

Research Update:

Ueno Bank S.A. Rated 'BB'; Outlook Stable

December 20, 2024

Overview

- We assigned our 'BB' long-term issuer credit rating to the Paraguayan bank Ueno Bank S.A.
- The rating reflects a one-notch upward adjustment due to ongoing support from the owner, Grupo Vazquez S.A.E. (not rated). This adjustment considers the group's experience in the financial sector and the synergies with other companies within the group, which bolster the bank's business and risk profiles.
- The stable outlook reflects our expectation that the bank will continue to execute its development plan after the recently acquired operations of Vision Banco.

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Rating Action

On Dec. 20, 2024, S&P Global Ratings assigned its 'BB' long-term issuer credit rating on Ueno Bank. The outlook is stable.

Rationale

The rating on Ueno Bank reflects its adequate position in the consumer and microcredit segments in Paraguay, bolstered by effective branding and innovative digital solutions that have facilitated the rapid expansion of its customer base. We expect the bank's capital base, along with the capitalization of earnings, to support the execution of its business plan, with a forecast risk-adjusted capital (RAC) ratio of approximately 5.5% for the next 12-24 months, calculated according to S&P Global Ratings' methodology. Our analysis considers Ueno Bank's growth strategy—both organic and inorganic—along with the associated risks from Vision Banco's loan portfolio. Furthermore, the rating reflects a stable, diversified, and geographically dispersed deposit base that is consistent with other banks in the system.

The ratings on the bank reflect a one-notch upward adjustment due to ongoing support from Grupo Vazquez. The adjustment considers the group's experience in the financial sector and the synergies with other companies within the group, which boost the bank's business and risk profiles. The synergies among companies enable the bank to access a customer base, providing valuable information that facilitates cross-selling opportunities. This approach helps mitigate

credit risks by enhancing the bank's understanding of its clients. Grupo Vázquez has been operating in Paraguay since 1945 in various economic sectors through equity participations and financial support to associated entities. The group has five business units: financial services, technology, retail, agribusiness, and real estate. Additionally, it has been active in the credit market since 1984 through Credicentro and it acquired Financiera El Comercio in 2021, which has since been integrated into Ueno Bank.

Anchor: 'bb' for commercial banks operating in Paraguay. 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. The anchor for banks operating only in Paraguay, like Ueno Bank, is 'bb'. (Please see "Banking Industry Country Risk Assessment: Paraguay," published Dec. 6, 2024.)

Ueno Bank is the first fully digital universal bank in Paraguay, primarily targeting small and midsize enterprises (SMEs), microcredit, and consumer segments. Following a series of acquisitions and organic growth, the bank received a banking license in 2023. As of September 2024, it ranks as the ninth-largest entity in the Paraguayan banking system in terms of credit and sixth in terms of deposits, with market shares of 4.2% and 5.9%, respectively, a notable increase from 1.2% and 1.3% in 2023 prior to its acquisition of Vision Banco. The corporate and SME lending segments represent the bank's largest business line, comprising 71% of its loan portfolio, followed by consumer loans at 20% and mortgages at 9%.

Approximately half of its revenue comes from net interest income, followed by fees and services (25%), and other operating revenues (25%). We view the bank's customer base as substantial and loyal, which we expect to enhance the fee income in the coming years, driven by the significant volume of credit cards issued and associated fees (such as acquiring and payment operations). Ueno Bank's profitability is similar to that of its peers, reporting return on equity of 22% and 14% as of September 2024 and December 2023, respectively, compared to the peer averages of 18% and 17%. Furthermore, the bank benefits from its affiliation with Grupo Vazquez, which provides significant advantages through cross-selling opportunities. This integration encompasses an insurance division, a broker-dealer, an asset management firm, a fiduciary business, and a digital payment processing network, all operating within a cohesive digital banking platform.

We expect Ueno Bank's capital base and earnings retention to support its business plan. To evaluate banks' capitalization levels, S&P Global Ratings applies a globally consistent risk-adjusted capital framework, independent of regional regulations and internal risk measures. Our RAC methodology compares total adjusted capital to risk-weighted assets, providing a more comparable risk metric than traditional regulatory ratios. Our forecast incorporates the following base-case scenario assumptions:

- Loan growth of approximately 320% in 2024, driven by the integration of Vision Banco and organic growth, followed by 35% growth in 2025 and 20% in 2026.
- Lower margins during 2024-2026 due to loans under special treatment, as these loans do not accrue interest while they are in this category.
- Return on average adjusted assets (ROAA) of 1.5%-2.0%.
- Nonperforming assets of 1.5%-2.0%, with net charge-offs in single digits, supported by high levels of loan-loss reserves.
- A gradual impact of losses from loans under special treatment, mainly in the next three years.

- No dividend distributions until the regulatory transitory measures are concluded.

Additionally, Ueno Bank reported solid regulatory capitalization metrics of 17.0% as of September 2024, significantly exceeding the regulator's minimum capital requirement of 12.0%.

Our risk profile evaluation considers the emerging risks associated with the aggressive growth strategy of Ueno Bank and the loan portfolio of Vision Banco, which is currently under special treatment. We assess Ueno Bank's asset quality as moderate, primarily due to the risks stemming from rapid growth—both organic and inorganic—and the challenges linked to Vision Banco's loan portfolio, which is undergoing a special treatment.

Ueno Bank anticipates that the loans under special measures will be amortized in the next six to seven years, a time is shorter than the tenor established with the central bank. And the bank expects manageable amortization of losses. As of September 2024, the nonperforming loan (NPL) ratio remained below the industry average; however, delinquencies from loans under the regulatory transitory measures are not classified as NPLs. We have observed some weakening of the repossessed assets, which are legacy assets from Vision Banco and are expected to be sold in the short to medium term. Prior to the acquisition, Ueno Bank's loan portfolio demonstrated strong performance, benefiting from origination models and data derived from the group's experience operating in the financial sector.

We anticipate Ueno Bank's asset quality to slip due to its rapid expansion into more risky lending segments. Additionally, the bank's NPL coverage ratio was 978% as of September 2024, compared with 127% as of December 2023, while the industry averages were 132% and 122%, respectively. We believe that Ueno Bank's loan portfolio is diversified in terms of single-name concentration, with the 20 largest loans constituting 19% of its total portfolio and 1.16x its tangible equity as of September 2024.

Our assessment of Ueno Bank's funding highlights its diversified and stable deposit base, supported by a comprehensive nationwide network and a varied retail depositor profile. As of September 2024, deposits remained the primary funding source, constituting approximately 92% of total funding. The remaining funding sources consisted of credit lines from financial institutions (5%) and subordinated debt (3%).

Ueno Bank's stable funding ratio was 131% in September 2024, averaging 119% for the past three fiscal years ending December 31. While Ueno Bank has the largest number of depositors within the banking system, it ranks eighth in terms of total deposit volume. The entity has a manageable concentration of deposits. The 20 largest deposits accounted for 25% of total deposits (about 10% are deposits from the country's pension fund, same percentage as for industry peers). For the next 12 to 18 months, we anticipate that Ueno Bank will continue to rely on deposits as a key funding source, while also diversifying its funding strategy through the incorporation of bank lines and debt issuance in both domestic and international markets.

In terms of liquidity, Ueno Bank is well-positioned, with broad liquid assets covering 2.5x its short-term wholesale funding as of September 2024, and the coverage ratio of averaging 1.1x for the past three years. Most of liquid assets are allocated in government bonds and high-quality instruments.

The rating does not incorporate notching from extraordinary support. We assess that Ueno Bank is effectively ring-fenced from its parent, Grupo Vazquez which owns 84% of the bank. As a condition for the acquisition of Vision Banco, the central bank of Paraguay approved a regulatory transitory plan that requires Ueno Bank to retain all profits for capitalization purposes for the plan's duration. Consequently, the bank can't distribute dividends until the loans under special

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treatment have been fully amortized which limits the capacity of the group to negatively influence the creditworthiness of the bank.

On the other hand, we consider Ueno Bank to be a moderately important institution in the Paraguayan financial system, ranking as the ninth-largest bank in the country. The bank's market share is in mid-single digits, characterized by a significant share of retail deposits and number transactions and participation in the payment system in the country. In this context, we anticipate that a default on Ueno Bank's senior secured obligations would have a negative impact on the Paraguayan financial system. We assess the Paraguayan government's propensity to support banks as uncertain. This, combined with the factors mentioned above, leads us to conclude that there is a low likelihood of extraordinary government support for Ueno Bank, as well as other systemic banks in the country, in the event of financial distress. Consequently, we do not forecast any notch uplift in the rating on the bank for support.

Outlook

The stable outlook on Ueno Bank for the next 12 months reflects our expectation that it will implement its development plan as a digital bank in Paraguay after the recently acquired operations of Vision Banco.

Downside scenario

We could lower the rating on the bank if the capitalization metrics erode, with RAC ratio before diversification below 5%.

Upside scenario

Upside is limited at this point as the entity is still in process to consolidate its organic and inorganic growth strategy.

Ratings Score Snapshot

Issuer credit rating	BB/Stable/--
Stand-alone credit profile	bb
Anchor	bb
Business position	Adequate (0)
Capital and earnings	Moderate (0)
Risk position	Moderate (-1)
Funding	Adequate (0)
Liquidity	Adequate (0)
Comparable rating analysis	+1
Support	
ALAC support	0
GRE support	0
Group support	0

Sovereign support 0

Related Criteria

- Criteria | Financial Institutions | General: Risk-Adjusted Capital Framework Methodology, April 30, 2024
- Criteria | Financial Institutions | General: Financial Institutions Rating Methodology, Dec. 9, 2021
- Criteria | Financial Institutions | Banks: Banking Industry Country Risk Assessment Methodology And Assumptions, Dec. 9, 2021
- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- General Criteria: Group Rating Methodology, July 1, 2019
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Ratings List

New Rating; CreditWatch/Outlook Action

Ueno Bank S.A.

Issuer Credit Rating	BB/Stable/--
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