MOODY'S INVESTORS SERVICE

CREDIT OPINION

30 June 2021

Update

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RATINGS

Coopeuch

Domicile	Santiago, Chile
Long Term CRR	A3
Type	LT Counterparty Risk Rating - Fgn Curr
Outlook	Not Assigned
Long Term Debt	Baa1
Type	Senior Unsecured - Fgn Curr
Outlook	Positive
Long Term Deposit	Baa1
Type	LT Bank Deposits - Fgn Curr
Outlook	Positive

Please see the ratings section at the end of this report for more information. The ratings and outlook shown reflect information as of the publication date.

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Coopeuch

Update to credit analysis

Summary

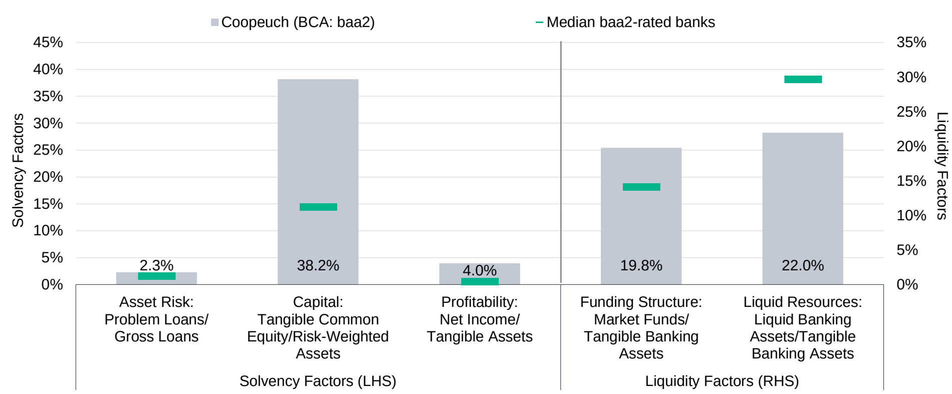
On 25 June 2021, we affirmed Coopeuch's Baa1 long-term senior unsecured debt and deposit ratings, and its baa2 Baseline Credit Assessment (BCA) and changed the outlook to positive, from stable. The rating action reflects Coopeuch's strong asset quality, in line with its moderate risk appetite; the benefits stemming from its cooperative niche franchise, which ensures a stable retail funding mix and solid capitalization; and ample profitability. Moreover, the cooperative bank's credit profile will be strengthened by a more ample holding of liquid assets and enhanced funding access.

Coopeuch's ratings benefit from one notch of uplift from its baa2 Adjusted BCA as a result of our assessment of moderate support from the Government of Chile (A1 negative) related to the very large number of individual associates who keep their savings with the cooperative.

Exhibit 1

Rating Scorecard - Key financial ratios

Coopeuch's scorecard ratios as of March 2021



For the problem loan and profitability ratios, we review the latest three year-end ratios, as well as the most recent intra-year ratio, where applicable, and base our starting point ratio on the weaker of the average of this period and the latest figure. For the capital ratio, we use the latest figure. For the funding structure and liquid asset ratios, we use the latest year-end figures.
Source: Moody's Financial Metrics™

Credit strengths

- Payroll-deducted loans to civil servants mitigates asset risks
- Capitalization to remain solid on the back of regular membership contributions
- Strong profitability, driven by a focus on higher-yielding retail financing and cheap funding
- Access to retail deposit funding coupled with increased liquidity buffers

Credit challenges

- High correlation between sources of funding and capital, and asset quality
- Focus on lower-income individuals, who are more exposed to economic cycles

Outlook

The positive outlook captures the strong asset quality, capital and profitability fundamentals maintained by Coopeuch following the economic crisis in 2020, which was supported by its granular loan book and disciplined risk management guidelines. At the same time, Coopeuch increased its holdings of liquid assets and will benefit from an enhanced funding access.

Factors that could lead to an upgrade

In line with the positive outlook, a contained increase in asset risks as loan payments normalize in the second semester of 2021, a stronger liquidity profile and the access to the central bank window would result in upward ratings pressure for Coopeuch.

Factors that could lead to a downgrade

Downward pressure on Coopeuch's ratings is more limited at this time, but would develop as a result of a substantial increase in risk appetite and as such a higher than expected deterioration in its asset risk metrics, which could lead to significant losses and hurt its capital.

Key indicators

Exhibit 2

Coopeuch (Consolidated Financials) [1]

	03-21[2]	12-20[2]	12-19[2]	12-18[2]	12-17[2]	CAGR/Avg.[3]
Total Assets (CLP Billion)	2,236.9	2,161.9	1,834.1	1,641.7	1,491.5	13.3[4]
Total Assets (USD Million)	3,113.8	3,042.8	2,439.1	2,365.6	2,425.2	8.0[4]
Tangible Common Equity (CLP Billion)	602.1	566.0	539.5	507.9	476.3	7.5[4]
Tangible Common Equity (USD Million)	838.1	796.6	717.5	731.9	774.4	2.5[4]
Problem Loans / Gross Loans (%)	1.6	1.5	3.1	3.0	3.1	2.5[5]
Tangible Common Equity / Risk Weighted Assets (%)	38.2	36.0	36.7	38.5	39.7	37.8[6]
Problem Loans / (Tangible Common Equity + Loan Loss Reserve) (%)	4.0	3.9	8.2	7.8	7.9	6.4[5]
Net Interest Margin (%)	9.4	10.1	11.3	11.9	12.0	10.9[5]
PPI / Average RWA (%)	6.9	6.5	8.0	8.3	8.8	7.7[6]
Net Income / Tangible Assets (%)	4.8	2.9	3.9	4.3	4.1	4.0[5]
Cost / Income Ratio (%)	51.7	53.7	49.0	49.6	47.8	50.3[5]
Market Funds / Tangible Banking Assets (%)	18.8	19.8	22.7	24.5	23.1	21.8[5]
Liquid Banking Assets / Tangible Banking Assets (%)	24.9	22.0	11.4	11.7	10.4	16.1[5]
Gross Loans / Due to Customers (%)	144.9	152.5	200.8	214.9	218.8	186.4[5]

[1] All figures and ratios are adjusted using Moody's standard adjustments. [2] Basel I; LOCAL GAAP. [3] May include rounding differences because of the scale of reported amounts. [4] Compound annual growth rate (%) based on the periods for the latest accounting regime. [5] Simple average of periods for the latest accounting regime. [6] Simple average of Basel I periods.

Sources: Moody's Investors Service and company filings

Profile

Headquartered in Santiago, Chile, Coopeuch reported CLP2.2 trillion ($3.1 billion) in total assets, CLP1.6 trillion in gross loans, CLP1.1 trillion in deposits, CLP529 billion in shareholders' equity and CLP27 billion in net income, and had about 921,000 members as of March 2021. Consumer loans represented 71% of loans, followed by residential mortgages, at 26%, as of March 2021. The cooperative also has a small portfolio of commercial loans, as well as small and micro businesses.

Coopeuch is by far the largest among the seven cooperatives regulated by the Comisión para el Mercado Financiero and the around 1,000 savings and loans cooperatives regulated by the Ministry of Economy. It is also the second largest in the country in terms of both the number of savings accounts and the volume of savings deposits.

As a cooperative, Coopeuch creates a mutually beneficial partnership with its members. As part of this partnership, the members provide funding in the form of capital through monthly membership contributions and, in turn, they are able to apply for loans. Members are also able to deposit at the cooperative.

Coopeuch was founded in 1967 and has been an open cooperative since the 1980s, when it stopped focusing exclusively on the personnel of the University of Chile.

Detailed credit considerations

Very strong profitability driven by its focus on higher-yielding retail lending and cheap funding

Coopeuch's profitability is ample, driven by its focus on higher-yielding retail lending and relatively low funding costs. The cooperative's focus on higher-yielding and highly granular loans to lower-income individuals results in high operating expenses and provisioning costs, which are nevertheless fully absorbed by the cooperative's ample net interest margin (NIM).

As of March 2021, Coopeuch's net income-to-tangible assets ratio increased to 4.8%, from 2.9% in 2020 and a 4.1% average for 2018-19, mainly because of the release of 27% of the provisions created in 2020, as well as lower operating expenses. The net provision release was 0.04% of gross loans (annualized) in Q1 2021, compared with net provisioning expenses of around 2.3% of gross loans reported in 2018-20, on average. This reflected the cooperative's focus on payroll-linked loans to public employees whose employment has been less affected by the current crisis than was the case for private-sector employees. In addition, Chile implemented ample public support measures for individuals affected by the pandemic, including pension savings withdrawals.

Moreover, as of March 2021, operating expenses declined 2.4% year over year, against a 12% increase in total assets. Still, efficiency remained relatively weak in comparison with large and diversified banks, with a cost-to-income ratio of 52%. Currently, investments in IT offset benefits from digitalization, but Coopeuch's efficiency will improve as more processes are automated.

On the other hand, the cooperative's NIM narrowed to 9.4% in Q1 2021, from 10.5% a year earlier and 11.7% in 2017-19, on average, because of lower origination volumes of consumer loans, coupled with a larger share of low-yielding liquid assets. In addition, net fees declined roughly 50% year over year, in line with still-weak business volumes. While NIM is unlikely to return to historical levels soon, mainly because low-margin liquid assets will remain above historical levels, fee income should gradually recover as economic activity resumes.

Risks stemming from Coopeuch's focus on consumer lending to lower-income individuals are partially offset by a large portion of payroll-deducted loans to public-sector employees

The cooperative's focus on payroll-linked consumer loans to public-sector employees as its main target market mitigates asset risks.

As of March 2021, Coopeuch's nonperforming loan (NPL) ratio declined to 1.6%, from 3.2% a year earlier, while the banking system's NPL ratio decreased to 1.6%, from 2.1%, over the same period. Borrowers used part of the proceeds from the pension fund withdrawals to repay their debt, which explains the improvement. At the same time, Coopeuch's net charge-offs also declined, to 2.1% of gross loans in 2020 and 0.9% in Q1 2021, from 2.6% in 2018-19 and 3.7% in 2016-17.

Moreover, Coopeuch's consumer NPL ratio of 1.4% as of December 2020 was also in line with the banking system average and well below the ratio for other non-bank lending institutions. Low delinquencies are explained by payroll deductions (payroll-linked loans represented almost 90% of consumer loans) of up to 25% of salaries and a focus on public-sector employees (about 87% of payroll-linked loans), who have a high degree of employment stability. The NPL ratio is higher within Coopeuch's mortgage (2.1%) and commercial (1.8%) portfolios, which are not linked to payrolls. Risks within the mortgage portfolio are mitigated by a low loan-to-value ratio, which on average was 67% as of March 2021 and also explained very low net charge-offs within this portfolio.

Because of lower delinquencies, the cooperative's loan-loss reserve coverage of problem loans also improved, to 206% as of March 2021, from a 140% average in 2016-19. Moreover, its loan-loss absorption capabilities are much higher than those of the banking system because of its high capitalization.

Coopeuch has actively adjusted its loan growth plans, which also supports its asset quality. Loans grew at a cumulative annual rate of 8% in 2018 and 2019 and slowed down to 2.5% in 2020 (in line with the banking system's 2.2%), while loans remained almost flat in Q1 2021. While short-term growth prospects are uncertain and depend on the speed of the economic recovery, in the medium term, the cooperative will accelerate its growth, but mainly by focusing on its own members who have a better risk profile. Private-sector employees, whose employment is more exposed to economic cycles, will continue to represent a small percentage of Coopeuch's loans.

Limited refinancing and repricing risks because of deep access to core deposit funding

Refinancing and repricing risks remain limited because of the cooperative's access to core deposit funding, which represented 66% of liabilities, as of March 2021. Moreover, retail deposits historically accounted for a high 90% of total deposits, while in 2020–March 2021, their share increased to 95%, as members kept part of the proceeds from pension fund withdrawals with the cooperative. This effect will only gradually dissipate, as the cooperative continues to strengthen its product offering to improve its competitive position.

On the other hand, its members' income levels are relatively lower and they are generally more vulnerable to economic downturns and, consequently, more likely to need to withdraw their deposits at exactly the same time the cooperative experiences an increase in delinquencies and needs funds to cover loan losses.

Coopeuch's dependence on less stable market funding is moderate, at 19% of tangible banking assets as of March 2021. Market funds have not increased as much as expected — they grew in line with the lower-than-expected expansion in loans. In the near term, Coopeuch aims to continue to fund its growth mainly with retail deposits and maintain limited reliance on market funding. Moreover, a proposed new legislation will allow Coopeuch access to the Central Bank of Chile's discount window, which will boost its funding access in times of stress.

Since 2017, the cooperative has been able to provide electronic fund transfers, and since 2011, it has been able to provide sight deposits, which allow it to act as the bank of choice for its associates and not only the bank where they place their savings and get a loan.

Capitalization will remain solid on the back of regular membership contributions

Coopeuch's full earnings distribution policy makes it dependent on the monthly membership fees paid by its members to maintain its capital levels and makes its high profitability largely irrelevant in terms of credit risk. Although Coopeuch's capitalization ratio is likely to decrease as capital is consumed by the rapid expansion in loans in the medium term, it will remain strong, supported by monthly contributions.

Coopeuch's members pay monthly membership dues, generating a stable flow of capital, which has led to the cooperative's very strong capitalization, illustrated by a tangible common equity-to-risk-weighted assets ratio of 38% as of March 2021. While the cooperative could theoretically reduce dividend payouts in the future, if necessary, this would be difficult to do in practice because of the likely strong opposition from the cooperative's associates, who may come to depend on this income stream.

The cooperative's dividend payout ratio, net of membership contributions, has averaged an adequate 50% of net income in the last three years.

The ratings also take into account the inability of the cooperative to raise capital from external sources, potentially limiting its financial flexibility in times of stress, which is precisely when its members will have less capacity to contribute additional capital and might want to withdraw previously contributed capital.

Liquidity profile has improved in line with higher holdings of liquid assets

The improvement in the liquidity profile, is also supported by Coopeuch's plans to maintain a higher stock of liquid assets in line with a clarification on a central bank directive for cooperatives, which also allowed Coopeuch to increase its investments in bank bonds. At 24.9% of tangible banking assets as of March 2021, liquid assets are now well above what was a low level when compared to peers, at 11% on average in 2017-19. The cooperative's liquid assets, including cash, bank deposits, government bonds and bank bonds, are of high quality.

Also, Coopeuch's liquidity coverage ratio was high, at 254.5% as of March 2021, well above the 100% regulatory minimum, benefiting from a large share of relatively more stable retail deposits.

Coopeuch's rating is supported by Chile's "Strong" Macro Profile

Credible and predictable macroeconomic and fiscal policies reflect the continued strength of Chile's institutions. The pandemic severely weakened economic growth in 2020 because of the magnitude and severity of the combined supply and demand shocks. The social protests that erupted in 2019, the process of drafting a new constitution and the presidential elections in 2021 will weaken investor confidence. In addition, Chile's economic diversification and GDP per capita lag those of its peers. Real GDP in Chile contracted 5.8% in 2020, and we expect it to expand 6.2% in 2021, but to slow to 3.6% in 2022. Although Chile has a high credit-to-GDP ratio, loan expansion has slowed in recent years. Chilean banks benefit from a stable and diversified mix of domestic funding sources, although the share of institutional and market funding is significant and above the Latin American average. The banking system is fairly concentrated, and Chilean banks tend to have significant pricing power.

Environmental, social and governance (ESG) considerations

Coopeuch's exposure to environmental risks is low, consistent with our general assessment for the global banking sector. See our Environmental risk heat maps for further information.

Overall, banks and cooperatives face moderate social risks. The most relevant social risks arise from the way they interact with their customers. Social risks are particularly high in the area of data security and customer privacy, which are mitigated by sizable technology investments and a long track record of handling sensitive client data. Fines and reputational damage because of product mis-selling or other types of misconduct are further social risks. Social trends are also relevant in a number of areas, such as shifting customer preferences toward digital banking services, increasing information technology cost, aging population concerns in several countries affecting demand for financial services or socially driven policy agendas translating into regulations that affect the revenue base. See our Social risk heat maps for further information.

Coopeuch's exposure to social risks is moderate, consistent with our general assessment for the global banking sector. Social protests and riots since late 2019 will continue to present a risk to the growth outlook even after the pandemic. We regard the pandemic as a social risk under our ESG framework because of the substantial implications for public health and safety.

Governance is highly relevant for Coopeuch, as it is to all participants in the banking industry. Corporate governance weaknesses can lead to a deterioration in an entity's credit quality, while governance strengths can benefit its credit profile. Governance risks are largely internal rather than externally driven, and for Coopeuch, we do not have any particular governance concerns. Overall, corporate governance remains a key credit consideration and requires ongoing monitoring.

Support and structural considerations

Government support considerations

We assess a moderate probability of government support for Coopeuch in times of stress, related to the very large number of individual associates (many of whom are low-income and public-sector employees) who keep their savings with the cooperative. As a result of government support, Coopeuch's ratings benefit from a one-notch uplift from its Baseline Credit Assessment of baa2. At the same time, our assessment takes into consideration the fact that Coopeuch's deposits represent merely 0.8% of the Chilean banking system and are not systemically important.

Counterparty Risk (CR) Assessment

CR Assessments are opinions of how counterparty obligations are likely to be treated if a bank fails and are distinct from debt and deposit ratings in that they (1) consider only the risk of default rather than both the likelihood of default and the expected financial loss, and (2) apply to counterparty obligations and contractual commitments rather than debt or deposit instruments. The CR Assessment is an opinion of the counterparty risk related to a bank's covered bonds, contractual performance obligations (servicing), derivatives (for example, swaps), letters of credit, guarantees and liquidity facilities.

Coopeuch's CR Assessment is positioned at A3(cr)/Prime-2(cr).

The CR Assessment, before government support, is positioned one notch above the Adjusted BCA of baa2 and, therefore, above deposit ratings, reflecting our view that the probability of default counterparty obligations is lower than that of deposits. We believe senior obligations represented by the CR Assessment will more likely be preserved to limit contagion, minimize losses and avoid the disruption of critical functions.

The CR Assessment also benefits from one notch of systemic support based on a moderate probability of public support, in line with our support assumptions on deposits. This reflects our view that any support provided by government authorities to a bank, which benefits senior unsecured debt or deposits, is very likely to benefit operating activities and obligations reflected by the CR Assessment as well. This is consistent with our belief that governments are likely to maintain such operations as a going concern to reduce contagion and preserve a bank's critical functions.

Counterparty Risk Ratings (CRRs)

CRRs are opinions of the ability of entities to honor the uncollateralized portion of non-debt counterparty financial liabilities (CRR liabilities) and also reflect the expected financial losses in the event such liabilities are not honored. CRR liabilities typically relate to transactions with unrelated parties. Examples of CRR liabilities include the uncollateralized portion of payables arising from derivatives transactions and the uncollateralized portion of liabilities under sale and repurchase agreements. CRRs are not applicable to funding commitments or other obligations associated with covered bonds, letters of credit, guarantees, servicer and trustee obligations, and other similar obligations that arise from a bank performing its essential operating functions.

Coopeuch's CRRs are positioned at A3/Prime-2.

The CRRs, before government support, are positioned one notch above the Adjusted BCA of baa2 and, therefore, above deposit ratings, reflecting our view that CRR liabilities have a lower probability of default than the deposits because they will more likely be preserved to minimize banking system contagion, minimize losses and avoid the disruption of critical functions.

The CRRs also incorporate our assumption of moderate government support, in line with our support assumptions on deposits.

Methodology and scorecard

About Moody's Bank Scorecard

Our scorecard is designed to capture, express and explain in summary form our Rating Committee's judgment. When read in conjunction with our research, a fulsome presentation of our judgment is expressed. As a result, the output of our scorecard may materially differ from that suggested by raw data alone (though it has been calibrated to avoid the frequent need for strong divergence). The scorecard output and the individual scores are discussed in rating committees and may be adjusted up or down to reflect conditions specific to each rated entity.

Rating methodology and scorecard factors

Exhibit 3

Coopeuch

Macro Factors		
Weighted Macro Profile	**Strong**	**100%**

Factor	**Historic Ratio**	**Initial Score**	**Expected Trend**	**Assigned Score**	**Key driver #1**	**Key driver #2**
Solvency						
Asset Risk						
Problem Loans / Gross Loans	2.3%	a3	↔	baa2	Sector concentration	Loan growth
Capital						
Tangible Common Equity / Risk Weighted Assets (Basel I)	38.2%	aa2	↔	aa2	Access to capital	Expected trend
Profitability						
Net Income / Tangible Assets	4.0%	aa2	↔	a1	Earnings quality	
Combined Solvency Score		a1		a2		
Liquidity						
Funding Structure						
Market Funds / Tangible Banking Assets	19.8%	baa1	↔	baa3	Market funding quality	Term structure
Liquid Resources						
Liquid Banking Assets / Tangible Banking Assets	22.0%	baa2	↑	baa3	Stock of liquid assets	
Combined Liquidity Score		baa1		baa3		
Financial Profile				a3		
Qualitative Adjustments				Adjustment		
Business Diversification				-1		
Opacity and Complexity				0		
Corporate Behavior				0		
Total Qualitative Adjustments				-1		
Sovereign or Affiliate constraint				A1		
BCA Scorecard-indicated Outcome - Range				a3 - baa2		
Assigned BCA				baa2		
Affiliate Support notching				0		
Adjusted BCA				baa2		

Instrument Class	**Loss Given Failure notching**	**Additional notching**	**Preliminary Rating Assessment**	**Government Support notching**	**Local Currency Rating**	**Foreign Currency Rating**
Counterparty Risk Rating	1	0	baa1	1	A3	A3
Counterparty Risk Assessment	1	0	baa1 (cr)	1	A3(cr)	
Deposits	0	0	baa2	1	Baa1	Baa1
Senior unsecured bank debt	0	0	baa2	1		Baa1

[1] Where dashes are shown for a particular factor (or sub-factor), the score is based on non-public information.
Source: Moody's Investors Service

Ratings

Exhibit 4

Category	Moody's Rating
COOPEUCH	
Outlook	Positive
Counterparty Risk Rating	A3/P-2
Bank Deposits	Baa1/P-2
Baseline Credit Assessment	baa2
Adjusted Baseline Credit Assessment	baa2
Counterparty Risk Assessment	A3(cr)/P-2(cr)
Senior Unsecured	Baa1

Source: Moody's Investors Service

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