OPENING REMARKS

RESULTS SUMMARY
(Slide 2)

JUAN CARLOS MORA: Good morning everyone. It is great to be back with you today to comment on the performance of the bank during the second quarter of 2017.

I am pleased to present these results, which are in line with our expectations and behave according to our plan for 2017. They have been generated in a challenging environment that we will discuss in a few minutes. Briefly, I want to point you attention to the following main points:

On the loan side, the portfolio maintains its growth dynamics and expands 8%. Colombia and Panamá are the markets that lead this expansion and consumer loans, in particular, is the segment that grows at a faster pace with a year on year increase of 19%.

On the liability side, we continue growing the deposit base, especially CDs with the corresponding benefit of having a stable base of funding and optimal liquidity conditions.

Regarding Capital, we continued with Tier 1 levels above 10%, which permit us to be prepared for the coming years with an adequate capital structure.

During this quarter we saw the 90-day past due loan ratio reach levels of 2.6%, mainly as a result of the economic cycle that we are going through. In Colombia in particular, the deterioration comes from:

1) Corporate clients such as Electricaribe, transportation related companies
2) SMEs which are impacted by the sluggish demand and effects of problems experiences in 2016 such as transportation strikes, el Niño phenomenon and FX volatility.

In the international front, we have experienced deterioration in consumer segment of the Banistmo operations.

Regarding NIM and according to our initial forecast, we have been able to maintain it above 6%, mainly supported by maintaining the right funding structure while reducing the total funding cost.

These numbers are the result of several strategies implemented over the last 18 months, namely:

1) **Focus on profitability**
   - We continue growing in the most profitable lines. In particular, consumer loans grow at levels close to 19%. This growth permits to increase revenues and maintain the level of risk under control as we are focusing in mid and high income individuals.
   - Our origination process has permitted to pre-approve 6.8 million new loans and originate close to 2 million, allowing us to deeper the relationship with many of our existing clients and reaching the growth levels aforementioned.
• We continue generating fees, taking advantage of increasing utilization of our channels and services. One great example that we have shared with you in previous meetings, is the bancasurance business. Today, we have more than 1.3 million policies that generate about 330 billion pesos per year in revenue. Similarly, our asset management unit with assets under management close to 18 trillion pesos and generation of about 350 billion pesos per year has been very successful.

2) Focus on efficiency

In the efficiency front, we have been taking actions to optimize processes and control expenses. These initiatives involve the automation of many components of the underwriting and origination process and the right-sizing of back office and business units.

In channel distribution, we have been optimizing the branch network by reducing it by 7% or 90 branches in the last year. At the same time, we increased the number of banking correspondents by 1000 or 12%. This facts permits us to operate at a lower cost and increase the capillarity of our footprint.

Similarly, we already interact with more than 50% of our retail clients through the mobile banking platform, and the volume of transactions conducted through the app represents 39% of the total transaction. This is the fastest growing channel, with more than 20% CAGR over the last three years. Our mobile application for business is also gaining traction and SMEs in particular, represents a huge opportunity to consolidate this channel not only to generate more revenues but also to reduce the unit cost per transaction. In the last twelve months, the number of transactions through this platform has more than doubled and today, 40 thousand SMEs and large corporates use this app on a regular basis.

These initiatives, among other, represent cost savings of 160 billion pesos per year approximately.

Additionally, we have been optimizing revenues by taking decisions in the pricing front. This initiative aims to enhance segmentation of clients and originate loans to the best risk-adjusted clients. Thanks to this initiative, we will generate additional revenues by 300 billion COP in 2017.

The combined effect of cost control and fee generation will permit us to reach a cost to income ratio of 45% by 2019.

3) Optimization of the Central American operation

Another aspect where we are focusing our efforts is the optimization of our businesses in Central America. This operations account for 27% of our assets and represent a big potential for profitability improvement. Let’s split this part in three main chapters:

• Banco Agrícola in El Salvador: The political situation of the country continues very polarized and the fiscal deficit is high. Nevertheless, the asset quality metrics remain in good shape and have not presented significant deterioration due to the economic slowdown. Our main goals for this operation today are:
  o Maintain the levels of efficiency, by keeping costs under control. Expenses this year should not increase more than 2%.
  o Maintain the yields on loans by adjusting prices and optimizing the asset allocation.
BAM in Guatemala: Over the last year, we have reduced the network of branches by 7% because it improves efficiency and puts the bank with the right size to compete in this market. We continue fine-tuning the processes in order to expand profitability.

Banistmo in Panama: We have been introducing new retail products and normalizing the quality of the corporate loan portfolio. During this quarter, there was an agreement to sell the Soho Mall allowing us to reverse some provisions. One of the mayor opportunities that we have in Panama is related to fee generation. We expect fees to represent 16 to 17% of total revenues, increasing as compared to the proportion that they had a few years ago.

These three points are levered by our innovation and digital initiatives which aim to simplify many of the processes that we conduct at a massive scale.

Examples of these levers in action are the implementation of robotics in the processing of credit applications, which has reduced the number of personnel involved in the operation and has shortened the response time to clients. Also, digital processes and digital channels are gaining more relevance in the bank’s daily operations, and today we process more than 90% of our transactions through them. The ultimate goal is to set up the conditions for a faster growth of loans and fees with little to zero marginal cost.

Having said this, I would like to continue with the presentation of Bancolombia’s financial results for the second quarter of 2017. Now, I will turn the presentation over to our Chief Economist Juan Pablo Espinosa, who will elaborate on the main economic topics, Juan Pablo.

JUAN PABLO ESPINOSA: Thank you Juan Carlos. Now, I will ask you to go to slide number three (3) in the presentation.

Slide 3

During the second quarter of 2017 the Colombian economy continued to expand at a slow pace. We estimate a YoY GDP variation of 1.4%, mainly due to a poor performance of internal demand, particularly private consumption and investment. Households and firms are cautious about their spending decisions because of a combination of factors, which includes the negative effect of the latest tax reform, low confidence levels, a weak pace of job creation and still contractionary monetary conditions.

On the positive side, the external sector is contributing positively to GDP growth given the recovery of non-oil exports and the small variations of imports. Among sectors, it is worth mentioning the recovery that is experience agriculture and the resilience of financial and nonfinancial services which, despite a moderating trend are expanding above average.

Going forward, we continue to predict that productive activity will slowly gain traction. This cyclical shift will be driven by the reduction of interest rates and its transmission to market rates and a positive base effect. We estimate that in second half of 2017 and the first half of 2017 growth rates will be slightly above 2%. Moreover, since the second half of next year the economy should be growing around 3%.

In terms of prices and interest rates, we foresee that in the next few months inflation will accelerate because of base effect and an upward correction of food prices. As a consequence, we foresee that inflation will close the year at 4.2%, above the ceiling of the target range. As a result of these growing
inflationary risks the scope for the Central Bank to accommodate its monetary policy stance is limited. We anticipate 2 additional 25-bps cuts for the remainder of the year, so that intervention rate by the end of the year will be 5%.

Finally, it is worth mentioning that the Colombian economy will face several medium-term challenges which will require the implementation of a comprehensive structural reform agenda. These include the increase of potential growth rate to levels above 3%, a further adjustment of the current account deficit and a sustained correction of the Central Government deficit.

[JUAN PABLO ESPINOSA: After this overview of the economic environment, let me turn the presentation to Jose Humberto Acosta, who will discuss the Bank’s results.]

JOSE: Thank you, Juan Pablo.

Before entering the numbers for this quarter I would like to highlight two main topics that were very relevant for our Business during the quarter.

First, we certainly continue through a demanding credit cycle and higher provision charges. Of course, we must frame the higher provisions within the economic situation that Juan Pablo just described. The economy in Colombia is growing at a slower pace and that has impacted the credit quality and credit demand to some extent. In particular, during the second quarter, we experienced some run-off in SMEs and new PDLs in consumer loans. Nevertheless, the cost of credit remains within the estimated range around 2%.

Second, regarding Central America, we want to share with you the recent performance of our operations there. Please go to slide number 4 where we can see a snapshot of the four main business, including Colombia, which complements the points that Juan Carlos mentioned at the beginning. Please be aware that this numbers are reported under full IFRS and differ from the regulatory numbers filed with regulators, they present cumulative numbers as of June 2016 and 2017. Also note that these numbers do not include our offshore Operation Bancolombia Panamá, Puerto Rico and Peru, as a result, the sum of the operations presented in this slide account for 96% of the loan portfolio.

It is important to highlight:

- **In Colombia:**
  - Net loans grew 10% over the last twelve months, driven by consumer loans which grew 25% in this period.
  - Additionally, we saw stability in NIMs despite recent interest rate cuts
  - Fees growing 8%, affected by the slow economic activity.

- **In Banistmo:**
  - Loan growth at 11%. The focus on 2Q has been on corporate clients.
  - Deposits growing at 12.8%, which allows us to build a solid funding base originated by clients.
  - The 35% growth in fees originated by the bancassurance and credit card business.
  - ROE of 17%, mainly cause by the reversion of provisions associated with Grupo Wisa and its Soho Mall.

- **In Banco Agrícola in El Salvador:**
  - An 8% loan growth focused on consumer loans and 12% in deposit growth.
  - Stability in operational costs, with a growth of just 0.9%, as a result of a strict expenses execution.
  - 14% growth in fees, driven mainly by bancassurance.
In Banco Agromercantil, a loan growth of 14, mainly driven by corporate clients.

Having said this; I would like to move now to slide 5 of the presentation, where we can see the evolution of assets and their composition.

Slide 5

We continue seeing a moderate demand of credit across the sectors and regions. This trend, is highly correlated with the pace of economic activity and outlook for growth in the private sector.

The loan growth that we have experienced so far reaches 8% and is in line with our expectations. Nevertheless, our strategy in the last year and a half has been to focus the origination process in medium and high income individuals with low indebtedness. The reaction has been positive in this segment and consumer loans have reacted to this strategy. This segment in particular grew 5% over the second quarter and has grown 19% over the last year.

Currently, we have identified more that 7 million commercial opportunities just in Colombia, many of the coming from our clients in the deposit side that do not have credit products. The analytical tools that we have been using permit us to increase the utilization of our portfolio by existing clients.

In the corporate side of the business, we also saw moderate demand, partially due to weak demand from consumers and enough installed capacity to absorb this demand. Corporate loans have grown 6.6% over the last year and our expectation is that for year end, we will experience an expansion of mid single digits.

Mortgages denominated, excluding mortgage leases, grew 14% year on year.

Please keep in mind 37% of our loan portfolio is denominated in US dollars and that the 5.7% depreciation of the Colombian peso during the quarter caused this portion of the portfolio to grow faster when converted to pesos.

Excluding the impact of FX, the loan growth would have been 6% year on year.

Regarding the outlook for the rest of the year, we remain with strict underwriting standards and do not expect to see a significant acceleration of loan grown. Our expectation is to grow 6 to 8% in 2017.

Slide 6

Moving on to slide 6, we present the situation of the credit quality as of June. We certainly are experiencing a credit cycle right now and that is highly explained by the economic situation.

Vintages that deteriorated in the first months of the year continue running off and as a result the 90 day PDL ratio increased to 2.6%. The relevant point here is that we maintain an adequate coverage ratio of 171%.

Nevertheless, it’s important to see that the pace of deterioration of 30 day PDLs was slower in the second quarter as compared to the first quarter. As a matter of fact, in 1Q, the PDL ratio increased 79 basis points whereas in 2Q, it increased 17 basis points, which somehow suggest that we are probably in worst part of the PDL cycle.

Today, In Colombia the sectors the present the largest formation of NPLs are the SMEs and consumer loans.

We continue making provisions in order to sustain the pace of charge off and keep a coverage ratio above 100%. 
Slide 7

The next slide, number 7, presents the provision charges of the quarter. As we can see in the blue bars, the provisions remained relatively stable as compared with 1Q and represented 2% cost of risk.

This cost has been in line with our expectations and we believe that for the next quarters it should remain around 800 billion per quarter.

As we just mentioned, the 926 billion pesos in new past due loans are mainly explained by SMEs and consumer loans that deteriorated in Colombia.

As loans reach the threshold necessary to be written off, we have seen acceleration in these charges, which were 424 billion for the quarter.

Again, we should see a sustained level of charge offs during the rest of the year and it should permit to keep cleaning the balance sheet.

Slide 8

Moving on to slide number 8, we see the evolution of Net Interest Income and the funding cost.

During the quarter, we saw stability in the net interest revenues as loan growth also moderated. The loan growth that we experienced in the period was offset by the NIM compression, specially NIM from investments. Nevertheless, the overall performance of NII has been quite positive and certainly, above our estimations at the beginning of the year as we were forecasting a faster NIM compression.

It is important to highlight that NII from loans still grows during the quarter and the compression is mainly experienced in NII from investments, which account for only 3% of total net interest revenues.

Regarding loans, we experienced a faster grown in NII form our retail business as the consumer credit increased at a significant pace (19% year on year).

Liquidity and interest rate dynamics in Colombia suggest that the cost of funds is reaching a turning point and we should see continued decline in the coming quarters. The first component where we saw a reduction in the cost is in time deposits.

In savings accounts we experienced some increase in the cost due to the fact that we attracted more deposits from institutional clients and the share of both checking and savings declined slightly during the quarter, which caused the overall cost of deposits to increase 5 basis points over the period.

Please note the loan to deposits ratio has come down over the last year as a result of three aspects:

1) The growth in the stock of deposits, in particular CDs,
2) During the last year, we have reduced the financial obligations with Colombian promotion banks,
3) during this quarter, we redeemed 200 million dollars of subordinated bonds that Bancolombia issued ten years ago, with the corresponding benefit in the cost of long term debt and in general the total funding cost.

Our strategy right now consists in reducing the funding cost in order to prevent a fast compression of NIMs.

In the structure of our funding we have:

- Time deposits with less than a year to maturity will reexpress at a lower interest rates
- Time deposits with more than one year to maturity are typically indexed, and therefore, their cost should decrease.
- Most of our bonds in pesos are also at variable rate and they should also reprice, helping the funding cost to come down as well.
This is a combination of tools that we have to reduce the total funding cost and defend the NIM for the rest of the year.

The fact that the loan portfolio is growing at a very moderate pace and that the bank generates free cashflow permanently, releases pressure from the funding side.

Slide 9

In the next slide, number 9, we present the NIM, which was impacted by the conditions we just described.

NIMs in Colombia, have shown a compression trend as the central bank continues cutting rates.

Nevertheless, in our operations in Panamá, both offshore and in Banistmo, we have started to see NIM expansion as a result of three facts:

1) First, the repricing of the loan portfolio, specially the mortgages and corporate loans indexed to LIBOR,
2) Second higher spreads on new originations.
3) The use of the liquidity in the offshore operation in Panama and Puerto Rico to fund the other operations in Central America that originate loans to clients.

In particular, Bancolombia Panamá has expanded NIMs by 50 basis and Banistmo has expanded 20 basis points over the last year.

These are trends that offset the compression in the peso denominated portfolio and permit to sustain the overall NIM as high as possible. We estimate the NIM to be between 5.7% and 6% at the end of the year.

Slide 10

On slide 10, we can see the evolution of fees.

This has been a challenging front in 2017, as the impacts of the fiscal reform have impacted consumption patterns of individuals in Colombia. This of course, has been a drag for the evolution of our credit card business. We continue promoting the use of plastic as a method of payment and increasing the client base.

Other key components of our fee generation strategy are doing very well. In particular, Asset Management fees are growing 24% year on year. Today, our Asset Management business oversees 18 trillion Colombian pesos, the largest money manager in the country. We recently launched an initiative to implement robotics to advise customers and scale the business in a market were only a fraction of the population is banked or has mutual funds as an investment vehicle.

Also, Bancasurance is performing well as the number of policies continues growing. Currently we have about 3 million policies outstanding, and half of them are voluntary policies, that is, they are not related to any loan. This business represents profits before taxes close to 360 billion per year.

In the international operation, it is remarkable the growth in fees in Banistmo with 34% and Banco Agrícola with 13%. Year on year.

Our forecast is to grow fees around 10% for the year as we expect that the second part of the year becomes more dynamic, especially for our credit card business.

Slide 11
Now, moving to slide 11, we present the evolution of expenses, which grew 1% during the quarter and 15% during the year.

This number is explained by some adjustments that were made intentionally in order to reduce the volatility in the next coming quarters regarding administrative expenses.

Labor expenses grew due to:
- Higher costs related to layoffs as the headcount has decreased over the last year.
- Higher provisions related to bonus plan payments

Administrative expenses increased during the quarter by 16%. Due to:
- We have programmed some IT, advertisement and cash transportation payments in a linear way along the year based on the contracts with vendors. This approach increases expenses in 2Q by around 45 billion pesos, but smooth the impact of expenses in the third and fourth quarters on this year. That means we are not experiencing any particular increase in expenses out of the budget. It is just a normalization of those expenses for the 3rd and fourth quarters.
- Also, the 5.71% FX variation during 2Q, impacted 35% our total expenses than are expressed in US Dollars
- Finally, the higher VAT that Bancolombia is paying this year, starting on March, represented an increase of 15 billion pesos in 2Q.

The cost to income ratio for the quarter was 52%. Our target is to maintain this number at around 51% for this year and under 50% in the long term.

We reaffirm that our goal for expense growth is 6 to 8% this year.

In the slide 12 There are several initiatives that we have been implementing to become a more efficient institution; we want to present some of them in three main fronts:

1) Regarding physical branches: we are analyzing our current footprint of branches and putting in place several strategies such as: not opening new branches and in some cases replacing them for banking agents, as you can see in the graphic we have reduced around 9% of our branches and increased banking agents by 311% in the last 5 years.
2) Regarding alternative low cost channels, we have grown the number of banking agents by 12% over the last year and today, for the first time; this channel performs a bigger number of transactions than the branch network.
3) Regarding the digital transformation, the participation of mobile banking plus internet over total transactions that we process is 72% and we have reached 6.4 million downloads in the personal App with 2.2 million active users and at around 52,000 downloads in App for companies with 39,000 active users.

We are going to continue enhancing the offer of digital services to our clients, maintaining an strict cost control, continue rebalancing the existing network and focusing in optimization.

Slide 13

Now, let’s move to slide 13 where we present the evolution of the capital position of the bank.

We continue accumulating capital and the fact that the loan portfolio expands a moderate pace, allows us to continue with this process during the rest of the year.

Our strategy in this front is to build up equity that will be deployed in organic growth when credit demand recovers, which we estimate, should happen in 2018.
As we have shared with you, we feel comfortable with the current levels of capital and consider them optimal for the business plan that we have set for the bank.

Slide 14

Finally, we present the ROE for the period, which was 12.3%. We maintain our estimation of ROE for the year between 12 and 13% considering our forecast for earnings and capital accumulation. For the long term view we want to reach the level of 15-16 % ROE in the next coming 3 years

RECAP AND FINAL MESSAGE:

As a conclusion we want to highlight:
On the balance sheet
- Loan growth according to our forecast (6% to 8%)
- Strong growth in deposits, faster than loan growth.
- Growth in the capital base with Tier 1 above 10 %

On the Income Statement
- A slight compression of the NIM coming from 6.3 % to 6.2 %
- Cost of credit according to our forecast which is 2 %, and,
- Efficiency levels according to our expectation with some internal adjustments in the second quarter

After presenting these slides and discussing our first quarter results, I would like to invite our audience to ask any questions you might have and we’ll gladly take it from there.

Questions And Answers

Operator
Thank you. We will now begin the question-and-answer session.
And we do have a first question from Guilherme Costa from Itau BBA.

Guilherme Costa, Analyst
Good morning, guys, and thank you for the opportunity. This is Guilherme Costa from Itau BBA. I have two questions. First, could you give us some additional details about the reversion in loan loss provision expenses of Banistmo. What was the name of the two groups, you said Grupo Wisa, the other one I didn't get the name. And have you reversed all the provisions you had for those two groups? And then my second question is about 2018, I know it's too soon to talk about 2018, but could you comment on general terms, what are your main expectations for 2018 in terms of margins, loan growth, asset quality, fees and expenses? Thank you.

Jose Humberto Acosta Martin, Chief Financial Officer
Thank you, Guilherme. Regarding your second question, our expectations about 2018, you see that the macro environment for the second half of this year is showing you a slight reduction of inflation, interest rates coming down, the unemployment level remains stable, industrial production is -- it's beginning to growing up, exports also. So we believe that 2018 will be a year in which probably the GDP growth will be at around 2.3%, 2.5%. That means that probably the loan growth for 2018 will be 8% to 10%. So we do foresee a better environment for business, for corporate business and also for retail business.

Regarding your first question on Wisa, remember that with Wisa, two quarters ago, we had to increase the level of provisions because they were in intervention. Finally, in the second quarter of this year, we sold the project to Soho Mall, and we were able to collect the gain there, the loan that we had and we only maintain a loan of that around 10% of the total exposure that we had in the past. So we reverse that provision in the second quarter, that explains the positive results of Banistmo. That accounts on this quarter more than 25% of the total income of the group.
Operator
Thank you. And our next question comes from Ernesto Gabilondo from Bank of America.

Ernesto Gabilondo, Analyst
Hi, good morning, guys, and thanks for taking my call. A couple of questions from my side. One question on NIMs, we saw that last year and a half, the repricing of your loan portfolio have helped net interest margins, but given the reduction of the reference rate by the Central Bank, I would like to know your due on NIMs for next year? My second question is on taxes, we saw that your effective tax rate was 29% in the second quarter, so just want to know this should be the level for the next quarters. I remember that last year you did some tax reversals in the last quarter of 2016. So, I just want to know if there is room to do the same this year? Or should we expect of comes in the last quarter of this year? Thank you.

Jose Humberto Acosta Martin, Chief Financial Officer
Thank you, Ernesto. Let me begin with your second question. The reason why the tax for the second quarter is low, below 30% is because as you saw in the presentation, the positive numbers coming from the international operation are relevant. So, remember that we're paying there 25% of tax, statutory tax and also the FX help us. So when you increase the net income from international operation, you are having less tax to pay. And the other point is, we had also a very positive second quarter of the offshore operation in Panama, we pay 0% tax because it is an offshore. So because of combination of those two factors, that was -- our tax was below the 30%. For the year end, we expect the tax statutory tax range between 32% to 35% in the second half of this year. Regarding your first question, NIMs, again, we are trying to maintain at a level of -- as we mentioned 5.7 to 6.

We expect the next year based on the economy growing and based on the interest rate we remained probably at the same level, we are forecasting a NIM at the same level; I mean, the NIM for 2018 that we are forecasting, it is between 5.6%, 5.7% to 6%, basically because we have to strengthen the funding cost and we are able to reduce the funding cost as well.

Operator
Thank you. And we have our next question from Jason Mollin from Scotiabank.

Jason Mollin, Analyst
Hello, thank you for the opportunity to ask a question. I'll keep it to one. From a strategic point of view, we've seen you according to the regulator numbers in Colombia gaining market share over three -- it looks like over 300 basis points from May 2016 to May 2017. Can you talk about that dynamic and this decision to grow faster than the system and maybe give us some color on who is losing share, how you're getting the share? And maybe thinking about the dynamic of the asset quality, you mentioned the economy being difficult and the decision to take this share at this point in time. Thank you.

Jose Humberto Acosta Martin, Chief Financial Officer
Thank you, Jason. First, yes, we have been growing a lot, but we have been growing because of combination of two factors. The first one that we mentioned, which is consumer loans, we are growing at a pace of 25%, and yes, we are gaining market share on the consumer business here in Colombia. How we are doing that? Basically, we are working with our current clients, because of the analytics have the better data base than we have today. We are pre-approving credits to our current clients and they're taking advantage of that and they are using the loans.

So we are not increasing our consumer loans with new clients, it is with existing clients demand and we are doing is, the generation of NII, it's better that the provisions that they have generated. So at the end of the day, it's a business that is helping to increase our NII to sustain the NIM and try to maintain the return on equity at our levels below above 40%.

Regarding other leasing operation, yes, we increased the loan volumes, because, remember that the last year we merged our leasing operation in our loan book in Colombia. That's the reason why it appears 300 basis points. It's basically a consolidation process.

Operator
Thank you. And our next question comes from Tito Labarta from Deutsche Bank.

Tito Labarta, Analyst
Hi, good morning, and thanks for the call. I'll ask one question as well. I think, the slide four on your presentation, I think it's very helpful, the breakdown by the different subsidiaries. But if we look at the ROE, which tell me if it wasn't for the provision reversals at Banistmo, it looks like your ROE would be around 10 or maybe slightly below that given the different subsidiaries. So, maybe if you can give some color for each of the subsidiaries and what kind of ROE should we expect, I know you said 15% or 16% you expect in two, three years, but what about by subsidiary. Can you give some -- maybe some granularity in each of the subsidiaries and where ROE should get to? Thank you.

Juan Carlos Mora Uribe, Chief Executive Officer
Thank you, Tito, for your question. Juan Mora here. Yes, you are right, the ROE of Banistmo at the second quarter of 2017 has some impact from an extraordinary income or there were some other provisions. What we are expecting regarding NIMs -- I'm sorry, ROEs on Banistmo, it's to be around 10% this year, coming from 6% that is -- around 5% last year. So it's a big improvement on the ROE of Banistmo, taking out the extraordinary issues around provisions. So we are improving our operation in Banistmo and for coming years, we expect that ROE to keep improving, reaching levels probably around 12% to 13%. In the case of the other operations, in Central America, Banagricola, we are expecting levels of ROE for the year on 11% to 12% and keeping at that level on the coming years. In the case of Banco Agromercantil, we are improving in that operation, it's slower than in the other ones, seems we are just -- just took control of the operation at the beginning of last year. So, the ROE will be around maybe less than 10%, up from 8%, but we will keep improving the ROE on also on BAM in the coming years.

Operator
Thank you. And our next question from Carlos Macedo from Goldman Sachs.

Carlos Macedo, Analyst
All right. Thanks. Good morning, gentlemen. A couple of questions, maybe following up a little bit in the last one, you talk about margins declining through the end of the year, cost of risk thing kind of where it is, loan growth not accelerating significantly, a bit of relief in expenses, but not too much. First half around 12% ROE and you talk about 12% to 13% maybe in the second half, where does the difference come from, given that you're not going to have much relief from elsewhere in your income statement? And then following up again into next year, cost of risk at 2% for this year, where do you think through the cycle cost of risk can be? In the past it was as low as 1.5, is that something that you can return to once the cycle is done in Colombia or given the mix with more consumer now would that be a bit higher? Thanks.

Jose Humberto Acosta Martin, Chief Financial Officer
Yes, Carlos. Regarding your question, the ROE, how we'll get the 12 to 13. The main driver in our operation, how to increase the return on equity for the next coming quarters? It is through the efficiency level, you are seeing that we came from 56% two years ago, and right now we are at 51% area. So at the end of the year, again, 12 to 13 because increasing of the equity side, but the key driver would be efficiency. Regarding the next year, basically -- I'm sorry, your question...

Juan Carlos Mora Uribe, Chief Executive Officer
Yeah, let me answer you the question, Carlos. Next year we are expecting the cost of credit to be around 1.6, 1.7. We don't expect next year to return to 1.5, but on long run, we sort of expect to be around 1.5, but not next year. Next year, we'll be more around 1.6 or 1.7. And then the complement, the answer about this year ROE. You're right, cost of credit is going to be around 2%. We will expect an improvement there. As Jose Humberto mentioned, we still have some room on the efficiency side and expenses to improve. Also, fee generation is going to be a source of income that we expect to help us reaching the ROE that we are forecasting.

Operator
And we have our next question from Domingos Falavina from JPMorgan.
Domingos Falavina, Analyst
Yes. Thank you, gentlemen. My question is more regarding with costs. I believe there was a little bit of a change in seasonality in this quarter. And also adding to Carlos question, the efficiency ratio it's ultimately a consequence of your top line and your cost, right. Even you are not expecting loan structurally too much next year and needs to be slightly come down, you would have to pretty much either cut cost or grow very close to zero. Is that the outlook you have for next year?

Jose Humberto Acosta Martin, Chief Financial Officer
Domingo, we expect to align the growth in expenses to inflation. So we expect next year that the increase of cost would be of the area of 4% to 5%, we have to invest, we have an operation or margin operations, but the relevant point is what's going on through our channel distribution. You see that every single quarter, we are reducing the volumes through the branches, which is the big generating of cost. And today we only processed 4% of our total transactions through branches. So that would be the best way to maintain align the cost, basically to inflation. So what we expect this year, we expect, as Juan mentioned, a reduction of cost of credit to 1.8%, maybe 1.7%. And expenses growth of around 5%. Loan growth will be of the area of 10% to 12%. If you combine those effects, we will probably get again a level of 14% to 15% of return on equity. But again, mainly -- the main driver would be efficiency.

Fee generation today accounts only 8%, but this is basically for the first half of the year, basically because of the economic cycle. But if you double check the numbers in the previous years, the fee generation, it's on the arena of 12% to 15%. So with the economic activity increase in the second half of this year or maybe next year, you'll see again a rebounding of the fee generation 10% to 12%.

Operator
And we have our next question from Alonso Garcia from Credit Suisse.

Alonso Garcia, Analyst
Hi, good morning, everyone. Thanks for taking my question. In regards to the NIM, I would just like to confirm the kind of NIM on securities that you expect, for that you are embedding in your 5.76% NIM, if I recall correctly, you had mentioned in the past that our normalized NIM on securities was close to 1%. So far this year it has been above that, it was 3% -- 3.2% in first Q1, 2.3% in second quarter. So just want to check, if you believe this 2.3% can be sustained or what kind of NIM on securities is embedded in your guidance? Thank you.

Jose Humberto Acosta Martin, Chief Financial Officer
Yes, Alonso. Our forecast for the NIM of the securities always would be at the range of 1%. What happened in the last two quarters the 3% down we are having. This is basically because of the volatility of the pace on the interest rates. But we always forecast at around 1%, assuming cost of funding 3%, and assuming the securities portfolio having an interest rate of 4%. So we don't expect more of that.

Operator
And we have our next question from Cristina Manotas from Davivienda Corredores.

Cristina Manotas, Analyst
Good morning. Thanks for the call. On shareholders equity, we are seeing a significant increase of 13% in the accumulated of the other comprehensive income, this has increased. Can we get more details about the situation? Thank you so much.

Jose Humberto Acosta Martin, Chief Financial Officer
It is a combination of the FX, remember that we have a portion of equity in US dollars. And we are talking about our FX, devaluation of 5% and the other is that we paying income from the previous periods. This is a relevant point, because if you double check the last six quarters, we have been gaining capital every quarter. And we would accumulate more on the first quarter of next year when we have our General Assembly.
Operator  
And our next question comes from Sebastian Gallego from Credicorp Capital.

Sebastian Gallego, Analyst  
Hi, good morning everyone. Thank you for the presentation. Just a follow-up on previous questions regarding efficiency. Do you have a specific target for branches for the next 12 months? Or do you have other specific targets that you could comment on and you can share the reduced OpEx? Thank you.

Jose Humberto Acosta Martin, Chief Financial Officer  
The target that we have as we mentioned previously, inflation, to increase same level of inflation, we don't expect – we don't have a specialized task to reduce the branches because this one of our strengths. We are optimizing and optimizing meaning maybe to merge some of them, but we don't expect that more reduction in a very important way of branches.  
In Colombia, branches is critical, because give us popularity and give us funding cost. On the international operation, we are contemplating and optimization of the branches in Banco Agromercantil de Guatemala, and you'll see maybe more reductions in branches that we expect in the next coming quarters.

Operator  
And our last question comes from Andres Duarte from Corficolombiana.

Andres Duarte, Analyst  
Hello, good morning. Thank you for the presentation. Regarding the tangible common equity ratio of 7.52% that your publishing. I want to know if you had a target ratio and what has been the evolution of it? Thank you very much.

Jose Humberto Acosta Martin, Chief Financial Officer  
Our target would be at the range of 8%. And again, our target to maintain the Tier 1, which is more relevant, it is to stay that 9.5% to 10.5% the next two years.

Operator  
And we have no further questions in queue.

Juan Carlos Mora Uribe, Chief Executive Officer  
We would like to thank you all for your interest on our presentation of the second quarter results, and we hope to see you on our next conference call. Thank you very much and have a good day.

Jose Humberto Acosta Martin, Chief Financial Officer  
Thank you.

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