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OTP Bank 1Q 2018 Results Conference Call — Friday, 11 May 2018

Anna Marshall: Good afternoon, everyone. This is Anna Marshall from the senior banks team at JP Morgan, and I have the pleasure of introducing today's speaker, Mr Laszlo Bencsik, Chief Financial and Strategic Officer, at OTP Bank. Laszlo, over to you, please.

Laszlo Bencsik: Thank you. Good morning, or good afternoon, depending on where you are, and thank you very much for joining us today for the first quarter 2018 results conference call. As usual, the presentation is available on the website, so I hope you have had a chance to download it, and you can follow it, together with me.

As usual, I'm going to go through the presentation first, and get some further remarks on this and expand on the message. Thereafter you will have a chance to ask your questions.

Starting the presentation on page two, which describes the quarterly results, we can see that the accounting profits, on a yearly basis, increased by 23%.

The adjustments were pretty similar to what we had last year in the first quarter, and the biggest item was the bank tax which we have to pay in Hungary, and we have to account the entire annual amount in the first quarter. If you take out these adjustments, then the adjusted profit after tax, which we usually consider the fundamental business result, increased 19%, and went up to 79.3 billion.

First of all, it's interesting to look at the composition of this number. As you can see, the contribution of the foreign group members increased to 46%, which we're quite happy about. This is the type of development we tried to achieve, and we hope that there will be a further increase of the non-Hungarian profits in the future.

On page three, it's nothing more than a further detailing of the one-offs, so I'm not going to spend time on this.

Maybe it's more interesting to look at page four, where we have the major P&L lines for the group on the adjusted basis. On this slide you can actually see the two most important contributions to the improvement of the quarterly results on a year-on-year, but also, on a quarterly basis. The first one is the contribution of the two new acquisitions we made last year, namely Splitska Bank in Croatia, and Vojvodjanska Bank in Serbia. These two entities were obviously not contributing to the consolidated results a year ago, but they contributed in the first quarter of 2018: these two together, plus the Leasing companies which were acquired as part of these packages or groups of companies, which we acquired through these two major acquisitions. So, all of these entities together contributed in the first quarter HUF 5.9 billion.

If you look at this page, on the right side you see two columns, and these are the without acquisition numbers. If you take out the contribution to the P&L of these entities, then the profit growth was 10%, and you can also see the corresponding P&L lines.

So, for instance, total income without the impact of acquisitions on a year-on-year basis grew 1%, and operating costs 3%.

The other very important contributor to the improvement of profits was the lower risk costs, as you can see on this slide. From last year to this year, risk cost went down from HUF 12.5 billion to 1.3 billion, so more than 11 billion improvement on the risk cost line.

The risk cost element also had an impact on the first quarter, quarter-on-quarter results. As you can see, part of the quarter-on-quarter improvement was due to the fact that we had much less risk cost compared to the last quarter of last year. This explains most of the improvement on a quarter-on-quarter basis.

On this slide you can see the result of the treasury share swap agreement, which was minus 1.8 billion. This is, more or less, a technical item, and this is going to be reversed in the second quarter, so this minus 1.8 is going to appear as a plus 1.8, and this is just related to how we have to recognise and book the appropriate items under the treatment of this structure.

Going to page five, you can see the composition of the consolidated adjusted after tax profit. As you can see here, in a number of group members we achieved improvement on a year-on-year basis: especially in Russia, in Ukraine, and obviously, in the countries where we made acquisitions, namely Croatia and Serbia.

But also in the case of other smaller subsidiaries such as Slovakia and Montenegro, the contribution became positive, and actually, visible. In all of these countries the improvement is mostly attributable to better risk costs. There are two entities in the group where we see a lower result year-on-year: at the Hungarian Core activity and the Bulgarian DSK Bank activity. More about this later on, when we look at the P&L lines line by line.

We've listed here, on page six, some miscellaneous items. We have been talking about all of these.

We have had an announcement about the first item. There's not so much more I can say about the fact that the National Bank of Romania did not approve our request for the acquisition, which we were going to make. And therefore the whole transaction fell through, because we ran out of time, which was originally stipulated in the contract.

The second item is the IFRS 9 implementation. Already, after the last quarter results and the annual figures, we communicated the expected impact of changing the methodology from IAS 39 to IFRS 9.

What you see here are the final numbers of this implementation of the new methodology: the after tax impact on the reclaimed earnings is HUF 50.4 billion negative. Because we applied the transition rules, this is going to hit our Common Equity Tier 1 ratio only by 3 basis points this year, because we have to take into consideration only 5% of the impact in this year.

The third item here is a recent news which came out, that the advocate general formed a preliminary option on one legal enquiry, which was made to the European Court. This is regarding whether the Hungarian courts can assess the fairness of the information provided by the banks when they gave FX loans to individual clients.

In our understanding, as we have written here, the opinion formulated by the advocate general does not seem to collide with the present Hungarian jurisprudence. Meaning, we believe that this is in line with what the Hungarian practice is. But the final ruling and verdict is going to come out somewhere in the second half of his year.

On page seven, we start the section that covers each P&L line on a cross sectional basis. Starting with the total income, year-on-year total income grew 9%. This is heavily influenced by the two acquisitions we made. Therefore, we also included a number which takes out the impact of these two acquisitions: so, without the impact of acquisitions, the growth was only 1%. On this slide, you can see these light grey bars, they represent the with acquisition, and the green ones, the without acquisition numbers. Obviously in the case of Croatia and Serbia these are material.

Other than that, the total income was relatively flat. Even if you look at it on a quarterly basis, most of the movements were related to technical items. I'm going to talk about it a bit later on, when I talk about the different parts of the total income.

In the case of the Hungarian operation, Slovakia, Romania, Montenegro, as you can see on these notes, most of the changes were related to technical items.

Some more evidence on this on page eight, where we talk about the net interest income. Again, without acquisitions, on a yearly basis, it was quite stable. And on a quarterly basis, as well, only 1% improvement, and even most of that 1% improvement came from this technical adjustment, which we had to make in the fourth quarter, due to accounting reasons. You might remember that there was a one-off negative item of HUF 2 billion, which we had to book in the last quarter in Romania. If you take this out, then this, more or less, explains the quarter-on-quarter changes.

I also have to remind you that this was a shorter quarter. There's a calendar effect, which was actually negative in the first quarter, compared to the last quarter last year. And also, in the second quarter, we expect some improvement here.

Talking about volumes on page nine, as you can see, the quarterly growth was 2%. This is the total group performing loan volumes, and FX rate adjusted. Across the group we have had positive numbers, and the dynamics you see here are more or less in line with what we originally expected for this year. We believe that we are right on this trajectory, which we foresaw when we made our forecasts for this year.

As you can see, the strongest dynamic in Ukraine was 6% just in one quarter. Also, Bulgaria was strong, 3%, and Hungary 2%, and so on. Basically, across the board we had decent growth rates.

Maybe the next page is even more informative, and this shows the lending activities. So, actually how many loans we originated in retail, especially in mortgages and cash loans. As you can see, the previous year's dynamics, which we have observed here, remain. The new production is growing much faster than the volumes. For instance, in Hungary, we increased mortgage production 32% on a year-on-year basis, in cash loans, 73, and so on in each country. In some cases, you see particularly high numbers and we are quite happy, for instance, in the case of DSK Bank in Bulgaria, which is another sizeable volume.

When you look at Croatia and Serbia, the numbers are less meaningful, because they also include the impact of the newly acquired entities there.

Looking at deposit volumes on page 11, the first quarter was 1% positive. This is not so much a priority at the moment to increase deposit volumes, but it's always a good sign, and it shows confidence of our customers. The intention is not to further increase our liquid reserves. Therefore, you see some adjustments. For instance, in Russia, we are optimising, short-term, the pricing of deposits. In the first quarter, it resulted in a lower volume of total deposits. Especially in corporate which is much more price sensitive, we lost part of the deposit portfolio. But again, this was deliberate and on purpose, and as you will see, it actually contributed to the margins in Russia. So, we find it as a good development.

On page 12, some information on the net interest margin development. First, starting from the group level. The first quarter of 2018 and in the fourth quarter of 2017 numbers are pretty similar: 0.3 percentage point decline in the overall margin, so I might say that it was stable.

In the lower part of this chart, you see the various elements and forces affecting the overall margin, which pretty much balanced each other during the first quarter.

More on this on the following page, on page 13, where you can see the margin development of the biggest group members.

Starting with Hungary, where we had a 10 basis points decline. Part of the decline, seven basis points, was actually attributable to the one-off accounting item which we did in the fourth quarter. If we took out that one-off item, then we would have a margin of 3.09% in the fourth quarter, and therefore, the decline would have been only 3 basis points. So, the actual fundamental business related decline was just 3 basis points.

Bulgaria continued to decline. However, the rate of decline decelerated, which we're quite happy about. This is what we flagged and expected for this year: further compression of the margin, but potentially, with a slower pace than it happened during the previous years.

Russia improved. There's slight improvement, but actually some visible improvement in the NIM. Again, this is related to optimising funding, and decreasing cost of funds in Russia by repricing some of the deposits.

Croatia was flat. In Romania, we see an increase - again, this is related to the technical booking item, which we made in the fourth quarter, so this is not related to business events. And Ukraine started to increase, which is partially related to the rate hikes, but also, to the very fast growth of loan volumes, as we have seen, in the first quarter loan volumes grew by 6% only in one quarter, and these are quite decent, juicy margin businesses.

Fee income on page 14. If you look at the quarter-on-quarter development of fee income, you see a quite sizeable decline. On this page we've tried to explain the reasons why this decline happened. I dare to say that these are more related to technical items, and very little is actually related to fundamental business processes.

The most important one is at the bottom of the page. It's the decline of the fee income related to the fund management activity. Now, you might remember that during the last quarter, we had a one-off, close to almost HUF 5 billion additional revenue, which is basically a success fee. The fund management company received a success fee from the funds, due to substantial over performance compared to the benchmarks. This always happens, if it happens at all, at the end of the year, so this item did not happen in the first quarter. It was not expected to happen either.

The other entities where we see one-offs are the Hungarian Core and in Montenegro. In Hungary last year, we had one negative item related to the refunds we had to make. But in the first quarter, we also had two negative items. We listed them here on the right side. There's this lump sum, accounting for the full annual card-related financial transaction tax, 1.6 billion.

This is what we always have to book in the first quarter. This expanse of 1.6 billion is not going to reappear in any of the following quarters this year.

The other item is another minus, and this is the Compensation Fund contribution, which we had to book in the first quarter. This is very similar, by the way, to what we did last year. In the first quarter, we booked 1.3 billion expense, so this is a negative item. And the compensation, because we get compensated for this, is going to come in the second quarter. So, the second quarter will actually be 1.3 billion technically higher due to this element, and the other 1.6 billion negative will not reappear. So, there might be some improvement on the net fee income in the second quarter, in case of the Hungarian operation, at least, due to these technical elements.

Other net non-interest income. Again, it increased on a quarterly basis by HUF 3 billion, and we listed the two items, which were again, more related to technical differences. No major fundamental improvement here.

On page 16, we see the operating costs. This is, obviously, in a strong focus, given its growth on a year-on-year basis. If you look at FX adjusted, because obviously, the FX adjusted numbers are more meaningful, in terms of showing us what happens exactly, so the overall growth was 16%. But here, the effect of acquisitions was also important. So, taking this out, we end up having 5.4% growth, based on the year-on-year numbers. This is pretty much in line with what we indicated when we talked about the expected growth rate of operational expenses for this year. The guidance was 6% on an annual basis, so we had 5.4% in the first quarter.

And this happens across the board, in all of our entities we're seeing increasing cost. As you can see from the comments on the right side of this page, typically this is the result of increasing personnel expenses, as we are in an environment where wage inflation is very strong. And, at the same time we are expanding quite rapidly, in terms of our economic activities, especially loan origination which requires more people in the network. We also invest a lot into digital, and this doesn't only mean CAPEX investment, but also hiring more people who have more skills, especially in IT, and therefore tend to be more expensive.

Finally, in this part of the presentation we've reached the last line of the profit and loss statement, and that is the risk cost. This was the biggest influencer of the quarterly results that we had hardly any risk costs. The nominal value of risk cost was minus 1 billion, which is much lower than what we had seen during the last, I would say, ten years.

Looking at the rate of the portfolio deterioration, which is on the next slide, but also in this slide we have this number of seven billion. This was the total worsening, and most of this came from Russia, where we have this normal churn of the portfolio, as we have higher risk costs, high APR, short-term, unsecured consumer loans.

But the rest of the portfolio is very stable, and as the total performing volume is growing, the 90 days past due ratio declined further. Obviously, the risk cost rate was close to zero.

On this page, you also see the constituents of this minus 1 billion risk cost. As you can see, in Hungary, again in the first quarter, we had a write back, so the risk cost was actually positive. This also happened in Ukraine, in Croatia, and Russia. Bulgaria had more normalised levels of risk costs.

On page 18, you see the details of those numbers I mentioned just now, so the nominal volume of portfolio deterioration by group members. Looking at this chart, you see that most of the deterioration came from the Russian business, which is the normal course of business there.

Now, leaving the cross-section group level, I'm going to talk briefly about the performance of the most important group members, starting with our Hungarian operations. I've covered what is on page 19, I've talked about the P&L lines in the cross-sections.

On page 20, I think there's some useful and informative data, which might be worth looking at. And this is talking about our Hungarian retail business and retail activities. We are very happy to see these numbers, especially the market share numbers, which you can also see on this page.

In the first quarter, the mortgage contractual amount market share increased to 28.5%, which is an increase, compared to last year. An even bigger achievement, I think, is the one related to our cash loan disbursement market share, which increased to 42% in the first quarter. And overall, our household savings market share also increased, quarter-on-quarter, up to 31.4%.

The other important message on this chart is the mortgage disbursement volumes growth. Because if you look at the first quarter, again, you see this 1% quarterly growth in Hungarian mortgage volumes, and this is, obviously, one of the numbers which are the most important in the future profit generation of the group. There is only 2% year-on-year growth so far. The stock growth numbers don't reflect the increase in economic activity, and the increase of the landing activity we have. For instance, on page 20, you see that in the first quarter this year, on a year-on-year basis, mortgage disbursements increased 32%.

There's acceleration in new production, which only started to appear in the stock volume growth numbers. In cash loans, we see quite positive figures already in the total volume number, as well. We have 40% growth in performing loan volumes year-on-year.

If we go to page 21, we see some details on our corporate business line performance. We are quite happy to see further increase in our corporate loan market share in Hungary. Having said that, I previously referred to this as being less of a priority to increase market share, and we want to be more selective in corporate.

Nevertheless, we are very happy that we managed to increase our corporate market share in the first quarter, especially because most of it came from micro and small companies, which remain our targets. We had 4% growth just in the first quarter, volume wise. The other important part is another sub-segment of the corporate loan market is the agricultural loans, which is another focus area for us. And here, we managed to further increase our market share last year.

Some more details about our Bulgarian, Russian, Croatian and Ukrainian businesses, starting with Bulgaria. Year-on-year, as I said, the profit declined slightly. This is primarily due to the fact that we had higher risk costs in the first quarter in Bulgaria than last year. This, by the way, is already attributable to the IFRS 9 provisioning methodology, where, for instance, in the case of Bulgaria, we expect some slowdown in the GDP growth, and therefore, we have to adjust the macro models, and somewhat increase the provisioning ratios. So, part of this provisioning was related to the IFRS 9 methodology, which is on a forward looking basis and it includes the expectations related to the changes of the macro environment. If we expect somewhat lower GDP growth than previously experienced, then this immediately translates into higher provisions in case of portfolios.

On a year-on-year basis we managed to grow total income by 2%. Unfortunately, costs, as well, grew by 9%. The first quarter return on equity was still decent, 17.3%, despite this relatively high risk cost we had to book. If you look at the business activity itself, new mortgage generation disbursements, in the first quarter this year we disbursed 17 billion. This is without refinancing, so this is the actual newly disbursed numbers. A year ago it was 11 billion, so there's more than 50% increase in the new origination. Likewise, in cash loans disbursements grew by 40% compared to the first quarter last year. These are quite decent numbers, and they show strong acceleration of the business activities there in Bulgaria, as well.

Russia. Here, the P&L lines are in Hungarian Forint, and I'm not going to talk much about this, because the currency rate has another important effect on those, and I previously talked about that on the cross-section part.

But the return on equity first quarter was 25.7%. Very good and increasing. You see here how fast our volumes are growing in POS, cash loan, credit card, and other loans. Other loans are mostly corporate, obviously. Probably the most important factor is that in the first quarter the risk cost rate went down to below 5% levels, it was 4.5%.

This is a number we last saw maybe in 2012, 2011, when we had the last positive part of the cycle in Russia in terms of consumer lending. We hope that the environment remains positive, and on a cyclical basis we'll see these lower levels of risk cost, which we only used to see more than six years ago.

Ukraine - incredible performance, especially if you look at the return on equity, the first quarter return on equity in Ukraine was 68%. If you look at the business activity, for instance, the POS loan disbursement and cash flow disbursement in the first quarter, year-on-year, grew by 50%, as you can see on this chart.

Also corporate volumes, just in one quarter, grew by 5%. Much of the growth in Ukraine is coming from machinery leasing, so not private individuals, but corporate leasing. This seems to be a successful business line there, and the profitability of the entity is quite promising.

Croatia. This is one of the group members where we clearly repositioned ourselves during the course of last year. This shows not only in our market shares and in our volumes, but also in our financial performance. The pro forma return on equity of the two units which we still have - we still have two separate banks, because the merger hasn't been finished, this is expected to happened somewhere closer to the end of the year – so, if we combine pro forma these two entities, then the return on equity was 12.8%, getting closer to the targeted 15%. This is quite promising, I would say, because these numbers we see here are without any synergies. In fact, we have additional costs related to the merger activities, what we pursue there.

With this slide, I actually reached the end of the presentation. I'd like to encourage you to ask questions, and I'd like to ask the operator to open the floor for questions.

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

Pawel Dziedzic: Good afternoon, and thank you for the presentation. I have two questions. The first one is on the operating environment in Hungary. Obviously, you made a very positive remark about potential for growth from here. You mentioned higher disbursements, and so on, and also, I think you referred to a longer term growth perspective, if we look at penetration of household debt, for instance, to GDP.

So, could you give us your thoughts about the growth rates that you can potentially achieve in 2018 across your portfolios? And how quickly it can change in the coming years. That would be the first part of the question. But also, related to that, you are now at your peak market shares.

And I'm wondering if you're seeing any more competition, or you expect to see more competition, that could change the dynamics a little bit when it comes to pricing, and maybe profitability of products. And the second question I have is a little bit more technical, but it's on Russia, and implications from the sanctions.

The backdrop to this quarter was very positive, and you also mentioned that in your opening remarks, but do you expect any changes in growth or in other drivers of your operating performance, for instance, the rates that would affect OTP going forward?

And then more technically, can you remind us of your hedging policy, and if the weakening of the rouble in Q2 will have any implications on the capital, and so on? And finally, since we are under IFRS9, what would it take, when it comes to a change in outlook for the country for the provisions in Russia to increase? Thank you.

Laszlo Bencsik: Operating environment in Hungary and growth rate in 2018. Last time when we talked about the expectations regarding loan growth in Hungary and in all the other countries, we said that we expect similar trends this year to last year. Last year overall performing group volumes grew organically by 10%. And the guidance was that we expected similar levels of growth across the group. This is also true for Hungary, overall. I also said last time when we made the guidance that we expect some change in the composition of growth in Hungary: maybe, having less corporate volume growth, and more retail, and within retail, maybe more mortgage volume growth to manifest this year than last year.

Indeed, this seems to have happened. At least, we do see 1% volume growth in mortgages in the first quarter, and we hope that this is going to continue and further accelerate during the course of this year. But we don't see any reason to change the expectations and the forecasts that we made last time.

Competition and our market share. Competition is very fierce, and this manifests in our margins. There's a continuous decline in the margins in Hungary, and now this is purely due to the price competition in new volumes, because the rate environment is stable. There wasn't any change in the rate environment quarter on quarter.

What you see here is primarily and fundamentally related to price competition, and this is going to continue. It's a very competitive market, indeed, and I expect this to remain so. Therefore, from this angle, we expect further pressure on margins and on the pricing of the new volumes.

Sanctions on Russia. So far, we haven't seen any impact on demand, or the pricing of new loans - maybe deposit prices. Certainly, one implication can be that the rate decline might be slower, or won't happen at all further, and that is going to have an impact on our cost of funding, that's clear. So, maybe deposit prices.

It's not obvious that we should expect material change in the level of demand for our consumer loans. Almost 90% of the book is unsecured consumer lending, therefore, our volume dynamics in Russia related to demand for consumer loans, and that is related to retail consumption. We don't expect much impact on retail consumption.

Overall, maybe the headline GDP figure might be somewhat less, but we expect continued GDP growth in Russia, and reasonably okay retail consumption growth, which creates a decent platform for our consumer lending business.

Hedging rouble risk. We don't have an open position to rouble, other than the one that is related to the local equity, which is in roubles.

When we consolidate the Russian bank, and we consolidate the equity of the Russian bank, then there's an FX translation impact, and this can have an effect on the overall equity of the group. Having said that, it also has an effect of the risk weighted assets, because, for instance, if the rouble weakens, then there's a negative impact on the group equity. But also, the risk weighted assets in Hungarian Forint terms decrease, therefore, the capital requirement decreases. So, this is more of a natural hedge from a point of view of capital adequacy. We don't hedge the equity position, other than this.

The other potential impact is the P&L impact. The profit of the Russian bank in Hungarian forint terms is depending on the FX rate. This is another element which is moving, depending on the FX rate.

IFRS9 expectation: indeed, technically, if the GDP growth expectations change, in positive or negative direction for the country, we have to adjust the IFRS9 ratios. Therefore, if we were to assess that the growth potential of the Russian market is much less than previously anticipated, then it would mean that on a one-off basis, we have to increase the ratios. So far, this is not so much the case. We believe that the impact on GDP growth, and especially on that part of the GDP growth which is important for us - because it's not just the overall macro numbers that matter, it matters related to the specific portfolios we have, the consumer lending portfolio, so here we have quite a sophisticated model, which defines the relationships between different macro indicators and the consumer loan quality. It's not a linear correlation between the two.

As a rule of thumb, if things get worse, then we have higher provisions, and if things get better, then we have lower levels of provisions. Obviously, the volatility of this, and how it exactly plays out, we will see in the future. I think, this is an interesting development across the banking sector in Europe, how the IFRS9 methodology will impact the risk cost level through this forward looking methodology basis.

Pawel Dziedzic: Thank you. That's very useful. Can I just have one follow-up? And that relates to the first question. You mentioned that this three bases points decline reflects the competition. Would it be fair to take it as a run rate for future development?

And related to that, you mentioned that this pricing related to fair mortgage product, has it impacted the new lending? Will it continue? Is it something that will, on a continuous basis, erode your margins? Or the impact of that is, let's say, overall, will be over soon?

Laszlo Bencsik: There's an underlying fierce price competition, so it's not this fair product stamp that makes pricing more competitive. The underlying price competition in Hungary is very strong. The impact of this programme is coming though when you look at the variable and fixed volumes distribution in new production. A year ago, new production predominantly was variable, and today, the recent number that was published by the central bank said that more than three quarters of the new production was fixed for at least five years. So, this is a more fundamental change caused by this programme.

I think the impact on pricing is less, and there's a much bigger impact on moving the new production into fixed, as opposed to variable. This we welcome, by the way, so this is something that we believe is good for the market and good for customers, and makes the entire system safe.

Operator: The next question comes from Gabor Kemeny of Autonomous Research. Your line is open, please go ahead.

Gabor Kemeny: Hi. I would like a follow-up on the Hungarian retail lending. You mentioned the fierce competition. You have been gaining decent market shares; you show this in consumer lending. So, what do you think has been driving this increase? Have you been under cutting competition, in terms of prices, or is it more a fair product differentiation?

And then staying with the margins. I think your net interest margin in the first quarter was something like 20 bases points below the 2017 levels. So, to get to the guidance of 10-15, you would need a slight improvement from here. But over the course of 2018, what do you think will drive this?

Laszlo Bencsik: Regarding retail, our consumer lending and our market share in new production in Hungary, indeed, we tried to match the pricing, as well, in the market. But I think the most distinguishing factor, starting from the beginning of last year, was that we were the first in the market to introduce end-to-end digital cash loan lending.

Customers can get a cash loan without any physical interaction with the bank. The share of this end-to-end digital product is rapidly increasing in the total production, and it seems to be very successful. I think this is, potentially, the biggest contributor to our recent success in this field.

Gabor Kemeny: That's interesting. Would you be able to comment on the share of digital sales?

Laszlo Bencsik: I don't think we have published it, and if we haven't, then we regard this as confidential data. Obviously, just because of what I've said, this is potentially an important distinguishing factor, and provides us competitive advantage. Obviously, we try to be less talkative about the details on this. But this seems to be quite successful.

The net interest margin guidance: if you carefully look at what we said when we gave the guidance, the basis was not the last year average, but the basis was the last quarter figure. Literally what we said was that the net interest margin erosion may continue compared to the fourth quarter 2017 level, which was 4.38%. The annual NIM may contract by around another 10-15 basis points.

We uphold this. Compared to the last quarter, the NIM didn't contract so much, it was almost flat. We believe that it's still a fair assumption to expect not more than 10-15 basis points decline during the whole course of the year. So, the guidance was related to the fourth quarter last year, and the average number for this year.

The reason behind choosing the base being the fourth quarter is that the Splitska acquisition, and also, the Vojvodjanska acquisition had a material impact on the overall group margin. If we just compared one year with another, for the whole year, then we would mess up the numbers with the acquisition. But, more or less, the last quarter, not entirely, because in terms of NII, Vojvodjanska only had it for one month out of the three, but at least it was consolidated into the balance sheet by year end. Vojvodjanska Banka is smaller than Splitska, but we wanted to look at a base which was relevant, and comparable to the whole year number this year.

Operator: The next question comes from Andrzej Nowaczek of HSBC. Andrzej, your line is open, please go ahead.

Andrzej Nowaczek: Thank you. Would you have a comment on Stage 3 loans? Is the amount what you expected it to be, and what explains the difference, compared to the value of 90 days past due loans? And also, this may or may not be related, but would you say that your cost of risk guidance now looks very conservative?

Laszlo Bencsik: Stage 3, well in Hungary, the opening balance of the IFRS9 staging was audited by the auditor, because we have to report the audited numbers to the Hungarian supervisor. Given the fact that the preliminary number was very much similar to the final number, yes, it's in line with what we expected.

So far, we have been typically reporting the 90 days past due ratio. The Stage 3 is obviously a new concept, but quite similar in terms of its definition to the NPL or NPE ratios used by the EBA. This number was something we expected, there's no surprise here.

Indeed, you are right that looking at the first quarter risk cost number, the initial guidance may seem conservative. I suggest waiting at least another quarter, and then we can ponder more about the expected level of risk cost for the entire year. I think one quarter is not enough to draw conclusions. Therefore we haven't revised the guidance we made for the risk cost level for this year.

Operator: The next question comes from Mate Nemes of UBS. Your line is open, please go ahead.

Mate Nemes: Good afternoon. Thank you for your presentation. I have three questions for you, the first two on Russia. First of all, the NIM increase in the first quarter, I think you commented that this was the result of lower funding costs. Can you just comment on how far you are with the repricing of deposits? Is this still ongoing?

And in light of this, if you could comment on your expectation for the net interest margin for the next two or three quarters. That would be helpful. And still staying in Russia, in the first quarter, you had, again, a solid fee income, and that comes after a strong Q4. I think you commented last time that it remains to be seen if the fee margins can be sustainable going forward.

How do you see this now? Is the fee margin sustainable at current levels? Or should we expect some decline from here? And thirdly, on Bulgaria. I appreciate that the NIM decline is slowing down. If you could, again, comment here on how far you are with the repricing of the retail loans. And then can we see the NIM decline really level off? Thank you.

Laszlo Bencsik: Indeed, I said that the Russian NIM increase in the first quarter was related to lower funding costs, and the optimisation of deposit pricing. Especially in corporate deposits in Russia the volumes are very sensitive to pricing. If you look at page 11, you see that in one quarter we lost 19% of our corporate deposits and 5% of the retail deposits as a result of this deposit repricing.

This is not something that is sustainable in a way that in each quarter we can do this, and then have further increases to the NIM. Having said that, this was more a one-off improvement; certainly we don't expect further quarterly improvements in the Russian NIM. At best, it can stay flat.

Having still quite competitive pricing levels especially in POS, and the expected further increase in deposit rates, potentially, if the impact on the financial markets continue of the sanctions, then I think the margin pressure will increase again in case of our Russian business.

The fee margin in the first quarter seems to be sustainable, there doesn't seem to be any strong reason why this should be very different.

Bulgarian margins and NIMs. Unfortunately, this is not the end of the repricing. As previously said, this was going to continue for the remaining quarters of this year. So, this was the original guidance we made, that in Bulgaria we expected further continuous decline in the NIM. We also said that probably it was going to be less than before, with a lower rate of decline, but the decline will continue. I'm afraid we are not seeing the end of the NIM cycle in Bulgaria; this is going to go further down in the coming quarters.

Operator: The next question is from Olga Veselova of Bank of America and Merrill Lynch. Olga, your line is open, please go ahead.

Olga Veselova: Thank you. I have several questions. One of them is a follow-up on margin. I think your deputy CEO commented to reporters that the net interest margin may bottom out this year. Is this comment about Group or OTP core business? And also, what gives you comfort to expect growth or stabilisation of margins next year, given that you just said the Russian margins will likely continue to erode.

And also, possibly the pricing pressure in Hungary will continue. So, that is my first question, your margin expectation for next year. My second question is a technical one. On slide 12, you talk about quarterly margin dynamics. And there is a factor, which is called composition effect. Can I just clarify what that is exactly?

And finally, my third question is about costs. What are your cost growth expectations for Hungary and Russia? And how high can the acceleration of wage pressure in Hungary, given that the impact from lower social tax will diminish versus last year.

And in Russia, was the cost growth in the first quarter, I think it was 12% year-on-year in rouble terms, was it driven by remuneration of salesforce or not? Thank you.

Laszlo Bencsik: Indeed, regarding the NIM, when last time I talked the guidance, the guidance was 10-15 basis points decline for the whole year 2018, compared to fourth quarter 2017. I also said that if all goes well, we might see the end of the rates cycle during the course of this year, meaning that there won't be further rate declines next year.

That is based on the assumption that the rate environment might turn around in the countries where we operate. It has already happened in Romania and Ukraine. Our expectation is that during the course of next year maybe the euro rate environment will start to increase.

Certainly, if that happens, or even somewhat before that, it might happen that the Hungarian rate environment might start to increase.

Just to remind you, in Hungary the base rate is 90 basis points, but the reference rate, which is relevant for the bank sector, is close to zero. The expectation is that that somewhere at the end of this year, but most probably during the course of next year this reference rate will start to grow. That would have a very beneficial impact on our margins and NII.

Indeed, you are right that from competition point of view, there's no reason to believe that there will be any type of easing or easier times. These markets in which we operate, especially Hungary, today seem to be very attractive for most or all of our competitors.

Therefore, everyone wants to grow and everyone is keen on having a price competitive product, as well, which is the normal level of competition. We haven't made a guidance for next year's NIM, so I'm not going do that today either.

Composition effect on page 12. When you decompose a rate or a changing factor, it always depends what the first one is when you do the decomposition. Then we have sub-decomposition, as well. It makes sense mathematically, but it would require a detailed disclosure of the model that we see. Fundamentally, we tend to refer to three, more or less independent factors. The first one is the interest rate effect. It means that for the entities in the group, their NIM, their net interest margin changes. It can go up, and it can go down.

When the net interest margin of one entity changes, it has an impact on the group level net interest margin, depending on the size of this entity. Assuming the same size, or same share, from the total volume, a given NIM change in an entity within the group has a given impact on the group level net interest margin. This is the first type of effect we want to capture under the interest rate effect.

The second is the composition: when the composition of the group volumes, and therefore the composition of the NII changes, due to volume changes.

If one entity grows more than another entity, then the contribution of that entity changes, as well, and can therefore have an impact on the overall net interest margin of the group. So, for instance, in the first quarter, Ukraine grew faster. We included Vojvodjanska Banka because it is not the closing volumes, it is the average volume that matters, because it's related to the margin, and margin is NII divided by average volume.

And the average volume of Vojvodjanska increased. Vojvodjanska has a lower net interest margin than the group, so therefore, this is negative. And the share of the Hungarian business decreased, for instance, slightly, and again, the Hungarian business is a lower margin than the group average, therefore the impact was positive.

The third effect is the FX rate changes. This is related to the fact that when the exchange rates change, then the Hungarian forint equivalent of a given entity's NII, and also volume changes, therefore it creates a composition effect, as well, and we separated that.

These are the three most important factors we find when we try to explain the NIM development from one period to another. We thought it might be useful for you, as well. That's more or less the rationale, if that's what you wanted to ask for.

Olga Veselova: That's clear, thank you.

Laszlo Bencsik: Now, cost growth. Again, the guidance we made last time on a group level was 6% FX adjusted growth in operating costs. And this is for the whole group, and we have not given more detailed guidance. We haven't given guidance on an entity level, but we still uphold the guidance for the entire group, which was 6%.

Olga Veselova: Does it remain valid, the previous guidance?

Laszlo Bencsik: Yes. For the group.

Operator: The next question comes from Robert Brzoza of PKO BP Securities. Robert, please go ahead.

Robert Brzoza: Good afternoon, gentlemen. I have a quick question on the changes in regulatory and the reported capital. Could you shed more light on the development there? The reported capital declined, whereas the regulatory capital and the capital ratios improved in quarter to quarter terms. Thank you.

Laszlo Bencsik: The Common Equity Tier 1 ratio at the end of the first quarter was 15% without the quarterly profit. If you take into consideration the pro forma quarterly profits minus the expected dividend, then the number was 15.6%.

The corresponding numbers for the year end, so the year end without last year's profit was 12.7%. If the last year profit was included, the year-end ratio was 15.3%. If you compare the common equity of our ratios, which include the period profits minus dividends, then the ratio increased from 15.3% to 15.6% in the first quarter. Is that what you asked for?

Robert Brzoza: Thank you.

Laszlo Bencsik: If you want to see further details, then if you look at the interim report, the Word document, which is also on the website, on page 39, there's a detailed explanation on how the retained earnings and reserves changes. If you want to understand how the equity changed, it is very elaborately explained there.

Robert Brzoza: Can I have one more question on the dividend policy, please. Because you are always saying that the dividend pay outs are depending on the M&A activity. And since the Romanian activity has essentially closed, I'm wondering whether it should not inspire any upward changes to the dividend pay outs going forward.

Laszlo Bencsik: Indeed, our Chairman and CEO made a guidance related to the dividend during the AGM, more precisely he said that we didn't have an exact guidance for the dividend. You can also access the AGM presentation on the website. What the Chairman and CEO said was that the dividend amount paid after 2018 earnings depended primarily on the acquisitions we can complete during this year. Therefore, the final suggested amount by the management and the board will be defined at the beginning of 2019, so before the AGM. He also said that nevertheless, we are going to identify a certain amount on a quarterly basis, which we label as expected dividend payment within the equity, and that was going to be similar to last year.

The running assumption regarding dividend and what we accrue on a quarterly basis, is equal to last year's dividend payment. The actual dividends can be different from this. Obviously, if you don't have any acquisitions, then it should be more than last year.

The Romanian one is just one element, and I would dare to say a rather small element of the entire picture. Needless to say, at the moment we have other opportunities that we are looking at. The Romanian event, in itself, doesn't have a major impact on our capital position, and therefore, it's not decisive related to the dividend.

The final guidance will come at the beginning of next year the latest. During the course of the year we'll have more knowledge, and we might have more precise indications.

Operator: Your next question comes from Stefan Maxian of Raiffeisen Bank. Your line is open, please go ahead.

Stefan Maxian: Good afternoon. Two or three questions from my side. One follow-up on Russia. With the deposit rates down 9% quarter-on-quarter, you come to a loan to deposit level of 170% roughly. Would you consider that you have to change your funding structure again, and become more aggressive in deposit pricing, in order to catch up in that respect?

The second question refers to Romania. After the Banka Romaneasca acquisition failed, what are your next steps there? Will you focus more on organic growth? Will you open up branches of your own, in addition? What's your plan B, more or less, there? And finally, regarding M&A ambitions in other countries, is it still, more or less, focused on the region where you are operating at the moment? Thank you.

Laszlo Bencsik: Related to deposit pricing in Russia, again, deposit price adjustment meant that we lost some of the hot corporate deposits. And if we wanted to get them back, we would have to raise prices, but this is not the case short-term. We will see how the market develops. Because it's not clear whether this is a short-term development, and the deposit pricing dynamics in Russia are more a trend, which we should continue to see in the future there. If there's more price competition of deposits, we will see. What I could say about that, I've already said, that it's unlikely that we continue to see further NIM improvement there.

It's quite the contrary, so there will be continued NIM pressure in the future, as well. This was more a one-off upward adjustment in the NIM in Russia.

Stefan Maxian: But you would feel comfortable with the current loan to deposit level?

Laszlo Bencsik: We'll see. It's the deposit pricing, and then how our customers react, and so on.. But we definitely try to optimise the funding costs in Russia. Seasonally, this is not a high growth period there. The really crucial part will be the last quarter of this year, by then we should know how much we have to pay for deposits, if we wanted to finance our Russian operations entirely from local deposits.

Our Romanian strategy. It's obvious that short-term, or even mid-term we may not be able to acquire a sizeable operation there, so that leaves us with organic growth. Indeed, we are quite motivated to grow organically. In the longer term, we haven't given up on acquisitions either, but this is probably not what we can do in short, or even mid-term.

According to this, we are reviewing our strategy in Romania, and trying to define what we are going to do, in order to boost and accelerate our organic growth in the country. We are not at the end of this; we've only started, so I don't have the answer yet. But definitely, the intention is now to focus on organic growth, and our ambitions are quite high, and we identify Romania as an attractive market strategically. We will continue to pursue along these lines.

M&A, yes, we continue to focus on the region where we are. The answer to your third question is yes.

Operator: Laszlo, your next question comes from Simon Nellis of Citibank. Simon, please go ahead.

Simon Nellis: Hi. Thanks for the call. Just a quick question on IFRS9. I see that the total provisions stock went up to 754 billion. I guess that's total provisions for all stages, Stage 1 through 3?

Laszlo Bencsik: Yes.

Simon Nellis: What is the coverage of Stage 1 and 2, versus stage 3? What is the level of Stage 2, as a percentage of gross loan, I'd be curious?

Laszlo Bencsik: We haven't disclosed these numbers yet.

Simon Nellis: Will you disclose them?

Laszlo Bencsik: We'll see. We look at what our competitors do, and then we will adjust our practises accordingly.

Operator: Your next question comes from Alan Webborn of Société Générale. Alan, please go ahead.

Alan Webborn: Hi. Thanks for the call. Two questions, if I may. Firstly, do you see areas within corporate lending where you feel pricing is becoming irrational in terms of low interest rate environments persisting, and absence of risk costs? Are you seeing examples of business that you don't want to do, because you feel the margins are simply not acceptable?

And do you think that is increasing? Is it always the same? Is it getting less bad? Just a view, in terms of your targeted lending volumes, and whether that's becoming more of an issue. That was one question. And the second question is in terms of your view of the corporate sectors to which you're exposed, in markets where you're having considerable wage increases. And increasing questions about capacity constraints, and a problem over investment.

Do you also feel that there are any signs, even early signs, of issues, in that respect, within the corporate sector in those markets? Because clearly, you've been through a crisis a number of years ago, where we went from night to day, from a very positive to a very negative scenario, with a very sharp turnaround in the fortunes of corporates.

And I just wondered whether you feel at the moment, given the quite high wage pressures, whether there were any issues, and where, if anywhere, you were seeing that within the corporate sphere that you're engaged with. Thank you.

Laszlo Bencsik: The corporate margins, indeed, the large corporate segment is becoming less and less attractive, and we are becoming more and more selective in large corporate lending. This is something that I referred to when we made the guidance, when I talk about the guidance in terms of volume growth.

When I was talking about Hungary, I said that we were expecting a similar level of growth as last year. But maybe within that growth, less corporate growth and more retail volume growth, just because of this reason that large corporate margins contracted considerably.

When we allocate capital within the different business lines, now the new large corporate lending seems less attractive. This is clear there.

This is a very interesting topic you raised, regarding the wage inflation. This is building into the cost structure of the real economy players, and therefore, our corporate clients, as well, and to what extent it should be taken into consideration.

We are very mindful of this, and we are monitoring the situation in different industries, and in particular clients, as well. So far, we haven't identified this as a material factor, in terms of increasing the risk profile of our clients or of our potential clients. But this is, obviously, something we have to look at, and we continue to monitor.

This is a very important factor we are looking at, and this is also a concern for our risk management. So, this is an important topic that you mentioned.

What we see today is more at a macro level, that the very tight labour market puts a lid on GDP growth. This is developing into an impediment to growth that a capacity increase, even if capital were available, and even if investments could be done, the scare labour supply creates limitation to growth overall.

In terms of relating this situation to the previous crisis we had ten years ago, I think the situation is very, very different.

Clearly, the 2008 crisis in Eastern Europe or in Hungary did not happen because of tight labour markets, or high wage inflation. This certainly was not the case. To what extent the current situation can turn sour, I don't know. Again, if anything, the tight labour market reduces the potential growth rate. Therefore, it somewhat cools down the overall GDP growth, just coming from the capacity constraint part.

You could argue that this is going to result in high inflation, for instance, but we don't see high inflation. Inflation is quite moderate. It's still below the target of the central bank; it lingers around 2%. It has not, so far, translated into high inflation, or it hasn't translated into excessive growth in consumption, for instance.

Or it hasn't translated into worsening terms of trade, or increase in current account deficit. We still have a material current account surplus. Consumption is growing, but the growth is less than 5%. It's 4.5% something as for consumption growth. Inflation is under control, so it doesn't seem to manifest any problematic signs, as such.

Alan Webborn: That's interesting. Thank you for your thoughts.

Operator: Laszlo, it appears that the final question today comes from Conrad Scheurkogel of Artha Capital. Conrad, please go ahead.

Conrad Scheurkogel: Laszlo, thank you for your presentation. I was going to ask about the M&A strategy, but in the last two or three questions, it came up on a number of occasions. Essentially, it was just to hear what the pipeline looks like beyond Romania, and what does pricing look like?

To a large degree, it's been answered. If there's anything else you want to add, you can. For argument's sake, I look at your slide 25 where you see the nice progression on the Croatia ROE, so it clearly makes sense to see successful M&A. Like I say, if you want to add anything to that, it would be welcome, otherwise, it's clear that you seem to look at other opportunities.

Laszlo Bencsik: Thank you for giving the opportunity, but honestly, at this stage, there's nothing more we can talk about. I hope that in the future, there will be concrete opportunities to share more on this.

Operator: We have one last question, which is a follow-up question from Pawel Dziedzic of Goldman Sachs. Pavel, please go ahead.

Pawel Dziedzic: I have a small follow-up question. You talked about pressure on costs in Hungary, and wage pressure. If I look at your employee number, it's actually growing up quite fast. There is more than 400 employees in the OTP Group, if I look over the last 12 months, and I think you added over 200, it seems, in the first quarter of this year. Could you just comment on that? What is it driven by, and maybe what are your expectations going forward? Thank you.

Laszlo Bencsik: Again, when we talk about investment into digital, it's not just Capex investments, it's also investing into people. We are hiring IT professionals in a big way, so that's quite a large part of this picture. We are trying to in-source IT development generally, so previously contracted developments we try to bring in-house, and we are hiring heavily in IT and in IT development.

Part of this is also related to the network. Our activity is related to new volumes of production. If new volumes of production grow 30%, 40% year-on-year, then, in fact, the burden on the network increases, as well. So, out of this 200 FTE (full-time employee) growth, for instance, in the first quarter, 60 was related to IT, and the rest was related to business, mostly the network. So, roughly 30% went to IT, the rest went to the business lines.

Pawel Dziedzic: I understand those that relate to IT, the personnel expense there will be, at least, partially offset by lower admin IT expenses? Or is this the wrong way to think about this?

Laszlo Bencsik: It should have an impact on the future amortisation and depreciation. Because, previously, when we contract external developers, and they develop the software, then we create an immaterial asset, and then we amortise it, and it comes through the depreciation line. Theoretically, the future depreciation will be less, and we have more upfront OPEX.

Pawel Dziedzic: Understood. Can I just ask one more clarification? And it relates to this opinion of the Advocate General of the European Court of

Justice. You mentioned, at the beginning of your presentation, that it doesn't really change anything when it comes to current situation of Hungarian courts.

So, can you just confirm if that, essentially, means that you will not expect any impact on the back of that, even, let's say, if the ruling will be such that it will allow the courts to rule on the fairness of FX loans?

Laszlo Bencsik: The Hungarian courts have been ruling on the fairness and properness of the banking information provided for clients, in case of contracting FX loans. There's a difference between the fairness of the contract and the fairness of the information provided to the clients.

The case here focuses on the latter, namely whether the banks informed clients properly and fairly, when they sold these loans. Whether the contract and the information provided to the customer was comprehensive enough to provide the necessary information for the customer, related to the FX risk, in particular, and other types of risk of this contractual obligation.

This element of these contractual relationships has been examined by Hungarian courts. We have court cases ongoing. In our understanding, it's not a question whether Hungarian courts can or cannot assess the fairness of the information provided at the time of contracting FX loans, because it's clear that they can and they have been.

Pawel Dziedzic: Is it possible that you will see increased charges on the back of those rulings? Is there a system that would, essentially, support individuals in questioning the legacy contract? Or perhaps it would be difficult, and each case would have to be dealt with separately, and so on. I'm trying to understand if there is a risk of any potential charge down the line, or is this more of a splitting hairs on something that is already a closed chapter in Hungarian, let's say, history with conversion?

Laszlo Bencsik: I think we have to differentiate here between the legal standing of FX loan contracts, and whether the banks provided the right level of information or not, and properly informed the customer, as they should have informed. The first aspect, in my understanding, is not a question.

Regarding the second one, the Hungarian courts have been examining this, based on individual court cases, whether banks provided the proper and fair level of information when contracting clients or not. This is not going to end. The clients will have the right to appeal to courts, and the courts will continue to rule on this.

Regarding the European Court decision, the verdict, we don't know what it's going to be. This is going to come out somewhere in the second half of this year. The Advocate General formulated an opinion, which, as far as I know, is not binding for the court. The court has the right to decide. From our point of view, as far as we understand the case and the situation, we don't expect that this is going to change in a meaningful way, the situation or the treatment of these FX contracts.

Pawel Dziedzic: That's very helpful. Thank you very much.

Operator: Laszlo, that was the final question, so I'll hand back to you for any further remarks.

Laszlo Bencsik: Thank you for participating on this conference call, and thank you for your very good questions and for your interest. I hope you will join us next time on the 10th August, when we are going to talk about the second quarter results. I wish you all the best, and good bye.

Note: unabridged transcript with minor English stylistic corrections.