

CREDIT OPINION

21 June 2019

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	Negative

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 following the affirmation on the Ba2 ratings, outlook remained negative

Summary

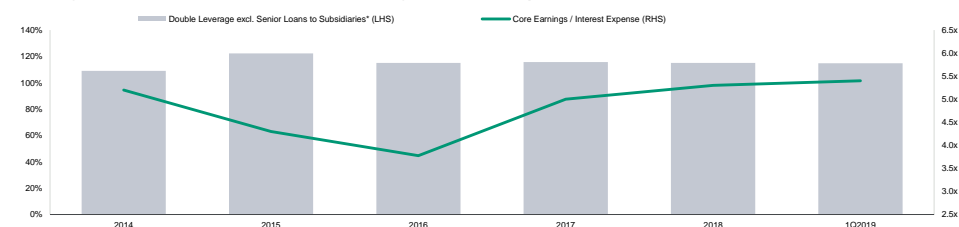
On 28 May 2019, we affirmed [Grupo Aval Acciones y Valores S.A.](#)'s (Grupo Aval) Ba2 issuer rating and maintained its negative outlook.¹ While Grupo Aval has multiple financial subsidiaries that include banks in Colombia, a merchant bank, a pension and severance fund manager and a Central America banking group, its negative outlook incorporates the downward pressure on [Banco de Bogotá S.A.](#)'s (Banco de Bogotá, Baa2 negative, ba1) baseline credit assessment (BCA), reflected in its own negative outlook. Banco de Bogotá is the group's chief operating entity, in which 64% of gross loans and 62% of dividends the consolidated group are booked as of March 2019. Grupo Aval's ratings incorporate the structural subordination of the bank holding company's liabilities versus the liabilities of the bank and its other subsidiaries and are notched off Banco de Bogotá's BCA. Moody's does not incorporate governmental support in the holding company's ratings.

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 remains adequate



*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

- » Ample and sound volume of dividend inflow from subsidiaries
- » Diversified source of earnings through multiple financial subsidiaries that include banks in Colombia, a merchant bank, a pension and severance fund manager and a Central American banking group

Credit challenges

- » Main operating subsidiary challenged by the more volatile and weaker Central American operating environments
- » The structural subordination of the bank holding company's liabilities to those of its highly regulated operating entities

Outlook

The negative outlook on Grupo Aval's ratings incorporates the downward pressure on Banco de Bogota's baseline credit assessment, reflected in its own negative outlook.

Factors that could lead to an upgrade

- » Upward pressures on Grupo Aval ratings would be associated with similar pressures on Banco do Bogota's BCA. Given the current juncture upward pressures are limited.
- » However ratings could be stabilized if and when Banco de Bogotá's ratings were stabilized following an improvement on Central American economic environments or if the bank is capable to maintain current asset quality coupled with constant profitability levels above 2.0% net income to tangible banking assets.

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, that could materialized if the current negative outlook is translated into deterioration in the bank's financial performance. More specifically 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. (Consolidated Financials) [1]

	1Q2019 [5]	2018	2017[5]	2016[5]	2015	2014	Average
Total Assets (COP Billion)	24,098	23,566	21,949	20,884	33,572	31,369	25,906
Investments in Subsidiaries (COP Billion)	19,095	19,580	18,197	17,108	17,198	15,529	17,785
Loans to Subsidiaries (COP Billion)	2,037	1,886	2,064	2,184	3,945	1,804	2,320
Total Debt (COP Billion)	4,817	4,924	4,657	4,467	6,032	4,447	4,891
Shareholders' Equity (COP Billion)	17,781	18,222	16,838	15,985	27,110	26,430	20,394
Core Earnings (COP Billion) [2]	357	1,360	1,355	1,351	1,204	1,135	1,127
Interest Expense (COP Billion)	66	259	273	358	283	218	243
Double Leverage excl. Senior Loans to Subs [3]	114.8%	115.0%	115.7%	115.0%	122.3%	109.0%	115.3%
Debt / Core Earnings [4]	3.4x	3.6x	3.4x	3.3x	5.0x	3.9x	3.8x
Core Earnings / Interest Expense	5.4x	5.3x	5.0x	3.8x	4.3x	5.2x	4.8x

[1] Grupo Aval + Grupo Aval Limited unconsolidated data. [2]Includes cash flow from dividends, investments and net operating cash inflows; IFRS. [3]Investments in subsidiaries, goodwill and subordinated loans to subsidiaries as percentage of shareholder's equity excluding asset revaluations [4]Core earnings have been annualized for comparability [5]Total Assets and Shareholders' Equity exclude revaluations (IAS 27 rule (IFRS))

Source: Moody's Investors Service; Company Filings

Profile

Grupo Aval Acciones y Valores S.A. is the largest financial conglomerate in Colombia, with COP258.3 trillion in total assets (\$82 billion) as of March 2019. The group owns the third-largest (Banco de Bogotá, 11.9%), fifth-largest (Banco de Occidente S.A., 5.9%), eighth-largest (Banco Popular S.A., 4.2%) and tenth-largest (Banco Comercial AV Villas S.A., 2.5%) 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 negative, 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 second-largest franchise in Colombia, with a combined market share of about 24.5% of the financial system's loans as of March 2019. The group has around 16 million clients in Colombia and Central America, with a network of 2,124 branch offices and 5,570 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. Further Grupo Aval maintains a pretty diversified banking operation and not only relies on income coming from its equity method interest. As such the group also has other sources of income as the proceedings of the loans the company has granted to its operating entities and the fees it charges to their banks due to the services it provides to them.

We also rate Grupo Aval's 10-year foreign-currency senior unsecured notes of \$1 billion, issued through Grupo Aval Limited (its subsidiary in the Cayman Islands), at Ba2, negative. The ratings on this debt consider that the cash flow used to pay the coupons of this issuance relies on the performance of the loans granted with the proceeds of this issuance to its operating companies what put this flows at the same level of any other interest payment of other financial obligation of any given Grupo Aval's subsidiary.

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 main source

of dividend has been its flagship bank, Banco de Bogotá. In 2018, Banco de Bogotá was responsible for providing 62% of the total dividends received by Grupo Aval, which represented a moderate payout ratio of 45% of the bank's net income. The second most important provider of dividends to Grupo Aval was Banco de Occidente with 14%, followed by the pension fund manager Provenir with 13%.

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 2019, reserve coverage and provisioning strategy for these credits were as follows: (1) SITP (total exposure: \$166 million): Grupo Aval has provisioned 39% of the exposure, which can change depending on the developments of the restructuring plan for the projects, (2) Electricaribe (\$232 million): reserves already cover 100% of the exposure; and (3) CRDS (\$224 million): Grupo Aval has covered 45% of the total exposure.

In addition, Grupo Aval may confront potential contingencies as it has been charged for three alleged violations to the Colombian free competition regime associated to the project². Fines could amount up to USD70 million or around 8% of the last year net income.

Double leverage ratio is stable, ample interest coverage

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 115% as of March 2019, remaining stable in the past years. Moody's considers double leverage high when it exceeds by a meaningful amount on a sustained basis the 115% threshold. At the same time, the company's coverage is high as core earnings represent 5.4x interest expenses.

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.

Under the Colombian Financial Conglomerates Law, which came into force on February 2019, Grupo Aval has become supervised by the Colombian banking regulator. In addition, Grupo Aval is registered and regulated under Colombia's National Registry of Shares and Issuers, 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 Ba2.³ 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 5

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

Source: Moody's Investors Service

Endnotes

- 1 Please see or release entitled:
- 2 For further details on the violations please see Grupo Aval's earnings transcript of [September 2018](#)
- 3 See Moody's Press Release titled "[Moody's assigns issuer and debt ratings to Grupo Aval](#)," 18 September 2012.

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