FitchRatings

RATING ACTION COMMENTARY

Fitch Downgrades Credivalores' IDR to 'C' as it Enters Grace Period

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Fitch Ratings - New York/Bogota - 08 Feb 2024: Fitch Ratings has downgraded Credivalores-Crediservicios S.A.'s (Credivalores) Long-Term Foreign and Local Currency Issuer Default Rating (IDR) to 'C' from 'B-' and its senior debt to 'C'/'RR4' from 'B-'/'RR4'. Fitch has also downgraded the Short-Term Foreign and Local Currency IDR to 'C' from 'B'.

Additionally, Fitch has downgraded Credivalores' Long- and Short-Term National Scale ratings to 'C(col)'/'C(col)' from 'BBB-(col)'/'F3(col)' and the company's partial credit guarantee (PCG) local issuance national rating to 'CCC+(col)'/'RR4' from 'A(col)', keeping the four notches relativity above Credivalores' Long-Term National Scale rating.

The downgrade follows the company's announcement on Feb. 7, 2024 of an exchange debt offer for its USD 210 million notes due February 2025 and the use of the 30-day grace period for the coupon due Feb. 7, 2024 to materialize the agreement to implement a debt restructuring.

Once the company discloses the terms and conditions of the exchange offer, Fitch will assess the terms of the exchange and concurrent consent solicitation to determine if it constitutes a distressed debt exchange (DDE). If the exchange offer is deemed as DDE, Fitch will downgrade Credivalores' IDR to 'Restricted Default' (RD) on completion of the DDE.

KEY RATING DRIVERS

Credivalores' IDRs are based on its standalone credit profile (SCP), which is below the implied SCP due to the weakest link of funding, liquidity and coverage.

Funding, Liquidity and Coverage Revised Downward: Fitch has downgraded its assessment of Credivalores' funding, liquidity and coverage factor score to 'c' from 'b' with a Negative trend and high importance, as this factor constitutes the company's main credit weakness. Although the refinancing of the Euro Notes reduced the pressure on short-term liquidity, the coupon of 2025 bonds and its maturity within the next 12 months is becoming challenging for the entity. Credivalores' liquidity coverage is pressured by the increasing proportion of short-term debt, which represented around 20% of the total debt at September 2023. At the same time, the core metric of liquid assets and undrawn committed facilities to short-term funding was close to 0.36x.

Challenging Operating Environment: Fitch expects Colombian non-bank financial institution (NBFI) performance to improve moderately during 2024 due to lower GDP growth, declining inflation but still above the central bank's 3+/-1% target, a slow decrease in funding cost and gradual improvement on asset quality after a peak reached during 2H23. Furthermore, exposure to global markets and political uncertainty will likely continue to pose challenges and headwinds to economic growth. Funding and liquidity will continue to weigh on NBFIs' growth and profitability, especially given investor risk aversion and more limited access to local debt markets.

Business Profile Affected by Leverage, Funding and Profitability: Credivalores is the largest NBFI in Colombia engaged in consumer lending to the low-to-mid income population that is not served by traditional banks in small and mid-sized cities. The company has been able to generate relatively stable total operating income (TOI) in the last four years with an average of USD30 million from 2019 to 2023. However, the business profile has been affected by structural issues regarding leverage, funding and profitability together with a higher risk loan portfolio.

Increased Execution Risk: In Fitch's view, Credivalores' plans to restructure its senior notes have a high execution risk. The payment relies on the successful completion of the agreement and positive advances in its payroll business strategy.

Higher Risk Profile: Credivalores has developed robust underwriting standards for the payroll business that is similar to other local competitors and follows Colombian regulations. However, the high proportion of unsecured loans underpins weak asset quality. Refinancing risk boosted market risk exposures, reflecting poor stability of financial results throughout the cycle and weak risk controls. Also, Credivalores is exposed to high currency risk as part of its debt is denominated in U.S. dollars, while revenue is generated solely in Colombian Pesos.

Tight Capitalization and Leverage: Credivalores' high leverage remains a credit weakness due to limited profitability. Successful completion of the exchange offer will reduce near-term refinancing risk and should gradually improve internal capital generation.

Weak Asset Quality: Asset quality remains a challenge as the level of impaired loans, over 60 days, to total loans continued to be high at 20.1% at September 2023. The reserve coverage ratio increased to 112% given the semi-secured portion of the portfolio and the decrease in the credit card business, a level below the banking system average of 186% at September 2023. The expected economic slowdown is likely to affect the metrics, mainly for the unsecured segment. NPLs will likely remain above 17% and the asset quality will gradually improve once the company's focus on payrolls starts to weigh on the loan portfolio.

Weak Profitability: The company reported low but positive results during 2023 after significant losses observed during 2022. The pre-tax ROAA of 0.4% as of September 2023 is similar to the average of 2018-2021 of 0.4%. A strong contraction on business volumes as a consequence of its 2022 payment of the financial commitments, the Colombian economy deceleration and high provision expenses were not offset by the significant increase on interest rate and the positive impact of FX. Fitch expects the change in profitability to continue in a 12-month to 18-month period, supported by the payroll focus strategy and the materialization of the new debt strategy based on the use of asset-backed founding sources.

RATING SENSITIVITIES

Factors that Could, Individually or Collectively, Lead to Negative Rating Action/Downgrade

--Fitch will downgrade Credivalores' Long-Term IDR to 'RD' once the exchange is completed and Fitch considered it is a DDE, and then reassess the company's IDR based on the post-restructuring capital structure.;

--Fitch will downgrade the ratings if the negotiation of the agreement exceeds the grace period as this also constitutes a RD.

Factors that Could, Individually or Collectively, Lead to Positive Rating Action/Upgrade

--Fitch will reassess Credivalores' SCP after the completion of the DDE to determine the Long-Term IDR and senior unsecured rating.

DEBT AND OTHER INSTRUMENT RATINGS: KEY RATING DRIVERS

PCG Issuance

Credivalores' partial guarantee bond local issuance for COP160.000 million is rated four notches above its national long-term rating. The level of enhancement above the base recovery corresponds to the additional recovery that the guarantee gives to the notes, which improves the recovery rate for the bond holders is case of default. The notes have an irrevocable partial guarantee for 70% for payment of interest or principal from Fondo Nacional de Garantias rated 'AAA(col)'.

DEBT AND OTHER INSTRUMENT RATINGS: RATING SENSITIVITIES

--The company's senior unsecured debt is expected to move in line with the Long-Term IDR, although a material increase in the proportion of secured debt could result in the unsecured debt being notched down from the IDR;

--The four-notch relativity of the PCG issuance above Credivalores' Long-Term National Scale rating could be reduced by future increases in the issuer rating or by an improvement in its intrinsic recovery according to Fitch's methodology;

--A downward move in Credivalores' Long-Term National Scale rating would negatively affect the PCG ratings.

ADJUSTMENTS

The Standalone Credit Profile has been assigned below the implied Standalone Credit Profile due to the following adjustment reason: Weakest Link - Funding, Liquidity & Coverage (negative).

The Business Profile score has been assigned below the implied score due to the following adjustment reasons: Business model (negative), Historical and future developments (negative).

The Earnings & Profitability score has been assigned above the implied score due to the following adjustment reason: Historical and future metrics (positive).

The Funding, Liquidity & Coverage score has been assigned below the implied score due to the following adjustment reasons: Business model/funding market convention (negative), Liquidity coverage (negative).

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

ESG CONSIDERATIONS

The highest level of ESG credit relevance is a score of '3', unless otherwise disclosed in this section. A score of '3' means ESG issues are credit-neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. Fitch's ESG Relevance Scores are not inputs in the rating process; they are an observation on the relevance and materiality of ESG factors in the rating decision. For more information on Fitch's ESG Relevance Scores, visit https://www.fitchratings.com/topics/esg/products#esg-relevance-scores.

RATING ACTIONS

ENTITY / DEBT	RATING			RECOVERY	PRIOR
Credivalores-Crediservicios S.A.	LT IDR	C	Downgrade		B- Rating Outlook Negative
	ST IDR	C	Downgrade		B

	LC LT IDR	C	Downgrade		B- Rating Outlook Negative
	LC ST IDR	C	Downgrade		B
	Natl LT	C(col)	Downgrade		BBB-(col) Rating Outlook Negative
	Natl ST	C(col)	Downgrade		F3(col)
senior unsecured	LT	C	Downgrade	RR4	B-
guaranteed	Natl LT	CCC+(col)	Downgrade	RR4	A(col)

VIEW ADDITIONAL RATING DETAILS

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PARTICIPATION STATUS

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APPLICABLE CRITERIA

National Scale Rating Criteria (pub. 22 Dec 2020)

Metodología de Calificaciones en Escala Nacional (pub. 22 Dec 2020)

Third-Party Partial Credit Support Rating Criteria (pub. 11 Jun 2021)

Metodología de Calificación de Soporte Parcial de Crédito por Terceras Partes (pub. 25 Aug 2021)

Metodología de Calificación de Instituciones Financieras No Bancarias (pub. 25 Jul 2023)

Non-Bank Financial Institutions Rating Criteria (pub. 17 Jan 2024) (including rating assumption sensitivity)

ADDITIONAL DISCLOSURES

Dodd-Frank Rating Information Disclosure Form

Solicitation Status

Endorsement Policy

ENDORSEMENT STATUS

Credivalores-Crediservicios S.A.	EU Endorsed, UK Endorsed

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The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Fitch also provides information on best-case rating upgrade scenarios and worst-case rating downgrade scenarios (defined as the 99th percentile of rating transitions, measured in each direction) for international credit ratings, based on historical performance. A simple average across asset classes presents best-case upgrades of 4 notches and worst-case downgrades of 8 notches at the 99th percentile. Sector-specific best- and worst-case scenario credit ratings are listed in more detail at https://www.fitchratings.com/site/re/10238496

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