

Rating Action: Moody's takes rating action on Hungarian banks

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Action follows the downgrade of the Hungarian government debt rating to Baa3

London, 07 December 2010 -- Moody's Investors service has today taken rating actions on the debt and deposit ratings of eight Hungarian banks to reflect the rating agency's reassessment of the country's capacity to support its banking system following the downgrade of the Hungarian government's rating to Baa3 from Baa1, which was announced yesterday, December 6. Further, Moody's lowered to Baa3 from Baa1 the country's ceiling on foreign currency bank deposit ratings; this has caused a more pronounced downward adjustment to the foreign currency deposit ratings of the three highest rated banks. Moody's notes that today's rating actions are not driven by a change in the agency's view on the Hungarian banks' intrinsic financial strength, which is captured in the banks' stand-alone bank financial strength ratings, the BFSRs. These ratings remain unchanged.

The rating actions on the affected banks are as follows: OTP Bank (the local and foreign currency deposit ratings downgraded to Baa2 and to Baa3, respectively); OTP Mortgage Bank (the local and foreign currency deposit ratings downgraded to Baa2 and to Baa3, respectively); K&H Bank (the local currency and foreign currency debt ratings downgraded to Baa1 and to Baa3, respectively); MKB Bank (the local and foreign currency deposit ratings downgraded to Baa3); Erste Bank Hungary (the local and foreign currency deposit ratings downgraded to Baa3), MFB Development Bank (the foreign currency deposit and debt ratings downgraded to Baa3) and Budapest Bank (the foreign currency deposit rating downgraded to Baa3). Moody's has also confirmed the deposit ratings of FHB Mortgage Bank at Baa3/Prime-3 with a negative outlook.

Please see below for a full list of the affected ratings.

RATINGS RATIONALE

The downgrade of the Hungarian government's rating has prompted Moody's to lower its assessment of the capacity of the Hungarian government to support its banking system, consistent with the change in the sovereign debt rating. Moody's utilizes a 'systemic support indicator' as the anchor to measure a country's capacity to support its banking system in case of need, and this is used by Moody's to assign the supported deposit and debt ratings of banks.

Hungary's systemic support indicator remains positioned one notch above the national government's debt rating. The rationale for maintaining the country's support indicator above the government rating -- despite the government's weakened fiscal position -- incorporates the range of (financial and nonfinancial) tools that could be deployed by the Hungarian government and the country's central bank to assist banks in case of need.

Moody's notes that today's rating actions are not driven by a change in the agency's view on the Hungarian banks' intrinsic financial strength, which is captured in the banks' stand-alone ratings, the BFSRs. Moody's added, however, that the BFSRs of all the Hungarian banks currently have negative outlooks, reflecting concerns regarding the development of their credit strength, in a continuing difficult operating environment. These negative outlooks have been in place since mid-2009 and will be resolved within the coming few months.

Moody's noted that a key vulnerability influencing the current negative outlook of the Hungarian banks is their high level of foreign currency lending (70% of total loans are denominated in a foreign currency), with many borrowers, particularly in the retail sector, being unhedged with respect to the currency risk on these loans. As a result, there is significant vulnerability to a depreciation of the Hungarian Forint, or to an increase in interest rates linked to these foreign currencies. More generally, Moody's noted that asset quality continues to deteriorate in Hungary and said that it will assess the extent to which this trend continues.

Conversely, Moody's acknowledged that the Hungarian banks are relatively well capitalized, providing a cushion to absorb potential losses. Further, Moody's credit assessment of the Hungarian banks also benefits from a high level of foreign ownership -- 80% of the Hungarian system, measured by assets, is foreign owned. The foreign owners of Hungarian banks have so far provided support in terms of both capital and foreign currency liquidity through the crisis of recent years and, at present, there is no evidence that this support would not remain forthcoming. Of the eight banks rated by Moody's in Hungary, four are foreign-owned (K&H Bank, MKB Bank, Erste Bank Hungary, Budapest Bank). Despite the downward adjustment in the country's systemic support indicator, the deposit and debt ratings of these banks continue to receive significant uplift from Moody's assessment of parental support. Moody's, however, cautioned that it will continue to assess the likely level of parental support. The difficult operating environment and more modest profitability may at some point render further investment in Hungarian banks less attractive to their foreign owners.

The specific rating changes implemented today are as follows:

OTP Bank

- Local currency long-term deposit ratings downgraded to Baa2 from Baa1
- Foreign currency deposit ratings downgraded to Baa3/Prime-3 from Baa1/Prime-2
- Foreign currency senior unsecured debt rating downgraded to Baa2 from Baa1
- Foreign currency subordinated debt rating (Lower Tier 2) downgraded to Baa3 from Baa2
- Local currency short-term deposit rating confirmed at Prime-2

All the above ratings carry negative outlook and the rating action concluded review for possible downgrade.

OTP Mortgage Bank

- Local currency long-term deposit rating downgraded to Baa2 from Baa1
- Foreign currency deposit ratings downgraded to Baa3/Prime-3 from Baa1/Prime-2
- Local currency short-term deposit rating confirmed at Prime-2

All the above ratings carry negative outlook and the rating action concluded review for possible downgrade.

K&H Bank

- Local currency long-term deposit ratings downgraded to Baa2 from A3
- Foreign currency deposit ratings downgraded to Baa3/Prime-3 from Baa1/Prime-2
- Local currency short-term deposit rating confirmed at Prime-2

All the above ratings carry negative outlook and the rating action concluded review for possible downgrade.

MKB Bank

- Local currency deposit ratings downgraded to Baa3/Prime-3 from Baa2/Prime-2
- Foreign currency deposit ratings downgraded to Baa3/Prime-3 from Baa2/Prime-2
- Foreign currency senior unsecured debt rating downgraded to Baa3 from Baa2
- Foreign currency subordinated debt rating (Lower Tier 2) downgraded to Ba1 from Baa3

All the above ratings carry negative outlook and the rating action concluded review for possible downgrade.

Erste Bank Hungary

- Local currency deposit ratings downgraded to Baa3/Prime-3 from Baa2/Prime-2
- Foreign currency deposit ratings downgraded to Baa3/Prime-3 from Baa2/Prime-2

The local currency deposit rating carries a stable outlook while the foreign currency deposit rating carries a negative outlook. The rating action concluded review for possible downgrade.

FHB Mortgage Bank

- Local currency deposit ratings confirmed at Baa3/Prime-3
- Foreign currency deposit ratings confirmed at Baa3/Prime-3

All the above ratings carry negative outlook and the rating action concluded review for possible downgrade.

MFB Development Bank

- Foreign currency deposit ratings downgraded to Baa3/Prime-3 from Baa1/Prime-2
- Foreign currency senior unsecured debt rating downgraded to Baa3 from Baa1

All the above ratings carry negative outlook and the rating action concluded review for possible downgrade.

Budapest Bank

- Local currency deposit ratings confirmed at Baa2/Prime-2
- Foreign currency deposit ratings downgraded to Baa3/Prime-3 from Baa2/Prime-2

All the above ratings carry negative outlook and the rating action concluded review for possible downgrade.

The previous rating actions on the above mentioned banks were:

Moody's last rating action on OTP Bank was on 23 July 2010 when local and foreign currency long- and short-term deposit and debt ratings of Baa1/Prime-2 and foreign currency subordinated debt rating of Baa2 were put under review for possible downgrade following a sovereign rating action.

Moody's last rating action on OTP Mortgage Bank was on 23 July 2010 when local and foreign currency long- and short-term deposit ratings of Baa1/Prime-2 were put under review for possible downgrade following a sovereign rating action.

Moody's last rating action on K&H Bank was on 5 August 2010 when foreign currency deposit ratings of Baa1/Prime-2 of K&H Bank were placed on review for possible downgrade following a sovereign rating action.

Moody's last rating action on MKB Bank was on 23 July 2010 when local and foreign currency long- and short-term deposit and debt ratings of Baa2/Prime-2 and the foreign currency subordinated debt rating of Baa3 were put under review for possible downgrade following a sovereign rating action.

Moody's last rating action on Erste Bank Hungary was on 23 July 2010 when local and foreign currency long- and short-term deposit ratings at

Baa2/Prime-2 were put under review for possible downgrade following a sovereign rating action.

Moody's last rating action on FHB Bank was on 23 July 2010 when local and foreign currency long- and short-term deposit ratings at Baa3/Prime-3 were put under review for possible downgrade following a sovereign rating action.

Moody's last rating action on MFB Development Bank was on 23 July 2010 foreign currency long- and short-term deposit and debt ratings of Baa1/Prime-2 were put under review for possible downgrade following a sovereign rating action.

Moody's last rating action on Budapest Bank was on 19 May 2009 when its BFSR was downgraded to D (Ba2) from D+ (Baa3) and bank's deposit ratings were downgraded to Baa2 (stable)/Prime-2 from A1/Prime-1 for the local currency and Baa1/Prime-2 for the foreign currency deposit ratings.

The principal methodologies used in this rating were "Bank Financial Strength Ratings: Global Methodology" published in February 2007, and "Incorporation of Joint-Default Analysis into Moody's Bank Ratings: A Refined Methodology" published in March 2007, and "Moody's Guidelines for Rating Bank Hybrid Securities and Subordinated Debt" published in November 2009.

Headquartered in Budapest, Hungary, OTP Bank reported consolidated total assets of HUF10 185 billion (EUR35.5 billion) as of 30 June 2010.

Headquartered in Budapest, Hungary, OTP Mortgage Bank reported consolidated total assets of HUF1 640 billion (EUR5.7 billion) as of 30 June 2010.

Headquartered in Budapest, Hungary, K&H Bank reported consolidated total assets of HUF3 317 billion (EUR11.55 billion) as of 30 June 2010.

Headquartered in Budapest, Hungary, MKB Bank reported consolidated total assets of HUF3 236 billion (EUR11.30 billion) as of 30 June 2010.

Headquartered in Budapest, Hungary, Erste Bank Hungary reported consolidated total assets of HUF3 044 billion (EUR10.6 billion) as of 30 June 2010.

Headquartered in Budapest, Hungary, FHB Mortgage Bank reported consolidated total assets of HUF830 billion (EUR2.89 billion) as of 30 June 2010.

Headquartered in Budapest, Hungary, MFB Development Bank reported consolidated total assets of HUF1 148 billion (EUR4.2 billion) as of 31 December 2009.

Headquartered in Budapest, Hungary, Budapest Bank reported consolidated total assets of HUF909 billion (EUR3.4 billion) as of 31 December 2009.

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London
Irakli Pipia
Vice President - Senior Analyst
Financial Institutions Group
Moody's Investors Service Ltd.
JOURNALISTS: 44 20 7772 5456
SUBSCRIBERS: 44 20 7772 5454

London
Yves Lemay
MD - Banking
Financial Institutions Group

Moody's Investors Service Ltd.
JOURNALISTS: 44 20 7772 5456
SUBSCRIBERS: 44 20 7772 5454

Moody's Investors Service Ltd.
One Canada Square
Canary Wharf
London E14 5FA
United Kingdom
JOURNALISTS: 44 20 7772 5456
SUBSCRIBERS: 44 20 7772 5454



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