

Rating Action: Moody's assigns Aa3 to Banco del Estado de Chile's Australian Dollar Senior Notes

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New York, May 10, 2017 -- Moody's Investors Service has assigned a Aa3 long-term foreign currency senior unsecured debt rating to Banco del Estado de Chile's (Banco Estado) ten-year senior unsecured notes of AUD110 million, maturing on 10 November 2027. The outlook on the rating is stable.

The notes are being issued under Banco Estado's current USD3 billion global medium-term note program.

The following rating was assigned to Banco Estado's ten-year AUD110 million senior unsecured notes, due 10 November 2027:

Long-term foreign currency senior unsecured debt rating: Aa3, stable outlook

RATINGS RATIONALE

The Aa3 debt rating incorporates the very high probability that the bank would receive government support if it faces severe financial stress. Although Banco Estado's obligations do not benefit from an explicit guarantee, Moody's views the bank as government-backed in line with its 100% ownership by the Republic of Chile, its status as the country's largest deposit-taking institution and mortgage lender, and its significant policy role. As Chile's sole government-owned bank, Banco Estado plays an important public policy role by (i) catering to low-income individuals with an explicit mandate towards promoting home ownership and national savings, (ii) offering financing to small and mid-sized enterprises (SMEs) and (iii) providing banking services to remote rural areas that are not served by private sector alternatives.

The rating also considers credit strengths in terms of funding and liquidity, as well as improved asset quality. Together with the very high probability of support, these offset the limited amount and poor loss absorption capacity of the bank's capital and its low profitability.

The market leader in savings deposits and individual clients, the bank has low reliance on market funds and ample holdings of high quality liquid assets, which equaled 35.7% of tangible banking assets as of year-end 2016, a level that is well above the bank's local peers. The bank's market funding is also well-diversified and comprised mainly of long-term, domestic debt issuances, reducing the bank's exposure to refinancing risks.

Asset quality has improved consistently over the past five years, exhibited by much lower nonperforming loans of 3.4% of total loans as of year-end 2016, from 4.1% as of year-end 2012. Despite the slowdown of Chile's economy in recent years and the incipient recovery, Moody's does not expect the bank's overall asset risk to deteriorate substantially because of the strong performance of its commercial loan portfolio and the substantial government guarantees the bank has on its most vulnerable portfolios of SMEs and residential mortgages.

In line with its banking methodology, Moody's adjusted capitalization ratio for Banco Estado is just 2.6%, which reflects the limited loss absorption capacity of a substantial portion of the bank's regulatory capital. Although Banco Estado's total regulatory capital ratio of 11.3% remains comfortably above regulatory minima, it is the lowest in the Chilean banking system. The bank's low profitability results from high operating expenses related to the large branch network needed to fulfill its mandate, a loan mix geared towards low-yielding commercial and mortgage financing, its high liquidity, and higher tax burden. The bank's net income of just 0.5% of tangible assets was well below that of its peers in Chile, as of year-end 2016.

WHAT COULD CHANGE THE RATING UP OR DOWN

Given Moody's view that Banco Estado is government-backed, an upward movement on Chile's government bond rating of Aa3 could lead to upward ratings pressure on the bank's debt and deposit ratings. Conversely, if the Chilean government's bond rating were to be downgraded, Banco Estado's senior debt and deposit ratings would also be equivalently affected. However, the ratings are not likely to be affected by any change in the bank's intrinsic financial strength.

The principal methodology used in this rating was Banks published in January 2016. Please see the Rating Methodologies page on www.moodys.com for a copy of this methodology.

Headquartered in Santiago, Chile, as of year-end 2016 and on a consolidated basis Banco Estado reported CLP34.8 trillion (USD51.9 billion) in total assets, CLP20.7 trillion in gross loans, CLP23.3 trillion in deposits, CLP1.6 trillion in shareholders' equity and CLP147.1 billion in net income.

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