

CREDIT OPINION

3 May 2018

Update

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RATINGS

Banco BOCOM BBM S.A.

Domicile	Rio de Janeiro, Rio de Janeiro, Brazil
Long Term Debt	Withdrawn
Type	Senior Unsecured - Dom Curr
Outlook	Rating(s) WithDrawn
Long Term Deposit	Ba3
Type	LT Bank Deposits - Fgn Curr
Outlook	Stable

Please see the [ratings section](#) at the end of this report for more information. The ratings and outlook shown reflect information as of the publication date.

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Banco BOCOM BBM S.A.

Update following sovereign action

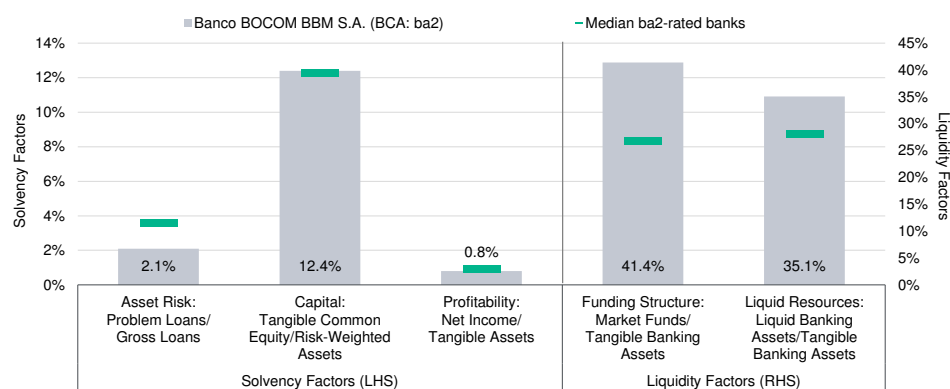
Summary

On 10 April 2018, the existing ratings and assessments assigned to [Banco BOCOM BBM S.A.](#) (BOCOM BBM) were affirmed. The outlook on all ratings was changed to stable from negative following the change in the outlook on [Brazil's](#) Ba2 sovereign rating to stable from negative on 9 April 2018.

BOCOM BBM's Baseline Credit Assessment (BCA) of ba2 incorporates the bank's modest asset risk, illustrated by a track record of low loan losses. Notwithstanding the recent rise in borrower concentration owing to an increase in loans with large corporations, the bank mitigates credit risk by focusing on customers with better risk profiles. At the same time, profitability could be positively influenced by the bank's lower cost of funds and higher gains of scale, which are likely to offset the potential credit cost fluctuation arising from its loan book concentration. Capital is likely to accommodate at still-solid levels despite the likelihood of increasing leverage. The bank's reliance on market funds is likely to remain high, but it will likely have access to a wider pool of investors and may even benefit from new funding facilities provided by its parent, China's [Bank of Communications Co., Ltd.](#) (BoCom, A3 stable, ba1).

Exhibit 1

Rating Scorecard - Key financial ratios



Source: Moody's Financial Metrics

BOCOM BBM's long-term local-currency deposit and senior unsecured debt ratings of Ba1 derive from its Adjusted BCA of ba1, which incorporate a one-notch uplift from its BCA of ba2. The uplift reflects the high level of affiliate support, given BoCom's majority ownership stake of 80% (acquired in November 2016) and the strategic importance of the subsidiary. We also assign a Ba3 long-term foreign-currency deposit rating, which is constrained by the country ceiling.

Credit strengths

- » Asset risk is mitigated by effective credit risk management, while higher borrower concentration is offset by the bank's improved risk profile
- » Strong capital position, despite increased leverage

Credit challenges

- » High reliance on market funding, partially offset by the bank's sizable cash position and the likely access to facilities from the parent
- » Volatile profitability, given the intrinsic borrower concentration in the bank's loan portfolio, which may be offset by lower cost of funds and gains of scale

Outlook

Since 10 April 2018, all ratings have a stable outlook. BOCOM BBM's Ba2 deposit ratings are at the same level as that of Brazil's sovereign bond rating and, therefore, the outlook is in line with the outlook on Brazil's sovereign bond rating.

Factors that could lead to an upgrade

- » There is no upward pressure at the moment because BOCOM BBM's ratings are currently constrained by Brazil's sovereign bond rating of Ba2. An upgrade of Brazil's bond rating would likely exert upward pressure on the bank's BCA and deposit ratings.

Factors that could lead to a downgrade

- » BOCOM BBM's ratings could be downgraded in case of a higher-than-expected deterioration in its capital position and asset risk profile following the new strategic focus and eventual higher balance sheet leverage. In addition, a multi-notch downgrade of BoCom's BCA could lead to a downgrade of BOCOM BBM's deposit ratings.

Key indicators

Exhibit 2

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

	12-17 ²	12-16 ²	12-15 ²	12-14 ²	12-13 ²	CAGR/Avg. ³
Total Assets (BRL billion)	5.1	4.1	3.8	3.1	3.2	12.3 ⁴
Total Assets (USD billion)	1.5	1.3	1.0	1.2	1.4	3.1 ⁴
Tangible Common Equity (BRL billion)	0.6	0.6	0.6	0.6	0.6	0.6 ⁴
Tangible Common Equity (USD billion)	0.2	0.2	0.1	0.2	0.2	-7.6 ⁴
Problem Loans / Gross Loans (%)	2.1	1.0	0.9	0.2	1.0	1.0 ⁵
Tangible Common Equity / Risk Weighted Assets (%)	12.4	14.1	13.3	18.5	21.3	15.9 ⁶
Problem Loans / (Tangible Common Equity + Loan Loss Reserve) (%)	7.9	2.2	2.1	0.5	2.0	3.0 ⁵
Net Interest Margin (%)	4.8	3.7	3.4	3.7	5.7	4.3 ⁵
PPI / Average RWA (%)	2.3	1.5	1.2	1.6	3.9	2.1 ⁶
Net Income / Tangible Assets (%)	0.8	0.8	1.1	1.4	1.5	1.1 ⁵
Cost / Income Ratio (%)	57.9	60.3	66.7	61.5	46.9	58.7 ⁵
Market Funds / Tangible Banking Assets (%)	41.4	41.2	58.1	44.9	13.2	39.8 ⁵
Liquid Banking Assets / Tangible Banking Assets (%)	35.1	50.7	58.1	47.6	43.8	47.0 ⁵

This publication does not announce a credit rating action. For any credit ratings referenced in this publication, please see the ratings tab on the issuer/entity page on www.moody's.com for the most updated credit rating action information and rating history.

Gross Loans / Due to Customers (%)	106.7	77.8	143.8	174.9	90.8	118.8 ⁵
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[1] All figures and ratios are adjusted using Moody's standard adjustments. [2] Basel III - fully-loaded or transitional phase-in; LOCAL GAAP. [3] May include rounding differences due to scale of reported amounts. [4] Compound Annual Growth Rate (%) based on time period presented for the latest accounting regime. [5] Simple average of periods presented for the latest accounting regime. [6] Simple average of Basel III periods presented.

Source: Moody's Financial Metrics

Profile

Founded in the northeast of Brazil in 1858, Banco BOCOM BBM S.A. started operations as Banco da Bahia, dedicated to retail and middle-market lending activities. In 1998, the bank's commercial arm, Banco da Bahia, merged with the investment bank Banco da Bahia Investimentos and formed a multiple banking structure, and changed its name to Banco BBM S.A. On May 2015, Bank of Communications Co., Ltd. announced the acquisition of an 80% stake in the bank. The remaining 20% of the bank is owned by the former shareholders, comprised mainly the Mariani family.

Originally, BOCOM BBM's core business was wholesale commercial lending, proprietary trading activities and asset management. In 2003, the bank began to diversify its earnings base by expanding commercial lending to upper-middle-market companies in Brazil, mainly in the form of working capital loans in local currency or trade-finance-related credit operations. As of today, the bank's corporate lending is largely secured by guarantees or contractual cash flow.

Detailed credit considerations

Higher borrower concentration will be offset by the improved risk profiles of customers

BOCOM BBM's Asset Risk score of baa3 reflects the bank's track record of low problem loan ratios, supported by strict underwriting standards and reduced charge offs. The score also incorporates the bank's expanded focus on large corporations, which increases borrower concentration. Despite that, the bank mitigates credit risk by focusing on customers with robust risk profiles.

The acquisition of Banco BBM's operations by BoCom has contributed to the expansion of the bank's loan book, particularly as a result of access to new borrowers, including large corporates and Chinese companies. Because the bank targets large corporations, its consistently strong asset quality may improve further, although the risk of increasing loan concentration may rise volatility in asset risk and earnings.

In December 2017, BOCOM BBM's total credit exposure, including guarantees, amounted to BRL3.4 billion, which represented 78% annual growth. The rise in lending was driven by the bank's efforts to increase credit leverage. At the same time, the bank's problem loan ratio increased to 2.0% from 1.0% a year earlier. Reserve coverage remained high, at 3.2% of total loans, reflecting management's conservative approach to credit risk.

Strong credit underwriting policies and entrenched controls have protected BOCOM BBM from credit and market risk disruptions through economic cycles. Historically, the bank has reported low problem loan ratios, supported by a rigid and recognized risk management architecture, and control parameters that have proved capable of supporting the bank's risk appetite, as well as collateralization of the portfolio in previous bad cycles.

At the same time, we note that the bank's portfolio is relatively concentrated, with the 20 largest borrowers representing 38% of total exposure in December 2017 and 225% of tangible common equity.

Capital remains strong despite robust loan growth

BOCOM BBM's Capital score of ba2 takes into consideration the current level of its capital ratio and the capital consumption arising from the likely increase in its leverage.

We expect the bank to leverage its balance sheet, leading to capitalization metrics that will be lower than the current 12.4% ratio of tangible common equity to risk-weighted assets and the 11.2% regulatory Common Equity Tier 1 capital ratio. However, the bank's capital position is likely stabilized at still-solid levels.

Profitability will likely benefit from lower funding costs and larger scale

BOCOM BBM's Profitability score of ba2 incorporates the potential incremental pressures from higher loan-loss provisions, which are likely to be counterbalanced by the lower cost of funds and higher gains of scale.

Profitability is likely to increase owing to the greater scale that the bank will gain as it grows its balance sheet size while maintaining almost the same administrative infrastructure. However, the improvement in profitability may be partially offset by lower yields from lending to newly targeted companies and by the higher risk of credit cost fluctuation from increased borrower concentration.

In December 2017, the ratio of net income to tangible banking assets increased slightly to 0.85% from 0.80% a year earlier. The high levels of credit costs were partially offset by the bank's ability to increase credit spreads, illustrated by the 4.80% net interest margin in 2017 versus 3.72% in 2016.

Defensive liquidity management mitigates high reliance on market funds

The Combined Liquidity score of ba3 reflects the bank's high reliance on market funding. However, it also incorporates the large amount of liquid assets held by the bank and a favorable tenor gap in its balance sheet.

We expect BOCOM BBM's reliance on market funds to remain high, although the bank will likely have access to a wider pool of investors. In addition, it will likely benefit from the new funding facilities provided by the parent. These factors will support the bank's expanded strategic focus, enabling it to appropriately manage its liquidity in response to a possible extension of its assets duration.

BOCOM BBM's reliance on market funds is illustrated by the concentration of its deposit base, with the 20 largest investors accounting for 69% of total funding in December 2017. However, the bank mitigates this concentration by maintaining tight gap controls and conservative hedging policies, which are part of the bank's asset and liability management standards. The bank has been managing tenor gaps and costs by issuing local-currency debt instruments (letras financeiras, with a minimum two-year tenor) and other asset-backed securities, such as agribusiness-linked notes and residential mortgage-backed securities. BOCOM BBM has also taken advantage of the increased demand for fixed income bonds, which, in some cases, have lower costs because banks are not required to place reserve requirements at the central bank. These local-currency instruments accounted for BRL2.4 billion in December 2017, representing about 59% of the funding mix. Although BOCOM BBM has a relatively low reliance on foreign-currency lines, which represent 28% of total funding and consist mainly of a term line from the [International Finance Corporation](#) (Aaa stable), this exposure will likely increase as the bank gains access to a wider pool of investors.

BOCOM BBM's large position in government securities works as a buffer in times of stress, together with a conservative cash policy, which is comfortable and meets the bank's 180-day horizon obligations. The bank also adopts strong rules that prioritize the duration of deposits, which allow the bank to work with no liquidity gap, unlike most of its peers.

BOCOM BBM's rating is supported by the Moderate- Macro Profile of Brazil

Brazil's Moderate- Macro Profile reflects the country's large and diversified economy, balanced by the country's weak economic performance following two years of recession and the difficult political scenario, which together increase challenges for Brazilian banks' operating environment. The pace of loan growth declined significantly in 2016 and falling inflation has resulted in monetary policy easing. However, banks remain reluctant to reduce lending rates, which has relieved part of the earnings pressure arising from asset risks. Although public banks hold a 57% share of total loans in Brazil, loan growth at these lenders has slowed significantly since mid 2016 owing to more prudent government guidelines, which we expect will remain in place, and help reduce pricing and tenor distortions. Capital and funding remain adequate, and exposure to the international capital markets will remain low. External vulnerability is also limited by Brazil's sizable international reserves, which reduce the country's sensitivity to external shocks, such as sudden stops in capital flows.

The change in Macro Profile to Moderate- occurred in June 2017 (previously Moderate), and resulted from the increased political risk that affected the Banking Country Risk component, a key driver in our Macro Profile Assessment. By lowering Brazil's Macro Profile to Moderate-, the factor scores used in assessing banks' individual financial profiles, and, thus, to define the BCA, are compressed at lower levels.

Support and structural considerations

Affiliate support

We believe there is a high probability of affiliate support for BOCOM BBM from its controlling bank, BoCom, given its majority ownership stake and the strategic importance that the Brazilian subsidiary may have for its parent bank. BoCom is expected to appoint executives to certain key positions at the bank and will closely engage in the subsidiary's strategic decisionmaking process, including

BOCOM BBM's support to the operations of Chinese companies in Brazil. Therefore, BOCOM BBM's Adjusted BCA of ba1 has a one-notch uplift from its ba2 BCA.

Government support

BOCOM BBM's local-currency deposit and senior unsecured ratings of Ba1 derive from its ba1 Adjusted BCA and do not benefit from government support uplift, given the bank's modest market share of domestic deposits.

Counterparty Risk (CR) Assessment

CR Assessments are opinions of how counterparty obligations are likely to be treated if a bank fails and are distinct from debt and deposit ratings in that they (1) consider only the risk of default rather than both the likelihood of default and the expected financial loss suffered in the event of default, and (2) apply to counterparty obligations and contractual commitments rather than debt or deposit instruments. The CR Assessment is an opinion of the counterparty risk related to a bank's covered bonds, contractual performance obligations (servicing), derivatives (for example, swaps), letters of credit, guarantees and liquidity facilities.

BOCOM BBM's CR Assessment is positioned at Baa3(cr)/Prime-3(cr)

The CR Assessment is one-notch above the bank's Adjusted BCA of ba1, and, therefore, above the deposit rating of the bank, reflecting our view that its probability of default is lower at the operating obligations than of deposits. BOCOM BBM's CR Assessment does not benefit from government support because government support is not incorporated in the bank's deposit ratings.

About Moody's Bank Scorecard

Our scorecard is designed to capture, express and explain in summary form our Rating Committee's judgment. When read in conjunction with our research, a fulsome presentation of our judgment is expressed. As a result, the output of our scorecard may materially differ from that suggested by raw data alone (though it has been calibrated to avoid the frequent need for strong divergence). The scorecard 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 methodology and scorecard factors

Exhibit 3

Banco BOCOM BBM S.A.

Macro Factors

Weighted Macro Profile	Moderate	100%
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Factor	Historic Ratio	Macro Adjusted Score	Credit Trend	Assigned Score	Key driver #1	Key driver #2
Solvency						
Asset Risk						
Problem Loans / Gross Loans	2.1%	baa3	← →	baa3	Sector concentration	
Capital						
TCE / RWA	12.4%	ba1	← →	ba2	Expected trend	
Profitability						
Net Income / Tangible Assets	0.8%	ba2	← →	ba2	Expected trend	
Combined Solvency Score		ba1		ba1		
Liquidity						
Funding Structure						
Market Funds / Tangible Banking Assets	41.4%	b3	← →	b3	Market funding quality	
Liquid Resources						
Liquid Banking Assets / Tangible Banking Assets	35.1%	baa3	← →	baa3	Quality of liquid assets	
Combined Liquidity Score		ba3		ba3		
Financial Profile				ba2		
Business Diversification				0		
Opacity and Complexity				0		
Corporate Behavior				0		
Total Qualitative Adjustments				0		
Sovereign or Affiliate constraint:				Ba2		
Scorecard Calculated BCA range				ba1-ba3		
Assigned BCA				ba2		
Affiliate Support notching				--		
Adjusted BCA				ba1		
Instrument class	Loss Given Failure notching	Additional Notching	Preliminary Rating Assessment	Government Support notching	Local Currency Rating	Foreign Currency Rating
Counterparty Risk Assessment	1	0	baa3 (cr)	0	Baa3 (cr)	--
Deposits	0	0	ba1	0	Ba1	Ba3

Source: Moody's Financial Metrics

Ratings

Exhibit 4

Category	Moody's Rating
BANCO BOCOM BBM S.A.	
Outlook	Stable
Bank Deposits -Fgn Curr	Ba3/NP
Bank Deposits -Dom Curr	Ba1/NP
NSR Bank Deposits	Aaa.br/BR-1
Baseline Credit Assessment	ba2
Adjusted Baseline Credit Assessment	ba1
Counterparty Risk Assessment	Baa3(cr)/P-3(cr)
PARENT: BANK OF COMMUNICATIONS CO., LTD.	
Outlook	Stable
Bank Deposits	A3/P-2
Baseline Credit Assessment	ba1
Adjusted Baseline Credit Assessment	ba1
Counterparty Risk Assessment	A3(cr)/P-2(cr)
Pref. Stock Non-cumulative	B1 (hyb)

Source: Moody's Investors Service

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