

August 18, 2017

AO UniCredit Bank

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Key rating assessment factors

Credit rating components	
Business profile	
First stage	a
Second stage	a+
Key risk factors	
Capital adequacy	Strong (+2)
Risk profile	Adequate (+1)
Funding and liquidity	Adequate (0)
SCA	aa+
Adjustments	
Systemic	0
Individual	0
Support	
Systemic importance	2
Group support	+5 notches to the SCA
State support	0
Credit rating	AAA(RU)
Outlook	Stable

Very high likelihood of shareholder extraordinary support. If necessary, UniCredit Group via its parent bank structure UniCredit S.p.A. (hereinafter – supporting organization, SO) is ready to provide [AO UniCredit Bank](#) with both, short-term and long-term financing, and replenish its capital due to:

- Strategic importance of the Russian market for UniCredit Group;
- Pronounced operating integration (SO exerts strategic and partially operating control over the Bank, being a part of a corporate investment business platform of UniCredit Group);
- Significant operating, financial and reputational risks arising in the event of the Bank's potential default.

The final assessment of country risk of the Group's jurisdiction of presence against Russia's country risk is defined by ACRA as generally strong, the assessment of SO's creditworthiness – as moderately strong, the degree of relationships between the Bank and its shareholder – as very strong. Consequently, UniCredit Bank's credit rating is defined by adding five additional notches to its standalone creditworthiness assessment (SCA).

Strong business profile. Due to rather universal nature of the Bank's activities, diversification of its operating income is assessed as moderately high (the Herfindahl-Hirschman index is 0.25). UniCredit Bank's strategy for 2017 is generally in line with current macroeconomic trends, and is defined by ACRA as adequate. High assessment of the Bank's management quality is manifested by successful long-term experience of its top managers both, in Russia and abroad, coupled with control over the Bank's activities on the part of UniCredit S.p.A.

A significant loss absorption buffer rests upon The Bank's high own capital level by both, Russian regulatory requirements (N1.2 and N1.1 amounted to 13.7% as of May 1, 2017) and international standards (Tier-1 equaled 17.2% as of April 1, 2017), which allows the Bank to withstand a significant (over 500 bps) growth of credit risk without notable regulatory consequences. Moreover, UniCredit Bank is marked by stable profitability regardless of a phase of an economic cycle, which, coupled with a conservative dividend strategy, conditions rather strong capital generation within the last five years (the Bank's averaged capital generation ratio, ACGR, amounts to 165 bps).

Adequate risk profile assessment is based on UniCredit Bank's high-quality risk management system, manifested through transparency and independence in internal decision-making, regularly streamlined risk policies, as well as stress testing of capital adequacy, liquidity, and market risk indicators. The Bank's loan portfolio (54% of assets) quality is defined as satisfactory due to an acceptable level of problem and potentially problem loans amounting to 10.1% of loan portfolio (of which 7% is attributed to NPL90+, and 3.1% is represented by restructured loans). Loan portfolio concentration on 10 largest groups of borrowers remains moderate (26%), while concentration thereof on industries bearing high risks remains low (24% of own capital).

Strong liquidity position is defined by a large amount of liquid and highly liquid assets, which translates into sufficient coverage of potential outflows with highly liquid assets (over the past six months, the liquidity coverage ratio, LCR, averaged 116%).

Satisfactory funding profile. The main share of UniCredit Bank's resource base is formed by corporate deposits (68% of liabilities), mostly raised on a fixed-term basis. Approximately 44% of the Bank's liabilities (over RUB 400 bln) is constituted by funds from ten largest depositors (creditors). UniCredit Bank does not raise funds from the regulator.

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 negative rating action may be prompted by:

- Negative changes in UniCredit Group's propensity to support the Bank;
- Material aggravation of SO's creditworthiness.

Brief information about the bank

UniCredit Bank is a systemically important bank, which is 100%-owned by UniCredit S.p.A (Italy). The Bank occupies leading positions in terms of assets and capital in the Russian banking sector (it is among the top 10 largest banking groups), and is an important player on the market of corporate banking services. UniCredit Bank operates a wide branch network scattered across six RF federal districts with a focus on Moscow, as well as a representative office in the Republic of Belarus.

Rating assessment factors **Business profile (a+)**

UniCredit Bank's adequate business profile is determined by its sustainable franchise, sufficiently high diversification of its operating income, high-quality management system, adequate development strategy, and transparent ownership structure.

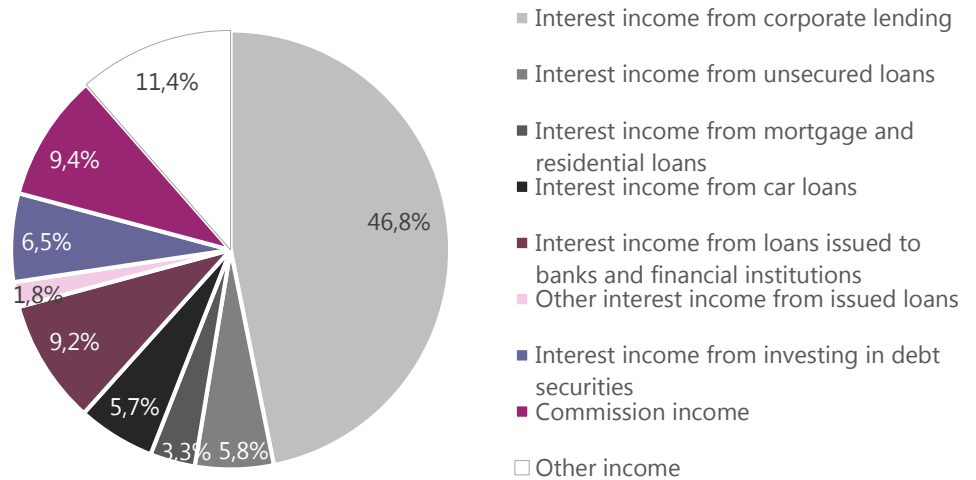
High assessment of the Bank's franchise factor is defined by significant positions of UniCredit Bank in the Russian banking system, which is confirmed by its strong and recognizable brand (as of March 31, 2017, the Bank's creditor base was constituted by approximately 200,000 legal entities and 765,000 individuals). The universal nature of the Bank's business translates into sufficiently high diversification of its pre-provision operating income (the Herfindahl-Hirschman index amounts to 0.25), whose dynamics is assessed as generally stable (with due account for the period of economic downturn in Russia starting from 2014).

The Bank's assets comprise issued loans (54%), mainly to corporate clients (45% of assets), interbank claims (27%), as well as investments in securities and other financial instruments (10%). Liabilities are formed mainly by clients' funds (85% of the resource base). We do not expect a significant change in the structure of the Bank's balance sheet in the next 12-18 months.

High quality of UniCredit Bank's management stems from successful long-term experience of its managers both in Russia and abroad, control over the Bank's activities on the part of the supporting organization, and availability of established vertical

decision-making and risk control systems within UniCredit Group. Macroeconomic assumptions included in the Bank's strategy for 2017 are assessed by ACRA as adequate.

Figure 1. Diversification of UniCredit Bank's operating income as of March 31, 2017



Source: AO UniCredit Bank

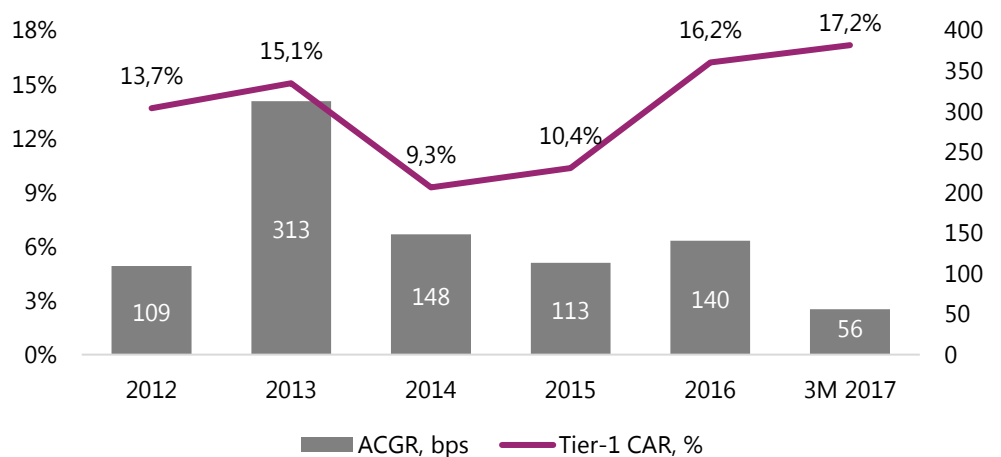
Key risk factors

Capital adequacy: strong (+2)

Strong assessment of UniCredit Bank's capital adequacy hinges on a significant loss absorption cushion in terms of accepted risks, sufficiently high capital generation, and efficient performance.

The Bank sustains a material capital adequacy cushion by both, international standards (Tier-1 amounted to 17.2% as of March 31, 2017, while the minimal recommended level is 6%) and Russian regulatory requirements (N1.2 was 13.7% as of May 1, 2017, against the minimal recommended figure of 7.6% including conservation buffer and premium for systemic importance). Due to this, the Bank is able to withstand an increase in the cost of risk significantly over 500 bps without breaking the regulatory standards in terms of the adopted development strategy. Moreover, UniCredit Bank is marked by a stable profitability regardless of a phase of an economic cycle, which, in combination with the conservative dividend strategy, translates into a sufficiently high capital generation (in 2012-2016, averaged capital generation ratio, ACGR, was 165 bps).

Figure 2. Capital adequacy and generation



Source: AO UniCredit Bank, ACRA

The level of UniCredit Bank's operating efficiency is sufficiently high: the pre-provision operating expenses to operating income ratio (cost-to-income ratio, CTI) for the past three years was 31.5%. At the same time, the net interest margin (NIM) amounts to 3.6%, which is slightly lower than the peer group average.

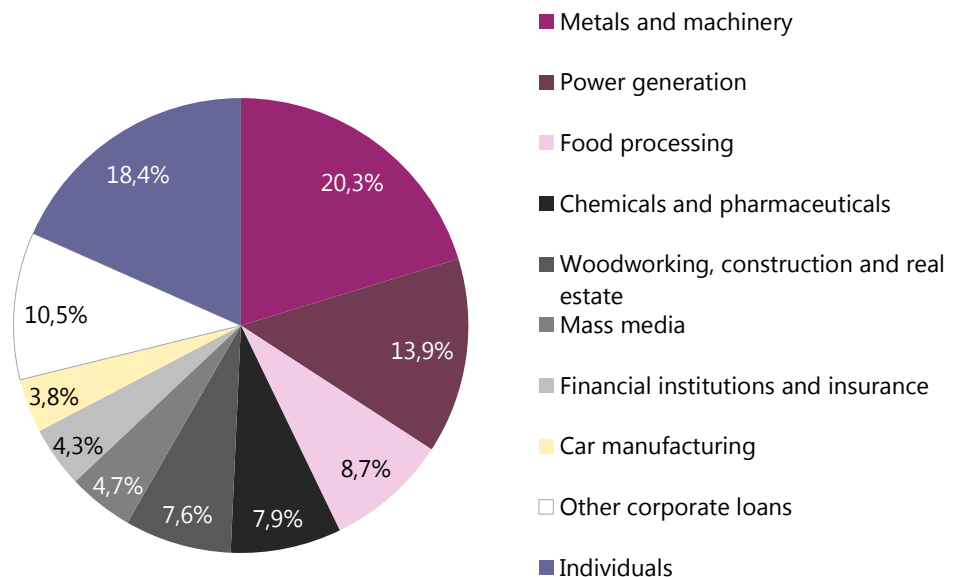
Risk profile: adequate (+1)

The adequate assessment of UniCredit Bank's risk profile is manifested by its high-quality risk management, acceptable level of problem loans, low concentration of the loan portfolio on largest borrowers and on companies pertaining to high-risk industries, as well as on high quality of the Bank's securities portfolio.

As of March 31, 2017, the share of problem and potentially problem loans in the Bank's loan portfolio equaled to 10.1%, of which 7% related to loans with a heightened risk level (overdue for more than 90 days), and 3.1% – to restructured loans. That said, approximately 50% of the abovementioned loans are covered with reserves. Concentration of the UniCredit Bank's loan portfolio on ten largest borrower groups is defined as moderate (26% of the portfolio), while concentration on high-risk industries is assessed as relatively low (24% of own capital). However, high asset concentration on related parties (143% of own capital) is due to the placement of funds mostly on accounts of the parent UniCredit S.p.A. as part of UniCredit Group's liquidity management policy. Loans in foreign currency represent a significant 50% portion of the portfolio; however, their share is being reduced, and the Bank efficiently manages its open foreign exchange position, remaining neutral to the currency risk in the long-term.

Levels of other types of risk, i.e. market and operational, do not appear to be significant (in quantitative terms, they do not exceed the Bank's own capital). At the same time, the quality of the securities portfolio (approximately 7% of assets) is assessed as high, given the significant share of OFZ (92% of the portfolio).

Figure 3. UniCredit Bank's loan portfolio structure as of March 31, 2017



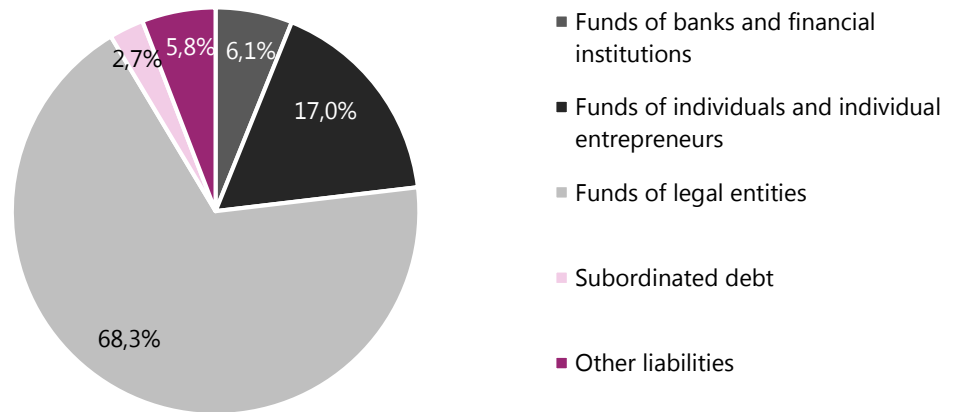
Source: AO UniCredit Bank

Taking into account the active use of standards adopted in the UniCredit Group, the Agency assesses the quality of UniCredit Bank's risk management and applied risk policies as high. The Bank implemented an independent risk management system. The strategy focuses on control over the risk function and on its modernization in the Group as a whole. Moreover, the Bank regularly performs stress testing of capital, liquidity, and market risk. UniCredit Bank adheres to a conservative policy when carrying out transactions in the interbank market and investing in securities.

Funding and liquidity: adequate (0)

UniCredit Bank's liquidity management policy is assessed by the Agency as strong due to the large volume of liquid and highly liquid assets, which translates into sufficient coverage of potential outflows of funds from the resource base (over the last six months, the liquidity coverage ratio, LCR, averaged 116%). In addition, the Bank has the ability to quickly raise short-term liquidity from the shareholder.

Figure 4. UniCredit Bank's resource base structure as of March 31, 2017



Source: AO UniCredit Bank

According to ACRA estimates, the funding factor of the Bank is satisfactory. The main portion of UniCredit Bank's resource base is formed by funds of corporate clients (68% of liabilities), attracted mainly on a fixed-term basis. Approximately the 44% share of the Bank's liabilities (over RUB 400 bln) is represented by the funds of the ten largest investors (creditors). Due to the lack of liquidity needs, UniCredit Bank does not attract regulatory funding.

Additional adjustments

Systemic

No grounds for applying systemic adjustments.

Individual

No grounds for applying individual adjustments.

Support

Systemic importance

The degree of UniCredit Bank's systemic importance in the context of the Russian banking sector is assessed by ACRA as moderate. Taking into account a significant amount of individuals' deposits (RUB 168 bln as of March 31, 2017) in the Bank's resource base, the Agency believes that a default of the Bank may lead to a systemic crisis in the Russian banking system and adversely affect the state of the Russian economy as a whole. UniCredit Bank is included in the list of systemically important credit institutions in accordance with the criteria of the Bank of Russia.

Group

On ACRA's opinion, if necessary, UniCredit Group via its parent bank structure UniCredit S.p.A. is ready to provide UniCredit Bank with both, short-term and long-term financing, and replenish its capital due to:

- Strategic importance of the Russian market for UniCredit Group;
- Pronounced operating integration (SO exerts strategic and partially operating control over the Bank, being a part of a corporate investment business platform of UniCredit Group);
- Significant operating, financial and reputational risks arising in the event of the Bank's potential default.

That being said, the degree of relationships between the Bank and its shareholder is assessed as very strong.

The final assessment of country risk of the Group's jurisdiction of presence against Russia's country risk is defined by ACRA as generally strong. In the course of the assessment, the Agency took into account levels of economic development and development of financial system of the Group's jurisdictions of presence, as well as factor of accessing international financial markets by residents of the abovementioned jurisdictions. With due account for the performed analysis, ACRA assesses the overall country risk of the Group's jurisdiction of presence substantially below the RF country risk, which corresponds to the strong jurisdiction of the Group's presence and allows the highest possible level of support for the rated entity's creditworthiness by the foreign SO provided the latter's creditworthiness gets a high final assessment.

Creditworthiness of the supporting organization is assessed as moderately strong given the quality of its loan portfolio, operating efficiency, as well as the level of capital adequacy and liquidity.

Consequently, UniCredit Bank's credit rating is defined by adding five additional notches to its SCA.

State

ACRA does not consider UniCredit Bank as a state-influenced organization.

Issue ratings

No outstanding issues have been rated.

Rating history

June 23, 2017 — AAA(RU), outlook Stable.

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](#), [Methodology for Analyzing Relationships Between Rated Entities and Supporting Organizations outside the Russian Federation](#), 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 AO UniCredit Bank for the first time. The credit rating and its outlook are expected to be revised within one year following the rating action date (June 23, 2017).

Disclosure of deviations from approved methodologies. The LTLSI and LTLSI indicators were not calculated, the liquidity factor assessment was performed by ACRA on the basis of statements drawn up by AO UniCredit Bank in compliance with forms 0409122 and 0409125. ACRA assessed the funding and liquidity factor one notch higher since the risk of low diversification of liabilities arising from a high proportion of corporate funds has already been taken into account while assessing concentration on largest creditors'/depositors' funds.

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

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

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

Appendix

Table 1. Consolidated balance sheet items, RUB mln

	2014	2015	2016	3M 2017
Assets	1,360,385	1,407,126	1,172,250	1,174,977
Cash and equivalents	19,074	14,356	12,508	10,217
Receivables from the Bank of Russia and the Ministry of Finance	58,799	8,374	48,081	46,336
Required reserve depositing with the Bank of Russia	5,894	3,875	6,282	9,775
Receivables from banks and financial institutions	291,662	332,870	261,218	316,570
Debt securities	140,495	154,927	135,087	120,211
Other financial assets assessed at fair value through profit or loss or available for sale	9	120	120	120
Loans to and receivables from legal entities, and individual entrepreneurs	676,072	749,441	567,072	523,117
Loans to and receivables from individuals	150,780	117,854	109,939	111,004
Intangible assets and goodwill	3,444	5,351	6,511	6,864
Investment property	51	47	48	47
Fixed assets	5,950	5,565	5,159	5,078
Deferred tax assets	12	0	0	0
Other financial assets	4,062	9,900	14,448	19,340
Other non-financial assets	4,082	4,446	5,777	6,300
Liabilities	1,218,319	1,242,599	990,575	987,658
Deposits by banks and financial institutions	115,110	104,538	122,931	60,265
Deposits by the Bank of Russia	81,093	38,293	0	0
Deposits by individuals and individual entrepreneurs	107,749	174,239	167,461	168,127
Deposits by legal entities	702,871	757,163	611,641	674,400
Debt securities issued	62,007	32,979	6,508	6,435
Subordinated debt	13,753	51,092	29,178	27,120
Deposits by the Deposit Insurance Agency	1	25	1	0
Deferred tax liabilities	2,609	7,391	7,573	7,426
Financial liabilities assessed at fair value through profit or loss	104,535	49,246	21,201	20,269
Other liabilities	28,591	27,634	24,082	23,615
Own funds	142,066	164,527	181,675	187,319
Charter capital	41,788	41,788	41,788	41,788
Share premium	437	437	437	437
Revaluation fund for financial assets available for sale and/or hedging	(10,612)	(3,668)	(544)	(645)
Retained earnings	110,453	125,971	139,994	145,739

Source: AO UniCredit Bank IFRS consolidated statements

Table 2. Consolidated profit and loss statement items, RUB mln

	2014	2015	2016	3M 2017
Interest income	94,918	129,941	117,454	26,508
Interest expenses	(59,302)	(89,581)	(72,354)	(15,714)
Net interest income	35,616	40,361	45,100	10,794
Impairment provision change	(4,414)	(14,621)	(17,218)	(1,658)
Net interest income after impairment provision	31,202	25,740	27,881	9,137
Commission income	7,826	8,704	9,944	2,241
Commission expenses	(1,406)	(4,325)	(3,968)	(627)
Net non-interest income	6,420	4,379	5,977	1,614
Other income net of expenses	(835)	3,807	787	549
Net income (expenses)	41,202	48,547	51,863	12,958
Administrative and other operating expenses	(13,202)	(14,943)	(17,043)	(4,107)
Income (loss) before taxes	23,586	18,983	17,602	7,193
Income tax expenses	(4,766)	(3,465)	(3,579)	(1,449)
Income (loss) after taxes	18,819	15,518	14,023	5,745

Source: AO UniCredit Bank IFRS consolidated statements

Table 3. Consolidated key financial ratios

	2014	2015	2016	3M 2017
Capital adequacy				
Tier-1 CAR	9.3%	10.4%	16.2%	17.2%
N1.2	11.75%	9.38%	13.00%	13.48%
Capital generation, bps	148	113	140	56
ACGR, bps	n/a	137	165	165
Leverage	6.1%	8.3%	10.8%	11.9%
NIM	3.4%	3.1%	3.6%	3.6%
CTI	32.1%	30.7%	32.2%	31.1%
Risk profile				
Share of NPL90+ relative to the loan portfolio	n/a	n/a	n/a	7.0%
Share of problem loans relative to the loan portfolio	n/a	n/a	n/a	10.1%
Share of 10 largest borrowers (groups of borrowers) relative to the loan portfolio	n/a	n/a	n/a	26.1%
Loan portfolio concentration on high-risk sectors (relative to own capital)	n/a	n/a	n/a	23.8%
Loan portfolio concentration on related parties (relative to own capital)	n/a	n/a	n/a	142.9%
Funding and liquidity				
Share of the largest funding source in total liabilities	57.7%	60.9%	61.7%	68.3%
Share of regulatory funding in total liabilities	6.7%	3.1%	0.0%	0.0%
Share of 10 largest clients (groups of clients) in total liabilities (net of funds borrowed from the Bank of Russia)	n/a	n/a	n/a	44.1%

Source: the Bank of Russia, ACRA

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