MOODY'S
INVESTORS SERVICE

Credit Opinion: Vozrozhdenie Bank

Global Credit Research - 29 Jun 2011

Moscow, Russia

Ratings

Category	Moody's Rating
Outlook	Stable
Bank Deposits	Ba3/NP
NSR Bank Deposits -Dom Curr	Aa3.ru/--
Bank Financial Strength	D-
Baseline Credit Assessment	Ba3
Adjusted Baseline Credit Assessment	Ba3

Contacts

Analyst	Phone
Eugene Tarzimanov/Moscow	7.495.228.6060
Semyon Isakov/Moscow	
Yves Lemay/London	44.20.7772.5454
Victoria Voronina/Moscow	

Key Indicators

Vozrozhdenie Bank (Consolidated Financials)[1]

	[2]**3-11**	[2]**12-10**	[2]**12-09**	[2]**12-08**	[2]**12-07**	**Avg.**
Total Assets (RUB billion)	**174.5**	**166.2**	**145.6**	**141.2**	**111.4**	[3]**11.9**
Total Assets (USD billion)	**6.1**	**5.4**	**4.8**	**4.6**	**4.5**	[3]**7.8**
Tangible Common Equity (RUB billion)	**17.1**	**16.7**	**16.2**	**15.0**	**11.8**	[3]**9.7**
Tangible Common Equity (USD billion)	**0.6**	**0.5**	**0.5**	**0.5**	**0.5**	[3]**5.7**
PPI / Avg RWA (%)	**--**	**--**	**6.1**	**5.5**	**3.1**	[4]**4.9**
Net Income / Avg RWA (%)	**--**	**--**	**1.1**	**2.7**	**1.7**	[4]**1.9**
(Market Funds - Liquid Assets) / Total Assets (%)	**-18.8**	**-21.3**	**-25.5**	**-5.0**	**-10.5**	[5]**-16.2**
Core Deposits / Average Gross Loans (%)	**113.5**	**124.2**	**116.6**	**100.2**	**120.6**	[5]**115.0**
Tier 1 Ratio (%)	**--**	**--**	**15.4**	**11.9**	**9.5**	[4]**12.3**
Tangible Common Equity / RWA (%)	**--**	**--**	**16.5**	**12.4**	**10.8**	[4]**13.2**
Cost / Income Ratio (%)	**70.8**	**72.5**	**48.7**	**52.7**	**62.6**	[5]**61.5**
Problem Loans / Gross Loans (%)	**7.5**	**10.0**	**8.9**	**2.2**	**2.1**	[5]**6.1**
Problem Loans / (Equity + Loan Loss Reserves) (%)	**33.1**	**41.1**	**32.7**	**10.8**	**11.6**	[5]**25.9**

Source: Moody's

[1] All ratios are adjusted using Moody's standard adjustments [2] Basel I; IFRS [3] Compound Annual Growth Rate based on IFRS reporting periods [4] Basel I & IFRS reporting periods have been used for average calculation [5] IFRS reporting periods have been used for average calculation

Opinion

SUMMARY RATING RATIONALE

Moody's assigns a bank financial strength rating (BFSR) of D- to Vozrozhdenie Bank (V-Bank), which translates into a Baseline Credit Assessment of Ba3. The rating is supported by the bank's adequate franchise in SME and retail segments, its more conservative risk appetite compared to regional peers, and solid fee generating capacity. At the same time, the rating is constrained by the relatively weak asset quality, high single-name exposures in loans, and weak bottom-line profitability.

V-Bank's Ba3/Not Prime long- and short-term deposit ratings do not include any possible shareholder support or systemic support in the event of need. V-Bank's BFSR and long-term ratings carry a stable outlook.

Credit Strengths

- Entrenched positions in the Oblast of Moscow, one of Russia's key regional markets

- Adequate franchise in retail and SME banking

- Relatively conservative risk-profile compared to peers

- Solid fee-generating capacity

Credit Challenges

- Relatively weak asset quality

- High single-name and industry loan exposures

- Weak bottom-line profitability due to a thin net interest margin

Rating Outlook

The outlook on V-Bank's BFSR and long-term ratings was changed to stable from negative in November 2011, driven by the stable trends in the key financial fundamentals of the bank following the 2008-2010 economic crisis in Russia.

What Could Change the Rating - Up

Rating upgrades are unlikely at this stage. Nevertheless, a steady increase in market share, particularly in the retail and SME segment, combined with sustainable improvements in profitability, efficiency and asset quality, could exert upward pressure on the BFSR. The bank's deposit ratings would move in line with the BFSR.

What Could Change the Rating - Down

A material deterioration in asset quality, capitalisation, liquidity or profitability, or noticeable weakening in business positions in the Oblast of Moscow could result in downward pressure of the BFSR and deposit ratings.

Recent Results and Company Events

Q1 2011 (unaudited reviewed IFRS)

The bank's assets stood at RUB174 billion (US$1 = RUB28.42) at 31 March 2011, representing a 5% growth from YE2010 (non-annualised). Over the same period, growth in gross loans was around 10%, which was higher than the market average.

Net profit for Q1 2011 stood at low RUB317 million (RUB97 million for Q1 2010), with a RoAA of 0.74%. The negative pressure on the net result stemmed from the bank's narrow net interest margin (NIM; 3.14% for Q1 2011) and new loan-loss provisions that have wiped out 47% of pre provision income. Profitability is likely to improve in the following quarters, due to fewer anticipated new loan loss provisions and a stable NIM.

Full year 2010 (audited IFRS)

In 2010, V-Bank's total assets increased by 14%, to RUB166 billion. For the same period, the net income decreased by 53%, to RUB581 million, impacted by a pressured NIM, new loan loss provisions and fewer FX trading gains.

DETAILED RATING CONSIDERATIONS

Detailed considerations for V-Bank's currently assigned ratings are as follows:

Bank Financial Strength Rating

The rating is supported by the bank's adequate franchise in SME and retail segments, its more conservative risk appetite compared to regional peers, and solid fee generating capacity. At the same time, the rating is constrained by the relatively weak asset quality, high single-name exposures in loans, and weak bottom-line profitability.

The assigned D- rating is one notch lower than the D outcome of Moody's bank financial strength scorecard, reflecting the credit challenges outlined above.

Qualitative Rating Factors (70%)

Factor 1: Franchise Value

Trend: Neutral

V-Bank is a midsize institution that positions itself as a "community bank for SMEs and individuals", and pursues a strategy of organic growth in Russia. The bank had a large client base of around 1.5 million individuals and more than 57.000 companies as of YE2010. V-Bank ranked 24th among Russian banks by assets at Q1 2011, with a market share of around 1%.

V-Bank benefits from its position as one of the leaders in the banking market of the Oblast of Moscow (this region surrounds the City of Moscow), one of Russia's key regional markets, where it boasted a share of around 12% in private deposits and 8% in loans to individuals at YE2010. The bank has a very good coverage in that region in terms of branches and offices (110 units, ranking second behind Sberbank), and in terms of ATMs (460 units). In addition to the Oblast of Moscow, V-Bank also focuses on South and North-West regions of Russia (especially St. Petersburg region). The 63 offices outside of Moscow and Moscow region generated 40% of total loans and about 20% of retail deposits; this share has been stable in the past years.

V-Bank has been historically focused on small and midsize companies; these loans comprised 58% of gross loans at Q1 2011. The share of midsize borrowers is largest by far, with a loan size of RUB100 - 750 million. The share of big-ticket loans tends to vary from 20% to 30% of gross loans; these loans are very concentrated.

V-Bank has resumed the growth of its retail loans in Q1 2011 and 2010, following a reduction of the retail book in 2009. Still, retail loans made up only 14% of gross loans at Q1 2011, compared to 18% at Q1 2009. Retail loans are dominated by mortgages and consumer loans. V-Bank also has a well developed plastic cards business, with more than 1.4 million cards issued. The card business is mostly based on payroll projects for corporate customers; the bank manages 10,000 such projects.

The trend for V-Bank's franchise value is neutral, as we expect that V-Bank would grow in line with the sector average this year at around 15%.

The bank scores D for this factor.

Factor 2: Risk Positioning

Trend: Neutral

The bank has achieved good progress in improving its corporate governance, particularly in such areas as information transparency, protection of minority shareholders' rights and control over economic activities. The volume of related-party transactions, as reported by the external auditor, is immaterial. The bank is controlled by its long-time CEO, Mr. Dmitriy Orlov (30.7% stake). Other significant stakes are held by Mr. Otar Margania (chairman of the board, 18.65%), and JPM Consumer holding (9.37%).

V-Bank has high single-party loan exposures, like most Russian banks. The top 20 borrowers accounted for 32% of gross loans at Q1 2011, or around 230% of core capital. Concentration levels are expected to stay close to the current level in the medium term, as the bank intends to grow in all market segments, including large corporate. The largest industrial exposures were to companies active in manufacturing (24% of loans), trade (24%), and construction (9%). The high share of loans to trade companies is explained by the bank's focus on SMEs.

V-Bank avoids taking on market risk, and invests in securities primarily for liquidity purposes. The structure of the portfolio is conservative, comprising mainly debt securities issued by the Russian government, the Central Bank of Russia (CBR), regional authorities and quasi-sovereign entities, mostly of investment grade quality. Foreign exchange operations are focused on meeting the needs of the bank's clients.

Risk management practices are modest, as the risk function is not fully independent and systems are still developing. Credit underwriting standards are fairly strict (branches have reasonable limits of their own and a common methodology is used for making all loans). Liquidity management tools include cash-flow projections and compliance with internal limits other than the CBR prudential ratios. Stress-testing is performed regularly.

V-Bank's quarterly unaudited financials are prepared under IFRS, and annual statements are audited by PricewaterhouseCoopers. The quality of financial disclosure and frequency are good. Although disclosures on asset quality have improved, we note that the bank did not disclose the amount of restructured loans in its 2010 accounts.

Factor 3: Regulatory Environment

The regulatory environment is evolving in Russia, which negatively affects V-Bank's ratings. Refer to Moody's Banking System Outlook on Russia, published in 2010, for information on this factor.

Factor 4: Operating Environment

Trend: Neutral

This factor is common to all Russian banks. Moody's assigns an E+ score for the overall operating environment.

Quantitative Rating Factors (30%)

Factor 5: Profitability

Trend: Improving

V-Bank's profitability remains low: net income for 2010 stood at RUB581 million, a 53% decrease from 2009. As a result, the bank's ROAA weakened to 0.37% in 2010 from 0.85% in 2009. The deterioration in profitability in 2010was derived from new loan loss provisions on the back of asset quality deterioration, and a lower net interest margin (NIM) due to a 310 basis points decrease in the average loan yield.

We expect profitability to improve somewhat in 2011, due to a lesser pressure on asset quality and MIN. In Q1 2011 the bank's net profit stood at RUB317 million, or more than one-half of the full-year 2010 result. Still, the bank's ROAA is unlikely to exceed 1% in 2011, which is below the 1.5%-2% Russian average.

The bank has a limited capacity to cope with low profits through cost optimization, without damaging its commercial franchise. In 2009 V-Bank slashed its costs by 10%, only to increase them by 13% in 2010. For 2011, the bank expects to increase its cost base by 5-6%, which could be difficult to achieve because Russia remains a high-inflation country (CPI likely to rise by 8.8% in 2011, according to Moody's).

Factor 6: Liquidity

Trend: Neutral

V-Bank's liquidity position is supported by a large core deposit base of corporate and individual clients, with customer deposits funding 78% of assets at Q1 2011. The gross loans to deposits ratio stood at a comfortable 87% at the same date, compared to around 110% system average. The bank maintains an adequate liquidity cushion (cash and money market items, and mostly investment-grade bonds) of around 30%of total assets.

The deposit base is dominated by retail clients (around 65% of deposits at Q1 2011). The bank's second-largest funding class is corporate deposits (35% of deposits). We note that V-Bank has very high single-party concentrations in deposits: its top-29 depositors accounted for around 44% of corporate funds. The bank's liquidity position could be weakened in case of a sudden outflow in large accounts.

The bank's reliance on market sources of funding is low -- there is a strict limit constraining the level of borrowings at not more than 100% of equity or 10% of total liabilities. At Q1 2011, the bank has only issued domestic promissory notes for around RUB7 billion, and has no domestic or foreign bonds outstanding.

Factor 7: Capital Adequacy

Trend: Neutral

V-Bank's total capitalisation ratio (CAR, under Basel 1) stood at an adequate 14.4% at YE2011. Capitalisation is likely to decrease somewhat in 2011, because the bank's weak internal capital generation will lag behind asset growth. We note that the bank has a weak ability to attract new capital from its existing shareholders, making a public share offering or subordinated debt raising more probable in late 2011 or early 2012.

Factor 8: Efficiency

Trend: Improving

Because of a drop in revenues, V-bank's efficiency weakened in 2010: the cost-to-income ratio went up to 73% from 49% a year before. We expect that efficiency might improve somewhat in the medium term, impacted by V-Bank's return to profitability.

Factor 9: Asset Quality

Trend: Weakening

V-Bank's asset quality is relatively weak, in line with other midsize Russian banks. The share of loans overdue by more than 90 days stood at 6.9% at Q1 2011, compared to 7.2% at YE2009. We note, however, that this slight decrease is mostly explained by the 33% growth in gross loans during that period, while the absolute amount of 90+ overdue loans increased by 29%. Most problem loans at V-Bank relate to its midsize and small corporates. The trend in asset quality remains negative, as corporate borrowers have not fully recovered from the financial crisis.

Similar to most Russian banks, V-Bank's asset quality is sensitive to the financial standing of its large borrowers. At Q1 2011, the top-20 borrowers accounted for around 230% of the shareholders' equity and 32% of gross loans.

Global Local Currency Deposit Rating (Joint Default Analysis)

The country support guideline for Russia is low. The history of bank failures is extensive and includes large institutions with only limited selective support being provided.

Moody's assigns a Global Local Currency (GLC) deposit rating of Ba3 to V-Bank. The rating is supported by the bank's Baseline Credit Assessment of Ba3 and does not factor any support - either systemic or from its shareholders.

National Scale Rating

V-Bank is rated Aa3.ru by Moody's Interfax on Russia's National Scale. NSRs are intended as relative measures of creditworthiness among debt issues and issuers within a country, enabling market participants to better differentiate relative risks.

Foreign Currency Deposit Rating

Moody's assigns a Ba3 foreign currency deposit rating to V-Bank. The rating is assigned at the same level as the bank's GLC deposit rating and is not constrained by the foreign currency deposit ceiling for Russia.

ABOUT MOODY'S BANK RATINGS

Bank Financial Strength Rating

Moody's Bank Financial Strength Ratings (BFSRs) represent Moody's opinion of a bank's intrinsic safety and soundness and, as such, exclude certain external credit risks and credit support elements that are addressed by Moody's Bank Deposit Ratings. BFSRs do not take into account the probability that the bank will receive such external support, nor do they address risks arising from sovereign actions that may interfere with a bank's ability to honor its domestic or foreign currency obligations. Factors considered in the assignment of BFSRs include bank-specific elements such as financial fundamentals, franchise value, and business and asset diversification. Although BFSRs exclude the external factors specified above, they do take into account other risk factors in the bank's operating environment, including the strength and prospective performance of the economy, as well as the structure and relative fragility of the financial system, and the quality of banking regulation and supervision.

Global Local Currency Deposit Rating

A deposit rating, as an opinion of relative credit risk, incorporates the BFSR as well as Moody's opinion of any external support. Specifically, Moody's Bank Deposit Ratings are opinions of a bank's ability to repay punctually its deposit obligations. As such, they are intended to incorporate those aspects of credit risk relevant to the prospective payment performance of rated banks with respect to deposit obligations, which includes: intrinsic financial strength, sovereign transfer risk (in the case of foreign currency deposit ratings), and both implicit and explicit external support elements. Moody's Bank Deposit Ratings do not take into account the benefit of deposit insurance schemes which make payments to depositors, but they do recognize the potential support from schemes that may provide assistance to banks directly.

According to Moody's joint default analysis (JDA) methodology, the global local currency deposit rating of a bank is determined by the incorporation of external elements of support into the bank's Baseline Risk Assessment. In calculating the Global Local Currency Deposit rating for a bank, the JDA methodology also factors in the rating of the support provider, in the form of the local currency deposit ceiling for a country, Moody's assessment of the probability of systemic support for the bank in the event of a stress situation and the degree of dependence between the issuer rating and the Local Currency Deposit Ceiling.

National Scale Rating

National scale ratings are intended primarily for use by domestic investors and are not comparable to Moody's globally applicable ratings; rather they address relative credit risk within a given country. A Aaa rating on Moody's National Scale indicates an issuer or issue with the strongest creditworthiness and the lowest likelihood of credit loss relative to other domestic issuers. National Scale Ratings, therefore, rank domestic issuers relative to each other and not relative to absolute default risks. National ratings isolate systemic risks; they do not address loss expectation associated with systemic events that could affect all issuers, even those that receive the highest ratings on the National Scale.

Foreign Currency Deposit Rating

Moody's ratings on foreign currency bank obligations derive from the bank's local currency rating for the same class of obligation. The implementation of JDA for banks can lead to high local currency ratings for certain banks, which could also produce high foreign currency ratings. Nevertheless, it should be noted that foreign currency deposit ratings are in all cases constrained by the country ceiling for foreign currency bank deposits. This may result in the assignment of a different, and typically lower, rating for the foreign currency deposits relative to the bank's rating for local currency obligations.

Foreign Currency Debt Rating

Foreign currency debt ratings are derived from the bank's local currency debt rating. In a similar way to foreign currency deposit ratings, foreign currency debt ratings may also be constrained by the country ceiling for foreign currency bonds and notes; however, in some cases the ratings on foreign currency debt obligations may be allowed to pierce the foreign currency ceiling. A particular mix of rating factors are taken into consideration in order to assess whether a foreign currency bond rating pierces the country ceiling. They include the issuer's global local currency rating, the foreign currency government bond rating, the country ceiling for bonds and the debt's eligibility to pierce that ceiling.

About Moody's Bank Financial Strength Scorecard

Moody's bank financial strength model (see scorecard below) is a strategic input in the assessment of the financial strength of a bank, used as a key tool by Moody's analysts to ensure consistency of approach across banks and regions. The model output and the individual scores are discussed in rating committees and may be adjusted up or down to reflect conditions specific to each rated entity.

Rating Factors

Vozrozhdenie Bank

Rating Factors [1]	A	B	C	D	E	Total Score	Trend
Qualitative Factors (70%)						E+	
Factor: Franchise Value						D	Neutral
Market Share and Sustainability				x			
Geographical Diversification				x			
Earnings Stability				x			

Earnings Diversification [2]							
Factor: Risk Positioning						**D**	**Neutral**
Corporate Governance [2]				**x**			
- Ownership and Organizational Complexity				x			
- Key Man Risk				x			
- Insider and Related-Party Risks				x			
Controls and Risk Management				**x**			
- Risk Management				x			
- Controls			x				
Financial Reporting Transparency			**x**				
- Global Comparability	x						
- Frequency and Timeliness		x					
- Quality of Financial Information				x			
Credit Risk Concentration				**x**			
- Borrower Concentration				x			
- Industry Concentration			x				
Liquidity Management			**x**				
Market Risk Appetite		**x**					
Factor: Operating Environment						**E+**	**Neutral**
Economic Stability					**x**		
Integrity and Corruption					**x**		
Legal System				**x**			
Financial Factors (30%)						**C+**	
Factor: Profitability						**B+**	**Improving**
PPI / Average RWA - Basel I	5.80%						
Net Income / Average RWA - Basel I		1.92%					
Factor: Liquidity						**B**	**Neutral**
(Mkt funds-Liquid Assets) / Total Assets	-17.26%						
Liquidity Management			x				
Factor: Capital Adequacy						**A**	**Neutral**
Tier 1 Ratio - Basel I	13.65%						
Tangible Common Equity / RWA - Basel I	14.45%						
Factor: Efficiency						**C**	**Improving**
Cost / Income Ratio			57.96%				
Factor: Asset Quality						**D+**	**Weakening**
Problem Loans / Gross Loans				7.01%			
Problem Loans / (Equity + LLR)			28.18%				
Lowest Combined Score (9%)						**D+**	
Economic Insolvency Override						**Neutral**	
Aggregate Score						**D**	
Assigned BFSR						**D-**	

[1] - Where dashes are shown for a particular factor (or sub-factor), the score is based on non public information [2] - A blank score under Earnings diversification or Corporate Governance indicates the risk is neutral