

# Letter from the Chairman of the Management Board

Alexander Dolgopolov

Chairman of the Management Board



Dear shareholders, colleagues and clients!

It was a successful year for Bank Vozrozhdenie, as we continued to expand steadily and took various steps towards creating a new, solid platform for growth in the future.

## Active operations

In 2012, the Bank increased its presence in key areas of the market: SME and retail segments. Our SME loan portfolio rose by 10.2% year-on-year to RUB 77.3 billion, as we continued to focus on companies in the real sector of the economy. To ensure that clients' interests were fully considered when deciding on loan rates, we worked closely with the regional SME development funds, entered into partnership programmes

with SME Bank, and devoted substantial effort to developing micro-lending with the European Bank for Reconstruction and Development. In addition, throughout the year, we continued to provide financing to our major strategic clients in the regions where the Bank is present.

Retail lending soared compared with 2011, as consumers were encouraged by lower inflation and greater public spending thanks to strong export revenues resulting from high oil prices. In 2012, Bank Vozrozhdenie's total retail loan portfolio expanded by 34.8% year-on-year, driven mainly by the mortgage portfolio, which was up 44.9% to RUB 22.3 billion. As a result, the Bank was the eighth largest in Russia by mortgages issued (loans provided under partnership programmes with major construction firms and realtors accounted for up to 80% of mortgage product sales). We also undertook measures to make consumer loans more attractive, focusing on our traditional client segments: users of payroll programmes and employees of large enterprises and government bodies. Over the year, despite the slight increase in interest rates in the second half, consumer loans in this segment increased by 27%.

While working hard to expand our loan portfolio, we put special emphasis on monitoring its quality. By the year-end, the share of non-performing loans (NPLs) stood at 9%, primarily due to impairment of several large corporate loans. In the key SME and retail segments, the share of NPLs fell throughout the year thanks to our prudent lending criteria. Nonetheless, given the slowing economy growth and difficult macroeconomic conditions worldwide, we have no current plans to reduce our provisions for loan impairment.

## **Funding**

As Bank Vozrozhdenie has traditionally funded its operations primarily using funds from clients, over the year we monitored the situation on the market, promptly adjusting interest rates and other deposit conditions where necessary. We took advantage of the savings drive by businesses, boosting our corporate deposits by 32.7% year-on-year, while the continued focus of retail clients on savings increased our individual deposits by 12.3%. Thanks to our moderate approach to raising interest rates on retail deposits, we were able to keep the cost of funding at a comfortable level of 4.4%.

## **Non-interest income**

Fees and commissions account for a substantial part of our operating income, and we are among the leaders in Russia in this respect. In 2012, we focused on maintaining the share of non-interest income in operating income. Fee and commission income rose by over 5% year-on-year, mainly due to settlement fees (up 7.7% for the year) and commissions on bank card transactions (up 7.4% for the year) widening. In the retail segment, we strived to encourage the use of remote channels (terminals, internet, and mobile bank) for payments and transfers, while making them more convenient and accessible for clients. Ultimately, our efforts were rewarded, as their share in such transactions overall increased. In the corporate segment, remote channels already account for 83% of payments and settlements, and we intend to increase this figure further. We view the development of remote services as a crucial part of our business strategy and a key source of non-interest income growth.

## **Capital**

In 2012, the ongoing expansion of our loan portfolio and the more stringent regulatory environment put pressure on our capital base. To comply with the Bank of Russia's requirements and the Basel III rules, which were expected to be implemented shortly, we raised two RUB 1 billion tranches of a subordinated deposit last year. Retained earnings ensured the growth of the core capital. By the year-end, our total capital adequacy ratio was 14.9%, while the tier 1 ratio was 12.3%. In early 2013, we received the third tranche of the subordinated deposit. Thanks to all of these measures, we began this year with a comfortable capital

position that will enable us to reach our planned growth targets.

## **Efficiency and income**

While our business grew steadily, we remained focused on making it more efficient. In 2012, operating expenses rose only slightly and at a rate lower than inflation. Over the year, we reduced the cost-to-income before provisions ratio by 6.3 percentage points to 58.5%. In the medium term, we aim to lower the figure to 50%. Cost control was one of the main contributors to income growth. Last year, net income rose by 46% to RUB 2.3 billion, which was above our target.

## **New operating model**

Further reductions in expenses will depend largely on the project of the Bank's operating model optimization, which aims to centralize many of the operational and support functions. We have already taken similar steps in the retail segment of our business by uniting our loan decision-making and monitoring processes in one center. Having carefully analyzed the functions of our branches, we now intend to centralize more of our back office functions, which will involve upgrading our IT infrastructure and operating structure. In our view, implementation of this project will not only reduce expenses and increase efficiency, but also enhance client service quality.

## **Outlook**

In summer 2012, I was appointed as Chairman of the Management Board, and I would like to thank all shareholders and the Board of Directors for their confidence in me. My main tasks, as I see them, are to continue expansion of the Bank's business and achieve high level of its profitability. In 2013, we intend to increase our loan portfolio even further, while monitoring its quality closely, and strive to retain our leading position in terms of share of non-interest income. Among other ongoing priorities there are ensuring balanced growth of our resource base and decreasing the cost of funding. We will also pay particular attention to preserving our corporate culture and our unique approach to servicing clients, which we have honed over the last 22 years.

**Chairman of the Management Board**  
**Alexander Dolgoplov**