FitchRatings

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Fitch Affirms Romanian UniCredit's IDR at 'BBB+'; Upgrades VR to 'bb+'

Fitch Ratings - Warsaw - 19 Nov 2024: Fitch has affirmed UniCredit Bank S.A.'s (UCBRO) 's Long-Term Issuer Default Rating (IDR) at 'BBB+' with a Stable Outlook. Fitch has also upgraded the Viability Rating (VR) to 'bb+' from 'bb' and removed it from Rating Watch Positive (RWP). A full list of rating actions is below.

The upgrade of UCBRO's VR reflects the strengthened operating environment for banks in Romania and its associated benefits for the bank's risk and financial profiles, but also continued improvements in its standalone financial performance. The removal from RWP reflects Fitch's assessment that following the upgrade of the VR, the anticipated benefits and positive implications of the planned merger with Alpha Bank Romania S.A. (ABR) are less likely to result in an immediate further upgrade of the VR upon the merger's closure.

Key Rating Drivers

Support-Driven IDRs: UCBRO's IDRs and Shareholder Support Rating (SSR) reflect a high probability of support from the bank's majority owner, UniCredit S.p.A. (BBB+/Positive), given its inclusion in UniCredit's single-point-of-entry resolution group and the considerable reputational risk for UniCredit from a default of its Romanian subsidiary.

Stable Outlook, Country Ceiling: Romania's country risks, in particular transfer and convertibility as expressed by the Country Ceiling of 'BBB+', may limit UCBRO's ability to use parental support to service its foreign-currency obligations. Given that we expect the Country Ceiling to move in tandem with the sovereign rating, the Stable Outlook on UCBRO's Long-Term IDR reflects that on the Romanian sovereign. UCBRO's Short-Term IDR of 'F2' mirrors that of the parent.

Strategic Subsidiary: Our support assessment also factors in the strategic importance of UCBRO to the parent and its small relative size, meaning any support would be immaterial relative to UniCredit's ability to provide it. UniCredit's commitment to the Romanian market is underpinned by the ongoing acquisition of ABR that will ultimately be merged with UCBRO, strengthening the group's position in the market. The common branding and the significant integration between the parent and the subsidiary also contribute positively to our assessment of UniCredit's propensity of support.

Gradually Improving Standalone Profile: UCBRO's VR reflects its moderate franchise and weaker through-the-cycle profitability than at larger domestic peers. It also considers its moderate asset quality, strong capital ratios for the rating level and reasonable funding and liquidity. The planned merger with ABR will enhance the combined entity's market position and holds potential for medium-term strategic and operational advantages, while generating operational risks in the short term.

Improved Operating Environment: Strong GDP growth, supporting income convergence with EU averages, labour market resilience and the sector's large exposure to Romanian sovereign (BBB-/Stable), coupled with larger scale, reduced fragmentation of the sector and improved diversification of income streams translate into better prospects for the standalone credit profiles of Romanian banks. Consequently, we have revised the operating environment score for Romanian banks to 'bbb-' from 'bb+'.

Asset Quality Converges to Peers: We expect UCBRO's impaired loans ratio, which has reduced to below 4% over the past two years, to remain broadly stable after the merger, given sound asset quality at ABR. The main source of credit risk from the merger primarily relates to ABR's higher exposure to commercial real estate. However, we believe that incremental loan impairment charges can be comfortably absorbed by UCBRO's healthy loan-loss buffers.

Improving Structural Profitability: UCBRO's structural profitability improved in recent years, driven by a stronger net interest margin, increased fee income generation and better operating efficiency. However, integration and restructuring costs are likely to impact the combined entity's profitability next year. As a result, we expect the operating profit/risk-weighted assets (RWAs) to temporarily weaken to around 3.7%, but to improve in the medium term due to synergies and cost savings.

Adequate Capital Buffers: Fitch views UCBRO's capital ratios as solid for its rating and risk profile with a common equity Tier 1 ratio (20.7% at end-1H24) that compares well with regional peers. Capitalisation benefits from sound internal capital generation, and provides flexibility for growth. The expected structure of the transaction, as a merger rather than acquisition due to UniCredit's direct participation, largely mitigates the risks to the combined entity's capital position.

Generally Stable Funding: UCBRO has a reasonably diversified funding mix, with higher reliance on wholesale funding and funding from the parent than its peers operating in CEE owing to its weaker, although organically growing, retail franchise. The enlarged franchise post planned merger with ABR will reinforce UCBRO's systemic importance, although the combined entity is likely to maintain a loans/deposits ratio (end-1H24: 90% at UCBRO) higher than direct peers.

Rating Sensitivities

Factors that Could, Individually or Collectively, Lead to Negative Rating Action/ Downgrade

UCBRO's IDRs and SSR could be downgraded if UniCredit's Long-Term IDR was downgraded or Romania's Country Ceiling was revised down. UCBRO's IDR and SSR could also be downgraded on an adverse change in the resolution strategy of the group with respect to UCBRO.

UCBRO's VR could come under pressure if there was a sustained weakening of the bank's impaired loans ratio above 5% that was not adequately provided for, coupled with profitability deterioration leading to a decline of operating profit to below 1.25% of RWAs on a sustained basis. The CET1 ratio falling materially below 16% without credible plans to swiftly restore it, would also be credit negative.

Factors that Could, Individually or Collectively, Lead to Positive Rating Action/Upgrade

An upgrade of UCBRO's IDRs and SSR would require both an upgrade of the parent's IDRs and an upward revision of Romania's Country Ceiling.

A VR upgrade could follow a successful completion of the merger, contingent upon a smooth integration process that strengthens the bank's business profile and enhances its franchise. An upgrade would also be contingent on UCBRO maintaining strong capital ratios with sizeable buffers over their regulatory minimum requirements, while achieving asset quality and profitability in line with the largest Romanian peers.

VR ADJUSTMENTS

The earnings & profitability score of 'bb+' is below the 'bbb' implied category score due to the following adjustment reasons: revenue diversification (negative).

The capitalisation & leverage score of 'bbb-' is below the 'a' implied category score due to the following adjustment reasons: business and risk profile (negative).

The funding & liquidity score of 'bb+' is below the 'bbb' implied category score due to the following adjustment reasons: deposit structure (negative).

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 are linked to UniCredit S.p.A.'s IDRs and Romania's sovereign rating.

ESG Considerations

The highest level of ESG credit relevance is a score of '3', unless otherwise disclosed in this section. A score of '3' 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. Fitch's ESG Relevance Scores are not inputs in the rating process; they are an observation on the relevance and materiality of ESG factors in the rating decision. For more information on Fitch's ESG Relevance Scores, visit https://www.fitchratings.com/topics/esg/products#esg-relevance-scores.

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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+	Upgrade		bb
	Shareholder Support	bbb+	Affirmed		bbb+

RATINGS KEY	OUTLOOK	WATCH
POSITIVE		
NEGATIVE		
EVOLVING		
STABLE		

Applicable Criteria

Bank Rating Criteria (pub.15 Mar 2024) (including rating assumption sensitivity)

Additional Disclosures

Solicitation Status

Endorsement Status

UniCredit Bank S.A.	EU Issued, UK Endorsed

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