MOODY'S
INVESTORS SERVICE

Rating Action: Moody's takes multiple rating actions on Hungarian covered bonds

29 Sep 2021

Madrid, September 29, 2021 -- Moody´s Investors Service ("Moody´s") has today taken the following rating actions:

- Upgraded the mortgage covered bonds issued by OTP Jelzalogbank Zrt. (OTP Mtge Bk) ("OTP" or the issuer) to A1 from A2

- Upgraded the mortgage covered bonds issued by UniCredit Jelzalogbank Zrt. ("UniCredit" or the issuer) to A1 from A2

RATINGS RATIONALE

Today's rating actions on Hungarian covered bond programmes follow Moody's raise of Hungary's local currency and foreign currency ceilings to A1 from A2, which in turn follows Moody's upgrade of Hungary's sovereign rating to Baa2 with a stable outlook from Baa3 with a positive outlook on 24 September 2021. Covered bond ratings are constrained by the local currency and foreign currency ceilings; consequently, the raise of the ceiling to A1 has resulted in upgrades for the two covered bond programmes that we rate. For more details on the rationale for the sovereign rating change, please refer to the press release: http://www.moodys.com/viewresearchdoc.aspx?docid=PR_454087 .

Following the upgrade of Hungary´s sovereign rating, the Counterparty Risk (CR) Assessments of the two covered bond issuers were upgraded. For more details on the rationale for the upgrade of OTP, please refer to the press release: http://www.moodys.com/viewresearchdoc.aspx?docid=PR_454827 . For UniCredit, at the request of the issuer, the CR assessment is not published.

For OTP Jelzalogbank Zrt. (OTP Mtge Bk) - Mortgage Covered Bonds and UniCredit Jelzalogbank Zrt. - Mortgage Covered Bonds the covered bond ratings are at the local-currency bond ceiling in Hungary of A1.

The upgraded covered bond ratings benefit from OC consistent with their new rating levels.

KEY RATING ASSUMPTIONS/FACTORS

Moody's determines covered bond ratings using a two-step process: an expected loss analysis and a TPI framework analysis.

EXPECTED LOSS: Moody's uses its Covered Bond Model (COBOL) to determine a rating based on the expected loss on the bond. COBOL determines expected loss as: (1) a function of the probability that the issuer will cease making payments under the covered bonds (a CB anchor event); and (2) the stressed losses on the cover pool assets following a CB anchor event.

The CB anchor for OTP Jelzalogbank Zrt. (OTP Mtge Bk) - Mortgage Covered Bonds and UniCredit Jelzalogbank Zrt. - Mortgage Covered Bonds is CR assessment plus 1 notch.

The cover pool losses are an estimate of the losses Moody's currently models following a CB anchor event. Moody's splits cover pool losses between market risk and collateral risk. Market risk measures losses stemming from refinancing risk and risks related to interest-rate and currency mismatches (these losses may also include certain legal risks). Collateral risk is derived from the collateral score, which measures losses resulting directly from the cover pool assets' credit quality.

For OTP Jelzalogbank Zrt. (OTP Mtge Bk) - Mortgage Covered Bonds and UniCredit Jelzalogbank Zrt. - Mortgage Covered Bonds, Moody's has lowered its refinancing margins and raised both TPI´s to Probable from Improbable. These adjustments are supported by a combination of factors that have lowered refinancing risk for Hungarian covered bond programmes, including: (i) the improvement of the Hungarian economy as reflected in the upgrade of the Hungary´s rating to Baa2 from Baa3, (ii) the near term implementation of the EU directive on covered bonds, which will reinforce strengths of the Hungarian covered bond law, and (iii) the systemic importance of covered bonds in Hungary.

The cover pool losses for OTP Jelzalogbank Zrt. (OTP Mtge Bk) - Mortgage Covered Bonds are 31.2% with market risk of 25.1% and collateral risk of 6.1%. The collateral score for this programme is currently 9.1%. The over-collateralisation in this cover pool is 27.7%, of which the issuer provides 0% on a "committed" basis. Under Moody's COBOL model, the minimum OC consistent with the A1 rating is 0%. These numbers show that Moody's is not relying on "uncommitted" OC in its expected loss analysis.

The cover pool losses for UniCredit Jelzalogbank Zrt. - Mortgage Covered Bonds are 32.4% with market risk of 25.8% and collateral risk of 6.6%. The collateral score for this programme is currently 9.8%. The over-collateralisation in this cover pool is 6.1%, of which the issuer provides 0% on a "committed" basis. Under Moody's COBOL model, the minimum OC consistent with the A1 rating is 0%. These numbers show that Moody's is not relying on "uncommitted" OC in its expected loss analysis.

For further details on cover pool losses, collateral risk, market risk, collateral score and TPI Leeway across covered bond programmes rated by Moody's please refer to "Covered Bonds Sector Update", published quarterly.

TPI FRAMEWORK: Moody's assigns a Timely Payment Indicator (TPI), which is our assessment of the likelihood of timely payment of interest and principal to covered bondholders following a CB anchor event. TPIs are assessed as Very High, High, Probable-High, Probable, Improbable or Very Improbable. The TPI framework limits the covered bond rating to a certain number of notches above the CB anchor.

RATING METHODOLOGY

The principal methodology used in these ratings was "Moody's Approach to Rating Covered Bonds" published in September 2021 and available at https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBS_1284753. Alternatively, please see the Rating Methodologies page on www.moodys.com for a copy of this methodology.

FACTORS THAT WOULD LEAD TO AN UPGRADE OR DOWNGRADE OF THE RATINGS:

The CB anchor is the main determinant of a covered bond programme's rating robustness. A change in the level of the CB anchor could lead to an upgrade or downgrade of the covered bonds. The TPI Leeway measures the number of notches by which Moody's might lower the CB anchor before the rating agency downgrades the covered bonds because of TPI framework constraints.

The TPI assigned to OTP Jelzalogbank Zrt. (OTP Mtge Bk) - Mortgage Covered Bonds is Probable. The TPI Leeway for this programme is 3 notches. This implies that Moody's might downgrade the covered bonds because of a TPI cap, if it lowers the CB anchor four notches all other variables being equal.

The TPI assigned to UniCredit Jelzalogbank Zrt. - Mortgage Covered Bonds is Probable. The TPI Leeway for this programme is unpublished.

A multiple-notch downgrade of the covered bonds might occur in certain circumstances, such as: (1) a country ceiling or sovereign downgrade capping a covered bond rating or negatively affecting the CB Anchor and the TPI; (2) a multiple-notch downgrade of the CB Anchor; or (3) a material reduction of the value of the cover pool.

REGULATORY DISCLOSURES

For further specification of Moody's key rating assumptions and sensitivity analysis, see the sections Methodology Assumptions and Sensitivity to Assumptions in the disclosure form. Moody's Rating Symbols and Definitions can be found at: https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_79004.

Moody's did not use any stress scenario simulations in its analysis.

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Moody's general principles for assessing environmental, social and governance (ESG) risks in our credit analysis can be found at http://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_1288435 .

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