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Research Update:

Banco Monex S.A. Rated Global Scale 'BB+/B', National Scale 'mxA+/mxA-1' Rating Affirmed

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Overview

- Mexico-based niche bank Banco Monex's operations and revenues are concentrated in its foreign exchange business segment.
- The bank's credit loss experience has been adequate due to a well collateralized loan portfolio coupled with adequate risk-adjusted capital.
- We are assigning our 'BB+/B' global scale issuer credit ratings and affirming the 'mxA+/mxA-1' national scale ratings on the bank.
- We expect Banco Monex to maintain its current business and risk positions, without major deviations from our current expectations, and a forecasted risk-adjusted capital ratio in the 9.75%-10.25% range.

Rating Action

On May 17, 2012, Standard & Poor's Ratings Services assigned its 'BB+/B' global scale issuer credit ratings to Banco Monex S.A. At the same time, we affirmed the 'mxA+/mxA-1' Mexican national scale ratings on the bank. The outlook is stable.

Rationale

The ratings on Banco Monex reflect its "moderate" business position, "adequate" capital and earnings and risk position, as well as our assessment of "below average" funding and "adequate" liquidity (as our criteria defines these terms). The bank's stand-alone credit profile is 'bb+'.

Our bank criteria use our Banking Industry Country Risk Assessment (BICRA) economic and industry risk scores to determine a bank's anchor, the starting point in assigning an issuer credit rating. Our anchor for a commercial bank operating only in Mexico is 'bbb'. In our view, the main risk for banks operating in Mexico is economic risk. This results from the population's low income level (from a global perspective) and the decrease in payment capacity amid a low level of domestic savings. Mexico's banks also face challenges associated with lending within a legal framework that is still establishing a track record of creditor rights. However, underwriting standards have improved. Also, we don't see any asset bubbles in the Mexican economy. Industry risk is not as high, because of conservative regulation, but supervision still needs to be strengthened. Healthy competitive dynamics drive the lending system. Funding is based on stable deposits, while the domestic debt markets are expanding rapidly. We classify the Mexican government as "supportive" to its banking system based on past experience and our belief that it has the capacity to help banks withstand problems.

Our assessment of Banco Monex's "moderate" business position is based on our view of concentrated business activities, which could harm the bank's business position due to lesser business stability compared with more diversified banks. Banco Monex mainly operates in the FX third-party transactions, which accounts for a significant part of its business operations. Despite enjoying a prominent leading position in this segment (market share in terms of total traded volume within the private sector of 17.2% at the end of 2011), we believe that any negative impact in the FX business line, stemming from lower traded volumes or lower spreads, could hurt its business and revenue generation. As opposed to other larger, more diversified banks, Banco Monex's revenues are highly concentrated, with more than 80% of the total from the FX segment. Despite its efforts to expand its credit operations, these represented only 11.8% of its total assets as of March 2012, and the bank's market share in terms of loans is just 0.2% of the total banking system. Given its long track record and experience in the FX business, we do not anticipate any significant business diversification in the next 12 to 18 months.

We view capital and earnings to be "adequate" due to our risk-adjusted capital (RAC) ratio forecast of 9.75%-10.25% during the next 12 to 18 months. Given that our forecasted RAC is on the borderline between "adequate" and "strong" capital assessments, the bank's moderate quality of earnings, stemming from its high revenue concentration in one segment, weakens our overall score to "adequate." In addition, expected double leverage at its parent could add pressures to the bank's quality of capital, if Holding Monex acquires more-than-expected debt. However, its earnings capacity is strong, with earnings buffer of 4.75% for our three-year average estimation, which compares well with larger regional banks. Our forecasted RAC takes into consideration a 30% average loan portfolio growth for the next two years and a reduced exposure to the Mexican Stock Exchange equity by selling all its position, which would translate into nil market risk weighted assets growth, and a 40% dividend payout to service its holding debt payment by upstreaming dividends during the next three years.

A well collateralized loan portfolio with credit losses below the industry's average supports our overall assessment of an "adequate" risk position, despite its loan portfolio concentration (top 20 exposures represented 53% of its total loan portfolio). We also consider that all relevant risks are not fully covered by our RAC framework, given that operating risks associated with its FX operations are not fully contemplated. Nevertheless, in our view, the bank does not carry out complex operations or offer products aiming for higher risk returns, and its future loan portfolio growth will be in sectors and segments already familiar to the bank risk management unit, such as small and medium enterprises and mortgage loans. Its credit losses during the past three years compared well within the Mexican banking industry's, at 1.7%. We believe that the bank's adequate collaterals, through high quality guarantees and credit insurance, have supported its low credit losses and loan portfolio concentration, and we expect this to remain so.

Banco Monex's funding structure is, in our view, "below average" compared to the system. This opinion stems from the low share of retail deposits in its funding structure, which at March 2012 accounted for about 30% of the total core customer deposit base. We view nonretail deposits as less stable and more sensitive to the competitors' interest rates, which makes Banco Monex more vulnerable. We continue to believe that achieving a higher share of retail deposits in its funding structure will remain a key challenge. Nevertheless, the bank's total net loans-to-deposits is healthy, at an average of 69.7% for the past three years. Based on our growth expectations, we expect this ratio to remain quite below 100% during the next two years. Also, as a result of high competition for deposits in Mexico, we do not expect the share of retail deposits to increase significantly.

Liquidity is "adequate" and reflects that cash on hand (deducting restricted liquidity due to the central bank's monetary restrictions plus restricted cash necessary to cover for its FX business operations) plus liquid securities (trading ones only and not public equity also deducting restricted securities) represented 1.1x of its core customer deposits and 41.3% of its total funding base as of December 2011. However, we do believe that the bank would not be able to survive in a stressful condition without access to other funding means, such as the central bank or other liquidity sources.

Outlook

The outlook is stable. The outlook reflects our view that Banco Monex will maintain its current business and risk positions without major deviations from our current expectations. It also reflects our RAC forecast in the 9.75%-10.25% range; including our view that quality of earnings will remain moderate as a consequence of its high revenue concentration in the FX business, which we estimate will account for more than 80% of the total. We take into consideration a 40% dividend payout in order to service the debt at the holding level.

A positive rating action would stem from a significant forecasted RAC improvement, consistently above 10%; if the bank is able to accrete more capital than we currently expect; and if revenues are less concentrated in the FX business (accounting for less than 75%). On the other hand, if there is a significant deterioration in the bank's risk position, due to aggressive growth in other business lines that could hamper its good credit loss experience, or if there are acquisitions that alter importantly its current risk exposures, a negative rating action could occur.

Ratings Score Snapshot

Issuer Credit Rating	BB+/Stable/B
SACP	bb+
Anchor	bbb
Business Position	Moderate (-1)

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   Capital and Earnings       Adequate (0)
   Risk Position              Adequate (0)
   Funding and Liquidity      Below Average and Adequate (-1)

Support                       0
   GRE Support                0
   Group Support              0
   Sovereign Support          0

Additional Factors            0
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Related Criteria And Research

- Banks: Rating Methodology And Assumptions, Nov. 9, 2011
- Group Rating Methodology And Assumptions, Nov. 9, 2011
- Banking Industry Country Risk Assessment Methodology And Assumptions, Nov. 9, 2011

Ratings List

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Ratings Assigned

Banco Monex S.A.
  Issuer credit rating
   Global scale                     BB+/Stable/B

Ratings Affirmed

Banco Monex S.A.
  Issuer credit rating
   National scale                   mxA+/Stable/mxA-1
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