

BICRA On Austria Revised To Group '2' From Group '3'

Primary Credit Analyst:

Markus Schmaus, Frankfurt (49) 69-33-999-155; markus_schmaus@standardandpoors.com

Secondary Contacts:

Dirk Heise, Frankfurt (49) 69-33-999-163; dirk_heise@standardandpoors.com

Harm Semder, Frankfurt (49) 69-33-999-158; harm_semder@standardandpoors.com

OVERVIEW

- We are reviewing our Banking Industry Country Risk Assessment (BICRA) on Austria in light of our updated methodology.
- We are revising our BICRA on Austria to group '2' from Group '3'.
- We are revising our economic risk score to '2' from '1' and assigning an industry risk score of '3'.

BICRA ACTION

On Nov. 9, 2011, Standard & Poor's Ratings Services said that it is revising its Banking Industry Country Risk Assessment (BICRA) on Austria to group '2' from group '3'. It is also revising the economic risk score to '2' from '1'. At the same time, it has assigned an industry risk score of '3'.

RATIONALE

We have reviewed the banking sector of the Republic of Austria (AAA/Stable/A-1+) under our updated BICRA methodology. Our criteria define the BICRA framework as one "designed to evaluate and compare global banking systems". A BICRA analysis for a country covers rated and unrated financial institutions that take deposits, extend credit, or engage in both activities. A BICRA is scored on a scale from 1 to 10, ranging from the lowest-risk banking systems (group '1') to the highest-risk (group '10'). Other countries in BICRA group '2' are Australia, Japan, Germany, and Norway.

Our economic risk score of '2' for Austria reflects our assessment of Austria's "economic resilience" as "very low risk", "economic imbalances" as "low risk", and "credit risk in the economy" as "intermediate risk", as our

criteria define these terms.

We view the Austrian economy as highly diversified and competitive, demonstrating the country's "economic resilience". Austria benefits from very stable GDP growth, which continues to exceed the European average. Its GDP per capita, which was \$45,000 in 2010, is among the highest in Europe. The government's finances and its fiscal and monetary flexibility are, in our view, very robust, underpinned by a stable and predictable political environment.

We consider the risk of "economic imbalances" to be low. Although we have observed a slight increase in housing prices over the past two years, it was much smaller than in many other Western European countries. At present, we do not see credit-fuelled asset price bubbles in Austria and we expect the country's current account balance to remain positive.

Our assessment of an intermediate level of "credit risk in the economy" reflects Austria's average level of private-sector indebtedness in the EU context. Although we consider Austrian banks to have conservative lending and underwriting standards, we view the comparably high level of domestic loans in foreign currencies as a possible area of concern if exchange rates were to become more volatile.

Our industry risk score of '3' for Austria reflects our assessment of Austria's "institutional framework" and "competitive dynamics" as "intermediate risk" and "systemwide funding" as "low risk".

In our view, the "institutional framework" for Austrian banks has strengthened materially to the "intermediate risk" level in recent years, following a series of deficiencies in banking regulation and supervision. The Austrian Financial Markets Authority was established in 2005 and is progressively taking a more proactive stance, in our view. Nevertheless, we believe the regulator may have to carry additional supervisory responsibilities because Austrian banks, unlike most European peers, have sizable assets outside their home base.

We generally consider the domestic profitability of Austrian banks to be very low compared with international standards. This, in our view, stems mainly from the large number of separate banking units, which is the basis for our "intermediate risk" assessment of the industry's "competitive dynamics". The growth of domestic banking assets is not a critical factor, in our view, because it is in line with the wider Austrian economy and outstripped by the far bigger growth momentum of operations in Central and Eastern Europe and the Commonwealth of Independent States. We believe this indicates that bank financing in Austria is not solely to gain market share and is unlikely to result in a credit bubble. We currently do not observe banking market distortions and do not expect new ones to arise.

We consider "systemwide funding" in Austria's banking sector as "low risk", based on the comparably low level of net external lending and satisfactory and

increasing deposit-to-loan ratios in the industry. Although we view Austria's capital market to be effective, the Austrian government may not have the capacity to support all the foreign operations of the large domestic banks.

We classify the Austrian government as "supportive" toward the domestic banking sector. We recognize the government's track record of providing support to the banking system in times of exceptional stress.

RELATED CRITERIA AND RESEARCH

- Banking Industry Country Risk Assessment Methodology And Assumptions, Nov. 9, 2011
- Standard & Poor's BICRAs Highlight The Shifting Balance In Global Banking, Nov. 9, 2011
- S&P's BICRAs Measure Banking Risks For 86 Countries, Nov. 9, 2011

Additional Contact:

Financial Institutions Ratings Europe; FIG_Europe@standardandpoors.com

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