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## Fitch Affirms Interstate Bank at 'BB+'; Outlook Stable

Fitch Ratings - London - 09 Aug 2021: Fitch Ratings has affirmed Interstate Bank's (IsB) Long-Term Issuer Default Rating (IDR) at 'BB+' with a Stable Outlook. Fitch has also affirmed the bank's Short-Term IDR at 'B'.

### Key Rating Drivers

IsB's ratings are support-driven and based on the rating of the bank's key shareholder, Russia (BBB/Stable). Fitch applies a two-notch downward adjustment from Russia's sovereign rating to reflect our assessment of the propensity of the key shareholder to provide extraordinary support to the bank. The Stable Outlook mirrors that on Russia's Long-Term IDR.

Fitch applies its supranational administrative body (SAB) approach to determine IsB's ratings given the bank's unique business model as a multilateral settlement institution operating in the Commonwealth of Independent States (CIS) and Eurasian Economic Union (EAEU). The bank's shareholders are nine CIS countries, represented by their central banks: Armenia (B+/Stable, accounting for 1.8% of bank's subscribed capital), Belarus (B/Negative, 8.4%), Kazakhstan (BBB/Stable, 6.1%), Kyrgyz Republic (1.5%), Moldova (2.9%), Russia (50%), Tajikistan (1.6%), Turkmenistan (1.5%) and Ukraine (B/Positive, 20.7%).

IsB continued to see strong resilient financial performance despite negative pressures from the Covid-19 crisis. Unlike most other Fitch-rated supnationals, the bank does not extend development financing. IsB provides cash and settlement services to its clients, both in national currencies of CIS countries and in freely convertible currencies. As of end-1H21, its settlement volumes more than doubled to RUB67 billion from a year earlier, driven by a significant increase in rouble operations. The bank's internal capital generation is primarily driven by treasury operations.

The bank's equity-to-assets ratio continued to decline to 42% at end-2020, from 48% a year earlier. A 35% increase in liabilities, including deposits from banks and international organisations that are used to fund settlement operations and carry negligible rates, underpinned this decline.

Fitch expects IsB's overall business model and strategy to remain stable despite recent changes in the bank's top management. IsB continues to adhere to its renewed strategy through 2025, which envisages greater participation in integration projects and collaboration with central banks, and an increase in cross-border transactions in national currencies. The bank continued to increase its usage and promotion of national currencies as demonstrated in a recent surge in settlement operations in CIS currencies.

The bank's risk management framework is prudent outside of its inherent concentration of Russian exposures. Liquidity management considers current and projected short-term cash outflows by currencies and maturities to ensure fulfilment of the bank's obligations, payments on instructions, and funding for asset-related transactions. Liquid investment securities serve as an important buffer for the bank's demanding liquidity needs. Furthermore, IsB faces minimal foreign-exchange (FX) risk as it does not hold open FX positions except for small cash balances. The bank transacts in the FX spot market to effect settlements in non-rouble currencies and passes any cost incurred in the transaction onto the payer.

IsB's rating incorporates the key shareholder's propensity to support the bank, which we assess as 'weak'. This translates into a two-notch downward adjustment from Russia's rating. Fitch's assessment primarily reflects the ease with which shareholders can leave the bank, as illustrated by the case of Uzbekistan in 2012. Ukraine, an inactive member of the bank for some years now, formally requested to withdraw from the bank's membership in 2019. In Fitch's view, the financial settlement resulting from Ukraine's eventual departure should not materially affect the bank's capital base or operations. The notching also factors in the limited size of the bank (total assets were RUB16.8 billion at end-2020) and operations relative to the CIS economy.

## **RATING SENSITIVITIES**

The main factors that could, individually or collectively, lead to positive rating action/upgrade:

Shareholder Support (Capacity): An upgrade of the Russian sovereign rating or a revision of its Outlook to Positive.

Shareholder Support (Propensity): A positive revision to our assessment of Russia's propensity to support the bank, which may arise from increased importance of the bank in the CIS/EAEU economic framework.

The main factors that could, individually or collectively, lead to negative rating action/downgrade:

Shareholder Support (Capacity): A downgrade of the Russian sovereign rating or revision of its Outlook to Negative.

Shareholder Support (Propensity): A negative revision to our assessment of Russia's propensity to support the bank, potentially stemming from additional departures by member states from the bank.

## **Best/Worst Case Rating Scenario**

International scale credit ratings of Sovereigns, Public Finance and Infrastructure issuers have a best-case rating upgrade scenario (defined as the 99th percentile of rating transitions, measured in a positive direction) of three notches over a three-year rating horizon; and a worst-case rating downgrade scenario (defined as the 99th percentile of rating transitions, measured in a negative direction) of three notches over three years. The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Best- and worst-case scenario credit ratings are based on historical performance. For more information about the methodology used to determine

sector-specific best- and worst-case scenario credit ratings, visit <https://www.fitchratings.com/site/re/10111579>.

## Key Assumptions

- Russia continues to own at least 50% of IsB's capital.
- No significant deviation from IsB's current strategy.
- Risk-management policies remain prudent.

## REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

## Public Ratings with Credit Linkage to other ratings

IsB's ratings take into account the rating of its key shareholder, Russia, which owns 50% of the bank's capital.

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## Rating Actions

ENTITY/DEBT	RATING		RECOVERY	PRIOR
Interstate Bank	LT IDR	BB+ 	Affirmed	BB+ 
	ST IDR	B	Affirmed	B

## RATINGS KEY OUTLOOK WATCH

POSITIVE		
NEGATIVE		
EVOLVING		
STABLE		

## Applicable Criteria

[Supranationals Rating Criteria \(pub.20 May 2021\) \(including rating assumption sensitivity\)](#)

## Additional Disclosures

[Solicitation Status](#)

## Endorsement Status

Interstate Bank UK Issued, EU Endorsed

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