MOODY'S
INVESTORS SERVICE

CREDIT OPINION
21 December 2022

Update

Send Your Feedback

Contacts

Maria Vinuela +34.91.768.8237
VP-Senior Analyst
maria.vinuela@moodys.com

Pablo Alvarado Andonegui +33.1.5330.3352
Associate Analyst
pablo.alvaradoandonegui@moodys.com

Laurie Mayers +44.20.7772.5582
Associate Managing Director
laurie.mayers@moodys.com

JSC Development Finance Institution Altum

Update to credit analysis following rating affirmation

Summary

JSC Development Finance Institution Altum's (Altum) long- and short-term issuer ratings are positioned at Baa1/Prime-2, reflecting the combination of a Baseline Credit Assessment (BCA) of baa3 and our assumption of a very high probability of support from the Government of Latvia (A3 stable). The support assumption is based on Altum's importance to the growth strategies of the Latvian government, as well as the government's strong track record of providing support to strategic companies. However, without explicit government guarantees to Altum, or to its creditors, the government support does not lead to a rating at par with the sovereign rating.

On 16 December 2022, we affirmed Altum's long- and short-term issuer ratings at Baa1/Prime-2, together with the baa3 BCA, reflecting the sound financial profile of the company, with very strong capitalisation, high provisioning coverage incorporated into its funding programmes, and low refinancing risk. Such strengths are balanced against high problem loan levels and low profitability. The BCA is also supported by the unique standing of Altum in Latvia, refecting its policy mandate to provide a distribution channel for state and European Union (EU) programme funds to both end-customers and other financial institutions.

Credit strengths

» Very high probability of government support

» High capitalisation

» Stable funding profile, with high share of public funding (EU structural funds and state budget)

Credit challenges

» High volume of problem loans, although coverage is very high

» Moderate profitability, resulting from its mandate as a development institution

Outlook

The stable outlook on Altum's long-term issuer rating reflects our expectation that the company's standalone credit profile, and the support from and dependence on the government will remain broadly in line with the current levels over the next 12-18 months.

Factors that could lead to an upgrade

An upgrade could follow if the Latvian government's ratings are upgraded or explicit government guarantees protecting creditors in case of failure are provided; or Altum improves its standalone credit fundamentals significantly, including reducing its volume of problem loans and the losses arising from venture capital and guarantees, as well as managing non-EU and state funding prudently.

Factors that could lead to a downgrade

A downgrade could follow if the Latvian government's ratings are downgraded or if the probability of government support decreases. In addition, a downgrade of Altum's rating could result from a combination of the company significantly changing its funding structure, and a significant deterioration in its risk-coverage reserves and capitalisation.

Key indicators

Exhibit 1
JSC Development Finance Institution Altum (Consolidated Financials) [1]

	06-22[2]	12-21[2]	12-20[2]	12-19[2]	12-18[2]	CAGR/Avg.[3]
Total managed assets (EUR Thousands)	1,044,930.0	976,204.0	850,704.0	560,061.0	495,939.0	23.7[4]
Total managed assets (USD Thousands)	1,092,417.4	1,106,142.6	1,040,883.9	628,667.5	566,930.0	20.6[4]
Net Income / Average Managed Assets (%)	1.3	1.5	0.8	1.6	0.9	1.2[5]
Tangible Common Equity (Finance) / Tangible Managed Assets (%)	37.4	45.1	44.8	41.3	44.5	42.6[5]
Problem Loans / Gross Loans (Finance) (%)	7.4	7.1	8.3	15.0	17.2	11.0[5]
Net Charge-offs / Average Gross Loans and Leases (%)	0.1	0.3	1.3	0.9	3.4	1.2[5]
Debt Maturities Coverage (%)	2974.1	4538.1	8462.9	42313.1	281.9	11714.0[5]

[1] All figures and ratios are adjusted using Moody's standard adjustments. [2] IFRS [3] May include rounding differences because of the scale of reported amounts. [4] Compound annual growth rate (%) based on the periods for the latest accounting regime. [5] Simple average of periods for the latest accounting regime.
Sources: Moody's Investors Service and company filings

Profile

JSC Development Finance Institution Altum (Altum) has a strong mandate by law to promote the advancement of the Latvian economy through the development, approval, implementation and monitoring of aid programmes. These programmes, consisting of credit lines and guarantees, are funded through the state budget, EU structural funding and a listed bond programme. Although not a systemically important institution in terms of size, Altum is the main development institution in Latvia and is of considerable importance for the delivery of the government's economic policy. Altum's shareholders comprise the Ministry of Finance (40%), the Ministry of Economy (30%) and the Ministry of Agriculture (30%).

Altum's main areas of activity relate to providing loans, guarantees, and investments in seed and venture capital funds. It also offers nonfinancial support in the form of consultations, education and mentoring. Altum's activity is mainly restricted to programmes (financial instruments or grants) that are developed and then monitored at the ministry level.

Altum's activities are regulated by a special law, the Development Finance Institution Law, passed by the Latvian Parliament in October 2014 and in force since March 2015. Altum's mandate, which was originally issued for 7 years, was prolonged in November 2022 until 31 December 2029 by the European Commission. Altum's creation was supported by the European Commission's decision "Latvia MLB development segment and creation of the Latvian Single Development Institution". The other laws applicable to the institution are the Law on Governance of Capital Shares of a Public Person and Capital Companies, the Commercial Law and other binding regulatory enactments. Altum was established in December 2013 following the merger of the following three enterprises:

» Latvian Development Finance Institution Altum SJSC (previously the Mortgage and Land Bank of Latvia), specialised in credit activities

» Latvian Guarantee Agency LLC (LGA), specialised in guarantees and investments in venture capital

» Rural Development Fund SJSC (RDF), specialised in credit activities for farmers

Altum is not a deposit-taking institution and does not have a banking licence. While it is obliged to prepare annual audited accounts in accordance with IFRS, the entity is not required to comply with minimum capital requirements.

As of the end of September 2022, Altum reported a total consolidated asset base of €1,108 million.

Detailed credit considerations

Strong capitalisation, supported by substantial risk-coverage reserves

We assign a Capital score of Aa3, one notch below the initial score, to reflect substantial risk-coverage reserves which support the high capital levels, as well as the large portfolio of off-balance-sheet guarantees and our view that the share of such guarantees in the business mix will continue to increase.

Altum has large capital buffers to withstand the volatility in earnings and to support future growth. Its Moody's-adjusted tangible common equity-to-tangible managed assets ratio stood at 37.4% as of end-June 2022. According to the Law on Development Finance

Institutions, prior to the approval of the programmes by the Cabinet of Ministers, ALTUM estimates the associated expected loss. Under this credit risk cover scheme, the sponsor (the Latvian state or the EU) takes the first losses within the portfolios of loans, venture fund investments or guarantees (the percentage varies from one programme to another). For that purpose, the corresponding portion of public funding is assigned to the "portfolio loss reserve", which is part of specific reserve capital (or alternatively accounted as provisions for risk coverage, part of the liabilities).

Altum's profit is not paid out in dividends. Instead, the company accumulates reserves to ensure financial stability and sustainable operations, as well as to mitigate programme risks.

Declining, although still-high, asset risk

The assigned Weighted Average Asset Risk score of B1 is two notches lower than the Ba2 initial score

Altum's problem loan ratio remained high at 7.4% as of June 2022, although it declined progressively since its creation, from 8.3% as of December 2020 and 30.6% as of December 2014. Credit risk is largely mitigated by sizeable government- and EU-backed asset-risk protection (see above section). By targeting customers that would not usually have access to the Latvian banking industry due to limited financial history or limited financial resources, and because of the nature of its mandate and the risk cover, the institution has a larger risk appetite than a commercial bank.

Altum's portfolio is diversified in terms of financial instruments (Exhibit 2), with a portfolio of financial instruments granted within the state aid programmes of €953 million as of September 2022 (December 2021: €896 million), made up of 33,579 projects (December 2021: 30,978) and consisting of the following:

» a guarantee portfolio of €460 million (2021: €415 million),

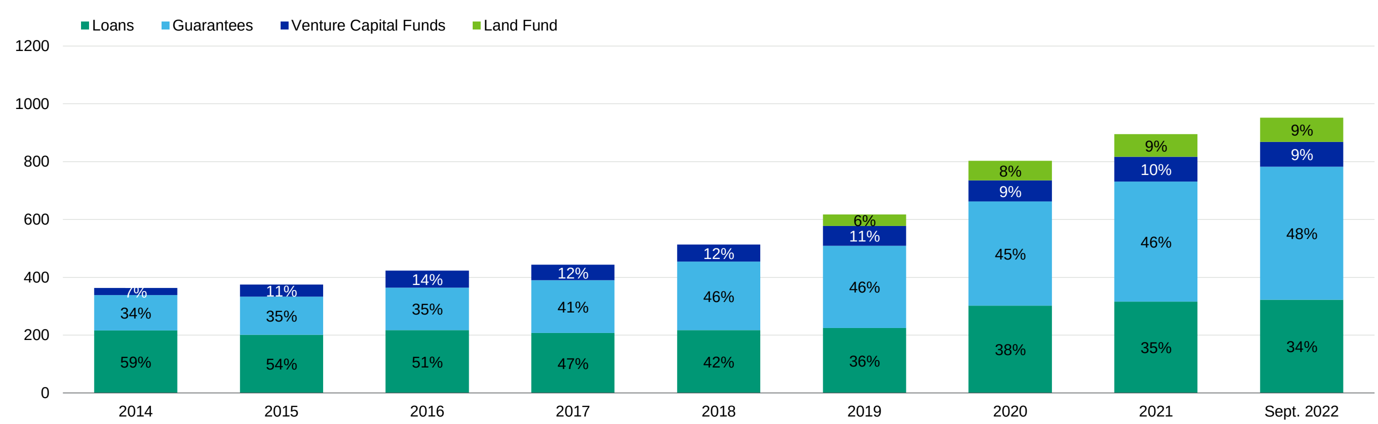
» a loan portfolio of €323 million (2021: €316 million),

» investments in venture capital funds of €86 million (2021: €88 million), and

» investments under the Latvian Land Fund of €84 million (2021: €79 million).

Since the start of the coronavirus pandemic and the subsequent military invasion of Russia in Ukraine, the loans and guarantees portfolio has consistently increased as Altum set up measures and facilities in place to counter the economic impact. During the first nine months of 2022, the volume of guarantees and loans grew by 11% and 2%, respectively.

Exhibit 2
Financial instruments outstanding



Percentages show the share of total financial instruments outstanding. Because of the growing size of the Land Fund, this is reported as a separate segment since 2019.
Source: Altum's financial reports

Altum expects a certain amount of loss on all its investments, depending on the programme structure and terms. The expected losses are estimated in advance and are covered by the credit risk cover, which is a percentage of a programme's funding.

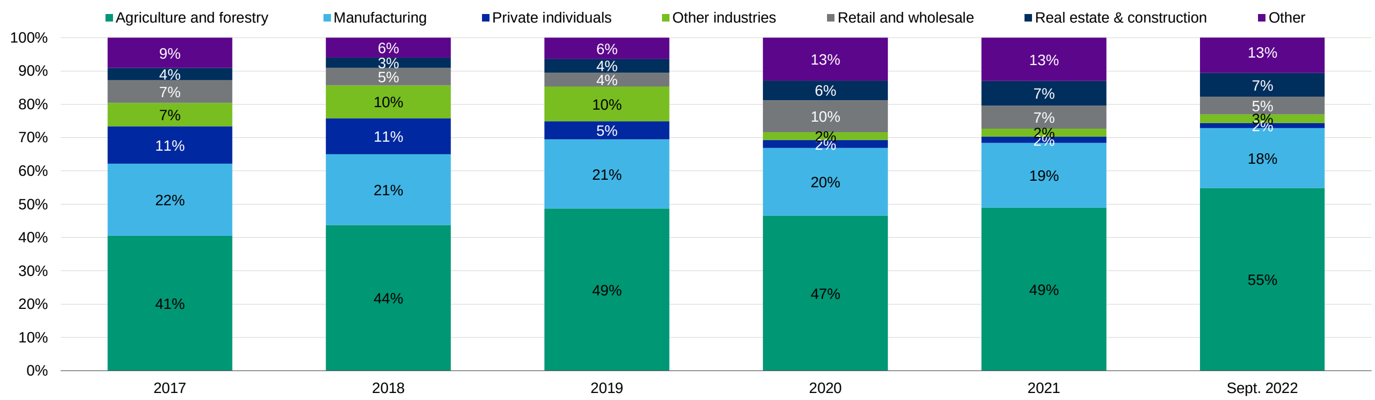
» Loans are given directly to companies and, to a lesser extent, to private individuals. The largest portion of loans are investment loans, aimed at helping smaller companies grow their businesses. Agriculture, including also the activities of the Land Fund, has traditionally been a large segment and constituted 55% of the loan portfolio as of September 2022. At the same time, loans extended to the manufacturing industry and private individuals accounted for 18% and 2% of total loans, respectively (Exhibit 3).

» Funds aimed at venture capital/equity investments are managed by external funds, with partnership agreements and consultation committees in place to ensure that the programmes are followed. Fund managers typically also invest their own money in these funds. The programmes aimed at equity investments typically have larger expected loss and associated risk-coverage reserves.

» Guarantees are given to banks to stimulate lending to borrowers who have viable business strategies but might lack enough own funds or collateral. Such products are extended as part of the state support package to the Latvian economy.

Exhibit 3

Loan book breakdown by industry



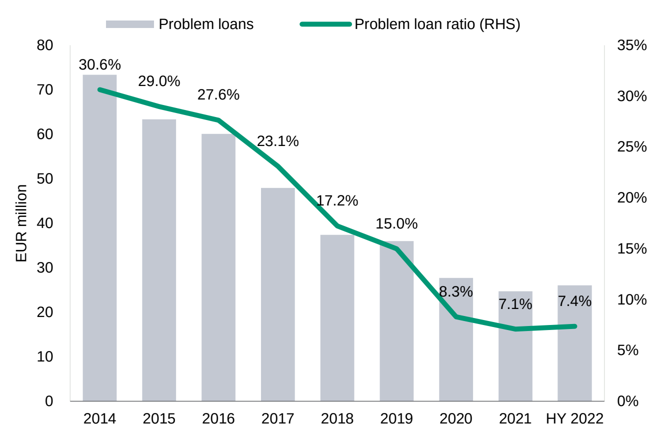
Percentages show the share of gross loans for each period.

Source: Altum's financial reports and Moody's Investors Service

Altum's nonperforming loans (NPLs)-to-gross loans ratio[1] was 7.4% as of June 2022, which is commensurate with the entity's business model because it is targeting borrowers with weaker risk profiles (Exhibit 4). The NPL ratio decreased from 15.0% as of December 2019 and 30.6% as of December 2014. As of June 2022, the company's loan loss reserves-to-problem loans ratio was a still-low 73% (2021: 75%) (Exhibit 5), although it jumps to 901% (2021: 644%) if we include the programmes' credit risk cover for guarantees.

Exhibit 4

Problem loan ratio

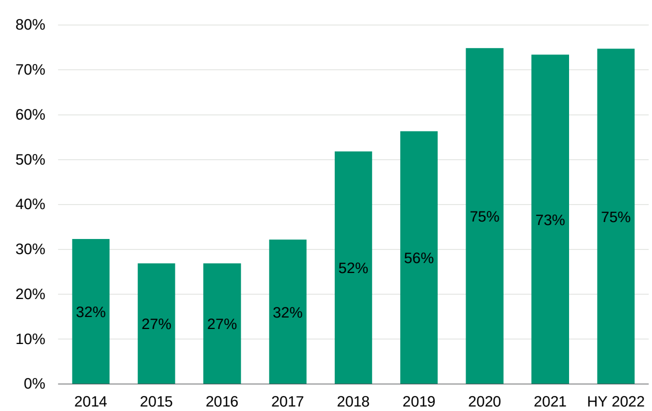


Source: Altum's financial reports and Moody's Investors Service

Exhibit 5

Provisioning coverage

Loan loss reserves as a percentage of nonperforming loans



Sources: Altum's financial reports and Moody's Investors Service

Strong liquidity, with funding coming from the Latvian state and European institutions

The Weighted Average Cash Flow and Liquidity score of Ba1, four notches below the initial score, reflects the fact that most programmes that are used to fund the institution have limited refinancing risks for Altum. This is balanced against its low funds from operations, which are used to repay market funding, constraining the Liquidity score.

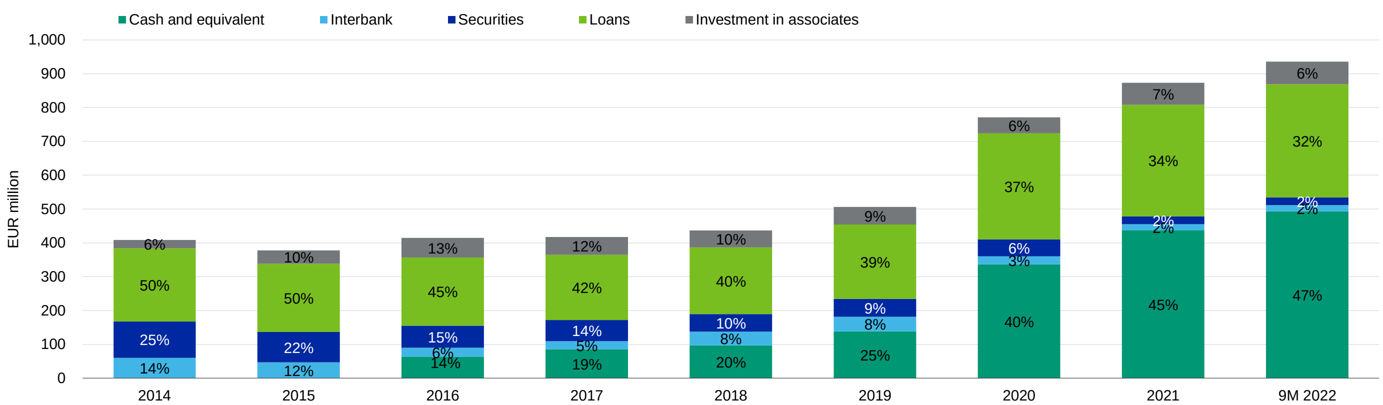
Altum is funded by borrowings from the Latvian state, European institutions and bond issuances. As of September 2022, 36% of Altum's liabilities came from support programme funding and state programmes. The remaining liabilities include bond issuances (at 17% of total liabilities), funding from general governments (at 30%) and from other credit institutions (at 8%).

Altum has a comfortable maturity profile, with 94% of funding (liabilities against credit institutions, general governments, issued debt, support programme funding and state aid) having a maturity of more than one year as of September 2022.

As of September 2022, Altum had sufficient liquid resources, consisting mainly of demand deposits in other credit institutions and the Latvian Treasury (€566 million), as well as Latvian government bonds (around €12 million) (Exhibit 6).

Exhibit 6

Breakdown of Altum's assets



The data labels refer to the percentages with respect to total assets.
Source: Altum's financial statements

Moderate profitability with earnings volatility, inherent to its business model

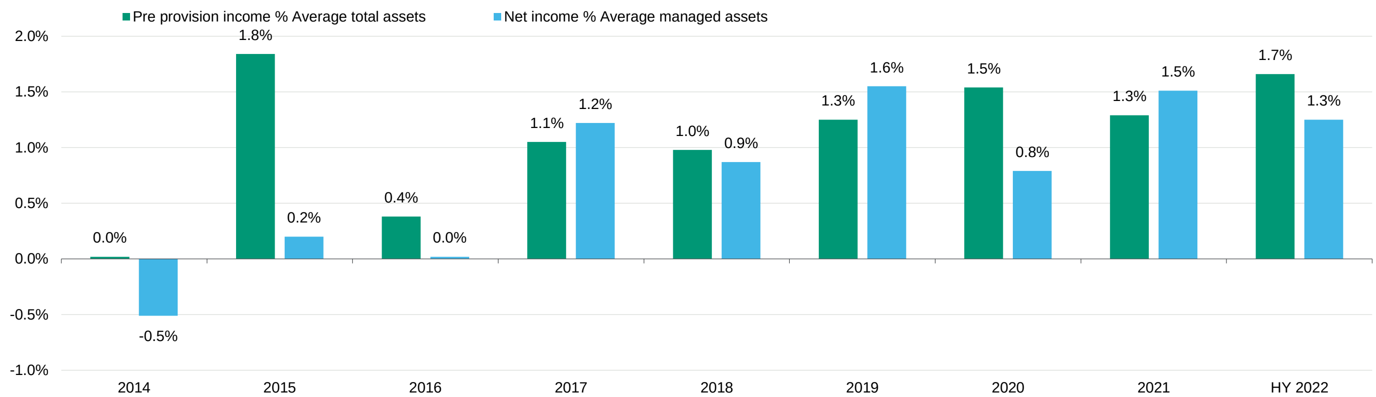
We assign a Profitability score of Ba1, one notch below the initial score to reflect our expectation of declining profitability.

Altum reported moderate core profitability levels throughout the past four years, thereby meeting its obligation under the law to remain profitable over the long term and preserving the capital invested by the state (a positive return on equity is, therefore, incorporated into the business strategy). However, because of its public mandate and lack of profit maximisation incentives, we expect internal capital generation to be constrained, while the credit impairments, which have increased during 2022 and are expected to further increase in 2023, will add additional pressure on bottom-line profitability.

Altum's top-line revenue mostly consists of net interest income, which remained stable, increasing 0.3% during 9M 2022 compared with 9M 2021. Non-interest income increased by 102% in 9M 2022 driven by a 70% increase in other income which related to a €1 million of profit realization from the first generation venture capital fund. During the first nine months of 2022, credit-related provisions increased by €4 million compared to 9M 2021, as a result of an increase in impairment losses (excluding reversals) to €9.9 million due to the uncertainty in the operating environment and the economic disruption, and despite a net reversal of €7.1 million.

Exhibit 7

Moderate profitability levels, constrained by high loan loss provisions during the first six months of 2022



Source: Altum's financial statements and Moody's Investors Service

Operating environment

A key component of our analysis is the extent to which external conditions can have a significant influence on Altum's credit profile. The Operating Environment score for Altum (Baa2) takes into account two factors: a Macro-Level Indicator (A3) and an Industry Risk score (Baa). The score for the Operating Environment is combined with the Financial Profile score to determine the Adjusted Financial Profile score.

As the Macro-Level Indicator is higher than the Industry Risk indicator, it receives 0% weight in calculating the Operating Environment score, which instead fully reflects the Industry Risk.

Macro-level indicator

The Macro-Level Indicator of A3 for Latvia reflects the intrinsic strength of its economy, the capacity of the government to implement sound economic policies, as well as political risk, government liquidity risk, financial sector risk and external vulnerability risk. The Economic Strength score of baa2 reflects the small but diversified export sector, with a proven track record of managing economic shocks. The a2 Institutions and Governance Strength score reflects the country's strong institutional capacity, as exemplified by the very significant macroeconomic adjustment and fiscal consolidation undertaken following the global financial crisis. Susceptibility to Event Risk is assessed at ba, driven by our assessment of the geopolitical risk in the region, affected by the military invasion of Russia in Ukraine.

Industry risk score

In assessing Industry Risk, we take into account the competitive position, exposure to cyclical economic forces and the track record of the product offering of a finance company's business line(s). The Industry Risk score for Altum is Baa, which reflects its stable position in the industry as a development institution, with limited exposure to competition from commercial banks and a specific government mandate regulated by law, and, within that scope, its ability to channel EU and state funding into the real economy. Therefore, economic cycles are less important for Altum than for other private finance companies. The track record of the company's business line is limited and, therefore, constrains the Industry Risk score. Altum was founded in December 2013 as a result of the merger of three state-owned organisations. The reorganisation was completed in April 2015, and the company's missions depend not only on the Latvian state but also on future allocations of EU structural funds to Latvia.

Support and structural considerations

The issuer ratings of Altum incorporate both the BCA and support considerations. The very high dependence on and the very high probability of support from the government lead to a two-notch uplift to a Baa1 rating. However, without explicit government guarantees to Altum, or to its creditors, the government support does not lead to a rating at par with the A3 sovereign rating.

Very high probability of government support

The Latvian government has a track record of providing support to strategic companies, including the electricity, postal services, airlines, railways and telecom sectors, as well as development institutions. The Latvian government has previously supported its development institutions by means of recapitalisation, liquidity support and guarantees. Because of the importance of Altum for planning and implementing growth strategies in the national economy, we assess that the probability of government support is very high.

Altum has very high dependence on the Latvian state

The very high default dependence reflects the strong probability that, in the event of a sovereign credit default, the risk of a potential financial crisis affecting Altum would be quite high, given the clear operational links with the government, whereby Altum has an explicit and well-recognised mandate to implement specific government policies; the geographical focus of Altum's activities in Latvia; and its high dependence on state funding.

ESG considerations

JSC Development Finance Institution Altum's ESG Credit Impact Score is Moderately Negative CIS-3

Exhibit 8

ESG Credit Impact Score

CIS-3

Moderately Negative

NEGATIVE IMPACT

POSITIVE IMPACT

For an issuer scored CIS-3 (Moderately Negative), its ESG attributes are overall considered as having a limited impact on the current rating, with greater potential for future negative impact over time. The negative influence of the overall ESG attributes on the rating is more pronounced compared to an issuer scored CIS-2.

Source: Moody's Investors Service

Altum's ESG Credit Impact Score is moderately negative (**CIS-3**). The score reflects that ESG considerations having a limited impact on the current rating, as government support and sizeable capital buffers mitigates the exposure to ESG risks.

Exhibit 9

ESG Issuer Profile Scores

ENVIRONMENTAL	SOCIAL	GOVERNANCE
E-3	S-3	G-3
Moderately Negative	Moderately Negative	Moderately Negative

Source: Moody's Investors Service

Environmental

Altum faces moderate environmental risks primarily because of its portfolio exposure to carbon transition risk. Altum is exposed to mounting business risks and stakeholder pressure to meet more demanding carbon transition targets. Altum is actively engaged in further developing its climate risk management and reporting frameworks, and optimizing its loan portfolio toward less carbon-intensive assets.

Social

Altum faces moderate social risks, partly reflecting its developmental and policy mandate, which entails regulated and mandated lending, and is linked to the company's public ownership. Altum's role as the main development institution in Latvia makes it susceptible to politically and socially motivated decisions that could affect its financial profile.

Governance

Altum's governance risks are moderate, reflecting its public ownership. Financial strategy and risk management are constrained by the company's high asset risk - albeit mitigated by the credit risk cover scheme and high capitalization - reflecting the government's influence over its mandate and decision-making process.

ESG Issuer Profile Scores and Credit Impact Scores for the rated entity/transaction are available on Moodys.com. In order to view the latest scores, please click here to go to the landing page for the entity/transaction on MDC and view the ESG Scores section.

Methodology and scorecard

The principal methodologies we use in rating Altum are our Finance Companies rating methodology, published in November 2019, and Government-Related Issuers rating methodology, published in February 2020.

Exhibit 10

JSC Development Finance Institution Altum

JSC Development Finance Institution Altum						
Financial Profile	**Factor Weights**	**Historic Ratio**	**Initial Score**	**Assigned Score**	**Key driver #1**	**Key driver #2**
Profitability						
Net Income / Average Managed Assets (%)	10%	1.28%	Baa3	Ba1	Expected trend	
Capital Adequacy and Leverage						
Tangible Common Equity / Tangible Managed Assets (%)	25%	37.36%	Aa2	Aa3	Other adjustments	Expected trend
Asset Quality						
Problem Loans / Gross Loans (%)	10%	10.12%	Ca	Caa1	Portfolio composition	
Net Charge-Offs / Average Gross Loans (%)	10%	0.82%	Aa2	Baa3	Portfolio composition	
Weighted Average Asset Risk Score			**Ba2**	**B1**		
Cash Flow and Liquidity						
Debt Maturities Coverage (%)	10%	4538.13%	Aaa	Baa3	Other adjustments	
FFO / Total Debt (%)	15%	2.61%	Caa2	Ba1	Other adjustments	
Secured Debt / Gross Tangible Assets (%)	20%	0.00%	Aaa	Ba1	Other adjustments	
Weighted Average Cash Flow and Liquidity Score			**A3**	**Ba1**		
Financial Profile Score	**100%**		**A3**	**Baa3**		
Operating Environment						
Home Country	**Factor Weights**	**Sub-factor Score**	**Score**			
Macro Level Indicator	0%		A3			
Economic Strength	25%	baa2				
Institutions and Governance Strength	50%	a2				
Susceptibility to Event Risk	25%	ba				
Industry Risk	100%		Baa			
Home Country Operating Environment Score			Baa2			
	Factor Weights			**Score**	**Comment**	
Operating Environment Score	**0%**			**Baa2**		
ADJUSTED FINANCIAL PROFILE				**Score**		
Adjusted Financial Profile Score				**Baa3**		
Financial Profile Weight	100%					
Operating Environment Weight	0%					
Business Profile and Financial Policy				**Adjustment**	**Comment**	
Business Diversification, Concentration and Franchise Positioning				0		
Opacity and Complexity				0		
Corporate Behavior / Risk Management				0		
Liquidity Management				0		
Total Business Profile and Financial Policy Adjustments				**Baa3**		
					Comment	
Sovereign or parent constraint				**A3**		
Standalone Assessment Scorecard-indicated Range				baa2 - ba1		
Assigned Standalone Assessment				baa3		

Source: Moody's Investors Service

Exhibit 11

JSC Development Finance Institution Altum

Government -Related Issuer	Factor
a) Baseline Credit Assessment	baa3
b) Government Local Currency Rating	A3
c) Default Dependence	Very High
d) Support	Very High
e) Final Rating Outcome	Baa1

Source: Moody's Investors Service

Ratings

Exhibit 12

Category	Moody's Rating
JSC DEVELOPMENT FINANCE INSTITUTION ALTUM	
Outlook	Stable
Issuer Rating -Dom Curr	Baa1
ST Issuer Rating -Dom Curr	P-2

Source: Moody's Investors Service

Endnotes

1 NPLs for 2018 onwards consist of Stage 3 loans as per the IFRS9 reporting standards, while for previous periods, NPLs consist of the reported impaired loans and past due but not impaired loans.

REPORT NUMBER 1350930

CLIENT SERVICES

Americas	1-212-553-1653
Asia Pacific	852-3551-3077
Japan	81-3-5408-4100
EMEA	44-20-7772-5454