S&P Global
Ratings

RatingsDirect®

Research Update:

Bank of Cyprus Upgraded To 'BBB-' On Improved Funding Profile Of The Sector; Outlook Stable

February 7, 2025

Overview

- Cypriot banks have further reduced their dependence on less stable non-resident depositors and improved their loans-to-core-deposits ratio increasing funding stability in Cyprus' banking system.
- Additionally, we believe the economic environment in Cyprus will remain supportive and banks' efforts to improve efficiency will partially offset the hit from falling interest rates.
- We therefore raised our long-term issuer credit ratings on Bank of Cyprus Holdings PLC and Bank of Cyprus Public Co. Ltd.
- The outlook on both entities is stable.

PRIMARY CREDIT ANALYST

Pierre Hollegien
Paris
+ 33 14 075 2513
Pierre.Hollegien
@spglobal.com

SECONDARY CONTACT

Regina Argenio
Milan
+ 39 0272111208
regina.argenio
@spglobal.com

Rating Action

On Feb. 7, 2025, S&P Global Ratings raised its long- and short-term issuer credit ratings on Bank of Cyprus Public Co. Ltd. (BOC) to 'BBB-/A-3' from 'BB+/B'. We also affirmed our long- and short-term resolution counterparty ratings on BOC at 'BBB/A-2'.

At the same time, we raised our long-term issuer credit rating on BOC's nonoperating holding company, Bank of Cyprus Holdings PLC, to 'BB+' from 'BB-' and affirmed the 'B' short-term rating. We also raised our issue rating on the holding company's subordinated debt to 'B+' from 'B-'.

The outlook on both BOC and its holding company is stable.

Rationale

Cypriot banks have further reduced leverage in recent years. We estimate that the average loan-to-domestic core customer deposits ratio was about 62%-63% at the end of 2024, well below the peak of 185% in 2013. We do not expect major changes over the next one to two years as banks' lending is only slowly resuming momentum. Over 2024, domestic customer deposits increased by 7.2%, broadly in line with new lending, and we expect the trend to continue. In addition, thanks to their ample liquidity buffers, Cypriot banks have exited targeted longer-term refinancing operations while keeping strong regulatory ratios. Banks' net stable funding ratio stood at 188% as of end-June 2024, well above the 150% level as of end-2020. At the same time, the system's liquidity coverage ratio stood at 328% at end-June 2024. The lack of competition for deposits, resulting from ample liquidity, has also benefited banks' earnings as the cost of funding remains among the lowest in the EU.

Non-residents deposits continue to fall. Deposits from non-residents are still significant and, in our view, the country's position as an international financial centre continues to carry risks for its banks. However, the share of non-resident deposits had declined to 14.1% of total systemwide deposits as of December 2024 from about 38% at year-end 2012, reflecting authorities' actions to close accounts related to Russian customers and the impact of Western sanctions on some Russian entities and individuals introduced over the past few years. At the same time, in our view, remaining non-resident deposits have proven rather stable over the past three years, and we consider that the risk of rapid deposit outflows has materially declined compared to a decade ago. While most non-resident deposits come from outside the eurozone, only a small share of these are Russia-related.

Cypriot banks' access to capital markets has also improved, although recourse to external funding will remain limited. Banks have tapped international capital markets only occasionally over the past couple of years and mostly to build up their minimum requirement for own funds and eligible liabilities. However, strong economic momentum and improved banks' creditworthiness have supported investor confidence, giving Cypriot banks easier access to foreign capital markets.

Consequently, we see now overall lower industry risk for banks in Cyprus. Our view of lower systemwide funding risks for Cypriot banks has led us to revise our industry risk score for Cyprus to '6' from '7', and we now consider the industry risk trend to be stable. Our economic risk score remains '6', and we still see a stable trend for economic risk. Altogether, this results in a stronger banking industry country risk assessment of '6' for Cyprus, versus '7' before. The anchor for a commercial bank operating only in Cyprus is now 'bb+'.

We upgraded BOC following the improved assessment of the operating environment for Cypriot banks. In line with the rest of the system, BOC has a highly liquid balance sheet, with about 29% of its assets being cash as of September-end 2024, and an ample depositor base. As of September 2024, BOC's loan-to-deposit ratio stood at 50%, with 20% of deposits from non-resident depositors, and only about 9% from outside of the EU. Its slightly above average share of non-resident depositors results from the bank's leading position in the international business segment.

In addition, we consider that BOC's risk-adjusted profitability will be resilient over the next two years. We expect BOC to suffer significant headwinds from the reduction in interest rates, considering the liquid structure of its balance sheet. However, the bank will benefit from the build-up of significant hedging positions that reduced the net interest income sensitivity to 11% at end-September 2024 from a very high 35% as of end-2022, as well as from its efforts to improve efficiency and increase digitalization in the past.

We expect cost of risk, including impairment on repossessed real estate assets, to decline to about 65 basis points (bps) at end-2026 from 83bps as of end-September 2024 (including impairments from inorganic transactions). This is on the back of fewer nonperforming asset (NPAs) sales and due to strong economic momentum in Cyprus leading to more recoveries and limited new NPAs inflows. After BOC's core earnings to S&P Global Ratings risk-weighted assets peaked at 2.8% in 2023, we expect it will drop but remain comfortably above pre-2023 levels, when it stood well below 1%. We forecast return on assets to be close to 2.4% at end-2024, before declining to 1.7% by end-2026. This compares well with peers in the investment-grade category. Consequently, we forecast that BOC's risk-adjusted capital (RAC) ratio will be 12.5%-13.0% over the next 18-24 months, despite BOC's plans to ramp up its dividend payout to above 50%.

We also raised our long-term issuer credit rating on BOC Holdings by two notches, to 'BB+' from 'BB-'. This is because we now rate the operating company, BOC, in the investment-grade category, and consider that the risk from potential constraints on BOC upstreaming resources to BOC Holdings has reduced. We also affirmed our 'B' short-term rating on BOC Holdings. At the same time, we raised our issue rating on the holding company's subordinated debt to 'B+' from 'B-'.

Outlook

The stable outlook on our ratings on BOC and BOC Holdings balances the bank's strong capitalization and its leading position in the Cypriot banking system against the still-elevated risks we see for banks operating only in Cyprus.

Downside scenario

We could downgrade BOC and BOC Holdings over the next two years if the operating bank's RAC ratio declined below 10% or if its risk-adjusted profitability deteriorated to level no longer on par with 'BBB—' rated peers. This could materialize if the impact from lower rates on profitability is materially higher than expected or if asset quality significantly deteriorated.

We could also downgrade BOC Holdings if we anticipated that double leverage was likely to significantly exceed 120%, which could prompt us to widen the notching differential between the operating and holding entities.

Upside scenario

We are unlikely to upgrade BOC and BOC Holdings. We could raise the ratings if we thought that the bank's capitalization would materially strengthen and its forecast RAC ratio would increase to sustainably above 15%, because of significantly stronger profitability, while asset quality metrics remained resilient.

BICRA Score Snapshot--Cyprus

	To	From
BICRA group	6	7
Economic risk	6	6
Economic resilience	Intermediate risk	Intermediate risk
Economic imbalances	Intermediate risk	Intermediate risk
Credit risk in the economy	Very high risk	Very high risk
Trend	Stable	Stable
Industry risk	6	7
Institutional framework	High risk	High risk
Competitive dynamics	High risk	High risk
Systemwide funding	Intermediate risk	High risk
Trend	Stable	Positive

Banking Industry Country Risk Assessment (BICRA) economic risk and industry risk scores are on a scale from 1 (lowest risk) to 10 (highest risk). For more details on our BICRA scores on banking industries across the globe, please see "Banking Industry Country Risk Assessment Update," published monthly on RatingsDirect.

Ratings Score Snapshot

Bank of Cyprus Public Co. Ltd.

	To	From
Issuer credit rating	BBB-/Stable/A-3	BB+/Positive/B
SACP	bbb-	bb+
Anchor	bb+	Bb
Business position	Adequate (0)	Adequate (0)
Capital and earnings	Strong (+1)	Strong (+1)
Risk position	Adequate (0)	Adequate (0)
Funding	Adequate (0)	Adequate (0)
Liquidity	Adequate (0)	Adequate (0)
Comparable ratings analysis	0	0
Support	0	0
ALAC support	0	0
GRE support	0	0
Group support	0	0
Sovereign support	0	0
Additional factors	0	0

SACP--Stand-alone credit profile. ALAC--Additional loss-absorbing capacity. GRE--Government-related entity.

Related Criteria

- Criteria | Financial Institutions | General: Risk-Adjusted Capital Framework Methodology, April 30, 2024
- General Criteria: Hybrid Capital: Methodology And Assumptions, March 2, 2022
- Criteria | Financial Institutions | Banks: Banking Industry Country Risk Assessment Methodology And Assumptions, Dec. 9, 2021
- Criteria | Financial Institutions | General: Financial Institutions Rating Methodology, Dec. 9, 2021
- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- General Criteria: Group Rating Methodology, July 1, 2019
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Related Research

- Banking Industry Country Risk Assessment Update: January 2025, Jan. 30, 2025
- Banking Industry Country Risk Assessment: Cyprus, Sept. 27, 2024

Ratings List

Ratings Affirmed		
Bank of Cyprus Public Co. Ltd.		
Resolution Counterparty Rating	BBB/--/A-2	
Upgraded		
	To	**From**
Bank of Cyprus Public Co. Ltd.		
Senior Unsecured	BBB-	BB+
Bank of Cyprus Holdings PLC		
Subordinated	B+	B-
Upgraded; Outlook Action		
	To	**From**
Bank of Cyprus Public Co. Ltd.		
Issuer Credit Rating	BBB-/Stable/A-3	BB+/Positive/B

Upgraded; Outlook Action; Ratings Affirmed

	To	From
Bank of Cyprus Holdings PLC		
Issuer Credit Rating	BB+/Stable/B	BB-/Positive/B