

# Fitch Ratings

## Fitch Upgrades VB-Verbund, Downgrades and Withdraws immigon's Ratings following Spin-Off

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Fitch Ratings-Frankfurt/London-27 August 2015: Fitch Ratings has upgraded Austria's Volksbanken-Verbund's (VB-Verbund) Long-term Issuer Default Rating (IDR) to 'BB+' from 'BB-' and removed it from Rating Watch Positive (RWP). The Outlook is Positive. Fitch has also downgraded immigon portfolioabbau ag's Long-term IDR to 'CCC' from 'B' and withdrawn its ratings.

The rating actions reflect immigon's spin-off from VB-Verbund, effective on 6 July 2015, and commencement of a major restructuring of the remaining banks in VB-Verbund. VB-Verbund is not a legal entity but a network of cooperative banks. Based on Fitch's criteria for rating banking structures backed by mutual support mechanisms, Fitch has assigned group ratings but no Viability Ratings (VRs) to VB-Verbund's member banks.

Fitch is withdrawing immigon's ratings as the entity has chosen to stop participating in the rating process. Fitch is also withdrawing the ratings of several members of VB-Verbund, which have left or are expected to leave VB-Verbund's mutual support scheme. Therefore, Fitch will no longer have sufficient information to maintain these ratings. Accordingly, Fitch will no longer provide ratings or analytical coverage for these entities. A full list of rating actions is available at the end of this rating action commentary.

### KEY RATING DRIVERS - VB-VERBUND's IDRs AND VR

The upgrade of VB-Verbund's Long-term IDR reflects the significant risk reduction achieved through immigon's spin-off, where the group's non-core, riskiest assets have been concentrated. Substantial further reorganisation of VB-Verbund is underway, which Fitch also views as positive for its ratings. As a result, we expect VB-Verbund's post spin-off profitability to become significantly more stable but initially modest.

The contract governing the member banks' obligations under the mutual support scheme has been thoroughly overhauled to recognise VB-Verbund as a single regulated group under the EU's Capital Requirements Regulation. The functions previously carried out by Oesterreichische Volksbanken-Aktiengesellschaft (OeVAG) as a central organisation for the VB-Verbund and related assets and liabilities have been transferred to Volksbank Wien-Baden AG (VBWB).

As a result, in addition to remaining by far VB-Verbund's largest member bank covering the Vienna region, VBWB has also become the group's new central institution. The new contract provides VBWB with significantly stronger authority to give individual or sector-wide directives to the primary banks. We believe that these changes increase the group's cohesion and strengthen its corporate

governance. This should also improve its cost and risk management.

To cut costs and reduce complexity, the group has initiated a far-reaching consolidation of its member banks to reduce their number from 43 mostly local entities to eight larger entities of regional scale supplemented by two specialised banks by 2017. This should enable them to achieve the critical size that increasingly demanding regulatory requirements are likely to make necessary for individual cooperative banks.

We believe that immigon's spin-off will enable VB-Verbund's long-term stabilisation as a fairly low-risk, medium-sized banking group predominantly focused on Austrian retail and small corporate clients. VB-Verbund's asset quality post spin-off is only moderately weaker than those of large, highly-rated European cooperative banking groups. Moreover, VB-Verbund's overhauled risk management practices should enable further convergence with these peers over the medium term.

A first debt buyback of EUR933m completed by immigon on 31 July 2015 included most of its outstanding debt held by VB-Verbund's members. As a result, VB-Verbund's net residual exposure to immigon, which hitherto materially constrained VB-Verbund's VR, has become negligible. This remaining exposure is also guaranteed by a third party, as required by the ECB to approve the spin-off.

#### KEY RATING DRIVERS - IMMIGON's IDRs

The downgrade of immigon's IDRs reflects its spin-off from VB-Verbund. VB-Verbund's negligible residual exposure to immigon and the fact that the latter has left the mutual support mechanism no longer create a material incentive for VB-Verbund to provide institutional support if needed.

immigon is highly vulnerable to a decline in assumptions on asset values either from a deterioration in the business and economic environment or a need to sell assets quickly to meet obligations, making a default a real possibility as indicated by the 'CCC' Long-term IDR. In particular, we view the ability of its small capital base inherited from OeVAG to absorb potentially large losses from its legacy assets as very limited.

immigon was established on 6 July 2015 as a partly-regulated wind-down entity without a banking licence and is the legal successor to OeVAG. OeVAG was VB-Verbund's former central organisation, whose troubles triggered VB-Verbund's restructuring following OeVAG's bailout by the Austrian government. This restructuring was initiated in 2012 and accelerated in 4Q14 as it became clear that OeVAG would fail the European Central Bank's (ECB) Comprehensive Assessment.

Central organisation functions and related assets and liabilities have been transferred to VBWB while all other assets and liabilities remain at immigon. immigon will focus exclusively on its accelerated orderly wind-down, which it expects to complete by 2017 through a combination of repayment of debt maturities, asset sales and debt buybacks. immigon is subject to partial regulation by the Austrian national regulators. Although it does not have to fulfil minimum regulatory capital requirements, it is subject to the Austrian legislation implementing the European Bank Recovery and Resolution Directive (BRRD) and its bail-in tool.

immigon's ratio of equity/total assets is low and volatile. The gone-concern valuation of its assets provides a fairly conservative assessment of its capitalisation. Moreover, major clean-up measures have been implemented before the spin-off (notably the sale of OeVAG's fairly large stake in its loss-making Romanian unit in April 2015, followed by several more modest divestments). However, immigon's ambitious run-off schedule creates additional uncertainty about the potential extent of losses.

#### KEY RATING DRIVERS - IMMIGON'S SUPPORT RATING

The downgrade of immigon's Support Rating to '5' from '4' reflects its spin-off from VB-Verbund and our view that the de-linking of its risks from VB-Verbund mean that there is no longer an incentive for the latter to provide any further support. Although VB-Verbund retains 43% of immigon's share capital, this stake has been fully written down by VB-Verbund's members. Similarly, the Austrian government also retains a 43% share of immigon's capital but has publicly ruled out future state support to the wind-down entity.

#### KEY RATING DRIVERS - IMMIGON'S SENIOR DEBT

We have affirmed immigon's debt ratings at 'B' and assigned a Recovery Rating of 'RR2' to reflect superior recovery prospects. This is based primarily on our view that most of the remaining rated debt instruments are likely to be repurchased by immigon at or close to par given its intention to do so and the debt repurchases already completed. This translates into a two-notch uplift to 'B' from its Long-term IDR of 'CCC'. The uplift also reflects our view that, if debt is not repurchased, in the event of default assets should be sufficient to allow superior recovery on remaining senior unsecured obligations.

#### KEY RATING DRIVERS - VB-VERBUND'S SUPPORT RATING AND SUPPORT RATING FLOOR (SRF)

We have affirmed VB-Verbund's Support Rating at '5' and its SRF at 'No Floor'.

These rating actions reflect our view that the BRRD and the Single Resolution Mechanism (SRM) are now sufficiently progressed to provide a framework for resolving banks that is likely to require senior creditors participating in losses, if necessary, instead of or ahead of a bank receiving sovereign support.

BRRD, which was implemented into Austrian legislation with effect from 1 January 2015, includes minimum loss absorption requirements before resolution financing or alternative financing (eg, government stabilisation funds) can be used. Austria is one of the first EU countries to have implemented the BRRD's bail-in tool.

#### RATING SENSITIVITIES - VB-VERBUND'S IDRs AND VR

As VB-Verbund's and its member banks' IDRs are driven by the group's VR they are subject to the same sensitivities as the VR.

The Positive Outlook on VB-Verbund's Long-term IDR reflects the ongoing consolidation of its

member banks and a high likelihood that it will be upgraded within the next two years, once the execution risk of the consolidation plan has sufficiently receded. We expect the planned consolidation to significantly improve the group's efficiency, which will lift earnings to levels that are commensurate with an investment grade rating.

VB-Verbund is required to repay EUR300m to the Austrian government between 2017 and 2023 for participation capital received by OeVAG as part of its bailout. Therefore, the cost savings arising from the primary banks' mergers will also be essential to strengthening VB-Verbund's internal capital generation before it starts repaying the state capital.

We believe that VB-Verbund has the potential to achieve a Long-term IDR comfortably within the 'BBB' range in the medium term, on successful execution of the primary banks' restructuring. However, a higher rating even in the long term is unlikely given the group's small market share of about 7% in the low-margin Austrian retail market, where it is concentrated. We expect the retail banking sector to continue to suffer from structural overcapacity, with little signs of relief in the foreseeable future.

Downside risk to the VR and IDRs could come from a failure to achieve the necessary cost savings from the restructuring. A downgrade could also result from heightened credit risk and a deterioration in asset quality either from a severe downturn in Austria's economy or extension of lending outside Austria, which would be a departure from VB-Verbund's current strategy, neither of which we expect.

#### RATING SENSITIVITIES - VB-VERBUND'S SUPPORT RATING AND SUPPORT RATING FLOOR

Any upgrade of VB-Verbund's Support Rating and upward revision of its SRF would be contingent on a positive change in the sovereign's propensity to provide support. This is highly unlikely in our view.

The rating actions are as follows:

#### VB-Verbund

Long-term IDR: upgraded to 'BB+' from 'BB-'; off RWP; Outlook Positive

Short-term IDR: affirmed at 'B'

Viability Rating: upgraded to 'bb+' from 'bb-'; off RWP

Support Rating: affirmed at '5'

Support Rating Floor: affirmed at 'No Floor'

We do not rate any debt instruments of any member of VB-Verbund.

#### immigon

Long-term IDR: downgraded to 'CCC' from 'B'; off RWN, and withdrawn

Short-term IDR: downgraded to 'C' from 'B'; off RWN, and withdrawn

Support Rating: downgraded to '5' from '4'; off RWN, and withdrawn

Debt issuance programme: affirmed at 'B'/'B', off RWE, assigned Recovery Rating 'RR2' and withdrawn

Senior unsecured notes: affirmed at 'B', off RWE, assigned Recovery Rating 'RR2' and withdrawn

Market linked securities: affirmed at 'Bemr', off RWE, assigned Recovery Rating 'RR2', and withdrawn

The IDRs of VB-Verbund's member banks listed below have been upgraded to 'BB+' / Positive / affirmed 'B' from 'BB-' / RWP / 'B', in line with VB-Verbund's IDRs. These group ratings are sensitive to the same drivers as VB-Verbund's IDRs:

start:bausparkasse e.Gen. Genossenschaft mit beschraenkter Haftung

Bank fuer Aerzte und Freie Berufe AG

Volksbank, Gewerbe- und Handelsbank Kaernten AG

IMMO-BANK AG

Oesterreichische Apothekerbank eG

SPARDA-BANK AUSTRIA Nord eGen

SPARDA-BANK AUSTRIA Sued eGen

Volksbank Alpenvorland e.Gen.

Volksbank Bad Goisern eingetragene Genossenschaft

Volksbank Bad Hall e.Gen.

Volksbank Donau-Weinland reg.Gen.m.b.H.

Volksbank Eferding - Grieskirchen reg.Gen.m.b.H.

Volksbank Enns - St.Valentin eG

Volksbank Feldkirchen eG

Volksbank Fels am Wagram e.Gen.

Volksbank Kaernten Sued e.Gen.

Volksbank Kufstein-Kitzbuehel eG

Volksbank Landeck eG

Volksbank Linz-Wels-Muehlviertel AG

Volksbank Marchfeld e.Gen.

Volksbank Niederoesterreich Sued eG

Volksbank NOe, St.Poelten, Krems Zwettl AG

Volksbank Oberes Waldviertel reg.Gen.m.b.H.

Volksbank Oberkaernten reg.Gen.m.b.H.

Volksbank Oberndorf reg.Gen.m.b.H.

Volksbank Obersdorf - Wolkersdorf - Deutsch-Wagram e. Gen.

Volksbank Obersteiermark eGen

Volksbank Ost reg.Gen.m.b.H.

Volksbank Oetscherland eG

Volksbank Ried im Innkreis eG

Volksbank Salzburg eG

Volksbank Schaerding, Altheim Braunau

Volksbank Steiermark Mitte AG

Volksbank Steirisches Salzkammergut reg.Gen.m.b.H.

Volksbank Suedburgenland eG

Volksbank Sued-Oststeiermark e.Gen.

Volksbank Tirol Innsbruck - Schwaz AG

Volksbank Tullnerfeld eG

Volksbank Voecklabruck-Gmunden e.Gen.  
Volksbank Vorarlberg e. Gen.  
Volksbank Weinviertel e.Gen.  
Volksbank Wien-Baden AG  
Waldviertler Volksbank Horn reg.Gen.m.b.H.

The IDRs of VB-Verbund's following member bank have been upgraded to 'BB+' / Positive / affirmed 'B' from 'BB-' / RWP / 'B' and withdrawn as a result of its merger into Volksbank Salzburg eG, another rated member of the group:

Volksbank Strasswalchen-Voecklamarkt-Mondsee eGen

The IDRs of VB-Verbund's following member banks remain at 'BB-' / 'B' and maintained on Rating Watch Evolving. The ratings have been subsequently withdrawn. These entities have recently left VB-Verbund's mutual support scheme or are expected to leave it in the near future. The RWE and the withdrawals reflect the limited information available on the plans for these entities and their ability to operate as viable stand-alone banks without VB-Verbund's support:

Volksbank Gmuend eingetragene Genossenschaft  
Volksbank Osttirol-Westkaernten eG  
Volksbank Almtal e. Gen.

The IDRs of VB-Verbund's following members remain at 'BB-' / 'B'. The Rating Watch on their Long-term IDRs has been changed to Evolving from Positive and the ratings have been subsequently withdrawn. These entities are expected to leave VB-Verbund's mutual support scheme. The RWE and the withdrawals reflect the limited information available on the plans for these entities and their ability to operate as viable stand-alone banks without VB-Verbund's support:

Spar- und Vorschuss-Verein der Beamtenschaft der Oesterreichischen Nationalbank reg.Gen.m.b.H.  
Spar- und Vorschussverein "Graphik" reg.Gen.m.b.H.  
Spar- und Vorschussverein der Mitarbeiter der Niederoesterreichischen Landesbank-Hypothekenbank AG, reg.Gen.m.b.H.  
Spar- und Vorschusskasse der Angestellten der "Wiener Staedtische Versicherung AG Vienna Insurance Group" e.Gen.

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### **Applicable Criteria**

Global Bank Rating Criteria (pub. 20 Mar 2015)  
([https://www.fitchratings.com/creditdesk/reports/report\\_frame.cfm?rpt\\_id=863501](https://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=863501))

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