Banking Activity Report

May 2022

Table of Contents

Executive Summary

In May 2022, the International Banking Center (IBC) continued to show high liquidity and solvency margins. The intermediation levels of the group of banks increased, which has allowed an improvement in profitability.

The banks making up the IBC have strong funding, consisting mainly of deposits, which gives great stability to their source of financing. Historically, funding diversification, deposit stability, and efficient use of hedging have contributed to mitigating liquidity risk. As of May 2022, the liquidity of the Banking System reached 58.0%. Regarding solvency ratios, the capital adequacy ratio on risk-weighted assets was 15.46% at the end of the 1Q2022, almost double the regulatory minimum of 8%. Currently, all banks running operations satisfactorily comply with the new bank capital regulatory standards.

The assets of the International Banking Center, as of May 2022, totaled USD 136.47 billion, a USD 7.89 billion increase versus May 2021, i.e., a year-on-year growth of 6.13%, which was the result of a rise in the net loan portfolio (10.1%) and the securities portfolio (15.9%) that keeps growing but at a slower pace. On the liquid assets' side, although they fell short (-13.0%), the banking system has high-quality instruments fully available to face stressed financial market conditions.

The securities portfolio recorded a year-on-year increase of USD 3.98 billion (15.9%). However, an assessment from December shows a 4.5% growth, explained by the underperformance of the foreign investment portfolio. During the last few months, major global stock markets showed devaluations like U.S. bonds throughout the curve, in accordance with the monetary policy rate hikes and the expectation of new hikes in the coming months. Nevertheless, to date, the volatility effects of the financial markets in the investment portfolio are being mitigated by the investment portfolio's short period. Given that corporate bonds and non-government securities account for a significant share of liquid resources, and could be less liquid in volatile periods, the SBP will be monitoring them closely.

As of the fifth month of the year, it has been possible to prove that banks loan portfolio once again showed an upward trend, where all new loans segments have accumulated positive results, but are beginning to weaken in their monthly components. These performances are leveraged by the improvement of deposits and other sources of stable funding that grew during the period, among others.

The domestic loan portfolio recorded a gross balance of USD 56.07 billion, a USD 1.86 billion or 3.4% increase. The constant growth in the loan portfolio responds mainly to the boost made by the entities in placing productive assets and preferential interest rate housing loans. The foregoing seems to indicate that employment recovery and economic improvement could be encouraging agents to have greater financing.

Regarding the performance of the loan portfolio's external component, it had a year-on-year growth of 28.96%, mainly as a result medium- and long-term projects that require financing from Latin American and Caribbean countries.

Recently, banking assets quality has improved, driven by the economic recovery, the high level of collateral protecting banks' portfolios, as well as their provisioning levels. Specifically, for the National Banking System (NBS), as of May 2022, a delinquency ratio of 4.6% is shown, of which 1.9% represents loans with arrears of 30+ days and 2.7% for loans with arrears of over 90+ days.

The modified [loan] portfolio as of May 2022 totaled USD 5.46 billion, 66% less than that of May 2021. Regarding loans that benefited from the relief program, which are under the modified doubtful and modified loss categories, they were reduced to only 2.1% of domestic gross loans.

At the end of the January – May 2022 period, IBC banks obtained profits of USD 804.8 million. This figure represents a 54.7% increase versus the results obtained in May 2021. The lower deterioration and performance of the loan portfolio income explains the drifting of credit institutions profits. These have also been favored by the better performance of most of the margins and extraordinary income by a banking group and by lower provisioning expenses.

IBC deposits rose by 4.1% compared to May 2021. This difference responds to increases in both domestic and external deposits, having in common that both react significantly to customer deposits growth, both in demand and savings deposits.

It is concluded that given that the Panamanian financial system has continued to show resilience and an overall solid position, it is able to support the pace, scope, and robustness necessary for economic recovery. However, we estimate that provisioning expenses will remain above pre-pandemic levels if banks continue to unwind their exposures to borrowers in the COVID context and the new stress scenarios in Europe and the global monetary policy standardization processes, which requires prudent behavior and careful risk monitoring, which could evolve and lead to new stress scenarios.

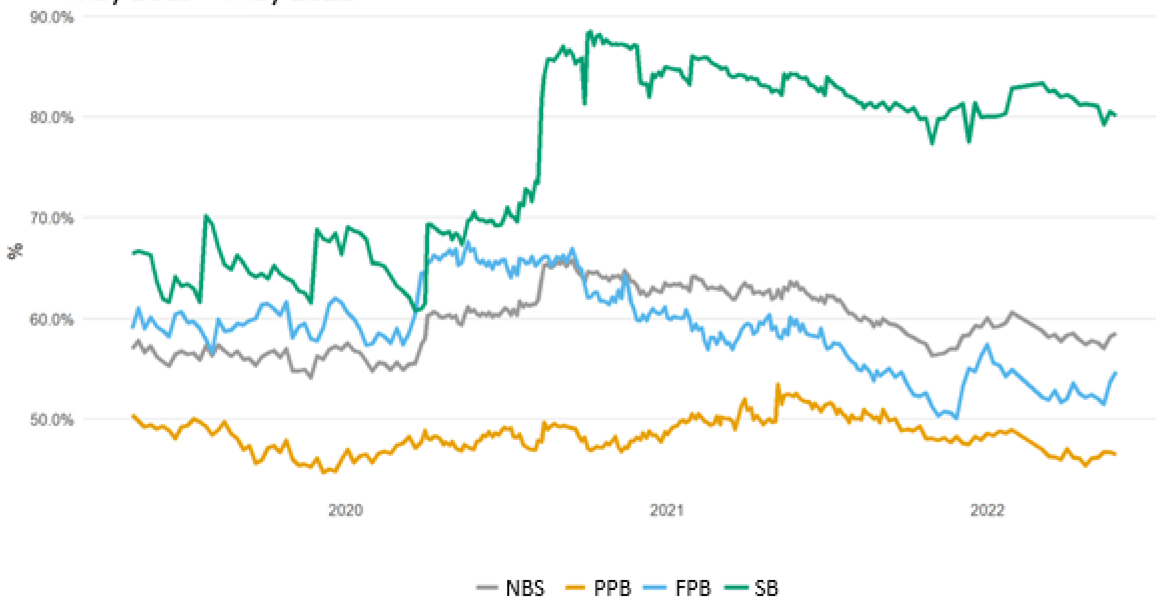
A. Liquidity

As of May 2022, the liquidity of the Banking System reached 58.0%, almost double the regulatory minimum. The domestic banking system has recorded a more well-heeled liquidity position since March 2020 (**see Graph 1**), because of the accumulation of short-term assets in a high uncertainty context, which responds 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 reached in 2021, the financial system maintains adequate liquidity levels at the aggregate level, with sufficient resources to meet its short-term financing needs and which, in turn, will make it easier to resume credit growth. The decreases recorded reflect greater loan disbursement.

Graph 1: Weekly average liquidity ratio

May 2019 – May 2022

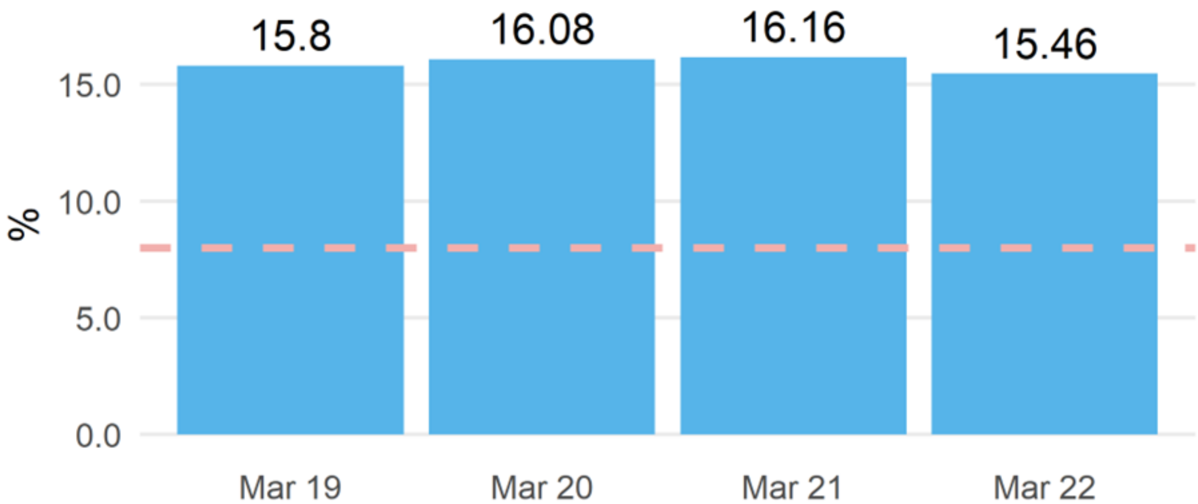


Source: General License Banks

B. Solvency

At the end of the 1Q2022, the International Banking Center's aggregate solvency ratios remained at high levels. The capital adequacy ratio on risk-weighted assets (RWA) was 15.46% at the end of the 1Q2022 (**see Graph 2**), almost double the regulatory minimum of 8%. The capital compliance of the group of banks did not record significant changes with respect to the 4Q2021. Currently, all banks running operations comply with bank capital regulatory standards.

Graph 2: Capital Adequacy Ratio
March 2019 – March 2022



Source: General and International License Banks

C. Income Statement

The banks making up the IBC reported profits for USD 804.8 million during the January – May period. This figure represents a 54.7% increase versus the results of the same period of 2021. The lower deterioration and underperformance of the portfolio income explains the performance of credit institutions. They have also been favored by the better performance of most of the margins, the extraordinary income by a banking group, and the lower provisioning expenses. It should be noted that profits during the period responded significantly to the increase in other income (+37.1%) and net interest income (+13.5%), in its portfolio interest income (+2.4%), deposits income (+10.2%) and securities (+12.6%).

Regarding general expenses, they amounted to USD 1.17 billion, a year-on-year growth of 23.2%. This increase responds in part to digitalization, innovation and sustainability initiatives undertaken by banks, which, although they will save costs, entail high initial investments.

Even though provisions for USD 274.1 million were set, they decreased by 17.0%, when compared with that of May 2021. We estimate that provisioning expenses should remain above pre-pandemic levels, as banks continue to write off exposures to borrowers that were unable to resume payments in the context of COVID-19 and the new stress scenarios in Europe. It should be considered that global monetary policy standardization requires prudent behavior and careful risk monitoring, which could evolve and lead to new stress scenarios.

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

International Banking Center	Jan.-May 2021	Jan.-May 2022	Difference %	Difference USD
Net interest income	928.3	1,053.9	13.5%	125.7
Other income	869.2	1,191.8	37.1%	322.6
Operating income	*1,797.5*	*2,245.8*	*24.9%*	*448.3*
General expenses	*947.2*	*1,166.9*	*23.2%*	*219.6*
Profit before provisions	850.2	1,078.9	26.9%	228.6
Provisioning expenses	330.1	274.1	-17.0%	-56.0
Profit for the period	**520.1**	**804.8**	**54.7%**	**284.7**

Source: General and International License banks.

The National Banking System recorded accumulated net profits, as of May 2022, of USD 605.4 million, 35.3% more than that of May 2021. Like what happened in the IBC, greater credit activity and lower provisioning had a positive impact on the sector's profits.

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

National Banking System	Jan.-May 2021	Jan.-May 2022	Difference %	Difference USD
Net interest income	883.6	986.6	11.7%	103.0
Other income	759.5	965.9	27.2%	206.4
Operating income	*1,643.1*	*1,952.5*	*18.8%*	*309.4*
General expenses	*866.7*	*1,078.1*	*24.4%*	*211.5*
Profit before provisions	776.5	874.4	12.6%	98.0
Provisioning expenses	329.1	269.0	-18.3%	-60.1
Profit for the period	**447.4**	**605.4**	**35.3%**	**158.0**

Source: General license banks.

Banks in the system are expected to continue with cost control and operational efficiency strategies. Currently, IBC efficiency levels are around 52%.

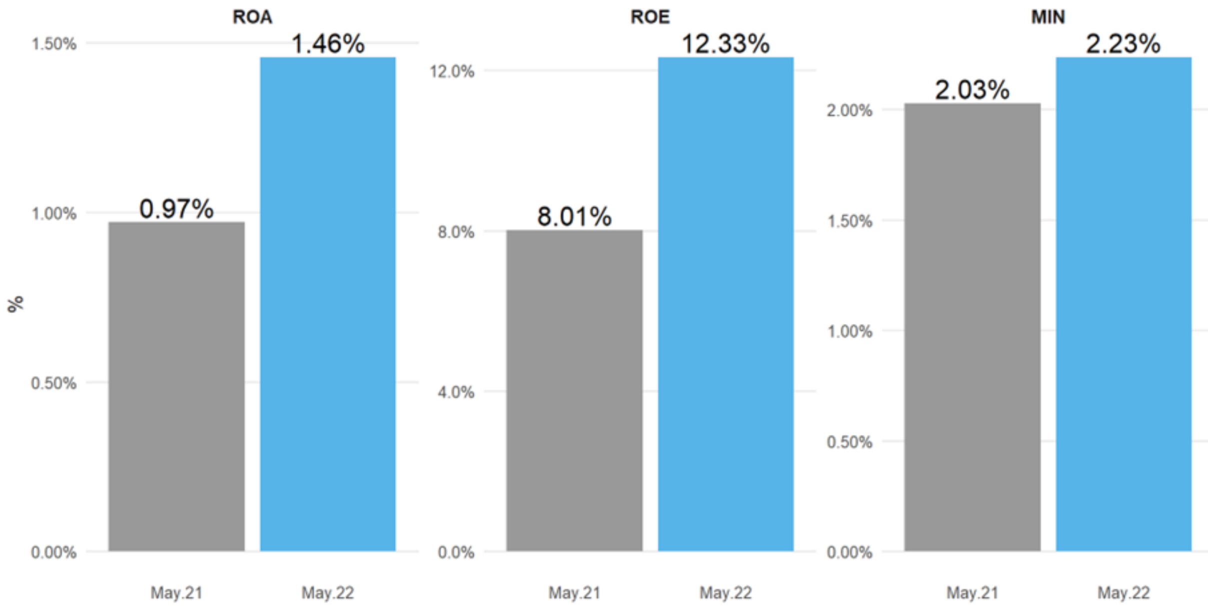
D. Profitability indicators

Regarding profit generation, in 2022, the IBC showed positive and higher profitability indicators versus May 2021 (**see Graph 3**). In the accumulated through May, the total IBC results reached 1.46% (ROA) and 12.33% (ROE); i.e., a 0.49 bp and 4.32 bp growth, respectively. This increase occurred in a context of higher income from financial intermediation and financial services provision, among others.

Although this result is positive, it is noteworthy that it is asymmetrical among credit entities, and there are still challenges to be faced, among which are to finish recognizing the impairment of modified loans, maintaining the capitalization of profits to continue having capital strength, and continuing with the process of phasing out temporary regulatory flexibilities.

Graph 3: Profitability Indicators - IBC

May 2021 – May 2022



Source: General and International License banks

E. Balance Sheet

The assets of the International Banking Center, as of May 2022, totaled USD 136.47 billion, a USD 7.89 billion growth versus May 2021, i.e., a year-on-year increase of 6.13%, which is the result of rises in the net loan portfolio (10.1%) and the securities portfolio (15.9%), which keeps growing, but at a slower pace. On the liquid assets' side, although they fell short (-13.0%), the banking system has high-quality instruments fully available to face stressed financial market conditions.

Regarding the net loan portfolio, the International Banking Center grew 10.1% to reach USD 78.49 billion. The sustained increase in the loan portfolio responds mainly to the boost given by entities to the placement of productive loans and preferential interest rate mortgages. On the performance of the external loan portfolio, it increased by 28.96% on a year-on-year basis, because of medium- and long-term projects that require financing from Latin American and Caribbean countries.

The securities portfolio recorded a year-on-year growth of USD 3.98 billion (15.9%). However, an assessment from December shows a 4.5% growth, explained by the underperformance of the foreign investment portfolio.

During this month, major global stock markets showed devaluations like U.S. bonds throughout the curve, in accordance with the monetary policy rate hikes and the expectation of new hikes in the coming months. Nevertheless, to date, the volatility effects of the financial markets in the investment portfolio are being mitigated by the investment portfolio's short period. However, given that corporate bonds and non-government securities account for a significant share of liquid resources, and could be less liquid in volatile periods, the SBP will be monitoring them closely.

Regarding the sources of bank financing, IBC deposits, as of May 2022, totaled USD 98.35 billion (+4.1%). Since the onset of the coronavirus pandemic in March 2020, deposits have been on an upward trend, which is why banks will continue to be funded mainly by deposits. The banks have solid funding, which gives great stability to their source of financing. 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.

On the other hand, obligations and other liabilities presented increases of 26.9% versus May 2021, respectively. It is worth noting that, although bank deposits are on a record high and are the core component of the loan portfolio, the income collected by these instruments is more focused on investments in physical assets and capital goods, the integration of working capital, the refinancing of liabilities, and the integration of capital contributions in controlled or related ventures.

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

Breakdown	2021	2022	May 22/May 21 Difference	
	May	May	Total	%
Liquid assets	25,368.6	22,086.4	-3,282.2	-12.9%
Net loan portfolio	71,279.5	78,480.9	7,201.4	10.1%
Domestic	*52,163.0*	*53,773.0*	*1,610.0*	*3.1%*
External	*19,116.5*	*24,707.9*	*5,591.4*	*29.2%*
Securities	25,038.4	29,017.0	3,978.6	15.9%
Other assets	6,890.2	6,878.1	-12.1	-0.2%
Total Assets	**128,576.7**	**136,462.4**	**7,885.7**	**6.1%**
Deposits	94,486.3	98,346.1	3,859.8	4.1%
Domestic	*62,220.2*	*62,980.3*	*760.1*	*1.2%*
External	*32,266.2*	*35,365.8*	*3,099.7*	*9.6%*
Obligations	14,748.8	18,712.0	3,963.2	26.9%
Other liabilities	3,755.6	3,658.1	-97.4	-2.6%
Capital	15,586.0	15,746.1	160.1	1.0%

Source: General and International License banks

As for the National Banking System (general license banks only), assets totaled USD 119.58 billion, USD 4.98 billion or 4.53% more than that of May 2021. The net loan portfolio of the National Banking System showed a USD 5.38 billion (8.2%) increase totaling USD 71.24 billion. Net external loans grew 27.5%, while the domestic portfolio had a performance of

3.1%. On the other hand, total deposits placed in the NBS totaled USD 85.38 billion, a 1.3% rise, which is mainly the result of customer deposits.

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

Breakdown	2021	2022	May 22/May 21 Difference	
	May	May	Total	%
Liquid assets	20,710.7	17,781.7	-2,929.0	-14.1%
Net loan portfolio	65,859.5	71,239.2	5,379.7	8.2%
Domestic	*52,163.0*	*53,775.6*	*1,612.6*	*3.1%*
External	*13,696.5*	*17,463.6*	*3,767.0*	*27.5%*
Securities	21,364.8	24,038.7	2,673.9	12.5%
Other assets	6,659.3	6,515.8	-143.5	-2.2%
Total Assets	**114,594.3**	**119,575.3**	**4,981.0**	**4.3%**
Deposits	84,278.4	85,376.0	1,097.6	1.3%
Domestic	*62,134.4*	*62,799.7*	*665.3*	*1.1%*
External	*22,144.0*	*22,576.3*	*432.3*	*2.0%*
Obligations	14,550.3	18,587.5	4,037.3	27.7%
Other liabilities	3,600.1	3,465.7	-134.4	-3.7%
Capital	12,165.6	12,146.1	-19.5	-0.2%

Source: General License banks

F. Loans

As of May 2022, the domestic loan portfolio amounted to USD 56.07 billion, a USD 1.86 billion or 3.4% increase. Regarding its performance, it should be noted that all productive activities showed better performances, except for loans to Financial Activities (-0.8%), Mining and quarrying (-8.4%), and Construction (-7.3%).

The household loan portfolio, made up of mortgages (+4.9%) and personal consumption (+4.3%), continues to show a positive performance in its different segments. Regarding the household portfolio, it maintained its performance, leveraged significantly by the preferential interest segment that grew 11.9%. Regarding consumer loans granted by commercial banks, it recorded a rise in almost all its segments, except for the automotive segment (that, even though it grew 1.1%, has been slowing down), which continues to be affected by global supply chains bottlenecks.

The performance of the household portfolio seems to indicate that employment recovery and higher economic growth could be encouraging agents to have more financing.

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

Sector	May 2021	May 2022	May 22/May 21 Difference	
			Total	%
TOTAL	**54,208**	**56,064**	**1,856**	**3.4%**
Public sector	**1,422**	**1,472**	**50**	**3.5%**
Private sector	**52,786**	**54,593**	**1,806**	**3.4%**
Financial & insurance activities	1,312	1,302	-11	-0.8%
Agriculture	406	454	47	11.7%
Livestock	1,349	1,387	38	2.8%
Fishing	82	88	6	7.7%
Mining & Quarrying	57	52	-5	-8.4%
Commerce	10,660	11,025	365	3.4%
Industry	2,702	3,038	336	12.4%
Mortgages	18,228	19,126	898	4.9%
Construction	5,557	5,154	-403	-7.3%
Personal consumption	12,434	12,968	534	4.3%

Source: General License banks

As of May 2022, the sectors that show the greatest growth are financing under credit lines granted by banks to the public sector for construction, the other important segment in May was loans granted between financial entities. On the other hand, consumer portfolio continues to provide new credit cards and personal and car loans.

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

Sectors	Jan.-May	Jan.-May	Jan.-May 21/22 Difference	
	2021	2022	Total	%
Public entity	**79.6**	**410.3**	**330.7**	**415.3%**
Financial companies	**266.0**	**531.9**	**265.9**	**100.0%**
Agriculture (incl. forestry)	65.6	116.8	51.3	78.2%
Livestock	210.3	287.6	77.4	36.8%
Fishing	11.7	10.6	-1.2	-9.8%
Mining & Quarrying	5.1	9.3	4.2	81.9%
Commerce (incl. Services)	2,514.7	4,220.9	-1,706.2	-67.9%
Industry	815.7	925.1	109.4	13.4%
Mortgages	635.6	810.2	174.6	27.5%
Construction	391.3	573.7	182.4	46.6%
Personal consumption	730.9	900.4	169.6	23.2%
TOTAL	**5,726.3**	**8,796.8**	**3,070.5**	**53.6%**

Source: General License banks

Graph 4: New Loans
May 2018 – May. 2022

Source: General License Banks

G. Performance of the Modified Portfolio of the National Banking System

After reaching the zenith, modified loans have gradually declined as borrowers steadily resume honoring their loans. The modified [loan] portfolio as of May is USD 5.46 billion, 66% less than that of May 2021.

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 the 1Q2022, the portfolios that could entail the greatest risk would be the modified doubtful and modified loss that altogether amount to USD 1.21 billion. All these performances are linked to the improvement in monthly installments, however, the portfolio classified in this category is still higher and could entail greater provisioning. Nevertheless, banks have increased loan-impairment reserves, which together with high collateral coverage will help absorb losses for borrowers who have not fully recovered their payment capacity.

Table 7
Modified loans of the National Banking System by Economic Activity
(in millions of USD)

Sectors	2021 May	2022 May	Total Diff.	% Diff.
Mortgages	7,106	2,638	-4,468	-63%
Consumer	3,088	1,323	-1,765	-57%
Construction	2,149	571	-1,578	-73%
Services	2,028	547	-1,482	-73%

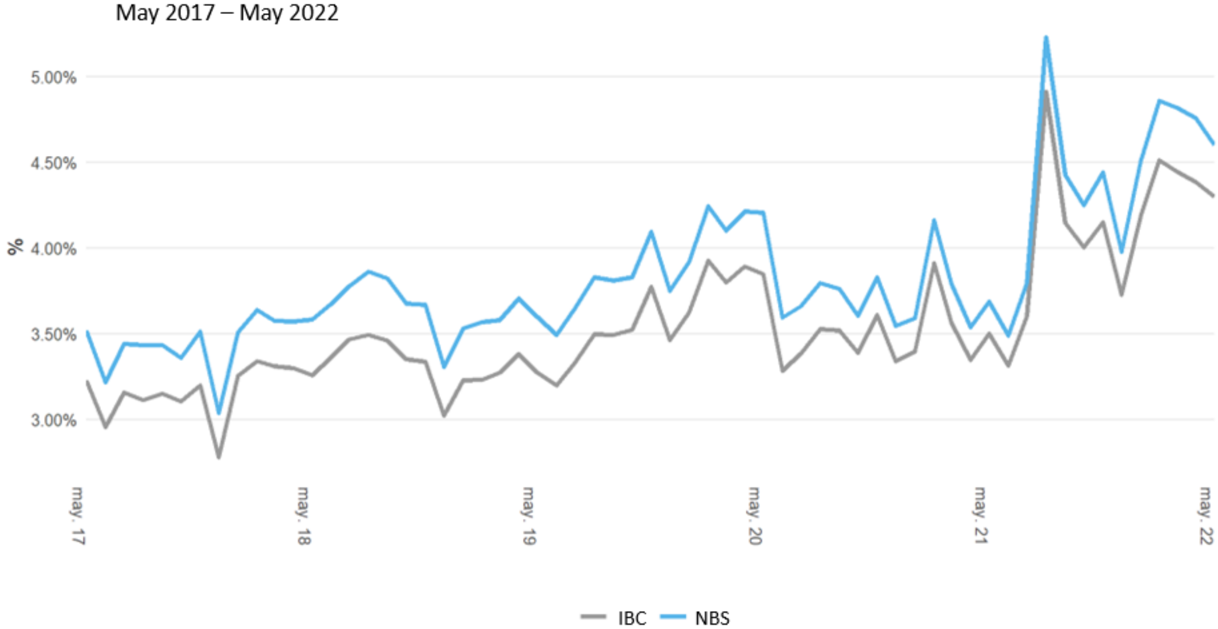
Sectors	2021 May	2022 May	Total Diff.	% Diff.
Commerce	955	207	-749	-78%
Industry	199	65	-134	-67%
Others	329	104	-225	-68%
Total	**15,854**	**5,455**	**-10,399**	**-66%**

Source: General License Banks

H. Credit Risk

Recently, asset quality has shown an improvement driven by the economic recovery, the high level of collateral protecting banks' portfolios, and their reserves level. In the case of the NBS, as of May 2022, it shows a delinquency ratio of 4.6%, of which 1.9% represents loans with arrears of 30+ days and 2.7% for loans with arrears of over 90+ days.

Graph 5: Portfolio Quality
May 2017 – May 2022



Source: General License Banks

On the other hand, and breaking down the delinquency of the portfolio by its main activities, a similar trend is observed over the surveyed periods that comprise May 2020 to May 2022. For the months between June and August 2021, an increase is seen in terms of portfolio quality ratio, in part this was due to the application of Article 4 of Rule 2-2021, which dictates the general conditions to restore modified loans according to Rule 4-2013.

For the Household sector, made up of Mortgages and Personal Consumption, as of the end of May 2022, the delinquency ratio is 7.7% and 6.8%, respectively. While for Agricultural activities, the delinquency is 8.9%; Construction has also been one of the most affected sectors during this period, its current delinquency is at 5.9%; meanwhile, Commerce has a default rate of 3.6%.

I. Deposits

As of May 2022, the deposits of the International Banking Center rose to 4.1% versus May 2021. This difference results from an increase in both domestic and external deposits, having in common that both respond significantly to the growth of customer demand and savings deposits. Such performance shows that domestic and external institutional depositors trust the strength of the IBC banks and the country's macroeconomic stability despite going through complicated times. The deposits placed in the market, as of May 2022, recorded a total of USD 98.35 billion, USD 3.86 billion more than that of May 2021 (**see Table 8**). If the analysis is focused on domestic deposits, an increase was recorded as of May 2022, reaching USD 62.98 billion, a 1.2% growth versus May 2021.

On the other hand, external deposits recorded an increase of USD 3.1 billion, amounting to USD 35.37 billion. In nominal terms, the largest deposits growth corresponding to May 2022 vs. 2021 come from Colombia, Peru, Chile. 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)

IBC	2021	2022	May 22 / May 21 Diff.	
	May	May	Total	%
Total Deposits	**94,486**	**98,346**	**3,860**	**4.1%**
Domestic	**62,220**	**62,980**	**760**	**1.2%**
Government	11,552	12,018	465	4.0%
Customer	46,798	47,716	918	2.0%
Banks	3,870	3,247	-623	-16.1%
External	**32,266**	**35,366**	**3,100**	**9.6%**
Government	132	467	335	253.6%
Customer	24,825	27,799	2,973	12.0%
Banks	3,823	5,278	1,455	38.0%

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 85.38 billion, a 1.3% increase versus May 2021, driven by domestic and external deposits (**see Table 9**).

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

NBS	2021	2022	May 22 / May 21 Diff.	
	May	May	Total	May
Total Deposits	**84,278**	**85,376**	**1,098**	**1.3%**
Domestic	**62,134**	**62,800**	**665**	**1.1%**
Government	11,552	12,018	465	4.0%
Customer	46,798	47,716	918	2.0%

NBS	2021	2022	May 22 / May 21 Diff.	
	May	May	Total	May
Banks	3,784	3,066	-718	-19.0%
External	**22,144**	**22,576**	**432**	**1.95%**
Government	132	465	333	252.1%
Customer	15,292	15,499	208	1.4%
Banks	6,720	6,611	-108	-1.61%

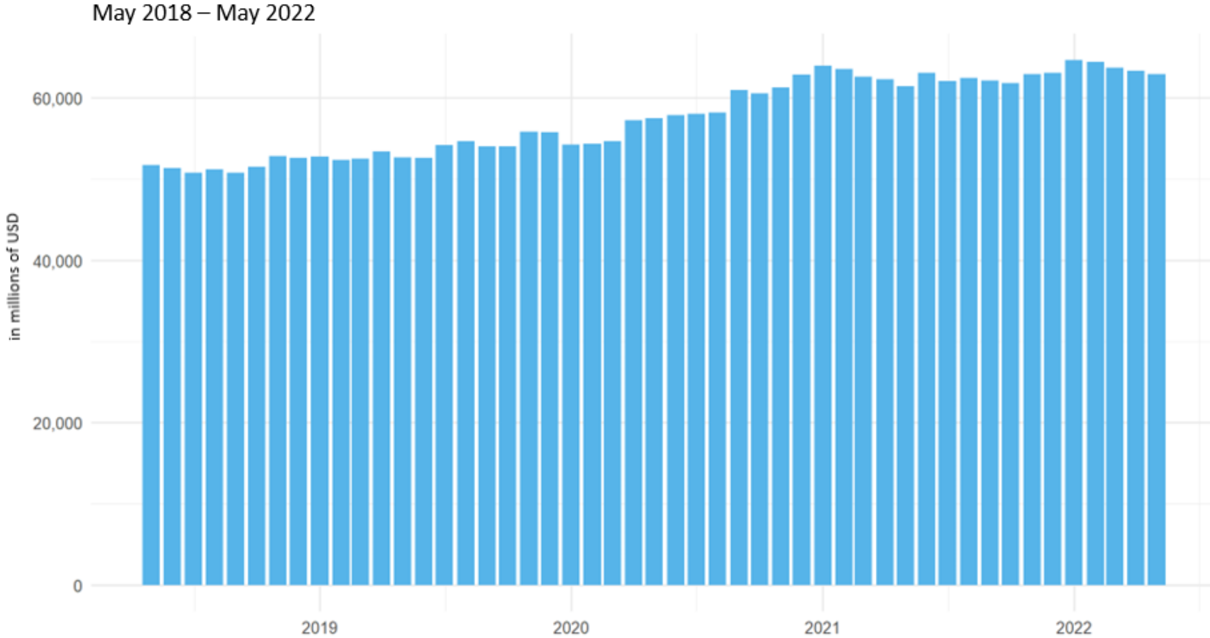
Source: General License banks.

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

It should be remarked that the domestic deposits of the National Banking System account for 74% 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 6** shows the evolution of domestic deposit balances.

Graph 6: Total Domestic Deposits

May 2018 – May 2022



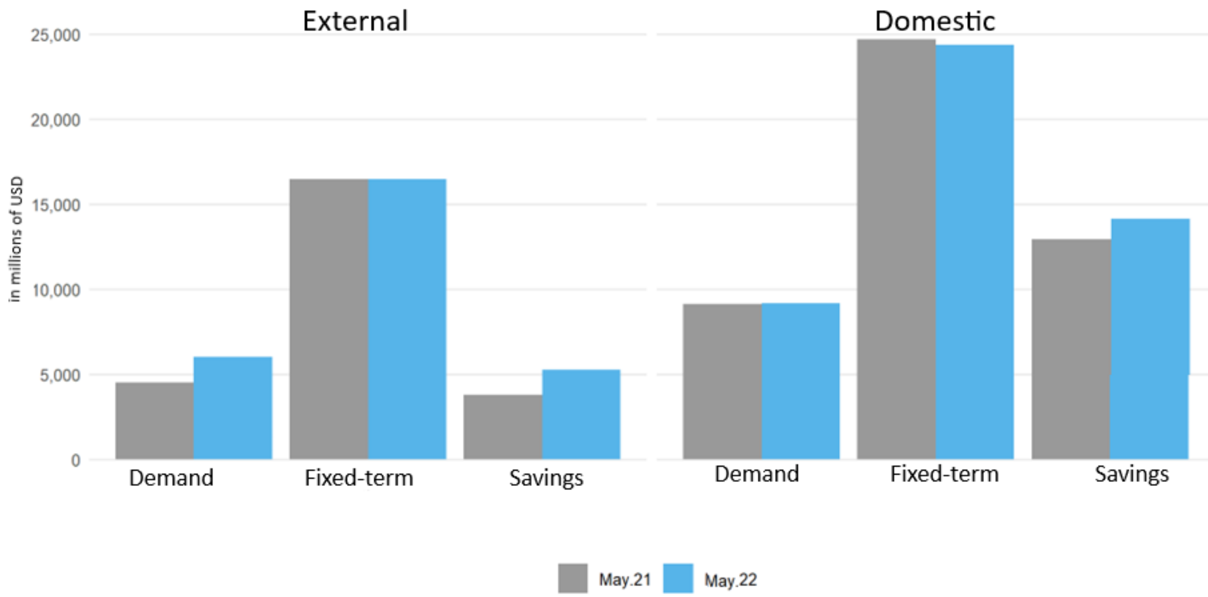
Source: General license banks.

Regarding the structure of domestic and external customer liabilities by maturity, fixed-term deposits continue to be the most important savings instrument. In the Banking Center, as of May 2022, domestic customer fixed-term deposits amounted to USD 24.40 billion, followed by savings rising to USD 14.15 billion, and demand deposits totaling USD 9.19 billion.

Graph 7: Customer Deposits

Graph 7: Customer Deposits

May 2021 –May 2022



Source: General and International license banks.

Domestic customer deposits kept in the financial system increased during the surveyed period, as follows: demand deposits (+0.81%) and savings deposits (+9.40%). 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. The reactivation of economic activity, which favored a greater flow of income from the sale of goods and services, as well as the substitution of part of term resources and their placement as savings, with immediate availability, could explain the increase observed in the performance of demand deposits.

The growth of fixed-term deposits has lost momentum. Although until a few months ago the reported balances had grown, in May 2022 customers fixed-term deposits showed a decrease. It should be noted that the performance observed in fixed-term deposits, as in any market, is related to the expectation of interest rate hikes. The underperformance of these financial investment instruments is consistent with the higher risk aversion, the start of an interest rate hikes cycle that reduces earnings expectations for this type of instruments in the short-term, and financial investment alternatives that could be more attractive. When there is an expectation that rates are going to rise, it is common for savers to leave their money [deposited] in the short-term. In this way, they would have capital available to invest when the increase in yields occurs and thus agree on best-rated operations.

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