EXECUTIVE BOARD MEETING

SM/22/55
Correction 1

March 25, 2022

To: Members of the Executive Board

From: The Secretary

Subject: **Colombia—Financial System Stability Assessment**

Board Action:	The attached corrections to SM/22/55 (3/11/22) have been provided by the staff:
Factual Errors Not Affecting the Presentation of Staff's Analysis or Views	**Page 2**
Typographic Errors	**Page 16**
Questions:	Ms. Arvai, MCM (ext. 38803) Ms. Cuervo, MCM (ext. 34379)

- The FSAP team was led by Zsofia Arvai (IMF) and Raquel Letelier, World Bank (WB), and included Cristina Cuervo (IMF) and Julian Casal (WB) as Deputy Mission Chiefs, Jorge Alvarez, Marco Arena, Aleksandra Babii, Carolina Claver, Lucyna Gornicka, Ziya Gorpe, Manuel Perez Archila, and Can Sever (all IMF); David Hoelscher and José Tuya (IMF experts); and Eva Gutierrez, Craig Thorburn, Maria Teresa Chimienti, Alexander Berg, Graciela Miralles, Andres Martinez, Oliver Masetti, Gonzalo Martinez, Cindy Paladines, Noelia Carreras and Ruben Barreto (all WB); and Ludovic Fagette, Miguel Otamendi, and Claudia Meek (WB experts). Research and administrative assistance were provided by Manuel Perez Archila, Alice Mugnier, Charmane Ahmed, and Anna Konopatskaya, respectively.

- The mission met the General Manager of the Central Bank (BR), the Financial Superintendent of Colombia (SFC), senior staff of the Ministry of Finance and Public Credit (MHCP), Financial Regulation Unit (URF), Superior Judiciary Council, Taxes and Customs Directorate (DIAN), Financial Entities Guarantee Fund (Fogafin), Superintendency of Solidary Economy (SES), Superintendency of Industry and Commerce (SIC), Superintendency of Companies (SS), Superior Court of the Judicial District of Bogotá, and also held many helpful meetings with other official agencies, financial sector representatives, industry representatives, and other stakeholders.

- FSAPs assess the stability of the financial system as a whole and not that of individual institutions. They are intended to help countries identify key sources of systemic risk in the financial sector and implement policies to enhance its resilience to shocks and contagion. Certain categories of risk affecting financial institutions, such as operational or legal risk, or risk related to fraud, are not covered in FSAPs.

- This report was prepared by Zsofia Arvai and Cristina Cuervo with input from the FSAP team.

Results of the Concentration Risk Sensitivity Analysis (December 2020)

	Exposures net of financial guarantees				Exposures before financial guarantees			
	Tier 1	Total CAR	Number of undercapitalized banks	Maximum capital shortfall (in % of GDP)	Tier 1	Total CAR	Number of undercapitalized banks	Maximum capital shortfall (in % of GDP)
Before stress	11.5%	16.3%	0	0	11.5%	16.3%	0	0
Top 1	10.8%	15.5%	0	0.00%	10.4%	15.2%	1	0.00%
Top 5	9.0%	13.8%	2	0.03%	8.1%	12.8%	5	0.28%
Top 10	7.4%	12.2%	5	0.21%	6.0%	10.8%	9	0.71%
Minimum requirement	*4.9%*	*9.0%*			*4.9%*	*9.0%*		

Note: The sensitivity analysis used December 2020 data on counterparty-level exposures data as well as the corresponding data on banks' capital adequacy ratios at end-2020.

17. Stress test results indicate that the banking system is broadly resilient to severe but plausible shocks, albeit with pockets of vulnerabilities in a few banks. High starting levels of system-wide capital and strong profit buffers allow most banks to absorb a large shock under the adverse scenario and retain substantial buffers, with domestic systemically important banks (DSIBs) impacted somewhat less than non-DSIBs (Figures 8 and 9). Similarly, domestically owned banks are less impacted than foreign-owned banks. Sensitivity tests show that some banks would be vulnerable to the default of their largest nonfinancial corporate exposures. Overall, the maximum capital shortfall for the banking system resulting from an adverse shock is negligible.

18. To strengthen the authorities' ability to monitor cross-border exposures, it would be important to fill data gaps on the exposures and risk metrics of ultimate subsidiaries. This would also enable the authorities to conduct a fully consolidated stress testing, incorporating potential contagion channels, and establish early-warning indicators to detect vulnerabilities as they are building up.

C. Liquidity Risk Analysis

19. The banking system is largely resilient to liquidity stress, with liquidity shortfalls relatively small in the very extreme funding shock. To assess the short-term resilience of banks to an abrupt withdrawal of funding, the stress tests, based on the Liquidity Coverage Ratio (LCR), included adverse scenarios that impose more severe assumptions on run-off rates for demand deposits than the regulatory scenario. These adverse scenarios simulate retail and wholesale demand deposit runs. The "wholesale" and combined adverse scenarios reveal some weaknesses in the event of very large deposit withdrawals. The stronger impact of simulated funding shocks on DSIBs reflects the fact that, even though their reliance on wholesale deposit funding is similar to non-DSIBs measured as a share of total assets, DSIBs hold relatively lower amounts of liquid assets. However, even in the very extreme scenario, the aggregate liquidity shortfall is of a manageable magnitude at 1.7 percent of total assets of banks in the sample, and liquidity shortfalls for the individual banks do not exceed 3 percent of total assets.