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Paul Formanko: Thank you operator. Hello everyone. Happy Friday. Thank you for joining us for this call. This is Paul Formanko from JP Morgan Banks team, and from Budapest joining is Laszlo Bencsik, Chief Financial and Strategic Officer. Hi Laszlo. The floor is yours please.

Laszlo Bencsik: Hi Paul, thank you very much. Welcome everyone and thank you for joining us today. Good morning and good afternoon depending where you are. The usual presentation is available on the website, so if you go to the English website it's under investor relations and then events and then presentations. I hope you have been all able to access it, and you can follow through the pages together with me.

If you look at the presentation, it's pretty much similar in terms of structure to what I presented last time, and it consists of two chapters. The first one is about the key pillars of the OTP investment rationale. Obviously there haven't been too many changes in this since the last conference call, but maybe two. I'm not going to go through in details the storyline here, but maybe just two points to highlight. On page 4 you can see the return on equity for the first nine months; i climbed up to 18% all in, including all one-offs and everything, which were positive ytd this year. Even the real return being adjusted with the ten year Hungarian government bond yield is getting close to 15% which I think is a quite reasonable result.

The other slide in this first chapter which might be worth looking at is about the Hungarian macro on page 8. Our recent forecast for the 2017 GDP growth in Hungary is close to 4%, actually 3.9%. We expect a quite well-balanced growth based on a good setup of different factors: we expect exports to continue to grow, investments should increase in a decent way, but most importantly we expect the domestic consumption to continue to grow with a reasonable rate. As you can see on this page, we expect similar growth for this year and next year, around 5%, and all of this is fuelled by growing real wages. We expect 3.8% real wages growth for next year, assuming an inflation of 2.2-2.3%. We also expect the house price index to continue to grow in Hungary.

Finishing the first chapter and jumping into the second one which details the specific results coming from the third quarter of this year, on page 14 you see an overview of the results which also tries to explain the drivers behind the improvement of the profits compared to last year. Both in the overall accounting profit and in the adjusted profit after tax we see considerable improvement. It is even bigger in the accounting numbers due to the very different dynamics of the one-offs or the adjustments. Last year there was a strong negative number of HUF 67.2 billion which this year turned into a slight positive number of 3.1 billion, largely due to the Visa transaction results which were booked into the P&L this year, and also a lower level of bank tax in Hungary.

If you only focus on the adjusted profit after tax, then again this can be split into two parts. One is related to the CEE countries, where the overall year-on-year growth was 4%, and the other element being the Russian and Ukrainian performance which is drastically better this year than last year. Instead of losses realized last year, we booked gains this year.

There's another perspective which you can use when you look at these numbers, and that's just the distribution of core Hungarian profits and non-Hungarian profits. Last year the adjusted results were largely dominated by the Hungarian one because due to the losses in Ukraine and Russia they basically offset the results of Bulgaria and the other small countries in our portfolio. Whereas this year due to the improving performance of our Russian and Ukrainian banks, the contribution of the foreign subsidiaries increased and they are up to 42% of the total profit of the entire group. This is a better representation of the profit generation potential of the group, and I hope that this ratio is going to continue to increase and we are going to have an even more balanced earnings contribution and distribution of profits within the group - I mean an increasing share of profit contribution from the foreign subsidiaries in the future.

On page 16 you can see the results country by country. If we look at Hungary on a quarter on quarter basis we had quite a substantial growth of 26% in after tax profits. This is due to lower tax, slightly higher income, slightly lower cost and somewhat smaller positive risk cost in the third quarter. Bulgaria was fairly stable. Likewise the smaller countries in our portfolio typically improved quarter on quarter and the contribution became better, but still they are not obviously the dominant factors in the overall performance. Russia and Ukraine managed to improve somewhat compared to the second quarter.

On page 17 you see the one-offs. I'm just going to explain them briefly. Let's start with the income tax matters. The first one, the HUF 8.6 billion, is basically a tax shield which came from a write-off of our investment to our Ukrainian factoring company. We managed to convert group funding to equity and then part of this equity had to be written off due to the value of this asset in Ukraine, and that created a tax shield. It had no other impact on the P&L because the losses were already recognised in the P&L which came from the negative results of the factoring company there, and if you might remember we had a negative equity in that entity. The equity value of the factoring unit is now close to zero, so we eliminated this sizable negative equity and we also reduced the group funding and we also realized a tax shield on this loss which occurred years ago.

The other one-off item was this HUF 7.5 billion. This is related to the implementation of the IFRS accounting standards in Hungary. There's a more detailed explanation of this within miscellaneous items, so I'm going to talk about it in more details there.

On page 18 you see the adjusted after tax profit, and here you can see the corporate tax line and this is markedly lower than it was in the third quarter last year, and also much lower than in the second or even the first quarter. This decrease in the tax payments is due to the subsidiary investments. There was a loss in the Hungarian books primarily due to the movement of the Rouble exchange rate against HUF, and therefore we had lower tax payments in Hungary, at OTP Core.

The other one of item is relatively small, an adjustment related to the share swap agreement, and here we come to the before tax profit without one-off items, and there we have 9% growth quarter on quarter. If we go into details of this number and we look at the revenue line, I think that's quite positive, what we see there. And even if we go within the revenues into the net interest income, we had an improvement there. A slight improvement, but nevertheless an improvement, which I think is quite an achievement in this current declining rate environment. Fees and commissions increased and other non-interest income increased as well slightly, whereas operating costs on a quarter on quarter basis went lower. This was due to the one-offs in the second quarter related to reorganisation costs. And the risk cost on a core basis was more or less flat.

Going to the miscellaneous items, I think there are some important points here. The first one is the AXA portfolio takeover that we announced. This transaction started at the beginning of the year. We have finalised the merger or the absorption of these volumes into our books at the end of October, technically on 1st of November. We have taken over these clients and we have booked the volumes into our books. You don't see it yet in the third quarter numbers. You will be seeing them in the fourth quarter numbers. In advance what we can tell is that the net growth of the performing, i.e. less than 90 days past due book, was HUF 162 billion, and the non-performing book increased net by 15 billion.

This has been quite a large and arduous road which our colleagues did. We basically completed the entire transfer in less than nine months. It was quite a large, laborious work which was done, so we are quite happy that we did it and now we have a number of new customers and new volumes which should contribute to our profitability from now on.

The second item as you can see on page 19 is coming from the fact that the Hungarian authorities decided to shun the Hungarian accounting standards, at least for financial institutions, and introduce the IFRS in local accounting as well. For many years we've been doing IFRS financial reports, obviously on a consolidated level, but also locally for the Hungarian entity. What we also used to do, and still do for this year, this is the last year, when we do financial statements according to local accounting standards which were somewhat different from IFRS. Most importantly these local accounting standards and their financial reports were the basis of taxation in Hungary. This is also changing, so from next year on the IFRS will be the basis of local taxation.

There shouldn't be many kind of direct impact on our numbers, but there's actually one which is related to the treatment of the investments in subsidiaries, because this was an item which had a different treatment under IFRS and local accounting standards: in each and every period when the exchange rates of the relevant currencies moved, we had a gain or a loss on the tax, because the tax was calculated based on the Hungarian numbers, and all the other elements of the financial statements were based on IFRS. Since we assumed so far that this difference was going to stay and was not going to be eliminated, therefore we had not created deferred tax liabilities for this difference.

In the third quarter we announced to the National Bank that we are going to switch to local IFRS accounting starting from January next year, because from next year there's an option to choose to introduce it early next year or wait for '18 when it's going to be compulsory for all financial institutions. We chose to do it earlier rather than later. Therefore we had to eliminate this difference in the respect of tax. As a result in the adjusted numbers we continued with the previous practice, i.e. making the treatment of the investment different under IFRS and

Hungarian accounting standards, therefore you saw this amount on page 18 being 2.3 billion gain on the tax shield of this item. At the same time we created a deferred tax liability which covers the entire cumulative impact of this tax liability and including the third quarter number it was HUF 7.5 billion negative. We created this 7.5 billion tax liability in order to be fully prepared for the change in the accounting standards by year end, consequently there won't be further net impact coming from this. Nevertheless, still in the fourth quarter if the exchange rates move, then you will see potentially an amount in the adjusted numbers and a similar amount with a different sign in the one-off or the adjustments. So that's really a technicality.

There's another issue we have to talk about, and this is the developments in Romania related to the mortgages. There were two recent developments. The first one was the "walk away" law which came into effect in May and has been criticised and amended by the constitutional court, therefore there will be changes in that legislation. More importantly, there was another legislation approved by the Romanian parliament on the 18th of October, and this is related to the conversion of all originally Swiss Franc originated mortgages to local currency at the exchange rate of the time of selling these loans. Now, what is quite controversial about this is that it also applies to those loans which have already been converted into local currency.

The government did not endorse this. The President didn't endorse it either, and the Governor of the Central Bank was against this legislation. The government sent it for a constitutional court review and it criticised certain elements of this, namely the fact that it also applies to those loans which have been already converted to local currency and the fact that the law doesn't have any kind of social implications and it does not target only those who are in a sort of social need of help. We don't know what's going to happen, but we believe that given the previous rulings of the constitutional court it's quite likely that they will amend this legislation as well, and some parts they will find unconstitutional.

Therefore we attach a potential low level of probability to this legislation to pass through as it is today. Nevertheless, there's a small chance that it is going to pass through as it is, and will be implemented. In that case we would have further losses. If it happened it would be a significant amount, but less than what we provisioned last year. Even calculating the exact number is difficult because it's a very short legislation and it does not detail exactly how the financial impact should be calculated.

We have not provisioned for this because our assessment is that it is a low probability event, number one. Number two, the constitutional court will deal with the case on the 23rd of November and we will know the results by the end of December, so in either case we will be able to close the books for this year properly reflecting the implications of this new legislation.

There was another event, or rather a non-event in the third quarter. The management team decided not to initiate the redeeming of two outstanding bonds which reached their redemption period, or optional redemption period. We have included the textual announcements which we made. I don't really have much to add to this.

Going back to the numbers and the details of our performance, total income increased as I said, on a quarter on quarter basis, which is I think quite an achievement in the current environment. Mostly it was due to volume growth. I'm going to talk about this in more detail. The growth came primarily from Hungary and from Russia. Going further, on page 22, you can see the net interest income. There was a tiny increase in Hungary which came already from volume growth basically. The margin was reasonably stable. And there was a slight negative impact in Ukraine where we made a change in the methodology of accounting for accrued interest. We stopped accruals in July and August and we are going to continue with this practice. Such step reduced interest income somewhat and also risk cost with a similar amount, i.e. we basically net out technically the two from now on.

In net fee and commission income, page 23, reflects quite a good increase, quarter on quarter +4%. In Hungary we had a 4% increase. This was due to growing number of transactions and therefore growing fee revenues. In Bulgaria there was a drop, but it was more due to the very high second quarter new corporate loan origination than anything else. And in Russia we had an increase which is related to the growing volumes. You will see that in Russia we finally started to slowly grow the volumes in consumer loans, and obviously the new production increased even more. There are fee revenues related to this coming primarily from the insurance commissions.

On page 24 you see other non-interest income. Also, one can see some slight improvement. In Hungary it was coming from higher FX gains. In Bulgaria it was slightly lower, but it's related basically to the swap agreement which DSK Bank concluded with OTP Hungary, so the opposite of this appears in Hungarian books. And in Russia there was a reclassification of the deposit protection fund contributions, it was a negative element in the other non-interest income. We took that out from there so it increased revenues altogether, and we put it into costs: costs increased with a similar number in the third quarter. So it's more technical.

Page 25 you see the margin developments. First of all, on the total group level, the margin went down somewhat. Four basis points, from 4.84 to 4.80 on the consolidated level, and here you can see where it came from. There was a very small decline in Hungary, just one basis point. A stronger decline in Bulgaria. Russia went down somewhat as well. This is more related to the exchange rate movement at the end of the third quarter than anything else. And in Ukraine there was a decline but this is mostly due to the fact that this methodological change which I explained reduced the accrued interest in the gross interest income and with the same amount the provisions as well.

Moving to volumes and talking about the loan to deposit ratio, that didn't change so much. We still have a very low level of leverage in Hungary and Bulgaria. Going to page 27, if we look at the first nine months development of the loan volumes, then overall we have a 2% growth on consolidated level. It mainly comes from Hungary and Bulgaria. So in Hungary we have 9% cumulative growth during this year, fuelled primarily by corporates. The corporate book grew by 12% and the consumer by 5% respectively. In Bulgaria, 5% growth, and here the most important driver is also the corporate sector.

If we go to page 28, then there are two points I would like to draw your attention to. One is the mortgage volume growth in Hungary. This is the upper left corner of this page. Hungary in the third quarter grew overall by 2%. Within this, consumer book increase was 2%, mortgage was zero and corporate was 4%. This is a big thing that mortgages did not decline further. This is the change which I used to talk about which we had expected to happen, and this is where for the fourth quarter we expect growth. Mortgages hopefully will turn into growth and be positive in the fourth quarter after stopping to decline in the third quarter.

The second important point I think is the Russian consumer loan growth which in the third quarter was 5%. Just to remind you, if you look back to the previous page, 27, you see that the nine months year-to-date growth was minus 8% and then within this the consumer book dropped by 8%, too. The good news is that the Russian consumer loan portfolio started to grow after two years of decline, so that's another turn in the trend of the loan volumes, and this is quite an important portfolio from the overall group profitability perspective. I think it's quite a good news and we're quite happy about this. And we believe that this is going to continue. It might even accelerate in the fourth quarter, which is the Christmas season and usually the strongest in each year for consumer loans sales in Russia.

If we go to deposits, not much has happened there. So the nine months cumulative change is 1%. That's okay. We are obviously not very keen on collecting more deposits as we are hyper liquid and the alternative rates at which we can invest these deposits are not very high.

Going to the cost slide on page 31, overall the second quarter was somewhat lower, but if you look at the nine months cumulative year on year change then it was nominally 2%, and if you adjust with the exchange rate then it was 4%. So 4% FX adjusted growth. Here you can see that, if we just look at the HUF figures, then the actual nominal growth was HUF 12 billion and HUF 10 billion nominal growth came from Hungary during the first nine months.

There is some explanation given here at the right upper corner. One is which we already told you, that from the beginning of this year there was a higher level of contribution to different protection funds: the deposit, investment and resolution funds, and that meant extra 2 billion in Hungary for the first nine months. And then there was this one-off cost of reorganisation in Hungary in 2Q, and we increased salaries by 4% as well, as wage inflation started in the country. These are more or less the reasons behind cost growth in Hungary. The other larger nominal increase came from Touch Bank, the Russian bank, which is the new internet bank what we have there. Obviously as we ramp up operations, sales costs started to increase, so this is not very surprising.

And now I'm going to say a few words as usual about the biggest markets. First comes Hungary. I already said a few words about the macro which we expected to further improve next year. If you look at the recent performance, on a quarter on quarter basis you see already somewhat improving revenues. Operating costs were lower, which is due to the fact that we had one-offs in the second quarter. The positive risk cost was somewhat lower, so overall that means it's somewhat higher. Depending from which point you look at it.

Looking at the business developments on page 33, you see that mortgage lending continues to be strong and it's growing on a year on year basis, new origination grew by close to 50%. New applications surged even faster, by 71% year on year. We have a quite robust market share at 29% from new contracts and new production. We have a strong market share in savings and an increasing market share in household savings despite the fact that we don't really pay much interest on deposits. In the corporate side, one can see positive developments. I already talked about it, that in the first nine months we had more than 12% growth in corporate loans, so this is the biggest driving force this year behind the loan growth in Hungary, and it's quite well balanced growth in corporate segment. Each sub-segment in corporates is growing with similar speeds.

As you can see here, the SME volumes grew by 12.7% in the first nine months, so this is even stronger than last year. Also, project finance is looking good and working capital lending is also strong. So in every front in corporate we are doing fine in terms of new developments and our market share is getting stronger and stronger. We are up to 14.4% market share in corporate loans.

Very briefly about Bulgaria. Bulgaria is doing quite well, stable. Here as well the corporate volumes were driving loan growth, and despite the fact that we have increasing sales in mortgages and consumer loans there, we also have early repayment so the portfolio growth is somewhat moderate. The risk profile of the portfolio is quite good and we managed to uphold the good profitability of the bank.

Russia, page 35, the driver of the much better performance this year is obviously the risk cost. You can see on page 35 the risk cost rates by the most important consumer loan segments: POS is down to 7.4%. Very importantly, credit cards were at 8.3% in the third quarter, which is quite a remarkable level compared to the fact that last year in first quarter it peaked at 25% and now it has moderated down to 8% level. Cash loans 7.1%, so these are very good numbers and they reflect levels which are achievable more or less in good years in the Russian market.

Volume growth is already visible in POS, whereas all the other segments decline, but if you flip one page to 31 here you can also see the new production volumes. In POS in the third quarter this year we sold 19% more than in the previous year. It's still lower than we had in the peak years of 2012 and 2013, but not so much lower. This is quite promising, especially if you take into consideration that during the third quarter consumption growth was still negative in Russia, so the turnaround in consumption dynamics has not yet happened in Russia. We expect that to happen at the year end, by the Christmas season. Real wages have already started to grow, but so far this has not turned into higher consumption. Again we expect this to happen soon, by the end of the year.

Also if you look at this page, that cash loan disbursements increased by 134%, more than doubled compared to last year, and also here we are getting closer to the previous good years' levels, and the only portfolio which lags behind in terms of portfolio development is the credit cards, but here we were quite conservative and we only started to sell credit cards during the summer. That's when we restarted the new production, but this is catching up as well.

Ukraine, the two biggest events which were happened in the third quarter in Ukraine I already talked about. One was this conversion of group funding to equity and the write-off of this investment and the realisation of the tax shield on this. The other one was the technical change in the accounting of interest. Other than that, the business is doing fine. We have a normal level of business activity which is quite profitable. Now we have a positive equity, at least by the end of this quarter we had a positive equity at the Ukrainian operation. It's around HUF 23 billion, and we will be able to calculate a meaningful return on equity which is going to be quite high. In the fourth quarter you will see that it's a very profitable business at the moment. But nevertheless, it is small within the total group, as you can see on page 38. It's less than 4% of the total consolidated performing loans what we have in Ukraine, but we are okay with this situation at the moment.

Going back to the kind of group level numbers and talk a little bit about the risk cost on the group level. We had a quarter with low risk cost rate and overall the risk cost was quite moderate as well. This was driven by the low level of deterioration across the group, and also there were write backs in Hungary which turned the Hungarian risk cost into positive territory. Coverage remained strong at 95%. There was a slow decline in the more than 90 days past due ratio, we hope this is going to continue.

If you go to page 40 you see the levels of portfolio deterioration in various countries. Ukraine was quite high compared to the size of the portfolio there. It's a portfolio already quite heavily provisioned which went finally into default, so it did not induce new provisioning requirements. It just went from restructured to actual default. More importantly, in Russia the nominal deterioration further decreased down to HUF 10 billion, and the rest of the portfolio has been quite stable during the last quarter.

Page 41, 42 further numerical details on the portfolio quality characteristics. On page 41 you can see risk cost rates by countries: write backs in Hungary, 0.4% risk cost rate in Bulgaria. Russia being at 6.7% which is, given that it's Russia, it's a very good number. And Ukraine went down to 3.3% as well. So we are overall quite comfortable with the risk cost.

That was pretty much the formal part of the presentation. I don't want to drag it longer. Please, if you have questions, ask them. Operator, please open the floor for Q&A.

Operator: To ask a question, please press star, one on your telephone keypad. To remove yourself from the queue press star, two, and please check you're unmuted locally. As a reminder that's star, one to ask a question. The first question today comes from Pawel Dziedzic from Goldman Sachs. Pawel, please go ahead.

Pawel Dziedzic: Good afternoon. Thank you for the presentation. I have two questions if I may. The first one is on your comments on the structurally lower cost of risk. You reported roughly 90 basis points, if I understand correctly, for the first nine months of the year and it comes partially on the back of write backs in Hungary. Could you please comment if you believe that those write backs could be still recurring in the next couple of quarters? And what would be outlook for your cost of risk if we look beyond this year, to 2017 and perhaps even beyond that to 2018 and so on?

And then I have a question on capital and how you think about your capital base currently. Your Core Tier 1 ratio you show very helpfully with recurrent items. With retained profits it would be over 15%. This is above the reference level of 12.5 that you use when you calculate your capital returns. You also showed that your leverage is above 12%, much above your regional peers. And obviously with a profitability you are easily able to cover your organic growth needs. So how should we think about your priorities when deciding on deployment of capital going forward? How much importance do you attach to M&A and how you think about your dividend policy going forward? Thank you.

Laszlo Bencsik: Thank you for the questions. Risk cost rate, I've been saying recently that we expect a structurally low risk environment in the coming years, and I also quite often say that this means that in certain quarters we might have negative figures. Or positive risk costs, especially in Hungary and Bulgaria where we have the highest levels of coverage. And this happened in case of Hungary in the second and third quarter. If you look back the last, I don't know how many years, but around 10, 15 years, then you can probably spot certain seasonality in the risk costs. At the year-end we usually tend to be hyper-conservative, even more than during the year, so when we will look at the portfolio at the end of the year. We will do everything to provision as much as possible under the accounting standards and regulations and try to be as prudent as possible. I don't know what it's going to mean, but this is usually the approach we have, and I don't see any reason why we should change it.

Regarding the long term run rate for the next couple of years, it's obviously hard to tell because it also depends on the composition. Namely, how big the Russian business is going to develop in the next couple of years. The Russian portfolio has a structurally different level of risk cost as you can see. Even in good years it's between 5% to 7% risk cost rate, which is structurally much higher than for the rest of the group. Obviously the profitability of these loans is much higher, as well. As a result, it does depend on the share of the Russian portfolio, and obviously depends on our ability to collect the non-performing loans in the countries where we have higher volumes, typically Ukraine, Hungary, Bulgaria. But overall something around 120 basis points is probably a good proxy for the next few years.

But take it into consideration that this is quite hard to predict, this is more or less the number which is the most probable expected average. But variations can be big, and honestly, we don't know what is going to happen exactly to that numerical level. However, I think the consensus is quite strong that if you look at the macro situation of these countries then they look strong and growing and there's not much overheating there in the countries where we are present. That's why I think it's quite safe and fair to say that for the next couple of years, three to five years, it's going to be in general a low risk environment.

Capital is a question which comes back all the time, and I always have the same answers. I'm not in a position now to give you a long term capital plan or strategy. I've been telling that we are going to revisit the capital strategy somewhere second half of next year when we more or less see what we could acquire or not. We have made it clear that acquisitions are a priority and we are pursuing a number of opportunities at the moment - only in the countries where we are present. The primary aim is to strengthen our market position and achieve a scale which provides the required level of profitability in the countries where we don't have that. These are the primary targets, but we also consider acquisitions in countries where we are bigger, like Hungary, that was the place of the most recent acquisition of the AXA portfolio.

We will see how much we can buy and to which extent it uses the excess capital what we have. What I can also tell is that we stick to the dividend guidance, and the number which we put aside for dividends which we pay after 2016 is HUF 53.2 billion. That's the expected amount of dividends to be paid out. It's exactly 15% nominal growth compared to the previous year dividends. So that's all I can tell. I mean, we pay this dividend and we try to do acquisitions which create value for shareholders. We believe that this is the time to do that because now we more or less foresee what's going to happen in these markets for the next couple of years and it looks quite positive, with decent growth, low risk. At the same time asset valuations are still in the region which seems to be meaningful and these are much lower levels than what we saw before the previous peak, before the crisis. So that's pretty much the answer. I know this doesn't satisfy you entirely, but that's what I can say at the moment.

Pawel Dziedzic: That's very helpful, thank you. And maybe a very minor follow-up. What would be the capital impact of AXA consolidation?

Laszlo Bencsik: It's basically the capital requirement coming from this 162 billion, so you have to…

Pawel Dziedzic: Okay…

Laszlo Bencsik: So 35% risk rate and then you…

Pawel Dziedzic: 35%. Okay. Perfect. Very clear. Thank you very much.

Laszlo Bencsik: Sure.

Operator: The next question today comes from Gabor Kemeny from Autonomous Research. Gabor, please go ahead.

Gabor Kemeny: Hi. Thanks for the presentation. The first question is on loan growth on the Hungarian mortgages. You showed that the mortgage origination has increased a lot, and this is now enough to keep your mortgage book stable. And when you say that you expect positive growth in the fourth quarter, do you assume a further increase in new origination? So do you think you need significantly more new loan sales to grow the book? And if yes, where do you think it may come from?

My second question is on the Tier 2 bonds which you decided not to call just at the first call date. I was wondering what's your thinking around this. Would this not be just a reasonable way to reduce your funding costs? I mean, to call these issues. And I wondered to what extent could your decision have been driven by MREL, so would these Tier 2 bonds qualify as bail-inable debt under MREL?

And my third question is on the NBH's three month facility which is now being phased out. You mentioned that you have quite a big portfolio, 760 billion in these three month instruments. And this is now being phased out. So how would you reinvest these amounts? Would you expect a drag on your NII from switching these to overnight deposits? Or do you see other, better options to invest?

Laszlo Bencsik: Okay. So mortgage growth, fundamentally it's coming from increasing demand and more new originations. Obviously there would be a one-off technical impact, but I was not referring to this. Due to the AXA portfolios there will be a step up in the overall volumes, but this is not the reason why I told that we expected growth. It's because we expect increasing demand and increasing originations in mortgages.

These two bonds which you referred to, they are both Tier 2 capital elements recognised by the national bank, and we need Tier 2. Their current pricing is actually much lower than a newly issued Tier 2 paper would be, so we don't see an opportunity here much to reduce the cost of Tier 2 capital elements. The MREL thinking has not been included into this, so that was not the reason.

Gabor Kemeny: Sorry, just to follow up on this, but do you actually need these? I understand this is cheaper than a new issue, but do you actually need this additional funding? I mean your liquidity position is so comfortable.

Laszlo Bencsik: We do need Tier 2 capital elements, because in the current regulation there's a room for it. You can provide the tier two elements from tier one capital, but that would be too costly. Yes, we do need Tier 2. In an efficient capital structure, you do have Tier 2 capital elements.

Gabor Kemeny: Okay.

Laszlo Bencsik: Your third question related to the liquidity, what we keep at the central bank and the decline of this. By the year-end we expect that the amount which we can deposit at the central bank at the base rate will be around HUF 200 to 250 billion, so that's the amount of HUF liquidity we can keep at the base rate. Everything above that either goes to the interbank market, and there we will have the interbank rate as a yield. The interbank reference rate recently moved below the base rates, it was 78-80 basis points, while the base rate is 90 bps. And the reference rate might go lower.

The other option is that we buy Hungarian sovereign bonds or we find other investment opportunities for this liquidity. The overall need for this type of placement will be less than the 700 billion what you mentioned, partially because we pay back some and also we have loan growth and so on and so on, various factors having influence on our short term liquidity. There will be another, let's say HUF 200-250 billion by the year end and beginning of next year for which we have to find a better place to allocate for than to keep it in the overnight.

Gabor Kemeny: Okay, and what would be your first impression? Would this have a significant impact on your NII? Or either way?

Laszlo Bencsik: It depends on our decision what to do with it. If we buy government bonds, then it will improve our NII, because government bonds have higher yields. If we don't, then it might have a slight negative impact.

Gabor Kemeny: Okay, thank you.

Laszlo Bencsik: Now that you asked this, I think here it's much more important how the reference rate of our variable rate loans move. Most of the loan book we have is variable rate; the reference rate is the interbank rate (BUBOR), not the base rate. We expect the interbank rate to move away from the base rate as it has already happened to some extent, and therefore it can happen that we have the same base rate what we have today, but the reference rate goes lower. That's actually a bigger problem that the reference rate which is the basis for all our variable loans can go lower than the base rate and this can create further pressures in the margins. That would have bigger impact than the other one which is just how much we can get for short term liquidity we place at the central bank.

Gabor Kemeny: That's useful. Can you give us any sensitivity on this? What could be the impact on your net interest income from lower interbank rate?

Laszlo Bencsik: On an annual basis, ten basis points difference in the interbank rate is roughly two basis points in the NIM. HUF 1.5 billion annually.

Gabor Kemeny: Okay. All clear. Thank you.

Laszlo Bencsik: Sure.

Operator: The next question comes from Simon Nellis from Citibank. Simon, please go ahead.

Simon Nellis: Thanks. Just a follow up question on one of the questions asked before. Can you just confirm that you said the normalised cost of risk should be 220 basis points? Is that what you said?

Laszlo Bencsik: No. No, sorry, I wasn't articulating right probably. It's 120 basis points.

Simon Nellis: 120. Okay, good. I had a bit of a shock. My question would be on the Ukraine. First the sub-debt that you converted to equity, what was the interest rate on that sub-debt and which division was it showing up in? And I guess I realise that converting to equity has no impact for the group, but I guess it…

Laszlo Bencsik: It wasn't a sub-debt. It was senior and it was short term. So it had a quite low interest rate, 2% or 3%. So it won't drastically change the profitability of the Ukrainian entity.

Simon Nellis: Where was the interest income on that loan being shown in the divisional reporting?

Laszlo Bencsik: Ultimately in Hungary. So the cost was in the Corporate Centre, and then there's a funding going from the bank to the Corporate Centre as well. Primarily it was in the Corporate Centre.

Simon Nellis: Okay. And on the Hungarian margin, I guess it sounds like there will be some pressure coming from, well I guess this but also from the lower reference rates. I mean, can you give us some guidance on how you see margin in Hungary developing over the next quarter and over the next, I don't know, next year if possible.

Laszlo Bencsik: Again, as I said, if you look at the sensitivity to the reference rate, a ten basis points decline in the reference rate would mean roughly HUF 1.5 billion decline in NII. Honestly, I don't know how low the reference rate can go. The base rate is 90 basis points and the current reference rate is 80.

Simon Nellis: Okay.

Laszlo Bencsik: It's up to you to decide. Maybe it goes down to 70, 60, I don't know. It's going to be volatile for sure, so that's something for sure. But this is roughly the magnitude, right?

Simon Nellis: And I guess loan growth next year you're hoping will offset some of the margin pressure.

Laszlo Bencsik: Yes. Yes, definitely. In a good scenario this should happen.

Simon Nellis: Thanks. My last question will just be on risk cost in Russia. I mean it's been quite volatile. It's come down nicely. Where do you think that that goes longer term? I mean, is it going to stay at the third quarter level or is that not the right level in your view?

Laszlo Bencsik: This is the level which represents a normal level of operation in Russia. The ratio itself can technically get better: if we have loan growth and if the denominator is growing fast, then it can technically bring the ratio, the risk cost rate lower. But the fundamental deterioration of the portfolio, in other words the migration from bucket to bucket what we see, this is pretty much what we used to see in good years a few years ago when we had very high levels of profitability. So, this is already a situation we are quite happy with.

Simon Nellis: Okay. Sorry, just one last question. Do you expect any change to resolution and deposit insurance costs next year? Or do you expect them to stay reasonably stable versus this year?

Laszlo Bencsik: No.

Simon Nellis: Okay, thank you.

Operator: The next question comes from Stefan Maxian from Raiffeisen Bank. Stefan, please go ahead.

Stefan Maxian: Yes, hello, thank you. Just a few questions. First you talked about Hungary wage inflation of about 4% for this year. What is the number that you would think is a good figure for next year on that? Second, looking at the Hungarian NII, we have seen from the split retail actually going a bit weaker versus on the Treasury it's stronger. What was the reason for that? Was it about this BUBOR reference rate drop as a rationale for that? And then maybe if you could share a little bit more on the earnings impact of the AXA portfolio, so in terms of NII from the AXA portfolio, operating costs, that would be helpful. And maybe finally on the CSOK programme, if you could let us know what's the current overall volume of CSOK loans and what is your market share at the moment. Thank you.

Laszlo Bencsik: Okay. Starting from the back, i.e. CSOK. We have roughly 50% market share, and the subsidy which we distributed so far, since the beginning of the programme, has been HUF 21 billion. We are close to 50% of the total market. The AXA impact on OPEX should be relatively minor. The NII is slightly lower than our average NII of the HUF portfolio in Hungary, but only slightly. Loan growth in Hungary next year. Well, we haven't given specific guidance for that. It's likely to remain single digit, but certainly higher single digit that we see this year. And then you had a question which I didn't fully understand. The line was not correct. It was retail and Treasury revenues?

Stefan Maxian: Yes, when we look at net interest income on Hungary Core, we see that the NII trend in retail is going down from 39.5 to 36.3, whereas in Treasury ALM we have a plus of roughly 4 billion.

Laszlo Bencsik: I have to look into this. We'll come back to you on this, okay?

Stefan Maxian: Okay. And maybe… What I was asking, not about loan growth in Hungary but about the expected wage growth for next year.

Laszlo Bencsik: The wage growth? Sorry. I'm sorry. The real wages growth we have on page 8. I mentioned 3.8% for the real wages growth. And that's for the market. Inflation is expected to be 2.2-2.3%. So that would mean nominally 6% wage growth on average for the market. This is not OTP Bank. So we haven't reached a decision about our wages for next year.

Stefan Maxien: Okay. Thank you.

Laszlo Bencsik: Sure.

Operator: The next question comes from Margarita Streltses from UBS. Please go ahead.

Margarita Streltses: Good afternoon, thank you very much for the presentation. I have a couple of questions left. Can you elaborate a little bit of what's going on with margin trends in Russia? Because we've seen some funding cost improvement but I don't think we've seen a reflection of this in the margin trend. And also can you maybe explain a little bit of what was driving this provision recoveries in Hungary? Was it just basically non-performing loans turning into performing which allowed the release of provisions? And whether you think we can see some similar trends in Russia. And my last question, just to follow up on the dividend question. I didn't really understand, do you expect the payout ratio to remain flat until the decision on acquisitions is made? Or if this is wrong, if you can correct me on this. Thank you.

Laszlo Bencsik: Sorry, the line is not perfect. Probably it's a problem on our side. So I haven't fully understood your questions, sorry, but the first one was margins in Russia. The margin itself is very much depending on the exchange rate, because the way we calculate the period denominator is this period beginning and period end and the average, and if the exchange rate moves then it can have a big impact on the margins. So if you look at the NII, the NII increased in Russia in the third quarter slightly from 22.899 billion HUF to 23.029. But nevertheless the net interest margin moved lower, but this is related to how the denominator is calculated as an average and it's calculated from HUF numbers. When the exchange rate moves it creates some distortion. If you look at the net interest income, it increased. And the other two questions, sorry, can you repeat them? I didn't get them.

Margarita Streltses: The second question was about the provision recoveries in Hungary. What's driving that? Whether it's just non-performing loans which are coming back to performance or how are those generated? And whether we can see more of those in other countries.

Laszlo Bencsik: They come from every source. We do work out and then we have recoveries from work out. The real estate sector is doing quite well, so recoveries on the defaulted in-work-out mortgages are getting better. We recovered on certain corporate exposures in the third quarter. This comes from various sources, and from time to time these can bring the risk cost into positive territory. If you look at the coverage ratios, it's basically Bulgaria where similar events can and might happen in the future.

Theoretically it can also happen in Ukraine, but I don't quite expect that. For that we should see further strong improvement in the environment and therefore in the ability of our clients who have been restructured or who have been defaulted to improve, or appreciation of the value of the collaterals and so on and so on. It can happen in Ukraine, but honestly this is not something I expect. But, in Bulgaria maybe. Bulgaria can behave in the future somewhat similarly to the situation in Hungary. In other countries the coverage ratios are not so high, and by the way the amounts in default nominally are much smaller as well, so even if this happened in the other countries, it wouldn't have a huge impact on a group level.

And then finally Russia where we have larger number of NPL volumes there, the probability of this type of improvements or write backs is quite unlikely there. It's a very fragmented consumer loan portfolio with small amounts. It behaves very statistically and the provisioning can therefore be very, very precise. Therefore in Russia I don't expect similar things to happen. And then you had a third question. Sorry…

Margarita Streltses: Yes. The third question was just a follow up on the dividend, because I didn't really understand when you were saying that there is not much clarity you can provide until you make a decision on potential acquisitions, but you said the dividend will stay as it is. Do you mean like a payout ratio will stay as it is? Or if you can just explain a little bit more.

Laszlo Bencsik: We said that we were going to pay HUF 53 billion after this year next year, and this is what you can see in the numbers. If you look at the analyst tables there's a line which shows this number, the amount which we put aside on a quarterly basis as the expected dividend payment. That was what I said. This suggests a 15% yearly increase. The expected dividend payments for this year is 15% higher than last year. That's what I said. A longer term dividend policy, that's an area which depends on the level of acquisitions we can make in the foreseeable future, and we will come back to this question somewhere in the second half of next year.

Margarita Streltses: Okay, thank you very much.

Laszlo Bencsik: Sure.

Operator: The next question comes from Danny Anson-Jones from Morgan Stanley. Danny, please go ahead.

Danny Anson-Jones: Hi, I was just wondering what your outlook is for loan yields in Bulgaria, given deposits have repriced to practically zero. Thank you.

Laszlo Bencsik: It's going to continue to decline. If you look at the quarterly decline which you have seen during this year, there will be potentially lower levels, diminishing levels further ahead, but it's going to decline.

Danny Anson-Jones: Thank you.

Operator: As a final reminder, to ask any further questions please press star, one on your telephone keypad. It appears we have no further questions.

Laszlo Bencsik: Okay, thank you very much. Thank you for attending this conference call. Thank you for your questions. I wish you all the best, a very nice weekend, and hopefully see you on the next conference call when we will discuss the annual results on 3rd of March next year. So thank you again. Bye-bye.

Note: unabridged transcript with minor English stylistic corrections.