MOODY'S
INVESTORS SERVICE

CREDIT OPINION
17 December 2018

New Issue

Rate this Research

RATINGS

Converse Bank CJSC

Domicile	Yerevan, Armenia
Long Term CRR	B1
Type	LT Counterparty Risk Rating - Fgn Curr
Outlook	Not Assigned
Long Term Debt	Not Assigned
Long Term Deposit	B2
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

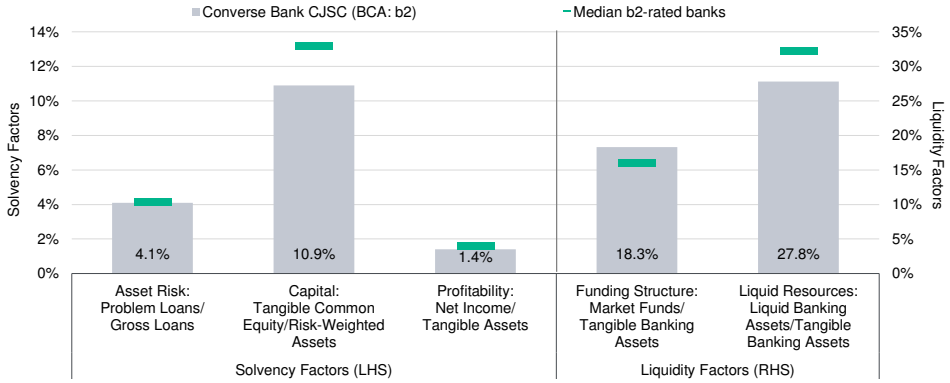
Update following rating action

Summary

We assign long-term global local- and foreign-currency deposit ratings of B2 to the Armenia-based Converse Bank CJSC (Converse Bank), which are at the same level as the bank's Baseline Credit Assessment (BCA) of b2 because moderate probability of support from the Government of Armenia (B1 positive) does not result in a rating uplift.

Converse Bank's b2 BCA reflects its (1) solid loss-absorption capacity, underpinned by its adequate capital buffer and healthy profitability; (2) adequate funding and liquidity profiles; and (3) strong financial and business support from its Argentinean shareholder. At the same time, Converse Bank's ratings are constrained by the recent rapid loan book growth, which strains its capital adequacy and could strain its asset quality upon seasoning, as well as its high foreign-currency exposure.

Exhibit 1
Rating Scorecard - Key financial ratios



Problem loans are defined as those loans that are classified as Stage 3 and corporate loans classified as Stage 2 as of the end of September 2018.
Source: Moody's Financial Metrics

Credit strengths

» Strong financial and business support from its Argentinean shareholder

» Solid loss-absorption capacity, underpinned by its adequate capital buffer and healthy profitability

» Adequate funding and liquidity profiles

» Moderate probability of government support in case of need, given the bank's solid 6% market share

Credit challenges

» Recent rapid growth of the loan book, which strains its capital adequacy and could strain its asset quality upon seasoning

» High foreign currency exposure (71% of gross loans as of 30 September 2018)

Outlook

The positive outlook on Converse Bank's long-term local-currency deposit rating is aligned with the outlook on the Armenian government's rating, after we incorporated a moderate probability of government support into the bank's ratings.

Factors that could lead to an upgrade

» Converse Bank's deposit ratings could be upgraded following an upgrade of Armenia's sovereign rating.

» Positive pressure on the bank's BCA could be exerted, if the bank sustains its good asset quality, materially reduces its foreign currency exposure and maintains solid capital and liquidity buffers.

Factors that could lead to a downgrade

» Given the positive outlook on the local-currency deposit ratings, the downside risk for Converse Bank's deposit ratings is currently limited. However, the bank's outlook could be changed to stable if the outlook on Armenia's sovereign rating is also changed to stable.

» Also, Converse Bank's BCA could be downgraded, if the bank's asset quality deteriorates and puts negative pressure on capital adequacy beyond our current expectations

Key indicators

Exhibit 2
Converse Bank CJSC (Consolidated Financials) [1]

	6-18[2]	12-17[2]	12-16[2]	12-15[2]	12-14[2]	CAGR/Avg.[3]
Total Assets (AMD million)	256,966	252,736	190,993	159,016	146,847	17.3[4]
Total Assets (USD million)	533	522	395	329	309	16.8[4]
Tangible Common Equity (AMD million)	30,987	30,397	27,320	16,974	17,925	16.9[4]
Tangible Common Equity (USD million)	64	63	56	35	38	16.4[4]
Problem Loans / Gross Loans (%)	4.0	5.0	6.2	9.1	7.3	6.3[5]
Tangible Common Equity / Risk Weighted Assets (%)	-	12.4	17.5	14.5	12.8	14.3[6]
Problem Loans / (Tangible Common Equity + Loan Loss Reserve) (%)	19.4	24.2	23.9	37.6	31.9	27.4[5]
Net Interest Margin (%)	4.3	4.3	4.2	4.4	4.5	4.3[5]
PPI / Average RWA (%)	-	2.8	2.3	2.4	2.9	2.6[6]
Net Income / Tangible Assets (%)	1.6	1.4	0.8	-0.4	1.4	1.0[5]
Cost / Income Ratio (%)	56.0	58.4	68.3	67.1	59.0	61.7[5]
Market Funds / Tangible Banking Assets (%)	15.7	13.4	4.9	10.9	12.0	11.4[5]
Liquid Banking Assets / Tangible Banking Assets (%)	29.6	30.7	32.6	41.4	29.1	32.7[5]
Gross Loans / Due to Customers (%)	102.8	97.7	88.5	78.1	101.4	93.7[5]

[1] All figures and ratios are adjusted using Moody's standard adjustments. [2] Basel I; IFRS. [3] May include rounding differences due to scale of reported amounts. [4] Compound Annual Growth Rate (%) based on time period presented for the latest accounting regime. [5] Simple average of periods presented for the latest accounting regime. [6] Simple average of Basel I periods presented.
Source: Moody's Financial Metrics

Profile

Converse Bank CJSC (Converse Bank) is a universal commercial bank that was ranked sixth by assets among 17 Armenian banks as of year-end 2017. The bank has been actively developing its retail (44% of gross loans as of 30 September 2018) and small and medium-sized enterprise banking segments (19% as of 30 September 2018). As of the first half of 2018, Converse Bank held the third-largest mortgage portfolio among local banks and was among the top five banks by retail loans.

As of end of September 2018, Converse Bank reported a consolidated asset base of AMD271 billion ($0.6 billion). Headquartered in Yerevan, the bank operates through 36 branches and offices in 11 cities in the Republic of Armenia.

Converse Bank's ultimate beneficiary shareholder is an Argentinean businessman, Eduardo Eurnekian, who is Armenian by origin. He owns the holding company Corporacion America Group, which includes a conglomeration of different companies that are active in the administration and operation of airports in Latin America and Europe, as well as in the agriculture, energy and infrastructure sectors. Corporacion America Airports S.A. launched its IPO on the New York Stock Exchange in the first quarter of 2018.

Detailed credit considerations

Strong financial and business support from the shareholder

Converse Bank benefits from financial support and business inflows because of its shareholder's connections. The shareholder provided a AMD9.5 billion ($19.6 million) capital injection to the bank in 2016, enabling it to meet new regulatory capital requirements and is committed to support the bank in the future both in terms of capital and funding, in case of need.

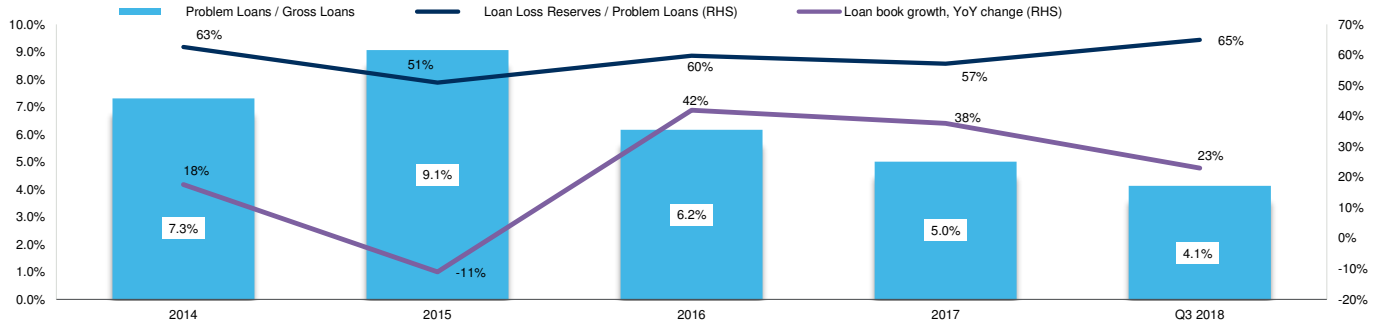
The shareholder is a net creditor to Converse Bank, given that related-party deposits exceed related-party loans. Loans to the shareholder's affiliated businesses abroad are backed by deposits and are thus risk free, but generate sound margins, supporting the bank's profitability. The bank's funding profile and commission income also benefit from servicing the suppliers of Yerevan airport, which is under the shareholder's operation.

Currently adequate asset quality might come under pressure from rapid loan growth upon seasoning

Converse Bank's asset-quality indicators are currently robust, with problem loans[1] amounting to 4.1% of gross loans as of the end of September 2018 (down from 5.0% as of year-end 2017) and 65% covered by loan-loss reserves (see Exhibit 3). An improvement in the bank's asset-quality metrics was mainly a result of write-offs in H1 2018. The introduction of IFRS9 and credit growth contributed around 0.3% to this reduction.

Exhibit 3

Converse Bank's currently robust asset quality will remain challenged by rapid credit growth; however, it will be supported by a favorable operating environment



Sources: Bank's IFRS reports, Moody's Financial Metrics

Converse Bank has a rather diversified loan book structure, with retail loans (consumer loans and mortgages) accounting for 43% of total loans and corporate loans accounting for the rest as of the end of September 2018. The top 10 gross loans accounted for 109% of equity as of the end of September 2018 and would be materially lower if adjusted for loans backed with related-party deposits (lower than 70% of equity according to our estimation). The concentration level is broadly in line with the Armenian banking sector average and somewhat lower than the Commonwealth of Independent States' (CIS) average (top 20 loans accounted for 174% of equity in Armenia and averaged 200% of equity in CIS in 2017)[2]. Net related-party exposure adjusted for cash covered deposits from the shareholder accounted for an adequate 11% of the bank's shareholders' equity as of year-end 2017.

Converse Bank's asset quality might come under pressure upon seasoning of its loan book, which has recently shown rapid growth, because of an expected slowdown in loan growth starting 2019. Converse Bank is targeting annual loan book growth of around 10% in 2019, after having grown by 23% in the 12 months ended September 2018 and by around 40% per annum in 2016-17. Although the current rebound in the Armenian economy with our forecasted GDP growth of 6% in 2018 and 5.5% in 2019 suggests benign operating conditions, we believe that the bank's recent aggressive growth trajectory poses downside risks to its asset quality in the next 12-18 months.

In addition, exposure to foreign-currency-denominated loans accounted for a high 71% of total loans as of the end of September 2018, a level that, although typical for many Armenian banks, renders the bank's asset quality vulnerable to potential foreign-exchange volatility.

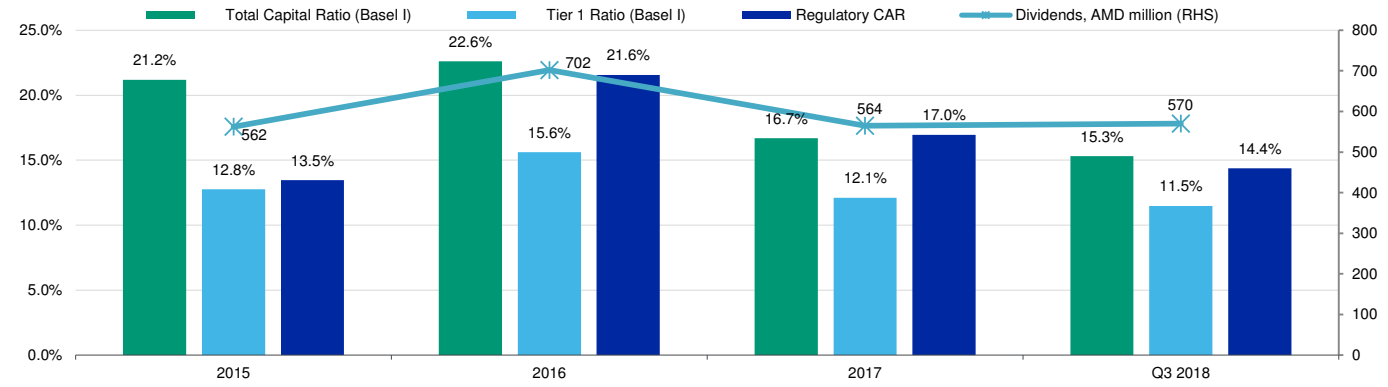
We assign Asset Risk score of b3 to Converse Bank, which reflects the balance between the current year's positive trend in asset quality and downside risks associated with the bank's recent rapid credit growth and its foreign-exchange exposure.

Capital adequacy has declined as a result of loan growth, but can be supported by the shareholder in case of need

Converse Bank's capital adequacy ratios have been on a downward trend during 2017 and in the first nine months of 2018, but they remain healthy and comfortably exceed regulatory requirements. The bank's regulatory capital adequacy ratio amounted to 14.4% as of the end of September 2018, well above the minimum required level of 12%. Its Basel I capital adequacy ratio (15.3% as of the end of September 2018) is higher than the regulatory one, which is typical of all Armenian banks because of stricter requirements of the Central Bank of Armenia in terms of provisioning and assigning risk weights to banks' assets.

Exhibit 4

Capital adequacy has declined; we expect it to stabilize in the next 12 months



Source: Bank's IFRS reports, Management data

We expect Converse Bank's capital adequacy ratios to stabilize in the next 12 months, as the bank's expected return on average equity approximately balances its planned risk-weighted asset (RWA) growth of 8%, after taking into account dividend payout (at a level similar to 2018) and management's plans for RWA optimization. These expectations are reflected in our assigned Capital score of b1.

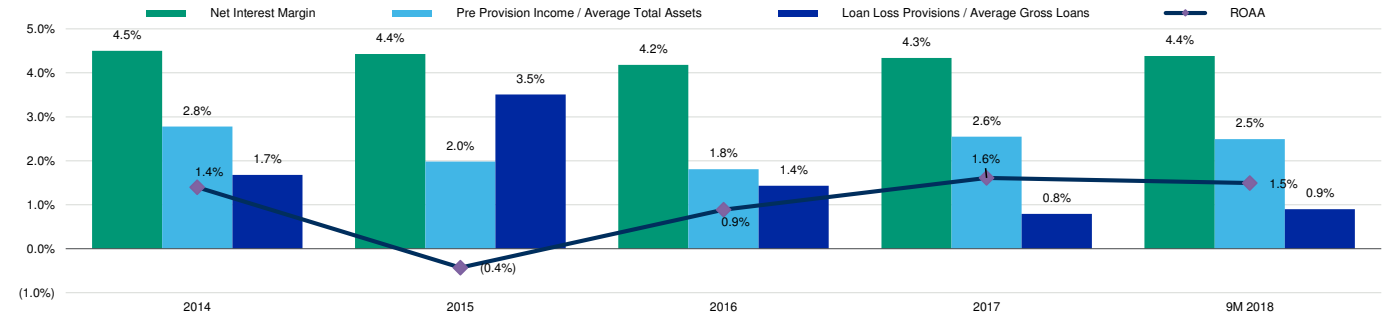
The shareholder is committed to providing capital support to Converse Bank in case of need, which underpins our view of the bank's sound loss-absorption buffer. The bank's capital adequacy was supported by a Tier 1 capital injection of AMD9.5 billion in 2016, following tightened regulatory minimum capital requirements of AMD30 billion for Armenian banks.

Sound profitability, supported by a focus on retail and small and medium-sized enterprise segments and favorable economic conditions

Converse Bank reported sound financial results for January-September 2018, underpinned by (1) a healthy recurring income (the sum of net interest income and net fee and commission income), accounting for more than 85% of the bank's revenue, and (2) a low credit cost of 0.9% (annualized). Fees and commissions are a stable revenue source, generating around 25% of the bank's pre-provision earnings, supported by the Converse Collection and Converse Transfer companies.

Exhibit 5

Converse Bank's profitability is sound



Source: Moody's Financial Metrics

We expect the bank's sound pre-provision income (at 2.5% of average assets in January-September 2018, annualized) to remain approximately stable and provide a sufficient buffer to absorb the potential increase in cost of risk. We expect the latter to exert moderate downward pressure on the bank's return on average assets in the next 12-18 months, as reflected in our adjusted Profitability score of ba3.

Adequate funding and liquidity, with moderate deposit concentrations and limited reliance on market funding

Converse Bank's reliance on market funding has recently increased and reached 18% of tangible assets by the end of September 2018, as the bank was actively issuing bonds and attracting funds from both domestic and international development institutions to fund its

lending growth. We expect this trend to continue in the next 12-18 months and forecast that Converse Bank's share of market funding will exceed 20% by the end of 2019. These expectations translate into a one-notch downward adjustment to the bank's Funding Structure score, to the level of b1.

Notwithstanding these changes, we generally view the bank's funding profile as adequate, with moderate deposit concentrations and manageable degree of market funding reliance. As of the end of September 2018, around 75% of the bank's liabilities are represented by customer accounts, almost half of which are retail deposits, including funds of high-net-worth individuals from the Armenian diaspora. Top 10 depositors accounted for 41% of customer funds as of the end of September 2018. The bank benefits from servicing the suppliers of Yerevan airport and pension inflows through post offices.

Converse Bank's liquidity provides a sufficient buffer against potential outflows, amounting to 28% of its assets as of the end of September 2018. We expect the bank's liquidity buffer to remain above 25% for the next 12-18 months, therefore we don't make any adjustment to its Liquidity Score of ba3.

Support and structural considerations

Government support

We incorporate a moderate probability of support from the Government of Armenia, to reflect the proven sustainability of the bank's recently regained market share of around 6% in total assets, loans and retail deposits. This support assumptions does not currently result in any rating uplift, given the small gap between the sovereign rating of B1 and Converse Bank's BCA of b2.

Counterparty Risk (CR) Assessment

CR Assessments are opinions of how counterparty obligations are likely to be treated if a bank fails and are distinct from debt and deposit ratings in that they (1) consider only the risk of default rather than both the likelihood of default and the expected financial loss suffered in the event of default, and (2) apply to counterparty obligations and contractual commitments rather than debt or deposit instruments. The CR assessment is an opinion of the counterparty risk related to a bank's covered bonds, contractual performance obligations (servicing), derivatives (e.g., swaps), letters of credit, guarantees and liquidity facilities.

Converse Bank's CR Assessment is positioned at B1(cr)/NP(cr)

The CR Assessment is positioned one notch above the BCA of b1 and, therefore, above senior unsecured and deposit ratings, reflecting our view that its probability of default is lower than that of senior unsecured debt and deposits. We believe senior obligations represented by the CRA will be more likely preserved in order to limit contagion, minimize losses and avoid disruption of critical function.

Counterparty Risk Rating (CRRs)

CRRs are opinions of the ability of entities to honor the uncollateralized portion of non-debt counterparty financial liabilities (CRR liabilities) and also reflect the expected financial losses in the event such liabilities are not honored. CRR liabilities typically relate to transactions with unrelated parties. Examples of CRR liabilities include the uncollateralized portion of payables arising from derivatives transactions and the uncollateralized portion of liabilities under sale and repurchase agreements. CRRs are not applicable to funding commitments or other obligations associated with covered bonds, letters of credit, guarantees, servicer and trustee obligations, and other similar obligations that arise from a bank performing its essential operating functions.

Converse Bank's CRRs are positioned at B1/NP

Converse Bank's global CRRs are positioned at B1 and Not-Prime, one notch above the bank's Adjusted BCA, reflecting our view that CRR liabilities are not likely to default at the same time as the bank fails and will more likely to be preserved to minimize banking system contagion, minimize losses and avoid disruption of critical functions.

About Moody's Bank Scorecard

Our scorecard is designed to capture, express and explain in summary form our Rating Committee's judgment. When read in conjunction with our research, a fulsome presentation of our judgment is expressed. As a result, the output of our scorecard may materially 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 6

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	6.1%	b3	← →	b3	Loan growth	Market risk
Capital						
TCE / RWA	12.9%	ba3	↓↓	b1		
Profitability						
Net Income / Tangible Assets	0.8%	b1	↓↓	ba3	Expected trend	
Combined Solvency Score		b1		b2		
Liquidity						
Funding Structure						
Market Funds / Tangible Banking Assets	13.4%	ba3	↓↓	b1	Expected trend	
Liquid Resources						
Liquid Banking Assets / Tangible Banking Assets	30.7%	ba3	↓	ba3		
Combined Liquidity Score		ba3		b1		
Financial Profile				b2		
Business Diversification				0		
Opacity and Complexity				0		
Corporate Behavior				0		
Total Qualitative Adjustments				0		
Sovereign or Affiliate constraint:				B1		
Scorecard Calculated BCA range				b1-b3		
Assigned BCA				b2		
Affiliate Support notching				0		
Adjusted BCA				b2		

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	b1	0	B1	B1
Counterparty Risk Assessment	1	0	b1 (cr)	0	B1 (cr)	--
Deposits	0	0	b2	0	B2	B2

[1] Where dashes are shown for a particular factor (or sub-factor), the score is based on non-public information.
Source: Moody's Financial Metrics

Ratings

Exhibit 7

Category	**Moody's Rating**
CONVERSE BANK CJSC	
Outlook	Positive(m)
Counterparty Risk Rating	B1/NP
Bank Deposits	B2/NP
Baseline Credit Assessment	b2
Adjusted Baseline Credit Assessment	b2
Counterparty Risk Assessment	B1(cr)/NP(cr)

Source: Moody's Investors Service

Endnotes

1 Problem loans are defined as those loans that are classified as Stage 3 and corporate loans that are classified as Stage 2 as of 30 September 2018. As of year-end 2017, problem loans included individually impaired loans and retail loans overdue by more than 90 days.

2 See Banks - Commonwealth of Independent States: Persistently high loan and deposit concentrations are credit negative ,September 2018

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Americas	1-212-553-1653
Asia Pacific	852-3551-3077
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