

Non-bank financials - Brazil

Year Ahead '24: it's cyclical. Buy payments and capital markets

Price Objective Change

Ideas: buy payments for 1H and capital markets for 2H

Payment companies should post the best EPS growth among non-banks in '24 given stronger card volumes and lower funding costs, boosted by the easing cycle. Valuation for the group remains below historical levels, making STNE and PAGS our top picks for 1H. XP (Buy) should post solid EPS growth in the year, although revenue momentum should accelerate in the 2H, once the Selic rate falls to single digits. We update our earnings estimates and POs (details on Exhibit 1).

Card volume could be a positive surprise for payments

We expect payment companies' EPS to grow c.20% in '24, 5% above Consensus. We expect card TPV growth to surprise positively, boosted by lower household indebtedness, softer inflation, and stronger credit origination. On top of this, the sector should benefit from lower funding costs, supporting higher margins. Nonetheless, the group still faces long-term challenges from new technologies and competition.

Lower rates to boost XP volumes

We expect a lower rate environment supporting increased capital market activity and investment mix supporting inflows, traded volumes and revenue yields in '24. If inflows and traded volumes return to '19-'22 levels, we estimate 5-10% upside to our EPS forecasts for XP. BofA expects the Selic rate to fall to single digits by June.

New revenue verticals could finally start to gain traction

Non-bank financials have been developing new revenue verticals, which could finally start to have a positive impact on earnings. Such as credit origination for STNE and PAGS, and banking for XP.

Stocks trading below pre-pandemic levels

Despite last year-end rally (nonbanks +30% since early November), valuation is still running 50% below pre-pandemic levels (PAGS, STNE and XP are most discounted).

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Exhibit 1: POs and ratings

We changed POs from STNE, PAGS, and XP

Company	PO		Rating	
	Old	New	Old	New
Payments				
STNE (USD)	18.0	20.0	Buy	Buy
PAGS (USD)	14.0	16.0	Buy	Buy
Capital markets				
XP (USD)	29.0	31.0	Buy	Buy

Source: BofA Global Research

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N: Neutral
PAGS: PagSeguro
STNE: Stone
TPV: total payment volume

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Refer to important disclosures on page 10 to 14. Analyst Certification on page 9. Price Objective Basis/Risk on page 9.

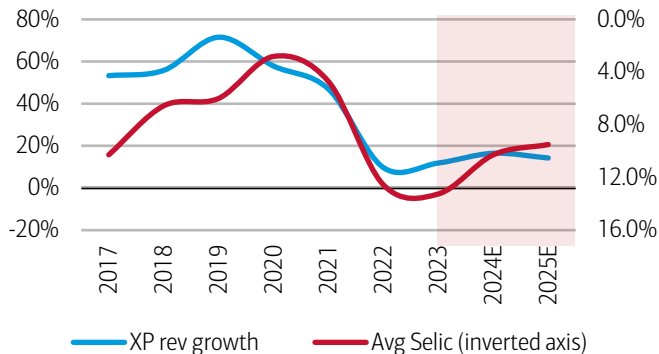
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Timestamp: 16 January 2024 05:51AM EST

2024 in charts

Exhibit 2: XP revenue growth

We expect revenues to accelerate in '24

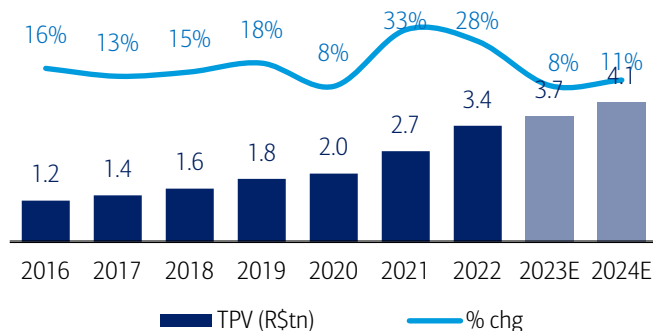


Source: Company, BofA Global Research

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Exhibit 3: Card industry TPV (R\$tn)

We expect TPV acceleration boosted by lower indebtedness, lower inflation and greater credit offering

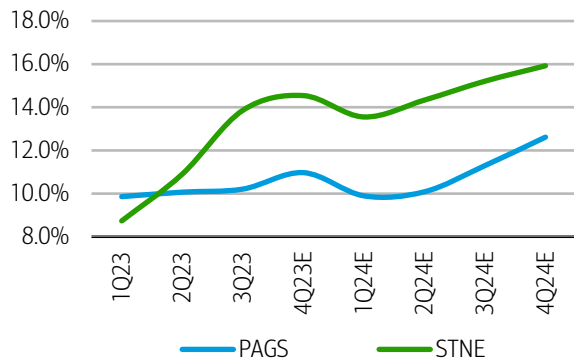


Source: ABCEC, BofA Global Research

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Exhibit 4: Payment companies' net margin

We expect sequential improvement on net margin

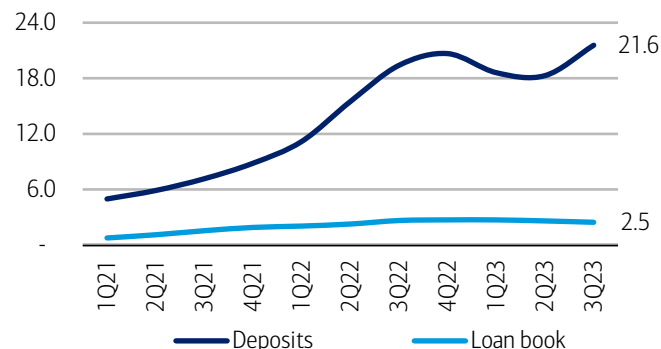


Source: Company, BofA Global Research

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Exhibit 5: PAGES loan book and deposits balance (R\$bnn)

PAGES has successfully expanded its deposits base, but maintained a conservative approach on lending

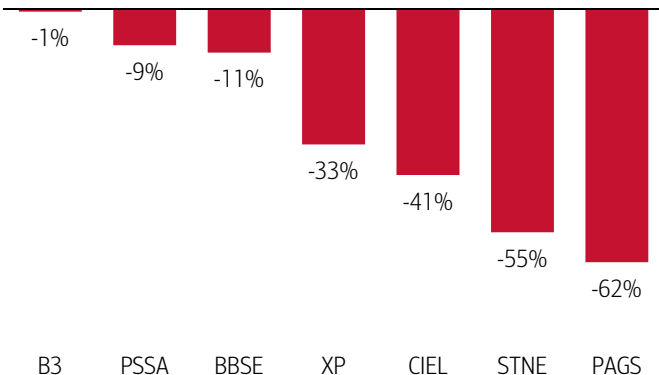


Source: Company, BofA Global Research

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Exhibit 6: Stock prices vs pre-pandemic levels ('19)

Stock prices are well below pre-pandemic levels

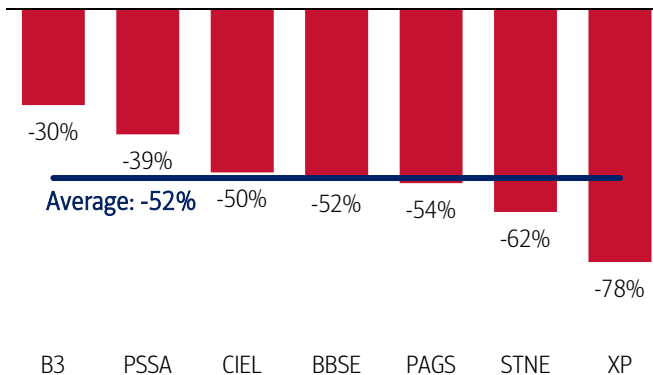


Source: Bloomberg, BofA Global Research

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Exhibit 7: Valuation (P/E) vs pre-pandemic levels ('19)

Valuations are running 50% below pre-pandemic levels



Source: Bloomberg, BofA Global Research

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Summary of our thesis

We prefer payments companies in 1H, when we expect upward revisions to consensus estimates (we are 5% above BBG). We forecast c.20% EPS growth in '24E, while stocks are trading at 9x '24E P/E, below an average of 19x in past three years. XP (Buy) should post 19% EPS growth, weighted in the 2H as the Selic rate should fall to single digits by June; the sub-sector is trading at 14x P/E below an average of c.20-25x during easing cycles.

Payment companies: it's cyclical

EPS growth should benefit from lower funding costs (lower rates) and higher TPV (lower debt service, lower inflation, and higher credit growth). We are 5% above BBG and expect upward revisions – particularly in 1H24. Importantly, the group still faces long-term challenges from new technologies and competition. We like STNE & PAGS (Buy), which are poised to post superior EPS growth, given faster TPV growth and higher sensitivity to lower Selic. We lift our PO for STNE and PAGS to \$20 (from \$18) and \$16 (from \$14), reflecting higher target multiple and higher forecasts, respectively.

Capital markets: expect volume recovery in 2H

On XP, we assume i) monthly net inflows back to pre-pandemic levels and ii) 4bp increase on revenue yield (reflecting riskier asset allocation). We estimate that stronger than expected capital markets and inflows into equities could represent 5-10% upside to our earnings estimates. We increase our PO for XP to \$31 (from \$29), as we increase our target multiple to 18x (in line with international peers) and maintain our Buy.

Exhibit 8: Summary of our coverage

We have Buys on PAGS, STNE and XP

	PO	Price	Upside	Dividend yield	Rating	Net income (2024)			EPS growth		P/E	
						BofAe	BBG	BofAe/BBG	24	25	24	25
Payments						5,923	5,655	5%	18%	13%	8.7	7.9
STNE	20.0	17.1	17%	0%	Buy	2,040	1,933	6%	36%	22%	10.5	8.9
PAGS	16.0	12.5	28%	0%	Buy	1,876	1,842	2%	13%	12%	9.5	9.0
Capital markets												
XP	31.0	25.8	20%	2%	Buy	4,706	4,981	-6%	19%	16%	12.6	10.9

Source: Bloomberg, BofA Global Research, upside-potential

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Key themes for 2024

Card volume could be a positive surprise for payments

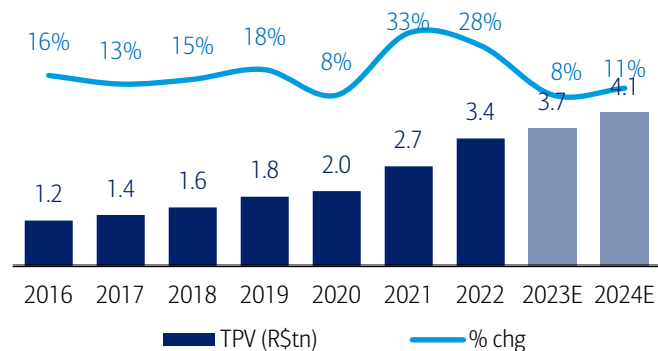
We believe that industry TPV growth should accelerate in '24, given i) declining household indebtedness, ii) lower inflation and iii) the resumption of credit offering, as



banks increase the appetite for riskier credit lines. We forecast 11% industry TPV growth. Banks reduced the origination of consumer credit origination (including credit cards), as indebtedness was at historical highs. Now, as Selic falls, we expect the opposite.

Exhibit 9: Industry TPV (R\$tn)

We expect TPV acceleration boosted by lower indebtedness, lower inflation and greater credit offering



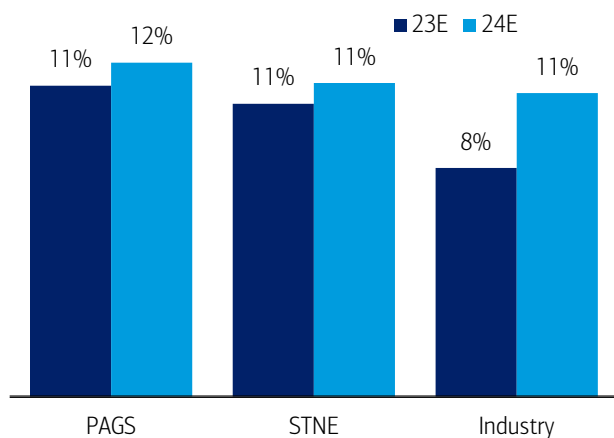
Source: ABECS, BofA Global Research

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The prepayment business gained significant relevance on payment companies as margins of the acquiring business fell, pressured by competition. These companies do not rely on retail funding as incumbent banks, leading to alternative (and expensive) sources of funding. In '24, lower Selic should relieve financial expenses, supporting net margin improvement. Importantly, the impacts of lower rates are not the same among the listed acquirers. We estimate c.15% upside to PAGS and STNE bottom-line for each 100bp contraction in average Selic. All in, we expect sequential net margin improvement on payment companies in '24, reflecting lower financial expenses and operating leverage gains, as opex growth should lag revenue growth.

Exhibit 11: TPV growth forecast

We expect volume growth acceleration across all players

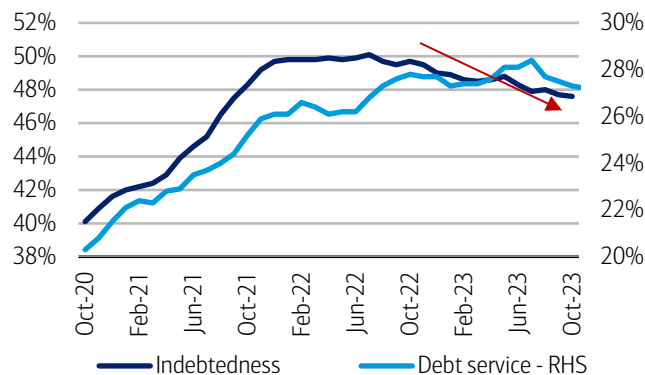


Source: BofA Global Research

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Exhibit 10: Indebtedness and debt service (%)

Indebtedness and debt service ratios are gradually improving

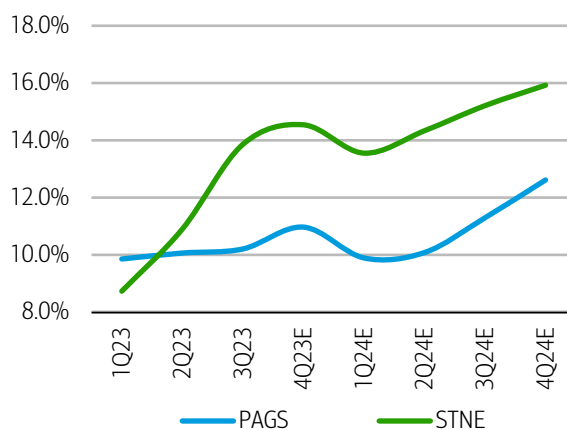


Source: BCB, BofA Global Research

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Exhibit 12: Payment companies' net margin

We expect sequential improvement on net margin



Source: Company, BofA Global Research

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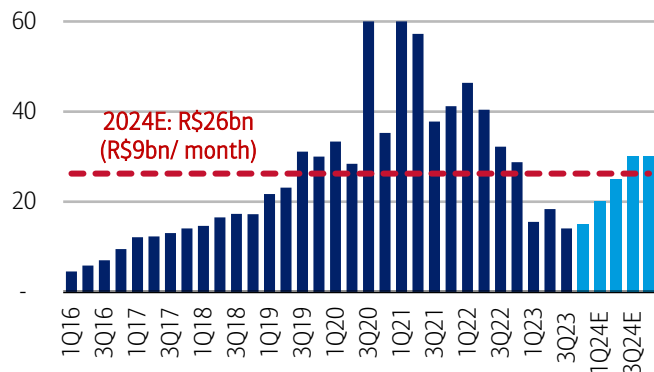
Lower rates to boost XP volumes

We forecast R\$9bn monthly net inflows into XP in '24, recovering from average of R\$5bn in '23 and in line with pre-pandemic levels. We also forecast retail revenue yield (ex-new verticals) to expand 4bp in '24, recovering from a low in '22, when mix was pressured by conservative asset allocation.

If retail inflows into equities recovered at faster than expected pace, revenue yield could surprise positively. If net inflows were 10% above BofAe (R\$10bn/month) and revenue yield increased 8bp (still well below historical levels), we forecast 4% upside to our R\$4.7bn forecast. If inflows reached R\$13bn/month and revenue yield increased 12bp, we expect 10% upside to BofAe. In fact, XP's revenue growth is historically negatively correlated to movements in interest rates, reinforcing expectations of acceleration ahead.

Exhibit 13: XP historical inflows and '24 forecast (R\$bn)

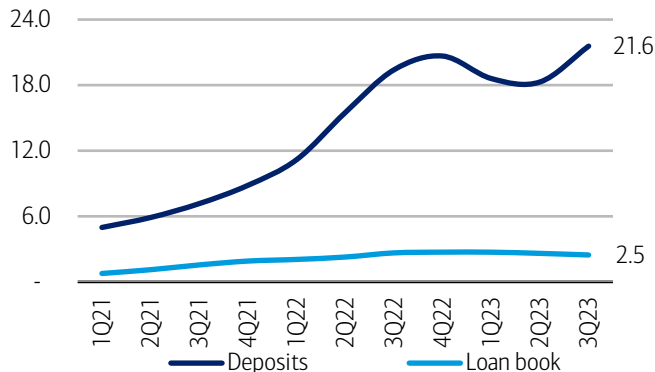
We expect sequential improvement on inflows



lending. As result, loan book remained stalled at c.R\$2.5bn (vs deposits base of R\$21bn). Likewise, STNE built a robust deposit base, but origination remains low as mgmt. tests the new product. We expect robust loan and deposit growth ahead, supporting bottom-line through new revenues (NII) and returns on deposits.

Exhibit 16: PAGS loan book and deposits balance (R\$bn)

PAGS has successfully expanded its deposits base, but has maintained a conservative approach on lending

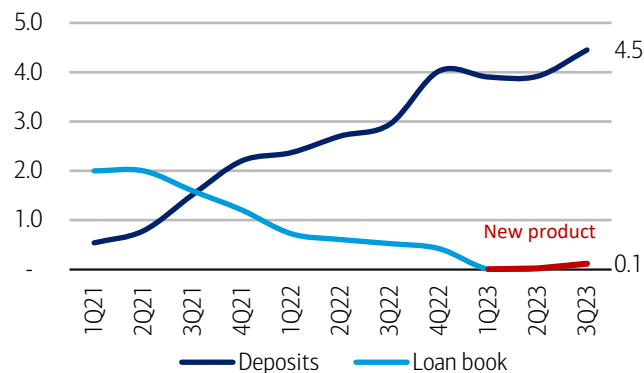


Source: Company, BofA Global Research

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Exhibit 17: STNE loan book and deposits balance (R\$bn)

STNE is just starting its new credit product



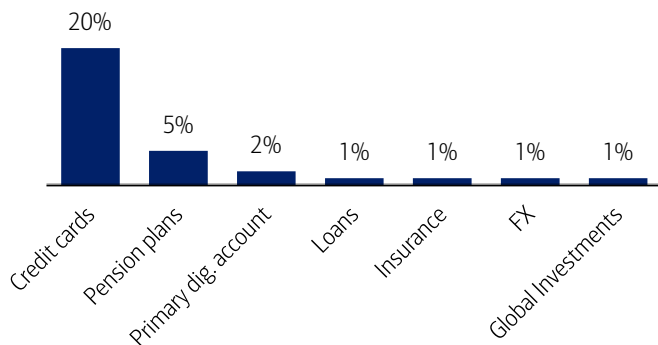
Source: Company, BofA Global Research

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XP's banking revenues are far behind initial forecasts; credit card is the only product that gained relevant scale. Now, a more focused mgmt. and the end of the investment phase could lead to stronger revenue growth.

Exhibit 18: Penetration of new products on XP's client base

Credit cards reached 20% of XP's client base, while other products remain little penetrated



Source: Company, BofA Global Research

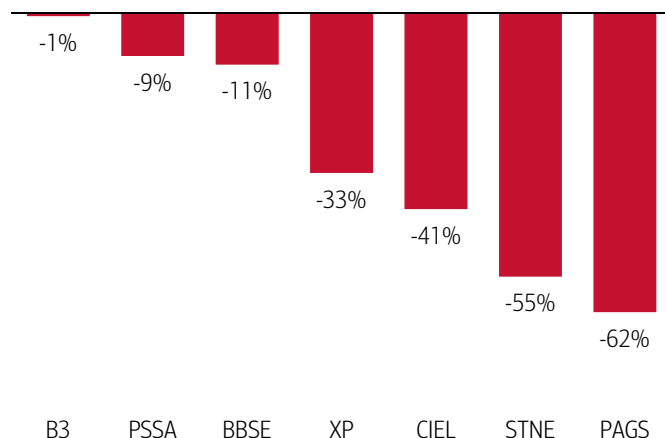
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Stocks trading below pre-pandemic levels

Non-banks rallied almost 30% since early November. Nonetheless, we note that stock prices and valuations remain well below pre-pandemic levels. Non-banks P/E ratios are running c.50% below prepandemic levels, especially on high growth names such as PAGS, STNE and XP.

Exhibit 19: Stock prices vs pre-pandemic levels ('19)

Prices are well below pre-pandemic levels

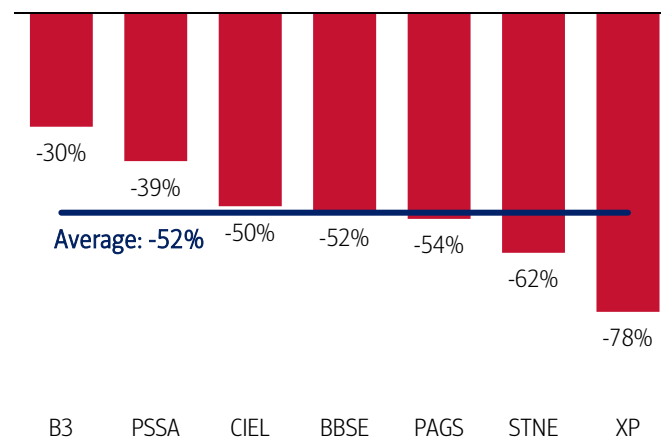


Source: Bloomberg, BofA Global Research

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Exhibit 20: Valuation (P/E) vs pre-pandemic levels ('19)

Valuations are running 50% below pre-pandemic levels



Source: Bloomberg, BofA Global Research

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New estimates, POs and ratings

Exhibit 21: Summary of our coverage

We prefer STNE, PAGS and XP

	PO	Price	Upside	Dividend yield	Rating	BofAe	Net income (2024)		EPS growth		P/E	
							BBG	BofAe/BBG	24	25	24	25
Payments						5,923	5,655	5%	18%	13%	8.7	7.9
STNE	20.0	17.1	17%	0%	Buy	2,040	1,933	6%	36%	22%	10.5	8.9
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Capital markets						9,654	9,981	-3%	13%	12%	13.7	12.4
XP	31.0	25.8	20%	2%	Buy	4,706	4,981	-6%	19%	16%	12.6	10.9

Source: Bloomberg, BofA Global Research, upside-potential

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Payments companies

PagSeguro: discounted valuation and earning acceleration

We increase our estimates for PagSeguro by +4%/+6%/+7% in '23/'24/'25 to incorporate stronger TPV growth. Our new PO of \$16 (from \$14), reflects our new model, while we maintain our target P/E unchanged at 14x, one standard deviation below the historical average (reflecting challenging industry perspectives in the long term). We expect TPV expansion of +11%/+12% in '23/'24, above industry growth, given expansion into the SME segment, which is also negative for take rate (2.28% in '24, vs 2.48% in '23) – leading to revenue growth of 6% (vs 5% in '23). Controlled costs, expenses, and funding costs should lead to net margin expansion (10.3%/11.1% in '23/'24). All in, we forecast EPS growth of +10%/+13/+12% in '23/'24/'25. The company trades at 9.5x '24E P/E, well below historical levels. Buy.

Exhibit 22: PagSeguro – model summary

We expect earnings growth of +10%/+13/+12% in '23/'24/'25

R\$mnn	'23E			'24E			2025E			2026E		% chg YoY			
	Old	New	Change	Old	New	Change	Old	New	Change	New		23/22	24/23	25/24	26/25
Net revenue	15,644	16,054	3%	16,555	16,976	3%	17,784	18,395	3%	20,095		5%	6%	8%	9%
Operating expenses	9,932	10,253	3%	10,862	11,324	4%	11,825	12,437	5%	13,660		2%	10%	10%	10%
Operating income	5,711	5,801	2%	5,693	5,652	-1%	5,959	5,958	0%	6,435		9%	-3%	5%	8%
EBITDA	7,081	7,162	1%	7,297	7,238	-1%	7,823	7,804	0%	8,601		11%	1%	8%	10%
Financial expenses	3,246	3,268	1%	2,914	2,742	-6%	2,807	2,630	-6%	2,946		4%	-16%	-4%	12%
Earnings before taxes	2,101	2,204	5%	2,379	2,510	6%	2,672	2,848	7%	3,009		16%	14%	13%	6%
Net income - reported	1,576	1,654	5%	1,759	1,876	7%	1,954	2,103	8%	2,218		10%	13%	12%	5%

Exhibit 22: PagSeguro – model summary

We expect earnings growth of +10%/+13/+12% in '23/'24/'25

Net income - non-GAAP	1,676	1,758	5%	1,856	1,958	6%	2,058	2,193	7%	2,317	10%	11%	12%	6%
EPS -- reported	4.83	5.09	5%	5.39	5.77	7%	5.99	6.47	8%	6.82	12%	13%	12%	5%
EPS -- non-GAAP	5.14	5.41	5%	5.69	6.02	6%	6.31	6.75	7%	7.13	12%	11%	12%	6%
Operating margin	37%	36%	-38 bp	34%	33%	-109 bp	34%	32%	-112 bp	32%	153 bp	-284 bp	-91 bp	-37 bp
EBITDA margin	45.3%	44.6%	-66 bp	44.1%	42.6%	-144 bp	44.0%	42.4%	-157 bp	42.8%	263 bp	-198 bp	-21 bp	38 bp
Effective tax rate	20.2%	20.3%	2 bp	22.0%	22.0%	0 bp	23.0%	23.0%	0 bp	23.0%	428 bp	174 bp	100 bp	0 bp
Non-GAAP net margin	10.1%	10.3%	23 bp	10.6%	11.1%	43 bp	11.0%	11.4%	45 bp	11.0%	50 bp	75 bp	38 bp	-40 bp
TPV (R\$ billion)	378	394	4%	416	441	6%	454	486	7%	534	11%	12%	10%	10%
Active clients (th)	6,610	6,620	0%	6,850	6,580	-4%	7,250	6,830	-6%	7,080	-7%	-1%	4%	4%
Gross take rate	4.07%	4.01%	-6 bp	3.92%	3.80%	-13 bp	3.87%	3.74%	-13 bp	3.72%	-27 bp	-22 bp	-5 bp	-3 bp
Net take rate	2.53%	2.48%	-5 bp	2.41%	2.28%	-12 bp	2.35%	2.23%	-12 bp	2.20%	-23 bp	-20 bp	-5 bp	-3 bp

Source: BofA Global Research

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Stone: a self-help story with strong earnings growth

We increase our PO for Stone to \$20 (from \$18), as we increase our '24 target P/E to 16x (from 14x), close to one standard deviation below the historical average. Our estimates remain unchanged, following our update on December. In our model we assume revenue growth of +28%/+12% in '23/'24, reflecting i) TPV growth of +11%/+11%, led by the MSMB segment, ii) take-rate expansion, supported by mix (2.91% in '24 vs 2.84% in '23) and iii) software revenues growth of +6%/+9% in '23/'24. We expect costs, expenses, and funding costs growth below revenue expansion, leading to non-GAAP net margin of 12.2%/14.8%/16.3% in '23/'24/'25. All in, we expect EPS growth of +36%/+22% in '24/'25. We maintain our Buy rating.

Capital markets**XP: expecting for better volumes and riskier asset allocation**

We lift our PO to \$31 (from \$29), as we increase our target P/E to 18x '24, in line with international peers, while our estimates remain unchanged. We expect +12%/+16%/+14% revenue growth in '23/'24/'25, reflecting benefits from a low-rate scenario. We forecast R\$9bn monthly net inflows, recovering from average of R\$5bn in '23 and in line with pre-pandemic levels. We also forecast retail revenue yield (ex-new verticals) to expand 4bp in '24. We forecast controlled costs and expenses, following headcount reductions, efficiency programs and lower expenses related to the development of banking products - leading to operating leverage gains and bottom-line expansion of +10%/+19%/+16% in '23/'24/'25.

Stocks mentioned

BofA Ticker	Bloomberg ticker	Company name	Price	Rating
PAGS	PAGS US	PagSeguro	US\$ 12.5	C-1-9
STNE	STNE US	StoneCo	US\$ 17.11	C-1-9
XP	XP US	XP Inc.	US\$ 25.81	C-1-9

Source: BofA Global Research

Price objective basis & risk

PagSeguro Digital Ltd (PAGS)

Our PO of US\$16 is derived from a target P/E of 14x to our '24 GAAP EPS estimate. The target PE is one standard deviation below the historical average, challenging perspectives for the industry in the long-term.

Downside risks: 1) more intense competition from peers, which could lead to take-rate pressure, 2) regulatory changes that could pressure profitability, 3) weaker macro economic scenario in Brazil, which could negatively impact TPV growth, and 4) slower decline in interest rates, which would maintain financial expenses pressured.

StoneCo (STNE)

Our PO of US\$20 is derived from a target P/E of 16x on our '24 non-GAAP EPS estimate. Our target PE multiple is one standard deviation below historical average, reflecting execution challenges.

Downside risks: 1) increased competition, which could limit growth in clients and TPV, and lead to lower profitability, 2) potential regulatory changes, which could pressure pre-payment revenues, 3) poor execution in deploying the credit product could lead to high credit losses.

XP Inc. (XP)

Our PO of \$31 is based on a target P/E multiple of 18x our '24 GAAP EPS estimate of \$1.68. Our target multiple is the midpoint of multiples during a high-rate environment and recent M&A transactions.

Downside risks are: 1) increased competition from incumbents and new players may lead to margin pressure, and limit XP's growth and profitability, 2) all of XP's revenues are denominated in BRL, and thus are vulnerable to FX volatility, and 3) potential share overhang as Itausa divests its stake.

Upside risks are: 1) continued growth of AUC as it gains share from incumbent banks, which should support solid growth over the medium to long-term, 2) the development of new banking products such as credit cards, credit, insurance, and pension, which could support revenue growth.

Analyst Certification

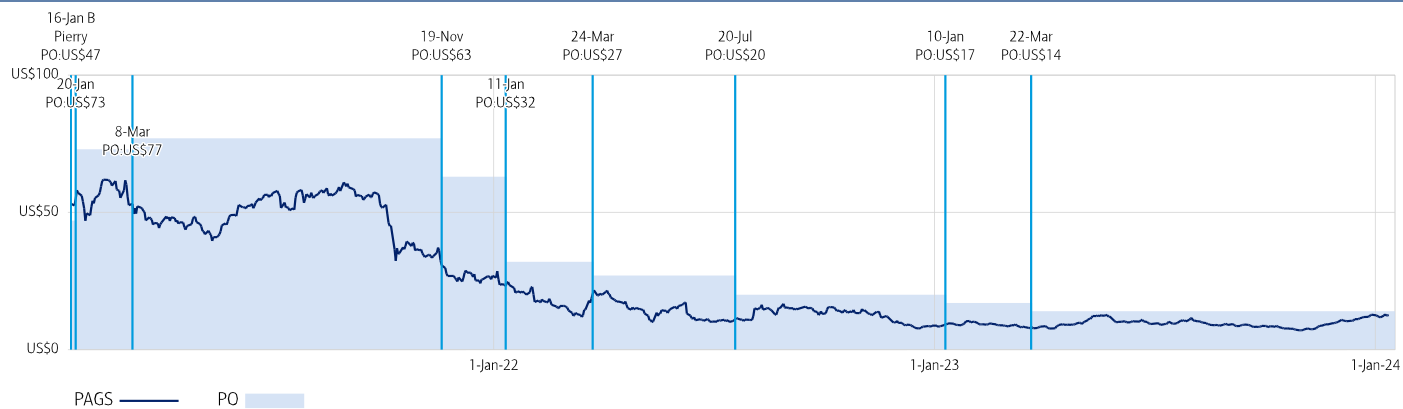
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Latin America - Financials Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
BUY				
	ABC Brasil	XBABF	ABCB4 BZ	Flavio Yoshida
	B3	XIMAF	B3SA3 BZ	Mario Pierry
	B3	BOLSY	BOLSY US	Mario Pierry
	Bajio	BBAJF	BBAJIO MM	Ernesto Gabilondo
	Banco do Brasil	XBBAF	BBAS3 BZ	Mario Pierry
	Banco do Brasil	BDORY	BDORY US	Mario Pierry
	Banco Pan	XQSFF	BPAN4 BZ	Flavio Yoshida
	Banco Santander Chile	BSAC	BSAC US	Ernesto Gabilondo
	Banco Santander Chile	XLDTF	BSAN CI	Ernesto Gabilondo
	Banorte	GBOOF	GFNORTEO MM	Mario Pierry
	Banorte	GBOOY	GBOOY US	Mario Pierry
	Bci	BZCIF	BCI CI	Ernesto Gabilondo
	BTG Pactual	XNXCF	BPAC11 BZ	Flavio Yoshida
	Caixa Seguridade	XDXUF	CXSE3 BZ	Mario Pierry
	Credicorp Ltd	BAP	BAP US	Ernesto Gabilondo
	Gentera	CMPRF	GENTERA* MM	Ernesto Gabilondo
	Grupo BMV	BOMXF	BOLSAA MM	Ernesto Gabilondo
	IFS	IFS	IFS US	Ernesto Gabilondo
	Inter	XBZIF	INBR32 BZ	Mario Pierry
	Inter	INTR	INTR US	Mario Pierry
	PagSeguro Digital Ltd	PAGS	PAGS US	Mario Pierry
	Porto Seguro	PSGUF	PSSA3 BZ	Mario Pierry
	Regional	RGNLF	RA MM	Ernesto Gabilondo
	StoneCo	STNE	STNE US	Mario Pierry
	XP Inc.	XP	XP US	Mario Pierry
NEUTRAL				
	Banrisul	XGRBF	BRSR6 BZ	Flavio Yoshida
	BB Seguridade	XBDPF	BBSE3 BZ	Mario Pierry
	BB Seguridade	BBSEY	BBSEY US	Mario Pierry
	Bradesco	BRDPF	BBDC4 BZ	Mario Pierry
	Bradesco -A	BBD	BBD US	Mario Pierry
	Cielo	CIOXF	CIEL3 BZ	Mario Pierry
	Cielo	CIOXY	CIOXY US	Mario Pierry
	Itau Unibanco	ITUBF	ITUB4 BZ	Mario Pierry
	Itau Unibanco	ITUB	ITUB US	Mario Pierry
	Nubank	NU	NU US	Mario Pierry
UNDERPERFORM				
	Banco Chile-ADR	BCH	BCH US	Ernesto Gabilondo
	Banco de Chile	XHNDF	CHILE CI	Ernesto Gabilondo
	Banco Macro	BMA	BMA US	Ernesto Gabilondo
	Banco Macro	BCVMF	BMA AR	Ernesto Gabilondo
	GFinbur	GPFOF	GFINBURO MM	Ernesto Gabilondo
	Grupo Financiero Galicia	GGAL	GGAL US	Ernesto Gabilondo
	Grupo Financiero Galicia	GGABF	GGAL AR	Ernesto Gabilondo
	Qualitas	QUCOF	Q* MM	Ernesto Gabilondo
	Santander Brasil	XCBDP	SANB11 BZ	Mario Pierry
	Santander Brasil	BSBR	BSBR US	Mario Pierry
	Supervielle	SUPV	SUPV US	Ernesto Gabilondo
	Supervielle	XAZFF	SUPV AR	Ernesto Gabilondo
RSTR				
	Bancolombia	CIB	CIB US	Ernesto Gabilondo
	Bancolombia	XAFFF	PFBCOLO CB	Ernesto Gabilondo

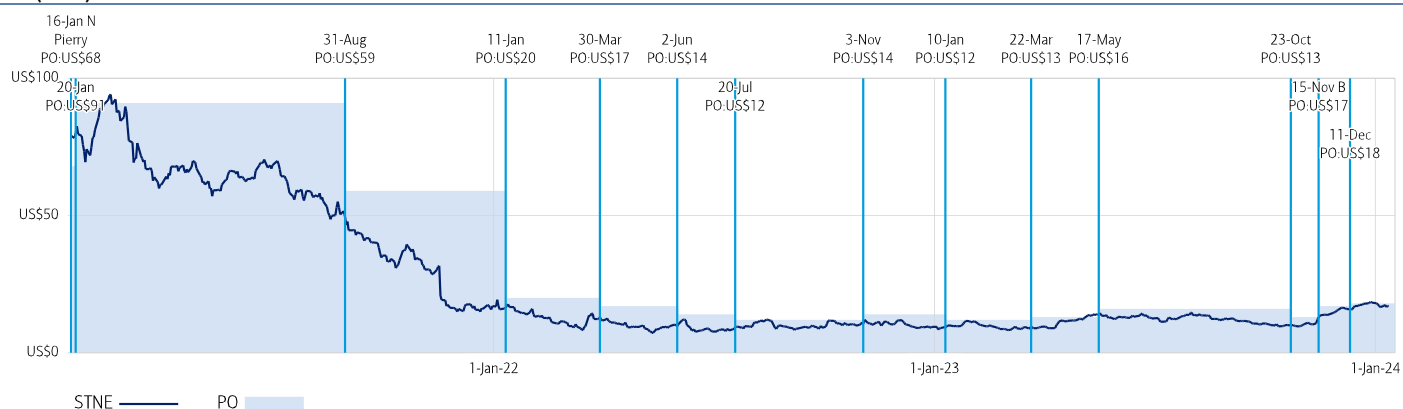
Disclosures

Important Disclosures

PagSeguro (PAGS) Price Chart

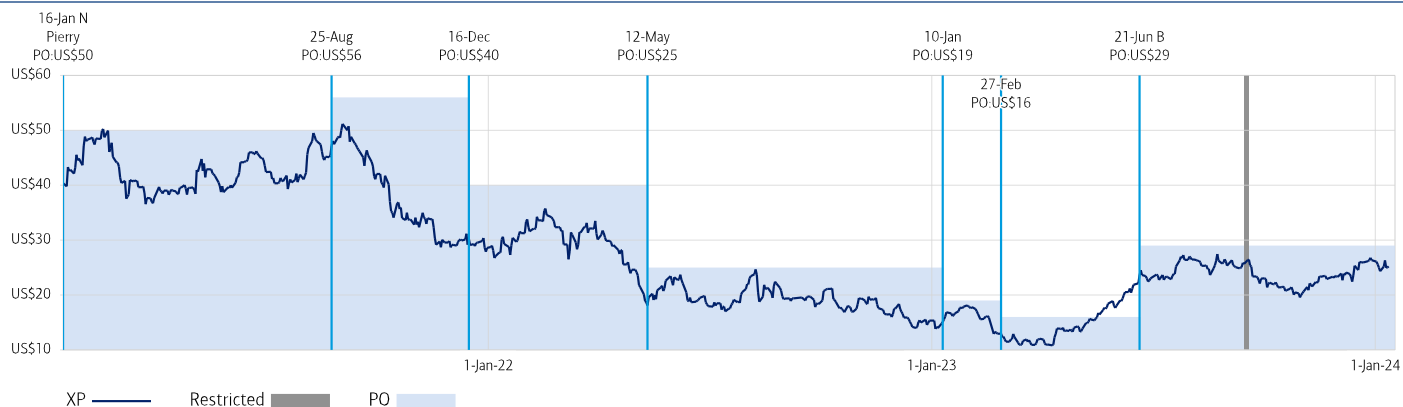
B: Buy, N: Neutral, U: Underperform, PO: Price Objective, NA: No longer valid, NR: No Rating

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StoneCo (STNE) Price Chart

B: Buy, N: Neutral, U: Underperform, PO: Price Objective, NA: No longer valid, NR: No Rating

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XP Inc. (XP) Price Chart

B: Buy, N: Neutral, U: Underperform, PO: Price Objective, NA: No longer valid, NR: No Rating

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Equity Investment Rating Distribution: Banks Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R1}	Count	Percent
Buy	100	49.75%	Buy	84	84.00%
Hold	54	26.87%	Hold	41	75.93%
Sell	47	23.38%	Sell	35	74.47%

Equity Investment Rating Distribution: Financial Services Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R1}	Count	Percent
Buy	156	53.79%	Buy	94	60.26%
Hold	72	24.83%	Hold	48	66.67%
Sell	62	21.38%	Sell	35	56.45%

Equity Investment Rating Distribution: Technology Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R1}	Count	Percent
Buy	215	53.09%	Buy	111	51.63%
Hold	97	23.95%	Hold	45	46.39%
Sell	93	22.96%	Sell	24	25.81%

Equity Investment Rating Distribution: Global Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R1}	Count	Percent
Buy	1895	53.62%	Buy	1083	57.15%
Hold	832	23.54%	Hold	454	54.57%
Sell	807	22.84%	Sell	383	47.46%

^{R1} Issuers that were investment banking clients of BofA Securities or one of its affiliates within the past 12 months. For purposes of this Investment Rating Distribution, the coverage universe includes only stocks. A stock rated Neutral is included as a Hold, and a stock rated Underperform is included as a Sell.

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Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster ^{R2}
Buy	≥ 10%	≤ 70%
Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

^{R2} Ratings dispersions may vary from time to time where BofA Global Research believes it better reflects the investment prospects of stocks in a Coverage Cluster.

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