

**INTERNATIONAL BONDS**

Instrument	Currency	Coupon (%)	Maturity	Original amount (USDm)	Amount outstanding (USDm)	Price	Yield (%)	Z-spread (bps)	Rating: M/S&P/F
2019 Sr. Unsecured	USD	7.5	13-March-2019	425	135	103.51	4.80	143	NR/BB+/BB+
2023 Sr. Unsecured	USD	7.25	20-June-2023	625	625	106.24	5.95	368	NR/BB+/BB+

Source: Debtwire Analytics, market data as of 31 October 2017.

**CREDITO REAL 3Q17 UPDATE: PORTFOLIO DETERIORATION BEYOND NPL RATIO**

**HIGHLIGHTS FOR 3Q17**

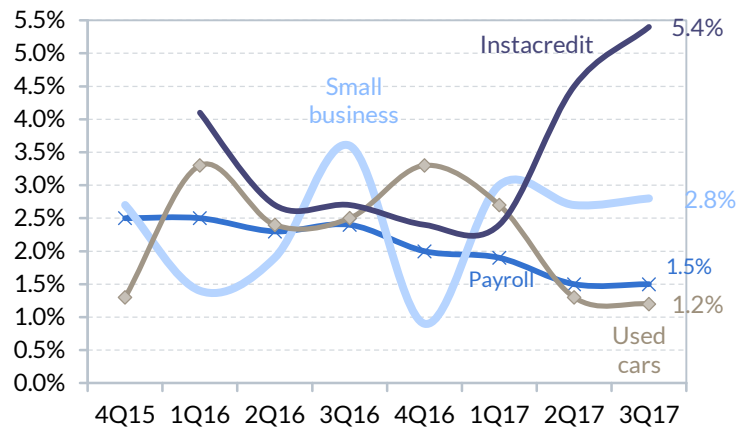
The key takeaway from Credito Real's (CREAL) latest results is NPLs and provisions for Instacredit, its Central American subsidiary, have increased, with NPLs more than doubling since 2017 began. As of 3Q17, they stood at 5.4% for Instacredit, rising quarter-over-quarter from 4.5% and doubling from 2.7% in 3Q16 (See Figure 1). Moreover, provision formation accelerated QoQ to MXN 191m from MXN 160m, and year-over-year from MXN 128m. This implied an annualized provisions rate of 17.9%, accelerating from 16.2% in 2Q17 and 14.1% in 3Q16, with CREAL probably expecting the portfolio to continue deteriorating (See Table 1). The maturing of the portfolio likely contributed to the rising provisions, as the former started to reflect more realistic measures of delinquency.

In the case of the used cars business, provision formation during 3Q17 was at an annualized rate of 11.2%, similar to 11.9% during 3Q16, but below the 15.1% in 2Q17. However, NPLs for the sector were at only 1.2% (or MXN 31m), the reason being that for Don Carro, a 90-day NPL almost never occurs as the company recovers the car much sooner when missed payments start to occur. In this way, it can sell it again, although there is a cost associated with the recovery, the return and the time until the vehicle is sold again.

The other segments of CREAL are doing well. The company grew its payroll-deductible loan portfolio by 4.5% QoQ and 22.8% YoY. A 3.4% increase in the number of customers, as well as an 18.7% increase in the average loan size, which itself was much higher than inflation during the period, explains the YoY growth. The number of customers decreased marginally QoQ, by 0.9%. Overall, this should lead to higher efficiency ratios (See Table 2).

Total loan interest income for 3Q17 was MXN 2.1bn, a 2.8% decline YoY, but a one-off MXN 293m income from closing part of the hedge for the 2019 bond explains the fall. Without this effect, interest income would be 12.8% higher, due to the 17.1% increase YoY in the loan portfolio value to MXN 26.7bn (See Figure 2).

**FIGURE 1: NPL (%)**



Source: Debtwire Analytics, company filings

**TABLE 1: ANNUALIZED PROVISION FORMATION (%)**

	2Q16	3Q16	4Q16	1Q17	2Q17	3Q17
Payroll	0.4%	0.6%	NA	0.9%	0.9%	1.1%
Small business	1.6%	3.3%	NA	1.0%	0.2%	7.3%
Used cars	7.4%	11.9%	NA	17.3%	15.1%	11.2%
Instacredit	6.9%	14.1%	NA	17.6%	16.2%	17.9%

Source: Debtwire Analytics, company filings.

**TABLE 2: PAYROLL-DEDUCTIBLE LOAN**

	3Q16	4Q16	1Q17	2Q17	3Q17
Gross loan portfolio (MXN m)	14,305	14,530	15,177	16,775	17,562
# Customers	354,699	352,667	341,445	370,310	366,928
Avg. loan size (MXN)	40,331	41,202	44,450	45,301	47,863

Source: Debtwire Analytics, company filings.

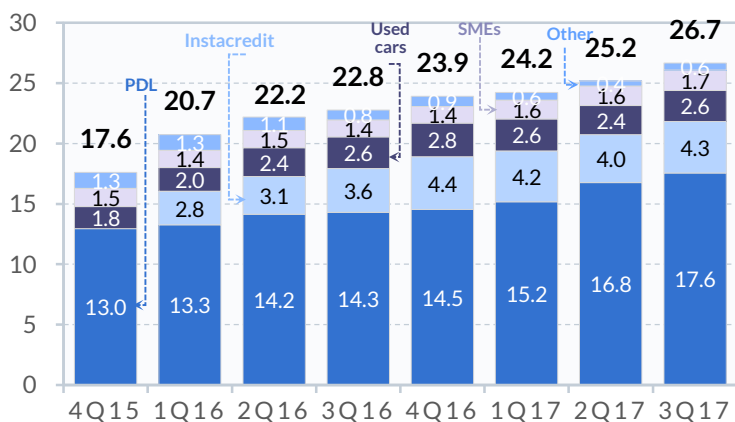
**LATIN AMERICA CREDIT RESEARCH**

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**RECENT DEBTWIRE COVERAGE**

[Credito Real taps two credit lines for MXN 800m \(5-Oct-2017\)](#)  
[RESEARCH: Credito Real 2Q17 Update - Back to its roots ... growth driven by PDL portfolio \(31-Jul-2017\)](#)

**FIGURE 2: LOAN PORTFOLIO (MXN bn)**



Source: Debtwire Analytics, company filings

Growth of 22.8%, 22.1% and 17.4% in payroll-deductible loans, small business and Instacredit (28.8% in local currency, offset partly by an ~9% translation effect), respectively, drove the rise in the loan portfolio. Offsetting these increases are the durable goods and groups loans that CREAL is slowly discontinuing.

**INDEBTEDNESS**

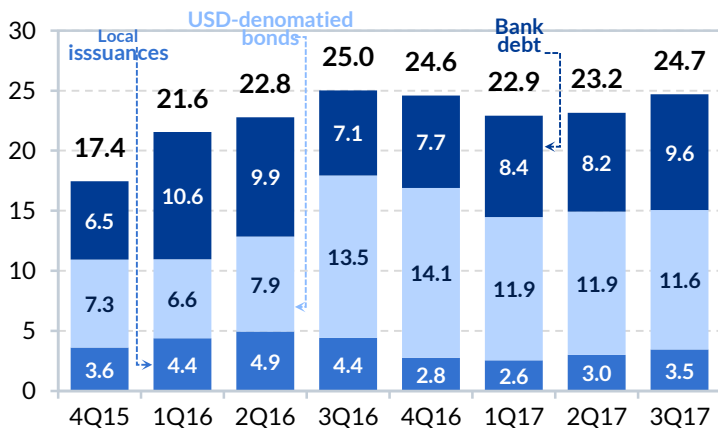
CREAL's total debt was MXN 24.7bn a jump of 6.7% QoQ from MXN 23.2bn, as it added MXN 1.4bn in banking credit lines maturing in 2018 and 2019 during the quarter, and MXN 1bn in securitization debt due 2018 (See Figure 3-Figure 4).

The cost of funding was almost flat QoQ, 11.2% compared to 11.3%, but increased 160bps YoY (See Figure 5). Looking at the QoQ dynamic, a higher TIIE was more than offset by a 50bps decline in spread, explained mostly by the fact that CREAL swapped all of its USD-denominated bonds (46.9% of indebtedness) to MXN at a fixed rate, as well as MXN 2bn in securitizations (8.1% of indebtedness). Hence, 55% of total indebtedness is already fixed at 11.1% in MXN, and unaffected by changes in the TIIE. The renegotiation of banking credit lines at a lower spread is probably the reason for the rest of the improvement. Using the company's securitizations as a benchmark, CREAL issued three- to six-month debt at a range of TIIE+ 115bps-135bps during 2016, while so far during 2017, the spread has tightened to 79bps-90bps. A 280bps increase in TIIE, partly offset by the increased hedging and debt in MXN, impacted the YoY dynamic.

**CAPITALIZATION**

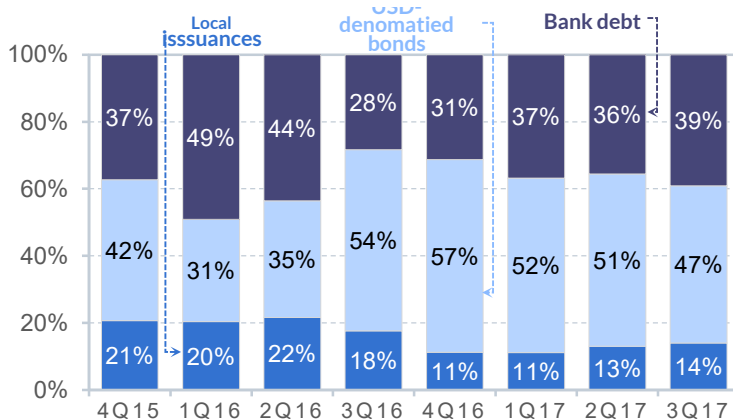
CREAL's capitalization as reported (shareholders' equity/net loan portfolio) stood at 35.2%, a fall of 411bps YoY from 39.3%, as the portfolio rose 17.1% during the same period. Our Basel-III like ratio, however, yielded a capitalization ratio of 22.8%, as a proportional increase in CREAL's equity has accompanied loan portfolio growth.

**FIGURE 3: FUNDING BREAKDOWN (MXN bn)**



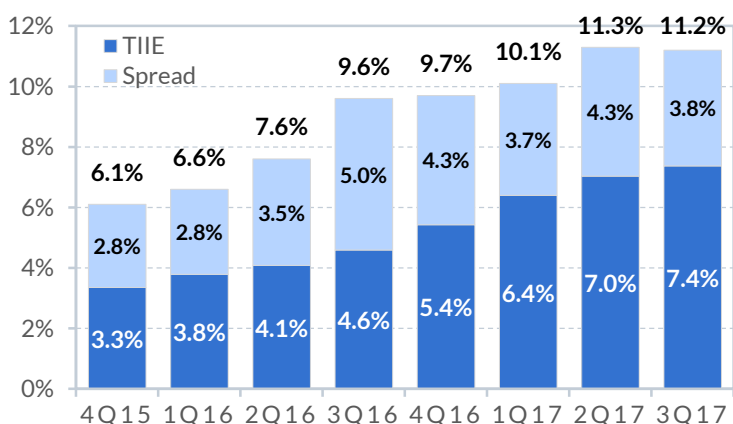
Source: Debtwire Analytics, company filings

**FIGURE 4: FUNDING BREAKDOWN (%)**



Source: Debtwire Analytics, company filings

**FIGURE 5: FUNDING COST (%)**

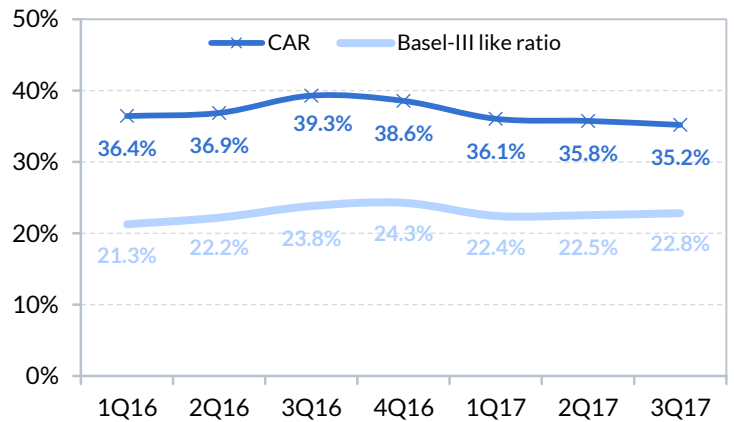


Source: Debtwire Analytics, company filings

**TRADING - Z-SPREAD CLOSE TO RECORD LOW**

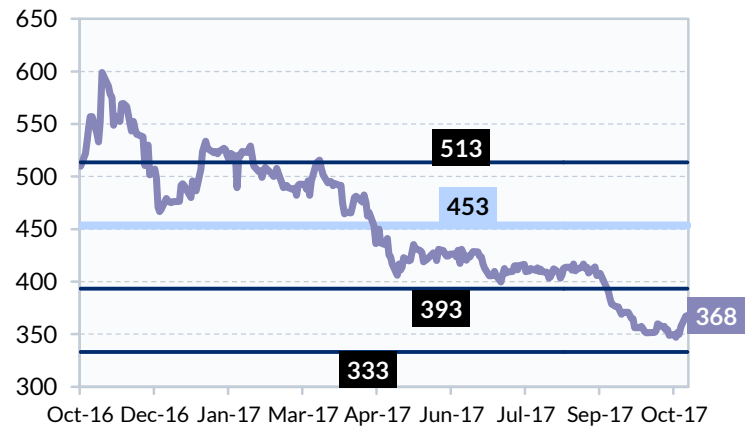
CREAL's 2023 bonds trade at a Z-spread of 368bps, and like most issuances in Latam, between one and two standard deviations below the LTM average. This represents a tightening of 154bps from a year ago. The spread compression between CREAL and the sovereign (Mexico 4 Oct 2023) is the primary reason for the tightening (61%, or 94bps), while the tightening of the sovereign (See Figure 7 - Figure 8) explains the remainder (39% or 60bps).

**FIGURE 6: CAPITALIZATION (%)**



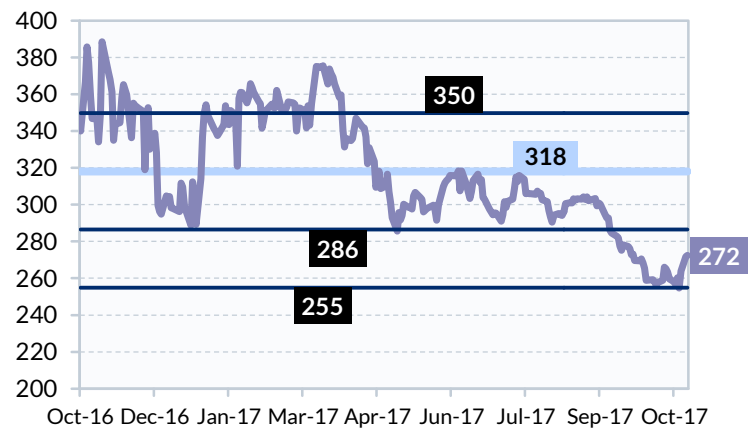
Source: Debtwire Analytics, company filings

**FIGURE 7: 2023s Z-SPREAD (bps)**



Source: Debtwire Analytics, market data

**FIGURE 8: 2023s SPREAD TO SOVEREIGN (MEXICO 2023) (bps)**



Source: Debtwire Analytics, market data

FINANCIAL SUMMARY (MXN m)														
	FY15	FY16	LTM 3Q16	LTM 3Q17	Δ % (LTM 3Q16 – LTM 3Q17)	4Q15	1Q16	2Q16	3Q16	4Q16	1Q17	2Q17	3Q17	Δ % (3Q16 – 3Q17)
Interest income	4,264	6,958	6,364	7,908	24.3%	1,245	1,339	1,655	2,125	1,839	2,015	1,988	2,066	(2.8%)
<i>PDL</i>	3,437	3,722	3,712	4,639	25.1%	946	897	897	971	956	1,209	1,193	1,281	31.9%
<i>Instacredit</i>		1,684	1,114	2,108	89.2%		161	458	495	570	504	517	516	4.4%
<i>SMEs</i>	224	272	260	317	21.8%	62	54	53	92	74	81	60	103	12.8%
<i>Used cars</i>	353	783	749	709	(5.3%)	149	174	205	220	184	202	179	145	(34.2%)
<i>Derivatives</i>		293	293						293					
Interest expense	(952)	(1,916)	(1,569)	(2,524)	60.9%	(252)	(323)	(423)	(571)	(600)	(599)	(655)	(670)	17.3%
Provisions for loan losses	(346)	(832)	(652)	(1,242)	90.5%	(111)	(47)	(208)	(286)	(290)	(316)	(282)	(355)	24.0%
Commissions and fees collected		540	393	746	89.7%		148	107	138	147	203	209	187	96.0%
Commissions and fees paid	(142)	(283)	(325)	(161)	(50.6%)	(28)	(59)	(76)	(163)	14	(64)	(56)	(55)	(26.2%)
Other income	36	643	635	443	(30.2%)	15	61	230	329	23	127	86	208	(62.8%)
Other administrative and operational expenses	(1,138)	(2,922)	(2,511)	(3,226)	28.5%	(396)	(564)	(747)	(805)	(807)	(833)	(781)	(806)	4.6%
Income taxes	(422)	(505)	(615)	(410)	(33.3%)	(123)	(133)	(149)	(211)	(12)	(149)	(89)	(159)	(40.0%)
<b>Net income</b>	<b>1,371</b>	<b>1,714</b>	<b>1,741</b>	<b>1,567</b>	<b>(10.0%)</b>	<b>372</b>	<b>406</b>	<b>375</b>	<b>588</b>	<b>345</b>	<b>397</b>	<b>423</b>	<b>403</b>	<b>12.7%</b>
<b>Total asset</b>	<b>25,996</b>	<b>35,915</b>	<b>36,330</b>	<b>36,431</b>	<b>0.3%</b>	<b>25,996</b>	<b>30,958</b>	<b>33,081</b>	<b>36,330</b>	<b>35,915</b>	<b>33,879</b>	<b>34,619</b>	<b>36,431</b>	
Cash	121	316	524	580	10.7%	121	919	172	524	316	456	732	580	
Total loans (net)	17,124	23,160	21,986	25,695	16.9%	17,124	19,932	21,367	21,986	23,160	23,322	24,237	25,695	
<i>Total loans (gross)</i>	17,610	23,927	22,789	36,678	17.1%	17,610	20,735	22,193	22,789	23,927	24,234	25,187	36,678	
<i>Allowances for loan losses</i>	(486)	(768)	(803)	(983)	22.4%	(486)	(804)	(826)	(803)	(768)	(913)	(920)	(983)	
Other accounts receivables	2,259	3,577	3,941	3,839	(2.6%)	2,259	3,002	3,369	3,941	3,577	3,828	3,826	3,839	
<b>Total liabilities</b>	<b>19,283</b>	<b>26,638</b>	<b>27,374</b>	<b>27,042</b>	<b>(1.2%)</b>	<b>19,283</b>	<b>23,402</b>	<b>24,897</b>	<b>27,374</b>	<b>26,638</b>	<b>25,142</b>	<b>25,613</b>	<b>27,042</b>	
Local bonds	3,610	2,759	4,407	3,463	(21.4%)	3,610	4,385	4,935	4,407	2,759	2,555	3,007	3,463	
USD-denominated bonds	7,335	14,129	13,514	11,584	(14.3%)	7,335	6,583	7,913	13,514	14,129	11,923	11,914	11,584	
Bank loans and borrowings	6,499	7,700	7,093	9,646	36.0%	6,499	10,593	9,940	7,093	7,700	8,437	8,230	9,646	
<b>Shareholders' equity</b>	<b>6,713</b>	<b>9,227</b>	<b>8,957</b>	<b>9,389</b>	<b>4.8%</b>	<b>6,713</b>	<b>7,556</b>	<b>8,184</b>	<b>8,957</b>	<b>9,227</b>	<b>8,737</b>	<b>9,006</b>	<b>9,389</b>	
Yield on income-generating assets	27.1%	31.0%	31.5%	32.3%	(80 bps)	29.4%	27.9%	30.8%	37.8%	31.5%	33.5%	32.2%	31.9%	(590 bps)
Average cost of funds	6.3%	8.2%	7.8%	10.2%	239bps	6.1%	6.6%	7.6%	9.6%	9.7%	10.1%	11.3%	11.2%	164bps
NIM	21.0%	22.5%				23.4%	21.2%	23.2%	27.6%	21.2%	23.5%	21.6%	21.5%	
NPLs	2.4%	2.2%	2.5%	2.3%	(14 bps)	2.4%	2.7%	2.3%	2.5%	2.2%	2.1%	2.2%	2.3%	
Provisions	2.8%	3.2%	3.5%	3.7%	16 bps	2.8%	3.9%	3.7%	3.5%	3.2%	3.8%	3.7%	3.7%	
Coverage ratio	116.7%	145.8%	142.2%	157.7%	1,548 bps	116.7%	145.2%	159.9%	142.2%	145.8%	176.6%	169.4%	157.7%	
Capitalization (as reported)	38.1%	38.8%	39.3%	35.2	(411 bps)	38.1%	36.4%	36.9%	39.3%	38.8%	36.1%	35.8%	35.2	

Source: Debtwire Analytics, company filings

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