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BRB - Banco de Brasilia S.A.

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Table Of Contents

BRB - Banco de Brasilia S.A.

SACP	bb-

Anchor	bb+	
Business Position	Weak	-2
Capital and Earnings	Moderate	0
Risk Position	Adequate	0
Funding	Average	0
Liquidity	Adequate	

\+

Support	-1

ALAC Support	0
GRE Support	-1
Group Support	0
Sovereign Support	0

\+

Additional Factors	0

Issuer Credit Rating
B+/Positive/B

Major Rating Factors

Strengths:	Weaknesses:
• Strong presence in the public employee payroll discount loans industry in the Federal District of Brazil (the Distrito Federal; DF), which is the Brazilian state with highest per-capita income; and • Stable and low-cost funding base, given that the bank is the main financial agent of the DF's government.	• High credit losses in its small and midsize enterprise (SME) lending portfolio; • Geographic concentration; and • DF's weaker financial conditions, which constrain the ratings on the bank.

Outlook: Positive

The positive outlook for BRB - Banco de Brasilia S.A. (BRB) reflects our view that there's a one-in-three chance of an improvement in the next 12 months in our opinion of its shareholder's credit quality, which constrains the ratings on the bank. We expect the DF to maintain its fiscal efforts over the next few years, enhancing its credit fundamentals, which could improve our view of its credit quality.

Upside scenario

We could raise the ratings on the bank following an improvement in the DF's credit quality, which could occur if DF maintains its efforts to improve its fiscal results.

Downside scenario

We could lower the ratings if we perceive a deterioration in the DF's credit quality. A negative rating action could also occur if the bank's forecasted risk-adjusted capital (RAC) ratio over the next two years weakens to below 5.0%, stemming from higher-than-expected credit losses or dividend payments alongside a downgrade of our Banking Industry Country Risk Assessment (BICRA) following a dip in Brazil's economy, which would result in a lower anchor for banks that operates in the country.

Rationale

Anchor: 'bb+' for commercial banks operating in Brazil

Under our bank criteria, we use our BICRA's economic risk and industry risk scores to determine a bank's anchor, the starting point in assigning an issuer credit rating. Our anchor for a commercial bank operating only in Brazil is 'bb+', based on the country's economic risk score of '7' and an industry risk score of '5'. (Please see "Banking Industry Country Risk Assessment: Brazil," published Feb. 2, 2018).

Table 1

BRB - Banco de Brasilia S.A. Key Figures					
	--Year-ended Dec. 31--				
(Mil. R$)	**2017**	**2016**	**2015**	**2014**	**2013**
Adjusted assets	13,967.6	13,452.4	13,543.8	12,611.9	11,506.8
Customer loans (gross)	8,626.0	9,358.2	9,494.3	9,082.9	8,002.4
Adjusted common equity	1,028.2	987.4	1,136.9	1,170.5	1,118.7
Operating revenues	2,439.6	2,374.9	2,160.1	2,076.3	1,956.1
Noninterest expenses	1,735.3	1,785.4	1,607.2	1,523.5	1,415.4
Core earnings	285.5	145.9	98.8	167.8	200.4

R$--Brazilian real.

Business position: Geographically concentrated in the DF

BRB's business position reflects its concentrated business profile due to its significant geographic concentration in the DF of Brazil and its small market share. With total assets of about BRL (Brazilian real) 14 billion as of Dec. 31, 2017, BRB is the 35th largest bank in the country in terms of assets, with less than a 0.2% market share. Since 2015, the bank has been mostly focusing on its retail portfolio, notably payroll-deductible loans, which represented 52% of total loans as of Dec. 31, 2017, followed by personal loans to public employees (21%), SMEs (10%), residential mortgages (9%), and other consumer loans (7%). Despite its geographic concentration, we believe that BRB continues to benefit from its stable client base, which primarily consists of government employees and government service providers, and from operations primarily conducted in a region that has one of the highest GDPs per capita in Brazil. Founded in 1964, BRB has acted as DF's financial agent to develop the local economy. The bank reviewed its most recent strategy to seek growth in SMEs in light of increasing nonperforming loans (NPLs) in this segment. As a result, the bank was able to improve its profitability, despite the difficult operating environment in Brazil. Going forward, the bank intends to continue expanding and diversifying its product portfolio, focusing mostly on the DF.

Table 2

BRB - Banco de Brasilia S.A. Business Position					
	--Year-ended Dec. 31--				
(%)	2017	2016	2015	2014	2013
Loan market share in country of domicile	0.3	0.3	0.3	0.3	0.3
Deposit market share in country of domicile	0.4	0.4	0.4	0.4	0.4
Return on equity	21.3	17.5	7.4	11.5	16.8

Capital and earnings: Projected RAC ratio of 5.2%-5.6%

Our assessment of BRB's capital and earnings is based on our forecasted RAC ratio before diversification of 5.4% for year-end 2018 and 2019. We expect BRB's asset quality to remain steady in the next two years as it reduces its SME portfolio, improving its internal capital generation capacity. Our RAC forecast considers our base-case scenario assumptions, which include:

- Brazil's real GDP growth of 2.4% in 2018 and 2.6% in 2019.
- Credit growth of 3% in 2018 and 5% in 2019, fueled by growth in payroll deductible loans and mortgages, while lending to SMEs continues to shrink.
- Net interest margins higher than historical average due to stable funding and business conditions in the DF, particularly from payroll lending to the state government employees.
- Noninterest expenses to have modest growth below inflation as the bank continues to have tight cost controls.
- Gradual improvement in credit loss provisions figures because of improving non-performing ratios, which we expect to range from 2.6% to 3.0%. This is based on a stable delinquency in the consumer portfolio driven by the good quality of the payroll loans.
- Profitability gradually improving in 2018 and 2019. Return on equity (ROE) should be close to 17.0%-18.0% over the next two years.
- A dividend payout ratio of 40% for the next two years.

Table 3

BRB - Banco de Brasilia S.A. Capital And Earnings					
	--Year-ended Dec. 31--				
(%)	2017	2016	2015	2014	2013
Tier 1 capital ratio	12.0	11.2	12.1	12.8	11.0
Adjusted common equity/total adjusted capital	100.0	100.0	100.0	100.0	100.0
Net interest income/operating revenues	80.0	77.6	76.8	69.6	71.1
Fee income/operating revenues	14.1	14.4	15.3	23.9	21.8
Noninterest expenses/operating revenues	71.1	75.2	74.4	73.4	72.4
Preprovision operating income/average assets	5.1	4.3	4.2	4.6	5.1
Core earnings/average managed assets	2.1	1.1	0.7	1.4	1.9

Risk position: Improving asset quality metrics following the lower share of SME loans

We continue to assess BRB's risk position based on its high share of good quality payroll loans and our expectation that the bank will continue reducing its SME lending exposure amid widening credit losses and restructured loans in this segment. As a result of this change, BRB's NPLs are already showing signs of improvement, which we expect to continue going forward. As of December 2017, the bank's NPLs and charge-offs reached 2.9% and 3.2%, respectively, compared with a three-year average of 4.1% and 3.4%. Despite this improvement, its SME portfolio continues to perform poorly because Brazil's economy remains challenging. In addition, the bank's corporate restructured loan portfolio is somewhat larger than the average for the system, which further pressures BRB's risk position. On the other hand, the asset quality of its payroll and consumer loans has remained sound, given that NPLs in this portfolio are lower than the system average. Moreover, the bank has a fairly diversified loan portfolio because of its focus on payroll deductible loans, with its 10 largest exposures representing about 3% of the total.

Table 4

BRB - Banco de Brasilia S.A. Risk Position					
	--Year-ended Dec. 31--				
(%)	2017	2016	2015	2014	2013
Growth in customer loans	(7.8)	(1.4)	4.5	13.5	25.4
Total managed assets/adjusted common equity (x)	13.7	13.7	12.0	10.9	10.3
New loan loss provisions/average customer loans	2.8	4.2	5.5	3.9	3.4
Net charge-offs/average customer loans	3.2	3.7	3.3	2.1	2.0
Gross nonperforming assets/customer loans + other real estate owned	2.9	4.5	5.1	4.2	3.7
Loan loss reserves/gross nonperforming assets	158.1	120.3	113.9	110.3	114.2

Funding and liquidity: Stable and low-cost funding base, given that the bank is the main financial agent of the DF's government

We view BRB's funding position as in line with the industry average. The bank benefits from a relatively diversified and stable funding structure when compared to other medium-sized banks in the country. Its branch network allows for the capturing of demand, savings, and time deposits from individuals, while its deposit base is stable because of its status as the payment agent of all of DF's public employees. Moreover, the bank has the DF's judiciary deposits on its balance sheet, which represent around 15% of total deposits. Consumer deposits are still increasing although BRB has been decreasing the yields for time deposits since the demand for loans has also decreased. As of December 2017, the bank's funding base was composed of 63% time deposits, 16% savings deposits, 8% demand deposits, and 13% of other funding sources. As of December 2017, 52% of its total deposits were from individuals, 20% from companies, 15% were judicial deposits, 11% from related parties, and 3% from others. The bank doesn't have material funding concentration due to its large pulverized client base. Furthermore, the bank's stable funding ratio (SFR) stood at 105.4% as of December 2017, which supports our funding assessment. In addition, we believe BRB has adequate liquidity. Its broad liquid assets to short-term wholesale funding ratio was comfortably 4.0x as of December 2017. The bank has adequate asset/liability management, with real time control and surveillance of its funding base compared to the resources applied. It calculates liquidity metrics on a daily basis in accordance with its governance policies, which calculate minimum liquidity metrics for multiple scenarios.

Table 5

BRB - Banco de Brasilia S.A. Funding And Liquidity

	--Year-ended Dec. 31--				
(%)	**2017**	**2016**	**2015**	**2014**	**2013**
Core deposits/funding base	85.8	84.6	86.0	88.3	89.8
Customer loans (net)/customer deposits	87.4	98.4	96.8	99.0	97.7
Long-term funding ratio	93.6	92.7	93.4	95.1	95.7
Stable funding ratio	105.4	97.0	96.2	96.2	96.0
Short-term wholesale funding/funding base	7.1	8.2	7.3	5.4	4.9
Broad liquid assets/short-term wholesale funding (x)	4.0	2.5	2.6	3.1	4.0
Net broad liquid assets/short-term customer deposits	39.7	20.7	19.4	18.1	22.7
Short-term wholesale funding/total wholesale funding	50.5	52.9	52.1	46.5	47.8

Support: Low likelihood of shareholder support

We consider BRB a government-related entity (GRE) because the DF's government is its majority owner and we believe there is a low likelihood that it would provide timely and sufficient extraordinary support to BRB if needed. Our view of the likelihood of support is based on the following factors:

- The difficult financial conditions of DF, which raises doubts about its capacity to support BRB's debt; and
- BRB's limited importance to the government as a regional bank and exclusive financial agent of the state, which could eventually be replaced by another entity.

Related Criteria

- General Criteria: S&P Global Ratings' National And Regional Scale Mapping Tables, Aug. 14, 2017
- Criteria - Financial Institutions - General: Risk-Adjusted Capital Framework Methodology, July 20, 2017
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- General Criteria: Rating Government-Related Entities: Methodology And Assumptions, March 25, 2015
- General Criteria: National And Regional Scale Credit Ratings, Sept. 22, 2014
- General Criteria: Group Rating Methodology, Nov. 19, 2013

- Criteria - Financial Institutions - Banks: Quantitative Metrics For Rating Banks Globally: Methodology And Assumptions, July 17, 2013
- Criteria - Financial Institutions - Banks: Banks: Rating Methodology And Assumptions, Nov. 9, 2011
- Criteria - Financial Institutions - Banks: Banking Industry Country Risk Assessment Methodology And Assumptions, Nov. 9, 2011
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009

Anchor Matrix

Industry Risk	**Economic Risk**									
	1	2	3	4	5	6	**7**	8	9	10
1	a	a	a-	bbb+	bbb+	bbb	-	-	-	-
2	a	a-	a-	bbb+	bbb	bbb	bbb-	-	-	-
3	a-	a-	bbb+	bbb+	bbb	bbb-	bbb-	bb+	-	-
4	bbb+	bbb+	bbb+	bbb	bbb	bbb-	bb+	bb	bb	-
5	bbb+	bbb	bbb	bbb	bbb-	bbb-	**bb+**	bb	bb-	b+
6	bbb	bbb	bbb-	bbb-	bbb-	bb+	bb	bb	bb-	b+
7	-	bbb-	bbb-	bb+	bb+	bb	bb	bb-	b+	b+
8	-	-	bb+	bb	bb	bb	bb-	bb-	b+	b
9	-	-	-	bb	bb-	bb-	b+	b+	b+	b
10	-	-	-	-	b+	b+	b+	b	b	b-

Ratings Detail (As Of May 11, 2018)

BRB - Banco de Brasilia S.A.		
Issuer Credit Rating		B+/Positive/B
Brazil National Scale		brA-/Positive/brA-2
Issuer Credit Ratings History		
28-Feb-2018		B+/Positive/B
18-Aug-2017		B+/Stable/B
23-May-2017		BB-/Watch Neg/B
14-Mar-2016		BB-/Negative/B
17-Feb-2016		BB-/Watch Neg/B
18-Jan-2016		BB-/Negative/B
10-Sep-2015		BB/Watch Neg/B
05-Mar-2015		BB/Negative/B
08-Oct-2014		BB/Stable/B
28-Feb-2018	*Brazil National Scale*	brA-/Positive/brA-2
18-Aug-2017		brA-/Stable/brA-2
23-May-2017		brA-/Watch Neg/brA-2
14-Mar-2016		brA-/Negative/brA-2
17-Feb-2016		brA-/Watch Neg/brA-2
18-Jan-2016		brA-/Negative/brA-2

Ratings Detail (As Of May 11, 2018) (cont.)	
10-Sep-2015	brA+/Watch Neg/brA-2
05-Mar-2015	brA+/Negative/brA-2
14-Apr-2014	brAA-/Stable/brA-1
26-Mar-2014	brAA+/Watch Neg/brA-1
29-Jan-2014	brAA+/Negative/brA-1
Sovereign Rating	
Brazil	BB-/Stable/B
Brazil National Scale	brAA-/Stable/--

*Unless otherwise noted, all ratings in this report are global scale ratings. S&P Global Ratings' credit ratings on the global scale are comparable across countries. S&P Global Ratings' credit ratings on a national scale are relative to obligors or obligations within that specific country. Issue and debt ratings could include debt guaranteed by another entity, and rated debt that an entity guarantees.