

# MOODY'S

## INVESTORS SERVICE

### Credit Opinion: Deutsche Bank Mexico, S.A.

Global Credit Research - 11 Jun 2015

Mexico, Mexico

#### Ratings

| Category                            | Moody's Rating |
|-------------------------------------|----------------|
| Outlook                             | Stable         |
| Bank Deposits                       | Baa3/P-3       |
| NSR Bank Deposits                   | Aa2.mx/MX-1    |
| Baseline Credit Assessment          | ba2            |
| Adjusted Baseline Credit Assessment | baa3           |

#### Contacts

| Analyst                          | Phone           |
|----------------------------------|-----------------|
| David Olivares Villagomez/Mexico | 52.55.1253.5700 |
| Felipe Carvallo/Mexico           |                 |
| M. Celina Vansetti/New York City | 1.212.553.1653  |
| Vicente Gomez/Mexico             | 52.55.1253.5700 |

#### Key Indicators

##### Deutsche Bank Mexico, S.A. (Unconsolidated Financials)[1]

|  | [2]3-15  | [2]12-14 | [2]12-13 | [3]12-12  | [3]12-11  | Avg.     |
|--|----------|----------|----------|-----------|-----------|----------|
| Total Assets (MXN million)                                       | 47,957.0 | 45,963.0 | 57,999.0 | 226,254.4 | 198,770.9 | [4]-29.9 |
| Total Assets (USD million)                                       | 3,148.0  | 3,118.3  | 4,428.4  | 17,423.0  | 14,243.3  | [4]-31.4 |
| Tangible Common Equity (MXN million)                             | 3,364.0  | 3,349.0  | 3,084.6  | 2,572.4   | 2,396.0   | [4]8.9   |
| Tangible Common Equity (USD million)                             | 220.8    | 227.2    | 235.5    | 198.1     | 171.7     | [4]6.5   |
| Problem Loans / Gross Loans (%)                                  | –        | –        | –        | 0.0       | 0.0       | [5]0.0   |
| Tangible Common Equity / Risk Weighted Assets (%)                | 12.2     | 12.8     | 13.8     | 20.0      | 11.7      | [6]12.9  |
| Problem Loans / (Tangible Common Equity + Loan Loss Reserve) (%) | 0.0      | –        | 0.0      | 0.0       | 0.0       | [5]0.0   |
| Net Interest Margin (%)  | 0.2      | 0.0      | 0.1      | 0.0       | 0.3       | [5]0.1   |
| PPI / Average RWA (%)  | 0.2      | 2.0      | 4.6      | 0.6       | 1.6       | [6]2.3   |
| Net Income / Tangible Assets (%)                                 | 0.1      | 0.6      | 0.9      | 0.0       | 0.1       | [5]0.3   |
| Cost / Income Ratio (%)  | 90.1     | 56.3     | 45.4     | 82.9      | 60.8      | [5]67.1  |
| Market Funds / Tangible Banking Assets (%)                       | 74.1     | 80.6     | 26.3     | 83.9      | 81.2      | [5]69.2  |
| Liquid Banking Assets / Tangible Banking Assets (%)              | 20.4     | 32.1     | 14.3     | 1.6       | 10.5      | [5]15.8  |
| Gross Loans / Total Deposits (%)                                 | 0.0      | –        | –        | 13.7      | 20.3      | [5]11.3  |

Source: Moody's

[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

#### Opinion

#### SUMMARY RATING RATIONALE

We assign a Baa3 long-term global local currency (GLC) deposit rating to Deutsche Bank México, S.A. (DB México), a small wholesale investment bank. This rating is based on the bank's ba2 baseline credit assessment (BCA), and incorporates two-notches of uplift from affiliate support based on our assessment of a high likelihood of extraordinary support in case of stress from its German parent Deutsche Bank AG (Deutsche, rated baa3, Pos(m)). Furthermore, following the introduction of the new bank rating methodology in March 2015, on 5 June Moody's assigned a Counterparty Risk Assessment (CR Assessment) of Baa2(cr) and Prime-2(cr) to DB México.

DB México's ratings, and specifically the BCA of ba2, reflect the bank's niche wholesale and investment banking operations (e.g., mono-line), with a narrow focus on wholesale banking and market risk driven operations. While the bank undertakes little or no proprietary trading at all, and consequently is not exposed to significant market risk, its business is less stable than traditional retail and commercial banking, which therefore constrains the bank's intrinsic strength.

DB México is highly dependent on its parent company to drive business and for operational support. In addition, the bank's parent retains a significant portion of the assets and profits generated by the Mexican subsidiary on its own books, which benefits the subsidiary's reported capitalization levels and asset risk indicators. This high level of integration with its parent company results in a modest standalone franchise. Therefore, DB México's Baa3 deposit ratings not only incorporates its standalone creditworthiness but also an expectation of a high probability of support from its parent in case of extraordinary need, which provides two notches of ratings uplift from the BCA of ba2.

#### **DB MÉXICO'S RATING IS SUPPORTED BY ITS MACRO PROFILE OF STRONG -**

While recent reforms have not yet begun to provide the expected benefits, Mexico's stable economic outlook and credit conditions provide a supportive operating environment for DB Mexico. The country has a well-diversified economy, limited susceptibility to event risk, and a predictable policy framework, and is not expected to be significantly affected by the recent drop in the price of oil. Mexico's moderate institutional strength balances a track record of sound economic policy weighed down by a relatively weak rule of law that has historically restricted loan growth. However, financial intermediation should gradually gain traction as Mexico's economy benefits from a series of recent structural reforms in key sectors including energy, telecommunications and financial services.

#### **Rating Drivers**

Limited- scope wholesale banking franchise

Wholesale banking orientation derives in less predictable revenues

Well capitalized operation, risk transfer to affiliates and integration to parent group

#### **Rating Outlook**

The outlook on DB México's ratings is stable.

#### **What Could Change the Rating - Up**

The banks' ratings are only likely to change if and when their parents' ratings change.

#### **What Could Change the Rating - Down**

The banks' ratings are only likely to change if and when their parents' ratings change.

#### **DETAILED RATING CONSIDERATIONS**

##### **LIMITED-SCOPE WHOLESAL BANKING FRANCHISE**

DB México exhibits a limited-scope business model centered on trading and wholesale banking, particularly fixed income, derivatives trading and hedging activities, equity trading, and trust and advisory services. This justifies the qualitative adjustment of -1 for low business diversification, in the scorecard.

##### **WHOLESAL BANKING OPERATION DERIVES IN LESS PREDICTABLE REVENUES**

Relative to more diversified commercial bank operations, DB Mexico's core earnings are less predictable, reflecting the inherent volatility of its wholesale business model. These considerations drive the scores of a3 and b3 in asset risk and profitability, respectively, in the scorecard.

## WELL CAPITALIZED OPERATION, RISK TRANSFER TO AFFILIATES AND INTEGRATION TO PARENT GROUP

Risk positioning at the Mexican subsidiary reflects its parent's risk appetite and practices, including the maintenance of a comfortable liquidity position, which is fully aligned to the parent's policies, as well as very comfortable capitalization. In this light, DB Mexico exhibits a good capitalization and a low risk profile because a significant portion of the risks related to its principal trading and investment banking activities are transferred to other entities of the Deutsche Bank group. Risk sharing with other entities of the Deutsche group is also reflected in financial metrics at the Mexican subsidiary level that do not necessarily reflect all the risks and business volume generated by the Mexican operation.

DB México's is highly integrated to other entities of Deutsche Bank resembling more a branch operation than a subsidiary. Effectively, there is a high level of integration with the parent bank in terms of strategy, controls, liquidity management, risk appetite and capitalization. This constrains DB Mexico's standalone strength.

### Notching Considerations

#### Affiliate Support

DB Mexico's Baa3 local currency rating incorporates two-notches of uplift from the bank's standalone ba2 BCA solely from parental support assumptions. We believe there is a good probability of parent support to the Mexican subsidiary if need be.

#### Government Support

DB México exhibits a modest systemic relevance; as a result, its ratings do not benefit from any uplift due to systemic support considerations.

#### Counterparty Risk Assessments

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.

The CR Assessment assigned to DB Mexico is positioned at Baa2(cr).

The CR Assessment is positioned one notch above the Adjusted BCA of baa3 and therefore above senior unsecured and deposit ratings, reflecting our view that its probability of default is lower than that of senior unsecured debt and deposits. We believe senior obligations represented by the CRA will be more likely preserved in order to limit contagion, minimize losses and avoid disruption of critical functions. No government support is considered for Deutsche CR Assessment.

#### 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 Factors

### Deutsche Bank Mexico, S.A.

|                        |          |
|------------------------|----------|
| Macro Factors          |          |
| Weighted Macro Profile | Strong - |

| Financial Profile                                      |                |                      |              |                |                                   |                         |
|--|----------------|----------------------|--------------|----------------|-----------------------------------|-------------------------|
| Factor   | Historic Ratio | Macro Adjusted Score | Credit Trend | Assigned Score | Key driver #1                     | Key driver #2           |
| <b>Solvency</b>  |                |                      |              |                |                                   |                         |
| <b>Asset Risk</b>                                      |                |                      |              |                |                                   |                         |
| <i>Problem Loans / Gross Loans</i>                     | 0.0%           | aa3                  | ← →          | a3             | Market risk                       | Non lending credit risk |
| <b>Capital</b>   |                |                      |              |                |                                   |                         |
| <i>TCE / RWA</i>                                       | 12.2%          | baa2                 | ← →          | baa2           | Access to capital                 |                         |
| <b>Profitability</b>                                   |                |                      |              |                |                                   |                         |
| <i>Net Income / Tangible Assets</i>                    | 0.1%           | b2                   | ← →          | b3             | Earnings quality                  |                         |
| <b>Combined Solvency Score</b>                         |                | baa1                 |              | baa3           |                                   |                         |
| <b>Liquidity</b>                                       |                |                      |              |                |                                   |                         |
| <b>Funding Structure</b>                               |                |                      |              |                |                                   |                         |
| <i>Market Funds / Tangible Banking Assets</i>          | 80.6%          | caa3                 | ← →          | caa3           | Extent of market funding reliance |                         |
| <b>Liquid Resources</b>                                |                |                      |              |                |                                   |                         |
| <i>Liquid Banking Assets / Tangible Banking Assets</i> | 32.1%          | a3                   | ← →          | a3             | Intragroup restrictions           |                         |
| <b>Combined Liquidity Score</b>                        |                | b1                   |              | b1             |                                   |                         |

|                                   |            |
|-----------------------------------|------------|
| Financial Profile                 | ba1        |
| Qualitative Adjustments           | Adjustment |
| Business Diversification          | -1         |
| Opacity and Complexity            | 0          |
| Corporate Behavior                | 0          |
| Total Qualitative Adjustments     | -1         |
| Sovereign or Affiliate constraint | A3         |
| Scorecard Calculated BCA range    | ba1 - ba3  |
| Assigned BCA                      | ba2        |
| Affiliate Support notching        | 2          |
| Adjusted BCA                      | baa3       |

| Instrument Class | Loss Given Failure notching | Additional notching | Preliminary Rating Assessment | Government Support notching | Local Currency rating | Foreign Currency rating |
|------------------|-----------------------------|---------------------|-------------------------------|-----------------------------|-----------------------|-------------------------|
| Deposits         | 0                           | 0                   | baa3                          | 0                           | Baa3                  | Baa3                    |

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