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BRAC Bank Ltd.

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Table Of Contents

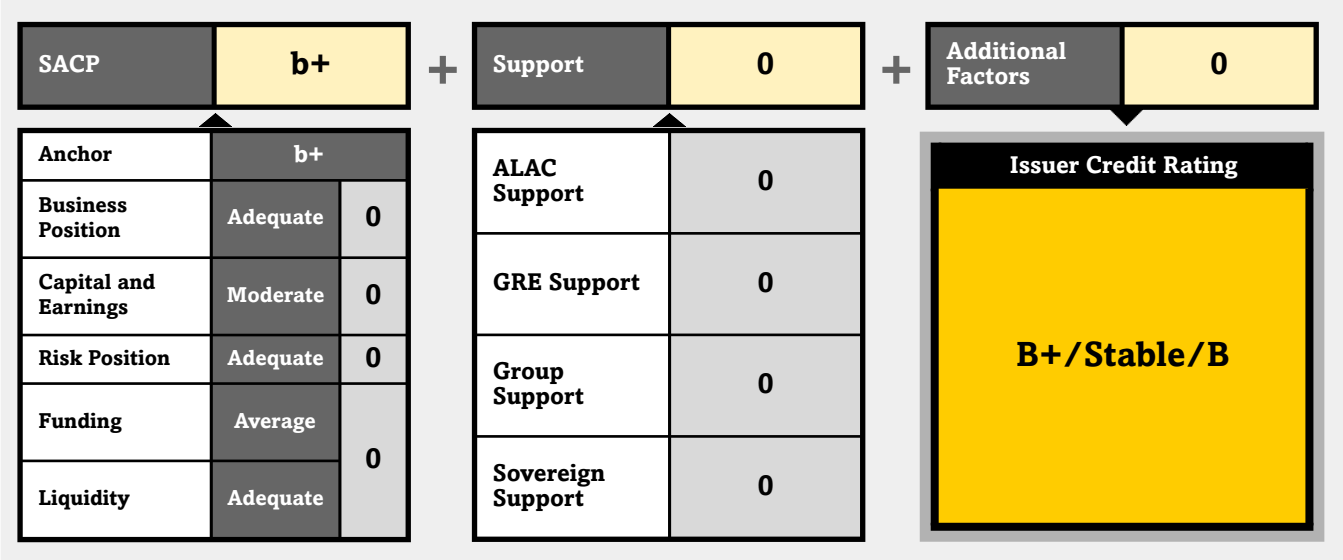
Major Rating Factors

Outlook

Rationale

Related Criteria

BRAC Bank Ltd.



Major Rating Factors

Strengths:	Weaknesses:
<ul style="list-style-type: none"> • Good management and business franchise in the domestic retail and SME segments. • Above-industry-average asset quality and capitalization. 	<ul style="list-style-type: none"> • Challenging operating environment amid COVID-19 induced economic slowdown and substantial credit risk in the economy. • Reduced profitability due to pressure on interest margin and credit cost.

Outlook: Stable

The stable outlook on BRAC Bank Ltd. reflects our view that the bank will steadily navigate challenging operating conditions in Bangladesh and maintain its financial profile over the next 12-18 months.

Upside scenario

We could upgrade BRAC Bank if its profitability improves while remaining higher than the industry average, and the bank increases its market share in a sustainable fashion without strategic or operational missteps. This could be shown by sustained good asset quality metrics, prudential underwriting standards, and healthy capitalization.

Downside scenario

We may lower the rating if the bank's asset quality deteriorates sharply, for example due to prolonged reduction in economic activity in Bangladesh.

Rationale

The rating on BRAC Bank reflects the bank's good franchise, particularly in the small and midsize enterprise (SME) and retail segments in Bangladesh. The bank enjoys above-industry-average asset quality and capitalization. We expect the bank's deposit base to remain adequate thanks to its satisfactory distribution network and brand name. Its credit exposures remain concentrated in Bangladesh, a country where banks face relatively high competition, substantial credit risk versus international peers, and a COVID-19 related economic shock that will increase stressed assets in the next nine to 12 months. We expect BRAC Bank's credit growth to slow compared with the past few years, given that businesses and individuals will have reduced demand for new loans in the wake of the economic slowdown in Bangladesh. We expect the bank's profitability to be muted relative to its average over 2016-2019, owing to higher credit costs and lower net interest margins (NIMs). However, its capitalization provides cushion to absorb such shocks. The rating is in line with the bank's stand-alone credit profile of 'b+'.

Anchor: 'b+' for a commercial bank operating in Bangladesh

In our opinion, Bangladesh's low-income economy, heavy development needs, and fiscal constraints limit its economic resilience. Bangladesh's economy, like most others in the world, has been hit hard by the COVID-19 pandemic in 2020. However, the country has healthy medium-term growth prospects and relatively low economic imbalances, with credit growing in line with nominal GDP and benign inflation and current account positions. Bangladesh's credit risk remains extremely high, with weak foreclosure laws and underwriting standards, weak governance at some banks, and client concentration leading to sizable stressed assets in the banking industry.

Bangladesh is aiming to implement international regulatory standards. However, supervision has gaps and results in limited market discipline. Weak asset quality and capitalization of some banks in the country reflect gaps in monitoring and in the system's inability to address problems early. In our view, Bangladesh's banking system has overcapacity and market distortions. A supportive core customer deposit base and low reliance on external funding temper these weaknesses.

Table 1

BRAC Bank Ltd.--Key Figures					
--Fiscal year ended Dec. 31--					
(Mil. BDT)	2020*	2019	2018	2017	2016
Adjusted assets	444,521.0	401,828.6	346,359.5	309,359.1	258,807.5
Customer loans (gross)	N.A.	264,870.3	238,400.4	203,431.0	175,841.4
Adjusted common equity	N.A.	43,245.8	38,600.1	26,204.9	21,414.2
Operating revenues	N.A.	27,804.8	26,000.9	23,687.3	20,181.7
Noninterest expenses	N.A.	18,859.4	16,691.1	14,248.9	11,544.5
Core earnings	N.A.	4,572.7	5,587.5	5,509.6	4,103.4

*Data as of Sept. 30. BDT--Bangladeshi taka. N.A.--Not available.

Business position: Diversified business mix

We expect BRAC Bank to maintain its market position and business stability over the next 12-15 months. It is among the top 15 banks in the country and accounts for about 2.4% of the system's loans and deposits. Bangladesh's banking

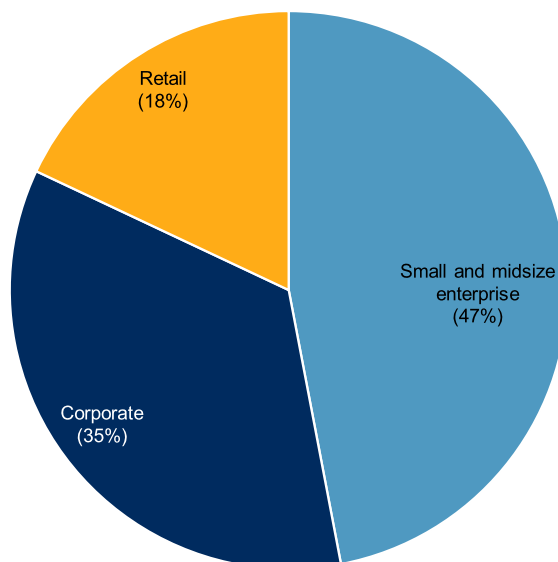
industry is quite fragmented and the bank competes with more than 50 other banks in the country. While business growth in the next six to nine months may be tepid, we expect BRAC Bank to continue to grow its franchise in the competitive yet underpenetrated financial services industry in Bangladesh over the medium to long term. As of end-December 2019, the bank's distribution network is spread over 187 branches, 424 ATMs, and 456 SME unit offices that service SMEs.

BRAC Bank has a diversified loan exposure to SMEs (47% of loans), corporates (35%), and the retail segment (18%) as of Sept. 30, 2020. The bank has a higher focus on retail and SME segments than other local banks. This compares with an industry average where loans to corporates comprise around 75% of total loans. BRAC Bank uses mobile-banking solutions--through its subsidiary bKash Ltd.--to reach a sizable underbanked and unbanked population in the country. Banks in Bangladesh have traditionally focused on the wholesale segment due to relationship-based lending and higher operating costs associated with SMEs and retail businesses. BRAC Bank's fee income comes mainly from mobile banking, trade finance, and card products. This income constituted around 25% of the bank's operating revenues on average in the past five years, which is relatively high compared with its peers, and adds to its business diversity.

Chart 1

BRAC Bank Has Diversified Loan Exposure

Loan mix as of Sept. 30, 2020



Source: Published results.

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We consider BRAC Bank's management to be satisfactory. The management team has identified SME and retail segments as the bank's niche and has since 2015 embarked on strategies to improve operating competitiveness. We

expect the bank to increasingly migrate customers from physical channels to digital ones to reduce operating cost and offer more convenience to the customers. BRAC Bank's management has shown prudence in managing its balance sheet by keeping above-industry-average capitalization and increasing liquidity in the first half of 2020. That said, the bank's profitability has come under strain owing to a 9% interest rate cap introduced by the regulator and the bank's higher exposure to SME businesses, which tend to have higher operating costs.

Table 2**BRAC Bank Ltd.--Business Position**

	--Fiscal year ended Dec. 31--				
(%)	2020*	2019	2018	2017	2016
Return on average common equity	8.3	13.1	17.9	21.3	18.3

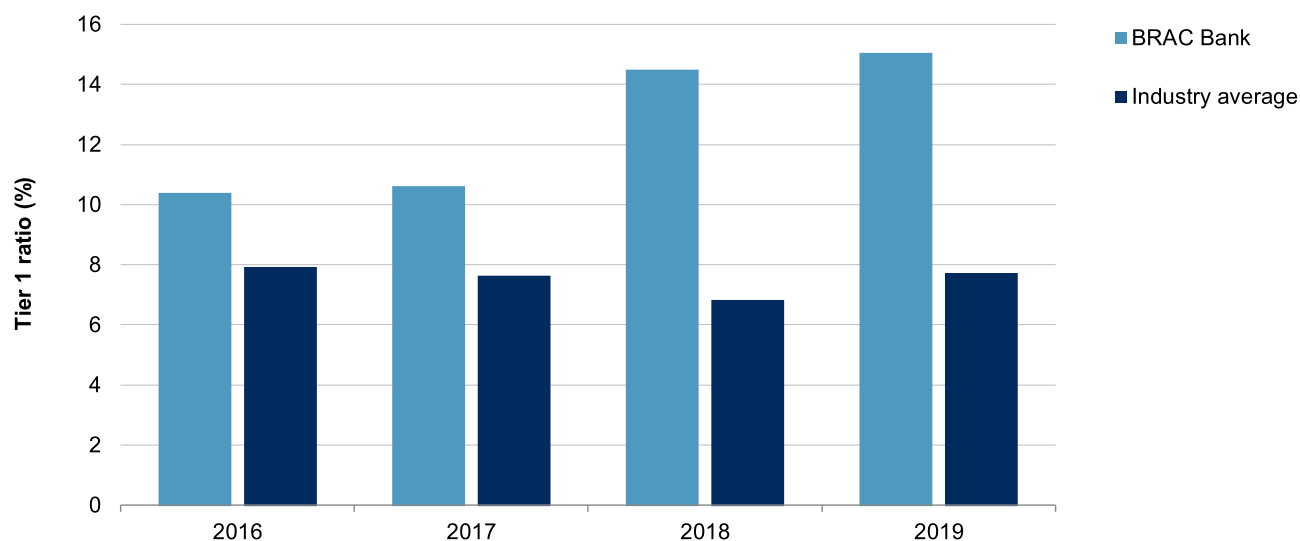
*Data as of Sept. 30.

Capital and earnings: Profitability to deteriorate, while above-industry-average capitalization provides some buffer

Our assessment of BRAC Bank's capital and earnings reflects our expectation that the bank's pre-diversification risk-adjusted capital ratio will remain above 5% over the next 12-18 months. The bank has above-industry-average capitalization due to historically high internal capital generation and retention, and additional capital injection by its subsidiary bKash in 2018. The enhanced capital base has supported its expansion in the fast-growing Bangladesh market.

Chart 2

BRAC Bank's Capitalization Is Better Than The Industry Average



Source: Bank reports, Bangladesh Bank.

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We anticipate BRAC Bank's credit growth will be in single digits in the next six to 12 months before reverting to double digits. Both the bank and its customers are likely to remain cautious this year. In our view, businesses and individuals will have lower demand for new loans amid weak economic conditions. Individuals could face reduced incomes and consumer confidence could weaken due to wage reductions or unemployment. Businesses would likely conserve cash and delay capital expenditure given economic uncertainties. In order to support its balance sheet, the bank is likely to pay modest dividends if any.

We expect BRAC Bank's profitability to remain below its 2016-2019 average over the next nine to 15 months. This is due to the twin effects of NIM compression and an increase in credit cost from the cyclically low levels of the past couple of years. The regulator has imposed an interest rate cap of 9% on all loans barring credit card loans since April 2020, which reduced the bank's spreads by around 200 basis points. At the same time, deposit rates are also getting repriced at a lower level, however BRAC Bank's NIM is unlikely to revert to earlier levels because it has sizable SME loans. Similarly, credit cost is likely to be elevated as the pandemic is straining cash flows of individuals and causing hardship to businesses, notwithstanding some improvement over time as peak COVID-19 stress recedes.

Given margin and credit cost pressures, the management of operating cost through increasing use of technology and rationalizing of existing infrastructure, securing noninterest income including investment income via opportunistic gains on government securities and dividend payouts will be key capital management drivers.

BRAC Bank's ratio of core earnings to average assets has averaged about 1.5% over the past five years, which is better than the industry average of 0.6%. The bank's profitability has been characterized by high NIMs owing to higher yields on its SME and retail portfolio, fee income contribution from mobile banking and trade finance, and competitive cost of funds due to sizable low-cost deposits. The bank's operating revenues has helped to offset elevated operating costs. The operating cost for the bank has been high due to its large SME clientele and investments in staff, infrastructure, and technology initiatives especially through its subsidiary bKash.

Table 3

BRAC Bank Ltd.--Capital And Earnings					
	--Fiscal year ended Dec. 31--				
(%)	2020*	2019	2018	2017	2016
Tier 1 capital ratio	N.A.	15.0	14.5	10.6	10.4
Adjusted common equity/total adjusted capital	100.0	100.0	100.0	100.0	100.0
Net interest income/operating revenues	N.A.	73.2	67.3	65.6	68.9
Fee income/operating revenues	N.A.	21.0	25.1	25.5	24.3
Market-sensitive income/operating revenues	N.A.	4.5	7.0	9.8	4.5
Cost to income ratio	N.A.	67.8	64.2	60.2	57.2
Preprovision operating income/average assets	N.A.	2.4	2.8	3.3	3.6
Core earnings/average managed assets	0.7	1.2	1.7	1.9	1.7

*Data as of Sept. 30. N.A.--Not available.

Table 4

BRAC Bank Ltd.--Risk-Adjusted Capital Framework Data			
(Mil. BDT)	Exposure*	S&P Global Ratings RWA	Average S&P Global Ratings RW (%)
Credit risk			
Government & central banks	70,852,192,931.5	59,615,618,793.9	84.1
Institutions and CCPs	54,127,081,291.1	104,048,488,365.9	192.2
Corporate	225,884,049,882.4	376,473,416,470.7	166.7
Retail	49,951,234,168.6	72,183,927,365.7	144.5
Of which mortgage	14,921,308,922.7	13,800,718,622.6	92.5
Other assets†	23,204,270,437.3	61,774,107,493.2	266.2
Total credit risk	424,018,828,710.9	674,095,558,489.5	159.0
Credit valuation adjustment			
Total credit valuation adjustment	--	--	--
Market risk			
Equity in the banking book	2,922,040,664.4	30,245,144,195.2	1,035.1
Trading book market risk	--	16,277,516,647.1	--
Total market risk	--	46,522,660,842.3	--
Operational risk			
Total operational risk	--	52,134,017,782.5	--
	Exposure	S&P Global Ratings RWA	% of S&P Global Ratings RWA
Diversification adjustments			
RWA before diversification	--	772,752,237,114.3	100.0
Total diversification/ concentration adjustments	--	278,103,572,186.0	36.0
RWA after diversification	--	1,050,855,809,300.3	136.0
		Total adjusted capital	S&P Global Ratings RAC ratio (%)
Capital ratio			
Capital ratio before adjustments		43,245,806,262.0	5.6
Capital ratio after adjustments‡		43,245,806,262.0	4.1

*Exposure at default. †Exposure and S&P Global Ratings' risk-weighted assets for equity in the banking book include minority equity holdings in financial institutions. ‡Adjustments to Tier 1 ratio are additional regulatory requirements (e.g. transitional floor or Pillar 2 add-ons). RWA--Risk-weighted assets. RW--Risk weight. RAC--Risk-adjusted capital. CCP--Central counterparty. BDT--Bangladeshi taka. Sources: Company data as of Dec. 31, 2019, S&P Global Ratings.

Risk position: COVID-related stress to rise

Our assessment of BRAC Bank's risk position reflects our view that the bank's credit losses--though higher than in the past few years--will remain within our normalized loss expectations over the next 12-15 months.

BRAC Bank has benefited from an economy that experienced one of the highest real GDP growth rates in Asia averaging over 7% in the past five years. The bank's overall loan book, comprising corporate, SMEs, and retail, is more balanced than the industry. Although BRAC Bank has corporate client concentration, its concentration is lower than

the industry average in Bangladesh. The corporate segment has been a source of poor risk culture in Bangladesh's banking industry. BRAC Bank's main corporate exposures include readymade garments and textiles (10% of loans in 2019 and a key export sector in Bangladesh) and sectors such as steel, food/allied, paper, auto, telecommunications, and power.

The bank's growth of unsecured exposures in the SME and retail segments are historically balanced by the granularity and high spreads on these exposures and good understanding of SME clients. BRAC Bank's SME business caters to entrepreneurs and small businesses with average ticket sizes of US\$7,000-US\$75,000; loans are given for business expansion. The smaller ticket-size loans are unsecured while the larger ones are secured by mortgages. The bank's retail loans consist of home loans (where the loan-to-value ratio has a regulatory cap of 70%), followed by personal loans and credit cards.

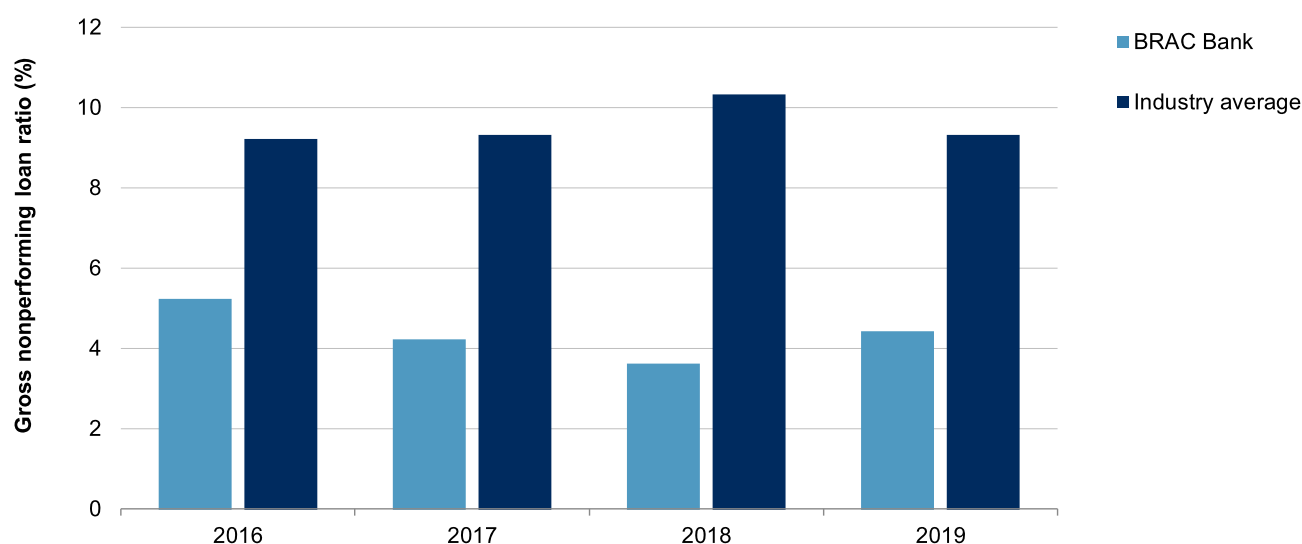
BRAC Bank had a lower gross nonperforming loan ratio of 4.4% as of December 2019 (3.2% as of September 2020) compared with the industry average of 9.3%. The banking system is also prone to moral hazard due to forbearance allowed in the form of rescheduling of loans which constituted 11.2% of total loans as of end-2019 compared with BRAC Bank's 0.55%.

However, the asset quality of BRAC Bank is likely to deteriorate over the next 12-15 months because individuals and businesses are facing weaker cash flows amid sluggish COVID-related demand, both externally and domestically (due to social distancing measures). We expect Bangladesh's economy to slow markedly to around 5% in the aftermath of the pandemic. While the country's exports have bounced back in recent months, the bank's textile and garment clients will remain exposed to fresh lockdowns in the U.S. and European economies.

In the wake of the COVID-related slowdown, the regulator has directed banks to extend debt relief to affected borrowers and imposed a moratorium on debt repayment till December 2020. As of September 2020, 76% of BRAC Bank's SME clients had availed of the moratorium (though 30% of those clients still paid their loans), while 5% of the bank's retail loans were under moratorium.

Chart 3

BRAC Bank's Asset Quality Is Better Than The Industry Average



Source: Bank reports, Bangladesh Bank.

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Table 5

BRAC Bank Ltd.--Risk Position

(%)	--Fiscal year ended Dec. 31--				
	2020*	2019	2018	2017	2016
Growth in customer loans	0.5	11.1	17.2	15.7	17.3
Total managed assets/adjusted common equity (x)	10.0	9.4	9.1	11.9	12.2
New loan loss provisions/average customer loans	0.9	0.6	0.3	0.6	1.0
Gross nonperforming assets/customer loans + other real estate owned	N.A.	4.5	3.6	4.2	5.2
Loan loss reserves/gross nonperforming assets	N.A.	82.8	99.6	94.0	88.4

*Data as of Sept. 30. N.A.--Not available.

Funding and liquidity: Deposit franchise supports funding

We expect BRAC Bank to maintain its diversified deposit franchise over the next 12-18 months. The bank's deposits, particularly its sizable low-cost current and saving accounts (CASA), support its funding profile. As of Dec. 31, 2019, deposits contributed to 87% of the bank's funding base, in line with the industry average of 89%. Household deposits accounted for around 56% of deposits in September 2020, followed by corporates (27%) and SMEs (17%). The bank's CASA ratio of around 50% in September 2020 was higher than the industry average of 41% as of Dec. 31, 2019. Its ratio of loans to customer deposits was 87% as of Dec. 31, 2019, in line with the industry average of 89%. BRAC Bank has increased its deposit base in the past few quarters and shored up liquidity in the wake of the loan moratorium provided to its clients. Excess liquidity has been parked in government securities amid the declining interest rate

environment, leading to sizable treasury gains this year.

BRAC Bank's assets in the form of cash and short-term funds underpin its liquidity. The bank's ratio of broad liquid assets to short-term wholesale funding was 3.9x as of Dec. 31, 2019, in line with that of global peers.

Table 6

BRAC Bank Ltd.--Funding And Liquidity					
	--Fiscal year ended Dec. 31--				
(%)	2020*	2019	2018	2017	2016
Core deposits/funding base	89.0	86.8	84.6	82.2	80.4
Customer loans (net)/customer deposits	82.1	86.8	94.9	94.6	98.7
Long-term funding ratio	N.A.	92.9	92.2	90.3	89.6
Stable funding ratio	N.A.	118.1	113.4	104.9	103.3
Short-term wholesale funding/funding base	N.A.	8.0	8.9	10.8	11.5
Broad liquid assets/short-term wholesale funding (x)	N.A.	3.9	3.4	2.7	2.4
Short-term wholesale funding/total wholesale funding	N.A.	60.8	57.5	60.6	58.5

*Data as of Sept. 30. N.A.--Not available.

Related Criteria

- 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: 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 December 2, 2020)*

BRAC Bank Ltd.

Issuer Credit Rating

B+/Stable/B

Issuer Credit Ratings History

26-Feb-2018

B+/Stable/B

Sovereign Rating

Bangladesh

BB-/Stable/B

*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.

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