

CREDIT OPINION

7 December 2017

Update

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RATINGS

Banco BBM S.A.

Domicile	Rio de Janeiro, Rio de Janeiro, Brazil
Long Term Debt	Ba1
Type	Senior Unsecured - Dom Curr
Outlook	Negative
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.

Contacts

Alexandre Albuquerque 55-11-3043-7356
VP-Senior Analyst
alexandre.albuquerque@moodys.com

Alcir Freitas 55-11-3043-7308
VP-Sr Credit Officer
alcir.freitas@moodys.com

Aaron Freedman 52-55-1253-5713
Associate Managing Director
aaron.freedman@moodys.com

Banco BBM S.A.

Update to credit analysis

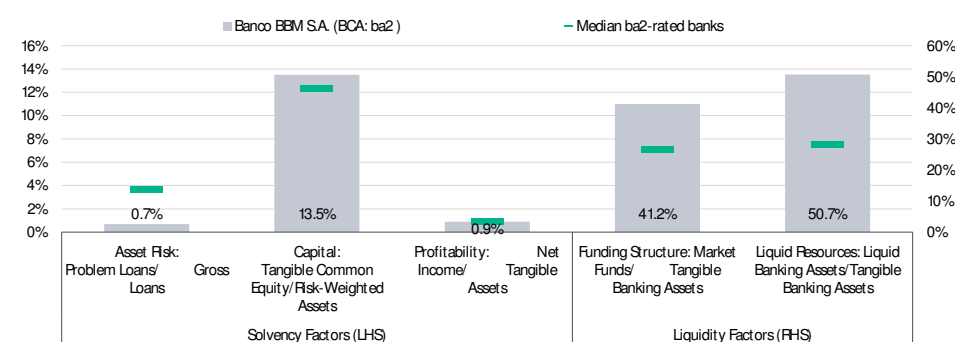
Summary Rating Rationale

[Banco BBM S.A.](#)'s (BBM) baseline credit assessment of ba2 incorporates the bank's modest asset risk, evidenced 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 better risk profile of customers. At the same time, profitability could be positively influenced by the lower cost of funds and higher gains of scale, which is expected to offset the potential credit cost fluctuation arising from loan book concentration. Capital is expected to accommodate at still solid levels despite the increasing anticipated leverage. BBM's reliance on market funds is expected to remain high, but the bank will likely have access to a wider pool of investors, and it may even benefit from new funding facilities provided by the parent.

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. It reflects the high level of affiliate support from China's Bank Communication Co., Ltd. (BoCom, A3 stable, ba1), given the majority ownership stake of 80%, acquired in November 2016, as well as the strategic importance of the subsidiary. We also assign a Ba3 long-term foreign currency deposit rating, which is constrained by the country ceiling.

Exhibit 1

Rating Scorecard - Key Financial Ratios



Source: Moody's Financial Metrics

THIS REPORT WAS REPUBLISHED ON 12 DECEMBER 2017 WITH CORRECTION TO TOTAL CREDIT EXPOSURE AND PROBLEM LOAN RATIOS IN THE THIRD PARAGRAPH ON PAGE 3, AND PARTICIPATION OF FOREIGN CURRENCY LINES TO TOTAL FUNDING IN THE FIRST PARAGRAPH ON PAGE 4.

Credit Strengths

- » Asset risk supported by effective credit risk management, while higher borrower concentration is offset by improved risk profile
- » Capital position is strong, despite increased leverage

Credit Challenges

- » Market funding reliance is partially offset by sizeable cash position and by the likely access to facilities from the parent
- » Profitability is subject to volatility given the intrinsic borrower concentration from its loan portfolio, while it may be offset by lower cost of funds and gains of scale

Rating Outlook

The outlook on BBM's global local currency deposit and foreign currency senior unsecured debt is negative, in line with the outlook on Brazil's sovereign bond rating.

Factors that Could Lead to an Upgrade

BBM's ratings could be upgraded if the support assumptions or the parent bank's BCA are raised. BBM's ba2 BCA is unlikely to be upgraded because it is already positioned at the same level of the sovereign bond rating.

Factors that Could Lead to a Downgrade

BBM's ratings could be downgraded if Brazil's sovereign rating and its country ceilings are downgraded. Also, a multi-notch downgrade on BoCom's BCA could lead to a downgrade on BBM's ratings. BBM's ratings could also be downgraded if its BCA is lowered, which could be associated with higher-than-expected deterioration of its capital position and asset risk profile, following the new strategic focus and an eventual higher balance sheet leverage.

Key indicators

Exhibit 2

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

	6-17 ²	12-16 ²	12-15 ²	12-14 ²	12-13 ²	CAGR/Avg. ³
Total Assets (BRL billion)	5.3	4.1	3.8	3.1	3.2	15.0 ⁴
Total Assets (USD billion)	1.6	1.3	1	1.2	1.4	4.4 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	-8.7 ⁴
Problem Loans / Gross Loans (%)	0.6	1.0	0.9	0.2	1.0	0.8 ⁵
Tangible Common Equity / Risk Weighted Assets (%)	13.5	14.1	13.3	18.5	21.3	16.2 ⁶
Problem Loans / (Tangible Common Equity + Loan Loss Reserve) (%)	2.0	2.2	2.1	0.5	2.0	1.8 ⁵
Net Interest Margin (%)	5.0	3.7	3.4	3.7	5.7	4.3 ⁵
PPI / Average RWA (%)	2.6	1.5	1.2	1.6	3.9	2.2 ⁶
Net Income / Tangible Assets (%)	0.9	0.8	1.1	1.4	1.5	1.1 ⁵
Cost / Income Ratio (%)	50.9	60.3	66.7	61.5	46.9	57.3 ⁵
Market Funds / Tangible Banking Assets (%)	33.1	41.2	58.1	44.9	13.2	38.1 ⁵
Liquid Banking Assets / Tangible Banking Assets (%)	30.4	50.7	58.1	47.6	43.8	46.1 ⁵
Gross Loans / Due to Customers (%)	99.6	77.8	143.8	174.9	90.8	117.4 ⁵

[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

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.

Detailed Rating Considerations

Higher borrower concentration will be offset by improved risk profile of customers

We score asset risk as baa3, which reflects BBM'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, BBM mitigates credit risk by focusing on customers with a better risk profile.

The acquisition of BBM's operation by BoCom will likely result in the expansion of the bank's loan book, because it will enable BBM to access a potential universe of new borrowers, including large corporate and Chinese companies. As the bank targets large corporations, its consistently strong asset quality may improve further, although the risk of increasing loan concentration may add volatility to asset risk and earnings.

In June 2017, BBM's total credit exposure, including guarantees, amounted to BRL3.2 billion, which represented a 63% annual growth and was driven by the bank's efforts to increase credit leverage. At the same date, BBM's problem loan ratio dropped to 0.4% from 0.7% in December 2016, staying slightly above the ratio of 0.3% one year prior. Reserve coverage also remained high, at 3.26% of total loans, reflecting management's conservative approach to credit risk.

Strong credit underwriting policies and entrenched controls have protected the bank from credit and market risk disruptions through economic cycles. Historically, BBM has reported low problem loan ratios, supported by a rigid and recognized risk management architecture and control parameters that have proven 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 37% of total exposure in June 2017, and 191% of tangible common equity (TCE).

Capital remains strong despite robust loan growth

We score capital as ba2, which takes into consideration the current level of BBM's capital ratio and the capital consumption arising from the expected increase in its leverage.

We expect the bank to leverage its balance sheet, leading to capitalization ratios that will be lower than the current 13.5% tangible common equity to risk weighted assets, and the 17.9% regulatory common equity tier 1 ratio. However, its capital position is likely stabilized at still solid levels.

Profitability will likely benefit from lower funding costs and larger scale

We score profitability as ba2, incorporating the potential incremental pressures from higher loan loss provisions, which are expected to be counterbalanced by lower cost of funds and higher gains of scale.

Profitability is expected to be positively impacted by the greater scale that the bank will gain as it grows its balance sheet size while keeping almost the same administrative infrastructure. However, profitability improvement may be offset partially by the lower yield of lending to the new targeted companies, and by the higher risk of credit cost fluctuation from the increased borrower concentration.

In June 2017, the ratio of net income to tangible banking assets fell to 0.88%, compared to 1.02% one year prior. The high levels of credit costs were offset partially by the bank's ability to increase credit spreads, evidenced by the 4.98% net interest margin in June 2017, versus 4.17% in June 2016.

Defensive liquidity management mitigates high reliance on market funds

The combined score of ba3 for liquidity 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 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 new funding facilities provided by the parent. This will support BBM's expanded strategic focus, enabling the bank to manage appropriately its liquidity in response to a possible extension of its assets duration.

BBM's reliance on market funds is evidenced by the concentration of its deposit base, with the 20 largest investors accounting for 77% of total deposits in June 2017. However, BBM mitigates this concentration by keeping 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 2-year tenor) and other asset-backed securities such as agribusiness linked notes and RMBS. BBM has also taken advantage of 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 BRL2.0 billion in June 2017, representing about 42% of the funding mix. Although the bank has small reliance on foreign currency lines, which represents 22% of total funding and consists mainly of a term line from the IFC, this exposure will likely increase as BBM gains access to a wider pool of investors.

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

BBM's rating is supported by the "Moderate-" macro profile on Brazil

Brazil's Moderate- macro profile reflects the country's large and diversified economy, balanced by its weak economy's performance following two years of recession and the difficult political scenario which together increase challenges to Brazilian banks' operating environment. The pace of loan growth reduced 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, under more prudent government guidelines, which we expect will remain in place, and which will help to reduce pricing and tenor distortions. Capital and funding remain adequate, and exposure to international capital markets will remain low. External vulnerability is also limited by Brazil's sizeable 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 at Moderate), and resulted from the increased political risk that affected the Banking Country Risk component, a key driver in Moody's macro profile assessment. By lowering Brazil MP to Moderate-, the factor scores used in assessing banks' individual financial profile, and, thus, to define the BCA, are compressed at lower levels.

Notching Considerations

Given the absence in Brazil of an operational going-concern resolution regime (ORR) wherein banks are resolved by bailing-in creditors, the impact of failure on a bank's different debt classes absent government support (i.e. bail-out) is unclear as we believe that resolution procedures will be determined on an ad-hoc basis, rather than being clearly defined ex ante. The expected loss of each debt class is derived from a standardized instrument notching for all non-ORR banks.

Affiliate Support

We believe there is a high probability of affiliate support for BBM from its controlling bank, Bank of Communications Co. Ltd., given its majority ownership stake and the strategic importance that the Brazilian subsidiary may have to its controlling bank. BoCom is expected to appoint executives to certain key positions at the bank and will closely engage in the subsidiary's strategic decision making process, including BBM's support to operations of Chinese related companies in Brazil. Therefore, BBM's adjusted BCA of ba1 has a one-notch uplift from its ba2 BCA.

Government Support

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 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 (e.g., swaps), letters of credit, guarantees and liquidity facilities.

BBM's CR Assessment is positioned at Baa3(cr), which is one-notch above the bank's Adjusted BCA of ba1, and, therefore, above the deposit rating of the bank, reflecting Moody's view that its probability of default is lower at the operating obligations than of deposits. BBM's CR Assessment does not benefit from government support, as the 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 BBM S.A.

Macro Factors

Weighted Macro Profile **Moderate** **100%**

Factor	Historic Ratio	Macro Adjusted Score	Credit Trend	Assigned Score	Key driver #1	Key driver #2
Solvency						
Asset Risk						
Problem Loans / Gross Loans	0.7%	a3	← →	baa3	Sector concentration	
Capital						
TCE / RWA	13.5%	baa3	← →	ba2	Expected trend	
Profitability						
Net Income / Tangible Assets	0.9%	ba2	← →	ba2	Expected trend	
Combined Solvency Score		baa2		ba1		
Liquidity						
Funding Structure						
Market Funds / Tangible Banking Assets	41.2%	b3	← →	b3	Market funding quality	
Liquid Resources						
Liquid Banking Assets / Tangible Banking Assets	50.7%	baa1	← →	baa2	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
Senior unsecured bank debt	0	0	ba1	0	Ba1	--

Source: Moody's Financial Metrics

Ratings

Exhibit 4

Category	Moody's Rating
BANCO BBM S.A.	
Outlook	Negative(m)
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)
Senior Unsecured -Dom Curr	Ba1
NSR Senior Unsecured	Aaa.br

Source: Moody's Investors Service

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