

Q3 2021 Earnings Call

Company Participants

- Joao Marcello Dantas Leite, Executive Officer and Chief Financial Officer
- Roberto Balls Sallouti, Chief Executive Officer

Other Participants

- Gustavo Schroden
- Jorge Kuri
- Pedro Leduc
- Tito Labarta

Presentation

Operator

Good afternoon and welcome to the third quarter of 2021 results conference call of Banco BTG Pactual. With us here today we have Roberto Sallouti, Joao Dantas and , Jose Miguel Vilela. We would like to inform you that this event is being recorded and all participants will be in a listen-only mode during the bank's presentation. After Banco BTG Pactual's remarks, there will be a question-and-answer session for investors and analysts when further instructions will be given. Today, we have a simultaneous webcast that may be accessed through the website www.btcactual.com/ir in the platform.

Before proceeding, let me mention that this call may contain forward-looking statements relating to the prospects of the business, estimates for operating financial results, and those related to the growth prospects of Banco BTG Pactual. These are merely projections and as such are based exclusively on the expectations of Banco BTG Pactual's management concerning the future of the business.

Such forward-looking statements depends substantially on changing market conditions, government regulations, competitive pressures, the performance of the Brazilian economy, and the industry among other factors and risks disclosed in Banco BTG Pactual's filed disclosure documents, and are therefore subject to change without prior notice.

Now, I'll turn the floor to Mr.Roberto Sallouti, who will begin the presentation. Mr.Sallouti, please go ahead.

Roberto Balls Sallouti {BIO 4150617 <GO>}

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Thank you very much. Good morning, everyone. Thank you for joining our call. If we go start at please on Page 3 of the presentation. We're very, very happy with the results of this quarter. Across the board, be it net new money, be it level of revenues or be it level of income.

So for the quarter, we had net new money of BRL88 billion. If you exclude last quarter where we had non-organic net new money from the acquisition of Necton, it's the highest ever. This takes our nine-month year-to-date net new money to BRL261 billion. Our AUM, assets under management or asset management business grew 65% year-over-year, reaching BRL542 billion, and wealth management grew 81% year-over-year, reaching BRL400 billion. This takes our total custody to BRL942 billion, very close to reaching the emblematic BRL1 trillion mark, which hopefully we expect to happen sometime this quarter.

Turning to Page 4, as I mentioned, we had another record quarter for revenues and net income. Revenues grew 55%, reaching BRL3.8 billion. Net income grew 77%, reaching BRL1.8 billion. This being the result of 20.1% return on equity for the quarter.

On Page 5, we show our funding, Basel and credit portfolio. We continue to have very strong funding inflows. We've been able to keep a very solid capital metrics and a high-quality credit portfolio even as we grow. So our own secured funding grew 45% year-over-year reaching BRL146 billion. We closed the quarter with a Basel ratio of 16.1% and our credit and -- our corporate and SME portfolio grew 43% reaching BRL98 billion, BRL14 billion of which in SME.

Important to qualify here that we have very -- basically no growth in SME because of the issues that we're having with the central clearing of the credit card receivables. So basically credit card receivables quarter-over-quarter decreased and we slightly increased our supply chain financing portfolio. And also important to mention that Q3 had very strong seasonality, so we expect a more moderate growth of our portfolio in the fourth quarter.

Turning to Page 6. We have what we have been showing since we became a public company, so just recapitulating some key figures here. For the third quarter we had revenues of BRL3.8 billion, net income of BRL1.8, ROE of BRL20.1. Our cost to income ratio has been on the lower margin of the band that we have, so historically we've been between 41% and 45%. Cost to income ratio this quarter was around 42.6%. We closed the quarter with total assets of BRL372 billion and shareholders' equity of BRL36.3 billion. And in the quarter, we had a share of VaR of 28 bps, below our historical levels.

Turning to Page 7, we return to the year-to-date results where we had revenues of BRL10.4 billion, net income of BRL4.7 billion. So, for the nine months of the year, a return on equity of 20.6%. Cost to income also on the lower band of the band that I mentioned, 42.1%.

Turning to Page 8, you see the distribution of the different business signs and the revenues, and you see very strong growth from our clients and less volatile businesses. So investment banking growing 80% - 81%, corporate lending 51%. Investment management,

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which is a combination of asset and wealth management 47%, and sales and trading 46%. You see that investment banking, corporate lending and investment management are all around 20% of our revenues. And we expect this number to continue growing over time, especially in corporate lending and investment management over the next few quarters and years.

If you go to Page 9, we mentioned some of the ESG and impact investing accomplishments for the quarter. To start, it's worth mentioning the two prizes that we got, basically the recognition for what we've been doing. So for global finance, we got the Outstanding Sustainable Financing in Emerging Markets Awards. And from Environmental Finance, the Impact Initiative of the Year for the Latin American and Caribbean region.

Our green portfolio reached BRL6.1 billion at the end of the quarter. And in the quarter, we distributed for our clients over \$1 billion in sustainable finance instruments, bringing our -- let's say, since 2016 that number to over \$7 billion. We also joined the task force for nature-related financial disclosure and the CFO task force for SDGs. We think this is state-of-the-art reporting regarding ESG. We also launched a new product, ESG recommended portfolio for our clients. And finally, in Q3, we announced a collaboration with The Nature Conservancy, the world's largest NGO focused on preservation. And they will be our impact advisors for our forest management business in the U.S.

And actually in the fourth quarter, we announced a partnership with Conservation International where they will be our impact advisors for the reforestation funds that we're launching in Latin America. So, I think this tests the quality of the work we're doing and how we are perceived by very important stakeholders in the environmental world. And we think we're very excited that these partnerships will allow us to increase the impact of this asset management business that we have.

With that, I pass the floor to Dantas, who will speak about the performance of each of the business units.

Joao Marcello Dantas Leite {BIO 17617595 <GO>}

Thank you, Roberto. Thank you all for joining our call. This has been a very important and strong quarter and there's many interesting highlights and ideas to share with you. So starting right away on Page 5, here we have -- sorry Page 11, here we have investment banking. The investment banking business reached BRL727 million of income, 81% above the same quarter one year-ago. And if you look at the right part of the graph, you will see that the accumulated revenues in the nine months of 2021 have reached close to BRL1.9 billion, which is already 43% above 2020 full-year, which was in turn 40% above 2019 full-year.

So, it's fair to say that our investment banking business has made a very strong progress in the last three years. We have not only maintained our leadership position in the industry, especially in ECM and M&A, but also we have captured an even higher share of the total fee pool in LATAM. M&A and DCM revenues are growing more than ECM, that's a trend for the last couple of years, and is also a trend that we expect for next year. And

we became leaders in both international and local DCM for Brazilian clients. We are amongst the top banks in Brazil for local DCM. And in the third quarter, we ranked the number one international DCM bank for Brazilian companies. So, that is what explains this new plateau of revenues for the business. Not only as I said, we're growing our participation in the total fee pool, but also we did a significant catch up on the DCM rankings, which is exactly where the fee pool is growing. So all in all, a very good quarter for investment banking.

Turning to Page 12, and starting from the right part of the page. You see that our corporate and SME lending portfolio reached BRL97.6 billion, of which BRL14.3 billion is from SME lending. That's a 13% growth compared to the third -- to the second quarter of 2021. So 13% in the quarter and 43% growth year-on-year. Our revenues reached BRL642 million, 51% above the same quarter one year ago, slightly below the second quarter for reasons I'll explain. Our portfolio is expanding quarter-on-quarter continuously for the last five years, and that portfolio continues to be composed of exposure to the best companies in Latin America. Even our SME lending is fully collateralized by credit for suppliers of top-quality large corporates as Roberto mentioned, today that's the main and almost only exposure we have inside SME lending, it's the supply chain financing. Revenues are growing very fast, 51% revenue growth year-on-year is even more than the 43% growth of the portfolio year-on-year and that is for two reasons.

Number one, as we grow the portfolio and we maintain the quality, or even expand I would say the quality of the disbursements, we also maintain the spread levels. And the second contribution, which has been very important for the revenues is special situations that also has been expanding over the years. Special situation revenues in the third quarter were smaller than in the second quarter, just slightly smaller. And that is what explains this small reduction in total revenues for the quarter. We don't expect the portfolio to continue to expand in the same pace in 2022, even though it will continue to grow. And we will continue to privilege as we grow the very high quality of the assets. We are very satisfied with the current level of provisions in there, satisfied with the result of corporate and the SME lending.

Just to finalize, I think it's an important recognition to mention. We were awarded the best SME bank in Brazil by global finance. Considering that we just launched our current account for SMEs, which is entirely digital and that we are operating still with a single product, which is the supply chain financing. We believe that this award is not only very important, but also indicates our potential as we deploy more products and services to that segment of clients.

Moving to Page 13, here we have a little bit of the sales and trading, which had a strong performance with larger contribution from three businesses and also a contribution from the sale of CredPago, which I will explain in more details. So starting from the right on the page, we have the VaR market risk metrics. You see that we have about 11% of our regulatory capital deployed to support market risk component of capital requirements, which is a historical -- historically very low level. And also we're running the bank, we have about 0.28% of average equity in terms of VaR, which is in the very low bound of that range of VaR usage. There is a clear trajectory of lower use of balance sheet with growing contribution of fees and flow to the revenue mix of sales and trading.

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The strong revenues in the quarter, which are our highest since our IPO, benefiting part from the sale of CredPago, which is our residential lease insurance platform, which we sold to Loft, which is a residential real estate platform in Brazil. As we announced to markets, the sale represents a BRL1.4 billion revenues that were generated in the transaction. Off which, BRL520 million are included in the sales and trading revenues in the current quarters. So, from the BRL1.3 billion of revenues we have about BRL500 billion coming from revenues, coming from the sale of CredPago, and BRL800 million from the other sales and trading businesses. We expect the remainder, the balance of the BRL1.4 billion of these revenues to materialize during 2022 and 2023. So all in all, a very strong quarter for sales and trading with this highlight of very low utilization of balance sheet resources to produce the revenues. So more contribution from fees and from flow trading, less usage of balance sheet in the quarter. And that is a trend that we expect to maintain going forward.

Moving on to Page 14, here we have our asset management business. And starting from the right part of the page you will see, this is our fourth consecutive quarter of record breaking net new money and growing management fee income in consequence of that. Our total assets under management have reached BRL542 billion, which is 8% above last quarter, and 65% above the same quarter one year ago. We had BRL50 billion net new money in the quarter. We had BRL136 billion net new money in the nine months of 2021. And that means approximately BRL15 billion of net new money per month only in our asset management business. Revenues are growing 8% quarter-on-quarter. They are now composed mainly of management fees, which are growing 31% year-over-year. If you just take the component of management fees inside the revenues of asset management, the growth is 31% year-on-year, which is of course a more stable revenue component for asset management.

And important to note, management fees have been stable in the last quarters and years inside each asset class. So there is a change in the mix of assets. We are growing as you know more in non-discretionary management -- mandates then on funds managed by our portfolio managers. And in turn, there's a change in mix. But inside each asset class, we have been being able to charge our clients the same ROEs because we already charge very competitive management fees in the industry. The strong AUM growth already commands for higher management fees going forward. That's a mathematical consequence of the higher average AUM that converges to the peak AUM. So as we continue to grow or even we stabilize at this higher plateau, we are able to produce more management fees going forward.

I would highlight last but not least point here on the page, which Roberto already touched upon, which is the launch of a new product in asset management which is a reforestation fund. It's a \$1 billion capital raising to finance projects in Brazil, Uruguay, and Chile in collaboration with Conservation International. What we're doing here are Timberland Asset Management business acquires degraded land and dedicates half of it for trees that are permanent forest. So local species that are planted and kept permanently, and the other half of the land is dedicated to commercial timber, so eucalyptus. It wouldn't be viable in terms of returns before, but now by adding the carbon certificates that you are able to issue with that kind of business, and which are going to be attested in this collaboration with Conservation International, then the business becomes

viable. So it's not only a good financial results for our clients and industry, but also a very significant impact to reforestation and for the nature.

Moving to Page 15, here is our wealth management and consumer banking results, a lot to highlight here. As you see, starting from the right of the page, our well under management reached BRL400 billion, growing 81% year-on-year. Our net new money in the quarter was BRL37.7 billion, only slightly below second quarter if we consider that in the second quarter we had the consolidation of Necton. So this not including the consolidation of Necton, net new money in the second quarter would have been BRL42 billion comparing to the BRL37 billion -- BRL37.7 billion in the third quarter. For the nine-month period of the year, our net new money was BRL124 billion or BRL14 billion per month. On top of the BRL15 billion per month that we attracted as net new money in our asset management business, so both businesses growing significantly in a very strong pace.

Revenues are growing 75% year-on-year and that's consistent with the growth in our wealth under management. I would say we could not be more satisfied with the results of this very hard and competent work that is being put out by all our teams, be the front office or back office teams. It's fair to say that Brazilian individuals continue to look for the best place where to put their investments and to invest their assets, and we are the main beneficiaries of that continuous flow that we see. So regardless of more allocation to fixed income or more allocation to equities, times of uncertainty underline even further the need for you to side with the best advisor for you to invest your investable assets with, one that understands your suitability and your risk appetite. And that provides the best returns given your risk appetite. And that's what we do. This is what maximizes long-term value.

The lifetime value of the customer relationship is maximized with that approach, even though in the short-term you can wave in part the potential to generate floating revenues more brokerage fees, but in the long-term you maximize your relationship with your customer. The perception of value added is more clear and that's the path that we want to pursue always. Also important to highlight our consumer banking developments, the consumer banking platform. Our current -- digital current account was awarded with two very significant awards in the quarter. The most -- we were awarded the most customer-centric bank by Global Economics and best customer service locally in Brazil. So I like to say that we are the best-in-class and most innovative digital consumer bank. Which sides with our best-in-class and most innovative digital investment platform, providing our clients have full range and one-stop-shop approach for banking and investments digitally.

Moving to page 16, now we have principal investments and participations over the last of our businesses, and the smallest since we have been by design reducing our allocations in principle investments. We reached BRL136 million of principal investment revenues basically coming from a very strong net income, share of profit from Eneva. And also, a share of profit from Prime Oil. It's smaller than the BRL242 million of the second quarter of 2021, even though there's strong contribution from these two investments, but we didn't make strong revenues from global markets in the quarter.

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Looking at participation earnings, we have stable net income flows from Banco and from Too Seguros, which is offset in part as demonstrated in the bar by goodwill amortization from our last acquisition of the voting shares from of Banco Pan from Corretora. So on that opportunity, we did acquire with a premium over the book value of Banco Pan. And because of that premium, and given Brazilian accounting standards, we need to amortize over time the goodwill from that investment, which reduces the BRL146 million of equity pickup revenues to BRL91 million, net of the amortization costs. Also important to remember, both our investments in Eneva, which is about BRL3.7 billion and in Banco Pan are booked at very -- are booked very below the mark-to-market even if you consider the current market prices. As we carry both under the equity method of accounting, more close to the book value and vary below in a conservative way from the market value.

Moving to Section 2. Here we have the expenses and main performance ratios. Our cost to income ratio is in this quarter in line with the historical average. Our average, as Roberto mentioned, ranges from 41% to 45% cost to income ratio. Probably going forward we will see cost to income ratio going slightly up to the upper bound of that range, but not -- we don't see reason to go beyond that. The cost base has expanded 9% quarter-on-quarter in salaries and benefits, and 27% quarter-on-quarter on administrative and other costs. This is basically a growth that is in line with the headcount increase. Also in administrative and other costs because there we have the cost of IT vendors. But it's fair to say that we continue to make significant additional investments. We are constantly upgrading launching more products and new services. And the number of people we have is compatible with the big advances that we see in our wealth management and consumer banking platform.

Mainly that one, but there are our technological advances throughout all our businesses, be it credit, be it sales and trading or corporate lending or any client franchise. And we are doing these additional investments without impacting the growth of our profit margin. As you saw, we are growing revenues 55%, but we're growing profits 75% year-on-year. So costs have increased nominally, but they don't put pressure in the increase of the margin, the bottom line contribution. Also important to highlight the effective income tax rate in the quarter of 21.1%, which we consider very efficient. This is due to the mix of revenues and to the use of JCP. And we expect that JCP will prevail, will be maintained in Brazil for the next year, and also we don't expect corporate income tax to go down since we don't expect at this point that the tax reform should be approved this year.

Moving to Page 20 on Section 3. This is the balance sheet analysis. As you see, we have reached BRL307.2 billion of assets growing from the BRL335.2 billion of assets of the previous quarter. We're running the bank with about 10.3x assets to equity, going up from about 9.6x assets to equity in the last quarter, which is still a conservative measure for us to run our balance sheet. It's a 11% increase quarter-on-quarter but mostly composed of more leverage in financial instruments and the financing of those financial instrument, so no structural increase here. We are running the bank with record liquidity. We have BRL50 billion in cash, which is almost 1.4x our net equity, which is a very strong measure in terms of the cash that we maintain compared to Brazilian peers or international peers and this is our record liquidity.

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And in result, our LCR, which is the short-term measure of liquidity under stress is at 214%, which is the -- one of the highest among the large banks in Brazil. The on balance sheet credit increased in the quarter BRL12.6 billion, less than the total increase of our corporate lending portfolio because some of the instruments are off balance sheet like standby letters of credit, and the BRL12.6 billion we grow from -- on the banking book, we compare with the BRL18.1 billion growth on the funding base. I'll explain about the funding base on the next page, but very healthy indication. We're growing our unsecured funding base in the quarter about 40% more than the on-balance sheet use of assets. Our coverage ratio is at 184%, which is also very comfortable. And our corporate lending portfolio has reached about 2.7x our net equity, which is also a measure that allows us to continue to expand credit. As I said, less than the current pace for the upcoming quarters. We don't expect the same pace, but we expect to continue to grow.

On Page 21, we have the evolution of unsecured funding base. You see that we reached BRL145 billion of unsecured funding compared to BRL100 billion a year ago, so 45% growth of our funding base. Inside the funding base, I would highlight first of all that the growth comes in all types of instruments, all types of tenors and all counterpart and client segments. So it's a very healthy distribution and a very healthy growth, that is a consistent trend across the last quarters and for the recent years. Demand deposits inside this BRL145 billion represent BRL8.4 billion already or almost 6% of the total funding base, which is quite relevant for a bank like us and indicates that we are really growing inside the upper-income retail.

Our share of retail funding, not only demand deposits, but also term deposit, continue to expand for Banco BTG Pactual alone. Our retail funding is already 15% of the total funding base. And if we include Banco Pan then it's 25% of the total funding base. And also I'd like to highlight here that we have obtained a new green facility, in the amount of \$300 million provided by DFC, which is a permanent multilateral organism International Development Finance Corporation to deploy across Latin America SME activities, and being able to pass the underwriting standards of DFC is something that we believe recognizes the quality of our credit underwriting policies and management.

And finally on Page 22, we have our BIS ratio and VaR. Our capital decreased from 17.3% to 16.1%, being composed predominantly of tangible equity. Our core equity Tier 1 is at 14.2%. We are deploying capital, but still maintain ourselves significantly above the average of the S-1 banks in Brazil, which is -- which are the domestically systemically important banks. We also take into consideration, I think it is important to highlight that post closing during October, we have raised \$900 million of local Tier 2 deposits bonds. And with that, our adjusted BIS capital ratio would have closed the quarter at 16.5%. So almost 50 basis points above the current level. It was a successful raising in the local market, it continues to be open. We can reach a little bit more than a billion on that. And our average daily trading VaR, as we said before, pretty much in line with the second quarter, which means we are producing more revenues and sales and trading with less use of balance sheet.

That is the end of our presentation. I would like once again thank everyone who's participate -- who's participating. And we open now the floor for questions. Thank you very much.

Questions And Answers

Operator

(Question And Answer)

Thank you. The floor is now open for questions for investors and analysts. (Operator Instructions) Our first question is come from Pedro Leduc from Itau.

Q - Pedro Leduc {BIO 16665775 <GO>}

Hello, hello.

Operator

Pedro you may proceed. Hi.

Q - Pedro Leduc {BIO 16665775 <GO>}

Yes. Okay. Hi. Sorry. Good afternoon, everybody. Two questions please here. First on the sales and trading division, like, where you will recognize the gain from the CredPago sale. You mentioned earlier about BRL500 million before in the Portuguese call. I would like to take the opportunity to try to estimate what it had on your bottom line, and I assume something closer to BRL200 million trying to take out SG&A bonus, other OpEx, income tax, so any color there? And how we should include it in the next quarter and remind us how you move to lost and the state there and how this will be booked, just a clarification on that. Thank you.

A - Roberto Balls Sallouti {BIO 4150617 <GO>}

Sure. Pedro. And I appreciate the opportunity to clarify. It's not just a straight forward transaction, but I think I can provide the clarifications that you asked. So, as you recall, we have this closer to markets that the sale of CredPago results in a revenue of about BRL1.4 billion for us. As you know, just to give you some context, we are generally very conservative in our approach to our balance sheet. The sale of CredPago has two components. Besides an upfront cash payment that we already received, there is a long-term receivable component that is not linked with or subject to any performance metrics and there's a smaller proportion of an equity stake in launch.

We are -- what we're doing, we're applying a conservative view to both of these components. So we recognize in this quarter BRL520 million of the total revenues. And for the remaining components, we are applying a conservative approach, which implies a haircut in the receivable and on the equity. As time passes, the uncertainties that we use it to estimate, the haircut will vanish, we believe they will vanish. Time flowing these should vanish, and this is why the full results shall flow through P&L during 2022 and 2023.

On your point of what is the bottom line impact, I won't give you a precise number, but I'll tell you how we do the math, BRL520 million is the top line of which we extract our bonus

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provision, which as you know is 25% of revenues minus costs. We extract transactional costs and we deduct the top line corporate income tax in Brazil, which for the bank who is the seller is 45%. So we can get to a rough estimate of what is the bottom line, which is probably a little bit below what you estimated. The same impact will apply to the upcoming revenue recognition from CredPago sales, everything maintains the same if corporate income tax rate doesn't change in Brazil, we won't change our bonus accrual process and the costs will be recognized as well in accordance with the recognition of revenue. So, this is how it's included in the results, in this quarter. As I said, BRL500 million on top line and the bottom line is about what I told you and close to what you estimate.

Q - Pedro Leduc {BIO 16665775 <GO>}

Okay. No that's super useful. Thank you. Very good. I have another question on the wealth management division, if I may, and here, it includes of course your digital bank and retail investments, wealth under management growth quarter-over-quarter strong net new money. But revenue yields, when we do simple math or revenues over this average flatter which is fine. But we'd like to understand a little more the forces behind these drivers for the wealth management division qualitatively or if you can go review a bit of channel mix between IFAs and direct net new money, product mix. Maybe a bit on the client harvest differences, how you're seeing it on the take rate? Thank you.

A - Roberto Balls Sallouti {BIO 4150617 <GO>}

Thank you, Pedro. So first of all, I think it's important to qualify one thing. The way we report here is we report net return on assets after we give the rebates to the IFAs or to the asset manager or to whatever channel it gets a rebate, so at the end of the day, the ROE of the traditional high-net-worth wealth management business. And let's say, the IFA network business will not be very different. You will have a larger ROE from let's say the direct retail and when consumer banking grows. So over time, you will probably see a gradual increase. But I think it's very important that expectations are adjusted, given how we have chosen to report this, which is the net ROE, net of rebates.

So in that sense, if you grow in the IFA network or if you grow in the wealth management business, there's not going to be a huge difference in ROE. That's a bit difference, when we start having more significant revenues from consumer banking and when you grow in the direct to clients in the investment world. But as you would expect, you have the different channels, so we had a higher beginning point of the traditional wealth management. We have seen a lot of growth from retail, stronger growth from IFAs. On that retail, let's say, a smaller number from the direct-to-consumer and still very just the beginning of consumer banking. So it is probably right to expect that you will have a small increase in our way over times, but given how we have chosen to report this, you will not see a huge increase. And depending on the different -- the behavior of the different channels, clearly we're seeing very strong growth from the new initiatives, from the markets that we had no market share four or five years ago that we answered -- that we entered. We are seeing much stronger growth there from the traditional wealth management where we've been present all of our life.

Q - Pedro Leduc {BIO 16665775 <GO>}

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That's very clear. Very complete also. Thank you.

A - Roberto Balls Sallouti {BIO 4150617 <GO>}

Thank you, Pedro.

Operator

The next question comes from Jorge from Morgan Stanley.

Q - Jorge Kuri {BIO 3937764 <GO>}

Hi. Hello. Can you hear me? It's Jorge Kuri from Morgan Stanley.

A - Roberto Balls Sallouti {BIO 4150617 <GO>}

Yes, we can hear you, Jorge. Go ahead.

A - Joao Marcello Dantas Leite {BIO 17617595 <GO>}

Hi, Jorge.

Q - Jorge Kuri {BIO 3937764 <GO>}

Hi. Good morning, everyone. Congrats on the numbers. I have one question on your expenses. I know you kind of like alluded to an efficiency ratio going forward, but I wanted to be more specific trying to understand just a moving parts on the expenses. Your headcount is about 55% over the last 12 months as you've been developing the new digital business and wealth management business. What do you think should be the growth in your employee base over the next two years? And then, yeah, the admin expenses are also up quite a lot of result of this, what -- how do you see that playing out over the next three years. And at what point do you think you should go back to normalize growth rate of expenses given these businesses that your building. Thank you.

A - Joao Marcello Dantas Leite {BIO 17617595 <GO>}

Thank you, Jorge. That's important question and gives us the opportunity to explain a few of the drivers here. So as I highlighted a new underlying the main component of the expansion on the costs is headcount. We don't expect to continue to grow headcount in the same pace, we actually took advantage of a good timing to add people. We were able to add people without even adding square meters to the office, we're adding square meters as we speak, people are returning to the office. Now, we have more people than office space. But as soon as we finish the renovation of the space, the additional space we got, we'll be able to bring them back.

Also, we were able to attract people in other cities in Brazil. So they work effectively remotely, it's a home office type of approach and especially in technology it worked very well and it allowed us to develop our digital investment platform and our consumer banking platform faster even than we expected. We don't expect the same growth going forward. We are actually expecting to normalize the growth. And so the pressure on the

cost base will reduce with that. I guess, we will still see the cost-to-income ratio go up slightly to the upper bound of our average cost-to-income ratio, which ranges from 41% to 45% in the recent past. And then what we will start to see is the kicking of additional revenues from consumer banking.

Now, as Roberto highlighted, we're not still producing significant revenues, it's kind of a testing period for our digital bank account. We're growing a lot number of users. The number of credit cards issued etcetera. So these two trends beyond 2022 will be very interesting to see very probably beyond '22 at a certain point in time. Wealth management and consumer banking will be the largest revenue in all our business areas. We're still not there, but we're going that direction very fast. And cost will stabilize because we're building a digital bank, we're building a bank with a self-service approach with a lot of digital functionalities, which take away the big part of the heavy burden of the day-to-day relationship and allow us to focus on the Rio value-adding service and the cost of the service will be pursued by the client as value-added on the relationship. So this is how we see and we're quite comfortable that these levels of costs that I indicate to you are the levels that we will probably pursue in 2022.

Q - Jorge Kuri {BIO 3937764 <GO>}

Thanks, Joao. Much appreciated.

A - Joao Marcello Dantas Leite {BIO 17617595 <GO>}

Thank you.

Operator

(Operator Instructions) The next question comes from Gustavo from Bradesco.

(Operator Instructions)

Q - Gustavo Schroden {BIO 22282474 <GO>}

Yes, I did.

A - Roberto Balls Sallouti {BIO 4150617 <GO>}

Now, we can hear you.

Q - Gustavo Schroden {BIO 22282474 <GO>}

You can hear me?

A - Roberto Balls Sallouti {BIO 4150617 <GO>}

Yes. We can.

Q - Gustavo Schroden {BIO 22282474 <GO>}

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Okay. Sorry, sorry. Thanks for taking my question, again. I'd like just to get your view regarding your corporate lending, especially on that SME, where we saw almost a flat quarter-on-quarter, the loan portfolio for SMEs at BRL14.3 billion versus of BRL14 billion last quarter, and you mentioned that it is related to some issues, some delays on the chamber of receivables. So could you give us any color here about the other credit lines for SMEs that you also offer? How these other credit for other SMEs are behaving? And what we should expect going forward in terms of a credit lending and also the breakdown between large SMEs? Thanks.

A - Joao Marcello Dantas Leite {BIO 17617595 <GO>}

Thank you, Gustavo. So, on the SME side, we basically have two products right now, supply chain financing and discount of credit card receivables. Supply chain financing continued to grow quarter-over-quarter, albeit, at a much slower pace, because would just come from BRL2 billion, a year-ago to over BRL13 billion, across BRL14 billion this quarter. At the same time, our portfolio of the discount of credit card receivables decreased and decreased because given the situation that we have in the clearing, we're not comfortable at increasing at this point.

We have a road map to roll out new products over 2022, but this will be very gradual and cautious, because we are now entering cleaner or riskier lines of credit and here the growth that you should expect from us is a slower one, because we want to make sure that we are taking the right steps with the right credit controls. It's one thing to discount supply chain financing or discount credit card receivables where we see the credit risk to be very controlled and basically either of the acquirer or of the large corp. So there we were happy to have a very strong growth. You should expect us to be more cautious here, but we still expect that once the problems with the central for credit cards is solved, we do expect to see a strong growth coming from there. But then it depends not on us, but on this issue of the market.

At the same time on the large corp, I think the seasonality of the third quarter was very strong. We expect some marginal growth, but at a much slower pace also in the fourth quarter, just because for some reason everything got pulled up to Q3 this year.

Q - Gustavo Schroden {BIO 22282474 <GO>}

That's very clear. I have another question if I may, now is that related to your asset and wealth management evolution, it's more related to net new money. It is still pretty strong special enough is managing this quarter, but also well if we exclude the last quarter positive impact from (inaudible), but it's still a strong number. My question is, how should we expect the net new money evolving in the coming quarters, especially in this more challenging market environment, higher interest rates and even higher inflation, a weaker GDP. So I know that, I mean, we should expect a migration from equities to fixed income. I think it's natural. But, overall, do you think that the pace of growth should continue at the same pace we've seen or do you expect some contraction in net new money evolution, not contraction, but deceleration in net new money, due to this weaker market condition is expected?

A - Joao Marcello Dantas Leite {BIO 17617595 <GO>}

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So what we see is that in periods, a very large volatility. You do have a slowdown in net new money, but it's probably more marginal than people expect. Just as people become more conservative and want to see understand what's going on in the markets, because before they make any movements. But once things stabilize, we tend to see flows resuming to similar levels that they were in the past. Maybe a bit higher, maybe a bit lower, but to similar levels, but as you said with a very different composition.

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Six, nine months ago, we were seeing very strong inflows into more illiquid products, into products linked to equities or to hedge funds. Now, we're seeing a very, very strong inflow into fixed income products, either CDs from the bank or especially tax-exempt products, especially of not only the bank, but also debentures. So you do see a shift in the composition, there is the change can be a little marginal up marginal down, but we continue to see strong inflows even with the volatility over the last I don't know, two months.

Q - Gustavo Schroden {BIO 22282474 <GO>}

Okay. Very clear and I thanks for the answers. Thank you.

A - Joao Marcello Dantas Leite {BIO 17617595 <GO>}

Thank you for Gustavo.

Operator

The next question comes from Tito Labarta from Goldman Sachs.

Q - Tito Labarta {BIO 20837559 <GO>}

Hi, good morning, good afternoon. Can you hear me okay, there?

A - Roberto Balls Sallouti {BIO 4150617 <GO>}

Yes, we hear you well, Tito.

Q - Tito Labarta {BIO 20837559 <GO>}

Okay, great. Thank you. Thanks for taking my question. I guess a couple follow-ups similar to the -- I was just on the outlook, tougher macro-environment rising rates, but more on I guess investment banking and sales and trading excluding with respect to CredPago. If you can give maybe some color on how you think that can evolve next year also going into a political Presidential election next year. Any color you can provide there would be helpful.

And then also one follow-up on the SME particularly on the credit card receivables. Is it because you slowed down to let me because you were planning to use those credit card receivables as collateral and you're comfortable doing that. And do you have any expectations for when those issues can get resolved? Thank you.

A - Joao Marcello Dantas Leite {BIO 17617595 <GO>}

So, starting with your second point on the credit card receivables, yes, that's exactly it. There's a lot of confusion on being able to spot and secure credit card receivables, which will guarantee your credit. So with that we're enough comfortable in expanding that business until we are sure that we're getting the right guarantees for credit.

And on the second question, on the businesses which are supposedly more cyclical like sales and trading and investment banking. We do think that clearly 2022, given just the market volatility that is expected and this can change in any moment, but let's assume that the scenario we have today continues for all of 2022. We probably see that these markets will probably be stable at the levels that they are now, but with a different composition. So within investment banking, you will probably have lower equity capital markets fees, but higher debt capital markets fees.

And also within that capital markets you'll also have a series of products, such as tax exempt products versus the non-tax exempt products and each of these different types of products have are more or less cyclical. And even sometimes, these products are even benefited from higher interest rates, especially the tax exempt ones. And also given let's say less rich valuations in public markets, we expect M&A transactions to pick up given that we see strategic players finding valuations more attractive.

And I would say the same thing for sales and trading, maybe you have a flattish equity brokerage fees year-over-year, but you see a growth in demand for hedges or in trading of corporate bonds, which helps you either grow slightly or maintain similar levels, but probably given what we're seeing right now and as supposing that we're going to have a scenario, close to what we're seeing in Q3, Q4 for the rest of the year. I would probably say that these markets were probably not grow significantly. So you would have probably marginal up, marginal down, but around the levels that we have.

Q - Tito Labarta {BIO 20837559 <GO>}

Great. That's very helpful. Thank you. And just one follow-up on the credit card receivables, any color or expectation for when you think those issues could get resolved?

A - Roberto Balls Sallouti {BIO 4150617 <GO>}

Should be soon, because most of the hard work, the heavy lifting is done by the market participants and so should be soon. It's a matter, we believe of details. Then once it's effectively launched and functioning in a way that we make sure we can really hold or block or secure the receivables against what lending we want to do then we're going to start gradually to deploy capital and understand the details as we always do, but it should be soon. I think this is going to benefit the SMEs in Brazil, it's another source of competitive funding to be provided and it's another way that we can understand the business of the SMEs. So to have a comprehensive view and understand the total exposure we want to take. So that's the view and so it should be soon.

Q - Tito Labarta {BIO 20837559 <GO>}

Okay, great. Thank you, Dantas. Thanks, Sallouti. I appreciate the color.

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A - Roberto Balls Sallouti {BIO 4150617 <GO>}

Thank you.

A - Joao Marcello Dantas Leite {BIO 17617595 <GO>}

Thank you, Tito.

Operator

Thank you. That bring us to the end of the question-and-answer session. I will now return the floor to Mr.Roberto Sallouti for his closing remarks.

A - Roberto Balls Sallouti {BIO 4150617 <GO>}

Thank you all for joining the call. Thank you for your continued support and partnership, and we look forward to being with you again sometime in early February, first to talk about the full-year results of '21. Have a great day and a great week. Thank you very much.

Operator

Thank you. This does concludes today's presentation. You may disconnect your line at this time, and have a nice day.

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