MOODY'S
INVESTORS SERVICE

Credit Opinion: OJSC Bank Eskhata

Global Credit Research - 23 Jul 2012

Tajikistan

Ratings

Category	**Moody's Rating**
Outlook	Stable
Bank Deposits -Fgn Curr	Caa2/NP
Bank Deposits -Dom Curr	B3/NP
Bank Financial Strength	E+
Baseline Credit Assessment	(b3)
Adjusted Baseline Credit Assessment	(b3)

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Key Indicators

OJSC Bank Eskhata (Unconsolidated Financials)[1]

	[2]**12-11**	[2]**12-10**	[2]**12-09**	[2]**12-08**	**Avg.**
Total Assets (TJS thousands)	**517**	**345**	**295**	**261**	**354**
Total Assets (USD billion)	**109**	**78**	**68**	**75**	**82**
Tangible Common Equity (TJS billion)	**50**	**39**	**30**	**34**	**38**
Tangible Common Equity (USD thousands)	**11**	**9**	**7**	**10**	**9**
Net Interest Margin (%)	**9.7%**	**7.7%**	**9.2%**	**10.2%**	**9.2%**
PPI / Avg RWA (%)	**8.97%**	**6.00%**	**--**	**--**	**7.49%**
Net Income / Avg RWA (%)	**4.54%**	**2.95%**	**--**	**--**	**3.75%**
(Market Funds - Liquid Assets) / Total Assets (%)	**15.6%**	**22.4%**	**12.3%**	**27.2%**	**19.4%**
Core Deposits / Average Gross Loans (%)	**76.6%**	**65.8%**	**68.5%**	**51.8%**	**65.7%**
Tier 1 Ratio (%)	**12.6%**	**14.1%**	**--**	**--**	**13.3%**
Tangible Common Equity / RWA (%)	**12.3%**	**13.5%**	**--**	**--**	**12.9%**
Cost / Income Ratio (%)	**66.2%**	**67.8%**	**58.5%**	**68.1%**	**65.2%**
Problem Loans / Gross Loans (%)	**4.8%**	**5.5%**	**13.7%**	**2.7%**	**6.7%**
Problem Loans / (Equity + Loan Loss Reserves) (%)	**21.7%**	**21.1%**	**49.6%**	**10.6%**	**25.7%**

Source: Moody's

[1] All ratios are adjusted using Moody's standard adjustments [2] Basel I; IFRS

Opinion

SUMMARY RATING RATIONALE

We assign a standalone bank financial strength rating (BFSR) of E+ to Tajikistan-based Bank Eskhata, mapping a standalone credit strength of b3, which reflects the (i) weak and potentially volatile operating environment in

Tajikistan; (ii) the bank's high credit risk appetite as demonstrated by recent rapid loan book growth, and (iii) a very high proportion of FX-denominated loans which increases uncertainty over the bank's asset quality.

At the same time, Eskhata's ratings are underpinned by: (i) the high granularity of its loan book, supported by the bank's focus on microfinance and retail business; (ii) good financial fundamentals including asset quality, liquidity and profitability; and (iii) currently sufficient capitalisation to absorb expected credit losses under Moody's central scenario.

Eskhata's Global Local Currency (GLC) deposit ratings of B3/Not Prime do not incorporate any element of systemic support and therefore, are based solely on its standalone credit strength. Eskhata's long-term ratings carry a stable outlook.

Rating Drivers

- Weak and potentially volatile operating environment in Tajikistan

-Good market position in servicing the microfinance sector and cash remittances

-High credit risk appetite, as demonstrated by recent rapid loan book growth and very high proportion of FX-denominated loans

- Good profitability, liquidity and asset quality

-Adequate capitalisation

Rating Outlook

All of Eskhata's long term ratings carry a stable outlook.

What Could Change the Rating - Up

An upgrade of Eskhata's ratings is unlikely in the near term, given the weak and potentially volatile operating environment in which the bank operates.

What Could Change the Rating - Down

Downward pressure could be exerted on Eskhata's ratings if economic conditions were to worsen beyond current expectations, leading to materially weaker asset-quality, impaired profitability and weaker capitalisation levels.

Recent Results and Company Events

Eskhata reported total assets of TJS562 million (US$118 million) and shareholders' equity of TJS86 million(US$18 million) - under unaudited local GAAP - as at 31 May 2012.

Eskhata reported -- as at 31 December 2011 -- total assets of TJS516.6 million (US$108.6 million), shareholders equity of TJS54.6 million (US$11.5 million) and net income of TJS15.8 million (US$3.3 million), according to its audited IFRS.

DETAILED RATING CONSIDERATIONS

Detailed considerations for Eskhata's currently assigned ratings are as follows:

Operating Environment

Eskhata's ratings are strongly dependent upon government policy and Tajikistan's operating and economic environment. Despite the acceleration of economic growth in recent years (Tajikistan GDP grew by 7.4% in 2011, and 6.5% in 2010), Tajikistan's economic conditions and the operating environment remain weak and constrained by the country's limited economic development, weak institutions and high levels of dollarisation.

Given the country's heavy dependence on remittances from expatriates working in Russia (in 2011 remittances accounted for around 50% of Tajikistan GDP), the local economy and the banking sector are highly vulnerable to external shocks - particularly to a drop in international oil prices which could affect Russia and lead to a drop in money transfers. We note that such a shock was experienced in 2009, when remittances decreased by around 30%.

Franchise

Bank Eskhata was established in Tajikistan in 1993 by the local Nasirov family. In 2005, the bank signed an equity investment agreement with the European Bank for Reconstruction and Development (EBRD) and Shore Capital - a US-based microfinance development institution (in 2010, Shore Capital sold its stake to the Nasirov family).

Eskhata's franchise development benefits from funding, technical and risk management assistance provided by the EBRD and other Western public-sector international financial institutions (IFIs). With total assets of TJS516.5 million at YE2011 (US108.5 million), Eskhata is a medium-sized bank in Tajikistan, ranking fifth by assets among the 16 banks in the system. As at YE2011, Eskhata held 7% of total assets, 10% of loans and 6.3% of retail deposits. The bank has historically focused on microfinance and retail business in Tajikistan, and has the second-largest retail portfolio in the country. At YE2011, retail and SME loans accounted for 44% and 24% of its total loan portfolio, respectively (the rest is allocated to corporate loans). The bank operates a relatively large distribution network of 15 branches and 166 operating offices. Domiciled in the city of Khudjant (north of the country)- Eskhata has historically good market positions in the northern parts of Tajikistan with smaller presence in the southern regions - which are somewhat less developed.

Eskhata has demonstrated strong lending growth over the past two years. Thanks to improving credit conditions in Tajikistan and increased demand for credit, its loan portfolio grew by 50% in 2011 and by 40% in 2010, exceeding the banking system's growth (17% in 2011). In recent years, Eskhata has become one of the leading players on the money transfer market, servicing remittance payments and accounting for 25% of all cash transfers to Tajikistan.

Risk Profile

Eskhata is majority owned by the local Nasirov family, which controls around 56% of the bank's shares. We note that the bank's corporate governance has been supported by a strong foreign shareholder, the EBRD, which control 21% of the voting shares, and is also represented on the supervisory board. The EBRD is planning to gradually exit the bank in the near future, and its stake could be purchased either by the Nasirovs or a foreign investor.

Credit risk remains the main source of risk for Eskhata, and is mainly related to the rapid lending growth. In addition, the loan book in 90%-dollarised, and a potential material weakening of the Tajik currency (the somoni) is likely to lead to a rise in level of the bank's problem loans.

As the bank has been focusing on microfinance and retail business, its single-party borrower concentration (measured as the 20 largest exposures to capital) has been satisfactory in recent years, and stood at 103% of Tier 1 capital or 22% of gross loans at Q1 2012. The bank's exposure to related-party loans is immaterial, according to its external auditor.

Profitability

In 2011, Eskhata reported a net income of TJS15.8 million, up from TJS11.8 million in 2010, which translated into a strong return on average assets (RoAA) of 3.67% and 2.63%, respectively in 2011 and 2010, according to the bank's audited IFRS report. Eskhata's strong profitability was supported by (i) growing business volumes, (ii) wide interest margins, (iii) strong fees and commissions, and (iv) stable asset quality.

The bank's healthy net interest margin of 9.7% in 2011 (2010: 7.7%) benefit from its focus on high-yielding retail and microfinance loans, and relatively cheap funding provided by IFIs.

Eskhata's profitability benefits from its strong fee-generating capacity. Its fee and commission income, mostly generated by the remittance business, remains one of the main income sources, generating around 32% of the total operating income at YE2011 (vs. 33% in 2010). FX operations are another important source of earnings for Eskhata, considering the high dollarisation of the Tajik economy and the banking system.

In our opinion, the bank's profitability will remain robust in 2012 considering currently stable credit conditions, and the growing volume of remittances.

Liquidity

Eskhata maintains an ample liquidity cushion which is necessary to support its money transfer operations. According to the IFRS report for 2011, cash and nostro accounts comprised approximately 26% of Eskhata's total assets. Eskhata non-equity liabilities represent a relatively stable and balanced funding mix between (i) interbank funding which accounted for 55% of total liabilities, and includes bilateral and subordinated loans from IFIs, and (ii) customer deposits which accounted for the remaining 45%. In recent years, Eskhata has been focusing on attracting retail deposits which grew by 85% in 2011, and accounted for around 70% of total customer funds. We note that retail deposits, while granular, represent a risk for the bank's liquidity position given the low depositor confidence in the banking system.

We currently regard Eskhata's exposure to refinancing risks as low, given the satisfactory short- to medium-term liquidity profile which is supported by the relatively long-term nature of its cross-border funding from foreign shareholder and other IFIs. We expect the bank to continue financing its lending growth with longer-term international borrowings and to continue focusing on the local deposit market in order to fund retail loans and maintain its liquidity buffer.

Asset Quality

The reported level of loans overdue for more than 90 days and restructured loans was relatively low: 1.8% and 2.6% of the gross loan portfolio, respectively, as at 31 December 2011. Provisioning coverage was maintained at 5% of gross loans, which provides sufficient problem loans coverage. We note, however, that the bank's true asset quality could be masked by the very rapid lending growth (approximately 50% per year), which we regard as a risk factor.

The bank's asset quality benefits from the high granularity of the loan portfolio and the low level of indebtedness in Tajikistan. In addition, accelerating inflows of remittances in the last two years had positive implications for the overall economy, including the SME and retail sectors. Remittances are an important source of income for most of Eskhata's clients, supporting borrowers' repayment capability, and positively affecting the overall asset quality of the bank.

In light of the currently stable operating environment, we expect asset quality to remain stable; however, we note that asset quality ratios could be further diluted if the bank maintains rapid loan-book growth, which could result in a higher level of delinquencies in a maturing loan portfolio.

The proportion of FX denominated loans has historically been high (which is common for Tajikistan), and accounted for around 90% of the bank's loan portfolio at YE2011, thus rendering asset-quality vulnerable to a potential local currency depreciation.

Capitalisation

In light of Eskhata's sufficient loan loss reserves and strong internal capital generating capacity, we regard its capitalisation as adequate, with Tier 1 and Total capital adequacy ratios at 13% and 15.6%, respectively, at 31 December 2011. This capital buffer is sufficient to absorb the bank's expected credit losses according to our central scenario. We also note that the bank is planning to increase its capital base by 25% in 2012 through the issue of new shares.

Global Local Currency Deposit Rating (Joint Default Analysis)

Moody's assigns a long-term GLC deposit rating of B3 to Eskhata.

Foreign Currency Deposit Rating

Moody's assigns Caa2/Not Prime foreign currency deposit ratings to Eskhata.

ABOUT MOODY'S BANK RATINGS

Bank Financial Strength Rating

Moody's Bank Financial Strength Ratings (BFSRs) represent Moody's opinion of a bank's intrinsic safety and soundness and, as such, exclude certain external credit risks and credit support elements that are addressed by Moody's Bank Deposit Ratings. BFSRs do not take into account the probability that the bank will receive such external support, nor do they address risks arising from sovereign actions that may interfere with a bank's ability to honor its domestic or foreign currency obligations. Factors considered in the assignment of BFSRs include bank-specific elements such as financial fundamentals, franchise value, and business and asset diversification. Although

BFSRs exclude the external factors specified above, they do take into account other risk factors in the bank's operating environment, including the strength and prospective performance of the economy, as well as the structure and relative fragility of the financial system, and the quality of banking regulation and supervision.

Global Local Currency Deposit Rating

A deposit rating, as an opinion of relative credit risk, incorporates the BFSR 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, they are intended to incorporate those aspects of credit risk relevant to the prospective payment performance of rated banks with respect to deposit obligations, which 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 recognize 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 Credit Assessment. In calculating the Global Local Currency Deposit rating for a bank, the JDA methodology also factors in the rating of the support provider, in the form of the local currency deposit ceiling for a country, Moody's assessment of the probability of systemic support for the bank in the event of a stress situation and the degree of dependence between the issuer rating and the Local Currency Deposit Ceiling.

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 high local currency ratings for certain banks, which could also produce high foreign currency ratings. Nevertheless, it should be noted 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.

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

Rating Factors

OJSC Bank Eskhata

Rating Factors [1]	**A**	**B**	**C**	**D**	**E**	**Total Score**	**Trend**
Qualitative Factors (70%)						**E**	
Factor: Franchise Value						**D+**	**Neutral**
Market Share and Sustainability			**x**				
Geographical Diversification					**x**		
Earnings Stability			**x**				
Earnings Diversification [2]							
Factor: Risk Positioning						**E**	**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				**x**			
- Borrower Concentration				x			
- Industry Concentration			x				
Liquidity Management				**x**			
Market Risk Appetite					**x**		
Factor: Operating Environment						**E**	**Neutral**
Economic Stability					**x**		
Integrity and Corruption					**x**		
Legal System					**x**		
Financial Factors (30%)						**C**	
Factor: Profitability						**A**	**Neutral**
PPI / Average RWA - Basel I	--	--	--	--	--		
Net Income / Average RWA - Basel I	--	--	--	--	--		
Factor: Liquidity						**D**	**Neutral**
(Market funds - Liqud Assets) / Total Assets				16.77%			
Liquidity Management				x			
Factor: Capital Adequacy						**A**	**Neutral**
Tier 1 Ratio - Basel I	--	--	--	--	--		
Tangible Common Equity / RWA - Basel I	--	--	--	--	--		
Factor: Efficiency						**C**	**Neutral**
Cost Income ratio			64.19%				
Factor: Asset Quality						**D**	**Neutral**
Problem Loans / Gross Loans				8.01%			
Problem Loans / (Shareholders' Equity + Loan Loss Reserves)				30.79%			
Lowest Combined Financial Factor Score (9%)						**D**	
Economic Insolvency Override						**--**	
Aggregate Score						**D-**	
Assigned BFSR							

[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.