

Research Update:

Banco Consorcio Assigned 'BBB' Ratings, Outlook Negative On Chile's Heightened Economic Risks

January 27, 2022

Overview

- We consider that Chile-based bank Banco Consorcio has a smaller scale and narrower business diversification than those of universal multipurpose banks. The bank also has a strong capital base supported by its stable revenue and capital injections that provide enough cushion to maintain its business strategy.
- We also believe the bank's asset quality ratios are in line with the banking system average, despite some slippage due to punctual cases in the corporate sector. The bank's funding base is stable despite its large share of wholesale and institutional clients, and its liquidity provides a comfortable cushion to meet short-term obligations.
- As a result, we assigned our 'BBB' long-term issuer credit rating to Banco Consorcio with a negative outlook and assigned a 'bbb' stand-alone credit profile (SACP) to the bank.
- The negative outlook on Banco Consorcio reflects the negative trend in our economic risk evaluation of Chile due to continuing pressures from medium-term economic and political uncertainties.

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Rating Action

On Jan. 27, 2022, S&P Global Ratings assigned its 'BBB' long-term issuer credit rating to Banco Consorcio. The outlook is negative.

Rationale

The rating reflects the bank's relatively small scale and limited diversification. This is because of Banco Consorcio's focus on the corporate lending, although its mortgage lending business has expanded in recent years. The rating also reflects Banco Consorcio's sound capital base with a forecasted risk-adjusted capital (RAC) ratio of about 10.3% for the next 12-24 months, supported by stable internal capital generation and a capital infusion in 2021, which provides enough cushion to sustain its business plan. The rating also incorporates the bank's low business complexity and healthy asset quality metrics, which are generally in line with the system average,

and its expected portfolio growth in less cyclical sectors. The rating also considers a funding profile that mainly consists of wholesale funding, which is less stable than traditional retail deposits, and its liquidity profile that provides a comfortable cushion to meet short-term obligations. As a result, Banco Consorcio's SACP is 'bbb'. The 'BBB' rating on the bank is the same level as its SACP because the latter doesn't incorporate notching from external support from either the government or the group at this point.

Our bank criteria use our Banking Industry Country Risk Assessment (BICRA) economic risk and industry risk scores to determine a bank's anchor, the starting point in assigning an issuer credit rating. The anchor for banks operating only in Chile, like Banco Consorcio, is 'bbb+', the strongest anchor in Latin America. (Please see "Banking Industry Country Risk Assessment: Chile," published Aug. 27, 2021.)

Banco Consorcio focuses on the corporate segment, although its mortgage and consumer loan units have recently grown. The Chilean financial system is very concentrated, with the top five banks generating 77% of total loans. Since its acquisition in 2009, Banco Consorcio has been growing. It's the ninth-largest entity in the Chilean system in terms of credit and deposits, with a market share of 2.2% and 2.0%, respectively, as of September 2021 (up from 1.3% and 1.6%, respectively, in 2016). The corporate segment has been the bank's traditional business, representing 76% of its loan portfolio (compared to 58% for the industry average), followed by mortgages (22%) and personal loans (2%) as of September 2021 (compared with 92%, 5%, and 3%, respectively, as of December 2017). The bank increased its exposure to the mortgage segment by taking advantage of the 2020 Financial Portability Law and low interest rates, which allowed clients to switch from one bank to another. In addition, until 2018, most of the mortgage portfolio was registered in the group's life insurance company, which had the long term-funding for this loan type. However, since that year, Banco Consorcio improved its funding profile, allowing it to incorporate mortgages on its books.

Banco Consorcio has relatively stable operating revenues, most of which stem from its lending operations. Net interest income represented about 70% of operating revenues and fee income 5% over the last years. Banco Consorcio's trading gains represented 25% of operating income; however, they're related to gains from derivatives (forwards) that the bank uses as part of its funding strategy. Banco Consorcio's profitability is in line with those of its peers, with return on average adjusted assets (ROAA) of 1.3% as of September 2021, compared with the 1.4% peer average.

For the next 12-24 months, we expect Banco Consorcio to maintain its competitive position, improve its business mix, and lower its exposure to the real estate sector. The bank's loan portfolio expanded almost 22% in 2021, and we expect it will remain stable in 2022, because Banco Consorcio will focus on credit management and improving capitalization before returning to growth. We expect the mortgage portfolio to represent about 30% of total loans in 2023, as commercial loans' share falls to 65%-68%, and personal loans representing the remainder. In addition, the bank will focus on improving cross selling to take advantage of the group's customer base.

The bank's sound capitalization is commensurate with its growth plan, together with comfortable regulatory capitalization. Our opinion of the bank's capital and earnings stems primarily from our forecasted RAC ratio of 10.3% for the next 12-24 months. Our forecast incorporates the following base-case scenario assumptions:

- A significant rebound in Chile's economy in 2021 and more moderate growth in 2022 and 2023.
- Loan growth of about 22% in 2021, a stable portfolio in 2022, and resuming growth in 2023.

- Higher margins in 2021 due to high inflation and contained interest expenses due to low-cost central bank lines and higher sight deposits. We expect margins will decrease in 2022 and 2023, but remain above historical levels.
- ROAA of 1.0%-1.1%.
- Nonperforming loans (NPLs) of 2.0%-2.1% with net charge-offs to average customer loans of less than 1%.
- High loan-loss reserves.
- Dividend distributions around 40%.
- Capital infusion of CLP44 billion in 2021.

In addition, Banco Consorcio had solid regulatory capitalization metrics of 16.2% as of November 2021, which are well in excess of the regulator's minimum of 8%.

The bank's risk position reflects its emphasis on lending and its manageable asset quality

metrics. Banco Consorcio has a diversified base of clients, with the top 20 exposures representing about 17% of its loan portfolio and 1.4x of its total adjusted capital. The bank has a large exposure to real estate developers--around 30% of its credit portfolio--but we capture this risk in our RAC ratio, which uses a much higher risk weight for these exposures than for other sectors. In addition, the bank has adequate financing guidelines and collaterals that mitigate risks. Banco Consorcio has historically registered better-than-system asset quality metrics, given its adequate underwriting standards, higher exposure to the corporate segment that in general has lower NPLs than the retail one, and focus on mortgages. However, in the last few months, NPLs have risen because of punctual cases in the corporate sector, although they're still manageable. The bank's NPLs edged up to 2.0% in November 2021 from 1.7% in 2020, only slightly above the industry average of 1.3% and 1.4%, respectively. In addition, as of September 2021, net charge-offs to average customers loans were only 0.3% and loan-loss reserves were 120% of total NPLs. For the next 12-24 months, we expect the bank's asset quality metrics to remain stable with the falling share of loans to the real estate developer sector.

The bank's funding base has a large share of wholesale and institutional clients and a smaller proportion of retail deposits than those of peers.

Nonetheless, in the last several years, Banco Consorcio has been diversifying its funding base, reducing the share of time deposits by issuing debt in the local market as its mortgage portfolio expands, increasing the use of central bank lines (likewise the industry), and raising gradually the share of retail deposits. As of September 2021, customer deposits remain Banco Consorcio's main funding source, accounting for 54% of its total funding base (7% sight deposits and 48% time deposits); below the Chilean banking system's average of 65%. About 70% of total deposits are from institutions (pension funds, mutual funds, and insurance companies), 22% from corporations, and the rest from retail clients. The other main funding sources are bonds (senior and subordinated; 27% of total funding base), the central bank's pandemic-related lines (16%), and bank loans (3%).

The bank's stable funding ratio (SFR) was 118% as of September 2021, and it has averaged 114% for the past three fiscal years, which is in line with the system average. For the next 24 months, we expect Banco Consorcio to maintain its current funding profile, with a SFR above 100%, and quickly replacing central bank lines after they expire with issuances and a larger deposit base.

Banco Consorcio's liquidity profile provides a solid cushion to cope with unexpected cash outflows in the next 12 months. The bank has a broad liquid asset to short-term wholesale funding ratio of 3.2x as of September 2021, and it averaged 2.4x in the last three fiscal years. Also, broad liquid assets to total assets reached 24%, in line with those of other rated banks in the country. Like domestic peers, Banco Consorcio uses sovereign and central bank securities as a primary instrument for liquidity management.

Banco Consorcio is fully owned by Consorcio Financiero (CF; not rated), a large financial conglomerate in Chile, and we view the bank as an important subsidiary. CF underwrites insurance policies in Chile through its operating subsidiaries, Consorcio Seguros VIDA--one of largest underwriters of pensions "rentas vitalicias"--CN Life Seguros de Vida, and Consorcio Seguros Generales. It provides banking products and services through Banco Consorcio. As a result, CF's wide range of business lines provide revenue stability. Banco Consorcio complements CF's financial services operations and represents a sizable share of the group's equity and assets.

Outlook

The negative outlook on Banco Consorcio for the next 12-24 months reflects the downside risks until Chile's economy fully recovers and prospects for the medium term become clearer amid the amendment of the constitution, the polarized political landscape after presidential elections, and/or other global developments.

Downside scenario

We could lower the ratings on Banco Consorcio by up to two notches in the next 24 months if our view of Chile's financial system worsens (resulting in a weaker BICRA score that would reflect higher risk and a lower anchor for banks). In addition, we could lower the rating if the bank's RAC ratio falls below 10%, which could result from higher-than-expected portfolio growth, higher exposure to real estate sector, and/or lower internal capital generation. In addition, a deterioration in the group's fundamentals could trigger the downgrade of the bank.

Upside scenario

We could revise the outlook on Banco Consorcio to stable in the next 12-24 months if we were to revise the trend in the economic risk on Chile's BICRA to stable from negative while the bank's credit factors remain unchanged.

Environmental, Social and Governance (ESG)

ESG factors have no material influence on our credit rating analysis of Banco Consorcio.

Ratings Score Snapshot

Issuer credit rating BBB/Negative/--

SACP bbb

Anchor bbb+

Business position Moderate (-1)
 Capital and earnings Strong (+1)
 Risk position Adequate (0)
 Funding and liquidity Moderate and Adequate (-1)
 Comparable rating analysis 0
 Support
 ALAC support 0
 GRE support 0
 Group support 0
 Sovereign support 0
 ESG Credit Indicators: E-2, S-2, G-2

Related Criteria

- Criteria | Financial Institutions | Banks: Banking Industry Country Risk Assessment Methodology And Assumptions, Dec. 9, 2021
- Criteria | Financial Institutions | General: Financial Institutions Rating Methodology, Dec. 9, 2021
- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- General Criteria: Group Rating Methodology, July 1, 2019
- General Criteria: Hybrid Capital: Methodology And Assumptions, July 1, 2019
- Criteria | Financial Institutions | General: Risk-Adjusted Capital Framework Methodology, July 20, 2017
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011
- Criteria | Insurance | General: Refined Methodology And Assumptions For Analyzing Insurer Capital Adequacy Using The Risk-Based Insurance Capital Model, June 7, 2010

Ratings List

New Rating

Banco Consorcio

Analytical Factors	bbb
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New Rating; CreditWatch/Outlook Action

Banco Consorcio

Issuer Credit Rating	BBB/Negative/--
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