

## RATING ACTION COMMENTARY

# Fitch Affirms BRDE's IDRs at 'BB'; Outlook Stable

Fri 31 May, 2024 - 17:11 ET

Fitch Ratings - Rio de Janeiro - 31 May 2024: Fitch Ratings has affirmed Banco Regional de Desenvolvimento do Extremo Sul's (BRDE) Long-Term Local and Foreign Currency Issuer Default Ratings (IDRs) at 'BB' and Short-Term Local and Foreign Currency IDRs at 'B'. Fitch has also affirmed BRDE's National Long-Term Rating at 'AAA(bra)' with a Stable Rating Outlook and its National Short-Term Rating at 'F1+(bra)'. The Outlook for the IDRs is Stable.

## KEY RATING DRIVERS

**Government Support Drives Ratings:** BRDE's IDRs and National Ratings are based on Fitch's expectation of support from the bank's shareholders, the states of Parana, Santa Catarina and Rio Grande do Sul, if need it. This is reflected in the bank's Shareholder Support Rating (SSR) of 'bb', which is in line with Parana's 'BB'/Outlook Stable IDR. Fitch does not publicly rate Rio Grande do Sul and Santa Catarina. However, the combined creditworthiness of all three states strongly influences BRDE's ratings.

**High Support Propensity:** Fitch believes the shareholder's propensity to provide BRDE support if needed is high, reflecting the bank's policy role and importance as a development bank in southern Brazil. Fitch expects support will be unquestioned as BRDE by law is not allowed to pay dividends, which is a strong indicator of State support. Additionally, Fitch believes that the local regulator would likely provide support to BRDE if needed, due to the backing of its member states.

BRDE's relatively small size compared to the financial capacity of each of its state shareholders, coupled with their financial flexibility, high reputational linkages and level of operational integration between the bank and the three subnational entities, also influences the assessment.

**Strong Policy Role:** BRDE's policy role is primarily achieved through the provision of medium- and longer-term lending to corporates, small-and-medium sized enterprises, and domestic cooperatives. On behalf of Brazil's largest development bank (BNDES,

rated BB/Stable), BRDE manages the disbursement of long-term and subsidized lending to the agricultural sector, making it one of the largest lenders of BNDES funds.

**Environmental Disaster:** Although the bank operates in three states in the southern region of Brazil, about 33% of its portfolio is in the state of Rio Grande do Sul. The state recently experienced destructive heavy rains that caused floods that threatened important infrastructure in the region. Roads, communication networks, energy distribution, water supply logistics and health services, as well agribusiness were negatively affected. While it is difficult to determine the exact effects on the bank's financial standing, Fitch believes that the bank will benefit from support provided by the three state shareholders.

**No VR:** Fitch does not assign BRDE a Viability Rating, as its business model is largely determined by its policy role and its ratings are entirely determined by Fitch's assessment of the support the bank would receive from the the states of Parana, Santa Catarina and Rio Grande do Sul.

**Financial Performance; Moderate Influence on Ratings:** Historically, BRDE has shown better asset quality than its peers, thanks to its cautious approach to risk, a focus on the robust agricultural sector, and a high level of secured loans. Fitch believes the bank's ability to generate profits will be somewhat affected by the extent of its financial exposures in the flood-affected area of Rio Grande do Sul State. This is expected to impact the bank's interest income as the need for credit provisions, and consequently expenses, may rise. However, it is not yet possible to determine the potential effects on the bank's performance indicators.

**Solid Capitalization and Gradual Funding Diversification:** Fitch believes BRDE is of high strategic importance to its three shareholder governments, given its role as the states' financial arm, and the support would receive if needed. The three states have supported BRDE's capitalization when needed in the past. In Fitch's view, the three states remain committed to maintaining the bank's ample capital buffers.

BRDE's regulatory Common Equity Tier 1 capital ratio was 21.2% at YE 2023, well above the minimum regulatory requirements. BRDE's primary funding source remains concentrated on BNDES, accounting for 45.8% of total funding at YE 2023. However, BRDE's efforts to further diversify its funding sources has helped to reduce concentration from previous years. During 2023, the bank had a record amount of contracts with external sources, BRL 1.3 billion; an increase of 180.4% compared to 2022. These sources corresponded to 22.1% of the total contracted operations.

## **RATING SENSITIVITIES**

## **Factors that Could, Individually or Collectively, Lead to Negative Rating Action/Downgrade**

NATIONAL RATINGS and SSR

--Since BRDE's ratings are driven by the SSR, they can be downgraded if one or more of its shareholders are also downgraded;

--There may also be a downgrade if there are changes in the propensity of the controlling states to support BRDE;

--A deterioration of Fitch's view of the creditworthiness of BRDE's three shareholders;

--A deterioration of Fitch's view of the three shareholders propensity to support BRDE.

## **Factors that Could, Individually or Collectively, Lead to Positive Rating Action/Upgrade**

IDRs, NATIONAL RATINGS and SSR

--An upgrade of BRDE's ratings would depend on the improvement of the parents' ability and propensity to provide support;

--An improvement of Fitch's view of the creditworthiness of the three shareholders states;

--An improvement of Fitch's view of the three shareholder state's propensity to support BRDE;

--The National Scale rating cannot be upgraded as it is at the maximum level of the scale.

## **REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING**

The principal sources of information used in the analysis are described in the Applicable Criteria.

## **PUBLIC RATINGS WITH CREDIT LINKAGE TO OTHER RATINGS**

The banks ratings are driven by the support from the shareholders Paraná State, Rio Grande do Sul State and Santa Catarina State

## **ESG CONSIDERATIONS**

The highest level of ESG credit relevance is a score of '3', unless otherwise disclosed in this section. A score of '3' means 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. Fitch's ESG Relevance Scores are not inputs in the rating process; they are an observation on the relevance and materiality of ESG factors in the rating decision. For more information on Fitch's ESG Relevance Scores, visit <https://www.fitchratings.com/topics/esg/products#esg-relevance-scores>.

## RATING ACTIONS

ENTITY / DEBT ↕	RATING ↕			PRIOR ↕
Banco Regional de Desenvolvimento do Extremo Sul (BRDE)	LT IDR	BB Rating Outlook Stable		BB Rating Outlook Stable
		Affirmed		
	ST IDR	B	Affirmed	B
	LC LT IDR	BB Rating Outlook Stable		BB Rating Outlook Stable
		Affirmed		
	LC ST IDR	B	Affirmed	B
	Natl LT	AAA(bra) Rating Outlook Stable		AAA(bra) Rating Outlook Stable
	Affirmed			
Natl ST	F1+(bra)	Affirmed	F1+(bra)	
Shareholder Support	bb	Affirmed	bb	

[VIEW ADDITIONAL RATING DETAILS](#)

## **FITCH RATINGS ANALYSTS**

### **Ana Carolina Baronto**

Senior Analyst

Primary Rating Analyst

+55 21 4503 2618

anacarolina.baronto@fitchratings.com

Fitch Ratings Brasil Ltda.

Av. Barão de Tefé, 27 – Sala 601 Saúde Rio de Janeiro, RJ 20220-460

### **Raphael Nascimento**

Director

Secondary Rating Analyst

+55 11 3957 3680

raphael.nascimento@fitchratings.com

### **Alejandro Tapia**

Senior Director

Committee Chairperson

+52 81 4161 7056

alejandro.tapia@fitchratings.com

## **MEDIA CONTACTS**

### **Elizabeth Fogerty**

New York

+1 212 908 0526

elizabeth.fogerty@thefitchgroup.com

Additional information is available on [www.fitchratings.com](http://www.fitchratings.com)

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## **APPLICABLE CRITERIA**

[National Scale Rating Criteria \(pub. 22 Dec 2020\)](#)

[Bank Rating Criteria \(pub. 15 Mar 2024\) \(including rating assumption sensitivity\)](#)

## ADDITIONAL DISCLOSURES

[Dodd-Frank Rating Information Disclosure Form](#)

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Banco Regional de Desenvolvimento do Extremo Sul (BRDE)

EU Endorsed, UK Endorsed



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