

December 14, 2007

Research Update:

Banco BAC San Jose S.A. 'BB/B' Rating Affirmed; Outlook Stable

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Rationale

On Dec. 14, 2007, Standard & Poor's Rating Services affirmed its 'BB/B' foreign currency and its 'BB+/B' local currency counterparty credit ratings on Banco BAC San Jose S.A. (BAC San Jose) The outlook is stable.

The ratings on Costa Rica-based BAC San Jose reflect the dollarized balance sheet and expanding lending activities in a small, nondiversified economy and the challenges imposed by a market where commercial public banks have a 50% penetration. The ratings are supported by good financial performance, low delinquency levels, and the benefits from the ownership by one of the most important financial institutions in Central America, BAC International Bank Inc. (BIB; BBB/Stable/A-2).

Despite the loan portfolio's good performance, BAC San Jose is highly exposed to foreign exchange movements because approximately 50% of its loan portfolio is dollar denominated, and it is not all related to net dollar generators. Although dollar exposure is gradually decreasing, given the operating dynamics of the country and competition, we do not expect a significant reduction in the medium term.

The banking system dynamics, where public banks have a very important market share, impose challenges, such as operating margin pressures and the small likelihood of gaining more importance within the banking system, which is limited by the large market share of public banks.

The bank displays good financial metrics with an ROA averaging more than 3% for the past four years, which compares well with other rated banks in the region. The latter has been achieved thanks to BAC San Jose's business mix and relatively low funding costs. Given the bank's increasing focus on retail loans, we anticipate profitability ratios to remain at least at current levels, although competition from large public banks and global banks entering the system might add pressure to interest margins. Thanks to tight risk management, NPL ratios have barely exceeded 1% during the past four years, and reserve coverage has been maintained at 1.5x for the same period. As the bank has started to penetrate the retail segment, we anticipate its overall asset quality to deteriorate slightly, but at manageable levels and according to its current rating category.

The ownership of BIB and Credomatic International Corp. (BBB/Stable/A-2) provides BAC San Jose access to a common brand and regional presence, increasing its position in the growing retail sector in Costa Rica, mainly in the high-end mortgage loans and credit cards segments. This is a definite competitive advantage, given the increasing and tougher competition in Central America. We expect BAC San Jose to continue benefiting from its current ownership structure.

Outlook

The stable outlook reflects BAC San Jose's commercial position in Costa Rica and its adequate financial profile, which place it in a satisfactory position to take advantage of economic growth in the country. All things being equal, a positive rating action on the sovereign foreign currency rating will prompt a similar action on the foreign currency rating on the bank. However, a change in the sovereign local currency rating would not necessarily prompt a similar action on the local currency rating on BAC San Jose. On the contrary, if the bank's performance deteriorates or if there is a negative rating action on the sovereign ratings on the Republic of Costa Rica, the rating on the bank could be pressured.

Ratings List

Ratings Affirmed

Banco BAC San Jose, S.A.

Counterparty Credit Rating

Foreign Currency BB/Stable/B

Local Currency BB+/Stable/B

Certificate Of Deposit

Foreign Currency BB

Local Currency BB+

BAC Bahamas Bank

Counterparty Credit Rating

Foreign Currency BB/Stable/B

Certificate Of Deposit

Foreign Currency BB

BAC International Bank Inc.

Counterparty Credit Rating BBB/Stable/A-2

Certificate Of Deposit BBB/A-2

Credomatic International Corp.

Counterparty Credit Rating BBB/Stable/A-2

Certificate Of Deposit BBB

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