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Fitch Affirms Romanian UniCredit Bank at 'BBB'; Outlook Stable

Fitch Ratings - Warsaw - 15 Dec 2022: Fitch Ratings has affirmed UniCredit Bank S.A.'s (UCBRO) Long-Term Issuer Default Rating (IDR) at 'BBB' with a Stable Outlook, and Viability Rating (VR) at 'bb'. A full list of rating actions is below.

Key Rating Drivers

UCBRO's IDRs and Shareholder Support Rating (SSR) reflect a high probability of support from the bank's majority owner, UniCredit S.p.A. (UC, BBB/Stable). The Stable Outlook on UCBRO's IDRs reflects that on the parent.

The bank's VR reflects certain weaknesses in UCBRO's standalone credit profile compared with larger domestic peers'. These include a higher impaired loan ratio, lower profitability ratio and weaker overall franchise. UCBRO's VR also captures its strong capitalisation and stable funding and liquidity profile.

Support-Driven IDRs: We believe UC would have a strong propensity of to support UCBRO, given the inclusion of UCBRO in UC's single-point-of-entry (SPE) resolution group and considerable reputational risk for UC from a default of its Romanian subsidiary.

Growing Economic Pressures: Romania's significantly slowing economic growth in 2023, coupled with high inflation and monetary tightening, will weigh on banking sector performance by limiting lending growth and exerting pressure on banks' operating expenses. However, improved interest margins, low unemployment and banks' generally reasonable underwriting should contain most of these risks. We believe that the operating environment for banks will be consistent with a 'bb+' score even in a one-notch downgrade of the Romanian sovereign IDR.

Reasonable Business Profile: UCBRO benefits from being part of the UniCredit group, but its domestic franchise is moderately weaker than that of other medium-sized Romanian peers rated by Fitch. The bank's sound capital and liquidity buffers support business-model stability, but its historically lower-than-peers' profitability and corporate focus result in sizeable concentrations on both sides of the balance sheet and continues to weigh on our business- and risk-profile assessments.

Prudent Underwriting, Above-Average Concentrations: We view UCBRO's underwriting standards as prudent and which adapt promptly to changing circumstances, while its risk controls are adequate for the bank's complexity. The bank remains exposed to higher industry concentrations than larger peers due to its business mix being skewed towards corporate-and-investment banking.

Asset-Quality Improved, Upward Pressures: UCBRO's Stage 3 loans decreased to 4.5% of gross loans

at end-1H22 (end-2021: 5.9%) due to lower impaired loan generation and some recoveries. We believe that residual risks related to the bank's impaired loans are small given solid coverage by loan loss allowances.

Pressure on asset quality may rise over the next two years, given the anticipated slowing of the Romanian economy affecting predominantly non-retail borrowers, but the impact on loan-quality metrics should be largely contained.

Profitability Below Peers': UCBRO's operating profitability at 3% of risk-weighted assets (RWAs) was stable in 1H22, as wider margins were offset by weaker trading results and higher operating costs and loan impairment charges. Higher interest rates should continue to support UCBRO's net interest margin (NIM) in 2023 but are likely to be partly offset by higher funding costs, moderating business growth, a rise in cost of risk, while inflation will continue to weigh on operating expenses.

Adequate Capital Buffers: UCBRO's dividend pay-outs, coupled with the negative revaluation of its securities portfolio due to rising interest rates, reduced the bank's common equity Tier 1 ratio to 16.3% at end-1H22. We expect the common equity Tier 1 (CET1) ratio to remain comfortable over the next two years, supported by higher profit retention, but also moderated growth.

Weaker Deposit Franchise: UCBRO has a reasonably diversified funding structure and maintains adequate liquidity. Its funding mix reflects its weaker deposit franchise in the retail segment and higher reliance on wholesale funding and funding from the parent relative to its peers operating in CEE. The bank's loans/deposits ratio (90% at end-1H22) remains above-peers'.

Rating Sensitivities

Factors that could, individually or collectively, lead to negative rating action/downgrade:

UCBRO's IDRs and SSR could be downgraded if UC's Long-Term IDR is downgraded. UCBRO's IDR and SSR could also be downgraded in case of an adverse change in the resolution strategy of the group with respect to UCBRO.

We could downgrade the VR if asset quality weakens due to a rise in problem loans that is not adequately provided for and without clear prospects for improvement, in particular if the impaired loan ratio rises towards 10% on a sustained basis. Operating profitability deterioration without clear prospects for recovery, reflected in a decline of operating profit/RWAs sustainably below 1.25%, could also result in a VR downgrade.

Factors that could, individually or collectively, lead to positive rating action/upgrade:

An upgrade of UCBRO's IDR and SSR would require an upgrade of the parent's IDRs.

An upgrade of UCBRO's VR would require a combination of: i) strengthening of the bank's overall business profile, including further diversification of its loan exposure and deposit base across customer segments and ii) strengthening of underlying profitability and asset quality.

VR ADJUSTMENTS

The operating environment score of 'bb+' is below the 'bbb' category implied score for Romania due to the following adjustment reasons: macroeconomic stability (negative).

The asset quality score of 'bb' is above the 'b & below' category implied score due to the following adjustment reasons: collateral and reserves (positive) and non-loan exposures (positive)

Best/Worst Case Rating Scenario

International scale credit ratings of Financial Institutions and Covered Bond issuers have a best-case rating upgrade scenario (defined as the 99th percentile of rating transitions, measured in a positive direction) of three notches over a three-year rating horizon; and a worst-case rating downgrade scenario (defined as the 99th percentile of rating transitions, measured in a negative direction) of four notches over three years. The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Best- and worst-case scenario credit ratings are based on historical performance. For more information about the methodology used to determine sector-specific best- and worst-case scenario credit ratings, visit <https://www.fitchratings.com/site/re/10111579>

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

Public Ratings with Credit Linkage to other ratings

UCBRO's IDRs and SSR are driven by support from UC and therefore linked to the latter's IDRs.

ESG Considerations

Unless otherwise disclosed in this section, the highest level of ESG credit relevance is a score of '3'. This means ESG issues are credit-neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg

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Rating Actions

ENTITY/DEBT	RATING		RECOVERY	PRIOR
UniCredit Bank S.A.	LT IDR	BBB 	Affirmed	BBB 
	ST IDR	F2	Affirmed	F2
	Viability	bb	Affirmed	bb
	Shareholder Support	bbb	Affirmed	bbb

RATINGS KEY OUTLOOK WATCH

POSITIVE		
NEGATIVE		
EVOLVING		
STABLE		

Applicable Criteria

[Bank Rating Criteria \(pub.07 Sep 2022\) \(including rating assumption sensitivity\)](#)

Additional Disclosures

Solicitation Status

Endorsement Status

UniCredit Bank S.A. EU Issued, UK Endorsed

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