MOODY'S
INVESTORS SERVICE

Rating Action: Moody's downgrades four Mexican banks and IPAB and affirms BBVA Mexico's ratings; changes outlook to stable

12 Jul 2022

New York, July 12, 2022 -- Moody's Investors Service ("Moody's") has today downgraded the deposit and issuer ratings assigned to Banco Mercantil del Norte, S.A. (Banorte), Nacional Financiera, S.N.C. (Nafin), Banco Nacional de Comercio Exterior, S.N.C. (Bancomext) and Instituto para la Protección al Ahorro Bancario (IPAB) to Baa2, from Baa1. The long-term Counterparty Risk Assessments (CR Assessments) and long-term Counterparty Risk Ratings (CRRs), in local and foreign currency, assigned to Nafin, Nacional Financiera, S.N.C., London Branch (Nafin London Branch), Bancomext and Banco Nacional de Comercio Exterior, SNC (CI) (Bancomext Cayman) were also downgraded to Baa2(cr), from Baa1(cr), and Baa2, from Baa1, respectively. The BCAs and adjusted BCAs assigned to Banorte, Nafin and Bancomext were affirmed at baa2, ba1 and ba2, respectively.

Moody's downgraded the baseline credit assessment (BCA) to baa2, from baa1, assigned to BBVA Mexico, S.A. (BBVA Mexico) and Banco Nacional de México, S.A. (Citibanamex). At the same time, Moody's also affirmed BBVA Mexico's long-term deposit ratings at Baa1, as well as the Baa1 long-term senior unsecured debt ratings of BBVA Mexico SA Ins Houston Agency (BBVA Houston Agency). The CR Assessments and CRRs assigned to BBVA Mexico and BBVA Houston Agency were also affirmed.

For all issuers, except Citibanamex, the rating outlook was changed to stable, from negative.

Moody's also said today that the ratings assigned to Banco Nacional de México, S.A. (Citibanamex) remain under review for downgrade. The review was initiated on 16 January 2022. Moody's also downgraded the subordinated debt ratings of Bancomext Cayman's subordinated capital notes to Ba1(hyb), from Baa3(hyb).

These actions follow the downgrade of the Government of Mexico's sovereign debt rating to Baa2, from Baa1, outlook changed to stable, on 8 July 2022. For additional information, please refer to the related press release: "Moody's downgrades Mexico's ratings to Baa2, changes outlook to stable from negative" (https://www.moodys.com/research/--PR_465313).

Please click on this link https://www.moodys.com/viewresearchdoc.aspx?docid=PBC_ARFTL467895 for the List of Affected Credit Ratings. This list is an integral part of this Press Release and identifies each affected issuer.

RATINGS RATIONALE

The downgrade of supported ratings assigned to Banorte, Nafin, Bancomext and IPAB was prompted by the downgrade of Mexico's sovereign debt rating to Baa2, from Baa1, which reflected the government's lower capacity to provide financial support to the banking system. As a result of the sovereign downgrade, several of the affected bank ratings no longer benefit from as much uplift from government support as was previously the case. Because of the close economic linkages to the Mexican government, the BCAs assigned to BBVA Mexico and Citibanamex were also downgraded to baa2, in line with the sovereign debt rating.

The downgrade of the Mexican government's rating was driven by economic and fiscal conditions that Moody's expects will continue to gradually – but persistently – undermine Mexico's overall credit profile. Moody's considers that economic activity will remain constrained by weak investment prospects and increased structural rigidities such that the economic scarring that took place during the pandemic will not be reversed and, consequently, GDP levels will remain below the pre-pandemic trend during the rest of this administration.

The stable outlook on the sovereign debt rating reflects Moody's expectations that, in the absence of unanticipated shocks, Mexico's credit profile will remain aligned with that observed in Baa2-rated sovereigns throug the end of the current administration despite rising economic and fiscal pressures. The stable outlook incorporates our expectation of policy continuity as Moody's anticipates the authorities will remain committed to macroeconomic stability during the rest of this administration.

AFFIRMATION OF BANORTE'S BCA AND DOWNGRADE OF SUPPORTED RATINGS

By affirming Banorte's baa2 BCA and adjusted BCA, Moody's acknowledges the bank's track record of strong profitability and capitalization, as well as its broad and steady core deposit base. The baa2 BCA also benefits from Banorte's well positioned franchise with high business diversification supported by disciplined risk management that ensures recurring earnings generation. The bank's funding costs are, nevertheless, higher relative to other large banks in Mexico.

Banorte's deposit and senior debt ratings were downgraded to Baa2, because of the downgrade of the Mexican sovereign rating to Baa2, and now stand at the same rating level as the sovereign. Although Moody's continues to incorporate a high support from the Mexican government, considering Banorte's systemic importance, the bank's Baa2 deposit ratings no longer benefit from an uplift of government support.

The stable outlook on Banorte's supported ratings is in line with its robust profitability that benefits from a low reliance on market funding and a capitalization policy focused on maintaining ample buffers, as well a conservative risk policy that supports consistently low delinquencies.

AFFIRMATION OF DEVELOPMENT BANKS' BCAS AND DOWNGRADE OF SUPPORTED RATINGS

Moody's affirmed Nafin's ba1 BCA reflecting the entity's narrow profitability that stems from its focus on indirect lending and the relatively high funding costs. The ba1 is supported by Nafin's historically strong capitalization, as well as a relatively low risk profile given its focus on on-lending via other financial institutions.

Moody's also affirmed Bancomext's ba2 BCA, which incorporates the bank's high capital position and good asset quality indicators supported by a conservative underwriting process maintained during Mexico's challenging economic recovery. The bank's BCA, however, remains constrained by its relatively limited liquidity position compared to other banks in Mexico, as well as its low profitability that reflects the bank's business focus on providing low-yielding loans to large corporates.

Nafin's ba1 and Bancomext's ba2 BCAs also consider the challenging scenario for asset risk and both banks' high single-borrower and industry concentrations, key risks limiting these banks' credit quality despite historically low problem loan ratios. These banks' high borrower concentration risks reflect their public policy mandates providing long-term financing aligned with the country's development policy. In addition, both Nafin and Bancomext benefit from solid access to capital markets, with the Mexican federal government providing statutory support for all liabilities.

Bancomext's and Nafin's issuer and debt ratings were downgraded to Baa2, from Baa1, and remain in line with the downgrade of Mexico's debt rating to Baa2. These ratings and outlook are aligned with those of the Mexican government.

DOWNGRADE OF BANCOMEXT'S SUBORDINATED CAPITAL NOTES

In line with the downgrade of Mexico's rating to Baa2, Moody's also downgraded to Ba1(hyb), from Baa3(hyb), the rating assigned to the subordinated capital notes issued by Bancomext Cayman Branch. The Ba1(hyb) rating for these notes continues to incorporate two notches of subordination from the bank's foreign currency senior unsecured debt rating of Baa2 and benefits from Moody's assessment of high government support, which results in a one-notch uplift from its ba2 BCA.

Moody's assesses a high government support for these capital eligible notes because of Bancomext's status as an arm of the government, with a specific public policy role to promote the export sector and those industries that attract foreign currency to Mexico. Bancomext also complements commercial banks' products, mainly in initial-stage projects, by offering US dollar long-term financing for investments, rather than short-term working capital in Mexican pesos. Moody's assumption of support to the subordinated capital notes also considers statutory support from the Mexican government, which is committed in Article 10 of Bancomext's Organic Law[1] to fulfill the bank's financial obligations. The support statute is not a blanket guarantee, and, as a result, does not qualify for credit substitution for the subordinated preferred notes when capital ratios fall below their minimum regulatory requirements, as stated in the indenture. Moreover, the government's statutory responsibility (i) only benefits Mexican individuals and both Mexican and foreign institutions, and explicitly excludes non-Mexican individual, (ii) does not include an explicit commitment to ensure timely payment, and (iv) is subject to budgetary restrictions. The government's ability to provide support is derived from its Baa2 bond rating, with a stable outlook.

DOWNGRADE OF BBVA MEXICO'S BCA AND AFFIRMATION OF DEPOSIT AND DEBT RATINGS

Moody's downgraded BBVA Mexico's BCA to baa2, from baa1, following the downgrade of the Mexican sovereign rating. The bank's BCA is constrained by the sovereign rating, reflecting the high direct and indirect risk correlation between BBVA Mexico's balance sheet and the sovereign credit profile.

The bank's baa2 BCA acknowledges BBVA Mexico's long-track record of strong financial fundamentals supported by its well-established franchise in Mexico, that ensures its widely diversified earnings generation, stable core deposit base and high-quality loan portfolio. BBVA Mexico has consistently been the most profitable bank in Mexico and the largest in the country with leading market shares in various asset classes and banking products. In line with a lower dividend payout and recurring profitability, BBVA Mexico's capital position has improved consistently over the last three years, reaching 15.6% (tangible common equity/ Moody's adjusted risk-weighted assets) in March 2022, complementing its ample reserves against loan losses, which, in turn, provides robust loss absorption capacity. Disciplined risk management has historically allowed the bank to maintain one of the lowest problem loan ratios in the banking system (2% in March 2022, versus 2.5% industry-average), with limited deterioration during the pandemic, and a conservative 163% reserve for loan losses over problem loans in March 2022, which will mitigate the asset risk challenges arising from Mexico's weak economic recovery.

The affirmation of BBVA Mexico's Baa1 deposit ratings and BBVA Houston Agency's Baa1 senior debt rating is in line with the affirmation of the bank's adjusted BCA of baa1. The adjusted BCA of baa1 considers moderate affiliate support from its Spanish parent Banco Bilbao Vizcaya Argentaria, S.A. (BBVA, A2 stable, baa2), that reflects the high level of independence of the Mexican subsidiary, both in terms of funding and business generation. Affiliate support acknowledges the importance of the Mexican subsidiary to the group, consisting of 19% of the group's total assets as of March 2022, and the benefits provided by a shared risk management standards and brand recognition. Moreover, the BBVA group exhibits a strong geographic diversification where each of its subsidiaries has a well-established de-centralized funding structure, as well as self-sufficient and diversified business channels and liquidity management.

In line with the affirmation of BBVA Mexico's adjusted BCA at baa1, Moody's also affirmed BBVA Mexico's long- and short-term CRRs and CR Assessments at A3/P-2 and A3(cr)/P-2(cr) and BBVA Houston Agency's long-term local currency contingent capital securities at Baa3(hyb) and long-term subordinated debt at Baa2.

The stable outlook for BBVA Mexico is in line with Moody's expectation that the bank will continue to benefit from ample support from its parent bank and an intrinsic financial strength that will benefit from its risk management and leading market shares.

DOWNGRADE OF CITIBANAMEX'S BCA AND MAINTAIN REVIEW FOR DOWNGRADE

Moody's downgraded Citibanamex's BCA to baa2, from baa1, following the downgrade of the Mexican sovereign rating. The bank's BCA is in line with the sovereign rating, reflecting the high direct and indirect correlation between Citibanamex's balance sheet and the sovereign credit profile.

Citibanamex's baa2 BCA and all other ratings remain on review for downgrade reflecting the uncertainties regarding Citigroup Inc.'s (Citi, A3 stable) planned divestiture of Citibanamex's consumer and small business operations and the implications on the bank's standalone credit profile. The review period was initiated on 16 January 2022. During the review period Moody's will assess the bank's competitive environment, whether with a focus on the Institutional Clients Group (ICG) and its private bank, or other segments in Mexico. Moody's will assess Citibanamex's post-divestiture ability to maintain a resilient asset quality, strong capitalization, ample profitability, and a stable funding mix while addressing the challenges related to Mexico's weak economic recovery and a much smaller and less diversified portfolio. During the review period, the appropriate levels of affiliate and government support will also be reassessed by Moody's.

Given the size and scale of Citibanamex in Mexico, this divestiture will likely take more time to be concluded and extend Moody's review of Citibanamex's ratings beyond the one- to three-month period.

DOWNGRADE OF THE IPAB'S RATINGS

The IPAB, in its role as the deposit insurance corporation, is an integral part of the Mexican government. The IPAB is largely funded by bonds that benefit from an implicit sovereign backing, whereas deposit insurance corporations elsewhere fund themselves privately. Therefore, IPAB's ratings and outlook are aligned with those of the Mexican government.

FACTORS THAT COULD LEAD TO AN UPGRADE OR DOWNGRADE OF THE RATINGS

NAFIN, BANCOMEXT AND IPAB

The Baa2 issuer ratings of Nafin, Bancomext and the IPAB are positioned at the same level of the sovereign bond rating and, therefore, there is no upward pressure on the entities' supported ratings at this point. Any upward pressure on these ratings would be in conjunction with an upgrade in Mexico's government bond rating. Pressure on Nafin's and Bancomext's BCA would depend on improvement in the standalone financial profile, including lower concentration risk, more diversified funding mix as well as higher profitability.

Conversely, if Mexico's government bond rating faced downward pressures, the entities' issuer ratings would be negatively pressured. Downward pressure on Nafin's and Bancomext's BCAs would emerge if these development banks were to experience further deterioration in asset quality.

BANORTE

Currently, there is no upward pressure on Banorte's ratings because its baa2 BCA and Baa2 deposit and senior unsecured debt ratings are at the same level as Mexico's Baa2 sovereign rating.

If Mexico's government bond rating is downgraded, Banorte's BCA, deposit and debt ratings would be downgraded as well. Banorte's BCA would be downgraded because of material decline in the bank's core capitalization or if there is a substantial deterioration of asset quality.

BBVA MEXICO

There is no upward pressure on BBVA Mexico's ratings, which are already one notch above Mexico's Baa2 sovereign rating and its parent bank's baa2 BCA.

A downgrade of BBVA Mexico's Adjusted BCA of baa1 and deposit ratings would result from a downgrade of its BCA because of a significant deterioration in the bank's asset quality that would require the bank to sharply increase its loan loss provisions, and/or by a strain the bank's profitability, reducing its internal capital generation and loss-absorption capacities. A downgrade of Mexico's Baa2 government bond rating would exert further pressure on BBVA Mexico's BCA and supported ratings. A sustained increase in the funding dependence of BBVA Mexico on its parent BBVA would exert downward pressure on the notching uplift that results in an Adjusted BCA that is one notch above BBVA Mexico's BCA.

CITIBANAMEX

Citibanamex's ratings would be confirmed at their current levels if following Moody's reassessment of the ratings, the rating agency concludes that the bank is able to maintain good asset quality that benefits from disciplined risk management and good corporate governance while maintaining a well-positioned franchise in Mexico that results in sound earnings generation capacity that lends support to capitalization, and if Moody's expects the bank to continue to benefit from existing levels of affiliate and government support. Because the ratings were placed on review for downgrade, an upgrade of the ratings is less likely at this moment. At the same time, an upgrade of the bank's BCA is unlikely because it is currently at the same level as the Mexican government's Baa2 ratings.

Citibanamex's ratings could be downgraded in line with a lower BCA that would result from higher asset risks without higher earnings generation, higher loan reserves and capitalization. A downgrade of Citibanamex's deposit ratings will also depend on Moody's reassessment of support from the Mexican government and affiliate support from Citigroup or the new owner of the bank.

The principal methodology used in rating Banco Mercantil del Norte, S.A., Banco Mercantil del Norte, S.A.(Cayman I), BBVA Mexico, S.A., BBVA Mexico SA Ins Houston Agency, Banco Nacional de Comercio Exterior, S.N.C., Banco Nacional de Comercio Exterior, SNC (CI), and Banco Nacional de Mexico, S.A. was Banks Methodology published in July 2021 and available at https://ratings.moodys.com/api/rmc-documents/71997. The principal methodologies used in rating Nacional Financiera, S.N.C and Nacional Financiera S.N.C., London Branch were Banks Methdology published in July 2021 and available at https://ratings.moodys.com/api/rmc-documents/71997 , and Government-Related Issuers Methodology published in February 2020 and available at https://ratings.moodys.com/api/rmc-documents/64864 . The principal methodology used in rating Instit.para la Protec.al Ahorro Bancario was Government-Related Issuers Methodology published in February 2020 and available at https://ratings.moodys.com/api/rmc-documents/64864. Alternatively, please see the Rating Methodologies page on https://ratings.moodys.com for a copy of these methodologies.

REGULATORY DISCLOSURES

The List of Affected Credit Ratings announced here are a mix of solicited and unsolicited credit ratings. For additional information, please refer to Moody's Policy for Designating and Assigning Unsolicited Credit Ratings available on its website https://ratings.moodys.com. Additionally, the List of Affected Credit Ratings includes additional disclosures that vary with regard to some of the ratings. Please click on this link https://www.moodys.com/viewresearchdoc.aspx?docid=PBC_ARFTL467895 for the List of Affected Credit Ratings. This list is an integral part of this Press Release and provides, for each of the credit ratings covered, Moody's disclosures on the following items:

• EU Endorsement Status

• UK Endorsement Status

• Rating Solicitation

• Issuer Participation

• Participation: Access to Management

• Participation: Access to Internal Documents

• Lead Analyst

• Releasing Office

For further specification of Moody's key rating assumptions and sensitivity analysis, see the sections Methodology Assumptions and Sensitivity to Assumptions in the disclosure form. Moody's Rating Symbols and Definitions can be found on https://ratings.moodys.com/rating-definitions.

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The ratings have been disclosed to the rated entity or its designated agent(s) and issued with no amendment resulting from that disclosure.

Regulatory disclosures contained in this press release apply to the credit rating and, if applicable, the related rating outlook or rating review.

Moody's general principles for assessing environmental, social and governance (ESG) risks in our credit analysis can be found at https://ratings.moodys.com/documents/PBC_1288235.

The below contact information is provided for information purposes only. For disclosures on the lead rating analyst and the Moody's legal entity that issued the rating, please see the issuer/deal page on https://ratings.moodys.com for each of the ratings covered.

REFERENCES/CITATIONS

[1] Ley Orgánica del Banco Nacional de Comercio Exterior 20-Jan-1986

Please see https://ratings.moodys.com for any updates on changes to the lead rating analyst and to the Moody's legal entity that has issued the rating.

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