

Rating Action: Moody's downgrades to Aa2 Hypo Alpe Adria's unguaranteed covered bonds

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Frankfurt am Main, August 03, 2010 -- Moody's Investors Service has today taken the following rating action on the unguaranteed covered bonds ("Öffentliche Pfandbriefe") issued by Hypo Alpe-Adria-Bank International AG ("Hypo Alpe Adria" or "the issuer") under its public sector covered bond programme:

- Public-sector covered bonds: Downgraded to Aa2 from Aa1; previously on 9 December 2009 downgraded to Aa1 on review for possible downgrade. The public-sector covered bonds which benefit from the State of Carinthia guarantee (guaranteed covered bonds) are not affected by this action and remain Aaa rated.

This rating action concludes the review on the unguaranteed public-sector covered bonds, which was initiated on 12 November 2008, when Moody's placed Hypo Alpe Adria's covered bond ratings on review for possible downgrade (see Moody's press releases 11 November 2008 and 12 November 2008).

Today's downgrade of the covered bonds was triggered by the downgrade of Hypo Alpe Adria's senior unsecured rating to Baa3 from Baa2 (see Moody's press releases dated 3 August 2010). Moody's has assigned a Timely Payment Indicator (TPI) of "High" to the public-sector covered bonds of Hypo Alpe Adria, which constrains the covered bond rating at Aa2, which is the issuer's revised rating level. Moody's notes that today's downgrade was not caused by any deterioration of the credit quality of the public-sector loans comprising the cover pool backing the covered bonds.

The minimum over-collateralisation level that is consistent with the Aa2 rating target is 33.5%. The current level of over-collateralisation is around 506%.

Hypo Alpe Adria's public-sector covered bonds rated by Moody's are governed by the Austrian Pfandbrief Act ("Pfandbriefgesetz"), which requires, among other factors, mandatory over-collateralisation of 2% on a nominal basis. Moody's understands that in March 2010 the issuer has entered into an agreement which creates the obligation to maintain a level of 38.5% over-collateralisation, which the rating agency considers "committed".

There is, however, a potential risk that the agreement to maintain the over-collateralisation in excess of the legally required 2% of over-collateralisation might be subject to rescission under relevant bankruptcy law of Austria if the issuer were to become bankrupt within a certain timeframe of up to twelve months upon conclusion of this agreement. In its assessment Moody's regards this claw-back risk as very low.

Moody's understand that holders of guaranteed and non-guaranteed covered bonds will rank pari passu amongst each other with respect to the cover assets upon issuer default.

RATING METHODOLOGY

Moody's rating for any covered bond is determined after applying a two-step process:

(1) Moody's Expected Loss (EL) Method: Moody's determines a rating based on the EL on the bond. This is modelled as a function of the issuer's probability of default and the stressed losses on the cover pool assets following issuer default.

(2) TPI Framework: Moody's assigns a TPI which indicates the likelihood that timely payment will be made to covered bondholders following issuer default. The effect of the TPI is to limit the covered bond rating to a certain number of notches above the issuer's rating.

Moody's monitors this transaction using the rating methodology for EMEA Covered Bond transactions as described in the Rating Methodology reports "Moody's Rating Approach to European Covered Bond", published in March 2010 and "Assessing Swaps as Hedges in the Covered Bond Market", published in September 2008. All are available on www.moody.com in the Rating Methodologies sub-directory under the Research & Ratings tab. Other methodologies and factors that may have been considered in the process of rating these transactions can also be found in the Rating Methodologies sub-directory on Moody's website. In addition, Moody's publishes a weekly summary of structured finance credit, ratings and methodologies in "Structured Finance Quick Check" at www.moody.com/SFQuickCheck

The rating assigned by Moody's addresses the expected loss posed to investors. Moody's ratings address only the credit risks associated with the transaction. Other non-credit risks have not been addressed, but may have a significant effect on yield to investors.

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