

Rating Action: Moody's assigns first-time Ba3 ratings to BRAC Bank

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Singapore, March 05, 2018 -- Moody's Investors Service has assigned the following first-time ratings to Bangladesh-based BRAC Bank Limited:

- Global local and foreign currency issuer ratings of Ba3/NP;
- Local currency deposit ratings of Ba3/NP;
- Foreign currency deposit ratings of B1/NP;
- A standalone baseline credit assessment (BCA) of b1; and
- An adjusted BCA of b1

The ratings outlook is stable.

Moody's has also assigned a Counterparty Risk Assessment (CR Assessment) of Ba3(cr)/NP(cr) to the bank.

RATINGS RATIONALE

The Ba3 long-term ratings assigned to BRAC Bank incorporate its BCA of b1 and a one-notch uplift to reflect Moody's assumption of moderate systemic support for the bank in case of stress. However, its foreign currency deposit rating remains positioned at B1 because Bangladesh's foreign currency deposit ceiling is capped at that level.

BRAC Bank is a commercial bank with a strong focus on small and medium-sized enterprise (SME) loans.

The bank was started in 2001 by BRAC, one of the largest non-governmental development organizations in the world, with a focus on serving SMEs. BRAC Bank has around a 2%-3% share of total loans in the domestic market.

BRAC Bank's BCA of b1 is driven by its high profitability, healthy asset quality metrics and good capital levels. In addition, its relationship with BRAC gives confidence that the bank is less susceptible to the corporate governance issues which are a lingering feature of the Bangladesh banking system.

On the other hand, Moody's assessment of the bank's BCA also factors in the risks to asset quality from the very strong loan growth of the last few quarters, as well as its relatively weak liquidity profile.

The bank's profitability, with a return on assets (ROA) of 1.9% for the nine months ended 30 September 2017, is a key credit strength. This high ROA is supported by the sizeable share of high-yielding SME loans in its portfolio, and its low cost of funds because of its high current account and savings account (CASA) ratio when compared to peers.

The bank's asset quality metrics are healthy, with a problem loan ratio of 3.4% and a loan loss coverage ratio in excess of 100% at the end of 2016.

In addition, nonperforming loan formation rates have been at very low levels. However, the risk of loans seasoning remains, given the strong loan growth seen in the riskier sub-segments of both the retail and SME segments, which account for around 60% of the bank's loan book.

The retail book and SME loan book grew at 35% and 14% respectively during 2014-2016.

The bank's capital levels, with a Common Equity Tier 1 (CET 1) ratio of 11.3% at the end of September 2017, compare well with those of its peers within the Bangladesh banking system. In addition, the bank has demonstrated its access to the capital markets.

At the same time, despite its relatively high return on equity of 21% over January-September 2017, Moody's

expects a modest deterioration in its capital ratios over the next two years because of expected strong loan growth.

The bank's funding profile is a key credit strength. Its CASA ratio of 56% at the end of September 2017 is one of the highest in the system. This strong deposit franchise is driven by its strong brand equity in the retail segment and its cash management products in the corporate segment.

The bank's liquidity profile is a relative weakness. The bank has consistently had one of the highest loan to deposit ratios among domestic peers. This is primarily due to the management strategy of prioritizing profitability over maintaining liquidity buffers.

Moody's assumption of a moderate level of systemic support for bank reflects the bank's modest share of around 2.5% of system advances and deposits in a fragmented banking system, as well as the country's central bank's — Bangladesh Bank's — record of providing regulatory support to the banking system.

Moody's assessment of systemic support results in a one-notch uplift to BRAC Bank's ratings to Ba3, a result which is higher than the bank's BCA of b1.

COUNTERPARTY RISK ASSESSMENT

BRAC Bank's CR Assessment is positioned at Ba3(cr)/NP(cr). CR assessments are opinions of how counterparty obligations are likely to be treated if a bank fails and relates to a bank's contractual performance obligations (servicing), derivatives (e.g., swaps), letters of credit, guarantees and liquidity facilities. Senior obligations represented by the CR Assessments will be more likely preserved to limit contagion, minimize losses and avoid disruption of critical functions.

What Could Change the Rating Up/Down

An improvement in the bank's asset quality — to levels better than Moody's expects — which in turn leads to higher profitability by way of lower credit costs, could provide upward pressure on the ratings.

The bank shows significant borrower concentration. If some of the large accounts turn into NPLs, BRAC Bank's NPL ratios will deteriorate materially, thereby putting downward pressure on the ratings.

Moreover, a decline in its net interest margins to levels lower than Moody's expects will lead to a reduction in profitability and put downward pressure on the bank's ratings.

A summary of BRAC Bank's first-time ratings as assigned by Moody's is as follows:

- Ba3 local currency long-term deposit ratings; outlook stable, B1 foreign currency long-term deposit ratings; outlook stable
- Ba3 local currency and foreign currency long-term issuer ratings; outlook stable
- b1 BCA and b1 adjusted BCA
- Ba3(cr)/NP(cr) long-term and short term counterparty risk assessments
- NP local currency and foreign currency short-term deposit ratings
- NP local currency and foreign currency short-term issuer ratings

The principal methodology used in these ratings was Banks published in September 2017. Please see the Rating Methodologies page on www.moodys.com for a copy of this methodology.

Headquartered in Dhaka, BRAC Bank Limited's consolidated assets totaled BDT295 billion (approximately \$3.6 billion) at 30 September 2017.

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