

Q1 2022 Earnings Call

Company Participants

- Guilherme Pacheco, Co-Founder and Partner
- Inacio Caminha, Head of IR and Funding
- Mauro Dutra, Chief Financial Officer

Other Participants

- Pedro Leduc, Analyst

Presentation

Operator

Good afternoon, ladies and gentlemen, and welcome to Banco PAN's Conference Call to discuss the First Quarter of 2022 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 in webcast platform with the respective presentation.

We would like to inform you that all participants will be in a listen-only mode during the company's presentation. After the company's remarks are completed, there will be a question-and-answer session. At that time, further instructions will be given. (Operator Instructions) Forward-looking statements are subject to known and unknown risks and certainties 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 obligation -- no obligation to update them in light of future event developments. With us here today, we have Mr. Mauro Dutra, Banco Pan CFO; Mr. Guilherme Pacheco, Mosaico's Founder and Banco Pan board member 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 proceed.

Mauro Dutra {BIO 21792010 <GO>}

Great. Thank you very much. Welcome everyone to our conference call of the First Q of 2022. It's always a pleasure to talk to you guys. I'd like to start by welcoming Pacheco who's first here -- for the first time, and I hope he will be here for a long time with us. So then I will start on this slide 2, of course with the highlights of the quarter and then we can talk about the business and our figures, okay. First of all, the key message here is even in a challenging scenario, this quarter, we were able to deliver another strong quarter in

terms of client growth, product and services diversification and of course, keeping high profitability levels because of the good results of the businesses.

First of all, start talking about clients. Our client base ended up the quarter with 19.4 million clients, which represents a very strong growth either quarter-by-quarter or year-over-year. The credit portfolio as of March was BRL36.2 billion growing 4% on the quarter. The transaction volume reached almost BRL20 billion representing a 5% increase in the quarter even considering the seasonality of the last quarter on each year.

Our bottom line was BRL195 million with an ROE level of 13.3. Regarding just the ROE accounting, we are using the net worth disconsidering the capital increase we had in March because of the Mosaico incorporation, right. So this is the accounting figure just considering the net worth without the capital increase that happened last month.

Moving on to slide 3, we have the evolution of the client base as I already mentioned, we reached almost 20 million clients in -- as of March, it is only worth to mention that this number includes 6800,000 [ph] clients of Mosaico. We are bringing Mosaico clients to our base for these -- for the release as those are clients for which we have a complete register with all the information we need to offer them products including credit. So this is an important driver looking forward. Moving on, we'll start to talk about the business by the update of the banking unit.

In -- on slide 5, we can bring this -- the key drivers of the quarter and then I'll give you some highlights with more detailed information. First of all, we are boosting the monetization of the client base because we are being able to expand the credit portfolio in the banking client segment, and also we are on a daily basis bringing more products for the client to be satisfied and for the client to be more profitable for us. So in this context, the first important thing to mention is the new app we launched in this quarter and you would be able to see some screens and what changed. The second message is the new product and channels we started to use during the first quarter. As examples, we have the new wording for the checking account using Whatsapp, the credit offering using also Whatsapp, and the launch of the Saude PAN program, I will give you more details further in the presentation.

Third important item to mention is the engagement and monetization of this client base, the portfolio in banking clients reached almost BRL15 billion as of March, which represents 40% of our total credit portfolio and this percentage has been increasing on a quarterly basis and at least we had the closing of the transaction with Mosaico. Pacheco is going to tell you more information about this, but we are of course very satisfied of accessing more information using Mosaico forum [ph] and then since November, we are offering the co-branded credit card in which we had more than 1.1 million requests.

Moving on slide 6. Now is the -- some important changes we made in our app, we launched the new app one month ago, the first important item to mention is the improvement in the performance, as an example, the login is now 5 seconds faster than it was because of the new architecture we created to this new app. Another important thing, the app is more intuitive for the client, so it's easier to find things, it's easier for the

client to get the product he wants once he opens the app and another and mainly -- maybe the most important point is we are now offering individualized product and service to each client.

So we can offer the client the correct product he is waiting for increasing our capability of selling things using the app.

On slide 7, moving on, we have the PAN Health program. PAN Health is like PAN Saude in English. but the real name of the product for the market in Brazil is Saude. This is a preventive health program. We are focused on offering our client a very cheap product which costs less than BRL10 per month and by paying this amount, our client and two more people of his family, they can have access to a lot of health services in Brazil such as discounts in drugstores, free telemedicine, assignments and consultations at a very small price, in personal consultations, it's a very small price for the people. So this is a product that almost the entire Brazilian population can use and we see this as very adequate to our client base.

So we hope to develop it from May 15 on when the product will be really available to the market. We are now working on friends -- family and friends model. We then move to the figures on Slide 8, we move to the figures of the banking unit, reached -- the client base reached 14.7 million clients as of March including the 600,000 clients coming from Mosaico, we see competitive cost of acquisition, almost flat quarter-over-quarter.

On the engagement side, we are increasing the engagement, the act -- the level of active clients reached 53% as of March increasing from the previous level of 52%. We keep on increasing the cross-sell index, we are now at 2.6 products per active client, we reached 6.1 million accounts with PIX key which is also very important indicator of engagement. We are seeing that the clients are using the checking account and the transaction volume reached almost BRL20 billion as I already mentioned.

So strong numbers in terms of activation, engagement, the clients are using the checking account and other services we offer in there. As another example on Slide 10, we brought some update in the insurance business, we ended March with 1.9 million clients with a outstanding policy -- outstanding insurance policy in banco PAN from which almost 600,000 in the banking unit. This is mainly due to the new products we have, we launched the PIX Insurance product during the 1Q and for the 2Q, we're going to have the FGTS insurance, which is a product that protects the client from loss in his salary or any problem, and in his salary accounts [ph] he anticipates the FGTS and Standard Life insurance product will also be offered in that. Talking about in the Slide 11, talking about the penetration of credit, we ended the quarter with 6 million banking clients with credit which also is a very important figure for us as we are on daily basis trying to get the credit business more closer to the banking unit as a cross-sell in a very important tool of monetization. We released in this quarter the on-boarding and the credit offering via Whatsapp. We improved the higher inflow of the personal loans and the FGTS loans and we started to offer the self-contracting of the payroll loans in which the client can use that and also Whatsapp too.

Moving on to Slide 12. This is the last slide talking about the figures of the banking unit before talking about Mosaico. We reached a credit portfolio in the banking unit of almost BRL15 billion and the main -- the key message of this slide is this dotted line in which we reached 40% of the banking -- of the entire banking portfolio being in the banking and being held by the banking clients, which is a very important indicator and as you can see, we are evolving on a quarterly basis and growing the penetration of credit in the banking unit.

So Pacheco, you want to explain the updates of Mosaico?

Guilherme Pacheco {BIO 17629561 <GO>}

Yeah, thank you, Dutra. Good morning, everyone. Starting with Slide 13, in early October, we announced that the transaction between Mosaico and Pan and after all regulatory approvals, we closed the transaction in mid-March and since then, we have worked as one company only, our nearly 300 employees joining more than 800 tech people in Pan forming a team of more than 1000 people, hopes it only improving customer experience and developing an integrated banking and consumer ecosystem.

We have a clear vision for the integration of the two businesses. Pan has a banking platform that is expanding both in terms of clients and its service offering. This platform has a very interest asset for us which is it's natural recurrence, financial services are one of the activities that generates most cellphones pickups slot [ph] them off. There are more than 40 million customers accessing the app and each interaction is an opportunity for us to show a personalized offer with cash back that the consumer receives directly in his bank accounts. We can also combine with a pre-approved line of credits. Mosaico in turn has millions of consumers who visit its platform monthly under the Buscape and Zoom brands seeking quality content about products, price comparisons, price alerts, coupons, and of course cash back which we started to offer a year ago and gained traction in the fourth quarter. Mosaico consumers can open a bank account at Pan to receive their cash back with benefits, they can finance their purchase, finance the acquisition of a new car, buy insurance related to their purchase or by Saude PAN

The integration of the two platforms creates a banking consumer ecosystem with cross data between the platforms that generates several opportunities to offer new products to our customers, or business, a free credit card with cash back, the buy now, pay later and also contextualize that offers with pre-approved credit. The integrated banking consumer ecosystems give us the opportunity to offer several high value services to our customers to increase engagement and raise their LTV.

Talking about integration on Slide 14, even before we announced the deal last October, we already had a commercial partnership with Pan in place, which allowed us to create the first integrated products and quickly seize operational synergies. We released the preliminary version of the Pan shop in time to take advantage of last year's shopping season. We have already generated the first millions [ph] in GMV and adding sites for the version 1.0, which will be released later this quarter. We have a dedicated and fully integrated team working in this front, followed by (inaudible) and Mosaico with mutual expertise. We also launched the Buscape credit card before Black Friday designed for

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consumers to enjoy the best value proposition in the market up to 2% cash back on purchase via Buscape and the lowest price warranty. We fulfilled all of the credit card pre-orders and today, we already have more than 1.1 card request in just a few month. In the wake of the good results of the Buscape credit cards, we are going to launch the Zoom credit card later this quarter.

The two brands have no user interact -- overlap, and Zoom, speaks to a younger audience than Buscape. Later this month, we will offer consumer finance within the Buscape journey, we have integrated the two companies database to offer pre-approved credit to consumers.

Talking about the results, Slide 15, in the fourth quarter of 2021, we had our first Black Friday with cash back integrated on our platform, a project that was fully developed in-house. We experienced significant growth and reached our highest GMV in history with more than BRL0.5 billion in just four days in the Black Friday period and BRL1.3 billion in the fourth quarter.

We have the tools to deliver the best value proposition, the lowest price in the market, combined with the cash back. And it has boosted our results in Q4. In the first quarter of '22, we had a decrease in GMV due to seasonality, a technical issue of cashback integration with a relevant merchant [ph] and a shift to profitability goals regarding the levels of cashback.

Our monetization capacity continues to increase, our take rate reached an all time high of 7.3% in the first quarter of '22. We have -- we had an new year-over-year revenue growth and we operated with positive results in the period. We have a clear vision of and a lot of opportunities in-house in creating this integrated banking and consumer ecosystem.

Our focus now is on execution, delivering new products that are increasingly integrated with banking, improving customer experience and seizing ecosystem synergies. Thank you, Dutra.

Mauro Dutra {BIO 21792010 <GO>}

Thank you, Pacheco. Very nice. Now I'm going to talk about the margins of the business and credit. So starting on slide 17, we brought our outlook for this year regarding this tougher scenario and what we expect to the credit metrics, right. First of all, very important to mention that even with this higher credit costs we are facing now, as expected, as already mentioned in the previous quarters, we get the margin after provisions at high levels, okay. This is very important we could re-price our products and we kept the margins at a very high level even with higher credit costs. The second item is our huge delinquency 90 days NPL ratio as of March was 6.8% up from 6.3% on December. However, we expect that this current level to stabilize and we expect the indicator to be around this level for the year. We expect that based on what we are seeing at margin in the previous months as of March and April and also the new actions we are taking in our collection unit. To end up the key messages, the credit portfolio should keep the same product mix we have now, I'll explain you later on, two slides from

now. We expect to keep the growth of the portfolio, but with the same mix, we do not expect to change the mix, as of now as we are more conservative in terms of credit in the origination.

So, with slide 18, brings the evolution of our margin of our NIM after credit cards, as you may see, it decreased a little bit in the quarter, but at a very high level in our view with a consistent portfolio growth over time and in every and almost every quarter of this year since the beginning of 2019. And we are diversifying the quality of this margin, as we have more different products now than we had in the past. So this is a very important thing to understand what -- how the business is performing.

On slide 19, moving on, we have in the left hand side of this slide, the mix of the portfolio, so the mix has been quite stable since December until March and this is the mix we expect looking forward during this year, during 2022 and on the right hand side, we bring here the delinquency rates. So one new concept -- one important concept we are using here is understanding how these indicators would be if we use the same mix of the pre-pandemic period, right. So we are using the mix of the portfolio we had at December 19, the short-term NPL ratio would be 8% instead of 8.6% and the 90 days NPL ratio would be 6% instead of 6.8%. Both indicators as you can see in this slide would be very similar to what we had in the pre-pandemic period. So the mix is basically the main explanation for this pickup over time.

Looking to the short-term indicator, we did have a pickup in the first quarter from 7.8% to 8.6%, but we understand this will not bring the 90 days' NPL to higher of all, we have seasonality in this short-term indicator and as I already mentioned, we are also seeing the results of our collection actions and we are seeing a best -- a better payment performance over the last days -- the last weeks. So we expect to be at the same level or around this level of 6.8% for the year. So then, I move to Inacio, who is going to take you to the financial highlights and we will be here to answer your questions after.

Inacio Caminha {BIO 19326001 <GO>}

Great. So moving on to slide 21. We have the main figures on our P&L, net interest margin stood very strong at BRL1.8 billion, 17.5% per year or 15% if you exclude the credit (inaudible) gains. This margin is very steady, even considering the carry of the portfolio or the gains that we have on the assignments. As for provision expenses, it increased as we expected given the scenario and the movements that we have seen in the NPL ratios, but credit remains under control and all the products that we are operating, have very strong margins.

So, all in, the pricing is still very, very positive. On expenses, personal loan and administrative expenses stood flat and we saw a reduction in the origination expenses mainly given to the smaller amount of loans that we originated in payroll loans and we get to net income of BRL195 million in this quarter, 13.3% accounting ROE also including a better effective tax rate that we have been benefited from all the investments that we have done in technology and also when you look at the forecast for the year, we expect to have lower tax rates as we had in '21, still something below 30%.

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On slide 22, we get to the origination on the retail credits. We kept a very strong base demonstrating not only the capacity that we have to originate these loans, but also the diversification in the different segments that we operate. The FGTS loans kept us a very strong level originating BRL2.1 billion in this quarter, we have more than 3 million clients with these loans already disbursed, vehicle financing as expected reduced a little bit because we increased the borrowing in credits process and also very connected to the scenario that we have seen, it's more like a preventive action instead of observing significant effects on the vintages itself. And as for payroll loans, we had a smaller amount in this quarter because of the margin debt was cut in the January 1, but it came back on March 30 and in these two last days of the quarter, we were able to originate BRL500 million showing how we are strong and well positioned in this business to capture all the opportunities whenever they come.

On slide 23, we have the overall credit portfolio breakdown, the BRL36.2 billion is -- has increased in all the different products that we have been operating, the overall collateralized ratio of the portfolio stood at 88% and we have almost no renegotiated portfolio. So the 4% increase and the 20% increase in the year, 4% in the quarter, they have led us to keep the same balance of mix that we had in last quarter and we'll probably keep the same mix throughout the year without increasing the share of products more exposed to the scenario.

On slide 24, we have the main figures of payroll loans and FGTS loans. These products are very defensive and important, especially in this time. We have kept the focus in originating federal codes for payroll loan and also the FGTS loans. The FGTS portfolio ended the quarter at BRL4.8 billion and this is well benefitted by the fact that we were the first mover in providing a full app experience to hire these loans and the payroll loan portfolio closed the quarter at BRL9.3 billion and as the margin was established in the end of the quarter, we'll probably have a stronger performance in the second Q. Moving on to slide 25, with the vehicle financing figures, this naturally was a product that we reduced the origination volumes that we have been landing over the last quarters. So this first Q, we disbursed only BRL2 billion in these products and we still see a lot of demand, but it's much more about the appetite that we have and the more credit strictness that we have employed in our models. So we have raised down-payment a little bit, we have increased interest rates that we charge, so that we have a very profitable and sound portfolio to keep doing this product. We have also been benefiting from the integration -- the full integration with Mobi Auto [ph] this has brought to us more proximity in more aspects to relate with our dealerships.

So we also believe that this acquisition will help us to to promote more leads and to have more pre-approved credit for our clients directing them to stores, to get the cars that they want to buy.

On slide 26, we have the credit cards detail. Naturally, we kept lower volumes of new credit cards issued in this quarter and we'll keep this for the coming months, seasonality affected a little bit the volumes that we have seen in terms of TPV in this first Q, but still at a very strong level of BRL4.9 billion in this quarter and the portfolio stood at BRL3.8 billion, still growing, but at a very assertive pace.

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Insurance on slide 27, we see small increase in premiums, but we have seen a faster pace of new clients with insurance outstanding, this is given mainly because of low tickets insurance that we have started to sell and we will add more products in our app such as the income insurance for FGTS loans and also life insurance for our clients.

So this will help us to improve cross-sell to have more ways to monetize our clients and diversify our fee income on our business. As for funding on slide 28, naturally it followed the increase in our assets. So we reached BRL36 billion in deposits diversifying among the sources that we have, funding cost has also dropped -- has been dropping on a daily basis and a great example is the banknotes that we just concluded a third public offering in April. So we don't see this amount of BRL861 million on first Q balance but this issuance was very well placed with a lot of demand and reducing rates coming from the previous public offer that we did last July.

And to conclude the presentation, we have our capital on slide 29 and now with the full incorporation of Mosaico, our CET1 is at 16.5% already in its full way. This provides us a very strong capital base, not only to keep deploying our strategy of growth, engagement and monetization, but also it is sustained by our very strong internal capital generation.

So with that, we conclude the presentation and open the floor for questions.

Questions And Answers

Operator

Thank you. We will now begin the question this session. (Operator Instructions). Our first question comes from Pedro Leduc, Itau BBA.

Q - Pedro Leduc {BIO 16665775 <GO>}

Hello everybody, thank you so much for taking the question and congrats on navigating a tough quarter. If I may pick your brains a bit on two fronts, first on loan book growth, you expect continued growth this year, we were wondering if there are any numbers you may suggest, so if it could be, still a double-digit loan book growth and you also mentioned it to be mix constant, but on the same time, you mentioned to be preferring a safer credit line, so you're balancing this out, how as the year goes? And then if you can already have a little bit of color on how origination is trending in the second quarter, as it's picked up, I imagine from 1Q lows? Thank you.

A - Mauro Dutra {BIO 21792010 <GO>}

Yeah. Thank you, Leduc. Thank you very much for the question. So our expectation for the loan book growth is to keep the current level, right. You can imagine growing this is approximately 20% a year. Regarding the origination of the -- at margin that we are seeing right now, we increased a lot the origination in the payroll segment as the government changes the margin of the product. In the end of March we are originating a lot much more than in the first quarter, keeping our more conservative approach in the vehicles business and in the credit card issuances. So we expect to keep the -- a very

healthy growth for the portfolio with the mix being concentrated on this no-credit risk products and/or the collateralized products.

Q - Pedro Leduc {BIO 16665775 <GO>}

That's clear. Thank you, Can I ask a second question?

A - Mauro Dutra {BIO 21792010 <GO>}

Of course. Go ahead.

Q - Pedro Leduc {BIO 16665775 <GO>}

All right. Then, moving down on to credit quality, here NPLs moved up above 50 bps sequentially above 7, part of that is mix explained but part is also deterioration in the overall scenario and then few questions here, now you've mentioned, do you expect NPLs to have roughly peaked by now to end the year close to where they are now? So here, just to make sure that it doesn't -- you don't see any peaks right going up in the next few quarters and then coming down by year-end, if it's something that's more related to adjustments that you have made in origination or collection? Or is it something that you are seeing in the widespread economy stabilization already into the second quarter? Or again you think it's more you that have adjusted the screws there a little bit more. Thank you.

A - Mauro Dutra {BIO 21792010 <GO>}

Good. So regarding the expectation of the NPLs, yeah, I think, did you expect this level to be the same at the end of the year. But we do not see a higher peak to then, goes -- go down, okay. Of course, it can be some variations quarter-over-quarter, but we expect to keep this level around this level, looking forward, and the reason of that is, as I mentioned that because we are seeing it happening in our portfolio, right, we are seeing a better performance of payments in the last months -- in the last weeks, difficult to say if this represents only our actions or only a normal performance of the clients, I would say it prevents both but we did adjusted the origination for the credit cards since September of last year and for the vehicles since November to December and besides that we changed a lot our collection actually -- we do collection actions there are starting to perform right now. So we did take actions and in our view, those actions are very important as we moved fast, they are important for this more stable view we have right now.

Q - Pedro Leduc {BIO 16665775 <GO>}

Perfect. Thank you so much, Dutra.

Operator

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

A - Mauro Dutra {BIO 21792010 <GO>}

Thank you very much. Thank you very much to everyone for being here with us. We are very happy of what we are delivering, we are very confident in our long-term strategy, we will keep on expanding our platform offering the clients the best experience possible and keeping healthy financial figures.

So, see you next quarter, and we are free to discuss any further details if you guys want. Thank you.

Operator

This concludes Banco Pan's conference call. You may disconnect your lines, now. Have a good day.

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