

## ACRA UPGRADES PROMSVYAZBANK PJSC TO AAA(RU), OUTLOOK STABLE

**SUREN ASATUROV**

Director, Financial Institutions Ratings Group

+7 (495) 139 04 80, ext. 130  
suren.asaturov@acra-ratings.ru

**IRINA NOSOVA**

Senior Director, Financial Institutions Ratings Group

+7 (495) 139 04 81  
irina.nosova@acra-ratings.ru

The credit rating of **Promsvyazbank PJSC** (hereinafter, PSB or the Bank) has been upgraded to the highest level, AAA(RU), which reflects ACRA's opinion on the growth of the Bank's importance to the state. The positive rating action is based on a combination of the following factors:

- The Agency assumes that over the long term, the state will continue to make significant efforts, which have increased substantially in recent years, to develop the country's defense industry, which strengthens the importance of PSB as the support bank for the defense industry.
- Recent changes in the law (including public order No. 2213-r dated August 16, 2024) define PSB's even greater uniqueness in terms of servicing state defense contracts (hereinafter, SDCs). In particular, PSB's absolute dominance in this segment due to the Bank's competitive position, which is fully protected at the regulatory level. Given these prerequisites, the share of SDCs serviced by the Bank may reach 100% in the near future (this ratio has increased from 30% to almost 90% from mid-2019 to the present).
- In the current realities, PSB remains practically the only financial institution that provides financial services in the new regions of the Russian Federation, and carries out initiatives to integrate these regions into the country's financial system and individual social projects in these regions. These facts increase the Bank's systemic importance to the state.
- ACRA's conclusions about the higher significance of PSB for the state are supported by the Bank's accumulated expertise in the defense industry segment. This is evidenced by its active involvement in expert and analytical activities in the interests of relevant ministries and government committees on issues of maintaining the sustainability and stability of the defense industry segment and its individual enterprises; this position has developed over the past few years. In addition, the Agency considers that such a system for assessing industry risks with the participation of PSB and government agents increases the chances of early identification of problematic situations and timely development of measures to support the Bank and/or the industry, if urgently needed.
- At the same time, the Agency notes significant growth of the Bank's market shares over the past three years in the assets and funds of individuals in the banking sector as a whole, which strengthens its role in the country's financial system.

Therefore, the Bank's credit rating at AAA(RU), outlook Stable, reflects PSB's close ties with the state and its high systemic importance, including in the context of PSB's status as the only

support bank for the country's defense industry. Based on the combination of the above factors, ACRA believes that the state will provide priority support to PSB if it is urgently needed.

Amid the strengthening of the Bank's position in the defense industry, the state regularly provides capital injections to the Bank, ensuring its ability to increase lending to this area, as well as to develop certain regions of the Russian Federation and for other goals of the strategy. Since 2019, total provision of additional capital to PSB by the state (to develop the defense industry and for other purposes) and from other banks has amounted to around RUB 164 bln.

At the same time, the ongoing gradual decline in the Bank's capitalization on a consolidated basis over the past 12 months has had a negative impact on the assessment of PSB's standalone creditworthiness assessment (SCA). Meanwhile, although the predisposition to market risk has become significantly lower, ACRA expects it to reach acceptable levels in the next 12–18 months as planned initiatives are carried out. All other things being equal, a delay or cancellation of the above initiatives leading to a slowdown in the reduction of market risks may lead to a decrease in the Bank's SCA.

Therefore, the Bank's SCA is determined by the moderately strong business profile, capital adequacy that has been lowered by one notch to weak, a risk profile that has been improved by one notch to satisfactory (due to the positive dynamics of market risk sentiment observed over the past 12 months and expectations of further stabilization of the situation in the next 12 months), and a satisfactory funding and liquidity position. ACRA assumes that risks facing the Bank's standalone creditworthiness will continue to be balanced by the very high potential of external support over the next 12–18 months.

## KEY ASSESSMENT FACTORS

**The very high degree of support to PSB from the state** is largely based on the dominating role played by the Bank in servicing Russia's military-industrial enterprises. This is evidenced by the substantial share of defense industry funding that goes through the Bank due to the consolidation of SDCs and other large government contracts. Payments for government contracts is the ultimate source for repaying these loans.

The Bank holds a significant position in the Russian banking system and therefore any disruption in its operations may cause a crisis of confidence in relation to the entire Russian banking sector and the Russian state-owned banks in particular; it may also trigger systemic financial shocks and give rise to significant financial and reputational damage to the state and social risks. ACRA notes that PSB is a dominating provider of financial services in the regions that became part of the Russian Federation in 2022.

In ACRA's opinion, the abovementioned factors combined with the Bank's total capital inflows over the past six years as part of the implementation of the strategy indicate the shareholder's very high degree of support for the Bank. The Agency's conclusions are supported by the state being strongly involved and participating in the management of the Bank's operations and making strategic decisions, since representatives of various ministries and agencies are members of the Bank's collegial bodies.

ACRA's opinion on the degree of support is expressed in PSB's credit rating being set at the same level as the Russian Federation.

**The moderately strong business profile (a-)** is determined primarily by the Bank's strong franchise, mainly its leading positions in servicing the defense industry and in the Russian financial system as a whole.

PSB's increased activity, expressed in a rapid expansion of business in 2022–2023, is due to the need to ensure ongoing maintenance and growth of business volumes of defense enterprises, as well as the Bank's implementation of its strategy to develop other business segments. Taking into account the views of PSB's management, ACRA expects, as the base case scenario, a decrease in the growth rate of the loan portfolio over the next 12–18 months, which in the Agency's opinion, indicates a relative reduction in risk appetite.

PSB quite actively participates in mergers and acquisitions, including Svyaz-Bank, ROSCOSMOSBANK, MInBank, SMP Bank's group, including MOSOBLBANK being in the financial recovery process, PSB Lugansk LLC and PSB Donetsk LLC (the former Central Republican Bank of the DPR and the State Bank of the LPR), which, in ACRA's opinion, may involve additional risk. An example of notable negative impact on the Bank's consolidated performance as a result of merger and acquisition has been observed in the past, which constrains the assessment of the business profile at the current level. Under the base case scenario, ACRA does not have any information about new M&A transactions in the next 12–18 months.

**The capital position has been downgraded from satisfactory to weak** in view of gradual negative dynamics of the consolidated capital metrics of PSB over the past 12 months amid growth of business volume.

The decline is partly offset by the Bank's financial performance, which has been maintained at high levels over the past 18 months. It is based on a more favorable interest margin due to the increase in the key rate starting from H2 2023. Last year's profit is also largely supported by volatile income items, which partially smooth out the negative impact of increased reserve expenses. In contrast, over 6M 2024, the impact of loan loss reserves and other volatile sources of revenue on the financial result was limited.

Another somewhat balancing factor is the actual and expected capital injections to the Bank by the state.

In the next 12–18 months, ACRA forecasts that profitability will decrease to values that will still be more than comfortable for the Bank, in the Agency's opinion. ACRA's main prerequisites include an increase in reserves created compared to the indicators of the first six months of 2024 (the forecast is based on the assumptions of maintaining the current level of non-performing loans and the level of their coverage by reserves with a moderate growth rate of total loans in the next 12–18 months), as well as a very significant increase in administrative expenses associated with both business growth and inflation, along with the need to maintain the large-scale network of points of presence that expanded last year, including in the new regions of the Russian Federation, together with the implementation of PSB's import substitution and digital transformation projects. At the same time, despite the predicted increase in operating costs, ACRA expects the ratio of operating costs to operating income to be maintained at a comfortable level.

**The risk profile assessment has been improved by one notch to satisfactory.** The change in assessment reflects a significant reduction in the Bank's sensitivity to market risk over the past 12 months and expectations that this positive trend will continue over the next 12–18 months. The improvement in the risk profile assessment is supported by PSB's intentions to follow a more restrained pace of portfolio growth, which in the future may help reduce the pressure from business growth on the Bank's capital.

The relatively high concentration of the loan portfolio on individual borrowers continues to constrain the assessment of its quality. Although the lending activity of previous periods has not yet led to an increase in non-performing exposures, which is reflected in the absence of negative

dynamics of Stage 3 loans in accordance with the IFRS classification by credit risk level, ACRA notes an increase in the share of loans classified as Stage 2 under IFRS over the past three years (this was triggered by the increase in sanctions pressure on the economy after the materialization of geopolitical risks in 2022, which, as a result, led to a deterioration in borrowers' conditions for doing business).

The Agency notes the relatively good quality of the loan portfolio formed by the Bank as part of the current business model<sup>1</sup> and the adequate level of impairment reserves. In the future, the assessment will depend on further changes in the quality of loans made during the period of rapid growth. The significant volumes of unsecured loans are likely to decline as a proportion of capital as the pace of credit growth slows. In addition, in ACRA's opinion, many of PSB's borrowers associated with the defense industry have high order backlogs supported by federal budget expenditures and regularly receive support from the state.

**Satisfactory funding and liquidity position.** Growth of the loan portfolio over the past 12 months led to a significant decline in the share of liquidity assets on the Bank's balance sheet. A further decline of the liquidity position is not expected due to the current more prudent appetite to business expansion. The status of a systemically important bank implies additional opportunities and the willingness of the state to provide emergency liquidity if necessary.

The key funding source is still client funds, the funding base is relatively stable and loyal and is often represented by companies that participate in SDCs; depositors are largely the same legal entities as borrowers in the loan portfolio. Significant volumes of current funds in PSB's structure of borrowings have a positive effect on the Bank's interest margin.

## KEY ASSUMPTIONS

- Prompt provision of sufficient capital and liquidity by the shareholder and related entities if necessary;
- Maintaining the current business model within the next 12 to 18 months;
- Further reduction of market risk appetite to maintain the current level of the SCA.

## POTENTIAL OUTLOOK OR RATING CHANGE FACTORS

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

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

- Lower level of the Bank's systemic importance or declining participation of the state in its operations.

## RATING COMPONENTS

SCA: **bbb**.

Adjustments: none.

Support: from the state, on par with the Russian Federation.

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<sup>1</sup> The loan portfolio was analyzed without non-performing loans of corporate clients that are almost 100% covered by reserves included in PSB's balance sheet prior to the completion of the financial recovery procedure, as well as acquired from credit institutions.

## ISSUE RATINGS

No outstanding issues have been rated.

## REGULATORY DISCLOSURE

The credit rating of Promsvyazbank PJSC has been assigned under the national scale for the Russian Federation based on the [Methodology for Assigning Credit Ratings with External Support](#), [Methodology for Assigning Credit Ratings to Banks and Bank Groups under the National Scale for the Russian Federation](#), and the [Key Concepts Used by the Analytical Credit Rating Agency within the Scope of Its Rating Activities](#).

The credit rating of Promsvyazbank PJSC was published by ACRA for the first time on October 30, 2018. The credit rating and its outlook are expected to be reviewed within one year following the publication date of this press release.

The credit rating was assigned based on data provided by Promsvyazbank PJSC, information from publicly available sources, and ACRA's own databases. The rating analysis was performed using the IFRS consolidated financial statements of Promsvyazbank PJSC and the financial statements of Promsvyazbank PJSC drawn up in compliance with the requirements of the Bank of Russia. The credit rating is solicited and Promsvyazbank PJSC participated in its assignment.

In assigning the credit rating, ACRA used only information, the quality and reliability of which were, in ACRA's opinion, appropriate and sufficient to apply the methodologies.

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

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Analytical Credit Rating Agency (Joint-Stock Company), ACRA (JSC)  
1 Bldg. 2 Bolshoi Gnezdnikovsky Lane, Moscow, Russia  
[www.acra-ratings.com](http://www.acra-ratings.com)

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