

3Q19 Results

Presentation
Transcription

BBVA Colombia

Audio-Conference 3Q19

[Alejandro Escobar] Good morning, good afternoon and good evening to our investors connected all around the world, you're welcome to our third quarter 2019 Results. My name is Alejandro Escobar and I'm part of the legal department of BBVA Colombia. In this event are also connected Diego Camilo Puentes- Financial Planning Manager, Alejandro Reyes- Principal Economist and Juan Pablo Herrera- ALM Director, who will give the presentation.

The corresponding documents were sent to you through email, both in English and Spanish, and will be available in our website in the section "Investor Relations" on the link "Agenda".

We ask you to please mute the microphone of your phones to have a better communication. Without further ado, I give the turn to Juan Pablo.

[Juan Pablo Herrera] Thank you very much Alejandro, Good Morning and welcome to all of our investors and shareholders connected to this call, in which I will present the results for the third quarter of 2019 for BBVA Colombia. As Alejandro mention, we have already sent you all the material via email both in English and Spanish through your email.

Slide 3 - Index

I will start with a brief overview of the macroeconomic scenario and later I will explain the highlights of our results for the quarter. First, I will start with our macroeconomic outlook on slide number 5.

Slide 5 – Macroeconomic environment

According to BBVA Research, based on the key assumption of ongoing tensions between the US and China, global growth forecast to reach 3.2% in 2019 and 3.1% in 2020. Below that recorded in previous years and less than previously expected (3.3% in 2019 and 2020). In this setting, is now more likely that tensions between the US and China will increase more than nowadays, thus, protectionism and uncertainty are likely to weigh further on global activity. With regard to oil prices and despite the heightened tensions in the Middle East, BBVA Research expects that prices will remain under control, declining from around USD 64 per barrel over the remainder of the year to approximately USD 57 by the close of 2020. Because of this, adjustments of central banks will continue with their accommodating policies in the long term.

US growth should gradually lose traction, converging with its potential growth rates: will increase 2.3% in 2019 and 1.8% in 2020; 0.2 percentage points below what was previously expected in both periods.

The Colombian economy expanded 3.0% in the first half of 2019, 40 percentage points of what was observed in 2018. The projection of growth over the remainder of the year, domestic demand is expected to abate as a result of tax uncertainty that faces the country by cause of the repeal of the financing law on investment decisions and high exchange rates. Thus, GDP will maintain similar growth over the remainder of 2019, at around 3.0% on average. To 2020, is expected a fresh boost over private investment, reaching growth of 4%, slowdown of imports and private consumption will slip. Leading to a full-year growth of 3.0% but once again with a different composition.

For public consumption, a slowdown in its growth is expected to be lower than that registered last year, conditioned by the labor market. On the other hand, private consumption showed, in the first half of 2019, a significant acceleration despite the deterioration of the labor market. The unemployment rate has increased, especially since the end of 2018. Forward, a moderation of household spending is expected towards levels of 3.8% in 2020 compared to the growing expectation of 4.3% this year.

Growth in domestic demand above GDP growth caused the current account to fall to a deficit of 4.3% of GDP in the first half of the year. This balance showed a larger deficit than posted in 2017, 3.3% of GDP, following the economic adjustment after a drop in oil prices. The increase of the deficit is mostly explained by the growth of imports, an aspect that has been evaluated within the estimates, a deterioration of the deficit that reaches 4.6% of GDP is expected for all 2019, a figure that would tend to the decline with the slowdown of imports in 2020 to 3.9% of GDP, still high.

Considering the latest records, the national economy shows adequate behavior. In the third quarter of the year, the country's GDP grew 3.3%, driven by financial activities and commerce, as a result of household consumption.

Slide 6 - Macroeconomic environment

Continue on slide number 6, there are several points to analyze from the monetary policy, in terms of its role in defining interest rate decisions. The first is inflation, which has been upward pressure mainly due to food prices impact generated by climate effect on crop reduction which ended up being less aggressive than anticipated, also caused by a significant demand outside the home and border shopping. With this in mind, it is expected that the transitory shocks that have occurred will gradually correct in the remainder of the year and early next to be able to converge to the goal in mid-2020. It is then projected that in December of 2019 inflation will remain at 3.8% and 3.3% in December of 2020.

Other topics that will be on the Central Bank's radar are the sustained high current account deficit, in line with rising imports of capital goods and the global economic situation, aspects

that generated a significant depreciation of the exchange rate over the year that has partially affected consumer inflation, however, BBVA Research has emphasized that an additional effect could be expected, since the different pass-through exercises account for a 4 month lag in transmission. By 2020, an adjustment in the external context are not foreseen, nor is an increase in the price of crude oil but if a better growth would benefit the depreciation of the peso, which would close 2020 at 3,370 with a year-round average of 3,380.

All of the above and considering that there are no longer face external upside pressure, monetary policy should be more flexible in developed countries. It is expected that Central Bank will maintain its interest rate stable for a long time, holding unchanged until early 2021.

Slide 7 – 3Q19 Performance Highlights

Under this macroeconomic environment, I would like to share the main highlights of our results in the third quarter of 2019, going into slide number 7.

During the first six months of the year, there was a more challenging environment from competitive against both local and international banks that pressed and limited the profit margins and reduced market share, especially on the retail side. However, despite a highly challenging environment, BBVA Colombia has a positive performance during the first nine months of the year. In fact, we have achieved a new record in billing in the consumer portfolio with 1,5 trillion pesos in September 2019; this figure is based on a new policy of risks and operational processes, in addition to a solid pricing strategy that allowed branches to maximize its management potential and achieve historical billing figures.

Our net interest income increased 2.8% in the first nine months of the year compared to the same period of the previous year mainly explained by a negative variation in the interest income for 6 billion pesos and a decrease in the interest expense for 60 billion pesos. Furthermore, the gross loan portfolio registered a growth of 151 billion pesos given the greater activity in the bank and given that net fee income showed an increase of 16.9% during the third quarter of the year. Finally, our net income decreased by 3.5% compared to the same period of 2018.

In terms of our balance sheet, total assets closed at 65 trillion pesos, with an increase of 11.8% compared to the last year; the gross loan portfolio registered an annual growth of 7.4%, ending the period at 48 trillion pesos, while customer deposits grew 3.2%, closing with a balance of 47 trillion pesos.

It is worth mention that during the year there was an annual growth of 708% in the money market operations due to an increase in the repo operations with the Central Bank, the above is due to the need to diversified funding sources by the treasury to support its position, which has

been increasing both in the portfolio of securities and cash in US dollars due to favorable market opportunities and the decrease in excess bank resources.

As for risk indicators, we saw a decrease of 25 bps in our NPL ratio compared to August of 2018 and a decrease of 28 bps compared to December 2018.

Otherwise, our cost of risk declined 27 bps in August 2019, compared to the same period of last year and also decrease 28 bps compared to December of 2018.

We have also maintained good solvency levels well above the minimum required by regulation, ending the third quarter of the year at 11.49%, decreasing 41 bps compared to the second quarter of 2019. These results mostly explained by the increase in the RWAs due to market risk in 2 billion pesos.

Finally, our efficiency ratio continues to improve, decreasing 40 bps compared to the previous year.

Slide 9 – Digital Transformation

On slide number 9, I would like to share our results in terms of the digital transformation in BBVA Colombia.

Nowadays, BBVA Colombia's customers prefer the cell phone to make their financial transactions rather than other channels. According to the latest report of monetary and non-monetary transactions from the Financial Superintendence of Colombia, BBVA Colombia recorded 115 million transactions made by its mobile banking application during the first half of the year; this figure is double as the previous year. Regarding the non-monetary operations, that is, balance inquiries or the status of products, closed with a total of 104 million operations of this type, with a growth of 52% compared to 68 million transactions made in the first half of 2018.

On the other side, the corresponding to the monetary operations which contemplate some type of money transfer, BBVA customers made a total of 11 million transactions between January and June 2019 compared to 6,17 million operations registered in the same period of the previous year. This growth reflects the greater approval of mobile devices as channels to make transactions quickly and safely. This is how practically all the operations that are done in the branches are available in the mobile banking application, in this way, we remain committed to offering 100% digital and innovative products and services to our clients, offering them greater options and possibilities of relating to banking through the cell phone, this includes both individuals and businesses.

Proof of our successful strategy is the significant increase in the use of our digital channels. We currently have 1,42 million digital clients in the third quarter of 2019, which 1,2 million are related only through the mobile banking application. For the third quarter, there was an increase of 22% compared to the previous year. We also have 23% more mobile customers compared to the same period of the last year. In addition, digital sales represented 26% of our total sales with a positive variation of 8%.

In this way, BBVA continues to consolidate itself as a digital bank that promotes closeness to its customers by offering investment alternatives according to their needs. The main challenge for the last months of the year is continue to maintain and strengthen the positioning we have with our clients, generating innovative solutions, with high added value and tailored to their needs, in order to continue strengthening the Bank's results.

Slide 10 – Consolidated Results for the 3Q19

I will now present the main figures for the third quarter of 2019, showing first the results of the period, then the highlights of our balance sheet and business activity and finally our solvency ratio.

Slide 11 – Net Interest Income

Moving on to slide 11, I would like to share the results of the third quarter of 2019.

The behavior of the bank's interest margin shows an interannual increase of 2.8% in the first nine months of the year, equivalent to 55 billion pesos. This growth is explained mainly by the expense side, where there was a reduction of 44%, equivalent to 61 billion pesos which are mainly explained by a decrease in term deposits for 145 billion pesos. Similarly, at the end of August of 2019, ordinary bonds worth 155 billion pesos were expired, which meant a lower cost for the month of September of 2019.

Interest income had a negative variation in the loan portfolio of 6 billion pesos mainly due to an increase in the retail loans income for 72 billion pesos and a reduction in the commercial loan for 82 billion pesos and a reduction in the mortgages loan for 26 billion pesos.

Slide 12 – Net Fee Income

On slide 12, our net fee income showed an increase of 16.9%, equivalent to 44 billion pesos compared to the third quarter of 2018. The annual increase of fee income is mainly explained by fewer days of the means of payment, also during the month of August, there was a higher fee income for the concession "Ruta del Cacao" for 765 million pesos.

Additionally, there was a variation of 149 billion pesos in fee income, which corresponds to the increase in bank guarantees by 4 billion pesos, in business affiliated with credit cards for 10 billion pesos, in network service for 8 billion pesos and other fees for 127 billion pesos. Similarly, there was a decrease in debit card management fees of 9,5 billion pesos such as: paying social security contributions, transfers, in house, biometric withdrawals, among others.

On the side of fee expenses there was an increase of 104 billion due to an increase in fees to REDEBAN network and bank transactions made with third parties, for this reason, the other expenses amount to 111 billion pesos concerning the same period of the previous year.

Slide 13 –Operational Costs and Efficiency Ratio

Moving on to slide 13, we see an outstanding evolution in our efficiency ratio with a decrease of 40 bps. This is explained by a moderate growth in expenses during the quarter, with a variation of 6% and with a variation of 4.8% in the first nine months of the year mainly explained by an increase in implementation of software and computer applications, especially corporate software for 4 billion pesos and a decrease in licenses by 3 billion pesos compared to the last year in order to improve the digital transformation process that are carried out in the bank and that has allowed us to improve some internal process.

Slide 14 – Net Income

Finally, as we show on slide 14, BBVA Colombia recorded a net profit of 512 billion pesos in the third quarter of 2019; which is a decrease of 3.5% compared to the third quarter of 2018. It is important to highlight that in the third quarter of last year, there was an adjustment in the income statement in provisions under IFRS9 regulation. Since December 2018, this adjustment was included in the balance sheet. Discounting this effect, BBVA Colombia showed an increase of 20.9% in the net income.

As for return on equity, BBVA Colombia saw an increase from 12.28% in August 2018 to 15.0% in August 2019, above the industry's average. The stable trend for the return on assets maintains, showing 1.06% in August 2019.

Slide 15 – Consolidated Income Statement

On the slide 15, you can find the main figures of our consolidated income statement.

Slide 16 – Balance Sheets and Business Activity

Now, I would like to present our highlights in terms of our Balance Sheet and Business Activity.

Slide 17 – Portfolio Composition

On slide 17, you can see that our loan portfolio increased by 7.4% to 48 trillion pesos. BBVA Colombia's main business activity is retail banking targeted at individuals through its extensive branch network, complemented with some corporate and investment banking activities. The retail segment represented close to 60.4% of the total gross portfolio in the third quarter of the year. This segment showed an increase of 8.6% compared to 2018 and closed with a balance of 29 billion pesos.

For the third quarter of the year, the consumer portfolio showed an annual increase of 8.4%, equivalent to 1,4 trillion pesos, the mortgage portfolio showed an increase of 8.8%, which represented a variation of 936 billion pesos, and at the end of September 2019 represents 23.9% of the gross portfolio, while the commercial portfolio showed an annual increase of 5.5% with a variation of 969 billion pesos, this category consists of corporate loans and loans to territorial entities. Besides, in the third quarter of 2019 we obtained a greater volume of recoveries, driven by a reactivation in the normalizations, which came to contribute 19% of the total recovered in September, an increase of 781 bps compared to June 2019.

Additionally, it is worth mention that during the first nine months of the year, as a result of teamwork, we managed to generate the necessary tools so that our sales force reached milestones in consumption billing that are historic; in the line of payroll loans, we had an annual growth of 108% compared to the same quarter of last year with a special focus on strategic groups; in free consumption the growth in billing was 58% in relation to the same period of the previous year. This record is also the reflection of a preferential offer in the vehicle loan, thus achieving an accumulated of 59% variation in the billing originated in the branches, making the profitability management of the product more efficient.

With these highlight in sales, we expect to have a positive impact on indicators such as market share in the segment of retail, growth in target customers, positioning in strategic groups and greater profitability through the cross-selling that we achieve on managed customers in what subtraction of the year.

Slide 18 – Funding Sources Composition

On slide 18, we show our funding sources composition.

In the first nine months of the year, customer deposits remained adjusted to the bank's liquidity needs and the deposits behaved in line with the dynamics of portfolio growth.

In this way, customer deposits grew at an annual rate of 3.2%, closing the quarter at 47 trillion pesos. This was led by a growth in saving accounts with a growth of 17.4%. This allowed us to reduce our funding with time deposits and checking accounts, and ultimately a reduction in our

financing costs. In this way, term deposits and checking accounts showed a decrease of 7.1% and 3% respectively.

Slide 19 – Market Shares

On slide 19, we show the main highlights of our business activity.

During the third quarter of the year, we decreased our market share by 34 bps. This is a result of our strong focus on optimizing returns on capital that lead us to create value mostly through high commercial spreads and less via volumes.

As a result, our market shares in commercial loans decreased by 31 bps in August of 2019. On the retail side, we saw a slower dynamic due to the macroeconomic slowdown. Following the latest data available, the country is growing at 3.3% and our estimate for the end of the year is 3%. In addition to this, the unemployment data are also not good and the potential of the economy is lower than what it was a few years ago. The consequence of this is that credit growth is much more subtle. Thus, consumer loans, credit cards, and mortgages showed a decrease in market share of 81 bps, 22 bps, and 21 bps respectively.

Regarding deposits, we saw a market share decrease of 77 bps, driven mainly by a reduction of 185 bps in term deposits, given our strategy to reduce our funding costs. Similarly, saving and current accounts showed a decrease in market share of 31 bps and 77 bps respectively.

Slide 20 – NPL Ratio

Now, on slide 20, within relevant events of the third quarter of 2019, the release in loan provisions in September 2019 as a result of the recalibration of parameters in the scope of IFRS9 stands out. A good behavior is maintained in terms of recovery management, with a variation compared to the previous quarter of 790 bps. The strategies proposed for the reduction of NPL ratio, in accordance with the implementation of the “Guide for NPL credit institutions” issued by the European Central Bank have allowed the NPL ratio to be 3.68% in August of 2019, showing a decrease of 25 bps compared to the ratio reported in the previous year. From the first part of the year, we are seeing that the NPL ratio dropped near to the average sector levels, with a decrease of 28 bps compared to December 2018. The portfolio that shows the greatest deterioration was the consumer loans, which deterioration is mainly explained by the slow recovery of employment.

It is important to indicate that BBVA’s write-offs are aligned to Basel III policies that allow the cancellation of assets only when there is no recovery viability. As shown in the chart, BBVA’s NPLs plus write-offs compare very positively vs. the sector, showing the higher quality of our portfolio.

Furthermore, the commercial portfolio's quality remains at lower levels than the average of the sector given our low participation in problematic transactions. Additionally, the mortgage's quality showed a deterioration of 78 basis points compared to August 2018.

Finally, we expect a recovery in the quality of assets in the medium term, below what was observed in 2017, taking into account the cancellation of Electricaribe's exposure and the tightening of the subscription standards for term loans, backed by Bank history of taking appropriate corrective measures to improve credit quality.

Slide 21 – Consolidated Balance Sheet

On slide 21, you can find our detailed balance sheet, of which I already mentioned in the main highlights.

Slide 23 – Solvency

Finally, in terms of our capital adequacy on slide 23, BBVA Colombia has capital sufficient in light of its asset quality, conservative risk management, profitability, and ordinary support. The bank has stable capital ratios, which are sustained by profitability and moderate dividend policy. BBVA Colombia closed the third quarter of 2019 with good solvency ratios, well above the regulatory requirements. However, we saw a decrease of 41 bps in the solvency ratio in the third quarter of 2019 compared to the second quarter of 2018 due to an increase of RWAs of 1,8 billion pesos in line with the portfolio growth mainly explained by an increase in the position and duration of trading book. This result is offset by an increase in the Total Regulatory Capital due to the devaluation of the Colombian peso that increases the value of the subordinated debt in dollars. Although, there was a change in the amount of the 2021 maturity of bonds from 40% to 20% worth 88 billion pesos. We expect that the forthcoming adoption of Basel III guidelines in Colombia will benefit the bank's capital, mainly due to changes related to RWAs' density, as the bank expects it to decrease between 200 and 300 basis points; increased capital buffers and more comparable capital definitions.

With this, I have finished my presentation and open the line for any questions you may want to ask.

[Carlos Rodríguez] Good morning everyone. My name is Carlos from Ultraserfinco; I have three questions if I may. The first one is to explain the decrease in the interest income during the quarter. The second one is if you could give us your guidelines in loan growth for the segment for the next year and my third question is related to the difference between the sector's NPL and Bank's NPL and if you expect a further deterioration of this segment given the unemployment rate in Colombia. Thank you.

[Juan Pablo Herrera] The decrease in the interest income is given that the activity of Colombia last year was quite slow, but the trend is change at the end of the second quarter. About your second question, as I mention, we expect that the unemployment rate could improve in the next year mainly due to an improving in the Colombian economy. In that line, we expect a better perform in the mortgage loan, also the commercial loan is going to be an important target for BBVA Colombia in the next year because we have a very good mix retail loans. About your last question, the difference between the Bank's NPL ratios vs. the sector's NPL as we show in the presentation, we are improving our NPL ratio due to two things; the first is about the policy of the bank for the credit; at the beginning of the year, Electricaribe's loan was provisioned. On March 20 of 2019, the entire portfolio was written-off with value of 249 billion pesos. And the second reason is due to our conservative risk management policy will be very positive for the next year and that means a positive differentiation with the competitors.

[Nicolás Alfonso] Hi. My name is Nicolás Alfonso from Compass Group; I have a couple of questions. The first one is related to the fee income, you presented a 51% decrease during the quarter and I would like to know what it means this reduction, and also what is your expectation going forward in fees. The second one, if you can give us the Risk-Weighted Assets as percentage of total assets? Thank you.

[Juan Pablo Herrera] Our business is related to be more transactional bank given our electronic platform that is supposed to improve our behavior in the fee side. This is a year for adjustments in several aspects in the Bank. One is really important because the Bank is making several investments in the technological side as a group BBVA we are moving toward to be a digital Bank. We are improving our platforms to provide a good experience to our clients; we could give us a benefit in the midterm. Related to your second question, we are in the middle of the change of the local regulation in the Capital. As you know, it will be implemented in 2020, so the next year we are going to prepare to the new regulation. For the Bank, we expect that the density of the RWAs is going to be lower that today. In general for the whole banks, we are expecting that the density is going to be lower that we have currently, that allows us to improve our solvency ratio.

[Alejandro Escobar] Since there are no more questions, then we conclude our event. We appreciate your participation and hope you have an excellent day.

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