

April 5, 2019

PJSC Sovcombank

Lead analysts:

Irina Nosova, Associate Director
+7 (495) 139-0481
irina.nosova@acra-ratings.ru

Valeriy Piven, Associate Director
+7 (495) 139-0493
valeriy.piven@acra-ratings.ru

Credit rating components	
Business profile	
First stage	bbb
Second stage	bbb
Key risk factors	
Capital adequacy	Strong (+2)
Risk profile	Satisfactory (0)
Funding and liquidity	Adequate (0)
SCA	a-
Adjustments	
Systemic	0
Individual	0
Support	
Systemic importance	+1
Group	0
State	0
Credit Rating	A(RU)
Outlook	Stable

Brief information about the Bank

[PJSC Sovcombank](#) (the Bank) is a universal bank that holds sustainable positions in both household lending and corporate lending segments. The Bank is among top 20 Russian credit institutions in terms of equity and assets and ranks 8th by the volume of private deposits.

Over the last years, the Bank's business has been growing both organically and by entering new market niches and purchasing loan portfolios of other banks, as well as through mergers and acquisitions.

At the end of 2018, Sovco Capital Partners N.V. accounted for 91.7% of the Bank's shares, of which 37.3% belong to Dmitry and Sergey Khotimsky, while the remaining 8.3% are held by minor shareholders, including foreign sovereign and investment funds and the Bank's managers.

Rating assessment factors

Business profile: adequate (bbb)

The Bank's adequate business profile is backed by its sustainable franchise in consumer lending, higher competitiveness in lending for large businesses and SMEs, and pronounced operating income diversification. The Bank's ownership structure is transparent, corporate governance system matches the scope of its business, and the strategy's assessment reflects the Bank's approaches to business development.

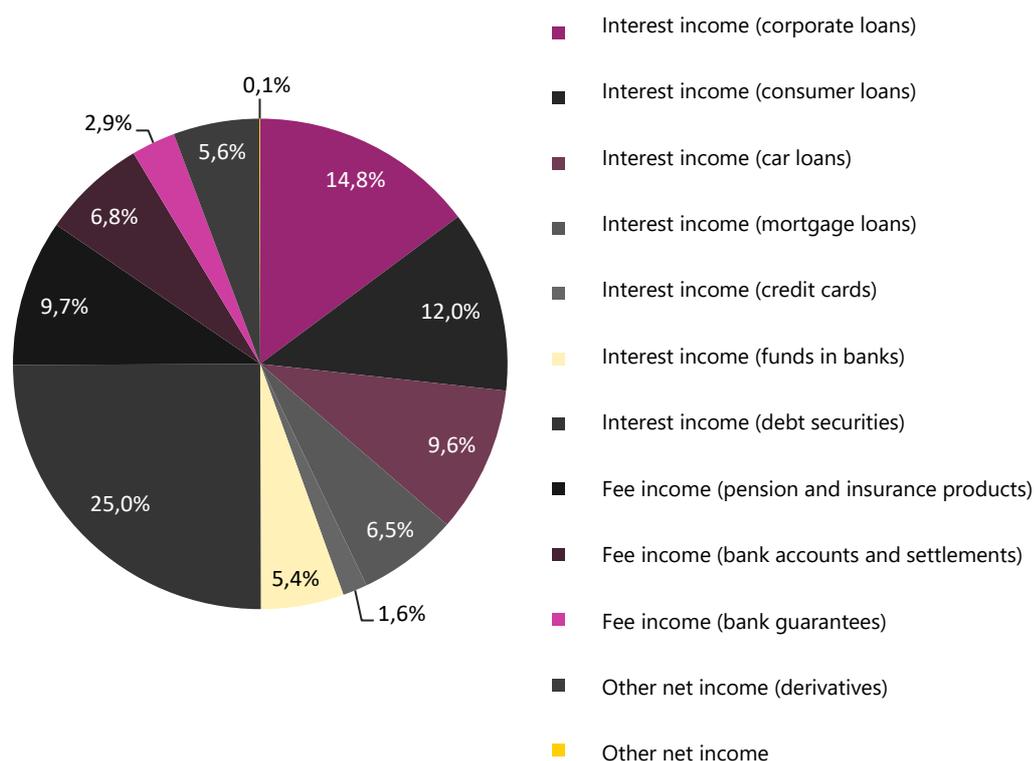
The 'high' assessment of the franchise factor takes into account brand awareness and competitive edge shown by the Bank in the key business lines over the last years. As of February 01, 2019, the Bank ranked 13th in terms of equity and 14th in terms of assets among Russian banks. The Bank occupies a sizable market share in the retail lending segment (including car loans, mortgage loans, and consumer loans) and the financing of regions and municipalities (mostly, by purchasing their bonds). In the corporate lending segment (including both large businesses and SMEs) and the bank guarantees market, the Bank's positions have become stronger, including through the acquisition of [Joint-stock Bank «ROSEVROBANK» \(ACRA's rating A\(RU\), outlook Stable, withdrawn on November 01, 2018\)](#) completed in 2018.

The strategy of the Bank includes the following:

- Intensive M&A transactions (the Bank acquired GE Money Bank in 2013, ICICI Bank Eurasia LLC (now, MCIB Bank LLC), Metcombank and Guarantee Bank–Moscow in 2016; in the same year, the Bank was appointed to rehabilitate Express–Volga Bank that is expected to be acquired by the Bank; in 2015–2018, the Bank increased its equity share in ROSEVROBANK from 9.5% to 100%) and purchases of good-quality loan portfolios (including the mortgage portfolio of Nordea Bank in 2017), which is positive for the Bank's share in the banking sector;
- Fast response to economic changes, based on the economic feasibility of each transaction, which allows the Bank to maintain its profitability and to increase operating income.

The Bank's operating income is well-diversified by income source, which is positive for the business profile assessment. The Sovcombank's business growth over the last few years has also been focused on asset universalization, thanks to which the Bank's management achieved significant operating income diversification (the Herfindahl–Hirschman Index amounted to 0.15 for 9M2018). ACRA also notes the adequate geographical diversification of the operating income generated by the Bank's branches present in all federal districts of Russia (about 2.7 thousand offices across 74 regions of Russia).

Figure 1. Operating income profile, 9M2018



Source: PJSC Sovcombank

ACRA assesses the quality of the Bank's corporate governance as adequate in the context of the Russian banking market, which hinges on the stable team of top managers and the effective corporate governance system.

The Bank's ownership profile is assessed as transparent.

Key risk factors

Capital adequacy: strong (+2)

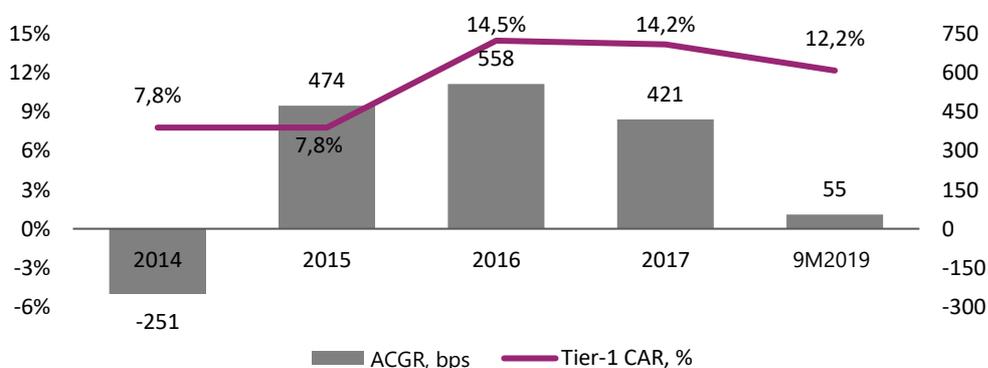
ACRA assesses the Bank's capital adequacy as strong because its substantial common capital cushion is combined with the strong ability to generate capital, which enables the Bank to comply with regulatory capital adequacy ratios in case of a sizable increase in the cost of risk.

The Bank has maintained a sizeable capital cushion under both international (as of September 30, 2018, Tier-1 ratio was 12.2% against minimum 6% under Basel I) and Russian standards (as of February 1, 2019, N1.2 ratio was 10.2% against minimum 6%, or 7.875% markup included). Therefore, the Bank is able to withstand a growth in the cost of risk by about 500 bps without its N1.2 ratio dropping below 6%.

At the same time, ACRA notes that over the first 9 months of 2018, the Tier-1 ratio decreased from 14.2% to 12.2%, because risk-weighted assets (RWA) grew by 1.6 times to RUB 906 bln (according to the Bank's consolidated financial statements as of September 30, 2018). The main reasons for the growth in the RWA are the acquisition of ROSEVROBANK by Sovcombank Group and the inclusion of market risk into RWA calculations in accordance with the requirements of Basel I (dated 1996) implemented in terms of market risk. Before September 30, 2019, the Bank excluded market risk from its capital adequacy calculations (as no such requirement was included in the 1988 version of Basel I that had been used by the Bank).

In 2018, the Bank started to apply IFRS 9 and reclassified about 40% of its securities portfolio as assets at amortized cost. In ACRA's view, this has significantly reduced the impact of market risk on the Bank's capital adequacy.

Figure 2. Capital adequacy and generation



Source: PJSC Sovcombank, ACRA

The Agency notes the Bank's sustainable ability to generate capital from retained earnings: the averaged capital generation ratio (ACGR) exceeded 300 bps over the last five years. The Bank's dividend policy is reasonable, as the priorities include investing in business and maintaining capital adequacy ratios.

As calculated by ACRA over the last three years, the operating efficiency indicators are rather high (including the net interest margin of 5–7% and the cost-to-income of 45.5%, which are typical for peer banks).

Risk profile: satisfactory (0)

The 'satisfactory' assessment of the Bank's risk profile is underpinned by the adequate quality of the loan portfolio on the backdrop of relatively high market risks. The quality of the Bank's risk management system is assessed as adequate.

The Bank's loan portfolio amounts to RUB 353 bln (or 41% of assets excluding bonds reflected in the financial statements at amortized cost) and consists of 50% of loans to households and 49% of loans to corporates. The share of problem and potentially problem, in ACRA's opinion, loans is relatively low and accounts for about 6% of the portfolio (including 2.7% of NPL90+), with an acceptable concentration on the top 10 groups of borrowers (18% of loans). At the same time, the concentration of loans on related parties and high-risk industries is insignificant. The Bank continues to pursue a policy aimed at diversifying its loan portfolio through the corporate sector and collateralized retail lending, which increases the Bank's business model's resistance to negative changes in the operating environment in terms of the implementation of credit risks.

As of 30 September 2018, the portfolio of securities held by the Bank amounted to RUB 392 bln (45% of assets), including 87.5% of Eurobonds and ruble bonds issued by companies and banks and 12% of regional and municipal bonds and federal loan bonds.

In Q3 2018, a significant portion of securities at fair value through profit or loss was reclassified to securities at amortized cost, which, in ACRA's opinion, allowed the Bank to reduce its estimated market risk from 3.9x (under the 1996 version of Basel I) to 1.8x of the Tier 1 capital (as calculated in accordance with the 1996 version of Basel I implemented in terms of market risk) and to keep the Tier 1 capital adequacy above 12%.

Securities categorized as "Financial instruments at fair value through profit or loss" (20% of assets) served a basis to calculate the market risk as of September 30, 2018. The actual general market risk is lower because the Bank is active in derivative transactions (interest rate swaps).

According to the Bank, bonds reflected in "Loans to customers and customers' securities at amortized cost" and "Cash held at banks and securities held by banks at amortized cost" (21% of assets) are expected to be held to maturity. Therefore, the Bank does not calculate the market risk for such securities. At the same time, ACRA notes that in case of need, such bonds may be sold before maturity, which potentially may be the source of additional market risk.

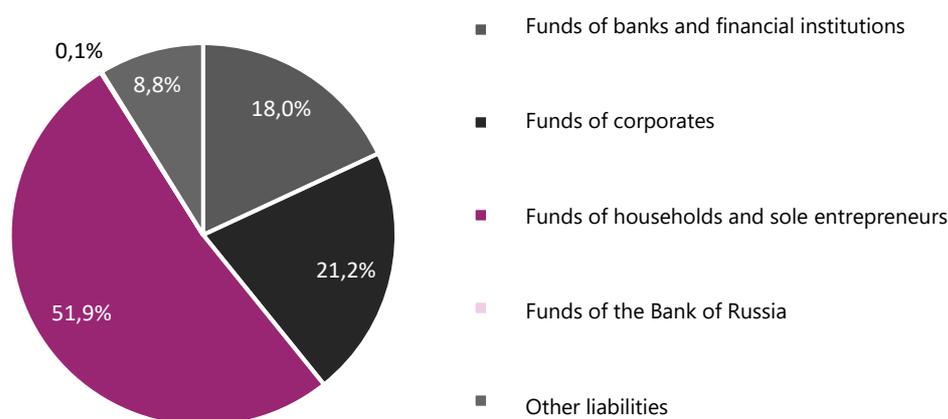
In ACRA's opinion, an additional source of market risk may be those securities that are categorized as "Investment securities at fair value through other comprehensive income" (about 4% of assets). However, the Bank excludes such bonds from its market risk calculations.

Funding and liquidity: adequate (0)

ACRA assesses the Bank's liquidity management policy as adequate, taking into account the Bank's ability to withstand the outflow of customer funds in the base case scenario (STLSI is positive, about RUB 60 bln). Under the stress scenario, the Bank demonstrates a short-term liquidity shortage of about 7.5% of liabilities. An additional source of liquidity may be securities that, as of September 30, 2018, were not encumbered under repurchase agreements (about a half of the debt securities on the balance sheet). For longer terms, the Agency also notes no significant imbalances (LTLSI exceeds 85%).

The funding profile is assessed as satisfactory and includes retail deposits (52% of the Bank's liabilities), funds held by corporates (21%, a significant increase after the Bank had purchased ROSEVROBANK), and short-term (up to 7 days) repos with banks (18%). The concentration of liabilities on the largest lenders is moderate (the share of the largest lender is 9% and the share of top 10 lenders is 24%).

Figure 3. Funding profile, 9M2019



Source: PJSC Sovcombank

In ACRA's opinion, the Bank's funding profile will not change significantly in the next 12–18 months, and no large loan repayments are expected in that period. The share of regulatory funds is insignificant (as of September 30, 2019, it was 0.1% of the Bank's resource base).

Adjustments

Systemic

There are no grounds for systemic adjustments.

Individual

There are no grounds for individual adjustments.

Support

Systemic importance

Local systemic importance. In ACRA's opinion, the Bank's bankruptcy may affect the financial sector and the socio-economic situation in certain Russian regions (including the Volga region and some regions of Siberia). As of February 01, 2019, the share of household deposits held with the Bank amounted to 1.4% of the total volume held in the entire banking system. Therefore, the Bank receives one support notch up to its SCA.

Group

The Bank is not a part of any identifiable group as defined in the [Methodology for Analyzing Member Company Relationships within Corporate Groups](#), which is expressed in no adjustments to the Bank's SCA.

State

The Bank is not a government-related entity, which is expressed in no adjustments to the Bank's SCA.

Issue ratings

[Certified exchange-traded interest-bearing non-convertible unregistered bond issued by PJSC Sovcombank, BO-05 series \(RU000A0ZYJR6\)](#); maturity date: November 25, 2027, issue volume: RUB 10 bln — **A(RU)**.

[Certified interest-bearing non-convertible unregistered bond issued by PJSC Sovcombank, 2B03 series \(RU000A0ZYWZ2\)](#), maturity date: February 21, 2029, issue volume: USD 150 mln — **BBB(RU)**.

[Certified interest-bearing non-convertible unregistered bond issued by PJSC Sovcombank, 1B02 series \(RU000A0ZYX28\)](#), maturity date: n/a, issue volume: USD 100 mln — **BB(RU)**.

Rating history

March 21, 2019 — A(RU), outlook Stable.

March 28, 2018 — A(RU), outlook Stable.

October 03, 2017 — A(RU), outlook Stable.

November 25, 2016 — A-(RU), outlook Stable.

Regulatory disclosure

The credit ratings were assigned to PJSC Sovcombank and the bonds (ISIN RU000A0ZYJR6, RU000A0ZYX28, RU000A0ZYWZ2) issued by PJSC Sovcombank 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 Analytical Credit Rating Agency within the Scope of Its Rating Activities](#). In order to assign credit ratings to the above bond issues, the Methodology for Assigning Credit Ratings to Individual Issues of Financial Instruments under the National Scale of the Russian Federation was also applied.

The credit ratings of PJSC Sovcombank and the bonds (ISIN RU000A0ZYJR6, RU000A0ZYX28, RU000A0ZYWZ2) issued by PJSC Sovcombank were first published by ACRA on November 25, 2016, December 07, 2017, March 28, 2018, and March 28, 2018, respectively. The issuer credit rating and its outlook and the issue credit ratings of the above bonds are expected to be revised within one year following the publication date of the relevant press release (March 21, 2019).

The credit ratings were assigned based on the data provided by PJSC Sovcombank, information from publicly available sources, as well as ACRA's own databases. The rating analysis was performed using the audited consolidated IFRS financial statements of PJSC Sovcombank and the financial statements of PJSC Sovcombank drawn up in compliance with the Bank of Russia Ordinance No. 4927-U dated October 08, 2018. The credit ratings are solicited, and PJSC Sovcombank participated in the rating process.

No material discrepancies between the provided information and the data officially disclosed by PJSC Sovcombank in its financial statements were discovered.

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

Appendix

Table 1. Consolidated IFRS balance sheet items, RUB mln

	2017	September 30, 2018
Assets	689,499	863,021
Cash and equivalents	5,988	7,922
Receivables from the Bank of Russia and RF Ministry of Finance	24,695	45,929
Mandatory reserves with the Bank of Russia	2,975	5,220
Receivables from banks and financial institutions	18,586	55,134
Debt securities	360,479	362,331
Other financial assets at fair value through income or loss or available for sale	13,379	10,186
Loans to and receivables from RF subjects and municipal authorities	24,762	3,960
Loans to and receivables from corporates, private entrepreneurs, and government agencies	84,049	174,670
Loans to and receivables from individuals	136,652	174,511
Intangible assets and goodwill	4,003	7,411
Investment real estate	58	58
Investments in subsidiaries and associates	8,730	1,141
Fixed assets	1,667	4,845
Deferred tax assets	459	512
Other financial assets	2,353	9,168
Other non-financial assets	664	23
Liabilities	604,081	749,882
Deposits from banks and financial institutions	194,135	135,177
Deposits from the Bank of Russia	-	610
Deposits from individuals and private entrepreneurs	302,641	388,875
Deposits from corporates	56,273	159,164
Debt securities issued	15,744	12,906
Subordinated debt	6,799	17,042
Funds of Deposit Insurance Agency	15,381	16,392
Deferred tax liabilities	5,244	4,941
Other liabilities	7,864	14,775
Capital	85,418	113,139
Charter capital	1,716	1,871
Other sources of capital	122	115
Retained earnings	806	(385)
Real estate revaluation reserve	2,852	25,680
Exchange premiums	78,302	83,912
Minority shares	1,620	1,946

Source: consolidated IFRS statements PJSC Sovcombank

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

	2017	9M2018
Interest income	68,723	63,880
Interest expenses	(35,745)	(29,902)
Net interest income	32,977	33,978
Impairment provision change	(4,438)	(6,592)
Net interest income after impairment provision	28,539	27,386
Fee income	20,282	17,784
Fee expenses	(2,232)	(3,196)
Net fee income	18,049	14,588
Other income net of expenses	14,437	1,358
Administrative and other operating expenses	(24,368)	(24,990)
Profit (loss) before taxes	36,658	18,342
Profit tax expenses	(7,088)	(2,775)
Profit (loss) after taxes	29,570	15,567

Source: consolidated IFRS statements of PJSC Sovcombank

Table 3. Consolidated key ratios

	2017	September 30, 2018
Capital adequacy		
Tier-1 CAR	14.2%*	12.2%**
N1.2	11.0%	9.9%
Capital generation, bps	421	55***
ACGR, bps*	322	n/a
Leverage	8.6%	9.1%
NIM	5.7%	6.2%
CTI	35.7%	49%
Risk profile		
NPL90+ (in loan portfolio before provisions)	2.6%	2.7%
Share of problem loans (in loan portfolio before provisions)	n/a	5.9%
Share of top 10 borrowers (borrower groups) (in loan portfolio before provisions)	n/a	17.9%
Loan portfolio concentration on high risk industries (% of Tier 1 capital)	n/a	21.6%
Loan portfolio concentration on related parties (% of Tier 1 capital)	n/a	0.8%
Market risk (% of Tier 1 capital)	n/a	176%**
Funding and liquidity		
Share of largest funding source in total liabilities	50.1%	51.9%
Share of regulatory funding in total liabilities	0.0%	0.1%
Share of the largest lender (lender group) in total liabilities, net of the Bank of Russia's funds	n/a	9.4%
Share of top 10 lenders (lender groups) in total liabilities, net of the Bank of Russia's funds	n/a	23.9%

* In accordance with Basel I.

** In accordance with Basel I (version of 1996).

*** y-o-y

Source: the Bank of Russia, ACRA's estimates

(C) 2019

Analytical Credit Rating Agency (Joint-Stock Company), ACRA (JSC)
75, Sadovnicheskaya embankment, Moscow, Russia
www.acra-ratings.com

Analytical Credit Rating Agency (ACRA) was founded in 2015, with its 27 shareholders representing major Russian corporate and financial institutions and its authorized capital exceeding RUB 3 bn. ACRA's main objective is to provide the Russian financial market with high-quality rating products. Methodologies and internal documents of ACRA are developed in compliance with the Russian legislation and with regard to global rating industry best practices.

The provided information, including, without limitation, credit and non-credit ratings, rating assessment factors, detailed credit analysis results, methodologies, models, forecasts, analytical reviews and materials, as well as other information placed on the ACRA website (further referred to as Information), coupled with the ACRA website software and other applications, are intended for information purposes only. Information must not be modified, reproduced or distributed by any means, in any way or form, either in whole, or in part, in marketing materials, as part of public relations events, in news bulletins, in commercial materials or reports without a prior written consent from, and reference to, ACRA. Any use of Information in violation of these requirements or the law is prohibited.

ACRA credit ratings reflect ACRA's opinion about the ability of a rated entity to meet its financial obligations or about the credit risk of individual financial obligations and instruments of a rated entity at the time of publication of the relevant Information.

Non-credit ratings reflect ACRA's opinion about certain non-credit risks assumed by interested parties interacting with a rated entity.

The assigned credit and non-credit ratings reflect all material information pertaining to a rated entity and known by ACRA (including the information received from third parties), the quality and reliability of which ACRA considers appropriate. ACRA shall not be responsible for the accuracy of information provided by clients or relevant third parties. ACRA does not audit or otherwise verify the provided data and shall not be held responsible for their accuracy and completeness. ACRA conducts rating analysis of information provided by customers using its own methodologies, with the texts thereof available on ACRA's website – www.acra-ratings.com/criteria.

No credit rating and/or credit rating outlook is regulated by the Central Bank of the Russian Federation, unless distributed so that such credit rating and/or credit rating outlook is in the public domain.

The only source that reflects the latest Information, including the one about credit and non-credit ratings assigned by ACRA, is ACRA's official website – www.acra-ratings.com. Information is provided on an "as is" basis.

Information shall be considered by users exclusively as ACRA's statement of opinion and must not be regarded as advice, recommendation or suggestion to buy, hold or sell securities or other financial instruments of any kind, nor shall it be viewed as an offer or advertisement.

Neither ACRA, nor its employees and persons affiliated with ACRA (further referred to as the ACRA Parties) provide any direct or implied guarantee expressed in any form or by any means regarding the accuracy, timeliness, completeness or applicability of Information for making investment and other decisions. ACRA does not act as a fiduciary, auditor, investment or financial advisor. Information must be regarded solely as one of the factors affecting an investment decision or any other business decision made by any person who uses ACRA's information. It is essential that each of such persons conduct their own research and evaluation of a financial market participant, as well as an issuer and its debt obligations that may be regarded as an object of purchase, sale or possession. Users of Information shall make decisions on their own, involving their own independent advisors, if they deem it necessary.

ACRA Parties shall not be responsible for any action taken by users based on Information provided by ACRA. ACRA Parties shall under no circumstances be responsible for any direct, indirect or consequential damages or losses resulting from interpretations, conclusions, recommendations and other actions taken by third parties and directly or indirectly connected with such information.

Information provided by ACRA is valid only as of the date of preparation and publication of materials and may be amended by ACRA in the future. ACRA shall not be obliged to update, modify or supplement Information or inform anyone about such actions, unless the latter was recorded separately in a written agreement or is required by the legislation of the Russian Federation.

ACRA does not provide advisory services. ACRA may provide additional services, if this does not create a conflict of interest with rating activities.

ACRA and its employees take all reasonable measures to protect all confidential and/or material non-public information in their possession from fraud, theft, unlawful use or inadvertent disclosure. ACRA provides protection of confidential information obtained in the course of its business activities as required by the legislation of the Russian Federation.