

Austria-Based Erste Bank Assigned 'A' L-T Rating; 'A-1' S-T Rating Affirmed

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Rationale

On Dec. 5, 2006, Standard & Poor's Ratings Services assigned its 'A' long-term counterparty credit rating to Austria-based Erste Bank der oesterreichischen Sparkassen AG (Erste Bank). The outlook is stable. At the same time, the short-term 'A-1' rating was affirmed.

The ratings on Erste Bank are based on the group's prominent market position in Austria and several countries in Central and Eastern Europe (CEE), and the continued profitability improvements in large parts of the group. It also reflects Standard & Poor's view of Erste Bank and the Austrian savings banks as a single economic group. These positive factors are partially offset by modest capital levels as a result of Erste Bank's acquisition strategy; still moderate earnings levels in the competitive Austrian market; and ambitious growth targets, which rely to a significant degree on continued positive prospects for CEE.

Erste Bank conducts retail and commercial banking operations, and is the central institution in the Austrian savings banks sector. The group forms the third-largest banking sector in Austria by total assets, and is among the market leaders in several fast-growing CEE countries, most of which are members of the EU. The group is well positioned to benefit from the higher-than-average growth opportunities in CEE, but is also exposed to still higher-than-average economic and industry risk. These risks are abating, however, and are adequately rewarded by higher returns.

Erste Bank has made steady progress in improving its profitability. CEE remains the key growth driver, benefiting from strong loan demand, mortgage lending in particular, and further efficiency gains. We expect Erste Bank to continue to expand its lending activities

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based on prudent lending standards. Various groupwide initiatives are expected to enhance sales productivity and limit cost growth.

Our view of the Austrian savings banks sector as an economic group is based on its sound level of cohesiveness and solidarity underpinned by a limited protection scheme. The positive rating implications on Erste Bank from the savings banks are limited, however, because the savings banks are much smaller, although they are better capitalized on average.

The group's capitalization is modest, particularly in view of its growing reliance on CEE markets. Pure levels of capital benefit considerably from the consolidation of the savings banks. The effect on capitalization of the recent large acquisition of Banca Comerciala Romana (BCR; BBB-/Stable/—) has been moderated by a capital increase, but ambitious volume growth should limit the group's ability to generate free capital over the next two or three years.

Profitability in Erste Bank's overbanked domestic market remains modest despite recent improvements. Conditions for small and midsize enterprise (SME) lending remain a particular concern. Over time, the domestic operations have potential for further improvement, but any progress from the current level is likely to be modest.

The acquisition of BCR highlighted Erste Bank's willingness to pay quite high premium prices if it sees a strong strategic rationale. As a leading player in Romanian retail banking, BCR fits neatly into Erste Bank's strategy, but it operates in an underdeveloped banking system. BCR's projected annual net profit growth target of above 40% per year until 2009 to achieve the expected 10% return on Erste Bank's investment is ambitious and is subject to a continued stable upward trend in the Romanian economic environment and a successful integration. We expect Erste Bank to focus primarily on organic growth over the next few years.

Outlook

The stable outlook reflects the expectation that Erste Bank should be able to address integration risks relating to the acquisition of BCR based on the bank's strong track record. Almost one year after the announcement of the takeover, no unexpected risks have emerged. We will continue to monitor the success of BCR's integration into Erste Bank and the speed and sustainability at which operating earnings improve at BCR. Material deviations from Erste Bank's earnings targets for BCR, which might put pressure on other parts of the group to offset any shortfall, would be viewed negatively. Further sizable acquisitions, which would delay the rebuilding of capital ratios and stretch management resources, would also be negative for the rating.

Stronger capitalization, a further reduction in the economic and industry risk in CEE, and major progress in the integration process and profitability of BCR could be positive for the rating.

Ratings List

	To	From
<i>Erste Bank der oesterreichischen Sparkassen AG</i>		
Long-term counterparty credit ratings	A/Stable	NR
Short-term counterparty credit rating	A-1	A-1
CP	A-1	A-1

NB: This list does not include all ratings affected.

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