MOODY'S INVESTORS SERVICE

Credit Opinion: Corporate Commercial Bank AD

Global Credit Research - 25 Apr 2012

Sofia, Bulgaria

Ratings

Category	**Moody's Rating**
Outlook	Stable
Bank Deposits	Ba3/NP
Bank Financial Strength	D-
Baseline Credit Assessment	(ba3)
Adjusted Baseline Credit Assessment	(ba3)

Contacts

Analyst	**Phone**
Elena Panayiotou/Limassol	357.25.586.586
Stathis A. Kyriakides, CFA/Limassol	
Yves Lemay/London	44.20.7772.5454
Ilias Avgeris/Limassol	357.25.586.586

Key Indicators

Corporate Commercial Bank AD (Consolidated Financials)[1]

	[2]**12-11**	[2]**12-10**	[2]**12-09**	[2]**12-08**	[2]**12-07**	**Avg.**
Total Assets (BGN million)	**4,044.4**	**2,702.8**	**2,041.8**	**2,106.1**	**1,771.3**	[3]**22.9**
Total Assets (EUR million)	**2,067.6**	**1,381.9**	**1,044.0**	**1,077.0**	**905.6**	[3]**22.9**
Total Assets (USD million)	**2,684.1**	**1,853.9**	**1,497.8**	**1,497.1**	**1,324.0**	[3]**19.3**
Tangible Common Equity (BGN million)	**357.5**	**297.7**	**254.7**	**190.9**	**150.7**	[3]**24.1**
Tangible Common Equity (EUR million)	**182.8**	**152.2**	**130.2**	**97.6**	**77.0**	[3]**24.1**
Tangible Common Equity (USD million)	**237.3**	**204.2**	**186.8**	**135.7**	**112.7**	[3]**20.5**
Net Interest Margin (%)	**2.4**	**3.3**	**3.3**	**2.6**	**2.8**	[4]**2.9**
PPI / Avg RWA (%)	**3.0**	**4.5**	**4.7**	**3.6**	**2.6**	[5]**3.7**
Net Income / Avg RWA (%)	**2.3**	**3.9**	**4.0**	**3.1**	**2.2**	[5]**3.1**
(Market Funds - Liquid Assets) / Total Assets (%)	**-26.5**	**-28.0**	**-21.0**	**-39.0**	**-52.7**	[4]**-33.4**
Core Deposits / Average Gross Loans (%)	**156.4**	**140.9**	**124.8**	**189.6**	**274.1**	[4]**177.2**
Tier 1 Ratio (%)	**10.5**	**11.9**	**12.6**	**11.2**	**12.0**	[5]**11.6**
Tangible Common Equity / RWA (%)	**11.8**	**14.4**	**14.7**	**12.7**	**14.2**	[5]**13.5**
Cost / Income Ratio (%)	**36.8**	**31.5**	**31.9**	**41.3**	**46.6**	[4]**37.6**
Problem Loans / Gross Loans (%)	**0.1**	**0.2**	**0.0**	**0.1**	**0.3**	[4]**0.1**
Problem Loans / (Equity + Loan Loss Reserves) (%)	**0.6**	**0.9**	**0.1**	**0.5**	**1.5**	[4]**0.7**

Source: Moody's

[1] All ratios are adjusted using Moody's standard adjustments [2] Basel II; IFRS [3] Compound Annual Growth Rate based on IFRS reporting periods [4] IFRS reporting periods have been used for average calculation [5] Basel II & IFRS reporting periods have been used for average calculation

Opinion

SUMMARY RATING RATIONALE

We assign a standalone bank financial strength rating (BFSR) of D- to Corporate Commercial Bank AD (CorpBank), which maps to ba3 on the long-term scale. The D- BFSR mainly reflects CorpBank's fast- growing franchise in Bulgaria (with a market share of around 5% of banking system assets at December 2011) and its good asset quality metrics which are superior to its peers.

CorpBank continues to report adequate profitability levels, although these have been trending downwards during the last two years; the decline in the bank's interest-rate margins in 2011 was the main factor underpinning the reduction in the bank's earnings-generating capacity. The bank has adequate capitalisation, with a Tier 1 ratio of around 10.5% at year-end 2011, although this is lower than the ratios reported by other rated Bulgarian banks.

Overall, the bank appears to be less affected by Bulgaria's economic slowdown than its peers. Nonetheless, any upward movement in its rating continues to be constrained by the elevated credit risks that it assumes by operating in Bulgaria, which currently has a high unemployment rate and a modest economic growth.

Additional factors that constrain any upward movement in the bank's ratings include (i) the large borrower concentration levels in the bank's books, which continue to account for a sizeable portion of its Tier 1, albeit to a lesser extent than before; and (ii) the large deposit concentrations in the bank's funding base to a small number of local corporates. CorpBank is 30% owned by the State General Reserve Fund (SGRF) of the Sultanate of Oman, which has two representatives on its five-member supervisory board of directors. Nonetheless, the majority of the bank's shares continue to be controlled by one local businessman, a factor that weighs negatively on the bank's risk-positioning assessment. Although Corpank is managed by a team of experienced bankers, "key-man" risk remains an issue for the bank.

CorpBank's Ba3 global local currency (GLC) is at the same level as the bank's standalone credit strength of ba3 (mapped from the D- BFSR).

Rating Drivers

- Strong asset quality metrics and good liquidity position

- Adequate, but declining profitability due to squeezed interest rate margins

- High funding and credit concentration levels (albeit to a lesser extent than before) and some corporate governance issues that weigh negatively on the bank's risk-positioning assessment

- Bulgaria's operating environment remains challenging, with a high unemployment rate and only modest economic recovery

Rating Outlook

All CorpBank's ratings carry a stable outlook.

What Could Change the Rating - Up

CorpBank's BFSR could be upgraded if it (i) further diversifies its shareholding structure and increases the number of independent members on its supervisory board; (ii) strengthens its core capital base; (iii) further eases the concentrations on both sides of its balance sheet (with top 20 loans declining below 150% of Tier 1); and (iv) expands and diversifies its funding base to include a higher level of retail deposits which are more granular.

What Could Change the Rating - Down

The BFSR could be downgraded if there is (i) a reduction in CorpBank's capitalisation; (ii) a material deterioration in its credit quality metrics; and (iii) a material weakening in its deposit franchise dynamics and overall funding base.

Recent Results and Company Events

FYE2011 results showed CorpBank's net income falling by 20% year-on-year to BGN59.8 million (EUR30.5 million), which was mainly due to a 27% drop in trading gains booked in 2011 and a 189% increase in credit costs over the same period. Return on average assets remained adequate at 1.8% during 2011, compared to 3.1% the year before.

The bank continued to report a low level of non-performing loans (NPLs), which were below 1% of loans at year-end 2011.

DETAILED RATING CONSIDERATIONS

Asset Quality

The bank maintains good asset quality metrics, which is one of its main credit strengths. NPL balances (loans 90+ days overdue) remained below 1% of total loans as the end of 2011 and were fully covered by loan loss reserves.

CorpBank has one of the lowest ratios of NPLs to total loans in the Bulgarian banking system. This reflects, to a large extent, the profile of the bank's corporate customer, as a large portion of its customers comprises prominent names in the field of energy production and infrastructure development (segments that are relatively low risky).

Nevertheless, the low NPL ratio must be viewed in the context of a rapidly expanding credit portfolio in a volatile and a still challenging operating environment. These concerns are exacerbated by CorpBank's high borrower concentration, which although well-covered by collateral, still accounts for a sizeable portion of the bank's Tier 1.

Capital Adequacy

CorpBank's Tier 1 ratio was approximately 10.5% at year-end 2011, while its total regulatory capital was approximately 12.4% at end-2011, slightly higher than the 12% regulatory minimum. The bank's capital ratios are, however, below those of its higher-rated peers in Bulgaria.

Profitability

CorpBank's net income dropped by 20% year-on-year to BGN59.8 million (EUR30.5 million) in FY 2011. Although net interest income increased by 5% during the year, non-interest income dropped by 19% due to lower trading gains booked in 2011 over the same period, putting pressure on the bank's recurring earnings. As a result, CorpBank's pre-provision income as a percentage of average assets dropped to 2.2% (compared with 3.6% during 2010), while return on average assets was approximately 1.8% at year-end 2011. Net interest rate margins also declined to 2.4% in 2011 (compared with 3.3% in 2010), a reflection of the increased competition in the market and the bank's higher than its rated peers funding costs.

CorpBank managed to grow its loan volumes by 58% during 2011, compared with annual growth of 4% for the domestic banking system. While we view positively CorpBank's ability to outpace the systemic credit growth in 2011, we have concerns regarding its credit expansion in Bulgaria's still fragile operating environment, which is characterised by high unemployment, sluggish retail trade and a depressed real estate sector. As at year-end 2011, the bank's exposure to the construction and real estate sector accounted for a sizeable 18% of its loan portfolio.

Liquidity

CorpBank has comfortable liquidity levels that underpin its BFSR. As of the end of December 2011, its ratio of net loans to customer deposits was 78%, one of the lower ratios among Bulgarian banks. At the same time, liquid assets accounted for an adequate 33% of the total balance sheet at year-end 2011.

On the funding side, CorpBank has no access to parental funding; therefore, unlike most of its peers it has traditionally relied on customer deposits to finance growth. At the end of 2011, customer deposits funded a high 84% of its total assets, a ratio that is higher than those of its foreign-owned peers. CorpBank's deposit base is highly concentrated, which increases its sensitivity to and the risks of a large deposit outflow. According to CorpBank's management, these deposits are stable and typically roll over when they mature, which partly mitigates our concerns.

Global Local Currency Deposit Rating (Joint Default Analysis)

We assign a long-term and short-term global local currency (GLC) deposit ratings of Ba3/Not-Prime to CorpBank. In accordance with Moody's Joint Default Analysis (JDA) methodology, the ratings do not incorporate any external support and are therefore at the same level as the standalone credit strength of ba3.

The introduction of the currency board in Bulgaria in 1997 has reduced the probability of systemic support. As a result, we assess a low probability of systemic support in the case of need, based on the bank's size (it ranks seventh in terms of assets, with a share of over 5% of total banking system assets).

Foreign Currency Deposit Rating

CorpBank's foreign currency deposit ratings of Ba3/Not Prime are unconstrained by Bulgaria's foreign currency deposit ceiling of Baa2.

ABOUT MOODY'S BANK RATINGS

A deposit rating, as an opinion of relative credit risk, incorporates the Bank Financial Strength Rating 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, Moody's Bank Deposit Ratings are intended to incorporate those aspects of credit risk relevant to the prospective payment performance of rated banks with respect to deposit obligations, and 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 recognise 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 Risk Assessment. In calculating the GLC rating for a bank, the JDA methodology also factors in the rating of the support provider, Moody's assessment of the probability of government support for the bank in case a stress situation occurs and the degree of dependence between the issuer rating and the systemic support indicator.

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. An 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 a high local currency ratings for certain banks, which could also produce high foreign currency ratings. Nevertheless, it should be reminded 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 obligations 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

Corporate Commercial Bank AD

Rating Factors [1]	A	B	C	D	E	Total Score	Trend
Qualitative Factors (70%)						D	
Factor: Franchise Value						E+	Improving
Market Share and Sustainability				x			
Geographical Diversification					x		
Earnings Stability					x		
Earnings Diversification [2]							
Factor: Risk Positioning						D	Neutral
Corporate Governance [2]				x			
- Ownership and Org. Complexity					x		
- Key Man Risk				x			
- Insider and Related-Party Risks							
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	--	--	--	--	--		
- Borrower Concentration	--	--	--	--	--		
- Industry Concentration	--	--	--	--	--		
Liquidity Management				x			
Market Risk Appetite	x						
Factor: Operating Environment						D	Weakening
Economic Stability					x		
Integrity and Corruption				x			
Legal System			x				
Financial Factors (30%)						B+	
Factor: Profitability						A	Weakening
PPI / Average RWA - Basel II	4.05%						
Net Income / Average RWA - Basel II	3.41%						
Factor: Liquidity						C+	Neutral
(Market funds - Liqud Assets) / Total Assets	-25.16%						
Liquidity Management				x			
Factor: Capital Adequacy						A	Neutral
Tier 1 Ratio - Basel II	11.65%						
Tangible Common Equity / RWA - Basel II	13.61%						
Factor: Efficiency						A	Neutral
Cost Income ratio	33.40%						
Factor: Asset Quality						A	Neutral
Problem Loans / Gross Loans	0.10%						
Problem Loans / (Shareholders' Equity + Loan Loss Reserves)	0.55%						
Lowest Combined Financial Factor Score (9%)						C+	
Economic Insolvency Override						Neutral	

Aggregate Score		**C-**	
Assigned BFSR		**D-**	

[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.