

## Update: Banco Regional S.A.E.C.A.

**Primary Credit Analyst:**

Celio P Neto, Sao Paulo +55 11 3039 4827; Celio.Neto@spglobal.com

**Secondary Contact:**

Ivana L Recalde, Buenos Aires + 54 11 4891 2127; ivana.recalde@spglobal.com

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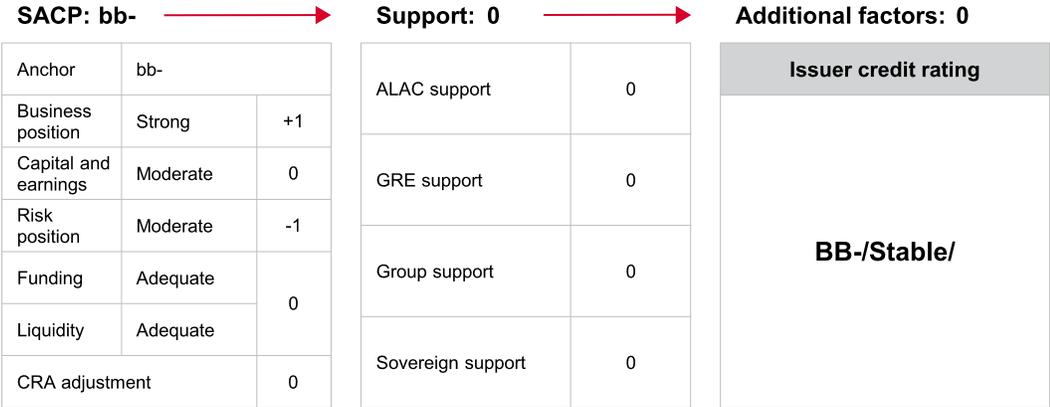
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# Update: Banco Regional S.A.E.C.A.

## Ratings Score Snapshot

**Issuer Credit Rating**  
BB-/Stable/--



ALAC--Additional loss-absorbing capacity. CRA--Comparable ratings analysis. GRE--Government-related entity. ICR--Issuer credit rating. SACP--Stand-alone credit profile.

## Credit Highlights

Key strengths	Key risks
Leading position in the agribusiness sector and one of the largest banks in Paraguay.	Higher-than-average loan portfolio concentration in the agribusiness sector that exposes the bank to economic cycles.
Rabo Partnership B.V. (Rabobank; not rated), one of the bank's shareholders, contributes its expertise in the agribusiness sector and good corporate governance practices.	Weakened asset quality metrics amid loan portfolio cleanup.
	Weakened internal capital generation amid higher provisioning.

**Banco Regional has been focusing on its business strategy to revamp profitability amid a challenging operating scenario.** Banco Regional is one of the largest financial entities in Paraguay, with a leading position in the agribusiness lending sector. However, in the past few years the bank's loan book has deteriorated, exacerbated by the challenging economic scenario in Paraguay. The difficult economic conditions stem from negative shocks such as the droughts in the 2018-2019 and 2021-2022 harvest seasons and the COVID-19 pandemic, which increased the risk perception in the financial system.

In this context, Banco Regional's credit provisioning has been higher than peers, considering its above-average exposure to the agriculture sector, indicating higher risk and a lack of enough provision coverage in its legacy portfolio. In parallel to that, the bank went through a transformation process to strengthen its credit risk management that included the cleanup of problematic loans. Although we recognize both the need for and importance of such a cleanup, the combination of factors has weakened the bank's profitability and capitalization. This has limited its growth capacity

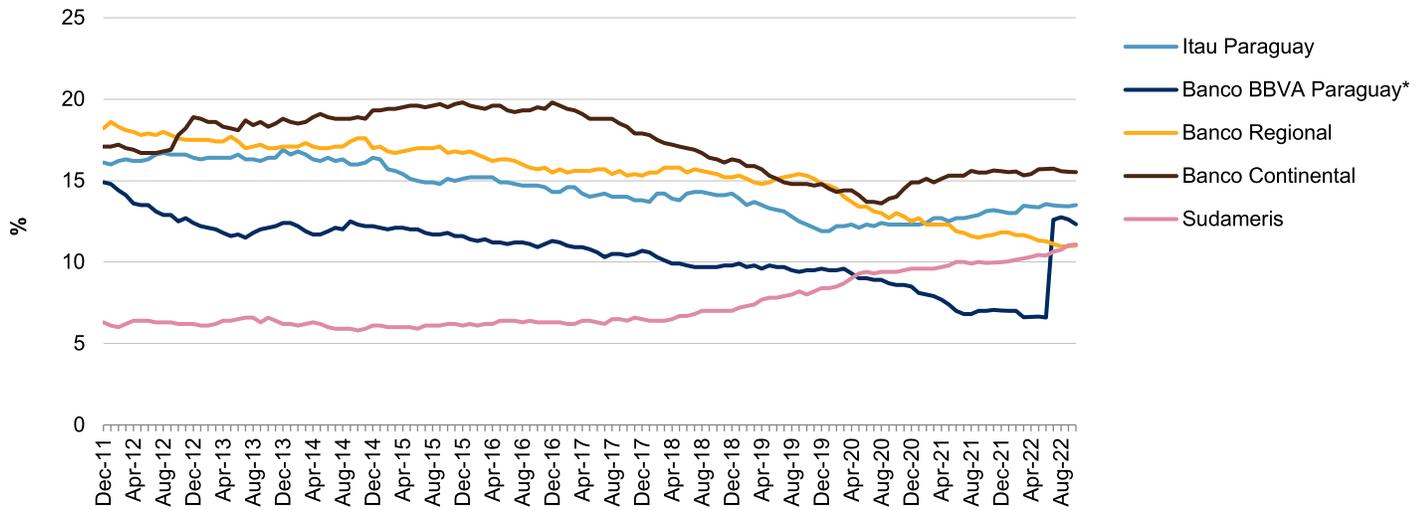
and hurt its overall business performance.

Amid this situation, Banco Regional has been focusing on its business strategy to revamp profitability, which involves restoring profitability by diversifying its loan portfolio, increasing its presence in the retail segment, and accelerating its digital transformation, while keeping its leading position in the agriculture loan business. To execute this strategy, the bank had been working to incorporate a new strategic partner. In this respect, in November 2022, Sudameris Bank S.A.E.C.A. (not rated) and Banco Regional announced their agreement to merge, which could result in Paraguay's largest lender in terms of loans and one of the top players in terms of deposits. Under the proposed structure, Sudameris will absorb Banco Regional. The closing of the merger is subject to regulatory approval. The announcement doesn't have immediate impact on credit fundamentals or the rating on Banco Regional, which continues to reflect its operations as a sole entity. We will continue monitoring the merger's progress in order to evaluate potential credit effect on Banco Regional.

**Chart 1**

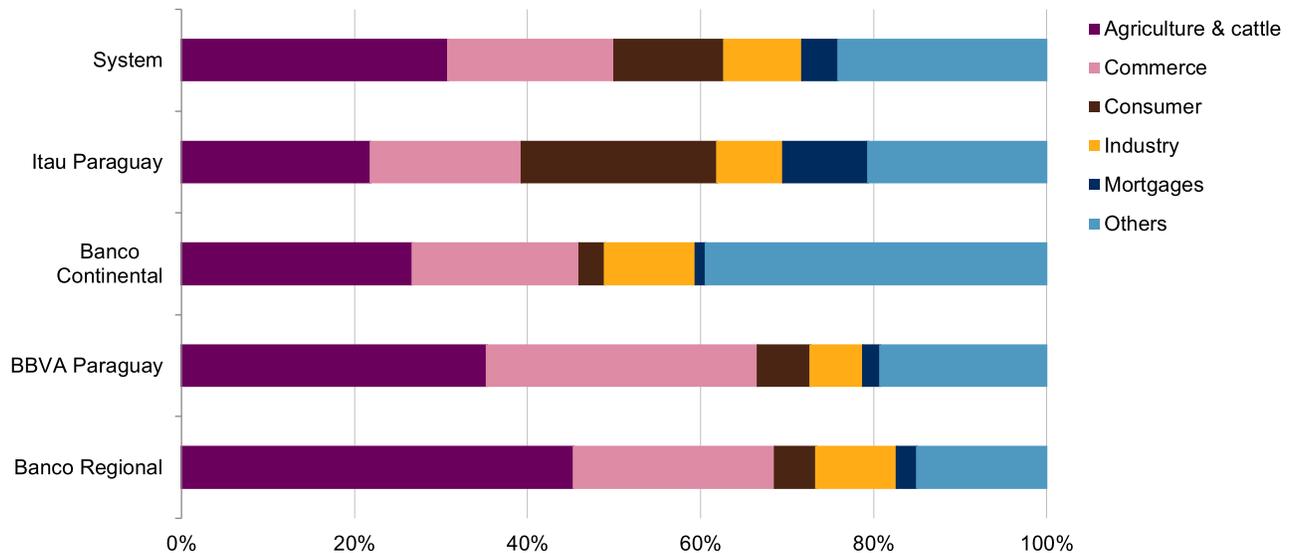
**Banco Regional Remains One Of The Leading Banks In Paraguay's Banking System**

Top five largest banks by loans



Source: BCP (Paraguayan Central Bank). \*Banco BBVA Paraguay: as of July 2022 onward, it includes Banco BBVA Paraguay and Banco GNB Paraguay S.A. combined data.

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**Chart 2****Banco Regional Is More Exposed To The Agriculture Sector Versus Peers**  
As of October 2022

Source: S&amp;P Global Ratings.

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*We forecast the bank to maintain a risk-adjusted capital (RAC) ratio of about 5% for the next 12-18 months.* However, Banco Regional's ability to grow is limited by its weak internal capital (due to heavy provisioning done via income statement and retained earnings in recent years), and the still weak profitability we expect for 2022. In addition, the bank's capital levels weakened amid the negative effect of the repurchase of preferred stocks last year (to which we give intermediate equity content and consider as part of the bank's equity).

We base our average projected RAC ratio of 5.0%-5.3% for the next two years on the following:

- Still subdued economic conditions in 2022 due to the drought in the country, but the economy recovering in 2023;
- Banco Regional's loan portfolio to remain flat in 2022 and to gradually resume growing in 2023 as the bank implements its new business strategy, although at low levels;
- Margins benefiting from higher base interest rate in the country following the monetary tightening cycle initiated in 2021;
- Credit loss provisioning to continue weighing on profitability and capital;
- No dividends payout on ordinary stocks in 2022 and 2023, while dividends on preferred stocks are capitalized in 2022 but paid in 2023;
- Extraordinary results from the sale of repossessed assets and specific portions of the loan portfolio as part of the bank's cleanup process;

- Return on equity (ROE) of about 3%-6% in the next two years, higher than in 2021 but below historical levels; and
- No capital injections.

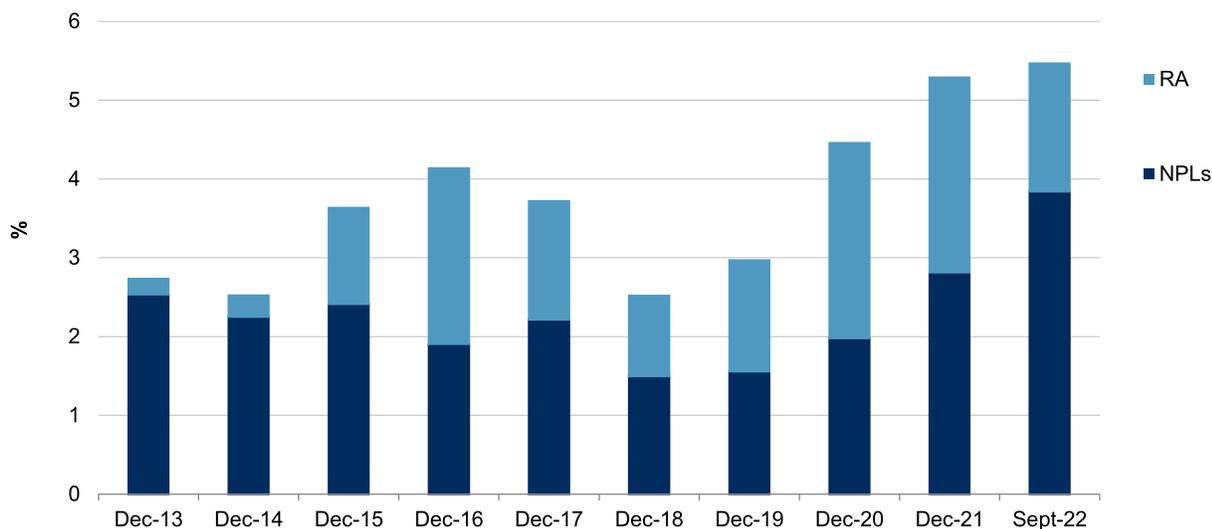
Our above assumptions for Banco Regional's capitalization don't consider the implications of the potential merger with Sudameris.

**Asset quality metrics pressured amid a more conservative risk approach and the cleanup of the loan portfolio.** As mentioned above, Banco Regional has undergone a business shift to enhance credit risk management, including cleaning up its loan portfolio (reducing the use of refinancing policies on its agriculture loans that increased nonperforming loans [NPLs]) and its repossessed assets. As a result, the bank's asset quality metrics have worsened beyond the industry average, with 60-days past due loans reaching 4.2% in October 2022 from 1.5% in December 2019, while charge-offs were 1.9% in September 2022 from 1.0% in December 2019. We expect nonperforming assets (NPAs) to remain high at the end of 2022 and in 2023, but to gradually decline as the bank resumes credit portfolio growth and as the repositioning of foreclosed assets declines as the loan portfolio cleanup ends.

**Chart 3**

**Banco Regional's Asset Quality Worsened Amid Its More Conservative Risk Approach**

60-days past-due loans (NPLs) + repossessed assets (RA)



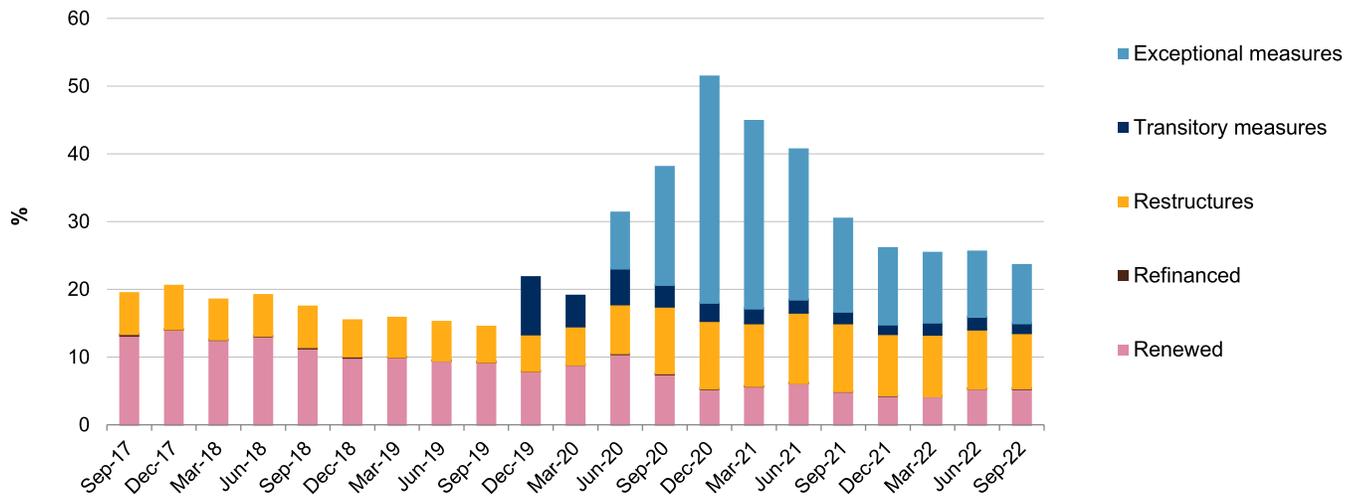
Source: S&P Global Ratings.

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Chart 4

**More Conservative Risk Approach Led To Higher Loan Restructuring As Central Bank Support Gradually Receded**

Renewed, refinanced or restructured\* (RRR) loans, plus central bank temporary measures



Source: S&P Global Ratings. Renewed: renewed loans, which are not overdue. Refinanced: Past-due loans that have their maturities extended (with same loan conditions). Restructured: Past-due loans with maturities are extended together with changes in interest and principal term conditions.

**Stable deposit base with prudent liquidity management.** Banco Regional's funding structure remains stable and benefits from a healthy deposit base, in line with that of the banking system. As of September 2022, 75% of its funding base relied on a stable customer deposit base, and the rest is made of loans from foreign and local financial institutions (21%) and local market senior and subordinated debt (4%). Its stable funding ratio (SFR) was 113% in September 2022, compared to 117% in December 2021, while its top 20 depositors represented 22.2% of total deposits as of September 2022 (17.7% in September 2021). Its top depositor accounted for 10.9% of total deposits as of the same date (6.0% in 2021). Liquidity management remains prudent, with a liquidity position that can comfortably meet short-term obligations. The bank's broad liquid assets to short-term wholesale funding ratio was 2.1x as of September 2022.

**The rating doesn't include notches of external support, but includes ongoing support from its minority shareholder, Rabobank, via gains in governance and agriculture expertise.** The 'BB-' issuer credit rating on the bank reflects its 'bb-' stand-alone credit profile (SACP) because the latter doesn't incorporate any external support from the government or the group. Banco Regional is owned by local investors that each have a minority stake.

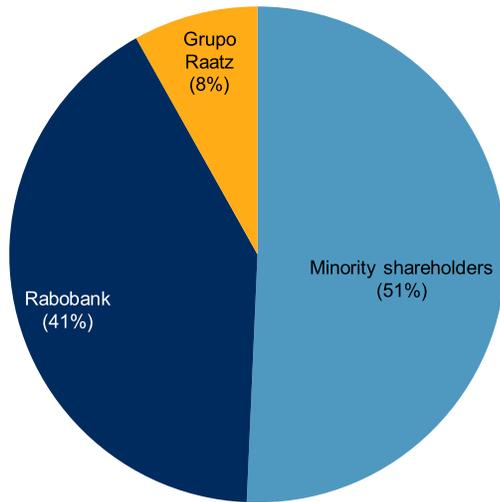
We don't incorporate any extraordinary support from Rabobank because it only owns a minority stake (38.40% of voting rights and 41.17% of total shares) in the bank. However, we think Banco Regional benefits from the shareholder's experience in agriculture segment and consider that the shareholder has strengthened the bank's

governance due to good corporate governance practices and ongoing supervision of credit risk.

**Chart 5**

**Rabobank Remains Relevant Minority Shareholder**

As of September 2022



Source: Company data.

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## Outlook

The stable outlook on Banco Regional for the next 12-18 months reflects our view the bank will continue cleaning up the problematic loans in its portfolio, while the focus on its business strategy could lead to recovering profitability and internal capital generation capacity, allowing for credit growth.

Our outlook also reflects Banco Regional's operations as a sole entity, and so doesn't currently incorporate the potential merger with Sudameris, in which Banco Regional would be absorbed by Sudameris.

### Downside scenario

We could downgrade Banco Regional if it undergoes significant financial losses that further hamper either its capital, asset quality, or its overall business performance and competitive position in the system.

### Upside scenario

We think the scenario for an upgrade is limited at this stage considering the bank as a sole entity.

## Environmental, Social And Governance

### ESG Credit Indicators

E-1	E-2	<b>E-3</b>	E-4	E-5	S-1	<b>S-2</b>	S-3	S-4	S-5	G-1	<b>G-2</b>	G-3	G-4	G-5
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ESG credit indicators provide additional disclosure and transparency at the entity level and reflect S&P Global Ratings' opinion of the influence that environmental, social, and governance factors have on our credit rating analysis. They are not a sustainability rating or an S&P Global Ratings ESG Evaluation. The extent of the influence of these factors is reflected on an alphanumerical 1-5 scale where 1 = positive, 2 = neutral, 3 = moderately negative, 4 = negative, and 5 = very negative. For more information, see our commentary "ESG Credit Indicators: Definition And Applications," published Oct. 13, 2021.

Environmental factors are a moderately negative consideration in our credit rating analysis of Banco Regional. We believe it, along with other banks operating in Paraguay, are exposed to climate risk due to their significant exposure to the agriculture and livestock sectors (about 31% of total loans), which expose the banking system to the cyclicity of the agriculture and weather events (including droughts and floods). Banco Regional primarily lends to the agriculture segment and has a higher exposure to this industry than the system average, but we view its climate risks in line with those of the industry.

## Key Statistics

**Table 1**

<b>Banco Regional S.A.E.C.A.--Key Figures</b>					
	<b>--Year-ended Dec. 31--</b>				
<b>(Mil. PYG)</b>	<b>2022*</b>	<b>2021</b>	<b>2020</b>	<b>2019</b>	<b>2018</b>
Adjusted assets	17,773,923.3	17,534,004.1	17,309,143.9	16,950,191.9	17,434,103.3
Customer loans (gross)	12,617,392.9	12,517,590.9	12,293,433.8	13,421,802.0	12,496,187.7
Adjusted common equity	1,219,783.3	1,192,688.7	1,249,345.2	1,061,199.8	1,378,762.9
Operating revenues	572,189.7	623,132.5	670,646.9	794,299.1	747,514.0
Noninterest expenses	317,581.2	400,062.0	382,952.6	388,515.1	421,548.7
Core earnings	3,823.8	32,311.5	59,661.2	131,704.5	95,789.4

\*Data as of Sept. 30. PYG--Paraguayan guarani

**Table 2**

<b>Banco Regional S.A.E.C.A.--Business Position</b>					
	<b>--Year-ended Dec. 31--</b>				
<b>(%)</b>	<b>2022*</b>	<b>2021</b>	<b>2020</b>	<b>2019</b>	<b>2018</b>
Loan market share in country of domicile	11.0	11.8	12.5	14.8	15.2
Deposit market share in country of domicile	9.7	9.7	9.7	11.2	12.1
Return on average common equity	3.6	0.3	4.8	8.1	7.2

\*Data as of Sept. 30.

**Table 3**

<b>Banco Regional S.A.E.C.A.--Capital And Earnings</b>					
	<b>--Year-ended Dec. 31--</b>				
<b>(%)</b>	<b>2022*</b>	<b>2021</b>	<b>2020</b>	<b>2019</b>	<b>2018</b>
Tier 1 capital ratio	13.5	12.8	16.3	12.7	13.6
S&P Global Ratings' RAC ratio before diversification	N/A	5.1	N/A	N/A	N/A
S&P Global Ratings' RAC ratio after diversification	N/A	3.2	N/A	N/A	N/A
Adjusted common equity/total adjusted capital	86.9	86.9	83.3	80.9	84.7
Net interest income/operating revenues	71.1	75.2	78.8	80.4	79.1
Fee income/operating revenues	15.8	16.6	15.9	15.0	15.9
Market-sensitive income/operating revenues	4.7	5.8	4.9	3.8	3.2
Cost to income ratio	55.5	64.2	57.1	48.9	56.4
Provision operating income/average assets	1.9	1.3	1.6	2.3	2.0
Core earnings/average managed assets	0.0	0.2	0.3	0.8	0.6

\*Data as of Sept. 30. N/A--Not applicable.

**Table 4**

<b>Banco Regional S.A.E.C.A.--Risk Position</b>					
	<b>--Year-ended Dec. 31--</b>				
<b>(%)</b>	<b>2022*</b>	<b>2021</b>	<b>2020</b>	<b>2019</b>	<b>2018</b>
Growth in customer loans	1.1	1.8	(8.4)	7.4	15.1
Total diversification adjustment/S&P Global Ratings' RWA before diversification	N/A	57.1	N/A	N/A	60.5
Total managed assets/adjusted common equity (x)	14.7	14.8	14.1	16.3	12.7

**Table 4**

<b>Banco Regional S.A.E.C.A.--Risk Position (cont.)</b>					
	<b>--Year-ended Dec. 31--</b>				
<b>(%)</b>	<b>2022*</b>	<b>2021</b>	<b>2020</b>	<b>2019</b>	<b>2018</b>
New loan loss provisions/average customer loans	2.6	1.5	1.7	1.7	1.5
Net charge-offs/average customer loans	1.9	1.4	0.9	1.0	1.6
Gross nonperforming assets/customer loans + other real estate owned	5.5	5.3	4.5	3.0	2.5
Loan loss reserves/gross nonperforming assets	77.6	85.6	114.5	178.3	86.8

\*Data as of Sept. 30. N/A--Not applicable.

**Table 5**

<b>Banco Regional S.A.E.C.A.--Funding And Liquidity</b>					
	<b>--Year-ended Dec. 31--</b>				
<b>(%)</b>	<b>2022*</b>	<b>2021</b>	<b>2020</b>	<b>2019</b>	<b>2018</b>
Core deposits/funding base	70.7	73.9	69.7	67.6	64.8
Customer loans (net)/customer deposits	106.3	102.2	107.8	122.5	121.7
Long-term funding ratio	89.2	92.7	96.6	95.8	95.7
Stable funding ratio	113.7	117.2	126.3	114.1	123.1
Short-term wholesale funding/funding base	11.8	8.0	3.7	4.6	4.7
Broad liquid assets/short-term wholesale funding (x)	2.1	3.1	7.4	4.2	5.6
Broad liquid assets/total assets	22.5	22.1	24.3	17.1	23.5
Broad liquid assets/customer deposits	35.4	33.4	39.5	28.6	40.7
Net broad liquid assets/short-term customer deposits	24.8	29.8	44.2	30.5	41.8
Short-term wholesale funding/total wholesale funding	38.7	29.4	11.6	13.4	12.8

\*Data as of Sept. 30.

**Banco Regional--Rating Component Scores**

<b>Issuer Credit Rating</b>	<b>BB-/Stable/--</b>
SACP	bb-
Anchor	bb-
Business position	Strong
Capital and earnings	Moderate
Risk position	Moderate
Funding	Adequate
Liquidity	Adequate
Comparable ratings analysis	0
Support	0
ALAC support	0
GRE support	0
Group support	0
Sovereign support	0
Additional factors	0

ALAC--Additional loss-absorbing capacity. GRE--Government-related entity. SACP--Stand-alone credit profile.

## Related Criteria

- General Criteria: Hybrid Capital: Methodology And Assumptions, March 2, 2022
- Criteria | Financial Institutions | General: Financial Institutions Rating Methodology, Dec. 9, 2021
- Criteria | Financial Institutions | Banks: Banking Industry Country Risk Assessment Methodology And Assumptions, Dec. 9, 2021
- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- Criteria | Financial Institutions | General: Risk-Adjusted Capital Framework Methodology, July 20, 2017
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

## Related Research

- Bulletin: Proposed Merger Of Banco Regional And Sudameris Bank Could Create Paraguay's Largest Lender, Nov. 29, 2022
- Banking Industry Country Risk Assessment: Paraguay, Oct. 26, 2022
- Research Update: Banco Regional Downgraded To 'BB-' From 'BB' Amid Higher Provisions Arising From Its Legacy Portfolio; Outlook Stable, Sept. 30, 2022

### Ratings Detail (As Of December 12, 2022)\*

#### **Banco Regional S.A.E.C.A.**

Issuer Credit Rating BB-/Stable/--

#### **Issuer Credit Ratings History**

30-Sep-2022 BB-/Stable/--

25-Oct-2021 BB/Negative/--

09-Apr-2018 BB/Stable/--

#### **Sovereign Rating**

Paraguay BB/Stable/B

\*Unless otherwise noted, all ratings in this report are global scale ratings. S&P Global Ratings' credit ratings on the global scale are comparable across countries. S&P Global Ratings' credit ratings on a national scale are relative to obligors or obligations within that specific country. Issue and debt ratings could include debt guaranteed by another entity, and rated debt that an entity guarantees.

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