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Corporacion Financiera de Desarrollo S.A.

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Corporacion Financiera de Desarrollo S.A.

SACP	bbb		+	Support	0	+	Additional Factors	0
Anchor	bbb-			ALAC Support	0		Issuer Credit Rating <div style="background-color: yellow; padding: 10px; text-align: center;"> BBB+ / Stable / A-2 </div>	
Business Position	Adequate	0		GRE Support	+1			
Capital and Earnings	Adequate	0		Group Support	0			
Risk Position	Strong	+1		Sovereign Support	0			
Funding	Average	0						
Liquidity	Adequate							

Major Rating Factors

Strengths:	Weaknesses:
<ul style="list-style-type: none"> • High likelihood of support from its majority shareholder, the Republic of Peru; • Operates in a banking system with a strong track record of adequate regulation and good economic growth prospects; and • Good business stability reinforced by its role in supporting Peru's crucial infrastructure needs. 	<ul style="list-style-type: none"> • Concentrated business profile; and • Higher-than-average external funding dependence, mitigated by the long-term nature of the funding.

Outlook: Stable

The stable outlook on COFIDE for the next 18-24 months reflects that on the sovereign, given our view of a high likelihood that the latter would provide extraordinary and timely support to the bank in the event of financial distress, in accordance with our criteria for GREs.

Upside scenario

If COFIDE disposes its investments in CAF shares that would benefit its capital position, we would raise the bank's SACP because we apply high risk weights to this exposure under our capital analysis. Still, a higher credit rating would rely on a similar action on the sovereign.

Downside scenario

We could lower the ratings in the next 18-24 months if the bank's SACP drops to 'bb+', but we don't expect such deterioration in its capital or risk position. Our current capital assessment is under pressure, close to the 7% threshold, which we could change to moderate from adequate if we revise our BICRA assessment downwards or if the bank posts weaker figures than in our projections. As such, we would lower SACP to 'bbb-' but the credit rating would remain unchanged. A downgrade is therefore unlikely without a prior downgrade on the sovereign.

Rationale

The ratings on Corporacion Financiera de Desarrollo S.A. reflect its "adequate" business position, "adequate" capital and earnings, "strong" risk position, and "adequate" funding and liquidity, as defined by our criteria.

Anchor: For a bank operating only in Peru is 'bbb-'

Our bank criteria use our Banking Industry Country Risk Assessment (BICRA) economic risk 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 Peru is 'bbb-'.

We believe that economic risk for banks operating in Peru has increased. Economic growth has slowed down significantly since 2014, and we have revised our assessment of Peru's growth prospects. We expect growth to average 3.7% between 2015 and 2018, 2.8% in per capita terms, which will hinder Peru's ability to catch up to its more developed peers in the medium term. Nevertheless, we believe that a strong fiscal position, prudent monetary policies, and a credible and effective central bank provide the country with enough flexibility to withstand present and future external shocks. Credit growth rates have fallen since 2014, but this growth continues to add more than 2 percentage points to leverage (credit to GDP) per year, which increases the risk of economic imbalances. Although credit and real estate prices have been growing steadily, Peru doesn't have a real estate bubble, in our view. Real estate prices have risen thanks to solid economic growth, an increase in household income, and an expanding middle class. We have observed a rapid alignment of real estate prices growth with slower economic growth since 2014.

We consider industry risk for banks operating in Peru to be, in general, lower than its peers'. We believe that the country has a sound regulatory framework, with ample supervisory coverage and periodic risk based supervision under a highly professional regulator. Both Peru's central bank and Superintendencia de Banca y Seguros, a banking and insurer regulator, are very active. In the past two years, authorities have introduced several prudent measures to

ensure financial stability at the macro level amid a weakened economy and rising external risk. The domestic financial system has generated strong profitability and adequate levels of capitalization in the past five years, and there are no significant market distortions that could alter the system's competitive dynamics in the near term. We also believe the country's financial system has a healthy and diversified funding mix through deposits, domestic market debt, and external debt (banks and markets), as well as strong government support to provide liquidity if needed.

Table 1

Corporacion Financiera de Desarrollo S.A. Key Figures					
--Year-ended Dec. 31--					
(Mil. PEN)	2016*	2015	2014	2013	2012
Adjusted assets	13,499.2	13,539.0	9,707.5	8,038.2	6,860.8
Customer loans (gross)	7,136.2	7,950.9	5,789.2	5,193.2	3,880.2
Adjusted common equity	2,356.3	2,392.6	2,247.1	2,190.5	2,223.6
Operating revenues	80.3	218.5	184.0	178.5	168.1
Noninterest expenses	19.1	76.6	88.6	72.0	72.0
Core earnings	26.4	82.3	77.1	76.4	74.1

*Data as of March 31. PEN--PEN-Peruvian nuevo sol.

Business position: Second-largest public bank in Peru, main focus on infrastructure

We view the bank's business position as "adequate," reflecting its role in supporting Peru's crucial infrastructure needs. Its key role as the only development bank in Peru bolsters our view of its high stability. With total assets of about Peruvian soles (PEN) 13.5 billion as of March 31, 2016, COFIDE is the second-largest government-owned bank in Peru in terms of assets (with a 25.9% market share) and in terms of loans (27.7% market share) among public banks. Within the financial system, it holds a market share of 3.3% in terms of assets and 2.7% in terms of loans.

COFIDE, as a development bank, provides financing through banks, municipal and rural financial institutions, credit unions, and entities specializing in financing small and midsize enterprises (SMEs). We believe COFIDE has adequate business stability because of its unique role in providing long-term financing to infrastructure projects crucial to country's economic development. COFIDE also offers competitive and long-term financing to the SMEs in economic sectors that the government wants to promote. We expect COFIDE to offer its credit lines across new sectors such as forestry, health, sanitation, and education in the next few years. As of March 31, 2016, the bank's financing of infrastructure projects constituted about 82% of its lending exposures, while the remaining exposures are directed to SMEs. We expect these lending mix to remain stable over the next five years. Because of its narrow range of products, COFIDE's business diversity is lower than that of commercial banks that offer a wide range of products across different business segments. Nevertheless, COFIDE's management has a satisfactory track record of successfully implementing operational policies. Although following the presidential election, COFIDE's board composition and senior management could change, we don't expect its strategy to change substantially, while Peru's infrastructure gap will continue to be an important issue for the new administration.

Table 2

Corporacion Financiera de Desarrollo S.A. Business Position					
--Year-ended Dec. 31--					
(%)	2016*	2015	2014	2013	2012
Return on equity	3.9	3.3	3.5	3.5	3.4

*Data as of March 31.

Capital and earnings: Projected RAC ratio before diversification of about 8%

We view COFIDE's capital and earnings as "adequate," with a projected risk-adjusted capital (RAC) ratio before diversification of 7.0%-7.5% for the next 12-18 months. Its RAC ratio is weaker than its regulatory capital ratios (currently at 30.5% as of December 2015) mainly because of the bank's large equity exposure through its investments in Corporacion Andina de Fomento (CAF; AA-/Negative/A-1+). We view this exposure as having higher risk weights under our capital methodology, in comparison with the regulator's methodology. Our base-case scenario forecasts Peru's GDP growth of 3.5% in 2016 and 3.8% in 2017 and loan growth of about 5% and 10% respectively, slower than in previous years because we expect the new government to take some time to promote new infrastructure projects. We expect COFIDE's net interest margins to decrease because of higher funding costs and unexpected pre-payments for some projects, slightly decreasing profitability in the next two years.

Table 3

Corporacion Financiera de Desarrollo S.A. Capital And Earnings					
--Year-ended Dec. 31--					
(%)	2016*	2015	2014	2013	2012
Adjusted common equity/total adjusted capital	100.0	100.0	100.0	100.0	100.0
Net interest income/operating revenues	61.5	84.3	84.9	87.9	85.5
Fee income/operating revenues	9.3	15.1	15.1	12.1	14.5
Noninterest expenses/operating revenues	23.8	35.1	48.2	40.3	42.8
Preprovision operating income/average assets	1.8	1.2	1.1	1.4	1.6
Core earnings/average managed assets	0.8	0.7	0.9	1.0	1.2

*Data as of March 31.

Risk position: Capital ratios overestimate the bank's risks due to CAF investments

COFIDE's risk position is "strong," reflecting our view that our risk-adjusted capital (RAC) overestimates the bank's risks relative to its peers'. Although we believe that the bank's investments in CAF are an insufficient buffer against unexpected losses, we believe the government will provide capital to COFIDE that will offset any such losses. As a result, we offset part of the negative effect these investments have on the bank's capital position through the risk position.

In December 2014, the bank's nonperforming loans (NPLs) sharply increased because of a single exposure, Maple Etanol, that defaulted in December 2014. The exposure was later sold to a large group and COFIDE was able to recover part of the loan. As of March 31, 2016, its NPL levels decreased to 0.78% from 2.51% in December 2014, and are now lower than the industry average. COFIDE is exposed to single-name concentration, given the size of the infrastructure projects it funds. The bank's top 10 clients represented 73.3% of its total gross loan portfolio as of March 31, 2016 because of its business as a development bank. However, the ultimate loans are less concentrated. Loans for

infrastructure projects are not guaranteed by the bank that transfers the funds, so the risk is associated with the project. However, the structure of these loans incorporates conservative overcollateralization, which COFIDE and the funding bank closely analyze to make sure all risks are covered. The bank has a higher share of loans denominated in foreign currency (61%) than the industry average (31.6%). Nevertheless, infrastructure loans in foreign currency are only allocated to projects that generate revenues in foreign currency. In addition, the SME loans are typically very granular and short term and the financial institution that distributes them guarantees repayment, mitigating the risk of default.

Table 4

Corporacion Financiera de Desarrollo S.A. Risk Position					
(%)	--Year-ended Dec. 31--				
	2016*	2015	2014	2013	2012
Growth in customer loans	(41.0)	37.3	11.5	33.8	33.8
Total managed assets/adjusted common equity (x)	5.7	5.7	4.3	3.7	3.1
New loan loss provisions/average customer loans	1.2	0.9	(0.2)	(0.0)	(0.6)
Net charge-offs/average customer loans	(5.1)	(1.7)	(2.3)	(1.8)	(3.5)
Gross nonperforming assets/customer loans + other real estate owned	0.8	0.7	2.5	0.0	0.1
Loan loss reserves/gross nonperforming assets	1,140.6	1,105.1	409.2	37,467.0	19,312.7

*Data as of March 31.

Funding and liquidity: Higher-than-average external funding dependence, mitigated by the long-term nature of the funding

COFIDE's funding and liquidity are "adequate." Although COFIDE, as a development bank, does not receive deposits, its financial flexibility benefits from the government's ongoing support. COFIDE's government-related entity (GRE) status gives it ample flexibility to refinance, as evidenced by strong demand for the bank's debt issuances. Although it receives higher-than-average external funding, we believe it has an adequate funding profile, given the long-term nature of the funding required for its loans. We expect the bank to continue matching tenors and currencies on its balance sheet to mitigate risk. As of Dec. 31, 2015, its funding consisted mainly of debt issuances from international capital markets (63%), loans from Peruvian commercial banks (14%), loans from international commercial banks (12%), debt from local capital markets (7%), and credit lines from multilateral organizations (4%). According to our methodology, the bank's stable funding ratio was 113.3% as of March 2016 and averaged 97.1% for the last three years.

We view COFIDE's liquidity as "adequate." As of March 31, 2016, its broad liquid assets covered 1.86x its short-term wholesale funding. Moreover, the fixed maturity terms of its funding support our assessment of its liquidity, coupled with the insusceptibility to acceleration. This provides the bank sufficient time to manage its liquidity risk. Moreover, we expect the government to provide support if necessary. Furthermore, COFIDE, has an investment of PEN2.3 billion in CAF, which we consider illiquid because this type of share is only government-owned. However, we expect the government of Peru to purchase these shares in case COFIDE requires support.

The rating on COFIDE's subordinated notes is one notch lower than the bank's SACP, reflecting subordination risk. The bank's current capital position is under pressure, close to the 7% threshold, which we could change to moderate from adequate if we were to revise our BICRA assessment downwards or if our forecast assumptions don't materialize.

In such a scenario, we could revise downward COFIDE's SACP to 'bbb-' and consequently lower COFIDE's subordinated notes to 'BB+'.

Table 5

Corporacion Financiera de Desarrollo S.A. Funding And Liquidity					
	--Year-ended Dec. 31--				
(%)	2016*	2015	2014	2013	2012
Core deposits/funding base	0.1	0.3	0.7	1.3	0.5
Customer loans (net)/customer deposits	64,289.1	22,448.1	10,923.2	6,399.2	16,693.9
Long term funding ratio	83.3	83.8	86.0	82.6	76.9
Stable funding ratio	113.3	107.0	98.4	85.8	81.3
Short-term wholesale funding/funding base	21.2	20.4	18.4	24.5	35.4
Broad liquid assets/short-term wholesale funding (x)	1.9	1.5	1.3	0.6	0.6
Net broad liquid assets/short-term customer deposits	23,020.6	4,474.2	980.6	(907.0)	(4,025.2)
Short-term wholesale funding/total wholesale funding	21.2	20.4	18.6	24.9	35.6

*Data as of March 31.

Support: "High" likelihood that the government would provide timely and sufficient extraordinary support

In our view, COFIDE is a GRE because the government of the Republic of Peru (foreign currency: BBB+/Stable/A-2; local currency: A-/Stable/A-2) owns 99% of the bank through "El Fondo Nacional de Financiamiento de la Actividad Empresarial del Estado" (FONAFE; created in 1999 to oversee the government's corporate activities and equity stakes), with the remainder owned by CAF through preferred shares. We believe there is a "high" likelihood that the government would provide timely and sufficient extraordinary support to COFIDE if it experiences financial distress, in accordance with our criteria for government-related entities (GREs). We base this view on COFIDE's "important" role in promoting and financing investments and public and private infrastructure throughout Peru. In addition, the bank has a "very strong" link with the government, evidenced by the several capital injections it has received. We don't expect significant changes to the bank's GRE status regardless of who wins Peru's presidential election.

Related Criteria And Research

Related Criteria

- General Criteria: Rating Government-Related Entities: Methodology And Assumptions, March 25, 2015
- Bank Hybrid Capital And Nondeferrable Subordinated Debt Methodology And Assumptions, Jan. 29, 2015
- Banks: Quantitative Metrics For Rating Banks Globally: Methodology And Assumptions, July 17, 2013
- Criteria - Financial Institutions - Banks: Revised Market Risk Charges For Banks In Our Risk-Adjusted Capital Framework, June 22, 2012
- Banks: Rating Methodology And Assumptions, Nov. 9, 2011
- Banking Industry Country Risk Assessment Methodology And Assumptions, Nov. 9, 2011
- Bank Capital Methodology and Assumptions, Dec. 6, 2010
- Use Of CreditWatch And Outlooks, Sept. 14, 2009
- Criteria - Financial Institutions - Banks: Commercial Paper I: Banks, March 23, 2004

Anchor Matrix										
Industry Risk	Economic Risk									
	1	2	3	4	5	6	7	8	9	10
1	a	a	a-	bbb+	bbb+	bbb	-	-	-	-
2	a	a-	a-	bbb+	bbb	bbb	bbb-	-	-	-
3	a-	a-	bbb+	bbb+	bbb	bbb-	bbb-	bb+	-	-
4	bbb+	bbb+	bbb+	bbb	bbb	bbb-	bb+	bb	bb	-
5	bbb+	bbb	bbb	bbb	bbb-	bbb-	bb+	bb	bb-	b+
6	bbb	bbb	bbb-	bbb-	bbb-	bb+	bb	bb	bb-	b+
7	-	bbb-	bbb-	bb+	bb+	bb	bb	bb-	b+	b+
8	-	-	bb+	bb	bb	bb	bb-	bb-	b+	b
9	-	-	-	bb	bb-	bb-	b+	b+	b+	b
10	-	-	-	-	b+	b+	b+	b	b	b-

Ratings Detail (As Of June 23, 2016)

Corporacion Financiera de Desarrollo S.A.

Counterparty Credit Rating	BBB+/Stable/A-2
Senior Unsecured	BBB+
Subordinated	BBB-

Counterparty Credit Ratings History

20-Aug-2013	BBB+/Stable/A-2
29-Aug-2012	BBB/Positive/A-2
11-Jul-2012	BBB/Stable/A-2
05-Sep-2011	BBB/Stable/A-3

Sovereign Rating

Peru (Republic of)	
Foreign Currency	BBB+/Stable/A-2
Local Currency	A-/Stable/A-2

Related Entities

Banco Agropecuario S.A

Issuer Credit Rating	BBB-/Negative/--
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Fondo Mivivienda S.A.

Issuer Credit Rating	BBB+/Stable/--
Senior Unsecured	BBB+

Peru (Republic of)

Issuer Credit Rating	
Foreign Currency	BBB+/Stable/A-2
Local Currency	A-/Stable/A-2
Certificate Of Deposit	
Local Currency	A-2
Senior Unsecured	A-
Senior Unsecured	BBB+

Ratings Detail (As Of June 23, 2016) (cont.)

*Unless otherwise noted, all ratings in this report are global scale ratings. Standard & Poor's credit ratings on the global scale are comparable across countries. Standard & Poor's credit ratings on a national scale are relative to obligors or obligations within that specific country. Issue and debt ratings could include debt guaranteed by another entity, and rated debt that an entity guarantees.

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