Strategy and Finance Division

Investor Relations & DCM

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Transcript

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P R E S E N T A T I O N

Operator

Dear ladies and gentlemen, welcome to the OTP Bank First Quarter and Full Year 2021 Conference Call. This conference will be recorded. May I now hand you over to László Bencsik, Chief Financial and Strategic Officer. Laszlo, please go ahead.

László Bencsik – Chief Financial and Strategic Officer

Good morning or good afternoon, depending where you are, and thank you very much for joining us today on OTP Group 2021 fourth quarter and annual results presentation and Q&A. Thank you that you dedicate your precious time in these turbulent times of today, especially. As usual, we have this presentation on the website available. Also, since we are doing it through Zoom app, we can hopefully see it on the screen as well.

As usual, I will go through it, but rather briskly because I'm sure most of your interest today is not around what we did last year. However, performance was exceptionally good last year, but most of our attention is now on the tragic events in Ukraine and especially the ramifications in Russia. This is where I'm sure most of your attention and certainly our time and effort has been spent during the last 2 weeks. I will try to do my best to give you an update. We have a modest number of slides on this, only one in this package, but if you have questions, I will elaborate more on the situation as of today in these 2 countries.

Starting the usual part of the presentation, Page 2 highlights our result last year. The 60% after-tax adjusted profit increase is due to 2 factors: very strong operational performance, 23% year-on-year operational profit growth; and the moderation of risk costs after the spike in risk costs, what we had in 2020 due to the COVID situation. These numbers are not distorted by acquisition so much because we did not acquire anything last year. There was only a divestiture back in 2020, our small Slovakian bank, so pretty much these numbers provide you a good reflection of what happened.

Really terrific year, I would say, last year, very strong volume performance. You will see that our performing loans grew 15% year-on-year. The margin started to level up and normalize. Even if you look at the fourth quarter figures, net interest margin increased on group level, that had not happened for long years. Now we have a quarter where there was an improvement in the NIM.

Capital position is highest ever. We have 16.9% common equity Tier 1 ratio at year-end. This was boosted by the sale of treasury shares: during the fourth quarter, we had a transaction where we sold around 4.5% of our treasury shares to an entity owned by employees. Liquidity is equally strong, the group level loan-to-deposit ratio is 75%. In Hungary alone, we are sitting on more than EUR 9 billion equivalent of liquid assets. Last year, deposit growth rate was higher than loan growth rate. Deposits grew at 16%. Given that there's 75% loan-to-deposit ratio, we generated a lot of excess liquidity last year.

Going through some of the details, you can see the overall consolidated accounting profit and the differences what we make as adjustments, the usual item is the bank tax. We had a very specific situation in 2020 and 2021 with the payment moratorium, especially in Hungary, due to which we had to book a loss and make the accounting adjustment. This reflects the time value difference of the cash flows because we do get back the cash flows which were suspended during the moratorium. The only difference is that it comes later in time.

These were one-off adjustments last year and in 2020, which we gradually drive back into NII. There are some costs related to the mergers and the previously accounted for PPAs in case of acquisitions, which we have to amortize. This is the number what you see here. Typically, the merger process after the acquisition takes 1 or 1.5, 2 years. We put here the costs related to the merger and the post-merger period. If we have a post-merger project, we typically put the additional cost of the projects on this one.

If we look deeper into the adjusted profit, what you saw on the first slide reflects back here as well. Very strong, 23% growth in operating profit - with some adjustments to make it an apple-to-apple comparison it is 19%, with 13% income growth and again, with proper adjustments, 8% operating expenses. The revenue growth is quite strong, especially in the fourth quarter. What we saw last year was a quarterly acceleration in revenue growth, which was a good development.
If you look at the entity results one by one, across the board there is improvement. It's not surprising, the economic environment last year was much better than in 2020. Some numbers stand out, especially in Serbia, where we finished the merger and now we started to reap the benefits of the new unified entity, that is performing very well. Croatia was particularly strong, as were Bulgaria and Romania. In Romania there is an interim period when the focus is not so much on growth and profitability because we are executing the organic growth strategy. We continue that.

Ukraine and Russia did incredibly well last year, and this makes it for us even more sad and regrettable that these recent events seem to have a very strong negative impact on the earnings potential of these entities.

We can go to Page 7 now, to net interest income. It shows a strong growth quarter-on-quarter, especially in Hungary, where roughly HUF 7 billion was a result of an ALM transaction, which had one lag here, another lag in other income. If you net the two, the impact was slightly positive. Keep in mind, that part of it was not business-related but technical. It is important to note that despite the profit improvement in Russia last year, revenues, net interest income went down year-on-year because of lower margins of the operation.

If we go to Page 8, we can see the margin. After so many years of declining margins, we had the fourth quarter last year showing some improvement, strongly boosted by OTP Core. As I indicated, part of it is technical, so it's not going to stay with us. Nevertheless, it's positive, and there's some improvement, which we're quite happy about.

Volume-wise, fourth quarter was strong, with 4% growth. I would say strong across the board, especially in Russia and Ukraine. Finally, Russia started to grow. For quite a long time, I was explaining the difficulties we had in terms of our strategic positioning. The fourth quarter started to show signs of some life in terms of volume development. Ukraine was extremely strong. As was the rest of the group. With all of this, we ended up last year with 15% group level performing loan growth, which is exactly what our last guidance was. If you remember, after the third quarter, we said that we expect around 15% and it was exactly 15%. Hungary was very strong, with 19%, consumer lending, housing loans, corporate segment all expanded. There were some bolstering by the moratorium. There's a technical uplift on the growth rate, 3 percentage points in Hungary and 1 percentage point group level due to the fact that we had high participation level in payment moratorium, that had a positive technical impact here. But even without that, it's quite an outstanding result. Ukraine grew more than 40% last year, showing very strong overall economic performance.

If we go further, you see the deposit growth, and perhaps it's better to look at the annual rate, that was 16%. Deposit growth was up HUF 3 trillion, almost HUF 1 trillion more than loan volume growth. Our deposit to loans liquidity gap increased on group level and some countries were exceptionally strong, especially Hungary.

For several years, we could not do much with deposits because of the very low yields. But in fact, with this higher rate environment, we started to make considerable money on deposits. We're happy to see this deposit increase because it shows the level of satisfaction of our clients with the services of the bank. We started to make serious money on deposits, especially in Hungary, which was not the case for many years. So, we're particularly happy about this development.

On Page 13, you see the net fee income. There are 2 events, which technically moved the numbers down and up. The downward was the usual one-off payment, what we have to pay for cashbacks, refunds for credit cards. We always account for this in the last quarter. It came in as well in Hungary, and almost all the quarter-on-quarter decline is explained by that. The other quarterly development is the Fund Management success fee. They did a good job last year, so they got a success fee, but on a year-on-year basis, as in 2020 they performed even better, there's a year-on-year decline in the success fee.

Overall, the net fee income growth was strong last year. That's a reflection of strong increase in economic activity and increasing inflation, that have an impact on fee income as it is related to transactional activity. And transactional activity is typically related to nominal GDP growth. So, it's not surprising we had such a good year, especially because 2020, the base, was weak due to the first waves of COVID, when there were serious restrictions.

Other income. As I mentioned, there's a technical other gross lag of the ALM position closing and changing during the fourth quarter. That's counterbalanced by revenues shown in interest income. Other than that, it is the Others line, which was strong. We included a couple of entities into the consolidation. We have a travel agency in Hungary, and we were quite happy that the private equity division of OTP, called PortfoLion, started to show very good results. We have strong contribution to profits coming from this activity, which was presented in the numbers last year.

We have other entities which we consolidated back at the beginning of last year. We have these revenues shown in other income and costs in the operational cost line. That, too, you have to net out in order to get to meaningful numbers. Part of these others growth was due to gross representation of some activities, which we recently consolidated.

Operating costs: in Hungary, we had a relatively strong year-on-year cost growth, but part of it was due to some technical changes or accounting methodology changes. We increased the provisions for untaken holidays, assuming that everything will be taken out. We also increased provisions for expected anniversary bonuses: every 5 years, we pay out 1 month extra bonus to employees who stay with us long. That will be reflected better in our books and that resulted in a one-off in the fourth quarter.

Even without that, we had a 9% year-on-year cost growth in Hungary, which reflects the high inflationary environment last year and the tight labor market that we have, furthermore the strong IT and digital developments, which are always costly.

The good thing is that in some countries, like Bulgaria, we continue to realize, as you can see from the year-on-year number, the long tail of cost synergies. Serbia and Montenegro started to provide cost synergies. These are the countries where we have recently completed mergers. Romania had a rather high cost growth, that is related to the organic growth strategy. On the Others line, you see this technical impact, the negative lag of these other activities, which have some costs.

A few words about Hungary and the acquisition in Hungary, and our home market. It remains strong, and we achieved strong year-on-year numbers. Especially cash loan market share improved a lot year-on-year. We were quite happy with our relative performance, not just the absolute performance last year. Again, importantly, the household savings market share continues to be stable and strong.

As you can see on the next chart, we have remained very active in distributing policy subsidized structures in Hungary for retail clients. These are products with very decent profitability and the market share tends to be higher than in case of some of our other products. These subsidized products have our strong focus. We always strive to have them available for our clients who want to get these products when they are available on the market. We also strive to make the availability of these products very convenient and easy to use for our clients. That's also the reason that we have a much higher share.

The Green Home program is the most recent subsidized housing loan product, that started in October last year with the aim to improve the homes' energy-efficiency. It's very, very popular. We continue to be very active on this front.

In terms of corporate, last year was exceptionally good. You can see our corporate loan market share improvement in terms of year-on-year growth, we went up from 16.6% to 18.6%. On this chart, you see the long journey and where we started, back in 2008. This is really a redefinition of our footprint and profile in the Hungarian corporate business, and I am happy to see that it's a very strategic move.

The good performance was also supported by being strong in servicing the subsidized schemes coming from the Central Bank. Such were the Funding for Growth Go! program - which is discontinued, but was still strong last year -, and the newly introduced Széchenyi Card Go! structure, which is an attractive SME-targeted, working capital loan structure.

On Page 19, you see the year-end status of the moratorium. Moratorium was restructured, the last phase started in October, where clients had to apply for the continuation of the moratorium. Surprisingly, participation rate dropped substantially, indicating that the payment moratorium is not a structural element anymore. It's still existing, and it's going to expire end of June 2022, but it's no longer a factor that would strongly influence numbers or something which should be taken into consideration.

In terms of development, we have a few slides about digital. Obviously, COVID19 was very difficult and had negative ramifications, but one aspect where it was, at least from a banking point of view, positive, was that clients increased or accelerated their usage of digital channels. In 2 years, we more than doubled the number of regular users of the mobile banking application. It's not just the customer usage profile, which shifted, we also substantially renewed our services. Last year, we launched our new Internet and mobile banking system, which is a completely new platform, developed in-house, offering a graphically different client or user experience. So far, the feedback is overwhelmingly positive.

ESG became strategic for us last year, and it was a very concentrated high-level management effort to structure this Group initiative into a solid, well represented organizational structure and detailed strategy with very specific actionable initiatives that should drive our performance on this front for the future. There's a lot of commitment and drive in the organization for achieving these goals and to continue to improve in that front. This was a big push from us. Hopefully we will soon see further improvements in our ratings and what we do will be reflected by these objective measures, as well.

Last year had good profitability, high nominal profit growth, strong volume growth, strongest ever capital position and strongest ever liquidity position. On top of that, we maintained our more conservative provisioning approach, maybe more conservative than some of our peers, as you can see, especially in case of performing loans. Stage 1 and Stage 2 loans we continue to provision as a percentage of the volumes. The volumes that we have are considerably, 2-4x more than that of some of our regional competitors. Last year we did not release the provisions that we created due to additional conservatism in 2020 when the COVID situation started, we kept this higher level of provisioning.

A few words about capital and the common equity Tier 1 ratio development. We see the requirements here, that increased year-on-year. We have this other systemically important buffer, which used to be 2% prior to 2020. When COVID hit, it was reduced to 0%. In 2020-2021, it was 0%, and now it started to increase gradually: this year, it's 0.5%. Next year it will be 1% and will go back to 2% in 2024. Our SREP ratio or Pillar 2 ratio also increased to 125%, as opposed to the 117%, which we used to have for a couple of years.

So much about last year. I will now attempt to give you a review of the situation in Ukraine and Russia. We were really shocked by what happened. It seems unbelievable that something like this could happen and such tragic and large war can break out in Ukraine. Obviously, the situation is not easy at all.

We have colleagues there who heroically maintain the operations of the bank. Services are available. Whenever a branch can be opened, given the security considerations of our clients and employees, they open the branch. Roughly half of our branches are open. Cash transactions are available. There are certain daily limits for local currency and foreign currency cash withdrawals established by the Central Bank. Obviously, lending activity froze. Online Internet banking is on and we -- as much as we can -- do everything to service our clients there.

It is however positive that deposits, in fact, grew, retail deposits increased. As you can see on this chart (page 25), from 23rd of February when the war started until 3rd of March, there was 4% increase in deposits. Even yesterday, we had an increase in deposit volumes.

We try to do everything to continue to provide for our colleagues in Ukraine who are working under very difficult conditions. Also, we do everything we can as an institution, and as individuals to support also the people who decided to leave Ukraine. There's a large number of refugees already entering the country, and we do our best to support them.

In terms of Russia, the operational situation is not under so much pressure. We operate all our branches as usual. There too, retail deposits are growing since 23rd of February. Lending activity is very limited. First, we stopped and then we restarted our POS lending activity very selectively. At the moment we do provide some POS loans. The previous restriction, the APR cap was released, so we provide these POS loans at a much higher rate than we used to. The capital regulations were somewhat eased, so the risk weights for our POS and cash loans were reduced, yet are still much higher than Europe or other parts of the world. There is a considerable excess capital buffer in the bank. RUB 7 billion release of capital requirement happened just because of this, in the last couple of days.

What makes operations difficult in Russia, is the financial intermediary sector. We are a primarily retail bank there, where we do have a small treasury, and it's very difficult to maintain the treasury operations with a central bank which only selectively or partially functions, and basic instruments are not fully available. It is a difficult year and involves extra cost to manage the small treasury portfolio. That's the operational challenge at the moment in our Russian business but we cope with the situation.

If you look at the financials, it's worth to calibrate the size of our exposure to Ukraine and Russia. On this slide (page 25), you can see every important metrics. One of the most important one is the share from the Group profits last year, which was 15%. In case of a situation where we are unable to conduct business in these 2 markets, this is the potential profit stream, which we may lose. It is also important and interesting to know that if we were unable to sustain our operations and then had to deconsolidate and write off the operations and the group funding in these 2 countries, the impact on our capital, common equity Tier 1 capital ratio would be 27 basis points for Ukraine and 116 basis points for Russia.

We don't fund the banks in these countries. In Ukraine we provide funding to the leasing entity there, and the bank keeps dollar deposits in OTP Hungary. On the chart, you can see the gross and the net amounts, the end of February figure was HUF 9 billion net, but the gross number is certainly bigger than what we provide to the leasing company. That HUF 75 billion was included when we calculated the 27 basis point loss. So, that amount was calculated in the assumption that this gross funding will be lost. In terms of Russia, there's no net funding, the gross and the net is the same, it's HUF 52 billion equivalent.

Basically, that's the situation today. We do have some more exposure to Russia and Ukraine outside the country. We have some sovereign bonds. We have on year-end and exchange rate basis HUF 88 billion equivalent of Russian sovereign bonds in Hungary and HUF 13 billion equivalent of Russian sovereign bonds in Bulgaria. These are longer maturity instruments; the maturities of these bonds are between 2025 and 2028.

We also have some clients across the Group who have exposure to Russia and Ukraine, however relatively moderate. There is around EUR 500 million funding or exposure to clients who have strong business connection with Russia, they either source their raw materials from Russia or they export to Russia. This portfolio we consider to be at risk.

We have very few clients, maybe 1 or 2 who have strong exposure to Ukraine but that's a much smaller amount. There's a potential spillover effect of the situation in Russia and Ukraine to other countries where we operate. That is obviously much more difficult to assess and calibrate. It depends a lot on what the outcome of this tragic situation is going to be.

The obvious development is the increasing inflation. We already see energy and food prices further increasing, especially grain prices. Ukraine is a large producer of food stuff. So, we should expect a higher inflationary environment this year -- even higher than in prior years, and that might have an impact on the economic environment in the countries we're in.

Regarding guidance: we did well on what we promised last year. The ROE, we said would be between 18% and 20%. It ended up 18.5%, with a conservative provisioning. We indicated 15% growth of loans, and it indeed grew 15%. We started the year, with around 10% guidance and then we gradually increased it. We ended up 15%. This year is obviously difficult. We plan to share more concrete expectations with you, but the last 2 weeks changed a lot in this sense.

We would not dare to exactly pinpoint what the end game is going to be in Russia and Ukraine, we simply don't know, and the range of potential outcomes is huge. So, we decided not to try to quantify the potential outcome other than showing you a very bad scenario in the previous page for the case of losing these operations and writing off the funding to these countries altogether as a one-off.
The question is what happens to the rest of the Group. The range of different scenarios is relatively big. Therefore, I don't think it's very responsible to tell what the numeric expectation and the most important indicators are for this year, even for the rest of the Group. We consider the best approach to be to start from a status quo situation. Assuming that there's no material or negative impact on the other countries where we operate, we would expect a similar year to last year. The only difference is a somewhat less loan growth, coming from a) non-moratorium; b) higher interest rate environment, which in some cases, especially in corporate lending, may slow down loan growth.

Regarding margin, we started to see some stabilization last year, and we believe that this is going to continue. We expect the margin environment to stabilize and normalize. Regarding all other indicators, our initial expectation was somewhat similar to last year in terms of risk cost rate and operating cost efficiency ratios. If all these manifested, we would have similar return on equity and profitability ratios and overall nominal improvement in profits.

I'm afraid this is not going to manifest like this. Even if there's a peace agreement and truce made today, a lot of harm has been done. If there's no agreement today, more damage will be done tomorrow. Day by day, more physical and structural damage is done. Therefore, there will be negative ramifications for the rest of the countries. How much and exactly where, is hard to tell.

If we look at the structure of the economies OTP Group countries, excluding Russia and Ukraine, the economic links are surprisingly small. Typically, from the exports of these countries Russia and Ukraine have between 1% to 3% share. There are some exceptions, like Moldova and Montenegro, for instance, but for the rest of the OTP Group countries, it's typically between 1% to 3% of their exports, which are directed to Russia and Ukraine.

The impact coming from the loss of direct trade to these countries is going to be potentially moderate. Again, there are some countries, especially Moldova, we are quite concerned about. This is a country we recently entered, albeit with a quite small exposure and activity. Nevertheless, we see strong geopolitical risk and large dependence on especially Ukraine and of course Russia in terms of economic activity.

Overall, sanctions, disruption and/or redirection of supply chains, potential losses of other players with exposures to Russia, higher cost of energy and food, and therefore high inflation, etc. point to a direction of negative impact on the economic development of the countries where we operate. Therefore, I'm afraid we are not going to have exactly as good results as we show on this slide.

Once we know the resolution or the lack of resolution of the situation, we are going to be able to quantify much better what we should or can expect and do a new budget for this year.

I'm sure you are interested about the dividend. We have HUF 119 billion, which we promised many times to pay out. We would like to pay this amount after 2019 and 2020. We still have not decided on whether or not and how much dividend we should suggest to the AGM to pay after 2021. We are going to have a Board of Directors' meeting in 2 weeks, where we will carefully assess the developments related to Russia and Ukraine. Based on that assessment we are going to formulate our proposal to the AGM. I think it's fair to say that it's quite likely that at least the HUF 119 billion will be suggested to be paid.

The last slide is about the usual disclaimer, which is especially important now because we don't know what the outcome of this situation is going to be.

So that was the formal presentation. I'm sure you have questions, and I hope I will be able to give you answers. Please, open the floor for questions from the participants.

QUESTIONS AND ANSWERS

Operator

The first question is from Máté Nemes, UBS.

Máté Nemes – UBS Investment Bank

Thank you for the presentation and thank you for sharing details on Russia and Ukraine, including operations, indirect exposures and so on. That's very helpful. If you don't mind, I would start my questions first still with Russia and Ukraine. I'm just wondering if you could share your thoughts on what developments or what change in the environment made you conclude that you cannot operate in these countries anymore? What would be these conditions?

The second question is still related to that. I think the Chairman and CEO, in the morning, during the press conference mentioned that OTP's long-term role in these countries but wouldn't take the risk of substantial additional exposure in these two markets. I'm just wondering if you could clarify what exactly that substantial additional exposure would mean? Would you be willing to put in smaller amounts of additional intragroup funding? Or would you be even willing to recapitalize these businesses if need be?

The last question is on your inorganic expansion strategy. Do you expect an extended pause in line of acquisitions or an outright stop of the expansionary strategy? In light of this, if you could give us an update also on the potential acquisition in Uzbekistan, that would be very helpful.

László Bencsik – Chief Financial and Strategic Officer

There are scenarios both for Ukraine and Russia, where it's not our decision what we do. Due to sanctions either by EU or by Russia, we can basically become unable to operate. This happened in Ukraine in 2014, when Crimea, Donbas and Luhansk regions were taken. We were not allowed to conduct any business activity in these parts of Ukraine. We had to write off every exposure day 1. It can happen due to EU sanctions, that we will not be allowed to operate in Ukraine. I hope this is not going to be the case because that obviously assumes a tragic outcome to this situation.

I think we have to face the reality that this can happen. In Russia, either from the side of the EU or from the side of Russia, the relationship can deteriorate further, that's also a possibility. I hope it won't and I don't know how to rationalize this, but I still see hope for a peaceful solution. There would be so much to gain for both countries from that solution and obviously, rest of the world.

We have to face the relationship between the EU and Russia, which can deteriorate to a level where either because of the EU or because of Russia we are not going to be able to operate there. These are relative in terms of our decisions because we don't have really a choice if that happens.

If there's a peace agreement tomorrow and that peace agreement is recognized by the EU and internationally, then miraculously everything can turn to very positive. We are obviously very happy to continue operations in both countries. These are the 2 extreme scenarios. In between, there are many other scenarios which are very difficult to quantify and describe or pinpoint.

In Ukraine, we have a relatively small leasing, local currency corporate banking and consumer lending business. We don't have any mortgages. If banking is possible in Ukraine and there's some meaningful economic activity, not to mention, if there is a peace agreement, then we are happy to continue in Ukraine. If you look at last year, Ukraine really started to grow on a sustainable and very promising path. That makes it even more sad and tragic what happens now.

Recapitalizing Ukrainian operation depends on the environment. We would obviously not like to do that, but there can be a situation where you want to do it. If there's a tremendous growth opportunity and the situation, the status of Ukraine is clear, there's full international support for Ukraine, and we see a large growth and value creation potential, it can be a situation where we would be quite happy to actually increase or recapitalize. But there can be other situations where it's just obvious that we do not trade but destroy value.
The situation is nothing like that. Our bank is very liquid. Actually, liquidity improves. Our bank is very well capitalized. The local capital common equity Tier 1 ratio is, if we include last year profits, 17-18%. There's no indication that capital or liquidity would be needed now. Likewise, in Russia, we don't have a single client on the sanction list. We provide core business, 80% of the loan book is subprime consumer loans.
We don't do mortgages. We do it in local currency. We have a smaller corporate business and an even smaller treasury. Even in harsh and difficult economic environment, this is usually a sustainable business. We have seen

difficult environments in both of these countries. We continue to operate. In case of Ukraine and Russia, we don't see any reason to be concerned about potential capital needs or liquidity needs because, as I just said, basically 1/3 of the balance sheet in Russia is equity. The risk rate for our POS loans used to be 388%. It was reduced to 191%, but it's still twice as much as we have in Europe, or the standard rate. The cash flows used to be 338%, that was brought down to 310% risk weight. Just this change released RUB 7.5 billion equivalent of capital in the entity excess capital.

It's very difficult to see a scenario where we actually have to increase in the foreseeable future capital or liquidity. Liquidity is improving. We have deposits coming in. It's hard to answer this question because in short term, there doesn't seem to be any need to put there any capital or liquidity. If things start to improve and there is an agreement and settlement and there's a bright future, then we have to put there capital because we are growing and we believe in the future, and then I think that can happen.

If we had to put in capital, because all of a sudden the Russian regulator will decide to double our capital requirements in order to force us to increase capital despite the fact that there doesn't seem to be any need for capital increase, that would be a different situation. Then we would consider it a hostile environment. So far, at least by the Central Bank and authorities in Russia, we have been treated fairly. We don't see any negative discrimination compared to locally owned banks. I guess that's as much as I can say about this.

M&A strategy. We have signed commitments to buy the Slovenian bank and the Albanian bank. We are going to proceed on our contractual agreement subject to regulatory approval, which we are still waiting for. These 2 are still likely to happen during the second quarter. Albania is interesting because they don't need any energy. The electricity is generated from hydropower and they seem to be, as much as possible, isolated from this situation in Ukraine and Russia.

Slovenia, not too much exposure.

Uzbekistan, honestly, we haven't thought about that last 2 weeks. In Uzbekistan, there's no agreement yet. We continue discussions, negotiations, but in the last 10 days, this was not the highest on our priority list to think about. I don't have an answer to that. But there's no commitment whatsoever there.

Máté Nemes – UBS Investment Bank

Okay. This has been very helpful. If I could just have one more follow-up related to capital in Russia. You mentioned that one hypothetical scenario where you would not be committed to recapitalize would be a regulatory imposed one, should risk rates double or increase significantly. What about the situation when loan losses increase very significantly and then perhaps that would start eating into capital. What would be your thinking in that scenario?

László Bencsik – Chief Financial and Strategic Officer

We would have to make a decision. That decision will be based on the future potential of the business and the amount which has to be committed and the environment in which locally and internationally, the Russian banking sector operates.

Operator

The next question is Hai Thanh Le Phuong, Concorde Securities.

Hai Thanh Le Phuong – Concorde Securities

Just a couple of questions from my side. The first one would be on a happier topic. I was wondering if you could repeat your Hungarian interest rate sensitivity now and I am curious whether it changed compared to your last call. Or is it the same considering the higher levels where you are now? Also, if you could tell us your expectation on Hungarian loan growth for this year, obviously, assuming no material harm stemming from Ukraine and Russia.

My second question would be: you mentioned during your press conference, that you may be interested in Sberbank assets. I was wondering if this is only true for Hungary? Or would you consider other operations in the region as well?

My third one, if you could repeat your Russian bond exposure, that would be helpful because I wasn't following.

László Bencsik – Chief Financial and Strategic Officer

The interest rate sensitivity or our earnings sensitivity to the rate environment, now, that the BUBOR is about 5 and the 2-week-deposit rate is about 5, the best guess is that it's close to 0. We don't expect further gains from further increases because deposit prices will start growing as well.

In terms of loan dynamics in Hungary. We shared with you the 10% Group average. Without Russia and Ukraine, in our initial or original budget for this year, Hungary was somewhat higher, in lower teens. It's likely that the events going to have a negative impact on the potential loan growth.
I am hopeful that we still can do at least 10%. Sberbank is gone. It went into default, into administration. I think it was yesterday or 2 days ago. They are bankrupt in Hungary; the deposit insurance fund is going to pay to depositors. It was a retail and SME bank. A large share of the deposits will be compensated and paid from the deposit insurance fund. It's over now here. I think in Croatia all of their assets were either sold or discontinued. In fact, this was, at least the Hungarian event, triggered by the liquidation of the Austrian holding company.
That triggered at least the collapse of the Hungarian entity because the Hungarian entity had its liquidity in the Austrian holding company, which also used to be a bank, and that went under administration first and they didn't pay back the deposits. That triggered a large capital loss in Sberbank Hungary, and they went default. It's a small entity. Still obviously painful and it didn't come at the right time, but it's over now.

Hai Thanh Le Phuong – Concorde Securities

Okay. On your Russian bond exposure, again, in total?

László Bencsik – Chief Financial and Strategic Officer

Outside Russia, we have HUF 88 billion equivalent calculated with year-end exchange rate in our Hungarian books and HUF 13 billion equivalent in our Bulgarian books. We have some in Russia as well, but it's in the Russian bank.

Operator

The next question is from Gabor Kemény, Autonomous Research.

Gábor Kemény - Autonomous Research

One other question on Ukraine. Can you remind us if there are any credit and capital forbearance measures in place in Ukraine? If there are, do these Ukrainian and the Russian forbearance measures you mentioned, do these impact your Group consolidated financials? Or are these just relevant for the local entity?

Then the other thing is on the crisis again. Can you comment on the refugee situation? I mean we see broadcasts. We hear anecdotes about many refugees arriving to Hungary and some neighboring countries. I wondered how this may impact the economic environment and the business environment for OTP.

Finally, a bit technical one on NII. You may have mentioned this, but an impressive growth in Hungary in 4Q. I think you are flagging that half of this came from a swap result. Was this a one-off actually?

László Bencsik – Chief Financial and Strategic Officer

In Ukraine, the February loan repayments and interest payments were delayed to March. In a way, it's an overall moratorium service on every credit. I don't know how long it's going to be the case, but so far, it's just 1 month. In Russia the only thing I'm aware of system-wise, is that they put a 3-year moratorium on foreclosures, but we don't have any mortgages. So, it does not apply to us, but it applies to those banks who have mortgages.

I'm not aware of any policies regarding restructuring, so we have not applied any. In Russia, life seems to go on, right? The sanctions so far have had a very immediate and direct impact on the financial intermediary sector: the stock exchange, central bank, clearing house, basically treasury, special money market instruments. But so far, the real economy impact is, at least from our perspective, related to our client service side, especially our retail business – we are a fundamentally a retail bank –, so, our retail clients have not experienced any shock because our loans are in local currency.

In fact, now the base rate is 20% and the better clients have lower than 20% consumer loan rates. We don't see worsening in delinquencies and collection as usual. Yesterday, we looked at the daily collection numbers and portfolio quality numbers, and so far we haven't seen any deterioration in the Russian business.

In terms of NII, fourth quarter, maybe I wasn't clear enough. In Hungary, we closed some of the ALM positions and swaps, and they had a small positive impact, but the accounting was in a gross way. We had a positive NII and a negative in other income. If you look at the magnitude, roughly HUF 7 billion. This is a one-off. If you net the two, then it's somewhat positive, a few hundred million positive.

You should look both on NII and other income in Hungary, fourth quarter, you can see NII went up. Half of that increase was due to this transaction. Then you see a drop in other income and most of the drop, HUF 6 billion, was related to this. If you net the two out, it's less than HUF 1 billion gain on that. It was a one-off. It creates a somewhat bigger movement in these 2 lines. But if you net the two together it's somewhat positive, but a rather small number.

Refugee situation, we have already more than 100,000 refugees from Ukraine who entered the country, roughly 20,000 per day. There's a very strong effort and a lot of activity going on to try to help these people and this is done by the government, by NGOs and by individuals. I personally, we accommodated 2 Ukrainian families. Typically, families mean a mother and kids because men between age of, I don't know, 18 and less than 60, so the military age, are not allowed to leave the country. We typically have women and children coming. A lot of people are trying to help and a lot of people are actually going to the border because one problem is that they don't have transportation.

It's basically housing and transportation. These are the first 2 immediate needs. There is a broad response from the society and from the government to do as much as we can. As far as we understand, most of these people don't intend to stay. They either want to go further west or obviously, they would love to return because, typically, these are, again, not full families and I don't know what the implications will be.

We are focused on providing as much help as possible. The bank itself is providing housing for the refugees and putting together a financial support package to help them. So that's our focus at the moment. There are Hungarian-speaking people living in Ukraine and I think a big share of those who so far entered the country are coming from that part of Ukraine, the Western part immediately bordering Hungary. For them, it's much easier to work in the country or to settle if they wanted to.

For those who don't speak Hungarian, it's not a very easy language long term. They are more than welcome. From a practical business point of view, one of the biggest problems structurally in Hungary is the decreasing demographics. If the f skilled labor increases, it's potentially positive. But this is a side consideration, and certainly, that's not what we are thinking about now. We are thinking about how much we can help as organizations and as individuals. Again, most of the people I know either helped or actually accommodated people, refugees from Ukraine at the moment.

Gábor Kemény - Autonomous Research

That's a very commendable support effort.

Operator

The next question is from an attendee joined via phone. (Operator Instructions)

Andrzej Nowaczek – HSBC

Hello. It's Andrzej Nowaczek of HSBC. Laszlo, what would you say the difference is between the 2014-2015 situation in Russia and Ukraine and the current situation, what could be in terms of impact be on OTP financials? I mean, I guess, more likely to be more severe now than then, right, but possibly also a bigger impact of the Russian business than 8 years ago. I wonder whether you agree.

László Bencsik – Chief Financial and Strategic Officer

Certainly. I mean, it depends on what the outcome is going to be. Certainly, the magnitude of damage so far has been much higher in Ukraine than in 2014-2015. Then, it was very local in a way or contained in certain parts of the country. If you expect or if you assume a negative scenario that this is going to continue and there's no resolution, which is globally accepted by all the parties involved and not involved, then obviously, this is going to have a much bigger effect and longer-term effect.

We tried to present the potential financial implication of a scenario like that. On the other hand, this is how this situation is going to be resolved, which has been there unresolved for 8 years, and still, I think there's a chance for everything to turn for better. Let's say there's a ceasefire tomorrow, and then the parties agree and a peaceful resolution is achieved, and Ukraine can continue to grow in all parts, so every territory involved will have a legal status acknowledged and accepted internationally, it could create a much better growth platform for the country or the countries involved.

I don't know how remote that option or possibility is given the current situation. But if you believe in that scenario like that, then it could even improve, right? Then the outcome should be not as bad as it was in 2014-2015. But again, I don't know how much hope we can put into that scenario. What happened so far is much worse obviously. The magnitude of the war is incomparably bigger than what was happening in 2014. Then also the sanctions on Russia are more -- a couple of magnitudes bigger -- than they were or rather, which were introduced in 2014-2015. So, in that sense, this is certainly a worse situation.

Operator

The next question is from an attendee who joined via phone.

Robert Brzoza - PKO PB Securities

Hello. This is Robert Brzoza from PKO BP Securities. Can you hear me?

László Bencsik – Chief Financial and Strategic Officer

Yes. Loud and clear.

Robert Brzoza - PKO PB Securities

Great. It's on the cost of risk guidance that you had given for 2021, of course, without considering Russia and Ukraine. You expect more or less the same cost of risk in 2022 as in 2021. Here goes my question, because to my understanding, if 2021 was burdened with a one-off related to the extension of moratoria which I would be expecting to reverse at some point once the moratoria expires, so does it imply that taking this into consideration, you actually expect on the remaining portfolio some deterioration in the provisioning outlook?

Secondly, if you could comment very briefly on the leasing subsidiary in Hungary, where you were making, I think, NPL sales, et cetera, which was also on Hungary factoring unit where we've seen in the past a positive contribution to the cost of risk, because as I understand from the report, this has changed regarding 2022 outlook.

László Bencsik – Chief Financial and Strategic Officer

The risk-cost rate of last year was 30 basis points. If you take out Russia and Ukraine, it was 19. I don't think this is high, even plus and minus on the moratorium-related provisioning because, indeed, that's the case. We had to provision extra in fourth quarter for those loans that remained in the moratorium after the last extension because those clients declared that they had payment problems. We had to worsen the stage buckets they were in and that created the one-off provisioning. In fact, we expect the opposite in the second quarter this year, where we hopefully will be able to take out clients who can participate in the moratorium and who pay regularly for 6 months. We will reclassify them to Stage 1 and we'll certainly use a one-off release.

That's one technical impact, which we expect. The other one is what you referred to, is that at the end of last year, we made another revaluation of the book value of the portfolio, which we have at Factoring and we had to do a one-off provision release and increase the book value of these loans in accordance with the methodology expected by our new auditor. Now the consensus is that it is where it should be. We still expect positive risk costs coming from these portfolios, but not in a way of one-offs. There won't be any more year-end one-off on that line.

Now having said that, I think this is similar to last year, which means, in this case, without Russia and Ukraine, slightly less than 20 basis points. I think it's rather optimistic. The war started last week. Since then, we haven't made a new budget, and we focus on other operationally pressing issues.

The way how we phrase it, is assuming that the conflict doesn't exert a material negative effect on the rest of the Group. If you believe that this is the case, then I think it's fair to assume that we are going to have 19-20 basis points risk cost for the rest of the Group. Then it depends on your view on how much negative ramification rest of Europe, not just the countries where we operate, actually undergoes or suffers due to this special situation what we have.

I don't think it's going to be 0. I think it's already clear that it's going to be negative. Higher energy and higher food prices and higher inflation is expected. It's fair to assume that at the end, we will have somewhat higher than 20 basis point risk cost for the rest of the Group because the economic environment is less favorable. It should be somewhat higher.

Don't take these lines and these statements, which stand here as guiding information, they are based on an assumption which we don't know to which extent holds. I think we will have to wait to be realistic. We could tell that it's going to be X and Z and Y, but I don't think it would be very responsible to do that. Once we know the type of resolution to the situation in Ukraine, and we know the parameters of operation for us for the rest of the year or even longer, then we will be able to make probably better assumptions and forecast and how it's going to have an impact on our numbers.

Operator

The next question is from Siva Natarajan.

Siva Natarajan – GW&K Investment Management

This is Siva Natarajan from GW&K Investments. Thanks for your candid views on everything. Just a follow-up on exposures. What are you seeing in terms of risks in the interbank markets in the countries that you operate in? Two, can you talk about your exposures in the derivative market like swaps, both direct and indirect to Ukraine and Russia?

László Bencsik – Chief Financial and Strategic Officer

There are no swaps in Ukraine. Since 2009, they just don't exist. In Russia, we have a local money market treasury book, which requires roughly USD 200 million equivalent of position. As of today, this is declining fast, but we have to finance that position, but this is done locally, 100% locally. We already closed the counterparty swap relationships with Russia. What we do have still is this line of funding, which is not to the bank actually, that's just loan, which goes to this SPV from which we issued the high NPV, high APR loans. This SPV is owned by the Group. It's not owned by the Russian bank. We have less than USD 40 million subordinated loan to the bank.

Siva Natarajan – GW&K Investment Management

What are you seeing in terms of the interbank funding in the different countries? Any risks developing there? I know you said Sberbank Hungary went bankrupt. Are there any impacts because of that? Not just that, but are you seeing risks develop because of potential further bankruptcies?

László Bencsik – Chief Financial and Strategic Officer

We have not had exposure to Sberbank Hungary or other Sberbank entities. I think it's a very specific situation. The listing was discontinued, I think, yesterday. But before, it was discontinued, the Sberbank GDRs in the London Stock Exchange were around 10 cent. I don't think it's a surprise to the subsidiary of an entity, which is in that situation, troubles. I am not certain, the resolution Board who conducted the solution for the Sberbank group, international group, I don't know how much coordination was done there and how much consideration was done given the countries, which were involved.

From my perspective, I don't see much coordination mostly. I said, the trigger for the case of the Hungarian entity was actually that the Austrian entity was discontinued. I don't see any other banking group or local bank having similar type of problem. We don't have any other, as far as I know, Russian owned commercial banking activity in the countries where we operate. I'm not sure about Western Europe. But certainly, in the countries where we operate, Sberbank was the only Russian-owned active commercial bank.

In the meantime, my colleagues tell me that we did have some exposure, which is under the local one, but it's a low single-digit million euro figure. So, it's not a big one. It's under settlement now with the local Sberbank. I think this is an isolated event with Sberbank International. I'm not sure it was managed perfectly. But I guess the reason is that it wasn't systemic in any of the countries where it operated. Therefore, essentially less regulatory or resolution focus was provided.

I don't see any other financial institution or bank having similar type of challenges at the moment. I hope it's not going to cause further events. At least I don't see anything in the countries where we operate.

Operator

The next question is from an attendee who joined via phone.

Jovan Sikimic – Raiffeisen CENTROBANK AG

It's Jovan from Raiffeisen. Can you hear me?

László Bencsik – Chief Financial and Strategic Officer

Yes, I can hear you very well.

Jovan Sikimic – Raiffeisen CENTROBANK AG

Perfect. Good. Great. Just one follow-up. If you could please repeat the exposure to corporates which are doing business to some extent with Russia. I think you mentioned the number earlier, but I somehow missed it, please. On the group level.

László Bencsik – Chief Financial and Strategic Officer

Okay.

Jovan Sikimic – Raiffeisen CENTROBANK AG

And the second one, if I may, on Slovenia, on the introduction of this controversial Swiss franc law. I think Nova Credit already announced some negative effect, but what would be, let's say, joint effect, including your current operations? And of course, maybe with this, is there any chance to adjust the pricing for Nova Credit now because of that?

László Bencsik – Chief Financial and Strategic Officer

Okay. So, exposure, I said, was around EUR 500 million. That's across the Group. This is the exposure to clients with substantial relationship, 90%-95% Russian, either exporting to Russia or sourcing from Russia.

Jovan Sikimic – Raiffeisen CENTROBANK AG

Is it however maybe more for -- okay.

László Bencsik – Chief Financial and Strategic Officer

Sorry?

Jovan Sikimic – Raiffeisen CENTROBANK AG

Is it may be like higher allocation, I don't know, in Bulgaria or Serbia compared to other group members, right?

László Bencsik – Chief Financial and Strategic Officer

It's evenly distributed. Yes, Serbia, to some extent. But it's everywhere. We don't consider them high risk exposures. It doesn't mean that all of these loans will have serious issues. It's just that, that's the exposure to clients we have, with exposure to Russia. It's not tremendously concentrated anywhere. It's across the board.

Again, as I said, it's quite surprising now that we look deep into the numbers, in terms of export, it's between 1% and 3%, which is to Russia and Ukraine. 2 exceptions are Moldova and Montenegro. In Montenegro, it's almost 8%-9%. They export pharmaceuticals to Russia. They have a lot of incoming tourists from Russia and Ukraine, ca. 25% of the tourists. I'm not sure whether that number is going to go up or down or if they will switch to being permanent residents. But these are the 2 countries. Moldova has also Russian gas dependence. The Russians increased there over the winter last year, the cost of gas 2.5 times, so they already have problems.

Regarding NKBM, we are very much on, we have not yet closed the deal, but we are considered competitors. We are competitors still. We only know what they have publicly announced roughly between EUR 45 million and EUR 50 million one-off loss coming from the Swiss franc problem. Ours is much less, less than half, based on our current estimate. As far as I know, there's no contractual opportunity to reflect this in the price of the asset.

Operator

As there are no further questions, I hand back to the speaker.

László Bencsik – Chief Financial and Strategic Officer

Thank you again for joining us today. Thank you for the very good questions you had. I'm sorry that I could not necessarily answer everything with a level of detail. But the situation is so fluid and difficult to foresee what exactly the settlement and the situation will be that I think we have to wait somewhat to see how exactly it's going to play out.

But certainly, we are doing our best to help wherever we can and to maintain the operations as much as we can. I wish you all the best, good health and, hopefully, see you or have you on the confcall, which we are going to do in early May. In between, we are going to have the AGM on the 13th of April. So, very much hopeful that most of you who are representative of investors here will come and vote on the AGM. Until then, thank you again, and goodbye.

Note: unabridged transcript with minor English stylistic corrections.