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Fitch Revises Credit Bank of Moscow's Outlook to Stable; Affirms at 'BB'

Fitch Ratings - Moscow - 24 Jun 2021: Fitch Ratings has revised the Outlook on Credit Bank of Moscow's (CBM) Long-Term Issuer Default Ratings (IDRs) to Stable from Negative and affirmed the IDRs at 'BB'. A full list of rating actions is below.

The rating action follows the revision of the outlook on Russia's operating environment score to stable from negative. The negative implications from the pandemic on the Russian economy resulted in an only moderate weakening of Russian banks' asset quality and profitability in 2020. We expect Russia's real GDP growth to recover to 3.7% in 2021 after a 3.0% contraction in 2020 and this should support sector performance in 2021.

The revision of the Outlook on CBM's IDRs also reflects the limited impact of the economic downturn on the bank's asset quality and profitability ratios, and CBM's stronger loss absorption capacity since our previous review in September 2020. We note a recovery in the bank's core pre-impairment performance in 2H20-1Q21 after a dip in 1H20, as well as strengthening of its core capital through the secondary public offering (SPO) in 2Q21.

Key Rating Drivers

IDRS, VIABILITY RATING (VR)

CBM's asset quality is supported by a large volume of low-risk reverse repos (46% of total assets at end-1Q21) and liquid assets of mainly investment-grade quality (16%), while credit risk mostly stems from the bank's loan book (34%). The bank's impaired loans (Stage 3 and purchased or originated credit-impaired) were 5% of gross loans at end-1Q21 and were reasonably covered at 67% by specific loan loss allowances (LLA). Stage 2 exposures were a limited 2% of gross loans.

Stage 3 and Stage 2 loans largely overlap with Fitch's assessment of the bank's high-risk assets. At end-1Q21, Fitch estimates that CBM's net high-risk assets amounted to RUB58 billion (or 0.3x common equity Tier 1 (CET1) capital), which is broadly unchanged relative to end-2Q20.

The bank reported a recovery in its core pre-impairment performance to a decent 3.6% of average gross loans in 2020-1Q21 from 2.5% in 1H20. This was mainly driven by an increase in business volumes, which supported net interest and fee income. We view the bank's annual pre-impairment profit as a reasonable buffer that covers about 60% of the high-risk assets.

Operating profit in 2020 was a good 1.9% of risk-weighted assets (RWAs), despite higher loan

impairment charges (LICs, 2% of average gross loans). The operating results were stronger in 1Q21 (2.5% of RWAs, annualised), supported by lower LICs (0.2% of average loans, annualised) amid receded asset quality risks. However, we note the significant dependence of the bank's profitability on its concentrated repo business, which boosts annual operating profit by 0.6%-1.0% of RWAs.

The CET1 ratio was a moderate 11.7% at end-1Q21. We estimate the ratio at 13% post SPO in May 2021, which aims to support growth in 2021-2022. The regulatory core Tier 1 capital ratio was a lower 8.9% at end-1Q21, due to higher loan provisioning in the local accounts. CBM targets a 9% regulatory core Tier 1 ratio, which provides only modest headroom over the mandatory fully loaded minimum of 8%, especially in the context of high single borrower and industry concentrations in CBM's corporate loan book. Fitch views CBM's ability to absorb additional losses through capital as limited. However, we do not expect credit losses to make a direct hit on capital due to a sufficient pre-impairment cushion and only moderate amounts of residual high-risk assets.

Our assessment of CBM's capitalisation considers significant 1.5x double-leverage at the level of the bank's holding company, Concern Rossium, which also holds stakes in several non-bank businesses. The holdco had around RUB100 billion of net debt at end-1Q21 and is largely reliant on upstreaming of liquidity and dividends to service it, potentially representing a significant burden for CBM. Positively, the expected dividends upstream from Rossium's non-bank subsidiaries in 2021 broadly cover the holdco's interest payments for 2021. Furthermore, the bank's key shareholders currently hold most of the holdco's debt, which somewhat reduces risks, although the funding sources for these debt purchases are unclear to Fitch.

The bank's total capital is bolstered by a large junior debt cushion, including additional Tier 1 perpetual debt and Tier 2 subordinated debt, which together equal RUB146 billion, or 8.6% of RWAs.

Liquidity risks are only moderate, despite high funding concentrations. Lumpy funding in the form of direct repos and certain large corporate deposits is matched with a large reverse repo portfolio secured with quasi-sovereign bonds. About RUB730 billion of these bonds received under reverse repos are currently unpledged and can be used to raise funding (equal to 41% of total deposits), if needed.

Excluding reverse repos and dedicated funding, CBM's liquidity buffer (comprising cash and equivalents, short-term interbank and unencumbered on-balance-sheet securities repo-able with the central bank) at end-1Q21 covered customer accounts by a decent 40%, while contractual repayments of wholesale debt are low for the next few years.

DEBT RATINGS

The ratings of senior unsecured debt issued through CBOM Finance PLC (special-purpose vehicle; SPV) are aligned with the bank's 'BB' IDRs.

CBM's Tier 2 subordinated debt (placed by the SPV) has been affirmed at 'B+', two notches below the 'bb' VR, which is the baseline notching for loss severity for these instruments.

CBM's perpetual notes (placed by the SPV) have been affirmed at 'B-'. The rating is four notches below the bank's VR, reflecting the perpetual notes' deep subordination relative to senior unsecured creditors, resulting in higher loss severity, and CBM's option to cancel coupon payments at its discretion, resulting in additional non-performance risk.

SUPPORT RATING AND SUPPORT RATING FLOOR

CBM's Support Rating Floor (SRF) of 'B+' reflects Fitch's view of a moderate probability of state support to privately-owned banks in Russia, as evidenced by bail-outs of senior unsecured creditors at larger Russian privately-owned banks in the past and the absence of senior creditors bail-in mechanism in Russian banking legislation. CBM's 'B+' SRF also captures its only moderate systemic importance (1.5% of system loans) and sizeable (in absolute terms) deposit base.

RATING SENSITIVITIES

Factors that could, individually or collectively, lead to positive rating action/upgrade:

An upgrade would require a strengthening of the bank's franchise and business model, including a reduction in balance-sheet and revenue concentrations. A marked improvement in asset quality, higher core capital ratios and reduced risks stemming from double leverage at the holdco level would also be credit positive.

Factors that could, individually or collectively, lead to negative rating action/downgrade:

CBM's IDRs would be downgraded if there was a material asset quality deterioration resulting in core capital erosion. For example, Fitch may take this view if annualised LICs exceed 3.5% of average gross loans in two to three consecutive semi-annual reporting periods, which could translate into negative or close to negative operating performance, or if our assessment of the bank's net high-risk assets rises significantly above 0.5x CET1.

The debt ratings are primarily sensitive to changes in their respective anchor ratings.

Best/Worst Case Rating Scenario

International scale credit ratings of Financial Institutions and Covered Bond issuers have a best-case rating upgrade scenario (defined as the 99th percentile of rating transitions, measured in a positive direction) of three notches over a three-year rating horizon; and a worst-case rating downgrade scenario (defined as the 99th percentile of rating transitions, measured in a negative direction) of four notches over three years. The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Best- and worst-case scenario credit ratings are based on historical performance. For more information about the methodology used to determine sector-specific best- and worst-case scenario credit ratings, visit <https://www.fitchratings.com/site/re/10111579>

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

ESG Considerations

CBM has an ESG Relevance Scores of '4' for Governance Structure and Group Structure due to significant level of relationship-based operations, a lack of transparency with respect to ownership structure and significant double leverage at the level of the bank's holdco. These considerations have a moderately negative impact on the credit profile, and are relevant to the ratings in conjunction with other factors.

Unless otherwise disclosed in this section, the highest level of ESG credit relevance is a score of '3'. This means ESG issues are credit-neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg

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Rating Actions

ENTITY/DEBT	RATING		RECOVERY	PRIOR
CBOM Finance PLC				
• senior unsecured	LT BB	Affirmed		BB
• subordinated	B-	Affirmed		B-
• subordinated	B+	Affirmed		B+
Credit Bank of Moscow	LT IDR	BB 	Affirmed	BB 
	ST IDR	B	Affirmed	B
	LC LT IDR	BB 	Affirmed	BB 
	Viability	bb	Affirmed	bb
	Support	4	Affirmed	4
	Support Floor	B+	Affirmed	B+

RATINGS KEY OUTLOOK WATCH

POSITIVE	⊕	◊
NEGATIVE	⊖	◊
EVOLVING	◊	◆
STABLE	◉	

Applicable Criteria

[Bank Rating Criteria \(pub.28 Feb 2020\) \(including rating assumption sensitivity\)](#)

Additional Disclosures

[Solicitation Status](#)

Endorsement Status

CBOM Finance PLC UK Issued, EU Endorsed

Credit Bank of Moscow UK Issued, EU Endorsed

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