Moody's
INVESTORS SERVICE

Credit Opinion: Banco Ribeirão Preto S.A. (BRP)

Global Credit Research - 07 Jun 2010

Ribeirao Preto, Brazil

Ratings

Category	Moody's Rating
Outlook	Stable
Bank Deposits	Ba2/NP
NSR Bank Deposits -Dom Curr	A1.br/BR-1
Bank Financial Strength	D

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Key Indicators

Banco Ribeirao Preto S.A (BRP)

	[1]**Dec-09**	**Jun-09**	[2]**Dec-08**	**Jun-08**	**Dec-07**	[3]**Avg.**
Total Assets (US$B)	**0.22**	**0.19**	**0.15**	**0.21**	**0.15**	[4]**19.92**
Share Equity (US$M)	**35**	**30**	**24**	**35**	**30**	[4]**6.71**
Pre-Provision Profit/Tt.Avg. Assets	**3.06**	**0.45**	**1.77**	**0.10**	**4.14**	**1.90**
ROAA	**1.01**	**-0.94**	**1.54**	**0.89**	**2.33**	**0.96**
NIM	**5.16**	**2.48**	**2.87**	**2.21**	**7.02**	**3.95**
Oper Expenses/Gross Op. Revenues	**42.84**	**82.83**	**72.84**	**95.76**	**43.31**	**67.52**
NPL/Gross Loans & Lease	**3.28**	**6.27**	**2.35**	**2.62**	**3.03**	**3.51**
BIS Ratio	**18.97**	**20.80**	**21.90**	**21.24**	**27.20**	**22.02**

[1] As of December 31. [2] Statement period in which the bank switched to Basel II accounting framework. [3] The average calculations are based on Basel I and Basel II data where applicable. [4] Compound annual growth rate.

Opinion

SUMMARY RATING RATIONALE

Moody's assigns a bank financial strength rating (BFSR) of D to Banco Ribeirão Preto S.A. (BRP). The rating translates into a Baseline Credit Assessment of Ba2. The BFSR captures the bank's long-standing regional franchise, which derives from a well-defined footprint in the SME lending segment. The rating is also backed by BRP's conservative leveraging philosophy and by sound financial fundamentals reported over the last years.

In addition, the rating acknowledges the bank's small asset and capital bases, which might limit BRP's capacity to carry out management's recent strategic decision to expand business beyond the bank's regional focus. Nevertheless, BRP's current capitalization level allows room for further growth. The stable outlook on the ratings reflects the fact that management should be able to handle challenges in new business segments as it moves beyond its historical regional presence. The evolution of the bank's business profile appears to be proceeding in an appropriate direction.

In Moody's view, BRP would receive no systemic support should a crisis occur, given the bank's small participation in the Brazilian retail deposit market. Therefore, Moody's assigns a global local currency (GLC) deposit rating of Ba2 to Banco Ribeirão Preto, which is derived from the Ba2 Baseline Credit Assessment.

Rating Drivers

- Conservative leverage position when compared with domestic peers': a 18.4% BIS ratio in March 2010

- Long-standing regional position and strong knowledge of its market niche; primarily developing the SME sector in a wealthy region that embraces over three million citizens and encompasses over 10% of São Paulo state's GDP.

- Lean cost structure: flexible and agile business model

- Low credit granularity, leading to some volatility in nonperforming ratios

- Limited franchise value because of BRP's small size and lack of product diversification compared with peers' (large Brazilian banks that cater to the same client base in the region)

- Challenge of growing competition in BRP's target market, which may particularly affect funding ability

- Sustain adequate profitability levels while the new approach towards proprietary trading business adds volatility to the bank's earnings profile

Rating Outlook

All the ratings have a stable outlook.

What Could Change the Rating - Up

Positive pressure on BRP's BFSR could derive from management's ability to maintain the bank's profitability at its current level in a low interest-rate environment, together with keeping credit and operating costs low. The diversification of business lines and successful geographical expansion may also benefit its ratings. Improvements in the bank's funding structure, which would involve further diversification, while keeping a tight gap position, would have positive influence on ratings as well.

What Could Change the Rating - Down

Aggressive loan growth beyond BRP's footprint could lead to substantial asset-quality deterioration and provisioning needs, which would hurt capital. Such a situation could hurt the ratings negatively. The bank's inability to fend off competition could also result in margin compression, in a scenario of declining interest rates.

Recent Results and Developments

After the net loss of R$1.2million in 1Q09, BRP posted a positive bottom line result of R$1.4 million in March 2010, reflecting improved credit dynamics and gains in trading positions, a component that continues to add volatility to the bank's results.

The credit book remained flat in the quarter in terms of volume, indicating relevant improvement in quality, with total overdue loans reducing from 6.32% at year-end 2009 to 1.64% in March 2010. This improvement considers a renegotiated loans (with a single client) in the amount of R$1.9 million, which accounted almost for 1% of the portfolio. The improvement in credit risk was reflected in the reserve coverage ratio, that still represented 3.9% of the loan book in 1Q10, same as in 2009, covering more than 230% of total credits in arrears, while in 4Q09 reserves covered 61.4% of total overdue credits.

Resources from BNDES (federal development bank) continued to contribute to increase the portfolio tenor: roughly 45% of the loans matures above 1 year. Credit risk concentration remains a concern given the small size of the bank, with 20 largest credit exposures accounting for 56.5% of total loans (51% in 1Q09 and 55% in YE09). Credit risk is mitigated by the secured natured of the loans, as well as a comfortable capital surplus (total BIS ratio of 18.37%, as of March 2010).

No major change to funding structure in the period, largely represented by deposits that responded for 37.5% and long-term resources from BNDES for 53.8%. Although, deposits from individual clients in the region remained stable in the period, concentration by client also remains a point of challenge (20 largest clients accounted for 75.3% of total deposits in 1Q10) .

DETAILED RATING CONSIDERATIONS

Detailed rating considerations for BRP's currently assigned ratings, as follows:

Bank Financial Strength Rating

Moody's assigns a D BFSR to BRP. Moody's believes the D rating is an appropriate measure of the bank's financial strength, capturing BRP's renowned position in Ribeirão Preto's region, as well as the bank's plans for geographical diversification and expansion of its loan book, particularly in view of medium- to long-term stable economic conditions. This BFSR also reflects the bank's small and limited franchise value.

The difference from the assigned D BFSR to the scorecard outcome is explained by the bank's limited size and scale, an increasingly competitive environment coupled with a declining interest rate, and the possible effects of the expansion strategy on the bank's good fundamentals.

Executive leadership is expected to be able to generate good quality earnings within the bank's new structure and maintain credit and operating costs at low levels. Management's ability to handle intense competition and thin margins is going to determine the extent to which BRP's financial fundamentals may strengthen.

Moody's BFSR scorecard outcome was positively affected by BRP's strong financial indicators, yielding C+ with higher scores for profitability, asset quality, and capital adequacy. The scorecard's outcome also benefited from Moody's general positive judgment about Brazil's regulatory environment.

Qualitative Factors (70%)

Factor 1: Franchise Value

Trend: Neutral

The overall score of D- for franchise value reflects the bank's limited market share in terms of retail deposits within the industry, as well as its modest size. BRP had a credit portfolio of R$233.4 million as of March 2009, soaring 106% over the last twelve months, and a client base comprised of around 400 active mid-sized companies in the region, with annual sales of up to R$150 million.

Since the end of 2006, business initiatives beyond its traditional geographic coverage, reinforcement of corporate governance and administrative capabilities have been driving its expansion plan and franchise strengthening, in an increasingly competitive environment. This business strategy involves the following: (a) bulking up its sales force; (b) enhancement of its product base, by adding leasing and mortgage loans; (c) the opening of a new branch in São Paulo, a highly competitive region, primarily to reinforce liquidity access and (d) the operation of a more active trading desk, aimed at exploiting market opportunities. Such strategic moves may positively affect earnings generation and diversification, if they succeed. We might revisit this score when -- and if -- this diversification strategy proves sustainable.

Founded in 1995, BRP historically centered its strategic plans on a strong regional knowledge and a conservative risk appetite. This philosophy was implemented, along with a well-defined focus on middle market lending, comprised of tailor-made products to agricultural producers, mainly those in sectors of sugar and alcohol, orange, coffee, soy bean, and cattle-rising. The bank attends a rich agribusiness region of the São Paulo state that accounts for approximately 10% of the state GDP. BRP still lacks the broader geographic coverage of its peers', however, the bank has a defensible market share in its core region, which is the countryside of São Paulo State.

Factor 2: Risk Positioning

Trend: Neutral

BRP obtained an overall score of D for risk positioning, which indicates a transition in terms of corporate governance and a very recent organizational and managerial restructuring to maintain the family-ownership structure. It is important to note that recent progress has been made in terms of better governance practices, with the implementation of a new Board of Directors last July, with one-third of the members independent.

Although the bank disciplined in terms of controlling risk, risk management needs to be strengthened because the management's credit appetite is increasing and the bank is expanding. Areas that need to an integrated approach to risk include the technological platform. Risk management has been efficient, but fairly basic when compared with other global players', but in accordance to the Central Bank's requirements. Executives and board members are deeply involved in the process and are aware of key risks.

Operational risk management has been implemented in compliance with regulatory requirements. Nevertheless, information on credit and market positions -- either individual or aggregate exposures -- can be extracted on-demand with relatively short delays. Industry and portfolio reviews take place on a regular basis. The same applies for stress tests, which are performed every month. In case of the latter, the bank has posted no minor or major control issues over the last five years.

Some improvements upon financial reporting transparency have been observed over the last six months, with further disclosure of risk-weighted assets and loan portfolio breakdown information. BRP reports in local GAAP and follows regulatory requirements; it releases adequate financial reports on a quarterly basis, which carries a preliminary auditing note, and these are publicly available on the Central Bank's website.

As a regional mid-size lender, BRP lacks credit granularity, scoring E for credit risk concentration, given the wholesale nature of the portfolio. Around 19% of the credit book is related to consumer-lending operations, which includes real estate financing. On the other hand, the bank enjoys a high turnover, with more than 28% of the loan book holding up to 90-day commercial loans (47% with maturity of up to one year), and roughly 85% of the portfolio is backed by collateral. Both of these actors mitigate BRP's concentration risk. In terms of industry diversification, the bank's operations are directly and indirectly linked to the agribusiness chain, the region's main economic sustainability, and an important region producing medical supplies.

Moody's continues to see limited funding diversification when BRP is compared with its local peers', which points to BRP's relative reliance on time deposits from local clients and banks. Of note is that this deposit base has proven to be stable during past market turbulences, which is explained by the strong brand image of the bank within its regional clients. We find relevant concentration within BRP's deposit base. Tightening liquidity conditions worsened in September 2008, have been pressuring funding costs and deposits sustainability, especially on those wholesale reliant banks. In the case of BRP, total deposits went down roughly 10% since the end of September, to R$82million up to Nov, 25th, evidencing a superior stickiness than observed at other midsize banks with a more professional-related deposit structure.

The ongoing progress in diversifying and strengthening the bank's funding profile so far has boosted total resources through short to medium-term government-sponsored facilities directed to coffee producers. However, BRP has been centering efforts to add institutional investors to its deposit base, especially from asset managers, given the importance of that industry to the system, already opening limits with important industry players.

Structured in 2007, new real estate-lending platform already accounted for R$23million at the end of the 3Q08, reaching the maximum 10% book share established by management. However the main dilemma is finding adequate medium to long-term funds to sustain such diversification strategy, and executive leadership does not rule out a partnership to build up synergies in the segment.

The B for Market Risk Appetite indicates relatively small trading activities, but increased risk appetite for proprietary trading activities over the last 18 months. Stress tests indicate that less than 5% of the bank's Tier 1 capital would be at risk due to market risk events (1.5% in 2006. Maintaining a comfortable cash liquidity, management indicated its intention to have a more active trading desk, thus taking greater advantage of market opportunities as they appear. The conservative risk philosophy of the bank should remain unaltered.

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 is derived from a score of E for economic stability (measured as nominal GDP volatility over the 20-year period), with a 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 Factors (30%)

Factor 5: Profitability

Trend: Weakening

BRP had a score B+ for profitability considering the 3year average of 2009.

Since the second half of 2007, performance has been influenced by the MTM adjustments on marketable securities portfolio, a volatile component of the bank's earnings. BRP holds equity position and government bond subject to recent heightening in interest rates volatility. Such move to increment trading activities, in a disciplined approach tough, was expected. Management is bullish about the equity investment held, despite current cycle of market turmoil. As a credit-driven bank, BRP has a recurrent earning flow supported by a prudent liquidity management and strict credit approach.

The bank's profitability profile is explained by BRP's specialized and regional operations. Management shares a good and long-standing relationship with its clients and is familiar with their businesses; hence, the bank has very loyal customers, which keeps credit costs low and sustains the quality of the loan book. Moreover, BRP's small size and lean structure favors a streamlined cost structure.

The weakening trend on profitability reflects the market competitive conditions, especially in BRP's region, that should reduce margins going forward, when compared to 2009 path. Although trading positions are not relevant to the bank's capital structure, Moody's sees a negative trend for this subfactor in face of the size of the bank and the loan origination that remains relatively flat over the last quarters, while most of the niche players resumed growth dynamics in the 1Q10 along with economic expansion.

Factor 6: Liquidity

Trend: Neutral

BRP has a low-leveraged balance sheet, which is mainly funded through time deposits and through government on-lendings from BNDES and FUNCAFE, which are medium to long-term funding programs to coffee producers sponsored by coffee industry in Brazil, managed by the Agriculture Ministry. The bank's small size restricts access to institutional investors, resulting in a funding structure that is mostly based on inter-bank operations and deposit certificates with small and medium-sized companies located in the regional market. The bank's deposit base has proven loyal over the past crisis, and in recent liquidity scenario, BRP's deposits have shown a modest reduction since the end of September to date, less affected than most of local smallcap peers' which are more institutional-funded.

With persist investors' selectiveness; we see continued pressure on funding, as the bank moves toward growth sustainability against fierce competition. BRP has a D- for liquidity in the scorecard.

Factor 7: Capital Adequacy

Trend: Neutral

BRP has a strong capital base, with a BIS ratio of 18.4% in March 2010, which although is far above the regulatory minimum of 11%, has been consistently pressured over the last 2 years. The bank is the main business of its shareholder, the Coselli family; therefore, BRP's comfortable capital position is a result of the shareholders' conservative approach to keep a low-leveraged balance sheet.

Although the ratio is likely to continue floating well-above the regulatory minimum, Moody's notes that it will gradually continue to worsen from the effects of growth in lending activities as management adds leverage to take advantage of a more benign economic environment. Nonetheless, the trend for capital adequacy is neutral at this stage, indicating further room to finance loan growth in the coming years.

Factor 8: Efficiency

Trend: Neutral

BRP's efficiency ratio reflects the bank's lean structure and small size. The skills of the bank on the agribusiness segment and its close client monitoring require a low degree of operational sophistication. Additional costs are foreseen, as management hires professionals, invests in IT systems, and reviews operational processes in order to support its expansion strategy and reinforce competitive power.

The scorecard gives an B for efficiency.

Factor 9: Asset Quality

Trend: Improving

After peaking levels of 6% by mid-2009, asset quality indicators improved significantly in 1Q10, as the bank was able to renegotiate on credit in the period and also reflects improved credit conditions ahead. The low granularity of the portfolio inputs reasonable volatility in times of stress, an intrinsic risk factor to the bank's profile. Management's proximity and long relationship with clients also adds value to the performance of the portfolio.

NPLs indicator improved to 0.47% in the 1Q10 from 3.28% in December 2009, back to historical levels, and well below the system's 4.5% average. The adequate capital cushion supports any stress in portfolio's quality. The scorecard shows a B for asset quality.

Global Local Currency Deposit Rating (Joint Default Analysis)

Moody's GLC deposit rating of Ba2 for BRP does not receive any lift from the bank's Baseline Credit Assessment of Ba2. Moody's assesses that no systemic support would be extended to the bank in case an eventual crisis occurs, due to the irrelevant participation of BRP in the retail deposit market in Brazil.

Notching Considerations

Ratings for BRP's junior obligations, if rated by Moody's, would be notched off the global local-currency deposit rating of Ba2, as per Moody's notching conventions.

National Scale Rating

BRP is rated A1.br/BR-1 by Moody's on Brazil's National Scale. The rating is supported by the BRP's deep knowledge of its regional niche market, strong track record of consistent performance, and conservative risk positioning.

Foreign Currency Deposit Rating

Moody's assigns a Ba2 foreign currency deposit rating for BRP.

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 Ribeirão Preto S.A. (BRP)

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 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						B+	Weakening
PPP % Avg RWA - Basel II	3.73%						
Net Income % Avg RWA - Basel II		2.03%					
Factor: Liquidity						D-	Neutral
(Mkt funds-Liquid Assets) % Total Assets					20.39%		
Liquidity Management				x			
Factor: Capital Adequacy						A	Neutral
Tier 1 ratio (%) - Basel II	18.62%						
Tangible Common Equity / RWA - Basel II	18.60%						
Factor: Efficiency						B	Neutral
Cost/income ratio		53.00%					
Factor: Asset Quality						B	Improving
Problem Loans % Gross Loans			2.89%				
Problem Loans % (Equity + LLR)	9.92%						
Lowest Combined Score (9%)						D-	
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