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## Fitch: BayernLB Remains on Rating Watch Negative on HGAA Sale Ratings

17 Dec 2009 10:02 AM (EST)

Fitch Ratings-London/Frankfurt-17 December 2009: Fitch Ratings is maintaining Germany-based Bayerische Landesbank's (BayernLB) Long-term and Short-term Issuer Default (IDR) ratings of 'A+' and 'F1+', respectively, and its Support Rating Floor of 'A+' on Rating Watch Negative (RWN). This follows the announcement that its 67% holding in Hypo Group Alpe Adria (HGAA) will be sold to the Austrian state for a nominal amount of EUR1. BayernLB's 'D/E' Individual rating and its '1' Support rating are affirmed.

Those obligations of BayernLB that continue to benefit from 'Gewährträgerhaftung' (a guarantee from the Free State of Bavaria; rated 'AAA'/Outlook Stable) as well as those issued under the EUR15bn debt issuance programme guaranteed by the German Financial Market Stabilisation Fund (FMSF or "Soffin") are affirmed at 'AAA'. The Long-term rating of BayernLB Capital Trust I USD850m trust preferred securities (XS 0290135358) - which are rated 'B+' - remain on RWN.

Although BayernLB has injected around EUR1.4bn of core and hybrid capital into HGAA over the past two years, the Austrian bank requires further capital as a result of asset quality problems identified in its central and eastern European (CEE) portfolio. Its three owners, BayernLB, the state of Carinthia (12.4%) and the insurance company Grazer Wechselseitige (20.5%) reached an agreement with the Austrian state on 14 December 2009, which will result in the nationalisation of the bank. BayernLB will sell its stake to the Austrian state for EUR1, waive EUR525m loans and a EUR300m silent participation and continue to provide EUR3.9bn liquidity facilities to HGAA. BayernLB acquired its stake in HGAA at a price of EUR1.6bn in 2007. The decision to dispose of its subsidiary was taken in order to reduce risks and also in view of ongoing state aid procedures at the European Commission (EC). The Bavarian bank's restructuring requires a substantial asset reduction and a focus on core markets.

Although the sale of HGAA will substantially increase BayernLB's 2009 net loss, the tier 1 ratio will continue to provide a buffer to absorb further losses from BayernLB's large loan portfolio, which Fitch expects to suffer well into 2010 under a depressed economic environment and amidst a restructuring process.

Fitch positively notes the reduction in CEE-related risks on BayernLB's balance sheet, but will look for more evidence of improvements in the bank's performance and asset quality, progress of its restructuring and possible additional implications from the EC's decision on state aid before reviewing the Individual Rating for a potential upgrade.

Generally, BayernLB's hybrid capital is not expected to pay interest and is likely to participate in the loss that will be reported under German accounting as well as IFRS. Fitch will resolve the RWN on the USD850m trust preferred securities once there is more clarity over the extent to which these will be affected.

BayernLB is one of Germany's largest Landesbanks by equity. It co-operates with the 75 Bavarian savings banks, which hold strong market shares in retail deposits and SME lending in one of Germany's strongest regional economies. BayernLB received support from the Free State of Bavaria in the form of a EUR4.8bn risk shield for its ABS portfolio and EUR10bn in fresh capital. As a result, Bavaria's stake in the bank increased to 94%, diluting the Association of Bavaria Savings Banks' stake to 6%.

In Fitch's rating criteria, a bank's standalone risk is reflected in Fitch's Individual ratings and the prospect of external support is reflected in Fitch's Support ratings. Collectively these ratings drive Fitch's Long- and Short-term IDRs.

Contacts: Andrea von Schnurbein, Frankfurt, Tel: +49 69 7680 76248, Michael Dawson-Kropf, +49 69 7680 76113.

Media Relations: Christian Giesen, Frankfurt am Main, Tel: + 49 (0) 69 7680 762 32, Email: christian.giesen@fitchratings.com; Hannah Warrington, London, Tel: +44 (0) 207 417 6298, Email: hannah.warrington@fitchratings.com.

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