Conference Transcription
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Speakers: Vladimir Chubar, Eric de Beauchamp, Elena Finashina

Operator: Good day, ladies and gentlemen, and welcome to the CREDIT BANK OF MOSCOW 1H 2015 Financial and Business Results Conference Call.

Today's conference is being recorded. At this time I would like to turn the conference over to your host. Please go ahead.

Elena Finashina: Thank you very much and good afternoon, ladies and gentlemen.

My name is Elena Finashina and I am Director of the International Business Division, in charge of investor relations. I am happy to present our speakers on today's webcast and conference call on CREDIT BANK OF MOSCOW 2Q 2015 financial and business results. By tradition here with me are Vladimir Chubar, Chief Executive Officer of the Bank, and Eric de Beauchamp, Senior Vice President. Vladimir Chubar will open today's call dwelling on the market sentiments and business results of the Bank and afterwards, Eric de Beauchamp will take the floor, proceeding with a detailed analysis of financial results of the Bank. All your questions and comments are very welcome after the presentation when we open the Q&A session.

Now I would like to turn the floor over to Vladimir.

Vladimir Chubar: Thank you, Elena. Ladies and gentlemen, thank you for joining today's call.

First of all, we must admit that last week turned out to be rich in the events due to a high season in corporate reporting, and the financial community became deeply involved in this process, losing an opportunity to enjoy the last days of summer. This is to be lived through.

And back on topic, we saw that, in general, Russian banking sector was still suffering from negative trends in the economy in 2Q 2015 but, at the same time, markets were calm and banks were operating in a rather stable environment. Stability stands for clarity in risk assessment, therefore offering a possibility to banks for a cool-headed appraisal of the situation.

Let's now move to our key developments. As you can see on **slide number 4** of the presentation in the table with the key financials, the Bank's shareholders' equity went up from RUB 60 billion to RUB 75.7 billion during the reporting period and total capital adequacy ratio increased from 15.8% to 19%. This resulted from two landmark deals on raise of additional capital which were closed in June.

- First of all, in early June the Bank signed a subordinated loan agreement with Deposit Insurance Agency in the amount of RUB 20.2 billion. Later, in mid-June, CBR approved the inclusion of this subordinated debt into the Bank's Tier 2 capital. Generally, we feel ourselves comfortable with the terms and conditions under these sub loan agreements as they do fit well the Bank's strategy.

- The second deal chronologically, but, at the same time, a milestone deal in the Bank's history, took place in end-June when the Bank went public on the Moscow Exchange. Over 450 orders were collected, most of which in terms of quantity were placed by individual investors. As a result of the offering, the Bank raised RUB 13.2 billion by selling 18.8% of its share capital in the open market.

- The Bank's ownership structure was changed respectively, which you can see on a pie chart in the bottom right of the slide. Post-IPO, Roman Avdeev through the Rossium Group has retained his economic and voting stake in the company at 70%, down from 86.2%. The combined stake of international financial institutions EBRD, IFC and RBOF decreased from 13.8% to 11.2%.

Let's now move further to **slide number 5** on corporate banking business development.

- Today corporate banking is a key business driver for the Bank. In the diagram at the upper left we can see that the growth rates for 1H 2015 are comparable to the whole year of 2014. We forecast that this trend will continue till the end of this year but maybe at a slower pace.

- Good diversification by industries is a valuable advantage in terms of risk management in such turbulent times as now. It gives us an opportunity to closely monitor businesses of our corporate customers and react swiftly in the event of worsening of their financial standing. It also gives us a good sense of how different sectors feel in this very moment and where we might find potential for further growth.

On **slide number 6**, there is a brief review of our retail banking business.

- Our retail lending growth slowed down significantly starting from late-2014 due to surged risks in this business segment coupled with lower demand from individuals. In order to maintain loan portfolio quality stable we tightened our lending standards which resulted in a reduction in origination of new loans. Our target segments are mortgage loans and unsecured cash loans.

- In addition, the Bank continued to optimise its distribution network by closing unprofitable branches and decreasing the number of payment terminals and ATMs. Record-low cost to income ratio is partly a result of the Bank's policy of economy.

And now I suggest moving further, Eric will provide details on the Bank's financial results. Eric, please.

Eric de Beauchamp: Thank you, Vladimir. Good afternoon, ladies and gentlemen.

So I suggest turning to **slide number 8** and starting our financial performance review from income and expense dynamics.

- During the reporting period, operating income showed positive dynamics, increasing by 4% up to RUB 14.8 billion, driven by the other net income item, particularly FX gains and gains on financial instruments.

- The net interest income reduced slightly by 4%, triggered by increased funding costs in 1H 2015 resulting in growing interest expenses by 87% to RUB 28.3 billion. The main source of interest income, which increased by 49% to RUB 38.7 billion, remains revenue on the corporate loan portfolio which demonstrated a 51% growth y-o-y and amounted RUB 21 billion or 53% of the total interest income.

- The growth of operating expenses is not significant, +1% up to RUB 4.8 billion as a result of increase in provisions for impairment of other assets. At the same time, the Bank's operational efficiency continued to stay very high as shown by cost to income ratio at the level of 29.5%.

- The decrease of ROA and ROE to 0.4% and 3.6% respectively was driven by the growth of provisions in 1H 2015 in light of the deterioration of the loan quality of a number of borrowers due to economic downturn.

On the next **slide - number 9**, we can see a review of the Bank's asset structure.

- The Bank's assets increased by 29% y-t-d driven by two main factors: the growth of loan portfolio and the increase of deposits in credit institutions which now represent 57% and 16% of total assets respectively.

- The net corporate loan portfolio demonstrated a 22% increase y-t-d, reaching RUB 314 billion, triggered mainly by property rental and equipment leasing sectors.

- The Bank concentrates on high-quality retail borrowers, whose loan demand is still declining. Moreover, CREDIT BANK OF MOSCOW requirements to new retail customers became more strict. As a result, the Bank's net retail loan portfolio shrank by 2% in 1H 2015 to RUB 118 billion.

- As for the second source of asset growth, the item due from credit institutions reached a level of RUB 117 billion, mainly due to increase of repo transactions backed by securities of first-class issuers.

Key loan portfolio metrics are covered on **slide number 10**.

- During the first six months of 2015 the level of nonperforming loans went up by 2.6 points, reaching 4.9%, as a result of worsening quality of corporate loan portfolio.

- The loan loss provision ratio increased by 0.7 points during the reporting period, up to 4.8%.

- Concentration on top 10 and top 20 largest borrowers slightly increased to 22% and 35% of the gross loan portfolio respectively. Related party lending remained at a low level of 1.6% of total equity.

More details on the loan portfolio quality are provided on **slide number 11**.

- The increase in corporate NPLs at the end of June to 4.3% is explained by the general deterioration of the financial condition of some of the Bank's large borrowers as a result of macroeconomic downturn. Around 60% of newly originated overdue loans in the corporate loan portfolio are linked with one large corporate borrower from the industrial and infrastructure construction sector which we closely monitor.

- The NPL coverage ratio of the corporate loan portfolio accounts for 94% which is in line with the market. At the end of 2014, the corporate loan portfolio was overprovisioned due to the absence of problem loans. Now, as the market conditions have changed, the Bank optimised the NPL coverage and in the near future plans to continue to maintain this level of coverage. The cost of risk increased by 1.5 points at the end of June to 3.5%, reflecting the complicated financial position of some borrowers, leading to the creation of additional provisions.

- The quality of the retail loan portfolio is maintained at a stable level with NPL and LLP ratios being 6.5% and 6.7% respectively. Despite the maturing retail loan book, its quality remains persistent with a cost of risk reduction to 5.3%.

The following **slide - number 12**, focuses on the funding structure of the Bank.

- The Bank's funding base is well diversified with significant share of customer deposits representing 60% of total liabilities with a 50% and 43% split between corporate and retail customers respectively. A significant inflow of corporate deposits took place during the reporting period that led to increase of corporate deposits by 36% y-t-d, reaching RUB 233 billion.

- A significant change in the Bank's funding structure is expressed in expanded share of deposits by the Central Bank, which now constitute 22% of total liabilities. The funds were raised from the Central Bank and backed by securities from the Lombard List received by the Bank from counterparties under reverse repurchase agreements.

- Despite the rouble situation, the Bank does not have any pressure on the liabilities side in terms of its debt repayment. Only RUB 18 billion and RUB 25 billion will have to be repaid in 2015 and 2016 respectively, among which only RUB 5 billion are denominated in foreign currency and will be repaid this September.

Let's proceed to **slide number 13** which provides information on the Bank's capital.

- During the first six months of 2015, the Bank managed to significantly reinforce its capital position thanks to the two following operations. The first one is the inclusion of a subordinated debt totalling RUB 20.2 billion to the additional capital, which was attracted from the Deposit Insurance Agency in the form of federal loan bonds. The second operation is the successfully completed IPO on the Moscow Stock Exchange where the Bank raised RUB 13.2 billion.

- As a result of these two deals, the Bank's total capital according to Basel III standards increased by 34.9% to RUB 121 billion, with a capital adequacy ratio of 19% and Tier 1 capital ratio of 11.6%. Capital adequacy ratio under Russian Accounting Standards went up to 16.8% for N1.0 and 9.2% for N1.1 and N1.2 as of the 1 August 2015.

These were the main highlights of the Bank's financial and business results for 1H 2015. Thank you for your attention and let's proceed to the Q&A session.

Operator: Thank you, ladies and gentlemen.

If you wish to ask a question over the telephone, please press *1 on your telephone keypad. Please ensure that the mute function on your telephone is switched off to allow your signal to reach our equipment and please state your name before posing your question. Once again, press *1 to ask a question. We will pause for a moment to allow participants to signal.

As a reminder, to ask a question at this time please press *1. As a reminder, ladies and gentlemen, to ask a question please press *1. Our first question comes from Tatiana Shubina from RBC Media. Please go ahead.

Tatiana Shubina: Hello, Vladimir.

I have one question about growth of assets in other banks and financial institutes. I see that it was very strong growth in first six months. How you can explain this? Does it mean that the Bank now prefer to give money to other banks, not to real sector and customers? Thank you.

Vladimir Chubar: Good evening.

Thank you for the question. First of all of course it's a very big increase, absolutely right. There is a set of the transactions that were made with several customers which are not rated but it is mostly REPO transactions when we use high-level bonds as a pledge and of course normally we take money to refinance this debt from CBR. So it's very simple.

Tatiana Shubina: Okay, thank you.