

## CREDIT OPINION

28 June 2016

Update

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## RATINGS

## Banco de los Trabajadores

Domicile	Guatemala City, Guatemala
Long Term Rating	B1, Possible Downgrade
Type	LT Bank Deposits - Fgn Curr
Outlook	Rating(s) Under Review

Please see the ratings section at the end of this report for more information. The ratings and outlook shown reflect information as of the publication date.

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## Banco de los Trabajadores

## Update Following Downgrade

## Summary Rating Rationale

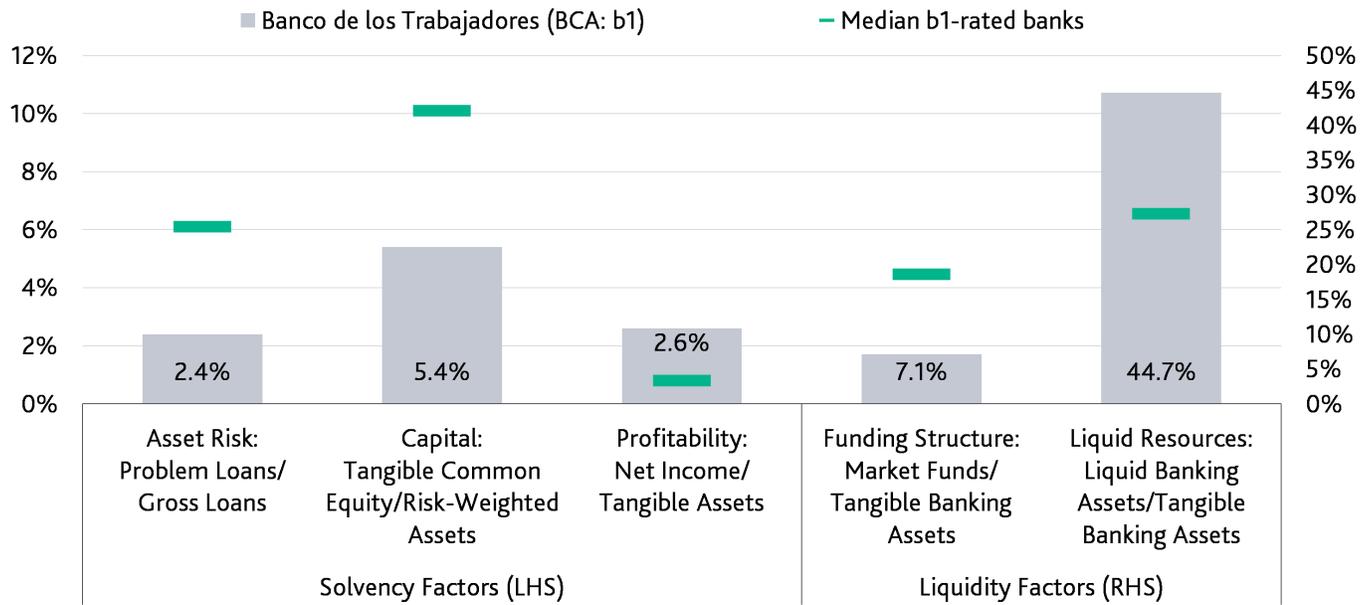
Moody's assigns a baseline credit assessment (BCA) of b2, under review for downgrade, to Guatemala's Banco de los Trabajadores (Bantrab). The BCA takes into account Bantrab's rising funding risks and weak core capital. The standalone assessment on the other hand gauges the bank's well-managed asset risks in part as a result of its preferential creditor status.

The B1 local and foreign currency deposit ratings, under review for downgrade, assigned to Bantrab incorporate one notch of uplift from the b2 BCA due to our assessment of a moderate probability of government support in case of need. This assumption is based on the bank's importance as a lender to Guatemalan public sector workers, as well as its government inception. Moody's also assigns a B1 foreign currency senior unsecured debt rating, on review for downgrade, to Bantrab Senior Trust (BST), a Cayman Islands-based trust guaranteed by Bantrab.

On 24 June 2016, we downgraded Bantrab's ratings and placed them on review for downgrade, reflecting the bank's loss of all of its correspondent banking lines which if not addressed in a timely manner could potentially prevent the bank from paying the November 2016 coupon of BST's global bond.

The review will focus on Bantrab's ability to secure new stable and reasonably priced correspondent banking lines in a timely manner. We will also reassess the probability that the bank will benefit from public support with a focus on any measures Guatemala's Superintendency of Banks and central bank may take to help ensure the bank's ability to repay foreign bondholders despite the loss of its correspondent lines.

Exhibit 1  
**Rating Scorecard - Key Financial Ratios**



Source: Moody's Financial Metrics

This publication does not announce a credit rating action. For any credit ratings referenced in this publication, please see the ratings tab on the issuer/entity page on [www.moody.com](http://www.moody.com) for the most updated credit rating action information and rating history.

## Credit Strengths

- » Asset quality supported by the bank's preferential creditor status

## Credit Challenges

- » Loss of correspondent banking lines could prevent the payment of Bantrab Senior Trust's November Coupon
- » Weak capital provides limited buffer to absorb credit and investment losses
- » Declining core profitability given narrowing net interest margins and a weak efficiency
- » Bantrab's ratings are constrained by Guatemala's weak Macro Profile

## Rating Outlook

All ratings and assessments are on review for downgrade.

## Factors that Could Lead to an Upgrade

Upward pressures on the ratings are limited at this juncture in light of the current review for downgrade.

## Factors that Could Lead to a Downgrade

Bantrab's ratings could be downgraded further if the bank does not manage to obtain new stable and reasonably priced correspondent banking lines in a timely manner, or if Guatemala's Superintendency of Banks and central bank appear less willing to take measures to help ensure the timely payment of BST's bond than we previously viewed them to be.

## Key Indicators

Exhibit 2

### Banco de los Trabajadores (Consolidated Financials) [1]

	3-16 <sup>2</sup>	12-15 <sup>2</sup>	12-14 <sup>2</sup>	12-13 <sup>2</sup>	12-12 <sup>2</sup>	Avg.
Total Assets (GTQ million)	17856.0	16944.5	14144.4	12599.5	9623.8	16.7 <sup>3</sup>
Total Assets (USD million)	2315.5	2219.8	1861.5	1606.6	1217.7	17.4 <sup>3</sup>
Tangible Common Equity (GTQ million)	1352.6	838.2	637.5	498.9	487.4	29.1 <sup>3</sup>
Tangible Common Equity (USD million)	175.4	109.8	83.9	63.6	61.7	29.9 <sup>3</sup>
Problem Loans / Gross Loans (%)	2.6	2.4	1.3	1.5	2.4	2.0 <sup>4</sup>
Tangible Common Equity / Risk Weighted Assets (%)	8.3	5.4	4.9	4.8	5.7	5.8 <sup>5</sup>
Problem Loans / (Tangible Common Equity + Loan Loss Reserve) (%)	13.7	18.0	12.5	15.5	19.6	15.9 <sup>4</sup>
Net Interest Margin (%)	6.8	8.5	9.3	10.5	9.8	9.0 <sup>4</sup>
PPI / Average RWA (%)	2.9	3.2	3.9	5.8	4.2	4.0 <sup>5</sup>
Net Income / Tangible Assets (%)	2.3	2.6	2.2	1.8	1.4	2.0 <sup>4</sup>
Cost / Income Ratio (%)	64.2	65.9	63.7	64.9	65.1	64.8 <sup>4</sup>
Market Funds / Tangible Banking Assets (%)	6.6	7.1	9.2	11.6	5.0	7.9 <sup>4</sup>
Liquid Banking Assets / Tangible Banking Assets (%)	46.4	44.7	38.1	43.6	39.4	42.5 <sup>4</sup>
Gross loans / Due to customers (%)	63.3	65.2	74.2	69.9	69.4	68.4 <sup>4</sup>

[1] All figures and ratios are adjusted using Moody's standard adjustments [2] Basel I; LOCAL GAAP [3] Compound Annual Growth Rate based on LOCAL GAAP reporting periods [4] LOCAL GAAP reporting periods have been used for average calculation [5] Basel I & LOCAL GAAP reporting periods have been used for average calculation

Source: Moody's Financial Metrics

## Detailed Rating Considerations

LOSS OF CORRESPONDENT BANKING LINES COULD PREVENT THE PAYMENT OF BANTRAB SENIOR TRUST'S NOVEMBER COUPON

As of last year, Bantrab had correspondent banking relationships in the U.S, which it relied upon to help administer the coupon payments on BST's bonds. The loss of Bantrab's final correspondent line in May 2016 appears to reflect in part concerns by the

counterparty regarding the recent seizure by Guatemala's Public Ministry (PM) in April 2016 of Bantrab's non-voting preferred shares that had been held by Panama-based DHK Finance Inc.

This development occurred in a context of a large political scandal in Guatemala and a generalized increase in risk aversion of international banks towards Central America due to rising apprehensions about weaknesses in regional banks' and regulators' anti-money laundering controls. The share seizure, following which we revised the bank's outlook to negative, was in response to allegations by Guatemala's Superintendency of Banks that the funds used to purchase these shares were obtained illegally and that potential wrongdoing might have occurred during the sale of those shares to DHK.

Bantrab's senior management reports that it is actively looking to secure new correspondent banking lines at the moment. Even if the bank manages to obtain new lines, however, they are likely to come at a significant cost and their stability will remain uncertain.

Thick liquidity buffers can help withstand funding volatilities. Bantrab maintains a large store of liquid assets on its balance sheet with a liquid banking assets to tangible banking assets ratio of 46% as of March 2016. Liquidity is chiefly in the form of required liquidity reserves at the central bank and Ba1-rated, with a negative outlook, government securities. The latter provide the bank some financial flexibility in the event of a funding squeeze.

#### LIMITED CORE CAPITAL MAY CONSTRAIN FRANCHISE DEVELOPMENT

Bantrab's core capital remains weak, having been pressured by historical sturdy loan growth and modest earnings generation, despite a relatively moderate payout ratio of 23%. As of March 2015, the bank's tangible common equity stood at about 6.5% of risk-weighted assets, when government securities are 100%-weighted as prescribed by Basel for Ba-rated sovereigns, and intangibles and goodwill are deducted. The seized preferred shares amounting Q157 million are not included in the calculation of the TCE, because they have non-deferrable payment features.

#### DECLINING CORE PROFITABILITY GIVEN NARROWING NET INTEREST MARGINS AND A WEAK EFFICIENCY

Bantrab's core profitability has been declining over the past three years. Pre-provision income has slid to 2.7% of total average assets as of March 2016 from 3.6% by year-end 2013. This trend is largely explained by a continued weak efficiency and declining NIMs, given competitive pressures on lending rates and higher funding costs largely explained by the global senior long-term bond which carries a 9% coupon, higher than the 7.8% average funding cost. We expect increases in funding costs in the case of volatilities in funding while the investigation on DHK is ongoing, which will further compress NIMs.

Return on assets have been, in turn, growing to a very strong 2.3% from 1.8% during the same period. However, this metric incorporates the non-recurring flow of recoveries from the clean-up of Banco de la Republica's. As these are largely complete, we expect the ROA to progressively decline to more sustainable levels.

Earnings will also be strained if Bantrab's loan growth is curtailed as a result of the investigation on DHK, as management focuses on addressing possible flaws in its internal controls rather than growing its business.

#### ASSET QUALITY SUPPORTED BY THE BANK'S PREFERENTIAL CREDITOR STATUS

The bank's asset quality benefits from its preferential creditor status (e.g. payment preference vis-à-vis other authorized deductions) per its Organic Law. The key risk to asset quality is the aforementioned hefty loan growth, especially amid the current economic deceleration in the country. NPLs rose to a still manageable 2.6% of gross loans as of March 2016 from 1.5% as of December 2013, in part explained by an internal policy change that reduced charge-offs. At the same time, reserves remained thick at 151% of NPLs and 3.9% of gross loans.

The lack of full board independence, especially amid the existing business linkages with the government, increases the bank's asset quality risks, given the absence of full independent oversight over how the bank deploys its resources. The President of the Republic directly appoints the Chairman of the Board.

## BANTRAB'S RATINGS ARE CONSTRAINED BY GUATEMALA'S WEAK MACRO PROFILE

Guatemala's macro profile reflects the country's low GDP per capita notwithstanding steady growth in recent years, and poor institutional strength that is weak overall despite relatively strong monetary and fiscal institutions. The change in both the macro profile and the government's outlook reflect increasing concerns about the strength of the country's institutional framework in light of ongoing corruption scandals implicating high ranking government officials that have led to widespread street demonstrations. Credit growth has been robust over the past several years, fueled by the steadily growing economy. Competition within the banking system has recently tightened, in line with the entrance of strong regional franchises.

### Notching Considerations

In the absence of a bail-in resolution regime framework Guatemala, as per the "Banks" Methodology, updated in January 2016, we align the B1 deposit rating with the senior unsecured rating of the notes issued through Bantrab Senior Trust. Both ratings are on review for downgrade.

### Government Support

We believe that there is a moderate likelihood of government support for Bantrab's bank deposits and senior unsecured debt ratings in the event of its failure. This assumption is based on the bank's importance as a lender to Guatemalan public sector workers, as well as its government inception.

### Counterparty Risk Assessment

The CR Assessment is positioned at Ba3(cr).

The CR Assessment is positioned two notches above the adjusted BCA of b2, and also benefits from two notches of government support, in line with our support assumptions on deposits and senior unsecured debt. This reflects our view that any support provided by governmental authorities to a bank which benefits senior unsecured debt or deposits is very likely to benefit operating activities and obligations reflected by the CR Assessment as well, consistent with our belief that governments are likely to maintain such operations as a going-concern in order to reduce contagion and preserve a bank's critical functions.

CR Assessments are opinions of how counterparty obligations are likely to be treated if a bank fails and are distinct from debt and deposit ratings in that they (1) consider only the risk of default rather than both the likelihood of default and the expected financial loss suffered in the event of default and (2) apply to counterparty obligations and contractual commitments rather than debt or deposit instruments. The CR assessment is an opinion of the counterparty risk related to a bank's covered bonds, contractual performance obligations (servicing), derivatives (e.g., swaps), letters of credit, guarantees and liquidity facilities.

### About Moody's Bank Scorecard

Our Scorecard is designed to capture, express and explain in summary form our Rating Committee's judgment. When read in conjunction with our research, a fulsome presentation of our judgment is expressed. As a result, the output of our Scorecard may materially differ from that suggested by raw data alone (though it has been calibrated to avoid the frequent need for strong divergence). The Scorecard 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 Methodology and Scorecard Factors

Exhibit 3

### Banco de los Trabajadores

Macro Factors						
Weighted Macro Profile	Weak	100%				
Financial Profile						
Factor	Historic Ratio	Macro Adjusted Score	Credit Trend	Assigned Score	Key driver #1	Key driver #2
Solvency						
Asset Risk						
Problem Loans / Gross Loans	2.6%	ba3	← →	b1	Loan growth	Sector concentration
Capital						
TCE / RWA	8.3%	b3	↓↓	caa2	Expected trend	
Profitability						
Net Income / Tangible Assets	2.2%	ba1	↓↓	ba3	Expected trend	
Combined Solvency Score		b1		b2		
Liquidity						
Funding Structure						
Market Funds / Tangible Banking Assets	7.1%	ba1	↓	caa1	Deposit quality	
Liquid Resources						
Liquid Banking Assets / Tangible Banking Assets	44.7%	ba1	↓	ba2	Quality of liquid assets	
Combined Liquidity Score		ba1		b2		
Financial Profile				b2		
Business Diversification				0		
Opacity and Complexity				0		
Corporate Behavior				0		
Total Qualitative Adjustments				0		
Sovereign or Affiliate constraint:				Ba1		
Scorecard Calculated BCA range				b1-b3		
Assigned BCA				b2		
Affiliate Support notching				0		
Adjusted BCA				b2		
Instrument Class	Loss Given Failure notching	Additional notching	Preliminary Rating Assessment	Government Support notching	Local Currency rating	Foreign Currency rating
Counterparty Risk Assessment	1	0	b1 (cr)	1	Ba3(cr) RUR Possible Downgrade	--
Deposits	0	0	b2	1	B1 RUR Possible Downgrade	B1 RUR Possible Downgrade

Source: Moody's Financial Metrics

## Ratings

Exhibit 4

Category	Moody's Rating
<b>BANCO DE LOS TRABAJADORES</b>	
Outlook	Rating(s) Under Review
Bank Deposits	B1/NP
Baseline Credit Assessment	b2
Adjusted Baseline Credit Assessment	b2
Counterparty Risk Assessment	Ba3(cr)/NP(cr)
<b>BANTRAB SENIOR TRUST</b>	
Outlook	Rating(s) Under Review
Bkd Senior Unsecured	B1

Source: Moody's Investors Service

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