

CREDIT OPINION

3 July 2018

Update

 Rate this Research

RATINGS
Grupo Aval Acciones y Valores S.A.

Domicile	Bogota, Distrito Capital, Colombia
Long Term CRR	Not Assigned
Long Term Issuer Rating	Not Available
Type	Not Available
Outlook	Stable

Please see the [ratings section](#) at the end of this report for more information. The ratings and outlook shown reflect information as of the publication date.

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Grupo Aval Acciones y Valores S.A.

Update to credit analysis - Double leverage and earnings stream remain adequate

Summary

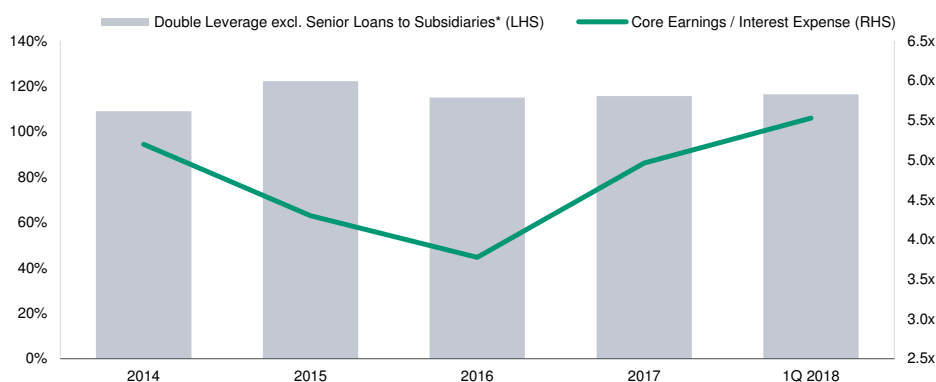
[Grupo Aval Acciones y Valores S.A.](#)'s (Grupo Aval) Ba2 issuer rating reflects the structural subordination of the bank holding company's liabilities to the liabilities of its highly regulated operating entities, particularly [Banco de Bogotá](#) (deposits Baa2/senior unsecured Baa2 negative, BCA ba1). Grupo Aval's ratings are notched off Banco de Bogotá's standalone Baseline Credit Assessment (BCA) of ba1. The one-notch differential takes into account the fact that not all resources flowing up from the operating entities into the group may be available in the event of stress.

The differential is limited to only one notch because it incorporates Grupo Aval's strong track record of intrinsic financial performance in terms of the dividend income from its subsidiaries. The group is a bank holding company controlling a diversified, multi-branded group of banks that target different segments of the financial market in Colombia. Banco de Bogotá, Grupo Aval's represents about 64% of its total consolidated gross loans.

We also assign a Ba2 rating to Grupo Aval's foreign-currency senior debt notes issued through Grupo Aval Limited, its subsidiary in the Cayman Islands. The senior debt ratings are based on Grupo Aval's irrevocable and unconditional guarantee of Grupo Aval Limited's liabilities under the indentures.

Exhibit 1
Debt service and leverage ratios

Leverage remains stable, while debt servicing has improved



*Investments in subsidiaries, goodwill and subordinated loans to subsidiaries as a percentage of shareholders' equity excluding asset revaluations.

Source: Moody's Investors Service

Credit strengths

- » Adequate and stable double leverage ratio
- » Ample and sound volume of dividend inflow from subsidiaries

Credit challenges

- » Results from operating subsidiaries affected by increasing credit costs
- » The structural subordination of the bank holding company's liabilities to those of its highly regulated operating entities

Outlook

Despite the negative outlook on Banco de Bogotá's ratings, Grupo Aval's ratings have a stable outlook, reflecting (1) the expected stability in the intrinsic strength of its main operating entities, irrespective of the recent deterioration in asset quality; and (2) its adequate leverage, which is expected to remain stable.

Factors that could lead to an upgrade

A rating upgrade would be associated with an upgrade of Banco de Bogotá's BCA, which in turn could be driven by an improvement in capital, coupled with the preservation of asset quality and profitability.

More specifically, Banco de Bogotá's BCA would face upward pressure if its nonperforming loan ratio (90+ days PDLs) remains below 1.5% on a sustained basis or its capitalization (tangible common equity/risk-weighted assets) is above 11.5%.

Factors that could lead to a downgrade

Debt issuances or further acquisitions by the group or its subsidiaries, resulting in a sustained deterioration in the double leverage ratio, would trigger a reassessment of the notching differential between the BCA of Banco de Bogotá and Grupo Aval's issuer and debt ratings.

A lower BCA for Banco de Bogotá could have a similar effect on the ratings.

More specifically, Banco de Bogotá's BCA would face downward pressure if its capitalization were to decrease below 6.5% or if the bank were to experience a substantial deterioration in asset risks, which would lead to a sustained deterioration in its profitability.

This publication does not announce a credit rating action. For any credit ratings referenced in this publication, please see the ratings tab on the issuer/entity page on www.moody's.com for the most updated credit rating action information and rating history.

Key Indicators

Exhibit 2

Grupo Aval Acciones y Valores S.A. [1]

	1Q 2018[4]	2017 [4]	2016[4]	2015	2014	2013	2012
Total Assets (COP Billion)	21,288	21,949	20,884	33,572	31,369	27,170	22,636
Investments in Subsidiaries (COP Billion)	16,997	18,197	17,108	17,198	15,529	12,757	10,659
Loans to Subsidiaries (COP Billion)	1,842	2,064	2,184	3,945	1,804	1,412	1,839
Total Debt (COP Billion)	4,417	4,657	4,467	6,032	4,447	3,807	4,704
Shareholders' Equity (COP Billion)	15,651	16,838	15,985	27,110	26,430	22,938	17,530
Core Earnings (COP Billion) [2]	358	1,355	1,351	1,204	1,135	994	835
Interest Expense (COP Billion)	65	273	358	283	218	276	243
Double Leverage excl. Senior Loans to Subs [3]	116.5%	115.7%	115.0%	122.3%	109.0%	113.4%	113.1%
Debt / Core Earnings [5]	3.1x	3.4x	3.3x	5.0x	3.9x	3.8x	5.6x
Core Earnings / Interest Expense	5.5x	5.0x	3.8x	4.3x	5.2x	3.6x	3.4x

[1] Source: Grupo Aval + Grupo Aval Limited's unconsolidated data in IFRS for 2015 and later periods, Colombian GAAP and dividend income in banking GAAP for all other periods; Moody's estimates.

[2] Includes cash flow from dividends, investments and net operating cash inflows.

[3] Investments in subsidiaries, goodwill and subordinated loans to subsidiaries as a percentage of shareholders' equity excluding asset revaluations. In 2018 Grupo Aval adopted IFRS 9 standards which reduced the shareholders' equity attributed to controlling interest by about COP \$500 billion, impacting negatively the double leverage ratio."

[4] Core earnings have been annualized for comparability.

[5] Total assets and shareholders' equity exclude revaluations (IAS 27 rule [IFRS]).

Sources: Grupo Aval, "Moody's Investors Service calculations"

Profile

Grupo Aval Acciones y Valores S.A. is the largest financial conglomerate in Colombia, with COP232.2 trillion in total assets (\$83 billion) as of March 2018. The group owns the third-largest (Banco de Bogotá), fifth-largest (Banco de Occidente S.A.), eighth-largest (Banco Popular S.A.) and 11th-largest (Banco Comercial AV Villas S.A.) banks in the country in terms of loans. Grupo Aval also incorporates geographic and industry diversification through (1) Banco de Bogotá's [BAC International Bank, Inc.](#) (BAC, deposits: Baa3 stable, BCA: baa3), a universal bank present throughout Central America; (2) Corporación Financiera Colombiana S.A., Colombia's largest merchant bank; and (3) the ownership of the country's largest private pension fund manager AFP Porvenir S.A. (Porvenir).

Together, Grupo Aval's banks constitute the largest franchise in Colombia, with a combined market share of about 25% and 26% of the financial system's loans and deposits, respectively, as of March 2018. The group has around 14 million clients in Colombia and Central America, with a network of 2,115 branch offices and 5,774 ATMs.

Detailed credit considerations

Structural subordination

Grupo Aval's Ba2 issuer rating "reflects the structural subordination of the bank holding company's liabilities to the liabilities of its highly regulated operating entities, particularly Banco de Bogotá. The differential takes into account the fact that not all resources flowing up from the operating entities into Grupo Aval may be available in the event of stress. That said, the upstreaming of dividends has been consistent across all subsidiaries.

Financial strength hinges on Grupo Aval's sound dividend income

Grupo Aval maintains a strong track record of dividend income from its subsidiaries. The group is a bank holding company controlling a diversified, multi-branded group of banks that target different segments of the financial market in Colombia.

The acquisitions made over time by Grupo Aval have strengthened the franchise of its existing operating entities and have resulted in an increase in goodwill. Banco de Bogotá's acquisition of Guatemala's Grupo Financiero Reformador and Banco BAC de Panamá (both completed in December 2013) strengthened BAC's market presence in two key growth markets in the region. The acquisition of BBVA Horizonte AFP S.A. in Colombia (1) added a notable market share to Porvenir, (2) assured Porvenir's dominance in the administration of mandatory pension funds and severance funds in Colombia, and (3) strengthened its position as the third-largest provider of voluntary pensions.

However, the bottom-line results generated by the group's operating companies have been affected by specific problematic credit exposures, such as (1) *Electrificadora del Caribe S.A. E.S.P. (Electricaribe)*, a distressed electricity distribution company that is one of the largest corporate borrowers in the country's banking system; (2) *Concesionaria Ruta del Sol S.A.S. (CRDS)*, a highway construction project that will unite Bogotá with Colombian ports on the Atlantic coast and in which the group had a minority interest; and (3) certain companies related to Bogotá's mass transportation system (SITP).

As of March 2018, the exposures, reserve coverage and provisioning strategy for this credits are as follows: (1) SITP (total exposure: \$180 million): we expect Grupo Aval to continue to provision throughout 2018 (current stock of reserves cover 15% of the total loan), (2) Electricaribe (\$232 million): reserves already cover 80% of the exposure and Grupo Aval's management expressed that it will not add more provisions for this particular credit; and (3) CRDS (\$342 million): reserves already cover 13% of the exposure and the most likely scenario is that this credit will need more provisions.

Double leverage ratio is stable and adequate

The more a bank holding company relies on debt to fund the equity in its subsidiaries, the greater the structural subordination imposed on holding company creditors.

Our calculation of double leverage includes investments in subsidiaries at book value, subordinated loans to subsidiaries and goodwill as a percentage of shareholders' equity (excluding asset revaluations). Grupo Aval's double leverage was at 116.5% as of March 2018, remaining somewhat stable in the past year. At the same time, its investments in subsidiaries, measured at book value, represented around 3.8x total debt.

Strong governance reduce concerns arising from family ownership

We acknowledge the depth and track record of Grupo Aval's professional management at all levels. The group and its subsidiaries maintain sound risk management policies and best practices, supported by experienced management teams at both the holding and operating entity levels.

The controlling family has had the right to elect a majority of directors and executive officers, and set management policies that have proven effective over time, reducing concerns about potential corporate governance risks. The controlling shareholders have also proven to be willing supporters of the group in the event of stress.

Although Grupo Aval is not supervised through banking regulators, it is registered and regulated under Colombia's National Registry of Shares and Issuances, and the US Securities and Exchange Commission, and is required to comply with corporate governance and periodic reporting requirements. Grupo Aval is traded on the NYSE Euronext under the ticker AVAL.

Foreign-currency debt rating

We rate Grupo Aval's 10-year foreign-currency senior unsecured notes of \$1 billion (coupon of 4.75%), issued through Grupo Aval Limited (its subsidiary in the Cayman Islands), at Ba2.¹ The Ba2 long-term foreign-currency debt rating is based on Grupo Aval's irrevocable and unconditional guarantee of Grupo Aval Limited's liabilities under the indentures.

Ratings

Exhibit 3

Category	Moody's Rating
GRUPO AVAL ACCIONES Y VALORES S.A.	
Outlook	Stable
Issuer Rating	Ba2
ST Issuer Rating	NP
BAC INTERNATIONAL BANK, INC	
Outlook	Stable
Counterparty Risk Rating	Baa2/P-2
Bank Deposits	Baa3/P-3
Baseline Credit Assessment	baa3
Adjusted Baseline Credit Assessment	baa3
Counterparty Risk Assessment	Baa2(cr)/P-2(cr)
BANCO DE BOGOTA S.A.	
Outlook	Negative
Counterparty Risk Rating	Baa1/P-2
Bank Deposits	Baa2/P-2
Baseline Credit Assessment	ba1
Adjusted Baseline Credit Assessment	ba1
Counterparty Risk Assessment	Baa1(cr)/P-2(cr)
Senior Unsecured	Baa2
Subordinate	Ba2
GRUPO AVAL LIMITED	
Outlook	Stable
Bkd Senior Unsecured	Ba2

Source: Moody's Investors Service

Endnotes

¹ See Moody's Press Release titled "[Moody's assigns issuer and debt ratings to Grupo Aval](#)," 18 September 2012.

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