

CREDIT OPINION

26 April 2019

Update

 Rate this Research

RATINGS

Banco BOCOM BBM S.A.

Domicile	Rio de Janeiro, Rio de Janeiro, Brazil
Long Term CRR	Ba1
Type	LT Counterparty Risk Rating - Fgn Curr
Outlook	Not Assigned
Long Term Debt	Withdrawn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Outlook	Rating(s) WithDrawn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.

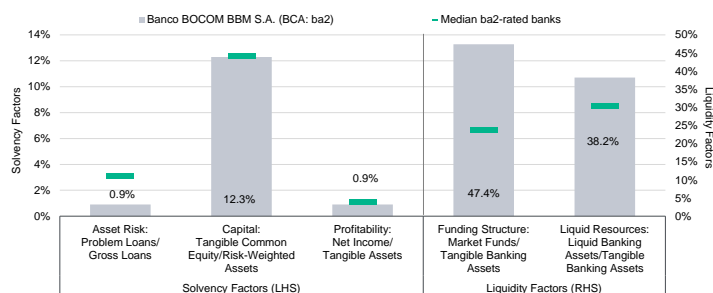
Update to credit analysis

Summary

[Banco BOCOM BBM S.A.](#)'s (BOCOM BBM) Baseline Credit Assessment (BCA) of ba2 incorporates the bank's high asset quality, which is reflected in its track record of low loan losses. However, the recent rise in the share of loans to large companies has increased borrower concentration relative to tangible common equity (TCE), which may increase asset risk. The bank offsets such risk by focusing on customers with better risk profiles. The ba2 BCA also reflects profitability metrics that have benefited from larger loan volume and margins. In addition, the BCA also incorporates a capital position that will likely accommodate at strong levels, despite the bank's increasing leverage, and a funding structure that relies on market funds and also has moderate participation of resources provided by its parent, [Bank of Communications Co., Ltd.](#) (BoCom, A2 stable, baa3).

BOCOM BBM's long-term local-currency deposit and senior unsecured debt ratings of Ba1 derive from its Adjusted BCA of ba1, which incorporates 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.

Exhibit 1
Rating Scorecard - Key financial ratios



Source: Moody's Financial Metrics

THIS REPORT WAS REPUBLISHED ON 2 MAY 2019 WITH AMENDMENTS TO THE AMOUNT OF CREDIT EXPOSURE, WITH THE ADDITION OF GUARANTEES, IN THE FIFTH PARAGRAPH, ON PAGE 3.

Credit strengths

- » The bank's effective credit risk management mitigates asset risk, while the improved risk profile of its loan book offsets higher borrower concentration relative to TCE.
- » Capital position remains strong, despite increased leverage.

Credit challenges

- » High reliance on market funding, partially offset by sizable cash position
- » Profitability subject to volatility, given the intrinsic borrower concentration in its loan portfolio, while it may be incremental revenue from rising loan volume

Outlook

All the ratings have a stable outlook. BOCOM BBM's Ba1 deposit rating is one notch higher than [Brazil's](#) sovereign bond rating. As a result, the outlook on the bank's deposit rating 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 3

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

	12-18 ²	12-17 ²	12-16 ²	12-15 ²	12-14 ²	CAGR/Avg. ³
Total Assets (BRL billion)	6.7	5.1	4.1	3.8	3.1	21.0 ⁴
Total Assets (USD billion)	1.7	1.5	1.3	1.0	1.2	10.1 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	0.2	0.1	0.2	-8.4 ⁴
Problem Loans / Gross Loans (%)	0.1	1.7	0.8	0.9	0.2	0.8 ⁵
Tangible Common Equity / Risk Weighted Assets (%)	12.3	12.4	14.1	13.3	18.5	14.1 ⁶
Problem Loans / (Tangible Common Equity + Loan Loss Reserve) (%)	0.8	7.9	2.2	2.1	0.5	2.7 ⁵
Net Interest Margin (%)	4.2	4.3	3.6	3.4	3.7	3.8 ⁵
PPI / Average RWA (%)	3.2	2.3	1.5	1.2	1.6	2.0 ⁶
Net Income / Tangible Assets (%)	1.0	0.8	0.8	1.1	1.4	1.0 ⁵
Cost / Income Ratio (%)	47.5	56.4	60.3	66.7	61.5	58.5 ⁵
Market Funds / Tangible Banking Assets (%)	47.4	41.5	41.2	58.1	44.9	46.6 ⁵
Liquid Banking Assets / Tangible Banking Assets (%)	38.2	35.1	50.7	58.1	47.6	45.9 ⁵
Gross Loans / Due to Customers (%)	126.9	129.1	99.4	143.8	174.9	134.8 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.

Profile

Founded in 1858, BOCOM BBM started operations as Banco da Bahia, dedicated to retail and middle-market lending activities. In 1998, the bank's commercial arm merged with the investment bank Banco da Bahia Investimentos and formed a multiple banking structure, changing its name to Banco BBM S.A. In May 2015, Bank of Communications Co., Ltd. (BoCom) announced the acquisition of an 80% stake in the bank. The remaining 20% of the bank is owned by the former shareholders, mainly comprising 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 and expanded its operations into commercial lending to upper-middle-market companies, 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 its track record of low problem loan ratios, which reflects the bank's prudent underwriting standards. The score also incorporates the bank's expanded focus on large corporations, which also leads to an intrinsic increase in borrower concentration. However, the bank mitigates credit risk by focusing on customers with robust risk profiles.

The acquisition of Banco BBM's operations by BoCom contributed to loan growth, particularly as a result of access to new borrowers, including large corporate clients 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 increase volatility in asset risk and earnings.

In December 2018, BOCOM BBM's total credit exposure, including guarantees, amounted to BRL4.41 billion, which represented 20.2% 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 improved to 0.15% from 1.70% a year earlier. Reserve coverage of 1.34% of total loans reflects 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, the bank's portfolio is relatively concentrated, with the 20 largest borrowers representing 272% of TCE and 38.6% of its total credit exposure in December 2018.

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 ongoing expansion of its lending activity.

We expect the bank to maintain moderate, but solid, capital metrics, at the same level as the current ratio of TCE to risk-weighted assets of 12.32% and the regulatory Common Equity Tier 1 capital ratio of 14.45%, down from 12.40% and 16.06%, respectively, a year earlier.

Profitability will continue to benefit from an increase in lending and larger scale

BOCOM BBM's Profitability score of ba1 incorporates the potential incremental pressures from loan loss provisions, which are likely to be counterbalanced by higher revenue from its lending operations and higher gains of scale. In December 2018, the ratio of net income to tangible banking assets increased to 0.96% from 0.85% a year earlier.

Profitability is likely to increase because of 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.

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 has been managing tenor gaps and costs by issuing local-currency debt instruments (letras financeiras, with a minimum two-year tenor) and other deposit-like instruments, 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. Total deposits and deposit-like instruments accounted for BRL2.8 billion in December 2018, representing about 55% of the funding mix. BOCOM BBM has a relatively low reliance on foreign-currency lines, which represented 25.9% of total funding in December 2018. 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. BOCOM BBM 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

The Macro Profile of Brazil reflects the large size and diversified nature of the country's economy, more credible monetary policy and increasing commitment to addressing corruption and improving overall government effectiveness, and very low susceptibility to external shocks. However, Brazil's economic rebound, which began in 2017 after a deep two-year recession, has been weaker than expected, reflecting the high degree of uncertainty surrounding policy continuity beyond 2019.

Although public-sector banks continue to account for a substantial portion of total credit, they have been contracting since 2015, which has reduced the market distortions created by their previous aggressive lending policies. Moderate economic growth in 2018 and 2019 will support modest lending growth over the next 12 months. Consequently, banks will face little to no pressure on their funding needs, while low interest rates and low inflation will improve borrowers' repayment capacity, leading to a stabilization of asset quality.

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 decision making process, including BOCOM BBM's support to the operations of Chinese companies in Brazil. Therefore, BOCOM BBM's Adjusted BCA of ba1 incorporates 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 for the operating obligations than that for deposits. BOCOM BBM's CR Assessment does not benefit from government support because government support is not incorporated into the bank's deposit ratings.

Counterparty Risk Ratings (CRRs)

Our CRRs are opinions of the ability of entities to honor the uncollateralized portion of non-debt counterparty financial liabilities (CRR liabilities) and also reflect the expected financial losses in the event such liabilities are not honored. CRR liabilities typically relate to transactions with unrelated parties. Examples of CRR liabilities include the uncollateralized portion of payables arising from derivatives transactions and the uncollateralized portion of liabilities under sale and repurchase agreements. CRRs are not applicable to funding commitments or other obligations associated with covered bonds, letters of credit, guarantees, servicer and trustee obligations, and other similar obligations that arise from a bank performing its essential operating functions.

BOCOM BBM's CRRs are positioned at Baa3/Prime-3

BOCOM BBM's global local-currency CRRs are positioned at Baa3 and Prime-3, one notch above the bank's Adjusted BCA, reflecting the lower probability of default of CRR liabilities and our expectation of a normal level of loss given default. The long-term global foreign-currency CRR of Ba1 is at the same level as Brazil's foreign-currency debt ceiling, while the short-term global foreign-currency CRR is positioned at Not Prime.

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 4

Banco BOCOM BBM S.A.

Macro Factors

Weighted Macro Profile	Moderate	100%
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Factor	Historic Ratio	Initial Score	Expected Trend	Assigned Score	Key driver #1	Key driver #2
Solvency						
Asset Risk						
Problem Loans / Gross Loans	0.9%	baa1	↓↓	baa3	Sector concentration	
Capital						
TCE / RWA	12.3%	ba1	← →	ba2	Expected trend	
Profitability						
Net Income / Tangible Assets	0.9%	ba2	← →	ba1	Expected trend	
Combined Solvency Score		baa3		ba1		
Liquidity						
Funding Structure						
Market Funds / Tangible Banking Assets	47.4%	b3	← →	b3	Market funding quality	
Liquid Resources						
Liquid Banking Assets / Tangible Banking Assets	38.2%	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 Rating	1	0	baa3	0	Baa3	Ba1
Counterparty Risk Assessment	1	0	baa3 (cr)	0	Baa3 (cr)	--
Deposits	0	0	ba1	0	Ba1	Ba3

[1] Where dashes are shown for a particular factor (or sub-factor), the score is based on non-public information.

Source: Moody's Financial Metrics

Ratings

Exhibit 5

Category	Moody's Rating
BANCO BOCOM BBM S.A.	
Outlook	Stable
Counterparty Risk Rating -Fgn Curr	Ba1/NP
Counterparty Risk Rating -Dom Curr	Baa3/P-3
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
Counterparty Risk Rating	A2/P-1
Bank Deposits	A2/P-1
Baseline Credit Assessment	baa3
Adjusted Baseline Credit Assessment	baa3
Counterparty Risk Assessment	A2(cr)/P-1(cr)
Pref. Stock Non-cumulative	Ba3 (hyb)

Source: Moody's Investors Service

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