

Rating-Agentur Expert RA confirmed the credit rating of Bank Saderat Tashkent at 'B' according to the international scale. The rating outlook is stable. The rating was withdrawn.

Rating-Agentur Expert RA confirmed the credit rating of Bank Saderat Tashkent at 'B' (Moderately low level of creditworthiness) according to the international scale. The rating outlook is stable which means that in the mid-term perspective there is a high probability of maintaining the rating score.

BANKING SYSTEM RISK ASSESSMENT:

The bank's operations are concentrated 100% in Uzbekistan, and the bank's funding base is concentrated 100% in Iran. The banking system risk (BSR) of Uzbekistan and Iran is high. Therefore, the overall systemic risk of Bank Saderat Tashkent was assessed as high.

MAJOR FACTORS THAT INFLUENCED THE RATING:

Positive factors:

- As expected, the capitalization metrics of the bank remain stable and solid as the Tier 1 capital adequacy ratio stood at 84,2% and the capital adequacy ratio at 84,4% as of June 2019, well above the 13% minimum requirement for capital adequacy of the Central Bank of Uzbekistan (CBU). We continue to expect the level for both capitalization indicators to remain at similar levels in the mid-term perspective;
- Due to the small loan portfolio (less than 2% of total assets), Bank Saderat Tashkent has no overdue loans of more than 30 days, making credit risk negligible. Bank Saderat Iran (BSI) also covers all the guarantees issued by the bank;
- Despite liquidity indicators having slightly decreased within the year, metrics remained very strong as the instant liquidity ratio stood at 306% and the current liquidity ratio (current assets divided by liabilities of up to 30 days) at 768%;
- The bank has limited exposure to interest rate risk as most of the funding is equity-based and interest income is mostly from deposits at fixed rates with BSI. However, these deposits have a remaining maturity of less than one year and represent around 90% of the interest income, i.e. there is a risk of a reduction in earnings in case there is an adverse effect in the interest rates due to the short-term nature of the deposits;
- High level of transparency of the ownership structure. There are no intermediate companies between Bank Saderat Tashkent and BSI and information about the largest beneficial owners has been disclosed.

Restricting factors:

- More than 90% of the total interbank term deposits lay on BSI accounts, which does not have an internationally recognized credit rating, restricting a positive assessment of the asset quality. However, BSI is systematically important for Iran and has the possibility to receive government support if such need arises;
- Profitability indicators deteriorated within the year, as ROA and ROE decreased by 2p.p. y-o-y down to 1,14% and 1,28% as of 2Q 2019. Both indicators are very much alike, indicating limited alternative funding sources (total liabilities do not exceed 12% of total banks' assets). Moreover, such level of ROE continues to be moderately low as compared to the Uzbek banking sector (ROE 17 % as of July 2019);

- Bank Saderat Tashkent continues to self-fund its activity as the equity source accounts for 89% of total funds (1,5p.p. less than a year before). The bank's liabilities are highly concentrated as around 64% of all external sources are in form of deposits and 86% of which belong to the Embassy of the Republic of Iran. However, a long-lasting relationship between the Embassy of the Republic of Iran and Bank Saderat Tashkent together with residual maturity of the deposits of more than two years, offset the risk of a sudden withdrawal to some extent. Nevertheless, all other liabilities of the bank in form of the funds due to other banks are from BSI;
- National currency fluctuations could affect the competitive position of the bank and increase financial results volatility. Total loss from currency operations in 2018 was UZS 78 m, as compared to a UZS 7812 m gain in 2017 (60% of overall income);
- Bank Saderat Tashkent has developed in line with the approved strategy of 2018-2019. The planned profit for 2018 was almost fulfilled (by 99%) thanks to the higher return from interbank deposit accounts and increasing of interest-free income from commissions. Moreover, we consider the figure of the approved profit growth of 40% by the end of 2019 to be reasonable. However, the objective of attracting resources from the local market still has not been met. Geopolitical tensions between the U.S. and Iran could be another obstacle for international activity and trade financing growth.

Negative factors:

- The systemic risk for Saderat Tashkent remains high according to our assessment of the Banking Sector Risk (BSR). The bank operates in Uzbekistan, while the source of funding and most of the interest income comes from Iran. Both countries are characterized by reduced transparency, highly underdeveloped financial markets and continue to be exposed to political and legislative risks;
- The captivity of the bank remains quite high as the bank's operations remain heavily dependent on BSI. More than 95% of total bank's assets were placed with related parties by the end of 2Q 2019. The figure has remained at the same level for the last two years. Moreover, more than 84% of total operational revenue was attributed to related parties (interest income from deposits in BSI);
- The bank continues to have an unfavorable competitive position and limited geographic reach. The bank operates in Uzbekistan with a single office in Tashkent. Moreover, as of June 2019, Saderat Tashkent's assets accounted for less than 0,2% of the Uzbek banking system and its loans to a merely 0,004% of the sector. As mentioned, the main source of income for the bank consists of having deposits in BSI, which continues to limit the potential of the bank to penetrate the Uzbek market.

External support factors:

- Support from the owners. The bank has received financial support from BSI in the form of additional capital during periods of non-financial distress and based on recommendation of the CBU. This demonstrates the shareholder's ability and willingness to support the bank if required (weak support factor).

SENSITIVITY ASSESSMENT:

The following developments could lead to an upgrade:

- Significant improvement in the economic and financial conditions of Uzbekistan and Iran according to our internal BSR assessment;
- Diversification of the funding base, loan portfolio and banking activities;
- Increase in the bank's competitive position as a result of a stronger penetration in the Uzbek market and higher non-deposit income.

The following developments could lead to a downgrade:

- Steep decline of the bank's profitability and liquidity indicators;
- Deterioration of the financial conditions of Bank Saderat Iran, the bank's main source of funding.

JUSTIFICATION OF THE RATING:

The Agency confirmed the rating of Bank Saderat Tashkent at 'B' based on stable capitalization, limited exposure to credit and interest rate risks and outstanding liquidity metrics. On the other hand, negative macro profile, low operational income and insignificant competitive position in the local market continue to be the main factors constraining the bank's creditworthiness.

Capital adequacy and liquidity indicators are well above the requirements of the Central Bank of Uzbekistan (CBU) and we expect the trend to be the same going forward. Moreover, the low amount of loans to customers reduces the potential impact of a counterparty default in the capital metrics of the bank. Moreover, despite the low interest rate risk, the fact that most of the income generating assets are short-term (mostly three months) could potentially hurt profitability in case there is a significant movement in the yield curve.

According to our calculations, the Banking Systemic Risk (BSR) score shows high level of systemic risk in Uzbekistan and Iran, as both countries have limited access to alternative funding, low transparency and, especially Iran, are exposed to geopolitical tensions. In addition, the competitive position of Saderat Tashkent remains negative and its geographical diversification minimal. The Uzbek market remains dominated by state-owned-banks, making it more difficult for the new commercial banks to penetrate the sector.

Additionally, the bank showed significant signs of captivity since 95% of the bank's assets and 84% of the income as of June 2019 were assigned to Bank Saderat Iran (BSI). Moreover, the funding base remains very concentrated as 86% of banks deposits are coming from the Embassy of the Republic of Iran, 100% of the funds due to other banks are from BSI and all the bank's equity is financed by the owner BSI. The combination of the concentration of assets and equity on BSI augments the risk of the sustainability of the bank's capitalization and profitability in case a distress situation were to occur in BSI.

Nevertheless, we consider BSI to be reliable as we assess it as a systematically important bank for Iran as it is one of the largest banks in the country, has a track record of adequate performance, maintains support from the Iranian government and has a global branch network. However, the lack of an internationally recognized credit rating restricts a fully positive counterparty risk assessment.

Profitability remains subdued as ROE declined down to 1,2%, that is significantly lower than the average market value in Uzbekistan of 17% as of June 2019. Previously higher financial results were driven by the FX revaluation effect and not from the core operating activity, making overall profit volatile from one year to another and dependent from further UZS depreciation against the USD.

The stable outlook still reflects our view of the bank's stable structure and operations. We believe the link of the bank to BSI serves as a regular and certain source of income and funding which contributes to the stability of the bank.

COMPANY PROFILE:

Bank Saderat Tashkent was established in 1999 and is a subdivision and a fully-owned subsidiary of the Bank Saderat Iran which is located in Tehran (Iran). The bank carries out its main activities on the basis of the banking license for banking operations issued by the Central Bank of the Republic of Uzbekistan No. 2 – D dated from 25 September 2004. The principal activity of the Bank is commercial and retail bank operations on the territory of the Republic of Uzbekistan and

beyond. These operations include operations with securities, foreign currency, attracting deposits and issuance of commercial loans in UZS, and in freely convertible currencies, rendering services to customers in realization of export and import operations. The Bank operates its principal activities in Tashkent city and does not have any branches in the Republic of Uzbekistan.

Related research:

- ◆ Research report on Uzbekistan – 08.03.2019

https://raexpert.eu/reports/Research_report_Uzbekistan_08.03.2019.pdf

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RATING HISTORY:

Date	Review reason	Rating Score	Outlook
01.08.2018	Scheduled review	B	stable
01.08.2017	Initial assignment	B	stable

Minute's summary:

The rating committee for Bank Saderat Tashkent was held on 31 July 2019. 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 – Full Version \(from September 2018\)](#)
- [Methodology for Assigning Banking Sector Risk Score – Full Version \(from September 2018\)](#)

Descriptions and definitions of all rating categories can be found 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.

The definition of default can be found on the Agency's website in the section for [Internal policies](#).

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:

- Annual IFRS report from the bank
- Monthly reports of the bank to the CBU
- Questionnaire from the bank
- Saderat Bank Iran website

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 process.

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

Risk warning

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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.

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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.