S&P Global
Ratings

RatingsDirect®

Research Update:

Bancolombia, S. A. y Companias Subordinadas Outlook Revised To Positive On Improving Capital; 'BB+/B' Ratings Affirmed

May 23, 2019

PRIMARY CREDIT ANALYST

Fernando Staines
Mexico City
(52) 55-5081-4411
fernando.staines@spglobal.com

SECONDARY CONTACT

Ricardo Grisi
Mexico City
(52) 55-5081-4494
ricardo.grisi@spglobal.com

Overview

- We're revising the outlook on Bancolombia to positive from stable, reflecting its strengthening risk-adjusted capital (RAC) ratio driven by its internal capital accumulation coupled with reduced risks in economies in which the bank operates.
- Although the bank's nonperforming assets (NPAs) and credit losses increased in the past two years due to economic slowdown and some specific projects such as Electricaribe and Ruta del Sol, we consider its asset quality metrics to be in line with the rest of the Colombian banking system.
- We're affirming our 'BB+/B' issuer credit ratings on the bank and on its core subsidiaries, Bancolombia Panama and Banistmo S.A. We're also affirming our 'BB+' issue-level rating on Banistmo's $500 million senior unsecured notes due 2022
- The outlook reflects that we could upgrade Bancolombia in the next year if its RAC ratio rises consistently above 5.25% while it keeps manageable asset quality indicators and its prominent business profile.

Rating Action

On May 23, 2019, S&P Global Ratings revised its outlook on Bancolombia S.A. y Companias Subordinadas (Bancolombia) to positive from stable, and affirmed its long-term 'BB+' and short-term 'B' issuer credit ratings (ICRs) on the company. At the same time, given that we view Bancolombia Panama S.A. and Banistmo S.A. as core subsidiaries to Bancolombia, we changed their outlooks to positive from stable and affirmed our 'BB+/B' ICRs on both entities. We also affirmed our 'BB+' issue-level rating on Banistmo's $500 million senior unsecured notes due 2022.

Rationale

Bancolombia's outlook revision follows its improving consolidated capitalization metrics driven by continuous internal capital accumulation and the lower increase of its risk-weighted exposures compared to our previous expectations. The latter is supported by fairly stable net income results and improving economic risks of some countries where Bancolombia operates (Panama and El Salvador). We reflect this in our forecasted RAC ratio of 5.16%, on average, for the next 24 months compared to our previous forecast of 4.8%.

The ratings also incorporate the bank's leading market position in the Colombian banking system and sound operations in Central America that support its business stability. A well-diversified loan portfolio in terms of geography and sectors, and asset quality metrics in line with competitors in the domestic banking system, underpin its risk profile. The ratings also consider that Bancolombia's large and stable deposit base continues to support its funding structure. In our opinion, the bank has sufficient liquidity to cover expected and unexpected cash flows in the near future. Its stand-alone credit profile (SACP) remains 'bb+'. We consider Bancolombia Panama and Banistmo as core entities of their ultimate parent, Bancolombia, which views Panama as a strategic growth market and has continued to develop its presence in Central America

Our bank criteria use our Banking Industry Country Risk Assessment (BICRA) economic and industry risk scores to determine a bank's anchor, the starting point in assigning an ICR. Our anchor for Bancolombia is 'bb+', reflecting the weighted average economic risk of '7' given the countries where the bank has its major loan portfolio exposures as of March 2019: Colombia (71%), Panama (14%), El Salvador (6%), and Guatemala (6%). The industry risk score for Colombian banks is '5', with a positive trend (see "Banking Industry Country Risk Assessment: Colombia" published Aug. 16, 2018).

During the past two years, the bank has improved its capital levels as it has continuously generated internal capital in relation to its risk-weighted exposures that have increased at a slower rate than our previous forecast. Our projected RAC ratio, on average, for the next two years is 5.16%. Although that's within the 25 basis points (bps) threshold for a higher capital and earnings assessment, we still consider Bancolombia's quality of capital as low because of the notable amount of goodwill in its capital structure. Therefore, in our view, the bank's capital is more sensitive to exchange rate fluctuations than other banks we rate regionally. Additionally, if the Colombian Congress approves a proposed law that eliminates debit and credit card fees and commissions charged by banks, our net income forecast could be reduced up to 20% and therefore decrease our RAC ratio. Moreover, if the uncovered exposures to deteriorated corporate loans require higher provision expenses than expected, we could also lower our RAC ratio forecast.

Bancolombia's profitability metrics and earning capacity have remained fairly stable, and in our base-case scenario, we expect them to slightly improve in upcoming years due to the implementation of cost control initiatives and loan growth. The bank's total operating revenues are mainly composed of interest income--around 67.5% as of March 2019 with a three-year average of 70.6%--which, in our view, stabilizes its profitability metrics. Finally, we expect that Bancolombia's digital strategy, coupled with better economic prospects in countries where it has significant exposure, will improve efficiency and drive profitability and growth in the next two years.

Our financial forecasts reflect our base-case assumptions, which include:

- Colombia's GDP to grow 2.9% in 2019 and 3.0% in 2020 (according to our last Credit Conditions article, "Credit Conditions Latin America: Dovish Fed Eases Short-Term Risks, But Political Challenges Persist," published on March 28, 2019);

- Relatively stable foreign exchange in the next two years: COP3,150 and COP3,200 per $1 for 2019 and 2020, respectively;
- Consolidated loan portfolio growing at about 8% in 2019 and 8.5% in 2020;
- Net interest margins (NIMs) of 5.65% for 2019 and 2020;
- Adequate profitability levels, with core earnings to adjusted assets and efficiency levels around 1.47% and 48.9%, respectively, for the next 12 months;
- Dividend distribution of COP1.05 trillion and 33% payout ratio for 2020;
- NPAs and credit losses at about 3.6% and 1.95%, respectively, fully covered by reserves; and
- No additional inorganic growth for 2019 and 2020.

The bank's business stability has remained sound, reflecting its position as the largest bank in Colombia and one of the largest financial groups in Central America. Its market share in Colombia increased to 26.3% in terms of loans as of March 31, 2019, and we consider it unlikely that Bancolombia will lose its leading position in upcoming years. The bank's business diversification also provides it with stable revenue. Bancolombia continues to participate in nearly all banking business lines. Consumer loans have been its main focus and driver of loan growth in the past year; however, commercial loans have historically represented the highest share of its loan portfolio (67%) as of March 31, 2019. We expect the bank will continue expanding primarily in the consumer segment to improve its risk-adjusted returns, supported by better dynamics in this sector than in other lending segments, and greater accessing the market through its digital platforms. Finally, we consider the bank's management has long experience in the banking sector and in our opinion, it will be fully capable of controlling risks and successfully implementing its strategy in the next few years, which includes digital transformation (encompassing digital transactions and sales mobile apps, pre-approved loans, and more) and optimizing its banking channels by replacing branches with more a cost-efficient banking agent framework.

We believe Bancolombia's asset quality deterioration reached its peak last year. Now, we expect an improvement in the Colombian economy's credit cycle that together with adjustments in the bank's origination processes should revert the negative trend in asset quality. The bank has had problems with projects Ruta del Sol and Electricaribe, and with its small to midsize (SMEs) business unit because of transport segment exposures. Despite these issues, we still believe that Bancolombia's risk position assessment and asset quality metrics compare adequately with its Colombian peers and with other banks with similar economic risks. For the next year, we project NPAs to slightly decrease to 3.6%, net charge-offs to hover around 1.9%, and NPA coverage ratio to be around 150%. Furthermore, even if the bank is concentrated in the commercial loans sector, its top 20 largest exposures only represented 7.2% of its consolidated total loan portfolio and 0.68x of its total adjusted capital as of December 2018. These metrics are in line with those of its closest peers.

Bancolombia's funding assessment is driven by a high and stable proportion of customer deposits, coupled with a stable funding ratio (SFR) of about 100%. As of March 31, 2019, its funding base hasn't changed significantly, and customer deposits were about 79% of the total funding base. The rest is made up of debt issuances (11%), interbank loans (8%), and a small amount of repurchase agreements (2%). The bank's SFR was 98.2% as of the first quarter of 2019, which we consider in line with its funding assessment, although it's slightly lower than the 101.6% average of the past three fiscal years and lower than that of the Colombian banking industry (104.6%). For the next 12 months, we don't expect the bank's funding structure to notably change, because we expect customer deposits will continue to be its main funding source since the bank benefits from its sticky customer base and strong brand.

Bancolombia's liquidity levels are underpinned by its broad liquid assets that covered short-term wholesale funding 1.6x as of March 31, 2019, with a three-year average of 1.8x. Furthermore, our liquidity assessment reflects the bank's manageable refinancing risk with a satisfactory maturity profile and its liquidity position, which is mainly composed of cash and government securities. We believe the bank adequately manages its liquidity risk to meet expected and unexpected cash flows in the following 12 months.

We continue to view Bancolombia as having high systemic importance within the Colombian financial system because of its leading market share in deposits, its importance to the country's payment system, and our belief that the government is supportive towards its financial system. The latter results in a moderately high likelihood of extraordinary government support to the bank. Nevertheless, we don't currently incorporate any additional notches of support into our ratings on Bancolombia, considering the long-term local currency sovereign rating ('BBB'). Therefore, the ratings reflect the bank's SACP.

Grupo de Inversiones Suramericana S.A. (BBB-/Stable/--) holds around 25% of Bancolombia's equity, standing as its most important shareholder. In our view, Bancolombia is moderately strategic for the investment holding company, which, according to our criteria, grants one notch of support to the company's SACP. However, this is subject to a cap of one notch below the GCP, which is the case, so we don't apply a notch.

Outlook

The positive outlook on Bancolombia for the next year reflects our expectation that the bank will maintain a positive trend in its risk-adjusted capital indicators, mainly propelled by internal capital generation, and reflected in a forecasted RAC ratio of 5.16%. Additionally, we expect Bancolombia will keep its leading business position in Colombia and its solid franchise in Central America. The positive outlook on Banistmo and Bancolombia Panamá, reflects the outlook on Bancolombia. The ratings will move in tandem with those on its parent due to its core status.

Upside scenario

We could upgrade Bancolombia in the next 24 months if it generates enough internal capital to consistently keep our projected RAC ratio above 5.25%, while asset quality metrics continue improving.

Downside scenario

We could revise the outlook back to stable in the next 12 months if the bank's RAC ratio or profitability levels are below our expectations. This could mainly happen if goodwill increases significantly due to Colombian peso depreciation, or if the draft law is enacted and reduces banking fees and commissions in Colombia, which could lower internal capital generation below our forecast. Larger amounts of provisions to cover deteriorated large corporate exposures could also pressure our RAC ratio. Finally, a downgrade of the bank without a downgrade of the sovereign is unlikely over the next two years because if the bank's credit fundamentals worsen by one category, leading us to revise its SACP downward, we could still reflect one notch of support from the sovereign.

Ratings Score Snapshot

Issuer Credit Rating: BB+/Positive/B

SACP bb+

Anchor bb+

Business Position Strong (+1)

Capital and Earnings Weak (-1)

Risk Position Adequate (0)

Funding Average (0)

Liquidity Adequate

Support 0

GRE Support 0

Group Support 0

Sovereign 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; Outlook Action

	To	From
Bancolombia, S. A. y Companias Subordinadas		
Bancolombia Panama S.A.		
Banistmo S.A.		
Issuer Credit Rating	BB+/Positive/B	BB+/Stable/B
Banistmo S.A.		
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.