# Banco Latinoamericano de Comercio Exterior

**CONFERENCE CALL ON BLADEX OPERATING RESULTS FOR THE THIRD QUARTER OF 2022.**

**Date:** 02.11.2022

**Participants:**

- Jorge Salas, Chief Executive Officer
- Ana de Mendez, Chief Financial Officer
- Samuel Canineu, Chief Commercial Officer
- Carlos Raad, Investor Relations Officer

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Moderator:

Good morning and welcome to Bladex's Third Quarter 2022 Earnings Call. A slide presentation is accompanying today's webcast and is available in the investor section of the company's website, www.bladex.com. There will be an opportunity for you to ask questions at the end of today's presentation. This conference call is being recorded. As a reminder, all participants will be in listen-only mode. Now I would like to turn the call over to Mr. Carlos Raad, Investor Relations Officer. Please go ahead.

Carlos Raad:

Good morning everyone and thanks for joining our Third Quarter 2022 Earnings Call. Before we begin our presentation, allow me to remind you that certain statements made during the course of this discussion may constitute forward-looking statements which are based on management's current expectations and beliefs and are subject to a number of risks and uncertainties that could cause actual results to materially differ, including factors that may be beyond the company's control. For a description of this risk, please refer to our filings with the U.S. Securities and Exchange Commission and our earnings release. Speaking on today's call is our CEO, Jorge Salas, who will provide an overview of performance for the quarter and review the drivers behind these results as Bladex advances on the execution of the renewed strategy. Ana de Mendez, our CFO will then discuss the quarter's financial results in more details and after that we'll open the calls for your questions. Also joining us today are some of my colleagues from the executive team that will be available for Q&A. With this, let me turn the call to Jorge. Please go ahead.

Jorge Salas:

Thank you Carlos, and good morning everyone. Let's continue to deliver strong results in the third quarter as we execute our strategic plan in advance on our goal of driving profitable growth. Economic activity in Latin America has been resilient with foreign trade close reaching record highs. The economic activity in the region together with tight credit markets and a successful execution of our strategy has contributed to higher commercial volumes as well as an expansion in lending spreads for Bladex.

Net income maintained a positive momentum were delivered in prior quarters, up 70% year-on-year to almost $27 million. This new level of net income, along with a more optimized capital structure resulted in an expansion of ROE to 10.3%. Our strategic initiatives contributed to sustained growth in our credit book to nearly $9 billion at quarter end, maintaining a very healthy asset quality with NPLs at nearly 0%. I want to point out that we have accomplished this strong performance while consistently improving our efficiency ratio and I will talk more about this shortly.

Now let's turn to slide four for a brief update on our progress of the strategic plan. As I mentioned last quarter, we aim to capitalize on the strengths we have consolidated in over 40 years of banking in Latin America with a goal of enhancing profitability, ensuring long-term sustainability, and of course increase the overall value creation for all stakeholders of Bladex.

Today I would like to highlight that the strong results we are presenting are largely the product of the strategic plan and to a lesser extent, driven by the current macro environment. The plan has been in place since the start of the year and in this nine months it is already delivering very positive results. During the first phase of our plan, we optimize the balance sheet allocating our capital more profitably.

We begin the year with a core equity tier one ratio of 19.1% and we close a third quarter with an optimized capital ratio of 14.4% as we expand our loan book while maintaining a very good asset quality. We also increase penetration with existing clients while we continue to expand our customer base. During the first nine months of the year, we increased new active customers by 13% with over 50% of the book growth driven by new customers. In addition, our profitability focus along with the overall higher rate have allowed us to expand net lending spreads. At the same time, we have continued to optimize the portfolio mix, both in terms of industries and geographies, all while maintaining a deep focus on cross selling. Just as an example, in just nine months, the penetrations of our letters of credit product increased by 10% within our client base.

We're also pleased with the progress achieved in terms of driving fee income from our loans indication desk that keeps showing good momentum. As a matter of fact, this week we announced another syndicated deal, $130 million senior secured amortizing facility for Favorita Fruit, a carbon neutral corporation and one of the largest banana exporters in Ecuador. Bladex acted as a sole leader ranger and book runner for this deal. I'm going to leave it here for now and turn the call back to our CFO who will walk you through our quarterly results in more detail. After that, I'll make some closing remarks before we open it up for questions. And that's it for now. Annie, can you please go ahead please?

Ana Graciela de Mendez:

Thank you, Jorge. Good morning to all. Starting with slide five total assets, continue the growth trend up another 4% during the quarter, reaching over $9 billion on the back of sustained loan growth complimented by an investment portfolio, which allows us to further diversify our exposures by country, including investments in non-LatAm issuers, mainly from the US representing 52% of the total.

Our cash position mostly invested with the New York Fed stood at 11% of total assets reflecting our rigorous liquidity management, which follows Basel III liquidity standards as required by the Panama banking regulator. The bank's core business, namely our commercial portfolio, is constituted by the loan portfolio which totaled $7.1 billion at quarter end together with contingencies or of balance sheet assets for another $0.8 billion. The latter mainly consisting of the issuance and confirmation of trade related letters of credit. We continue to expand the loan book lately reflecting the increase in cross sell and deeper penetration with the existing customer base and the addition of new clients as contemplated in the initial phase of our five year plan. We have also experienced higher demand given sustained economic activity and trade flows in Latin America.

Further on we will explain in more detail how this asset growth has been consistently supported by a well diversified funding structure. As shown on slide six, our geographic exposure remains diversified with Brazil maintaining the largest share at 16% followed by Mexico at 12% commensurate with the size of these economies where we plan to continue focusing on expanding our client base.

We remain and will remain well diversified in other countries throughout the region with an important portion in non-LatAm investment grade exposures, mostly in the US, Europe, and Asia related to transactions carried out in Latin America and the Caribbean. Overall, exposures in investment grade countries represented 43% of the total commercial portfolio. In terms of sectors, financial institutions represent 43% of the portfolio, up by two percentage points from the prior quarter as we capitalize on business opportunities arising from the liquidity constraint in the region, all while keeping a stringent focus on maximizing credit spreads.

Exposure to top tier corporates throughout the region continue to be influenced by growth in commodity related sectors such as oil and gas, mainly downstream, which now represents 16% of the total followed by manufacturing industries at 8% while electric power and food and beverage accounted each for 7% of total exposure.

Turning to slide seven again this quarter, credit disbursements of over $4 billion exceeded collected maturity and represented over half of the commercial portfolio. This denotes the short term nature of our portfolio, characteristic of our business model with 70% of loans maturing within the next 12 months and the average remaining tenor of the portfolio at approximately one year. This provides agility to rebalance our book through economic cycles in the region. Lending spreads on new loans exceeded those of maturing by 14 basis points, reflecting our focus on optimizing our portfolio mix to maximize net lending spreads and margin expansion.

Moving on to slide eight, sustained asset growth is supported by a well diversified funding structure. Our resilient deposit base accounted for 42% of Bladex funding sources while 48% of deposits come from our central bank Class A shareholders. This strong deposit base is complemented by an ample availability of bilateral credit lines from a wide range of correspondent banks and by the continuous access to the global capital markets where Bladex is a recurrent issuer mainly, but not exclusively in the US and Mexico, as well as the global syndicated loan market, all of which represent the remaining 58% of the bank's funding sources. In August, Bladex closed a new public issuance in the Mexican market, which amounted to 5.5 billion Mexican pesos or the US dollar equivalent of $275 million with two tranches of three and a half years and five years.

Turning to slide nine, the bank's capital strength remains a pillar of our business model and a critical factor recognized in our ratings. In recent quarters, we have taken advantage of increased demand for short term trade financing while widening lending spreads, allowing us to achieve a more efficient use of capital. We remain committed to maintaining a sound capital position and anticipate a deceleration in loan growth in the common quarters, unexpected slowdown of economic activity and commodity prices. In this sense, we expect an inflection point in capital ratios having reached a Basel III Tier 1 ratio of 14.4% and the Panamanian regulators capital equity ratio of 12.2%, both well above regulatory minimums. In addition, the board recently declared a dividend of 25 cents per share for the quarter unchanged from preceding quarters, representing a payout of 34% of third quarter earnings. We continuously analyze capital management alternatives to optimize our capital structure and to support growth opportunities.

Please turn to page 10. Top line revenue growth remains mainly driven by solid NII performance, which in turn is backed by strong net interest margin and net interest spread expansion. Net interest spread representing the rate differential between interest earning assets and financial liabilities have been continuously expanding on the account of increased lending spread as mentioned earlier. In turn, net interest margin, which also considers the portion of assets financed by our equity was supported by both higher net interest spread and by the impact of increasing market rates on the overall yield of assets financed by the bank's equity.

Let's now move on to slide 11. Presenting in more detail the quarterly evolution of NII, which increased by $7.5 million sequentially. The continued positive trend in net interest margin that I just discussed up 23 basis points sequentially and reaching 1.77% in the third quarter resulted in a rate effect increase in NII of $5.3 million in the period. At the same time, the average loan portfolio increased by $423 million sequentially, accompanied by the related increase in financial liabilities and a continued proactive liquidity management. This resulted in a positive net volume impact on NII of an additional $2.2 million for the period.

Moving on to slide 12. Fee income from letters of credit remained stable from previous quarter and up from last year representing a consistent support in fee generation complimented by loan structuring and syndication fees. An activity that picked up during the quarter with four transactions executed resulting in a sequential increase of $2 million. Syndications activity is transaction based, so its trend should be analyzed on an annual basis. After a period of nearly no activity during the pandemic, we started to see transactions again since the second half of 2021. In the trailing 12-month period ending September 30, 2022 fees from syndication activity total $6 million.

As shown on slide 13, Bladex maintains strong asset quality levels. Provisions for this quarter increased to $4.8 million compared to the $0.8 million in the prior quarter. Stage 1 exposure, which accounts for 98% of the total increased by $204 million during the quarter on new loan origination requiring $1 million in credit allowances at a 41 basis point reserve coverage. Lower Stage 2 credit exposure was offset by the increase in reserve coverage at close to 15% as the result of a $3.9 million credit provision requirement in connection with a couple of isolated credits with increased risk since origination. In addition, NPLs or Stage 3 credits remain unchanged at close to 0% of total loans. Reserve coverage increased nine percentage points for this loan compared to the previous quarter, compensated by recoveries from loans written off in previous three years, resulting in minimal Stage 3 provisions.

Moving on to slide 14. During the third quarter, the efficiency ratio improved to 31.6% as strong revenue growth more than offset an increase in operating expenses, which totaled $14.6 million. The new variable compensation structure closely tied to strategy, execution, and financial performance together with new hires supporting the underlying business growth remained the main driver behind the $2.8 million annual increase in salary-related expenses. The increase in other operating expenses mostly relates to strategy implementation costs. By design, strategy execution expenses have been programmed so that they can be covered by incremental revenue throughout this process, as it continues to be the case in this quarter. As we scale up the business under the new strategy, we expect to see further improvements in efficiency in the medium term.

Turning to slide 15, we delivered this quarter and annualized ROE of 10.3% up from 9.1% in the second quarter and 6.1% a year ago. This improvement in profitability was driven by several factors including the sustained trend in margin enhancement, continued loan growth, resulting in a more efficient use of capital. This together with top line growth, including higher field generation, ongoing capture of operating efficiencies more than offset increasing expenses and credit provision, all of which resulted in a profit of $27 million for the quarter, up by 17% sequentially and 71% year in year. I would now like to turn the call back to Jorge for closing remarks. Thank you.

Jorge Salas:

Thanks, Annie. So we are pleased to report another quarter consistently delivering an improved operational and financial results capitalizing on Bladex's unique position with operations in over 30 countries across the region. Prior to closing this call, I'd like to remind you that we'll be hosting a virtual investor day on November the 14th. That day, we will take a deeper look in our strategic plan. Several members of my management team will join me in sharing with you more details about the different phases of our plan and the progress on each front. We will discuss how we are focusing on attracting and retaining the required talent and improving our processes and infrastructure to effectively scale our operations. Moreover, we will provide near term and midterm operating and financial goals in KPIs to track progress over time. We look forward to sharing our plans with you. In the meantime, our investor relations team is available to you to answer any questions. And now I would like to close the call and open it up for the Q&A.

Moderator:

Thank you. We will now move to the question and answer section. If you would like to ask a question, please press star two on your phone and wait to be prompted. If you are dialed in by the web, you can either type your question in the box provided or request to ask a voice question.

So our first question comes from Ricardo Vallarino from Ingenieria Orion. There are actually two questions. Question one, can you please give us specific numeric goals for the five year plan? For instance, ROE, capital ratios and lending margins. Where do you see the range for all of these at the end of the five year plan? And question two, can you share the rationale behind the decision by the Board of Directors to not raise dividends? The latest EPS of not quite $0.74 gives a projected annual EPS run rate of approximately $3. The current payout ratio is 33%, which is the lowest Bladex has had for more than 15 years.

Jorge Salas:

Yes, thank you Ricardo, for your two questions. I'm going to tackle the first one first. We will talk extensively about our metrics and the guidance and the rationale behind in the upcoming virtual investor day. As I just mentioned, it's November the 14th. I can say however, that we plan to achieve sustained ROE in the mid-teens by the end of 2026. Additional value added products on the commercial side and the treasury side will be discussed extensively and that will be key for that increased ROE. I can tell you that the pace of growth will not be as fast as you have seen this year. The focus will be profitability and our base case is to grow organically through retained earnings accumulation.

And the second question was about dividends and the fact that we have the lowest payout ratio in years. It is true, it is the lowest payout ratio in years, but it is also true that for years life has experienced very minor changes. I mean very limited growth and frankly, subpar returns certainly below our cost of capital. Bladex has entered a new phase. The plan we have put together is delivering and will be delivering growth and higher returns going forward. And in this volatile context, the board is having active discussions on capital management. I can tell you though that one principle that is not going to change is the strong capitalization will remain. It's a pillar of our ratings and I know that will not change going forward.

Moderator:

Thank you. So our second question is a voice question and comes from James Adam from Mac Solutions. James, please go ahead. Hi James. I'm not sure if you are mute, but we can't hear you. Are you there? I think we'll have to come back to James.

So our next question is a text question and it comes from Patrick Brown. Patrick says, Congratulations on the good results. You explained well how Bladex has done a good job of taking advantage of the current context and implementing the new strategic plan. But just in regards to perhaps some headwinds, that's mostly a slowdown in growth due to a deterioration in the regional and global economic context. My question is, what does that do for your business? Are you going to be able to keep the margin expansion?

Jorge Salas:

Thank you, Patrick. There's no doubt that rising rates combined with inflation and the quick tightening of the monetary conditions have made the world more volatile and more uncertain. It is also true that for Latin America, the economic outlook has deteriorated. We see fiscal pressures growing, financing costs have risen, and you see a lot of countries with currency evaluation pressures. But our model has allowed this bank to successfully navigate through challenging environments like this before. The performance, during the pandemic is perhaps the clearest and most recent example. And I can say certainly not the only one. We did, as I've said before, very active risk management.

We are able to reshuffle the portfolio and keep asset quality under control actually improving. Now the flip side of this is that historically in lockdown, in moments of crisis, or recession like this one larges competition from global bank reduces. Also the debt capital markets alternatives become less available and more expensive for our clients, corporates, and NFIs as well. So that combination has historically favored Bladex. Favors because it allows us to increase our margins as we are doing today. And we do not expect this time around to be different. I would also like to mention that the pricing discipline that has been installed by our new chief commercial officer is here to stay and we will favor margins even if that means reducing our volumes going forward.

Moderator:

Thank you. So our next question is a voice question that comes from Jim from Singular Research. So Jim, please go ahead.

Jim:

Yes, thank you. Can you hear my question and hear my voice?

Moderator:

Yes, we can hear you.

Jim:

Hello? Okay, great. So yes, a very encouraging quarter. The results are a clear indication that you are managing the business very effectively and prudently. You also explained well in regards to the risks that Bladex faces, particularly in the LatAm region. However, I am just curious in regards to just future direction in terms of preparing for any type of headwinds.

So as you mentioned, we have a high inflationary environment, a currency devaluation in many of the countries in which you service. We're facing higher interest rates by many of your clients. And so I'm just kind of trying to get an understanding what are some of the actions that you are looking to do going forward to address that? So I know that you've kind of strengthened the loan portfolio, but what about in terms of provisions? Are you going to be booking higher provisions going forward and just any other things that you're going to do in terms of managing that business? Thank you.

Jorge Salas:

Joining the call Sam Canineu, our Chief Commercial Officer.

Samuel Canineu:

Thanks James. Thanks for the question. I'll say first and foremost, I'll split the answer in two. When we look at, from a credit standpoint, when we look at the headwinds, we believe that we come strong in terms of how our portfolio composition in terms of the type of clients that we have. We are not, I mean our NPL ratios, the reality which is a low risk portfolio and given our portfolio is so short term, we basically tested quarterly. We basically had almost 4 billion of repayments in the last quarter and we collected all. So I think from that side, I think we came well prepared. We continue to manage prudently every new client that we had meet such standards.

And then when we look from the commercial side, I think it's actually a great opportunity because I think as Jorge mentioned earlier, we can reprice fast and take advantage of higher spreads. I think much more than the average. And in moments like this, and also as it was mentioned by Jorge, we managed to really take advantage of increasing spreads to, I would say, to hire great clients who normally wouldn't pay such margins. But in moments like this, they want to tap liquidity, they want build cushion, and we do keep limits approved on uncommitted limit. So it doesn't cost us much, but to be ready to take advantage of such opportunities and when we're pricing such transactions, we're looking at our cost of opportunity being the bond prices if the client has public instruments as well as other sources. So I think all in all, we believe that this can be favorable. Of course we are managing very carefully and being selective, but I like from a commercial standpoint, I think it's very reward- I like where it's going. Thank you.

Jim:

Yeah, that's great. You addressed the operationally what you plan to do forward and that's very encouraging. Can I also ask, is there any thought towards any M&A activity? Is there any kind of thought into perhaps any acquisitions of maybe a smaller bank or joint venture or acquiring different product footprint like perhaps retail banking or investment banking or brokerage or anything else that relates to banking? Is there any thought towards any expansion and taking advantage of market opportunities that way?

Jorge Salas:

Thank you for that question. The short answer is no. This plan has been put together on top of the competitive advantages that Bladex has. We believe that there are lots of opportunities within the trade space. We will not change our focus from trade. We'll be expanding our product mix within trade, both on the commercial side and on the treasury side. But the profile of our customers will not change and we'll not be adding additional product lines aside of those within that, let's say that trade and trade-related world. Just perhaps what the only thing that I mentioned in the last call is we are starting to get our feet wet with the project financing and we'll be talking more of that in our investor day.

Jim:

Okay, thank you Jorge.

Moderator:

Thank you very much. I'm not seeing any more questions, so perhaps I can hand back to the Bladex team for closing remarks.

Jorge Salas:

Well, thank you all very much for your questions and looking forward to have you all so we can discuss extensively on our virtual investor day, November the 14th. Thank you very much.

Moderator:

That concludes the call for today. Thank you and have a nice day.