Fitch Ratings-London/Moscow-14 December 2015: Fitch Ratings has affirmed Credit Europe Bank NV's (CEB) and its Russia-based subsidiary, Credit Europe Bank (CEBR)'s, Long-term Issuer Default Ratings (IDRs) at 'BB-'. The Outlook on CEB's IDR is Stable. The Outlook on CEBR's IDR is Negative. A full list of rating actions is available at the end of this rating action commentary.

KEY RATING DRIVERS
CEB's IDRS AND VR
CEB's Long-term IDR and Viability Rating (VR) reflect the bank's high exposure to volatile operating environments and cyclical industries inherent to its business model. They also reflect a niche but established trade finance franchise, the bank's acceptable asset quality, and sound liquidity and funding.

The Stable Outlook reflects Fitch's view that CEB's continued weak performance in Russia will be offset by its other operating markets, and over the longer term, a gradual shift towards trade finance and Turkish corporate lending. Nonetheless, CEB will remain concentrated in emerging economies, and at end-June 2015, exposures to Russia, Turkey and Romania represented 35%, 21% and 16% of its gross loan book respectively.

The quality of the Russian and Romanian exposures is weak. Russia continues to struggle with recession and Romania mortgage lending was affected by the appreciation of the Swiss franc in the beginning of 2015. The better-performing Turkish loan book and exposures to developed markets somewhat offset these pressures.

Non-performing loans (NPLs) rose to 7.7% of gross loans at end-June 2015 (5.8% at end-2014), and individual provisions are only moderate, in Fitch's view, and expose CEB's equity to fluctuations in collateral values (net NPLs equalled a significant 32% of Fitch core capital, (FCC)). CEB's sizeable portfolio of sub-standard loans (6.1% of gross loans at end-June 2015) also represents a risk for the bank.

CEB is exposed to cyclical industries, particularly construction and real estate, which made up over a quarter of corporate loans (1.2x FCC) at end-June 2015. Single-name concentration remains high, with the 20-largest borrowers accounting for almost half of corporate loans (1.8x FCC). Fitch expects the bank will maintain these large exposures under close scrutiny.

Granular deposits are CEB's main funding source, and most are collected in the Netherlands and Germany (44% of total liabilities at end-June 2015). A vast majority of deposits is covered by the Dutch deposit guarantee, which contributes to funding stability. CEB also accesses wholesale markets, particularly through its Russian subsidiary in the Russian market. Maintaining a significant liquidity buffer is key and liquid assets amounted to 16% of total assets at end-June 2015.

CEB's capitalisation strengthened in 4Q14-1Q15 following the conversion of USD126m subordinated perpetual debt into common equity, and a EUR100m equity injection from CEB's ultimate owner. The bank's consolidated common equity Tier 1 (CET1) capital ratio of 10.8% at end-June 2015 was acceptable, although remains exposed to high concentrations and unreserved NPLs.
CEB's profitability weakened in 2014-1H15, mainly as a result of shrinking asset yield in euro terms and higher loan impairment charges in Russia. Fitch expects CEB's lending in developed markets and to Turkish borrowers to be the main profit generator in 2H15 and 2016 (50% of pre-impairment profit in 1H15 and 100% of net income). The Russian business should break-even, provided loan impairment charges are contained.

CEB's SUPPORT RATING AND SUPPORT RATING FLOOR
CEB's Support Rating of '5' and Support Rating Floor of 'No Floor' reflect Fitch's view that support from the Dutch state cannot be relied upon. This reflects the bank's lack of systemic importance in the Netherlands, as well as legislative, regulatory and policy initiatives (including the implementation of the Bank Recovery and Resolution Directive (BRRD)) that have substantially reduced the likelihood of sovereign support for EU commercial banks in general.

Similarly, support from the bank's private shareholder, although possible, cannot be reliably assessed.

CEBR'S IDRS, VR, SENIOR DEBT, NATIONAL RATING AND SUPPORT RATING
The affirmation of CEBR's Long-term IDR and VR reflects only moderate pressure on the bank's capital to date, driven by a rise in funding cost and high impairment charges, and Fitch's view that despite a tight liquidity position, the bank's refinancing risks should be manageable. Indirect liquidity support CEBR has received from the parent bank in 2014-2015 is also credit-positive. The Negative Outlook on the bank's IDR reflects Fitch's view that CEBR's asset quality may deteriorate further, pressured by sluggish economic growth, weaker consumption and investment, and a drop of household real disposable income.

Asset quality deterioration has been only moderate to date, as reflected in an annualised 8% non-performing loans origination rate (defined as the increase in NPLs over the period plus write-offs, divided by average performing loans) in 1H15; up from 7% in 2014. The bank's corporate loan book remains highly concentrated (top 20 borrowers accounted for 1.7x of end-1H15 FCC) and is significantly dollarised (around 80% of total), while most borrowers have limited access to USD-denominated revenue. However, collateral valuation in most cases is reasonable, moderately mitigating credit risks. Also, CEBR is about to sell all Turkey-related corporate exposures to other group entities due to negative tensions against Turkey in Russia.

Russian retail borrowers have been burdened by the weaker economic environment, leading to higher consumer indebtedness, by a rise in inflation and unemployment rates, and a drop in real disposable incomes. Credit losses in the retail loan book widened to 10.8% in 1H15 (annualised) from 7.3% in 2014. However, secured products (car loans and mortgages, 42% of total retail book at end-1H15) have fairly high recovery rates and should reduce the magnitude of losses. Nonetheless, medium-term performance will largely depend on the broader state of the economy.

CEBR's refinancing risks are high in light of large potential repayments in 2016 (RUB34bn, including RUB18bn of put options, or 27% of liabilities at end-November 2015). Only 40% of these redemptions are covered by liquid assets. Fitch believes that CEBR may refinance at least some of this wholesale debt. Furthermore, CEBR has some deleveraging capacity and may also sell some corporate loans to other companies within the wider group, which should help the bank to preserve liquidity. In addition, a pre-committed credit line from the parent of EUR120m is available in case of need, according to management.

The bank's capitalisation is reasonable, although pressured by negative net income in 1H15 and revaluation of FX-denominated assets. Despite potentially weaker asset quality translating into limited internal capital generation capacity, Fitch does not expect the bank's capital ratios to decline significantly in 2016 due to limited planned loan growth.
CEBR's senior unsecured debt is rated in line with the bank's Long-term IDR.

CEBR's Support Rating of '4' reflects the limited probability of support from CEB, in case of need. This view is based on (i) CEB's somewhat constrained ability to provide capital support, given CEBR's large size (around 25% of group's assets at end-2014); and (ii) increasing uncertainty over the longer-term business prospects for the Russian market.

CEB'S AND CEBR'S SUBORDINATED DEBT
CEB's and CEBR's dated subordinated debt is rated one notch below the banks' respective VRs, reflecting below-average recovery prospects of this type of debt.

RATING SENSITIVITIES
CEB's IDRS, VR, SUPPORT RATING, SUPPORT RATING FLOOR AND SUBORDINATED DEBT
Upside potential for CEB's Long-term IDR and VR is currently limited although a stabilisation of the Russian operating environment would be credit-positive. Ratings could be downgraded in case of further asset quality deterioration, which in Fitch's view would be most likely to occur in the Russian portfolio, leading to a material erosion of CEB's capitalisation.

An upgrade of the Support Rating and upward revision of the Support Rating Floor would be contingent on a positive change in the Netherlands' propensity to support its banks. While not impossible, this is highly unlikely in Fitch's view.

Subordinated debt rating is likely to move in tandem with CEB's VR.

CEBR's IDRs, VR, NATIONAL RATING, SUPPORT RATING AND DEBT RATINGS
CEBR's Long-term IDR and VR could be downgraded if the weaker operating environment translates into further deterioration of the bank's asset quality and significant erosion of capital; or prospects for Russia's economy and macroeconomic stability continue to deteriorate significantly. Upside potential is currently limited, but stabilisation of the operating environment would be credit-positive.

CEBR's Support Rating is sensitive to CEB's ratings (and hence, its ability to provide support) and any marked changes in the group's strategic commitment to the Russian market.

CEBR's senior and subordinated debt ratings are sensitive to changes in the bank's Long-term IDR and VR respectively.

The rating actions are as follows:

Credit Europe Bank NV
Long-term IDR: affirmed at 'BB-', Outlook Stable
Short-term IDR: affirmed at 'B'
Viability Rating: affirmed at 'bb-
Support Rating: affirmed at '5'
Support Rating Floor: affirmed at 'No Floor'
Subordinated debt: affirmed at 'B+'

Credit Europe Bank
Long-term IDR: affirmed at 'BB-', Outlook Negative
Short-term IDR: affirmed at 'B'
National Long-term rating: affirmed at 'A+(rus)', Outlook Negative
Viability Rating: affirmed at 'bb-'
Support Rating: affirmed at '4'
Senior unsecured debt: affirmed at 'BB-/A+(rus)'
Subordinated debt (issued by CEB Capital SA): affirmed at 'B+'

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Applicable Criteria
Global Bank Rating Criteria (pub. 20 Mar 2015)

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