Superintendencia de Bancos de Panamá

Banking Activity Report

January 2022

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As we kicked off 2022, the Panamanian Banking Center maintained a solid, resilient position, with capital and liquidity levels above regulatory minimums. The latest global capital ratio showed 15.9%, almost double the regulatory minimum of 8%. This performance was based on solid regulatory parameters that have been strengthened by regulatory mandates since before the pandemic. In terms of liquidity, the Banking system reached 59.6%, almost double the legally required as well. Currently, all banks running operations comply with bank capital regulatory standards and liquidity provisions.

In this context of strong banking fundamentals, it has been possible to prove that the International Banking Center's (IBC) business volume showed, at the beginning of 2021 (sic), an increasing volume of credit operations, leveraged by growing deposits and other sources of stable funding, such as obligations and other liabilities that grew during the period. The uncertainty caused by credit risk will be the main vulnerability for the stability of the financial system in the medium-term.

During the first month of 2022, the assets of the International Banking Center totaled USD 134.97 billion, a USD 4.18 billion increase versus January 2021, i.e. a year-on-year growth of 3.2%, which is the result of increases in the net loan portfolio (4.0%) and the securities portfolio (11.3%).

Throughout the first 31 days of the year, the domestic loan portfolio recorded a total of USD 55.32 billion, a USD 1.14 billion or 2.1% increase. It should be noted that, although the country is undergoing an economic recovery, it has been asymmetrical as some sectors are still recovering. The new loans processed by banks, as of January 2022, totaled USD 1.34 billion, a 43.0% increase compared to a year earlier. However, a decrease was observed in the monthly evolution, versus previous months, which responded to the fact that during January there was a record high of infections, which, coupled with a seasonal component in loans disbursement, resulted in an underperformance. In the monthly difference, new loans decreased by 32.3%.

In terms of credit, it is noteworthy to mention the positive performance of the external component of the portfolio, which highlighted the IBC's key role in meeting the financing needs of Latin American and Caribbean countries. In the future, we envision that maintaining this position will require having a strong financial sector, with effective supervision, and prudential regulations adapted to international standards and best practices, which will make it possible to reinforce our leading role in the regional financial context.

Regarding the modified [loan] portfolio, it followed the trend observed at the end of 2021. As of January 2022, it totaled USD 8.29 billion, a USD 14 billion or 64% decrease, versus January 2021, and about USD 900 million [less] that that of December 2021. Household and real estate are the sectors with the greatest shift to the regular portfolio covered by Rule 4-2013.

The International Banking Center recorded net profits, as of January 2022, of USD 130.4 million, USD 31.3 million more than on the same date in 2021, that is, a year-on-year growth of 31.6%. Profits showed a lower accumulation in provisioning and, although there was lower income per portfolio, they were offset by the greater relevance of financial services income. The lower level of provisioning expenses is related to the fact that, on the same date last year, the scenario was still unclear, specifically what the economic normalization and the readjustment process of the portfolio subject to the financial relief program would be like. This situation caused the banks to fix additional provisions, i.e., they saved resources given the possibility of a more complicated scenario. At the end of the last quarter of 2021, a significant shifting of modified loans that could improve their financial condition and return to Rule 4-2013 was observed, showing a decrease compared to last year. However, it should be remarked that a segment of recorded provisions went through capital and it was not showed in the income statement account.

Deposits placed in the market, as of January 2022, recorded a total of USD 98.56 billion, a USD 2.11 billion increase compared to January 2021. If the analysis is focused on domestic deposits, they recorded an increase, as of January 2022, to reach USD 64.79 billion, a 1.2% growth versus January 2021. It is noteworthy to mention that in January there was a record high of infections, due to the Omicron variant, which resulted in both companies and households increased their deposits, particularly the most liquid ones.

Customer demand (+5.5%) and savings (+11.1%) deposits held by the financial system increased. In this way, a rearrangement of bank deposits continued to be recorded, as immediate demand deposits increased since depositors sought to have greater availability and liquidity of their resources.

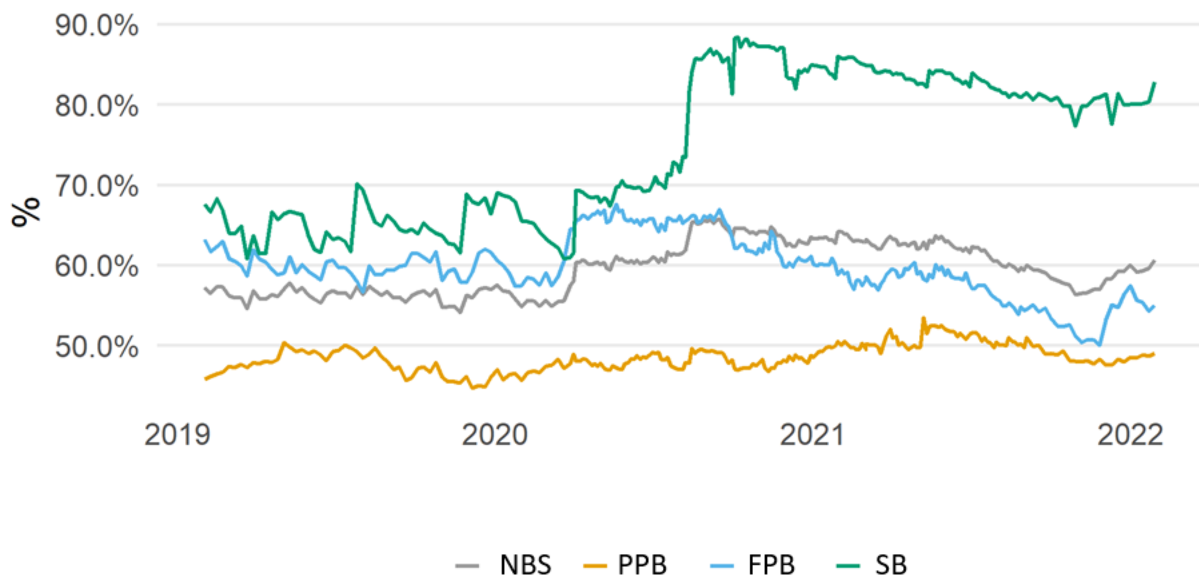
A. Liquidity

As of January 2021 (sic), the liquidity of the Banking System reached 59.6%, almost double the regulatory minimum. The domestic banking system has recorded a more comfortable liquidity position since March 2020 (**see Graph 1**), as a result of the accumulation of short-term assets in a high uncertainty context, which responded to the comprehensive strategy of caring for the quality of assets, provisioning and expanding liquidity, guided by prudential principles promoted by the Superintendency.

In relation to liquidity to date, although there has been certain decrease in ratios versus the levels they reached in 2020, the financial system maintained adequate liquidity levels at the aggregate level, with sufficient resources to meet its short-term needs and which, in turn will make it easier to resume credit growth. The decrease recorded reflect great loan disbursement.

Graph 1: Weekly average liquidity ratio

January 2019 – January 2022



Source: General License Banks

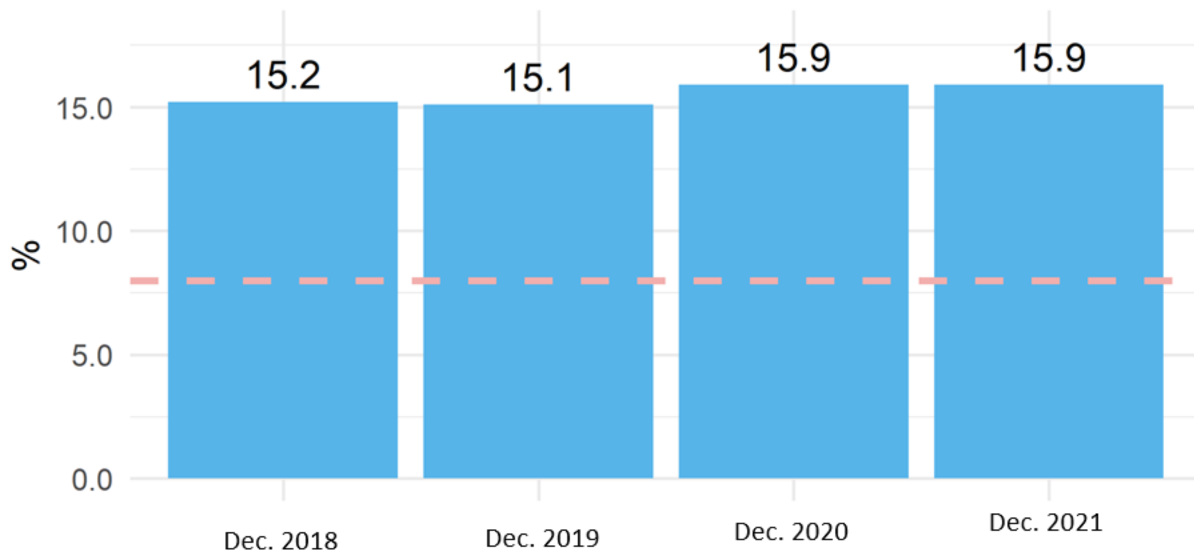
It should be noted that banking in Panama has maintained abundant liquidity levels since the onset of the pandemic, which has been an important factor in coping with the effects of the complicated scenario we have had since March 2020. The foregoing is explained, in part, because banks increased their liquidity reserves, because of the implementation of the Rule on Liquidity Coverage Ratio (LCR). The LCR and high-quality liquid assets (HQLA) requirements are especially relevant given the absence of a central bank and a deposit guarantee, which is why this provision has remained in place in the context of the COVID-19 contingency. The regulations set December 2021 as the deadline to comply with the LCR established in the Rule. To date, the banks running operations comply with the applicable provisions in this regard, in accordance with the corresponding brackets.

B. Solvency

The capital adequacy ratio on risk-weighted assets was 15.9% as of the end of 2021 (**see Graph 2**), because of higher capital growth in relation to regulatory requirements, this represents twice the regulatory minimum of 8%. This increase can be explained by the recapitalization of some entities, the reduction in the payment of dividends, and the lower balance of assets subject to risk. Currently, all banks running operations comply with bank capital regulatory standards.

Graph 2: Capital Adequacy Ratio

Dec. 2018 – Dec. 2021



Source: General and International License Banks

C. Income Statement

The International Banking Center recorded net profits, as of January 2022, of USD 130.4 million or USD 31.3 million more than on the same date in 2021, i.e. a year-on-year growth of 31.6%. The performance of profits showed a lower accumulation in provisioning, and although there was lower income per portfolio, these were offset by the greater relevance of financial services income. The result was mainly driven by the reduction in net provisioning (-15.8%), the increase in other income (+2.4%), and the stability in operating income in portfolio interest income and securities income, where the performance of the latter showed positive yields mainly by bondholding or instruments at fair value and the purchase and sale of foreign currency. Seen from a broad perspective, the lower provisioning had a positive impact on the sector's profit, which placed it in positive figures.

However, it should be remarked that a segment of recorded provisions went through capital and it was not showed in the income statement account. It is important to mention that, in view of the modified loan facility produced in the context of the pandemic, interest under this modality is recorded under the accrual method, that is, accrued interest is recorded but not necessarily collected. This must be considered at the face of the potential occurrence of default events.

Table 1: International Banking Center
Accumulated Income Statement
(in millions of USD)

International Banking Center	January 2021	January 2022	% Diff.	Total Diff.
Net interest income	193.06	204.69	6.02%	11.63
Other income	172.03	176.12	2.38%	4.08
Operating income	365.09	380.80	4.30%	15.71
General expenses	194.35	190.10	-2.19%	-4.24
Profit before provisions	170.74	190.70	11.69%	19.96
Bad debt provision	71.64	60.31	-15.82%	-11.32
Profit for the period	99.11	130.38	31.55%	31.28

Source: General and International License banks.

As indicated above, the COVID-19 pandemic has had a negative effect on the income-generating capacity of banks. This is because that, in the current situation, the performance of loans continues at a reduced rate when compared to the pre-pandemic performance.

The National Banking System recorded accumulated net profits (sic), as of January 2022, of USD 120.6 million, 50.4% more than that of January 2021. Like what happened in the IBC, lower provisioning had a positive impact on the sector’s profit.

Table 2: National Banking System
Accumulated Income Statement
(in millions of USD)

National Banking System	January 2021	January 2022	% Diff.	Total Diff.
Net interest income	183.2	192.2	4.91%	9.0
Other income	147.4	161.8	9.77%	14.4
Operating income	330.6	354.0	7.08%	23.4
General expenses	178.6	174.4	-2.35%	-4.2
Profit before provisions	152.0	179.6	18.16%	27.6
Bad debt provision	71.8	59.0	-17.83%	-12.8
Profit for the period	80.2	120.6	50.37%	40.4

Source: General license banks.

Thus far, the NBS will not record financial margins like pre-pandemic ones, although, a month-by-month loan improvement is seen, which in turn will produce higher levels of financial income. General license banks are expected to continue with cost control and operational efficiency strategies. Currently, IBC efficiency levels are around 52%.

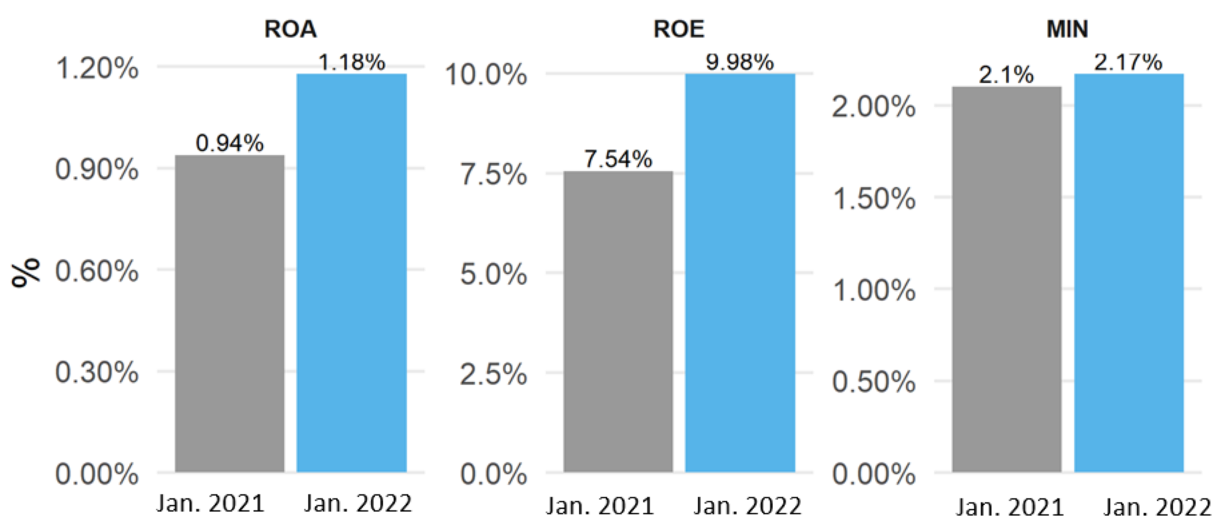
D. Profitability indicators

As for profitability, ROA and ROE indicators have changed the trend that began with the pandemic and it is already possible to observe a slight improvement. The reduction in financial income was the component that explained, to a greater extent, the reduction in profitability.

The increase in profits implied that the return on average equity went up to 9.98% (7.54% January 21) and the return on assets to 1.18% (0.94% January 21). In an environment of still incipient recovery, IBC banks profitability continued with a weak performance. This is mainly due to the lower interest rates at which new loans were placed and the decrease in placements compared to pre-pandemic periods. It should be noted that these lower bank profitability levels, which have been accentuated during the COVID-19 crisis, were also observed in a significant sample of countries, i.e. it has not been an exclusive situation of banks in the country.

Graph 3: Profitability Indicators - IBC

January 2021 – January 2022



Source: General and International License banks

E. Balance Sheet

During the first month of 2022, the assets of the International Banking Center totaled USD 134.97 billion, a USD 4.18 billion growth versus January 2021, i.e. a year-on-year increase of 3.2%, which is the result of the rise in the net loan portfolio (4.0%) and the securities portfolio (11.3%). Although there was a decrease in liquid assets (-6.4%), they remained higher in a broad time context, since from the beginning of the health contingency, most institutions strengthened their positions to mitigate their sensitivity to the negative shocks triggered by the health crisis.

Since mid-2021 there has been a rearrangement of productive assets. Thus, the loan portfolio, its main component, would have exhibited an upward trend that sped up its growth during the second half of the year. Regarding the net loan portfolio, as of January 2022, the International Banking Center presented a 4.0% rise to reach to USD 74.34 billion. As for the credit demand recovery rate, this has been asymmetrical between portfolios, but it already showed a positive performance in the aggregate. Another important factor that contributed to the growth of IBC lending operations was the shift of liquid assets and loan flows to the securities portfolio, which amounted to USD 28.12 billion, a USD 2.86 billion rise. So far this year, this component recorded a positive performance (a year-on-year increase of 11.3%) and would reflect the search for bank profitability.

The evolution of liabilities is especially related to the performance of its main component: deposits. Regarding bank financing sources, deposits recorded an increase of USD 2.11 billion (2.2%), which is the result of the performance of growing domestic deposits (1.2% or USD 755 million) and external deposits (4.2% or USD 1.36 billion) in nominal terms. As main components, customer deposits can be highlighted as the most liquid one. The deposits of the International Banking Center as of January 2022 amounted to USD 98.56 billion. It should be remarked that the performance of customer deposits – both by domestic and external depositors – can be understood as that they have remained confident on the stability of the banking system, which is reflected in greater funding of establishments. As indicated in previous reports, bank liabilities showed a rearrangement towards more liquid instruments. In fact, it has been found that this growth has been underpinned by demand and savings deposits. It is noteworthy that during the analyzed period, there were increases in other liabilities (+1.6%) and obligations (+10.9%).

Table 3: International Banking Center
Balance Sheet
(in millions of USD)

Breakdown	2020	2021	Jan. 22/Jan. 21 Difference	
	January	January	Total	%
Liquid assets	27,292	25,542	-1,750	-6.4%
Net loan portfolio	71,456	74,339	2,882	4.0%
Domestic	52,254	53,037	783	1.5%
External	19,202	21,302	2,099	10.9%
Securities	25,257	28,111	2,854	11.3%
Other assets	6,789	6,977	188	2.8%
Total Assets	**130,794**	**134,969**	**4,175**	**3.2%**
Deposits	96,447	98,554	2,107	2.2%
Domestic	64,034	64,789	755	1.2%
External	32,413	33,765	1,352	4.2%
Obligations	15,107	16,751	1,644	10.9%
Other liabilities	3,741	3,802	61	1.6%
Capital	15,499	15,862	364	2.3%

Source: General and International License banks

In the case of the National Banking System (general license banks only), assets totaled USD 119.18 billion, USD 3.06 billion or 2.6% more than that of January 2021. The net loan portfolio of the National Banking System showed a USD 2.55 billion (3.8%) increase to reach to USD 68.19 billion. Net external loans grew 13.1%, while the domestic portfolio had a higher performance of 1.5%. On the other hand, total deposits placed in the NBS totaled USD 86.88 billion, a 1.4% rise, which is mainly the result of customer deposits.

Table 4: National Banking System
Balance Sheet
(in millions of USD)

Breakdown	2020 January	2021 January	Dec. 21/Dec. 20 Difference Total	%
Liquid assets	22,204	21,294	-910	-4.10%
Net loan portfolio	65,647	68,188	2,541	3.87%
Domestic	52,254	53,040	786	1.50%
External	13,393	15,148	1,756	13.11%
Securities	21,690	23,065	1,374	6.34%
Other assets	6,588	6,633	45	0.68%
Total Assets	**116,129**	**119,179**	**3,051**	**2.63%**
Deposits	85,976	86,871	896	1.04%
Domestic	63,937	64,702	764	1.20%
External	22,039	22,170	131	0.60%
Obligations	14,425	16,531	2,105	14.59%
Other liabilities	3,619	3,567	-51	-1.42%
Capital	12,109	12,210	101	0.84%

Source: General License banks

F. Loans

During the first month of the year, the domestic loan portfolio recorded a total of USD 55.32 billion, a USD 1.14 billion or 2.1% increase. It should be noted that, although the country is undergoing an economic recovery, it has been asymmetrical and some sectors are still recovering to improve the demand for credit they had in 2019, with which, the sectoral performance of the different loan portfolios has not been similar. Regarding the performance of these, as of January 2022, except for loans from Financial Activities (-26.8%); Mining & Quarrying (-10.1%), and Construction (-9.3%), the rest of productive activities had positive figures. The performance of these sectors is due to the fact that, although at the beginning of the pandemic, companies resorted to the lines of credit they had in force to face the effects triggered by the contingency, they later stopped the demand for credit or resorted to other sources of financing.

Regarding the balance of the corporate loan portfolio, it recorded, as of January 2022, a nominal year-on-year difference of 4.3%, better than that recorded in December

2021. The consumer loan portfolio made up of mortgages (+4.2%) and personal consumption (+4.6%) had a positive performance in its different segments but has begun to show a slight slowdown. Greater inflationary pressure coupled with precautionary reasons associated with the different waves of infection experienced at the beginning of the year were shown in an intermittent and somewhat moderate recovery in consumption which limited the demand for this type of lending and affected the lower new loans granted.

Table 5: National Banking System
Balance of domestic loan portfolio by economic sectors - (in millions of USD)

Sectors	January 2021	January 2022	Jan.-Jan. 22/21 Difference	
			Total	%
Public entities	**54,174.3**	**55,313.2**	1,138.9	2.1%
Financial companies	**1,402.7**	**1,469.5**	66.8	4.8%
Agriculture (incl. forestry)	**52,771.6**	**53,843.7**	1,072.1	2.0%
Livestock	1,489.7	1,090.4	-399.3	-26.8%
Fishing	397.2	436.6	39.4	9.9%
Mining & Quarrying	1,312.8	1,341.3	28.5	2.2%
Commerce (incl. Services)	82.9	87.3	4.4	5.3%
Industry	56.1	50.4	-5.7	-10.2%
Mortgages	10,474.2	10,921.4	447.2	4.3%
Construction	2,767.5	2,942.0	174.5	6.3%
Personal consumption	18,053.6	18,811.6	758.0	4.2%
Total	5,787.0	5,246.4	-540.6	-9.3%

Source: General License banks

New loans processed by banks, as of January 2022, totaled USD 1.34 billion, a 43.0% increase compared to a year earlier. However, a decrease was observed in the monthly evolution versus previous months (**see Graph 4**), which responds to the fact that during January there was a record high of infections, which, coupled with a seasonal component in loans disbursement, resulted in an underperformance. In the monthly difference, new loans decreased by 32.3%.

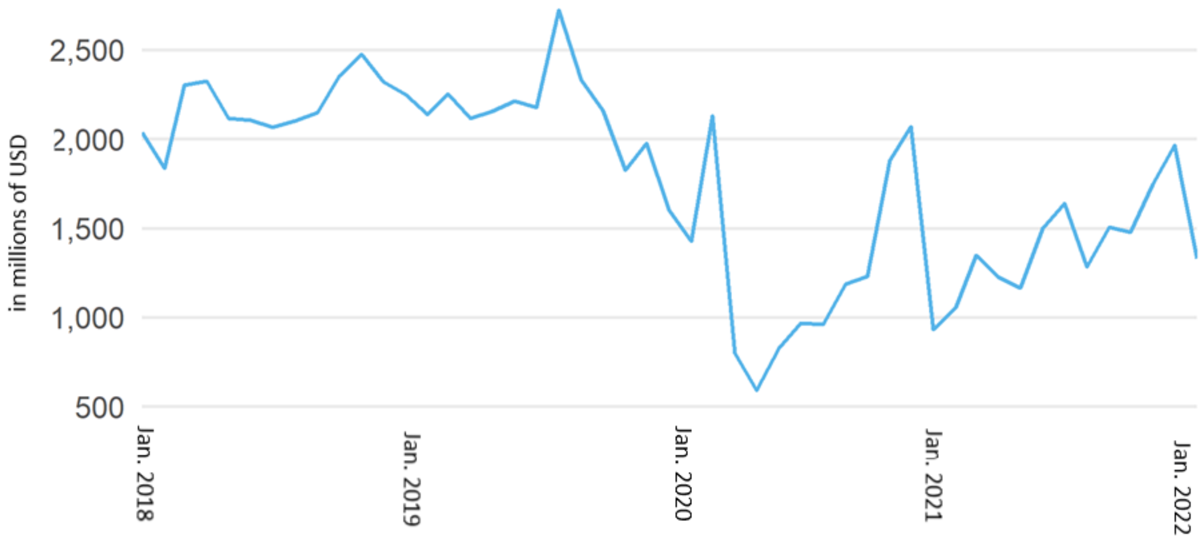
Table 6: National Banking System
New domestic loans by sectors and activities - (in millions of USD)

Sectors	January 2021	January 2022	Jan.-Jan. 22/21 Difference	
			Total	%
Public entities	5.7	10.0	4.3	75.5%
Financial companies	32.7	44.1	11.4	35.0%
Agriculture (incl. forestry)	9.1	22.1	13.0	143.0%
Livestock	38.9	32.2	-6.8	-17.4%
Fishing	1.1	0.6	-0.5	-45.9%
Mining & Quarrying	1.4	0.4	-1.0	-73.9%
Commerce (incl. Services)	448.8	691.9	243.1	54.2%
Industry	142.4	130.3	-12.0	-8.5%
Mortgages	98.3	149.0	50.7	51.5%
Construction	60.0	109.9	50.0	83.3%
Personal consumption	92.2	140.1	47.9	52.0%
Total	**930.5**	**1,330.7**	**400.1**	**43.0%**

Source: General License banks

Graph 4: New Loans

Jan. 2018 – Jan. 2022



Source: General License Banks

The positive performance of the external loan portfolio (+13.2%) stood out, which highlighted the IBC's key role in meeting the financing needs of Latin American and Caribbean countries. Said increase could be driven by the country's competitive rates in a context in which most of the countries in the region began increasing their monetary policy rates that have already impacted the credit granting rates. In the future, we envision that maintaining this position will require having a strong financial sector, with effective supervision and prudential regulations adapted to international standards and best practices, which we believe will allow us to reinforce our leading role in the regional financial context.

In an economic reactivation context and a currently controlled health outlook, the credit risk indicator has remained at limited levels, as a result of the exceptional credit support measures applied by the SBP during the pandemic, and that would have ended in September 2021. As of January 2022, the total delinquency rate[1] stood at 4.2%, slightly below that of 2021. Going forward, the uncertainty caused by past due loans will be the main vulnerability for the stability of the financial system. Regarding provisions, they allow credit risk coverage, representing more than 100% of overdue loans subject to the stipulations of Rule 4-2013.

[1] Understood as the delinquent and past due components with respect to the total portfolio

G. Structure of the Loan Portfolio and the Performance of the Modified Portfolio

The modified [loan] portfolio, as of January 2022, amounted to USD 8.29 billion. The issuance of prudential regulations promoted the achievement of agreements between banks and their clients, with which as of the second half of 2021, there were important shifts towards the unmodified [loan] portfolio. This represented a USD 14 billion or 64% decrease, versus the same period of 2021, and about USD 900 million [less] that that of December 2021. Household and real estate are the sectors with the greatest shift to the regular portfolio covered by Rule 4-2013.

On the other hand, in the context of the classification established by Board of Directors' General Resolution SBP-GJD-0003-2021, as of the end of January, the portfolio that could entail the greatest risk would be the modified doubtful and modified loss categories, due to the fact that, to date, they have not been able to make a larger payment arrangement, and together amounted to USD 1.53 billion or 18.4% of the total modified [loan] portfolio. All these performances relate to the improvement in the monthly payments, however, the portfolio classified in this category is still very high and could lead to higher provisioning.

Table 7: Modified loans of the National Banking System by Economic Activity
In millions of USD

Sectors	January 2021	January 2022	Total Diff.	% Diff.
Mortgages	9,485	3,648	-5,837	-62%
Consumer	4,386	1,865	-2,521	-57%
Construction	3,479	1,020	-2,459	-71%
Services	2,907	1,070	-1,837	-63%
Commerce	896	426	-470	-52%
Industry	447	90	-357	-80%
Others	1,392	170	-1,222	-88%
Total	**22,992**	**8,289**	**-14,703**	**-64%**

H. Deposits

As of January 2022, the deposits of the International Banking Center rose to 2.2% versus January 2021. This difference responds to an increase in both domestic and external deposits, having in common that both responded significantly to the growth of customer deposits, both in demand and savings deposits. Such performance showed that domestic and external bank depositors trust the strength of IBC banks and the country's macroeconomic stability despite going through a complicated environment.

Deposits placed in the market, as of January 2022, recorded a total of USD 98.56 billion, USD 2.11 billion more than that of January 2021 (**see Table 8**). If the analysis is focused on domestic deposits, an increase was recorded as of January 2022, reaching USD 64.79 billion, a 1.3% growth versus January 2021. It is noteworthy that in January there was a record high of infections, due to the Omicron variant, which resulted in both companies and households increasing their deposits, particularly the most liquid ones.

On the other hand, external deposits recorded an increase of USD 1.36 billion, amounting to USD 33.77 billion. In nominal terms, the largest deposit increases came from Peru, Colombia, and El Salvador. It is worth noting that the increase in global inflation, as well as the expectation that major central banks will fix interest rate hikes in the future, in addition to exchange rate uncertainty, have affected the demand for domestic financial assets and liabilities in the past.

Table 8: International Banking Center
Total Deposits
(in millions of USD)

Accounts	2021	2022	Jan. 22 / Jan 21 Diff.	
	January	January	Total	%
Deposits	**96,447.4**	**98,554.1**	**2,106.7**	**2.2%**
Domestic	**64,034.1**	**64,788.2**	**754.1**	**1.2%**
Government	14,159.6	13,742.9	-416.7	-2.9%
Customer	45,483.2	47,816.3	2,333.1	5.1%
Banks	4,391.4	3,229.1	-1,162.3	-26.5%
External	**32,413.3**	**33,765.9**	**1,352.6**	**4.2%**
Government	139.8	335.7	195.9	140.1%
Customer	23,608.4	26,400.1	2,791.7	11.8%
Banks	8,665.1	7,030.1	-1,635.0	-18.9%

Source: General and International License banks.

In the case of the banks of the National Banking System, there is a trend like that of the IBC, recording a balance of USD 86.88 billion, a 1.0% increase versus January 2021, driven by domestic and external deposits (**see Table 9**).

Table 9: National Banking System
Total Deposits
(in millions of USD)

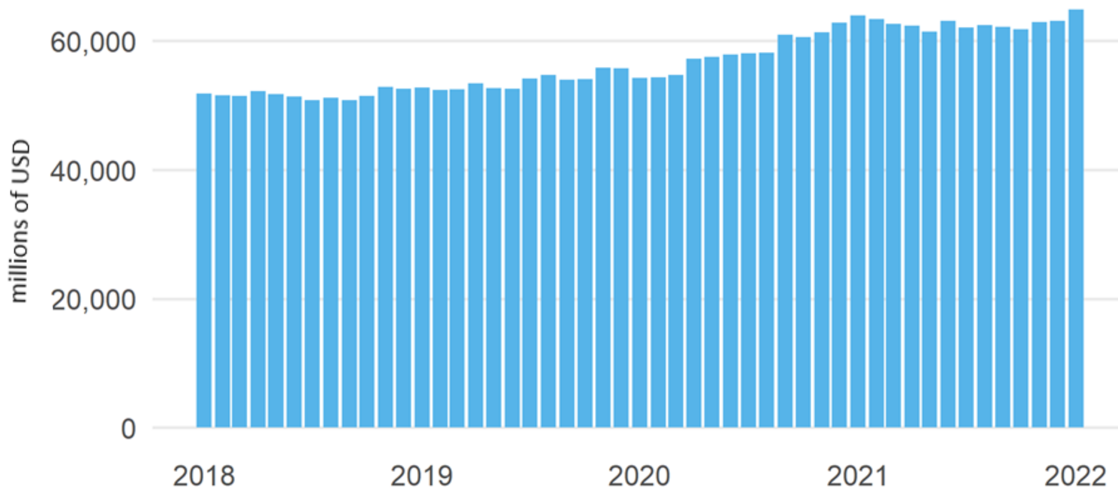
Accounts	2021	2022	Jan. 22 / Jan 21 Diff.	
	January	January	Total	%
Deposits	**85,975.9**	**86,871.5**	**895.5**	**1.0%**
Domestic	**63,937.3**	**64,701.5**	**764.2**	**1.2%**
Government	14,159.6	13,742.9	-416.7	-2.9%
Customer	45,483.2	47,816.2	2,333.0	5.1%
Banks	4,294.5	3,142.4	-1,152.1	-26.8%
External	**22,038.7**	**22,170.0**	**131.3**	**0.6%**
Government	139.7	333.5	193.8	138.7%
Customer	13,668.6	15,271.7	1,603.1	11.7%
Banks	8,230.3	6,564.7	-1,665.6	-20.2%

Source: General License banks.

The structure of IBC deposits is based mainly on collecting customers and corporate deposits, which hold 85% of total deposits, the remaining 15% are interbank positions.

It should be remarked that the domestic deposits of the National Banking System represented 73.7% of total NBS deposits. To date, it was observed that customer deposits have shown resilience and there are no short-term reductions that could indicate that there could be a situation that exposes the group of banks. **Graph 5** shows the evolution of the balance of domestic deposits.

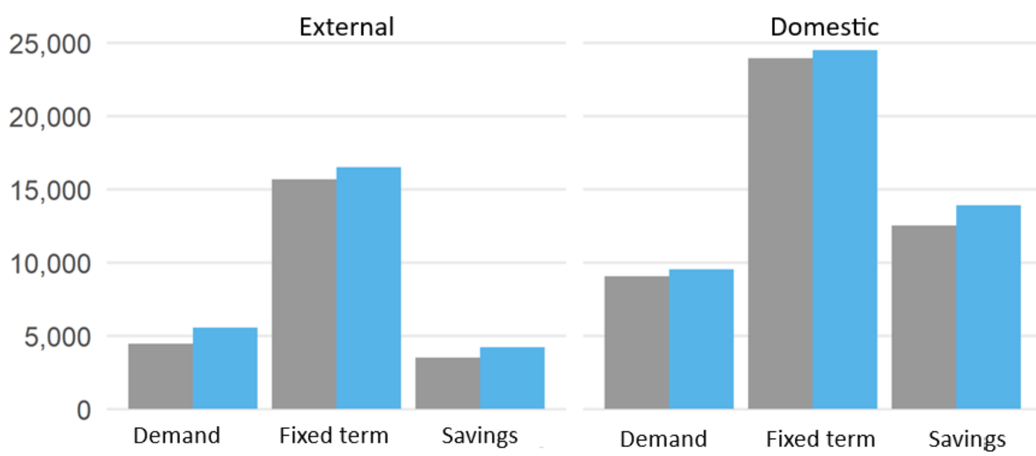
Graph 5: Total Domestic Deposits
Jan. 2018 – Jan. 2022



Source: General license banks.

Regarding the structure of customer liabilities by maturity, fixed term deposits continue to be the most important savings instrument. As of January 2022, they represented 51.1% of customer domestic deposits by totaling USD 24.50 billion, followed by savings rising to USD 13.91 billion; and demand deposits amounting to USD 9.52 billion.

Graph 6: Customer Deposits
January 2021 – January 2022



Source: General and International license banks.

Customers demand deposits (+5.5%) and savings deposits (+11.1%) held by the financial system grew. In this way, a rearrangement of bank deposits continued to be recorded, by increasing the collection of demand accounts as depositors sought to have greater availability and liquidity of their resources. The reactivation of economic activity, which benefited a greater inflow from the sale of goods and services, as well as the substitution of fixed term deposits could explain the increase observed in the performance of demand deposits.

It is worth noting that, although fixed term deposits have remained relatively stable throughout 2020 and 2021, they have been less energetic than more liquid components.

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