TRANSLATION

Superintendencia de Bancos de Panamá

Financial Studies Division

Banking Activity Report

November 2019

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I. Domestic Economic Environment

A. Monthly Economic Activity Index (MEAI)

At the beginning of the fourth quarter of 2019, domestic economic activity maintained a moderate growth trend consistent with the outlook to this date. The Monthly Economic Activity Index (MEAI) for the Republic grew 3.3% from January to October[1] 2019 compared to the same period in 2018. The annual difference through October 2019 registered 3.4% compared to the figure for 2018.

The economic activities that have had a positive performance are trade; transportation, storage and telecommunications; public administration; financial intermediation; agriculture; construction; utilities (water and electricity); household services; and mining and quarrying.

Transportation and telecommunications had favorable performances thanks to the expanded Panama Canal and the container movement (in TEUs) in the National Port System. **It is noteworthy that, for the Panama Canal, the Liquid Gas Transportation segment has grown consistently in the almost two years since the inauguration of the waterway expansion, which has positioned the Panama Canal as an important link in the global NLG supply chain.**

The agriculture sector grew in cattle raising and banana for export. Utilities (water and electricity supply) had a great performance due to greater thermal energy generation from natural gas.

Trade registered positive results thanks to domestic wholesaling and retailing.

B. Consumer Price Index (CPI)

The Consumer Price Index (CPI) published by the Comptroller General indicates that the accumulated inflation from January to November 2019 was 0.3% lower than in 2018. As a result, the accumulated Domestic Urban CPI from January to November registered a difference of -4%.

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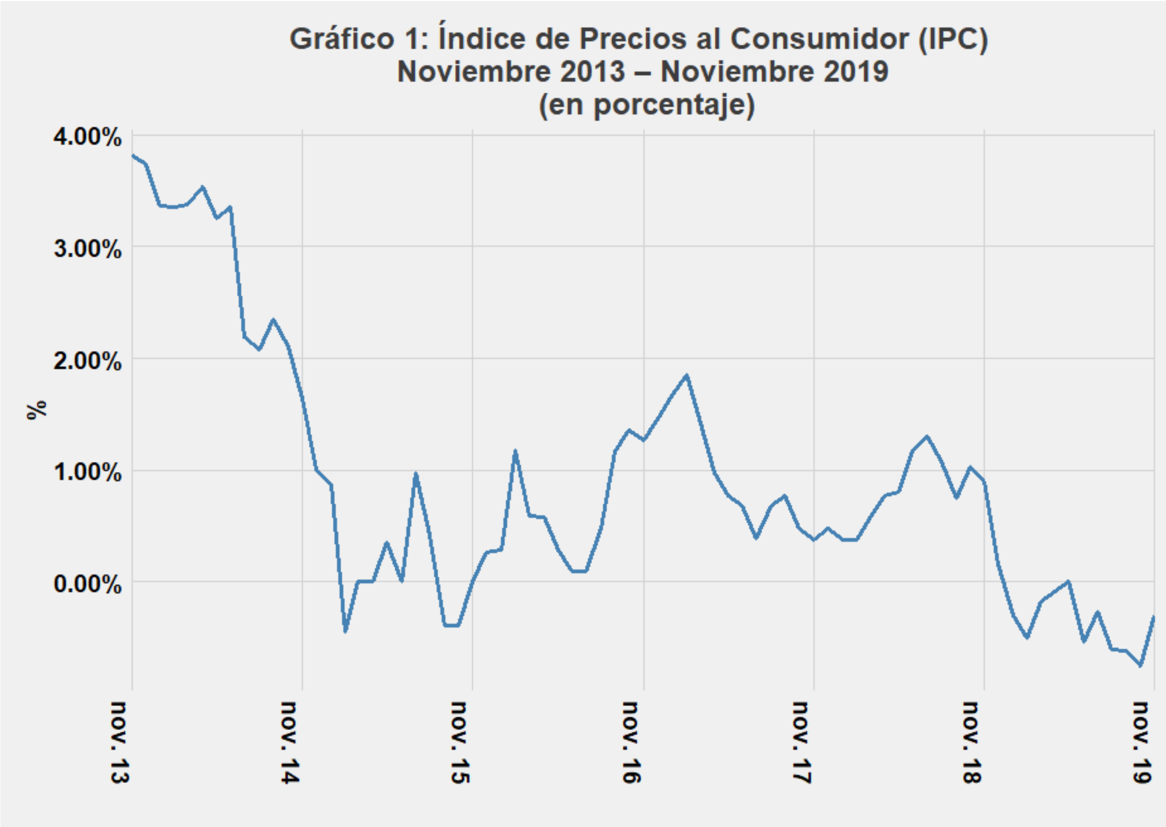
[1] Data through November has not been released as of the date of this report. This data will be updated as soon as the official sources make them available.



Source: SBP with NISC data.

The IPC for November 2019, compared to November 2018, showed decreases in Transportation (-1.6%); Telecommunications (-1.2%); Furniture, home appliances and household maintenance (-1.1%); Clothing and footwear and Entertainment and culture (both at -0.4%); and Alcoholic beverages and tobacco (-0.2%). Housing, Utilities (water, electricity and gas) and Miscellaneous goods and services remained unchanged.

On the other hand, increases were registered in Restaurants and hotels (1.3%); Healthcare (0.9%); and Education (0.7%). The CPI for November did not differ from that of October 2019. The groups that registered decreases were: Food and non-alcoholic beverages (down 0.5%); Alcoholic beverages and tobacco (-0.4%); Healthcare and Miscellaneous goods and services (both at -0.2%); Telecommunications and Entertainment and culture (both at 0.1%). Increases were registered in Transportation (0.7%); Furniture, home appliances and household maintenance and Restaurants and hotels (both at 0.1%).

II. International Banking Center

The performance of the Banking Center is still showing a stable financial footing. It maintained a moderate growth as a result of a less favorable external financial context and a moderate domestic economic growth.

As of November 2019, the net profit for the Banking Center showed the same level as that of 2018, with a 0.2% increase. **Financial efficiency levels registered 1.9 times income vs. expenses.**

At the same time, in November 2019 the International Banking Center had **assets totaling USD 124.08 billion, a 2.9% increase or USD 3.48 billion more than was reported at the end of November 2018. For the National Banking System (NBS), assets totaled USD 107.27 billion, a 3.7% growth.**

Total deposits registered USD 87.25 billion, a 5.5% growth. The IBC's domestic deposits increased 5.7%, USD 3.03 billion over November 2018. For its part, foreign deposits increased 5.0%. A substantial part of this performance comes from an increase in official deposits, as a result of accounting registries of foreign funding received by the Central Government. Although the increase in deposits has a positive impact in the Banking Center's balance sheet, it also produces a negative impact on the financial margin that is not recurrent. This is due to the fact that the greater growth of total deposits came from an increase in liquid allocations from state-owned banks.

Analyzing IBC operations, it is noteworthy that the domestic loan portfolio has been growing at a moderate pace of 2% throughout 2019. The investments portfolio grew USD 1.21 billion, mainly because of the performance of its foreign component, which was mostly in US and Latin American bonds.

A. Balance Sheet and Profit Statement

Table 1: International Banking Center
Balance Sheet
(in millions of USD)

International Banking Center	2018	2019	Nov. 19/Nov. 18 Difference	
	November	November	Total	%
Liquid assets	16,413	19,230	2,817	17.2%
Loan portfolio	77,933	76,591	-1,342	-1.7%
Domestic loan portfolio	53,588	54,566	978	1.8%
Foreign loan portfolio	24,345	22,025	-2,319	-9.5%
Securities investment	21,462	22,672	1,210	5.6%
Other assets	4,796	5,581	786	16.4%
Total Assets	**120,604**	**124,074**	**3,470**	**2.9%**
Deposits	82,729	87,241	4,512	5.5%
Domestic deposits	52,935	55,961	3,026	5.7%
Foreign deposits	29,794	31,281	1,486	5.0%
Obligations	19,586	16,633	-2,953	-15.1%
Other liabilities	3,599	4,035	437	12.1%
Equity	14,690	16,165	1,475	10.0%

Source: General and international license banks.

We emphasize the increase in Equity for the IBC and NBS of 10.0% and 9.7%, respectively. This improves the capability of the banks' own equity to face unforeseen risks.

As of November 2019, the balance sheet for the National Banking System (general license banks only) has assets totaling USD 107.27 billion, a 3.7% growth.

The domestic loan portfolio, as mentioned above, registered increases, while the foreign [loan portfolio] registered a decrease which has resulted in a lower performance in the portfolio as a whole.

Total deposits registered USD 75.96 billion, a 4.7% increase. For its part, liabilities totaled USD 14.51 billion, 7.7% less than that of the same period in 2018, including loans greater than 186 days and securitizations. This behavior occurs as a contrast to higher growth in deposits allocations, which means that banks are returning to traditional methods of obtaining funds.

Table 2: National Banking System
Balance Sheet
(in millions of USD)

National Banking System	2018 November	2019 November	Nov. 19/Nov. 18 Difference Total	November
Liquid assets	12,229	14,019	1,790	14.6%
Loan portfolio	68,110	68,560	450	0.7%
Domestic loan portfolio	53,588	54,566	978	1.8%
Foreign loan portfolio	14,522	13,994	-527.9	-3.6%
Securities investment	18,592	19,354	762	4.1%
Other assets	4,469	5,336	867	19.4%
Total Assets	**103,401**	**107,269**	**3,869**	**3.7%**
Deposits	72,539	75,952	3,413	4.7%
Domestic deposits	52,879	55,843	2,964	5.6%
Foreign deposits	19,661	20,108	448	2.3%
Obligations	15,718	14,510	-1,207	-7.7%
Other liabilities	3,304	3,822	518	15.7%
Equity	11,839	12,985	1,146	9.7%

Source: General license banks.

The profit of the International Banking Center totaled USD 1.68 billion, a 0.2% growth.

Table 3: International Banking Center
Profit Statement
(in millions of USD)

International Banking Center	Nov. 18	Nov. 19	12-month diff.	Total diff.
Net interest income	2,555	2,545	-0.4%	-10
Other income	2,012	1,977	-1.7%	-35
Operating income	4,566	4,522	-1.0%	-44
General expenses	2,345	2,329	-0.7%	-16
Profit before provisions	2,221	2,193	-1.3%	-28
Provisions for bad debt	552	521	-5.7%	-31
Income for the period	1,669	1,672	0.2%	3

Source: General and international license banks.

The income obtained from financial assets as of November increased by 6.1%. However, paid interest showed a 12.8% increase through November, almost twice the increase in interest income. An important part of this performance in paid interest is due to greater official deposits, which meant a 25% increase in interest paid by state-owned banks. As this operation is short-term, the increase in liabilities was placed as a less profitable liquid asset.

In addition, the “Other income” item did not create a backstop this year, as it showed a decrease of 17%, affected by decreases in Dividends from Private Banking.

For its part, the Banking System showed a decrease in revenue, based in part by the above. Profitability decreased 2.8% compared to the same period in 2018. It is worth noting that the reduction in dividend income was from private banks.

Table 4: National Banking System
Profit Statement
(in millions of USD)

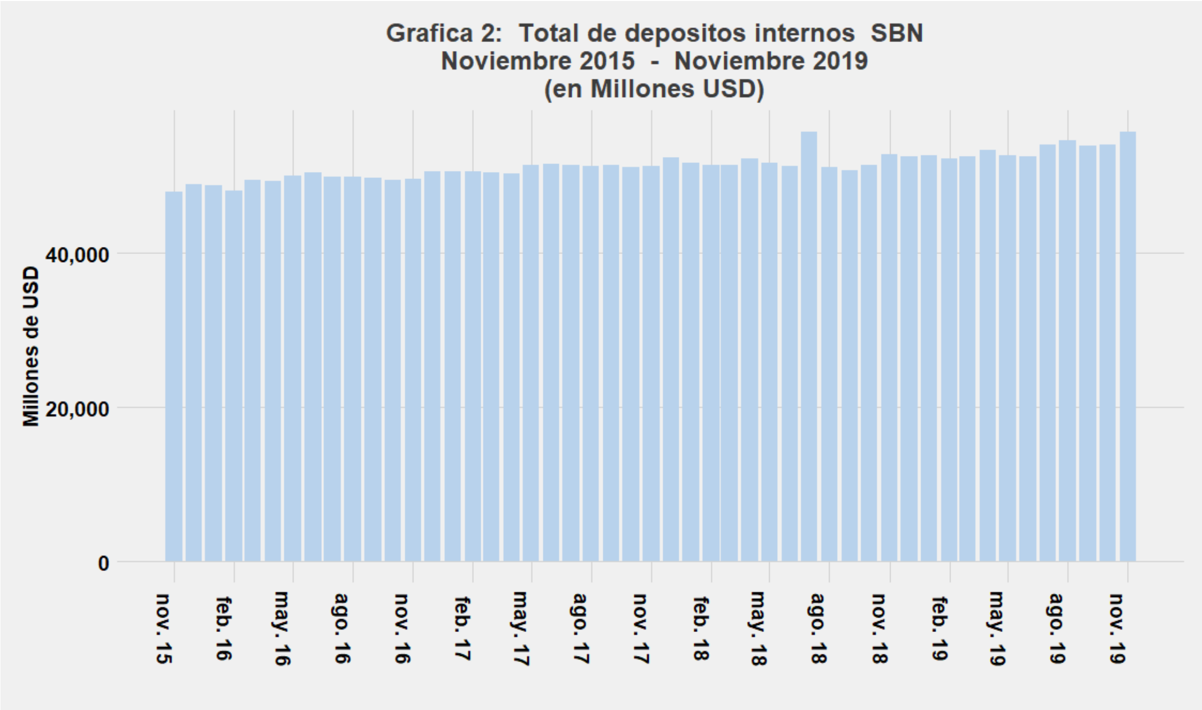
National Banking System	Nov. 18	Nov. 19	12-month diff.	Total diff.
Net interest income	2,311	2,329	0.78%	18
Other income	1,708	1,665	-2.52%	-43
Operating income	4,019	3,994	-0.62%	-25
General expenses	2,122	2,165	2.04%	43
Profit before provisions	1,896	1,828	-3.60%	-68
Provisions for bad debt	551	520	-5.61%	-31
Income for the period	1,345	1,308	-2.77%	-37

Source: General license banks.

B. Deposits

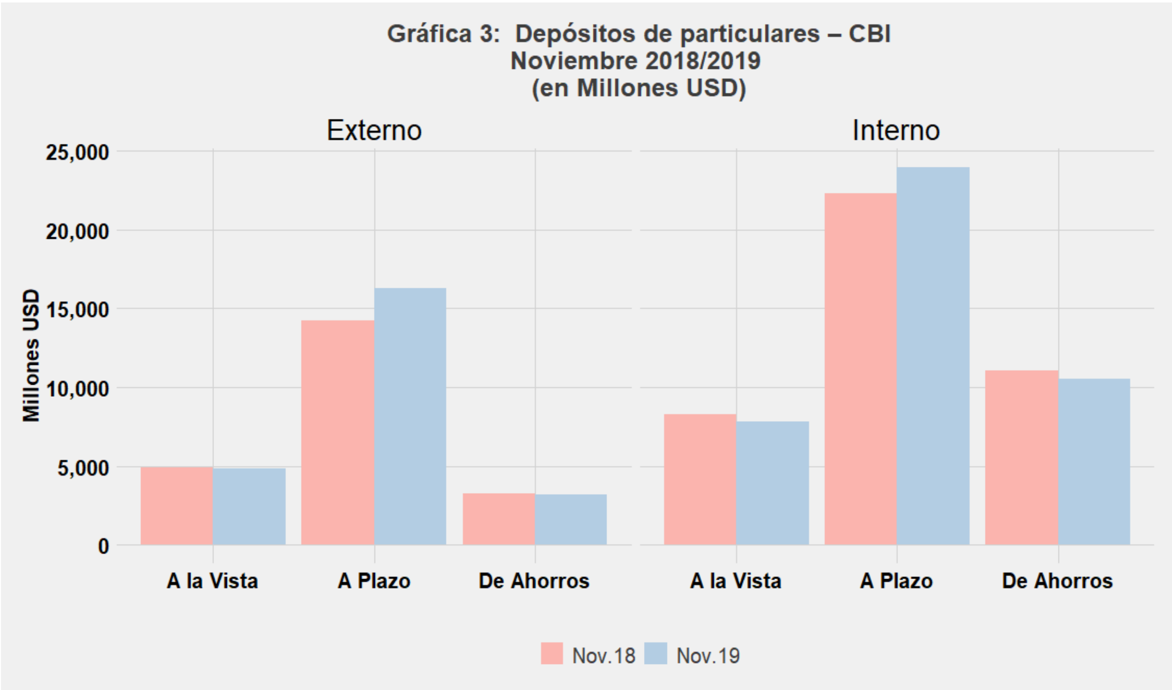
Domestic deposits in the International Banking Center showed an increase of 5.7%, i.e. USD 3.03 billion over November 2018, while foreign deposits grew 5.0%.

Domestic deposits in the National Banking System represent 73.5% of total System deposits. Chart 4 shows the annual evolution of the balance of domestic deposits.



Source: General license banks.

As of November, private domestic deposits increased 1.7%, driven by a 7.4% increase in time deposits, while savings accounts decreased by 4.8% (due to the withdrawal of Christmas savings and other savings), and demand deposits decreased 5.3%.



Source: General and international license banks.

C. Loans

Domestic loans to the private sector showed a 2.5% growth vs. the same period of 2018. The sectors driving domestic loan [performance] are related to retail banking, especially mortgages (5.0%) and personal loans (5.7%).

Table 5: National Banking System
Domestic loan portfolio by sectors and activities
(in millions of USD)

Sector	2018	2019	Nov. 19/Nov. 18 Diff.	Nov. 19/Nov. 18 Diff.
	November	November	Total	%
TOTAL	**54,626**	**55,723**	**1,097**	**2.0%**
Public sector	**1,060**	**813**	**-247**	**-23.3%**
Private sector	**53,566**	**54,910**	**1,344**	**2.5%**
Finance & insurance activities	1,373	1,649	276	20.1%
Agriculture	468	408	-60	-12.8%
Livestock	1,312	1,338	26	2.0%
Fishing	89	83	-6	-6.7%
Mining & quarrying	33	55	22	66.7%
Commerce	11,595	11,508	-87	-0.8%
Industry	3,309	3,225	-84	-2.5%
Mortgages	16,868	17,716	848	5.0%
Construction	6,567	6,381	-186	-2.8%
Personal consumption	11,952	12,546	594	5.0%

Source: General license banks.

1. Mortgage portfolio

For banking, mortgages are still showing positive results by reaching a 5.0% increase compared to November 2018, which is equal to USD 848 million, and remain one of the activities that contributes the most to domestic loan portfolio growth.

Residential mortgages as a whole registered a total of USD 15.79 billion, a 6.4% annual growth. This is a reflection of the important stock of residential projects, which is still available through mortgage financing. It is noteworthy that preferential interest mortgages are the ones driving results. As of November 2019, this component totaled USD 6.11 billion, a USD 958 million growth (18.6% from November 2018-19).

Table 6: National Banking System
Mortgages
(in millions of USD)

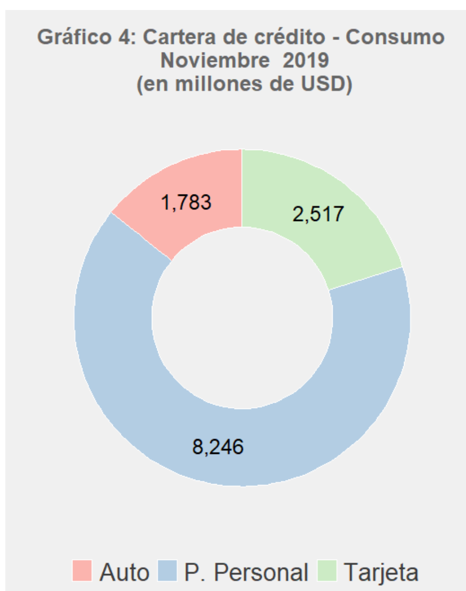
	Main Residence		Second home mortgages	Mortgage loans
	Preferential	Non-preferential		
Nov. 15	3,892	6,810	585	11,287
Nov. 16	4,079	7,826	775	12,679
Nov. 17	4,672	8,444	856	13,971
Nov. 18	5,151	8,710	969	14,830
Nov. 19	6,109	8,620	1,055	15,784

Source: General license banks.

2. Personal consumption portfolio

The domestic consumption portfolio (credit cards, personal loans and cars) represents 23% of the total domestic private portfolio, which is key to loan growth with 5.0% or USD 595 million in total values as of November 2019.

The Personal consumption portfolio consists mainly of personal loans, which represent 86% [of the total] and include credit cards. Car loans represent the remaining 14%.



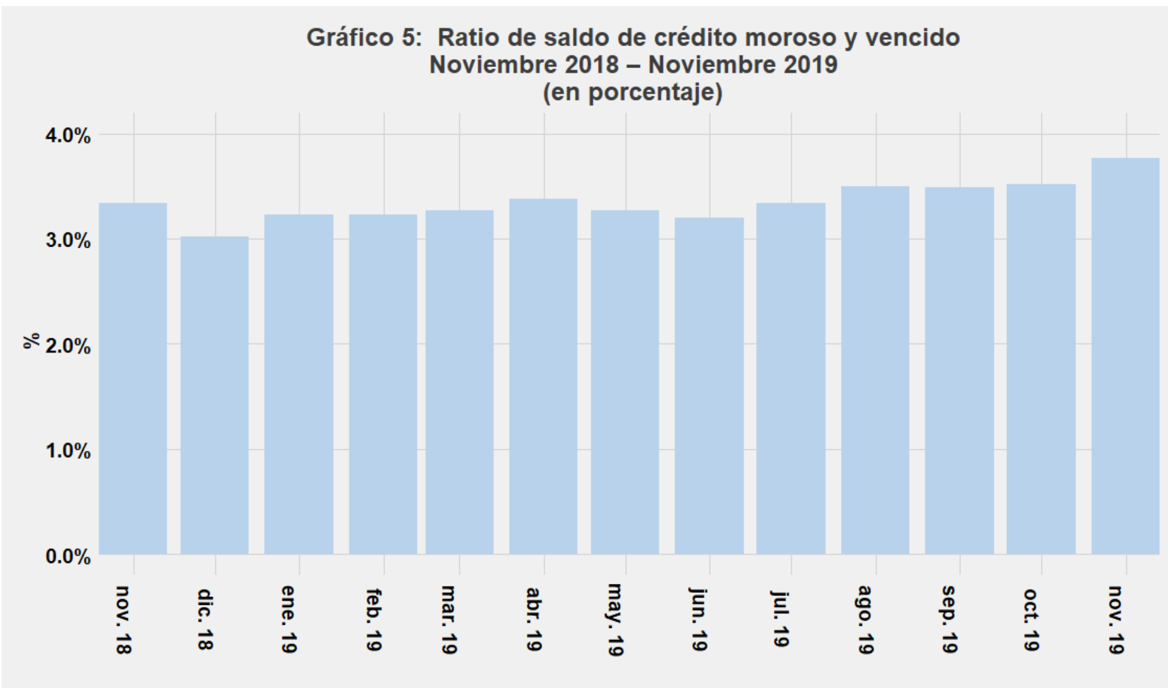
Source: General license banks.

3. Commercial portfolio

The commercial portfolio showed a 0.7% growth or USD 87 million; loans to the Free Trade Zone still show a negative trend compared to the same period in 2018.

D. Portfolio quality

As for the quality of the International Banking Center portfolio, its past due balance was 1.9% (30 – 90 days), while nonperforming loans were 1.8% (over 90 days). [These figures are] still within the lowest in the region.



Source: General license banks.

The regulatory framework requires banks to exhaustively analyze the cash flow capacity of debtors and to take prudential actions to create specific reserves showing the real value of loan performance.

As is known, banks require real collateral in their loan management process to mitigate potential impairments in loan exposure. **Data as of November 2019 show increases in accounting provisioning to equal provision levels of USD 1.42 billion, i.e. a USD 91 million or 6.9% growth compared to the same period in 2018.** This shows the banks' conservative management in covering loan exposure operations (IFRS 9).

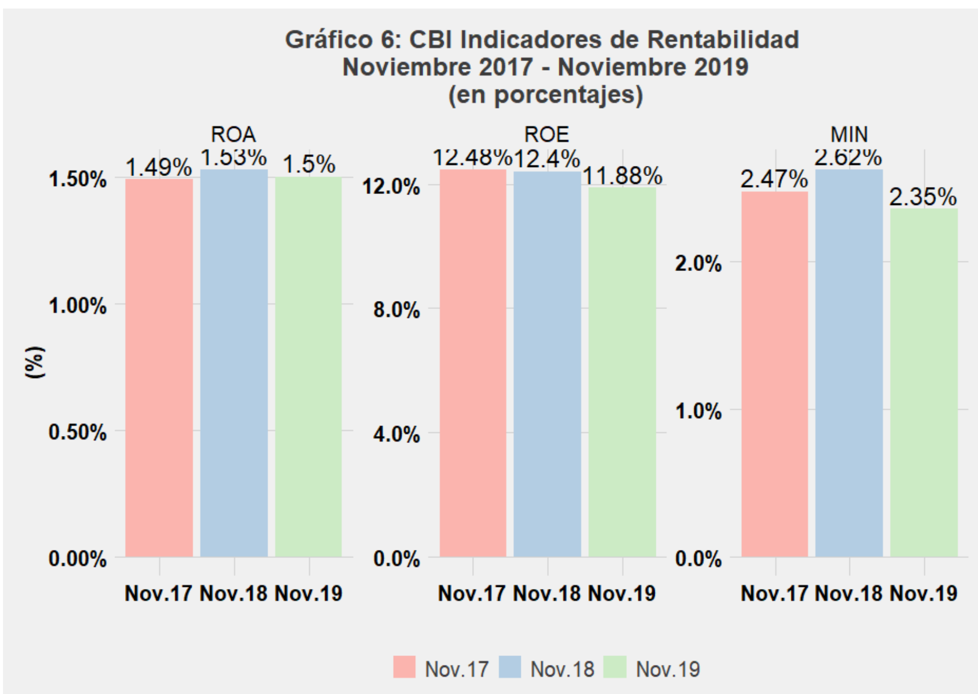
As of 2012, the reporting of financial statements by banks in the Banking Center must use IFRS criteria. Therefore, in addition to calculating the regulatory provisions under Rule 4-2013, they must also calculate provisions under IFRS. Should there be a difference in favor of regulatory provisions, this difference must be shown as Equity Reserve.

IFRS 9, current since January 2018, introduced a significant change for the calculation of provisions. Unlike IAS39, which was based on incurred losses (objective evidence of deterioration), IFRS 9 establishes that provisions must be calculated on the expected losses that operations may present.

On the other hand, dynamic provisions were created on the increase of all loans lacking assigned specific provisions, i.e. on loans classified as normal.

E. Profitability indicators

The return on assets (ROA) for the International Banking Center registered 1.5% as of November 2019, while the same indicator for the National Banking System (general license banks only) registered 1.36%

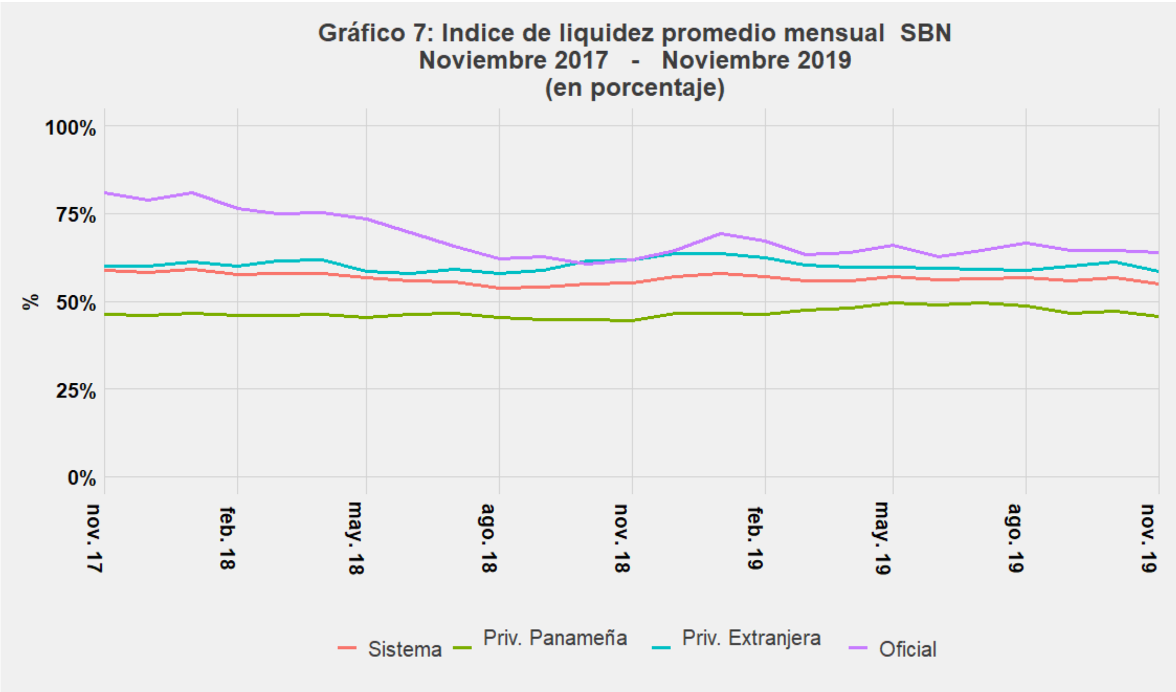


Source: General and international license banks.

Benefits have evolved hand in hand with profitability on equity (ROE) in the International Banking Center. The ROE – which measures the return to shareholders for each dollar invested – registered 11.88% for the IBC. It is worth noting that both indicators have been showing consistent improvements and show, in a complementary manner, that earnings have a positive performance.

F. Liquidity

As of November 2019, the monthly average liquidity ratio was 62.74% for the IBC, almost double what is legally required. For the National Banking System (general license banks only), the liquidity ratio was 54.9%. By type of banking, the average was 63.9% for state-owned banks, 58.5% for foreign banks, and 45.7% for Panamanian banks. The strong liquidity position should permit banks to face short- and medium-term maturities comfortably. The sensitivity analysis, through liquidity stress-testing, suggests that the Panamanian Banking System currently has rapidly convertible cash assets. This test resulted in banks maintaining liquidity levels higher than those required by regulation, even in restrictive scenarios. It is noteworthy that greater total deposits growth benefit the liquidity conditions of the financial system.



Source: General license banks.

G. Solvency:

The latest solvency ratios show equity soundness reflecting 16.65%, far above the legally required percentage. The particular solvency ratio for the banking industry shows the banks' capacity to face unexpected losses (the minimum required by law for the country is 8%, the same requirement established by Basel III).

Panamanian banking has made important progress as a result of the above-mentioned Rules, and includes elements such as the definition of basic capital (tier one) and additional capital (tier two) equity (aligned to Tier 1 and Tier 2 definitions) and management of hybrid bonds (in detriment to current subordinated bonds). It also established the minimum tier one capital at 4.5%

All banks currently meet the new regulatory standards on banking capital satisfactorily.

It is noteworthy that bank capital adequacy is consistently increasing along with equity increases, which improves the capacity of the banks' own capital to face obligations.

III. New Banking Regulations

Below, we have included the most recent regulatory changes to date for the system's stability, especially on accounting, risk and AML/CFT/WMD.

These changes are a set of measures that are part of the agenda adopted by the Superintendency of Banks to improve the quality of capital, measure the risk to which the banks are exposed, update to International Financial Reporting Standards and remove the Republic of Panama from discriminatory and non-cooperative jurisdiction lists. Currently, the SBP has approved rules on market risk, operating risk, short-term liquidity coverage ratio (LCR) and derivative instruments, among others, some of which are already undergoing implementation according to the schedule developed by the SBP.

Similarly, all of the information on the current regulations for banking operations in Panama is available on the SBP's website. The Superintendency of Banks' URL address is http://www.superbancos.gob.pa.

Table 1: Recent Regulations

Document	Topic
2017 -2019	
Rule 14 (2019)	Amends the percentage set in Article 20 of Rule 4-2008 on the legal liquidity index. Requires general license banks to maintain assets in Panama equal to sixty percent (60%) of their domestic deposits.
Rule 13 (2019)	Amends Article 3 of Rule 6-2018 updating the special services fees. Adds the collection of fees for requests to acquire or transfer trust shares.
Rule 12 (2019)	Prescribes new provisions on securities investment. Upgrades the regulatory framework for securities investment to international regulatory standards.
Rule 11 (2019)	Amends Article 27 of Rule 4-2013 on credit risk management and administration inherent in loan portfolio and off-balance sheet operations.
Rule 10 (2019)	Adds Article 8-A to Rule 6-2009 on the risk concentration limits to economic groups and related parties. Recognizes an exception in the application of Article 7 of Rule 6-2009 to bank holding companies of banks for which the Superintendency of Banks of Panama is home supervisor, in the case of loans granted on exposures of sovereign debt of the country in which the parent company is located.
Rule 9 (2019)	Amends Article 2 of Rule 6-2012 on accounting technical standards applied by Banks established in Panama. Allows bank holding companies to use the US Generally Accepted Accounting Principles (US-GAAP) for reporting financial statements, as long as the banking group's characteristics justify its use and [the entity] receives prior authorization from the Superintendency of Banks.

Rule 8 (2019)	Adds Article 11-A to Rule 5-2011 on Corporate Governance. Further develops the provisions of Law 56 of 2017 and Executive Decree 241-A dated 11 July 2018 by means of which banks are required to appoint women to a minimum of thirty percent (30%) of the positions on its board of directors.
Rule 7 (2019)	Amends Article 1 of Rule 5-2015 on the prevention of the misuse of services rendered by other reporting entities supervised by the Superintendency of Banks. Article 1 is amended to remove money service businesses and exchange bureaus from the scope [of this rule], as exclusive rules for these entities were issued providing guidelines on AML/CFT/WMD.
Rule 6 (2019)	Amends Rule 3-2018 establishing capital requirements for financial instruments registered in the trading book. Aspects related to the trading book and market risk management were amended. Additionally, it requires the Boards of Directors of banks without securities investments to submit an affidavit certifying that the bank does not have any trading instruments to which the capital requirement calculation must be applied.
Rule 5 (2019)	Guidelines for Banks and trust companies providing services as alternate insurance marketing channels. Establishes the guidelines that must be met by banks and trust companies providing services as alternate marketing channels (of companies that are not part of their economic group) when providing and promoting the products of an insurance company, in order to avoid confusion with direct banking and trust activities.
Rule 4 (2019)	Amends Article 2 of Rule 6-2017 on shared banking. Amends Article 2 of Rule 6-2017 to exempt banks providing services as alternate marketing channels for insurance from the prohibition on the use of front office areas and staff.
Rule 3 (2019)	By means of which the Technical Appendix of Rule 11-2018 on new provisions on operating risk was amended.

Rule 2 (2019)	Amends Rule 10-2015 on the prevention of the misuse of banking and trust services. By means of Articles 1 and 2 of Rule 2-2019, Articles 14 (**Customer profile for individuals**) and 15 (**Customer profile for legal entities**) are amended, specifically to strengthen due diligence to improve AML risk management by including the risk of tax evasion,. For individuals, the customer's tax number for the country or countries of tax residence will be required. In addition, an affidavit will be required certifying that the inflow and outflow of money complies with and will comply with the tax obligations of the country or countries of tax residence. For legal entities, the tax identification number will be required, along with an affidavit stating that the inflow and outflow of money complies with and will comply with the tax obligations of the country or countries of tax residence. Additionally, for those cases in which the country has entered into automatic exchange of information agreements, the final beneficiary's tax number for the country or countries of tax residence will be required. Similarly, the aforementioned Rule provides that for Panamanian or foreign legal entities conducting foreign operations and holding accounts in banks in Panama, the bank must request an affidavit certifying that the money deposited in these accounts has complied with and will comply with the relevant tax obligations.
Rule 1 (2019)	Red flags catalog for the detection of operations related to the Financing of Terrorism.