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Key rating assessment factors

ACRA affirms BB+(RU) to «AVANGARD» JSB, outlook Stable, and BB+(RU) to bond issue

The credit rating of [«AVANGARD» JSB](#) (hereinafter, the Bank) is based on the Bank's satisfactory business profile, adequate capital adequacy, critical risk profile, and adequate funding and liquidity. The Bank's creditworthiness is strong in the short time, with increased sensitivity to negative changes in Russia's business, financial, and economic environment.

The Bank is a private bank operating a wide branch network that spans across all federal districts of Russia. It is among the top 50 Russian credit institutions in terms of capital. The Bank focuses on SME lending (predominantly in agribusiness and manufacturing sectors), stock market and interbank market operations, and transactional business. Kirill Minovalov is the majority shareholder of the Bank with 99.99% shares. He also serves as the Bank's President and Chairman of the Board of Directors.

Satisfactory business profile. The Bank's strategy provides for an increase in risk-free transactional income and liquid assets a decrease in credit risk accepted, which the Bank attributes to high risks in the operating environment. In order to support clients during quarantine restrictions, the Bank provided them with preferential terms of service, which led to a decrease in the Bank's commission income in H1 2020. These measures are expected to be temporary and the Bank's commission income should resume growth next year. Operating income is highly diversified, with the Herfindahl–Hirschman Index at 0.17 for 2019. ACRA assesses the Bank's corporate governance quality as satisfactory, matching the scope of Bank's business. ACRA notes that the key shareholder of the Bank, Kirill Minovalov, actively participates in resolving strategic and most significant operating matters.

The Bank's adequate capital position is based on high regulatory capital adequacy (as of August 1, 2020, N1.2 was 17.5%, compared to minimum recommended 7.875% including conservation buffer). This enables the Bank to withstand a moderate increase in the cost of risk without breaching regulatory standards due to, among other things, the depreciation of problem and potentially problem loans. The Bank's ability to generate capital generation is assessed as very high, with the average capital generation ratio exceeding 300 bps over the last five years. Moreover, CTI and NIM were equal to 40% and 6.8%, respectively, as calculated by ACRA for the last three years.

The critical risk profile assessment is based on the low quality of the loan portfolio (28% of assets), which includes a high share (about 50%) of NPLs and potentially NPLs (including 21.2% of NPL90+). Coverage on NPLs and potentially NPLs stands at 52%. The portfolio concentration on the top ten groups of borrowers equals to 62% of total loans, which is assessed as substantial. In ACRA's opinion, the share of loans and liabilities due from the parties directly or indirectly related to the Bank may be as high as 50% of common capital (excluding the non-listed shares of JSC Avangard-Agro). At the same time, loan portfolio coverage is around 80%.

The Bank's exposure to market risk is assessed as relatively low, as the securities portfolio (29% of assets) includes about 42% US Treasury bonds, 9% Russian sovereign debt obligations, as well as Eurobonds and blue chips and shares in a related party, JSC Avangard-Agro ([BBB-\(RU\), outlook Stable](#)).

Receivables from financial institutions total 21% of the Bank's assets and mostly include funds held on accounts with the Bank of Russia and reverse repurchase transactions made through the central counterparty.

The Bank's risk management system is assessed as satisfactory.

Adequate liquidity and funding positions. The Bank is able to withstand an outflow of client funds in both the base case scenario (short-term liquidity surplus is RUB 35 bln) and stress scenario (12% of liabilities). In addition, the Bank may raise additional funds through repo transactions, if necessary, in view of the almost unencumbered securities portfolio. In the longer term, there are no liquidity imbalances (as of June 30, 2020, the long-term liquidity shortage indicator was 93%).

The Bank's resource base is stable and mostly includes corporate client funds (around 50% of liabilities) and retail client funds (around 40%). About 57% of client funds are demand deposits, which is positive for the funding costs of the Bank. The share of the largest groups of lenders in the resource base is low (largest at 1.0%, ten largest at 4.7%). No significant outflow of funds is expected over the next 12 months. As of June 30, 2020, the Bank had no borrowings from the Bank of Russia.

Key assumptions

- Maintaining the current business model within the 12 to 18-month horizon;
- Maintaining NIM at about 6%;
- Maintaining N1.2 above 10% within the 12 to 18-month horizon;
- Maintaining the current resource base profile.

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:

- Consistently high ability to generate capital;
- Substantially lower share of NPLs and lower concentration on the largest borrowers.

A negative rating action may be prompted by:

- Substantial financial support to Bank affiliates;
- Lower liquidity and higher concentration on the largest lenders.

Rating components

SCA: bb+.

Adjustments: none.

Support: none.

Issue ratings

Rationale. The issue represents senior unsecured debt of «AVANGARD» JSB. Due to the absence of either structural or contractual subordination of the issue, ACRA regards it as *pari passu* with other existing and future unsecured and unsubordinated debt obligations of the Bank. According to ACRA's methodology, the credit rating of the issue is equivalent to that of «AVANGARD» JSB, i.e., BB+(RU).

[Certified exchange-traded interest-bearing non-convertible unregistered bond issued by «AVANGARD» JSB, BO-001P-02 series \(RU000A1007Q1\)](#); maturity date: February 28, 2029, issue volume: RUB 3 bln — BB+(RU).

Regulatory disclosure

The credit ratings were assigned to «AVANGARD» JSB and bond issued by «AVANGARD» JSB (RU000A1007Q1) under the national scale for the Russian Federation based on the [Methodology for Credit Ratings Assignment 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 [Methodology for Assigning Credit Ratings to Individual Issues of Financial Instruments under the National Scale of the Russian Federation](#) was also applied to assign the credit rating to the above bond issue.

The credit rating assigned to «AVANGARD» JSB and the credit rating assigned to bond (RU000A1007Q1) issued by «AVANGARD» JSB were first published by ACRA on September 28, 2017, and March 23, 2019, respectively. The credit rating and credit rating outlook of «AVANGARD» JSB as well as the credit rating assigned to bond (RU000A1007Q1) issued by «AVANGARD» JSB are expected to be revised within one year following the publication date of this press release.

The credit ratings were assigned based on the data provided by «AVANGARD» JSB, information from publicly available sources, as well as ACRA's own databases. The rating analysis was performed using the IFRS statements of «AVANGARD» JSB and the financial statements of «AVANGARD» JSB drawn up in compliance with Bank of Russia Ordinance No. 4927-U of October 8, 2018. The credit ratings are solicited, and «AVANGARD» JSB participated in their assignment.

No material discrepancies between the provided information and the data officially disclosed by «AVANGARD» JSB in its financial statements have been discovered.

ACRA provided no additional services to «AVANGARD» JSB. No conflicts of interest were discovered in the course of credit rating assignment.

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