bank levy following a one-off payment in 2016, we expect this burden to be substantially reduced in 2017. Together with our expectation of continued low risk costs, we believe profitability to stabilise around the levels achieved in 2016.

As of 31 December 2016, Erste reported a 31% growth in its bottom-line profitability (after minorities) to €1,265 million from a year earlier, supported by significantly reduced net risk costs (down an absolute €533 million from a year earlier) and stable core operating earnings. The bank's operations in the Czech Republic and Slovakia accounted for 49% of its pre-tax profits. Romania recovered and contributed an additional 12% in 2016. Each of the bank's operations in CEE was able to contribute positively to the result, a meaningful achievement when compared with previous years. These positive trends continued in Q1 2017.

Deposit-rich and highly liquid balance sheet, with moderate reliance on wholesale funding

Erste's a3 Funding Structure score reflects its balanced funding profile and its continued reduction in wholesale funding dependence. Together with its sound and largely unencumbered liquid asset base leading to an assigned Liquid Resources score of baa1, the bank's overall Combined Liquidity score stands at a3.

Erste's funding structure continues to be a relative strength, with a sustained loan/deposit ratio below 100% over the past few years (Q1 2017: 91.9%; 2016: 94.7%; 2015: 98.4%). The bank continues to benefit from its access to a broad and diversified base of customer deposits, accounting for more than two-thirds of its total liabilities. Around 55% of the bank's customer deposits are generated from its domestic Austrian operations, with the remaining portion being CEE-related deposits (although concentrated in the Czech Republic and Slovakia). Our assigned a3 Funding Structure score further reflects the high granularity of Erste's deposit base, which mainly relies on deposits from retail investors, and small and medium-sized enterprises.

Erste's liquidity position is comfortable. The bank held liquid assets equivalent to approximately 30% of its balance sheet as of 31 December 2016. This solid liquidity position is further supported by low liquid asset encumbrance. Moreover, the bank's outstanding debt securities account for around 13% of its total liabilities, of which covered bonds represented approximately one-third (€9.3 billion). We estimate Erste's annual long-term refinancing needs to be around €2.5 billion for the next two years, a very low figure compared with the bank's balance-sheet size of €208 billion as of 31 December 2016 (Q1 2017: €223 billion). Additionally, Erste's market funding profile benefits from an average debt maturity of around eight years.

These considerations also take into account the Austrian regulator's recommendation that the country's three major banks limit their new lending in CEE subsidiaries to 110% of local deposits, plus funding in local capital markets and funding from supranational institutions. This more locally based funding model mitigates potential risks resulting from possible funding imbalances in local markets. Erste displayed a sound profile as of the end of 2016, with deposits exceeding loans for all of Erste's larger CEE franchises.

Erste's 'Strong' Macro Profile supports its rating

Erste benefits from operating in a diverse range of countries, with its home market Austria accounting for around 50% of the bank's exposures at year-end 2016. However, owing to its exposures to jurisdictions with slightly lower Macro Profiles (primarily the CEE economies) through its foreign subsidiaries, the overall Macro Profile for Erste Bank is Strong, below Austria's Strong+ Macro Profile.

The recent improvement in the bank's Macro Profile to 'Strong' from 'Strong-' takes account of the gradual shift in the bank's exposures towards CEE countries with higher Macro Profiles (e.g. the Czech Republic) as opposed to those with weaker Macro Profiles (e.g. Romania and Hungary). We believe this shift to be sustainable and we further anticipate improvements in the operating environment and, thus, potentially the Macro Profiles of some of the CEE countries Erste operates in, thereby supporting its Macro Profile over the next 12 to 18 months.

Notching considerations

Loss Given Failure (LGF) analysis

Erste is subject to the European Union Bank Recovery and Resolution Directive (BRRD), which we consider an operational resolution regime. Therefore, we apply our Advanced LGF analysis, considering the risks faced by the different debt and deposit classes across the liability structure, should the bank enter resolution. In line with our standard assumptions, we assume residual tangible common equity of 3% and losses post-failure of 8% of tangible banking assets, a 25% run-off in junior wholesale deposits, a 5% run-off in preferred deposits, and assign a 25% probability to deposits being preferred to senior unsecured debt.

For Erste's senior unsecured debt and deposits, our LGF analysis indicates a very low loss-given-failure, leading to two notches of rating uplift from the bank's baa2 Adjusted BCA.

Additional notching for subordinated and hybrid debt instruments

For other junior debt classes, our Advanced LGF analysis indicates a high loss-given-failure, given the limited volume of debt and limited protection from more subordinated instruments and residual equity. Absent any government support uplift, Erste's subordinated debt is rated Baa3, one notch below the bank's baa2 Adjusted BCA.

Additional notching applies to Erste's junior subordinated debt instruments, reflecting the risk of a missed coupon payment and the timeliness of those payments. The bank's cumulative junior subordinated debt maturing in June 2019 (ISIN: XS0303559115) is rated Ba1(hyb), two notches below the bank's baa2 Adjusted BCA. The rating reflects the junior subordinated claim in liquidation and cumulative deferral features tied to the breach of a net loss trigger.

Additional Tier 1 (AT1) instruments

We assign a (P)Ba2 rating to Erste's AT1 note program and a Ba2(hyb) rating to the two €500 million AT1 notes issued under the program, three notches below the bank's baa2 Adjusted BCA.

The ratings reflect our assessment of the instruments' deeply subordinated claim in liquidation as well as its non-cumulative coupon deferral features. In addition, the securities' principal is subject to a partial or full write-down on a contractual basis if (1) Erste's CET1 ratio falls below 5.125%, (2) the issuer receives public support, or (3) the Austrian Financial Market Authority determines that the conditions for a full write-down of the instrument are fulfilled and orders such a write-down as a precautionary measure to prevent insolvency.

Government support

The wider scope of the BRRD implementation in Austria and its recent application, triggering a resolution of Heta Asset Resolution AG (Ca stable[3]), illustrates the Austrian government's willingness to apply burden sharing to bondholders. We have, therefore, eliminated government support from our Austrian banks' ratings, assuming a low probability of Erste receiving support from the government.

About Moody's scorecard

Our Scorecard is designed to capture, express and explain in summary form our Rating Committee's judgment. When read in conjunction with our research, a fulsome presentation of our judgment is expressed. As a result, the output of our Scorecard may materially differ from that suggested by raw data alone (though it has been calibrated to avoid the frequent need for strong divergence). The Scorecard output and the individual scores are discussed in rating committees and may be adjusted up or down to reflect conditions specific to each rated entity.

Rating methodology and scorecard factors

Exhibit 3

Erste Group Bank AG

Macro Factors		
Weighted Macro Profile	**Strong**	**100%**

Factor	**Historic Ratio**	**Macro Adjusted Score**	**Credit Trend**	**Assigned Score**	**Key driver #1**	**Key driver #2**
Solvency						
Asset Risk						
Problem Loans / Gross Loans	6.3%	ba1	↑	baa3	Quality of assets	Expected trend
Capital						
TCE / RWA	9.9%	ba1	↑	baa1	Capital fungibility	Expected trend
Profitability						
Net Income / Tangible Assets	0.4%	ba1	←→	baa3	Return on assets	Expected trend
Combined Solvency Score		ba1		baa2		
Liquidity						
Funding Structure						
Market Funds / Tangible Banking Assets	17.1%	baa1	←→	a3	Market funding quality	
Liquid Resources						
Liquid Banking Assets / Tangible Banking Assets	31.2%	a3	←→	baa1	Asset encumbrance	
Combined Liquidity Score		baa1		a3		
Financial Profile				baa1		
Business Diversification				0		
Opacity and Complexity				0		
Corporate Behavior				0		
Total Qualitative Adjustments				0		
Sovereign or Affiliate constraint:				Aa1		
Scorecard Calculated BCA range				a3-baa2		
Assigned BCA				baa2		
Affiliate Support notching				0		
Adjusted BCA				baa2		

Balance Sheet	**in-scope (EUR million)**	**% in-scope**	**at-failure (EUR million)**	**% at-failure**
Other liabilities	43,164	30.3%	43,164	30.3%
Deposits	75,837	53.3%	75,837	53.3%
Preferred deposits	56,119	39.4%	53,313	37.5%
Junior Deposits	19,718	13.9%	14,788	10.4%
Senior unsecured bank debt	11,916	8.4%	11,916	8.4%
Dated subordinated bank debt	6,078	4.3%	6,078	4.3%
Junior subordinated bank debt	20	0.0%	20	0.0%
Preference shares (bank)	1,000	0.7%	1,000	0.7%
Equity	4,269	3.0%	4,269	3.0%
Total Tangible Banking Assets	142,283	100%	142,283	100%

Debt class	De Jure waterfall		De Facto waterfall		Notching		LGF Notching Guidance vs. Adjusted BCA	Assigned LGF notching	Additional notching	Preliminary Rating Assessment
	Instrument volume + subordination	Sub-ordination	Instrument volume + subordination	Sub-ordination	De Jure	De Facto				
Counterparty Risk Assessment	26.8%	26.8%	26.8%	26.8%	3	3	3	3	0	a2 (cr)
Deposits	26.8%	8.0%	26.8%	16.4%	2	3	2	2	0	a3
Senior unsecured bank debt	26.8%	8.0%	16.4%	8.0%	2	2	2	2	0	a3
Dated subordinated bank debt	8.0%	3.7%	8.0%	3.7%	-1	-1	-1	-1	0	baa3
Junior subordinated bank debt	3.7%	3.7%	3.7%	3.7%	-1	-1	-1	-1	-1	ba1 (hyb)
Non-cumulative bank preference shares	3.7%	3.0%	3.7%	3.0%	-1	-1	-1	-1	-2	ba2 (hyb)

Instrument class	Loss Given Failure notching	Additional Notching	Preliminary Rating Assessment	Government Support notching	Local Currency Rating	Foreign Currency Rating
Counterparty Risk Assessment	3	0	a2 (cr)	0	A2 (cr)	--
Deposits	2	0	a3	0	A3	A3
Senior unsecured bank debt	2	0	a3	0	A3	A3
Dated subordinated bank debt	-1	0	baa3	0	Baa3	--
Junior subordinated bank debt	-1	-1	ba1 (hyb)	0	Ba1 (hyb)	--
Non-cumulative bank preference shares	-1	-2	ba2 (hyb)	0	Ba2 (hyb)	--

Source: Moody's Financial Metrics

Ratings

Exhibit 4

Category	Moody's Rating
ERSTE GROUP BANK AG	
Outlook	Positive
Bank Deposits	A3/P-2
Baseline Credit Assessment	baa2
Adjusted Baseline Credit Assessment	baa2
Counterparty Risk Assessment	A2(cr)/P-1(cr)
Senior Unsecured	A3
Senior Subordinate -Dom Curr	Baa3
Jr Subordinate -Dom Curr	Ba1 (hyb)
Pref. Stock Non-cumulative -Dom Curr	Ba2 (hyb)
Commercial Paper -Dom Curr	P-2
Other Short Term -Dom Curr	(P)P-2
CESKA SPORITELNA, A.S.	
Outlook	Stable
Bank Deposits	A2/P-1
Baseline Credit Assessment	baa1
Adjusted Baseline Credit Assessment	baa1
Counterparty Risk Assessment	A1(cr)/P-1(cr)
ERSTE BANK HUNGARY ZRT.	
Outlook	Stable(m)
Bank Deposits	Baa3/P-3
Baseline Credit Assessment	b1
Adjusted Baseline Credit Assessment	ba2
Counterparty Risk Assessment	Baa2(cr)/P-2(cr)
ERSTE BANK, NEW YORK	
Outlook	Positive
Bank Deposits	A3/--
Counterparty Risk Assessment	A2(cr)/P-1(cr)
ERSTE FINANCE (DELAWARE) LLC	
Bkd Commercial Paper	P-2
BANCA COMERCIALA ROMANA S.A.	
Outlook	Positive
Bank Deposits	Ba1/NP
Baseline Credit Assessment	b2
Adjusted Baseline Credit Assessment	ba3
Counterparty Risk Assessment	Baa3(cr)/P-3(cr)

Source: Moody's Investors Service

Endnotes

1 Supervisory Review and Evaluation Process, as determined by the European Central Bank

2 The transfer of the amount of own funds is limited to capital elements exceeding the respective member banks' minimum capital requirements. As such, any individual member of the IPS is only obliged to contribute to the extent that such contribution does not result in a violation of the regulatory requirements applicable to that member

3 The ratings shown in this report are the bank's backed senior unsecured debt rating and outlook

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