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Analysts Say There's No Avoiding VTB Share Issue

By The Moscow Times

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Propping up VTB's capital adequacy ratio with Russia's first perpetual bond issue is not enough, experts say. **Vladimir Filonov**

VTB will likely still need to resort to a share issue to boost its capital reserves, analysts said Friday, after the bank hailed an unusually-structured bond issue as offering a vital repair to its capital levels.

VTB needs to bolster its finances to keep up its strong lending growth, after its ill-fated takeover of Bank of Moscow last year knocked its core capital position — also under pressure from loan provisions and a weak ruble.

The bank expects its Tier 1 capital adequacy ratio — a measure of a lender's ability to absorb shocks — to improve by up to 1 percentage point following a $1 billion perpetual bond issue, chief financial officer Herbert Moos said Friday.

The first of its kind to be issued in Russia, perpetual bonds are permanent interest-only loans that issuers do not have to repay, allowing them to count the money raised towards capital.

But analysts say the bond deal would only postpone an inevitable additional share issue, needed by the state-controlled lender to boost its capital longer term.

"A deal [bond] of this size does not seriously address VTB's weak capital position. ... While this Tier 1 bond placement ... is not a panacea, it could be regarded as a viable short-term alternative to equity raising," broker Troika Dialog said in a note.

Moos did not provide specific figures or estimates of the bank's current Tier 1 level.

VTB's Tier 1 capital ratio stood at 9.6 percent at the end of March, compared to a ratio of 11.8 percent at its larger peer Sberbank. Broker Uralsib estimates VTB's current Tier 1 at 9.4 percent.

According to Troika's estimates, the bond will add about 50-60 basis points to VTB's Tier 1 — smaller than Moos' expectation of the impact.

Yevgeny Tarzimanov, vice president at Moody's in Russia, said the bond deal would increase VTB's Tier 1 capital to around 10.1 percent, assuming its capital adequacy level stood unchanged as of the end of March.

"VTB has a long way to go because its Tier 1 will still remain below an average 13 percent Tier 1 for large Russian banks with similar ratings," Tarzimanov said.

VTB priced its bond deal at the lower end of an initial guidance of 9.50 percent to 9.75 percent.

Analysts viewed a similar deal by Banco do Brasil, Latin America's biggest bank by assets, as a guidance for VTB's issue.

Banco do Brasil sold $1 billion in perpetual bonds with a yield of 9.25 percent in January, topping up the issue later.

A banking source previously said that VTB's bond attracted strong demand of around $1.65 billion, meaning there is still room to increase the volume of the issue. However, Moos said the lender has no such plans at the moment.

Analysts warned that VTB might need to raise cash to allow it to continue lending after it bought Bank of Moscow last year, which triggered a $13 billion state-run bailout, hitting its Tier 1 capital.

Lending grew by 50 percent last year, helping to boost VTB's profit by 65 percent.

But Uralsib analysts say that, even after the bond issue, VTB's capital ratio will not be sufficiently high to show much strength in its lending growth, estimating a rise of 14 percent for the year.

VTB's core capital is also under pressure because of extra provisions for deteriorating loans, VTB said last week in a prospectus marketing the perpetual bond, adding that its capital adequacy ratios may suffer further.

Also, Troika estimates that a weak ruble in the second quarter, hit by global risk aversion due to European debt issues, has eroded VTB's Tier 1 level by 20-30 basis points.

However, the Russian government has hinted it may sacrifice privatization plans aimed to fulfill its budget and instead dilute state stakes in Sberbank and VTB through capital increases, a measure needed by VTB.

The government owns 75.5 percent of VTB, while the Central Bank owns 57.6 percent of Sberbank.

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