

First Read

Banco Davivienda

2Q16 strong beat on improved asset quality

Beat in 2Q16 driven by lower provisions

Net income reached COP403bn (11% above UBSe, 19% above cons.), leading to ROE of 18.2% (ROA of 1.8%). Asset quality improved from an abnormally weak 1Q16, confirming that commercial NPL in 1Q16 were led by special situations. The healthy growth and low capital base beg the question of a potential capital raise. **Positives:** loan growth of 23% yoy and still good margins at 6.2%. The cost of risk improved to 1.7% (2.7% in 1Q16) as select situations were resolved. **Negatives:** low Tier I of 7.4%. Results were better than for [Bancolombia 2Q](#). We expect a positive market reaction.

2Q16: strong top line and lower provisions

Loan growth reached +23%yoy, driven by commercial loans (+27%yoy), while consumer remains slow (+16%). The net interest margin contracted to 6.2% (6.7% in 1Q16). Asset quality improved: while the NPL ratio was stable at 1.9%, the cost of risk improved (provisions/loans) to 1.7% (2.7% in 1Q16) with a resolution in corporate exposures (2Q write-offs were mostly in oil). The coverage ratio remained stable at 154% (158% in 1Q16). The cost to income ratio was 44% and the tax rate was 33%. Tier I ratio remains low at 7.4%, suggesting the bank may have to consider some capital action (lower growth, capital optimization, asset sale, or follow on).

2016 outlook: 17% ROE with market share gains, upside risk

Davivienda continues to deliver strong growth in 6 countries, gaining market share, especially in corporate lending. We forecast loan growth at 12% in 2016, with margins at 6.2%, helped by rising policy rates. We estimate opex growth at 11%, and a slightly higher cost of risk of 2.4%. We expect EPS growth of 12% p.a. in 2016-18.

Valuation: Buy rating (PT 34,000, based on residual income model)

Within Andean banks our top picks are Credicorp and Davivienda, both Buy-rated, vs. SanChile (Neutral) and CIB (Sell). Davivienda valuation is attractive: it trades on 8x PE 16e and 1.3x PBV 16e vs. 11.2x/1.3x for CIB.

Equities

Americas
Diversified Financial

12-month rating **Buy**

12m price target **P34,000.00**

Price **P28,040.00**

RIC: DVI_p.CN BBG: PFDVAVND CB

Trading data and key metrics

52-wk range	P28,100.00-20,180.00
Market cap.	P12,456bn/US\$4.22bn
Shares o/s	444m (ORD)
Free float	23%
Avg. daily volume ('000)	418
Avg. daily value (m)	P11,258.7
Common s/h equity (12/16E)	P9,866bn
P/BV (12/16E)	1.3x
Tier 1 ratio	8%

EPS (UBS, diluted) (P)

	UBS	Cons.
12/16E	3,561.33	3,121.04
12/17E	3,953.36	3,466.62
12/18E	4,483.27	3,734.61

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Figure 1: 2Q16 Earnings review – main highlights

COP bn	Consensus	2Q16a	2Q16e	1Q16a	2Q15a	QoQ	QoQ	QoQ	A vs Cons
NIM		6.2%	5.9%	6.7%	5.8%	-52 bps	36 bps	27 bps	
NPL		1.9%	2.0%	1.9%	1.9%	-2.27157	-4.47928	-6.5016	
C/I		43.7%	43.2%	39.6%	50.5%	406.8875	-680.033	48.768	
Net income	340	403	362	424	237	-5.0%	69.9%	11.2%	18.5%

Source: Company data and UBS estimates. Bloomberg for consensus.

Highlights (Pbn)	12/13	12/14	12/15	12/16E	12/17E	12/18E	12/19E	12/20E
Revenues	4,303	4,960	5,389	6,639	7,143	7,840	8,594	9,403
Profit before tax	1,090	1,442	1,619	2,198	2,440	2,767	3,054	3,383
Net earnings (local GAAP)	852	1,062	1,361	1,582	1,756	1,992	2,198	2,435
Net earnings (UBS)	852	1,062	1,361	1,582	1,756	1,992	2,198	2,435
Tier 1 ratio %	7.0	6.5	9.7	7.9	8.5	9.1	9.7	10.2
EPS (UBS, diluted) (P)	1,918.06	2,390.96	3,064.37	3,561.33	3,953.36	4,483.27	4,948.82	5,482.26
Profitability/valuation	12/13	12/14	12/15	12/16E	12/17E	12/18E	12/19E	12/20E
ROE (UBS) %	15.0	16.3	16.9	17.0	16.8	16.9	16.6	17.3
P/PPOP (diluted)	5.9	5.5	3.9	3.3	3.1	2.8	2.6	2.4
P/BV x	1.8	1.8	1.3	1.3	1.1	1.0	0.9	0.8
P/BV (UBS) x	1.8	1.8	1.3	1.3	1.1	1.0	0.9	0.8
P/E (UBS, diluted)	12.8	11.6	8.1	7.9	7.1	6.3	5.7	5.1
Net dividend yield %	1.1	5.1	3.2	3.1	4.3	4.8	5.4	6.0

Source: Company accounts, Thomson Reuters, UBS estimates. Metrics marked as (UBS) have had analyst adjustments applied. Valuations: based on an average share price that year, (E): based on a share price of P28,040.00 on 23 Aug 2016 12:48 EDT

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Forecast returns

Forecast price appreciation	+21.3%
Forecast dividend yield	4.3%
Forecast stock return	+25.6%
Market return assumption	12.0%
Forecast excess return	+13.6%

Valuation Method and Risk Statement

Latin American banks can be affected by changes in both global and local economic conditions and are also subject to political, interest rate, and foreign exchange risks. Our target prices are highly dependent on the level of country risk. Risks specific to Davivienda include any issues with Colombia, to which it is mostly exposed. The bank commands leading market share, and this is at risk from higher competition both on the deposit/funding and services sides of the business. Given Davivienda's asset-sensitive balance sheet, it would be particularly affected by reductions in interest rates.

Our Davivienda PT is Residual Income model derived, with a CoE of 12.4%, long term ROE of 15.0% and long term growth of 6.5%. Our Credicorp PT is Gordon Growth Model derived, with a CoE of 11.6%, sustainable ROE of 19.75% and growth of 5.0%. Bancolombia PT is Gordon growth model derived, with a CoE of 12.3% sustainable ROE of 13.5% and growth of 6.5%. Santander Chile PT is Gordown Growth Model derived, with a CoE of 11.3%, adjusted sustainable ROE of 18.5% and growth of 5.0%.

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12-Month Rating	Definition	Coverage ¹	IB Services ²
Buy	FSR is > 6% above the MRA.	47%	32%
Neutral	FSR is between -6% and 6% of the MRA.	38%	25%
Sell	FSR is > 6% below the MRA.	15%	21%
Short-Term Rating	Definition	Coverage ³	IB Services ⁴
Buy	Stock price expected to rise within three months from the time the rating was assigned because of a specific catalyst or event.	<1%	<1%
Sell	Stock price expected to fall within three months from the time the rating was assigned because of a specific catalyst or event.	<1%	<1%

Source: UBS. Rating allocations are as of 30 June 2016.

1:Percentage of companies under coverage globally within the 12-month rating category.

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UBS Brasil CCTVM S.A.: Frederic De Mariz; Mariana Taddeo. **UBS Limited:** Philip Finch.

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Company Name	Reuters	12-month rating	Short-term rating	Price	Price date
Banco Davivienda ^{5, 6a, 6b, 7}	DVI_p.CN	Buy	N/A	P27,820.00	22 Aug 2016
Bancolombia ^{5, 6a, 6b, 7, 16}	CIB.N	Sell	N/A	US\$38.92	22 Aug 2016
Credicorp ^{7, 16}	BAP.N	Buy	N/A	US\$160.00	22 Aug 2016
Santander Chile ^{5, 7, 16}	BSAC.K	Neutral	N/A	US\$21.70	22 Aug 2016

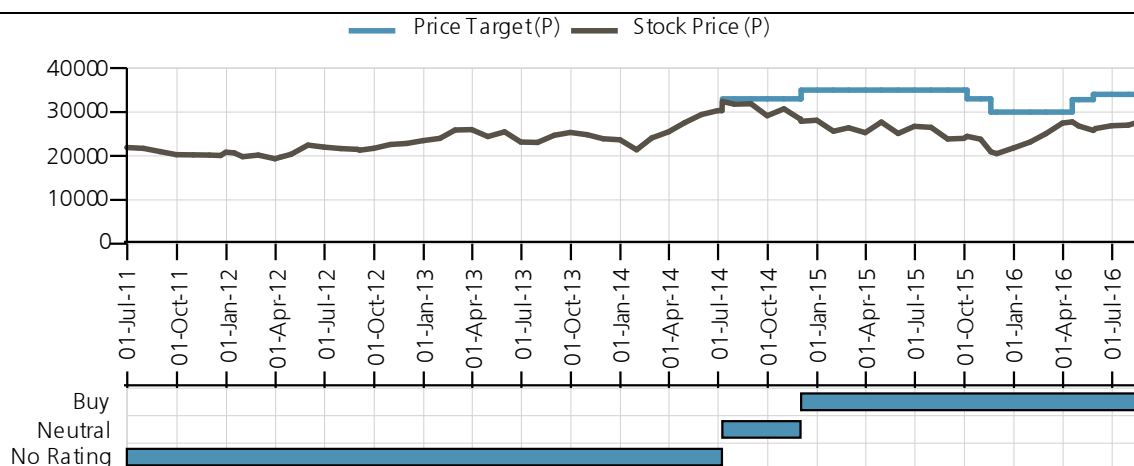
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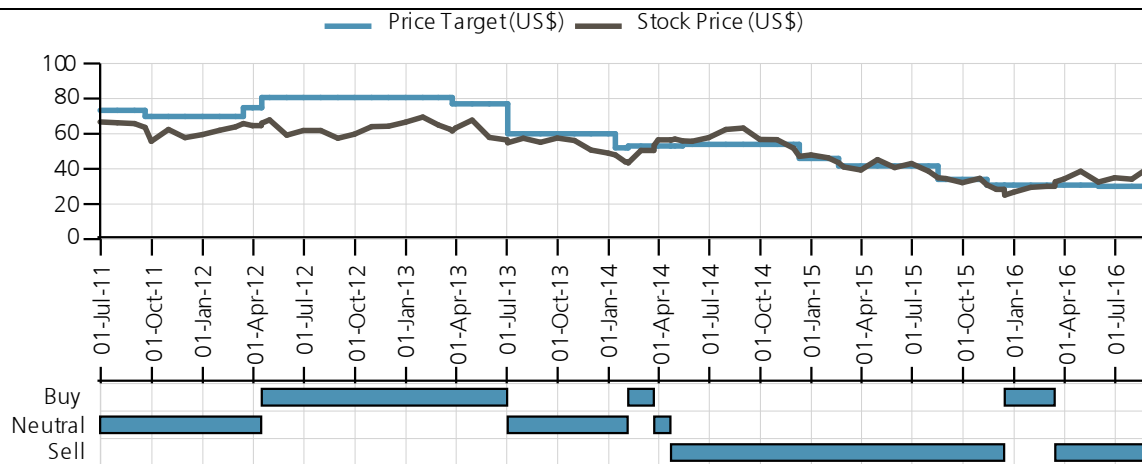
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Banco Davivienda (P)



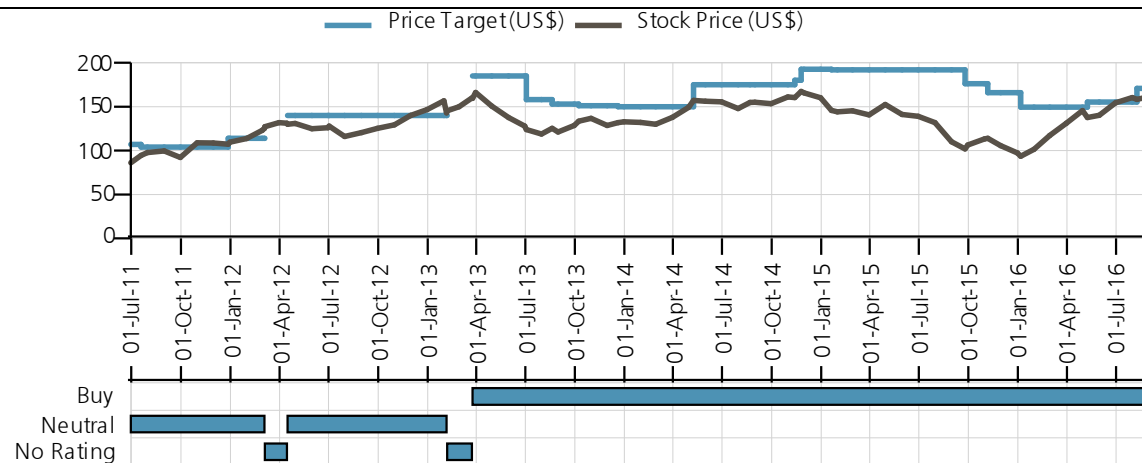
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Bancolombia (US\$)



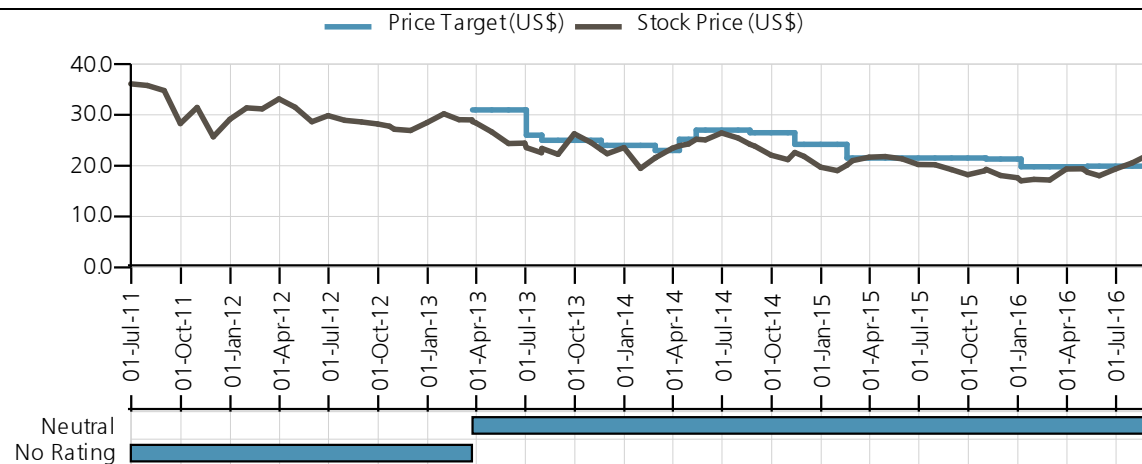
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