

Ratings On Two Hungarian Banks Affirmed On Reduced Economic Risk

August 18, 2021

- We consider that Hungary's economy has weathered the pandemic well and demonstrated increased economic resilience, as highlighted by the country's rising income levels and improved economic prospects.
- We project real GDP growth of over 6% in 2021 and over 5% in 2022, which we expect will reduce economic risk for Hungarian banks and be supportive for their domestic operations.
- While this reflects positively on the overall creditworthiness of OTP Bank PLC, we affirmed our 'BBB/A-2' ratings on the bank and its core subsidiary OTP Mortgage Bank, given that we continue to cap our ratings at the level of our foreign currency sovereign rating on Hungary (BBB/Stable/A-2). The outlook on both banks remains stable.

FRANKFURT (S&P Global Ratings) Aug. 18, 2021--S&P Global Ratings today affirmed its 'BBB/A-2' long- and short-term issuer credit ratings on OTP Bank PLC and OTP Mortgage Bank. The outlooks on both banks remains stable.

Hungarian MTB Magyar Takarekszovetkezeti Bank Zrt. was not part of the review, since we believe that our ratings on the bank already adequately reflect the macroeconomic upside potential.

We believe the resilience of the Hungarian economy has increased, as indicated by the country's rising income levels and improved economic prospects. Hungary's open economy was hit severely by the pandemic in 2020, with real GDP contracting by 5%. However, supported by quick release of restrictions following a swift vaccination campaign and sizeable fiscal stimulus by the government, we believe that its real GDP will rebound by 6.1% in 2021. Main near-term risk to the projections pertain to the evolution of the pandemic, while medium-term risks relate to the timely availability of EU grants, which are an important factor for the country's further economic development (see "Hungary 'BBB/A-2' Ratings Affirmed; Outlook Remains Stable," published Aug. 13, 2021, on RatingsDirect).

In our assessment, Hungary's banks have weathered the pandemic well. Sizeable fiscal support from the government, an easing of regulatory and lending standards, as well as the Hungarian central bank's accommodative monetary policy effectively supported the economy and the banking sector, in our view. We expect that some measures, such as the country's payment moratorium, will be rolled back in the short-to-medium term. These measures have so far contributed to stability of the labor market, supporting households' and corporates' income levels and the asset quality of banks' loan books. Banks' profitability weakened during 2020, but we do not see increasing risks to the banking system's stability.

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While we believe that a delayed exit of the moratorium masks risks, we consider the banking sector to be sufficiently profitable and well capitalized to withstand an expected increase in nonperforming loans (NPLs). The increase will most likely come mainly on the back of increased vulnerability of corporates, especially small and midsized enterprises and sectors most impacted by the pandemic. Hungary's use of the government's loan moratorium remains the highest among all European countries (decreasing to about 30% as of June 2021). While the scope of the moratorium has materially decreased in 2021, the government prolonged it again until Sept. 30, 2021. The beginning of the loan moratorium phase-out has not yet led to rising NPLs, but tail risks remain. In our view, the residual impact of the pandemic will not be visible before 2022.

OTP Bank PLC & OTP Mortgage Bank

We affirmed our ratings on OTP Bank and its core subsidiary OTP Mortgage Bank and maintained a stable outlook on both entities. In our view, the improved economic environment in Hungary is supportive for the OTP group and contributed to its solid performance in first-half 2021. The improvement of the bottom line was underpinned by lower risk costs and a continued increase in operating profits.

Reflecting the improved economic resilience in OTP group's domestic market, we have revised upward our assessment of OTP Bank's stand-alone credit profile (SACP) to 'bbb+' from 'bbb'. This reflects that we revised the starting point for our rating on the bank to 'bbb-' from 'bb+'. A central assumption behind the improvement is that the group's acquisition strategy abroad will not result in a material deterioration of its risk profile. In our analyses, we already reflect the upcoming acquisition in Slovenia, which we consider to have a similar risk profile as its Hungarian exposures. Given OTP Bank's sound track record of previous acquisitions, we believe that the group has the capacity for prudent execution of the Nova KBM deal, which will significantly improve its market position in Slovenia.

At the same time, we continue to cap our issuer credit rating of OTP Bank at the level of our foreign currency sovereign ratings on Hungary, because we doubt that the bank would have sufficient resources to absorb the impact on the capitalization in a hypothetical sovereign default scenario. This is notably due to its high holdings of Hungarian government debt. The bank fails our stress test to be rated above the sovereign, which measures the resilience to a hypothetical scenario whereby the domestic sovereign defaults both in local and foreign currency.

Outlook

The stable outlook on OTP and its core subsidiary OTP Mortgage Bank reflects our view that the bank will successfully continue its growth path and manage an increase in credit losses after the moratorium phase-out. Based on its track record, we expect that the group will also ensure sufficient capitalization in case of further acquisitions and increasing credit losses.

Downside scenario: A negative rating action on OTP Bank could stem from a similar rating action on the sovereign or a material deterioration in the bank's stand-alone creditworthiness following decreasing capital or deteriorating asset quality. However, we consider the latter scenario remote since we would need to revised downward the SACP by two notches for it to trigger a downgrade.

Upside scenario: A positive rating action could result from an upgrade of the sovereign, while OTP's SACP remains unchanged at 'bbb+'. Alternatively, should the group's capitalization improve to the extent of absorbing eventual losses from a hypothetical sovereign default in Hungary, we

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could consider an upgrade. An upgrade would hinge on our view that the overall creditworthiness of the group would be on par with 'BBB+'-rated peers.

OTP Bank PLC--Ratings Score Snapshot

| | To | From |
|-----------------------|-------------------------------|-------------------------------|
| Issuer credit rating | BBB/Stable/A-2 | BBB/Stable/A-2 |
| SACP | bbb+ | bbb |
| Anchor | bbb- | bb+ |
| Business position | Strong (+1) | Strong (+1) |
| Capital and earnings | Adequate (0) | Adequate (0) |
| Risk position | Adequate (0) | Adequate (0) |
| Funding and liquidity | Above average and strong (+1) | Above average and strong (+1) |
| Support | 0 | 0 |
| GRE support | 0 | 0 |
| Group support | 0 | 0 |
| Sovereign support | 0 | 0 |
| Additional factors | (1) | 0 |

SACP--Stand-alone credit profile. GRE--Government-related entity.

Related Criteria

- General Criteria: Group Rating Methodology, July 1, 2019
- Criteria | Financial Institutions | General: Methodology For Assigning Financial Institution Resolution Counterparty Ratings, April 19, 2018
- Criteria | Financial Institutions | General: Risk-Adjusted Capital Framework Methodology, July 20, 2017
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- Criteria | Financial Institutions | Banks: Bank Rating Methodology And Assumptions: Additional Loss-Absorbing Capacity, April 27, 2015
- General Criteria: Ratings Above The Sovereign--Corporate And Government Ratings: Methodology And Assumptions, Nov. 19, 2013
- Criteria | Financial Institutions | Banks: Quantitative Metrics For Rating Banks Globally: Methodology And Assumptions, July 17, 2013
- Criteria | Financial Institutions | Banks: Banking Industry Country Risk Assessment Methodology And Assumptions, Nov. 9, 2011
- Criteria | Financial Institutions | Banks: Banks: Rating Methodology And Assumptions, Nov. 9, 2011
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Related Research

- Hungary 'BBB/A-2' Ratings Affirmed; Outlook Remains Stable, Aug. 13, 2021
- OTP Bank Strengthens Its Franchise By Acquiring Slovenian Bank Nova KBM, June 1, 2021
- Tech Disruption In Retail Banking: CEE Banks Are On The Digital Fast Lane, May 6, 2021
- OTP Bank PLC, April 29, 2021
- Banking Industry Country Risk Assessment: Hungary, Feb. 20, 2020

BICRA Score Snapshot

Hungary

| | To | From |
|----------------------------|-------------------|-------------------|
| BICRA group | 5 | 5 |
| Economic risk | 5 | 6 |
| Economic resilience | Intermediate risk | High risk |
| Economic imbalances | High risk | High risk |
| Credit risk in the economy | Intermediate risk | Intermediate risk |
| Trend | Stable | Stable |
| Industry risk | 5 | 5 |
| Institutional framework | Intermediate risk | Intermediate risk |
| Competitive dynamics | High risk | High risk |
| Systemwide funding | Intermediate risk | Intermediate risk |
| Trend | Stable | Stable |

Banking Industry Country Risk Assessment (BICRA) economic risk and industry risk scores are on a scale from 1 (lowest risk) to 10 (highest risk). For more details on our BICRA scores on banking industries across the globe, please see "Banking Industry Country Risk Assessment Update," published monthly on RatingsDirect.

Ratings List

***** OTP Bank PLC *****

Ratings Affirmed

OTP Bank PLC

OTP Mortgage Bank

Issuer Credit Rating BBB/Stable/A-2

Resolution Counterparty Rating BBB/--/A-2

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors,

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have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. A description of each of S&P Global Ratings' rating categories is contained in "S&P Global Ratings Definitions" at https://www.standardandpoors.com/en_US/web/guest/article/-/view/sourceld/504352 Complete ratings information is available to subscribers of RatingsDirect at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column. Alternatively, call one of the following S&P Global Ratings numbers: Client Support Europe (44) 20-7176-7176; London Press Office (44) 20-7176-3605; Paris (33) 1-4420-6708; Frankfurt (49) 69-33-999-225; Stockholm (46) 8-440-5914; or Moscow 7 (495) 783-4009.

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