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Research Update:

Banco de Bogota S.A. y Subsidiarias 'BB+/B' Ratings Affirmed; Outlook Remains Stable

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Overview

- Banco de Bogota continues to have a leading position in the Colombian and Central American market, where it participates through BAC International Bank.
- The bank continues to show solid geographic risk diversification that's resulted in stable asset quality metrics, despite recent deterioration in the Colombian banking system.
- We are affirming our long-term 'BB+' and 'B' short-term global issuer credit ratings on the bank. We are also affirming our 'BB+' issue-level rating the bank's senior unsecured debt.
- The stable outlook on BBogota reflects our expectation that the bank will maintain an RAC ratio of around 4.0% over the next two years. This would result from credit growth that'd help it to maintain current capitalization levels and stable asset quality metrics despite challenging economic condition in the region.

Rating Action

On June 12, 2018, S&P Global Ratings affirmed its long-term 'BB+' and short-term 'B' global scale issuer credit ratings on Banco de Bogotá S.A. y Subsidiarias (BBogota). The outlook is stable.

At the same time, we affirmed the 'BB+' issue-level rating on the bank's senior unsecured debt.

Rationale

The issuer credit ratings on BBogota continue to reflect its solid business position, as evidenced by its leading position in Colombia and in Central America through its main subsidiary, BAC International Bank. It also reflects our view of the bank's capital and earnings; we expect a risk-adjusted capital (RAC) ratio of 4.0% for the next 24 months, as well as stable asset quality metrics, supported by its strong geographic diversification. BBogota's funding continues to be supported by its large and stable deposit base, with no significant liquidity needs in the near future. Its stand-alone credit profile (SACP) is 'bb+'.

Our bank criteria use our Banking Industry Country Risk Assessment (BICRA) economic risk and industry risk scores to determine a bank's anchor, the starting point in assigning an issuer credit rating. Our anchor for BBogota is 'bb+', reflecting the weighted average economic risk of '7', given the countries in which the bank has its major loan portfolio exposures--Colombia (55%), Panama (12%), Costa Rica (12%), Guatemala(8%), Honduras (5%), El Salvador (4%), and Nicaragua (4%). The industry risk score for Colombian banks is '5' with a stable trend (see"Banking Industry Country Risk Assessment: Colombia," published Sept. 14, 2017).

Our business position assessment for BBogota continues to reflect its leadership in Colombia and in the Central American countries in which the bank operates through is core subsidiary, BAC International Bank Inc (BB+/Stable/B). As of March 31, 2018, BBogota is the second-largest by assets in Colombia, with a market share of 14.2% by total assets, following Bancolombia (BB+/Stable/B) and Davivienda (BBB-/Stable/A-3), which hold 25.1% and 13.4% of the market in Colombia, respectively. If we consider Grupo Aval (not rated)--, the group is the largest player in the Colombian system with a market share of 26.3%.

BBogota participates in all banking segments; however, it has historically focused on the commercial segment. In fact, this line of business represents around 61% of BBogota's total consolidated loans (including Central America, which exposure represents around 43% of total consolidated loans as of March 2018) Furthermore, it has maintained a leading market position in most Central American countries where it operates, with market shares above 10%. Its presence in Panama should grow at a higher pace for the next few years. BBogota's operating revenues are mainly concentrated in net interest and fee income, providing stability to its profitability metrics. Furthermore, its strong geographic diversification has also supported BBogota's stable revenues due to the solid profitability levels in its Central America operations that represents around 49% of BBogota´s total consolidated operating revenues as of March 31, 2018. For the next 24 months, we expect operating revenues to remain positive, with Central America income hovering between 50%-47% of BBogota's consolidated figures.

Our capital and earnings assessment is supported by our projected RAC ratio of 4.0% on average over the next 24 months. Our assessment includes our view of the bank's quality of earnings, which is mainly made up interest income and fees, and its adequate internal capital generation capacity, which is beneficial the company's dividend policy.

Our financial forecasts also take into consideration our base-case scenario assumptions, which include:

- Colombian GDP growth of 2.5% for 2018 and 2.6% for 2019. Central American economies expand during 2018: Costa Rica by 3.2%, Guatemala by 3.3%, Honduras by 3.7%, El Salvador by 1.4%, and Panama by 5.9%.
- Lower foreign exchange volatility in the next two years of COP3,150 per

$1 in 2018 and 2019;

- No expected additional acquisitions during the next 24 months.
- Consolidated loan portfolio growing on average at about 7.5% in 2018 and 2019;
- Net interest margins (NIMs) gradually increase, reflecting the growing participation of small and medium enterprises (SMEs) and consumer loans within BBogota's consolidated loan portfolio of around 5.6%-5.7%, which would somewhat offset increasing funding costs;
- Profitability levels will be stable during the next 24 months, with core earnings to adjusted assets of 1.7% and an efficiency ratio (measured by non-interest expenses to operating revenues) of 50%. Additionally, we expect credit loss provisions to represent around 20% of operating revenues;
- Nonperforming assets (NPAs) and net charge off (NCO) ratios of about 2.5% and 1.4% respectively, with full reserve coverage.
- An average dividend payout ratio of 50% for the next two years.

The bank's quality of capital remains adequate, given the absence of hybrid capital instruments within our estimated total adjusted capital (TAC). However, goodwill generated by past acquisitions represents an important portion of its total equity (about 30%). Considering the goodwill generated in foreign currency, it is possible to see some volatility in its RAC although this is not our base case scenario. As of March 31, 2018, core earnings to average adjusted assets stood at 1.60% and have averaged 2.2% over the past three fiscal years, which is in line with local and regional peers. In our view, BBogota's profitability levels will be supported by the bank's efforts to improve efficiency during the next two years, coupled with an increase in retail segment loans.

In our view, BBogota's risk position is still adequate, despite economic challenges in Colombia and Central America. The bank's adequate risk diversification in terms of geography, economic sector, and client underpins our assessment. Growth and exposure changes, as well as exposures that are not covered its RAC, were in line with other banks we rate in the region. BBogota's loan portfolio grew by 8.0% during 2017. We believe BBogota's future growth rates will be around average for the Colombian banking system, which we expect to grow around 8% for the same period of time. Finally, in our view, we expect that BBogota will maintain conservative underwriting standards that would allow it to cope with the harsh economic environment through the next 12 months.

Banco de Bogota's loan composition did not change significantly in 2017. The bank's goal is to promote efforts in the consumer and mortgages segments, though we expect little change. As of March 31, 2018, corporate and commercial loans represented the majority of the portfolio, with 59.9%, while consumer loans and mortgage loans represented 27.7% and 12.1%, respectively.

For the next 12-18 months, we expect mortgages and consumer loans to have higher rates because the management wants to gradually increase those exposures through its broad customer base in Central America and Colombia, with an emphasis on strategic products such as credit cards, payroll, and mortgage loans. Its top 20 largest exposures only represented 12.86% of its total consolidated loan portfolio and 118% of its total adjusted capital as of March 31, 2018; this level compares positively against other regional peers that maintained higher levels of concentration.

Banco de Bogota has managed to maintain adequate asset quality performance, despite constant loan growth and a more challenging economic environment in Colombia since the global drop in oil prices. Our NPA ratio stood at 2.47% as of March 2018, with a three year average of 1.72% before 2017. We still consider these levels to be adequate relative to other banks in the region with the same economic risk. As of March 2018, the Colombian banking system had NPAs of 2.6%. Despite pressures on asset quality metrics, the bank has stabilized delinquency levels and has increased reserve coverage, mainly after the implementation of international financial reporting standards (IFRS 9). As of March 2018, reserve coverage represented 160% of total NPAs compared to 128% as of year-end 2017. NPAs should be around 2.5% with full reserve coverage based on our expectations of better origination and conservative underwriting standards. Net charge offs were 1.6% as of March 2018, and we expect them to remain so for the remainder of 2018.

BBogota's funding is in line with the industry norm. Its funding structure is mainly composed of customer deposits (22% are retail deposits), which accounted for 80% of total funding sources as of March 31, 2018. The majority of those deposits are wholesale, especially in Colombia. The remaining 20% are borrowings from banks and interbank funds (12%), bonds (6%), and other (2%). In terms of deposit concentration, its top 20 depositors accounted for around 13.85% of BBogota's total consolidated deposit base as of first quarter 2018, reflecting below average retail deposit participation with respect to other peers in Latin America. The bank's ample deposit base in translates into satisfactory stable funding ratios (SFRs). As of March 31, 2018, its SFR was 106% and had averaged 107% for the past three fiscal years. Given our expected stable funding needs and funding structure for over the next two years, we anticipate that its SFR will remain above 100%, which we view as adequate, and it will continue to compare adequately against the Colombian banking system.

Our liquidity assessment remains adequate, mainly supported by its coverage of short-term wholesale funding with liquid assets and by its comfortable debt maturity profile. Our broad liquid asset to short-term wholesale funding ratio stood at 2.04x as of March 2018 with a three-year average of 2.7x. BBogota's short-term wholesale funding (excluding deposits) is low--representing 8.9% of its funding base--and it's supported by manageable its refinancing risk over the next 12 months. BBogota has above average liquidity ratios that allows it to offset the high participation of wholesale deposits within its deposit bases. The bank's main subsidiary, BAC International Bank, is a highly liquid entity as a consequence of the lack of a lender of last resort in certain Central America countries. Its liquidity management should remain adequate.

Outlook

The stable outlook on BBogota´s reflects our expectation that the bank will maintain its RAC ratio around 4.0% over the next two years as a result of manageable credit growth (around 7.5% in 2018 and 2019), stable asset quality metrics, and a stable dividend payout ratio. We also expect the bank to maintain its solid market position in Colombia, as well as funding and liquidity metrics in line with the system.

Downside scenario

We could lower the ratings if its RAC ratio drops to below 3%. This could happen if it shows higher than expected loan growth rates, weakening asset quality that could pressure internal capital generation capacity, or a higher-than-expected dividend payout ratio that could weigh on its capital base.

Upside scenario

If the bank's RAC ratio in the next 12 months crosses the 5% threshold, we could raise the bank's capital and earnings assessment, which would in turn improve BBogota's SACP, allowing us to raise it to 'bbb-'. This could happen if the bank has higher than expected internal capital generation while maintaining stable asset quality metrics.

Ratings Score Snapshot

Issuer Credit Rating	BB+/Stable/B
SACP	bb+
Anchor	bb+
Business Position	Strong (+1)
Capital and Earnings	Weak (-1)
Risk Position	Adequate (0)
Funding and liquidity	Average and Adequate (0)
Support	0
GRE Support	0
Group Support	0
Government Support	0
Additional Factors	0

Related Criteria

- Criteria - Financial Institutions - General: Risk-Adjusted Capital Framework Methodology, July 20, 2017
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings , April 7, 2017
- Criteria - Financial Institutions - Banks: Bank Hybrid Capital And Nondeferrable Subordinated Debt Methodology And Assumptions, Jan. 29, 2015
- General Criteria: Group Rating Methodology, Nov. 19, 2013
- Criteria - Financial Institutions - Banks: Quantitative Metrics For Rating Banks Globally: Methodology And Assumptions, July 17, 2013
- Criteria - Financial Institutions - Banks: Banks: Rating Methodology And Assumptions, Nov. 9, 2011
- Criteria - Financial Institutions - Banks: Banking Industry Country Risk Assessment Methodology And Assumptions, Nov. 9, 2011
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009

Ratings List

Ratings Affirmed

Banco de Bogota S.A. y Subsidiarias	
Counterparty Credit Rating	BB+/Stable/B
Senior Unsecured	BB+

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. Complete ratings information is available to subscribers of RatingsDirect at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column.