

Corporate Bonds

Russian Standard Bank



Sector: Financials

20 September 2007

Recommendation (6 month horizon)

Buy RUB 8.485% 2010*

* on a spread basis

Rating

Standard & Poor's: BB- (stable)

Moody's: Ba2 (stable)

Fitch: BB (stable)

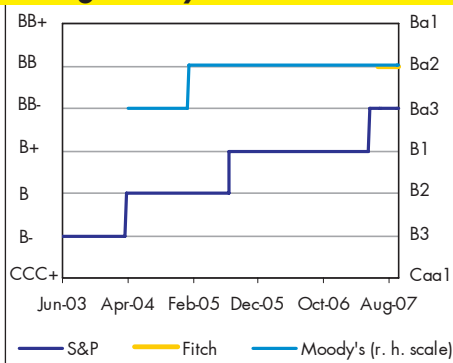
Credit picture*

Fundamental situation	+
Valuation	+
Technical picture	=
Event risk	=
News flow	-
Total	+

*+... credit positive, -... credit negative,
=... credit neutral

Source: Raiffeisen RESEARCH

Rating history



Source: Bloomberg

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Russian Standard Bank (RSB) is a leading consumer finance institution in Russia, beneficially owned by prominent entrepreneur Roustam Tariko. RSB was the first bank which targeted mass consumer business offering point-of-sale (POS) loans, then shifting its focus to car loans and credit cards. At end-H1 07, it was the 10th largest bank in terms of assets countrywide and ranked second after state-owned giant Sberbank in the retail segment.

Fundamental situation

Due to its first mover advantage in the booming consumer lending market in Russia, the bank grew rapidly and almost tripled its assets both 2004 and 2005. During H1 07 its retail portfolio grew only by 3%. In our opinion, this is mainly due to the recent changes in the product mix, as Russian Standard is substituting risky POS-loans with credit cards and is actively marketing car loans, which became the key growth driver in 1H2007. At present, RSB conducts 30% of its operations in Moscow and around. In early 2007 it acquired a small bank in the Ukraine.

Credit positive factors

Despite such tremendous growth, RSB runs a profitable business. At end-H1 07, the net interest spread stood at 40.1% and return on average equity made up 69.0%. The bank has achieved sufficient scale of operations with cost-to-income ratio of 24.1%. Given the seasoning of the loan book, the adjusted non-performing loan ratio grew over the last years and became stable at 13.7% at the end of H1 07. We would like to highlight that the specificity of the sector results in the high amount of bad loans, whereas RSB has the best asset quality among its peers. We do not expect the asset quality to deteriorate any further due to the following reasons: (i) the loan book is seasoned, (ii) the bank has accumulated sufficient default statistics to estimate future losses and (iii) has shifted its focus towards more secure products. A short-term nature of the RSB's assets results in a positive liquidity surplus of RUR 78.5 bln on 6 months horizon as of end-1H2007. Therefore, we believe RSB will comfortably cover its refinancing needs in the nearest future.

Risk factors

Although the current profitability is high, we see several factors which exercise pressure on RSB margins. According to the new legislation RSB has to cancel commissions on already granted loans. RSB's management estimates, this will cause losses of RUR 6.2-6.7 bn. Another weak point of the bank is its heavy reliance on wholesale funding. Though this year RSB has to redeem only one Eurobond issue of RUR 7.7 bln (USD 300 mln) or 3.8% of its assets, the largest part of the currently outstanding debt must be refinanced between 2008 and 2010. Obviously, new funds will be borrowed at higher prices compared to the previous issues. However, as the global risk repricing is still being in progress, the exact impact on margins remains uncertain. All in all, we do not see any immediate danger to the bank's ability to fulfil its obligations. Should the access to the capital market remain constrained for a longer period, RSB will have to revise its growth plans at least for the second half of this year.

Financial figures

in RUR mn	2005	2006	H1 06	H1 07
Total assets	112,736	192,909	150,978	203,965
Loans	98,678	163,694	129,136	171,354
Customer accounts	10,523	14,313	9,257	14,979
Net interest income before LLP	19,497	52,148	21,201	30,057
Net profit	5,863	14,547	6,575	10,200
ROAE	59.5%	78.0%	76.8%	69.0%
Net interest spread	28.4%	39.4%	24.3%	40.1%
Cost/income ratio	24.6%	22.1%	22.4%	24.1%
NPL to gross loans*	8.4%	13.8%	n/a	13.7%
Internal capital generation	59.5%	78.0%	76.8%	69.0%
Tier 1 ratio	11.3%	14.0%	n/a	n/a

* We use the most conservative estimate: non-performing loans plus loan write-offs to average portfolio. Ratios are annualised where appropriate
Source: company data, Raiffeisen RESEARCH estimates

Rating

According to the rating agencies, a positive macroeconomic situation and a booming consumer demand in Russia support the rating of RSB. Other positive impacts on rating come from the bank's established business franchise and strong profitability. The rating remains constrained by the general risks of doing business in the Russian Federation and increasing competitive pressure. Furthermore, high dependence on international capital markets is viewed negatively, though the bank's liabilities are well diversified by instruments and investor types.

Valuation and technical situation

Following the recent sell-off in the Russian corporate segment and the negative newsflow due to the investigations arranged by Russian authorities, Eurobonds of RSB substantially underperformed the market, while the spread of RUSB 7.5% 2010 to JP Morgan RUBI Bank widened by 240 bps since the beginning of the summer. RSB announced two securitisation deals, which are already structured and waiting to be placed at the market. We await further issuance in 2008.

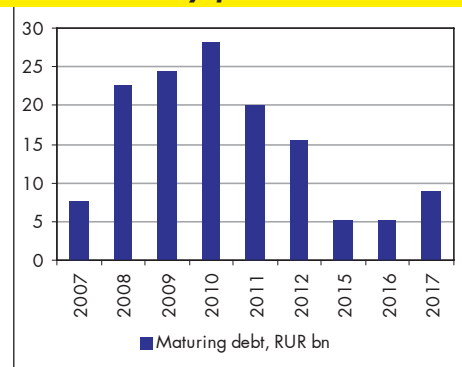
Outlook and recommendation

We think RSB has one of the most advanced and the most flexible business models in its market and is well-prepared to withstand the current turmoil. In our opinion, at the current spread levels RSB Eurobonds look cheap given the fundamental credit quality of the bank, which is supported by high historical profitability, solid asset quality, sufficient short-term liquidity, adequate capitalisation and its well-established franchise in one of the most dynamic segments of the Russian banking market. We recommend to buy RUSB 8.485% 2010 on a spread basis as it offers the best value on RSB curve.

ISIN	Name	Coupon	Maturity	Amount*	Yield	OAS**	Rating
XS0217845246	RSB	8.125	4/21/08	300	9.24%	630	Ba2/BB-
XS0267953387	RSB	6.825	9/16/09	400	10.60%	651	Ba2/BB-
XS0308286078	RSB	8.485	6/29/10	400	11.11%	745	Ba2/BB-
XS0231380774	RSB	7.500	10/7/10	500	10.85%	687	Ba2/BB-
XS0253166655	RSB	8.625	5/5/11	350	11.37%	733	Ba2/BB-
XS0238091507	RSB	8.875	12/16/15	200	11.12%	658	Ba3/B
XS0275728557	RSB	9.750	12/1/16	200	11.76%	743	Ba3/B

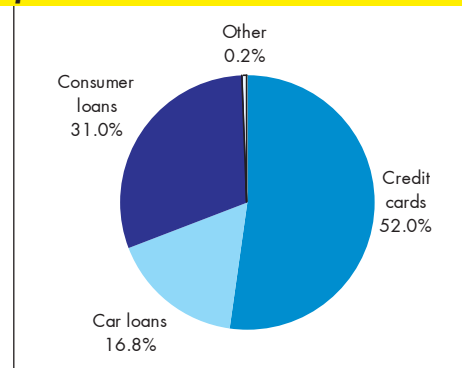
*in USD mn; ** in basis points
Source: Bloomberg

Debt maturity profile



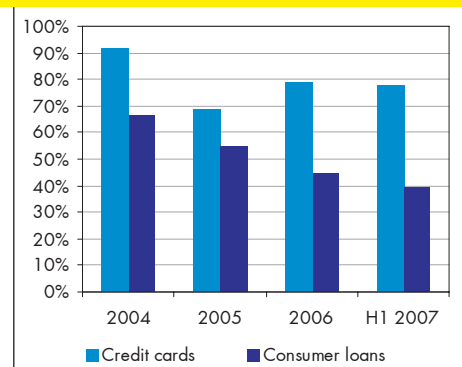
Source: company data, Cbonds.ru

Loan portfolio breakdown by products as of end H1 07



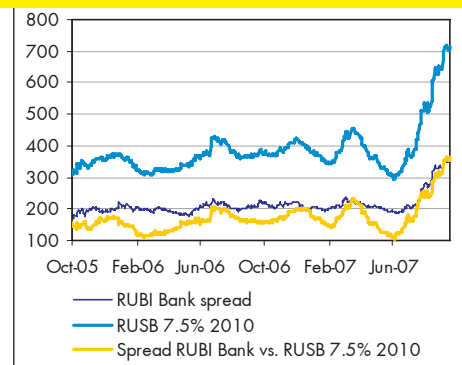
Source: company data, Raiffeisen RESEARCH

Effective rates on rouble loans



Source: company data, Raiffeisen RESEARCH

RUSB 7.5% 2010 vs. RUBI Bank



Source: JP Morgan, Bloomberg, Raiffeisen RESEARCH

Russian Standard Bank Acknowledgements

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