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Ratings

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Banco Regional S.A.E.C.A.

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Banco Regional S.A.E.C.A.

SACP	bb

+

Support	0

+

Additional Factors	0

Anchor	bb-	
Business Position	Strong	+1
Capital and Earnings	Moderate	0
Risk Position	Adequate	0
Funding	Average	0
Liquidity	Adequate	

ALAC Support	0
GRE Support	0
Group Support	0
Sovereign Support	0

Issuer Credit Rating
BB/Stable/--

Major Rating Factors

Strengths:	Weaknesses:
• Rabo Partnership B.V. (Rabobank; not rated), one of the bank's shareholders, contributes expertise in the agribusiness sector and good corporate governance practices. • Adequate risk management, with better-than-system average asset quality metrics.	• Higher-than-average loan portfolio concentration in the agribusiness sector that's exposed the bank to economic cycles. • High degree of dollarization in the banking system. • Weak public institutions and structural challenges that continue to hamper effective policymaking in the country.

Outlook: Stable

The stable outlook on Banco Regional for the next 12 months reflects our expectation that the bank will keep its sound competitive position in the Paraguayan financial system and a leading position in the agribusiness sector. We also expect that the bank will have manageable asset quality metrics, although they could slightly worsen until the economy starts to recover after weaker economic activity in the country during 2019.

Downside scenario

We could lower the ratings on the bank in the next 12 months if Banco Regional's capitalization metrics further decline, with our risk-adjusted capital (RAC) ratio declining to consistently below 5%, which could happen if the bank's assets grow above its internal capital generation.

Upside scenario

Ratings upsides are limited at this point, and would depend on us upgrading the sovereign and revising the Banking Industry Country Risk Assessment (BICRA) score for Paraguay to a stronger category while all other credit factors of the bank remain stable.

Rationale

The ratings on Banco Regional reflect its sound competitive position as one of the largest financial entities in Paraguay, with a leading position in the agribusiness lending segment (including agriculture and cattle), and the benefits it gains from the expertise in the agribusiness sector and good corporate governance practices introduced by its shareholder, Rabobank (with a 39% minority interest). In 2019, Banco Regional's capital levels declined after it acquired an insurance company and launched a new broker house. Nonetheless, we expect the bank to maintain capitalization metrics in the upcoming months at 2019 levels, with a projected RAC ratio of 5.6% for the next 12-18 months.

Additionally, the ratings reflect the bank's adequate risk management with better-than-system-average asset quality metrics due to more conservative underwriting standards and active management of the bank's repossessed assets. This helps the bank mitigate the higher exposure to agriculture segment, which is a more cyclical segment. The ratings also incorporate Banco Regional's funding structure which remains stable and benefits from a healthy deposit base, in line with that of the banking system. We also factor in its liquidity position that provides adequate cushion to meet short-term obligations.

Anchor: 'bb-' for banks operating only in Paraguay

Our bank criteria use our BICRA economic risk and industry risk scores to determine a bank's anchor, the starting point in assigning an issuer credit rating. The anchor for banks operating only in Paraguay, where Banco Regional operates, is 'bb-'.

We view economic risks in Paraguay to be higher than the global average. In recent years, Paraguay has remained resilient to the region's economic struggles, growing somewhat above peers. However, economic growth came to a halt in 2019, following adverse climate conditions, subdued economic growth in main trading partners, and political uncertainty, which highlight the still highly volatile and concentrated economic base. We expect the country to somewhat regain GDP growth in 2020, increasing about 3.3% in real terms, but still below Paraguay's historical 4%-5% growth. Additionally, Paraguay's still evolving political institutions continue to face challenges.

Following a weaker economic performance in 2019, credit expansion slowed to 9% (year-on-year on a nominal basis) as of November 2019, affected by the 9% increase of the PYG to US$ exchange rate. Additionally, given the softer economic conditions this year, we expect weaker asset quality in the system (with higher 60-days nonperforming loans [NPLs] as well as higher stock of repossessed assets) but for them to remain manageable. The country continues to have low GDP per capita; about $5,600. Furthermore, the banking system has high credit risk given its considerable exposure to foreign currency loans and to cyclical sectors such as agriculture and cattle.

The banking sector's industry risk reflects our view of Paraguay's regulatory framework that, although improving, is still behind international standards. We believe the government does not have a record of effective support to the banking sector. Furthermore, we consider that the presence of relatively large cooperatives (credit unions) and unregulated finance companies introduce market distortions. In late 2019, the central bank (BCP for its Spanish acronym) introduced new regulation for unregulated finance companies, which starting in July 2020 will have to be registered with the central bank in order to continue operating. We view this initiative as positive because it could improve the system's supervision and transparency. The banking system continues to rely mostly on deposits for funding both in local and foreign currency. Dollarization remains high because of the economy's exposure to dollar-generator sectors.

Table 1

Banco Regional S.A.E.C.A. Key Figures					
		--Year-ended Dec. 31--			
(Mil. PYG)	**2019***	**2018**	**2017**	**2016**	**2015**
Adjusted assets	17,770,332.3	17,434,103.3	14,627,122.4	15,026,145.6	15,297,794.6
Customer loans (gross)	13,480,442.3	12,496,187.7	10,853,708.7	10,523,728.0	11,366,320.5
Adjusted common equity	1,443,154.4	1,378,762.9	1,318,199.9	1,198,523.6	1,000,698.7
Operating revenues	589,453.2	747,514.0	776,009.4	847,631.3	795,033.3
Noninterest expenses	292,564.8	421,548.7	400,123.8	392,681.6	384,352.6
Core earnings	135,718.6	95,789.4	144,869.9	194,725.0	175,149.5

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

Business position: Sound competitive position as one of the largest financial entities in Paraguay

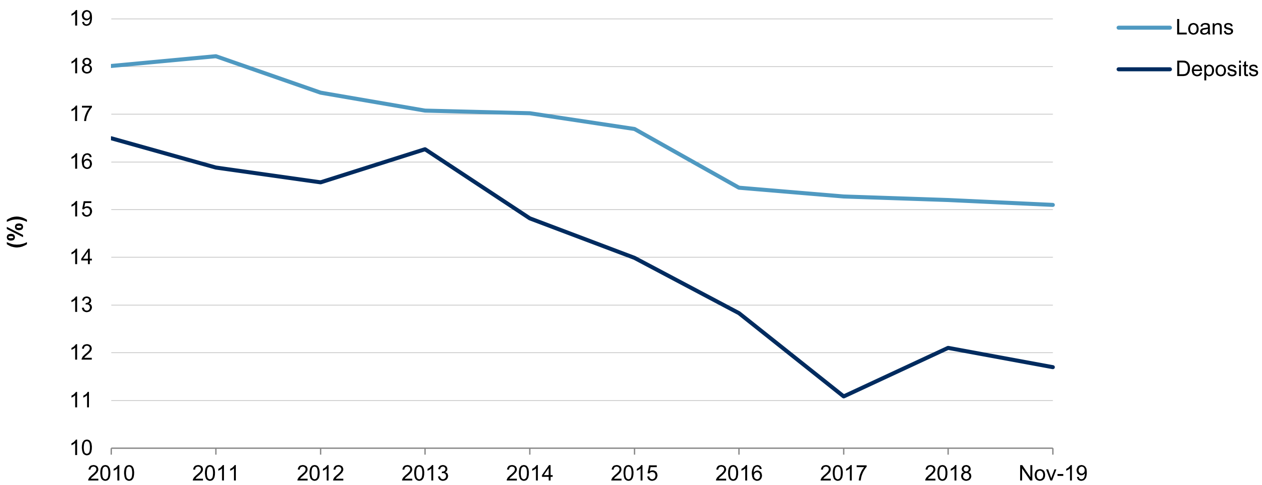
We view Banco Regional's business position as a credit strength given the bank's sound competitive position in the Paraguayan financial system. It's one of the largest financial entities in the country, with a leading position in the agribusiness lending sector and longstanding customer relationships, all of which confer significant business stability.

As of November 2019, Banco Regional was the largest lender in terms of loans and the third largest in terms of deposits, with a market share of 15.1% and 11.7%, respectively. In addition, it maintained its leading position in loans to the agriculture sector, with a market share of 24%. Banco Regional offers a wide array of products through 37 branches, 89 ATMs, and 52 auto service terminals throughout Paraguay.

In line with its diversification strategy, in the first months of 2019, Banco Regional acquired an insurance company, Regional Seguros S.A. (not rated), and created a new broker house, Regional Casa de Bolsa S.A. (not rated). In the next few years, both companies will enable Banco Regional to develop new businesses and expand, as well as modernize its offerings of financial products, which should help to diversify and provide greater stability to the bank's revenues as they grow.

Chart 1

Market Share Evolution



Source: BCP (Paraguayan Central Bank).

Table 2

Loan Market Share As Of November 2019

Bank	%
Banco Regional	15.14
Banco Continental	14.73
Banco Itau Paraguay	12.09
BBVA Paraguay	9.53
Sudameris Bank	8.25
Banco Nacional de Fomento	6.52
Banco GNB Paraguay	6.40
Vision Banco	5.79
Banco BASA	5.08
Banco Atlas	4.71

Table 3

Deposit Market Share As Of November 2019

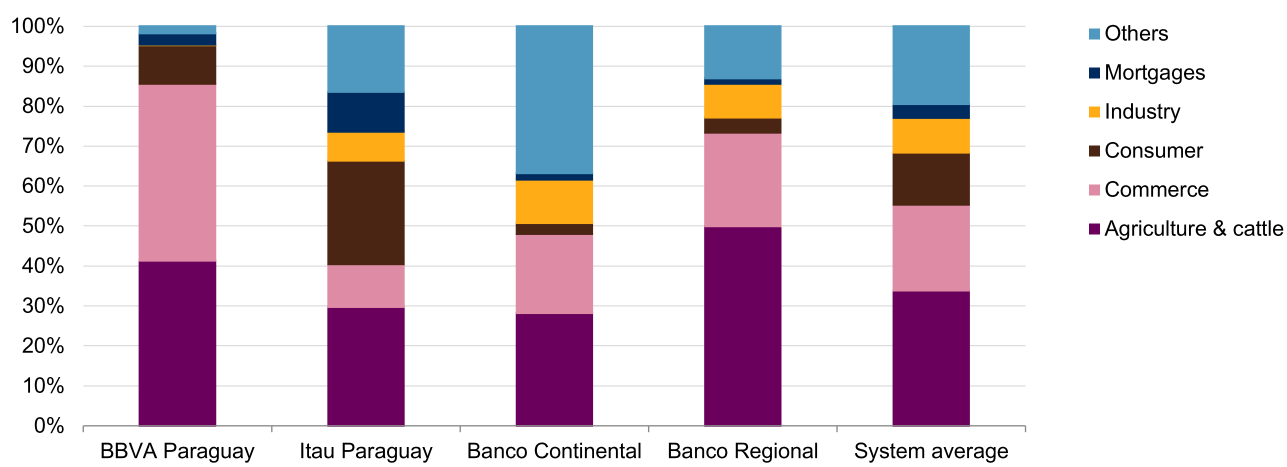
Bank	%
Banco Itau Paraguay	15.41
Banco Continental	13.72
Banco Regional	11.70
BBVA Paraguay	10.04
Banco Nacional de Fomento	8.18
Banco GNB Paraguay	6.87
Sudameris Bank	6.57
Vision Banco	5.85
Banco Atlas	4.78
Banco BASA	4.67

The bank focuses on lending to the corporate and small- and mid-size enterprise (SME) segments, which accounted for 95% of its total loans as of September 2019, with special focus on the agribusiness sector, which represents 50% of the bank's total portfolio. Consumer loans accounted for 6% of the bank's total loans.

For the next 12-18 months, we expect Banco Regional to maintain its competitive position, with the agribusiness-lending unit accounting for the largest share of the loan portfolio, but gradually increasing its diversification in other segments. The bank will continue to focus on enhancing cross-selling in the retail and SME segments, and on improving efficiency by encouraging the use of its self-service technology platform and automated channels, with strict control of administrative expenses.

Chart 2

Loan Portfolio Distribution for Paraguay's Largest Banks
As of November 2019



Source: S&P Global Ratings.

Table 4

Banco Regional S.A.E.C.A. Business Position

		--Year-ended Dec. 31--			
(%)	**2019***	**2018**	**2017**	**2016**	**2015**
Loan market share in country of domicile	15.4	15.2	15.3	15.5	16.7
Deposit market share in country of domicile	11.6	12.1	11.1	12.8	14.0
Return on average common equity	11.2	7.2	13.8	17.7	18.5

*Data as of Sept. 30.

Capital and earnings: RAC ratio of about 5.6% for the next 12-18 months

We view Banco Regional's capitalization as moderate based on our average forecasted RAC ratio of 5.6% during the next 12-18 months. Banco Regional's capitalization metrics declined in 2019 after it acquired Regional Seguros and launched its new broker house. These companies' investments are deducted from the bank's total equity for both the regulatory capital and our calculation of the RAC ratio.

Our RAC ratio forecast considers our base-case scenario assumptions, which include:

- Flat GDP growth in 2019 and a gradual recovery of 3% in 2020.
- Loan portfolio growth of 9% in 2019 and 6%-8% in 2020, in line with the banking system's growth pace and affected by exchange rate depreciation.
- Return on average common equity of 10.5% in 2019 and 14.0% in 2020.
- Efficiency metrics (measured as non-interest expenses to operating revenue) below 50% in 2019-2020, given the bank's efforts to control administrative expenses.
- Dividend payment of about 30% of 2019 results on ordinary stocks, and a PYG30.0 billion dividend payment for preferred stocks from 2019-2023.
- Deteriorating asset quality metrics (NPLs plus repossessed assets) for 2019 mainly due to adverse economic conditions in the country despite the bank's focus on asset quality. In the long term, the bank aims to have NPLs close to 1%, fully covered by loan loss provisions; cost of risk at around 1x; and net charge-offs to average about 1% of customer loans.

Our RAC ratio compares our definition of total adjusted capital (TAC) to our risk-weighted assets (RWAs). We apply our risk-adjusted capital framework (RACF) to banks consistently across the globe, and it's independent of national regulations and banks' internal risk measurements. Our RACF is intended to adjust the banks' capital and the value of assets and exposures to reflect degrees of risk in a more consistent fashion than are reflected in regulatory ratios. These adjustments can result in significant differences between our capital ratios and the regulatory ones. For example, in Paraguay, we have RWA for market and operating risk and apply a higher risk weight to the majority of the credit risk exposures. We deduct goodwill and, in the case of Banco Regional, exclude Tier 2 subordinated hybrid capital, because of their residual maturity. Our RAC ratio calculations do include preferred stocks as part of the bank's capital, to which we assign intermediate equity content.

As of September 2019, Banco Regional had a total regulatory capital of 14.2% and a Tier 1 regulatory capital of 12.9% compared to the 12% and 8% minimum regulatory requirements, respectively. However, Paraguay capital definitions are under Basel I international standards, which we view as more lax than Basel III.

Congress approved a new banking law at the end of 2016 that moves towards Basel II. The law includes changes to weights and the regulatory capital composition, with potential increases in capital per year of no more than 100 basis points. However, the law hasn't yet been fully implemented and we don't expect it to be in the short term. We will monitor how the implementation of this new law evolves and the implications it could have for Banco Regional's capitalization metrics.

In 2019, Banco Regional's earnings were hurt by higher provisioning in the last quarter amid an economic slump in the country that offset the bank's improved operating results from higher net interest margins and tight control of administrative expenses. These expenses declined 3% in 2019 from the extraordinary high expenses in 2018. We expect profitability to improve in 2020 as the origination of new loan loss provisions declines once the economy recovers.

Table 5

Banco Regional S.A.E.C.A. Capital And Earnings

		--Year-ended Dec. 31--			
(%)	**2019***	**2018**	**2017**	**2016**	**2015**
Tier 1 capital ratio	12.9	13.6	14.6	13.8	11.0
Adjusted common equity/total adjusted capital	85.2	84.7	84.1	82.7	80.0
Net interest income/operating revenues	79.9	79.1	81.5	82.0	81.6
Fee income/operating revenues	14.8	15.9	14.5	13.4	13.6
Market-sensitive income/operating revenues	3.9	3.2	3.4	4.0	4.5
Noninterest expenses/operating revenues	49.6	56.4	51.6	46.3	48.3
Preprovision operating income/average assets	2.2	2.0	2.5	3.0	2.8
Core earnings/average managed assets	1.0	0.6	1.0	1.3	1.2

*Data as of Sept. 30.

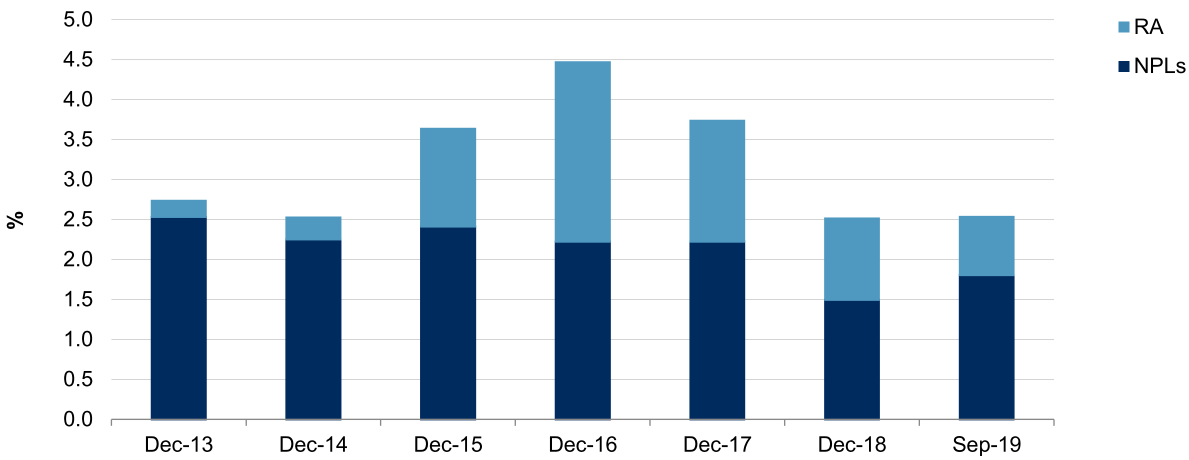
Risk position: Healthy asset quality metrics despite soft performance of the economy

Despite a feeble economic performance in the country over the year, Banco Regional was able to maintain asset quality metrics better than the industry average. The bank's nonperforming assets (NPAs) over total loans (including NPLs and repossessed assets) was 2.6% as of September 2019, in line with year-end 2018 and below the banking industry average of 4.4% as of September 2019. This is explained by Banco Regional's active management of its repossessed assets that mitigated the deterioration in the bank's NPLs (please refer to chart 3). Repossessed assets declined to 0.9% of total loans as of September 2019, down from its highest level of 2.2% in December 2016, with a reduction of 58% over that period (and a 22% decline over the first three quarters of 2019). On the other hand, NPLs (which exclude repossessed assets) increased to 1.8% of the total loan portfolio from 1.5% at the end of 2018, but still are better than the 2015-2016 figures.

Loan-loss reserve coverage accounted for 81% of NPAs as of September 2019, compared with 87% and 72% at the end of 2018 and 2017, respectively (coverage goes up to 114%, 146%, and 121%, respectively, when excluding repossessed assets). Additionally, net charge-offs to average customer loans reached 0.9% as of September 2019 (annualized) from 1.6% at the end of 2018.

Chart 3

Asset Quality Evolution



Nonperforming assets (NPAs) include nonperforming loans (NPLs) and repossessed assets (RA). Source: S&P Global Ratings.

The bank maintained its low complexity of operations and manageable single-name exposure concentrations, with the top 20 exposures representing about 21% of its total loan portfolio and 1.4x its equity as of September 2019. Banco Regional continues to focus on agribusiness lending, which represents about 43% of the bank's total loan portfolio, compared with the financial system's 30% average. As a result, the bank's exposure to dollarization is higher than the system average because this segment produces commodities priced in dollars. However, Banco Regional operates under a prudent policy for managing currency mismatches, and originates loans in dollars only for customers that are dollar generators.

For the next 12-18 months, we expect some deterioration in the bank's asset quality, in line with our expectations for the banking system, explained largely by the softer economic conditions in the country in 2019, but metrics should remain manageable with NPAs at about 2.8% and charge-offs of 1.5% at the end of 2019.

Table 6

Banco Regional's Dollarization Compared To System Average As Of November 2019

	Banco Regional		System	
	LC	**FC**	**LC**	**FC**
Total assets	43%	57%	55%	45%
Total loans	37%	63%	53%	47%
Total liabilities	36%	64%	51%	49%
Total deposits	43%	57%	55%	45%

LC--Local currency. FC--Foreign currency.

Table 7

Banco Regional S.A.E.C.A. Risk Position

		--Year-ended Dec. 31--			
(%)	**2019***	**2018**	**2017**	**2016**	**2015**
Growth in customer loans	10.5	15.1	3.1	(7.4)	20.8
Total diversification adjustment/S&P Global Ratings' RWA before diversification	N/A	60.5	63.0	59.3	N/A
Total managed assets/adjusted common equity (x)	12.3	12.7	11.1	12.5	15.3
New loan loss provisions/average customer loans	1.1	1.5	1.6	1.8	1.7
Net charge-offs/average customer loans	0.9	1.6	1.6	2.3	0.6
Gross nonperforming assets/customer loans + other real estate owned	2.6	2.5	3.7	4.1	3.6
Loan loss reserves/gross nonperforming assets	81.3	86.8	71.7	62.5	81.3

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

Funding and liquidity: Stable and diversified deposit base and prudent liquidity management

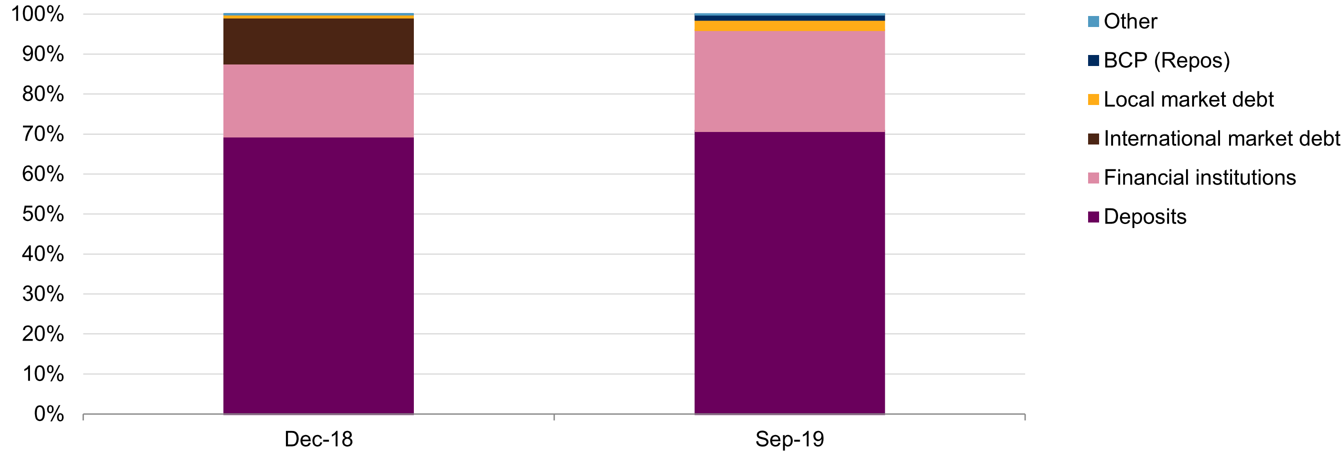
We believe that Banco Regional's funding has a similar structure to that of the industry. It relies on a stable customer deposit base, which represented 71% of funding as of September 2019. The remaining 29% is composed of senior unsecured notes (12% of total funding), loans from financial institutions (25%), repos (1%) and a small amount of local market senior and subordinated debt (2% and 1%, respectively).

The bank's stable funding ratio (SFR) was 107% as of September 2019 compared to 101% at the end of 2018, and is in line with those of the rated peers. We calculate the ratios as available stable funding (mainly composed of customer deposits [67%], loans from financial institutions and issuances with maturities greater than one year [22%], and equity [11%]) divided by stable funding needs (mainly customer loans). In 2019, the SFR improved to 2017 levels after declining in 2018 following the maturity of a $300 million international bond at the end of January 2019. The bank has replaced this funding mainly with lines from international multilateral/bank lines for approximately $320 million (with scattered maturities) and some local market issuances for a total of $45 million with maturities in 2024. This changed Banco Regional's funding mix, with a larger proportion of bank lines from both local and international institutions than in 2018, but our overall view of the funding profile hasn't changed--it still largely depends on deposits.

We expect deposits to continue to be the main funding source and for Banco Regional to maintain a larger proportion of local funding (from deposits, local bank lines, and local market issuances) in its total funding base.

Chart 4

Banco Regional's Funding Breakdown



Source: S&P Global Ratings.

Banco Regional has prudent liquidity management. Its liquidity position can comfortably meet short–term obligations, with a broad of liquid assets to short–term wholesale funding ratio of 1.6x as of September 2019 compared to 1.8x as of December 2018. As of the same date, Banco Regional's liquid instruments (mainly cash, money market instruments, and central bank securities) represented 32% of total deposits. Like other banks in the country, Banco Regional uses the central bank's securities as a primary instrument for liquidity management. For the next 12-18 months, we expect Banco Regional's liquidity to remain adequate given the manageable maturities of loans from multilateral banks.

Table 8

Banco Regional S.A.E.C.A. Funding And Liquidity					
		--Year-ended Dec. 31--			
(%)	**2019***	**2018**	**2017**	**2016**	**2015**
Core deposits/funding base	65.6	64.8	68.5	71.5	70.9
Customer loans (net)/customer deposits	127.6	121.7	120.8	107.7	112.9
Long-term funding ratio	88.2	80.1	86.7	93.4	93.0
Stable funding ratio	106.8	102.9	108.2	124.1	117.4
Short-term wholesale funding/funding base	13.1	22.0	14.9	7.3	7.7
Broad liquid assets/short-term wholesale funding (x)	1.6	1.2	1.6	4.0	3.2
Net broad liquid assets/short-term customer deposits	15.1	8.4	17.4	38.1	29.8
Short-term wholesale funding/total wholesale funding	36.4	59.8	44.7	24.1	24.8

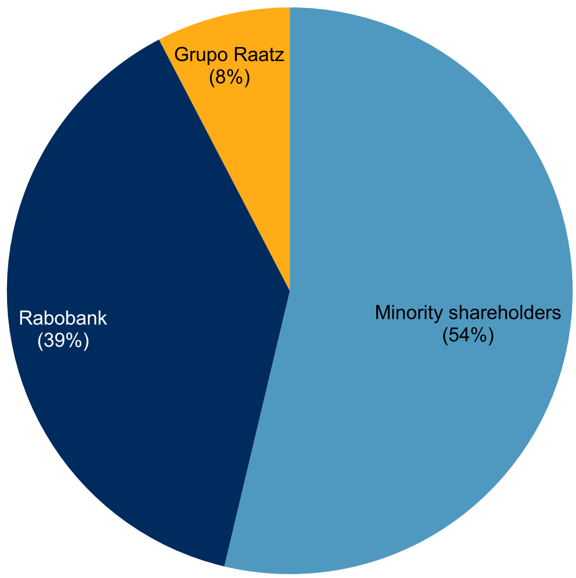
*Data as of Sept. 30.

Support: No notches of support from the government or group

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. Additionally, we do not incorporate any extraordinary support from Rabobank because it only owns a minority stake (38.63%) of the bank.

Chart 5

Banco Regional's Shareholders
As of September 2019



Source: Company data.

Related Criteria

- General Criteria: Group Rating Methodology, July 1, 2019
- Hybrid Capital: Methodology And Assumptions, July 1, 2019Criteria | Financial Institutions | General: Risk-Adjusted Capital Framework Methodology, July 20, 2017
- Criteria | Financial Institutions | Banks: Quantitative Metrics For Rating Banks Globally: Methodology And Assumptions, July 17, 2013
- Criteria | Financial Institutions | Banks: Banks: Rating Methodology And Assumptions, Nov. 9, 2011
- Criteria | Financial Institutions | Banks: Banking Industry Country Risk Assessment Methodology And Assumptions, Nov. 9, 2011
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009

Anchor Matrix

Industry Risk	Economic Risk									
	1	2	3	4	5	6	7	**8**	9	10
1	a	a	a-	bbb+	bbb+	bbb	-	-	-	-
2	a	a-	a-	bbb+	bbb	bbb	bbb-	-	-	-
3	a-	a-	bbb+	bbb+	bbb	bbb-	bbb-	bb+	-	-
4	bbb+	bbb+	bbb+	bbb	bbb	bbb-	bb+	bb	bb	-
5	bbb+	bbb	bbb	bbb	bbb-	bbb-	bb+	bb	bb-	b+
6	bbb	bbb	bbb-	bbb-	bbb-	bb+	bb	bb	bb-	b+
7	-	bbb-	bbb-	bb+	bb+	bb	bb	bb-	b+	b+
8	-	-	bb+	bb	bb	bb	bb-	**bb-**	b+	b
9	-	-	-	bb	bb-	bb-	b+	b+	b+	b
10	-	-	-	-	b+	b+	b+	b	b	b-

Ratings Detail (As Of January 24, 2020)*

Banco Regional S.A.E.C.A.	
Issuer Credit Rating	BB/Stable/--
Issuer Credit Ratings History	
09-Apr-2018	BB/Stable/--
08-Feb-2017	BB/Negative/--
26-Jun-2014	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.