

**Mexico
Credit Update**

Banco Inbursa

Ratings

Banco Inbursa, S.A.

Foreign Currency

Long-Term IDR	BBB
Short-Term	F3
Outlook	Stable

Local Currency

Long-Term IDR	BBB
Short-Term	F2
Outlook	Stable

Individual Support	C
Support Rating Floor	4
	B

National

Long-Term	AA+(mex)
Short-Term	F1+(mex)
Outlook	Stable

Sovereign Risk

Foreign Long-Term IDR	BBB
Local Long-Term IDR	BBB+
Outlook	Positive

Country Ceiling

Foreign Long-Term	A-
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Financial Data

Banco Inbursa, S.A. (C.)

	31 Dec 06	31 Dec 05
Total Assets [USDm]	7,442	7,185
Total Assets [MXPm]	80,981	77,439
Equity [MXPm]	24,239	23,924
Net Income [MXPm]	101	1,034
ROA (%)	0.13	1.26
ROE (%)	0.42	4.38
Capital Adequacy (%)	25.73	23.28

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Rating Rationale

- Banco Inbursa's (Inbursa) ratings reflect its strong capital adequacy, ample liquidity and historically low asset quality problems. Together, these factors partially offset the challenges associated with low and volatile profitability, sizeable market risks and large borrower concentrations.
- Earning volatility is highly correlated with the variability in trading revenue (market-related losses were reported in 2005 and 2006). Adequate margins and well-contained operating costs (less than 3% of average assets) partially alleviate overall profitability. Inbursa is very active in interest rate swaps, which aim at providing a hedge in the event of a sudden increase in local interest rates. In view of their ample notional values, relatively long maturities and Inbursa's position as the fixed-rate payer, declines in interest rates negatively affect their market value and net income. Earnings volatility is further exacerbated by the bank's extremely conservative provision approach. Inbursa typically provisions 2.5% of average loans p.a., regardless of historically marginal amounts of problem assets.
- While past-due loans have historically accounted for less than 1% of total loans, reserve coverage stands at 13% of total loans as of December 2006. Delinquency and charge-offs could eventually be somewhat pressured upward by a gradually increasing contribution from retail loans, but we believe the bank's main source of credit risk will remain its corporate portfolio. Further improving diversification by borrower and economic sector is a major challenge. While related-party lending is relatively high, sovereign exposure is very low.
- Inbursa's exposure to market risk is high given its sizeable securities portfolio and hefty derivatives positions in the form of interest rate swaps. At end-March 2007, the bank estimates that a 100bp decline in domestic interest rates could potentially harm its equity base by roughly 5%.
- The bank's historically wholesale-funding structure is rapidly changing towards customer deposits (48% of liabilities in the form of demand accounts at end-2006) with the introduction of high yielding deposit products targeted at higher and middle-income brackets of the population. The bank generally holds ample liquid assets, which partially offsets some funding concentration.
- Inbursa's capital adequacy is strong and provides a comfortable cushion against risk appetite and earnings volatility. At end-2006, the bank's free capital to banking assets ratio remained at a high 26.0%.

Support

- If required, we believe the bank would look to its shareholders for support. Given its slowly increasing, though small, systemic importance by deposits, support could also be provided by official sources, although the probability is limited.

Rating Outlook and Key Rating Drivers

- The outlook on Inbursa's ratings is stable as we expect it will likely maintain its financial profile in the near future. Over time, its Individual and Issuer Default ratings (IDRs) could benefit from higher and stable profitability, lower loan concentrations and sustained diversification in its business and revenue mix.
- Downside risk could stem from deterioration in its cushion of capital and loan loss reserves, or discontinuation in its ability to contain problem loans.

Profile

- Inbursa was Mexico's seventh largest bank at end-March 2007, with market shares by loans, assets and deposits of 5%, 4% and 3%, respectively. Inbursa is wholly-owned by Grupo Financiero Inbursa (GFInbursa). In turn, roughly 70% of GFInbursa is held by a group of Mexican investors led by the Slim family.

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