Conference Call Transcript
Banco PAN (BPAN4 BZ) – 1Q20 Results
May 7, 2020

Operator:

Good afternoon, ladies and gentlemen, and welcome to Banco PAN conference call to discuss the 1Q20 results.

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

We would like to inform that all participants will be in listen-only mode during the Company's presentation. After the Company' 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 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 further future developments.

With us here today, we have Mr. Mauro Dutra, Banco PAN CFO and IRO; and Mr. Inácio Caminha, Head of Investor Relations and Funding.

Now I will turn the conference over to Mr. Mauro Dutra, who will begin the presentation. Please, Mr. Mauro, you may begin your conference.

Mauro Dutra:

Thank you. Good morning to you all on the call. Thank you very much for being here in our conference call for the results of the 1Q20.

In this 1Q, we had a major change in the macroeconomic scenario, caused by the COVID-19 pandemic. And so it brings here a lot of challenges and mainly uncertainties for the future.

So in this first slide, slide three, we highlighted the actions we have taken in this period and which are being revised on a daily basis. Those actions are based on three pillars. The first pillar is our people, of course. We are worried about their health and to give them the right conditions to work, or to do their job. In this context, we now have 97% of our office staff in home office with a very well connected leadership.

We paid in advance in the month of April, salaries, vouchers and half of the 13th salary. We are also offering to our employees a 24-hour medical assistance using telehealth. And also, we are offering psychological, legal and financial orientation support for them.

The second pillar of our actions in the COVID-19 scenario is our clients. We are trying to be very supportive to them in order to understand the moment and their needs. In this context, we have now 100% digital relationship and services. We can reach our clients and help them only digitally.

The second step is our customized benefits and extended offers, which are made on a tailor base. Overdraft rates have been reduced to 4% per month, and we also extended the installments of the credit card product up to 24 months.

The third pillar is our business. In this pillar, we are being very conservative and trying to move fast in order to have our balance sheet strong and our profitability maintained in the period.

In our business, we increased our liquidity position, our cash position, since the beginning of the crisis. We are having a very conservative approach in credit, not only in vehicles but in all our credit products. We are maintaining our solid capital level and increasing cost efficiency.

Moving to slide four, before I start to present the slide, I would highlight that those actions are only tactical. Our long-term strategy has not changed. And on the contrary, we think we are very well positioned with the digitalization of our businesses and our competitive advantage in this moment.

To understand this competitive advantage, we brought here some figures about the digital formalization of our payroll loans business and the vehicles business. On payroll loans, we reached 41% of digital formalization in the 1Q and more than R$3 billion since April 2019. In the vehicle business, we reached 70% of digital formalization in the 1Q and more than R$1.2 billion since October 2019.

In our digital bank, we launched the digital account app on February 5, three months ago. We enhanced the customer servicing via WhatsApp. And our origination of credit card reached 71% of digital channels.

We also closed important new partnerships in this period, which we think will help us not only in distribution channels, but also in new products to our clients and new ideas to our business.

Moving to slide five. Here, we indicate the main figures of our results. The first one is our credit portfolio, which reached R$25 billion in the 1Q, 19% increase in the last 12 months. We had, for this period, a monthly average retail origination of R$1.8 billion, slightly below last quarter, and we'll talk about it later.

Our customer base, our customers under management number, reached 5.3 million. Our managerial net interest margin for this period was 18.3%, a little below the last quarter of 2019, mainly because the volume of credit assignments. And we will also mention this in detail soon.

Our net income was R$170 million in the 1Q20, slightly above last quarter. The ROE for this period was 13.7% and the adjusted ROE was 23.5%. Both figures indicate the robust profitability of our business and are in line with the last quarter.

To end the highlights section, I would mention our shareholders' equity, our net worth, which is worth R$5 billion in March 2020 and our Basel ratio of 15.7%, which is a very strong level in our view and prepare us to the crisis we are already facing, and we are going to face during this period.

I will now let Inácio talk to you about the earnings and detail the figure of the business.

Inácio Caminha:

Thank you. Moving to slide six, we have the first graph about the results. So in the upper left chart, we see the net interest margin, reducing a little bit, as Dutra mentioned, basically because of the reduction on credit assignments. We assigned R$1.7 billion in 4Q, and we assigned around R$900 million in this 1Q20. This led to this reduction in the margin, but we still keep very strong levels of spreads in the credit portfolio, contributing to the levels of this net interest margin.

As of provisions, we ended the portfolio with R$322 million, and this is gross expenses. When we compare the net expenses over the portfolio, we see a reduction to 3.8%. And this quarter, we sold a written-off portfolio for R$33 million, and this contributed to the recovery, so totaling R$89 million in the quarter.

As for origination expenses, we had R$276 million, expanding a little bit mainly because of volume and mix of the loans originated in the quarter. And personnel loan administrative expenses totaled R$378 million, decreasing in 3 months due to one-off expenses in the fourth Q, for example, marketing and operational expenses.

Looking at the chart for the income before tax and net income. We had R$210 million before tax and R$171 million net income, emphasizing the recurrence of the results and also showing that our strategy has improvement right over the past quarters. For the adjusted ROE, we ended at 23.5%, at a strong level.

On slide seven, we have the breakdown, showing how we get to this 23.5%, coming from the net income. So basically, we have 2 adjustments. The first one is to exclude the excess of financial expenses coming from fixed rate deposits issued between 2005 and 2008. And if we do that, comparing to the price that we currently pay to the market, we would have R$225 million net income in the quarter.

And the other adjustment is to exclude the excess of DTA related to legacy as well, coming to a R$3.8 billion equity instead of the R$4.9 million, average equity in the quarter.

This leads us to the 23.5% ROE instead of the 13.7% on the accounting basis. These are two very simple metrics to understand and to calculate and show better the performance of the Bank in the margin.

Moving to slide eight, we have details of our origination. So we granted R$1.8 billion in this Q, totaling R$5.4 billion in 3 months, increasing 13% in the last 12 months. In payroll, we reached an average of R$933 million per month this quarter, marginally higher than comparable quarters, but with a greater concentration of social security loans, the INSS.

In vehicle financing, we had an average origination of R$483 million per month, 11% lower than last quarter, but 17% higher than the first Q '19. And this recent reduction reflects the increase in competition in the beginning of the quarter and also the first signs of the COVID crisis in the second half of March.

For credit cards, we had an average of R$375 million per month, reducing a little bit over 4Q, mainly because of seasonality, but increasing almost 50% in 12 months.

So in this quarter, we received around 750,000 credit requests per month and granted credit to an average of almost 200,000 new clients per month, ending the quarter with 5.3 million clients under management.

On page nine, we show the composition of our portfolio. In the first table, we can notice that payroll remains as the largest portfolio with R$13.3 billion, increasing 6% in the quarter and 13% in 12 months. Vehicle comes with R$9.3 billion outstanding, increasing 5% in the quarter and 26% in 12 months. And credit cards with R$1.1 billion, also increasing 5% in the quarter and 37% year-over-year.

The last two are the running off portfolios, corporate and real estate, which have been declining. And in total, we had a 5% increase in the portfolio in the quarter and 15% in 12 months, reaching R$25 billion.

And here is worth mentioning, especially in this moment, that the portfolios with collateral and also payroll loan portfolios accounts for 93% of the entire portfolio, giving us a very solid balance to face this moment. And besides retaining credits on our portfolio, we also have the strategy to assign credits without recourse. And as I mentioned, this totaled R$850 million in this quarter, significantly lower than the R$1.7 billion we assigned in the 4Q19.

So when we look at the originated portfolio, adding up the portfolios assigned to the controlling shareholders, we ended the quarter with R$32.3 billion, flat over last quarter but increasing the retained portfolio.

As for credit quality, looking at retail, on Slide ten, we can highlight, first, the conservative credit origination approach. For payroll, for instance, we have 88% focused on federal codes with 35-month duration and an average ticket of R$2,400. This lower ticket in the quarter reflects the readjustment that we had for benefits of the retirees and pensioners, so resulting in lower loans amount.

As for vehicles, we also have a very good standards of underwriting with 35% down payment on vehicles and 21% in motorcycles. Remembering that in vehicles we financed mostly used cars from 4 to 8 years of usage. And in motorcycles, we are talking about new motorcycles.

And in this quarter, looking at the NPLs, we noticed an improvement of 20 bps in the ratio, ending the quarter at 5.7%. This is mainly related to the increase in the portfolio and also the dynamics of credit assignment that changed, as I mentioned. And the spreads in this portfolio remains at a very robust level.

Moving on to slide 11, we have information about payroll. So our strategy is to keep focusing on federal codes, and we can see that in the upper right table, where we have 88% on federal codes, but increasing the share of the INSS to 75%. In the quarter, we originated R$93 million per month. Out of those, 92% regarding loans and 8% in credit cards.

As Dutra mentioned, we averaged 41% of these loans formalized through our digital platform, and this has been very important as a competitive differential in the market. And if you look at March alone, it was responsible for 49% of our origination.

Since the beginning, we did R$3 billion of loans formalized in this way, improving the efficiency, profitability of the operation, especially in this time of lockdown restrictions. And the portfolio, as I mentioned, ended the quarter at R$13.3 billion, representing 53%.

On slide 12, we have some data on vehicle financing. The lower volume of originations relates to the competition that we saw in the beginning of the quarter, as I mentioned, and also the second half of March already showing first signs of the COVID crisis.

And when we look at the standards of origination, the portfolio is still very conservative with good levels of down payments, considering also the tenor of the loans. And here, we also see the digital platform reaching very relevant levels. So in the first 5 months of the operation when it was launched in October, we had already formalized R$1.2 billion in these digital loans for vehicle financing. In the first Q, it was 70%. If we look at March alone, it was 76%, so showing a very good trend, also helping not only the customers but also the dealerships that work with us, especially in this moment of lockdown.

On payments, talking a little bit about credit cards, we have strengthened the relationship with partners to expand the distribution of credit cards in marketplaces and also launching co-branded cards in addition, obviously, to the new digital bank that we launched.

All these initiatives contributed to the increase of credit cards, which totaled 258,000 new credit cards in this quarter, significantly higher than the previous quarters, but with a very conservative credit approach to manage this type of products, especially in these times. We ended the portfolio at R$1.1 billion, also transacting R$1.1 billion in the entire quarter.

As for insurance premiums on Slide 14, we originated a monthly average of R$30 million in the quarter, largely related to the origination of vehicle financing, mostly credit insurance.

For funding on slide 15, we show the increase of 15% in 12 months, reaching R$24.8 billion by the end of March. Time deposits remain contributing to the diversification of our funding through direct clients and also through distribution platforms. And it's important to mention that in April, we settled the subordinate bonds in the total amount of $457 million, which was totally hedged, and we continue with a comfortable liquidity position, operating in a conservative way.

And to conclude the presentation, we have on slide 16 the details on our capital base. We increased a little bit from 15.6% to 15.7% all full CET1, so giving us a very high level of capital, especially considering the current scenario.

And with that, we conclude the presentation and open the line for questions.

Jorge Kuri, Morgan Stanley:

Good morning, everyone. I hope everyone is well. Two questions, if I may. The first one is, could you talk about origination trends during the month of April for your key products?

And second, any idea at this point where the cost of risk may end up for the year? Thank you.

Inácio Caminha:

Thank you, Kuri, for the questions. For the first question, about the origination trends, what we have been seeing, not exclusively for us but for the entire market, is that payroll, for instance, has been increasing demand because of the recent regulatory changes concerning the product. So the term extension, also the interest rate cap reduction, all these measures, they implicate in higher volumes of origination.

And, on the other hand, vehicle financing market has suffered a little bit more because of the lockdown. There was some news about the vehicle sales dropping significantly. So in these two big markets, which are our two main products, we have these different trends. In the end, one may balance the other, but these are the individual movements that we have been seeing.

For credit cards, it's a little bit sideways.

Mauro Dutra:

And about the cost of risk, I would like to divide this answer in two. The first one is our balance sheet. And when we look to our balance sheet, we can see a credit portfolio that is focused on very defensive products. As Inácio explained, 93% of the portfolio is focused on payroll loans and collateralized loans. So this gives us a good position to face this crisis.

And another point I would like to mention is that in the last quarter of 2019, we increased our provision level, mainly in the runoff portfolios. And now we have a portfolio with companies, 100% provisioned, and we see a lot of value in this portfolio. So we think we have a good level of provision at the moment to face the crisis.

The second part of this answer is the NPL ratios. We expect the NPL ratios of the vehicles business mainly to increase. In the last crisis in 2015, 2016, we saw those levels up like 15% to 20%. We do not know yet what will be the level of this crisis we are facing, but we expect those levels to rise. So we are looking at these figures on a daily basis.

We are taking credit actions also on a daily basis, and we expect the Bank is well prepared to face the moment, not only in its business, but also on its balance sheet.

Jorge Kuri:

Thank you very much.

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:

Well, thank you all again for the presence and for the questions. I hope you are all safe and be safe until next quarter. Thank you. Bye-bye.

Operator:

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