

## Corporacion Financiera de Desarrollo S.A.

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# Corporacion Financiera de Desarrollo S.A.

<b>SACP</b>	<b>bb-</b>	+	<b>Support</b>	<b>+4</b>	+	<b>Additional Factors</b>	<b>0</b>
<b>Anchor</b>	<b>bbb-</b>		<b>ALAC Support</b>	<b>0</b>		<b>Issuer Credit Rating</b>  <b>BBB/Stable/A-2</b>	
<b>Business Position</b>	Moderate -1		<b>GRE Support</b>	<b>0</b>			
<b>Capital and Earnings</b>	Moderate -1		<b>Group Support</b>	<b>0</b>			
<b>Risk Position</b>	Moderate -1		<b>Sovereign Support</b>	<b>+4</b>			
<b>Funding</b>	Average 0						
<b>Liquidity</b>	Adequate 0						

## Credit Highlights

Key strengths	Key risks
Corporacion Financiera de Desarrollo S.A.'s (COFIDE's) role as the agent in promoting the Peruvian government's key objectives prompts the latter to support the bank if financial stress persists.	Credit exposure to remain concentrated by single-name and sector, which makes capital and asset quality metrics volatile.
Large role in the economy with lending and trust administration of government programs.	Still high equity exposure in its banking book impairs the bank's capitalization position.

*The long-term rating on COFIDE is four notches above its stand-alone credit profile (SACP) because there is a very high likelihood of extraordinary support from the Peruvian government.* We base our view of this support on COFIDE's very important role in meeting the government's key economic and social objectives and its very strong link with the government.

*COFIDE manages several government funds for economic recovery.* These include Reactiva Perú, Fondo Crecer, and the Fondo de Apoyo Empresarial program specifically to small and midsize enterprises (lending programs under the scope of Fondo de Apoyo Empresarial include FAE -MYPE, FAE- Turismo and FAE-Agro) that lead to higher fee income. In addition, the bank's 30% loan portfolio growth in 2020 was driven by loans guaranteed by the government under the FAE programs through financial institutions, which also implies the bank's lower use of capital. This year, we expect lower loan portfolio growth as the FAE portfolio begins to mature and following the slow recovery of the infrastructure sector.

*Strengthening capitalization.* In June 2021, the Ministry of Economy and Finance (MEF) partially executed the comfort letter, acquiring 14% of COFIDE's shares in Corporacion Andina de Fomento (CAF). This improved COFIDE's risk-adjusted capital (RAC) ratio because the exposure to equity in the banking book diminished. On the other hand, this sale allowed to COFIDE to build \$100 million of provisions, tempering its results.

*We forecast COFIDE's asset quality to worsen due to two punctual cases in its infrastructure lending.* However, we expect one of the cases to be resolved in the next 12 months, which will stabilize the bank's nonperforming loans (NPLs) at 10%-12%. The bank has kept sound reserve coverage--220% as of June 2021.

**Outlook: Stable**

The stable outlook on COFIDE in the next 24 months reflects our view that the bank will remain an important financing tool for the government to revive Peru's infrastructure sector and an important intermediary of loans to SMEs distributed through the banking system. Furthermore, we expect the bank will maintain its current capitalization levels, considering the sale of 14% of the bank's shares in CAF to the government, with high provisions and some volatility in asset quality metrics.

**Downside scenario**

We could lower the ratings in the next 24 months if asset quality metrics worsens beyond our expectations as COFIDE's credit exposure remains concentrated by customer and sector. Also, we could downgrade the bank if its RAC ratio drops consistently below 5% due to higher-than-expected provision requirements or credit risk growth. In addition, we could lower the rating if we did the same on the sovereign.

**Upside scenario**

An upgrade would require better prospects for the infrastructure sector and COFIDE's more diversified and less vulnerable credit risk exposure. In addition, we could upgrade the bank if it's able to consistently maintain a RAC ratio above 7%, which could be possible through capital injections from the government.

**Key Metrics****Corporacion Financiera de Desarrollo S.A.--Key Ratios And Forecasts**

	--Fiscal year ended Dec. 31 --				
(%)	2018a	2019a	2020a	2021f	2022f
Growth in customer loans	(15.5)	(12.4)	30.3	3.2-4.0	(12.0)-(15.0)
Growth in total assets	(7.1)	(6.0)	19.1	3.8-4.7	(4.1)-(5.1)
Net interest income/average earning assets (NIM)	1.0	0.8	1.4	0.1-0.2	0.2-0.3
Return on average common equity	0.9	1.3	1.0	0.8-1.0	0.7-1.0
Return on assets	0.1	0.2	0.2	0.1-0.3	0.1-0.3
Gross nonperforming assets/customer loans	6.3	7.7	9.6	10.5-14.5	10.5-12.5
Risk-adjusted capital ratio	5.9	5.8	5.8	6.3-6.7	6.3-6.7

All figures are S&P Global Ratings-adjusted. a--Actual. f--Forecast.

**Anchor: 'bbb-' For Banks Operating In Peru**

Our bank criteria use our Banking Industry Country Risk Assessment's (BICRA) economic 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 Peru is 'bbb-'.

Peru's economic risk reflects its low per capita GDP (about \$6,000) and relatively high exposure to cyclical sectors such as SMEs and microlending. We forecast GDP to grow 11% in 2021, mostly explained by a very large rebound

from the 11% GDP decline in 2020. Due to political instability, investors will likely remain more cautious, which will contribute to slower GDP growth in 2022 of 3.5%. We expect credit to expand at low single digits in the next two years and asset quality to weaken in 2021 due to the large informal economy and low income levels when loan moratoriums and support packages are lifted, and start recovering in 2022.

The industry risk for banks operating in Peru benefits from a solid regulatory framework, with ample supervisory coverage and periodic risk-based supervision under a highly professional regulator. Both the central bank and Superintendencia de Banca y Seguros (SBS)--which regulates banks and insurance companies--are very active. Moreover, Peru has implemented Basel III standards tailored for the domestic financial system. Peruvian banks have enjoyed strong profitability, although this has weakened during the pandemic, but we expect gradual recovery. We also believe the country's financial system has healthy capital metrics and a diversified funding mix with a significant share of deposits from loyal customers, as well as strong government support to provide liquidity if needed. We don't expect the recent law on interest rate caps to significantly affect banks' profitability, but additional measures like this could weaken the system's competitive dynamics.

### **Business Position: Weak Interest Collection Because Sovereign-Guaranteed SME Loans Drove Loan Growth, And High Delinquency Levels**

The bank has been an important arm of the government to manage and disburse the sovereign-guaranteed SME loans. The government's programs aim to provide liquidity in the market and diminish disruption across multiple sectors of the economy. COFIDE manages several government funds, which drives growth of its fee income, but it also has exposure to some lending programs such as FAEs through other financial institutions.

COFIDE's long-term financing of projects and lending to the infrastructure sector have constituted roughly more than three-quarters of its total loan exposure in the past few years. However, its participation diminished in 2020 and in the first half of 2021 because its loan portfolio growth last year was driven by sovereign-guaranteed SME loans, through financial institutions, which constituted almost 30% of the bank's portfolio. As of June 2021, COFIDE's loan book had contracted almost 4% after some government programs ended and almost flat infrastructure disbursements. Nevertheless, its infrastructure disbursements should outpace financial intermediation in the long term given Peru's considerable infrastructure needs and much larger loan amounts demanded in this business. We expect low loan portfolio growth over the next 24 months as the FAE loans begin to amortize and government programs come to an end, along with the slow recovery in the infrastructure sector.

We forecast low interest collection and increasing credit loss provisions will continue to hit the bank's profitability. The sale of COFIDE's shares in CAF had a neutral effect on the bank's results, because the gains from this transaction allowed it to create provisions for almost the same amount (about \$100 million). On the other hand, we expect higher fees income from the bank's administration of government trusts. For the next 12-24 months, we expect return on average assets (ROAA) to remain 0.1%-0.3%, with return on equity (ROE) of about 1%.

We also consider COFIDE to have weaker risk and financial management controls than those of its industry peers. The higher credit exposure to and concentration in complex corporate and legal structures could rapidly impair financial

and operating performance. Despite management's measures to address aggressive risk tolerances and poor internal controls with adjustments in committee and concentration policies and active management of troublesome credit exposures, we believe that the controlling ownership may still negatively influence strategic decisions made because of COFIDE's role to support infrastructure investments in the country. Funding to construct large assets might be under scrutiny from international sponsors that have relatively weaker balance sheets after the pandemic, which could disrupt the government's plan to attract private investors without increasing its stake in projects.

## **Capital And Earnings: Capitalization Propelled By Lower Market Risk Following Sale Of CAF Shares**

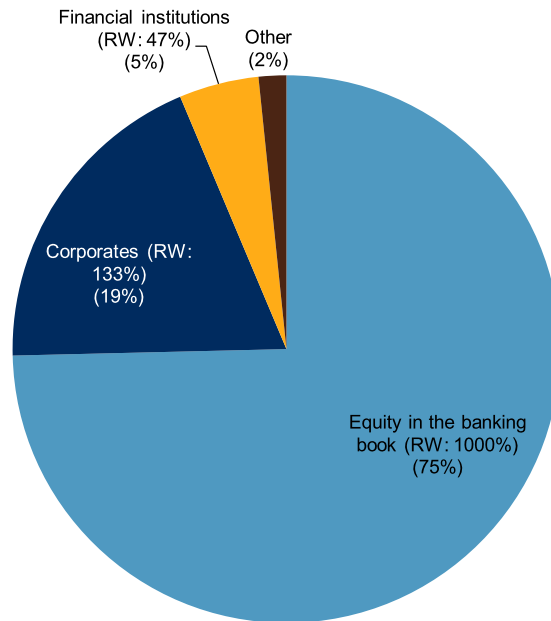
As of December 2020, COFIDE's RAC ratio was 5.8%, given that the 30% loan portfolio growth last year was driven by FAE loans, which the government guarantees, implying lower use of capital for COFIDE. We expect the bank will maintain its RAC ratio at an average of 6.5% over the next two years, considering the lower market risk following its sale of CAF shares to the MEF. In addition, we continue to believe that the government will provide capital in exchange for COFIDE's remaining shares in CAF to cover unexpected losses, which could boost capitalization metrics if the bank runs into financial difficulties.

Our base-case scenario assumes the following factors:

- Peru's GDP to grow 11% for 2021 and 3.5% for 2022.
- Loan portfolio to grow almost 4% in 2021, due to the government's support programs, and to contract about 15% in 2022, driven by the amortization of the government program and slow recovery in the infrastructure sector.
- Weak net interest margins below 0.5%, given the still high delinquency levels that impair loan payments and interest collection.
- Agreement with the MEF to sell 14% of COFIDE's CAF shares, which allowed it to constitute provisions for \$100 million in 2021.
- ROE between 0.8% and 1.0%.
- NPLs of about 11.0% in 2021 and 14.5% in 2022 due to punctual cases in the infrastructure portfolio. We also expect NPLs to remain comfortably covered by reserves.
- Market risk decreasing 12.4% in 2021 following the sale of the CAF shares, and then staying stable in 2022.
- Dividend payout of almost PEN2 million in 2021 and 2022.

**Chart 1**

**Breakdown Of S&P's RWA**  
As of December 2020



RWA--Risk-weighted assets. Source: S&P Global Ratings.  
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## Risk Position: Volatile Asset Quality Given The High Concentration In Infrastructure Projects

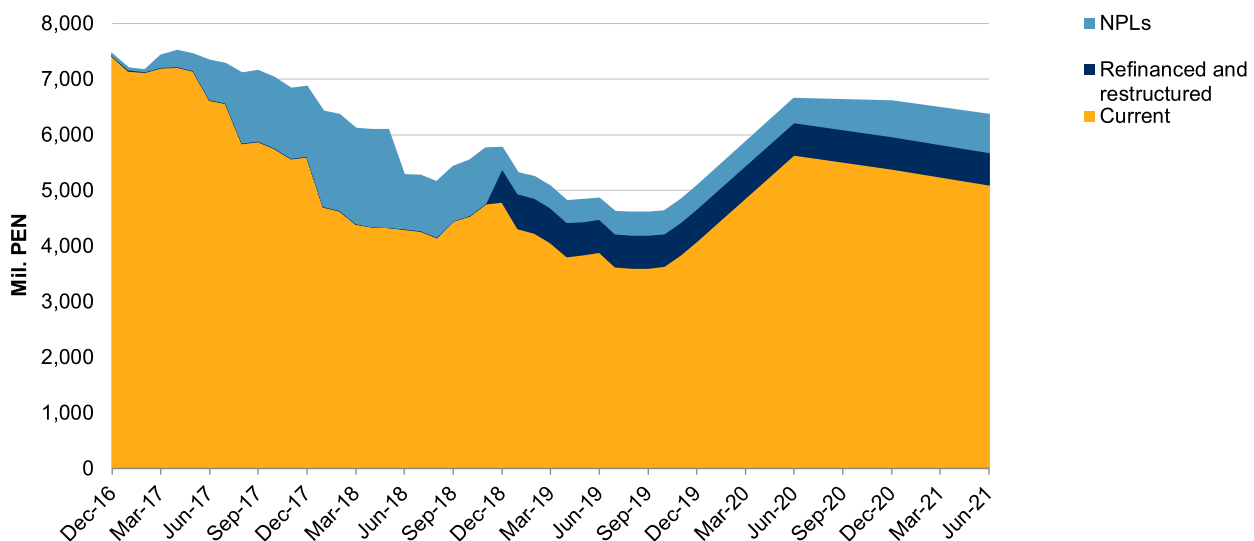
COFIDE ended the first half of this year with NPLs at 10.6% of its credit portfolio from 9.6% at the end of 2020 and 7.8% in 2019. The deterioration was driven by the past-due loan of a infrastructure project related to the energy sector for about \$60 million. COFIDE has already provisioned 60% of this loan, although it could be resolved in the next 12 months with COFIDE collecting the total amount of the loan. We also expect another project to become past due in the second half of the year, totaling about \$80 million with 90% already provisioned, further hurting the bank's metrics. The reserve coverage ratio was 220% against NPLs in June 2021. The bank's NPLs could end 2021 around 14.5% and then decrease to about 11% once COFIDE resolves the energy infrastructure case, with reserve coverage to NPLs surpassing 150%.

In addition, we still see challenges stemming from economic recovery and political instability. In our opinion, the uncertain recovery path of Peru's infrastructure, energy, transportation, and construction sectors could make asset quality metrics volatile. Loans under government programs constitute 22% of the bank's portfolio as of June 2021, so we expect the government guarantee to help buffer the bank's credit losses.

In line with its role to promote infrastructure in Peru, COFIDE usually finances more complex projects than the market is willing to invest in, which may carry construction risk and greater cash flow sensitivity. We deem the bank's concentration in infrastructure lending as high--the 20 largest loans account for 48% of total loans and 1.3x of common equity as of June 2021, which could potentially weaken the bank's capital base. Nonetheless, these risks are mitigated by our expectation that the government would provide capital in exchange for the bank's remaining shares in CAF. We still believe that our RAC ratio overestimates COFIDE's risks relative to those of its peers, supporting the bank's current risk position assessment.

**Chart 2**

**Loan Portfolio Evolution**



NPL--Non-performing loan. PEN--Peruvian nuevo sol. Source: SBS (Superintendencia de Banca, Seguros y AFP).

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**Funding And Liquidity: Low Liquidity Needs In The Next 12 Months And Good Access To Capital Markets**

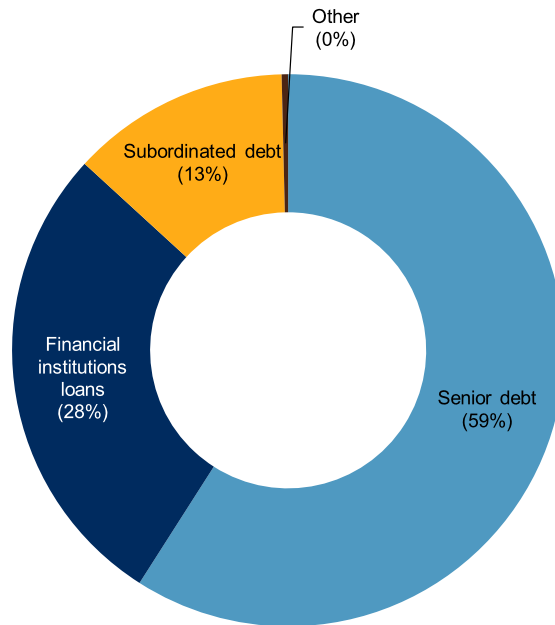
The bank's funding assessment reflects its stable funding ratio (SFR) of 112.1% as of June 2021 (105% on average for the past three years), similar to that of most Peruvian banks. Our baseline expectation is that COFIDE's SFR will be above 100% for the next two years. Unlike private banks, COFIDE isn't allowed to receive deposits. However, its financial flexibility benefits from the government's ongoing support, allowing COFIDE to refinance its debt, as seen in the strong demand for its issuances. Although the bank receives higher-than-average external funding, we believe it has an adequate funding profile, given the latter's long-term nature required for the loans. We expect the bank to continue matching tenors and currencies on its balance sheet to mitigate risks.



COFIDE continues to maintain a sufficient liquidity cushion to cope with unexpected cash outflows over the next 12 months. Its broad liquid assets covered 2.9x of its short-term wholesale funding. The debt maturity profile provides the bank sufficient time to manage its liquidity risk.

**Chart 3**

**Funding Breakdown**  
As of June 2021



Source: S&P Global Ratings.  
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**Support: Four Notches Of Uplift For Government Support**

Our assessment of the likelihood of extraordinary government support reflects COFIDE's increasing role in meeting the government's key economic and social objectives. For the government, supporting corporate activity through the COVID-19 pandemic and developing infrastructure are the main priorities boost economic growth and productivity for the next few years.

Moreover, the government's explicit commitment to supporting the bank corroborates our review of this assessment. As mentioned above, the MEF acquired part of COFIDE's shares in CAF, partially executing the comfort letter signed in 2017 when the government announced its intention to buy up to 20% of the bank's shares in CAF in the next four years, if needed. Also, in November 2017, Fondo Nacional de Financiamiento de la Actividad Empresarial del Estado (FONAFE) injected \$18 million into the bank, then capitalized \$102 million of the bank's multilateral debt in January

2018, and finally injected \$51 million in May 2018. FONAFE approved the retention of the bank's net income for several years.

## Environmental, Social And Governance

We believe ESG credit factors, especially social and governance, affect COFIDE's credit quality more than its industry and local peers in Peru.

COFIDE has been a key social tool for implementing public policies and government programs to mitigate the economic impact of COVID-19, which reaffirms our expectation of extraordinary government support toward this entity, bringing more stability to its ratings compared to private banks.

On the other hand, risk management and governance standards continue to pose major challenges to avoid abrupt asset quality deterioration and capital injection needs, as has been the case in the past few years. In our view, the Peruvian banking system has generally had satisfactory corporate governance practices, although multiple corruption cases (such as the fallout of the "Car Wash Operation" corruption probe in Brazil) have affected high-ranking politicians, major companies, and the judicial system have exposed banks to challenging credit conditions, particularly in the country's infrastructure and construction sector. In this context, COFIDE's credit fundamentals were hampered during 2017-2018 and then stabilized in 2019 after the bank's capital strengthening plan and other risk-control measures.

Since September 2016, COFIDE's new management has focused on overhauling its risk management strategy and raising provisioning from souring loans to construction companies and affected projects (NPLs peaked at 28.7% in 2018). Despite these efforts to address aggressive risk tolerances and poor internal controls, we believe that the government may still negatively influence strategic decisions because of COFIDE's role in promoting infrastructure investments in Peru amid increasing structural rigidities and private investment scrutiny.

## Key Statistics

Table 1

Corporacion Financiera de Desarrollo S.A.--Key Figures					
	--Year ended Dec. 31--				
(Mil. PEN)	2021*	2020	2019	2018	2017
Adjusted assets	12,526.9	12,444.4	10,450.1	11,115.9	11,970.1
Customer loans (gross)	6,385.5	6,626.3	5,083.7	5,803.7	6,867.5
Adjusted common equity	2,182.1	1,941.4	1,939.9	1,922.8	1,908.8
Operating revenues	49.5	183.8	97.3	124.2	140.3
Noninterest expenses	33.0	62.3	65.9	68.6	75.3
Core earnings**	(158.4)	19.1	27.3	14.3	1.7

\*Data as of June 30. \*\*In 2021 not including the gains from the sale of CAF shares. PEN--Peruvian nuevo sol. N/A--Not applicable.

**Table 2**

<b>Corporacion Financiera de Desarrollo S.A.--Business Position</b>					
<b>--Year ended Dec. 31--</b>					
<b>(%)</b>	<b>2021*</b>	<b>2020</b>	<b>2019</b>	<b>2018</b>	<b>2017</b>
Return on average common equity	2.1	1.0	1.3	0.9	0.2

\*Data as of June 30.

**Table 3**

<b>Corporacion Financiera de Desarrollo S.A.--Capital And Earnings</b>					
<b>--Year ended Dec. 31--</b>					
<b>(%)</b>	<b>2021*</b>	<b>2020</b>	<b>2019</b>	<b>2018</b>	<b>2017</b>
Adjusted common equity/total adjusted capital	100.0	100.0	100.0	100.0	100.0
Net interest income/operating revenues	16.2	72.6	70.8	76.8	78.7
Fee income/operating revenues	79.1	26.7	28.4	23.2	21.3
Cost to income ratio	66.6	33.9	67.7	55.2	53.7
Preprovision operating income/average assets	0.3	1.1	0.3	0.5	0.5
Core earnings/average managed assets **	(2.5)	0.2	0.3	0.1	0.0

\*Data as of June 30. \*\*In 2021 not including the gains from the sale of CAF shares. N/A--Not applicable.

**Table 4**

<b>Corporacion Financiera de Desarrollo S.A.--Risk Position</b>					
<b>--Year ended Dec. 31--</b>					
<b>(%)</b>	<b>2021*</b>	<b>2020</b>	<b>2019</b>	<b>2018</b>	<b>2017</b>
Growth in customer loans	(7.3)	30.3	(12.4)	(15.5)	(12.4)
Total diversification adjustment/S&P Global Ratings' RWA before diversification	N/A	N/A	125.9	118.0	105.2
Total managed assets/adjusted common equity (x)	5.7	6.4	5.4	5.8	6.3
New loan loss provisions/average customer loans	11.9	2.0	(0.1)	0.5	0.8
Net charge-offs/average customer loans	(1.1)	(0.8)	(0.8)	10.9	(0.0)
Gross nonperforming assets/customer loans + other real estate owned	10.6	9.6	7.7	6.3	18.2
Loan loss reserves/gross nonperforming assets	220.2	167.5	228.8	253.0	91.2

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

**Table 5**

<b>Corporacion Financiera de Desarrollo S.A.--Funding And Liquidity</b>					
<b>--Year ended Dec. 31--</b>					
<b>(%)</b>	<b>2021*</b>	<b>2020</b>	<b>2019</b>	<b>2018</b>	<b>2017</b>
Long-term funding ratio	89.2	88.4	84.2	75.8	89.8
Stable funding ratio	112.1	109.7	108.3	97.3	109.2
Short-term wholesale funding/funding base	13.5	14.2	19.9	29.6	12.5
Broad liquid assets/short-term wholesale funding (x)	2.9	2.4	1.7	1.1	2.6
Short-term wholesale funding/total wholesale funding	13.5	14.2	19.9	29.6	12.5

\*Data as of June 30. N.M.--Not meaningful.

## Related Criteria

- General Criteria: Group Rating Methodology, July 1, 2019
- Criteria | Financial Institutions | General: Risk-Adjusted Capital Framework Methodology, July 20, 2017
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- General Criteria: Rating Government-Related Entities: Methodology And Assumptions, March 25, 2015
- Criteria | Financial Institutions | Banks: Quantitative Metrics For Rating Banks Globally: Methodology And Assumptions, July 17, 2013
- Criteria | Financial Institutions | Banks: Banking Industry Country Risk Assessment Methodology And Assumptions, Nov. 9, 2011
- Criteria | Financial Institutions | Banks: Banks: Rating Methodology And Assumptions, Nov. 9, 2011
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

## Related Research

- Banking Industry Country Risk Assessment: Peru, Aug. 9, 2021

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 August 30, 2021)\*

#### Corporacion Financiera de Desarrollo S.A.

Issuer Credit Rating	BBB/Stable/A-2
Senior Unsecured	BBB
Subordinated	BBB-

#### Issuer Credit Ratings History

13-Aug-2019	BBB/Stable/A-2
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**Ratings Detail (As Of August 30, 2021)\*(cont.)**

17-Aug-2017	BBB/Negative/A-2
20-Aug-2013	BBB+/Stable/A-2
<b>Sovereign Rating</b>	
Peru	
<i>Foreign Currency</i>	BBB+/Stable/A-2
<i>Local Currency</i>	A-/Stable/A-2
<b>Related Entities</b>	
<b>Fondo Mivivienda S.A.</b>	
Issuer Credit Rating	BBB+/Stable/--
Senior Unsecured	BBB+
<b>Peru</b>	
Issuer Credit Rating	
<i>Foreign Currency</i>	BBB+/Stable/A-2
<i>Local Currency</i>	A-/Stable/A-2
Certificate Of Deposit	
<i>Local Currency</i>	A-2
Senior Unsecured	A-
Senior Unsecured	BBB+

\*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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