Moody's Investors Service

Credit Opinion: Banco BBM S.A.

Global Credit Research - 25 Apr 2012

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]**12-11**	[2]**12-10**	[2]**12-09**	[2]**12-08**	[3]**12-07**	**Avg.**
Total Assets (BRL billion)	**2.3**	**5.0**	**10.6**	**14.2**	**17.3**	[4]**-39.4**
Total Assets (USD billion)	**1.3**	**3.0**	**6.1**	**6.1**	**9.7**	[4]**-40.1**
Tangible Common Equity (BRL billion)	**0.5**	**0.5**	**0.6**	**0.7**	**1.0**	[4]**-14.5**
Tangible Common Equity (USD billion)	**0.3**	**0.3**	**0.4**	**0.3**	**0.6**	[4]**-15.5**
Net Interest Margin (%)	**2.8**	**1.9**	**2.5**	**1.9**	**7.4**	[5]**3.3**
PPI / Avg RWA (%)	**1.1**	**1.7**	**2.3**	**1.4**	**15.4**	[6]**1.6**
Net Income / Avg RWA (%)	**2.9**	**1.4**	**1.5**	**1.9**	**10.3**	[6]**1.9**
(Market Funds - Liquid Assets) / Total Assets (%)	**5.0**	**39.8**	**2.0**	**51.2**	**15.7**	[5]**22.7**
Core Deposits / Average Gross Loans (%)	**86.3**	**46.5**	**44.2**	**50.2**	**86.8**	[5]**62.8**
Tier 1 Ratio (%)	**22.5**	**24.1**	**14.5**	**14.5**	**16.3**	[6]**18.9**
Tangible Common Equity / RWA (%)	**21.9**	**24.0**	**14.2**	**14.2**	**16.1**	[6]**18.6**
Cost / Income Ratio (%)	**78.3**	**72.0**	**61.2**	**72.6**	**17.3**	[5]**60.3**
Problem Loans / Gross Loans (%)	**0.5**	**6.7**	**1.2**	**-0.4**	**1.0**	[5]**1.8**
Problem Loans / (Equity + Loan Loss Reserves) (%)	**0.8**	**6.1**	**2.0**	**-1.6**	**4.0**	[5]**2.2**

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 that captures a SME focused operation and a long-track record of volatile earnings generation with strong contribution from 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 weigh the volatile earnings component from trading gains which continues to be relevant, despite the recent business resdimensioning.

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 remains sound, helping to absorb the negative effects of this strategy. Since the end of 2010, based on improved credit conditions, the bank decided to pick up its lending pace, though, in a very contained fashion. At present, BBM is challenged to resume loan growth in 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, despite the relevant participation of individual clients that account for 34% of total time deposits, 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 through cycles

- Swings in strategy as the bank adopted a conservative approach to credit risk have affect performance over last 3 years: needs to improve earnings recurrence generation, sustaining performance while maintaining a balanced approach to credit activities

- Still restrictive funding structure with a well concentrated deposit portfolio

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

Banco BBM reported net income of R$67 million in 2011, up by 42.5% year over year. Bottom line results were benefited by increasing credit activities that adds recurrence to performance, but still positively influenced by reversion of provisions for loan losses in the amount of R$81 million in 2011 (R$27 million in 2010), a non-recurring gain. Operating revenues were composed 55% by credit income, 36.6% trading activities and 8.4% by fee services from the asset management business controlled by Banco BBM until April 2011. In 2011, the performance was positively influenced by the cost re-dimensioning that reduced by 25% administrative and personnel expenses . In June 2011, the annualized net income over risk-weighted assets reached 3.63%.

While total assets reduced by 53.3% in 2011, loan book jumped 62.5% in the year presenting high concentration issues mitigated by strong collateral framework of the portfolio, a factor that is in line with peers'. In June 2011, the loan book amounted to R$967 million on a consolidated basis with 1% of total loans presenting delays in payment and only 0.5% with delays over 90 days. Despite the significant amount of reverted provisions, BBM maintains a reserve coverage ratio of 3.7% of the portfolio.

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 1.8x (credit portfolio over equity) with management indicating a cap of 3 times as the bank expands, both Tier 1 and total capital ratio stood at high 22%, leaving substantial room to support growth.

DETAILED RATING CONSIDERATIONS

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

LIQUIDITY

BBM is a wholesale-funded institution, demonstrating management's clear and successful efforts to increase the mix and tenor. The high concentration of its deposit base -- 20 largest depositors accounted for 73% of total deposits in 2011 -- is mitigated by BBM's tight gap controls and conservative hedging policies, which are part of the bank's business-sustainability philosophy. In 2011, the average tenor of the bank's deposit base was 475 days and the average tenor of total loans was 268 days.

Management has centered efforts on instruments diversification that brings tenor lengthening and more predictability to cash management. The bank has been increasing the issuance of local currency fixed income instruments such letra financeira and other asset-backed securities such as agribusiness linked notes and RMBS, taking advantage of increased demand for fixed income bonds, which in some cases have good cost conditions since banks are not required to place reserve requirement at the Central Bank.

The large position in government securities works as a cushion in times of stress together with a conservative cash policy comfortable to meet the bank's 90-day horizon obligations and strong rules that prioritize the duration of deposits that allows the bank to work with no liquidity gap, different from most of its peer's conditions. In December 2011, the bank had R$899 million in cash liquidity that accounted for 113% of total deposits.

ASSET QUALITY / RISK POSITIONING

Strong credit underwriting policies and entrenched controls have protected the bank from credit and market risk disruptions through cycles. The temporary jump in NPLs ratios between 2009 (6.84%) and 2010 (15.54%) resulted from a decision to deleverage the lending activities anticipating the liquidation of some outstanding. This strategy was absorbed by a high level of reserves and ample capital base, as well as a strong collateral framework on the credits that allowed the bank to recover all credits without incurring in significant losses (NCO ratio was 3.99% and 2.33% in 2010 and 2009, respectively). Historically, BBM presented a low NPL ratio below 1%.

BBM has a rigid and recognized risk management architecture and control parameters that have proven capable of supporting the bank's risk appetite through cycles. This has provided a high level of comfort to the trading activities, as well as strong framework of collateralization of the portfolio that worked well during 2008 and 2009.

The risk concentration is an intrinsic challenge for BBM and similar rated banks. The existing concentration of large groups is managed through a secured portfolio (70% of the portfolio is collateralized) and by the application of high credit standards, as indicated by the low levels of non-performing loans. In 2011, the 20 largest loans accounted for 80.5% of reported Tier 1 equity and for more than 8 times pre-provision income reported in 2011.

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. We expect asset quality to recover to historically superior levels than its midsize peers (NPLs below 1%), reflecting the bank's high degree of selectiveness in credit relationships and credit scoring that results in prudent levels of provisions to absorb unexpected losses.

CAPITAL

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. Capital has always support the strategic repositioning which has been present over the life of BBM always prioritizing risk controls and positive performance.

While the aggressive credit growth projected by management is expected to reduce the high capital level reported over the last three quarters, we expect that as the portfolio grows the internal earnings generation should improve supporting the replenishment of capital. For 2012, management indicated that a maximum credit leverage of three times the equity to be ideal as the bank expands, a ratio that stays well below the peaked 4.12 times in 2007. At the end of 2011, the leverage ratio was 1.8 times the equity and a 22% BIS ratio formed by high quality capital fully composed of Tier 1 instruments.

PROFITABILITY

The deleveraging of credit portfolio started in 2008 drained profitability ratios that are expected to recover as the bank resumes lending activities and enhancing recurring earnings generation. Reduced credit income and a hike credit costs exhausted pre-provisions profits. However, at the same time, management conducted significant reduction in cost structure and the bank now works with a leaner model that should positively influence performance in the long-run. In 2011, the expansion of credit activities has helped to improve recurring results with credit for accounting for 55% of total operational revenues, trading gains for 37% and asset quality for 8%.

With an active trading desk, BBM's performance carries a volatile component that exposes the bank to adverse scenario. However, treasury activities are largely related to spot FX transactions as the bank acts as a FX dealer in the system and proprietary positions in interest rates mitigated by conservative VaR limits in terms of equity; 2% established since May 2009. Over the last 5 years, BBM did not report losses, which proves the bank's strong market risk management.

For the next 12-18 months, profitability is expected to improve as BBM resume to credit growth compensating the decline of fee-income from the asset management activities fully segregated since the second half of 2011. Since 2011, efforts to reduce operational cost by 25% should also help to improve bottom line results.

FRANCHISE VALUE

BBM's business franchise has been anchored on wholesale-banking activities and a long track record of robust performance from trading operations. BBM has experience in the lending business since its inception, however the credit strategy depends on credit and funding conditions, rapidly increasing risk aversion and deleveraging the credit portfolio in times of heighted uncertainties. Therefore, earnings stability is the main issue of BBM's franchise, that, different from peers, presents great volatility across the cycles as the focus moves from credit to trading and vice-versa

At present, BBM has a niche operation focused on small and medium size companies with annual sales above R$180 million, with no major market position within this industry, and maintains an active proprietary trading that responded for roughly 37% of operating earnings in 2011.

Despite an established focus and well-disciplined risk-management framework, BBM is challenged to expand market share in a 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.

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%)						**C-**	
Factor: Franchise Value						**D**	**Neutral**
Market Share and Sustainability				**x**			
Geographical Diversification				**x**			
Earnings Stability				**x**			
Earnings Diversification [2]							
Factor: Risk Positioning						**D**	**Neutral**
Corporate Governance [2]				**x**			
- Ownership and Org. Complexity				x			
- Key Man Risk				x			
- 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					**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**	**Improving**
PPI / Average RWA - Basel II			2.29%				
Net Income / Average RWA - Basel II			1.49%				
Factor: Liquidity						**C-**	**Neutral**
(Market funds - Liqud Assets) / Total Assets				15.60%			
Liquidity Management			x				
Factor: Capital Adequacy						**A**	**Neutral**
Tier 1 Ratio - Basel II	20.38%						
Tangible Common Equity / RWA - Basel II	20.00%						
Factor: Efficiency						**D**	**Neutral**
Cost Income ratio				70.47%			
Factor: Asset Quality						**B**	**Improving**
Problem Loans / Gross Loans			2.79%				
Problem Loans / (Shareholders' Equity + Loan Loss Reserves)	2.94%						
Lowest Combined Financial Factor Score (9%)						**C-**	
Economic Insolvency Override						**Neutral**	
Aggregate Score						**C-**	
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.