Moody's INVESTORS SERVICE

Credit Opinion: Banco BBM S.A.

Global Credit Research - 03 Nov 2011

Rio de Janeiro, Brazil

Ratings

Category	Moody's Rating
Outlook	Stable
Bank Deposits	Ba1/NP
NSR Bank Deposits -Dom Curr	Aa2.br/BR-1
Bank Financial Strength	D+
Baseline Credit Assessment	Ba1
Adjusted Baseline Credit Assessment	Ba1

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Key Indicators

Banco BBM S.A. (Consolidated Financials)[1]

	[2]**6-11**	[2]**12-10**	[2]**12-09**	[2]**12-08**	[3]**12-07**	**Avg.**
Total Assets (BRL billion)	**4.9**	**5.0**	**10.6**	**14.2**	**17.3**	[4]**-27.1**
Total Assets (USD billion)	**3.1**	**3.0**	**6.1**	**6.1**	**9.7**	[4]**-24.7**
Tangible Common Equity (BRL billion)	**0.5**	**0.5**	**0.6**	**0.7**	**1.0**	[4]**-14.6**
Tangible Common Equity (USD billion)	**0.3**	**0.3**	**0.4**	**0.3**	**0.6**	[4]**-11.7**
Net Interest Margin (%)	**1.7**	**1.9**	**2.5**	**1.9**	**7.4**	[5]**3.1**
PPI / Avg RWA (%)	**0.5**	**1.7**	**2.3**	**1.4**	**15.4**	[6]**1.5**
Net Income / Avg RWA (%)	**3.6**	**1.4**	**1.5**	**1.9**	**10.3**	[6]**2.1**
(Market Funds - Liquid Assets) / Total Assets (%)	**18.7**	**39.8**	**2.0**	**51.2**	**15.7**	[5]**25.5**
Core Deposits / Average Gross Loans (%)	**95.4**	**46.5**	**44.2**	**50.2**	**86.8**	[5]**64.6**
Tier 1 Ratio (%)	**21.6**	**24.1**	**14.5**	**14.5**	**16.3**	[6]**18.7**
Tangible Common Equity / RWA (%)	**21.8**	**24.0**	**14.2**	**14.2**	**16.1**	[6]**18.5**
Cost / Income Ratio (%)	**87.9**	**72.0**	**61.2**	**72.6**	**17.3**	[5]**62.2**
Problem Loans / Gross Loans (%)	**3.0**	**15.5**	**3.6**	**-0.1**	**1.0**	[5]**4.6**
Problem Loans / (Equity + Loan Loss Reserves) (%)	**3.7**	**14.1**	**5.8**	**-0.5**	**4.0**	[5]**5.4**

Source: Moody's

[1] All ratios are adjusted using Moody's standard adjustments [2] Basel II; LOCAL GAAP [3] Basel I; LOCAL GAAP [4] Compound Annual Growth Rate based on LOCAL GAAP reporting periods [5] LOCAL GAAP reporting periods have been used for average calculation [6] Basel II & LOCAL GAAP reporting periods have been used for average calculation

Opinion

SUMMARY RATING RATIONALE

Moody's assigns a D+ (D plus) bank financial strength rating (BFSR) for Banco BBM based on the bank's focused operations as a lender to upper middle-market companies and on its long track record of successful trading activities, supported by sophisticated risk controls. The D+ BFSR translates into a Baseline Credit Assessment of Ba1, which is also the bank's long-term local- currency deposit rating. Systemic support was not considered, given the bank's limited share of the industry's deposit base.

The ratings acknowledge the bank's robust risk management and expertise in treasury activities have allowed the franchise to successfully transit between credit, asset management and trading across cycles, while the bank has preserved adequate credit quality, disciplined liquidity profile and capital surplus, when compared to similar sized banks. The ratings continue to weight the volatile earnings component from trading gains which continues to be relevant, despite the recent business restructuring.

Traditionally very cautious about credit expansion, BBM decided in mid-2008 to promote a significant deleveraging as management saw uncertain funding and credit environment. As a consequence, recurring profitability levels have been pressured down, indicating the reduced business volumes. Of note, the bank's capital ratios and cash position are sound, which can help it absorb the potential negative effects on performance of this reduction. Since the beginning of 2010, based on improved credit conditions, the bank decided to pick up its lending pace, though, in a very contained fashion. Now, BBM is challenged to resume loan growth in highly competitive scenario for corporate lending.

The strict credit risk management and good level of collateralization of its loan book should shield the bank's return to lending segment. The bank has proven to be able to reshape its strategy during uncertainties and reposition the bank's operations without incurring in risks. In addition, BBM's rigid asset & liabilities management philosophy and relatively restrictive leverage guidelines help the bank to withstand the difficult times for the system's midsize banks during the fourth quarter, caused by the selectiveness of local investors.

The ratings are still constrained by the intrinsic vulnerability of this type of wholesale funding and also the challenge faced by BBM's operations of lending in a competitive segment with many rivals, especially with the entrance of the large players.

Rating Drivers

- Sophisticated risk management and expertise allow BBM to successfully adjust its operations -- between credit, asset management and treasury -- through different economic cycles

- Disciplined assets & liabilities management and capital adequacy has been key to support the bank's financial strength

- Need to improve earnings recurrence generation, sustaining performance and profitability improvements at the asset management while maintaining a balanced approach to credit activities

- Still restrictive funding diversification

Rating Outlook

All ratings have stable outlook.

What Could Change the Rating - Up

Positive ratings pressure would be forthcoming if recurring earnings flow proves to be sustainable. Management's efforts to diversify its funding structure have already been underway, as signaled by BBM's access to a term IFC (International Financial Corporation) line of credit and by alternative ways it may use to access the capital markets. Sustaining adequate capital levels would also work to push credit quality up in the short run.

What Could Change the Rating - Down

Overaggressive lending practices as the bank resumes to growth, possibly resulting in eroded asset quality, would be harmful to the bank's credit standing. These riskier practices might follow a period of substantial expansion in lending, particularly if such growth is directed towards higher-risk market segments. The ratings could also be hurt if management fails to cope with competitive pressures and/or if profitability erodes. At this point, any loosening of risk management practices or consistent increase in market risk appetite could pressure the ratings down.

Recent Results and Developments

In the first six months of 2011, BBM reported a net income of R$ 41.9 million, up by 76.4% year-on-year. The bulk of the bank's income from financial intermediation was related to trading activities, that accounted for 86.5% of total income. The performance was positively influenced by the cost re-dimensioning phase that reduced by 43%+ administrative and personnel expenses in 12 months, to a lean structure, and the reduction in loan loss expenses following the adjustments in lending strategy . In June 2011, the annualized net income over risk-weighted assets reached 3.63%. Management also decided for a complete segregation of the asset management activity of the group from the banking operations, which was legally separated in the 3Q11, a movement that is expected to negatively impact the fee-services results, that in June 2011 already declined 31.4% compared to June 2010.

After two years of deleveraging, BBM set up a maximum loan leverage ratio of 3 times equity, targeting companies with annual sales over R$100 million. Management also set up rigid concentration parameters reducing the average ticket and increasing even more the collateralization framework of the portfolio. In June 2011, the loan book amounted to R$692.9 million on a consolidated basis, down by 15.5% when compared to same period in 2010. Consolidated NPLs ratio stood at 3.02% in June 2011, well covered by 211% of reserves.

In June 2011, total consolidated assets amounted to R$5.2 billion, relatively flat compared to June 2010, as part of the shifts promoted in bank's business mix. The bank maintains a vigilant liquidity approach, maintaining a conservative cash position built on government securities. Funding is largely composed of time deposits, with low reliance on foreign currency lines. With a low leverage ratio of 1.3x (credit portfolio over equity) out of a limit of 3 times, both Tier 1 and total capital ratio stood at high 23.86%, leaving substantial room to support growth.

DETAILED RATING CONSIDERATIONS

Detailed considerations for Banco BBM's currently assigned ratings are as follows.

Bank Financial Strength Rating

Moody's assigns a D+ rating, reflecting BBM's dynamic and capable business model, with a commercial lending operation supported by a prudent risk-evaluation framework that prioritizes the bank's asset quality and liquidity management profile. There is no difference between the scorecard outcome and the assigned BFSR of D+, which reflects the deterioration in asset quality ratio between 2008 until 2010 and the reduction of credit income as part of the portfolio deleverage process conducted until the end of 2009. The profitability factor also reflects the volatile earnings profile of BBM, with historically important proprietary trading gains. The high scores on Regulatory Environment also boost Moody's ratings.

Qualitative Rating Factors (70% weighting)

Factor 1: Franchise Value

Trend: Neutral

BBM's business franchise has been anchored on well-established wholesale-banking activities and a long track record of robust performance from proprietary trading operations. BBM has experience in the lending business since its inception, although the bank has shifted from its original target clients over the last few years.

In times of stress, the bank tends to adopt a more conservative attitude towards risk. At present, BBM holds a well-defined niche position focusing on upper-midsized companies, but it does not possess a major market share within this industry. In the beginning of 2010, management decided to resume to lending activities though with a limited leverage of 3 times equity base, while maintaining a proprietary trading portfolio that should be responsible for 30% to 40% of total earnings. However, still in June 2011, more than 70% of operating earnings derived from trading-related gains. Despite an established focus and well-disciplined risk-management framework, BBM is challenged to expand market share in a highly competitive environment--one dominated by major banks and foreign players. Scale should be a limiting factor in a more aggressive lending market with declining interest rates. Based on historical behaviors, we see BBM adopting a more cautious credit strategy as the bank resume to loan growth, than those of similar rates banks.

Factor 2: Risk Positioning

Trend: Neutral

BBM's E score on risk positioning is hurt by the influence of executive management and main shareholders at the board, which limits its corporate governance assessment. About 30% of the board of directors is composed by independent members. The bank counts on rigid and recognized risk management tools and control parameters, developed in-house. This provides a high level of comfort to trade in the local market, as well as aiding international positioning. Although ownership control is familiar, BBM is structured under a partnership, providing better governance than most other family-owned institutions.

The risk management function is completely detached from performance, although the key position on risk controls is performed by the CEO and the representative of the controller, the main shareholder of the institution. Consequently, this situation presents what we consider to be a "key man" risk.

Despite the tight controls, the bank's financial reporting is fairly limited, with restricted information on business lines, risk weighted assets, and Tier 1 equity.

The existing concentration of large groups is managed through a secured portfolio (69% of the portfolio is collateralized) and by the application of high credit standards, as indicated by the low levels of non-performing loans. BBM maintains a high level of liquidity on its balance sheet, which is largely encompassed by federal T-bills and overnight "repos."

Nevertheless, funding is mostly from the instruments of institutional investors, which tend to be expensive in nature; moreover, these are increasing in tenor length as they are part of meeting management's diversification targets.

Market risk appetite for a credit bank is still reasonable, although BBM reshaped its risk guidance centering its profit center in the credit platform.

Factor 3: Regulatory Environment

Moody's will comment on the Brazilian regulatory environment in a separate report.

Factor 4: Operating Environment

Trend: Neutral

Moody's grades the Brazilian operating environment at D. The D derives from a score of E for economic stability (measured as nominal GDP volatility over the 20-year period of 1985-2005, and there is also D rating for integrity and corruption. The integrity and corruption index is based on data from the World Bank, which ranks approximately 200 countries worldwide.

The legal system's score of C indicates the average length of time required for the execution of guarantees in Brazil in the absence of reliable references for mortgage foreclosure.

Quantitative Rating Factors (30% weighting)

Factor 5: Profitability

Trend: Neutral

Since 2009, profitability has suffered as the bank reduced the credit portfolio in face of higher risk aversion. Reduced credit income and a hike credit costs exhausted pre-provisions profits. As the bank walked through the negative cycle, cash liquidity was preserved in light of a difficult funding dynamics which required a prudent liquidity management, also a drain to performance.

Going forward, performance is expected to accommodate the growing lending activities that should compensate the reduction of fee-service gains as the asset management platform is fully segregated from the bank. However, at the same time, management conducted a significant reduction in cost structure and the bank now works with a leaner model that should positively influence performance in the long-run.

Factor 6: Liquidity

Trend: Neutral

BBM is a wholesale-funded institution, demonstrating management's clear and successful efforts to increase the mix and tenor. BBM has tight gap controls, and conservative hedging policies, which are part of the bank's business-sustainability philosophy. The large position in government securities works as a cushion in times of stress. The weakening trend evidences the vulnerability of its wholesale nature funding structure.

The bank's cash position is high and comfortable to meet the bank's obligations in the short-term.

Factor 7: Capital Adequacy

Trend: Neutral

Strong capitalization is contractually supported by shareholders. BBM have historically preserved a comfortable capital cushion to absorb both expected and unexpected losses in the credit and trading portfolio. As of June 2011, the bank has posted a 23.9% BIS ratio.

Factor 8: Efficiency

Trend: Neutral

An efficient cost structure is critical to keep the bank's ability to rapidly reshape strategy when needed, in response to market momentum. Despite the downsizing promoted in 2010/11, the cost to income ratio (in the scorecard) still reflects the declined earnings flow in this period.

Factor 9: Asset Quality

Trend: Improving

Asset quality score of C+ is expected to improve in the coming years, as the bank resume to lending activities and maintains a stringent risk profile. The C+ score still reflects the 3 year average considering 2009, 2009 and 2010, three years of strategic deleveraging and management decision to call on credits not yet matured that resulted in ratio deterioration. However, it is worth mentioning that with this approach management was able to successfully test the collateralization frameworks in a high risk scenario period, that reinforced their philosophy to maintain a rigid formalization of guarantees that are strong in risk periods.

The level of delinquency reported by BBM since the end of 2008 was quite distant from the bank's historically low NPLs ratio, a result from the balance sheet deceleration factor.

So, we expect asset quality score to improve going forward proven that BBM has superior asset quality. There is a high degree of selectiveness in credit relationships, which is reflected by the bank's low non-performing ratio over the last three years. BBM's delinquency ratio is far below its peers' indicators. The asset quality is also backed by adequate safeguards through guarantees and collateral.

Global Local Currency Deposit Rating (Joint Default Analysis)

Moody's Ba1 global local-currency deposit rating reflects BBM's very modest participation in the deposit market, and translates, in Moody's view, into no probability of systemic support. The partnership organizational structure, we believe, suggests that support would be forthcoming from this group, as proven by shareholders' historical behavior seeking capital protection. Therefore, the local currency rating is a direct mapping of BBM's Baseline Credit Assessment.

National Scale Rating

BBM is rated Aa2.br/BR-1 by Moody's on Brazil's National Scale. The rating is supported by creditworthiness in the domestic market; hence, the credit strength also reflects the wholesale nature of its business. This rating derives from the bank's global local-currency rating.

Foreign Currency Deposit Rating

Moody's assigns a Ba1 foreign currency deposit rating for Banco BBM. The rating is no further constrained by the country's foreign currency deposit ceiling for Brazil.

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. Bank Financial Strength Ratings 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 honor its domestic or foreign currency obligations. Factors considered in the assignment of Bank Financial Strength Ratings include bank-specific elements such as financial fundamentals, franchise value, and business and asset diversification. Although Bank Financial Strength Ratings 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.

Moody's uses the Baseline Credit Assessment (BCA) to map BFSRs onto the 21-point Aaa-C rating scale and like the BFSR, it reflects a bank stand- alone default risk. Each point on the Aaa-C scale represents a specific probability of default and therefore allows Moody's to use the BCA as an input to Moody's Joint Default Analysis (JDA), described below. The baseline credit assessment reflects what the local currency deposit rating of the bank with the given BFSR would be without any assumed external support from a government or third party.

Global Local Currency Deposit Rating

A deposit rating, as an opinion of relative credit risk, incorporates the Bank Financial Strength Rating 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, Moody's Bank Deposit Ratings are intended to incorporate those aspects of credit risk relevant to the prospective payment performance of rated banks with respect to deposit obligations, and 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 any external elements of support into the bank's Baseline Credit Assessment. In assigning the local currency deposit rating to a bank, the JDA methodology also factors in the rating of the various potential support providers (parent company, cooperative group, regional or national governments), as well as the degree of dependence that may exist between each one of them and the bank. Moody's assessment of the probability of systemic support (by a national government) is derived from the analysis of the capacity of a government and its central bank to provide support on a system-wide basis. The systemic support indicator is determined for a particular country and serves as an input for all bank ratings in that country. The support indicator can be set at, above or, in rare cases, below the government's local currency bond rating for that country.

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 a 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 obligations 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

Banco BBM S.A.

Rating Factors [1]	**A**	**B**	**C**	**D**	**E**	**Total Score**	**Trend**
Qualitative Factors (70%)						**D+**	
Factor: Franchise Value						**D**	**Neutral**
Market Share and Sustainability				**x**			
Geographical Diversification				**x**			
Earnings Stability				**x**			
Earnings Diversification [2]							
Factor: Risk Positioning						**E**	**Neutral**
Corporate Governance [2]					**x**		
- Ownership and Organizational Complexity				x			
- Key Man Risk				x			
- Insider and Related-Party Risks					x		
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					**x**		
- Borrower Concentration					x		
- Industry Concentration		x					
Liquidity Management			**x**				
Market Risk Appetite			**x**				
Factor: Operating Environment						**D**	**Neutral**

Economic Stability					x		
Integrity and Corruption				x			
Legal System			x				
Financial Factors (30%)						C	
Factor: Profitability						C	Neutral
PPI / Average RWA - Basel II			1.79%				
Net Income / Average RWA - Basel II			1.60%				
Factor: Liquidity						D	Neutral
(Mkt funds-Liquid Assets) / Total Assets					31.01%		
Liquidity Management			x				
Factor: Capital Adequacy						A	Neutral
Tier 1 Ratio - Basel II	17.73%						
Tangible Common Equity / RWA - Basel II	16.89%						
Factor: Efficiency						D	Neutral
Cost / Income Ratio				68.60%			
Factor: Asset Quality						C+	Improving
Problem Loans / Gross Loans				6.34%			
Problem Loans / (Equity + LLR)	6.46%						
Lowest Combined Score (9%)						D	
Economic Insolvency Override						Neutral	
Aggregate Score						D+	
Assigned BFSR						D+	

[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