Q1 2020 Earnings Call

Company Participants

- Inacio Caminha, Investor Relations Superintendent
- Mauro Dutra Mediano Dias, Chief Financial Officer and Investor Relations Officer

Other Participants

- Jorge Kuri, Analyst

Presentation

Operator

Good afternoon ladies and gentlemen and welcome to Banco PAN Conference Call to discuss the First Quarter of 2020 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/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 section. At that time, further instructions will be given.

(Operator Instructions)

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.

With us here today, we have Mr. Mauro Dutra; Banco PAN CFO and IRO and Mr. Inacio 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 Mediano Dias {BIO 21792010 <GO>}

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 first quarter of 2020.

In this first quarter, we had a major change in the macro-economic scenario caused by the COVID-19 pandemic. And so it brings here, a lot of challenges -- and mainly uncertainty for the future. So in this first slide, slide three. We highlighted the actions we've 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 condition 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, 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 are 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. I mean we can reach our clients and help them only digitally. The second step is our customized benefits and extended offers, which are made on tailored base. Overdrafts rated have been reduced to 4% per month and we also extended the installments of the credit card products up to 24 month.

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 products, all our credit products, we are maintaining our solid capital level and increasing cost efficiency.

Moving to the slide four, I would highlight, before I start to present the slide. I would highlight that those actions are only tactical. Our strategy, our long-term strategy hasn't 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 reached 41% of digital formalization in the first quarter, and more than BRL3 billion since April '19. In the vehicle business, we reached 70% of digital formalization in the first quarter, and more than BRL1.2 billion since October '19. In our digital Bank we launched the digital account app on February 5th, two months ago approximately three months ago, sorry.

We enhance 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 BRL25 billion in the first quarter, and 19% increase in the last 12 months. We had for this period, a monthly average retail origination of BRL1.8 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 BRl170 million in the first quarter of the year, slightly above last quarter.

The ROE for this period was 13.7% and the adjusted ROE was 23.5%. Both figures indicate robust profitability of our business and a lot in-line with the last quarter. To end the highlight section. I would mention, our shareholders' equity, our net worth, which is worth BRL5 billion in March '20 and our Basel ratio of 15.7%, which is a very strong level in our view and prepare us to the crisis we are going to face, we are already facing and we are going to face during this period.

I will now let Inacio, talk to you about the earning and detailed figure of the business.

Inacio Caminha {BIO 19326001 <GO>}

Thank you. So 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 reducing the credit assignments. We assigned 1.7 billion in 4Q, and we assigned around BRL900 million in this 1Q'20. So this let to reduction in the margins. But we still keep very strong levels of spreads in the credit portfolio contributing to the level of this net interest margin. As of provisions, we ended the portfolio with BRL322 million and this gross expenses when we compare the net expenses over the portfolio, we see a reduction to 3.8%.

And this quarter we had a -- we sold written-off portfolio for BRL33 million, and this contributed to the recoveries, so totaling BRL89 million in the quarter. As for origination expenses, we had BRL276 million, expanding a little bit, mainly because of volume and mix of the loans originated in the quarter. And personnel and administrative expenses totaled BRL378 million, decreasing in three months due to one-off expenses in the 4Q. For example marketing and operational expenses. Looking at the chart for the -- the income before tax and net income we have BRL210 million before tax and BRL171 million net income emphasizing the recurrency of results and also showing that our strategy has been proven right, over the past quarters.

For the ROE adjusted, 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 two 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 paid to the market, we would have BRL225 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 BRL3.8 billion equity instead of the BRL4.9 million average equity in the quarter. So, 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 BRL1.8 billion in this Q, totaling BRL5.4 billion in three months, increasing 13% in the last 12 months. In payroll, we reached an average of BRL933 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 BRL483 million per month, a 11% lower than last quarter, but 17% higher than the 1Q '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 BRL375 million per month, reducing a little bit over 4Q, mainly because of seasonality. But increasingly, 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 BRL13.3 billion, increasing 6% in the quarter and 13% in 12 months.

Vehicle comes with BRL9.3 billion outstanding, increasing 5% in the quarter and 26% in 12 months and credit card with BRL1.1 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 BRL25 billion.

And here it is worth mentioning, especially in this moment that the portfolios with collateral and also payroll loan portfolio 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, these totaled BRL850 million in this quarter, significantly lower than the BRL1.7 billion we assigned in the 4Q'19. So when we look at the originator portfolio adding up the portfolios assigned to the controlling shareholders we ended the quarter with BRL32.3 billion flat over last quarter, but increasing the retained portfolio.

As for credit quality, looking at retail on slide 10. We can highlight first the conservative credit origination approach for payroll for instance, we have 88% focused on federal codes, with 35% months duration and an average ticket of BRL2,400. This lower ticket in the quarter reflects the readjustment that we had for benefits of the retirees and pensioners.

So resulting in lower loan amount. As for vehicles, we also have a very good standards of underwriting with 35% down payments on vehicles and 21% in motorcycles, remembering that in vehicles, we financed mostly used cars from four to eight 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 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 BRL93 million per month out of those 92% regarding loans and 8% in credit cards.

As Dutra mentioned, we average 41% of these loans formalized through our digital platform. And this has been very important as a competitive differential in the market. And if we look at March alone, it was responsible for 49% of our origination. So, since the beginning we did 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 BRL13.3 billion representing 53%.

On slide 12, we have some data on vehicle financing. The lower volume relates to -- of origination 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 signs of the -- 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-payment, considering also the tenor of the loans. And here we also see the digital platform reaching very relevant levels. So in the first five months of the operation when it was launched in October, we had already formalized BRL1.2 billion in the digital loans for vehicle financing, 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 these moments of lock down. On payments, talking 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 the -- this type of products, especially in these times.

We ended the portfolio at BRL1.1 billion, also transacting BRL1.1 billion in the entire quarter. As for insurance premiums on slide 14, we originated a monthly average of BRL30 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 BRL24.8 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 is 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% of 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.

Questions And Answers

Operator

Ladies and gentlemen, we will now begin the Q&A section. (Operator Instructions) Jorge Kuri from Morgan Stanley, would like to make a question.

Q - Jorge Kuri {BIO 3937764 <GO>}

Hi, good morning, everyone. Hope everyone is well. And two questions if I may. The first one is could you talk about origination trends during the month of April for your key product. And second any idea at this point, where the cost of risk may end up for the year? Thank you.

A - Inacio Caminha {BIO 19326001 <GO>}

So 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 -- in 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 markets has suffered a little bit more because of the lockdown. There was a news about the vehicle sales dropping significantly. So, in these two big markets, which are the 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.

A - Mauro Dutra Mediano Dias {BIO 21792010 <GO>}

And about the cost of risk, Kuri this is Dutra speaking here. This answer I'd like to divide in two. The first one is our balance sheet. When we look to our balance sheet, we can see a credit portfolio that is focused on very defensive products, Like -- as Inacio 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'd like to mention is that in the last quarter of 2019, we increased our provisional 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 to face -- at the moment to face the crisis. The second part of this answer is the NPL ratios. Right. 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 where 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.

Q - Jorge Kuri {BIO 3937764 <GO>}

Thank you very much.

Operator

(Operator Instructions) Since there seems to be no further questions, I would like to turn the floor over to Mr. Inacio Caminha for his final remarks.

A - Inacio Caminha {BIO 19326001 <GO>}

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

Operator

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