Conference Call Transcript
Banco PAN (BPAN4 BZ) – 4Q19 Results
February 5, 2020

Operator:

Good afternoon, ladies and gentlemen, and welcome to Banco Pan's conference call to discuss the 4Q19 results.

This event is also being broadcast simultaneously on the Internet, both audio and slideshow, which can be accessed on the Company's IR website, www.bancopan.com.br/ir, and MZiQ platform, with the respective presentation.

We would like to inform you that all participants will be in listen-only mode during the Company's presentation. After the Company's remarks are completed, there will be a question and answer session. At that time, further instructions will be given. Should any participant need assistance during this call, please press *0 to reach the operator.

Forward-looking statements are subject to known and unknown risks and uncertainties that could cause the Company's actual results to differ from those in the forward-looking statements. Such statements speak only as of the date they are made, and the Company is under no obligation to update them in light of future developments.

Now, I will turn the conference over to Mr. Inácio Caminha, Investor Relations Superintendent, who will begin the presentation. Mr. Inácio, you may begin your conference.

Inácio Caminha:

Thank you. Good morning to everyone. Welcome to our earnings release conference call for the 4Q19. We had another strong quarter with an important increase in our results.

Starting on page three, we proudly announced the launch of our digital accounts, focused on low-income individuals. This digital account is a natural evolution of our business and will be very relevant to optimize cross-sell and upsell opportunities, also to increase our product portfolio and our customers' loyalty.

Today, they are more than 4.9 million clients, and we receive hundreds of thousands of credit requests on a monthly basis. And in addition to that, we have more than 10 million individuals who have been our customers at some point.

As transparency is one of the main pillars of our digital strategy, we have developed a clear and intuitive credit card bill in order to provide the customer with a full understanding of the amounts charged. Additionally, we have a team prepared to answer all questions and make any clarifications about the digital account, also through chatbot.

We believe that credit is the main instruments for attracting, engaging and monetizing our clients. This is in our DNA, and we can address the biggest pain of our clients.

Since 2011, we have granted more than R$160 billion in loans to those individuals. And also the assertiveness of using data is another great advantage of the account. So allowing our credit and pricing models to be even more assertive in defining rates and limits, delivering to our clients exactly what they need.

On the next slide, we have some additional information about the app design process. The platform design and UX definitions were made together with our clients, so both in large centers and also on the outskirts. The idea was to experience the context of a Brazilian's life to identify when and how people use financial products and services.

We have more than 200 hours of recording, interviewed more than 40,000 individuals, designed 18 different prototypes and tested the better ones with more than 200 individuals on the street. This creative process enables us to deliver a very simple and intuitive app with a differentiated design, which guarantees total clarity in the use of the digital accounts.

In the next slide, we present some features of the digital accounts. Our clients now have access to a complete checking account, 100% digital without maintenance fees with the zero-cost monthly transfer package, access to ATMs, deposits through slips, utilities payments in addition to several credit products and services.

When opening the account, our clients will receive a zero fee card for debit and credit, and they have access to an emergency limit and personal credit with personalized rates and limits. In addition to that, we will offer discounts at drugstores, supermarkets and online stores through agreements with several partners.

The launch takes place after a short period of soft launch, reaching more than 40,000 digital accounts.

Now, our customer acquisition strategy will be based on six main pillars: first, offering to our active and former clients these benefits; also to the flow of potential clients requesting credit on a monthly basis; also using digital marketing; physical distribution network; new origination partners; and a member get member program.

We are developing more features, and we will add more products for credit, also including insurance, for instance, also including simple investment options that make sense to our clients, financial education contents to help them in their daily lives and many other services, such as mobile top-up. All these features are suited to increase the loyalty of our customers, helping them to overcome their financial challenges.

On the next slide, we bring some of our financial highlights. Credit portfolio ended the year at R$23.8 billion, growing 16% year-over-year. And if you look at the core portfolio, it increased 20% in 12 months. We originated R$1.8 billion in new credits in the quarter, 4% more than previous quarter and 24% more than 4Q18. We ended the year with 4.9 million clients, advancing over the 4.3 million in 2018. Our NIM remained strong at almost 20%, increasing over last quarters. And we posted a net income of R$168 million in the quarter.

The total net income in the year was R$516 million. Very important results, more than doubling the results that we had in 2018. This generated a ROE of 13.7% in the quarter, and the adjusted ROE, which is the best way to evaluate the Bank's performance, ended the quarter at 24.6%. For the 12 months ended on December, the adjusted ROE was 22.5%, and we ended the year with R$4.9 billion equity and 15.6% Basel ratio, already considering the capital increase approved by the Central Bank on January 20.

On slide 7, we present the effects of the increase in the social contribution on net income tax rate. On November, an increase from 15% to 20%, the tax rate applicable to banks. This change has generated an extraordinary result of R$337 million due to the increase in the DTA.

And to offset that impact, we have adopted two following measures: The first was the R$141 million write-off of DTAs related to losses from a subsidiary of Banco PAN to avoid the increase in the consolidated balance of DTAs on our books; and also a very conservative additional provisioning, strengthening our balance sheet. These runoff businesses already had a strong level of provision. For example, the corporate portfolio is now 100% provisioning, excluding guarantees.

Even so, we will continue to act in the same way with respect to collection, execution and foreclosure. Therefore, the net effect was only R$10 million in the quarter and also in the year, restating the strong operational results that we have in the period.

Regarding the quarterly results on slide eight, we present some of the highlights. In the first chart, we show the evolution of our NIM, which ended the 4Q at 19.9% as a result of a strong spread on credit portfolio and also from credit assignment results.

The provisions on the retail portfolio remained stable in R$301 million, showing the assertiveness in credit. And the ALL expenses over the portfolio ended the quarter at 4.1%, without considering the additional provision mentioned before.

Regarding the expenses, we had an increase in the origination as expected, and a relative increase in personnel and administrative expenses. This growth can be explained by the increase in the number of employees, also investment in expenses related to the digital bank, besides investments in advertising and marketing campaigns.

Despite that, income before tax reached R$250 million in the quarter, getting to the R$168 million net income, emphasizing again the recurrence of results and showing the Bank is assertively following its strategy.

On slide nine, we present the evolution of our annual figures comparing to 2018. The dynamics are similar to the quarterly figures. And we also see an improvement in the margin, stable credit expenses over the portfolio, general expenses advancing due to the Bank growth, and overall delivering an earned before tax and net income much higher than 2018, getting to the accumulated net income of R$516 million in 2019.

On slide ten, we present the P&L statement with the reallocation of the tax rate effect, as we believe this is the best way to analyze the numbers, placing all the adjustments after the earnings before tax. So then we can see the R$10 million effect considering the net gain and the provisioning.

Regarding the ROAE on Slide 11, we have the two measures, the accounting and the adjusted unaudited, both annualized. The accounting ROE in the quarter stood at 13.7%, improving over the comparable quarters. And when you look at the adjusted metrics, it also expanded significantly, removing the effects of the fixed rate time deposits issued between 2005 and 2008. Without that, we would get to R$227 million net income in the 4Q and R$737 million in 2019. And also excluding the effect of the excess of DTAs from our equity, we get to the 24.6% adjusted ROAE for the quarter and 22.5% adjusted ROAE for the year.

On the next page, we have the details of our origination. We have granted a monthly average of R$1.8 billion in the quarter, increasing 4% over the last quarter and 24% in the annual comparison. In payroll loans, we reached R$930 million per month in the quarter, 8% less than previous quarter, basically due to seasonality. And on the other hand, we increased 16% in 12 months. Generally speaking, the year starts stronger due to the readjustments in salaries and benefits, this is why we see the seasonality.

In vehicle financing, we had an average origination of R$540 million per month in the quarter, increasing 15% in the quarter and 30% in 12 months. Transactions with credit cards totaled an average of almost R$400 million per month, showing also a relevant increase in the quarter and the year comparison, and we believe that the launch of the digital account will contribute a lot here.

We received around 500,000 credit requests per month in this quarter, and granted credit to an average of 115,000 new clients per month, getting to the 4.9 million clients under management.

On page 13, we show the composition of our credit portfolio. We see in the table, despite a reduction in the 4Q, payroll remains as the largest portfolio with R$12.5 billion. We have assigned R$1.7 billion in this quarter versus R$1.1 billion in the 3Q19.

Besides that, the portfolio increased 16% in 12 months, increasing more than the financial system.

Then we see the vehicle financing portfolio, ending at R$8.9 billion, advancing 27% year-over-year, also increasing more than the financial system. And the credit card portfolio ended at R$1.1 billion, increasing 24% in 12 months.

Then we have the two declining portfolios, corporate and real estate, which ended at R$732 million and almost R$500 million, respectively. So we get to the total of R$24 billion, growing 16% year-over-year.

On page 14, we present our strategy regarding credit and collection. Since 2017, we have been implementing machine learning models to improve credit decisions, analyzing more than 1,000 variables of structured and nanostructured data. All that brings a lot of agility and efficiency on granting credit. Besides that, our clients benefit from a more assertive credit proposal according to their credit profile and personal needs.

We have also been working to improve the assertiveness of our collection using data analytics and digital platforms. In 2019, for instance, we recovered more than R$600 million through these digital platforms, bringing more dynamism and reducing costs.

As we saw in the previous slide, the payroll portfolio registered a decrease mainly due to an increase in the volumes of credit assignment. The decrease of this portfolio has resulted not only in a different portfolio dynamic, but also in a change of the mix of products and clients profile on the overall retail portfolio. The combined effect corresponds to 40% of the 50% bps increase on our 90-days NPL. We are very comfortable with this movement because we clearly saw that provisions expenses over portfolio remains stable, and the product spreads remain at a very robust level.

In payroll, our strategy is to keep being a relevant player focused on federal loans, figuring among the top originators in the INSS loan market. This quarter, we originated R$2.7 billion in new credits. Out of those, 92% in loans and 8% in credit cards. When we look at the breakdown, the federal represented 88% in 2019, out of which 64% comes from the INSS. Portfolio ended the quarter at R$12.5 billion, representing 53% of the total portfolio.

And on the digital front, our formalization platform is increasing, and we have reached already more than R$2 billion in credit operations formalized digitally, making the operation more efficient and safer, and also more profitable.

On slide 16, we present more details about the vehicle segment. We see a strong growth in origination, reaching R$540 million per month. We are covering a greater number of dealerships, more than 11,000, basically due to the efficiency that we have with the digital formalization platform, and also due to the expansion of the commercial team; we went from 400 to 500 employees over the 2H.

Our focus remains to finance used cars, mainly from between four and eight years of use, and new motorcycles in which we are a market leader only excluding a captive finance company.

The portfolio kept its growth pace, ending the year at R$8.9 billion, with an adequate level of loan-to-value and also long term.

By the end of October, we launched the digital formalization platform also for vehicle financing. And by year-end, we had formalized a total of R$200 million, and this number has been growing at a very strong pace.

On page 17, we show the evolution of our credit cards. We have been improving the credit card origination, issuing credit cards without fees. We issued 177,000 credit cards in this 4Q versus only 55,000 in the same period of 2018.

All these movements are being leveraged by the increase in sales actions, in line with improvements in cross-sell, improved efficiency in analytics and also CRM and, obviously, continuous development in the high-end journey of this product directly through our website, and now also through the digital app.

We have also been constantly searching for new partnerships to expand the distribution of these credit cards in marketplaces, and also to offer new co-branded credit cards. The portfolio, as I mentioned, ended the year at R$1.1 billion, totaling R$3.7 billion in transactions in 2019.

On page 18, we show the evolution of insurances. We originated a monthly average of R$28 million in premiums in the last quarter, basically following the vehicle origination volume.

In funding, on slide 19, we presented an increase getting to R$23.7 billion. Time deposits remain contributing to the diversification of our funding, either through market-direct clients and also distribution platforms.

The funding through interbank deposits increased in this quarter. It was a specific movement just to get the Bank ready to start 2020 growing our assets, given the capital increase approval by the Central Bank on January, and also the stronger seasonality that we see commonly in payroll in the 1Q.

On slide 20, we have information about capital. Our Basel ratio stood at 15.6% considering capital increase of R$522 million approved by the Central Bank on January.

With that, we close the presentation and open the line for questions.

Operator:

Since there seems to be no further questions, I would like to turn the floor over to Mr. Inácio Caminha for his final remarks.

Inácio Caminha:

Thank you all again for attending the conference call. Have a nice day, and see you next quarter.

Operator:

This concludes Banco PAN's conference call. You may now disconnect, and have a good day.