

Global Credit Research - 16 Jun 2011

Donetsk, Ukraine

Ratings

Category	Moody's Rating
Outlook	Stable
Bank Deposits -Fgn Curr	B3/NP
Bank Deposits -Dom Curr	B2/NP
NSR Bank Deposits -Dom Curr	A2.ua/--
Bank Financial Strength	E+
Bkd Senior Unsecured	B2

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Key Indicators

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

	[2]12-10	[2]12-09	[2]12-08	[2]12-07	[2]12-06	Avg.
Total Assets (UAH million)	17,705.2	15,918.1	17,789.2	11,310.3	5,278.2	[3]35.3
Total Assets (USD million)	2,222.2	1,987.3	2,317.8	2,241.2	1,045.0	[3]20.8
Tangible Common Equity (UAH million)	3,038.0	2,620.5	3,025.9	2,081.2	750.3	[3]41.9
Tangible Common Equity (USD million)	381.3	327.2	394.3	412.4	148.5	[3]26.6
PPI / Avg RWA (%)	--	--	5.6	3.3	3.3	[4]4.1
Net Income / Avg RWA (%)	--	--	0.7	1.7	1.2	[4]1.2
(Market Funds - Liquid Assets) / Total Assets (%)	4.1	23.4	31.4	23.3	7.7	[5]18.0
Core Deposits / Average Gross Loans (%)	58.8	38.9	46.1	68.8	71.5	[5]56.8
Tier 1 Ratio (%)	--	--	18.3	17.5	16.2	[4]17.3
Tangible Common Equity / RWA (%)	--	--	18.1	17.4	15.9	[4]17.1
Cost / Income Ratio (%)	45.4	36.2	38.0	48.8	52.5	[5]44.2
Problem Loans / Gross Loans (%)	34.3	40.7	15.3	3.0	1.6	[5]19.0
Problem Loans / (Equity + Loan Loss Reserves) (%)	79.3	104.7	53.7	9.8	5.2	[5]50.6

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 standalone bank financial strength rating (BFSR) of E+ to First Ukrainian International Bank (FUIB), which maps to the long-term scale of B2. The BFSR is constrained by (i) its substantial reliance on market funding, while refinancing risks were deferred until 2014 - i.e. after the conclusion of scheduled restructuring, (ii) weakening financial fundamentals, especially in terms of asset quality, as a result of challenging credit conditions in which the bank operates; and (iii) its single-name concentrations in the loan book. At the same time, the BFSR is underpinned by the bank's visibility in both corporate and retail segments within Ukraine, adequate capital adequacy - to date - as well as its relatively diversified funding.

FUIB's global local currency (GLC) deposit rating of B2 does not incorporate any probability of external support as the bank's majority shareholder SCM Group is not rated by Moody's.

Credit Strengths

- Sound franchise in servicing both large and medium-sized corporates as well as individuals

- Adequate level of capital adequacy, to date
- Healthy recurring income generation capacity

Credit Challenges

- Substantial reliance on market funding while refinancing risks were deferred till 2014 after the conclusion of scheduled restructuring
- Still challenging operating conditions which put some pressure on the bank's ability to develop the business
- High levels of single-name concentrations in the loan book
- Recovery of stressed assets is uncertain

Rating Outlook

The outlook on the bank's BFSR is stable (reflecting the fact that even if the BCA were to be lowered by one-notch the BFSR would remain the same), although the bank's long-term local currency deposit and foreign currency debt ratings carry a negative outlook, which reflects adverse credit conditions in which the bank operates.

What Could Change the Rating - Up

A combination of the following factors could have positive impact of the bank's debt and deposit ratings: (i) sustainable development of the bank's franchise; (ii) maintaining a sufficient level of capital to absorb potential credit losses; and (iii) a reduction in its borrower concentration.

In addition, FUIB's B2 debt and deposit ratings have upside potential in the near term, given the bank's intention to merge business activities with its sister bank Dongorbank (rated B2, with a negative outlook). Moody's views the consolidation of these two players as a good opportunity to build more a visible and diversified franchise in Ukraine; however, the rating agency notes that consolidation is subject to the regulator's approval and execution risk.

What Could Change the Rating - Down

Weakening of the bank's liquidity profile as well as further asset quality deterioration could exert downward pressure on the bank's BFSR and deposit ratings.

Recent Results and Company Events

As at 31 December 2010, FUIB's total audited IFRS assets were reported at US\$2.2 billion along with net income of US\$54.4 for the year then ended.

In 2010, the bank's shareholder adopted a plan to consolidate FUIB and its sister bank Dongorbank

DETAILED RATING CONSIDERATIONS

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

Bank Financial Strength Rating

Moody's assigns a BFSR of E+ to FUIB, which maps to the long-term scale of B2. The BFSR is underpinned by the bank's visibility in both corporate and retail segments within Ukraine, adequate capital adequacy - to date - as well as its relatively diversified funding. However, the bank's rating is constrained primarily by (i) its substantial reliance on market funding while refinancing risks were deferred till 2014 - i.e. after the conclusion of scheduled restructuring, (ii) weakening financial fundamentals, especially in terms of asset quality, as a result of still challenging credit conditions in which the bank operates and (iii) single-name concentrations on both sides of the balance sheet.

As a point of reference, the assigned BFSR is two notches lower than the D- outcome of Moody's bank financial strength scorecard. In our opinion, E+ rating is an adequate measure of the bank's financial strength given the issues mentioned above.

Qualitative Factors (70%)

Factor 1: Franchise Value

Trend: Neutral

FUIB is one of three banks owned by SCM Group (the other two being Donetsk-based DonGorBank, B2/E+, negative outlook, and Kiev-based Bank Renaissance Capital). FUIB is ranked 13th among Ukrainian banks in terms of total assets (2%), with consolidated market shares of 1.9% and 1.6% in corporate and retail lending, respectively, as at end-Q1 2011.

FUIB's franchise is concentrated in the eastern industrial regions of Ukraine and in Kiev. The bank is focused on corporate and SME lending, which collectively account for 70% of its loan portfolio as at YE2008. FUIB has established relationships with a number of large companies with good credit quality. Although the bank has developed its retail franchise, its contribution to net income still remains moderate. At Q1 2011, FUIB's branch network comprised 11 branches and 124 sales outlets.

Historically, the bank was oriented on servicing large and mid-sized Ukrainian corporates (loans to legal entities represents over 75% of the bank's loan book as of 1 January 2011). The bank's business line and product strategy is dependent on the success of the planned merger with its sister bank - Dongorbank.

We maintain neutral trend along with D- score for Franchise value.

Factor 2: Risk Positioning

Trend: Neutral

In Moody's view, the bank is exposed to some degree of political risk, as we see Mr. Renat Akhmetov's status as a politically connected person with possible political implications for the bank.

Although FUIB has a relatively advanced risk management system and prudent underwriting standards (which were partly inherited from FUIB's previous shareholders: including Fortis, and the European Bank for Reconstruction and Development), there are some corporate governance and risk management concerns, including the absence of independent oversight over the bank's decision-taking processes as well as some concentration issues given its high risk appetite.

FUIB's borrower concentration remains relatively high; at YE2010, the bank's top 20 exposures accounted for 130% of Tier 1 capital (YE2009: 146%) and remained quite sizeable in relation to the bank's pre-provision income (over 450% both in 2010 and in 2009).

FUIB scores E for risk positioning.

Factor 3: Regulatory Environment

For a discussion of the regulatory environment, see Moody's Banking System Outlook on Ukraine, published in December 2010.

Factor 4: Operating Environment

Trend: Neutral

This factor is common to all Ukrainian banks. Moody's assigns an E+ score for the overall operating environment. For a discussion of the operating environment, see Moody's Banking System Outlook on Ukraine, published in December 2010.

Quantitative Factors (30%)

Factor 5: Profitability

Trend: Improving

FUIB returned to profitability in 2010 and reported net income of US\$54.4 million as at YE 2010 according to audited IFRS 2010 (2009: net loss of US\$54.3 million). Over the same period, the bank's net interest margin remained almost at the same level (5.6% in 2010 and 5.8% in 2009). The bank's improved profitability with return on average assets (RoAA) of 2.6% and return on average equity (RoAE) of 13.4% was driven by the decrease of loan provisions related to expenditures as the bank made significant loan loss provision charges in 2009.

We believe that the bank's profitability will gradually improve, and we assign an improving trend to a C+ score for this factor.

Factor 6: Liquidity

Trend: Neutral

FUIB has historically been dependent on market funding. However, its average gross loan-to-average deposits ratio improved in 2010 and amounted to 197% compared to 235% in 2009. FUIB was subject to severe liquidity strains associated with recent deposit outflows, which slowed in March 2009 and demonstrated some recovery in late 2009 and early 2010. Moreover, deterioration of the operating environment, which limited the bank's ability to refinance its borrowings, has led to a weakening of the bank's liquidity position.

In December 2009, FUIB reached an agreement to restructure US\$512 million of its foreign debt (US\$275 million in Eurobonds and US\$237 million in loan facilities), with the maturity of these obligations extended to 31 December 2014. The restructuring brought significant relief to the bank's liquidity profile and postponed refinancing risks.

FUIB scores E+ for liquidity, with a neutral trend.

Factor 7: Capital Adequacy

Trend: Neutral

The bank's capital position is adequate, with a Tier 1 ratio and total Capital Adequacy Ratio of 21.9% and 26.2%, respectively, as at YE 2010 according to IFRS. The bank's capital buffer is expected to be maintained at adequate levels as the bank's current loan loss allowance adequately covers potential credit losses while recurring income generation capacity has started to recover. We also note that significant concentrations in the loan book exert pressure on the bank's capital.

The bank scores A for this factor with a neutral trend.

Factor 8: Efficiency

Trend: Neutral

The bank's efficiency was on a weakening trend in 2010, with the cost-to-income ratio and cost-to-average assets ratios of 45.4% and 3.3%, respectively (2009: 36.2% and 2.8%). This trend was explained by increased operating expenses related to personnel and merger expenses, and the decline in operating income.

The bank scores A for this factor was adjusted to B and a neutral trend was assigned.

Factor 9: Asset Quality

Trend: Neutral

FUIB's non-performing loans (NPLs, defined as overdue for more than 90 days) accounted for 22.8% of total loans as of YE2010, while 34.3%

of the bank's loan book was considered to show evidence of impairment under IFRS. The level of provisions (17.8% of total loan book), in our opinion, is sufficient to cover potential credit losses. Moody's believes that FUIB's asset quality will not deteriorate significantly as the existing problem loans have already materialised and we do not expect more loans to migrate into the problem category.

The bank scores E for this factor with a neutral trend.

Global Local Currency Deposit Rating (Joint Default Analysis)

Moody's assigns a global local currency (GLC) deposit rating of B2 to FUIB. The probability of systemic support in the event of a stress situation is judged to be none, based on the bank's insignificant national market share and relatively low importance to the country's banking system. Consequently, the bank's GLC deposit rating is at the same level as its B2 Baseline Credit Assessment.

National Scale Rating

FUIB is rated A2.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 B3 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 B2 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. AAaa 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

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]					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%)						D+	
Factor: Profitability						C+	Improving
PPI / Average RWA- Basel I	5.59%						
Net Income / Average RWA- Basel I				0.67%			
Factor: Liquidity						E+	Neutral
(Mkt funds-Liquid Assets) / Total Assets				19.63%			
Liquidity Management					x		
Factor: Capital Adequacy						A	Neutral
Tier 1 Ratio - Basel I	18.26%						
Tangible Common Equity / RWA- Basel I	18.15%						
Factor: Efficiency						A	Neutral
Cost / Income Ratio	39.88%						
Factor: Asset Quality						E	Neutral
Problem Loans / Gross Loans					30.10%		
Problem Loans / (Equity + LLR)					79.26%		
Lowest Combined Score (9%)						E	
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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