

## CREDIT OPINION

5 July 2023

Update



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### RATINGS

#### Converse Bank CJSC

Domicile	Yerevan, Armenia
Long Term CRR	Ba3
Type	LT Counterparty Risk Rating - Fgn Curr
Outlook	Not Assigned
Long Term Debt	Not Assigned
Long Term Deposit	B1
Type	LT Bank Deposits - Fgn Curr
Outlook	Stable

Please see the [ratings section](#) at the end of this report for more information. The ratings and outlook shown reflect information as of the publication date.

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## Converse Bank CJSC

Update following rating action

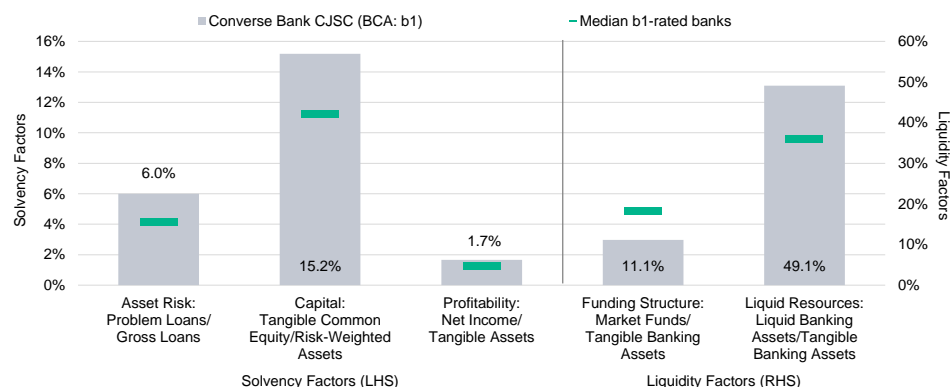
### Summary

[Converse Bank CJSC's](#) (Converse Bank) B1 deposit ratings are based on the bank's Baseline Credit Assessment (BCA) of b1. The BCA reflects its solid loss absorption capacity, stable funding profile and ample liquidity, and counterbalanced by high exposure to foreign-currency loans, and low loan loss reserve coverage of problem loans.

Our assumption of a moderate probability of support from the [Government of Armenia](#) (Ba3 stable), based on the bank's market share of around 6% in total assets, loans and retail deposits, does not result in any uplift from its b1 BCA.

Exhibit 1

#### Rating Scorecard - Key financial ratios



Note: Problem loans and profitability ratios are the weaker of the three-year averages and the latest reported figures; the capital ratio is the latest reported figure; and the funding structure and liquid assets ratios are the latest year-end figures.

Source: Moody's Investors Service

### Credit strengths

- » Robust loss-absorption capacity, underpinned by solid capital buffers and profitability
- » Strong liquidity buffer and moderate reliance on market funds
- » Moderate probability of government support in case of need

### Credit challenges

- » Low provisioning coverage of problem loans
- » High exposure to foreign-currency loans

## Outlook

The outlook on Converse bank's long-term deposit ratings is stable, reflecting our view that the bank will maintain its sound fundamentals over the next 12-18 months.

## Factors that could lead to an upgrade

- » An improvement of the asset-quality metrics, coupled with sustainable robust profitability and capital levels, may lead to an upgrade of the bank's BCA and deposit ratings in the next 12-18 months.

## Factors that could lead to a downgrade

- » Converse Bank's BCA and deposit ratings could be downgraded or the outlook on the long-term deposit ratings could be changed to negative if the bank's solvency or liquidity were to deteriorate materially or in case of remarkable deterioration of operating environment.

## Key indicators

Exhibit 2

### Converse Bank CJSC (Consolidated Financials) [1]

	12-22 <sup>2</sup>	12-21 <sup>2</sup>	12-20 <sup>2</sup>	12-19 <sup>2</sup>	12-18 <sup>2</sup>	CAGR/Avg. <sup>3</sup>
Total Assets (AMD Million)	464,136.0	377,571.8	332,436.9	325,628.5	281,119.4	13.4 <sup>4</sup>
Total Assets (USD Million)	1,179.3	786.4	636.1	678.8	581.1	19.4 <sup>4</sup>
Tangible Common Equity (AMD Million)	62,552.0	48,970.5	44,952.9	39,626.7	34,028.6	16.4 <sup>4</sup>
Tangible Common Equity (USD Million)	158.9	102.0	86.0	82.6	70.3	22.6 <sup>4</sup>
Problem Loans / Gross Loans (%)	5.1	6.7	6.2	4.3	4.2	5.3 <sup>5</sup>
Tangible Common Equity / Risk Weighted Assets (%)	15.2	14.2	13.6	13.1	11.8	13.6 <sup>6</sup>
Problem Loans / (Tangible Common Equity + Loan Loss Reserve) (%)	16.6	28.2	27.5	22.2	22.0	23.3 <sup>5</sup>
Net Interest Margin (%)	4.0	4.1	4.4	4.5	4.4	4.3 <sup>5</sup>
PPI / Average RWA (%)	5.4	2.4	3.0	2.8	2.8	3.3 <sup>6</sup>
Net Income / Tangible Assets (%)	3.1	1.1	0.8	1.7	1.7	1.7 <sup>5</sup>
Cost / Income Ratio (%)	39.6	57.9	50.6	55.0	55.5	51.7 <sup>5</sup>
Market Funds / Tangible Banking Assets (%)	11.1	15.7	15.6	14.8	16.5	14.7 <sup>5</sup>
Liquid Banking Assets / Tangible Banking Assets (%)	49.1	36.8	26.8	25.9	26.1	32.9 <sup>5</sup>
Gross Loans / Due to Customers (%)	65.2	87.6	104.6	104.0	107.2	93.7 <sup>5</sup>

[1] All figures and ratios are adjusted using Moody's standard adjustments. [2] Basel I; IFRS. [3] May include rounding differences because of the scale of reported amounts. [4] Compound annual growth rate (%) based on the periods for the latest accounting regime. [5] Simple average of periods for the latest accounting regime. [6] Simple average of Basel I periods.

Sources: Moody's Investors Service and company filings

## Profile

Converse Bank is a universal commercial bank that ranked sixth among 17 Armenian banks by assets as year-end 2022, with a consolidated asset base of AMD464 billion (\$1.2 billion). Headquartered in Yerevan, the bank operates a network of 34 branches.

Converse Bank's ultimate beneficiary shareholder is an Argentine businessman, Eduardo Eurnekian, who is Armenian by origin. He owns the holding company Corporacion America Group, which includes a conglomerate of different companies that are active in the administration and operation of airports in Latin America and Europe, and also in the agriculture, energy and infrastructure sectors. Corporacion America Airports S.A. is listed on the New York Stock Exchange since 2018.

This publication does not announce a credit rating action. For any credit ratings referenced in this publication, please see the issuer/deal page on <https://ratings.moody.com> for the most updated credit rating action information and rating history.

## Detailed credit considerations

### Improving asset quality amid ongoing economic growth

Converse Bank's problem loans (defined as Stage 3 lending<sup>1</sup>) peaked at 7.7% of gross loans in Q1 2021 and since then has improved to 5.1% as of year-end 2022. Meanwhile, the problem loan coverage increased to 51% up from 36% as of the end of 2021, but still remains noticeably lower than its regional and local peers. We assign Asset Quality score of b3 which captures expected positive trends and 1-notch downward adjustment for modest provisioning coverage and high exposure to foreign currency risk.

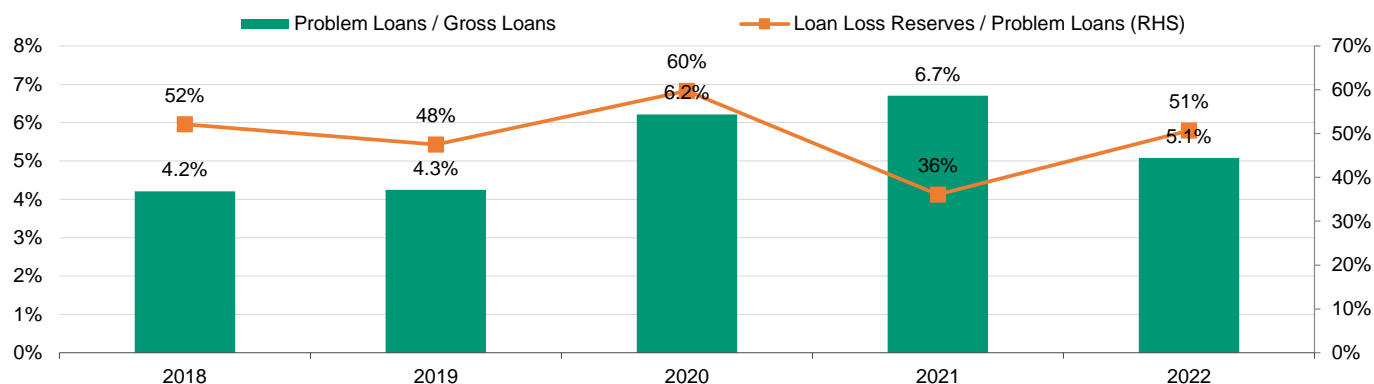
Converse Bank has a relatively diversified loan book. Retail loans accounted for 51% of total loans as of year-end 2022, while corporate loans including small and medium-sized enterprise (SME) lending accounted for the remaining 49%. The bank's net related-party exposure, a key credit consideration in the region, is insignificant as most of the loans are collateralised by cash deposits.

Converse Bank, as is the case with its domestic peers, has a large exposure to loans denominated in foreign currency, which are sensitive to exchange rate and capital flow fluctuations. About 44% of the bank's gross loans are denominated in foreign currency. While credit and currency exposures remain significant, the risks are somewhat mitigated by robust capital position. Problem loans as a percentage of tangible common equity and loan loss reserves stood at a comfortable 17% at the end of 2022 (28% as of year-end 2021).

Increase in problem loans in 2021 (see Exhibit 3), both in absolute and relative terms, was associated with lifting of regulatory forbearance measures applied during the pandemic and reclassification of a portion of restructured loans into nonperforming category. Converse Bank's problem loan (PL) ratio steadily fell to 5.1% as of year-end 2022 from 6.7% as of year-end 2021 but remained still higher than the pre-pandemic level of around 4-5%.

Exhibit 3

#### Asset quality is steadily improving



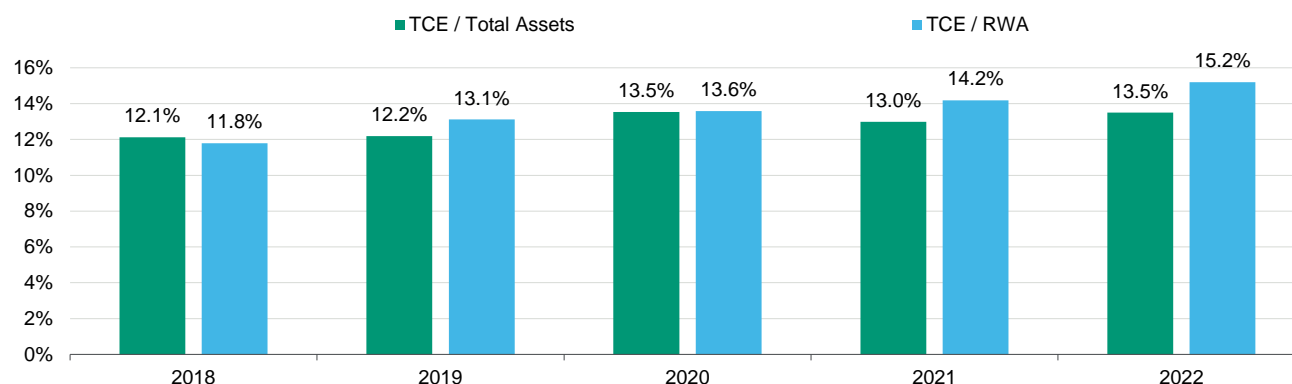
Source: Moody's Investors Service

We expect the bank will continue to work out impaired loans and write off problem loans. In our central scenario the bank's PL ratio to fall within 4-5% range in the next 12-18 months, supported by an ongoing economic growth, improved operating conditions for the borrowers along with resumed loan book expansion.

### Robust loss-absorption capacity, underpinned by solid capital buffers

Converse Bank's capital position is robust, with tangible common equity (TCE)/risk-weighted assets (RWA) ratio of 15.2% as of year-end 2022, the highest level seen since 2017 amid very high profitability posted in 2022. The bank's leverage is moderate, with shareholders' equity/total assets ratio of 13.5% as of year-end 2022. We expect Converse Bank's capital buffers to remain solid, although they can be vulnerable to unexpected losses in case of dramatic operating conditions' deterioration.

Exhibit 4

**Capital ratios are steadily improving**

Source: Moody's Investors Service

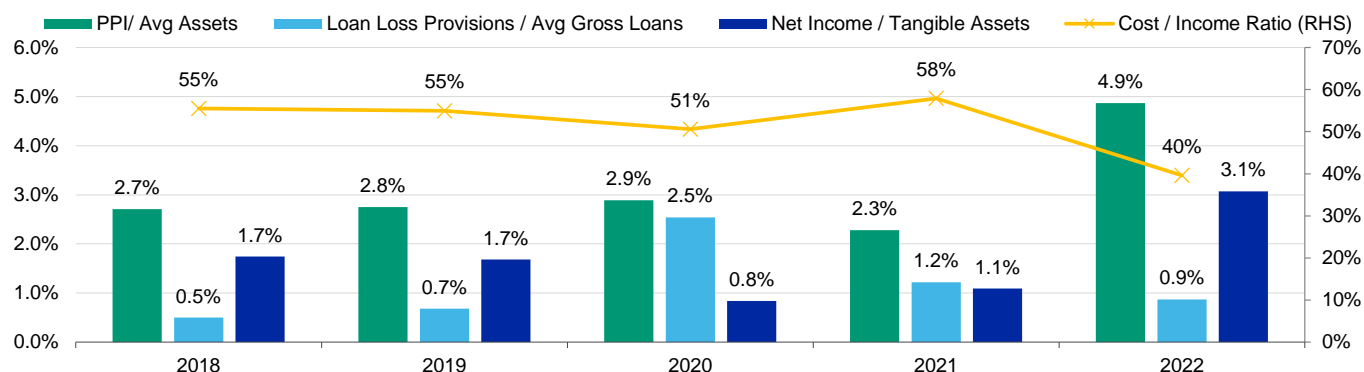
We expect that TCE ratio will fall within 14%-15% range amid likely dividend payouts and further expansion of the loan portfolio in the next 12-18 months. The bank halted dividend payments in 2020 and 2021 to better cope with the adverse operating environment, but historically paid around 15% of net income as dividends (ca. 4% in 2022).

Additional pressure on capital can stem from the depreciation of Armenian dram against US dollar. In the event of a sustained depreciation of the local currency, Converse Bank's capital metrics would be strained, given the bank's large volume of loans denominated in dollars. These loans would translate into higher RWAs, straining the capital metrics. We assign Capital Score of ba2 in line with expected trends.

**Historically stable profitability, with unprecedented foreign-exchange gains in 2022**

For the full year of 2022, Converse Bank reported a net profit of AMD14 billion, up from AMD4 billion reported in the year-earlier period. The bank's return on tangible assets was 3.0%, substantially higher than the median for b1 BCA banks. However, we do not expect such profitability to preserve in the future. In our central scenario the bank's return on tangible assets will normalise at 1.5%-1.7% in the next 12-18 months. We assign Profitability score of ba2 in line with expected trends.

Exhibit 5

**Good through-the-cycle profitability**

Source: Moody's Investors Service

Converse Bank's pre-provision income (PPI) benefits from its stable net interest margin (NIM). Through the cycle, Converse Bank reported consistent results with the NIM remaining above or at 4%, supporting the bank's net interest income.

In 2022, the bank's non-interest income benefited from material trading gains over AMD13.9 billion, or 3.0% of total assets, compared with AMD2.0 billion for the same period last year. The key drivers were high volatility of regional currencies as well as high interest rate environment in general. While we expect some arbitrage opportunities to remain, given still volatile currency environment the trading

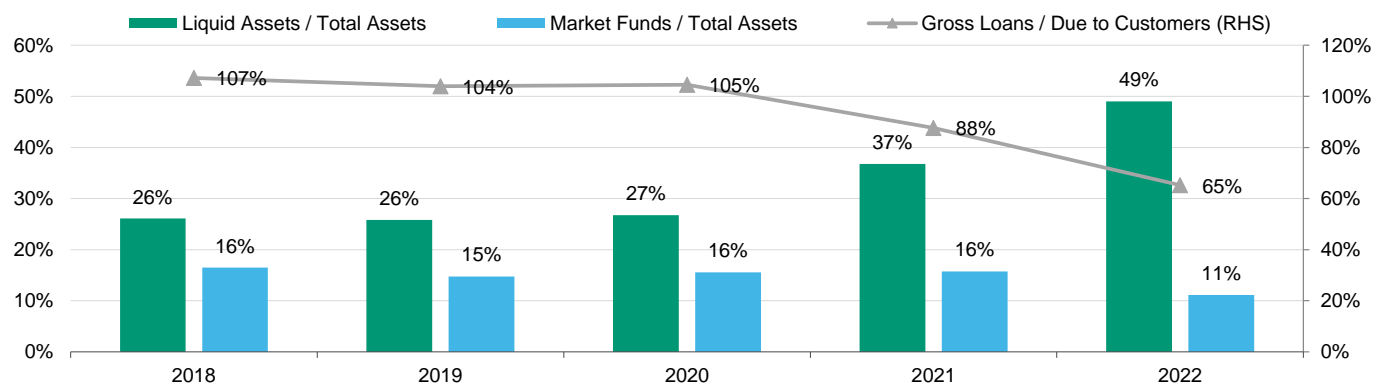
gains of the bank this year will likely be lower than in 2022. Additional pressure on the bank's net financial result could stem from higher provisioning charges amid relatively low level of problem loan coverage.

### Ample liquidity and moderate reliance on market funding

Abundant liquidity and low market funding will preserve in the next 12-18 months in our central scenario. Converse Bank's funding profile improved in 2022 from its already strong historic levels. The bank's reliance on market funding is modest, with market funds accounting for 11.1% of tangible banking assets as of year-end 2022, down from 15.8% as of year-end 2021.

Exhibit 6

#### Converse Bank's market funding is stable and liquidity is comfortable



Source: Moody's Investors Service

In 2022 the bank experienced material inflow of customer deposits which surged by 31% largely owing to non-resident customers coming from Russia. The bank conservatively allocated these funds into cash and securities instead of financing loan growth as deposit stickiness is still to be tested. We expect the bank's funding position to remain strong, but volatile depending on further cross-border capital flows, which drives our downward adjustment to funding structure score to b2.

Absent last year one-offs the bank's moderate deposit concentration supports its funding quality. As of year-end 2022, customer funds accounted for around 85% of the bank's liabilities. Large portion of the customer deposits are from retail clients, including deposits of high-net-worth individuals from the Armenian diaspora abroad. The relatively low deposit concentration provides additional funding stability. Converse Bank's liquidity provides a sufficient buffer against potential outflow, amounting to more than 40% of its tangible assets as of year-end 2022.

Our Combined Liquidity score of b1 reflects recent developments and the expected trends.

## ESG considerations

### Converse Bank CJSC's ESG Credit Impact Score is Moderately Negative CIS-3

Exhibit 7

#### ESG Credit Impact Score

# CIS-3

## Moderately Negative



For an issuer scored CIS-3 (Moderately Negative), its ESG attributes are overall considered as having a limited impact on the current rating, with greater potential for future negative impact over time. The negative influence of the overall ESG attributes on the rating is more pronounced compared to an issuer scored CIS-2.

Source: Moody's Investors Service

Converse Bank CJSC's ESG Credit Impact Score is moderately negative (**CIS-3**), reflecting the bank's governance risks related to a concentrated ownership structure. The credit impact of environmental and social risk factors on the bank's ratings is limited.

Exhibit 8

#### ESG Issuer Profile Scores



Source: Moody's Investors Service

#### Environmental

Converse Bank CJSC faces moderately negative environmental risks primarily because of its portfolio exposure to carbon transition risk. In line with its peers, the bank is facing mounting business risks to meet broader carbon transition goals. The bank's exposure to physical climate risks (primarily, heat and water stress) in Armenia is mitigated by its loan book diversification with limited exposure to the agricultural sector.

#### Social

Converse bank CJSC faces moderately negative social risks related to customer relations, tightening regulatory and compliance standards, and the impact of potential technological disruptions associated with an increasingly digitally active customer base. However, the bank is generally focused on intermediation with simpler product ranges with few identified conduct issues and has been subject to looser regulatory scrutiny on consumer protection. Demographic and societal challenges include small and aging population and risk of further military conflict between Armenia and Azerbaijan.

#### Governance

Converse Bank CJSC faces moderately negative governance risks. Main corporate governance risks arise from the concentrated ownership structure with one controlling shareholder. The bank demonstrates an appropriate level of financial strategy and has credible management and track record. Its compliance, reporting and organizational structure are in line with industry best practices and adequate for its business complexity.

ESG Issuer Profile Scores and Credit Impact Scores for the rated entity/transaction are available on Moodys.com. In order to view the latest scores, please click [here](#) to go to the landing page for the entity/transaction on MDC and view the ESG Scores section.

### Support and structural considerations

#### Government support considerations

Converse bank's long-term deposit ratings of B1 are based on the bank's BCA of b1 and Moody's assessment of a moderate probability of government support for the bank in the event of need, based on the bank's market share of around 6% in total assets, loans and retail deposits. However, this support does not provide any rating uplift to Converse bank's long-term deposit ratings.

#### Counterparty Risk (CR) Assessment

##### Converse Bank's CR Assessment is Ba3(cr)/NP(cr)

The CR Assessment is positioned one notch above the BCA of b1 and the deposit ratings of B1. This reflects our view that its probability of default is lower than that of senior unsecured debt and deposits in the absence of government support. Senior obligations represented by the CR Assessment will more likely be preserved to limit contagion, minimise losses and avoid the disruption of critical functions.

## Counterparty Risk Ratings (CRRs)

### Converse Bank's CRRs are Ba3/NP

Converse Bank's CRRs are positioned at Ba3/Not-Prime, one notch above the bank's Adjusted BCA. This reflects our view that CRR liabilities are not likely to default at the same time as the bank fails and will more likely be preserved to minimise banking system contagion, minimise losses and avoid the disruption of critical functions.

## Methodology and scorecard

### About Moody's Bank Scorecard

Our scorecard is designed to capture, express and explain in summary form our Rating Committee's judgement. When read in conjunction with our research, a fulsome presentation of our judgement is expressed. As a result, the output of our scorecard may significantly differ from that suggested by raw data alone (though it has been calibrated to avoid the frequent need for strong divergence). The scorecard 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 methodology and scorecard factors

Exhibit 9

## Converse Bank CJSC

## Macro Factors

Weighted Macro Profile	Weak	100%					
Factor	Historic Ratio	Initial Score	Expected Trend	Assigned Score	Key driver #1	Key driver #2	
Solvency							
Asset Risk							
Problem Loans / Gross Loans	6.0%	b2	↔	b3	Collateral and provisioning coverage		
Capital							
Tangible Common Equity / Risk Weighted Assets (Basel I)	15.2%	ba1	↓	ba2	Expected trend	Capital retention	
Profitability							
Net Income / Tangible Assets	1.7%	ba2	↔	ba2	Expected trend		
Combined Solvency Score		ba3		b1			
Liquidity							
Funding Structure							
Market Funds / Tangible Banking Assets	11.1%	ba3	↔	b2	Deposit quality		
Liquid Resources							
Liquid Banking Assets / Tangible Banking Assets	49.1%	ba1	↓	ba2	Expected trend		
Combined Liquidity Score		ba2		b1			
Financial Profile				b1			
Qualitative Adjustments				Adjustment			
Business Diversification				0			
Opacity and Complexity				0			
Corporate Behavior				0			
Total Qualitative Adjustments				0			
Sovereign or Affiliate constraint				Ba3			
BCA Scorecard-indicated Outcome - Range				ba3 - b2			
Assigned BCA				b1			
Affiliate Support notching				0			
Adjusted BCA				b1			

Instrument Class	Loss Given Failure notching	Additional notching	Preliminary Rating Assessment	Government Support notching	Local Currency Rating	Foreign Currency Rating
Counterparty Risk Rating	1	0	ba3	0	Ba3	Ba3
Counterparty Risk Assessment	1	0	ba3 (cr)	0	Ba3(cr)	
Deposits	0	0	b1	0	B1	B1

[1] Where dashes are shown for a particular factor (or sub-factor), the score is based on non-public information.

Source: Moody's Investors Service

## Ratings

Exhibit 10

Category	Moody's Rating
<b>CONVERSE BANK CJSC</b>	
Outlook	Stable
Counterparty Risk Rating	Ba3/NP
Bank Deposits	B1/NP
Baseline Credit Assessment	b1
Adjusted Baseline Credit Assessment	b1
Counterparty Risk Assessment	Ba3(cr)/NP(cr)

Source: Moody's Investors Service



## Endnotes

<sup>1</sup> we adjust it for unearned income on leases and reverse repo contracts

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