

**Banks
Peru
Credit Analysis**

BBVA-Banco Continental

Ratings

	Current Rating
Banco Continental	
Foreign Currency	
Long-Term IDR	BBB-
Short-Term IDR	F3
Local Currency	
Long-Term IDR	BBB
Short-Term IDR	F3
National	
Long-Term IDR	
Short-Term IDR	
Individual Support	C/D 2
Sovereign Risk	
Foreign Long-Term IDR	BB+
Local Long-Term IDR	BBB-
Country ceiling	BBB-

Outlook

Continental IDR/Individual Sovereign IDR	Positive/Stable Positive
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Financial Data

Continental	9/30/07	12/31/06
Total Assets (USDm)	7,166	5,819
Total Assets (PENm)	22,465	18,594
Equity (PENm)	1,815	1,710
Net Income (PENm)	421	488
ROA (%)	2.74	2.65
ROE (%)	31.87	30.37
Equity/Assets (%)	8.08	9.20

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Rating Rationale

- BBVA-Banco Continental's (Continental) Issuer Default Ratings (IDRs) reflect the support it would receive from its key stakeholder - Spain's BBVA, rated AA- by Fitch Ratings - should it be required. The long-term foreign currency IDR is constrained by Peru's country ceiling but has a Positive Outlook in line with Peru's sovereign ratings' outlook. Continental's individual rating reflects its sound performance and strong franchise but is constrained by rapid growth, slim capital and some margin pressure.
- Continental's loan growth accelerated into 2007 driven by retail banking; growth into higher margin segments improved net interest margin in spite of a relative increase in funding costs; non-interest income improved bringing diversification and stability to revenues. Loan loss provisions increased reflecting the portfolio shift and increased credit risk; however, a lean operating structure and economies of scale derived from BBVA's network of centralized operative hubs, allowed Continental to maintain costs well under control, improving efficiency to record levels. As a result, ROE exceeds 30% and ROA remains between 2.5% and 3% since 2005. Going forward, results should become less spectacular but remain in the mid 20%'s (ROE) and above 2% (ROA).
- Portfolio growth and adequate risk origination processes combined to improve asset quality while reserves slightly decreased compared to PDLs; coverage is however deemed adequate considering Continental's operating environment and sound credit policies. Overall, the portfolio appears better diversified and little concentrated.
- Continental's deposit mix improved as the bank willingly lost market share in time deposits. Deposit concentration improved slightly while borrowings become increasingly important. Rapid growth created pressure on capital ratios; increased earnings retention and subordinated debt sustained growth while achieving capital efficiency but - according to Fitch's methodology - such debt does not have equity-credit hence, capitalization ratios appear stretched

Support

- In spite of owning only 46% of Continental's stock, BBVA considers the bank important to its regional goals and treats it as a key subsidiary, hence - in Fitch's view - there is a high probability that such support would be forthcoming, if needed, absent any severe deterioration in the operating environment, which we currently consider unlikely.

What Could Trigger an Upgrade?

- Should Peru's sovereign rating and country ceiling be upgraded, Continental's foreign currency IDR could be upgraded by one notch. Downward risk for IDRs is limited but some pressure on the individual rating would arise if the bank is not able to sustain its performance, sees its assets deteriorate or allows its capital to weaken.

Profile

- Continental is Peru's second largest bank, with a market share of over 22% of deposits. Holding Continental (50% BBVA, 50% Grupo Brescia) controls 92.08% of the bank, the rest being hold mainly by institutional investors. The bank is fully integrated within BBVA's network, policies and management. BBVA appoints the CEO, CFO and Risk Manager.

- Second largest bank in the Peruvian banking system
- Active across all markets with a strong franchise and important support from BBVA

Profile

Incorporated in 1951, BBVA - Banco Continental (Continental) is Peru's second largest bank with 22% of deposits and 26% of loans at September 2007. Continental was controlled by Chase Manhattan Bank (51%) from 1965 to 1970 when it was nationalized; as political and economic trends shifted, the bank was privatized in 1995. The bank went through a thorough restructuring between 1995 and 2000 when BBVA's best practices and policies were implemented; once the framework in place, the bank shifted its focus to growth; aiming to exploit the opportunities created by the stabilization and expansion of Peru's economy. Growth was exclusively organic as the bank chose not to participate in the consolidation process of the Peruvian banking system. Modest growth rates marked the early years of the decade but since 2003, portfolio and assets surged, averaging 20% annual growth and increasing 33% yoy at September 2007. Continental operates as a universal bank offering a broad array of financial products through Peru's second largest branch network (210), the third largest ATM network (392) and over 3,600 employees.

Historically, Continental has been oriented to serve the corporate segment. Since its integration within the BBVA family, the bank segmented its target market in three business units: 1) Global Corporate Bank (Banca Mayorista Global or BMG), 2) Middle market (Banca de Empresas e Instituciones) and 3) Retail banking (Banca Minorista). BMG will remain its main target market but the bank is gradually diversifying into the promising retail segment through innovative products and aggressive marketing (See Strategy). Lending and services for the retail and middle markets were scarce until recent years, when a rapidly developing local capital market and broadening access to international markets for corporate clients resulted in lower margins and led top banks, to develop credit and service products for these underbanked markets. As Peruvian's GDP per capita grew rapidly, so did consumer, mortgage, and middle market lending. As of September 2007, Continental's Retail business contributes over 50% of net income.

Grupo Continental

(Figures in PEN m)

	Assets	Equity	Net Income
Banco Continental	22,465	1,815	421
Continental Bolsa	23	13	4
Continental Fondos	27	23	2
Continental Soc. Titulizadora	3	3	0
Inmueb. y Recup. Continental	62	59	13

Source: SBS, Conasev, Bank Reports. As of Sep/07

Holding Continental controls 92.08% of BBVA-Banco Continental, the rest is held by four private pension funds (AFP Prima, 1.97%; AFP Horizonte, 0.97%; AFP Profuturo, 0.82% and AFP Integra, 0.40%) and other private and institutional investors with less than 1% each (total: 3.76%). Holding Continental is a Peruvian holding company controlled at 50% by BBVA (Spain, rated AA- by Fitch) and 50% by Grupo Brescia, a local group active in mining, real estate, tourism, fishing,

etc. that derives most of its revenues from Holding Continental. The bank has four wholly owned subsidiaries in the financial services industry. Continental Bolsa SAB is the group's brokerage house, ranks among the top brokers in the Bolsa de Valores de Lima in both fixed income and equity trading. Continental SAF, the second mutual fund manager in Peru, had about \$895m in assets under management as of Dec/05; that is a 21% market share. Continental Sociedad Titulizadora is the securitizing arm of the group. Inmuebles y Recuperaciones Continental is a special vehicle created to hold and manage troubled assets and foreclosed property and equipment; it purchases assets from the bank at book value then collects and liquidates them. Besides, Holding Continental has a 54.4% stake in AFP Horizonte (pension fund managers) which is not consolidated under Grupo Continental as BBVA holds the balance directly.

Corporate Governance: Continental's corporate governance structure is set out in its By-laws, Internal Guidelines and Annual Report on Corporate Responsibility; the bank fully complies with the Peruvian Corporate Governance Guidelines (Principios de Buen Gobierno para las Sociedades Peruanas). Continental's board currently consists of 9 Directors, including 2 independent, 3 from BBVA (including the CEO) and 4 from Grupo Brescia. The board has organized two committees: Remunerations Committee (four members including the CEO) and the Audit and Compliance Committee (six members). A board member also participates in the Market Risk and Country Risk Committee (six members). The local affiliate of PriceWaterhouseCoopers audits the bank's books since 2000; the audit team is rotated every 5 years. The Audit Division, reports directly to the Board and to corporate audit (BBVA) in a matrix structure; the Compliance Officer also reports to the board.

Strategy: Continental's strategy is to focus on profitability rather than market share. Having achieved a comfortable second place in terms of market share, Continental has been gradually shifting its balance sheet towards higher margin retail loans and, better matched funding. Growth is and will remain an objective but the ultimate goal is to grow revenues and net income - rather than assets or market share - by diversifying from interest income to service fees as well as by generating steady revenue from capital markets transactions (e.g. mortgage securitization, investment banking, securities brokerage, fund management, etc.). Accordingly, the bank has implemented aggressive marketing plans aiming to deepen relationships with customers, increase share of wallet and improve cross-sell. Having the second largest market share in mortgages - in an economy where institutional investors lack investment options - the bank has the potential for further portfolio growth and development of the securitization market; it has recently led the first mortgage securitization in the market; the amounts are yet modest but the process and legal framework are now in place. Continental's strategy leverages its natural cost advantage, sound credit process and efficient operative framework.

Presentation of Accounts: This analysis is based on Continental's audited, consolidated year-end financial statements, as well as unaudited interim statements for the first nine months of 2007. The audited statements, prepared in accordance with Peruvian GAAP, received an unqualified opinion from the Peruvian affiliate of PriceWaterhouseCoopers.

- Economic conditions remain favorable, internal demand and investments fuel growth
- Continental's performance is driven by solid loan growth and successful cost control
- Loan loss provisions increase significantly in line with riskier portfolio; efficiency improves to record levels

Performance

The operating environment for Peruvian banks has improved steadily over the last five years. Peru's economic performance has been driven by favorable global trends which underpinned rapidly growing exports. Investment increased its contribution to GDP, which combined with the favorable external environment has accelerated growth to an average of 6.3% for the five years ending in 2007. The economic expansion bolstered tax revenue, which combined with controlled government spending, lead to fiscal surpluses in 2006 and 2007. Macroeconomic policy continuity has also served Peru well in recent years. A conservative fiscal policy - focused on improving tax administration, optimizing expenditure and reducing debt - as well as policies intended to foster private investment, should allow growth to continue as the government attempts to address poverty. While growth was regionally affected by the earthquake that devastated Pisco and Ica, the overall impact on economic growth was immaterial. As was the case in other emerging markets, inflation picked up in 2H07, mostly as a result of higher oil and food prices. However, strong domestic demand coupled with high utilization of installed capacity could also be contributing to underlying inflationary pressures. Going forward, a gradual cooling of export markets is expected but strong domestic demand, as well as the recently approved free-trade agreement with the US, should continue to fuel growth in excess of 6% through 2009. Peru's sovereign rating was upgraded to "BB+" in 2006 and

has a Positive Outlook.

The positive economic backdrop benefited the highly concentrated banking system. After several years of asset quality deterioration and depressed results, banks' balance sheets began to grow again in 2004, and growth has been steady since, reaching 35% ytd at September 2007. Loan growth has been led by lending to the retail market - mortgage and consumer loans - and, to a lesser but growing degree, to SMEs. Accordingly, revenues and loan portfolios are better diversified; asset quality has shown steady improvement thanks to the strong economy and to the effect of loan growth on traditional asset quality indicators. Portfolio growth, in turn, has boosted returns, revenues have benefited from lending to higher margin segments and net loan provisions have fallen steadily thanks to asset recoveries. Going forward, we expect loan growth and the aging of growing retail and SME portfolios will push provisions higher, though the favorable local environment should allow continued strong results.

Continental's performance through September 2007 has been driven by a growing revenue trend sustained by a strong loan portfolio growth (mainly in the retail bank) and an increasingly strong contribution of non-interest income. Costs remain well under control and efficiency gains are significant. Loan loss provisions have increased significantly to reflect the bank's riskier portfolio mix while reserve coverage is relatively stable and adequate. Net income improved significantly in 2006 and is in pace to set new records at September 2007.

Operating Revenues: Continental's revenues have significantly increased since 2004 driven by a strong loan portfolio growth (+33% yoy at September 2007, +36% in 2006, +34% in 2005) coupled with strong margins and an increasingly important contribution of non-interest income (+41% yoy at September 2007, +100% in 2006, +136% in 2005). Furthermore, higher non-interest revenues produced a welcome diversification of the revenue stream as they have passed from less than 17% (2003) to about 31% of total revenues at September 2007. Non-interest income is well diversified, with non-credit related fees accounting for more than 80%, and the balance generated principally by

Peruvian Banks, Financial Highlights

	Continental			BCP			Scotiabank			Interbank			System Average		
	9/07	12/06	12/05	9/07	12/06	12/05	9/07	12/06	12/05	9/07	12/06	12/05	9/07	12/06	12/05
Assets (PENm)	22,465	18,594	18,263	37,985	31,891	29,226	15,336	13,508	2,459	9,110	7,422	6,275	98,391	82,553	78,188
Equity (PENm)	1,815	1,711	1,504	3,042	2,861	2,791	1,586	1,284	193	764	669	562	8,895	7,875	7,217
Net Income (PENm)	421	488	402	718	662	692	336	262	19	168	161	113	1,832	1,716	1,483
Net investments (PENm)	2,606	1,977	3,604	8,478	6,145	5,782	2,411	2,039	203	1,421	1,235	342	15,986	12,240	12,424
Net Loans (PENm)	15,114	12,341	9,048	20,468	16,291	14,186	8,762	7,243	1,699	5,279	4,110	3,845	58,750	47,466	40,806
Deposits (PENm)	15,676	13,653	14,288	25,920	22,610	19,380	11,457	10,455	1,615	6,773	5,724	4,533	67,739	59,290	54,560
Subordinated debt (PENm)	221	0	0	710	712	334	291	320	70	137	159	165	1,386	1,228	903
PDLs/Gross Loans (%)	1.14	1.10	1.41	0.80	1.09	1.54	2.38	2.38	2.55	1.39	1.92	2.86	1.51	1.63	2.14
Restructured Loans/Gross Loans (%)	0.87	1.11	1.95	1.05	1.86	3.21	3.71	5.43	4.95	2.41	4.89	7.02	1.58	2.45	4.13
Loan Loss Reserves /PDLs (%)	291	311	327	313	274	267	266	286	202	268	235	176	250	251	235
Non-interest expense/Margin (%)	36	39	40	41	48	47	50	56	61	52	53	56	46	51	52
ROAE (%)	33.5	32.1	29.7	30.9	25.0	27.8	31.3	23.8	10.6	33.5	27.3	22.1	28.5	23.9	22.2
ROAA (%)	2.8	2.7	2.6	2.6	2.2	2.8	3.1	2.0	0.8	2.8	2.3	1.9	2.6	2.2	2.2
Local Currency Liquidity (%)	31.3	33.9	50.5	50.1	56.9	45.2	52.1	51.1	33.7	31.8	30.5	22.8	40.6	43.1	38.6
Foreign Currency Liquidity (%)	39.2	37.8	53.5	45.8	52.0	57.8	38.1	44.1	25.6	38.5	51.6	43.9	40.7	45.0	49.2
Regulatory BIS ratio (%) ^a	11.2	11.3	12.0	11.7	11.8	11.0	11.8	15.1	12.1	11.2	11.8	12.1	11.9	12.5	12.0

^aBIS ratio as of Aug/07
Source: SBS. Unconsolidated.

recurring trade services fees. Non-credit fees are also diversified, with significant contributions from account services, credit/debit card commissions, transfers and collections, corporate finance advisory, fund management and securities brokerage. This non-interest revenue offsets the increased interest expense and improves the bank's resistance to margin pressures.

Although the bank's time deposits market share has decreased, an increasingly important medium-long term funding, including subordinated debt, has contributed to increase Interest Expense in absolute (+28% yoy at September 2007, +31% in 2006) and relative terms (from 3.05% to 3.55% of average earning assets since December 2006). The competitive environment limits active interest rates and as a result, the bank's margin is lower than in 2005 although it appears stable into 2007. This is somewhat offset by non-interest income and non-recurring revenues arising from recoveries.

Going forward, growth in the (retail) loan portfolio should remain strong - albeit at a lower pace - and continue supporting net interest revenues while non-interest revenues maintain their contribution.

Non-Interest Expenses: Personnel expenses increased 15% in 2006 in line with the bank's expansion; the trend is maintained into 2007 as personnel expenses grow 13% yoy at September 2007. General and administrative expenses increased 25% in 2006 and 15% yoy at September 2007; most of the increase is due to important investments in marketing as the bank aggressively targets the retail market. Other non-interest expenses remained fairly flat in 2007. Continental's cost structure benefits from the support and economies of scale that the integrated operation within BBVA brings. Some processes are carried out in a centralized hub in Mexico and, best practices and efficiency initiatives cross-fertilize BBVA's different subsidiaries in the region. As a result, overall efficiency shows a positive trend as costs have significantly decreased from 53% of revenues at December 2005 to 39% at September 2007; Continental is by far and large, the most efficient large Peruvian bank and, the management acknowledges that this would not be possible without BBVA's support. Going forward, general and administrative expenses should increase slightly as the bank continues to grow; efficiency should suffer more from a contraction of margins than from increased costs, but it is likely to remain below 50% in the next few years.

Loan Loss and Other Provisions: Loan loss provisions decreased in 2006 to PEN32m but increased significantly in 2007 reaching PEN107m at September. This change reflects both the size and the mix shift in Continental's loan portfolio as it grew rapidly and largely driven by growth in the retail bank; besides, it also reflects the management's desire to maintain adequate coverage levels. Historically, after the high levels following the 2001 crisis, provisions have consumed between 5% and 18% of profits before provisions and taxes. After bottoming in 2006 at about 4%, the ratio is back to 14% in 2007 and should remain at that level into 2008. Increased loan volume and relatively stable margins should provide the revenue cushion to absorb this increase.

Prospects: Driven by continued portfolio growth, albeit at a lower pace, results into 2008 should continue strong. Retail banking should maintain its dynamic growth while corporate banking should benefit from expansion oriented to the local market. Provisions should continue rising as the loan mix shift continues and the portfolio matures; margins should remain stable in the short run although pressures in the retail banking area may appear when growth slows and as new entrants seek to acquire market share. Overall, increased volume should allow Continental to maintain a strong performance with ROE in the mid-twenties and ROA in the 2%-2.5% range.

- Asset quality is good and stable
- Loans grow across all business lines, but will be driven by Retail
- Concentration and diversification improve thanks to strong portfolio growth

Risks

Continental's principal risk is the credit risk inherent in its loan and securities portfolios. It also faces market risk, as well as liquidity and operational risks. The bank is fully integrated within BBVA's risk management structure and thoroughly applies its risk management policies. Risk management resides in a centralized area independent of the units where the risk is generated; this area oversees credit exposure to Corporate, Middle Market and Retail customers, reports directly to the CEO and has a matrix reporting to corporate risk management (BBVA). Operational and market risks are also overseen by the risk management area.

Credit Risk: Credit authority is delegated to credit committees where individual credit officers - as opposed to positions - are entitled to approve credit within limits set according to their background, training and expertise and, considering customer risk rating, the transaction structure and market requirements. In a typical branch, the credit committee will comprise the Branch Manager, the assistant branch manager and the account manager (or relationship manager). Transactions over \$8m and loans to local subsidiaries of global corporations that imply assuming country risk must be approved by BBVA Spain.

Continental manages credit risk of multi-national entities in a consolidated manner through the BBVA network. A unit close to the customer headquarters manages the whole relationship and coordinates lending and other services with all the regions/banks involved. Corporate and middle market credit initiation process is clearly structured as the bank prepares industry studies for key economic sectors and derives credit criteria from these analyses. After passing initial filters (industry, size, AML, etc.), credits are analyzed by the line unit using rating/scoring models for loans below \$2.8m (typically SMEs/micro-credit) and using rating models above that limit. Internal risk ratings follow BBVA guidelines, are more stringent than those required by the bank regulator and drive the allocation of loan loss reserves. They are assigned initially by the account officers and reviewed periodically by internal Audit. An independent risk management team verifies that rating/ scoring tools are adequately used and that credit policies are fully applied. The outcome of such verification is considered to delegate credit authority.

Credits granted in the retail bank are mostly to individuals (there is a little microcredit portion) that are either mortgages or unsecured consumer loans and credit cards; mortgages account for roughly 35% of the retail portfolio at September 2007. Mortgages can go up to a maximum of 100% of the independently appraised value of the collateral, with debt service limited to up to 30% of verified income levels. The bank's pitch product is "Casa 120", a mortgage loan that finances up to 100% of the

home value plus 20% to furnish it. According to the management, this product brings customers to the bank but is not widely taken hence the overall loan to value of the mortgage portfolio is below 100% (approximately 80%). Lending to individuals is concentrated among the higher income segments of the population. Loan growth has been steady and accelerating since 2004, with total loans growing 34% in 2005, 36% in 2006 and 33% yoy at September 2007. Thanks to a continuous marketing effort and

Loan Portfolio

(%)	9/07	12/06	12/05	12/04	12/03
Corporate	25.62	28.16	24.7	23.9	26.3
Middle Market and Institutional	31.78	31.12	34.4	35.1	34.9
Treasury	0.22	0.13	0.7	1.1	0.8
Retail Bank	42.38	40.60	39.8	39.7	37.9
SME	15.73	14.24	12.8	11.9	11.1
Mortgage	14.70	15.78	17.7	18.3	18.0
Consumer and Credit Card	11.95	10.58	9.3	9.4	8.8

Source: SBS and ASBANC

innovative products, Continental's loan portfolio has shifted from 62% wholesale/38% retail in December 2003 to 60% wholesale/40% retail in December 2005 and to 58% wholesale/42% retail at September 2007.

While concentrations per industry are difficult to avoid in small economies, Continental has been gradually diversifying its quickly growing portfolio; its largest sector exposure at September 2007 was to manufacturing (25% vs. 34% a year earlier), followed by wholesalers/retailers (16% vs. 23%), transportation and communications (6.0% vs. 7.9%), real estate (4.9% vs. 6.1%), utilities (3.9% vs. 7.2%) and petroleum & mining (3.8% vs. 5.8%). Manufacturing and wholesale/retail are broad categories that include from food preparation to textiles and are well diversified in sub-segments. No other sector comprised more than 4% of credit exposure. Likewise, the borrower concentration has decreased; as of September 2007, the largest 20 exposures were equal to 11% and 122% of total loans and contingencies and total equity, respectively (21% and 128% at year-end 2005); all of the top 20 exposures are classified in the best risk category. Rapid growth in the retail bank should continue diminishing concentration going forward.

Related party lending, defined as lending to shareholders with more than 4% of equity, the companies they control, and to employees, also decreased to less than 1% of the total loan portfolio and about 8.5% of the equity at September 2007 (1.46% of loans and contingencies, about 11% of equity at December 2005). It is important to note that about 38% of that exposure is to related financial services' subsidiaries or affiliates.

As most Peruvian banks, Continental's balance sheet is highly dollarized; Dollar denominated loans dominate the corporate portfolio, most are extended as either trade finance or dollar loans to borrowers with dollar cash flows; they also dominate the mortgage and auto finance portfolios of the Retail bank, where the great bulk of the borrowers are not dollar generators. In order to decrease its credit exposure in dollars to non-dollar-generating debtors Continental encourages loans in local currency by introducing new products and penalizing dollar loans with a 50bp additional cost to the extending unit. Accordingly, the USD/PEN proportion of the loan portfolio has improved from 75%/25% as of Dec/03 to 63%/37% as of Sep/06 and to 52%/48% at September 2007; the management expects to further decrease the Dollar portfolio but progress should be slower going forward. On the other hand, Peruvian regulation requires that banks evaluate this risk, with capital allocations required where the borrower's exchange risk is not well controlled; Continental developed an in-house risk assessment model to rate debtors' vulnerability in case of a devaluation.

Loan Loss Experience and Reserves: Asset quality at Continental has been improving steadily over recent years as a result of concerted recovery efforts, improved portfolio/risk management processes and thanks to the positive economic environment; ratios have also seen the benefits of rapid portfolio growth. The level of past due loans ("Impaired" in the spreadsheet) fell from 1.43% of gross loans at December 2005 to 1.11% at December 2006 and remains flat into 2007 reaching 1.14% at September. Moreover, restructured loans continue decreasing in absolute and relative terms; they amount to 0.84% of Gross loans at September 2007 vs. 1.82% at December 2005.

Portfolio quality

(%)	9/30/07	12/31/06	12/31/05	12/31/04
A: Normal	95.71	95.44	92.29	89.83
B: Pot.Prob.	1.86	2.06	4.09	4.95
C: Substandard	0.82	0.68	0.90	1.40
D: Doubtful	0.81	0.87	1.10	0.77
E: Loss	0.80	0.95	1.62	3.05
C-E/Total Loans	2.43	2.50	3.62	5.22

Reserves covered 296% of past-due loans at September 2007 and have consistently been

about 300% since 2004. The more stringent ratio of reserves to past-due and restructured loans improved to 170% at September 2007, up from 143% at December 2005. These coverage levels are considered adequate by Fitch, given the level of historic losses, the good portfolio quality and positive economic prospects. Continued growth should further reduce restructured loans in absolute terms, although past due loans relative to the portfolio may rise as the loan mix continues to shift towards more retail and SME lending; margins in this segments should remain strong enough to absorb additional provisioning levels.

Other Earning Assets: Other earning assets are largely investments (12% of total assets) and deposits with banks (14%). As of Sep/06 Continental's total investments amount to PEN2.5bln that are largely fixed-income securities. They include PEN1.8bln of short term Central Bank CDs, up from PEN529m a year earlier, due to Continental's role as market maker for these liquidity instruments. Besides, the bank holds PEN620m of Peruvian Sovereign Bonds (down from PEN897m) and PEN 22m of public companies' bonds (down from PEN91m). Exposure to sovereign risk (mostly Peruvian) totaled 0.36 times equity as of September 2007 (down from 0.7 times a year earlier), excluding short-term CDs issued by the Central Bank.

Market Risk: Continental's primary market risks are interest rate risk and foreign exchange risk; it also faces liquidity risk. Decisions affecting the management of these risks are made by the ALCO, which is comprised of eleven members including the CEO, the CFO, the Risk Manager, the Treasurer and the heads of each business unit. An ALCO meets monthly, while tactical day-to-day decisions are made by the Financial Management area in conjunction with the Treasurer.

Continental uses various tools to measure, control and monitor market risk, including an internal VAR model, sensitivity limits, and stop loss limits by product and risk type. VAR is calculated at a 99% confidence level for a ten-day holding period using a historical data base of 252 days. Additionally, the bank periodically performs backtests and stress-tests to validate the accuracy and sufficiency of these tools. The VAR Limit is set at PEN62.6m or about 3.5% of the capital since March 2007 (the previous limit was PEN51.2m or 3.25% of the capital), which Fitch believes conservative. Average VAR was PEN13.2m in 1H07, with peak VAR at PEN18.1m due mainly to the interest rate volatility during 1Q07. The objective of the bank is to maintain Market Risk exposure and the associated VAR limits stable. Tenor mismatches between assets and liabilities are common to the region, given largely short-term deposit bases. In the case of Continental, as of September 2007, 69% of its deposits and liabilities mature within one year compared to only 45% of loans. The bank uses three models (regulatory, internal, corporate) to assess the earnings at risk due to existing gaps and estimates, as of September 2007, that a 100bp move in interest rates would not result in a gain or loss of more than 2.8% of regulatory net worth (the legal limit is 5%).

Liquidity remains ample although somewhat lower than at December 2006. Liquidity ratio (liquid assets to deposits and money market funding) has decreased to about 21% at September 2007 after being largely above 25% in the past. The growth in loans, the increase in long tenor mortgages (15 years) and the voluntary decrease in market share in time deposits has impacted ratios. Nevertheless, Continental comfortably complies with regulatory liquidity limits (20% in US\$, 8% in PEN) and the expanded liquidity ratio (including marketable securities, largely short term Central Bank CDs) shows an improvement when compared to its value at September 2006. Going forward, liquidity should remain stable as the bank gradually improves its asset/ liability matching by securitizing its mortgage portfolio.

Basel II/Operational Risk: Operating Risk is actively managed since 2001, following guidelines and policies established by BBVA and applied globally. As a result, Continental is more advanced than its local peers in measuring and managing operational risk. This process should allow the bank to go beyond the Standard Approach to Operating Risk and achieve the corporate goal of using an advanced model. Under SBS direction, Peruvian banks have completed five impact studies modeled after QIS 5 based on the alternative standardized model and on foundation IRB models. The impact in terms of capital is estimated at 8%–9% of equity but no firm date has yet been set for implementation of Basel II guidelines.

- Continental has a relatively costlier funding base
- Borrowings and sub-debt are increasingly important
- Growth pressures capital ratios

Funding and Capital

Funding: Given its business strategy, Continental's deposit base - although increasing - has somewhat trailed the growth rate of its peers; the bank lost market share in deposits passing from 25.5% at December 2005 to 22% at September 2007; the relative decrease is mainly due to the relative reduction of costly time deposits. Time deposits represented 61% of total funding as of Dec/2002 and gradually decreased to 54% as of Dec/05 and to about 41% at September 2007. Accordingly, Continental's funding saw a reduction of deposit concentration; the top 20 depositors account for about 23% of total deposits at September 2007, versus 25% at June 2006 and 33% at December 2005. Moreover, the bank is perceived as a safe-heaven in times of stress given its strength and the importance of its key stakeholder. Borrowed funds have significantly increased since 2005 (roughly a PEN1bln increase on a PEN240m base) hence contributing to a relatively higher cost of funds but also, responding to the bank's need to better match its long term assets.

Capital: Continental's capital is mostly Tier I, unencumbered and growing steadily albeit at a lower pace than assets; strong loan portfolio growth resumed in 2007 putting additional pressure on Continental's capital ratios. The bank's management has efficiency goals that call for relatively low capital and Continental historically showed higher local operating leverage than most of its local peers. Peruvian banks report bank-only risk-adjusted leverage ratios (risk-weighted assets/regulatory capital) and the regulatory limit is 11 times (equivalent to a 9.1% BIS ratio); regulatory capital deducts 100% of investments in subsidiaries, and no breakdown between Tier I and Tier II is provided. Continental's leverage ratio increased from 6.9x (equivalent to a 14.5% BIS ratio) at FY04 to 8.3x at FY05 (12.0%) and to 8.8x at FY06 (11.3%) but improved to 8.3x (12.1% BIS) at September 2007 thanks to a PEN218m issue of subordinated debt that is considered capital by local regulators. In Fitch's view, as this subordinated debt does not have a deferral feature, it receives no equity credit; the adjusted leverage ratio would be 9.5x (10.5% BIS). Dividend policy calls for a distribution of 60% of the earnings to Continental's shareholders; strong growth, recurring revenues and, ample reserve coverage have historically helped the bank to generate the capital it needs to operate below local regulatory maximums. Plans for capital/ funding growth in the future involve raising new subordinated debt including long term loans from multilaterals. In spite of the relatively tight capital ratios, strong results, good portfolio quality coupled with adequate loan loss coverage, as well as the support of its parent BBVA, allow Continental to sustain its place among similarly rated banks.

Balance Sheet Analysis – Banco Continental, SA

	9/30/2007				12/31/2006		12/31/2005		12/31/2004	
	Nine Months – 3rd Quarter		As % of Assets Original	Average PENm Original	Year End PENm Original	As % of Assets Original	Year End PENm Original	As % of Assets Original	Year End PENm Original	As % of Assets Original
	USDm Original	PENm Original								
A. Loans										
1. Customer	4,890.8	15,332.6	68.25	12,201.0	9,069.3	48.78	7,454.1	40.89	5,738.6	41.65
2. Other	NA	NA	—	NA	1,967.8	10.58	789.9	4.33	580.8	4.22
3. Leased Assets	NA	NA	—	NA	1,461.3	7.86	938.1	5.15	484.7	3.52
4. Restructured	41.9	131.5	0.59	137.8	144.0	0.77	173.2	0.95	218.7	1.59
5. Impaired	57.1	178.9	0.80	160.7	142.4	0.77	135.7	0.74	155.7	1.13
6. (Loan Loss Reserves)	168.8	529.1	2.36	486.2	443.3	2.38	443.5	2.43	451.1	3.27
Total A	4,821.0	15,113.9	67.28	13,727.7	12,341.5	66.37	9,047.5	49.64	6,727.4	48.83
B. Other Earning Assets										
1. Deposits with Banks	1,026.6	3,218.3	14.33	3,263.1	3,307.9	17.79	4,997.2	27.42	2,905.0	21.09
2. Marketable Securities	806.3	2,527.9	11.25	2,252.5	1,977.0	10.63	3,504.3	19.23	3,545.8	25.74
3. Other Investments	31.7	99.4	0.44	NA	NA	—	4.8	0.03	4.8	0.03
4. Equity Investments	NA	NA	—	NA	NA	—	NA	—	NA	—
Total B	1,864.6	5,845.6	26.02	5,565.3	5,284.9	28.42	8,506.3	46.67	6,455.6	46.86
C. Total Earning Assets (A+B)	6,685.6	20,959.5	93.30	19,293.0	17,626.4	94.80	17,553.8	96.30	13,183.0	95.69
D. Fixed Assets	88.8	278.5	1.24	275.5	272.4	1.46	262.1	1.44	249.0	1.81
E. Non-Earning Assets										
1. Cash and Due from Banks	185.5	581.6	2.59	370.6	159.5	0.86	96.0	0.53	62.8	0.46
2. Other	206.0	645.7	2.87	590.7	535.7	2.88	315.9	1.73	282.1	2.05
F. Total Assets	7,166.0	22,465.3	100.00	20,529.7	18,594.0	100.00	18,227.8	100.00	13,776.9	100.00
G. Deposits and Money Market Funding										
1. Demand	1,322.1	4,144.7	18.45	3,550.6	2,956.4	15.90	2,591.8	14.22	2,156.8	15.66
2. Savings	987.3	3,095.2	13.78	2,987.1	2,879.1	15.48	2,459.5	13.49	2,017.1	14.64
3. Time	2,686.1	8,420.9	37.48	7,984.0	7,547.0	40.59	9,018.3	49.48	7,269.8	52.77
4. Interbank	597.9	1,874.5	8.34	1,793.9	1,713.2	9.21	1,217.2	6.68	230.8	1.68
5. Other	176.4	552.9	2.46	690.7	828.5	4.46	804.5	4.41	381.2	2.77
Total G	5,769.8	18,088.2	80.52	17,006.2	15,924.2	85.64	16,091.3	88.28	12,055.7	87.51
H. Other Funding										
1. Other Borrowings	392.0	1,228.9	5.47	792.5	356.1	1.92	239.6	1.31	161.6	1.17
2. Subordinated and Convertible Debt	69.5	217.9	0.97	NA	NA	—	NA	—	NA	—
3. Hybrid Capital	NA	NA	-	NA	NA	—	NA	—	NA	—
I. Other (Non-int. bearing)	355.8	1,115.4	4.96	859.3	603.1	3.24	392.9	2.16	247.9	1.80
L. Equity										
1. Preference Shares	NA	NA	—	NA	NA	—	NA	—	NA	—
2. Common Equity	578.9	1,814.9	8.08	1,762.8	1,710.6	9.20	1,504.0	8.25	1,311.7	9.52
Total L	578.9	1,814.9	8.08	1,762.8	1,710.6	9.20	1,504.0	8.25	1,311.7	9.52
M. Total Liabilities and Equity	7,166.0	22,465.3	100.00	20,529.7	18,594.0	100.00	18,227.8	100.00	13,776.9	100.00
Exchange Rate		USD1 = PEN 3.1350			USD1 = PEN 3.1955		USD1 = PEN 3.4300		USD1 = PEN 3.2790	

Income Statement Analysis — Bank Continental, SA

	9/30/07		12/31/06		12/31/05		12/31/04	
	Income Expenses	As % of Total AV	Income Expenses	As % of Total AV	Income Expenses	As % of Total AV	Income Expenses	As % of Total AV
	PENm Original	Earning Assts Original	PENm Original	Earning Assts Original	PENm Original	Earning Assts Original	PENm Original	Earning Assts Original
1. Interest Received	1,335.6	9.23	1,453.4	8.26	1,354.4	8.81	1,022.9	8.11
2. Interest Paid	513.3	3.55	536.3	3.05	409.1	2.66	211.0	1.67
3. Net Interest Revenue	822.3	5.68	917.1	5.21	945.3	6.15	811.9	6.43
4. Other Operating Income	364.2	2.52	380.4	2.16	189.4	1.23	80.0	0.63
5. Provision for loan losses	106.7	0.74	31.5	0.18	41.7	0.27	33.6	0.27
6. Other Provisions	NA	—	NA	—	NA	—	0.2	0.00
7. Personnel Expenses	205.3	1.42	251.9	1.43	219.6	1.43	210.9	1.67
8. Other Non-interest Expenses	262.1	1.81	471.0	2.68	377.1	2.45	305.2	2.42
9. Operating Profit	612.4	4.23	543.1	3.09	496.3	3.23	342.0	2.71
10. Other Non-operating Income	NA	—	162.5	0.92	106.7	0.69	47.4	0.38
11. Extraordinary Items	4.7	0.03	NA	—	NA	—	NA	—
12. Pre-Tax Profit	617.1	4.26	705.6	4.01	603.0	3.92	389.4	3.09
13. Tax	195.7	1.35	217.4	1.24	200.8	1.31	114.9	0.91
14. Inflation Adjustment	NA	—	NA	—	NA	—	(41.1)	(0.33)
15. Net Income	421.4	2.91	488.2	2.78	402.2	2.62	233.4	1.85

Ratio Analysis – Banco Continental, SA

	9/30/07	12/31/06	12/31/05	12/31/04
	Original	Original	Original	Original
I. Profitability Level				
1. Net Income/Equity (av.)	31.87	30.37	28.57	18.77
2. Net Income less Pref. Div./Common Equity (av.)	31.87	30.37	28.57	18.77
3. Net Income /Total Assets (av.)	2.74	2.65	2.51	1.77
4. Operating Profit/Total Assets (av.)	3.98	2.95	3.10	2.59
5. Costs/Income	39.39	55.71	52.59	57.87
6. Costs/Total Assets (av.)	3.04	3.93	3.73	3.91
7. Net Int. Revenue/Total Assets (av.)	5.34	4.98	5.91	6.16
II. Capital Adequacy (Year End)				
1. Internal Capital Generation	31.87	30.37	28.57	18.77
2. Equity/Total Assets	8.08	9.20	8.25	9.52
3. Equity/Loans	12.01	13.86	16.62	19.50
4. Capital/Risks — Tier 1	NA	NA	11.98	14.53
5. Capital/Risks — Total	NA	NA	11.98	14.53
III. Liquidity (Year End)				
1. Liquid Assets/Deposits and Money Mkt Funding	21.01	21.77	31.65	24.62
2. Liquid Assets and Marketable Debt				
Securities/Deposits and Money Market Funding	34.96	21.77	53.28	53.91
3. Loans/Deposits and Money Market Funding	83.56	77.50	56.23	55.80
IV. Asset Quality				
1. Loan Loss Provisions/Gross Loans (av.)	1.00	0.28	0.50	0.50
2. Loan Loss and other Provisions/Profit before Provisions and Taxes	14.74	4.27	6.47	7.99
3. Loan Loss Reserves/Impaired Loans	295.75	311.31	326.82	289.72
4. Loan Loss Reserves/Gross Loans	3.38	3.47	4.67	6.28
5. Gross Impaired Loans/Gross Loans	1.14	1.11	1.43	2.17
6. Restructured Loans/Gross Loans	0.84	1.13	1.82	3.05
7. Net Impaired Loans/Equity	(19.30)	(17.59)	(20.47)	(22.52)
8. Net Charge-offs/Gross Loans (av.)	NA	NA	0.88	0.66

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