

## CREDIT OPINION

9 January 2018

Update

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### RATINGS

#### Grupo Aval Acciones y Valores S.A.

Domicile	Bogota, Distrito Capital, Colombia
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 - Higher credit costs have taken their toll on profits

### Summary

Grupo Aval Acciones y Valores S.A.'s (Grupo Aval) Ba2 issuer rating reflects the incorporation of structural subordination of the bank holding company's liabilities versus the liabilities of its highly regulated operating entities, mainly composed of [Banco de Bogotá](#) (deposits Baa2/senior unsecured Baa2 stable, 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 that not all resources flowing up from the operating entities into Grupo Aval could be available, in case of stress.

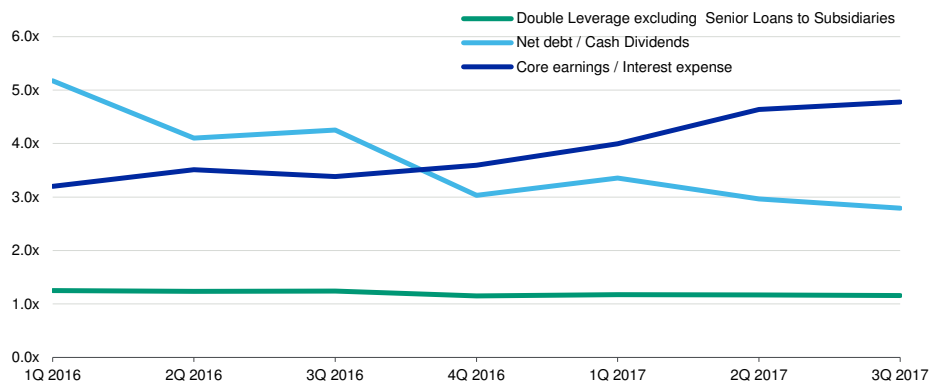
The differential is limited to only one notch because it incorporates Grupo Aval's strong track record of intrinsic financial performance based on dividend income from its subsidiaries. The group is a bank holding company controlling a diversified, multi-branded group of banks that target different segments of the financial market in Colombia. Banco de Bogotá nevertheless contributes with about 60% of total dividends received, but the rest of dividends have also been consistently streamed up to the holding company.

Moody's also assigns a Ba2 rating to Grupo Aval's foreign currency senior debt notes issued through its subsidiary in the Cayman Islands, Grupo Aval Limited. 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

Stable leverage while debt servicing has improved



Source: Moody's Investor Services

## Credit challenges

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

## Credit strengths

- » Ample and sound volume of dividend inflow from subsidiaries
- » Double leverage ratio is adequate and stable

## Rating outlook

Grupo Aval's ratings have a stable outlook reflecting the stable outlook on Banco de Bogotá's ratings. Also, it incorporates the company's adequate leverage position, which is expected to remain stable.

## Factors that could lead to an upgrade

An upgrade in Grupo Aval's ratings would be associated with an upgrade of Banco de Bogotá's BCA, which in turn, could be driven by the improvement in capital coupled with preserved asset quality and profitability.

## Factors that could lead to a downgrade

A downgrade of Banco de Bogotá's standalone BCA could have a similar effect on Grupo Aval's ratings.

In addition, debt issuances or further acquisitions by Grupo Aval or its subsidiaries resulting in sustained deterioration of double leverage ratios, would trigger a reassessment of both (i) the intrinsic strength of the group's operating entities and (ii) the notching differential between the BCA of Banco de Bogotá and Grupo Aval's issuer and debt ratings.

## Key Indicators

Exhibit 2

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

	3Q2017 [5]	2016[5]	2015	2014	2013	2012
Total Assets (COP Billion)	21,754	20,884	33,572	31,369	27,170	22,636
Investments in Subsidiaries (COP Billion)	17,744	17,108	17,198	15,529	12,757	10,659
Loans to Subsidiaries (COP Billion)	1,759	2,184	3,945	1,804	1,412	1,839
Total Debt (COP Billion)	4,573	4,467	6,032	4,447	3,807	4,704
Shareholders' Equity (COP Billion)	16,391	15,985	27,110	26,430	22,938	17,530
Core Earnings (COP Billion) [2]	981	1,351	1,204	1,135	994	835
Interest Expense (COP Billion)	205	358	283	218	276	243
Double Leverage excl. Senior Loans to Subs [3]	116.0%	115.0%	122.3%	109.0%	113.4%	113.1%
Debt / Core Earnings [4]	3.5x	3.3x	5.0x	3.9x	3.8x	5.6x
Core Earnings / Interest Expense	4.8x	3.8x	4.3x	5.2x	3.6x	3.4x
Total Liabilities / Total Assets	24.7%	23.5%	19.2%	15.7%	15.6%	22.6%

[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 percentage of shareholders' 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: Grupo Aval and Moody's calculations

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](http://www.moody's.com) for the most updated credit rating action information and rating history.

## Profile

Grupo Aval is the largest financial conglomerate in Colombia with COP228 trillion in total assets (78 US billion) as of September 2017. The Group owns the third largest bank in the country in terms of loans, Banco de Bogotá, as well as the fifth largest Banco de Occidente S.A. (unrated), the eighth largest Banco Popular S.A. (unrated) and the eleventh largest Banco Comercial AV Villas S.A. (unrated). Grupo Aval also incorporates geographic and industry diversification through Banco de Bogotá's [BAC International Bank, Inc.](#) (BAC, Baa3 stable, baa3), a universal bank present throughout Central America and Corporación Financiera Colombiana S.A. (Corficolombiana, unrated), Colombia's largest merchant bank, as well as from the group's ownership of the country's largest private pension fund manager AFP Porvenir S.A. (Porvenir, unrated).

Combined, Grupo Aval's banks comprise the largest franchise in Colombia, with a combined market share of about 25% and 27% of the financial system's loans and deposits, respectively, as of December 2016. The group has around 14 million clients in Colombia and Central America with a branch network of 1,438 branch offices and 3,809 ATMs in Colombia and 351 branch offices and 1,930 ATMs in Central America.

## Detailed credit considerations

### Structural subordination

Grupo Aval's Ba2 issuer ratings reflect the incorporation of the structural subordination of the liabilities of the holding company versus the liabilities of its highly regulated operating entities, namely Banco de Bogotá. The differential takes into account that not all resources flowing up from the operating entities into Grupo Aval may be available, in case of stress. That said, upstream of dividends has been consistent among 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 yet these have also carried an increase in goodwill. Banco de Bogotá's acquisitions of Guatemala's Grupo Financiero Reformador (unrated) and Banco BAC de Panamá (unrated), both completed in December 2013, strengthened the market presence of BAC in two key growth markets in the region. The acquisition of BBVA Horizonte AFP S.A. in Colombia added notable market share to Porvenir and assured Porvenir's dominance in the administration of mandatory pension funds and severance funds in Colombia and its position as the third-largest provider of voluntary pensions.

However, the bottom line results generated by its operating companies have been affected by specific problematic credit exposures, such as Electricadora del Caribe S.A. E.S.P. (Electricaribe, unrated), a distressed electricity distribution company that is one of the largest corporate borrowers in the country's banking system, Concesionaria Ruta del Sol S.A.S. (CRDS, unrated), 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 certain companies related to Bogotá's mass transportation system (SITP).

In this context, credit costs have been increasing consistently in 2017, and we expect this trend to continue as the group keeps provisioning for exposures to problematic SITPs, amounting to USD 160 million (current stock of reserves cover 12% of total and are expected to reach up to 50% throughout 2018). Results will be less impacted in 2018 for Electricaribe USD 200 million exposure (reserves already cover 70% of the exposure as of December 2017 and management expects to increase them to 80% by the first quarter of 2018). The credit cost pressures also derive from the weak economic environment impacting corporate borrowers and high unemployment affecting loans to households.

However, we expect some relief to earnings pressures in the first quarter of 2018 as the group informed that in January 2018 the Colombian National Infrastructure Agency (Agencia Nacional de Infraestructura) had paid around USD 130 million to the banks belonging to the group. After this first installment CRDS exposure was lowered to USD 307 million from the USD 441 million reported in September 2017.

### 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.

Moody's 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, which therefore, was equivalent to 116% in September 2017, remaining somewhat stable in the last year. At the same time, Grupo Aval's investments in subsidiaries measured at book value represent around 3.8-times total debt.

### Strong governance bodies reduce concerns from family ownership

Moody's acknowledges 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 ability to elect a majority of directors, executive officers and set management policies which 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 cases 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 in the NYSE Euronext under ticker AVAL.

### Foreign Currency Debt Rating

Moody's rates ten-year foreign currency senior unsecured notes of USD1 billion (coupon of 4.75%); first rated on 18 September 2012<sup>1</sup> and issued through Grupo Aval's subsidiary in the Cayman Islands, Grupo Aval Limited at Ba2. 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 indenture:

### Ratings

Exhibit 3

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

Source: Moody's Investors Service

### Endnotes

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

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