MOODY'S
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CREDIT OPINION
22 February 2021

Update

Rate this Research

RATINGS

Siauliu Bankas, AB

Domicile	Siauliai, Lithuania
Long Term CRR	Baa1
Type	LT Counterparty Risk Rating - Fgn Curr
Outlook	Not Assigned
Long Term Debt	Not Assigned
Long Term Deposit	Baa2
Type	LT Bank Deposits - Fgn Curr
Outlook	Positive

Please see the ratings section at the end of this report for more information. The ratings and outlook shown reflect information as of the publication date.

Contacts

Simon James Robin Ainsworth +44.20.7772.5347
Associate Managing Director
simon.ainsworth@moodys.com

Sean Marion +44.20.7772.1056
MD-Financial Institutions
sean.marion@moodys.com

Mattias Eric Frithiof +46.8.5179.1264
AVP-Analyst
mattias.frithiof@moodys.com

Emma Jonasson +46.8.5179.1283
Associate Analyst
emma.jonasson@moodys.com

Siauliu Bankas, AB

Update following ratings affirmation, outlook changed to positive

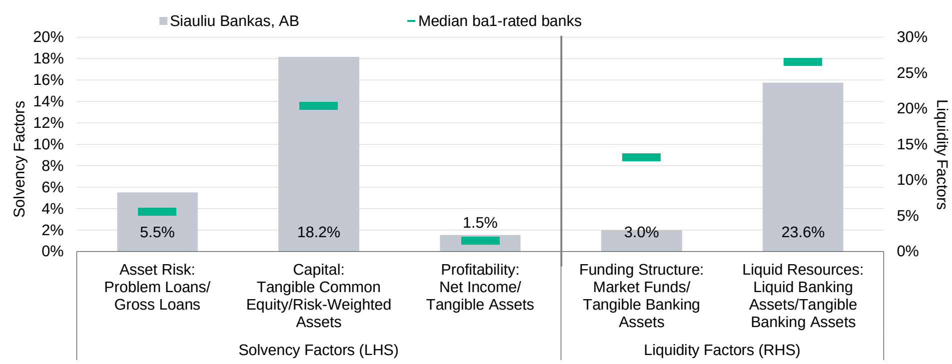
Summary

Siauliu Bankas, AB's (Siauliu Bankas) Baa2/Prime-2 deposit ratings incorporate a ba1 Baseline Credit Assessment (BCA) and Adjusted BCA and a two-notch uplift resulting from our Advanced Loss Given Failure (LGF) analysis. We also assign a Counterparty Risk (CR) Assessment of Baa1(cr)/P-2(cr) and Counterparty Risk Ratings of Baa1/P-2. The ratings and assessments were affirmed on 17 February 2020 with the outlook on the long-term deposit ratings changed to positive.

The ratings reflect the operating environment in Lithuania, where the bank has all of its lending, the bank's increased capitalisation, illustrated by its tangible common equity (TCE) to risk-weighted assets (RWAs) ratio of 18.2% as of the end of September 2020, and a strong recurring profitability. This is balanced against the bank's relatively high level of non performing loans, historical high level of loan growth, and sector concentration in small- and medium-sized enterprise (SME) and in consumer finance.

We view the probability of support from the Government of Lithuania (A2 stable) to Siauliu Bankas as low, resulting in no further uplift for the deposit rating.

Exhibit 1
Rating Scorecard - Key financial ratios



These are our Banks Methodology scorecard ratios. Asset risk and profitability reflect the weaker of either the three-year average or the latest reported ratio. The capital ratio is the latest reported figure. The funding structure and liquid asset ratios are the latest year-end figures.
Source: Moody's Investors Service

Credit strengths

» Robust capital, with important headroom above regulatory requirements

» Strong profitability, which supports internal capital generation capacity

» Sound funding and liquidity, underpinned by its stable deposit base

Credit challenges

» Relatively high level on non performing loans

» Sector concentration towards the more vulnerable SME segment along with high loan growth

Outlook

The positive outlook on Siauliu's long-term deposit ratings reflects Moody's expectation that the bank will: maintain a strong capital position with tangible common equity to risk weighted assets of around 18%; demonstrate a resilient profitability, with net income to tangible banking assets of at least 1.5%; and, successfully manage asset risk and risk appetite with a problem loans to gross loans ratio of below 6%.

Factors that could lead to an upgrade

Siauliu Bankas' ratings could be upgraded should the bank maintain its current profitability and capitalization alongside a continuing resilience in terms of its problem loan ratios over coming quarters.

Factors that could lead to a downgrade

Conversely, downward pressure on Siauliu Bankas could develop if the operating environment deteriorated significantly, resulting in a significant deterioration in the bank's asset quality, profitability or capital. Furthermore, the rating could come under pressure if the risk appetite of the bank was to increase, resulting in a weakening of its asset quality and or increase volatility in its earnings.

Key indicators

Exhibit 2

Siauliu Bankas, AB (Consolidated Financials) [1]

	09-20[2]	12-19[2]	12-18[2]	12-17[2]	12-16[2]	CAGR/Avg.[3]
Total Assets (EUR Million)	2,910.7	2,508.2	2,261.7	2,030.8	1,861.3	12.7[4]
Total Assets (USD Million)	3,413.2	2,815.4	2,585.5	2,438.5	1,963.2	15.9[4]
Tangible Common Equity (EUR Million)	329.0	295.0	271.9	204.9	175.0	18.3[4]
Tangible Common Equity (USD Million)	385.8	331.1	310.8	246.1	184.6	21.7[4]
Problem Loans / Gross Loans (%)	5.1	5.3	6.2	5.5	7.2	5.8[5]
Tangible Common Equity / Risk Weighted Assets (%)	18.2	17.0	17.4	15.8	15.8	16.8[6]
Problem Loans / (Tangible Common Equity + Loan Loss Reserve) (%)	24.1	27.0	28.0	28.4	36.1	28.7[5]
Net Interest Margin (%)	2.8	3.1	3.0	3.0	3.1	3.0[5]
PPI / Average RWA (%)	3.8	4.0	4.5	2.9	4.2	3.9[6]
Net Income / Tangible Assets (%)	1.5	2.0	2.3	1.5	1.8	1.8[5]
Cost / Income Ratio (%)	37.3	38.8	35.1	51.0	45.5	41.5[5]
Market Funds / Tangible Banking Assets (%)	6.8	3.0	4.0	3.8	4.8	4.5[5]
Liquid Banking Assets / Tangible Banking Assets (%)	31.9	23.6	27.4	29.4	34.4	29.3[5]
Gross Loans / Due to Customers (%)	78.5	84.9	78.1	74.8	71.5	77.6[5]

[1] All figures and ratios are adjusted using Moody's standard adjustments. [2] Basel III - fully loaded or transitional phase-in; 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. [6] Simple average of Basel III periods.

Sources: Moody's Investors Service and company filings

Profile

Siauliu Bankas, AB (Siauliu Bankas) was established in 1992 in Siauliai, Lithuania, and is publicly traded on Nasdaq Vilnius. The bank had 10 subsidiaries as of the end of September 2020. Siauliu Bankas is focused on finance leasing and consumer credits, life insurance, investment management activities, real estate management activities and the development of residential areas in Lithuania, and it commenced offering deposit services in Germany in April 2019. The bank was 26% directly owned by the European Bank for Reconstruction & Development (EBRD, Aaa stable) as of the end of September 2020.

Siauliu Bankas held €2.9 billion in assets as of the end of September 2020, and with a market share of 7.7% in terms of deposits and 8.9% in terms of loans as of end of October 2020, it is the fourth-largest bank in Lithuania. The bank operates in all major cities and financially active regional centres of Lithuania. As of 30 September 2020, the bank had 59 regional customer service points across the country and 755 employees.

Recent developments

We expect advanced economies to grow in 2021, following a significant contraction in 2020. However, the economic recovery in 2021 will be highly dependent on three factors: (1) the development and distribution of a coronavirus vaccine, (2) effective pandemic management, and (3) government policy support. Over time, we expect better pandemic management and the availability of an effective vaccine or treatments to reduce the importance of the virus as a macroeconomic variable.

In 2020 Siauliu Bankas completed the acquisition of Danske Bank AS' (A3 stable/A2 negative, baa2)[1] Lithuania branch private customers credit portfolio. The major part of the portfolio consists of housing loans, increasing Siauliu Bankas' market share to 3.2%.

Detailed credit considerations

The ratings reflect the bank's Lithuanian operations, incorporating a Strong - Macro Profile

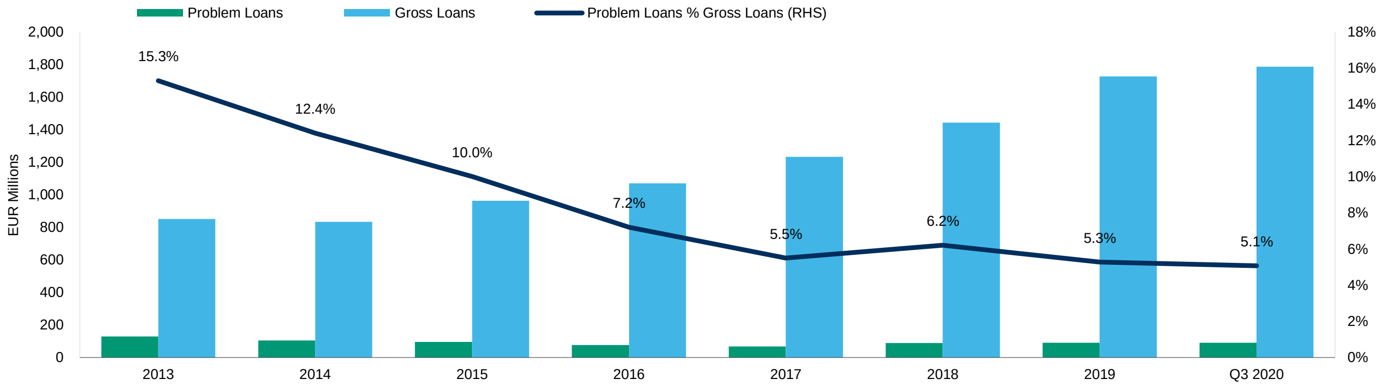
Moody's decision to revise Lithuania's macro profile to Strong (-) from Moderate (+) follows the upgrade of Lithuania's issuer and senior unsecured rating to A2 from A3, on 12 February 2021. This rating action reflects Lithuania's strong medium-term growth prospects and Moody's expectation that Lithuania's debt burden will remain lower than that of most A2 rated peers notwithstanding the impact of the crisis, with fiscal strength supported by strong debt affordability metrics and a reduction of foreign currency debt. Siauliu Bankas operates in Lithuania, and therefore, its Macro Profile is aligned with the Strong (-) Macro Profile of Lithuania[2].

High loan growth in recent years

Lithuania's economy has outperformed most European peers during the pandemic, allowing Siauliu to continue improving its problem loans to gross loans ratio to 5.1% at the end of September 2020, from 5.3% at the end of 2019, and 6.2% in 2018. Following the acquisition of Ukio Bankas in 2013, which had a higher credit risk profile, Siauliu Bankas has focused on reducing the stock of problem loans through recoveries and write-offs. The bank's nonperforming loan (NPL) ratio stood at 15.3% as of the end of December 2013 (see Exhibit 3). Despite the improvement, the ratio remain above the global 3.7% median of its ba1 BCA peers and the improvement in the NPL ratio also reflects rapid lending growth in recent years.

The coverage ratio (loan-loss reserves/problem loans) was 52.2% as of the end of September 2020, slightly higher than the 46.6% as of year-end 2019.

Exhibit 3
Problem loans decline because of a disciplined review of the legacy portfolio from Ukio Bankas along with strong lending growth



The increase in the problem loan ratio in 2018 is because of a change in definition (stage 3, gross loans) following the introduction of IFRS9.
Source: Company reports, Moody's Investors Service

The growth in Siauliu Bankas' loan portfolio slowed to 3.4% for the first nine months of 2020 compared to the very rapid loan growth in 2019 of 19.8%. We anticipate the loan growth will return when economic activity increases but expect it to be lower than in 2019 as competition banks is likely to increase as well. We continue to incorporate downside risks because of the rapid loan growth and concentration towards the more vulnerable SME segment and therefore assign an Asset Risk score of b2.

Robust capital with important headroom above the regulatory requirements

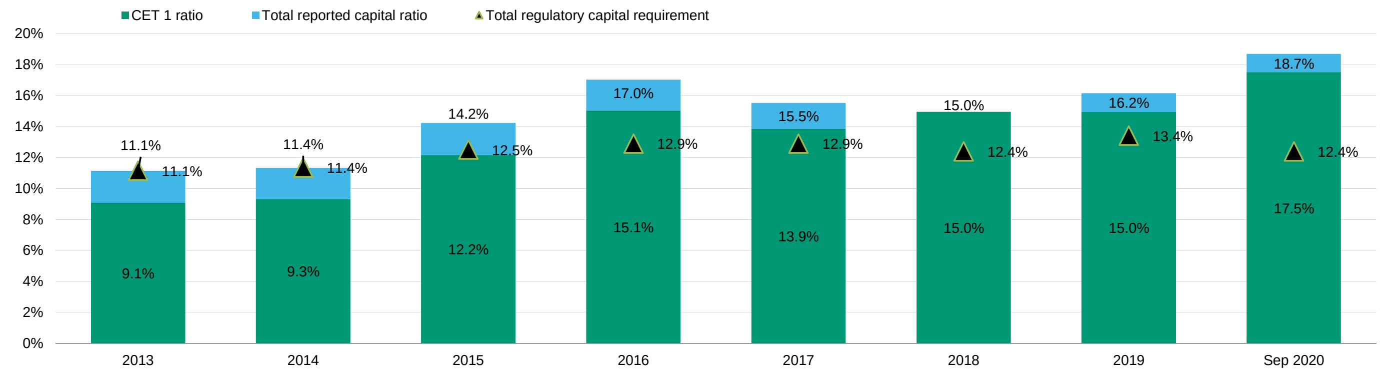
As of the end of September 2020, the bank's Tangible Common Equity (TCE) to RWA ratio was 18.2%, up from 17.1% as of year-end 2019. In 2018, the bank's capital increase was supported by the conversion of a €20 million subordinated convertible loan extended by the EBRD into equity[3]. At the same time, the leverage ratio (TCE to total assets) was 11.3% as of the end of September 2020 (compared to 11.8% as of year-end 2019).

Siauliu Bankas has strong internal capital generation capacity. In 2018, the bank updated its dividend policy to pay out at least 25% of the group's annual earnings as dividends. The bank will not pay dividends for 2019 because of the coronavirus outbreak, however.

Siauliu Bankas reported a phased-in CET1 capital ratio of 17.5% as of end-September 2020 and total capital ratio of 18.7%, which corresponds to a significant headroom above the total regulatory requirement of 12.4% as of end-September 2020, including a 0.5% Other Systemically Important Institution (O-SII) buffer (set to increase to 1.0% by year-end 2021)[4], a capital conservation buffer of 2.5% and a Pillar II requirement of 1.4% (see Exhibit 4). As of 31 December 2020 Additionally, following the Supervisory Review and Evaluation Process (SREP), an additional capital requirement was set by the ECB, Pillar 2 Requirement of 1.6% which will replace the previous additional capital requirement of 1.4%.

Our assessment of Siauliu Bankas' robust capital is reflected in the assigned a1 Capital score.

Exhibit 4
Siauliu Bankas capital ratio development



Source: Company reports, Moody's Investors Service

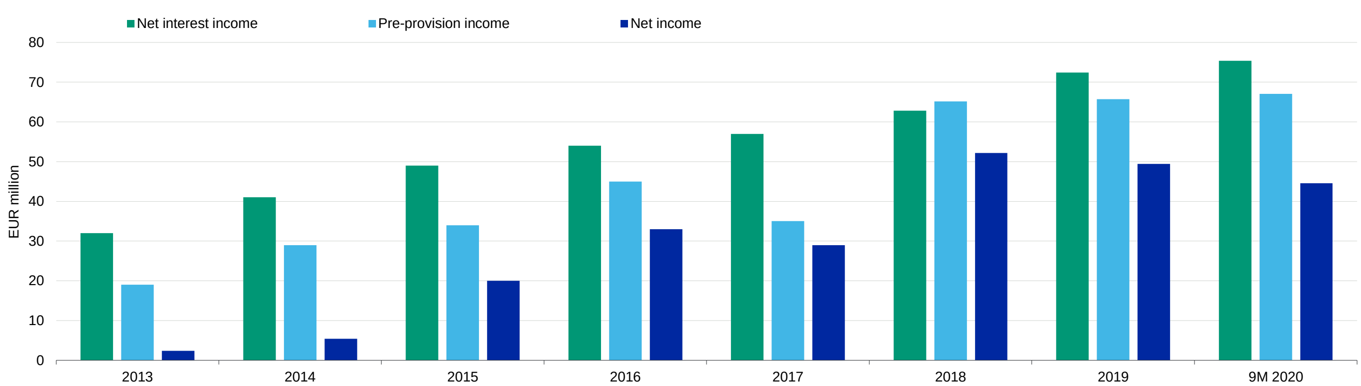
Strong profitability will be challenged

Siauliu Bankas' profitability has increased significantly in recent years, and we expect the bank's recurring revenue generation capacity to remain strong. Our Profitability score of baa1 captures the bank's sound profitability metrics, which have improved over the last few years, balanced against some volatility in earnings, the low interest rate environment and increasing competition at some point in the future. The bank will also likely face further profitability friction in 2020 and 2021 from coronavirus-induced disruptions.

In Q3 2020, the bank reported a lower net profit of €34.2 million compared with €40.6 million in Q3 2019. The bank's net income to tangible assets ratio was 1.53% for Q1-Q3 2020, compared with 1.97% in 2019 mostly driven by higher provisions for credit losses and poor performance in trading related business. Net interest income improved due to strong growth in mortgage lending due to the acquisition of the private customers' credit portfolio from Danske Bank A/S Lithuania branch. Net fees and commissions decreased by 8% the first nine months 2020 compared with the same period in 2019, mainly due to lower contribution from foreign exchange transactions and money transfer operations.

In 2021, provided that the operating environment improves with the Lithuanian economy returning to growth, we forecast Siauliu Bankas' net income to tangible assets ratio to increase to 1.6%, only slightly higher compared with 2020 and below the level of 2019. In the first half of the year net income is likely to continue to be pressured by effects stemming from coronavirus disruptions resulting in muted credit growth and continued provisioning. We also expect competition to increase which will limit loan growth.

Exhibit 5
Profitability evolution has been strong in recent years



Please note metrics for 9M 2020 are annualised
Source: Company reports, Moody's Investors Service

Sound funding and liquidity, underpinned by a deposit-based funding model

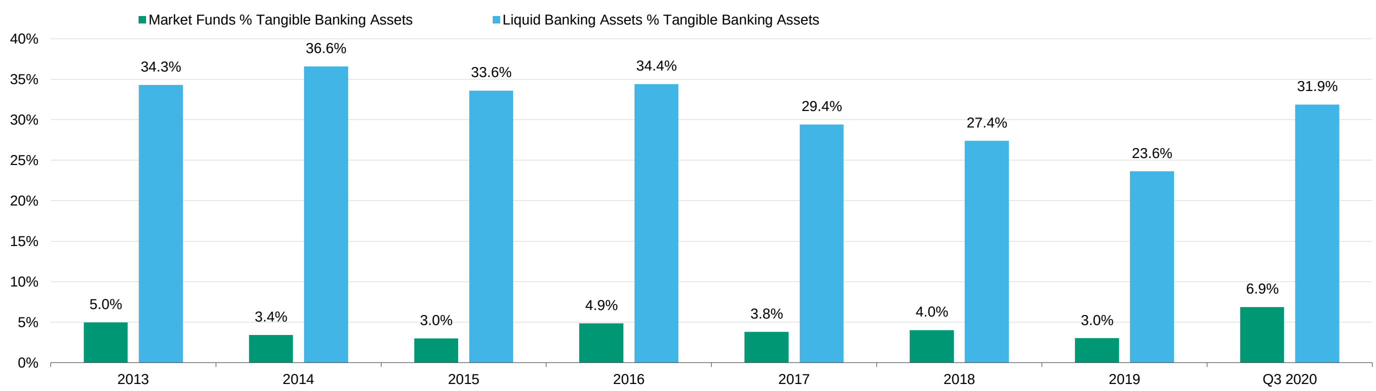
We assess Siauliu Bankas' funding and liquidity based on its funding structure and stock of liquid assets. We assign a Funding score of baa2, adjusted five notches below the Macro-Adjusted score. We anticipate the bank to increase its share of market funding to comply with its Minimum requirement for eligible liabilities and own funds (MREL) but the adjustment also highlights the relatively high share of corporate deposits, which tend to be more volatile than retail deposits.

Siauliu Bankas' liquidity benefits from its deposit-oriented business model, with deposits funding 78% of total assets as of the end of September 2020, and primarily coming from domestic residents. As of the end of September 2020, the bank reported a loan-to-deposit ratio of 76%, because of a more rapid growth in deposits (at 12%) than in loans (at 3%) during the first three quarters of 2020 and the bank's decision to take part of TLTRO 3 which boosted the liquidity position to 32% of tangible banking assets, reflected in the assigned score of Baa1.

Most of the securities in the bank's liquidity portfolio are debt securities, mainly Lithuanian government bonds. Siauliu Bankas mainly invests in investment-grade assets.

Exhibit 6

Siauliu Bankas' funding and liquidity constrained by more volatile junior deposits



Source: Company reports, Moody's Investors Service

Sources of facts and figures cited in this report

Unless noted otherwise, the bank specific figures originate from banks' reports and Moody's Banking Financial Metrics. All figures are based on our own chart of accounts and may be adjusted for analytical purposes. Please refer to the document Financial Statement Adjustments in the Analysis of Financial Institutions, published on 9 August 2018.

ESG considerations

In line with our general view for the banking sector, Siauliu Bankas has a low exposure to environmental risks, see our Environmental risks heat map for further information.

The most relevant social risks for banks arise from the way they interact with their customers. Social risks are particularly high in the area of data security and customer privacy, which are partly mitigated by sizeable technology investments and banks' long track record of handling sensitive client data. Fines and reputational damage because of product mis-selling or other types of misconduct are further social risks. Societal trends are also relevant in a number of areas, such as shifting customer preferences towards digital banking services increasing information technology cost, ageing population concerns in several countries affecting the demand for financial services or socially driven policy agendas that may translate into regulation that affects banks' revenue base. We also regard the coronavirus outbreak as a social risk under our ESG framework, given the substantial implications for public health and safety. Overall, we believe banks, including Siauliu Bankas, face moderate social risks. For more details see our Social risks heat map.

The rapid and widening spread of the coronavirus outbreak, deteriorating global economic outlook, falling oil prices, and asset price declines are creating a severe and extensive credit shock across many sectors, regions and markets. The securities sector has been one of the sectors affected by the shock given the profound economic and financial market upheavals it has caused. We regard the coronavirus outbreak as a social risk under our ESG framework, given the substantial implications for public health and safety

Governance is highly relevant for Siauliu Bankas, as it is to all entities in the banking industry. Corporate governance weaknesses can lead to a deterioration in a bank's credit quality, while governance strengths can benefit its credit profile. Governance risks are largely internal rather than externally driven, and for Siauliu Bankas, we do not have material governance concerns. Nonetheless corporate governance remains a key credit consideration and requires ongoing monitoring.

Support and structural considerations

Loss Given Failure analysis

We apply our advanced LGF analysis to Siauliu Bankas because the bank is subject to the European Union Bank Resolution and Recovery Directive, which we consider an operational resolution regime. For this analysis, we assume that equity and losses are at 3% and 8%, respectively, of tangible banking assets in a failure scenario. We also assume a 25% run-off of junior wholesale deposits, a 5% run-off in preferred deposits and a 26% proportion of junior deposits. These are in line with our standard assumptions.

Siauliu Bankas' deposits are likely to face very low loss given failure because of the loss absorption provided by the large volume of junior deposits. Siauliu Bankas' deposits are rated two notches above the ba1 Adjusted BCA because of a significant buffer of liabilities eligible for bail-in.

Counterparty Risk Ratings (CRRs)

CRRs are opinions of the ability of entities to honour the uncollateralised portion of non-debt counterparty financial liabilities (CRR liabilities) and also reflect the expected financial losses in the event such liabilities are not honoured. CRRs are distinct from ratings assigned to senior unsecured debt instruments and issuer ratings because they reflect the fact that, in a resolution, CRR liabilities might benefit from preferential treatment compared with senior unsecured debt. Examples of CRR liabilities include the uncollateralised portion of payables arising from derivatives transactions and the uncollateralised portion of liabilities under sale and repurchase agreements.

Siauliu Bankas' CRRs are positioned at Baa1/P-2

Siauliu Bankas' CRRs are positioned at Baa1/P-2, incorporating three notches of uplift from the LGF analysis.

There is a considerable volume of loss-absorbing liabilities junior to the CRR obligations. In this case, we assume a nominal volume at failure, because we are not able to accurately assess the volume of CRR liabilities at failure or the inherently more volatile nature of such liabilities as the bank approaches failure. The ratings incorporate three notches of uplift for the CRRs from the bank's Adjusted BCA of ba1.

Counterparty Risk (CR) Assessment

CR Assessments are opinions of how counterparty obligations are likely to be treated if a bank fails and are distinct from debt and deposit ratings in that they (1) consider only the risk of default rather than both the likelihood of default and the expected financial loss suffered in the event of default, and (2) apply to counterparty obligations and contractual commitments rather than debt or deposit instruments. The CR Assessment is an opinion of the counterparty risk related to a bank's covered bonds, contractual performance obligations (servicing), derivatives (for example, swaps), letters of credit, guarantees and liquidity facilities.

Siauliu Bankas' CR Assessment is positioned at Baa1(cr)/P-2(cr)

The CR Assessment, before government support, is positioned three notches above the Adjusted BCA of ba1. The main difference with our Advanced LGF approach used to determine instrument ratings is that the CR Assessment captures the probability of default on certain senior obligations, rather than the expected loss; therefore, we focus purely on subordination and take no account of the volume of the instrument class.

Government support considerations

We assign a low probability of government support for deposits, which does not translate into any uplift. Likewise, the CR Assessment does not benefit from government support.

Methodology and scorecard

About Moody's Bank Scorecard

Our scorecard is designed to capture, express and explain in summary form our Rating Committee's judgement. When read in conjunction with our research, a fulsome presentation of our judgement is expressed. As a result, the output of our scorecard may materially differ from that suggested by raw data alone (though it has been calibrated to avoid the frequent need for strong divergence). The scorecard output and the individual scores are discussed in rating committees and may be adjusted up or down to reflect conditions specific to each rated entity.

Rating methodology and scorecard factors

Exhibit 7

Siauliu Bankas, AB

Macro Factors						
Weighted Macro Profile	**Strong -**	**100%**				

Factor	**Historic Ratio**	**Initial Score**	**Expected Trend**	**Assigned Score**	**Key driver #1**	**Key driver #2**
Solvency						
Asset Risk						
Problem Loans / Gross Loans	5.5%	ba1	↔	b2	Sector concentration	Loan growth
Capital						
Tangible Common Equity / Risk Weighted Assets (Basel III - transitional phase-in)	18.2%	aa3	↔	a1	Stress capital resilience	
Profitability						
Net Income / Tangible Assets	1.5%	a3	↔	baa1	Expected trend	
Combined Solvency Score		a3		baa3		
Liquidity						
Funding Structure						
Market Funds / Tangible Banking Assets	3.0%	aa3	↓↓	baa2	Deposit quality	
Liquid Resources						
Liquid Banking Assets / Tangible Banking Assets	23.6%	baa3	↑↑	baa1		
Combined Liquidity Score		a3		baa2		
Financial Profile				baa3		
Qualitative Adjustments				Adjustment		
Business Diversification				0		
Opacity and Complexity				0		
Corporate Behavior				0		
Total Qualitative Adjustments				0		
Sovereign or Affiliate constraint				A2		
BCA Scorecard-indicated Outcome - Range				baa2 - ba1		
Assigned BCA				ba1		
Affiliate Support notching				0		
Adjusted BCA				ba1		

Balance Sheet	**in-scope (EUR Million)**	**% in-scope**	**at-failure (EUR Million)**	**% at-failure**
Other liabilities	524	18.0%	756	26.0%
Deposits	2,274	78.3%	2,042	70.3%
Preferred deposits	1,682	57.9%	1,598	55.0%
Junior deposits	591	20.3%	443	15.3%
Dated subordinated bank debt	20	0.7%	20	0.7%
Equity	87	3.0%	87	3.0%
Total Tangible Banking Assets	2,905	100.0%	2,905	100.0%

Debt Class	De Jure waterfall		De Facto waterfall		Notching		LGF Notching Guidance vs. Adjusted BCA	Assigned LGF notching	Additional Notching	Preliminary Rating Assessment
	Instrument volume + subordination	Sub-ordination	Instrument volume + subordination	Sub-ordination	De Jure	De Facto				
Counterparty Risk Rating	19.0%	19.0%	19.0%	19.0%	3	3	3	3	0	baa1
Counterparty Risk Assessment	19.0%	19.0%	19.0%	19.0%	3	3	3	3	0	baa1 (cr)
Deposits	19.0%	3.7%	19.0%	3.7%	2	2	2	2	0	baa2

Instrument Class	Loss Given Failure notching	Additional notching	Preliminary Rating Assessment	Government Support notching	Local Currency Rating	Foreign Currency Rating
Counterparty Risk Rating	3	0	baa1	0	Baa1	Baa1
Counterparty Risk Assessment	3	0	baa1 (cr)	0	Baa1(cr)	
Deposits	2	0	baa2	0	Baa2	Baa2

[1] Where dashes are shown for a particular factor (or sub-factor), the score is based on non-public information.
Source: Moody's Investors Service

Ratings

Exhibit 8

Category	Moody's Rating
SIAULIU BANKAS, AB	
Outlook	Positive
Counterparty Risk Rating	Baa1/P-2
Bank Deposits	Baa2/P-2
Baseline Credit Assessment	ba1
Adjusted Baseline Credit Assessment	ba1
Counterparty Risk Assessment	Baa1(cr)/P-2(cr)

Source: Moody's Investors Service

Endnotes

1 The ratings shown in this report are the long-term senior unsecured and long-term deposit ratings, and the Baseline Credit Assessment.

2 Please refer to Macro Profile – Lithuania: Strong -, 17 February 2021.

3 Please refer to Siauliu Bankas' capital metrics will strengthen with EBRD's debt-to-equity conversion, 13 August 2018.

4 Please refer to Lithuania raises Siauliu Bankas' capital requirements, a credit positive, 3 December 2018.

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EMEA	44-20-7772-5454