S&P Global
Ratings

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Alfa-Bank JSC

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Alfa-Bank JSC

SACP	bb+		+	Support	0	+	Additional Factors	0
Anchor	bb-			ALAC Support	0		Issuer Credit Rating	
Business Position	Strong	+1		GRE Support	0		BB+/Positive/B	
Capital and Earnings	Adequate	0		Group Support	0			
Risk Position	Strong	+1		Sovereign Support	0			
Funding	Average	0						
Liquidity	Adequate							

Major Rating Factors

Strengths:	Weaknesses:
• Strong market position and proven track record of sustainable earnings generation. • Efficient risk management framework. • High systemic importance for the Russian banking sector.	• Challenging operating environment in Russia, exacerbated by the COVID-19 pandemic. • Declining, but still-high, single-name concentrations in the loan book. • High level of foreign currency lending, although historically well-managed foreign currency risk.

Outlook: Positive

The positive outlooks on both ABHF and Alfa-Bank reflect S&P Global Ratings' expectation that Alfa-Bank will continue outperforming its peer group in terms of earnings generation and capital build-up over the next 12-18 months, successfully navigating through the pandemic.

Upside scenario

We may raise the ratings on Alfa-Bank if we see that the bank is able to maintain a double-digit return on equity, with asset quality metrics remaining broadly stable, and a RAC ratio sustainably exceeding 7%. Additionally, an upgrade of ABHF would depend on our view that there are no material regulatory or tax restrictions that would disrupt potential cash flows from the operating entity.

Downside scenario

We may revise the outlook to stable if, contrary to our expectations, the bank's asset quality indicators deteriorate to below-system-average levels, or its capitalization falls sharply due to unexpected provisioning needs.

Rationale

Our analysis focuses on the consolidated accounts of ABHF, the NOHC of Alfa-Bank. We refer to ABHF as the Alfa banking group, or the group, in this report. Alfa-Bank houses ABHF's banking operations in Russia, which are by far the group's largest operations and its backbone. We therefore view Alfa-Bank as a core entity of ABHF.

The ratings on Alfa-Bank incorporate our 'bb-' anchor for banks operating predominantly in Russia, as well as our view of Alfa-Bank's longstanding leading competitive position among private-sector banks in Russia in terms of assets, product lines, and efficiency. We also take into account some recovery of margins due to decreasing funding costs and better profitability metrics than privately owned domestic peers. We view positively the bank's efficient risk-management framework and absence of directed lending, as well as its very swift reaction to collateral foreclosure, which supports asset-quality management, even in downturns.

Alfa-Bank benefits from a stable funding base and sufficient liquidity coverage and has better access to capital markets than local peers. We consider Alfa-Bank to have high systemic importance in Russia and believe there is a moderately high likelihood that the Russian government would provide extraordinary support to Alfa-Bank if needed. However, this is neutral for the rating because of the too-narrow difference between the sovereign's creditworthiness and that of Alfa-Bank.

Anchor:'bb-' for a bank operating predominantly in Russia

Our bank criteria use our Banking Industry Country Risk Assessment (BICRA) economic and industry risk scores to determine a bank's anchor, the starting point in assigning an issuer credit rating. The anchor for a commercial bank operating only in Russia is 'bb-', based on an economic risk score of '8' and an industry risk score of '7'.

The COVID-19 pandemic has hit Russia's economy, as it has countries and regions across the globe. S&P Global Ratings forecasts economic growth of about 3.3% for Russia in 2021 and average growth of 2.2% for 2022-2024.

Despite positive news about progress on potentially effective vaccines, the quality of banks' loan books will continue to occupy investors' minds at least throughout 2021. Although Russian banks are performing better than we previously anticipated, in our base case we assume market conditions will remain challenging given that uncertainty regarding the progress of vaccinations and potential pandemic containment measures could continue to hamper the debt-servicing capacity of some households and private-sector businesses.

We believe Russian banks' loan books will likely demonstrate moderate growth of about 7%-10% in 2021 overall (net of foreign exchange revaluation) largely driven by mortgages in retail portfolios, while we expect still-restrained demand from corporate borrowers.

In our base case, we assume that, despite an expected economic recovery in 2021, challenging operating conditions will continue to affect the debt-servicing capacity of certain corporate, small and midsize enterprise (SME), and individual borrowers through 2021. We assume overall asset-quality deterioration, reflected in Stage 3 loans, could fall into the 10%-12% range (before write-offs) in 2021, compared with 8% at year-end 2020. We expect Russian banks' credit costs to remain elevated throughout 2021, potentially reaching 1.5%-2.0% of average lending portfolios.

We believe the share of bonds and fixed-income funds in households' financial assets will continue to increase as more conservative investors enter the market. Individuals will seek alternatives to bank deposits because of low real interest rates, new interest-income taxes, and the general attractiveness of an ever-widening range of investment opportunities and easy-to-use digital user interfaces. The trending move from savings to investments, centered around a handful of larger players, is likely continue in the next few years. In the long term, this could lead banks to convert their business models into less-capital-intensive and more-service-oriented operations. We also note that individual investors' increasing interest in corporate debt could enhance the market's depth and diversity. Debt securities issued by nonfinancial corporations accounted for modest 8.2% of GDP at year-end 2020.

Table 1

Alfa-Bank JSC--Key Figures

	--Year ended Dec. 31--				
(Mil. $)	**2020**	**2019**	**2018**	**2017**	**2016**
Adjusted assets	61,730.0	59,275.0	47,049.0	44,568.0	38,079.0
Customer loans (gross)	42,044.0	38,569.0	29,626.0	27,889.0	23,243.0
Adjusted common equity	7,628.0	6,980.0	6,100.0	5,489.0	4,822.0
Operating revenues	3,704.0	2,989.0	3,132.0	2,334.0	1,979.0
Noninterest expenses	1,282.0	1,254.0	1,170.0	1,125.0	906.0
Core earnings	1,173.3	745.9	1,380.4	851.0	568.0

Business position: The largest privately owned bank in Russia, successfully competing with government banks.

With total assets at $61.9 billion as of year-end 2020, Alfa-Bank JSC remains the largest privately owned bank in Russia and ranks No. 4 in terms of assets among Russian banks (and No.1 among privately owned banks), successfully competing with larger government-owned entities. The bank has 7.3 million active retail clients and more than 631 thousand corporate clients in Russia, and we believe that the client base is broad and relatively sticky.

In 2020, the bank continued to demonstrate good revenue generation capacity despite the COVID-19 pandemic and economic recession in Russia. The bank has reported 16% return on equity on a consolidated basis (10.7% including other comprehensive income), which is above most of its peers in Russia. We believe that Alfa Bank's good market knowledge and balanced approach to risk-taking are key factors that support its earnings sustainability. Also, over the past few years, the bank has put significant efforts into expanding its digital presence and keeping up with the latest financial technologies. We consider that Alfa Bank is one of the most advanced entities in Russia in terms of digitalization. This is also partly reflected in its efficiency ratios, with its cost-to-income ratio standing at below 37% and net fee and commission income covering operating expenses by a high 97% for 2020.

The group's management and strategy are key strengths for the bank's overall business position. Alfa-Bank's rapid and successful recovery after the downturns of the past decade, notably the efficient workout of problem loans, demonstrates its focused strategy and leads us to believe that it will continue to manage the risks arising from pressured macroeconomic conditions. The bank's ultimate owners, foremost among them Mikhail Fridman, have been with Alfa-Bank since early 1990s, and we consider them committed to banking activities in Russia.

Alfa-Bank continues to focus mainly on corporate lending. However, the bank is also increasing its retail lending portfolio quite rapidly, with a particular focus on personal instalment loans, credit, and mortgages. Retail lending represented about 27% of the loan portfolio as of year-end 2020 versus a target of 30% over the next two years. We think that expansion in retail over the previous years could contribute to the bank's future provisioning needs, putting additional pressure on profitability. However, we believe that an increase in cost of risk will be manageable given Alfa-Bank's long track record in the Russian market, as well as its cautious and balanced approach to risk taking.

Table 2

Alfa-Bank JSC--Business Position

	--Year ended Dec. 31--				
(%)	**2020**	**2019**	**2018**	**2017**	**2016**
Loan market share in country of domicile	5.1	4.5	3.8	3.8	3.3
Deposit market share in country of domicile	4.7	4.3	4.0	3.4	3.3
Total revenues from business line (currency in millions)	3,704.0	2,985.0	3,154.0	2,362.0	1,979.0
Commercial banking/total revenues from business line	50.6	57.6	47.2	59.2	58.2
Retail banking/total revenues from business line	42.8	45.6	38.3	44.3	44.0
Commercial & retail banking/total revenues from business line	93.4	103.2	85.5	103.5	102.2
Trading and sales income/total revenues from business line	(0.8)	1.5	(2.0)	(5.6)	(3.9)
Other revenues/total revenues from business line	7.5	(4.7)	16.5	2.2	1.7
Investment banking/total revenues from business line	(0.8)	1.5	(2.0)	(5.6)	(3.9)
Return on average common equity*	15.8	10.2	22.4	15.0	11.3

*Calculations based on ABHF profit for the year (not on total comprehensive income).

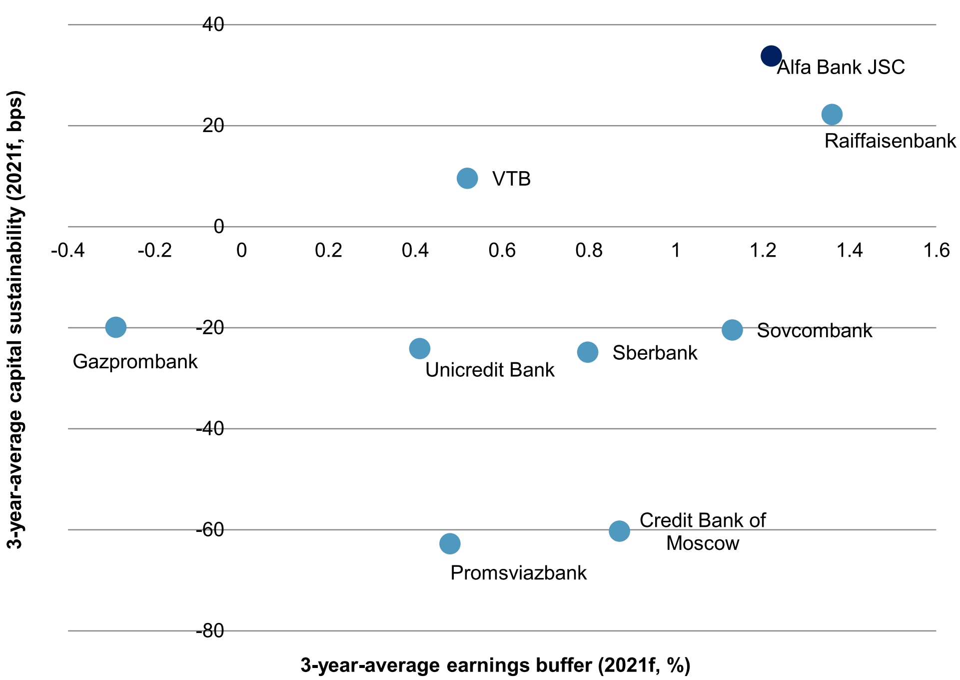
Capital and earnings: Adequate capitalization, supported by sound earning buffers

We expect that the group will continue to show positive results and that internal capital generation capacity will be sufficient to cover the growth in risk-weighted assets. Therefore, we expect the group's capitalization, measured by our RAC ratio, to stay at around 8.5%-8.7% over the next 12-18 months (versus 8.3% at year-end 2020). We expect that the bank's consolidated balance sheet will expand 6%-8% over the forecasting period. We also believe that Alfa Bank is likely to be able to retain its net interest margin at about 4%, both due to the bank's efforts to support marginal lending and recent key rate increases by Russia's central bank. We do not expect material dividends to be paid from ABH in the next 12-18 months.

The group's historical profitability metrics are better than privately owned domestic peers' and align more with those of government-owned banks and foreign subsidiaries. We expect that revenue generation capacity will remain strong in 2021-2022, with return on equity at above 10%. In our assessment of capital and earnings, we also look at earnings capacity and earnings buffers to measure the capacity for pre-provision income to cover normalized credit losses through the cycle. We expect the bank's earnings buffer to stay well above 100 bps of S&P Global Ratings' RWAs over the next two years.

Chart 1

Projected Earnings Buffer And Capital Sustainability For Alfa Bank JSC Are Better Than For Most Of Its Peers



f--Forecast. Source: S&P Global Ratings.

We understand that the shareholders are ready and capable to provide Tier 1 capital for Alfa-Bank, if needed. However, in our base case, we do not include any additional capital injections for the next two years. This is because Alfa-Bank and the larger group have sufficient capital buffers, in our view, thanks to good internal capital generation capacity.

Table 3

Alfa-Bank JSC--Capital And Earnings

	--Year ended Dec. 31--				
(%)	**2020**	**2019**	**2018**	**2017**	**2016**
Tier 1 capital ratio	16.4	16.3	17.3	15.7	16.2
S&P Global Ratings' RAC ratio before diversification	8.2	7.9	8.7	7.5	8.6
S&P Global Ratings' RAC ratio after diversification	7.9	7.3	7.9	6.7	7.5
Adjusted common equity/total adjusted capital	89.3	87.8	86.6	88.8	87.3
Net interest income/operating revenues	61.3	75.3	64.2	74.5	69.2
Fee income/operating revenues	33.5	34.9	31.2	36.2	32.0
Market-sensitive income/operating revenues	7.5	(6.2)	7.3	(9.5)	1.0
Cost to income ratio*	34.6	42.0	37.4	48.2	45.8
Preprovision operating income/average assets	4.0	3.3	4.3	2.9	3.1
Core earnings/average managed assets	1.9	1.4	3.0	2.1	1.6

RAC--Risk adjusted capital. *Calculations based on ABHF profit for the year (not on total comprehensive income).

Table 4

Alfa-Bank JSC RACF [Risk-Adjusted Capital Framework] Data

(Mil. US$)	**Exposure***	**S&P Global RWA**	**Average S&P Global RW (%)**
Credit risk			
Government & central banks	3,558	0	0
Of which regional governments and local authorities	0	0	0
Institutions and CCPs	7,548	4,540	60
Corporate	33,759	63,748	189
Retail	11,519	17,851	155
Of which mortgage	3,068	2,838	92
Securitization§	0	0	0
Other assets†	2,050	5,125	250
Total credit risk	58,434	91,265	156
Credit valuation adjustment			
Total credit valuation adjustment	--	0	--
Market Risk			
Equity in the banking book	0	0	0
Trading book market risk	--	5,540	--
Total market risk	--	5,540	--
Operational risk			
Total operational risk	--	6,945	--
(Mil. US$)	**Exposure**	**S&P Global RWA**	**% of S&P Global RWA**
Diversification adjustments			
RWA before diversification	--	103,751	100
Total Diversification/ Concentration Adjustments	--	5,087	5
RWA after diversification	--	108,837	105

Table 4

Alfa-Bank JSC RACF [Risk-Adjusted Capital Framework] Data (cont.)		
(Mil. US$)	Total adjusted capital	S&P Global RAC ratio (%)
Capital ratio		
Capital ratio before adjustments	8,546	8.2
Capital ratio after adjustments‡	8,546	7.9

*Exposure at default. §Securitization Exposure includes the securitization tranches deducted from capital in the regulatory framework. †Exposure and S&P Global Ratings' risk-weighted assets for equity in the banking book include minority equity holdings in financial institutions. ‡Adjustments to Tier 1 ratio are additional regulatory requirements (e.g. transitional floor or Pillar 2 add-ons). RWA--Risk-weighted assets. RW--Risk weight. RAC--Risk-adjusted capital. Sources: Company data as of 'Dec. 31 2020', S&P Global Ratings.

Risk position: Asset quality is stronger than the system average, although single-name concentrations remain significant in an international context

In recent years, the group proved to be more resilient than peers' to the ongoing economic problems besetting the Russian economy. We acknowledge the group's track record in navigating financial crises and consider its risk position to be strong and better than most peers'. Alfa-Bank's cost of risk is below the system average, despite COVID-19 pressures and recent fast growth in the risky retail segment. In 2020 the group's cost of risk stood at 1.72%, lower than the estimated system average of around 2.5%-3.0% and below our expectations. We expect the bank's cost of risk to remain below 2% in the next 12-18 months, and continue to compare favorably with domestic peers.

We also acknowledge the group's progress in reducing single-name concentrations, with the top-10 loans dropping to 18% of total loans as of year-end 2020. We foresee single-name concentrations remaining high in an international context, reflecting the concentrated structure of the Russian economy and the group's market position as one of the leading lenders to large Russian corporates. That said, the top-10 loans are to blue-chip Russian companies with higher-than-average credit quality. We expect the single-name portfolio concentrations to decrease slowly over the next two years, but still remain high in an international context.

We believe that the bank would be able to expand retail lending without a significant increase in cost of risk, mostly because the management team's experience and market knowledge would facilitate cautious and sustainable expansion in the segment.

We also note the group's efficient risk-management framework and absence of direct lending, as well as its very swift and proactive reaction to collateral foreclosure, which supports asset-quality management, even in downturns. While some new problems may appear on the back of the higher growth rate we anticipate, we do not expect any material problem loans will arise, and expect nonperforming loans to remain at least stable, at around 4%, with the majority of problem loans well provisioned and coverage ratio of above 80%.

About 29% of the group's loans are in foreign currencies, mostly U.S. dollars and euros, leaving the bank exposed to currency risk. However, these are matched by a 28% share of customer deposits denominated in foreign currencies. The group holds its net position in foreign currency close to zero, while foreign currency loans are extended mostly to exporting companies with foreign currency revenue and good operating performance.

Table 5

Alfa-Bank JSC--Risk Position

	--Year ended Dec. 31--				
(%)	**2020**	**2019**	**2018**	**2017**	**2016**
Growth in customer loans*	9.0	30.2	6.2	20.0	10.7
Total diversification adjustment/S&P Global Ratings' RWA before diversification	4.9	7.1	9.3	12.2	14.0
Total managed assets/adjusted common equity (x)	8.1	8.5	7.7	8.1	7.9
New loan loss provisions/average customer loans	1.7	2.0	0.9	0.2	1.2
Net charge-offs/average customer loans	0.9	1.2	0.9	1.5	3.2
Gross nonperforming assets/customer loans + other real estate owned	4.1	4.2	3.5	2.6	4.4
Loan loss reserves/gross nonperforming assets	84.5	73.3	86.6	114.2	110.5

RWA--Risk weighted assets. *Figures shown in reporting currency (USD), and do not account for foreign currency movements effect.

Funding and liquidity: The group benefits from lower funding costs than its peers

We assess funding as average and liquidity as adequate. The group's customer accounts increased by 5.5% over 2020 (20% accounting for foreign exchange movement effects), amid the decreasing cost of funding mostly stemming from low-interest rates in Russia through 2020.

In our view, the group benefits from Alfa-Bank's strong and stable retail deposit franchise. It is the third-largest Russian bank by retail deposits, with a 10% market share, after Sberbank and VTB Bank JSC. We also believe that the bank's corporate depositors have long-standing relationships with the bank, adding to funding-base stability. Over the past few years, the bank has decreased its single-name deposit concentrations, with the top-10 largest customers accounting for about 11% of core deposits as of year-end 2020.

Alfa-Bank also benefits from large volumes of cheap and stable current accounts, mainly because of its good infrastructure and client services. The bank's ratio of interest expense to average funding is 2.8%, one of the lowest among its peers, and it is one of the few banks in Russia that has historically enjoyed relatively regular access to both domestic and international bond markets. The share of wholesale funding remained stable at 17% as of year-end 2020. We also note positively that Alfa-Bank is the largest bank issuer on the market not under sectoral sanctions, and consequently benefits from access to international markets.

As of year-end 2020, the group had about 30% of its assets in liquid assets and securities eligible for repurchase transactions. Broad liquid assets amply cover short-term wholesale funding at all times, while the debt redemption schedule appears to be smooth. There are limited refinancing needs over the next year, with more than 80% of outstanding debt maturing after year-end 2021, which we consider a positive. The owners have a track record of providing liquidity to the group in times of need.

Table 6

Alfa-Bank JSC--Funding And Liquidity

	--Year ended Dec. 31--				
(%)	**2020**	**2019**	**2018**	**2017**	**2016**
Core deposits/funding base	84.7	82.9	82.7	79.9	71.0
Customer loans (net)/customer deposits	92.9	90.2	89.5	91.6	101.8
Long-term funding ratio	92.0	93.4	94.4	92.5	84.6

Table 6

Alfa-Bank JSC--Funding And Liquidity (cont.)

	--Year ended Dec. 31--				
(%)	**2020**	**2019**	**2018**	**2017**	**2016**
Stable funding ratio	120.2	126.8	131.4	127.5	119.8
Short-term wholesale funding/funding base	9.3	7.6	6.7	8.7	18.2
Broad liquid assets/short-term wholesale funding (x)	3.3	4.4	5.3	4.0	2.2
Net broad liquid assets/short-term customer deposits	65.3	60.4	61.2	58.4	54.4
Short-term wholesale funding/total wholesale funding	54.6	39.9	33.8	39.7	58.2
Narrow liquid assets/3-month wholesale funding (x)	9.0	13.0	12.8	7.6	4.1

Support: High systemic importance

We consider Alfa-Bank to have high systemic importance in Russia. We believe there is a moderately high likelihood that the Russian government would provide extraordinary support to Alfa-Bank if needed. However, we do not incorporate additional notches of support from the Russian government into the ratings on Alfa-Bank because given that the bank's stand-alone creditworthiness stands at 'bb+', the gap between the bank's and sovereign's creditworthiness is now too narrow for substantial extraordinary support that would translate into additional rating notches.

Additional rating factors:

No additional factors affect the ratings.

Environmental, Social, And Governance

We believe ESG factors, specifically governance, are a more positive influence on Alfa Bank's credit quality than on its Russian peers, although we assess governance and transparency in the Russian banking sector as relatively weak by global standards. This is one of the reasons behind our strong assessment of the bank's business position. Alfa Bank is privately owned, which insulates it more than peers from state interference. We also note its consistent and reasonable strategy, led by an experienced management team. We believe the bank's balanced approach to risk taking has led it to navigate more successfully than peers through several crises in its core markets, especially in Russia.

At the same time, we recognize that the group's legal structure is complex, with several holdings within the shareholding structure. The Alfa Banking Group (at the level of ABH Holdings S.A., Luxembourg), led by prominent Russian businessman Mikhail Friedman and several others, is the ultimate owner of the bank. We do not see unusual links between Alfa Bank and the other shareholders' businesses. Bank regulation in Russia focuses less on consumer protection than in Western Europe. Therefore, Alfa Bank appears less exposed to retail misselling or conduct risks compared with its EMEA counterparts. As with any large bank in Russia, Alfa Bank has exposure to the oil and gas and metals and mining sectors. This mirrors the structure of the Russian economy and the sectors where the largest and most creditworthy borrowers operate. Alfa Bank will not escape global trends in terms of energy transition and will likely have to gradually reduce concentrations to the most carbon-intensive industries, although we do not expect to see this happen in the near-to-medium term. We will observe how Amsterdam Trade Bank, Dutch subsidiary of Alfa Bank (74.4%) active in trade and commodities, will adjust its business model and manage the evolving environmental regulations in Western Europe, which are changing faster than in Russia.

Related Criteria

- General Criteria: Group Rating Methodology, July 1, 2019
- General Criteria: Hybrid Capital: Methodology And Assumptions, July 1, 2019
- Criteria | Financial Institutions | General: Risk-Adjusted Capital Framework Methodology, July 20, 2017
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- Criteria | Financial Institutions | Banks: Quantitative Metrics For Rating Banks Globally: Methodology And Assumptions, July 17, 2013
- Criteria | Financial Institutions | Banks: Banking Industry Country Risk Assessment Methodology And Assumptions, Nov. 9, 2011
- Criteria | Financial Institutions | Banks: Banks: Rating Methodology And Assumptions, Nov. 9, 2011
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Related Research

- Russian Banks Face A Tougher Path To Profit, Jan. 27, 2021
- Russia 'BBB-/A-3' Foreign Currency And 'BBB/A-2' Local Currency Ratings Affirmed; Outlook Stable, Jan. 15, 2021
- Banking Industry Country Risk Assessment: Russia, Nov. 16, 2020

Anchor Matrix

Industry Risk	Economic Risk									
	1	2	3	4	5	6	7	**8**	9	10
1	a	a	a-	bbb+	bbb+	bbb	-	-	-	-
2	a	a-	a-	bbb+	bbb	bbb	bbb-	-	-	-
3	a-	a-	bbb+	bbb+	bbb	bbb-	bbb-	bb+	-	-
4	bbb+	bbb+	bbb+	bbb	bbb	bbb-	bb+	bb	bb	-
5	bbb+	bbb	bbb	bbb	bbb-	bbb-	bb+	bb	bb-	b+
6	bbb	bbb	bbb-	bbb-	bbb-	bb+	bb	bb	bb-	b+
7	-	bbb-	bbb-	bb+	bb+	bb	bb	**bb-**	b+	b+
8	-	-	bb+	bb	bb	bb	bb-	bb-	b+	b
9	-	-	-	bb	bb-	bb-	b+	b+	b+	b
10	-	-	-	-	b+	b+	b+	b	b	b-

Ratings Detail (As Of May 25, 2021)*	
Alfa-Bank JSC	
Issuer Credit Rating	BB+/Positive/B
Russia National Scale	NR/--/--

Ratings Detail (As Of May 25, 2021)*(cont.)		
Issuer Credit Ratings History		
15-Apr-2021		BB+/Positive/B
27-Feb-2018		BB+/Stable/B
20-Feb-2017		BB/Positive/B
01-Jun-2016		BB/Stable/B
02-Jun-2017	*Russia National Scale*	NR/--/--
04-Feb-2015		ruAA/--/--
30-Dec-2014		ruAA+/Watch Neg/--
Sovereign Rating		
Russia		
Foreign Currency		BBB-/Stable/A-3
Local Currency		BBB/Stable/A-2
Related Entities		
ABH Financial Ltd.		
Issuer Credit Rating		BB-/Positive/B
Senior Unsecured		BB-
Alfa Holding Issuance PLC		
Senior Unsecured		BB-

*Unless otherwise noted, all ratings in this report are global scale ratings. S&P Global Ratings' credit ratings on the global scale are comparable across countries. S&P Global Ratings' credit ratings on a national scale are relative to obligors or obligations within that specific country. Issue and debt ratings could include debt guaranteed by another entity, and rated debt that an entity guarantees.