Bladex

Q2 2024 EARNINGS CALL

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Participants:

- Jorge Salas, Chief Executive Officer
- Ana de Mendez, Chief Financial Officer
- Samuel Canineu, Chief Commercial Officer

Operator:
Good morning, ladies and gentlemen, and welcome to Bladex Second Quarter 2024 Earnings Conference Call. A slide presentation is accompanying today's webcast and is also available on the Investors 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. Please note, today's conference call is being recorded.
I would now like to turn the call over to Mr. Jorge Salas, Chief Executive Officer. Sir, please go ahead.

Jorge L. Salas
Chief Executive Officer

Good morning, everyone, and thank you for joining us today for our Second Quarter 2024 Earnings Call. I'll start by summarizing our performance for the quarter. Then, as usual, Annie, our CFO, will provide a detailed analysis of our financial statements. After that, I will update you on a key initiative from our strategic plan before we open the call for questions.

So, moving on to Slide 2. Here you can find a high-level summary of our quarterly results. I'm pleased to report that they are very much aligned and even slightly better than the guidance that we provided at the beginning of the year. Our commercial portfolio achieved a solid 6% growth quarter-on-quarter, primarily driven by our unfunded business, that includes loan commitments and also letters of credit.

Deposits kept growing steadily and have reached a record level of $5.3 billion, an increase from the last quarter and an impressive 29% year-on-year growth. This $500 million surge marks our largest quarterly deposit increase since the implementation of our strategic plan a couple of years ago. This growth was largely fueled by deposits from corporate clients and financial institution clients as well as our Yankee CD program.

Deposits provided by Central Bank's Class A shareholders also increased by 18% during last quarter. Back in 2021, deposit growth was identified as a key goal of our strategic plan, not only from the point of view of further enhancing the diversification of our funding sources, but also from the cost efficiency perspectives. With this purpose in mind, the Bank focus on reengineering and automating key processes to support higher transactional levels, while also implementing a targeted commercial plan with clear KPI for deposits and the balanced workers of our front line teams.

There is still a lot of work to be done in this front, but there is no doubt that the alignment of clearly defined commercial and operational objectives has been essential to achieving this substantial increase in our depositor base. Deposits have grown $2.2 billion, 73% since we started implementing the plan at the beginning of 2022.

Today, Bladex's loan-to-deposit ratio is 1.4x as opposed to 1.9x with a portfolio that is now almost $1.7 billion bigger than a couple of years ago. Moreover, they now represent 58% of total funding as opposed to 45% a couple of years ago. Also on the funding side, Bladex successfully raised $400 million with a syndicated loan this quarter, the largest syndicated loan in our history, involving 33 banks from across Asia, Europe, and the Americas. I am proud of my Treasury team for this achievement that highlights our robust global bank relationships and the access to international debt capital markets.

On the P&L side, despite the significantly more competitive environment with capital markets widely open for top Latin American names and a clear increase in liquidity, both in dollars and in most domestic currencies in Latam, our net interest income remained essentially unchanged. Annie will delve into this later.

Net interest margin stood at 2.43% for the quarter, slightly below last quarter. Having said that, our projections are still aligned with our guidance for the year, with the net interest margin in the 2.5% area.

Moving on to fees, we have great news in this front. Fee income generation has been another key focus of Bladex's new plan. We have achieved a 32% quarter-on-quarter increase and 93% year-on-year increase. This exceptional performance was driven by our syndications and structuring team, who had a record-breaking quarter. The enhanced syndication team led 5 transactions, reaching $1.2 billion during the quarter. Transactions were closed across Mexico, Guatemala, Colombia, Chile, and the Dominican Republic, serving clients in energy, industrial and also the financial sectors.

Furthermore, the team has a robust pipeline for the second half of the year, which should sustain the momentum we have achieved in our fee income. I am proud of the traction our syndication team is gaining, which reinforces their well-deserved reputation of one of the region's top structuring and syndication teams. Also on fees, our letters of credit business also continued to perform strongly with a 9% increase quarter-on-quarter.

On the expense front, we closed the first half of the year with an efficiency ratio of 25%. As I said in our last call, you should expect an increase in expenses in the second half of the year due to planned initiatives to enhance -- to keep enhancing, I will say, operational capabilities. We may, however, still end the year with an efficiency ratio below our projected 30%.

All this led to a strong net income of $50 million for the quarter, consistent with the previous quarter and representing a substantial 35% increase compared to the same period last year. There is no doubt that this robust year-over-year growth on the bottom line is a testament of our continued strength of our business model and the successful execution of our strategic plan.

Finally, I am pleased to report a return on equity of 16.2% for the second quarter, an increase of 279 basis points compared to the same period last year. This reflects the strong profitability of a bank that has optimized its capital allocation and operates with a minimum liquidity gap, no FX risk and historically excellent asset quality.

I'll now hand it over to Annie, our CFO, for a detailed financial analysis. Annie, go ahead.

Ana Graciela de Mendez
Executive VP & CFO

Thank you, Jorge, and good morning, everyone. Let's now move to Slide 3. As Jorge mentioned, the Bank has maintained a strong performance trend with quarterly net income reaching over $50 million for the second consecutive quarter, marking an annual increase of 35%. These results represent a 2% return on assets and a 16% ROE and add up to a $101.4 million net income for the first half of the year, up by 37% from last year.

Jorge has touched upon the main drivers of this bottom-line performance, so let me expand on it a bit more, starting with our asset growth and composition on Slide 4. Loans increased by 9% on an annual basis and were up by 1% from the previous quarter. Including off balance sheet items, commercial portfolio grew by 13% from last year.

During this second quarter, we have observed a substantial increase in liquidity in our operating markets, leading to heightened competition and margin pressure. Nonetheless, we continue to see demand and business growth, particularly in our trade-related lines of business, such as letters of credit confirmation and the discounting of cross-border receivables or vendor finance. This growth is driven by our efforts to add new clients and cross-sell as well as by increased structured transactions on both products, all while maintaining our focus on providing tailor-made solutions for our clients.

We were also able to increase longer-tenor transactions with a robust performance of our newly formed project finance and infrastructure business, along with the ones originated through our syndications desk, where we see a strong pipeline going forward. Overall, average loans and lending spreads remained stable quarter-on-quarter and denote an increase from last year.

In the next slide, we present our commercial portfolio on the right, which continues to be well diversified throughout the Latam region, with top exposures to Brazil at 12% and to Mexico and Colombia at 11% each, closely followed by Guatemala and the Dominican Republic at 10% each. Both countries in the Central American and Caribbean region with good economic prospects, where we continue to execute on solid risk/reward opportunities.

On the left-hand side, the Bank's Investment Securities portfolio remain at $1.1 billion at quarter end, same as the prior quarter. 78% of this portfolio is placed with non-Latam issuers, mostly from the U.S., providing country risk diversification to our credit book. Furthermore, 86% is placed with investment-grade issuers and is eligible to be discounted with the Federal Reserve through our New York agency, thus providing contingent liquidity funding. The average remaining tenor of the portfolio is a little over 2 years.

On Slide 6, you can see our credit exposure, that is loans, investments and off-balance sheet items combined, classified by stages as per IFRS 9. Stage 1 or low-risk exposure accounted for 94.5% of total exposure at $9.8 billion, an increase of over $300 million or 3% from the previous quarter, which explains most of the increase in credit reserves. Of the $6.7 million in credit provision charges for the quarter, Stage 1 growth represented most of it, totaling $6.2 million.

On the other side, Stage 2 exposure now represents 5.5% or $563 million. Notably, although Stage 2 exposure has increased from 3% of total exposure on the preceding quarter, its overall quality has improved. This is explained by the collection of scheduled maturities of higher risk exposures categorized as special mentioned and/or monitoring, which has been offset by the increase of low risk, mostly very short tenor and quasi government exposures with revised downward risk ratings as part of our proactive client risk evaluation process.

As a result, Stage 2 allocated reserves remained relatively stable with a credit reserve requirement of only $0.4 million during the second quarter. Finally, only a minimum 0.1% of total exposure remains classified as Stage 3 impaired credits or NPLs, amounting to $10 million, with a total reserve coverage of 7.5x. Overall, the quality of the portfolio remains strong with a robust reserve coverage.

Now moving to Slide 7. Our funding base remains well diversified with deposits now accounting for 58% of the total financial liabilities. As highlighted by Jorge, our deposit base continues to show a robust growth trend, reaching $5.3 billion, which represents a 29% increase from last year and up 11% from the preceding quarter. Central Banks, our Class A shareholders, who place a part of their U.S. dollar international reserves with us, account for 39% of total deposits, a very stable source of funding over time. The remaining 61% comes from our client banks and corporations, a source that has been showing a strong growth over the last several quarters as a result of our cross-selling efforts.

As Jorge pointed out, our Yankee CD program, which operates out of our New York agency through broker-dealers distribution, continues to provide both volume and granularity, representing 26% of total deposits at the end of June. Jorge has also already mentioned another important funding transaction in the global syndicated market, which, along with our recurrent access to global capital markets and a broad network of correspondent banks worldwide, provides a solid funding base with ample geographic and tenor diversification.

The Bank's equity position presented on Slide 8 continues to be enhanced by strong earnings generation. Our Board recently declared a $0.50 per share quarterly dividend, unchanged from the preceding quarter on the back of strong financial performance. Even as we continue to grow our business and our balance sheet, we aim to maintain our capital ratios at current levels as a reflection of our internal risk appetite and in defense of our investment-grade ratings.

Moving on to P&L performance on Slide 9, you can see the evolution of net interest income and margins, the main component of revenues. Net interest income has remained stable over the last 2 quarters at close to $63 million, representing an annual increase of 15%. Sustained margins and higher average asset volumes have driven this strong top line performance.
Over the last year, we have seen a positive trend in net interest spread or NIS and net interest margin, or NIM, continuing the momentum that began with the execution of our new strategy in 2022. Enhanced financial margins reflect improved lending spreads with a strict emphasis on pricing and optimization of capital allocation at a transaction level. It also reflects efficient cost of funds management, supported by a higher deposit base, along with higher market interest rates.

During the second quarter, we saw a slight reduction in NIS and NIM from the preceding quarter, reaching 1.74% and 2.43%, respectively, mainly resulting from the effect of the inverted yield curve on a higher, very short-tenor deposit base, reducing the base rate differential between assets and liabilities. When market interest rates begin to decline as widely anticipated, we expect a correction in the yield curve, which should benefit our short-tenor interest rate gap position.

Slide 10 showcases our solid fee income performance. In the second quarter of 2024, it nearly doubled compared to the same period of last year. Our letter of credit business, a key strategic pillar, has grown to a quarterly level of $6.5 million, having streamlined processes benefiting from new client additions as well as some very profitable control opportunities.

Once we complete the automation phase of this key trade finance product, we should be able to continue to scale this important revenue stream. As Jorge mentioned, we also had a strong quarter in our structuring business, having closed 5 transactions during the quarter, generating $3.7 million in fees for a total of $5 million in the first half of the year, denoting an outstanding performance.

On Slide 11, expenses remained stable quarter-on-quarter at $18 million, improving efficiency to a level of 24% for the quarter on strong revenue growth. The annual 17% increase in quarterly expenses mostly relates to a higher salary base as our workforce increased by close to 50% over the last couple of years in line with our focus on strengthening Bladex's execution capabilities, as outlined in our strategic plan.

Let me now turn the call back to Jorge. Thank you.

Jorge L. Salas
Chief Executive Officer

Thank you very much Annie.

Before we open the call for questions, I'd like to share an important update on the progress of Phase 2 of our 2026 Strategic Plan.

As I mentioned in our last call, and in line with our goal to maintain our position as a leading provider of trade finance solutions in LatAm, I'm excited to announce that after a careful vendor selection process, Bladex has selected the state-of-the-art trade platform developed by the top IT consulting firm CGI to optimize our processing and management of letters of credit and working capital solutions.

This award-winning platform is utilized by major banks supporting foreign trade in over 85 countries across Asia, Europe, North America and Oceania. But Bladex will be the first Latin American bank to adopt this world-class technology. This trade platform will significantly enhance efficiency, security and transparency in Bladex's operation, enabling our corporate clients to manage their financial needs swiftly and accurately on a single integrated global platform.

The implementation of this project started just a few days ago with a dedicated multidisciplinary team from both institutions collaborating over the next 10 to 12 months to deploy this advanced trade finance technology under the supervision of Bladex's PMO office. We will keep you updated on the progress of this and other key projects.

I'm going to leave it here for now and open the call for questions. Operator?

Q&A Section of the Call

Our first question comes from Íñigo Vega from Jefferies.
This is Inigo Vega from Jefferies. Very quick 3 questions. First one is on the super high growth we've seen in commitments and guarantees off-balance sheet. I see that growth is much higher than on-balance sheet lending. Can you say where is it coming from? Is it commitments? Is it [less updates? And if there's any concentration in any particular country?

Second one is on the partnership on the trade finance platform you mentioned with GCI. Can you sort of give some color on when would we expect some revenue or additional revenues from this? What is the pipeline of new products? I understand you can launch new products with the platform. So if you can give us some color on that would be super helpful.

And the last one is on competition. You mentioned the market is competitive. Capital markets are wide open. I've seen that lending yields are down like 4 bps in the quarter. It's not a lot, but if you can sort of comment on where is the competitive environment today, and where do you see the competitive environment over the next few months? That's all for me.

Jorge Salas, CEO:
Hola Inigo. Great questions. Let me start by the last one on margins. Sam, our Chief Commercial Officer, is here with me. He is going to tackle that one, and then I'm going to talk about the other 2 questions on off balance sheet and the trade finance platform.

So, Sam, do you want to tackle the first one?

Samuel Canineu, CCO:
Sure. Thanks, Jorge. We're definitely facing a very competitive environment on lending, which was already referred by you and Annie in your initial remarks. Besides the pressures of excess liquidity in U.S. dollar in general and a much more active international DCM market, the other point of pressure has been more favorable local markets for borrowers compared to U.S. dollars, as some countries have started to cut rates before the Fed.

Despite such pressures, however, we're happy with how we have been able to hold up our net interest margins rather stable, and that is partially due to the continuous rollout of this strategic plan. Special mention here to the strengthening of our syndication practice, which was already mentioned that not only bring fees but also deals with higher margins, given their medium-term nature for the most part as well as the good ramp-up of our project finance and infrastructure business.

Case in point, the closing of the refinancing of the AERODOM transaction in the Dominican Republic, Aeropuertos Dominicanos which we acted as one of the joint lead arrangers in a $440 million credit facility to support the first-class global sponsor in a country that has a quite pungent economy, particularly fed by the international tourism that has been -- that has grown infrastructure needs.

We do expect the margin pressures to continue, but we also do expect the rollouts of the new strategy with transactions that comes with the higher margins to continue as well and to counter that pressure. I feel that we continue to be navigating well and we -- I hope to continue -- to stay like that. Thank you.

Jorge Salas, CEO:
Okay, that's -- that answer your question, Inigo? I mean...

Íñigo Vega, Jefferies:
Absolutely. Super helpful. Yes, very clear.

Jorge Salas, CEO:
Let me talk now about the increase in the off-balance sheet item. It was a significant increase about 33%, as you mentioned. The bulk of that is related to one off, I'm going to say, very short-

term trade-related opportunistic transactions that involve one of our Class A shareholders. Those are mostly letters of credit. Those are responsible for the bulk of our Stage 1 reserves this quarter, but it's more due to the country risk rating, and I'm talking about Argentina here.

We're basically financing imports related to the most basic energy needs in the country. I mean, essential for the country to run. Bladex has done this many times over the year with impeccable track record. If you think about it, Inigo, this is our bread and butter, very short term, trade-related and attractive returns. Don't forget, we also have preferred creditor status in that country. So, that's basically it. We are following the developments in Argentina closely and we believe that the country is going in the right direction, and there might be more opportunities there going forward.

As far as the CGI investment on the trade finance platform, let me just share some key assumptions of the business case behind the investment. We believe that once the platform is up and running, we can be able to process 2.5x the transactional volume we are – just on letters of credit that we are processing today. We expect that to be there about 2x, 2.5x in approximately 2 years. It's very clear that the demand is there even with our current customer base. So, without growing our customer base, it's very clear that we can reach that volume.

Now, the average dollar amount of the, let's say, the incremental transactions will be substantially smaller, maybe half the size of -- per ticket. But the average fee on those tickets tends to be higher. Also, the other important thing is that we will not need to keep adding people to the team to handle this, say, this incremental volume. All this is just on the letters of credit.

On the supply chain finance, the rationale is similar. I mean, it will be able to boost our current vendor finance business very efficiently. In other words, making -- being able to process more volume of smaller tickets with minimal headcount increase. In any case, we expect the incremental revenues just on the letter of credit business will be enough to pay back the cost of the whole platform in about 18 months. That's basically the rationale for the trade finance platform. It's CGI, and it's -- we're very excited with it.

Operator:
Our next question comes from Valentina Marin from Grupo Bancolombia. Her question is:

Valentina Marin from Grupo Bancolombia
Taking into account the economic and political context in EU where inflation has had favorable behavior, and it's expected that the Fed will cut rates in September. And at the same time, the commercial tensions, rates in -- commercial tensions that have been generated, how do you see this impacting the countries in the region?

Jorge Salas, CEO:
Yes, let me take a -- talk a little bit about how we see the region on a country-by-country basis. First of all, regarding rates, it's clear that Central Banks in advanced economies have started to ease their monetary cycles. And that, of course, will impact Central Banks in the region, perhaps

later than we originally thought. So, real interest rates in the region may remain restrictive towards the end of the year.

Now, on a country-specific basis, we see -- we have like 3 groups of countries. So first, Uruguay, Guatemala where we have grown a lot, Costa Rica, Paraguay, Dominican Republic also an important country for us, are perhaps the best prepared in terms of economic fundamentals and policy response from -- so that will be the first, let's say, strategic group for us.

Second, obviously, Brazil and Mexico remain important for us due to their size. They do face clear fiscal and political risks. Then we have -- so another group of countries where we have Chile, Peru, Colombia and Panama. There are persistent political risk and, I will say, weak growth outlooks. And then we have Ecuador, Argentina, El Salvador, Bolivia, where we have minimal exposure. Those are countries that face structural challenges and are undergoing significant economic adjustments.

I mean, those are the countries that -- now, in any case, I think it's always important, Valentina, to keep in mind that our client base consists of large, solid corporations and banks that we have a very long-term relationships with most of them and very deep knowledge.

Sam, do you want to add something?

Samuel Canineu, CCO:
Yes. I think it's -- just to finalize the answer to this question, I think it's very important also to remind that in times of a little bit more noise in the region, that's when really Bladex can take a more opportunistic approach and find profitable transactions that have short-term duration. And historically, those have been good times for Bladex as liquidity from, let's say, the global players tend to dry up. So we're positioned to capture, if that indeed happens.

Operator:
Okay. Thank you very much. That's all the questions we have for today. I'll pass the line back to Mr. Jorge Salas for the concluding remarks.

Jorge Salas, CEO:
Okay. So, thank you for joining. In summary, I'm going to say another great quarter for Bladex with over $50 million in net income and over 16% ROE. Strategic initiatives on our business plan keep yielding very tangible, sustainable results. Deposit balances are record levels. Fees are record levels. The team as a whole is very motivated, very focused on the implementation of key projects in this phase of the plan. Credit quality remains sound and a top priority, and we're looking forward to share more progress on our plan in our next call. That's it for us. Thank you very much, and see you in the next call. Goodbye.

Operator:
Bladex conference call is now concluded. You may disconnect and have a nice day.