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Key rating assessment  
factors

## ACRA assigns A(RU) to the Russian National Commercial Bank (public joint-stock company), outlook Stable

The credit rating of the [RUSSIAN NATIONAL COMMERCIAL BANK \(public joint stock company\)](#) (hereinafter – RNCB, or the Bank) is based on its stable, but concentrated business profile, strong capital adequacy position, weak risk profile and adequate liquidity and funding assessment. An additional rating factor rests with Bank's moderate systemic importance for the Russian economy and a very strong state influence on its creditworthiness, according to the ACRA methodology.

RNCB is the largest credit institution of the Crimean region and a dominant player in the Republic of Crimea and the city of Sevastopol by most of performance indicators, ranking 69<sup>th</sup> on the national scale in terms of assets (as of February 01, 2017) and 48<sup>th</sup> in terms of own capital. The Bank is owned by the Russian Federation (100% control), while its nominal shareholder is the Federal Agency for State Property Management.

**High probability of extraordinary state support.** As RNCB is a dominant player in the Crimea, a strategically important market, its failure may lead to a significant deterioration of economic environment in the Republic and pose certain risks for its population, as the Bank is responsible, among other things, for servicing a significant amount of social payments. At the same time, RNCB's default would hardly significantly impact the federal budget and the budgets of regions it operates in. According to ACRA, the said factors point to a medium degree of RNCB's systemic importance.

The state executes shareholder control (through its 100% ownership) and operational control (by defining strategy and providing capital) over RNCB's activities. Providing loans for financing pivotal infrastructure projects in Crimea and Sevastopol, RNCB is thus involved in activities of national importance. The Agency believes that the state has a very strong influence on the Bank's performance.

**Business profile risks are related to regional specifics of RNCB's activities, as well as to the uncertainty arising in the course of merger with Krayinvestbank.** Presently, the Bank's strategy aims at building up its loan portfolio, mainly through lending to SMEs and individuals in the Republic of Crimea and the city of Sevastopol. The Agency points out that, to date, loan portfolio growth was not accompanied by a significant increase in bad debt. However, as loans given out in the Crimea mature, the situation may change to the worse.

According to ACRA, the Bank is a dominant player in its core region of presence, mainly due to the fact that financial service market leaders abstain from operating in the Crimea for fear of international sanctions. The Agency believes that a reduction in the sanctions-related risk might well hamper RNCB in implementing its strategy.

This factor, coupled with risks pertaining to operational integration of Krayinvestbank and related strategic uncertainties, caps the Agency's assessment of RNCB's strategy.

The Bank's business profile assessment is based on its strong operating income diversification and a pronounced regional concentration.

The Agency believes that RNCB looks weaker than its peers in terms of business profile, which forces ACRA to lower this factor's assessment.

**High own capital adequacy** by both international standards (Tier1 equaled 67% at end-2016) and Russian regulatory requirements (N1.2 stood at 45.93% as of March 1, 2017) provides for a significant loss absorption cushion.

RNCB maintains operational profitability and pays out part of its net income as dividends, with its averaged capital generation ratio (ACGR) standing moderately high at 438 bps. However, the Agency notes that Bank's capital generation indicators are to a large extent influenced by its 2014 results, achieved before the Bank opted for the current strategy.

ACRA believes that RNCB will keep its capital adequacy high in the process of merging with Krayinvestbank which may result in additional loan loss provisioning

ACRA highlights a high level of net interest margin (8.2% in 2016) along with capped operational efficiency (CTI stood at approximately 70% in 2016).

**ACRA assesses the Bank's risk profile as weak** due to the possible significant increase of bad debt share within RNCB's loan portfolio resulting from merger with Krayinvestbank.

By the Bank's estimate, as of December 31, 2016, the proportion of bad debt (NPL 90+) within its portfolio was not exceeding 1%. ACRA believes that this indicator may soar in the process of merging with sanated Krayinvestbank, whose loan portfolio quality is extremely low.

However, RNCB's portfolio is highly concentrated due to a number of large loans in it (loans to 10 largest borrowers make up over 40% on the Bank's total portfolio).

As for the sectoral structure of the Bank's portfolio, there is no concentration on industries marked by high risks. The Agency notes that RNCB provides loans for financing infrastructure projects that may bear higher risks. However, their share in the Bank's portfolio (40% of Tier-1) does not entail adjustment of risk profile assessment under ACRA's methodology.

Although the Bank's loan portfolio demonstrated substantial growth (approximately 100%) in 2016, it was largely attributed to the low base effect, which gives the Agency grounds to limit negative adjustment. However, ACRA would like to point out that rapid growth of loan portfolio planned by the Bank may become a negative factor for RNCB's credit rating in the future.

The Bank places a large share of its assets (6%) into securities; however, funds are invested into high-quality instruments resulting in accepted market risk mitigation. The Bank's operating risk is also acceptable.

The Agency assesses the Bank's risk management quality as satisfactory.

**Liquidity and funding position of RNCB is assessed as adequate.** The Agency points out that the Bank's liabilities maturing in less than 90 days are well backed by liquid assets.

The short-term liquidity shortage indicator (STLSI), calculated for RNCB, shows that under the base case scenario the Bank has a liquidity surplus amounting to RUB 44.3 bln. Under the stress scenario, excessive liquidity of the Bank stands at 38.9%.

This situation is mainly defined by the fact that RNCB keeps roughly 60% of its assets in the form of cash and receivables from banks and financial institutions (represented by companies with high creditworthiness levels). The Bank's securities portfolio may be an additional source of liquidity.

ACRA also foresees no imbalances in the longer terms. The long-term liquidity shortage indicator (LTLSI) exceeds 75%, which implies adequate backing of liabilities.

The Agency notes the Bank's low dependence on largest creditors' (depositors') funds, which positively affects funding assessment. At the same time, as of December 31, 2016, over 60% of the Bank's total liabilities were represented by funds of individuals and private entrepreneurs.

## Key assumptions

- Retaining the Russian government's shareholder control over the Bank;
- Retaining the current business model of the Bank within the 12 to 18-month horizon;
- Retaining the current liability structure;

- Tier-1 capital adequacy (N1.2) not lower than 10% within the 12 to 18-month horizon;
- NPL 90+ lower than 5%.

## Potential outlook or rating change factors

The **Stable outlook** assumes that the rating will most likely stay unchanged within the 12 to 18-month horizon.

### A positive rating action may be prompted by:

- A successful implementation of the current strategy;
- An increase in the business scale of the Bank;
- A decline in concentration of the loan portfolio while retaining its quality.

### A negative rating action may be prompted by:

- A deterioration of competitive environment in the key region of presence;
- A decline in asset credit quality as a result of a rapid loan portfolio growth;
- A material deterioration of RNCB's financials after merging with Krayinvestbank;

## Rating components

**Standalone creditworthiness assessment (SCA):** bbb.

**Adjustments:** state influence, 3 notches up against the SCA level.

## Issue ratings

No outstanding issues have been rated.

## Regulatory disclosure

The credit rating has been assigned under the national scale for the Russian Federation and is based on the [Methodology for Credit Ratings Assignment to Banks and Bank Groups Under the National Scale for the Russian Federation](#), the [Methodology for Analyzing Relationships Between Rated Entities and the State](#), and the [Key Concepts Used by the Analytical Credit Rating Agency Within the Scope of Its Rating Activities](#).

A credit rating has been assigned to RNCB for the first time. The credit rating and its outlook are expected to be revised within one year following the rating action (April 7, 2017).

Disclosure of deviations from the approved methodologies. The RNCB's risk profile assessment has been lowered by one notch against the calculated level, as the Agency considers very likely a deterioration in the Bank's loan portfolio credit quality on a consolidated basis, accounting for Krayinvestbank's assets.

The assigned credit rating is based on the data provided by RNCB, information from publicly available sources, as well as ACRA's own databases. The rating analysis was performed using IFRS consolidated statements of RNCB and statements of RNCB composed in compliance with the Bank of Russia Ordinance No. 4212-U dated November 24, 2016. The credit rating is solicited, and RNCB participated in its assignment.

No material discrepancies between the provided data and the data officially disclosed by RNCB in its financial statements have been discovered.

ACRA provided no additional services to RNCB. No conflicts of interest were discovered in the course of credit rating assignment.

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