

Rating Action: Moody's confirms Altum's Baa1 issuer rating; outlook stable

25 Mar 2019

Paris, March 25, 2019 -- Moody's Investors Service ("Moody's") today confirmed JSC Development Finance Institution Altum's (Altum) Baa1 long-term issuer rating. The baseline credit assessment (BCA) was upgraded to baa3 from ba2. The short-term issuer rating was affirmed at P-2. The outlook has been changed to stable from rating under review.

This action concludes the review for upgrade initiated on 12 December 2018 following the introduction of an updated finance companies methodology on 10 December 2018.

A list of affected ratings can be found at the end of this press release.

RATINGS RATIONALE

RATIONALE FOR THE UPGRADE OF THE BASELINE CREDIT ASSESSMENT

Altum's BCA upgrade to baa3 from ba2 reflects: 1) the strong financial profile of the company with very strong capitalization and the large share of loss coverage incorporated in the funding programmes, also resulting in low refinancing risks, balanced against high levels of problem loans and moderate profitability; and 2) the unique standing of Altum in Latvia's financial services industry reflecting its policy mandate to provide a distribution channel for state and EU program funds to both end-customers and other financial institutions.

The first important driver in the BCA is Altum's strong financial profile, underpinned by very strong capitalization, with tangible common equity to managed assets of 44% at year-end 2018 (based on preliminary figures). Furthermore, Altum's funding programs incorporate large shares of loss coverage, which largely mitigate the credit risk the company takes on. Although the problem loans to gross loans ratio is considerably higher than for Latvian banks at 17.2% at year-end 2018, Moody's understands that risk coverage of problem loans was 240%. Furthermore, these programs have limited refinancing risks as the company can continue using program specific funds as long as they are invested in line with the intent of that program, even after its stated end date. Although profitability during 2017 and 2018 has been strong, with net income to average managed assets 0.82% and 0.83% (based on preliminary figures) respectively, the public nature of its mission and lack of profit maximizing incentives point to moderate to low profitability going forward.

The next important driver underpinning the BCA is Altum's unique position in the Latvian financial services industry, as a government related institution with a clear mandate to promote the Latvian economy. It is the sole conduit for European Union (EU) structural funds into the Latvian economy, and is also used to disperse government programs. Altum takes on this role by lending to companies and households, providing venture capital to startups, and through its growing volumes of guarantees to both companies and households.

By targeting customers that would not usually have access to the Latvian banking industry due to limited financial history or limited financial resources, Altum provides funds either directly or by helping customers to access banking services. Although barriers to entry are moderate in this segment, its services are complementary to commercial banks.

Altum has an institution specific law, which is unique for financial institutions in Latvia. Therefore, its existence is not dependent on the stability of the Latvian banking sector. Its focus on fulfilling its mandate by providing financial instruments is in line with current and future EU structural funding ambitions. Thus it is well positioned to continue managing EU structural funding programs.

RATIONALE FOR THE CONFIRMATION OF ALTUM'S ISSUER RATINGS BASED ON ASSESSMENT OF GOVERNMENT SUPPORT

The confirmation of Altum's Baa1 issuer rating incorporates the baa3 BCA and ratings uplift under a joint default analysis as Government Related Issuer. The assessment of a very high dependence on the sovereign, Latvia (A3, Stable), and a very high probability of government support, provides two notches of uplift above the BCA. Altum is considered to be an important tool for the government in its policy work, and Moody's expects a

very high probability that the government would inject additional capital into the company in case of need. 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.

OUTLOOK

The stable outlook on Altum is in line with the outlook on the Latvian's government ratings. Furthermore, Moody's forecasts that the standalone credit fundamentals will develop gradually, with strong capitalization, slightly lower profitability, stable asset quality and over time, higher reliance on market funding.

FACTORS THAT COULD LEAD TO AN UPGRADE

An upgrade could follow if the Latvian government ratings are upgraded, or if Altum improves its standalone credit fundamentals significantly, including demonstrating lower volumes of problem loans and 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 ratings are downgraded, or if the probability of government support decreases, or a combination of (1) Altum significantly changing its funding structure and; (2) its risk coverage reserves significantly deteriorating; or (3) capitalisation deteriorating significantly.

Issuer: JSC Development Finance Institution Altum

..Confirmed:

...Long-term Issuer Rating (local currency), Baa1

..Affirmation:

...Short-term Issuer Rating (local currency), affirmed P-2

..Outlook Action:

...Outlook changed to Stable from Rating under Review

PRINCIPAL METHODOLOGIES

The methodologies used in these ratings were Finance Companies published in December 2018, and Government-Related Issuers published in June 2018. Please see the Rating Methodologies page on www.moodys.com for a copy of these methodologies.

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