SECTOR PROFILE
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Banks – Colombia: Q1 2024 Update

Profit still materially restrained by high loan-loss provisioning, weak activity

Below are key takeaways from the Q1 2024 results reported by the four largest Colombian banks: Bancolombia S.A. (Bancolombia, Baa2 stable, ba1)[1], Banco Davivienda S.A. (Davivienda, Baa3 stable, ba2), Banco de Bogotá S.A. (Bogotá, Baa2 stable, ba1), and BBVA Colombia S.A. (BBVA Colombia, Baa2 stable, ba1). All comparisons are to Q4 2023 unless otherwise stated.

The four biggest banks in Colombia (Baa2 stable) had combined net income of COP 1,471 billion ($380.6 million) in Q1 2024, a 22.6% increase from Q4 2023. This rise derived mostly from Bancolombia's robust earnings, while Bogotá improved from a weak Q4 2023 and the two other banks posted net losses. Loan-loss provisions remained at historically high levels, reflecting the still-large volume of problem loans in the banking system. Key credit developments in the quarter included:

» Bancolombia's strong earnings benefited from a 23.7% QoQ decline in loan-loss provisions and a 8.1% drop in operating expenses, further supported by continued strong margins. Results at the other banks were hit mostly by provisioning expenses, while funding costs, though still high, fell after five consecutive quarters of increases. Colombia's policy interest rate held at double-digits as of 31 March — 12.25%. Despite that, banks' income from lending operations was constrained by low business activity and strict loan underwriting policies and lower interest rates. Profitability will likely stay strong for Bancolombia in the next two to three quarters, although with some margin pressure as interest rates come down, while it will remain negative or at low levels for the other three banks.

» Loan delinquency remained high in Q1 2024, still reflecting weak consumer loan quality. In addition, problem loans at small- and midsized companies and mortgages are at their highest level in recent years. The group's average problem-loan ratio, measured as Stage 3 loans[2] to gross loans, was flat at 5.8% from Q4 2023. Conversely, 90 days past-due loans to gross loans increased a slight 10 basis points (bps) to 3.9%. We maintain our view that loan delinquency in the consumer portfolio will be more stable in second half 2024. Also, we expect loan-quality metrics to improve steadily only in 2025, provided that interest rates and inflation come down, benefiting economic activity.

» The average Moody's ratio of Tangible Common Equity to risk-weighted assets (TCE/RWA)[3] for the four banks fell 40 bps to 10%, mainly due to dividends distributed in March. All banks but Davivienda had modest growth in lending operations, which also weighed on RWAs. Davivienda's TCE/RWA went up benefiting from new share issuance in March and higher RWAs from Q4 2023.

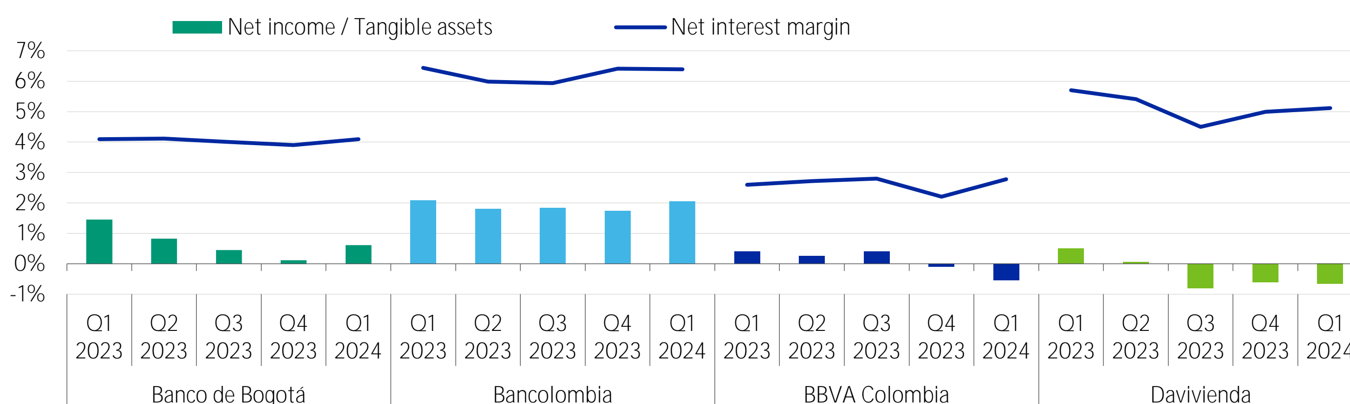
Material profit difference highlights banks' loan portfolio characteristics

In Q1 2024, Bancolombia stood out among its peers for its earnings, with net income up 14.9% to COP 1,663 billion. This alone supported a 22.6% rise in the four banks' combined bottom-line results, to COP 1,471 billion. At the same time, Davivienda and BBVA Colombia posted losses of COP 287.6 billion and COP 135.3 billion, respectively. Bogotá reported a profit of COP 209 billion, still below historical averages but up from COP 40.2 billion in Q4 2023. The three banks posted higher provision expenses than the previous quarter, which led to the weak quarterly results. In addition, bottom lines were also limited by interest expenses on funding instruments, which have been high since new regulatory long-term funding requirements began in Q1 2023, changing funding cost dynamics, and interest rates remained high in Colombia and globally. Funding costs have been inching lower despite Colombia's high policy interest rates, with Q1 2024 showing the first decline after five consecutive quarters of increases.

The average ratio of net income to tangible assets (NI/TA) was 0.4% in Q1 2024, up from 0.3% in the previous quarter (see Exhibit 1). In addition, the average net interest margin (NIM) for the four banks also improved slightly, by 20 bps to 4.6%, from one quarter prior. In the next two to three quarters, we expect margin pressure to subside as funding costs ease in line with lower policy rates, although income will be constrained by limited credit demand and banks' conservative appetite for expanding loan origination. At the same time, however, the still-high interest rates and subdued economic activity will also undermine borrowers' ability to pay bank loans, which will likely require the four banks to maintain high provision volumes, which will weigh on their bottom-line results.

Exhibit 1

Profitability will likely remain subdued for next two quarters, curbed by loan-loss provisions and low business volumes



Moody's net interest margin = net interest income as percentage of average interest earning assets

Source: Banks' financial reports, Moody's Ratings

Davivienda posted losses for the third straight quarter. The bank's net interest income (NII) was virtually flat (+0.5%), reflecting efforts to improve loan quality and the gradual reduction in interest rates, which together weighed on income from lending operations — down 1% in Q1 as the portfolio of high-margin consumer loans fell 5.7%. BBVA Colombia also reported losses, reflecting an increase in provision expenses and less interest income from securities investments.

In Q1 2024, Bogotá's net income benefited from a drop in funding costs and an increase in noninterest income, resulting in net income 5.2x that of the previous quarter. In Q4 2023, the bank also reported a nonrecurring tax expense that weighed on its quarterly profit. However, large provision expenses kept the bank's bottom-line result 58% below that of Q1 2023.

In addition, low business volume is also hurting the origination of fee income for the four banks. On the positive side, all four banks focused on cutting operating expenses to improve efficiency and reduce pressure on bottom-line results (Exhibit 2).

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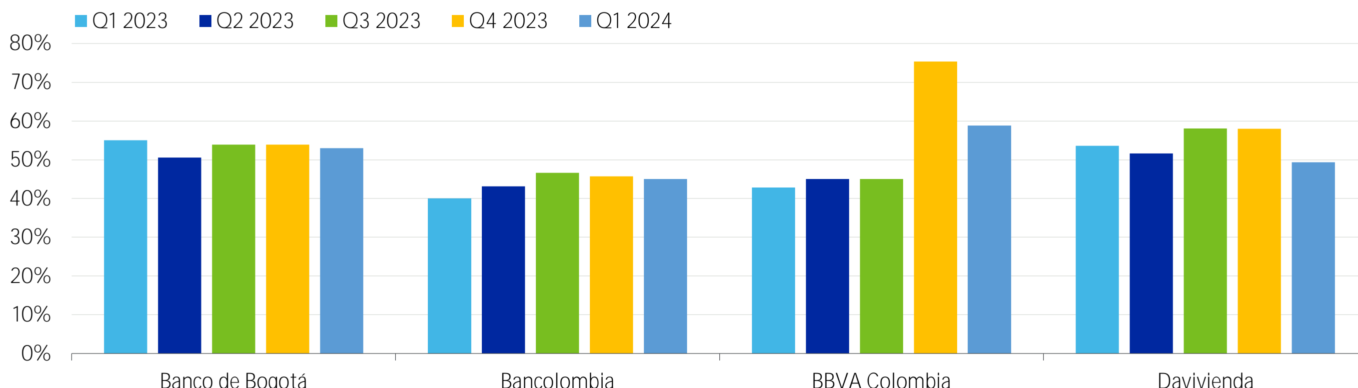
Exhibit 2

Cuts to operating expenses helped Q1 efficiency, but improvement to ratios will hinge on stronger business volume

Banks' cost-to-income ratios, as calculated by Moody's



Source: Banks' financial reports and Moody's Ratings

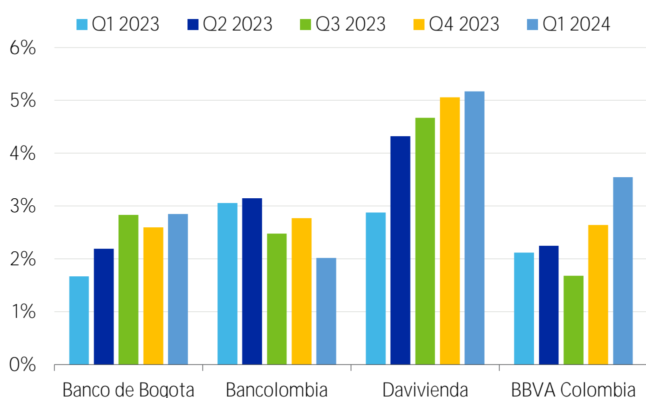
Loan-loss provisions will remain high, reflecting the system's still-large problem-loan volumes

For the second consecutive quarter, the group's average ratio of loan-loss provision expenses to gross loans increased, up 10 bps to 3.4%. Bancolombia, however, posted a 0.7% drop in its ratio (Exhibit 3), driven by a roughly one-quarter reduction in provision expenses (Exhibit 4) as the bank reported a halt in the weakening of its loan book quality. The bank had the lowest provisions among its peers. Akin to Q4 2023, BBVA Colombia posted the largest rise in the ratio, showing a more intense jump in provisions compared with peers. Davivienda had the highest provisions, still reflecting the large volume of problem loans in its consumer portfolio, although the bank's problem-loan ratio in that segment fell in Q1 (6.04%) from its record in Q4 2023 (6.97%). For consumer loans, Davivienda had a reduction in provisions reflecting the decline in loan volume in that portfolio. Conversely, the bank made additional provisions for commercial loans, a segment that was affected more by the negative credit cycle.

Exhibit 3

Banks maintain conservative levels of provisions to withstand credit losses

Loan-loss provision expenses / gross loans

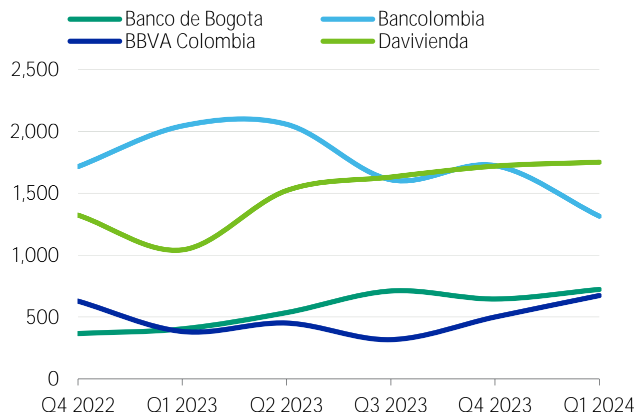


Source: Banks' financial reports and Moody's Ratings

Exhibit 4

Bancolombia reported the most significant decline in provisions among its peers

Quarterly loan-loss provision expenses, in COP billion



Source: Banks' financial reports and Moody's Ratings

Consumer loan delinquency is flattening, while commercial and mortgage continues to weaken

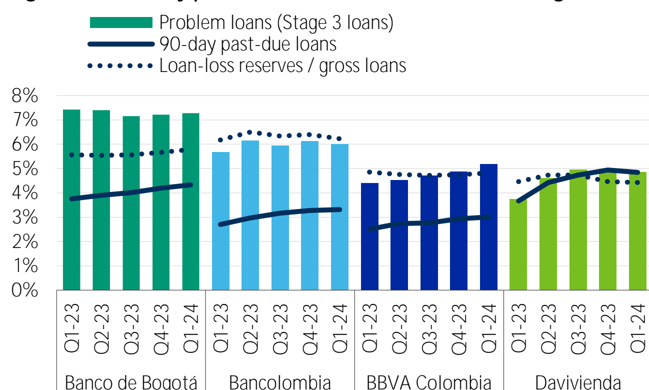
In Q1 2024, banks started to report stabilization, or declines, in the problem-loan ratios associated with their consumer loan portfolios, reflecting conservative underwriting policies adopted throughout 2023. Within that segment, Davivienda reported a 93 bps drop to 6.04%, in its problem-loan ratio, calculated using 90-day past-due loans, compared with the previous quarter. Bancolombia's loan delinquency in consumer loans was flat (at 4.8%), while Bogotá's went up (4.1% from 3.8%). Despite lower inherent risks in the commercial loan and mortgage segments, the group reported a continued gradual rise in problem-loan ratios for the two sectors.

The group's average problem-loan ratio, measured as Stage 3 loans, remained stable at 5.8% in Q1 2024. Bogotá continued to report the largest problem-loan ratio (7.3%) among the four banks, followed by Bancolombia at 6% (see Exhibit 5). Davivienda posted a 10 bps fall to 4.9% supported by decline in problem-loans in the consumer portfolio. For the group, loan delinquency, calculated as 90-day past-due loans to gross loans, went up 10 bps to 3.9%, keeping the same pace as in the two previous quarters. Although new problem-loan formation is beginning to show signs that is becoming less intense than in 2023, we expect the overall level of problem loans will only reduce consistently toward the end of 2024 and early 2025, provided inflation and policy rates continue to decline and Colombia's economy recovers. In addition, banks' conservative approach has contributed to a low volume of loan origination (Exhibit 6), which will also lead to upward pressure on problem-loan ratios in the next one to two quarters.

Exhibit 5

A turning point in asset quality will likely happen toward year-end 2024

Stage 3 loans, 90-day past-due loans and loan-loss reserves to gross loans

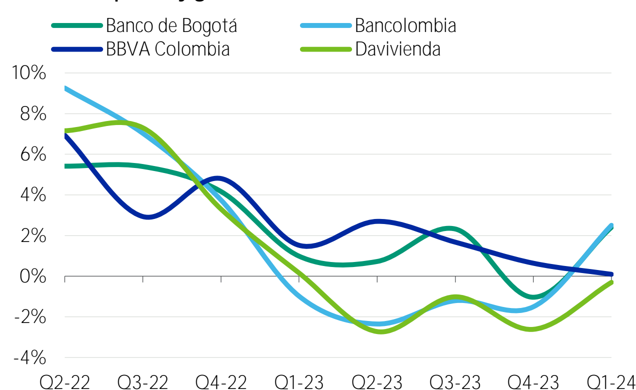


Source: Banks' financial reports and Moody's Ratings

Exhibit 6

Weak volume of new loans in Q1 in line with expectation of modest loan growth rates for 2024

Gross loans, quarterly growth



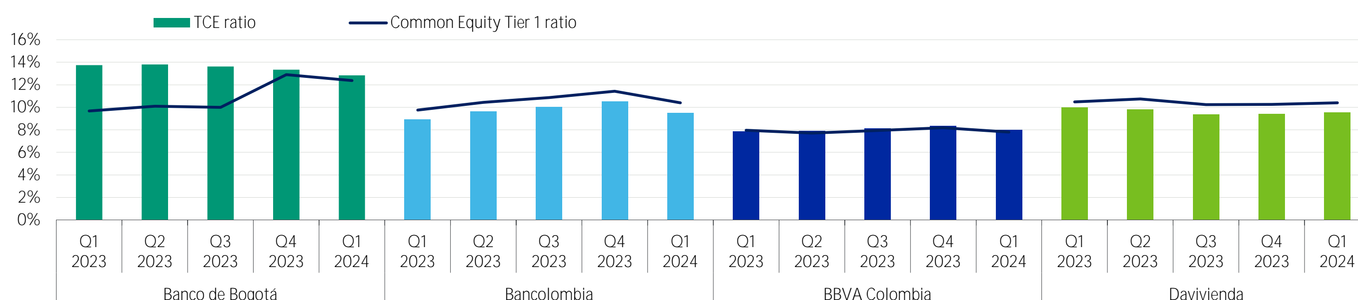
Source: Banks' financial reports and Moody's Ratings

Capital ratios incorporate adjustments from dividend distribution

The average Moody's ratio of Tangible Common Equity to risk-weighted assets (TCE/RWA), our preferred measure of capital for reasons of global comparability, declined to 10% from 10.4% in the previous quarter (Exhibit 7). Davivienda had a 20 bps rise in its TCE/RWA stemming from its March issuance of 36 million new shares, equivalent to COP 720 billion, counterbalancing the drag on its capital ratio from net losses in the quarter. Despite the strong earnings Bancolombia reported, the bank's TCE/RWA ratio fell 100 bps on the distribution of COP 3.4 billion in dividends as of March. The bank's RWA also increased in the period on expansion of its loan book (+2.5%). Likewise, Bogotá's capital ratio declined on dividend distribution (COP 277 billion) and an increase in loan operations (+2.4%). Conversely, the decline in BBVA Colombia's capital ratio reflected its dividend distribution, the net losses and reduction in total assets reported in the period. The group's capital position, measured as regulatory Common Equity Tier 1 to RWA, also declined in the period, to an average ratio of 10.3% from 10.7% one quarter prior.

Exhibit 7

Capital ratios will likely show limited improvement in the next three quarters



Source: Banks' financial reports and Moody's Ratings

Endnotes

1 The bank ratings shown in this report are the long-term deposit ratings and the respective Baseline Credit Assessment (BCA), where available.

2 Stage three loans include 90+ days past-due loans as well as impaired restructured loans and certain other risky exposures.

3 Our preferred measure of capital for reasons of global comparability. Tangible Common Equity (TCE) = (Common shares + retained earnings and related reserves + treasury stock + foreign currency translation) minus (Goodwill and other Intangible Assets) minus (Deferred Tax Assets) plus (Impact of Cap on Deferred Tax Assets).

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