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Larrain Vial S.A. Corredora de Bolsa

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Larrain Vial S.A. Corredora de Bolsa

Major Rating Factors

Issuer Credit Rating

BBB/Stable/A-2

Strengths:	Weaknesses:
<ul style="list-style-type: none">• Sound competitive position;• Strong capitalization metrics with solid earnings capacity; and• Low-risk operating conditions in Chile.	<ul style="list-style-type: none">• Significant competition in the Chilean brokerage industry; and• Profitability susceptible to securities market fluctuations and transaction volumes.

Outlook

The stable outlook on Larrain Vial S.A. Corredora de Bolsa (LVCB) incorporates our expectation that for the next 24 months it will maintain its business position in the Chilean market, despite stiff competition. The outlook also reflects LVCB's risk-adjusted capital (RAC) metrics of 10%-15%, which are in line with a strong capital and earnings assessment, its maintenance of an adequate risk profile, adequate funding (with gross stable funding ratio [GSFR] over 90%), and adequate-high metrics (with liquidity coverage metric [LCM] above 100%).

Downside scenario

We could lower the ratings if risk levels at the firm increase, if capital drops sharply (resulting in RAC of less than 10%), or if funding and liquidity weaken to below adequate levels. In addition, a downgrade is possible if industry conditions in Chile deteriorate, scenario that's less probable at this stage.

Upside scenario

Possibility of an upgrade is limited at this point and would depend on the improvement of the anchor for security firms operating in Chile, while LVCB's credit factors remain unchanged.

Rationale

Our ratings on LVCB reflect its solid business position as one of the largest brokerage houses in Chile with wide business diversification, its expected RAC ratio of 10%-15% during the next 12-18 months thanks to solid earnings capacity, and its prudent risk management with adequate controls. The ratings also reflect our view of LVCB's stable

and long-term funding sources relative to its needs, and its sound ability to meet its liquidity demands under stressful conditions for at least 12 months. The firm's stand-alone credit profile (SACP) remains at 'bbb'. The long-term issuer credit rating on LVCB is at the same level as its SACP because the latter doesn't incorporate notching from external support from either the government or the group.

Anchor: 'bb+' for securities firms operating in Chile.

The 'bb+' anchor for securities firms indicates our view of Chile's economic and industry risks. The anchor for securities firms in Chile is three notches below our anchor for domestic banks. This is so, compared with our standard two-notch adjustment, to reflect our view of the higher risks for securities firms in Chile, given more volatile and less liquid domestic capital markets in the country compared with those in other countries.

Our standard two-notch adjustment generally reflects our view that the funding risk for securities firms is higher than for banks because these firms typically lack access to the central bank's credit lines, as is the case in Chile, as well as strong competition from banks and among securities firms. Nonetheless, Chilean securities firms benefit from favorable competitive conditions thanks to the country's privatized pension system. This system has helped diminish cyclicity, even though the sector's revenues are more transactional than those of banks.

While regulatory standards are relatively adequate and oversight is fairly comprehensive, we believe the institutional framework for securities firms is weaker than the one for Chilean banks.

Table 1

Key Financial Data					
	2018	2017	2016	2015	2014
(CLP)					
Adjusted assets	555,282,529	351,023,108	288,862,872	258,566,765	268,519,498
Adjusted common equity	77,378,006	71,923,648	67,287,369	63,767,535	65,143,883
Total Adjusted Capital	77,378,006	71,923,648	67,287,369	63,767,535	65,143,883
Operating revenues	24,226,907	46,270,426	44,232,075	41,206,227	49,764,313
Noninterest expenses	16,428,904	28,757,543	34,741,754	38,788,295	41,263,849
Net income	7,330,512	15,081,551	7,374,346	3,535,063	4,893,636
Core earnings	7,351,392	14,984,632	9,199,103	3,240,616	11,771,907

*Year to date.

Chart 1**IPSA Stock Index Evolution**

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Business position: Solid competitive position amid leading position in Chilean market

We view LVCB's business position as a credit strength based on its sound competitive position in the Chilean financial system. LVCB is one of the leading independent brokerage firms in Chile offering a broad range of financial services and long-term relationships with customers, all of which provides a stable revenue base to the firm.

As of June 2018, LVCB remained the leader in equity intermediation in Chile, with an 18% share (considering accumulated figures of only third-party accounts in the Santiago Stock Exchange and Bolsa Electrónica) while it was the ninth-largest in corporate bonds, with a share of 3%. Equity intermediation volumes for LVCB have risen since 2016 when the firm resumed operations with pension funds after reaching an agreement on past allegations.

LVCB operates in Chile, Peru, Colombia, and the U.S, which provides some diversification, but revenue from Chile continues to make up the bulk of its total revenue. As of March 2018, operations from abroad represented 5.4% of the brokerage house's total revenue, and we expect this share to rise to about 10% over the medium term. The firm's operations in capital markets, investment banking, trading, and wealth management help mitigate market cycles. In our opinion, LVCB has a qualified management team with extensive experience in financial markets. For the next 12-18 months, we expect the firm to remain the leader in equity intermediation in Chile, expanding its customer base--despite stiff competition--and widening its geographic diversification in terms of revenue and volumes. Improved

conditions for Chile's financial industry after the elections in 2017 and higher copper prices than in 2016 should help mitigate effects of regional and global volatility and maintain favorable fundamentals for Chile's securities firms.

Table 2

Business Position					
	2018*	2017	2016	2015	2014
(%)					
Net interest income/operating revenues	(7.22)	(7.84)	(8.93)	(9.83)	(10.19)
Fee income/operating revenues	49.66	50.14	50.88	53.59	50.64
Market-sensitive income/operating revenues	2.09	(2.78)	(3.47)	11.37	6.35
Pretax profit/operating revenues	32.10	38.09	17.20	6.40	7.10
Core earnings/average adjusted common equity	19.70	21.53	14.04	5.03	18.62

*Year to date.

Capital, leverage, and earnings: Expected RAC ratio of 10%-15% for the next 12-18 months with sound earnings capacity.

We assess LVCB's capital, leverage, and earnings as a credit strength based on our expected RAC ratio before diversification of 10%-15% for the next 12-18 months and the firm's strong earnings capacity.

As of March 2018, the firm's RAC ratio was 12.2%. We expect the firm's shareholders to continue to support the company so it can maintain sound capital metrics through moderate and flexible dividend distributions. The company continues to enjoy healthy core earnings (with core earnings to risk-weighted assets averaging about 1.9% as of March 2018), with about 50% of operating revenue from recurring fees and commissions. In 2017, LVCB's net income roughly doubled to CLP15.081 billion from CLP7.374 billion in 2016 thanks to stronger operating revenues due to higher fees from brokerage commissions and lower noninterest expenses, as some expenses were relocated in a new company of the group. In the first half of 2018, results increased 17%, stemming from higher brokerage commissions but impacted by lower income from the finance instrument and higher administrative expenses, due to a change in the accounting criteria of some expenses. In 2018, we foresee that LVCB will continue to improve its profitability owing to higher net brokerage commissions and expected volumes traded.

Table 3

Capital, Leverage, And Earnings					
	2018*	2017	2016	2015	2014
Leverage Ratio (IFRS)	14.35	21.82	23.56	24.91	24.47
Adjusted total equity/adjusted assets	12.08	17.99	19.67	21.44	20.54
Adjusted common equity/total adjusted capital	100.00	100.00	100.00	100.00	100.00
Personnel expenses/operating revenues	20.26	10.20	9.99	10.71	15.28
Cost-income ratio	67.81	62.15	78.54	94.13	82.92
Core earnings/operating revenues	30.34	32.38	20.80	7.86	23.66
Internal capital generation/prior year's equity	20.38	22.41	11.56	5.43	7.98
Net interest income/average earning assets	(2.41)	(2.98)	(3.16)	(2.82)	(2.86)
Core earnings/S&P RWA before diversification	N/A	2.87	N/A	0.65	N/A

*Year to date.

Risk position: Prudent risk management

We believe LVCB has a prudent risk profile consistent with historical levels and those of peers. In our view, LVCB manages principal risks because it has strengthened its risk management practices and taken a comprehensive risk approach. The firm applies formal market risk controls based on value-at-risk measures and stress-testing analysis, incorporating major transaction risks. We also consider that LVCB is diversified in terms of geography, clients, and sectors.

Table 4

Risk Position					
	2018*	2017	2016	2015	2014
(%)					
Annualized adjusted assets growth rate	116.4	21.5	11.7	(3.7)	(29.3)
Adjusted common equity/managed assets	13.8	20.2	22.9	24.3	24.0

*Year to date June.

Funding and liquidity: Stable and long-term funding sources and sound ability to meets its liquidity demands

LVCB's funding assessment reflects its stable and long-term funding sources relative to its needs. As of June 2018, the company's GSFR was 99%, averaging 139% for the past three fiscal years, and we expect this ratio to be above 90% in the next 12-18 months. The firm also has access to intra-day liquidity through credit facilities from several Chilean banks.

Our liquidity assessment reflects our view of LVCB's ability to meets its liquidity demands. Our LCM on the firm has been above 100% over the last few years, 144% as of June 2018, and 133% as of December 2017. LVCB's broad liquid assets are mainly composed of its investment portfolio, which is mainly allocated in government bonds and short-term corporate and bank securities. Its liquidity needs are mainly short-term repurchase agreements. We expect the firm to maintain its LCM above 100% and to comply with its liquidity needs under potential stressful market conditions for the next 12 months.

Table 5

Funding And Liquidity					
	2018*	2017	2016	2015	2014
Gross stable funding ratio (%)	98.62	135.41	142.47	141.74	123.73
Short-term wholesale funding/adjusted assets	23.24	23.22	29.57	38.36	43.21
Liquidity coverage metric (x)	1.46	2.15	1.84	1.54	1.39

*Year to date June.

Support: No additional notches for external support

We don't incorporate notching for external support into the issuer credit ratings on LVCB. Larrain Vial S.P.A. (not rated) is a private Chilean holding company specializing in financial services and investment and finance consultancy that directly and indirectly owns 100% of LVCB. Larrain Vial's group credit profile is at the same level as the credit rating on LVCB, because the latter is the group's main subsidiary that accounts for about 80% of its total consolidated assets.

Related Criteria

- Criteria - Financial Institutions - General: Risk-Adjusted Capital Framework Methodology, July 20, 2017
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- Criteria - Financial Institutions - General: Nonbank Financial Institutions Rating Methodology, Dec. 9, 2014
- General Criteria: Group Rating Methodology, Nov. 19, 2013
- Criteria - Financial Institutions - Banks: Quantitative Metrics For Rating Banks Globally: Methodology And Assumptions, July 17, 2013
- Criteria - Financial Institutions - Banks: Banking Industry Country Risk Assessment Methodology And Assumptions, Nov. 9, 2011
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009

Ratings Score Snapshot

Issuer Credit Rating BBB/Stable/A-2

SACP bbb

Anchor bb+

Business Position Strong (+1)

Capital and Earnings Strong (+1)

Risk Position Adequate (0)

Funding and Liquidity Adequate and Adequate -High (0)

Support

GRE Support 0

Group Support 0

Government Support 0

Additional factors 0

Ratings Detail (As Of September 26, 2018)

Larrain Vial S.A. Corredora de Bolsa

Issuer Credit Rating

BBB/Stable/A-2

Issuer Credit Ratings History

22-Aug-2018

BBB/Stable/A-2

08-Aug-2017

BBB/Negative/A-2

Ratings Detail (As Of September 26, 2018) (cont.)

14-Jul-2017	BBB/Watch Neg/A-2
27-Jan-2017	BBB/Negative/A-2
10-Dec-2014	BBB/Stable/A-2
12-Sep-2014	BBB+/Negative/A-2
14-Feb-2014	BBB+/Watch Neg/A-2

Sovereign Rating

Chile

Foreign Currency

A+/Stable/A-1

Local Currency

AA-/Stable/A-1+

*Unless otherwise noted, all ratings in this report are global scale ratings. S&P Global Ratings' credit ratings on the global scale are comparable across countries. S&P Global Ratings' 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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