

## ANALYSIS

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This Analysis provides an in-depth discussion of assessment(s) for Franklin Templeton Investimentos Brasil and should be read in conjunction with Moody's most recent research and assessment information available on Moody's website.

# Franklin Templeton Investimentos Brasil

São Paulo, Brazil

## Assessment Rationale

### Assessment: MQ1 (Excellent)

Moody's assessment of Franklin Templeton Investimentos Brasil (FTIB) investment manager quality is MQ1 (Excellent). FTIB is a Brazilian domiciled asset management company with BRL2.2 billion (approximately US\$0.7 billion) of assets under management as of 30 June 2015. The MQ1 assessment reflects Moody's view of the asset manager's excellent management characteristics.

The MQ1 assessment is primarily based on: (i) support and oversight of its ultimate parent, Franklin Resources, Inc. (A1, stable), (ii) the company's disciplined and process-oriented investment methodologies, (iii) strong fiduciary culture and established risk management procedures, (iv) the high level of expertise and qualifications of its professionals, and (v) the solid risk-adjusted performance of its funds. The challenges ahead of FTIB are: (i) growth considering the competitive landscape, (ii) improving its multimarket funds' risk-adjusted performance, and (iii) diversification of its distribution channels.

## Recent Developments

In the first half of 2015, FTIB experienced BRL427 million of outflows. Flows for the asset management industry have been weak, given elevated volatility and slowdown of the economy. That said, the company has experienced volatile growth in assets under management over the years.

FTIB continues to present solid risk-adjusted performance in most categories of funds. In light of recent regulations that increased flexibility for local investors to invest abroad, the Brazilian sub will benefit from the strong franchise of Franklin Resources, Inc., which provides it with a competitive advantage with respect to product offerings and extensive international knowledge.

## Asset Manager Overview

EXHIBIT 1

### Asset Management Entity

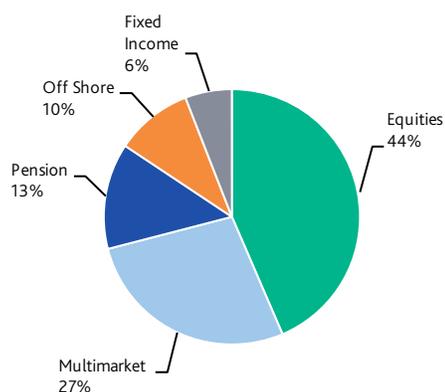
Name	Franklin Templeton Investimentos Brasil
Commencement of Operations	1997
Moody's Assessment	<b>MQ1</b>
Assets Under Management (June/15)	BRL2.2 Billion (US\$0.7 Billion) 72 <sup>nd</sup> largest Manager in the country (37th independent manager, 0.1% market share <sup>1</sup> )
Headcount	30 (17 directly involved in investment management activities)

Headquartered in São Paulo, Brazil, FTIB falls under the umbrella of Franklin Resources, Inc. (A1/Stable). Globally, the group manages approximately US\$866.5 billion in assets as of 30 June 2015. Franklin Templeton initiated its operations in Brazil in 1997, through a joint venture with Banco Bradesco (Bank deposit rating Baa3/Stable), under the name Bradesco Templeton Asset Management. In 2006, Franklin Resources, Inc. acquired Bradesco's share and established FTIB in Brasil as an independent asset management company, expanding its investment strategies and product offerings.

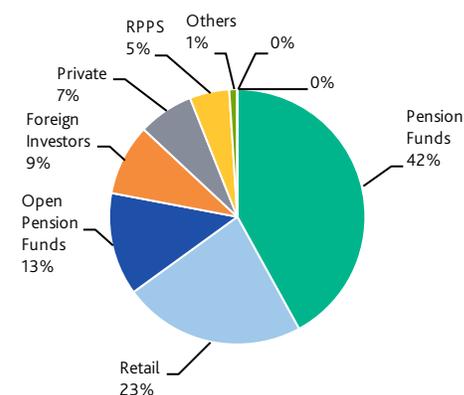
EXHIBIT 2

### Assets Under Management

#### Fund Mix



#### Investors Mix



Source: ANBIMA and Investidor Institucional (Jun/2015)

## Factor 1 – Investment Management Activities

**Investment Methodologies:** We consider Franklin Templeton Investimentos Brasil's investment identification process, the quality of its asset allocation processes as well as its capacity to match a fund's objective with an investment strategy as positive factors when evaluating the company's investment decision process. For its equity funds, FTIB relies on an intensive bottom-up analytical approach, focusing on companies' fundamentals and uses several valuation models, including Discounted Cash Flow (DCF), multiples and sensitivity analysis to identify investment opportunities, seeking stocks with attractive upside potential and currently mispriced relative to their intrinsic values. The analysis is also supported by proprietary tools that evaluate competitive advantage, profitability, and management quality of target companies. For its fixed income and multimarket funds, FTIB evaluates local and global economic and political environments, and benefits from the group's global presence and expertise, as it exchanges information with other teams worldwide. The investment team establishes a

<sup>1</sup> The independent asset managers are considered those not directly related to a financial institution.

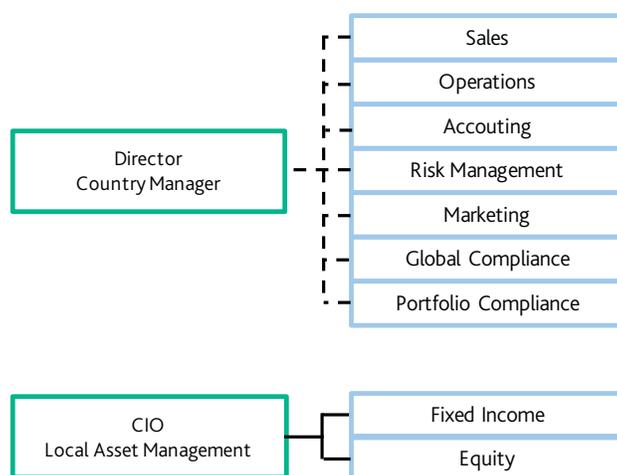
This publication does not announce a credit rating action. For any credit ratings referenced in this publication, please see the ratings tab on the issuer/entity page on [www.moodys.com](http://www.moodys.com) for the most updated credit rating action information and rating history.

macroeconomic scenario and seeks mispriced assets into different strategies (e.g. yield curve, foreign exchange, inflation). Investment decisions are made within committees (e.g. investment, equity, etc.), which are generally comprised of directors, portfolio managers and analysts. Risk management is an integral part of FTIB's investment management activities. The risk management team consistently monitors the set of guidelines and exposure limits, considering value-at-risk (VaR), stress test and liquidity risk of its funds.

**Investment Infrastructure:** FTIB has an excellent investment infrastructure, with real time portfolio management, risk controls and compliance systems. The firm has been continuously investing to upgrade its investment technology, compliance as well as back-office systems. We consider that FTIB has a very low exposure to business interruption risk.

**Organizational Structure:** FTIB's asset management area is comprised of 30 employees, 17 of which are directly involved in investment management activities. The management team has strong professional and educational credentials. The well-balanced organizational structure support the Brazilian subsidiary's operations. Features include independent functions and well-developed risk management and compliance activities. In addition to reporting to FTIB's Country Manager, the local investment, risk, compliance and operations officers maintain independent reporting lines to equivalent global officers at Franklin Resources, Inc., which increases managerial independence and enhances FTIBs access to Franklin's global expertise and allowing the Brazilian franchise to effectively replicate Franklin Resource's global standards.

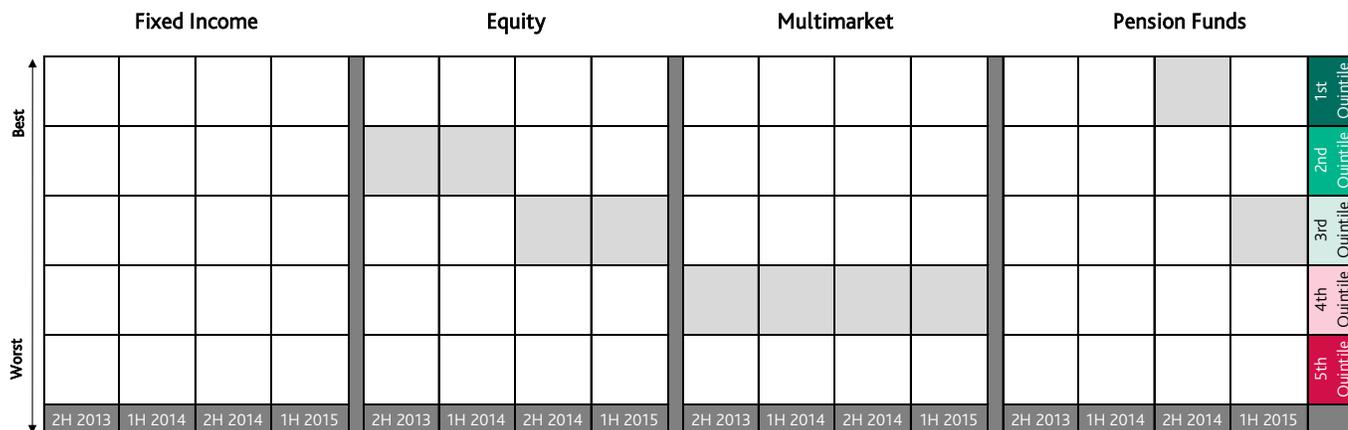
## EXHIBIT 3

**Organization Structure**

Source: Franklin Templeton Investimentos Brasil

**Factor 2 – Investment Results**

**Investment Skill and Risk (\*):** FTIB's Investment Skill and Risk scores are solid and funds have shown good risk-adjusted performance relative to local benchmarks and local peers. In the Equity Segment, the company maintained its position in the 3<sup>rd</sup> quintile. In the Multimarket Segment, the company has consistently maintained its position in the 4<sup>th</sup> quintile. In the Pension Segment, performance has deteriorated in the last semester and the company dropped to the 3<sup>rd</sup> quintile. Overall, Moody's views the company's investment performance to be solid and funds have generally outperformed their respective benchmarks, although they have not consistently outperformed local peers. Moody's expects FTIB's investment performance relative to local peers to improve going forward, given its excellent investment management capabilities.



\* Based on the following metrics and weights: Information Ratio (55%), Merton Skill (17%), Alpha (13%), Sharpe Ratio (7%), beta (5%) and Maximum Drawdown (3%). Further details on Appendix 1.

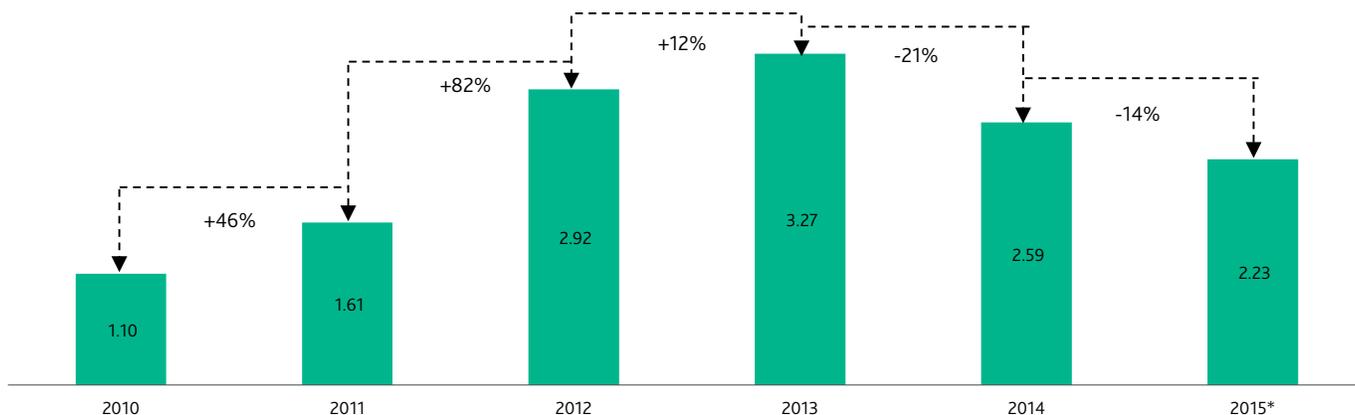
### Factor 3 – Financial Profile

**Revenue and Profitability Levels and Stability:** FTIB's financial profile is constrained given its moderate size, which ultimately results in modest revenues and net income for the company. That said, the company generates a good profit margin. FTIB has a relatively low level of income volatility, which results in stable revenues and profit.

**Corporate Organization:** Franklin Templeton Investimentos Brasil benefits from the support provided by its ultimate parent, Franklin Resources, Inc.. The support results in strong capacity to finance the current operations of FTIB as well as sustain its future business endeavors and investment needs.

**Assets Under Management:** Franklin Templeton Investimentos Brasil has a relatively diversified product offering, with multimarket and equities being the main products. Also, the company has a diversified client base, composed of pension funds, retail, foreign and private investors. Moody's notes that FTIB has experienced volatile growth in assets under management over the years and has yet to restore its asset base which peaked in 2013.

EXHIBIT 4  
AUM (BRL Billion) – Franklin Templeton Investimentos Brasil



Source: Franklin Templeton Investimentos Brasil. (jun/2015)

## Factor 4 – Client Servicing

**Retention and Replacement of Clientele:** FTIB exhibits relatively strong client retention, with low rates of client turnover, albeit net outflows in 2010 and 2014 negatively impacted these metrics. The company's replacement rate, measured by the percentage of assets lost that are being replaced by new subscriptions from investors, is relatively solid.

## Other Considerations

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### What Could Change the Assessment – Down

The company's funds risk-adjusted investment performance deteriorates significantly – both relative to peers and local benchmarks

The funds experience a substantial decrease in assets under management

There are significant deviations in the firm's investment processes, which increase exposure to operational risks

## Appendix 1: Investment Performance Measurement

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### 1. Fund Sampling

The SI-ANBID database includes a large number of active mutual funds (about 14,400), and we selected a sample funds that met some pre-determined criteria for use in our historical performance analysis:

1. **Fund Segments:** narrowing the sample down to the most popular mutual fund segments among investors, we selected the following segments: Equity, Fixed Income, Multimarket ("Multimercado") and Pension.
2. **Length of Existence:** we only considered mutual funds that have traded for at least three years.
3. **Fund Size:** only funds with a minimum of BRL25 million in total assets as of June 30th, 2015 were included in the sample.

After filtering, we came up with a sample of 1,228 funds.

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### 2. Performance Measurement

We analyze the historical risk-adjusted return performance achieved by individual products or representative portfolios of like funds across assets, offered by the firm. The analysis, covers a three-year period. Results are aggregated, compared to a universe of similarly managed products, and scored on the basis of quintile ranks. The firm's ranking in each segment is the average score of all performance metrics weighted by AUM.

In the case of risk-adjusted performance results, we compute the median three-year Sharpe Ratio using monthly total rates of return for a representative sample of portfolios. The median Sharpe Ratio is then compared to a distribution of Sharpe Ratios stratified into quintiles for local peers.

In a similar fashion, we extend this form of analysis to the other key risk measures including Maximum Drawdown, Beta and  $R^2$ . To this, we add measures of manager skill, including such key measures as Alpha, the Information Ratio and the Merton Skill Measure.

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#### Basic Measures Used to Evaluate Investment Results, Risk, and Manager Skill:

**Alpha** measures the difference between a fund's actual returns and its expected performance, given its level of risk (as measured by beta). It can be used to calculate the "skill" of a fund manager.

**Beta** is a measure of a fund's volatility relative to the market, which for stocks in the US, for example, may be represented by the S&P 500 Index.

The **Sharpe Ratio** measures the fund's risk-adjusted return. It is the portfolio's average return in excess of the risk-free rate divided by the portfolio's standard deviation.

$R^2$ , or the R-squared value, is the fraction of variance in the dependent variable that is explained by variance in the independent variable.

The **Information Ratio** is the ratio of a manager's excess return (Alpha) divided by the standard deviation of that excess return. It is a measure of the value added by an active manager.

The **Maximum Drawdown** is the worst period of "peak-to-valley" performance for a fund or other investment vehicle, regardless of whether or not the drawdown consists of consecutive months of negative performance.

The **Merton Skill Measure** is a returns-based measure of market timing skills that includes a ratio of unsuccessful to successful "down market" calls.

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