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Research Update:

BAC International Bank Inc. 'BBB-/A-3' Ratings Affirmed; Off Watch Negative; Outlook Negative

Primary Credit Analyst:
Jesus S Sotomayor, Mexico City (52) 55-5081-4486; jesus.sotomayor@spglobal.com

Secondary Contact:
Alfredo E Calvo, Mexico City (52) 55-5081-4436; alfredo.calvo@spglobal.com

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Overview

- We have concluded our stress test for BAC International Bank (BIB) to be rated above the sovereign, after the downgrade on Costa Rica, and assessed the bank's strategic direction for growth in Central America.
- We believe BIB will remain the largest financial institution in Central America, on a consolidated basis, while continuing its successful diversification strategy by geography and economic sector.
- We are affirming our 'BBB-' long-term and 'A-3' short-term issuer credit ratings on BIB and its core subsidiary Credomatic International Corp. (CIC) and removing them from CreditWatch with negative implications where we placed them on Feb. 25, 2016.
- The negative outlook reflects that on its parent, Banco de Bogota (BBB-/Negative/A-3), given the core status of both entities to the group. In consequence, our ratings on both will move in tandem with those on BdB.

Rating Action

On July 28, 2016, S&P Global Ratings affirmed its 'BBB-' long-term and 'A-3' short term issuer credit ratings on BAC International Bank Inc. (BIB) and its core subsidiary, British Virgin Island-based Credomatic International Corp. (CIC). We removed those ratings from CreditWatch with negative implications, where we placed them on Feb. 25, 2016. The outlook on both entities is negative, reflecting that on their parent (Banco de Bogota; BBB-/Negative/A-3).

Rationale

The rating action follows the conclusion of our stress test analysis for ratings above the sovereign after the recent Costa Rica--where BIB holds a significant exposure of its loan portfolio—downgrade. At that time, we assessed the bank's growth strategy in Central America, particularly in Costa Rica. We believe that its business diversification provides enough of a capital base and ample liquidity sources to support day-to-day operations in the hypothetical event that Costa Rica defaults. In that sense, taking into account our expectation of BIB's projected diversification strategy over the next 12 to 18 months (consistent 25% exposure to Panama and Costa Rica), we expect BIB will continue to pass our sovereign stress test for Costa Rica as long as this exposure does not increase materially. We also consider Panama (BBB/Stable/A-2) as the relevant sovereign foreign currency rating, given that

BIB is domiciled in Panama and it is subject to its regulatory framework. Consequently, the ratings on BIB will move in tandem with those of its parent and will not be capped by Costa Rica sovereign ratings as long as it continues to pass our stress test.

Our ratings on BIB currently reflect our view of its strong business position, supported by its leading market position in Central America on a consolidated basis. Its business stability reflects its large customer base and its moderate capital and earnings reflect its solid internal capital generation and its conservative dividend payout policy. Its adequate risk position reflects its stable asset quality metrics and its highly diversify loan portfolio (location and sector), and its large retail deposit base supports its average funding. Meanwhile, its adequate liquidly reflects its manageable short term obligations.

The 'bb+' anchor draws on our Banking Industry Country Risk Assessment (BICRA) methodology and our view of our expected weighted average economic risk in the countries in which BIB will has exposure over the 12 to 18 months through its loan book--Panama (25%), Costa Rica (25%), Guatemala (18%), El Salvador (10%), Honduras (11%), and Nicaragua (8%) at year-end 2015. As a result, the weighted economic risk is about '7'. A BICRA is scored on a scale from 1 to 10, ranging from the lowest-risk banking systems (group '1') to the highest-risk (group '10'). The common factor driving this economic risk score is low income in the countries where the bank operates, which affects the country's vulnerability to external shocks, and debt and payment capacity in countries with weak rule of law.

Our industry risk assessment recognizes that Panama's regulatory framework lags behind some international standards, but the regulator's adequate track record and the banks' competitive dynamics provide stability to the financial system.

Nevertheless, our industry risk assessment remains limited by the absence of a lender of last resort in the country. Although the government offered liquidity support to all banks in 2008, we are uncertain about the timeliness and efficiency of this type of support in the event of an adverse economic or liquidity scenario. Our assessment also incorporates the long history of low loan loss ratios and Panama-based banks' high profitability.

Our opinion of BIB's strong business position has not changed and it continues to reflect the bank's leading position in Central America within the consumer segment, mainly in credit cards, giving it strong business stability with no particular business concentration by geography, economic sector, or client. Its management expertise focuses on executing a comprehensive corporate strategy. BIB is the largest bank in Central America with operations in almost the entire region. Its market share by country is adequate (it's generally in the top-five largest banks), but it's measurably the largest financial institution in the region on a consolidated basis, with asset of around $18.7 billion, total loans of $13.1 billion, and total deposits of $12.3 billion. BIB has a 9.4% loan market share and 8.1% deposits market share regionally.

Additionally, the bank maintained its leading position in card issuances, with a large consumer client base. Its loan portfolio as of March 2016 was 40% in the commercial segment, 21% in residential commercial mortgage loans, and 37% in consumer loans--of which 17% was credit cards--14% personal and consumer loans, and 6% auto loans. The remaining 2% corresponds to leasing operations. In terms of geography, 27% of its loan portfolio is located in Costa Rica, 25% in Panama, 18% in Guatemala, 11% in Honduras, 10% in El Salvador, and 8% in Nicaragua as of March 2016. In our opinion, the bank is will show successful integration in Guatemala and Panama in the future and it will start to increase its exposure and loan growth rates in both countries after the integration process is concluded.

We assess BIB's capital and earnings as moderate. The latter continues to be based on our forecast RAC ratio, which we project will hover around 6.8% over the next 12 to 18 months. As of December 2015, our RAC ratio stood at 6.67% and our forecast RAC ratio for the next two years takes into account the following base-case scenario assumptions:

- Panama's GDP grows 5.5% in 2016 and 2017 (according to our last credit conditions, April 15, 2016);
- The remaining Central American economies expand as follows in 2016: Guatemala: 3.6%; Honduras: 3.6%; El Salvador: 2.5%; Costa Rica.
- BIB's loan portfolio grows 12.5% in 2016 and 2017, considering a growth trend as of March 2016 and its strategy to increases operations in Panama and Guatemala.
- Net interest margins (NIMs) slightly decrease in 2016 and 2017, as we expect the highly competitive environment in the region will continue to put pressure on interest margin.
- The forecast goodwill already incorporates the 2013 and 2014 acquisitions at about $390 million;
- A $15 million dividend payment in 2016 and 2017;
- Efficiency ratio of about 60% over the next two years, in line with its historical levels (three year average 59%);
- Non-performing assets and credit losses will remain stable at 1.56% and 1.36%, respectively, over the next two years.
- No acquisitions over the next two years.

We continue to see a strong quality of capital and earnings, based on the high quality of its capital, but most importantly because of the sound, resilient, and diversified quality of earnings. Its earnings give it sufficient financial stability to pass our sovereign stress test for companies with sovereign exposure of 25% or higher. Its main metrics continue to compare well with other large, regional players within the same industry risk score. As of March 2016, core earnings to average adjusted assets stood around 1.82% and have hovered around 2.00% over the past three years. We expect them to be at around 1.60% over the next 12 to 18 months. Net interest income has accounted for around 62% of total revenues, fees for 30%, trading for 5%, and other income for 1.9% and we expect this mix to remain about the same over the next two years. Its adequate cost to income ratio, which has been around 59% over the past three years, and the low share of both trading gains and other revenues in the mix (5%) also support its quality of earnings. We forecast quality of capital and earnings will remain strong in the foreseeable future as a result of our expected growth and the maintenance of good underwriting and cost policies.

Our view of an adequate risk position continues to be mainly driven by what we consider adequate growth and changes in exposure, healthy risk diversification in terms of geography, economic sector and client, and stable asset quality metrics. Overall, the bank has been able to continue adequately growing in its targeted markets without major disruptions. We expect BIB's loan portfolio to grow around 12.5% during in 2016 and 2017, considering historical growth levels, growth strategy (mainly in Guatemala and Panama), and the expected economic growth in the region. Its commercial/corporate portfolio does not show concentration in terms of single exposures or by economic sector. As of March 2016, its loan portfolio was composed by commercial (42%), mortgages (21%), credit card (20%), auto (6%) and personal and other consumer loans (11%). We are not expecting its loan portfolio composition to significantly change during the next two years. In terms of loan portfolio concentration by client, its top 20 largest exposures represented only 9.11% of its total loan portfolio and only 62% of its total adjusted capital. The latter reflects a high retail focus in its credit operations, keeping its loan portfolio relatively pulverized. Credit loss experience has remained stable because of its adequate loan origination policies and its adequate expansion strategy in segments where the bank historically has operated. Non-performing assets (NPAs) and credit losses stood at 1.36% and 1.52%, respectively, as of March 2016, and we estimate NPAs to remain between 1.5% and 2%, and credit losses to remain at less than 1.5% over the next two years. As we already mentioned, the sound credit loss experience is a result of historically prudent and conservative underwriting practices, as well as a deep understanding of its various market segments and economies.

We continue to view its funding as average, based on its large deposit base and its stable funding metrics. As of March 2016, its stable funding ratio (SFR) was 117% with a three year average of 116%. The main source of its funding base is customer deposits, accounting for 79%, of which around 40% is composed of retail deposits, which we view as relatively stable. Its deposit base compares adequately with other banks in the region. The remaining funding base is primarily composed of credit lines and repos from local and external commercial banks. We anticipate no changes in BIB's funding structure, given that we expect our forecasted deposit base growth to continue to provide it with the necessary resources to continue growing, with a healthy SFR hovering at around 110%.

Our assessment of its adequate liquidity is based on the bank's prudent liquidity and its manageable short term obligations as a result of its large deposit base. We believe that refinancing risk is low because its maturity profile continues to be adequate and it has a large deposit base. As of March 2016, its liquidity ratio stood at 8.3x with a three year average of 4.66x. We view the bank's liquidity as adequate. Most of its security holdings are largely composed of securities that trade in the local and undeveloped capital market, where there is isn't a deep and developed secondary market that could provide liquidity. There is no lender of last resort in the Panama. We do not anticipate significant liquidity needs in the next 12 months, and the banks' large deposit base will continue to support its funding and liquidity needs.

We continue to view BIB, and in turn Credomatic, as core entities for Banco de Bogotá. Among other things, BIB operates in the same business lines as its parent and is closely linked to Banco de Bogotá's reputation and risk management. BIB keeps its performance in line with the group's expectations. At year-end 2015, BIB (on a consolidated basis including Credomatic) accounted for 35% of Banco de Bogota's total reported equity, 39% of total loans, and 31% of total operating revenues.

Outlook

The negative outlook on BIB and its subsidiary CIC continue to reflect that on the parent. We BIB to maintain its strong presence and leadership in Central America over the next two years. We think that its very profitable operations and its geographic diversification strategy will help to maintain its business stability. We expect BIB and CIC to maintain their core status to BdeB in the future. BIB, on a consolidated basis, continues to account for a great portion of its parent's earnings and capital, and the group continues to view it as a cornerstone for its future strategy. In this regard, the ratings on BIB and CIC will move in tandem with those on the parent.

Downside scenario

We could lower the rating on BIB and CIC over the next two years we downgrade their parent. On the other hand, if BIB significantly increases its exposure in Costa Rica, which could lead BIB to fail our sovereign stress test, we could downgrade them it to be on par with the sovereign ratings.

Upside scenario

We will revise the outlook back to stable if we did so to its parent.

Ratings Score Snapshot

Issuer Credit Rating	BBB-/Negative/A-3
SACP	bbb-
Anchor	bb+
Business Position	Strong (+1)
Capital and Earnings	Moderate (0)
Risk Position	Adequate (0)
Funding and Liquidity	Average and Adequate (0)

Support	0
GRE Support	0
Group Support	0
Government Support	0

Additional Factors

Related Criteria And Research

Related Criteria

- General Criteria: Ratings Above The Sovereign--Corporate And Government Ratings: Methodology And Assumptions - November 19, 2013
- Criteria - Financial Institutions - Banks: Quantitative Metrics For Rating Banks Globally: Methodology And Assumptions - July 17, 2013
- Criteria - Financial Institutions - Banks: Bank Capital Methodology And Assumptions - December 06, 2010
- Criteria - Financial Institutions - Banks: Revised Market Risk Charges For Banks In Our Risk-Adjusted Capital Framework - June 22, 2012
- General Criteria: Group Rating Methodology - November 19, 2013
- Criteria - Financial Institutions - Banks: Banks: Rating Methodology And Assumptions - November 09, 2011
- Criteria - Financial Institutions - Banks: Banking Industry Country Risk Assessment Methodology And Assumptions - November 09, 2011
- General Criteria: Use Of CreditWatch And Outlooks - September 14, 2009
- Criteria - Financial Institutions - Banks: Commercial Paper I: Banks - March 23, 2004

Ratings List

Ratings Affirmed; CreditWatch/Outlook Action

	To	From
BAC International Bank Inc.		
Credomatic International Corp.		
Counterparty Credit Rating	BBB-/Negative/A-3	BBB-/Watch Neg/A-3

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.globalcreditportal.com and at www.spcapitaliq.com. All ratings affected by this rating action can be found on the S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column.