

Rating-Agentur Expert RA GmbH confirmed the credit rating of JSC CB Assotsiatsiya at 'BB-' according to the international scale. The rating outlook is stable.

Rating-Agentur Expert RA GmbH confirmed the credit rating of JSC CB Assotsiatsiya at 'BB-' (Sufficient level of creditworthiness) according to the international scale. The rating outlook is stable which means that in the mid-term perspective the likelihood of the credit rating stability is high.

BANKING SYSTEM RISK ASSESSMENT:

The bank's operations are concentrated as follows: 100% in Russia. The banking system risk (BSR) of Russia is Moderate. Therefore the overall risk exposure to the banking system of JSC CB Assotsiatsiya is Moderate.

MAJOR FACTORS THAT INFLUENCED THE RATING:

Positive factors:

- Maturities of assets and liabilities are well matched in the short and the long run, as evidenced by the liquidity ratios: N2=269,5%, N3=393,4% and N4=16,8% as of February 2017¹;
- Sufficient capital adequacy as shown by the capital adequacy ratios: N1.0=18,8%, N1.2=14,5%, N1.1=14,5%² as of February 2017. In addition, these ratios would still remain above the minimum statutory level if as much as 9,5% of the loan portfolio would be fully impaired;
- Reduced currency risk as the open currency position in all currencies was equal to 0,1% of the bank's capital as of February 2017;
- High level of collateral to loan portfolio ratio. The coverage of the loan portfolio (without taking into account interbank loans) by collateral, including securities, guarantees and sureties, was 574,6% and as high as 147,5% when excluding securities, guarantees and sureties as of February 2017;
- High level of reliability of funds placed on correspondent accounts and issued interbank loans.

Restricting factors:

- The provision policy still poses a risk for the bank as the difference between the calculated reserve ratio and minimum possible reserve ratio stood as low as 0,8 p.p. as of February 2017;
- The quality of the loan portfolio remains deteriorated despite having improved over the past 12 months: the overdue debt on loans was equal to 3,1% as of February 2017, as compared to 3,4% a year ago;
- Significant geographical concentration of transactions. The share of funds raised in the base region was equal to 95% while the share of loans issued in the base region was equal

¹ N2 – instant liquidity normative ratio; N3 – current liquidity normative ratio; N4 – long-term liquidity normative ratio.

² N1.0 – capital adequacy ratio; N1.2 – Tier 1 capital ratio; N1.1 – Common Equity Tier 1 (CET 1) ratio.

to 88% as of February 2017. Nonetheless, Nizhny Novgorod oblast is characterized by a minimal level of investment risks³;

- High level of restructured and rolled over loans in the total loan portfolio. As of February 2017, the share of loans reclassified as loans with better quality to total loans to legal entities, individual entrepreneurs and individuals, equaled 31%⁴. Additionally, the share of rolled over loans was equal to more than 10% of total loans;
- High concentration of the corporate loan portfolio among industries. Loans to the three largest industries equaled 54,4% of the total loan portfolio of legal entities and individual entrepreneurs as of February 2017;
- Concentration of credit risks on the largest customers remains high despite its positive dynamic: the largest credit risks to total assets net of reserves amounted to 24,6% as of February 2017, compared to 36,1% as of June 2016.

Negative factors:

- High concentration of funding from the largest creditors combined with a decline of the funding base. The amount of raised funds decreased by 7,4% over the past 12 months as of February 2017. Despite having declined by 6,6p.p. between February 2016 and February 2017, the share of the 10 largest creditors in the balance sheet remained high at 22,1%. Additionally, the share of the largest creditor in the balance sheet remained at 11,5% as of February 2017;
- Lack of specific risk-analysis instruments and certificates of management quality. The bank's strategic planning is short-term oriented (the bank's strategy is limited up to 2017). Additionally, the bank does not have a mandatory policy for collateral insurance;
- Decreasing profitability indicators as shown by negative dynamics of return on equity calculated without reversible components (net income from foreign exchange transactions and revaluation of it, etc.): from 7,0% in 1Q 2016 to 6,3% in 4Q 2016.

SENSITIVITY ASSESSMENT:

The following developments could lead to an upgrade:

- Reduction of the loan portfolio concentration on the largest borrowers, which would reduce the pressure on the bank's capital in case of credit risk materializations;
- Significant and sustainable improvements of the bank's profitability indicators combined with a sustainable increase of the bank's net interest income;
- Considerable and sustainable decrease of the share of overdue debt within the following quarters.

The following developments could lead to a downgrade:

- Significant decrease of the bank's ROE (calculated without reversible components), combined with instability of the bank's financial results;
- Tightening of the CBR policy regarding loans to related parties, given elevated share of related parties in the bank's assets;
- Deterioration of the bank's financial metrics as a result of an unexpected withdrawal of short-term customer's funds.

³ Nizhny Novgorod oblast was rated as the 2A "moderate potential - minimal risk" in the rating of investment attractiveness by RAEX-Moscow in 2016.

⁴ This figure refers to the indicator "the share of loans classified in accordance with paragraph 3.10 of regulation №254-P to total loans to individuals, legal entities, individual entrepreneurs and banks".

JUSTIFICATION OF THE RATING:

The Agency confirmed the credit rating of JSC CB Assotsiatsiya at 'BB-' with a stable outlook. The rating remains restrained by highly concentrated funding base, deteriorated quality of the loan portfolio and significant geographical concentration of transactions combined with decreasing profitability indicators. At the same time, the rating assessment was positively supported by solid liquidity ratios, sufficient capital adequacy as well as high levels of loan collateral and reliability of interbank assets.

As a medium-sized Russian bank, JSC CB Assotsiatsiya has historically specialized on the provision of financial services (current accounts and deposits) to the group of industrial enterprises from its core region (Nizhny Novgorod oblast). This exposes the bank to a high concentration of its funding base on a reduced number of clients and geographical locations. The share of 10 largest creditors constituted for 22,1% of the balance sheet as of February 2017. Such a concentration had a direct impact on the bank's funding base stability as the amount of raised funds decreased by 7,4% over the past 12 months as of February 2017. However, the Agency noticed a sustained downward trend for the bank's funding base concentration. In addition, most of the bank's creditors are related parties, which can reduce the risks of sudden funds withdrawal.

The asset transactions of JSC CB Assotsiatsiya are also exposed to the geographical and industry concentration risks, as the share of loans issued in Nizhny Novgorod oblast accounted for 88% of total loans and loans to the three largest industries equaled 54,4% of the total loan portfolio of legal entities as of February 2017. This, combined with the significant share of corporate borrowers in risky segments such as local SMEs and construction businesses, contributed to the deterioration of the loan portfolio quality. This was evidenced by a 10% of rolled-over loans as well as 3,1% of overdue debt (despite improving over the past 12M) respectively as of February 2017. Moreover, the Agency assessed the decreasing profitability indicators as a negative factor as return on equity calculated without reversible components decreased from 7,0% in 1Q 2016 to 6,3% in 4Q 2016.

The aforementioned risks are partly mitigated by very high level of liquidity ratios, as well as sufficient capital adequacy ratios. These metrics resulted from the bank's policy, which was based on placing part of its funds in the short-term interbank loans and correspondent accounts in banks with high credit ratings (including foreign banks and Central Bank of Russia). The share of this type of assets increased substantially over the past 12 months and reached more than 25% of total assets as of February 2017.

In addition, the deterioration of the loan portfolio is partially offset by a large coverage of loans by collateral which amounted to 574,6% as of February 2017 respectively. Moreover, the currency risk exposure of the bank is almost negligible, as the open currency position on all currencies was equal to 0,1% of the bank's capital as of February 2017.

The stable outlook reflects the Agency's opinion that the bank's financial stance is likely to remain unchanged within next 12 months with a high probability. We expect the bank to remain exposed to risks related to the funding base concentration, as well as geographical and industry concentration of assets. In addition, we do not expect significant changes in the levels of overdue debt and profitability indicators, taking into account the overall stance of the Russian banking system and entity's specific characteristics.

COMPANY PROFILE:

JSC CB Assotsiatsiya (number of license - 732) specialized on issuing loans to SMEs and big local enterprises, raising funds from individuals and local big enterprises (current accounts and deposits). The head office of the bank and 25 additional branches are located in Nizhny Novgorod oblast, where the bank conducts the largest part of its operations. The bank also has one additional office and filial in Kostroma oblast. Assets of the bank was equal to RUB 10 476 m as of 01.04.2017 (202nd place in the ranking of Russian banks by assets), the bank's equity was equal to RUB 1 243 m as of the same reporting date. The bank had profit after taxes equal to RUB 6,2 m for the 3m 2017.

Responsible expert: Vladimir Gorchakov, Rating Associate of Rating-Agentur Expert RA GmbH.

Reviewer: Gustavo Angel, Rating Associate of Rating-Agentur Expert RA GmbH.

Related research:

- ◆ Research Report on the Russian Banking Industry – 28.11.2016:
http://raexpert.eu/files/Industry_report_update_banks_28.11.2016.pdf

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RATING HISTORY:

Date	Review reason	Rating Score	Outlook
26.04.2016	Initial assignment	BB	Stable
02.09.2016	Unscheduled review	BB	Negative
28.11.2016	Unscheduled review	BB-	Stable

Minute's summary:

The rating committee for JSC CB Assotsiatsiya was held on the 25 April 2017. The quorum for the rating committee was present. After the responsible expert presented the factors which influenced the rating assessment, the members of the committee expressed their opinions and suggestions within the framework of the Banks methodology. The chairman of the rating committee ensured that every member of the committee expressed his/her opinion before proceeding to the rating class voting.

The rating was disclosed to the rated entity prior to the publication and was not changed during the process of coordination.

The following methodology was used for the rating assessment: methodology for assigning credit ratings to banks. Short Public Version (from December 2016) can be found under the following link: http://www.raexpert.eu/files/methodology/Methodology_Short_Credit_Ratings_BanksV3.pdf. Descriptions and definitions of all rating categories can be found under the following link: under the "Rating scale" section. The user of the rating shall read the methodology in order to have a full understanding of the rating procedure.

This rating is solicited. The rated entity participated in the rating assignment process.

No other third party participated in the preparation of the rating.

Main sources of information:

- Questionnaire from JSC CB Assotsiatsiya based on the form provided by the Agency;
- Financial statements from JSC CB Assotsiatsiya, following RAS form for the past 24 months: 101, (102, 806, 807, 808, 345)*, 110, 115, 116, 117, 118, 123, 125, 128, 129, 135, 155, 157, 202, 302, 303, 501, 603, 634, 711;
- Audited annual reports of JSC CB Assotsiatsiya according to IFRS (including the auditor's report and notes to the accounts) for 2012-2015;
- Statute of JSC CB Assotsiatsiya;
- Documents regulating risk management of JSC CB Assotsiatsiya;
- Documents defining development plans of JSC CB Assotsiatsiya for 2016-2017;
- Documents regulating corporate governance of JSC CB Assotsiatsiya;
- Answer for additional request based on the form provided by the Agency;
- Information received during the interview with the management of the bank;
- Information from media and other public sources.

*On a quarterly basis.

Limits of the Credit Rating

During the rating assignment process, Rating-Agentur Expert RA GmbH (the Agency) used publicly available information as well as non-public information (obtained from the rated entity and/or other third parties) which was considered to be reliable, complete and non-biased. The responsible expert performed rating assessment of the bank with information considered as the most reliable and up to date in accordance to the overall position of the bank and the Agency's internal criteria for selecting data providers. The information and data used for this specific assessment can be considered as of sufficient quality.

Conflict of interest

The responsible expert was neither influenced nor biased by third parties during the rating assessment. The experts involved in the rating assessment and revision of the rated entity showed no conflict of interests before initiation of the rating review.

Rating-Agentur Expert RA GmbH is completely independent from the activities of other agencies from RAEX group.

Risk warning

The Agency disclaims all liability in connection with any consequences, interpretations, conclusions, recommendations and other actions directly or indirectly related to the conclusions and opinions contained in the Agency's press-release.

This press-release represents the opinion of Rating-Agentur Expert RA GmbH and is not a recommendation to buy, hold or sell any securities or assets, or to make investment decisions.

Office responsible for preparing the rating

The office responsible for the preparation and issuance of this credit rating is the office of Rating-Agentur Expert RA GmbH in Frankfurt am Main, Germany.

Rating-Agentur Expert RA GmbH is a credit rating agency established in Germany and therefore shall comply with all applicable regulations currently in force in the European Union.

The European Securities and Markets Authority (ESMA), the EU's direct supervisor of credit rating agencies (CRAs), has registered Rating-Agentur Expert RA GmbH as a CRA under Regulation (EC) No 1060/2009 of the European Parliament and of the Council of 16 September 2009 on credit rating agencies, with effect from 1 December 2015.

Rating-Agentur Expert RA GmbH applies the Code of Conduct Fundamentals for credit rating agencies issued by the International Organization of Securities Commissions (IOSCO Code) and includes the basic principles of IOSCO Code in its Code of Conduct.