



Moody's Investors Service

## Rating Action: **Moody's reviews Brazilian government-owned banks**

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Global Credit Research - 07 Jul 2009

### **Foreign currency ratings reviewed for upgrade, local currency ratings for downgrade**

New York, July 07, 2009 -- Moody's Investors Service has placed on review for possible upgrade the Ba2 long-term foreign-currency deposit ratings of Banco do Brasil S.A. (BB) and its subsidiary Banco Nossa Caixa S.A.(NC), as well as those of Caixa Econômica Federal (CEF), and of Banco Nacional de Desenvolvimento Econômico e Social S.A. (BNDES), following similar actions taken on the sovereign ratings of the Brazil government. (For further details on the government-related action, please refer to Moody's press release on Brazil dated July 6, 2009 "Moody's places Brazil's ratings on review for possible upgrade".) The Not Prime short-term foreign currency deposit ratings are not affected and remain unchanged. Moody's also placed on review for possible upgrade the Baa3 foreign currency debt ratings assigned to bonds issued by BB and BNDES.

At the same time, Moody's has placed on review for possible downgrade the A1/ Prime-1 long- and short-term global local currency deposit ratings of Banco do Brasil, Banco Nossa Caixa and Caixa Econômica Federal, as well as the A1 local currency issuer rating assigned to BNDES; these actions are being taken in response to Moody's global reassessment of the systemic support available to banks following the global financial crisis. Also placed on review for possible downgrade are the A1 local currency issuer and debt ratings assigned to BNDES Participações S.A. - BNDESPAR.

Moody's explained that of the 37 banks it currently rates in Brazil, only the four government-owned banks (BB, NC, CEF, and BNDES) are likely to be affected by this reassessment of systemic support because their deposit and issuer ratings benefit from several notches of uplift. Moody's also noted that the review is focused on bank ratings and, therefore, there is no current or expected similar impact on ratings of Brazil's government-owned non-financial companies.

The national scale deposit ratings of Aaa.br assigned to BB, NC, CEF and BNDES have all been affirmed, with a stable outlook. Also, the Aaa.br national scale issuer and debt ratings assigned to BNDESPAR are not affected by this action and remain unchanged.

Separately, Moody's affirmed Banco do Brasil and Banco Nossa Caixa's C bank financial strength ratings (BFSR, which maps to a baseline credit assessment - BCA - of A3), but changed the outlook on them to positive, from stable. Caixa Econômica Federal's BFSR of D+ (BCA of Baa3) was also affirmed with a stable outlook. (As a non deposit-taking government related issuer, BNDES is not assigned a financial strength rating). These specific actions follow Moody's initiative of recalibrating banks' stand-alone ratings in light of heightened emphasis on utilizing scenario analysis of banks' risk assets to determine adequacy of capitalization under both Moody's expected and adverse macroeconomic outlooks.

#### Review of Foreign Currency Debt and Deposit Ratings

The review for possible upgrade of the banks' foreign-currency deposit and debt ratings is the direct result of the sovereign action announced yesterday; Moody's will review for possible upgrade the Ba2 country ceiling for foreign currency bank deposits and the Baa3 country ceiling for foreign currency bonds. Because BB and BNDES's current debt ratings of Baa3 are constrained by the country ceiling for foreign currency debt, the potential upgrade of the ceiling would be expected to result in the upgrade of the banks' bond ratings.

#### Review of Local Currency Deposit and Debt Ratings

The review of the local-currency deposit and debt ratings of BB, NC, CEF and BNDES follows Moody's global reassessment of probable systemic support available to these bank ratings. The review will determine the extent to which the level of systemic support that is currently incorporated into these banks' local currency ratings -- which ranges from two to seven notches of uplift -- should be more closely aligned to the Brazilian government's local currency bond rating.

Moody's believes that most governments are at least as likely, if not more likely, to support their banking systems as they are to service their own debt -- a view that has traditionally led to bank ratings often benefiting from significant uplift because of the probability of systemic support. However, the rating agency has also recognized that the capacity of a country and its central bank to support the nation's banks may converge with -- and may even be increasingly constrained by -- the government's own debt capacity when faced with situations of systemic stress. This is particularly true when governments are faced with systemic crises that could place indiscriminate pressure on the major banks in a system; the current financial crisis has exposed this risk in many systems globally, requiring Moody's to reassess the amount of uplift above the debt ratings of governments that is appropriate in its evaluation of systemic support of banks.

The details of this approach are outlined in Moody's recent Special Comment entitled "Financial Crisis More Closely Aligns Bank Credit Risk and Government Ratings in Non-Aaa Countries" (published in May 2009 and available on [www.moody.com](http://www.moody.com)).

Moody's again explained that it currently rates 37 banks in Brazil, but that only the four government-owned banks are likely to be affected by this reassessment because their deposit ratings benefit from several notches of uplift due to systemic support.

At present, the rating agency does not incorporate any probability of systemic support to the deposit ratings of many of the medium and small rated Brazilian banks. Large private banks, whose intrinsic financial strengths are already at Brazil's A1 ceiling for bank deposits, also do not benefit from systemic support on their deposit ratings, while those subsidiaries of foreign banks primarily gain uplift from parental support.

As part of its review, Moody's will analyze the specific circumstances of Brazil to determine the appropriate level of systemic support for Brazilian bank ratings, as well as the implications for the deposit ratings of the above-mentioned banks. Factors that the agency will consider in its assessment of systemic support include the banking industry's size in relation to government resources, the level of stress in the system, its foreign currency obligations relative to the government's own foreign exchange resources, and any changes to the government's political patterns and priorities.

In this regard, Moody's will also take into account the particular factors being evaluated in the review for possible upgrade of the sovereign ratings.

Amid the current global crisis, the rating agency emphasized that the Brazilian authorities have acted forcefully to ensure the stability of the banking system by employing safeguards that have been long-built into their regulatory framework. Among the most relevant measures are the use of sizable reserve requirements on deposits and the application of part of the central bank's foreign currency reserves to support banks' liquidity and funding needs (with no fiscal consequences).

Moody's also notes that the government-owned banks have played an important role in supporting the economy and in the orderly performance of the banking system, commanding significant deposit inflows in this period -- a dynamic that in part explains the positive outlook on Banco do Brasil's stand-alone BFSR rating (detailed below).

In Moody's view, the level of credit stress in the Brazilian banking system has been muted, although signs of asset quality deterioration and pressures on profits are evident and could increase further, were economic conditions to deteriorate.

#### Affirmation of Bank Financial Strength Ratings

In its reassessment of the banks' financial strength ratings and their outlooks, Moody's employs scenario analysis to determine the potential for expected losses on loan and investment portfolios; this method evaluates both anticipated and highly stressed scenarios to estimate the resulting impact on bank capitalization. In light of the weakened global economic environment, such an approach places greater emphasis on banks' capital adequacy and future earnings prospects.

The refinement in Moody's approach to banks' financial strength ratings is discussed in the Special Comment "Calibrating Bank Ratings in the Context of the Global Financial Crisis", published in February 2009.

In affirming Banco do Brasil and Banco Nossa Caixa's C bank financial strength ratings with a positive outlook, Moody's acknowledges the favorable trends for the banks' franchise and competitive positions, as well as for their financial metrics, which continue to converge with those of higher rated banks. The positive outlook also reflects Banco do Brasil's dominant deposit franchise and liquidity, which have been further strengthened in the current market turmoil.

Moody's also pointed out that the banks' capitalization is positioned to withstand potentially higher credit losses over the near term at its current rating level, despite the challenges of a robust recent growth in lending. This assessment is predicated on the banks' earnings-generation capacity and diversity, as well as on adequate provisioning policies.

In affirming Caixa Econômica Federal's D+ (D plus) bank financial strength rating with a stable outlook, Moody's explained that the bank's capitalization could well withstand potentially higher credit losses in the near term at its current rating level. The rating agency also noted that CEF's high growth rates over the past quarters could translate into an improved earnings stream, although such growth could strain its operating structure and pressure its financial fundamentals, as well.

#### Previous Ratings Actions and Principal Methodologies

The principal methodologies used in rating these banks were "Bank Financial Strength Ratings: Global Methodology" and "Incorporation of Joint Default Analysis into Moody's Bank Ratings: A Refined Methodology", which can be found on [www.moody.com](http://www.moody.com) in the Credit Policy & Methodologies directory in the Ratings Methodologies sub-directory. Other methodologies and factors that may have been considered in the process of rating the banks can also be found in the Credit Policy & Methodologies directory.

The last rating action on Banco do Brasil was on January 15, 2009 when all of its ratings were affirmed following the announcement of the partnership with Banco Votorantim S.A.

The last rating action on Banco Nossa Caixa was on March 24, 2009; at that time, Moody's upgraded its BFSR and global local currency deposit ratings following regulatory approval for its acquisition by Banco do Brasil. NC's foreign currency deposit and national scale ratings were also affirmed.

The last rating action on Caixa Econômica Federal (CEF) was on August 23, 2007 when the long-term foreign currency deposit rating was upgraded to Ba2, following the upgrade of Brazil's foreign currency deposit ceiling.

The last rating action on Banco Nacional de Desenvolvimento Econômico e Social (BNDES) was on August 23, 2007 when the long-term foreign currency deposit rating was upgraded to Ba2, following the upgrade of Brazil's foreign currency deposit ceiling.

The last rating action on BNDESPAR was on July 7, 2008, when Moody's rated its local currency debentures.

The detailed ratings and actions are listed below:

Banco do Brasil S.A.

- Bank Financial Strength rating of C: outlook changed to positive from stable
- Global long and short-term local currency (GLC) deposit ratings of A1/ Prime -1: placed on review for possible downgrade
- Long-term foreign currency deposit rating of Ba2: placed on review for possible upgrade
- Long-term foreign currency debt rating of Baa3: placed on review for possible upgrade
- Long and short-term national scale deposit ratings of Aaa.br/ Br-1: affirmed with stable outlook
- Short-term foreign currency deposit rating of Not Prime: affirmed

Banco do Brasil, Cayman Branch:

- Foreign currency senior and junior subordinated debt ratings of Baa3: placed on review for possible upgrade

Banco Nossa Caixa S.A.

- Bank Financial Strength rating of C: outlook changed to positive from stable
- Global long and short-term local currency (GLC) deposit ratings of A1/ Prime -1: placed on review for possible downgrade
- Long-term foreign currency deposit rating of Ba2 - placed on review for possible upgrade
- Long and short-term national scale deposit rating of Aaa.br/ BR-1: affirmed with stable outlook
- Short-term foreign currency deposit rating of Not Prime: affirmed

Caixa Econômica Federal

- Bank financial strength rating of D+: affirmed with stable outlook
- Global long and short-term local currency (GLC) deposit ratings of A1/ Prime 1: placed on review for possible downgrade
- Long-term foreign currency deposit rating of Ba2: placed on review for possible upgrade
- Long and short-term national scale deposit rating of Aaa.br/ BR-1: affirmed with stable outlook
- Short-term foreign currency deposit rating of Not Prime: affirmed

Banco Nacional de Desenvolvimento Econômico e Social S.A.

- Global long and short-term local currency (GLC) issuer ratings of A1/ Prime 1: placed on review for possible downgrade
- Long-term foreign currency deposit rating of Ba2: placed on review for possible upgrade

- Long and short-term national scale deposit rating of Aaa.br/ BR-1: affirmed with stable outlook
- Short-term foreign currency deposit rating of Not Prime: affirmed

BNDESPAR -- BNDES Participações S.A.:

- Global local currency issuer rating of A1: placed on review for possible downgrade
- Global local currency debt rating of A1: placed on review for possible downgrade
- National scale issuer rating of Aaa.br: affirmed with stable outlook.
- National scale debt rating of Aaa.br: affirmed with stable outlook

New York

M. Celina Vansetti

Senior Vice President

Financial Institutions Group

Moody's Investors Service

JOURNALISTS: 212-553-0376

SUBSCRIBERS: 212-553-1653

Sao Paulo

Ceres Lisboa

Vice President - Senior Analyst

Financial Institutions Group

Moody's America Latina Ltda.

55-11-3043-7300



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