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Credit Opinion: InFinBank

Global Credit Research - 20 Jun 2012

Tashkent, Uzbekistan

Ratings

Category	Moody's Rating
Outlook	Stable
Bank Deposits	B3/NP
Bank Financial Strength	E+
Baseline Credit Assessment	(b3)
Adjusted Baseline Credit Assessment	(b3)

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Key Indicators

InFinBank (Consolidated Financials)[1]

	[2]**12-11**	[2]**12-10**	[2]**12-09**	[2]**12-08**	**Avg.**
Total Assets (UZS million)	**191,320.6**	**110,858.9**	**83,598.1**	**21,821.5**	[3]**106.2**
Total Assets (USD million)	**106.6**	**67.6**	**55.3**	**15.7**	[3]**89.5**
Tangible Common Equity (UZS million)	**16,161.3**	**13,889.0**	**6,980.9**	**5,607.9**	[3]**42.3**
Tangible Common Equity (USD million)	**9.0**	**8.5**	**4.6**	**4.0**	[3]**30.8**
Net Interest Margin (%)	**3.4**	**3.1**	**4.8**	**4.0**	[4]**3.8**
(Market Funds - Liquid Assets) / Total Assets (%)	**-35.2**	**-44.7**	**-59.8**	**-45.0**	[4]**-46.2**
Core Deposits / Average Gross Loans (%)	**265.0**	**241.1**	**383.6**	**126.8**	[4]**254.1**
Tier 1 Ratio (%)	**13.6**	**22.8**	**--**	**--**	[5]**18.2**
Cost / Income Ratio (%)	**64.0**	**52.8**	**50.2**	**63.5**	[4]**57.6**
Problem Loans / Gross Loans (%)	**6.8**	**7.8**	**0.6**	**--**	[4]**5.1**
Problem Loans / (Equity + Loan Loss Reserves) (%)	**27.0**	**19.9**	**2.1**	**--**	[4]**16.3**

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] 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

We assign a standalone Bank Financial Strength Rating (BFSR) of E+ to Infinbank, which maps to a standalone credit assessment of b3. The standalone rating is constrained by the bank's (i) high single-name credit concentration, (ii) its involvement in related-party business, (iii) the unseasoned nature of Infinbank's rapidly augmented loan portfolio and insufficient level of loan loss reserves, and (iv) capital adequacy which lags behind the rapid growth of business volumes. We also note that Infinbank has significant investments in fixed assets.

At the same time, factors underpinning Infinbank's standalone rating include (i) its strong profitability and the recurring nature of its income sources, and (ii) the bank's conservative liquidity position which addresses the structural weaknesses of its funding mix.

Infinbank's Global Local Currency (GLC) deposit ratings of B3/Not Prime do not incorporate any element of systemic support given the bank's limited franchise value and its low importance for the Uzbek banking system as a whole.

Rating Drivers

- High single-name concentration of the bank's loan portfolio

- Strong recurring profitability supported by a sizeable fee-and-commission component

- Sufficient liquidity cushion which addresses the potential risks of sudden chunky withdrawals by the bank's depositors

- Increase in capital levels lags behind growth of business volumes; quality of capital is under pressure from the material level of related-party lending and investments in fixed assets

- Rapid growth of the loan book raises concerns about loan seasoning, and the loan loss reserves appear to be insufficient

Rating Outlook

All of the bank's ratings carry a stable outlook.

What Could Change the Rating - Up

Infinbank's standalone BFSR has limited upside potential at its current level. However, in the longer term, the BFSR might map to a higher standalone credit assessment, as opposed to b3 currently, if the bank were to strengthen its franchise value and increase its core business volumes while also reducing credit concentrations and lengthening the maturity of its funding base. In order to achieve higher ratings, all the conditions mentioned above would need to be accompanied by stable and sound financial fundamentals.

What Could Change the Rating - Down

Negative pressure could be exerted on Infinbank's standalone ratings as a result of (i) any failure by the bank's shareholders to support the institution's rapid growth by additional capital injections, and (ii) any notable increase in concentration on either the asset or the liability side of the balance sheet (or both). A substantial increase in the volume of related-party business or non-core investments (such as equities or fixed assets) represent another factor that could have an adverse impact on Infinbank's ratings.

Recent Results and Company Events

Domiciled in Tashkent, Infinbank reported total IFRS assets of UZS191 billion (US$106.6 million) at YE2011, a 73% increase from the YE2010 level, while its total equity grew only by 15% mainly due to capitalisation of profits. Infinbank reported net IFRS income of UZS6.0 billion (US$3.4 million) for 2011.

DETAILED RATING CONSIDERATIONS

Detailed considerations for Infinbank's currently assigned ratings are as follows:

Risk Positioning

Infinbank's ownership structure includes a number of legal entities and individual shareholders; one of these individuals (Mr F.D. Mamadjanov) owned a 40.00% stake in the bank as of YE2011 - and he is the only shareholder holding a blocking stake. Related-party loans extended by Infinbank accounted for approximately a quarter of its Tier 1 capital at YE2011, a high level by international standards, although comparable with that reported by the bank's peers in the Commonwealth of Independent States.

Single-name concentration in Infinbank's loan portfolio is high, with the aggregate credit exposure to the top 20 loans amounting to 64% of total gross loans and 265% of Tier 1 capital at YE2011. Industry concentration does not appear significant, with the largest exposures to the trade and manufacturing sectors (27% and 23% of total gross loans, respectively, at YE2011) being fairly well diversified internally.

Profitability

Infinbank posted return on average assets (ROAA) of 4.0% and return on average equity (ROAE) of 39% in 2011, a very strong result even against the background of generally robust profitability of other Uzbek-based peers. In 2011, the bank relinquished effective control over its insurance subsidiary "Asia Insurance LLC", which had contributed about 21% of the institution's total revenues in 2010. The cessation of this revenue stream was compensated by strengthening of Infinbank's core income sources - net interest income and net fees and commissions - which grew by 64% and 40%, respectively, and together comprised over 90% of the bank's total revenues in 2011.

We note that fees and commissions (largely those earned on settlement operations) are the largest component of the bank's earnings, which we view positively as they are less susceptible to market fluctuations. The rapid pace of lending growth improved the bank's net interest margin (NIM) to 3.37% in 2011 compared to 3.09% a year earlier. However, NIM is still suppressed by Infinbank's need to maintain a high portion of liquid assets given the short-term nature of its funding sources. We expect Infinbank to continue demonstrating strong profitability going forward, although we caution that the bank's operations are largely concentrated on only a handful of key clients, rendering its performance vulnerable to any potential negative developments that may affect these clients' businesses or relationships with the bank.

Liquidity and Funding

Infinbank's funding base is mainly composed of customer accounts which exceeded 80% of total non-equity funding as at YE2011. We note the relatively granular nature of this funding source, with no single depositor dominating and top 20 deposits together accounting for 30% of total customer funding. At the same time, short-term and "on demand" accounts represent the bulk of customer funding. Borrowings from other banks (16% of total liabilities at YE2011) facilitate just a slight lengthening of the liabilities structure. Overall, only one third of Infinbank's liabilities have contractual duration of more than three months (although the volume of stable customer balances is actually higher); therefore, the bank has to maintain a substantial liquidity cushion (approximately half of total assets) to mitigate the potential risks of outflow of customer funds.

Capital Adequacy

Although Infinbank's Tier 1 ratio of 13.61% at YE2011 complied with the regulatory minimum requirements, we note the rapid growth of the bank's business, whereby its total assets and gross loan book increased by 73% and 83%, respectively, during 2011. Despite the healthy internal capital growth capacity of 23% in 2011 (2010: 39%), this increase does not match the rapid pace of business growth; we therefore expect that regular capital injections will be required to bolster the business expansion. In April 2012, the bank benefited from a fresh capital injection amounting to UZS7 billion, thus easing pressure on capital adequacy. However, the quality of capital remains under pressure from the material level of related-party lending (approximately a quarter of Tier 1 capital) and high investments in fixed assets (another three quarters of Tier 1).

Asset Quality

In 2011, Infinbank's reported impaired loans increased by 60%, but impaired loans as a proportion of total gross loans declined to 6.8% at YE2011 from 7.8% at the beginning of that year because the volume of impaired loans grew from a low base and the loan portfolio increased rapidly. Such rapid growth is likely to generate more problem loans as the portfolio starts to mature. We also caution about the low level of loan loss reserve (LLR) accumulated by Infinbank. At YE2011, the LLR covered only 25% of impaired loans (YE2009: 29%), which, in our opinion, fails to address the pace of growth of the loan book and its potential deterioration in the future. Nor does the LLR capture Infinbank's high credit risk concentrations, with its asset quality metrics rendered vulnerable to the performance of just a handful of large borrowers.

Global Local Currency Deposit Rating (Joint Default Analysis)

Infinbank's Global Local Currency (GLC) Deposit Ratings of B3/Not Prime are based solely on its b3 standalone credit assessment.

Foreign Currency Deposit Rating

Infinbank's foreign currency deposit ratings are B3/Not Prime, in line with the bank's GLC deposit ratings.

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

InFinBank

Rating Factors [1]	A	B	C	D	E	Total Score	Trend
Qualitative Factors (70%)						E	
Factor: Franchise Value						E	Neutral
Market Share and Sustainability					x		
Geographical Diversification					x		
Earnings Stability					x		
Earnings Diversification [2]							
Factor: Risk Positioning						E	Neutral
Corporate Governance [2]					x		
- Ownership and Org. 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%)						B-	
Factor: Profitability						A	Neutral
PPI / Average RWA - Basel I	--	--	--	--	--		
Net Income / Average RWA - Basel I	--	--	--	--	--		
Factor: Liquidity						C+	Neutral
(Market funds - Liqud Assets) / Total Assets	-46.60%						
Liquidity Management				x			

Factor: Capital Adequacy						**A**	**Neutral**
Tier 1 Ratio - Basel I	18.19%						
Tangible Common Equity / RWA - Basel I	18.19%						
Factor: Efficiency						**C**	**Neutral**
Cost Income ratio			55.68%				
Factor: Asset Quality						**C**	**Neutral**
Problem Loans / Gross Loans				5.08%			
Problem Loans / (Shareholders' Equity + Loan Loss Reserves)		16.34%					
Lowest Combined Financial Factor Score (9%)						**C**	
Economic Insolvency Override						**Neutral**	
Aggregate Score						**D**	
Assigned BFSR						**E+**	

[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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