MOODY'S
INVESTORS SERVICE

Credit Opinion: Banco de Bogota S.A.

Global Credit Research - 21 Dec 2015

Bogota, Colombia

Ratings

Category	**Moody's Rating**
Outlook	Stable
Bank Deposits	Baa2/P-2
Baseline Credit Assessment	baa3
Adjusted Baseline Credit Assessment	baa3
Counterparty Risk Assessment	Baa1(cr)/P-2(cr)
Senior Unsecured	Baa2
Subordinate	Ba1
Parent: Grupo Aval Acciones y Valores S.A.	
Outlook	Stable
Issuer Rating	Ba1
ST Issuer Rating	NP
BAC International Bank, Inc	
Outlook	Stable
Bank Deposits	Baa3/P-3
Baseline Credit Assessment	baa3
Adjusted Baseline Credit Assessment	baa3
Counterparty Risk Assessment	Baa2(cr)/P-2(cr)

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Key Indicators

Banco de Bogota S.A. (Consolidated Financials)[1]

	[2]**9-15**	[3]**12-14**	[3]**12-13**	[3]**12-12**	[3]**12-11**	**Avg.**
Total Assets (COP billion)	**146,444.3**	**118,107.3**	**100,402.0**	**80,506.4**	**68,809.6**	**--**
Total Assets (USD million)	**47,437.7**	**49,698.4**	**51,968.1**	**45,561.0**	**35,496.1**	**--**
Tangible Common Equity (COP billion)	**5,723.9**	**6,748.1**	**5,342.2**	**4,573.5**	**3,539.4**	**--**
Tangible Common Equity (USD million)	**1,854.1**	**2,839.6**	**2,765.1**	**2,588.3**	**1,825.8**	**--**
Problem Loans / Gross Loans (%)	**1.6**	**1.4**	**1.3**	**1.2**	**1.3**	[4]**1.6**
Tangible Common Equity / Risk Weighted Assets (%)	**4.5**	**6.5**	**6.0**	**6.3**	**5.6**	[5]**4.5**
Problem Loans / (Tangible Common Equity + Loan Loss Reserve) (%)	**19.2**	**11.2**	**11.0**	**9.6**	**11.6**	[4]**19.2**
Net Interest Margin (%)	**4.2**	**4.6**	**5.1**	**5.3**	**4.0**	[4]**4.2**
PPI / Average RWA (%)	**4.3**	**3.9**	**4.5**	**4.2**	**5.1**	[5]**4.3**
Net Income / Tangible Assets (%)	**1.9**	**1.7**	**1.4**	**1.7**	**1.7**	[4]**1.9**
Cost / Income Ratio (%)	**49.3**	**60.6**	**58.6**	**60.2**	**55.9**	[4]**49.3**
Market Funds / Tangible Banking Assets (%)	**25.5**	**17.2**	**17.1**	**17.8**	**16.9**	[4]**25.5**

Liquid Banking Assets / Tangible Banking Assets (%)	**17.5**	**28.2**	**31.6**	**33.5**	**30.7**	[4]**17.5**
Gross loans / Due to customers (%)	**104.2**	**95.9**	**90.7**	**89.0**	**92.2**	[4]**104.2**

Source: Moody's

[1] All figures and ratios are adjusted using Moody's standard adjustments [2] Basel I; IFRS [3] Basel I; LOCAL GAAP [4] IFRS reporting periods have been used for average calculation [5] Basel I & IFRS reporting periods have been used for average calculation

Opinion

SUMMARY RATING RATIONALE

Moody's assigns a baa2 standalone baseline credit assessment (BCA) to Banco de Bogotá S.A. in line with the bank's proactive and institutionalized risk management that ensures low levels of problem loans. Ample financial margins and an efficient cost structure, as well as a stable funding base of core deposits. At the same time, the bank's capitalization compares negatively with regional and global peers, and affects the bank's capacity to absorb losses in the event of stress. Also, the bank's presence in riskier countries in Central America exposes its balance sheet to greater volatility in terms of profitability and asset quality and could test the bank's capitalization going forward.

Moody's also assigns long- and short- term global local currency (GLC) and foreign currency deposit ratings of Baa2 and Prime-2, respectively, a long-term foreign currency senior unsecured debt rating of Baa2 and a foreign currency subordinated debt rating of Ba1 which is one notch below Banco de Bogotá's baa3 BCA, following Moody's notching practices for these types of debt instruments.

Moody's also assigns long- and short-term Counterparty Risk (CR) Assessments of Baa1(cr)/Prime-2(cr) to Banco de Bogotá.

All ratings of Banco de Bogotá have a stable outlook.

Rating Drivers

Low core capitalization levels

Challenging operating environment

Resilient levels of returns underscored by ample margins and an efficient cost structure

Proactive and institutionalized risk management

Moderate Macro Profile

Rating Outlook

All ratings of Banco de Bogotá have a stable outlook.

What Could Change the Rating - Up

A higher rating for the Colombian government (Baa2 stable) would add upward ratings pressure on the bank's local and foreign currency deposit and senior debt ratings.

The bank's BCA of baa3, and its Ba1 subordinate debt rating, may come under positive pressure in the event Banco de Bogotá's capitalization ratio improves materially and sustainably.

What Could Change the Rating - Down

We could lower the standalone BCA if the bank were to experience asset quality problems that could affect its earnings generation and capital levels. An announcement of another major acquisition would prompt further reassessments of the bank's BCA given the bank's already high levels of goodwill, which Moody's deducts from goodwill.

At the same time, downward ratings pressure on Banco de Bogotá's local and foreign currency deposit ratings and foreign currency senior debt ratings is more limited given Moody's assumption of very high government support.

DETAILED RATING CONSIDERATIONS

LOW CAPITALIZATION

Moody's views Banco de Bogotá's capitalization as low. Moody's uses as a measure to gauge capitalization a ratio that seeks to emulate Basel's Common Equity Tier 1 (CET1) ratio, which is tangible common equity (common stock plus retained earnings minus intangibles, which in Banco de Bogotá's case is a sizable amount of goodwill).

Banco de Bogotá's tangible common equity to risk weighted assets (RWAs) of 6.5% as of year-end 2014 is low due to high holdings of goodwill. When incorporating into Banco de Bogotá's TCE its related minority interest, the bank's capitalization increases to 8%.

While as of year-end 2014, the bank's common equity is a high COP11.2 trillion (includes the Nov14 COP1.5 trillion capitalization) versus risk weighted assets of COP104.6 trillion, attributable goodwill represents a high COP4.4 trillion, mainly related to the acquisitions of:

1) BAC (BAC International Bank, Inc. BAC, Baa3/- stable, baa3) from GE (COP2.3 trillion in 2014) in 2010,

2) Banco BAC de Panamá from BBVA (COP749 million in 2014) in 2013,

3) Grupo Financiero Reformador (COP637 million in 2014) in 2013,

4) MegaBanco from the government (COP441 million in 2014) in 2005, and

5) AFP Horizonte from BBVA (COP425 million in 2014) in 2013.

Grupo Aval has raised upwards of COP5 trillion in the last two years, COP2.4 trillion from its shareholders and COP2.6 trillion in the NYSE Euronext, of which 56% was down-streamed to Banco de Bogotá.

Capital Is Low Even When Including Related Minority Interest

Moody's excludes minority interest because this type of capital would not be available to absorb losses at the consolidated level. Minority interest in Banco de Bogotá's case is a substantial COP3.9 trillion (versus common equity of COP11.2 trillion), mainly because of the high capitalization levels of its subsidiaries, but also because Banco de Bogotá only holds a small minority ownership in two nonetheless consolidated subsidiaries, Corficolombiana S.A. (unrated) and AFP Porvenir S.A. (unrated).

Banco de Bogotá consolidates these two entities even though it owns less than 51% in both based on a shareholder agreement. Banco de Bogotá owns 38.2% of Corficolombiana and 46.9% of Porvenir, but adding all related ownerships, Grupo Aval's ownership of these entities adds up to 57.9% of Corficolombiana and 100% of Porvenir.

The 19.8% of Corficolombiana and the 53.1% of Porvenir that is owned by related parties, represents a substantial COP1.6 trillion. These related third parties include sister entities such as Banco de Occidente S.A. (unrated), Banco Popular S.A. (unrated), Banco AV Villas S.A. (unrated) or Porvenir itself.

CHALLENGING OPERATING ENVIRONMENT

Banco de Bogotá has market presence in Colombia and Central America, a macroregion of a GDP of USD588 billion (2014), where it is the second largest bank. The bank's operations are mainly in its home market of Colombia (59% of gross loans), but with substantial presence in Panama, Costa Rica, Guatemala, El Salvador, Honduras and Nicaragua, as well as a small credit card book in Mexico, as of September 2015. Banco de Bogotá entered Central America in 2010 with the acquisition of BAC.

While BAC has provided Banco de Bogotá with ample geographic diversification to several countries with high GDP growth and a low correlation with Colombia, it has also exposed the bank to higher volatility in assets, profitability and capitalization, and dollarization. Central America has higher poverty and inequality indicators, coupled with low and more volatile economic and institutional strength.

Foreign currency exposures will continue to expose the bank's capitalization to fluctuations in the valuation of assets and goodwill.

RESILIENT LEVELS OF RETURNS UNDERSCORED BY AMPLE MARGINS AND AN EFFICIENT COST STRUCTURE

Banco de Bogotá's stable generation of core earnings results from an ample net interest margin (4.6% as of year-end 2014) related to a low cost funding base and a growing and diversified loan portfolio, both closely referenced to the benchmark interest rate and the 90-day CD rate (DTF).

Banco de Bogotá has also successfully integrated BAC, with further beneficial effects on core earnings and their predictability, based on the business diversification that BAC's retail business and uncorrelated operating environments bring to the bank's portfolio.

The bank's profitability is ample and largely in line with that reported prior to acquisitions with net income to tangible banking assets of 1.7%, as of year-end 2014, versus the average 1.6% of the previous three years.

PROACTIVE AND INSTITUTIONALIZED RISK MANAGEMENT

Banco de Bogotá's conservative management and credit policies have resulted in healthy asset quality indicators and delinquency ratios that have traditionally been among the region's lowest. The bank's acquisitions have incorporated higher 90+ days past due loans (PDL or problem loans) but remain well below the 1.5% level.

As of year-end 2014, the bank's PDLs as percentage of gross loans of 1.4% are in line with the bank's average of 1.3% during the previous three years. While we do expect some deterioration going forward, as the economy expands at a slower pace than expected, the effect should be limited by the bank's focus on commercial lending and its geographic diversification. BAC reported an also low 1.2% PDL ratio as of year-end 2014.

Banco de Bogotá has a diversified loan book with 64% of its loans directed to corporate loans and leases, followed by consumer loans with 24% and residential mortgages with 11%, as of September 2015 (excludes loans to employees).

Banco de Bogotá's portfolio nevertheless has high concentrations, measured as top 20 exposures against fully adjusted Tier 1 of 1.8x or against core earnings of 2.4x as of year-end 2014, which could expose the bank to potentially rapid asset quality deterioration, but from very low levels of PDLs. These exposures are expected to increase substantially through the end of the year, as Banco de Bogotá begins to disburse large single ticket loans to infrastructure projects in Colombia.

Banco de Bogotá is ultimately family-owned, which increases Moody's evaluation of the bank's risk profile. However, no major issues in terms of corporate governance have been observed in the bank. The bank's related party loans represent 10.2% of fully adjusted Tier 1 capital, as of year-end 2014.

CORE DEPOSIT FUNDING AND AMPLE LIQUIDITY

Because of its strong core deposit base in all the markets in which it operates, Banco de Bogotá does not rely on either interbank or capital markets funding.

Most of Banco de Bogotá's funding is sourced from customers with deep relations with the bank, in the form of deposits in local currencies, limiting its sensitivity to contagion risks in times of stress or to a negative shift in market sentiment in the event of a sovereign crisis. Banco de Bogotá's deposit-based funding is also diversified between Colombia and Central America. Deposits represent 72.5% of total funding and 98.1% of net loans, as of September 2015.

The bank also maintains ample liquid assets diversified between cash and cash equivalents, Colombian government securities which are rated Baa2 and Central American government securities, rated on average Ba1 in local currency. Liquid assets represent 28.2% of total assets as of year-end 2014.

BANCO DE BOGOTÁ'S RATING IS CONSTRAINED BY A WEIGHTED MACRO PROFILE OF MODERATE

Banco de Bogotá's Macro Profile is Moderate, weighted by the group's loan exposures to Colombia and Central America.

Colombia's Macro Profile is Moderate+ and represents about 60% of the bank's loan book, while its remaining operations are focused in Central America. Central American exposures include Costa Rica (Macro Profile of Moderate-), Panama (Moderate), Guatemala (Weak) and El Salvador (Weak), as well as Honduras and Nicaragua.

Colombia has a robust growth outlook, supported by strong domestic demand, though tempered by the country's low GDP per capita and high inequality. Despite average indicators for government effectiveness, the country benefits from a favorable investment climate and policy predictability. Colombia faces event risk related to its dependence on oil exports as well as ongoing problems with armed insurgencies, which have mounted an increasing number of attacks on its oil pipelines in recent years. Peace negotiations are progressing, albeit slowly.

Notching Considerations

In the absence of a bail-in resolution regime framework in Colombia, as per the "Global Banks" Methodology, under "Guidelines for Rating Junior Bank Obligations", updated in July 2014, we take into account the key features of the bank's outstanding notes. As 'plain vanilla' subordinated debts with no skip mechanisms, these instruments commonly absorb losses only in a liquidation scenario. In those cases, the notching approach for 'plain vanilla' subordinated debt is one notch of subordination risk off the bank's adjusted baseline credit assessment (BCA) of the issuer.

Government Support

We believe there is a very high likelihood of government support for Banco de Bogotá's rated wholesale deposits and senior unsecured debt. This reflects Banco de Bogotá's large market share of deposits in Colombia and hence the material systemic consequences that would result from an unsupported failure. Banco de Bogotá's deposit and senior debt ratings of Baa2 benefit from one notch uplift from government support from the bank's BCA of Baa3.

Foreign Currency Debt Rating

Moody's assigns a Baa2 long-term foreign currency debt rating to Banco de Bogotá's five-year USD600 million senior unsecured notes due 15 January 2017 (coupon of 5%). The assigned rating is based on the bank's local currency deposit rating of Baa1.

Moody's assigns a Ba1 long-term foreign currency subordinate debt rating to the bank's ten-year USD500 million subordinate debt issuance due 19 February 2023 (coupon of 5.375%).

Counterparty Risk Assessments

Banco de Bogotá's long- and short-term CR Assessments are positioned at Baa1(cr)/Prime-2(cr).

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 suffered in the event of default 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 (e.g., swaps), letters of credit, guarantees and liquidity facilities.

The CR Assessment, prior to government support, is positioned one notch above the Adjusted BCA of baa3 and therefore above senior unsecured and deposit ratings, reflecting our view that its probability of default is lower than that of senior unsecured debt and deposits. We believe senior obligations represented by the CR Assessment will be more likely preserved in order to limit contagion, minimize losses and avoid disruption of critical functions.

The CR Assessment also benefits from one notch of systemic support, in line with our support assumptions on deposits and senior unsecured debt. This reflects our view that any support provided by governmental 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, consistent with our belief that governments are likely to maintain such operations as a going-concern in order to reduce contagion and preserve a bank's critical functions.

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 Factors

Banco de Bogota S.A.

Macro Factors	
Weighted Macro Profile	**Moderate**

Financial Profile						
Factor	**Historic Ratio**	**Macro Adjusted Score**	**Credit Trend**	**Assigned Score**	**Key driver #1**	**Key driver #2**
Solvency						
Asset Risk						
Problem Loans / Gross Loans	1.3%	baa1	←→	baa1	Geographical diversification	Geographical diversification
Capital						
TCE / RWA	5.6%	caa2	↑↑	b3	Access to capital	
Profitability						
Net Income / Tangible Assets	1.7%	baa1	←→	a3	Earnings quality	
Combined Solvency Score		ba2		ba1		
Liquidity						
Funding Structure						
Market Funds / Tangible Banking Assets	17.2%	baa3	←→	baa2	Deposit quality	
Liquid Resources						
Liquid Banking Assets / Tangible Banking Assets	28.2%	baa3	←→	baa3	Quality of liquid assets	
Combined Liquidity Score		baa3		baa2		

Financial Profile	**baa3**

Qualitative Adjustments	**Adjustment**
Business Diversification	0
Opacity and Complexity	0
Corporate Behavior	0
Total Qualitative Adjustments	**0**

Sovereign or Affiliate constraint	Baa2
Scorecard Calculated BCA range	**baa2 - ba1**
Assigned BCA	**baa3**
Affiliate Support notching	**0**

Adjusted BCA				baa3		

Instrument Class	Loss Given Failure notching	Additional notching	Preliminary Rating Assessment	Government Support notching	Local Currency rating	Foreign Currency rating
Deposits	0	0	baa3	1	Baa2	Baa2
Senior unsecured bank debt	0	0	baa3	1		Baa2
Dated subordinated bank debt	-1	0	ba1	0		Ba1

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