Credit Opinion: GarantiBank International N.V.

GarantiBank International N.V.

Amsterdam, Netherlands

Ratings

Category	Moody's Rating
Outlook	Stable
Bank Deposits	A3/P-2
Bank Financial Strength	C
Subordinate -Dom Curr	Baa1
Parent: Turkiye Garanti Bankasi AS	
Outlook	Stable
Bank Deposits -Fgn Curr	B1/NP
Bank Deposits -Dom Curr	A3/P-2
Bank Financial Strength	C-

Contacts

Analyst	Phone
Edward Vincent/London	44.20.7772.5454
Lynn Exton/London	
Adel Satel/London	

Key Indicators

GarantiBank International N.V.

	[1]**2006**	**2005**	**2004**	**2003**	**2002**	**Avg.**
Total assets (EUR billion)	**2.62**	**2.28**	**1.91**	**1.76**	**1.52**	[2]**11.47**
Total capital (EUR billion)	**0.26**	**0.21**	**0.21**	**0.20**	**0.18**	[2]**6.32**
Return on average assets	**1.01**	**0.99**	**1.26**	**1.06**	**0.86**	**1.04**
Recurring earnings power [3]	**1.58**	**1.59**	**1.79**	**1.67**	**1.51**	**1.63**
Net interest margin	**1.57**	**1.86**	**1.98**	**1.89**	**1.90**	**1.84**
Cost/income ratio (%)	**43.16**	**45.52**	**44.44**	**51.01**	**56.30**	**48.08**
Problem loans % gross loans	**0.26**	**0.21**	**0.65**	**0.77**	**1.46**	**0.67**
Tier 1 ratio (%)	**10.70**	**14.00**	**17.39**	**19.23**	**19.14**	**16.09**

[1] As of December 31. [2] Compound annual growth rate. [3] Preprovision income % average assets.

Opinion

SUMMARY RATING RATIONALE

The Bank Financial Strength Rating (BFSR) of C assigned to GarantiBank International N.V. (GBI) reflects its role as a niche player in the competitive segment of international trade finance, its strong financial fundamentals and asset quality, historically low credit losses, a reliable funding profile and solid profitability, while also taking into consideration GBI's exposure to emerging markets, particularly the risk of the Turkish market.

GBI's deposit ratings of A3/Prime-2 do not at present incorporate any likelihood of support from its parent in the event of distress, but are standalone ratings mapped from the BFSR of C. GBI is a 100% owned subsidiary of Türkiye Garanti Bankasi A.S. (Garanti, rated A3/P-2/D+ domestic currency and B1/NP foreign currency). GE Consumer Finance, a subsidiary of GE Capital Corporation (Aaa/P-1), is a key strategic shareholder in Garanti, through a 25.5% interest it has pooled in a voting block with a 25.9% interest held by the Dogus Group of Turkey. Given Moody's assessments of the probability of support for GBI and the default dependence, GBI's ratings cannot enjoy any uplift from the B1 foreign currency rating of Garanti, which is constrained by the country ceiling for Turkey.

Credit Strengths

These include:

- An established franchise with a good competitive position - albeit in the relatively narrow niche of trade finance

- Consistent revenue generation and profitability, mainly built on know-how relating to trade finance risk-taking in emerging markets

- Solid asset quality and capitalisation

- Operational independence to date from parent bank in Turkey

- Scope for ongoing operational support from new key shareholder in parent bank.

Credit Challenges

These include:

-- Limited earnings diversification

-- Meaningful - although diminishing - related-party exposures

-- Significant - albeit reduced - exposure to Turkey (36% of risk-weighted assets) and to other emerging markets, which could impact negatively upon financial performance

-- Existence of some risk concentrations - in terms of counterparties and Turkish sovereign bonds - despite low risk costs and low impaired loan ratios.

Rating Outlook

The stable outlook on GBI's BFSR reflects Moody's expectation that the bank's business and operating model should continue to deliver reasonable pre-provision profitability, restrained risk costs and problem loans and thus an impressive degree of internal capital generation. This outlook also assumes that the current strategy will prevail - namely, continued growth through GBI's proven core strengths in trade finance and private banking, gradual establishment of physical presences in a number of targeted countries and increasing diversification and reducing the proportion of exposure to Turkey.

What Could Change the Rating - Up

Factors which would likely exert upward pressure on the BFSR include:

-- A clear demonstration of diversification sufficient to mitigate for generalised event risks affecting groups of emerging markets - through the increased contribution of private banking profits and/or through geographic expansion of trade finance activities

-- A reduction in individual borrower and sector risk concentrations and related-party exposures

-- Internal capital generation sufficient to ensure a high level of Tier I - driven surplus above bespoke regulatory capital requirements following the transition to the Basel II regulatory regime

-- Improvements in risk-adjusted profitability ratios sustaining beyond the transition to the Basel II regulatory regime

An upgrade of the foreign currency deposit rating of Garanti (which could in turn arise if the foreign currency deposit ceiling of Turkey is raised) could lead to an upgrade in GBI's deposit rating independently of an upgrade in GBI's BFSR.

What Could Change the Rating - Down

Factors which would likely exert downward pressure on the BFSR and deposit ratings include:

-- Deterioration in surplus above bespoke regulatory capital requirements following the transition to the Basel II regulatory regime

-- Deterioration in risk-adjusted profitability ratios sustaining beyond the transition to the Basel II regulatory regime

-- An evident deterioration in credit underwriting conditions or standards in trade finance leading to an increased cost of credit risk and/or deterioration in asset quality

-- Significant increase in the ratio of lending to parent or related parties as a percentage of tier I capital

-- Increased dependence on trading revenues and the resulting higher market risk appetite

-- Changes in ownership and/or strategy.

Recent Results and Developments

For the full year 2006, consolidated net profit increased from EUR20.7 million to EUR24.7 million with consolidated pre-provision profit rising from EUR33.4 million in 2005 to EUR38.7 million in 2006. GBI's total consolidated assets increased from EUR2280 million at 31 December 2005 to EUR2624 million at 31 December 2006, with shareholders' funds rising from EUR174 million to EUR183 million.

DETAILED RATING CONSIDERATIONS

Detailed considerations for GBI's currently assigned ratings are as follows:

Bank Financial Strength Rating

Moody's has assigned a C BFSR to GBI, versus the C+ rating generated by Moody's bank financial strength rating scorecard. Moody's believes the C rating is an appropriate measure of the bank's financial strength given the geographic mix of earnings and assets (which would be accurately reflected in an adjusted operating environment score), the more limited surplus of regulatory capital above bespoke regulatory requirements than would appear from the "headline" capital adequacy ratios, the likely pressure on capital adequacy ratios arising from the forthcoming change to a Basel-II based regime and the related pressure on risk-adjusted profitability ratios.

Moody's BFSR scorecard outcome was positively affected by GBI's strong quantitative indicators, yielding A scores for profitability, capital adequacy and efficiency. Scores for controls, liquidity and market risk appetite and regulatory environment were reasonable, while the overall outcome was weighed down by the scores for market share and sustainability, earnings stability and diversification, the significant - albeit diminishing - level of related-party loans to Tier I capital and credit risk concentrations.

QUALITATIVE RATING FACTORS (50% WEIGHTING)

FACTOR 1: FRANCHISE VALUE

Trend: Improving

GBI is a Netherlands-based niche commercial bank specialising in trade finance. It has two core customer franchise units: (1) International Trade Finance; and (2) Private Banking. The activities of these two business units are supported and augmented in revenues by a treasury unit and by direct retail banking deposit-taking.

The overall franchise value score of D is in part due to low sub-factor scores for earnings stability / diversification and for market share and sustainability which reflect the bank's narrow niche presence. Trade finance accounts for 62% of revenues, whilst treasury - including the spread from direct retail deposit-taking activities - and private banking account for 22% and 16%, respectively. The key trade finance business - despite having well-established and efficient processes and a client franchise that has proven to be durable - nevertheless has a limited (albeit growing) presence outside the relatively narrow niche of trade finance related to Turkey. However, the franchise value score is likely to be improving through the increased contribution of private banking and greater geographical diversification, a trend that we see continuing in 2007.

FACTOR 2: RISK POSITIONING

Trend: Improving

GBI's overall score of D- for risk positioning is in part due to low scores for related-party risks, borrower concentration and risk governance structures.

Related-party exposures amount to 34% of Tier I capital, although this has fallen significantly from a high of EUR 524 million at end-2000 to EUR 55 million at end-2006 and the reduction has been a secular trend since then. On credit risk concentration, there are some significant large exposures, with the top 20 corporate loans amounting to over 200% of Tier I capital. Largest exposures to emerging market-based banks also aggregate to a level above this threshold. The Turkish sovereign bond exposure has also been important in terms of concentration risks, though this has been falling over time.

Weak scores for the risk management and financial disclosure sub-factors arise from a rigorous interpretation of Moody's BFSR methodology criteria - the key considerations here are (i) the lack of a formal role for the supervisory board in risk appetite-setting, (ii) the fact that reporting on doubtful loans and/or NPLs (which are at low levels) to internal governance structures and externally appear not to be to international standards and (iii) the absence of a veto-empowered role of chief risk officer. However, Moody's notes that the bank has advanced credit monitoring processes and practices and a very tight credit selection, which would be reflected in an adjusted score. In general, the control culture appears to be very tight, which results in an extremely strong score for the controls sub-factor. Turkish and other sovereign bond position risks are limited not only by nominal limits applying to the trading and investment books but also through tighter currency position risks aimed at minimising outright currency mismatches.

Liquidity risk management appears prudent, with the bank being able to use the experience of the crisis affecting Turkey in 2000 and 2001, during which the retail deposits from Germany and the Netherlands proved sticky, in order to determine the size of a liquidity reserve and the extent of bilateral facilities - the latter has been diversified and is regularly tested for availability while the subordinated bond issuance has also added to funding diversification.

FACTOR 3: REGULATORY ENVIRONMENT

All banks in the Netherlands are subject to the same score on the regulatory environment, which Moody's considers to be supportive of Netherlands-based banks' creditworthiness. This factor does not address bank-specific issues; instead, it evaluates whether or not regulatory bodies are independent and credible, demonstrate enforcement powers and adhere to global standards of best practices for risk control.

FACTOR 4: OPERATING ENVIRONMENT

Trend: Neutral

The unadjusted factor of A- shown on the scorecard applies to all Netherlands-based banks. However, an adjusted score for operating environment that is based on the estimated weighted average of the scores for the countries that account for GBI's assets and revenues is D+.

QUANTITATIVE RATING FACTORS (50% WEIGHTING)

FACTOR 5: PROFITABILITY

Trend: Weakening

With a risk-weighted recurring earning power ratio of 2.99% in 2006, GBI's risk-adjusted pre-provisions profitability is excellent, reflecting the relatively higher margin of structured and trade finance businesses and the spreads on Turkish government bonds. In accounting terms, the revenue mix in 2006 was broadly similar to that prevailing in full years 2005 and 2004, with interest income representing ca. 55% of operating income, fee and commission income 30% (mostly from non-volatile activities) and trading profit 15%. However, this ratio has been declining due to pressure on margins arising from strong competition and lower yields on Turkish securities. Risk-weighted assets (RWAs) have been rising faster than revenue, and this could be exacerbated by the impact of the transition to a Basel II-based regulatory regime, after which Turkish sovereign exposures and interbank exposures will no longer benefit from the respective 0% and 20% weightings applied to all OECD member state exposures under Basel I (although some of the impact may be offset by the possible abolition of the country add-on for Turkey applied by the Dutch regulator).

The same pressures apply to the ratio of net income to risk-weighted assets, which was 1.91% in 2006, compared to 2.74% in 2004. Considering the current market conditions, Moody's sees the profitability continuing to be pressurised in 2007.

In Moody's view, the adjusted profitability score should be viewed as C+ compared to the unadjusted B+.

FACTOR 6: LIQUIDITY

Trend: Neutral

GBI has an extremely strong liquidity ratio as measured by the extent to which market funds are exceeded by liquid assets, expressed as a percentage of total assets - this arises from the weight of deposits gathered through the resilient direct retail deposit base. The ratio (one where a negative sign reflects stronger liquidity) has declined from -48% in 2004 to -30% in 2006 as a result of the bank choosing to have deposit rates no longer at the top end of "best buy" tables for direct deposits, given (i) excess liquidity and (ii) less attractive reinvestment yields in relation to the top rates.

The overall liquidity score of B- reflects the combination of the score of A for the liquidity ratio and the C score for liquidity management.

FACTOR 7: CAPITAL ADEQUACY

Trend: Neutral

GBI's extremely strong capital adequacy ratios have been declining in 2005 and 2006 but remain within the A range (Tier I was 17.4% in 2004, 14.0% in 2005, 10.7% in 2006, while tangible common equity to risk-weighted assets was 17.4%, 16.1% and 12.75% for those years respectively).

However, Moody's considers an adjusted score of C+ to be more appropriate reflecting the following considerations: (i) the higher bespoke requirements of the Dutch regulator for the minimum capital ratios applicable to GBI and similar banks, implying that the "headroom" over the regulatory requirement is not as high as would appear; (ii) the likely increase in RWAs as calculated under Basel II arising from the fact that Turkish interbank and sovereign exposures no longer benefit from the current favourable treatment of Turkey (20% for interbank, 0% for sovereign) on the grounds that it is an OECD country; (iii) rapid growth in RWAs under the current basis of calculation, which weighs on the capital adequacy score; and (iv) the forthcoming operational risk charge, which also weighs on the capital adequacy score.

In addition, we note that GBI has made important efforts as regard to timing of the Basel II implementation as well as the adoption of the IRB approach on the Credit Risk calculation. GBI also opted for the Standardized approach for the market risk and for the Basic Indicator approach as regard to the Operational risk.

That said, Moody's also notes that GBI has been taking measures to bolster capital adequacy, in particular by forgoing the payment of a dividend to the parent in 2007 for the account of financial year 2006, and will be monitoring the development of capital adequacy ratios closely, especially in view of the recent market conditions.

FACTOR 8: EFFICIENCY

Trend: Improving

GBI has benefited from scale efficiencies in processing trade finance while at the same time management has maintained a strict control on expenses in recent years, resulting in a significant improvement in efficiency ratios. Moody's sees this trend to be confirmed in 2007.

FACTOR 9: ASSET QUALITY

Trend: Improving

Extremely tight credit selection, based in particular on a dual counterparty risk and transaction risk scoring system and "intelligent" systems driving this process, has contributed to extremely low credit losses. The ratios have improved partly as a result of the bank's withdrawal from consumer finance in 2004.

Global Local Currency Deposit Rating (Joint Default Analysis)

GBI's global local currency deposit ratings of A3/Prime-2 do not at present incorporate any likelihood of support from its parent in the event of distress, but are standalone ratings mapped from the BFSR of C. GBI is a 100% owned subsidiary of Türkiye Garanti Bankasi A.S. (Garanti, rated A3/P-2/D+ domestic currency and B1/NP foreign currency). GE Consumer Finance, a subsidiary of GE Capital Corporation (Aaa/P-1), is a key strategic shareholder in Garanti, through a 25.5% interest it has pooled in a voting block with a 25.9% interest held by the Dogus Group of Turkey. Given Moody's assessments of the probability of support probability (90%) and the default dependence (100%), GBI's ratings cannot enjoy any uplift from the B1 foreign currency rating of Garanti, which is constrained by Turkey's country ceiling. Moody's views the probability of systemic support for GBI and similar Netherlands-based banks as zero.

Notching Considerations

Ratings for GBI's junior obligations should be notched off the fully supported deposit rating, or GBI's global local currency deposit rating, because Moody's believes that there is no legal authority mechanism in place for the Netherlands bank regulators to impose losses on subordinated creditors outside of a liquidation scenario. Thus, Moody's assigns a Baa1 local currency debt rating for subordinated debentures issued by GBI.

Foreign Currency Deposit Rating

As with the local currency deposit ratings, GBI's foreign currency deposit ratings of A3/Prime-2 do not at present incorporate any likelihood of support from its parent in the event of distress, but are standalone ratings mapped from the BFSR of C. Given Moody's assessments of the probability of support probability and the default dependence, GBI's ratings cannot enjoy any uplift from the B1 foreign currency rating of Garanti, which is constrained by Turkey's country ceiling. Moody's views the probability of systemic support for GBI and similar Netherlands-based banks as zero. Given Moody's assessments of the probability of support probability (90%) and the default dependence (100%), GBI's ratings cannot enjoy any uplift from the B1 foreign currency rating of Garanti, which is constrained by Turkey's country ceiling. Moody's views the probability of systemic support for GBI and similar Netherlands-based banks as zero.

ABOUT MOODY'S BANK RATINGS

Bank Financial Strength Rating

Moody's Bank Financial Strength Ratings (BFSRs) represent Moody's opinion of a bank's intrinsic safety and soundness and, as such, exclude certain external credit risks and credit support elements that are addressed by Moody's Bank Deposit Ratings. BFSRs do not take into account the probability that the bank will receive such external support, nor do they address risks arising from sovereign actions that may interfere with a bank's ability to honour its domestic or foreign currency obligations. Factors considered in the assignment of BFSRs include bank-specific elements such as financial fundamentals, franchise value, and business and asset diversification. Although BFSRs exclude the external factors specified above, they do take into account other risk factors in the bank's operating environment, including the strength and prospective performance of the economy, as well as the structure and relative fragility of the financial system, and the quality of banking regulation and supervision.

Global Local Currency Deposit Rating

A deposit rating, as an opinion of relative credit risk, incorporates the BFSR as well as Moody's opinion of any external support. Specifically, Moody's Bank Deposit Ratings are opinions of a bank's ability to repay punctually its deposit obligations. As such, they are intended to incorporate those aspects of credit risk relevant to the prospective payment performance of rated banks with respect to deposit obligations, which includes: intrinsic financial strength, sovereign transfer risk (in the case of foreign currency deposit ratings), and both implicit and explicit external support elements. Moody's Bank Deposit Ratings do not take into account the benefit of deposit insurance schemes which make payments to depositors, but they do recognize the potential support from schemes that may provide assistance to banks directly.

According to Moody's joint default analysis (JDA) methodology, the global local currency deposit rating of a bank is determined by the incorporation of external elements of support into the bank's baseline credit assessment. In calculating the Global Local Currency Deposit rating for a bank, the JDA methodology also factors in the rating of the support provider, in the form of the local currency deposit ceiling for a country, Moody's assessment of the probability of systemic support for the bank in the event of a stress situation and the degree of dependence between the issuer rating and the Local Currency Deposit Ceiling.

National Scale Rating

National scale ratings are intended primarily for use by domestic investors and are not comparable to Moody's globally applicable ratings; rather they address relative credit risk within a given country. A Aaa rating on Moody's National Scale indicates an issuer or issue with the strongest creditworthiness and the lowest likelihood of credit loss relative to other domestic issuers. National Scale Ratings, therefore, rank domestic issuers relative to each other and not relative to absolute default risks. National ratings isolate systemic risks; they do not address loss expectation associated with systemic events that could affect all issuers, even those that receive the highest ratings on the National Scale.

Foreign Currency Deposit Rating

Moody's ratings on foreign currency bank obligations derive from the bank's local currency rating for the same class of obligation. The implementation of JDA for banks can lead to high local currency ratings for certain banks, which could also produce high foreign currency ratings. Nevertheless, it should be noted that foreign currency deposit ratings are in all cases constrained by the country ceiling for foreign currency bank deposits. This may result in the assignment of a different, and typically lower, rating for the foreign currency deposits relative to the bank's rating for local currency obligations.

Foreign Currency Debt Rating

Foreign currency debt ratings are derived from the bank's local currency debt rating. In a similar way to foreign currency deposit ratings, foreign currency debt ratings may also be constrained by the country ceiling for foreign currency bonds and notes; however, in some cases the ratings on foreign currency debt obligations may be allowed to pierce the foreign currency ceiling. A particular mix of rating factors are taken into consideration in order to assess whether a foreign currency bond rating pierces the country ceiling. They include the issuer's global local currency rating, the foreign currency government bond rating, the country ceiling for bonds and the debt's eligibility to pierce that ceiling.

About Moody's Bank Financial Strength Scorecard

Moody's bank financial strength model (see scorecard below) is a strategic input in the assessment of the financial strength of a bank, used as a key tool by Moody's analysts to ensure consistency of approach across banks and regions. The model 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 Factors

GarantiBank International N.V.

Rating Factors [1]	A	B	C	D	E	Total Score	Trend
Qualitative Factors (50%)						D+	
Factor 1: Franchise Value (20%)						D	Improving
Market Share and Sustainability				x			
Geographical Diversification			x				
Earnings Stability					x		
Earnings Diversification [2]							
Factor 2: Risk Positioning (20%)						D-	Improving
Corporate Governance [2]				x			
- Ownership and Organizational Complexity							
- Key Man Risk							
- Insider and Related-Party Risks				--	--		
Controls and Risk Management			x				
- Risk Management				x			
- Controls	x						
Financial Reporting Transparency				x			
- Global Comparability	x						
- Frequency and Timeliness				x			
- Quality of Financial Information					x		
Credit Risk Concentration	--	--	--	--	--		
- Borrower Concentration	--	--	--	--	--		
- Industry Concentration	--	--	--	--	--		
Liquidity Management			x				
Market Risk Appetite			x				
Factor 4: Operating Environment (5%)						A-	Neutral
Economic Stability	x						
Integrity and Corruption		x					
Legal System	x						
Financial Factors (50%)						B+	
Factor 5: Profitability (7.9%)						B+	Weakening
PPP % Avg RWA		3.35%					
Net Income % Avg RWA	2.20%						
Factor 6: Liquidity (7.9%)						B-	Neutral
(Mkt funds-Liquid Assets) % Total Assets	-38.73%						
Liquidity Management			x				
Factor 7: Capital Adequacy (7.9%)						A	Weakening
Tier 1 ratio (%)	14.03%						
Tangible Common Equity % RWA	14.71%						
Factor 8: Efficiency (3.5%)						A	Improving
Cost/income ratio	44.37%						

Factor 9: Asset Quality (7.9%)						**A**	**Improving**
Problem Loans % Gross Loans	0.37%						
Problem Loans % (Equity + LLR)	1.45%						
Lowest Combined Score (15%)						**B-**	
Economic Insolvency Override						**Neutral**	
Total Scorecard Implied BFSR						**C+**	
Assigned BFSR						**C**	

[1] - Where dashes are shown for a particular factor (or sub-factor), the score is based on non public information
[2] - A blank score under Earnings diversification or Corporate Governance indicates the risk is neutral