



## Rating Action: Moody's affirms Banco Davivienda's Baa3 deposit ratings and downgrades BCA to ba2, outlook remains stable

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New York, April 28, 2023 -- Moody's Investors Service, ("Moody's") has today affirmed Banco Davivienda S.A.'s (Davivienda) long- and short-term local and foreign currency deposit ratings at Baa3 and Prime-3, respectively. The rating agency has also affirmed the bank's long- and short-term local and foreign currency Counterparty Risk Ratings at Baa2 and Prime-2, respectively, and long- and short-term Counterparty Risk Assessments at Baa2(cr) and Prime-2(cr), respectively. Concurrently, Moody's downgraded Davivienda's Baseline Credit Assessment (BCA) and Adjusted BCA to ba2 from ba1. Moody's also downgraded to B2(hyb) from B1(hyb) the foreign currency subordinated debt rating on Davivienda's Additional Tier 1 subordinated notes. The outlook on the long-term deposit ratings remains stable.

### RATINGS RATIONALE

According to Moody's, the downgrade of Davivienda's BCA to ba2 reflects metrics for profitability and capital, measured under Moody's Banks Methodology, that are inherently lower than those of peer banks in Colombia and also compared to the bank's historic levels. The bank's profitability ratios and capitalization showed little change in the past two years, despite its strategy to accelerate business growth that resulted in strong market share gains in loans and deposits in Colombia in recent years.

In December 2022, Davivienda's net income to tangible assets ratio was 0.89%, 50 basis points above the ratio in December 2021, but still below the 1.23% reported at the end of 2019, just before the coronavirus pandemic. The bank's performance in 2022 reflected increased credit costs, operating expenses and funding costs in the period, which offset the improvement in loan income as a result of the strong credit growth of 22% in the 12 months ended in December 2022. The bank's strong operational growth, with total assets up 20.6% year-over-year, also strained profitability ratios. We expect Davivienda to report a flat performance in 2023 as new loan origination slows down amid weakened economic activity in the period. Credit costs remain high, as loan delinquency will inch up, which is in line with the overall trend expected for the Colombian banking system.

Davivienda's capitalization, measured by Moody's ratio of tangible common equity (TCE) to risk weighted assets (RWA), remained below that of its peers in Colombia in December 2022 due to higher dividend payout ratio of 40%, above historical average level of about 30%. Moody's acknowledges, however, that Davivienda's regulatory Common Equity Tier 1 (CET1) ratio of 11.07%, as of December 2022, remained fairly stable over the previous 12 months and provided the bank a robust cushion over the regulatory minimum level of 4.5%. During the next 12 months, we anticipate the bank's capital ratio will also remain relatively stable, with slower loan origination easing pressure on capital consumption, which will partly compensate a modest increase in net income and will support a dividend payout in line with previous years.

At the same time, the bank's ba2 BCA is supported by asset quality metrics that remained below its peers' and improved in the past four to six quarters. In December 2022, Davivienda's problem loan ratio, measured as Stage 3 loans under IFRS to gross loans, stood at 3.21%, down from 4.27% one year prior. While the loan delinquency ratio incorporated a 22.1% growth in gross loans, there has

been an improvement in the recovery of past-due loans in the period and an increase in loan granularity provided by the bank's growth into consumer lending. Despite that, we expect Davivienda's problem loan ratios will rise gradually in the next three to four quarters – in line with other banks in Colombia – with loans maturing under a less favorable scenario that will continue to pressure households' repayment capacity. With that, the bank's still adequate volume of loan loss reserves as of December 2022, at 135.89% of Stage 3 loans and 4.36% of gross loans, will provide an important cushion to absorb additional deterioration in asset quality in 2023.

As a result of the downgrade of the adjusted BCA to ba2, Davivienda's subordinate debt rating was also downgraded to B2(hyb) from B1(hyb). The subordinate debt rating remained positioned three notches below the bank's Adjusted BCA of ba2, in line with Moody's standard notching guidance for contractual non-viability perpetual maturity securities.

The affirmation of the bank's Baa3 long-term deposit ratings reflects our assessment of a very high probability of support from the Government of Colombia (Baa2, stable). In our view, Davivienda would benefit from government support in an event of financial stress considering its 15% market share in local deposits as of December 2022. This results in two notches of uplift from the bank's ba2 BCA.

## FACTORS THAT COULD LEAD TO AN UPGRADE OR DOWNGRADE OF THE RATINGS

Davivienda's BCA could be upgraded if the bank reports sustainable and material improvement of its profitability and capital metrics in the next 18 months. A possible upgrade of the bank's BCA would also depend on asset quality metrics that remain in line with levels observed currently.

Moody's could downgrade Davivienda's BCA if there is a sizable and consistent weakening in the bank's asset quality metrics. The BCA could also be lowered if the bank's profitability and capitalization weakens materially. The bank's deposit ratings would not be affected by a downgrade of the Government of Colombia's sovereign bond rating of Baa2, which is unlikely at this time given the stable outlook on the rating.

## METHODOLOGY USED

The principal methodology used in these ratings was Banks Methodology published in July 2021 and available at <https://ratings.moodys.com/api/rmc-documents/71997>. Alternatively, please see the Rating Methodologies page on <https://ratings.moodys.com> for a copy of this methodology.

## REGULATORY DISCLOSURES

For further specification of Moody's key rating assumptions and sensitivity analysis, see the sections Methodology Assumptions and Sensitivity to Assumptions in the disclosure form. Moody's Rating Symbols and Definitions can be found on <https://ratings.moodys.com/rating-definitions>.

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