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CREDIT OPINION
23 October 2018

New Issue

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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

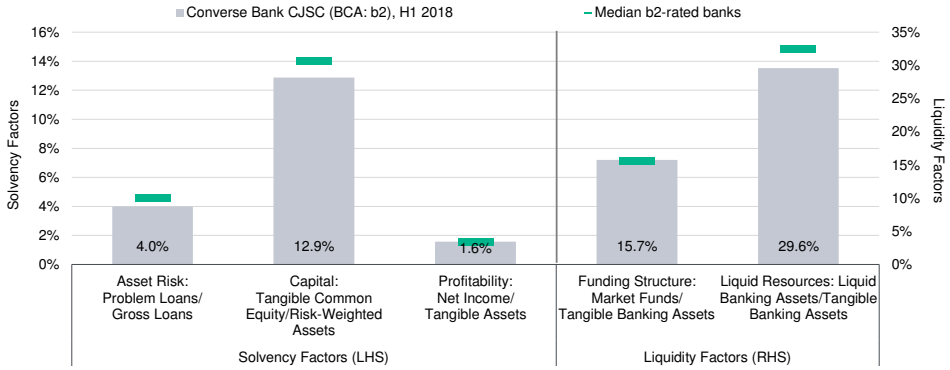
Semiannual Update

Summary

We assign long-term global local-currency 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 we do not incorporate any element of government support.

Converse Bank's b2 BCA reflects its (1) solid loss-absorption capacity, as illustrated by its high capital adequacy and sound 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 bank's rapidly growing loan book, 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 mid-2018.
Source: Moody's Financial Metrics

Credit strengths

» Strong financial and business support from the shareholder

» Solid loss-absorption capacity, as illustrated by the bank's high capital adequacy and sound profitability

» Adequate funding and liquidity profiles

Credit challenges

» Rapidly growing loan book, which strains its capital adequacy and could strain its asset quality upon seasoning

» High foreign-currency exposure

Outlook

The long-term deposit ratings carry a stable outlook, which reflects our expectation of the bank's stable performance over the next 12-18 months. The stable outlook balances the bank's adequate solvency profile and potential support from its shareholder with the asset-quality risks stemming from rapid loan growth and high foreign-currency exposure.

Factors that could lead to an upgrade

Positive rating action might be considered following:

» A further strengthening of the bank's financial profile, with demonstrated good asset quality, despite rapid loan growth

» A material decrease in the bank's foreign-currency exposure

» The maintenance of the bank's solid capital and liquidity buffers

Factors that could lead to a downgrade

Negative pressure could be exerted on Converse Bank's ratings in the case of:

» A material deterioration in the bank's asset quality

» Capital erosion

» A shortage of liquidity

This publication does not announce a credit rating action. For any credit ratings referenced in this publication, please see the ratings tab on the issuer/entity page on www.moodys.com for the most updated credit rating action information and rating history.

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 (%)	12.9	12.4	17.5	14.5	12.8	14.0[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 (%)	2.6	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 mid-2018) and small and medium-sized enterprise (SME) banking segments (16% as of year-end 2017). 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 June 2018, Converse Bank reported a consolidated asset base of AMD257 billion ($0.5 billion). Headquartered in Yerevan, the bank operates through 33 branches and offices in 11 cities in the Republic of Armenia (Government of Armenia: B1 positive).

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 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.

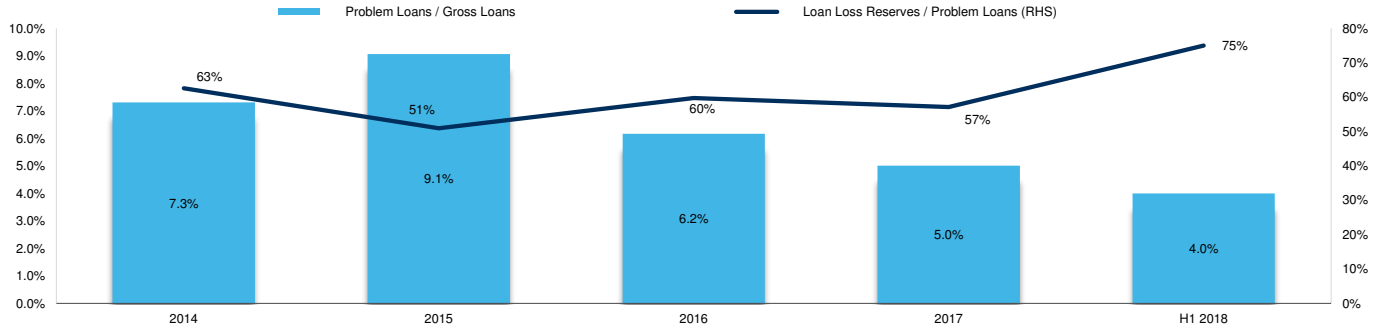
The shareholder is a net creditor to Converse Bank, given that related-party deposits exceed related-party loans. Loans to the shareholder's affiliated businesses abroad are backed by deposits and are thus risk free, but generate sound margins, supporting the bank's profitability. The bank's funding 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 4.0% of gross loans as of the end of June 2018, down from 5.0% as of year-end 2017, and adequately covered by loan-loss reserves at 75% (see Exhibit 2). An improvement in the bank's asset-quality metrics was mainly a result of write-offs in the first half of 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



Source: Bank's IFRS

Converse Bank has a rather diversified loan book structure, with retail loans (consumer loans and mortgages) accounting for 44% of total loans and corporate loans accounting for the rest as of the end of June 2018. The top 10 gross loans accounted for 109% of equity as of mid-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 the rapidly growing loan book, which should be tested by time. Converse Bank is targeting annual loan book growth of around 30% in 2018 (the growth of loans not backed by deposits was estimated at 15% in January-June 2018, higher than the reported 3% increase in gross loans) after a 38% increase in 2017, with a focus on the SME and retail segments. Although the current rebound in the Armenian economy with our forecasted GDP growth of 6% in 2018 and 5.5% in 2019 suggests better operating conditions, we view such a loan growth strategy as aggressive.

In addition, exposure to foreign-currency-denominated loans accounted for a high 77% of total loans as of year-end 2017, a level that, although it is typical for many Armenian banks, renders the bank's asset quality vulnerable to potential foreign-exchange volatility. However, we expect the bank's asset quality to remain stable in the next 12 months.

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

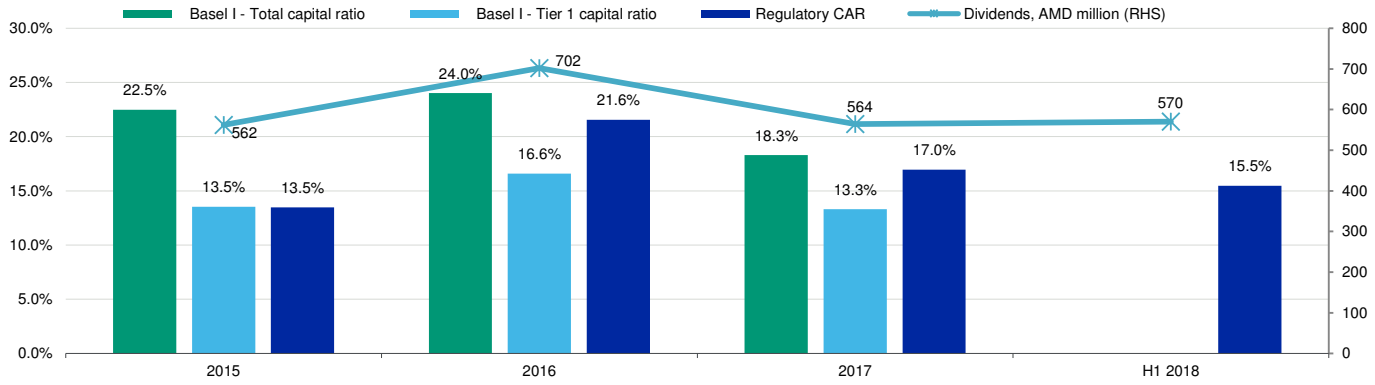
Currently high capital adequacy is decreasing amid loan growth, but can be supported by the shareholder in case of need

We expect Converse Bank's capital adequacy to continue its declining trend amid rapid credit growth, subordinated debt amortization, and dividend payouts in the next 12-18 months. The bank's regulatory capital adequacy ratio amounted to 15.5% as of mid-2018, well above the minimum required level of 12%, and was on a downward trend during 2017-H1 2018. The bank's Basel I capital adequacy ratio, which has historically stood at a higher level than the regulatory one (which is typical of all Armenian banks) because of stricter requirements of the Central Bank of Armenia in provisioning and assigning risk weights to banks' assets, is also declining. We expect a further decline in capital adequacy since the return on average equity (11% in June 2018, which doesn't include dividend payouts) is unlikely to balance the bank's loan growth expected in 2018-19.

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 recently 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.

Exhibit 4

Capital adequacy will remain on a downward trend in the next 12-18 months



Sources: Bank's IFRS reports, Management data

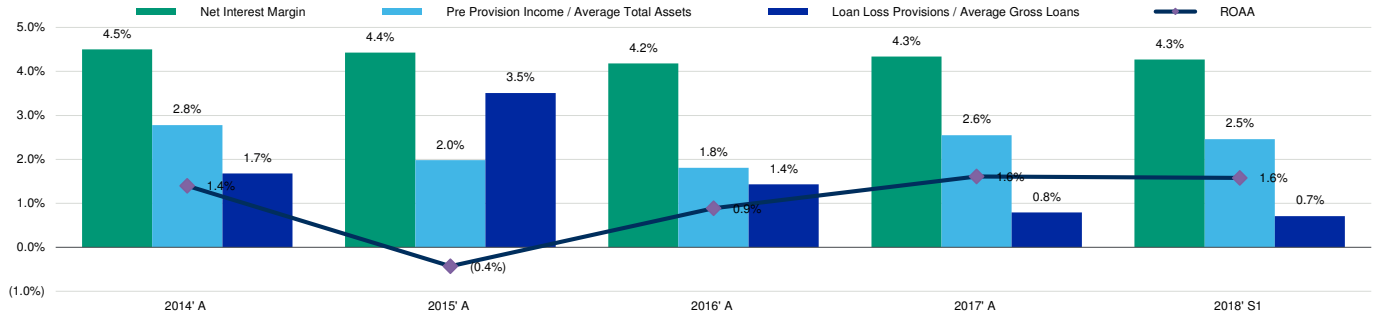
Our assigned Capital score of b1 reflects forecasted capital adequacy following loan growth and dividend payouts.

Sound profitability, supported by a focus on retail and SME segments and favorable economic conditions

Converse Bank reported sound financial results in H1 2018, underpinned by a healthy recurring income accounting for more than 80% of the bank's revenue and a low credit cost of 0.7%. Fees and commissions provide 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 sound profitability results



Source: Bank's IFRS

We expect Converse Bank's recurring profitability to strengthen further, supported by an improving net interest margin, given the focus on high-yielding products, and strong economic growth, which is 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 funding profile is adequate, with moderate deposit concentrations and low reliance on market funding of around 16% of assets as of the end of June 2018. Around 78% of the bank's liabilities are represented by customer accounts, half of which are retail deposits, including funds of high-net-worth individuals from the Armenian diaspora. Top 10 depositors accounted for 47% of customer funds as of mid-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 and amounted to 30% of assets as of the end of June 2018. We expect further lending expansion to result in a gradual depletion of the liquidity buffer and market funding growth, although at a moderate extent, and thus don't make any adjustments for the bank's Funding and Liquidity scores.

Support and structural considerations

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 CR Rating is 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.

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, 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 (for example, swaps), letters of credit, guarantees and liquidity facilities.

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

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	Expected trend	
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	← →	ba3		
Liquid Resources						
Liquid Banking Assets / Tangible Banking Assets	30.7%	ba3	← →	ba3		
Combined Liquidity Score		ba3		ba3		
Financial Profile				b1		
Business Diversification				0		
Opacity and Complexity				0		
Corporate Behavior				0		
Total Qualitative Adjustments				0		
Sovereign or Affiliate constraint:				B1		
Scorecard Calculated BCA range				ba3-b2		
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	Stable
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 mid-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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