

Credit Opinion: First Ukrainian International Bank, PJSC

Global Credit Research - 26 Sep 2013

Donetsk, Ukraine

Ratings

Category	Moody's Rating
Outlook	Rating(s) Under Review
Bank Deposits -Fgn Curr	*Caa2/NP
Bank Deposits -Dom Curr	*Caa1/NP
NSR Bank Deposits -Dom Curr	**Ba3.ua/--
Bank Financial Strength	E
Baseline Credit Assessment	(caa1)
Adjusted Baseline Credit Assessment	(caa1)
Bkd Senior Unsecured	**Caa1

* Rating(s) within this class was/were placed on review on September 25, 2013

** Placed under review for possible downgrade on September 25, 2013

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Key Indicators

First Ukrainian International Bank, PJSC (Unconsolidated Financials)[1]

	[2]12-12	[2]12-11	[2]12-10	[2]12-09	[2]12-08	Avg.
Total Assets (UAH million)	27,751.9	29,804.3	25,648.0	15,918.1	17,789.2	[3]11.8
Total Assets (USD million)	3,447.4	3,720.9	3,219.1	1,987.3	2,317.8	[3]10.4
Tangible Common Equity (UAH million)	4,413.1	4,126.6	3,675.8	2,620.5	3,025.9	[3]9.9
Tangible Common Equity (USD million)	548.2	515.2	461.3	327.2	394.3	[3]8.6
Net Interest Margin (%)	3.8	3.3	3.8	5.8	6.2	[4]4.6
PPI / Average RWA (%)	3.2	3.4	3.5	—	5.6	[5]3.9
Net Income / Average RWA (%)	1.3	2.6	4.0	—	0.7	[5]2.1
(Market Funds - Liquid Assets) / Total Assets (%)	-11.8	-23.7	-15.1	22.9	31.4	[4]0.7
Core Deposits / Average Gross Loans (%)	87.3	109.3	99.2	38.9	46.1	[4]76.2
Tier 1 Ratio (%)	19.8	20.3	21.9	—	18.3	[5]20.1
Tangible Common Equity / RWA (%)	19.4	20.0	26.1	—	18.1	[5]20.9
Cost / Income Ratio (%)	57.8	58.2	57.1	36.2	38.0	[4]49.5
Problem Loans / Gross Loans (%)	27.1	30.8	35.1	40.7	15.3	[4]29.8
Problem Loans / (Equity + Loan Loss Reserves) (%)	69.6	76.8	84.5	104.7	53.7	[4]77.9

Source: Moody's

[1] All figures and ratios are adjusted using Moody's standard adjustments [2] Basel I; IFRS [3] Compound Annual

Growth Rate based on IFRS reporting periods [4] IFRS reporting periods have been used for average calculation
[5] Basel I & IFRS reporting periods have been used for average calculation

Opinion

SUMMARY RATING RATIONALE

On 25 September 2013 Moody's lowered the baseline credit assessments (BCAs), as well as downgraded the deposit, debt and National Scale Ratings (NSRs) of 14 financial institutions in Ukraine.

At the same time, Moody's placed on review for further downgrade these financial institutions' deposit and debt ratings, and NSRs, of 13 banks (2 banks' deposit ratings were at Caa1 level already) and one leasing company.

First Ukrainian International Bank's (FUIB) ratings were affected as follows:

- BFSR downgraded to E from E+, now equivalent to a caa1 BCA (formerly b3)
- Long-term local-currency deposit rating downgraded to Caa1 from B3
- Long-term foreign-currency deposit rating downgraded to Caa2 from Caa1
- Long-term foreign-currency senior unsecured debt rating downgraded to Caa1 from B3
- NSR downgraded to Ba3.ua from Baa3.ua

The BFSR carries a stable outlook; all the other long-term global-scale ratings and NSR were placed on review for downgrade

These rating actions were prompted by the weakening of Ukraine's credit profile, as reflected by Moody's downgrade on 20 September 2013 of Ukraine's government bond rating to Caa1 from B3 and the related adjustments to the country's ceilings, mainly (1) the foreign-currency bank deposit ceiling lowered to Caa2 from Caa1; (2) the local-currency bank deposit and bond ceiling lowered to Caa1 from B2; and (3) the foreign-currency bond ceiling lowered to Caa1 from B3.

These ceilings cap the maximum ratings that can be assigned to banks and other issuers domiciled in the country, thereby prompting the downgrades of the 11 financial institutions and one leasing company. The sovereign ratings were also placed on review for further downgrade, which informs our decision to place the financial institutions' debt and deposit ratings on review for further downgrade.

Rating Drivers

- Exposure to Ukraine's weak and volatile economic environment
- Mediocre profitability
- Weak asset quality
- Satisfactory capital adequacy
- Acceptable liquidity profile
- Established franchise

Rating Outlook

The BFSR carries a stable outlook; all the other long-term global-scale ratings and NSR are on review for downgrade.

What Could Change the Rating - Up

The last rating action follows the weakening of Ukraine's credit profile, as reflected by downgrades of the sovereign ratings and country ceilings. A confirmation of the sovereign ratings would lead to a confirmation of the bank's ratings, which are currently placed on review.

What Could Change the Rating - Down

A further downgrade of the sovereign ratings would lead to a downgrade of the bank's ratings.

DETAILED RATING CONSIDERATIONS

EXPOSURE TO UKRAINE'S WEAK AND VOLATILE OPERATING ENVIRONMENT

Almost all of FUIB's business is concentrated in Ukraine, which poses the bank to serious challenges given the weak and volatile operating environment in the country. The difficult economic conditions weigh on the bank's asset quality, profitability and franchise strength. However the negative implications stemming from economic conditions have been less pronounced compared with most Ukrainian banks, reflected in FUIB's better than average financial indicators in the past several years.

Apart from the overall weak economy, FUIB's exposure to Ukraine's sovereign bonds (rated b3 with negative outlook) is another key rating constraint. The bank's exposure to these bonds accounted for 64% of its equity as of YE2012, making the bank vulnerable to a further possible weakening of the sovereign credit quality.

MEDIOCRE PROFITABILITY

FUIB reported a net income of \$34.67 million for 2012, 38.5% lower than in 2011. The reduction in the profit was driven by higher funding costs, provisioning charges and operating expenses. The bottom line result was supported by increased interest and fee income. We expect the bank's profitability to remain under pressure in the short-to-medium term due to limited business growth potential and still rising loan loss charges.

WEAK ASSET QUALITY

FUIB's problem loans (defined as individually and collectively impaired loans under IFRS) accounted for 27% of total loans as of YE2012, down from 30.7% at YE2011. Loan loss reserves of 14.8% as of YE2012 will have to increase in the near-term to cover all expected credit losses, especially as economic conditions continue to weaken.

SATISFACTORY CAPITAL ADEQUACY

The bank's capital position is adequate, with a Tier 1 ratio and total Capital Adequacy Ratio of 19.8% and 23.5%, respectively, at YE2012 according to the bank's IFRS report. While we further loan loss charges in the near-term, we believe that these charges will be covered by FUIB's pre-provision income, therefore having little or no adverse effect on the capital. Another challenge for FUIB's capital adequacy may be a potential material weakening in Ukraine government's credit quality to which the bank has a sizable exposure. Based on our scenario analysis (stress-test) FUIB will still have acceptable capital under the central scenario, which assumes only moderate sovereign credit deterioration.

ACCEPTABLE LIQUIDITY PROFILE

FUIB is predominantly funded by customer accounts and deposits. The bank doesn't have to make any significant repayments on international debt till 2014 due to the restructuring agreements reached in 2009. The largest repayment of international debt on bank's Eurobonds in the amount of \$252,488 million (less than 10% of liabilities as at YE 2012) is due in December 2014. As of YE2012 liquid assets accounted for 29% (about 17% excluding government bonds) of the bank's total assets. This cushion of liquidity, coupled with moderate funding concentration - top 10 customer accounts made up 15% of the total customer funds - renders acceptable liquidity profile.

ESTABLISHED FRANCHISE

In 2011 FUIB finished its merger with Dongorbank and as a result improved its market shares and regional coverage. FUIB's franchise covers 24 regions in Ukraine with 48 branches and outlets and 169 point of sales. The bank is focused on corporate and SME lending, which collectively account for 73% of its loan portfolio as at YE2012. FUIB has established relationships with a number of large companies with relatively good credit quality. Merger with Dongorbank allowed the bank to acquire new corporate and retail customers and diversify its franchise. Although the bank has developed its retail lending, its contribution to net income still remains moderate. Going forward the bank is planning to increase SME and retail lending however corporate lending will stay its priority.

Global Local Currency Deposit Rating (Joint Default Analysis)

The rating is based on FUIB's caa1 standalone credit strength and does not factor any external support.

National Scale Rating

FUIB is rated Ba3.ua by Moody's on Ukraine's national rating scale. National Scale Ratings (NSRs) are intended as relative measures of creditworthiness among debt issuers and issuers within a country, enabling market participants to better differentiate relative risks.

Foreign Currency Deposit Rating

Moody's assigns a Caa2 foreign currency deposit rating to FUIB. The rating is constrained by the country foreign currency deposit ceiling for Ukraine.

Foreign Currency Debt Rating

Moody's assigns a Caa1 global foreign currency debt rating to FUIB's senior unsecured obligations.

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 Credit 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

First Ukrainian International Bank, PJSC

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						E	Neutral
Corporate Governance [2]	--	--	--	--	--		
- Ownership and Organizational Complexity	--	--	--	--	--		
- Key Man Risk	--	--	--	--	--		
- Insider and Related-Party Risks	--	--	--	--	--		
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	--	--	--	--	--		
- Borrower Concentration	--	--	--	--	--		
- Industry Concentration	--	--	--	--	--		
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+	Neutral
PPI % Average RWA (Basel I)		3.35%					
Net Income % Average RWA (Basel I)	2.64%						
Factor: Liquidity						C-	Neutral
(Market Funds - Liquid Assets) % Total Assets	-16.87%						
Liquidity Management					x		
Factor: Capital Adequacy						A	Neutral
Tier 1 Ratio (%) (Basel I)	20.66%						
Tangible Common Equity % RWA (Basel I)	21.85%						
Factor: Efficiency						C	Neutral
Cost / Income Ratio			57.71%				
Factor: Asset Quality						E	Neutral
Problem Loans % Gross Loans					30.98%		
Problem Loans % (Equity + LLR)					76.97%		
Lowest Combined Financial Factor Score (9%)						E	
<i>Economic Insolvency Override</i>						Neutral	
Aggregate BFSR Score						D-	
Aggregate BCA Score						ba3	
Assigned BFSR						E	
Assigned BCA						caa1	

[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.



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