



## Fitch Upgrades BS2's National Ratings to 'BBB+(bra)'/F2(bra)'; Affirms IDRs at 'B+'; Outlook Stable

Fitch Ratings - Rio de Janeiro - 11 November 2019:

Fitch Ratings has affirmed Banco BS2 S.A.'s Long-Term Foreign and Local Currency Issuer Default Ratings (IDRs) at 'B+' and Viability Rating (VR) at 'b+'. At the same time, Fitch has upgraded BS2's Long-Term and Short-Term National Ratings to 'BBB+(bra)'/F2(bra)' from 'BBB(bra)'/F3(bra)'. The Rating Outlooks for the Long-Term IDRs and National Scale Ratings are Stable.

The upgrade of BS2's National Ratings reflect Fitch's view on the bank's ongoing efforts over the last years to consolidate its different business lines in a service-oriented platform that is expected to lead the bank to a better diversified revenues composition in the medium term among domestic peers.

### Key Rating Drivers

#### KEY RATING DRIVERS

#### VR, IDRs, NATIONAL RATINGS

BS2's VR and IDRs are highly influenced by its company profile. It primarily reflects the challenges inherent to the development of its new business lines, as well as by the pressures on profitability and regulatory capital ratios by the ongoing growth of assets, despite successive capital injections made over the last two years.

BS2 strategy is to become a service-oriented digital business hub, providing both own and third-party products to its customer base through partnerships. In early 2019, BS2 launched its own digital platform for both individuals and SME clients. At the same time, the bank continues to expand in other areas. Currently, BS2 also operates with judicial securities issued by Brazil's federal and states governments (Precatorios), SME lending, foreign exchange and acquiring operations. A good part of BS2's business units have been performing well and are already contributing to bank profitability. However, other segments benefits (especially those linked to its digital strategy) will likely come in the medium term, as the bank gains scale and its new businesses are more relevant to its results. Fitch notes that BS2's digital platform implementation has required material investments throughout 2019. As any other entity opening a new business strategy, BS2 is exposed to potential regulatory and/or operational risks, which may reduce as its new businesses' evolves and consolidates.

Fitch also positively factors BS2's strategy on revenue diversification through fee products, which has brought higher and more diverse revenues (that tend to be more stable along the cycles) while requires less capital, allowing the expansion of its credit activities. BS2's profitability during 2019 was pressured, operating profit/risk-weighted assets ratio stood at weak 0.16% as of 1H19 and 2.8% in 1H18. Weaker results in 2019 reflect the substantial investments and expenses derived from the development and launch - including marketing and staff - of BS2's digital platform.

Despite the modest results in 2019, Fitch expects that BS2's trend in results, observed during 2017 and 2018, will return in 2020, despite still slightly lower than in previous years given the upfront costs that are necessary in its digital effort.

BS2 continues to post good asset quality ratios, consolidated loan portfolio (which include receivables) classified as 'D-H' ratings reached 2.6% in June 2019, from to 2.3% at the end of 2018, while non-performing loans (NPLs) represented a low level of 0.7% of the total portfolio on both periods which is better than the average of its peers, benefited by the strong growth of the portfolio of receivables. Fitch notes that the maintenance of rapid loan growth pose some risks. At the same time, given the successive capital injections, 10 largest loan exposures to Core Equity Tier 1 (CET1) has considerably fell over the last two year, now representing 1.4x the CET1 , from 2.2x in June 2018 and 3.2x in June 2017.

BS2's capitalization ratios have remained adequate, even considering the strong growth of assets in recent years. Over the last 18-24 months, shareholders injected, through the holding, BRL245 million - last injection occurred in September 2019 and totaled BRL 100 million, to support the pace of growth of the bank's operations. In June 2019, the FCC ratio rose to 11.4% from 10.3% and 10.2% at the end of 2018 and 2017 - CET1 ratio of 11.2%, 9.6% and 9.5% respectively, while total regulatory capital reached 12.8% from 11.5% and 13.1%. Considering the last injection, CET1 and total regulatory would be close to adequate 12.5% and 14.6%, respectively. Although the capital injections increased BS2's capital position, its reported FCC and CET1 level are still below the average of other midsize banks.

The bank's funding profile has been focused on its institutional investors and later on brokerage agreements, which, in turn, distribute BS2's funding products to its retail customers through its own platforms. BS2 digital platform is another step towards funding diversification, which Fitch considers to have potential to become relevant in the medium term. Despite the greater diversification of investors, with granularity on the final end of the brokerage companies, BS2 still shows concentrations in specific dealers. Its liquidity remained strong and well above its short-term needs, cash totaled BRL1.1 billion in June 2019, covering high 1.9x of its funding with maturities of less than one year, BRL716 million and 0.9x in June 2018.

#### SUPPORT RATING AND SUPPORT RATING FLOOR

BS2's Support Rating of '5' and its Support Rating Floor of 'No Floor' were affirmed, reflecting the bank's low systemic importance. In Fitch's view, the bank is not likely to benefit from external support.

#### RATING SENSITIVITIES

##### IDRs, VR and NATIONAL RATINGS

Although unlikely in the short term, BS2's ratings could arise from the consolidation of its business model and a significant improvement in its franchise, together with the ability to maintain its risk appetite under control, while posting adequate and consistent financial metrics in the upcoming years. BS2's ratings could be downgraded if the bank does not achieve its operational breakeven point during 2020 and/or its FCC and/or CET1 ratios fall to a level below 10%.

#### SUPPORT RATING AND SUPPORT RATING FLOOR

A potential upgrade of BS2's Support Rating and Support Rating Floor is unlikely in the foreseeable future, since this would only arise from a material gain in the bank's systemic importance.

#### ESG Considerations

Unless otherwise disclosed in this section, the highest level of ESG credit relevance is a score of 3 - ESG issues are credit neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity.

For more information on Fitch's ESG Relevance Scores, visit [www.fitchratings.com/esg](http://www.fitchratings.com/esg).

### RATING ACTIONS

ENTITY/DEBT	RATING	PRIOR
Banco BS2 S.A.	LT IDR B+ ● Affirmed	B+ ●
	ST IDR B Affirmed	B
	LC LT IDR B+ ● Affirmed	B+ ●
	LC ST IDR B Affirmed	B
	Natl LT BBB+(bra) ● Upgrade	BBB(bra) +
	Natl ST F2(bra) Upgrade	F3(bra)
	Viability b+ Affirmed	b+
	Support 5 Affirmed	5
	Support Floor NF Affirmed	NF

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## Applicable Criteria

National Scale Ratings Criteria (pub. 18 Jul 2018)  
Bank Rating Criteria (pub. 12 Oct 2018)  
Short-Term Ratings Criteria (pub. 02 May 2019)

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