Fitch Affirms Bancolombia and Related Entities' ratings; Outlook Negative

Fitch Ratings, New York, 14 June 2019: Fitch Ratings has today affirmed the international ratings for Bancolombia S.A., certain local and foreign subsidiaries, and a related entity. Bancolombia's Viability Rating (VR) and Issuer Default Ratings (IDRs) were affirmed in 'bbb' and 'BBB', respectively. Under Criteria Observation (UCO) status on Bancolombia and subsidiaries' Short-Term (ST) Ratings was removed. A full list of rating actions is at the end of this rating action commentary.

KEY RATING DRIVERS - BANCOLOMBIA
IDRS, VR, NATIONAL RATINGS AND SENIOR DEBT
Bancolombia's VR is highly influenced by Fitch's assessment on the operating environment of the jurisdictions in which the bank's businesses are performed. Additionally, Bancolombia's ratings consider its robust company profile and sound financial performance for its rating category, although capital adequacy metrics continue to compare unfavorably with similarly rated international peers (emerging market commercial banks in the 'bbb' rating category).

Bancolombia’s consolidated NPLs greater than 90 days increased moderately to 3.08% at YE18 from 2.94% the prior year, and stabilized in 3.05% at 1Q19. This is a reflection of the bank’s greater retail orientation as well as its exposure to specific corporate names in the transportation, infrastructure, and electricity sectors, which hit not only Bancolombia but other large Colombian banks as well. Fitch expects NPLs ratio to stabilize given that the corporate loans default cycle seems to be ending, however, it will likely be higher than the historical average due to the bank’s strategic focus on retail and consumer lending.

Bancolombia reported lower profitability in 2018, with an operating profit over RWA of 1.8% compared with 2.25% the prior year, below its closest Colombian peers and similar rated international peers. The bank’s declining profitability in 2018 and over the prior four years has been mainly related to the increasing credit cost and low loan growth. Fitch expects performance to improve during 2019 as is demonstrated at 1Q19 when operating profit over RWA reached 2.53% driven by lower impairment charges, as troubled corporate loans have been largely provisioned.

Capitalization remains as Bancolombia’s main weakness in its financial profile and deteriorated in 2018, as the bank grew its loan portfolio in 8.3%, above the financial system average of 6.1%. Ample loan growth reverted the previous positive trend on capital as FCC declined to 10.3% of risk weighted assets at YE18 (10.4% the year prior). Dividend payments (42.5% payout on an unconsolidated basis) drove a decrease in equity during 1Q19, and as a result the bank’s FCC ratio declined to 10.2%. Fitch expects that the forthcoming adoption of Basel III guidelines in Colombia will generally benefit Colombian banks capital ratios by between 150 and 350 bps due to a lower risk weighted assets density, increased capital buffers and more comparable capital definitions.
Bancolombia benefits from a well-diversified and low cost deposit base and has the highest deposit market share in the country across all major products, including demand, savings and time deposits. Bancolombia has proven access to local and global capital and debt markets. Accordingly, the loan-to-deposits ratio remained stable at 122.3% at YE18, as Bancolombia actively uses capital markets to better match its assets and liabilities term profile. At YE18, the bank's liquid assets covered 18% of total deposits and short-term funding.

Fitch has affirmed Bancolombia's ST rating of 'F2' as a result of the application of its updated ST Rating Criteria. Under the revised criteria Bancolombia's 'BBB' Long-Term (LT) IDR is on a new cusp point. Fitch has applied the higher of the two Short-term IDR options mapping to the 'BBB' LT IDR, as Bancolombia's liquidity assessment of 'bbb+' is at the minimum liquidity assessment at which the higher option would apply at the 'BBB' cusp point.

SUPPORT RATING AND SUPPORT RATING FLOOR
Fitch has affirmed the bank's Support Rating of '2' and Support Rating Floor of 'BBB-', reflecting the agency's estimation of a high probability of sovereign support, if required, given the bank's systemic importance. The ability of the sovereign to provide support is based on its 'BBB'/Rating Outlook Stable IDRs.

SUBORDINATED DEBT AND OTHER HYBRID SECURITIES
Bancolombia's plain vanilla subordinated debt is rated one notch below its IDR to reflect higher expected losses in case of liquidation but no additional notching for non-performance given the gone concern-only characteristics.

The local Tier II capital subordinated notes are rated two notches below Bancolombia's VR of 'bbb' and reflect loss severity exclusively. There is no notching due to incremental non-performance risk. Notwithstanding, these securities rank pari passu with other existing subordinated indebtedness and the loss severity notching is wider on the proposed notes due to the existence of a full write-down feature, which is not contained in other outstanding subordinated debt.

KEY RATING DRIVERS - BP, BPR, TUYA, FIDUCOLOMBIA AND VB

IDRs, NATIONAL RATINGS, and SENIOR DEBT
Bancolombia Panama SA (BP), Bancolombia Puerto Rico Internacional Inc. (BPR), Compania de Financiamiento Tuya S.A. (Tuya), Fiduciaria Bancolombia S.A. (Fiducolombia) and Valores Bancolombia S.A. (VB)'s ratings reflect the potential support they would receive from Bancolombia, should it be required. In Fitch's view, these entities are an integral part of its parent's business model and core to its strategy; therefore, their LT and ST IDRs mirror those of Bancolombia. Fitch also incorporates in its support rational the negative reputational implications of a potential default of BP, BPR, Fiducolombia and BV for the parent. In the case of Tuya, Fitch also considers the support track record of the parent toward the entity.
SUPPORT RATINGS
Fitch believes Bancolombia's willingness to support BP and BPR is substantial, should it be required, given that they are core to the parent's business strategy and regional expansion. This also underpins a support rating of '2'. The bank's ability to support these entities is reflected in Bancolombia's 'BBB' IDR.

RATING SENSITIVITIES - BANCOLOMBIA
IDRS, VR, NATIONAL RATINGS AND SENIOR DEBT
Any negative rating action on the sovereign would also lead to a similar action on Bancolombia’s IDRs. ST IDRs would be negatively affected either by a downgrade in the LT IDRs or if the loan-to-deposits ratio rises above 125%. Negative rating actions could arise if the bank is not able to sustain a FFC ratio of around 10%. A sustained deterioration in its impaired loan ratio above 4%, or a weaker financial performance (operating ROAA relative to risk weighted assets consistently below 1.5%), could also trigger negative ratings actions on Bancolombia's ratings.

SUPPORT RATING AND SUPPORT RATING FLOOR
Bancolombia's Support and Support Rating Floor ratings would be affected by a change in Colombia's ability or willingness to support the bank.

SUBORDINATED DEBT
The subordinated debt ratings are sensitive to a change in Bancolombia's VR. The ratings are also sensitive to a wider notching from the VR if there is a change in Fitch's view on the non-performance of these instruments on a going concern basis, which is not the baseline scenario.

RATING SENSITIVITIES - BP, BPR, Tuya, Fiducolombia AND VB
IDRs and SENIOR DEBT
The IDRs and Senior Debt of BP and BPR are support-driven and aligned with its parent's ratings. Therefore, these ratings would mirror any changes in Bancolombia's IDRs.

NATIONAL RATINGS - Tuya, Fiducolombiana and VB A negative change in the capacity or propensity of Bancolombia to provide support to Tuya, Fiducolombiana or VB could pressure creditworthiness.

SUPPORT RATINGS BP and BPR's SR would be affected if Fitch changes its assessment of its parents' willingness and/or ability to provide support.

Fitch has affirmed the following rating actions:

Bancolombia
--Long-Term Foreign Currency IDR at 'BBB'; Outlook Negative;
--Short-Term Foreign Currency IDR at 'F2'; UCO removed
--Long-Term Local Currency IDR at 'BBB'; Outlook Negative;
--Short-Term Local Currency IDR at 'F2'; UCO removed
--Viability Rating at 'bbb';
--Support Rating at '2';
--Support Rating Floor at 'BBB-';
--Senior unsecured debt at 'BBB';
--Subordinated debt at 'BBB-';
--Subordinated debt at 'BB+';
--National Long-Term Rating at 'AAA(col)'; Outlook Stable;
--National Short-Term Rating at 'F1+';
--Senior unsecured debt national rating at 'AAA(col)';
--Subordinated debt national rating at 'AA+(col)'.
--Subordinated debt national rating at 'AA(col)'.

Bancolombia Panama
--Long-Term IDR at 'BBB'; Outlook Negative;
--Short-Term IDR at 'F2'; UCO removed
--Support Rating at '2';
--Long-Term Deposits at 'BBB';
--Short-Term Deposits at 'F2'.

Bancolombia Puerto Rico
--Long-Term IDR at 'BBB'; Outlook Negative;
--Short-Term IDR at 'F2'; UCO removed;
--Support Rating at '2'.

Compania de Financiamiento Tuya
--National Long-Term Rating at 'AAA(col)'; Outlook Stable;
--National Short-Term Rating at 'F1+'.

Fiduciaria Bancolombia
--National Long-Term Rating at 'AAA(col)'; Outlook Stable;
--National Short-Term Rating at 'F1+'.

Valores Bancolombia
--National Long-Term Rating at 'AAA(col)'; Outlook Stable;
--National Short-Term Rating at 'F1+'.

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