MOODY'S
INVESTORS SERVICE

CREDIT OPINION
18 May 2016

Update

Rate this Research

RATINGS

Banco Paulista S.A.

Domicile	Sao Paulo, Sao Paulo, Brazil
Long Term Rating	B2
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.

Contacts

Alcir Freitas 5511-3043-7308
Senior Credit Officer
alcir.freitas@moodys.com

Farooq Khan 55-11-3043-6087
Analyst
farooq.khan@moodys.com

Aaron Freedman 52-55-1253-5713
Associate Managing Director
aaron.freedman@moodys.com

Banco Paulista S.A.

Update Following NSR Repositioning

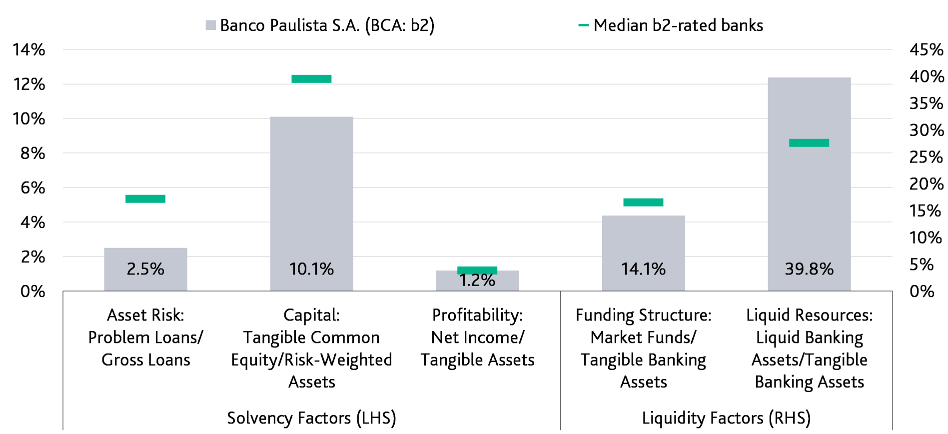
Summary Rating Rationale

Banco Paulista S.A.'s (Paulista) baseline credit assessment (BCA) of b2 is supported by its appropriate capital position, liquidity profile and profitability, while negatively weighted by asset risk and low business diversification. Moody's understands that Paulista's niche foreign exchange activity that is centered in the import of Brazilian Reais involves significant operational and compliance risks that are difficult to anticipate, therefore somewhat limiting the visibility on future earnings performance. These risks become particularly relevant in light of the relevant contribution of this segment to total revenues. Finally, revenue growth potential in this segment may be somewhat limited by Paulista's apparent sizeable market share in its core business.

The deposit and senior debt ratings of B2 derives from Paulista's BCA of b2, and does not benefit from government support uplift given Moody's assessment of low probability of support, based on the bank's modest market share in the domestic deposits.

On 9 May 2016, Moody's repositioned Paulista's long- and short-term Brazilian national scale deposit rating to Ba1.br and BR-4, from Baa3.br and BR-3, respectively, in conjunction with the recalibration of the Brazilian national rating scale. This action followed the publication of Moody's updated methodology "Mapping Moody's National Scale Ratings from Global Scale Ratings" on 9 May 2016.

Exhibit 1
Rating Scorecard - Key Financial Ratios



Source: Moody's Financial Metrics.

Credit Strengths

» Adequate capital position

» Liquidity supported by large amount of liquid assets and reduced loan leverage

Credit Challenges

» Asset risk impacted by relatively high operational risk in the Import of Brazilian Reais

» Foreign exchange business represents a relevant contribution to revenues

» Adequate profitability, but still highly concentrated on foreign exchange revenues

Rating Outlook

The outlook on all ratings is stable.

Factors that Could Lead to an Upgrade

Positive pressures on BCA would come from (1) improved business diversification; (2) enhanced asset risk, supported by lower exposure to FX business.

Factors that Could Lead to a Downgrade

Currently, there are limited negative pressures to its BCA, which could be driven by a large decline in capitalization and by its inability to sustain positive results.

Key Indicators

Exhibit 2

Banco Paulista S.A. (Unconsolidated Financials) [1]

	12-15[2]	12-14[2]	12-13[2]	12-12[3]	12-11[3]	Avg.
Total Assets (BRL billion)	2.2	1.7	1.4	1.4	1.4	12.6[4]
Total Assets (USD billion)	0.6	0.7	0.6	0.7	0.7	-6.7[4]
Tangible Common Equity (BRL billion)	0.1	0.1	0.1	0.1	0.0	57.2[4]
Tangible Common Equity (USD billion)	0.0	0.1	0.1	0.0	0.0	30.3[4]
Problem Loans / Gross Loans (%)	0.2	4.2	3.1	5.8	4.4	3.5[5]
Tangible Common Equity / Risk Weighted Assets (%)	10.1	13.5	15.3	8.2	3.2	13.0[6]
Problem Loans / (Tangible Common Equity + Loan Loss Reserve) (%)	0.4	6.4	5.2	14.1	31.1	11.5[5]
Net Interest Margin (%)	9.7	14.6	13.7	17.0	16.0	14.2[5]
PPI / Average RWA (%)	2.4	4.9	5.1	8.5	11.1	4.2[6]
Net Income / Tangible Assets (%)	1.2	2.0	1.5	2.3	1.0	1.6[5]
Cost / Income Ratio (%)	84.2	72.9	73.7	62.5	52.5	69.2[5]
Market Funds / Tangible Banking Assets (%)	14.1	14.0	20.8	46.4	41.7	27.4[5]
Liquid Banking Assets / Tangible Banking Assets (%)	39.8	40.3	46.1	51.1	50.5	45.5[5]
Gross loans / Due to customers (%)	45.0	39.0	44.2	39.0	62.5	45.9[5]

[1] All figures and ratios are adjusted using Moody's standard adjustments [2] Basel III - fully-loaded or transitional phase-in; LOCAL GAAP [3] Basel II; LOCAL GAAP [4] Compound Annual Growth Rate based on LOCAL GAAP reporting periods [5] LOCAL GAAP reporting periods have been used for average calculation [6] Basel III - fully-loaded or transitional phase-in & LOCAL GAAP reporting periods have been used for average calculation
Source: Moody's Financial Metrics

Detailed Rating Considerations

OPERATIONAL RISK REMAINS RELEVANT

We score asset risk as b3 which mainly reflects the significant operational and compliance risks arising from Paulista's niche foreign exchange activity that is centered in the import of Brazilian Reais. The bank is one of the few players in this business, holding a significant market share in the local market.

Paulista's loan book is focused on the corporate segment, which increased by almost 60% in the twelve months ended in December 2015. Although the recent growth may represent a risk given the adverse economic environment, the bank may have the ability to closely monitor customers' repayment capacity as 84% of total loan portfolio matures within 90 days.

Paulista's volatile delinquency derives from its relatively concentrated exposures. However, problem loan ratio (measured by past due loans under risk levels E to H as a percentage of total loans) fell sharply in December 2015 to 0.18%, from 4.19% in December 2014. At the same time, Paulista maintained conservative coverage level, with loan loss reserves to problem loans representing 1591% in 2015. At the same time, the outstanding volume of loans classified in the riskier categories - from E to H - have collectively represented 3.1% of total loans in December 2015 (8.5% in December 2014), which are 93% covered by loan loss reserves (92% in December 2014).

ADEQUATE CAPITALIZATION

We score capital as ba2, which reflects its current capital position, and also factors the capital allocation for the foreign exchange service activity, which follows the regulatory standardized approach to calculate operational risk, based on a percentage of historical revenues.

Tangible common equity to risk weighted assets declined to 10.0% in December 2015, from 13.5% in December 2014. Capital consumption was driven by a 37% year over year increase in risk-weighted assets, which in turn, derived from credit and market risk exposures. Therefore, of total capital requirement in December 2015, about 65% was related to credit risk, followed by operational risk (18%) and market risk (16%). Operational risk is mainly related to the foreign exchange business, and its importance increased due to the gradual implementation of regulatory capital requirement for this type of risk.

PROFITABILITY IMPACTED BY HIGHER FUNDING COSTS

We score profitability as ba3, which reflects the recent performance coupled with its high dependence on FX revenues.

Paulista's revenues grew by 29% in 2015 when compared to the same period of 2014 with FX revenues accounting for 60%, trading revenues for 42% and credit related revenues the remainder. We see that a relevant portion of FX revenues have a recurrent pattern, but it also carries some degree of earnings volatility, Paulista is one of the captive players in the foreign exchange segment, and is one of the few banks dealing in the Brazilian Reais import business.

The bank's profitability in 2015 was markedly lower however driven by higher costs of funding. On the other hand, lowering loan loss provisions and increased investment income were the key elements in sustaining Paulista's profitability. Fee revenues rose by 25% over 2014, mainly due to higher advisory, asset management, custody and banking service fees. As a result, in the fiscal year ended in December 2015, the bank reported net income of BRL 26 million versus BRL 34 million in the previous year, a decline of 25%.

LIQUID RESOURCES OFFSET FUNDING PROFILE

The ba2 combined liquidity score is positively weighted by the large amount of liquid assets, which partially offsets the high dependence on market funds.

Paulista's necessity to raise funds faces lower pressures given the somewhat reduced loan leverage, equivalent to 2.3x the shareholders' equity in December 2015. Also, we note that the bank carries a meaningful volume of liquid assets in its balance sheet, which according to our estimates covers over 60% of total funding. Therefore, current balance sheet structure provides more flexibility in liquidity management during periods of market squeeze. Deposits represent 56% of total funding, of which 17% matures within 3 months and another 19% in the following 9 months.

PAULISTA'S BCA IS SUPPORTED BY BRAZIL'S MODERATE MACRO PROFILE

Brazil's Moderate macro profile reflects the country's large and diversified economy, while the combination of ongoing economic recession, persistently high inflation and the difficult political scenario increases challenges to Brazilian banks' operating environment. The pace of loan growth has reduced significantly in the last year and tightening monetary policy allowed banks to raise lending rates, which has relieved part of the earnings pressure arising from asset risks. Public banks hold a 56% share of Brazil's loan market, which is reflected in the adjustment for industry structure. Capital and funding remain adequate, and exposure to international capital markets will remain low. External vulnerability is also limited by Brazil's sizeable international reserves, which reduce the country's sensitivity to external shocks, such as sudden stops in capital flows.

Notching Considerations

Government Support

We believe there is a low likelihood of government support for Paulista's rated deposits, which reflects its modest market share of deposits in Brazil.

Counterparty Risk Assessment

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.

Banco Paulista's CR Assessment is positioned at B1(cr) / Not-Prime (cr), which is one- notch above the bank's Adjusted BCA of b1, and, therefore, above the deposit rating of the bank, reflecting Moody's view that its probability of default is lower at the operating obligations than of deposits. The CR Assessment does not benefit from government support, as the government support is not incorporated in the bank's deposit ratings.

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 Paulista S.A.

Macro Factors						
Weighted Macro Profile	**Moderate**	**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	2.5%	baa2	↓↓	b3	Operational risk	Single name concentration
Capital						
TCE / RWA	10.1%	ba2	←→	ba2	Stress capital resilience	
Profitability						
Net Income / Tangible Assets	1.2%	baa3	←→	ba3	Earnings quality	
Combined Solvency Score		baa3		b1		
Liquidity						
Funding Structure						
Market Funds / Tangible Banking Assets	14.1%	baa2	←→	b2	Deposit quality	
Liquid Resources						
Liquid Banking Assets / Tangible Banking Assets	39.8%	baa1	←→	baa1	Expected trend	
Combined Liquidity Score		baa2		ba2		
Financial Profile				ba3		
Business Diversification				-2		
Opacity and Complexity				0		
Corporate Behavior				0		
Total Qualitative Adjustments				-2		
Sovereign or Affiliate constraint:				Ba2		
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)	0	B1 (cr)	--
Deposits	0	0	b2	0	B2	B2

Source: Moody's Financial Metrics

Ratings

Exhibit 4

Category	Moody's Rating
BANCO PAULISTA S.A.	
Outlook	Stable
Bank Deposits	B2/NP
NSR Bank Deposits	Ba1.br/BR-4
Baseline Credit Assessment	b2
Adjusted Baseline Credit Assessment	b2
Counterparty Risk Assessment	B1(cr)/NP(cr)

Source: Moody's Investors Service

REPORT NUMBER 1022947

Contacts

Alcir Freitas 5511-3043-7308
Senior Credit Officer
alcir.freitas@moodys.com

Aaron Freedman 52-55-1253-5713
Associate Managing Director
aaron.freedman@moodys.com

Rafael B Amaral 55-11-3043-6065
Associate Analyst
rafael.amaral@moodys.com

Farooq Khan 55-11-3043-6087
Analyst
farooq.khan@moodys.com

M. Celina Vansetti 212-553-4845
Managing Director - Banking
celina.vansetti-hutchins@moodys.com

CLIENT SERVICES

Americas	1-212-553-1653
Asia Pacific	852-3551-3077
Japan	81-3-5408-4100
EMEA	44-20-7772-5454

MOODY'S INVESTORS SERVICE