Banks - LatAm

European investors looking to add to structural longs

Industry Overview

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Equity
Latin America
Banks

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Renewed expectations of lower rates in Brazil

We spent the past week meeting with investors in Europe. While the recent inflation print in Brazil led to a significant re-rating of growth names on renewed expectations of lower rates in the future, we sensed that investors were already positioned in equities and looking to add to their positions. While most agreed that operating trends should be unexciting in 2023, they were generally positive about the technicals, as valuations appear attractive on a relative and historical basis and low allocation from domestic investors.

XP preferred among Brazilian nonbanks

Discussions centered on the magnitude of rate cuts rather than on the direction of rates. Those more bullish that rates have room to decline more aggressively were most interested in discussing XP. The payments sector attracted lukewarm demand given concerns about competitive dynamics, although Stone seemed preferred given a potential self-help story. The insurance sector was mostly viewed as last year's story.

Bradesco on the radar; concerns about the sector

Bradesco was the most demanded name among Brazilian banks, as valuation is hovering around historical lows. The debate was on whether the bank was having structural rather than just cyclical issues, and thus investors were not necessarily willing to give management the benefit of the doubt (waiting for earnings to inflect before buying). Overall, most investors were concerned about the banking sector's earnings growth potential in a challenging operating environment (deteriorating asset-quality trends and declining revenue generation on loan book de-risking) and uncertain regulatory and competitive environment. Finally, contrary to our recent meetings in the US and Brazil, we saw low demand on Nubank due to valuation.

Secular trends could support premium valuation in Mexico

Mexican banks remained well liked as the reshoring theme is well understood. While LatAm-dedicated investors were mostly concerned about recent outperformance and premium valuation to the rest of the region, global investors argued that premium valuation should be supported by scarcity premium and as Mexico could be about to enter a secular credit lending cycle.

Peru most attractive in the Andean region

We noticed only small interest in the Andean region, but investors agreed that Peruvian banks (BAP and IFS) enjoy better earnings growth and modestly better profitability. On the other hand, investors are looking closely at Santander Chile on expectations of an earnings inflection in the second half of the year.

Refer to important disclosures on page 7 to 9. Analyst Certification on page 5. Price Objective Basis/Risk on page 3.
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Brazil banks

We maintain our Neutral rating on Bradesco, as earnings momentum should remain weak, while valuation should prevent further underperformance.

We like Nubank's earnings momentum, but we find valuation expensive at 4.0x 2023E price/book value (P/B). We maintain our Neutral rating.

Brazil non-banks

XP should benefit from lower rates, but downward revisions on consensus and expected weak momentum in coming quarters should prevent outperformance. We maintain our Neutral rating.

We like Stone's earnings momentum in 2023, but we maintain our Neutral rating, as we wait for better visibility on strategy and execution following changes in senior management, and we find valuation demanding at 17x 2023E P/E

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Andean banks

We expect Peruvian banks Credicorp (BAP) and Intercorp Financial (IFS) to show double-digit earnings growth and higher ROAEs, and we maintain our Buy ratings.

We think that Santander Chile is poised to show EPS contraction in 2023 due to lower inflation, political uncertainty, and the economic recession. We maintain our Underperform rating.

Exhibit 1: Stocks mentioned
Prices and ratings for stocks mentioned in this report

BofA Ticker	Bloomberg ticker	Company name	Price	Rating
BRDPF	BBDC4 BZ	Bradesco	BRL 13.79	B-2-7
BBD	BBD US	Bradesco -A	US$ 2.81	C-2-7
BAP	BAP US	Credicorp Ltd	US$ 131.62	B-1-7
IFS	IFS US	Intercorp Financial	US$ 23.9	C-1-7
NU	NU US	Nubank	US$ 4.66	C-2-9
BSAC	BSAC US	Santander Chile	US$ 18.72	B-3-7
XLDTF	BSAN CI	Santander Chile	CLP 37.46	A-3-7
STNE	STNE US	StoneCo	US$ 11.84	C-2-9

Exhibit 1: Stocks mentioned
Prices and ratings for stocks mentioned in this report

XP	XP US	XP Inc.	US$ 13.87	C-2-9

Source: BofA Global Research

BofA GLOBAL RESEARCH

Price objective basis & risk

Banco Santander Chile (BSAC)

Our price objective for Santander Chile of USD18 per ADR / CLP$37 per share is based on a Gordon Growth model, assuming a sustainable ROE of 19%, cost of equity of 13.4% in nominal CLP and a perpetual growth rate of 4% in nominal CLP. Our cost of equity is derived using a capital asset pricing model with a Chile sovereign spread of 165 bp and a beta of 1.1x (political/macro uncertainty)

Upside risks to our PO are higher inflation levels, greater cost-controls and better than expected macro impacting loan growth and asset quality.

Downside risks to our PO are NIM margin pressure from lower inflation levels and an upward trend in the effective tax rate.

Banco Santander Chile (XLDTF)

Our price objective for Santander Chile of USD18 per ADR / CLP$37 per share is based on a Gordon Growth model, assuming a sustainable ROE of 19%, cost of equity of 13.4% in nominal CLP and a perpetual growth rate of 4% in nominal CLP. Our cost of equity is derived using a capital asset pricing model with a Chile sovereign spread of 165 bp and a beta of 1.1x (political/macro uncertainty)

Upside risks to our PO are higher inflation levels, greater cost-controls and better than expected macro impacting loan growth and asset quality.

Downside risks to our PO are NIM margin pressure from lower inflation levels and an upward trend in the effective tax rate.

Bradesco (BRDPF / BBD)

Our price objective (PO) for Bradesco of R$15/US$2.73 is derived from the Gordon Growth Model, assuming a sustainable ROE of 15%, a COE of 14.7%, and 4% growth in perpetuity. Our PO implies a target '23E P/BV multiple of 1.0x. Our USD/ADR PO is derived from the local PO converted at a 5.50 FX rate.

Downside risks to our PO are 1) weaker economic activity could negatively impact loan growth, 2) corporate NPL deterioration, and 3) regulatory changes could be detrimental to profitability. Upside risks include: 1) stronger than forecasted loan portfolio growth, 2) earlier than expected Selic rate cuts benefiting Market NII and, 3) lower than expected provision charges.

Credicorp Ltd (BAP)

Our price objective for Credicorp of US$161 ADR is based on a Gordon Growth valuation model. The main inputs are sustainable ROE of 18%, cost of equity of 13.0% and growth of 4%. Our PO implies a target P/BV of 1.5x

Downside risks to our PO are (1) unfriendly economic policies, and (2) higher deterioration in the bank's retail, SME and microfinance portfolio. Meanwhile, upside risk imply (1) a faster economic growth supported by metals and domestic economy, (2) lower asset quality deterioration, and (3) and pro-market economic policies announced by the new administration.

IFS (IFS)

Our price objective for IFS of US$34 per share is derived from the Gordon Growth Model, assuming a COE of 13.6% (reflecting a US risk-free rate of 3.0%, Peru country risk of 180bp, and beta of 1.2x (uncertainty on the economic policies of the new administration, and lower liquidity vs. BAP), a sustainable ROE of 18% (in line with our estimates) and 4% growth in perpetuity.

Downside risks are 1) asset quality deterioration under a weaker macro scenario, 2) political noise on presidential elections, 3) a potential currency mismatch & changes in interest rates, 4) regulatory risks on the insurance business, and 5) lower demand for commodities by China.

Upside risks are 1) stronger economic activity, 2) entering the SME and unbanked segments, while maintaining solid asset quality trends, 3) improved efficiencies by migrating to digital channels, 4) pro-market economic policies.

Nubank (NU)

We calculate our price objective of $5.5 based on a DDM model, assuming payout increasing from 0% to 35% at perpetuity, and ROE reaching 24% in perpetuity. We assume CoE of 15.0%, reflecting: i) risk free rate of 350bp, ii) country risk of 350bp, equity risk premium of 570bp and beta of 1.4.

Downside risks to our price objective are: 1) an economic downturn, 2) intensifying competitive landscape, and 3) adverse changes to the regulator environment.

StoneCo (STNE)

Our PO of US$13 is derived from a target P/E of 20x on our '23 non-GAAP EPS estimate of US$0.65, one standard deviation below historical average, reflecting a higher rate environment, and 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) the company's dual-class capital structure leaves most of the voting powers to founding shareholders and prevents the stock from being included in certain indices, such as FTSE Russell, S&P Dow Jones and MSCI, 4) M&A risks from the Linx transaction and 5) worst than expected performance of the credit business.

Upside risks: 1) faster than expected economic recovery, 2) better than expected growth of Ton, 3) better than expected integration with Linx, leading to operating leverage gains and 4) better than expected recovery of the credit business.

XP Inc. (XP)

Our PO of $16 is based on a target P/E multiple of 13x our '23 GAAP EPS estimate of $1.25. Our target multiple is in line with a global peer average, which we think is appropriate considering XP's higher longer-term growth potential but more challenging outlook in the short-term.

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

We, Mario Pierry, Antonio Ruette, Ernesto Gabilondo and Flavio Yoshida, hereby certify that the views each of us has expressed in this research report accurately reflect each of our respective personal views about the subject securities and issuers. We also certify that no part of our respective compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

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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
	Banco do Brasil	XBBAF	BBAS3 BZ	Mario Pierry
	Banco do Brasil	BDORY	BDORY US	Mario Pierry
	Bancolombia	CIB	CIB US	Ernesto Gabilondo
	Bancolombia	XAFFF	PFBCOLO CB	Ernesto Gabilondo
	Banorte	GBOOF	GFNORTEO MM	Mario Pierry
	Banorte	GBOOY	GBOOY US	Mario Pierry
	BB Seguridade	XBDPF	BBSE3 BZ	Mario Pierry
	BB Seguridade	BBSEY	BBSEY US	Mario Pierry
	Bci	BZCIF	BCI CI	Ernesto Gabilondo
	BTG Pactual	XNXCF	BPAC11 BZ	Flavio Yoshida
	Caixa Seguridade	XDXUF	CXSE3 BZ	Mario Pierry
	Cielo	CIOXF	CIEL3 BZ	Mario Pierry
	Cielo	CIOXY	CIOXY US	Mario Pierry
	ClearSale	XZUOF	CLSA3 BZ	Flavio Yoshida
	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
NEUTRAL				
	Bajio	BBAJF	BBAJIOO MM	Ernesto Gabilondo
	Banrisul	XGRBF	BRSR6 BZ	Flavio Yoshida
	Bradesco	BRDPF	BBDC4 BZ	Mario Pierry
	Bradesco -A	BBD	BBD US	Mario Pierry
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	Itau Unibanco	ITUB	ITUB US	Mario Pierry
	Nubank	NU	NU US	Mario Pierry
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	StoneCo	STNE	STNE US	Mario Pierry
	XP Inc.	XP	XP US	Mario Pierry
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	Grupo Financiero Galicia	GGABF	GGAL AR	Ernesto Gabilondo
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	Santander Brasil	BSBR	BSBR US	Mario Pierry
	Supervielle	SUPV	SUPV US	Ernesto Gabilondo
	Supervielle	XAZFF	SUPV AR	Ernesto Gabilondo

Disclosures

Important Disclosures

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

Coverage Universe	Count	Percent	Inv. Banking Relationships R1	Count	Percent
Buy	88	50.87%	Buy	72	81.82%
Hold	40	23.12%	Hold	29	72.50%
Sell	45	26.01%	Sell	34	75.56%

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

Coverage Universe	Count	Percent	Inv. Banking Relationships R1	Count	Percent
Buy	152	52.41%	Buy	92	60.53%
Hold	73	25.17%	Hold	44	60.27%
Sell	65	22.41%	Sell	41	63.08%

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

Coverage Universe	Count	Percent	Inv. Banking Relationships R1	Count	Percent
Buy	1869	53.01%	Buy	1030	55.11%
Hold	827	23.45%	Hold	476	57.56%
Sell	830	23.54%	Sell	389	46.87%

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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