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GRUPO AVAL ACCIONES Y VALORES S.A.

2Q2016 CONSOLIDATED EARNINGS RESULTS CALL TRANSCRIPT

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PARTICIPANTS

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Chief Executive Officer

Participants Question and Answer Session
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Nicolás Riva – Citi
Sebastián Gallego – Credicorp
Alonso Aramburu – BTG Pactual
Carlos Gomez – HSBC
Mayara Riddlebaugh – Wells Fargo

PRESENTATION

Operator

Good morning, ladies and gentlemen, and welcome to the Grupo Aval Second Quarter 2016 Consolidated Results under IFRS Conference Call. My name is Richard and I'll be your operator for today's call. At this time, all participants are in a listen-only mode. Later, we will conduct a question-and-answer session.

Grupo Aval Acciones y Valores S.A., Grupo Aval, is an issuer of securities within Colombia and in the United States, registered with Colombia's National Registry of Shares and Issuers, Registro Nacional de Valores y Emisores, and the United States Securities and Exchange Commission, SEC. As such, it is subject to the control of the Superintendency of Finance and compliance with applicable US securities regulation as a foreign private issuer under Rule 405 of the U.S. Securities Act of 1933. Grupo Aval is a not a financial institution and is not supervised or regulated as a financial institution in Colombia.

As an issuer of securities in Colombia, Grupo Aval is required to comply with periodic reporting requirements and corporate governance, however, it is not regulated as a financial institution or as a holding company of banking subsidiaries and, thus, is not required to comply with capital adequacy regulations applicable to banks and other financial institutions. All of our banking subsidiaries, Banco de Bogotá, Banco de Occidente, Banco Popular, Banco AV Villas, Porvenir and Corficolombiana, are subject to inspection and surveillance as financial institutions by the Superintendency of Finance.

Although we are not a financial institution, until December 31st, 2014, we prepared the unaudited consolidated financial information included in our quarterly reports in accordance with the regulations of the Superintendency of Finance for financial institutions and generally accepted accounting principles for banks to operate in Colombia, also known as Colombian Banking GAAP, because we believe that presentation on that basis most appropriately reflected our activities as a holding company of a group of banks and other financial institutions.

However, in 2009, the Colombian Congress enacted Law 1314 establishing the implementation of IFRS in Colombia. As a result, since January 1st, 2015, financial entities and Colombian issuers of publicly traded securities, such as Grupo Aval, must prepare financial statements in accordance with IFRS. IFRS is applicable under Colombian regulations differs in certain aspects from IFRS as currently issued by the IASB. The unaudited consolidated financial information included in this document is presented in accordance with IFRS as currently issued by the IASB. Details of the calculations of non-GAAP measures such as ROAA and ROAE, among others, are explained when required in this report.

Because of our recent migration to IFRS and recent implementation of IFRS accounting principles, the unaudited consolidated financial information for the first and second quarters of 2016, and the comparative information for the relevant unaudited consolidated periods of 2015 presented herein, may be subject to further amendments.

This report may include forward-looking statements, which actual results may vary from those stated herein as a consequence of changes in general, economic and business conditions, changes in interest and currency rates and other risk factors as evidenced in our Form 20-F available at the SEC webpage. Recipients of this document are responsible for the assessment and use of the information provided herein.

Grupo Aval will not have any obligation to update the information herein and shall not be responsible for any decision taken by investors in connection with this document. The content of this document and the unaudited figures included herein are not intended to provide full disclosure on Grupo Aval or its affiliates.

When applicable, in this document, we refer to billions as thousands of millions.

Today, the call will be conducted by Mr. Luis Carlos Sarmiento Gutiérrez, Chief Executive Officer of Grupo Aval; Mr. Diego Solano, Chief Financial Officer of Grupo Aval; Mrs. Tatiana Uribe, Investor Relations Officer of Grupo Aval.

And I will now turn the call over to Mr. Luis Carlos Sarmiento. Mr. Sarmiento, you may begin.

Luis Carlos Sarmiento Gutiérrez – Grupo Aval Acciones y Valores S.A. – CEO

Thank you, Richard. Good morning and thank you very much for joining our call. To start with, it is my pleasure to report that our second quarter results met our expectations. In the next few minutes, I will highlight a few of our results and later on in the call, Diego will address these and other points in detail.

But I feel that I should first address Banco de Bogotá's deconsolidation of Corficolombiana. As you recall, last May during our first quarterly call, we shared with you our concern over our rating agencies' actions with respect to Banco de Bogotá's capital structure. We mentioned that Moody's had downgraded Banco de Bogotá's stand-alone baseline credit assessment, as well as its long term foreign denominated subordinated debt, and furthermore, that it had placed these ratings and credit review for further downgrades.

Grupo Aval's own ratings had been dragged down by Banco de Bogotá's for Moody's policy to act on a holding company's ratings after it takes action on one of its subsidiaries. We further explained that we have committed to present the plan of action to Moody's during June and that our plan would hopefully prevent further downgrades by Moody's.

We did in fact present Moody's with our plan that consisted in Banco de Bogotá's ceding control of Corficolombiana to Grupo Aval, its holding company. This action entailed substantial, financial and capital structure benefits for Banco de Bogotá and for Grupo Aval, it represented the opportunity to directly control Corficolombiana. We explained these benefits in detail to the market on a pro forma basis during our late June call in which some of you participated.

I am now happy to report that the deconsolidation of Corficolombiana was done successfully and that the resulting effects were very much in line and even better than forecasted. In fact, after capitalizing the Ps. 2.2 billion (Mr. Sarmiento meant trillion) non-recurrent gain that Banco de Bogotá generated as a result of this transaction, its June 30, 2016 Tier 1 capital ratio will improve to 9.3% and its total solvency ratio to 14.3%. As you recall, we had estimated these numbers as 9.1% and 13.6%, respectively.

Finally, although Moody's completed its credit review without further downgrades, we expect that during our future evaluation, this improvement, which is no longer an estimation but rather a reality, will be taken into consideration for a rating upgrade.

And now let me refer briefly the Colombia's current macroeconomic landscape. Just as we had anticipated, in the midst of high inflation and a contractionary monetary policy, Colombia's economy has continued to slow down. In fact, our expectations are now in line with the Bloomberg consensus of analysts that place real GDP growth for 2016 at around 2.3%. We do however continue to believe in the efficacy of the Central Bank's monetary policy, and therefore we expect that inflation will be contained starting next month, and that at the end of the year, this pricing index will be at least 150 basis points lower than the 9% observed at the end of July.

We also believe that the Central Bank will probably not have to increase its discount rate any further during this year or at most another 25 basis points. Although DTF has continued to rise, it sometimes moves unexpectedly and not in unison with the Central Bank's discount rate. Therefore, we are making serious efforts to price our largest commercial loans off of the Central Bank's rate or IBR.

We remain confident that positive trends in inflation, current account deficit and growth will start to be seen towards the end of 2016, and that these will carry on to 2017. We are optimistic about the impact on consumer and investor confidence arising from the recently agreed upon peace treaty with the FARC guerrilla and we foresee a positive impact, as yet unquantifiable, on the economy as a result.

Finally, we continue to see sources for GDP and loan growth from the 4G infrastructure projects over the next few years. We feel that unemployment continues to be manageable at levels of 10%. The exchange rate has revalued throughout 2016 and continues to hold steady in a level that we believe sustainable for the rest of this year between Ps. 2,950 and Ps. 3,050 per dollar, especially if oil prices continue to hover between $45 and $50 per barrel.

Finally, we have high hopes that the government will understand the need to pass through Congress a business friendly tax reform and also for a mild "El Niño" climate occurrence. If these hopes don't pan out, we might have to re-evaluate our current economic estimations. With respect to our other major market, Central America continues to be benefited by the US economic progress and by relatively low prices of oil. As a result, our forecast for growth in this region remains unchanged at approximately 4% for 2016.

Now turning to Aval's financial results, these are the main highlights. Diego will refer to each of these in more detail following this summary. Attributable net income for the quarter was Ps. 601.1 billion or Ps. 27 per share showing a 6% increase versus the comparable second quarter 2015 result of Ps. 569 billion or Ps. 26 per share. Attributable net income for the first semester of this year amounted to Ps. 1,247 billion, showing an increase of 12% versus the attributable net income for the first semester of 2015, which amounted to Ps. 1,112 billion, both numbers exclude the non-recurrent wealth tax expense.

Our total net loan portfolio grew by 13.3% in the last 12 months and by 1.6% in the quarter. In absence of the exchange rate movements of the period, the net loan portfolio grew by 2.4% in the quarter. Deposits grew by 11.8% in the last 12 months and by 0.1% in the quarter. Once again, in absence of the exchange rate movements of the period, the deposits grew by 0.9% in the quarter. Consequently, the ratio of deposits to net loans closed at 96% in June 30, 2016.

As the Central Bank has increased its discount rate by 200 basis points this year, the DTF has kept up and has increased similarly, however, in a much more volatile manner. Consequently, average yield on loans has increased by 140 basis points in the last 12 months and 41 basis points between the quarters ending in March and June 2016, closing at 11.3% for this quarter.

Cost of funds on the other hand, increased by 110 basis points in the last 12 months and 47 basis points in the quarter closing at 4.5%. Therefore, the spread between average yield on loans and average cost of funds has expanded by 30 basis points in the last 12 months. NIM on loans was 6.5% for the quarter and increased 10 basis points versus the NIM on loans 12 months back and held steady versus the same ratio during the first quarter of this year.

NIM on total investments was 0.8%, steady when compared to the same ratio during the second quarter of 2015, but 50 basis points less than the 1.3% observed for the first quarter of 2016.

Total NIM was 5.6% in the second quarter of 2016 and increased by 30 basis points versus this same number during the second quarter of 2015. Mostly as a result of the decrease in the NIM and investments, total NIM for this past quarter showed a slight decrease versus the total NIM of 5.7% in the first quarter of this year.

Total cost of risk during the second quarter of 2016 continued to be affected by non-recurrent provisions, mostly as a result of the Pacific Rubiales default. Cost of risk, which amounted to 2.1% before recoveries of allowances for loan losses and 1.9% after recoveries of allowances for loan losses would have been 1.9% and 1.7%, respectively, in the absence of these non-recurrent provisions.

We have now provisioned and written-off in its entirety the Pacific Rubiales risk and expect to have steady quarters going forward as far as cost of risk goes, and consequently, we expect that the full year's cost of risk will not exceed 1.9% before recoveries of allowances for loan losses.

Our consolidated efficiency ratio, measured as cost to income, was 47.2% for the quarter, in line with our expected efficiency for this year, 100 basis points better than our efficiency for 2015 and similar to our 2014 efficiency.

As of June 30, 2016, all our banks will show Tier 1 capital ratios in excess of 9.35% and as high as 10.1%. In the presentation, Banco de Bogotá is shown on an actual and pro-forma basis as this Tier 1 ratio will be materialized after the bank holds its shareholders' meeting on September 13, 2016 in which it will capitalize a substantial portion of its first semester 2016 earnings, including a Ps. 2.2 billion (Mr. Sarmiento meant trillion) non-recurrent gain from the deconsolidation of Corficolombiana.

Finally, during the second quarter of 2016, our return on average assets was 1.7%, and our return on average equity was 16.3%. Including the wealth tax expense, for the full year, we expect that our ROE will approximate 15%.

I now pass on the presentation to Diego, who will expand on the highlights that I just shared with you. Thank you and good day.

Diego Solano Saravia – Grupo Aval Acciones y Valores S.A. – CFO

Thank you, Luis Carlos. I will start with the evolution of the macroeconomic environment. I'll move to the power point presentation on page five. On that page, we present the evolution of some key macro drivers of our industry. Real GDP growth for the second quarter of 2016 was reported earlier this week at 2%, slightly below market expectations. Market consensus on Real GDP growth, as reported by Bloomberg, remained stable at 2.3% for 2016 and 3% for 2017. We share this view expecting 2016 growth to be in the 2.25% to 2.50% area and a mild improvement during 2017.

Some of the headwinds for recovery have lost strength. The improvement in international oil prices, the progress towards the construction initiation of fourth generation concessions, a more stable Colombian peso, our lower current account deficit, lower expected inflation and the end of the current interest rate cycle will favor recovery. Downsides will come from the potential impact of the terms of the tax reform and from oil price volatility as in the past.

Regarding the unemployment rate, the last three months have shown the mild deterioration that we expected. The number of jobs continues to increase though at a slower pace. The last data point available is that for July 2016 released yesterday. The figure reported was 9.8%, up from 8.8% reported for the same month a year earlier. Nevertheless, absolute current account figures continue to be fragile, relevant progress has been made since the peak of close to 8% in September 2015.

First quarter of this year, the current account deficit reached 5.6%. The Central Bank estimates a further improvement throughout the year going down to 5.3% by the end of the year. Lower demand of imported goods, the lower factor income outflows drove this improvement. On the financing side, the increase in direct and portfolio investment and higher remittances favored this result.

Moving to page six, we present inflation and some interest rate benchmarks. 12-month inflation negatively surprised the market since our last call. The truckers strike propelled 12 month July inflation up to close to 9%. Even though this high level appears to be short-lived, it resulted in an increasing market consensus on 2016 inflation from 6.95% to 7.4% as of yesterday.

We still expect inflation to be lower in the latter part of the year as we experience lower transference of the currency depreciation into inflation and the effect of Central Bank recent actions ceding to the economy, as well as the impact of the truckers strike and the climate issue on food prices fade away. We expect yearend 12 month inflation to trend downwards to the mid 7% area.

Consistent with the recent inflation data, the Central Bank has continued to raise its rates accumulating 325 basis points since August 2015 reaching 7.75%. The Central Bank voted six out of seven in favor of a pause in the yesterday's meeting. This change in policy may signal the end of the rising interest rate cycle with at most one or none additional hikes left. With inflation close to 9%, the Central Bank continues to have a negative real interest rate. The DTF, our benchmark rate has tracked the repo rate hovering in the 7.25% to 7.5% area over the past two weeks.

On page seven, we present oil prices effect on foreign exchange. The Colombian peso/dollar exchange rate closed June at Ps. 2,919, near 3% stronger than three months earlier and 12% weaker than the year earlier. Second quarter average exchange rate was Ps. 2,993, stronger than the previous quarter and 20% weaker than the same quarter a year earlier. Even though weaker than in the past, the negative correlation exists between the Colombian peso/US dollar exchange rate and the performance of oil prices.

During the quarter, capital flows and remittances into Colombia strengthened the Colombian peso. Over the past few days, the US dollar has strengthened against other currencies following Mrs. Yellen's recent positive comments on the US economy. In addition, oil producing countries' currencies have weakened as oil prices have slightly corrected downwards, following the inventory data and the OPEC members comments. The main drivers for the Colombian peso/US dollar exchange rate in the near future are expected to be the yearend monetary policy in the US and the oil supply demand balance as we get closer to 2017.

On page eight, we present our chart on Central America macroeconomic drivers. Our view on Central America continues to be positive. 2015 to 2018 GDP growth forecast for the region is 4.3% per IMF estimates. Monetary policy is expansionary, a positive correlation to the Consumer US economy will favor the region.

I will now move to the results of Grupo Aval starting on page nine with our asset evolution.

Balance sheet and P&L accounts that you find in this report reflect the presentation standard used on our 20-F. Total assets grew at 11.2% during the last 12 months, and presented a slight increase of 0.4% during the last quarter. In absence of the effect of the Colombian peso fluctuations on Central America, assets would have grown 7.8% and 1.2% respectively.

Broken down by region, over the past 12 months, our Colombian assets grew at 8.5%, while the Central American assets grew at 5.1% in dollar terms, an 18% growth in peso terms. For the quarter, our Colombian assets grew at 1.1%, while our Central American assets grew at 1.1% as well in dollar terms, a 1.7% contraction in peso terms.

Our consolidated balance sheet structure was similar to that in place at the end of June 2015 and March 2016 with a slight increase in the weight of our loans and leases in total assets. Our net loans account for 66% of our assets, up from 64.8%, 12 months earlier and 65.2%, three months earlier. Lower weight of fixed income investments resulting from adjusting our portfolios when increasing interest rate environment has compensated this increase. Fixed income investments now account for 11.1% of assets, down from 13.2% one year ago.

Colombian assets account for close to 72% of our balance sheet, 58 basis points higher than three months ago. Central American assets have increased their weight over the past 12 months moving from 26% to 28%. Both changes, both the annual and the quarterly change are mainly due to the Colombian peso fluctuation.

On page 10, we present our portfolio, our loan portfolio evolution. Gross loans increased by 13.1% over the last 12 months. In absence of the effect of the peso depreciation on Central America, 12 months growth would have been 9.7%. This change resulted from our Colombian book growing at 9.4% and Central America at 24.1%, or 10.5% in dollar terms. Mortgages continued to be our dynamic portfolio growing at 23.2% over the last 12 months, consumer and commercial loans grew 17% and 9.7% respectively during the same period.

Broken down by region, mortgage loans grew 26.6% in Colombia and 7.8% in dollar terms in Central America. Consumer loans grew 12.7% in Colombia and 13.1% in US dollar terms in Central America. Commercial loans grew 7% in Colombia and 9.7% in dollar terms in Central America.

During the second quarter of 2016, gross loans increased 1.4%. In absence of the effect of the peso appreciation on Central America, three-month growth would have been 2.2%. This growth resulted from Colombian operation growing at 2.1% and the Central American at 2.3% in dollar terms, this is a 0.4% decrease in peso terms.

The structure of our gross loan portfolio remained stable when compared to the previous quarter. Commercial loans account for 60% of our portfolio, while consumer and mortgages account for 30% and 9.5% respectively. Loans to individuals, which includes consumer mortgage and microcredit loans were 1.8 percentage points higher than a year earlier.

Colombia accounted for 73% of our loan portfolio, up from 72%, three months earlier and down from 75%, 12 months earlier. The increase in weight of our Central American operations has been mainly due to the Colombian peso fluctuation. We expect 2016 loan growth to be short of 10%, the corporate loans growing at 7% to 8% and loans to individuals growing between 12% and 14%. Growth in Colombia and growth in Central America in dollar terms will be similar.

On page 11, we present several loan portfolio quality ratios. On the top left of the page, you will find the evolution of our loans past due more than 30 days in our non-performing loans, both as a percentage of total loans excluding interest account receivables. During this quarter, our delinquency ratio measured as 30 days past due loans to total loans deteriorated by 5 basis points from 2.7% to 2.8%. Delinquency measured as NPLs to total loans improved by 6 basis points from 1.8% to 1.7% during the second quarter.

Moving to the right, annualized net provision expenses, net of recoveries of charged-off assets for the quarter was 1.9% of average loans, the same as three months earlier and up from 1.6% reported 12 months earlier. Provision expenses for Pacific had a relevant impact on our cost of risk, contributing to expense 80 billion and 63 billion during the first and second quarter, respectively. Excluding this event, the cost of risk net of charged-off assets for both quarters would have been 1.7%.

At the bottom left, you will find the annualized ratio of charge-offs to average NPLs. This ratio was 1.1 times during the second quarter of 2016; excluding the Pacific related charge-offs, the ratio would have remained stable at 0.9 times.

Finally, on the bottom right, we present several loan impairment allowance coverage ratios. Our allowances are 2.7% of our total loans, and cover 1.6 of our NPLs, and 1 times our 30 days past due loans. We expect full year 2016 gross cost of risk to be in the 1.85% to 1.90% area, incorporating 10 basis points impact from Pacific. Recovery of charged-off assets would reduce this figure by 15 to 20 basis points.

On page 12, you'll find further detail on the quality of our loan portfolio. This page you will find the evolution of our loans past due more than 30 days and our non-performing loans as a percentage of total loans. We will also refer to 90 days past due loans even though not included on this chart.

During this quarter, our delinquency ratio slightly deteriorated when measured as 30 days PDLs to total loans by 5 basis points from 2.7% in the first quarter to 2.8% during the second quarter. During the quarter, our 90 days PDLs to total loans improved by 7 basis points to 1.5% and our NPLs to total loans improved by 6 basis points to 1.7%. All ratios are calculated as a percentage of total loans excluding interest account receivables.

Broken down by type of loan on quarterly basis. Commercial loans slightly deteriorated by 7 basis points to 2.1%, when measured as 30 days PDLs, while improved 11 basis points to 1.3% when measured as 90 days PDLs and 11 basis points to 1.3% when measured based on NPLs.

Consumer loans remained stable at 4.1% when measured as 30 days PDLs, at 1.9% when measured as 90 days PDLs and 2.7% when measured based on NPLs.
Mortgage loans improved their quality from 2.9% to 2.7% when measured as 30 days PDLs from 1.2% to 1.1% when measured based on NPLs.

Funding and deposit evolution are presented on page 13. Total funding grew 12% over the last 12 months and 0.6% during the last quarter. In absence of the effect of the Colombian peso exchange rate fluctuation and Central America, 12 months and 3 months growth would have been 8.6% and 1.4%, respectively.

Broken down by region, Colombia funding grew at 10.4% over the last 12 months and 1.5% during the quarter. Central American funding grew at 4.1% in US dollar terms or 17% in Colombian peso terms over the last 12 months. Over the second quarter of 2016, Central American funding grew at 0.8% in US dollar terms, this is a 1.9% decrease in Colombian peso terms.

Deposits increased at 11.8% during the last 12 months and 0.1% during the last quarter. In absence of the effect of the peso depreciation and Central America, 12 months and 3 months growth would have been 8.5% and 0.9% respectively.

Broken down by region, Colombia accounted for 73.4 of total deposits. Colombian deposits grew 9.2% over the last 12 months and 0.9% during the quarter. Central American deposits grew 19.6% in Colombian peso terms or 6.5% in US dollar terms over the last 12 months.

Over the quarter, Central American deposits increased by 0.6% in dollar terms, 2.2% decrease in peso terms. Our funding and deposits structure had minor changes during the quarter. Deposits accounted for 75.2% of our total funding, at the end of period, our deposit cover 96% of our total net loans.

On page 14, we present the evolution of our total capitalization, our attributable shareholders' equity and the capital adequacy ratios of our banks. Our total equity defined as attributable equity plus minority interest was Ps. 23.8 trillion as of the end of the second quarter of 2016.
This implies a 7.1% increase over the last 12 months and 3.9% during the last quarter. Attributable equity accounted for 63.4% of total equity as of June 2016. Total equity was Ps. 15.1 trillion as of end of June. This implies a 6.8% growth during the last 12 months and a 4.9% growth during the quarter.

On this chart, we also show the consolidated solvencies of our Banks. Solvencies at the end of period were 13% for Banco de Bogotá; 12.4% for Banco de Occidente; 9.7% for Banco Popular and 11.2% for Banco AV Villas. The deconsolidation of Corficolombiana was completed and accounted for during June, this process generated Ps. 2.2 trillion in income according to IFRS Standards. This income contributed to secondary capital at 50% as of the end of the period.

We plan to fully capitalize this amount in our shareholders' meeting during mid-September. This results in a 2.5 percentage point increase in primary capitalization and a 1.3 percentage point increase in total solvency.

On page 15, we present our net interest margin. Our net interest margin expanded to 5.6% from 5.3% recorded during the same quarter a year earlier. This increase was driven by an expansion in net interest margin on loans and a higher share of loans over the average interest earning assets. Compared to the previous quarter, total net interest margin experienced a slight contraction of 0.1 percentage points driven by lower net interest margin on investments.

The net interest margin on loans was 6.5% during the second quarter of 2016, up from 6.4% a year earlier and at the same level as of previous quarter. Net interest margin on investments was 0.8% down from 0.9% a year earlier and down from 1.3% a quarter earlier.

Our quarterly net interest income, including net trading income from investments held for trading through a profit and loss grew 16.7% from Ps. 2 trillion in the second quarter of 2015 to Ps. 2.4 trillion in the second quarter of 2016. Net interest income had a 1% decrease compared to the previous quarter. We expect a 10 to 15 basis point expansion in net interest margin on loans as the repricing of loan catches up with the repricings of funding given the expected end of the monetary cycle.

On page 16, we present net fees and other income.

Fee income is presented on the top of the page.

Gross Fee Income grew 18% compared to the same period a year earlier and decreased by 0.3% to that received during the 1st quarter of 2016, mainly explained by the Colombian Peso fluctuation. When excluding the effect of the FX movements, fees grew by 10.8% and 3.2%, respectively compared to those periods.

Broken down by geography, Colombia accounted for 61% of total gross fees, domestic fees grew at 7.8% over the last 12 months and 3.8% during the quarter. Central American quarterly fees grew by 15.8% in dollar terms, this is 38.8% increase in Colombian peso terms over the last 12 months. During the quarter, Central American fees increased by 2.2% in dollar terms, 6.1% decrease in Colombian peso terms. Bottom of the page represents other income. Other income for the quarter was 770 billion.

On page 17, we present efficiency. On this page, we show our operating expenses as a share of total income and of average assets. Our efficiencies slightly deteriorated during the period. Efficiency measured as operating expense divided by average assets showed a deterioration from 3.4% in the first quarter 2016 to 3.5% in the second quarter of 2016. In Colombia, this ratio deteriorated by 21 basis points to 2.9%; in Central America, the ratio improved by 6 basis points to 4.8% in peso terms.

Efficiency measured as operating expense divided by total income was 47.2% during the quarter, up from 44.1% recorded during the previous quarter. In Colombia, this ratio deteriorated from a particularly favorable 38.5% during the first quarter to 43.5% during this quarter. In Central America, this ratio improved from 55.4% to 54.8% in peso terms. This quarterly cost to income results are in line with our full year expectation of 47%, a 100 basis points improvement versus 2015.

On page 18, we present our net income and profitability ratios. Attributable net income for the quarter was Ps. 601 billion or Ps.27 per share. Year-to-date attributable net income, net of effect of the PS.179 billion of attributable equity tax was Ps.1,246 billion, 12% higher than that for the same period a year earlier. Return on average assets and return on average equity for this quarter were 1.7% and 16.3%, respectively.

Before we move to Q&A, I want to recap our guidance for 2016. Growth in loans in absence of FX movements will be short of 10%. We expect similar growth for our Colombian and our Central American operations. The quality of loans is expected to remain stable at current levels.

Gross cost of risk will be between 1.85% and 1.9%. Net of recoveries, this ratio will be 15 to 20 basis points lower. These figures incorporate 10 basis points impact of Pacific. We expect the net interest margin on loans to increase 10 to 15 basis points as the repricing of loans catch-up with the repricing of funding. We expect total net interest margin to be in the 5.7% to 5.8% area. This result will depend on the performance of our investment portfolio.

Regarding efficiency ratios, we expect this year or full year to end at 47% gaining back a 100 basis points of what was lost during 2015. Finally, as previously guided, we expect our ROE to be close to 15%.

I now will open it to questions.

Question and Answer Session

Operator

Thank you. We will now begin the question and answer session.

(Operator Instructions)

And our first question on line comes from Carlos Macedo from Goldman Sachs. Please go ahead.

Carlos Macedo - Goldman Sachs

Thank you. Good morning, gentlemen. One question really on margins. We saw in the quarter, the net interest margin was down and you attributed that a lot to the investment margin that was down as well. When we look at the sequential growth in NII, and even the year-over-year growth, do you see a significant growth in the cost of deposits and that's understandable given how far rates have moved. You don't really see a comparable increase in the yields from loans. How do you expect that to behave going forward?

I mean, first what happened in the quarter, you had 15% expansion in the cost of deposits and loan NII, loan interest income was up only about 5%. Is your balance sheet more sensitive or your liability is more sensitive to raise, than your assets, I mean, how should we think about that?

Diego Solano Saravia – Grupo Aval Acciones y Valores S.A. – CFO

Carlos, actually our balance sheet is asset sensitive. The reason for that is that we fund our operation. We've had a substantial amount of checking accounts and retail saving accounts. Those accounts are not sensitive to the changes that we've experienced. Therefore, we end up with an asset sensitive balance sheet.

This is a combination of a couple of situations. One, the repricing of funding happens much faster than the repricing of the lending type. Our portfolio has different kinds of performance. The corporate portfolio reprices with DTF and it reprices pretty fast, but just to follow the sequence, what you will find happening in Colombia, it happens around the world is, you get a Central Bank interest increase, that is followed several weeks after by the benchmark rate, in our case DTF, catching up, and then you have our portfolios that are based on or are floated on DTF repricing at different points in time, basically over a three-month horizon. Such an environment repricing of loans still has a lag to the repricing of our funding.

Given that we've been in a process, a non-stop interest rate hike cycle, by the time our loans are repricing, funds are also repricing faster. Therefore, we pointed out, during the speech, the relevance of the pause in the monetary policy, what happens at that point is that our loans continue to reprice, but our liabilities cease to reprice. Therefore, there is a slight lag there.

The other element to take into account is, given the cycle, we've been keen on deposit growth. If you compare our results to other players, we are making sure that we're getting our deposits, perhaps in a more aggressive way. We believe that it's absolutely key for growth in the future, or looking into the short-term horizon, to be able to source potential loans with the appropriate maturities as well as available funds.

If we had given up our deposit to loan relationship, we would have been able to retain or to defend our cost of funds more. In addition, to try to put some events to what I just said, I mentioned that we are working on generating a longer maturity on our funding side. An evidence of that is the bond recently issued by Banco de Bogotá, in addition, the loan that we gave them last year as well plus other local capital market operations that they've been floating.

Therefore, we are increasing the maturity, hence the cost of fund of our portfolio. We are getting prepared to disburse the fourth generation concession loans that should start to be seen later this year.

Carlos Macedo – Goldman Sachs

Okay. So just to make it clear. What you were saying is that rates, the rate hikes may have paused, may go up a little bit more, but eventually, probably next year you're going to start seeing rate cuts as inflation starts to recede. What you're saying is that, the inverse of what's happening now should happen next year then with your margins staying more resilient in the first part of the cut cycle as your liabilities reprice quicker than your loans. Would that be accurate?

Diego Solano - Grupo Aval Acciones y Valores S.A. – CFO

Yeah, I believe so, trying to summarize what we expect to see is further expansion on our NIM on loans as I mentioned before. Just to make a precision on the numbers that you stated at the beginning. Our average cost of funds has increased by 110 basis points, while our average yield on loans has increased by 140, this is a 30 basis points expansion over the last 12 months.

In addition, we expect to see a further expansion in the 15 to 20 basis points area. So we would end up with an expansion of around or close to 0.5%.

Operator

Thank you. Our next question on line comes from Nicolás Riva from Citi. Please go ahead.

Nicolás Riva – Citi

Yeah. Thanks, Diego and Luis Carlos for taking my question. My question is in loan loss provisions. So they increased to 2.1% of loans this quarter, you explained that this was related to provisions for Pacific Rubiales. I remember, in the last conference call, you had guided for 1.7% of loans for this year. That number, the 1.7% looking into next year, is that a reasonable number to assume for next year the 1.7%? Thank you.

Diego Solano Saravia – Grupo Aval Acciones y Valores S.A. – CFO

Nicolás, you're right, we had guided to a lower number. We actually reviewed our guidance in this call, it is slightly up to reflect what has happened. It is not only the Pacific event what we're basing this adjustments on, but also reflecting some deterioration on the consumer portfolio that you could expect with what we've seen in unemployment.

Moving into next year, even though we are cautious on giving guidance on next year until we get more clarity throughout this quarter. Our expectation is however that we should see improvement in the cycle. We believe we might have peaked already what we were to see. We, as market consensus, believe that there could be around 100 basis points of further GDP growth next year. And I went through a long release of some other positives to this result.

To summarize, yes, you're right, we're expecting to see some improvement. I would be careful on telling you we're returning to this 1.7%, but it would be a fair estimate at this point.

Operator

Thank you. Our next question comes from Sebastián Gallego from Credicorp. Please go ahead.

Sebastián Gallego – Credicorp

Hi, good morning everyone. Thanks for the presentation. I want to ask regarding on the effective tax rate. What can we expect for this year? And moving forward, can you provide a little bit more color on what could we expect in terms of effective tax rate given the operations that you are doing between Banco de Bogotá and Leasing Panama? Thank you.

Diego Solano Saravia – Grupo Aval Acciones y Valores S.A. – CFO

Sebastián, I believe what you are pointing to was effective tax rate, am I right?

Sebastián Gallego – Credicorp

Right.

Diego Solano Saravia – Grupo Aval Acciones y Valores S.A. – CFO

Okay. Well, the way to think about our theoretical tax rate is, you have to bear in mind that around 30% of our operation happens in Central America, and in that region, we have a tax rate of around, let's say, 25% to 28%. The remaining is what happens in Colombia. Therefore, when you blend our Central American operation with our Colombian operation, the theoretical tax rate should be somewhere between 36% and 37%.

The variations around this number depend on tax specific issues, such as how tax returns are affected by depreciation and other specific issues, but the theoretical tax should be somewhere around that number. Up to this point, our effective tax rate has been around 35% in what has been happening throughout the year. There could be some increase during the second quarter.

This is business as usual. However, there is something that we're still working on and it is the potential impact of merging Banco de Bogotá with Leasing Bogotá Panama that has a positive impact due to bringing the amortization of goodwill into Colombia, but we are still in the process of making calculations on that. So once we have something clear there, as in the past when we decided to deconsolidate Corficolombiana, we will be more precise on what we expect.

Operator

Thank you. Our next question on line comes from Alonso Aramburu from BTG Pactual. Please go ahead.

Alonso Aramburu – BTG Pactual

Hi, good morning. Thank you for the call. Just a follow-up on the margin question initially. Is it your assumption that the Central Bank will pause for the rest of the year on your 10 to 15 basis point increase on the NIM? And related to that, well, in this quarter in your deposits, I mean, we saw checking accounts decline about 8% quarter-on-quarter and time deposits increase close to 4% and I guess that's in line with your comments that you are being more aggressive on capturing deposits. Are you factoring that into your cost of funding for the second half of the year? I mean, is it a trend that we should expect to continue?

Diego Solano Saravia – Grupo Aval Acciones y Valores S.A. – CFO

Answer for both, yes. We believe this pause could be permanent. We believe that there might be at most an additional interest rate increase. We need to see more information coming out from the Central Bank. However a six to one vote on pause is a relevant signal that this could be the end of the cycle. And we do expect to see inflation moving back down to the 7.5% area. Therefore, more arguments why this could be the last pause.

In factoring our changes in mix to a net interest margin expectations, yes, they are already factored in. And to tell you what's happening there is part of what we've been working on is strengthening some of the funding structures of some of our banks, particularly Banco Popular where you will find this kind of change. The other area we're working on, is on increasing deposits from our retail branch.

Operator

Thank you. Our next question on line come from Mr. Carlos Gomez from HSBC. Please go ahead.

Carlos Gomez – HSBC

Hi, good morning. Two brief questions. First on the capital side, you show us the capital ratio for each of your individual banks, and we see a particular decline in Banco de Bogotá relative to 6.8% in the quarter. So I would like to understand exactly how the capital moves there?

And second, could you clarify again on the tax rate, you mentioned 36%, 37%, that is for the Colombian part of the business or for the company as a whole? Thank you.

Diego Solano Saravia – Grupo Aval Acciones y Valores S.A. – CFO

The tax is for the company as a whole. If you do the blended numbers of around 40% for Colombia and around 25%, 28% for Central America, you will end up with those numbers.

Regarding the capital side, if you refer to the presentation, we included two columns for Banco de Bogotá. One, as reported for June and the other a pro forma column once we capitalized the gains from the deconsolidation of Corficolombiana. The way it mechanically works is, in our previous shareholders' meeting, we declared how much of our earnings we were to retain in the next shareholders' meeting, but we were to capitalize in the next meeting, that was 50% in the case of Banco de Bogotá. Therefore, given that these earnings were generated end of semester before we had our shareholders' meeting, where we capitalized those earnings, this is treated as general earnings. Therefore, it only contributes at 50% of that value to a secondary capital.

Once we have a shareholders' meeting and we capitalize those earnings, they move into Tier 1 at 100%. That's the reason, why you see a 6% that when you move to the right, it becomes a 9%, and it says, these earnings haven't yet become Tier 1 capitalization.

The reason why you temporarily see those numbers falling is that, we do get a negative effect when we deconsolidate Corficolombiana the way minority interest had contributed in the past to its capitalization. So that's why you see a number that is temporarily low, but this number should move up within this month.

Operator

Thank you. And our final question comes from Mayara Riddlebaugh from Wells Fargo. Please go ahead.

Mayara Riddlebaugh – Wells Fargo

Hi. Thank you for taking my question. My question is also on the solvency ratios but related to Popular.

There was almost a 200 basis point decline of the solvency ratios quarter-over-quarter. I was wondering if you could explain that or give us a little bit more detail on that, on what happened and if that's the level that we should see going forward?

Diego Solano Saravia – Grupo Aval Acciones y Valores S.A. – CFO

It's a combination of two reasons. One, organic, it's a bank that is growing the most, and then also in the process of deconsolidating Corficolombiana, there is a change in the way the minority interest is treated.

What we've been looking into Popular as we've been looking into the rest of our banks is that, in the past, we haven't used secondary capitalization as much as we could and we're starting what we could do on that front.

Operator

Thank you. We have no further questions at this time. I'd like to turn the call over to Mr. Sarmiento for closing remarks.

Luis Carlos Sarmiento Gutiérrez – Grupo Aval Acciones y Valores S.A. – CEO

Thank you very much, Richard. I think that's basically very good questions. I hope we were able to provide answers. If not, we'll be happy to take any questions offline to the extent that we can answer them and nothing else, just to say thank you very much for attending our call and we'll see you next quarter. And thank you, Richard.

Operator

Thank you, ladies and gentlemen. This concludes today's conference. Thank you for participating. You may now disconnect.