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WHY DID WESTERN BANKS EXPAND INTO RUSSIA AND WESTERN CIS COUNTRIES, WHAT WENT WRONG AND WHAT COMES NEXT?

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Why did Western banks expand into Russia and Western CIS countries, what went wrong and what comes next?

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1. Introduction

One of the most peculiar developments in European banking markets over the past 15 years, was the opening up of conventional banking markets in the former COMECON countries, firstly in Central Europe (CE) and Southeastern Europe (SEE), and then in the former Soviet bloc. This development has started and progressed with a significant capital and funding participation of a few leading Western European banking groups. Most leading Western banks that have a strong orientation towards the region of Central and Eastern Europe (CEE) in traditional commercial and retail business, including Russia and the Western CIS countries, started their regional expansion in the CE countries by the end of the 1990ies. The expansion to or upscaling in less mature markets in SEE and the Western CIS countries (mostly Russia, Ukraine or Kazakhstan) took place in the years 2002-2008 (following hefty losses by foreign banks in Russia back in 1998/1999). Moreover, at the top of the market conquering phase in Russia and Western CIS countries a lot of players which were fairly new in the region also made their entry into those markets in retail and commercial banking (via own subsidiaries or minority share acquisitions). This holds especially true for Russia and Ukraine. In contrast to the market conquering phase until 2008 the last few years were characterised by withdrawals of Western banks, pulling either out of Russia and/or other Western CIS countries. There are at least some 30 market exits or sales of minority participations of Western (European) banks active in Russia and Western CIS markets which are documented (see Appendix). In some cases the expansion and pull-back had been very costly, as previous acquisitions were high-priced. That said for a lot of Western banks the expansion to Russia and the Western CIS countries later in the 2000s did neither meet the expectations of the management, nor the ones of shareholders and/or stakeholders. This holds especially true for players that entered the CIS markets very aggressively and at a later stage (e.g. just prior to the global financial crisis), largely based on very optimistic long-term expectations.

The following papers outlines the main push and pull factors that supported the spreading of Western CEE banks into the Western CIS region, which partially reversed over the last few years. The paper in hand shows that the expansion of Western banks deeply into the Russian market and larger Western CIS markets in traditional retail and commercial banking (that requires substantial capital and risk exposure locally) was based on too optimistic assumptions regarding the long-term economic prospects as well as the sustainability of economic growth. Moreover, there was too much optimism that there will be secular institutional improvements in Russia and other Western CIS countries. Risks stemming from institutional weaknesses for the standard banking business had been underestimated. The same holds true for the rising market impact of state-owned or state-near banks as well as the effect of vested interests in the corporate sector and their influence on (economic) policymaking. Outside of the economic sphere nationalist and/or geopolitical factors had been underestimated as well.

2. Why did Western banks expand into Western CIS countries?

Due to a complex mix of host country factors and external (global) drivers the expansion of leading Western banks to CE and later SEE starting by the end of the 1990ies (following a banking sector restructuring and bad loan clean-up beforehand) had been a success story. Firstly, loan-to-GDP ratio had been low in most CE/SEE markets supporting easy catching-up asset growth (i.e. banking sector growth could easily outpace GDP growth for a sustained period of time), while the former communist countries had to establish a two-tier modern banking and financial system. Secondly, the push of Western banks into the CE/SEE markets went hand in hand with a sturdy global/European credit growth cycle. This exceptional boom phase supported, self-fulfilling and finally overoptimistic through-the-cycle profitability and convergence expectations regarding banking in CE/SEE. Based on - at that time - positive experiences in CE/SEE banking markets, i.e. strong balance sheet growth and high profitability, there was a complex mix of push and pull factors at play that then supported an expansion of Western banks further east, i.e. into the Western CIS countries. Moreover, Western banks expected that their future profits in CE/SEE markets will decrease substantially with growing maturity in the respective banking markets (i.e. when banking growth cannot outpace GDP growth on a sustained basis). Basically, there were very optimistic expectations that all CE countries and possibly a lot of SEE countries can join the EU and euro area very quickly without many frictions. Usually such integration into EU/euro area structures erodes parts of the banking profit pool in a given country (e.g. due to decreasing country risk premia, increasing competition on the local market or the elimination of foreign exchange business in case of entry into the euro area). Such more defensive motives definitely played a role at Western European banks in forming their strategies of moving further east, i.e. into Russia and Western CIS markets, with higher risk premia that were less likely to shrink quickly. Yet, with the benefit of hindsight it is obvious that fears about a swift erosion of banking margins in CE/SEE markets were overdone. Thirdly, there was a certain belief that Russia and the Western CIS countries may partially follow the economic and institutional developments seen in (some) CE and SEE countries. At the beginning of the 2000s there were some signs that Western CIS countries are willing to integrate deeply into Western economic structures (e.g. with Russia and Ukraine embarking on WTO membership), fostering a transition into more open and market-oriented economies without too much economic and political frictions down the road. Therefore, expectations built up that the banking sector maturity in CIS countries may come closer to one in more mature CE/SEE countries. Hence, it was expected that loan-to-GDP ratios in Western CIS countries may reach similar levels like in CE/SEE. Such a long-term convergence setting is usually very supportive for banking business (e.g. via increasing creditor rights, lower costs of funding etc.). Especially in case of Ukraine there were hopes during the previous decade that this country may follow the route of neighbouring CE/SEE countries. In case of Belarus there was also hope that at some point the country may (have to) open up. In retrospect one may say that hopes for convergence to Western market standards and deep integration into Western market structures were too optimistic.

Fourthly, there was a growing trust in the macroeconomic management of competent national authorities (also partially rewarded by external rating agencies). For instance, Russia and Kazakhstan pursued fairly sound macroeconomic policies prior to the global financial crisis in 2008/2009. Even in case of Ukraine or Belarus there was some superficial macro-financial stability prior to the 2008/2009 crisis, although the overall economic position remained fairly shaky in both cases. Moreover, the macroeconomic stabilisation seen in the Western CIS region from 2000-2008/2009 was supported by an exceptionally strong global economic, banking and commodity price growth cycle. This "super-cycle" has helped to mask structural economic flaws and macro-financial risks. However, recent years have shown that macro-financial risks in Russia as well as the Western CIS countries can be very damaging, especially for foreign-owned banks. With the benefit of hindsight macro-financial risks had been underestimated by foreign banks in Russia and Western CIS countries. Finally, Western banks were attracted by the sheer size of some Western CIS markets (compared to some smaller CE/SEE markets). In terms of total assets the Russian banking market itself is more or less as big as all other regional banking markets in CE and SEE taken together (i.e. even a fairly small market share in such a huge market implies substantial earnings potential). Despite all the suffering seen in recent years the Ukrainian banking market is still bigger than the biggest banking market in SEE, i.e. Romania. Moreover, Russian exports and imports are fairly sizeable in absolute terms, a fact that also supported the appetite of banks to participate in potential business opportunities here. Furthermore, Western banks were attracted by strong headline profitability (e.g. Return on Equity readings in double-digit territory) in Russian and Western CIS banking markets. However, it has to be stressed that expectations regarding risk-adjusted through-the-cycle profitability were too optimistic; a function of all the factors mentioned beforehand.

From a more micro-oriented perspective it is also interesting is to track the decision-making at Western European banks, and the following steps to conquer market share, which have eventually led to the substantial expansion in the CIS region, and among that predominantly in Russia. The first phase which can roughly be called the initial phase of entry started in the late 1990ies and lasted until approximately 2004-2005. During this period of time – supported by macroeconomic stability - banking products were enjoying very strong demand amidst quite high margins. The expansionary business stance was also supported by booming equity and corporate debt markets, and increasingly sanguine expectations of these positive developments to be sustained. Moreover, domestic competitors (state-owned or privately owned) were still not very competitive. During that period of time foreign banks were entering the Russian and other CIS markets, and anchored their presence by so-called “boutique-type” models, characterised by a low number of branches and cherry-picking of customers, both in corporate and retail banking. Another factor was that at this stage, all foreign banks in the market had entered and operated under their own brand names. At that time their business behaviour looked rather like market testing. The first experience of most market entrants was by and large positive, due to their ability to generate sufficient and cheap local funding as well as competitive advantages in banking know-how versus local rivals. Huge success and windfall profits during the first phase of Western banks' penetration into Russia and CIS banking markets perhaps diverted the attention away from risks. Hence, the Western banks' expansion in Russia and other Western CIS markets accelerated. Its second phase was characterised by a switch from limited and organic growth, to very rapid acquisition-driven growth and attempts to gain market share over and above that of the nearest competitors. Such strategies dominated the period from 2004-2007/2008 and the major examples of acquisitions and expansion in the Russian or Ukrainian market were the following: Societe Generale – Rosbank (Russia); Raiffeisenbank – Impex Bank (Russia) and Aval (Ukraine); UniCredit – full rebranding of International Moscow Bank (Russia) and acquisition of Ukrsotsbank (Ukraine), BNP Paribas acquisition of Ukrsibbank (Ukraine). Within this period of time, the major Western players in the Russian and CIS markets were aggressively growing (most acquisitions carried out during this period finally caused then some write-offs). However, previously purchased local banks were often seriously flawed with inefficiencies and inferior management practices before the acquisition. Hence, large investments were required for the adjustment of their business practices and business ethics towards Western banking standards. Moreover, the increasing market power of state-owned, state-near and locally owned domestic competitors as well as their growing sophistication forced some Western banks to go down the credit quality/rating scale to acquire a sufficient critical mass for their enlarged franchises. As a result more and more credit quality risks had been accumulated. The last and seemingly desperate attempt to revive the profits of the past was an excessive consumer lending boom during

2010-2013 on the Russian market. However, that story has ended more or less the same way – the previously high-margin business opportunities bumped into abruptly escalated credit risks. That said it is no surprise that the developments in 2013-2014, have provoked a straightforward and fairly justifiable decision by most Western players in Russia and also Western CIS markets – rescaling and in some cases even contraction or market exit.

3. Which risks had been underestimated in Western CIS markets?

In retrospect it is obvious that expectations of Western (European) banks regarding banking markets in the Western CIS countries (including Russia) had been too optimistic. By and large the following constraints for a sustainable long-term economic and banking sector development in Western CIS countries and Russia had been underestimated:

- Characteristics of typical emerging market economies (including damaging economic policies, corruption)
- Lack of institutional progress, investment climate improvement, protection of property rights
- Existence of market distortions and non-transparent practices in the corporate sector and banking sector

In the following those dimensions of over-optimistic expectations are discussed in more detail and an attempt is made to explain the past Russia/Western CIS optimism.

3.1. Characteristics of typical emerging markets

The Western CIS countries and Russia have to be considered as classic emerging markets in terms of their economic structures, their overall degree of macroeconomic volatility (especially the Russian economy is characterised by the highest macroeconomic volatility among major emerging markets) and macro-financial vulnerabilities. This fact was clearly misjudged by a lot of Western players that entered those markets in the boom phase from 2000-2008. Underestimation of emerging market risks is of special importance for long-term banking sector trends. There is empirical evidence that loan-to-GDP ratios tend to be lower for emerging markets compared to more mature markets (also like in more mature CE/SEE markets) due to a complex mix of distinguishing factors (e.g. lower accumulated wealth levels, higher share of shadow economy, less mature financial markets, large urban-rural gaps, lack of credit bureau infrastructure etc.). That said and from a purely economic perspective the belief that the banking sector size and maturity in Russia and Western CIS countries may reach the same levels as in some of the more mature CE and partially SEE countries (e.g. that loan-to-GDP ratios may reach levels like in CE/SEE) was overoptimistic. Moreover, it has to be added that the macroeconomic recovery seen in Russia, Ukraine and Kazakhstan starting from 2000 on, was partially supported by a disappointing previous decade.

Developments prior to the global financial crisis in 2008/2009, but also over the last few years have shown that Russia and some Western CIS countries followed very damaging and pro-cyclical economic policies. This risk was possibly underestimated by major foreign investors in the region (including major Western banks). For instance Russia never made any meaningful progress in diversifying its economy and privatisation targets had always been missed. De facto there was even an increase in the state-influence in major economic sectors (including banking) over the last few years. Moreover, the Russian economy became more and more addicted to high and ever increasing energy prices. In case of Ukraine and Belarus it is obvious that both countries followed a combination of harmful exchange rate, fiscal and banking sector policies prior to the global financial crisis as well as in the following years. Such unsustainable economic policies increase the risk of large and negative external liquidity and economic shocks – a factor that had been underestimated by major foreign investors (including Western banks active in Russia and the Western CIS countries). The willingness to follow unsustainable economic policies – that may still serve some vested interests in a given country, but not the country as a whole – is also mirrored in the unwillingness or inability to follow IMF-led stabilisation and reform packages in countries such as Ukraine or Belarus. In contrast to a more reforming Ukraine, Belarus opted for an increasing reliance on Russian support, a move that was also linked to increasing economic influence in the respective economies (also in the banking sectors with increasing influence of Russian-owned banks in Ukraine and Belarus).

Likewise and in contrast to more developed markets the risk of strongly negative developments, with low recovery possibilities, is much larger in emerging economies like Russia or other CIS countries in case of a negative domestic or external financial shocks. The key point here is the lack of solid and tested banking and monetary sector regulation, coupled with the absence of valid stabilisation tools and smoothing policies. The reasons for that are derived straight from the CIS markets' emerging nature: unsustainable economic growth, resting on speculative factors; absence of valid monetary policy instruments; low trust of population into the banking sector and easily-orchestrated banking panics; weak legislative base with low protection of banks' funding side (deposits are de-facto mostly on-call, for example), extremely sensitive and volatile exchange rates, and as a result a higher probability of systemic risks. Moreover, the 2007-2009 economic and financial downfalls in Russia or Ukraine were more of a spillover from international markets and respectively were largely heeled by the stabilisation of those in the end. In contrast, the current development in Russia and CIS is endangered by the fact that the countries have to cope with the hardships by themselves, not only without help, but also with certain counteractions by the international community (e.g. sanctions against Russia). Consequently, it is quite difficult to estimate possible losses that can emerge from this situation; likewise, it is hard to project the length of the weak development.

3.2. Lack of institutional progress, existence of market distortions in the corporate and banking sector

Despite all macroeconomic stabilisation and advances in the period from 2000-2008, not much institutional progress could be observed in Russia and the Western CIS countries. Institutional weaknesses played out in a very harmful way once the boom times ended in Russia and the Western CIS countries. For instance, Western banks faced huge collateral problems in markets such as Ukraine or Kazakhstan. Furthermore, the resolution of non-performing loans turned out to be very challenging due to malfunctioning judicial systems. Moreover, the lack of institutional progress, high corruption and less and less fit to the more liberal economic models pursued in Western Europe and parts of CE/SEE finally resulted in increasing isolationist economic policies in Russia and some Western CIS countries. This policy turn in Russia and Western CIS countries implies cumbersome drawbacks for foreign investors (including major

Western banks). Firstly, this development increased the risk of major disruptions (like in Ukraine) and eventually political, economic and financial sanctions (like in Russia or Belarus). Secondly, the lack of institutional progress resulted in a low willingness in the Western world to actually provide support in case of a stress scenario. Thirdly, the lack of institutional progress also resulted in increasing commercial, reputational and legal risks for Western banks operating in Russia and Western CIS countries. Therefore, shareholder and stakeholder support for aggressive business strategies in the region has been decreasing over time, with a boost in most recent years.

The developments during the global financial crisis and in most recent years have also shown that the existence of market distortions and non-transparent practices in the banking and corporate sector had been underestimated by foreign investors active in Russia and Western CIS countries. For instance, investors that had either acquired locally-owned banks in Russia or Western CIS countries or had tried to participate in the market via (minority) participations finally faced a lot of negative and unexpected experiences. Some Western banks had difficulties in establishing proper governance structures within local banks they had acquired (as a majority or minority shareholder). Moreover, the impact from multifaceted and non-transparent conflicts within complex share- and stakeholder structures had been underestimated. With regards to complex and non-transparent corporate governance and stakeholder practices it has to be added that some negative high-profile topics popped up in the banking sectors of Russia, Ukraine and Kazakhstan in recent years (e.g. serial defaults of Kazakh Bank TuranAlem with international repercussion, Bank of Moscow failure in 2011, non-transparent and dubious banking sector restructuring in Ukraine in 2009, failure of the fourth largest bank in Ukraine, Deltabank, in 2015). On top of the sketched ownership problems the negative and market distorting effects resulting from the strong presence of state-owned and state-connected banks as well as smaller or larger oligarchic banks (with business models strongly geared towards related party lending) on the overall banking market had been underestimated as well. This is of high relevance as the share of state-owned banks was on a trend increase in major Western CIS markets over the last few years, while the influence of Russian state-owned banks outside of their home market was on the rise as well. Such an underestimation of distorted competition is not specific to the Russian market, e.g. there is evidence that Western banks also underestimated the negative influence of large state-owned and state-near banks on their own business prospects in a country such as China. In light of all factors sketched above it is no surprise that there were several market exits of Western banks out of minority shareholder positions in the Western CIS markets and even larger participations or 100%-owned subsidiaries were being sold out over the last few years. In addition, a lot of representative offices of Western banks (that can lay the base for a later market entry) were closed in Russia and the Western CIS region in recent years. Interestingly most divestment transactions by Western banks in Russia and Western CIS markets involved a locally-owned buyer, which indicates limited interest of foreigners still present to increase their gearing towards Russia and the Western CIS countries. In contrast a lot of divestment transactions by Western European banks seen in other CE/SEE markets (e.g. in Poland, Romania) in recent years involved other Western European banks on the buyer side.

3.3. How to explain the past Russia/Western CIS optimism?

It seems that a complex mix of various factors supported the risk underestimation seen in Western CIS countries and Russia. Firstly, a lot of Western European banks that entered were unexperienced in emerging market settings. Local business partners (in banking alliances or bank clients) were partially exploiting this feature during the strong upcycle seen from 2000-2008. Secondly, expectations regarding the long-term business prospects in Russia and Western CIS countries had been too optimistic, as simple comparisons made to the initial success of some Western banks during their expansion to CE/SEE. The push to Russia and other CIS markets was based on the solid belief that those countries have entered a path of building up democratic political systems and are moving towards market-based capitalism. That said it was not fully realized that the success of Western European banks on CE/SEE markets was driven by very specific political and economic catching-up and during a period of very supportive global economic and financial conditions that could not be repeated easily elsewhere. Moreover, the initial success during the CE/SEE expansion contributed to (management) overconfidence at Western CEE banks, e.g. in terms of their steering/management and trough-the-cycle earnings capabilities in challenging CIS markets. Moreover, rivalries among leading Western CEE banks also contributed to an overshooting in terms of the CEE expansion. Furthermore, Western banks were attracted by a certain fundamental banking sector under penetration in Russia and in the Western CIS markets, without questioning the reasons why regional banking markets were underdeveloped compared to peers (also outside of the CE/SEE context). Nevertheless, there are also other factors which explain the push of Western European banks into Russia and Western CIS markets, which are not per se linked to overconfidence. Western Europe is still the major trading partner for Western CIS countries and a major investor there, i.e. there is a lot of viable commercial bank business to be done with Western CIS countries. However, for such business no big local presence is required. Yet what is more important, Western European banks tend to be more international than US banks or other emerging market banks (e.g. due to the small size of European bank markets and strong global European trade linkages). Further it should be noted that in case of Russia the entry and positioning of Western European banks was seen less critical by local authorities than a situation with large US banks having a strong position in the local banking market.

4. Western banks rolling back expansion to Western CIS countries – no near-term replacement by other foreign-owned banks

Major Western CEE banks scaled down their on-shore exposures in Western CIS countries and Russia significantly over the last few years. This holds especially true for retail and commercial banking business, which require more capital and risk exposure locally (i.e. inside Western CIS jurisdictions) than pure international investment banking. There were also several outright market exits of institutions which entered the markets very late in a boom phase or which had too optimistic expectations with regards to their ability to withstand distorted competition. Moreover, cross-border banking exposures of Western banks to the region (which also include interbank lending, trade finance etc.) are shrinking substantially due to the deterioration of the regional economic outlook, external trade, increasing financial market risks etc. On top of that there is a trend at international investment banks of scaling down their staff and presence in the large Russian market. This trend can mostly be attributed to subdued growth prospects, distorted competition and limited business opportunities within an environment of Western financial sanctions. Some dedicated Western CEE lenders, which are pursuing a long-term regional strategy, also decided to either cut or reduce their exposures in Russia and or Western CIS countries. Given the sketched market trends the footprint of state-owned and state-near banks in the Russian market is set to rise (most likely above 60% of total), a trend that may further dilute best-practice banking in the domestic market.

Despite first initial moves a few very dedicated Western CEE banks might be still more reluctant to cut their exposures in Russia and Western CIS countries compared to the market average, betting on possible rewards in transactions with state-owned or state-near institutions once the current situation calms (a strategy that paid off following the 1998/1999 crisis). Leading Western banks on the Russian market (French Societe Generale, Italian UniCredit, Austrian Raiffeisen and US-based Citi) have issued various statements in recent months that they remain committed to their business. However, with regards to the broader market outlook more cautious business strategies of Western banks in Western CIS countries and Russia are likely to dominate in the years to come and this holds true for the leading Western banks as well. Firstly, expectations regarding the long-term economic development in the Western CIS markets and Russia had been far too optimistic and were sharply reversed in previous years. Moreover, economic, financial and legal risks that unfolded in recent years and are reflected in sanctions, weak currencies, lower country risk ratings and higher country risk premia are unlikely to fully reverse in the coming years. Secondly, a risk management approach dominates with regards to exposures in the CIS region at Western European banks at present. Hence some still feasible business opportunities could be missed going forward. Thirdly, a lot of damage has been done in view of investor confidence. This holds especially true in case of Russia; although Russia is likely to remain an important market for selected Western banks. From an economic policy perspective it seems that political hardliners are having a stronger influence on actual Russian policymaking than more market-oriented actors. Or in other words: reform orientated (economic) liberals seem to be politically weaker than assessed by some external observers. Moreover, given the current harsh Russian positioning in international policies it seems likely that Russia's relations with the West will be burdened for a longer period of time. Therefore, in economic and financial terms it seems likely that the EU-Russian relations (e.g. as measured in growth of bilateral exchange in goods, growth of investments and financing etc.) in absolute as well as in relative terms may have peaked. Therefore, a cautious business strategy of Western banks active in Russia and Western CIS countries is currently being requested by shareholders, regulators etc. Moreover, a certain pro-cyclical development (such as seen in the previous upcycle) is likely to be visible in the years to come. Hence, many Western banks with a still sizeable presence in Russia and Western CIS markets may return to the "boutique-style" business model that they followed during their initial phase of market entry (which implies less risk and deep local embeddedness). Nevertheless, it has to be mentioned that some market exits in Western CIS countries and Russia or ongoing restructurings can also be explained by a global trend of cutting more risky and/or less profitable foreign operations at Western banks. This trend was particularly strong at Western European banks. Given the leading role of Western European banks in Russia and the Western CIS countries the impact of this global trend was particularly felt there. Some institutions either had to fix their capitalisation needs in recent years (e.g. Raiffeisen, partially UniCredit) or were forced to trim their international footprint in exchange for state-support (e.g. Commerzbank, KBC, Volksbank International, WestLB). Furthermore, from a longer term perspective the Russian banking market seems to be a market where banks are entering and exiting more actively than in other and/or mature CEE markets anyways.

Currently, there is excitement in Russia about a turn to Asian markets, also in finance. Hence a major question will be to what extent Asian/Chinese banks are ready and willing to compensate for more conservative strategies of Western (European) banks in Russia. However, in Russia Chinese banks are still niche players compared to their Western (European) counterparts (the assets of the leading Chinese banks in Russia are at around 2-3% of the assets base of the leading Western banks), while Western (European) banks are still dominating the list of large and complex global financial institutions. Moreover, we see limitations in circumventing EU and US banks. Although EU and USA cannot prevent non-EU and or non-US entities to lend to sanctioned companies, it will be hard to circumvent US or EU banks for large transactions on a sustained basis. Moreover, we also see certain limits for Asian and Arab investors in boosting their Russia exposures very significantly within in a short-period of time due to risk management and reputational considerations (including legal and compliance regulations).

5. Appendix

Table 1: Market exits/divestments

Market exits/divestment of Western banks in Russia and other Western CIS markets (Russia, Ukraine, Kazakhstan, Belarus)		
Country/Year	**Parties involved in the transaction**	
Russia	**Seller (Country of headquarters)**	**Buyer**
2010	MorganStanley (Commercial banking, mortgage bank)	Orient Express Bank linked to Russian businessman Igor Kim
2010	Santander (Commercial banking, retail banking)	Orient Express Bank linked to Russian businessman Igor Kim
2011/2012	Commerzbank selling stake in Promsvyazbank	
2011	Rabobank	Bank have back its licence
2011	Barclay	Local Expobank, linked to Russian businessman Igor Kim
2011	HSBC	Closure of retail announced
2012	KBC	Local consortium
2012	WestLB	Local Expobank, linked to Russian businessman Igor Kim
2013	GE Money Bank (US)	Sovcombank, locally-owned
2013	Deutsche Bank selling UFG asset management	Local Aton capital, linked to Russian business man Yevgeny Yuryev.
2014	Blackrock announced market exit	
Market strategies, potential market transactions/exits		
Intesa considers small subsidiary as non-core, divestment cannot be ruled out		
Raiffeisen has announced to cut Russian exposure by some 20% in the years to come, the first branches had been already closed in the so-called "Far East", presence in some 20 larger cities might be reduced		
Societe Generale announced much more cautious market strategy, especially with regards to cross-border funding		
Ukraine	**Seller**	**Buyer**
2009	Home Credit Bank (CZ)	Local Platinum Bank
2010	Dresdner Bank	Closure Representative Office
2010	Renaissance Credit (RU)	SCM, linked to Ukrainian businessman Rinat Akhmetov
2011	HSBC	Closure Representative Office
2011	Bayerische Landesbank	Closure Representative Office
2011	Kookmin Bank (KR)	Closure Representative Office
2011	Conversbank (RU)	Local Ukrainian investors
2012	Bank of Georgia	Local Ukrainian investors
2012	Volksbank International (AT)	Sberbank
2012	SEB Bank (SE)	Fidobank, locally-owned bank
2012	Commerzbank (Bank Forum)	Locally-owned holding, consortium
2012	Societe Generale (Profin Bank)	Alfa-Bank (RU)
2013	Erste Bank (AT)	Fidobank, locally-owned bank
2013	Swedbank (AT)	Deltabank, locally-owned bank
2013	Alpha Bank (GR)	Deltabank, locally-owned bank
Market strategies, potential market transactions/exits		
Raiffeisen Bank Aval (AT), planned sale in 2013 did not materialise due to economic/security situation in Ukraine, now substantial downsizing is on the agenda, assets might be cut by some 30%, Raiffeisen is looking to partner with EBRD in Ukraine		
UniCredit announced the intention to exit the market if conditions allow for such a divestment		
Kazakhstan	**Seller**	**Buyer**
2006	Raiffeisen selling minority stake in TuranAlem	
2013	UniCredit sells ATF bank	Consortium around Kazakh businessman firm owned by Kazakhstan businessman Galimzhan Yesenov
2014	HSBC (after acquiring RBS business in Kazakhstan in 2010)	Biggest local lender Halyk Bank
Belarus	**Seller**	**Buyer**
2012	Belarusbank (subsidiary of Rosbank, owned by	Alfa Bank (RU)

	French Societe Generale)	
Market strategies, potential market transactions/exits		
Priorbank (Raiffeisen Bank International) may cut assets by some 20%, i.e. the market share of the only larger Western foreign-owned bank will decrease substantially going forward		

Source: Media, individual banks, Raiffeisen RESEARCH

Table 2: Market shares Western European banks: Regional CIS exposures (Russia, other Western CIS countries) and overall CIS share in emerging market exposures

	1999	Peak 2008-2010	2014
Russia (% of total CIS)	97	77	88
Other Western CIS (% of total CIS)*	3	23	12
Russia + other Western CIS (% of global cross-border emerging markets exposure)	6.0	8.3	5.6

* Other Western CIS: Ukraine, Belarus, Kazakhstan

Source: company data, Raiffeisen RESEARCH CEE Banking Reports, Bank of International Settlements

Table 3: Upscaling of Western European banks in Russia: From a "boutique-style model" to a "larger domestic player model"*

	2004	2013
Total assets (EUR bn)	5.4	54.7
Number of branches	99	930

* Largest three Western European banks Societe Generale, UniCredit, Raiffeisen on the Russian market

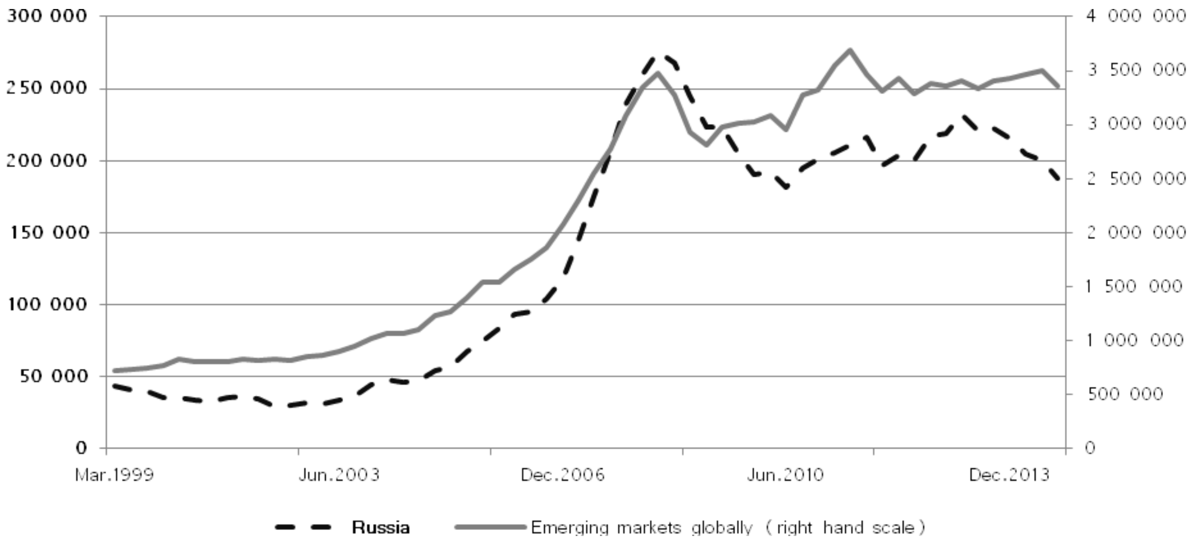
Source: company data, Raiffeisen RESEARCH CEE Banking Reports

Table 4: Western CIS countries banking markets compared to CE and SEE

Loan-to-GDP ratios (%)	**1999**	**2009**	**2013**
Central Europe (CE)	38	61	58
Southeastern Europe (SEE)	11	56	51
Western CIS markets	11	56	51
Russia	12	42	49
Banking profitability (Return on Equity, %)	**Average 2000-2008**		**2009-2013**
Central Europe (CE)	17.1		12.4
Southeastern Europe (SEE)	12.3		2.0
Western CIS markets	17.3		12
Russia	18.3		13.6

Source: national central banks, Raiffeisen RESEARCH CEE Banking Reports

Graph 1: Cross-border banking exposure Western European banks (USD million)



Source: Bank of International Settlements

Table 5: Market shares Russian banking market, leading Western banks vs. largest Chinese/Indian banks (2014)

Market position	Bank (Country of headquarters)	Net assets (RUB thousands)
10	UniCredit (IT)	1384673921
12	Rosbank (Societe Generale, FR)	983627067
13	Raiffeisen (AT)	890907411
24	Citibank (US)	400472851
94	Industrial and Commercial Bank of China (CN)	61260538
132	Bank of China (CN)	38191401
374	ICICI Bank Eurasia (IN)	5393499

Source: national sources, individual banks, Raiffeisen RESEARCH

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