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Summary: Banco BAC San Jose, S.A.

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Rationale

The ratings on Banco BAC San José S.A. (previously named Banco de San José) reflect the bank's good financial profile, the benefits from its ownership by the largest Central American credit card issuer, Credomatic International Corp. (CIC; BBB-/Stable/A-3), and its increasing position in the growing retail sector in Costa Rica. The ratings on BAC San José are partially offset by the small and nondiversified Costa Rican economy and the risks inherent to a highly dollarized balance sheet.

BAC San José has exhibited high profitability in recent years with ROAs of more than 2.5% thanks to its business mix and decreasing funding costs. In addition to being profitable, asset quality has been stable as nonperforming assets have been low, thanks to a diversified loan portfolio with no significant concentrations by industry, economic group, or individual exposures, which is unusual for a bank operating in a small market. The ownership of CIC gives BAC San José access to a common brand and regional presence. In addition, BAC San José's increasing participation in cash management services has provided an edge in the market, as this participation, along with its credit card business, allows the bank to generate a significant amount of fee income. In Standard & Poor's Ratings Services' view, profitability is expected to slightly decrease in 2005 at the expense of stronger liquidity management policies, but overall should remain at adequate levels.

While Costa Rica's economic performance has been adequate in the past, it is currently decelerating, is very small, concentrated in a few economic sectors, and highly dollarized, although formally, transactions are performed in local currency. Over time, BAC San José's commercial loan book has gained share, making overall loan performance more dependant on local economic conditions. Additionally, given that dollar loans are preferred to loans in colones, BAC San José has historically maintained a high foreign-currency mismatch, as a portion of its dollar-borrower clients are not net-dollar generators. While the bank protects itself with strict credit policies and expects the guarantees to cover the effect of an abrupt devaluation, we still believe that the risks of this portfolio are higher.

In August 2004, BAC San José suffered a deposit run precipitated by false rumors in the market, and was able to

successfully surpass this event, satisfying payment of depositors' monies in full. Although the liquidity contingency plan was overrun by reality, everything worked well along with support from authorities, and as of October 2004, BAC San José had already recovered the deposits that were withdrawn during the deposit run.

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Outlook

The negative outlook mirrors the outlook on the sovereign ratings assigned to Costa Rica. All things being equal, a rating or outlook change on the sovereign would prompt a similar change on the ratings or outlook on the bank.

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