Bladex

Q3 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 to discuss our third quarter results. I'll begin with an overview of another record-breaking quarter for Bladex. Following that, Annie, our CFO, will provide a detailed analysis of our financial results for the quarter. Right after that, I will update you on the progress of our strategic plan and also provide a revised guidance for the remaining of the year. After that, we will open the call for questions.

So moving on to Slide 2, the summary slide. On the balance sheet, the commercial portfolio reached $9.7 billion for the first time, representing a quarter-on-quarter growth of 5% and a year-on-year growth of 17%. Deposits also reached a new record of $5.6 billion, growing 34% in the last 12 months with corporate client deposits nearly doubling compared to last year. This remarkable growth in our most cost-efficient source of funding is a result of the coordinated efforts of our commercial and treasury teams guided by clear deposit growth KPIs in their balanced scorecards. The resulting shift in the funding mix has allowed us to reduce our funding spreads.

We're very pleased with the progress, but more importantly, we see significant potential for further expanding our deposit base in the near future. On the P&L side, despite the more competitive

lending environment due to increased dollar liquidity, widely open debt capital markets for Latin American top names and lower local interest rates in most countries, we have once more achieved record results.

I would especially like to highlight the evolution of non-interest income. Total fees for the first 3 quarters are up 45% compared to the same period last year. The letters of credit business also had a record performance, generating $7 million in the last 3 months, a growth of 8% Q-on-Q and 12% year-on-year. Syndication fees decreased slightly this quarter, but we feel confident that with the pipeline we have, we are on track to close the year also with record figures in both the number of deals and total syndication fees.

Regarding expenses, as we have forecasted in previous calls, our costs have increased in line with the anticipated investments required by this second phase of our strategic plan. As a result, and in line with expectations, our efficiency ratio rose slightly to 27%, which is in line with the guidance we have been providing for the year.

These strong financial results culminated in a record net income of $53 million for the quarter, a 16% increase compared to the same period last year, which resulted in a return on equity of 16.4%. Given this stronger-than-expected performance, I will provide you all with a revised guidance for the year before opening the call for questions.

Let me now hand it over to Annie, our CFO, for a detailed financial analysis. Annie, please go ahead.

Ana Graciela de Mendez
Executive VP & CFO

Thank you, Jorge, and good morning to everyone. Let's now move to Slide 3. Quarterly profitability continues to be enhanced by sustained top line performance, as Jorge mentioned, driving third quarter net income to $53 million, marking an annual increase of 16% and up by 6% quarter-on-quarter and representing $1.44 per share.

Year-to-date, net income for the first 9 months of this year reached over $154 million, a solid 29% growth from the same period of last year. In the graph, you can see the growth trend since we started executing our strategy in 2022 with year-to-date results that have more than tripled from 2021's levels. The bank has sustained its profitability for the last 3 quarters at a ROE level above 16% and an ROA of 1.9%. When compared with the levels observed at the inception of our strategic plan, ROE has tripled from the same period of 2021, while ROA has more than doubled.

Let me now go into more detail over balance sheet growth and other profitability drivers into more detail, starting with the asset composition on Slide 4. Total assets reached $11.4 billion, up by 13% from last year and 5% quarter-on-quarter. This was mainly the result of strong loan growth, surpassing the $8 billion mark for the first time in Bladex's history, up by 17% from last year and 9% from the preceding quarter.

The commercial portfolio, which includes loans and off-balance sheet items, reached $9.7 billion as our significant loan growth was coupled by a letter of credit business continuing to grow in scale. A liquidity position of $1.7 billion, mostly placed with the New York Fed representing 15% of total assets and 30% of deposits, reflecting a prudent liquidity management aligned with Basel's liquidity coverage ratio.

As can be seen in Slide #5, on the left-hand side, the securities portfolio amounting to $1.2 billion is mostly placed with investment- grade non-Latam issuers, mostly from the U.S., therefore, providing further country risk diversification to our overall credit exposure. Most of this portfolio is booked in our New York agency and is therefore eligible to be discounted with the Federal Reserve, allowing for contingent liquidity funding if needed. The portfolio has a relatively short duration with an average remaining tenor of approximately 2 years.

The composition of the commercial portfolio on the right denotes a well-diversified country exposure across LATAM. Brazil and Mexico represent strategic markets for Bladex, given the size of their economies and relevance to the trade activity of the region. They are among the bank's top country exposures at 14% and 11% of the total, respectively, along with other relevant country exposures in South America, such as Colombia at 11% and Peru at 9%.

We are also focusing our growth strategy in certain Central American and Caribbean countries, particularly the Dominican Republic and Guatemala, both with good economic fundamentals where we continue to execute on solid risk/reward opportunities, each representing 10% of total exposure at quarter end. The commercial portfolio remains short-term in nature, with 75% scheduled to mature within the next year, having an average remaining tenor of 12 months at quarter end.

In fact, the portfolio has a high rotation of about 2x in a year. This means that more than half of the portfolio matures every quarter and new loans are placed. This agile business model allows us to quickly react to market conditions and be able to jump on profitable opportunities as they arise. This agile short-term business model with a top-tier client base of banks and corporations across Latin American countries and industries is the foundation of Bladex's strong asset quality, as shown on Slide 6.

At quarter end, 95.7% of the credit portfolio, including loans, investment securities and off-balance sheet items, was classified as low risk or Stage 1 as defined by IFRS 9. Only 4.1% of the portfolio was classified as Stage 2, down from close to 6% in the preceding quarter as we collected maturities of exposures that had been classified in Stage 2 during prior quarters. Although Stage 2 exposures represent credit with increased risk since its origination, all of them are currently performing.

Finally, only a minimal 0.2% of total exposure is classified as Stage 3 impaired credits or NPLs amounting to $17 million with a total reserve coverage of close to 5x. During the third quarter, a $7 million loan was classified from Stage 2 to Stage 3. This represents an isolated Colombian

exposure in the oil and gas supply chain sector, which has been in runoff mode since before the pandemic and which in our assessment has recently further deteriorated. Credit provision charges for the third quarter were $3.5 million, mostly relating to individual reserves in Stage 3, partly offset by a $1 million recovery from a loan charged off several years back. Overall, the quality of the portfolio remains strong with robust reserve coverage.

Now moving to Slide 7. Our well-diversified funding sources continue to support strong asset growth. Our deposit base carries on with a strong growth trend, reaching yet another record level at $5.6 billion at quarter end, representing a notable 34% annual growth and 7% quarter-on-quarter. Deposits now account for 59% of total funding.

Our Class A shareholders, mostly central banks who place part of their U.S. dollar international reserves with us account for 43% of total deposits, a very stable source of funding over time. The remaining 57% comes from our client banks and corporations, a source that has been showing a positive growth trend over the last several quarters, as a result of our cross-selling efforts. 24% of total deposits at the end of September came from our Yankee CD program, which operates out of our New York agency, predominantly through broker-dealers distribution and continues to provide both volume and granularity.

The bank's equity position presented on Slide 8 continues to be enhanced by strong earnings generation, remaining within our target capitalization levels despite strong balance sheet growth. Our Board recently declared a $0.50 per share quarterly dividend, marking the third consecutive quarter at this level on the back of strong financial performance. We expect earnings generation to continue to support business growth as well as dividend distribution as decided and declared by our Board on a quarterly basis.

Moving on to P&L performance on Slide 9, you can see the evolution of net interest income and margins. Net interest income of $66.6 million for the third quarter was up by 10% from the year before and by 6% from the preceding quarter. This top line growth is mostly explained by the net effect of higher average loan balances, which were up by 9% annually and by 3.5% quarter-on-quarter, improving the mix of average interest-earning assets and positively impacting the net interest spread and net interest margin.

Despite a more competitive market environment, as Jorge pointed out, we have been able to sustain lending credit spreads over the last several quarters as we continue to emphasize pricing optimization, coupled with improved levels of funding spreads benefiting from increased deposits. Hence, net interest spread and net interest margin for the quarter reached 1.78% and 2.55%, respectively. Year-to-date, NIM at 2.49% reflects our stated target levels.

As showcased in Slide 10, the bank had a solid fee income performance, reaching $10.5 million for the quarter and $32.5 million for the first 9 months of the year. This represents a 45% increase compared to the first 9 months of last year. Our letter of credit business continues to perform well with fees for the third quarter of close to $7 million.

As we have mentioned before, the continued growth in this business has been the result of streamlined processes and client additions. We are currently in the process of implementing our new LC platform, which should start to bear fruits towards the end of next year, when we should be able to further scale this important fee revenue stream.

Structuring and syndication fees decreased during the third quarter to $1.5 million, having closed two transactions after a stellar second quarter when we were able to close five transactions. As this is a transaction-based business, we see some quarterly fluctuations. But in any case, we foresee a strong performance for the remaining of the year with a solid pipeline of transactions on the way.

On Slide 11, even though expenses for the third quarter increased by 15% quarter-on-quarter and 8% from last year, our cost-to- income ratio stood at 27%, right on target. The main driver in expense growth is a higher salary base due to increased headcount aimed at enhancing business volumes through product deployment and client additions as well as new functions supporting our strategy. Personnel expenses for the quarter also increased on the account of higher provisions for performance-based compensation, given yet another year of earnings growth above our initial projections.

Let me leave it here for now and turn the call back to Jorge. Thank you.

Jorge L. Salas
Chief Executive Officer

Thank you, Annie. Let me now take a step back and give you a bigger strategic picture on the successive phases of our 5-year plan that we started executing in 2022. As I have mentioned in previous calls, we are transitioning from the optimization phase to the expansion phase of our plan. Phase 1 objectives have been achieved. We've optimized our balance sheet leverage. We've expanded our customer base, preserving the risk profile. We have significantly increased deposits. We have strengthened our teams, and we have improved operational efficiencies.

The results have surpassed our initial expectations, unlocking more value than we had anticipated. While we have accomplished a great deal, some of our most challenging work still lies ahead as we transition to the second phase of our strategy. Phase 2 focuses on the expansion of our product offering. This phase involves implementing two new platforms to support our trade finance business and our treasury business. As we have highlighted, we believe that these two areas hold significant upside. The trade platform will not only digitalize our letters of credit unit with a state-of-the-art client interface, but also add substantial transactional processing power to our working capital solutions business.

I'm pleased to report that we're making solid progress in the implementation with our partner, CGI, announced last quarter. Project is on target. We have already completed close to 30% of the work, and we anticipate having the platform up and running in the second half of next year. On the other hand, the treasury platform enabled us to offer derivative products to our clients and to

further enhance our capability to provide local currency lending, always hedging the resulting FX exposures. We believe that offering treasury products to our client base will unlock a relevant source of noninterest income that Bladex has never been able to capture.

These products are a natural complement of the different lines of products that the bank is already delivering, such as letters of credit, bilateral and syndicated medium-term credit facilities.
Our strong franchise provides an ample regional client platform that we will leverage to foster the development of this new line of business, which we expect to gradually gain relevance as a source of income. We are now in the final stages of our vendor selection process for this initiative. So you can expect to see a joint press release regarding this partnership in the upcoming weeks.

To sum up, the results we've reported in the last 9 quarters are essentially the consequence of the implementation of the initial phase, the optimization phase that is of our strategic plan. The potential benefits of Phase 2 are not yet reflected in these numbers, which means there's substantial additional upside, particularly in the noninterest income generation as we gradually roll out these new capabilities in the coming quarters.

This additional noninterest income, as Annie mentioned, will further consolidate and expand the growth trend that we have maintained in the last quarters and will be key to make our results less sensitive to market rate fluctuations, further reinforcing Bladex's capabilities to deliver robust and sustainable profitability levels.

As far as guidance for the year, we now anticipate our commercial portfolio to grow close to 14% given the increased demand we're seeing in most markets. In terms of deposits, we also expect to exceed our initial forecast of 12% to 14%. Given our performance thus far, we are now aiming at 30% average deposit growth for the year. We've also made significant strides in operational efficiency, and we now expect to end the year with an efficiency ratio of approximately 26%, a notable improvement from our initial estimate of 30%.

As a result of these positive trends, we're revising our 2024 ROE guidance upward. Our new projected range is 15% to 16%, up from the initial forecast of 14% to 15%. This performance demonstrates two things: one, the resilience of a uniquely flexible business model that given the short-term nature of the diversified high-quality loan book and essentially a matched balance sheet enables management to profitably navigate to uncertain times; and two, the disciplined execution for almost 3 years now of a well-crafted strategic plan aimed at maximizing the upside potential of this unique bank.

Once again, as we look forward to the future, we are confident that the full implementation of our strategic plan will unlock even greater potential for growth and value creation, building on the strong foundation we have established thus far.

I'm going to leave it here and ask the operator to please open the call for questions. Thank you.

Q&A Section of the Call

Operator
Our first question comes from Ricardo Buchpiguel with BTG.
Ricardo Buchpiguel
I have two here on my side. So first, we saw that part of the deceleration in the commercial portfolio came from higher loans in Brazil, right? So meanwhile, spreads in the country are a bit more -- meanwhile, we see that spreads in the country are a little bit more compressed due to the higher activity in DCM, right? So I want to understand if you are indeed seeing lower spreads in loans, specifically in Brazil and if we should expect a spread compression at least in this region? And for my second question, I see that we have the U.S. election approaching. So I want to hear your thoughts on, how do you believe a potential election of Trump could negatively impact trade volumes in LATAM and therefore, the commercial portfolio? And also, how was Bladex impacted when he was elected in 2016, if there was any significant impact?

Jorge L. Salas
Chief Executive Officer
Ricardo, I'm going to start with the second question first, the U.S. elections upcoming in a few days. And then I'm going to pass it on to Samuel, our Brazilian Chief Commercial Officer, that will better explain the margins and our exposures in Brazil. First thing I have to say, as you mentioned, it is clear that the presidential elections in the U.S. are very relevant for the region.
Yes. The resulting effects for the overall region are hard to predict. I mean you have short-term effects, you have long-term effects, you have direct, indirect, you have -- depending on the country and the economic dynamic of the country, you may have in the trade partners, you may have a different reality.

Having said that, we see primarily three impacts. One is remittances flows, especially relevant for Central American countries. Also, overall trade flows, particularly relevant for South American countries and Mexico, and of course, inflation and interest rates, which is relevant for everyone.
We're monitoring the effects of remittances flows, particularly in countries where we have relevant exposures like Guatemala, for example, where we have close to 10% of exposure and remittances there represent close to 15% of GDP or the Dominican Republic or in Mexico, where remittances are 3.5% of GDP.

On the trade flows, we are vigilant on the ongoing tensions with China. Keeping in mind also that in the not so long-term, additional disruptions in the global supply chains could potentially accelerate the nearshoring trend as companies potentially move to Mexico or some other Central American countries looking for more resilient suppliers closer to the U.S.

In any case, and having said all that, we feel confident that the short-term nature of the business model will allow us to navigate the potential volatility that will, for sure, take place and also take advantage of the opportunities that for sure will arise given that. I don't know, Samuel, do you want to.

Samuel Canineu
Executive VP & Chief Commercial Officer
Yes. On Brazil, thanks for the question, Ricardo. And you are right, Brazil, we are seeing more competition, particularly from the international DCM side, and that is obviously putting pressure on spreads. Brazil is probably the most competitive market of LATAM, the one that we compete. On the other hand, Brazil is still, I would say, quite underrepresented in our portfolio given its potential. Our growth in Brazil has more to do with the fact that we are now -- as we've been rolling out our new strategy, we've been -- we have a better or more suited product offering for Brazil or for how sophisticated Brazilian clients are.

So we are basically capturing some share on that, and that is driving our growth. So everything to do with the new strategy, particularly on the structured trade finance side. And our growth in Brazil will not be necessarily correlated with the low market conditions as well as the GDP because, again, we are -- as we roll out our new strategy, we're able to onboard clients that in the past, we did not have the right product to onboard.

Operator
Our next question comes from Daniel Mora with Credicorp Capital.
Daniel Mora
I have also a couple of questions. The first one is regarding margins. We have seen a very positive performance, not only in recent quarters, but in the last couple of years. But I would like to understand what will be or what is the current NIM sensitivity to interest rates? And what can we expect of NIM given the decreases in interest rates coming from the Fed? And how can we think this under the analysis that you normally present considering the volume effect and the interest rate effect because we can initially think that we should observe a normalization of margins going forward considering the decreases in rates. And I would like to understand what will be the effect of this also on profitability given that we currently observe at 16% ROE. That will be my first question.

And the second one is, given the fact that we are now in the expansion phase with the deployment of the new two initiatives and the increase of net interest income, do you have a target of what percentage can that net interest income represent of the total income compared to what we are seeing right now? And if given the strong results that we are seeing right now, we can expect of a higher ROE above the current guidance between 13% and 15% for 2026.

Jorge L. Salas
Chief Executive Officer
Daniel, on interest rate sensitivity, I'm going to let Annie, our CFO, speak to that, and then I'll tackle the second question. Annie, you want to?

Ana Graciela de Mendez
Executive VP & CFO

Okay. Yes. Thank you. So yes, you're right, and we have mentioned in several occasions that we are sensitive to market -- U.S. dollar market interest rates. So -- and to talk about the sensitivity, our sensitivity to interest rates and net interest margin is every 100-basis points movement in interest rates could have like a 12-basis points impact on our net interest margin that all translates into like 100 basis points ROE as well. That's basically because we have a floating book in both sides of the balance sheet. And so the assets and liabilities reprice very similarly, although we do have some short-term positions.

And at the end, the overall asset yield that diminishes and that is invested by -- in our equity, it has an impact. And then what we see going forward is that definitely the strategy that we are -- have in place, and that pretty much relates to your second question that Jorge is going to address, but we do anticipate through the structured trade transactions that Sam mentioned and the deployment of new products, both noninterest and also margin related, it should be able to enhance our lending spreads and sustain the profitability. But I'll leave it for Jorge now to continue.

Jorge L. Salas
Chief Executive Officer
Yes, that's exactly right, Annie. The platforms are exactly geared to generate additional noninterest income. Currently, our noninterest income represents about 13% of total revenues and we expect this to gradually climb up to 18% by the end of 2026. That's our target as of today.

Operator
Our next question comes from Miruna Chirea with Jefferies.
Miruna Chirea
Jefferies LLC, Research Division

I just had a quick one on loan growth, please. I can see that you are growing your loans 5% this quarter on what looks like very good margins as well. So I was wondering, where do you see this growth over the next two years? And how do you think about the longer- term growth opportunity and capital management?

Jorge L. Salas
Chief Executive Officer
Yes. Well, loan growth, for sure, has been stronger than we initially expected this year. Brazil, Guatemala, the Dominican Republic have surpassed our initial growth estimates. Sam already talked a little bit about Brazil. Guatemala and the Dominican Republic are also noteworthy. They ranked fourth and fifth today in our largest exposure is about 10%.

In Dominican Republic, in particular, portfolio growth has been fueled, I will say, by increased investments in the energy sector, which has been supported through our recently created project finance and infrastructure unit, along with the country's overall robust growth dynamics. Mexico represents slower and steady growth, also very much driven by the new product rollouts as part of the new strategy.

That's for 2024. 2025, the way to think about portfolio or country diversification, I mean, it's relatively correlated with, obviously, with the size of the economy. There are some countries that are underrepresented in that sense, like Brazil and Mexico, like Sam said, and some countries that are overrepresented like Guatemala or the Dominican Republic. But it's hard to say now what our exposures would be even by next year, given the short-term nature of the portfolio. Do you want to add something, Sam?

Samuel Canineu
Executive VP & Chief Commercial Officer
I think we -- as part of the new strategy, we favor quality versus quantity. So we will continue to have our price discipline. If we see that the opportunities are there to continue to grow profitably, we will continue. We've been experiencing that. We're still rolling out the new strategy, which is opening new markets for us. And we believe there is -- we will always strive also to use our capital efficiently. And we will -- we see there is room to grow as we grow our capital base. That is the focus, but yet maintaining pricing discipline as we established since the initial phase of the plan.

Operator
Our next question comes from William Hayes
Congratulations on some superb results. But it's interesting to note that these results haven't really moved the needle in the marketplace. And I would suggest that a payout ratio of 35% is quite conservative in both your historical and peer comparisons. Given not only your actual earnings but expectations and especially your focus on noninterest income growth, which does not really require capital allocations, when do you intend to increase your payout of earnings through dividends?

Jorge L. Salas
Chief Executive Officer
Good question. Annie, do you want to tackle that? I mean the -- I'll let Annie complement. But as you well known, dividend policy, it's an ongoing discussion, broader capital management, I would say, it's an ongoing discussion. In the case of Bladex, it's a quarterly decision that the Board takes. And the ongoing discussion revolves around total shareholder value and making sure that the upside and the stock price is there, and that's our job, but also the dividend yield is attractive enough. I don't know, Annie, if you want to complement anything else?

Ana Graciela de Mendez
Executive VP & CFO
Yes, -- right on, Jorge, it's always a discussion. Sam just mentioned about us always looking at profitable opportunities. So it's a balance between growth and returning capital. Right now, we are performing very well at 16% ROE. And so that being the case, we think that the current dividend level, and that's the Board's decision is pretty good. And it's an ongoing discussion at the Board level on a quarterly basis. So I think that's what we can say about that.

Operator

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

Jorge L. Salas
Chief Executive Officer
Thank you, Sophia. Before we conclude, I would just like to extend a warm welcome to two prominent sell-side analysts who have recently initiated coverage on Bladex, Credit Corp and BTG Pactual. The inclusion of these respected institutions in our coverage universe is a testament, we feel, of the growing interest in our renewed Bladex. We look forward to engaging with their teams and appreciate their commitment to providing valuable insights to the investment community across Latin America and the world.

With that, we'll leave the call there and thank you very much for joining.

Operator
This does conclude today's conference call. You may disconnect and have a nice day.