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Co. reported 1H16 net profits of RUB263b.

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PRESENTATION

Operator

Ladies and gentlemen, thank you for standing by and welcome to Sberbank Group's 2Q 2016 IFRS results call hosted by Sberbank's management team. Live webcast is available, and you can find the link on Sberbank.com. (Operator Instructions) I must advise you that this conference is being recorded today on Thursday, August 25, 2016.

I would now like to hand the call over to Mr. Jyrki Talvitie. Please go ahead.

Jyrki Talvitie - *Sberbank Rossii PAO - Strategic Partners and Investors*

Thank you very much, and very much welcome from -- on our behalf as well, to the Sberbank Group IFRS results six months of 2016. Today we will have presenting and President Alexander Morozov, Deputy Chairman of the Management Board and CFO; Alexander Vedyakhin, Head of our Risk; and Julia Tseplyaeva, our Chief Economist. With that I would like to hand over to Alexander Morozov to some opening words.

Alexander Morozov - *Sberbank Rossii PAO - Deputy Chairman of Management Board, CFO*

Good afternoon or good time of the day, colleagues. I'd like to thank you, all of you, for being with us today on our regular conference call to discuss our half-year results.

I have to say within the second quarter of year 2016 the operating environments in Russia continued to show some improvements, with oil and commodity prices stabilizing and the ruble strengthening a little bit, and corporate results improving. After a period of decline we also saw some real income population to stabilize in second quarter despite the fact that -- less [fact] in July, and now we see some further deterioration. But in second quarter it was some temporary stabilization of that, and as a result we expect Russia to return to positive GDP growth in second half-year 2016.

Very important to notice that we see serious slowdown in terms of inflation expectations. Inflation will be definitely lower than we expected at the beginning of the year. So we see some positive signals from the markets, and against this backdrop we see some improvements on business activities as well.

We achieved net profits for the first six months of the year RUB263 billion, and which in terms of return on equity gives us something like 21.1%. It was driven primarily by strong interest income and a high-teens growth in fees and commission income.

These numbers includes also a one-off sales effect of RUB12.2 billion related to the noncore asset disposal, Krasnaya Polyana, related to Sochi Olympic Games. It is fully explained in Note 11 of our financial statements, and I'll be ready to answer additional questions if you have during the conference call.

Altogether we see some positive developments to be continued since our full-year guidance with regard to return on equity. Now we change it to high teens, which means 17% to 20%.

Cost growth accelerated [relative] to second quarter and came to 9.2% for the first half-year of 2016. As a result we saw a cost-to-income ratio at a level 37.7%.

Taking into account that the biggest part of this growth is due to change of compensation: indexation of our salaries of our employees. We didn't do that last year and the year prior to that, so it [was] time. That was [occurrence] we started to increase a little bit compensation to our -- just field staff employees; and we see the full results when we present full-year results.

But altogether we maintain our guidance at around 40% cost-to-income ratio for the full year, and definitely a positive dynamic on a year-on-year basis, and these positive trends looking forward.

What's most important to notice, both credit and deposit growth have slowed down this year as we are in a declining inflationary environment. It's why loan rates are still at a quite decent level.

We maintain our sector guidance of low single-digit growth on loans. At the same time we revise our deposit guidance for retail to high single digits. So we are a little bit cautious now.

We maintain single-digit growth for corporate deposits. That's for the market, the Russian market.

As for Sberbank, we are a bit more optimistic. We maintain our guidance in line with that with regards to corporate, both loans and deposits. At the same time we'll be better than the sector in terms of retail.

Also in deposits, first of all expect us to show substantial growth of deposits in last quarter this year and loans. Loans, we continue to focus on mortgages, on consumer finance now. We have to [ease] product because this profile is improving; and more details to be addressed by my colleague Alexander Vedyakhin. So we'll be better than the sector in terms of retail, both deposits and loans.

With a combination of slow growth and at the same time improved profitability, we expect with our Tier 1 ratio, which has already risen to 10.4% in just two quarters we see despite the payment of higher dividends in the second quarter. But we will -- we continue at the ratio; we continue to improve, and full year out it will be safely, safely above 10.5%.

Definitely [work through the terms] on foreign exchange rate. As of now, we expect it will be at more of a stable, at current level of RUB65 per $1. But in our guidance we put that assumption on the lines.

Our operating environment outside of our core market, Russian business, has been very eventful during the year. We continue to optimize our European network.

In July we announced finalization of the sale of our subsidiary bank in Slovakia. It was not reflected in our second quarter; it will be reflected in the first-quarter results. But nevertheless, that's an important event which [really] happened.

And what's also important to notice with our Turkey subsidiary, it's showing improving results in first half of year 2016, despite very high uncertainties affecting the region's economies. As a matter of fact, we are very satisfied with our development of the Group in Turkey.

Ukraine is more or less stable, and with regard to Ukraine, I would like to mention just one number. Our full exposure in Ukraine continued to reduce, and actually it's about 0.2 percentage points of our total assets. So it reduces by 2 times from our previous discussion.

So, having said that I would like to pass the words to Alexander Vedyakhin, our Head of Risk Management, to comment our asset quality developments. And we'll be ready to answer your specific questions during the Q&A session which will follow. Thank you.

Alexander Vedyakhin - *Sberbank of Russia LLC - Managing Director of Risks Department*

Okay. Thank you very much, Alexander. Good afternoon from myself as well.

Actually, I can say that asset quality is showing its first signs of stabilization and I can say improvement, with NPLs down in the second quarter of this year to 4.9% from 5.2%, even with our overall loan portfolio contracting in ruble appreciation. Cost of risk came in at the lower end of our guidance at 202 basis points, and at the same time our coverage ratio improved to 134 from 121.

Our portfolio for structured loans grew in second-quarter 2016 to 19.9% from 17.8% in the first quarter of this year. But actually this was driven by two modifications of interest rates of major clients with high credit quality in the telecom and power generation sectors.

Due to the Russian market specific of [fixed planning] rates, going forward we will see a growing amount of this type of modification as we're more into a lower interest rate environment. And as you know, those modifications are included in our structured portfolio and do not migrate out until maturity.

About internal classification of our top 100 restructured portfolio, we can say that improved result, combined black and red zone, is decreasing to 39% from 41.1%; and our yellow and green zones are increasing respectively. The NPL ratio of the restructured portfolio dropped from 11.3 to 8.3, and specific provision coverage of these NPLs rose from 65.9% to 74.9%.

You remember very well the previous discussion, and as previously promised we will be changing our reporting format so that, instead of reporting the current combination of restructurings and modifications, we will report them separately. We will also look at various options on when to migrate loans out of the restructured portfolio as the performance warrants this. We'll start with from the third-quarter 2016, I think.

And finally, as we see the trend of stabilization continuing, we are changing our cost of risk guidance to around 200 basis points for the full year. Thank you very much. That's all from my side.

Jyrki Talvitie - *Sberbank Rossii PAO - Strategic Partners and Investors*

Okay, thank you very much, Alexander and Alexander. That concludes our opening remarks, and we would like to go to Q&A.

We would like, if there are questions related to the economy, macro economy, etc., for Julia Tseplyaeva, our Chief Economist -- if those questions could be done first, as she has other engagements coming up shortly. Operator, we're ready for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Olga Veselova, BoA.

Olga Veselova - *BofA Merrill Lynch - Analyst*

Thank you. My questions are not about the economy; my question's about the Company, if that's all right. I have a couple of questions.

One is about Turkish exposure. Do you think there is a risk of potential extra provisions in Turkey?

What provision coverage do you have now? And if you see any risks in addition to provisioning -- maybe volumes, margins, or anything else that might change and might be meaningful for the Group financials? That is number one.

Number two is I noticed a small [net] release of provisions on other assets, other than loans, which goes against the trend in the nearest competitor. I appreciate we would not comment what's going on there; but I wonder: How do you view the credit risk on non-loan exposures, such as guarantees and other?

And what is your view on such exposures overall? Do you want to keep reducing them or not going forward?

And my third question is about your Tier 1 ratio. I appreciate that the Company improved Tier 1 ratio in the first quarter and in the second quarter, and that is really very, very welcome. But that came together with no loan growth.

When you target 12% Tier 1 in the next two to three years, what loan growth assumptions would you have in mind? It doesn't have to be a number; it might be a range.

Or, we shouldn't think about sustainability of muted lending dynamics; we should think about the improvement of risk-weighted assets to total assets ratio? That's my third question. Thank you.

Alexander Morozov - *Sberbank Rossii PAO - Deputy Chairman of Management Board, CFO*

Okay. Let's go step-by-step, question-by-question. First of all, Turkey.

Net interest margin in Turkey [fixed] in first half of the year was about 4.8 percentage points, which is quite good for Turkish market, and it's much better than it used to be in the past. Cost of risk is 110 basis points, and return on equity 16.5%. So it's a quite decent result.

What's really important for us is that our Turkish colleagues now focus on efficiency of their business, and they're clearly aiming to noticeably reduce cost-to-income ratio gradually, which is really important for us. It will be below 50%, I assume, this year and with positive dynamics the year after -- which is important for us.

We feel our self quite comfortable today in Turkey, and we believe that our Turkish team is a very good team really -- really today. And it's [robust] to pass safely through the very eventful season and very unstable period of development. So we believe that we have enough [ambition], focus, and professionalism we can (inaudible) to do it in the future as well.

So that's with regard to the future of DenizBank. I hope I have answered your question.

With regards to your second question, what are the other provisions, RUB7.6 billion as far as I understand. That's release of provisions for the off-balance-sheet commitments like credit lines and guarantees.

We see a reduction on the Bank level of the losses there for RUB5 billion in the quarter as a result of [doing] repayment of these guarantees and just the end of our commitments. So I think that's [now] our business and there's nothing else behind it.

On top of this RUB5 billion, RUB2.6 billion was the fact received as a results of the Court actions undertaken by the Bank; so it's recovery.

And we get to your third question, the Tier 1 ratio. Yes, I put it in a way -- I can [sort] you for it. So we will be safely above 10.5%.

We will continue to work on the ratio, believe that 10.5% is definitely not enough. I have already mentioned that we have to assure at least average -- capital adequacy ratio average for European levels, so above 12% core [adequacy Tier 1] ratio, and it's according to Basel II.

Basel II we are going to implement, are adopting for next year and where there will be some -- not significant, but some potentially a bit negative effect as a result of implementation of operational risk calculation. But nevertheless, we have to prepare that.

On top of that, we are going to reassess the value of our fixed assets. We are going to complete it fourth quarter this year, taking into account that the last two years there actually is also [quite small concession]. I cannot exclude that the result of this valuation of our fixed assets might give us some -- not substantial, but nevertheless negative result, which we also have to take into account when we make our forecast for full year.

So, that's how I see it, gradually taking into account that we are very cautious with our risk-weighted assets. And so we will continue to deliver our promises with regards to superior [on] average return on equity. We believe that we will be able to achieve a decent level of Tier 1 core equity capital for organic way in relatively short term.

Olga Veselova - *BofA Merrill Lynch - Analyst*

Thank you. May (multiple speakers)

Alexander Morozov - *Sberbank Rossii PAO - Deputy Chairman of Management Board, CFO*

Yes, please.

Olga Veselova - *BofA Merrill Lynch - Analyst*

If I could, one thing. You mentioned that Basel II is planned for implementation for the next year. Is this right: that you plan to move IFRS accounts to Basel II in 2017, and you expect negative impact on Tier 1?

Alexander Morozov - *Sberbank Rossii PAO - Deputy Chairman of Management Board, CFO*

We evaluate the full implication of our IFRS definitely. I mean that next year we will report our results in front of Basel II under IFRS. That's what we're going to undertake.

We will talk -- [you may find] the topic on our next conference call when we present our third-quarter results. Now I'm -- my [analysis], but it will definitely happen next year.

And the implication, we may expect complication from just the full operational risk. I think that my colleague Alexander Vedyakhin may try to clarify the question, but again it will lead to or return to a topic to that question with more details when we present our third-quarter results. And we will try to announce some guidance with regard to the effect out of implementation of Basel II now, current results, on our capital adequacy ratio next year.

Olga Veselova - *BofA Merrill Lynch - Analyst*

That's useful. And also, to clarify, did I understand correctly that you do not expect any potential additional provisions on Turkey exposure? Is this right?

Alexander Morozov - *Sberbank Rossii PAO - Deputy Chairman of Management Board, CFO*

In Turkey, we will continue to make our provisions in line with -- just with normal business. We do not see any specific [funnels]. We do not see any urgency.

Do not have any specific situations and our coverage ratio in Turkey is fully in line with Turkish market, as it reflects our best understanding of the quality of Turkish portfolio.

Alexander Vedyakhin - *Sberbank of Russia LLC - Managing Director of Risks Department*

I can give some additional details actually about Turkey. We have some concerns about tourism sector because of relationship with Russia. But now, as you very well know, this relationship has significantly improved, on one hand; on another hand, in 2016 there was a big program of Turkish government to support hotels and resorts in Turkey, and it gives us as a bank big comfort about quality of portfolio and tourism.

So other sectors are not so [heartened] by the situation in Turkey. If I can mention that GDP of Turkey is still growing, and actually because of this we are more or less a comfortable zone. That's growing at around 3%, so that's pretty good.

Olga Veselova - *BofA Merrill Lynch - Analyst*

Okay, thank you.

Operator

Andrzej Nowaczek, HSBC.

Andrzej Nowaczek - *HSBC - Analyst*

Thank you. I'm curious what changed your view on the consumer finance market. Is it the inflation expectations falling? Is it the wage growth? Or is it something to do with perhaps your scoring models or changes in competitive dynamics?

Alexander Morozov - *Sberbank Rossii PAO - Deputy Chairman of Management Board, CFO*

Strategics and quality of our existing portfolio. We see that the quality of our new vintages -- so vintages generated after serious adjustments we made to our risk models after the beginning of the crisis -- are much better than they used to be before that. So that's not only the case of Sberbank of Russia; I believe that's more or less typical for all Russia, the whole Russian market.

So we may think about some changes to the behavior of the customers and overall improvement of the market. Definitely we had serious changes in our risk-scoring metric and the processes behind it. And Alexander Vedyakhin may add more colors to that.

Alexander Vedyakhin - *Sberbank of Russia LLC - Managing Director of Risks Department*

Thank you, Alexander. Actually, we are always improving our ways to -- how to score the clients. I mean, the retail clients. So we're always improving our Gini qualifications; and, for example, when previously we were using really limited sources of information, how to score our clients, now we are using, for example, social media. We are using other sources of data for clients to be scored.

It improves our Gini coefficient of our model, and it gives more stability, so to say, in financial results.

Andrzej Nowaczek - *HSBC - Analyst*

Okay; that's helpful. Thank you. And now something different. Why hasn't the issue of Visa merger come up in any of our previous discussions?

Is it because you work with other issuers? Will it still come and show in the results later in the year?

Alexander Morozov - *Sberbank Rossii PAO - Deputy Chairman of Management Board, CFO*

We haven't yet shared why is that. It's not yet in our numbers. But (inaudible), it will be reported in later periods. Not yet in our numbers.

Andrzej Nowaczek - *HSBC - Analyst*

But is it significant?

Alexander Morozov - *Sberbank Rossii PAO - Deputy Chairman of Management Board, CFO*

Yes, I think so.

Andrzej Nowaczek - *HSBC - Analyst*

Okay. On that topic, the Slovakian subsidiary sale, what impact will it have on your financials in Q3?

Alexander Morozov - *Sberbank Rossii PAO - Deputy Chairman of Management Board, CFO*

It will be reflected in our Q3 results. But the effect is very small, negligible. So it's very small.

Andrzej Nowaczek - *HSBC - Analyst*

Okay. Thank you very much, Alexander. Thank you.

Operator

Alex Kantarovich, JPMorgan.

Alex Kantarovich - *JPMorgan - Analyst*

Thanks. It's Alex Kantarovich from JPMorgan. Alexander, I have a question on provisioning. If we calculate the delta in loan loss reserves, that would be RUB35 billion sequentially. If we throw in write-offs of RUB50 billion, we would arrive to around RUB85 billion gross reserves added.

But your actual provisioning figure through the P&L was more than RUB10 billion higher, at RUB96 billion. So, my question is: What accounts for this gap, whether this is anyhow related to the credit guarantees, a counter-effort of sorts, or this is a different effect? That's my first question.

Alexander Vedyakhin"

Actually, the answer is in the report, and [Al Holex] can explain to you in detail, because there are a lot of reasons for this.

Alexander Morozov - *Sberbank Rossii PAO - Deputy Chairman of Management Board, CFO*

I can give more details a little bit about our provision charge, about our RUB98.3 billion, which we reported in second quarter. So RUB89.3 billion total provision charge may be split in two numbers: so RUB84.4 billion, that's corporate part; and RUB14.8 billion, that's retail part.

As [provision] cost of risk on corporate side, 174 basis points; and on top of that 28 basis points retail. On corporate -- on retail I have nothing certain, but information on corporate side [would held] to split with 48.4. So some collective impairment; that's the biggest portion, let's say, about RUB86.1 billion.

One, we have one specific customer from construction material areas, where we added provisions in the amount of RUB4 billion. One, another construction customer was a one-off, RUB5.7 billion. And finally we have some ruble growth which reduced overall reserves by RUB11.4 billion.

So we believe that today we do not know any specific big cases of the magnitude of major, something like that, which might potentially affect our cost of risk in the future, and everything is already in. So that maybe might be considered to be just a normalized, more or less, level.

That's why we believe that full year is out, just in terms of cost of risk, will be around 200 basis points. Which means that still be 200 area, potentially slightly higher, but potentially slightly lower than that.

Alex Kantarovich - *JPMorgan - Analyst*

Yes. Alexander, this 200 basis points -- thanks for updating your guidance -- does this include a provision for credit, latest commitments? Or this is purely a loan credit adjustment, loan loss reserves?

Alexander Morozov - *Sberbank Rossii PAO - Deputy Chairman of Management Board, CFO*

Was just purely loans, no credit commitment impairments included. But I would not expect any significant numbers from that part, any noticeable numbers.

Alex Kantarovich - *JPMorgan - Analyst*

Okay. On operating costs, can you give us more color how salaries increased? There was quite an escalation quarter-on-quarter from -- in Q2; so obviously the rest of the year you will have a bit of a headwind costwise. And yet you give commitment to cost-to-income of 40%. If you can give us some color on how OpEx will progress in the second half.

Alexander Morozov - *Sberbank Rossii PAO - Deputy Chairman of Management Board, CFO*

Okay. With regard to staff costs, they on a quarterly basis increased by 13.6%, with phaseout of some indexation of the salary payments and a little bit higher due to results -- variable part. So quarterly payments, what we have there are related to our performance. So, all together something like 13.6 percentage points growth.

Full year, I discuss the topic with my colleagues, and the 40% cost-to-income ratio, which is more than 4 percentage points improvement versus the previous year, what we guide now definitely is not the final target. We are looking beyond year 2016, and the dynamic on cost-to-income ratio will be a positive one.

So next year it will be further improvement versus that level. So no doubt.

That suggests our target for this year for the (inaudible) year. And this number takes into account some seasonal spike in our expenses, which you may notice when you annualize our quarter results year after year in the fourth quarter. Seasonally, due to a number of reasons, expense line is always slightly higher than other quarters.

It relates to a number of reasons, but the biggest reason is that in fourth quarter we a little bit enhance our provisions created for full-year annual bonus for our whole staff. So that number relates to our final results.

So definitely this year we create some provisions for annual bonus payment. But nevertheless you may see this correction in the fourth quarter.

So this correction relates to the factual results, taking into account that this year we are going to deliver to our shareholders a (inaudible) percentage on equity. I may assume very high chance that provisions for annual bonus will be slightly amended as well.

So fourth-quarter cost side will be slightly higher than average; and as a result cost-to-income ratio in the fourth quarter will be a little bit affected.

But full year out, any way, it will be around 40% as we guide it now. We (multiple speakers) the year 2017.

Alex Kantarovich - *JPMorgan - Analyst*

Yes, I appreciate that. Thanks, Alexander. No further questions.

Operator

Alan Webborn, Societe Generale.

Alan Webborn - *Societe Generale - Analyst*

Oh, hi; thanks for the call. Clearly a very good margin performance in the second quarter, and your target is still to be above 5% for the full year, clearly well above that the first-half stage.

Alex, looking at your loan yields and your deposit costs -- and clearly the improvement's coming from pushing down the cost of deposits both on the corporate side and a little bit less on the retail side -- I wonder: A, do you think that the loan yields that you're achieving now are sustainable? Or do you think there's going to come a point where, as the economy normalizes, maybe there's a little bit more competition?

We hear anecdotally that corporates are quite keen to get the best funding that they can, and therefore they're quite price-sensitive at the moment. We're seeing that from some of the smaller banks, I think.

I just wonder whether you feel that you will actually have to give a little bit back in terms of what you are taking away on deposit costs in terms of your average loan yields, as perhaps the economy ticks into a slightly more positive phase than we've seen in the last six months. So I'd be interested in your view on that and what you think that's going to mean for managing your NIM going forward.

And I suppose the second question is: How should we interpret the fact that your fee income is still growing really quite nicely despite not a great deal going on on the loan side? Clearly the transaction banking is picking up. Are you seeing that across the board?

Is it increased business activity? Is it simply SMEs using your services more? How long do you think that phenomenon that you're seeing at the moment is likely to persist in what's still a relatively low-growth environment? Thank you.

Alexander Morozov - *Sberbank Rossii PAO - Deputy Chairman of Management Board, CFO*

I'll start with NIM dynamic. Thank you very much for your question. I will start with net interest margin dynamic and after that address your second question.

Net interest margin, you're absolutely right. There are a number of factors, a number of drivers on both hands. On the one hand, we now seriously, noticeably reduce cost of our funds; number of drivers behind that.

First, we paid in full our expensive funding to Russian Central Bank. That's more than RUB3 trillion being repaid over last two years; and we completed it as we promised in June.

That was the most expensive part of our fundings. Definitely it seriously affects for positive our overall cost of funds.

Secondly, we have made an emphasis on [accounting] our contractual maturities where we pay close to zero interest rate; that's card accounts, settlement accounts, current accounts. It's a blend of corporates and retails, and so a change in our composition gradually helps us a lot.

[Probably] we reduced substantially our interest rate payable first of all on hard currency deposits, both for corporates and retail. And now I can confess that we do not make any losses on replacing our short-term deposits attracted from the local markets, replacing them to deposits abroad. Okay? So here we are looking small profit.

So out of that you may conclude how much we pay on our liability side for short-term deposits. And for long-term deposits, which were our most expensive long-term deposits, which were attracted from the period of the high in a very (inaudible) [pit] of the crisis beginning of 2014, were either already expired or expiring now.

And that process will continue, so I would expect further reduction of our cost of funds. However, there's definitely a chance which will be continued and [first] forwards it will be driven by a greater reduction of cost of retail deposits of medium- and longer-term who are expiring now.

And on the other hand, on the asset side you're absolutely correct. We face increased deficit, still deficit of good quality demand, and we are competing for good corporates, for good credit risks.

That's why we have to renegotiate some of our good exposures; part of it was two big renegotiated loans which were posted in second quarter. And the fact was more than 90% explanation of the growth of our negotiated portfolio in second quarter, with just a change of the price of our two really good names: one from telecom as Alexander Vedyakhin mentioned; another one from energy.

This is not a result of compromising of quality. This is a result of fierce competition for good borrowers.

So this is also a trend which will be continued, and we are trying a little bit to mitigate it by increasing our exposure and our dynamic on retail part.

So that's why. It's not only mortgage; mortgage itself also quite good portfolio; we has been quite profitable. But also consumer finance, consumer loans.

That's why we are focusing now more on consumer finance, to offset some negative implication on the margin from reduction of the interest rate in corporate segment. So that's why we're increasing a little bit our approval rate on consumer finance, provided we have stable credit quality.

Looking forward, what's also important was the currency composition we have on asset side, liability side. And here we also have actually a dynamic quality for us.

Looking forward, I can say I believe we have enough -- we're margin focused and we have enough levers to drive it to preserve the margin at actual level. I would not expect margin to post a new record; but nevertheless, we have really returned to our pre-crisis margin level, which we haven't discussed. And out from now I would say it will be more or less stable for some period of time.

Looking even further forward, definitely we will experience serious pressure on our margin, and we expect it, and it will be put in our business model. And looking forward to, let's say, two or three years from now, we should be able to compensate reduction in our margin by higher fees and commission income not related to interest income.

That's why we continue to focus on our fees and commission income -- and here I start to answer your second question. Fees and commission income that's, at the end of the day, the function out of your ability to provide the customer with most convenient tools to perform some transactions.

If we put it in our press release, as Mr. Jyrki Talvitie has mentioned, that we have more than 33 million online customers, retail customers, who perform their wire transactions exclusively only through distant channels. And this number is growing currently.

We have more than 90% of all transactions made by private individuals made through distant channels. So that's not only cost-reduction; that's also increase of number of transactions. That's about convenience we create for our customers.

So major [book] for our commissions comes from card-related operations, from payments, from settlements. And looking forward I would expect that some revitalization of consumer finance will help us a lot to increase our fees and commissions from related business -- I mean, insurance.

Also looking forward I would say that asset management and related businesses will contribute much more where they contribute today. So we are preparing much more ambitious plans as we get to the development of fees and commission business not related to risk-taking activities, and so we'll address it later on when we present our guidance for the next year.

So I have some arguments for some decent optimism with regard to the further development of fees and commissions. I believe we will be able to preserve that dynamic which we posted up to date also next year.

Alan Webborn - *Societe Generale - Analyst*

That's very helpful. Thank you.

Operator

Mikhail Shlemov, UBS.

Mikhail Shlemov - *UBS - Analyst*

Yes. Good afternoon; thank you very much for the call. I've got two questions actually, starting with capital. We already touched that the capital build-up looks very impressive, and also there should be some regulatory changes coming through.

So perhaps you could update us on the progress with the IRB introduction, when you expect to be phased in. And shouldn't it be able to partly affect the negative impact from the operational risk introduction which you have mentioned specifically in terms of Basel II?

And the second question relates on the margin. I know that you have said that just like you probably want to give margin here stable on. But does it basically mean that you are a little bit driving out of a runway in terms of a way where you could drive your NIM higher? Thank you.

Alexander Vedyakhin - *Sberbank of Russia LLC - Managing Director of Risks Department*

Okay; thank you very much for the question. About IRB I can say that now we are in the process of validation of Central Bank. As you very well know we are the first bank that's applied to the permission under the IRB, permission of Central Bank; and we are still number one.

We hope to receive preliminary act of Central Bank in a short period of time. And afterwards we will -- we have to make some improvements that Central Bank will require.

And I hope, but this is -- I have to make some disclaimers, because we didn't see yet the report. So I hope that in the beginning of 2017 we could receive and start IRB. But I have to mention this is the Russian standards of accounting; and the IFRS standard of accounting we will make a little bit further.

And about your question about compensation of actually operational risk issue, we will try to compensate it; but we have to calculate the exact result. I would like to mention one more time about IRB that all data I have mentioned, this is really preliminary as this is appraisal from our side. The Central Bank will give real [terms], and we will follow the recommendation of the regulator. Okay? Thank you very much.

Mikhail Shlemov - *UBS - Analyst*

Alexander, thank you.

Alexander Morozov - *Sberbank Rossii PAO - Deputy Chairman of Management Board, CFO*

With regard to your second question in regard to the margin, all of you know my personal attitude towards our guidance and forecasts. I prefer to refrain from some overoptimistic statements and overoptimistic guidance.

We have a number of really high uncertainties in front of us as they -- with regard to the margin. One of these uncertainties is still our ability to find proper good, acceptable credit quality risk on the market on the corporate side, especially big corporates.

And because I'd like to stretch your attention, as of now we have an excess of liquidity in American dollars, the [euro], and in [card] currency. So my loan-to-deposit ratio is slightly below 80%, which is too expensive for us on dollars.

Overall, it looks not the best; it's something like 90%. But nevertheless, on our currency that's around 80%.

That seriously affects my -- less structural (inaudible) [cash] seriously affect my ability to increase the margin. So margin will be stable, I assume. It doesn't exclude that some quarter risk, for the first quarter or fourth quarter seasonally, may be slightly better when we posted today.

But looking forward to the trends -- and we are here to discuss trends and not just specific quarter results, which might be better -- looking forward, I believe that we should expect more or less stable margin at that level, above 500 basis points. And that's safe enough to assure the business model and the guidance in terms of return on equity promised to our shareholders.

Mikhail Shlemov - *UBS - Analyst*

That's better; thank you very much. If I may follow up a little bit on the capital, I think earlier you had said that the IRB introduction should bring at the first stage roughly 60 basis points capital relief on the Russian accounting standards level. Does this estimate still hold up?

Alexander Vedyakhin - *Sberbank of Russia LLC - Managing Director of Risks Department*

Actually, as I said, now we are in talks with Central Bank and I would like to avoid any estimations or any figures about this issue. I hope this is the same, but it's -- so you have to understand that we are in negotiations, talks with our regulators, and it is difficult to judge.

Alexander Morozov - *Sberbank Rossii PAO - Deputy Chairman of Management Board, CFO*

I would say no additional piece of information since our last conference call which we held as a result of first-quarter results. No additional information from that periods on that specific matter.

Alexander Vedyakhin - *Sberbank of Russia LLC - Managing Director of Risks Department*

Exactly. Actually, what we -- that we had in talks with Central Bank that sharpened the issue, but all data about implementation, that's explicitly on the side of Central Bank. All decisions are on the side of Central Bank.

Mikhail Shlemov - *UBS - Analyst*

Thank you very much, gentlemen. Appreciate it.

Operator

Jason Hurwitz, VTB Capital.

Jason Hurwitz - *VTB Capital - Analyst*

Good afternoon. I have another question relating to the Basel II IRB approach. And that is: Given that, as well as the fact that you have produced some very good bottom-line figures that have added to your capital, is there any chance that you might have a positive revision to your payout ratio for dividends next year?

And as a second question related to your loan quality, you mentioned earlier that you were doing significant renegotiations with your good clients. Yet when we look at the renegotiated loan portfolio structure that you provide on page 22 of your presentation, we see a decline in this green part of the data.

So those two statements, they don't necessarily contradict each other, but it does seem that the amount of the good clients has been declining even in the second quarter. Could you help us to understand how those two statements -- or that statement and this information coincide with each other? Thanks.

Alexander Morozov - *Sberbank Rossii PAO - Deputy Chairman of Management Board, CFO*

Let me start with answering your first question, and Alexander will answer the second one. With regards to the dividend payout ratio, I would not expect us to change our recommended dividend payout ratio right now for the year 2016 results. As I already mentioned, we have to achieve average European level of core equity Tier 1 ratio, which is above 12% under Basel II requirements and de facto Basel III.

So I think that it's not yet the time. Basel III in time, looking forward at some point of time in the future, definitely as we discussed it as well, will -- turn to the topic for us. What's important to assure what we deliver to our shareholders: positive economic value added. And this is really critically important for us; let's say that's a cornerstone.

So from that perspective, I would not exclude what Sberbank to reconsider the dividend policy a little bit upward; but not immediately.

Alexander Vedyakhin - *Sberbank of Russia LLC - Managing Director of Risks Department*

And answering your second question, I can say that actually the green zone and the yellow zone that you could see on the slide doesn't mention actually a bad quality of the loan. Green zone means that everything is really fine; and yellow zone, it means there is needing some attention, like additional monitoring, but nothing special.

The real problem is the red zone and the black zone. And the red zone and the black zone are decreasing, and you can see this in the figures.

Yes, they are decreasing not so significantly as we would like to see. But as I mentioned, that actually they are showing just the first signs of stabilization and first signs of improvement of our asset quality.

Also it's important to mention that I hope that starting from the next meeting, we will provide to you a new reporting format, that instead of reporting the current combination of restructurings and modifications, we will report them separately. And you will see another and more interesting and more detailed picture. Thank you.

Jason Hurwitz - *VTB Capital - Analyst*

That's great. But as long as we still have this particular structure, could you give us some indication of what is the typical provisioning level for the green versus for the yellow loans? So we could help to understand just how big is the difference between the quality of those types.

Alexander Vedyakhin - *Sberbank of Russia LLC - Managing Director of Risks Department*

So, according to our approach, we only give it for NPLs. Because, for example, for green it's difficult to say that. It depends on -- from one loan to another loan.

And that for NPL you can see coverage on the page number 21. So for example, our coverage for NPL has increased from 66% to almost 75%; and NPL share, the shaded loans is decreasing. So that's improving on one side of our quality of assets.

On another side, we can say that we are still really cautious about our loan portfolio and giving additional provisions.

Jason Hurwitz - *VTB Capital - Analyst*

So if a loan were to migrate from this green to this yellow category, would that usually involve some increase of provisioning?

Alexander Vedyakhin - *Sberbank of Russia LLC - Managing Director of Risks Department*

No, no. It just involves additional monitoring, additional attention. So it's like -- why we are changing actually this methodology, because we are showing for you our internal indicators of attention. And yellow means that -- me, for example, I have to look on these loans every month but not every quarter, as I am doing for green zone. And so, I mean, that's nothing special.

Jyrki Talvitie - *Sberbank Rossii PAO - Strategic Partners and Investors*

May I add, Jason, that it's also very important with the NPLs that the NPLs that we have in the restructured portfolio, they are included in the overall NPL number for the portfolio.

Because there is still some confusion. Some people still double-count, and you cannot do that.

Jason Hurwitz - *VTB Capital - Analyst*

Yes, thanks. We are aware; we also avoid the double-counting. Just trying to get a better picture of what's going on in the better part of the renegotiated loans. But, okay, thanks very much for all your answers.

Operator

(Operator Instructions) Gabor Kemeny, Autonomous Research.

Gabor Kemeny - *Autonomous Research LLP - Analyst*

Hi; thank you for taking my questions. The first one, I'd like to follow up on, margins, especially on your deposit repricing. How much further room do you see to reprice your deposits downwards?

I mean, the average deposit on your retail term deposit book is still 6%, so still quite high. Maybe if you could give us a sense: What is the interest rates you pay on the new deposits, and how does that compare with the back book?

And more broadly, do you think you would need Central Bank base rate cuts from here to have upside, more upside in terms of your deposit pricing?

And the second question is on your provisioning guidance. In the first half you were 2% provisioning; you guide for a similar amount for the full year. But in the first half you managed to build a decent amount of coverage, decent amount of NPL coverage with these levels.

So the full-year guidance looks a little bit conservative. Is it that you would expect some additional provisioning need on your restructured book -- I mean on the red and black zones, obviously? Or how do you think about the outlook for the second half?

Alexander Vedyakhin - *Sberbank of Russia LLC - Managing Director of Risks Department*

I can start with the answer with your second question. Yes, you're absolutely right; we are quite conservative in the provisioning. So we think that -- actually, you can see we have only first signs of stabilization and improvement, and I would like to believe that everything will be good. But me as Head of Risk and Alexander as Chief Financial Officer still would like to be cautious about our future and to be enough conservative.

I think this is in line with the situation we have now in Russia, and that's in line with our budget. I mean that we are comfortable with this.

And also very important to mention that in the first half of the year, we had some one-offs that we will not have in the second half.

Gabor Kemeny - *Autonomous Research LLP - Analyst*

Sure.

Alexander Morozov - *Sberbank Rossii PAO - Deputy Chairman of Management Board, CFO*

Okay, as regards to the margin discussion, yes, we have some room for maneuver here. Because again, what average customer deposit costs, that's a combination of a number of factors. That's a composition of -- Alex had mentioned -- accounts [without] contractual maturities and time deposits, and that's a split of different currencies.

Since the beginning of the year, we saw increase of our deposits in Russian rubles, no in American dollars. So we didn't have that negative impact from further devaluation of Russian rubles, so (inaudible) obligations related to that.

As of now, we [accept] new deposits in rubles. I will give you just -- now, let's see -- one number for most typical deposits, large deposits. In Russian rubles, something like three years with something like [5] on the [yield]. And maximum price you pay -- on the time horizon, one year, let's say, around 6 percentage points. That's quite typical for Russian rubles. As we have inverted yield curve on deposit side.

On American dollars, if we look at this, we pay much, much less. We pay less than 1 percentage point on all American dollar deposits, with just very small exceptions. The maximum rate we pay, that's something 1.3; but it's actually the [max] we pay to our most important customers for longest terms.

And that more or less gives you some impression out of new rates. So, yes, you're absolutely right. We have some room for further improvement in terms of cost of funds; but at the same time, I would expect some further reduction of our average yield on corporate portfolio, first of all.

On retail as well, but taking into account that the biggest part of retail -- that is mortgage portfolio -- is fixed rate. So some erosion of the asset side margin on retail will be less noticeable and much lower.

But the corporate side, we will be exposed to quite serious margin pressure. What we will have as the (inaudible) will be, what will be the result, our guidance, we sure enough to give guidance above 500 basis points full year; and so I give more indication, let's say, give you more a stable level. I assume, but I do not assume serious deterioration of the margin within the next year, year to follow, 2017.

So it will be more or less at this level. But looking forward, year 2018 and in the end of 2017 maybe, yes, you should expect serious pressure on the margin. The positive effect from the liability side margin expansion will be -- might be potentially seriously offset, if not in full, by a reduction of the interest rate payable by our corporate customers.

Gabor Kemeny - *Autonomous Research LLP - Analyst*

That's very helpful. Just to quickly follow up, would you then assume that to bring down your ruble deposit rate significantly from here you would need lower base rates? I mean, you would need the Central Bank to cut the base rate from here?

Alexander Morozov - *Sberbank Rossii PAO - Deputy Chairman of Management Board, CFO*

No, no. We already pay to our customers interest modestly below key interest rate set by Russian Central Bank. And our deposit rates are not related to key interest rates at all.

Gabor Kemeny - *Autonomous Research LLP - Analyst*

Okay. Okay, thank you.

Alexander Morozov - *Sberbank Rossii PAO - Deputy Chairman of Management Board, CFO*

So, definitely, we depend on market prevail increase. We have to take into account rates payable by our competitors on the market. We are not alone at all; thank God, we welcome competition.

And as you may notice from our market share, our market share is relatively stable in terms of retail deposits. It's not growing very fast.

At the beginning of the year, our retail deposits accounted for 45 points, 97 percentage points of the market share. As of now, it's just 46.13, so almost the same. So it means that we do not buy market share.

But we have to pay some decent interest rates, attractive enough to preserve our existing customer base, to preserve their loyalty, and not to deteriorate our deposit base in the medium term. This is the trend.

Gabor Kemeny - *Autonomous Research LLP - Analyst*

Thank you.

Operator

Hugo Swann, Credit Suisse.

Hugo Swann - *Credit Suisse - Analyst*

Hi, there; thanks for the call. Two quick questions please. Firstly, the guidance for ROE for the full year, does that assume any gain on Visa?

And then my second question: There's been an increase in proportion of your loan book that is three years plus in maturity, and that's risen quite a bit in the first half of the year. Could you give us a little bit of detail as to what's going on with that increasing maturity of that book? Thank you.

Alexander Morozov - *Sberbank Rossii PAO - Deputy Chairman of Management Board, CFO*

Okay. First question is a very short answer. We haven't yet completed that transaction to get to Visa, so it's not yet reflected. So we'll have some positive run-off upside potential, and it will be reflected as soon as the transaction is completed, sometime in the future.

With regards to maturity breakdown, yes, as a result of some restructuring of some of our exposures when we renegotiate other terms and conditions, one of those renegotiated terms and conditions is maturity, and we prefer to get stable interest income flow for longer term, because we expect an overall reduction of the prevailing interest rate not only in Europe but also in Russia.

And to the possible extent we are trying to fix the rate for potentially longer term than average. So that's one of the reasons; that's the major reason.

Hugo Swann - *Credit Suisse - Analyst*

Okay. Just to follow up on that, if you weren't going to lengthen that term out significantly, would you be reflecting a higher impairment charge in your accounts? Or does it not have any impact on the P&L? Thank you.

Alexander Morozov - *Sberbank Rossii PAO - Deputy Chairman of Management Board, CFO*

There is no direct correlation between those two things.

Hugo Swann - *Credit Suisse - Analyst*

Okay. Many thanks.

Operator

Hadrien de Belle, KBW.

Hadrien de Belle - *Keefe, Bruyette & Woods, Inc. - Analyst*

Hello; thanks for the presentation. I have three questions, please. Retail credit quality, it's been a little bit volatile in the last three quarters. Could you explain or give us a sense of how it will improve or they stay at low level in the next couple of quarters?

Second question is on the tax rate. It's been dropping in the first half versus 2015. Where do you think we should put a tax rate for the full year?

And the last question is you mentioned Visa as a positive one-off; asset revaluation as a negative one off. I understand you probably don't have the precise figures, but do those two one-offs balance each other out? That would be my third question. And I'm fine; thank you.

Alexander Vedyakhin - *Sberbank of Russia LLC - Managing Director of Risks Department*

Okay, so let me start with your first question. This is a really good question. I can say we have three major reasons why the quality of our retail portfolio is improving.

The first reason is that, yes, we have made some amendments to make our risk policy more stronger. And now we can see a result of these actions.

Second is that our portfolio is, so to say, migrating to mortgages. So it means that the structure of our portfolio we have left -- consumer loans and small mortgages -- and mortgage in Russia is always more stable and more secure for the Bank because a person is always paying the mortgage for the Bank.

And we had in the first quarter another one-off because of methodology as well. And also -- so this is important to mention, as Alexander Morozov mentioned as well -- that overall in Russia we can see that retail market in terms of portfolio quality is stabilizing. So we see this tendency in Sberbank as well.

Alexander Morozov - *Sberbank Rossii PAO - Deputy Chairman of Management Board, CFO*

With regard to your two other questions, first, for the sake of your model I would suggest to put effective tax rate at 20%. So now it's a little bit below that level, but full-year I think it will be around 20%. Maybe slightly better than that, but not significantly.

As for the second question, yes, to some extent a positive result out of Visa-MasterCard transaction partly will offset negative effect from revaluation of our fixed assets. But not in full.

Hadrien de Belle - *Keefe, Bruyette & Woods, Inc. - Analyst*

Perfect. Thank you.

Operator

Thank you. I would now like to advise any English-speaking journalist to ask any questions. (Operator Instructions) There seem to be no questions via the English side, so I would now like to switch the call over to the Russian side of the call for any questions. (Operator Instructions)

Jyrki Talvitie - *Sberbank Rossii PAO - Strategic Partners and Investors*

Okay; please continue. Okay. Do you have any questions?