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CREDIT OPINION
13 September 2022

Update

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RATINGS

Banco de Reservas de la Republica Dominicana

Domicile	Santo Domingo, Dominican Republic
Long Term CRR	Ba3
Type	LT Counterparty Risk Rating - Fgn Curr
Outlook	Not Assigned
Long Term Debt	Not Assigned
Long Term Deposit	Ba3
Type	LT Bank Deposits - Fgn Curr
Outlook	Stable

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 Reservas de la Republica Dominicana

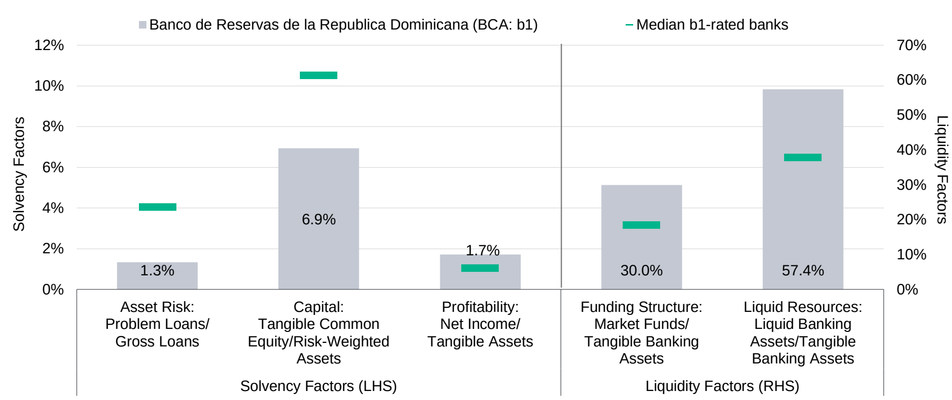
Update to credit analysis

Summary

Banco de Reservas de la Republica Dominicana (Banreservas) has a Baseline Credit Assessment (BCA) of b1, reflecting the bank's consistent track record of good asset quality and improved profitability metrics the bank has reported in the past two years. The BCA also reflects Banreservas' access to low-cost, granular retail deposits, supported by its franchise as the largest bank by assets in the Government of the Dominican Republic (DR, Ba3 stable), which enhances the bank's strong liquidity position. However, these credit strengths are counterbalanced by Banreserava's weak adjusted capital position as measured by Moody's.

Banreservas' Ba3 local- and foreign-currency deposit ratings are at the level of the DR's rating, and receive one notch of uplift from the bank's b1 BCA because of our assumption of full government support given the bank's 100% ownership by the DR' government . In addition, the assumption of government support reflects the close financial and business links between the two entities and the importance of the bank's deposit and lending franchise.

Exhibit 1
Rating Scorecard - Key financial ratios
Historical scorecard ratios as of June 2022



For the asset-risk ratio and profitability ratios, we review the latest three year-end ratios, as well as the most recent intra-year ratio, where applicable, and base our starting point ratio on the weaker of the average of this period and the latest reported figure. For the capital ratio, we use the latest reported figure. For the funding structure and liquid resources ratios, we use the latest year-end figures.
Source: Moody's Financial Metrics

Credit strengths

» Consistent track record of good asset quality

» Improved profitability on the back of lower loss provisioning, higher non-interest income and stable operating expenses

» Good base of stable low-cost deposit funding, supported by its franchise as the largest bank by assets in the Dominican Republic, and strong liquidity position that balances the short-term liability maturities

Credit challenges

» Rapid loan grow in recent quarters may pressure asset quality metrics

» Fastest funding re-pricing has led to a deterioration in interest margins

» Weak adjusted capital position as measured by Moody's

» The DR's operating environment for banks, as measured by its Macro Profile of Weak+

Outlook

The outlook on Banreservas' deposit ratings is stable, in line with the outlook on the DR's Ba3 government bond rating.

Factors that could lead to an upgrade

An upgrade in Banreservas´ standalone BCA would stem from a steady improvement in the bank's capital position, combined with sustainably superior asset quality fundamentals during the recovery of economic activity in the country. In addition, a strengthening in profitability metrics would also affect the bank's BCA positively. Finally, deposit ratings would go up depending on an upgrade of the DR´s sovereign rating.

Factors that could lead to a downgrade

The bank's BCA could be downgraded in case of consistent deterioration in asset risks and profitability that would have a negative impact to capitalization. Additionally, a significant increase in the transfers of earnings to the government would also affect the bank's capacity to replenish capital, factors that would have downward pressure on its BCA. A downgrade in the sovereign rating would result in a downgrade in Banreservas' deposit ratings.

Key indicators

Exhibit 2

Banco de Reservas de la Republica Dominicana (Consolidated Financials) [1]

	06-22[2]	12-21[2]	12-20[2]	12-19[2]	12-18[2]	CAGR/Avg.[3]
Total Assets (DOP Million)	1,026,072.0	914,640.9	717,013.1	570,493.7	505,388.5	22.4[4]
Total Assets (USD Million)	18,775.3	15,962.3	12,331.5	10,691.4	10,110.8	19.3[4]
Tangible Common Equity (DOP Million)	52,568.6	45,829.5	35,605.3	29,196.1	25,163.0	23.4[4]
Tangible Common Equity (USD Million)	961.9	799.8	612.4	547.2	503.4	20.3[4]
Problem Loans / Gross Loans (%)	0.8	1.2	1.9	1.4	1.5	1.4[5]
Tangible Common Equity / Risk Weighted Assets (%)	6.9	6.5	6.3	6.9	6.9	6.7[6]
Problem Loans / (Tangible Common Equity + Loan Loss Reserve) (%)	4.2	6.3	11.1	12.8	14.6	9.8[5]
Net Interest Margin (%)	4.9	6.5	6.6	6.7	6.7	6.3[5]
PPI / Average RWA (%)	4.0	5.4	4.9	3.9	3.4	4.3[6]
Net Income / Tangible Assets (%)	2.0	1.8	1.5	1.6	1.4	1.7[5]
Cost / Income Ratio (%)	66.8	56.8	62.7	68.9	71.3	65.3[5]
Market Funds / Tangible Banking Assets (%)	39.2	30.0	28.9	30.7	35.3	32.8[5]
Liquid Banking Assets / Tangible Banking Assets (%)	58.0	57.4	53.5	36.3	33.0	47.6[5]

Gross Loans / Due to Customers (%)	81.7	71.0	78.9	111.8	126.8	94.0[5]

[1] All figures and ratios are adjusted using Moody's standard adjustments. [2] Basel I; LOCAL GAAP. [3] May include rounding differences because of the scale of reported amounts. [4] Compound annual growth rate (%) based on the periods for the latest accounting regime. [5] Simple average of periods for the latest accounting regime. [6] Simple average of Basel I periods.
Sources: Moody's Investors Service and company filings

Profile

Banreservas is the DR's largest bank, accounting for about 40% of the banking system's assets. The bank offers a wide range of financial products, including loans, deposits, insurance, pension fund management and underwriting services. Banreservas mostly focuses on commercial and consumer lending. Commercial loans to the private sector comprised 50% of the bank's loan book as of June 2022, followed by consumer loans (27%), mortgages (14%) and loans to public entities (9%).

The bank is 100% controlled by the Dominican State, and it reported total assets of $18.8 billion as of June 2022.

Recent developments

The outlook on the Central American banking systems is stable, based on a continued strong economic recovery in the region and banks' resilient fundamentals. Economic activity in the region will largely benefit from US growth through remittances and tourism, which will support banks' asset quality and business growth. Commodity price shocks will increase inflationary pressures and FX volatility given that the region is a net commodity importer. This dynamic will weigh on borrowers' repayment capacity. Record-high reserve coverage will help absorb expected loan losses, while profitability will benefit from increasing interest rates and business volumes, supporting internal capital generation. Although largely core deposit funded, increased market volatility will likely increase costs of cross-border financing for banks in the region more than in other countries in Latin America.

The Dominican Republic's Government, the Central Bank and the Superintendency of Banks have implemented several measures that involve the banking system to address the economic impact of the pandemic, including a reduction of minimum reserve requirements for banks that lend to households and small companies at capped interest rates, forbearance for the recognition and provisioning of problem loans, interest rate reduction and introduction of liquidity lines for banks both in local and foreign currency.

Detailed credit considerations

Consistent track record of good asset quality, which may be affected by recent high loan growth

Banreservas has reported consistent track record of good asset quality in the past 12 months, despite relatively rapid loan growth and the lagging effects of the coronavirus pandemic. The bank reported low level of nonperforming loans (NPLs) at 0.8% of gross loans, lower than 1.6% reported as of June 2021, and down from 1.2% in December 2021. Loan loss reserves were strong at about 7.8x of NPLs as of June 2022, higher than 5.8x in December 2021 and 3.9x in June 2021. However, asset quality may deteriorate, evidenced by a recent increase in restructured loans as a % of gross loans, to 1.6% in June 2022, from 0.8% in December 2021.

Banreservas' asset quality metrics have improved since year end 2020. The end of government's loan restructuring measures to provide relief to households and commercial borrowers because of the coronavirus pandemic did not impact the asset quality of the bank. Banreservas has built prudential provisions against expected credit losses, with total loan loss reserves representing 6.3% of gross loans as of June 2022, in line with June 2021, and at 780% of problem loans.

In addition, asset risk may rise because of previous rapid growth in the inherently higher-risk consumer financing segment, coupled with still high borrower concentration in loans to the public and private sectors. Loans to consumers accounted for 27% of gross loans in June 2022, in line with the amount reported in June 2021. However, this came after loans to consumers grew 22% year-over-year as of June 2022. Also in June 2022, the NPL ratio for consumer loans was at a still-manageable level of 1.6%, yet higher than the metric for the overall portfolio. At the same time, the 20 largest loan exposures comprise about 1.1x the bank's tangible common equity (TCE) as of June 2022.

Banreservas loan dollarization, at 17.2% of total loans in June 2022, is lower than the system average of 23%, but it still exposes the bank to the risk of a sudden depreciation of the Dominican peso, considering that a large portion of these loans are granted to industries that in some cases do not generate hard currency.

Moody's-adjusted core capital ratio remains low

Banreservas' core capitalization remains weak when measured by our preferred TCE to risk-weighted assets (RWA) ratio, which was 6.9% as of June 2022. At this level, the TCE/RWA ratio provides limited loss absorption of unexpected credit or investment losses. We have a more conservative view on capital adequacy and adjust the TCE/RWA ratio by assigning a 100% weight for government securities.

Despite that, Banreservas' regulatory total capital ratio remained strong at 14.5% of risk-weighted assets in June 2022. The regulatory ratio benefits from non-tradable government bonds that the government has used to capitalize the bank in the past and a zero risk weight accorded to the bank's holdings of government securities and to loans to the public sector.

Banreservas has historically paid high levels of dividend payments, above 60% of net income in the period 2017-21, which is in line with Banreservas' organic law. The latter mandates that 35% of earnings must be retained, 15% must be used to repay the government's outstanding debt with the bank and 50% may be distributed as dividends after paying at least 5% of the National Treasury's outstanding bonds.

Profitability has increased on the back of lower loss provisioning, higher non-interest income and stable operating expenses

Banreservas reported improvements in profitability in June 2022 with net income to tangible assets increasing to 1.98%, compared to 1.8% in Q1 2022 and December 2021 and above the 1.90% in June 2021. While net interest income increased a shy 2% in June 2022 compared to the same period in 2021, earning generation was supported by a 63% fall loan loss provision and 37% increase in non-interest income, coupled with mild increase 5% increase in operating expenses in the same period, all helping to reduce the effect of higher interest expense.

The mild growth in net interest income was driven by a 25% increase in interest expense while interest income only grew 7% in the first half of 2022, compared with the same period in 2021. This has driven a deterioration in the net interest margin (NIM) which have decreased to 4.9% in June 2022 from the 6.5% reported a year earlier. This deterioration in the interest margin evidenced the fastest repricing of the bank's funding base as market rates increase, in contrast to its largely fixed-rate loanbook.

On the other hand, credit costs decreased in 2022 and the bank reported a 64% decrease in loan loss provisions in June 2022 from the previous year, reaching a low 1.0% of gross loans in 2Q 2022, which is below historic levels above 2%. In addition, Banreservas' fee income and other non-interest income has been rising gradually, 23% and 55% higher in June 2022 than a year earlier, respectively.

Flattish operating costs also supported Banreservas bottom line results. While DR inflation was at 9.5% in the 12-month trailing June 2022, operating expenses contracted 2.5% in the same period. Despite remaining high, operating costs improved to 4.5% of total assets in June 2022 from 5.6% reported a year earlier. Consequently, the reported deterioration in the cost to income ratio, to 67% from 58%, is largely explained by the decrease in core earnings generation rather than a spike in operating expenses.

The key risks to the bank's profitability include potentially rising credit costs amid a challenging operating environment characterized by higher inflation and interest rates. However, margins should strengthen as the bank manages to reprice its loans at a higher rate while it expands into the consumer sector, which would partly offset the increases in funding costs.

Stable low-cost deposit funding and good liquidity balance the short-term liability maturities

Because of its status as the largest bank in the country and its state ownership, Banreservas also benefits from ample access to low-cost deposits. The bank's reported market funds were at 39% of its total assets as of June 2022; however, if certificates of time deposits (valores en circulación) were deducted from market funds, the metric would have declined to 9%, indicating limited refinancing and repricing risks. The time certificates of deposits are reportedly equal to time deposits. The key difference is currency; certificates of time deposits are largely denominated in Dominican pesos, while time deposits are denominated in US dollars.

However, the deposit base is concentrated, with the top 20 deposits representing close to 33% of the total deposits in June 2022. In addition, the bank's funding structure is significantly skewed toward short-term maturities, reflected by the fact that approximately 49% of its total liabilities are due in less than 30 days. However, as of June 2022, 91% of total deposits comprised core deposits (demand deposits and savings accounts), which tend to be sticky, allowing for a better match of the longer-term loan book.

Liquidity remains thick and has recently improved in line with the growth of the deposit base and slower loan growth, with liquid banking assets representing 58% of tangible banking assets, chiefly constituting government securities and deposits at the central bank.

Banreservas' credit profile is influenced by the DR's Weak+ Macro Profile

The DR's Weak+ Macro Profile balances robust medium-term growth prospects and contained external and government liquidity risks with weak fiscal and institutional strength. The coronavirus pandemic caused a severe negative shock to the economy and to the government's fiscal and debt metrics. While the debt burden will remain lower than the Ba median, debt affordability is notably weaker. We expect revenue-enhancing measures to bolster this long-standing credit weakness.

After growing by 12.3% in 2021, in line with the country's potential growth rate. For 2022, we forecast real GDP growth of 5.0%, supported by strong recovery in tourism, construction and investment.

Notwithstanding that credit has grown in the last decade, financial intermediation remains low, at around 27% by the end of 2021. NPLs have remained relatively low as a percentage of gross loans, and we expect asset quality to remain stable as remittance inflows and tourism demand support economic growth and households' payment capacity, helping to offset macroeconomic pressures, including inflation.

ESG considerations

Banreservas' exposure to environmental risks is low, consistent with our general assessment for the global banking sector. See our environmental risk heat map for further information.

Overall, we view banks as facing moderate social risks. The most relevant social risks for banks arise from the way they interact with their customers. Social risks are particularly high in the area of data security and customer privacy, which is partly mitigated by sizable technology investments and banks' long track record of handling sensitive client data. Fines and reputational damage because of product mis-selling or other types of misconduct are further social risks. Social trends are also relevant in a number of areas, such as shifting customer preferences toward digital banking services increasing information technology costs, aging population concerns in several countries affecting demand for financial services or socially driven policy agendas translating into regulations that affect banks' revenue base. See our social heat map for further information.

Governance is highly relevant for Banreservas, as it is to all participants in the banking industry. Corporate governance weaknesses can lead to a deterioration in a bank's credit quality, while governance strengths can benefit its credit profile. Governance risks are largely internal rather than externally driven, and for Banreservas, we do not have any particular governance concerns. Nonetheless, corporate governance remains a key credit consideration and requires ongoing monitoring.

Support and structural considerations

Government support

The bank's local and foreign currency deposit ratings of Ba3 receive a one-notch uplift from the adjusted BCA of b1 reflecting our assessment that, as a government-backed bank, Banreservas receives full government support. Banreservas is 100% owned by the government of the DR. In addition, there are close financial and business links between the bank and the government. The full support is also based on the importance of Banreservas' deposit and lending franchise as the country's largest bank.

The B2 foreign-currency subordinated debt rating reflects a low probability of government support for the bank's subordinated debt because the purpose of this instrument is to absorb losses.

Counterparty Risk (CR) Assessment

Banreservas' CR Assessment is positioned at Ba3(cr)/NP(cr)

The CR Assessment is positioned one notch above the Adjusted BCA of b1 and, therefore, in line with the deposit rating, reflecting our view that its probability of default is in line with deposits. We believe senior obligations represented by the CR Assessment will be more likely preserved to limit contagion, minimize losses and avoid disruption of critical functions.

Counterparty Risk Ratings (CRRs)

Banreservas' CRRs are positioned at Ba3/NP

The CRR is positioned one notch above the Adjusted BCA of b1 and, therefore, in line with deposit ratings, reflecting our view that CRR liabilities have a the same probability of default than the bank's deposits.

Methodology and scorecard

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 Reservas de la Republica Dominicana

Macro Factors							
Weighted Macro Profile	**Weak +**	**100%**					
Factor		**Historic Ratio**	**Initial Score**	**Expected Trend**	**Assigned Score**	**Key driver #1**	**Key driver #2**
Solvency							
Asset Risk							
Problem Loans / Gross Loans		1.3%	baa3	↔	ba2	Single name concentration	Loan growth
Capital							
Tangible Common Equity / Risk Weighted Assets (Basel I)		6.9%	b3	↔	caa1	Capital fungibility	
Profitability							
Net Income / Tangible Assets		1.7%	ba1	↔	ba2		
Combined Solvency Score			ba3		b1		
Liquidity							
Funding Structure							
Market Funds / Tangible Banking Assets		30.0%	b1	↓↓	ba3	Deposit quality	Term structure
Liquid Resources							
Liquid Banking Assets / Tangible Banking Assets		57.4%	baa2	↔	ba2	Quality of liquid assets	
Combined Liquidity Score			ba2		ba3		
Financial Profile					b1		
Qualitative Adjustments					Adjustment		
Business Diversification					0		
Opacity and Complexity					0		
Corporate Behavior					0		
Total Qualitative Adjustments					0		
Sovereign or Affiliate constraint					Ba3		
BCA Scorecard-indicated Outcome - Range					ba3 - b2		
Assigned BCA					b1		
Affiliate Support notching					0		
Adjusted BCA					b1		

Instrument Class	**Loss Given Failure notching**	**Additional notching**	**Preliminary Rating Assessment**	**Government Support notching**	**Local Currency Rating**	**Foreign Currency Rating**
Counterparty Risk Rating	1	0	ba3	0	Ba3	Ba3
Counterparty Risk Assessment	1	0	ba3 (cr)	0	Ba3(cr)	
Deposits	0	0	b1	1	Ba3	Ba3
Dated subordinated bank debt	-1	0	b2	0		B2

[1] Where dashes are shown for a particular factor (or sub-factor), the score is based on non-public information.

Source: Moody's Investors Service

Ratings

Exhibit 4

Category	Moody's Rating
BANCO DE RESERVAS DE LA REPUBLICA DOMINICANA	
Outlook	Stable
Counterparty Risk Rating	Ba3/NP
Bank Deposits	Ba3/NP
Baseline Credit Assessment	b1
Adjusted Baseline Credit Assessment	b1
Counterparty Risk Assessment	Ba3(cr)/NP(cr)
Subordinate	B2

Source: Moody's Investors Service

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