Q4 2012 Earnings Call

Company Participants

- Luiz Carlos Angelotti, Executive Managing Director, IRO
- Paulo Faustino da Costa, Market Relations Department Director

Other Participants

- Boris Molina, Analyst
- Carlos Macedo, Analyst
- Daniel Abut, Analyst
- Jorge Kuri, Analyst
- Maclovio Pina, Analyst
- Mario Pierry, Analyst
- Regina Sanchez, Analyst
- Saul Martinez, Analyst
- Victor Galliano, Analyst

Presentation

Operator

Good morning, ladies and gentlemen. We would like to welcome everyone to Banco Bradesco's Fourth Quarter 2012 earnings results conference call. This call is being broadcasted simultaneously through the Internet and the website www.bradesco.com.br/ir. In that address, you can also find the banner through which the presentation will be available for download.

We inform that all participants will only be able to listen to the conference call during the Company's presentation. After the presentation, there will be a question and answer session. At that time, further instructions will be given. (Operator Instructions)

Before proceeding, let me mention that forward-looking statements are being made under the safe harbor of the Securities Litigation Reform Act of 1996. Forward-looking statements are based on the beliefs and the assumptions of Banco Bradesco's management. And on information currently available to the Company.

Forward-looking statements are not guarantees of performance. They involve risks, uncertainties. And assumptions because they relate to future events and therefore depend on circumstances that may or may not occur in the future.

Investors should understand that general economic conditions, industry conditions. And other operating factors could also affect the future results of Banco Bradesco. And could cause the results to differ materially from those expressed in such forward-looking statements.

Now I'll turn the conference over to Mr. Paulo Faustino da Costa, Market Relations Department Director.

Paulo Faustino da Costa {BIO 6436050 <GO>}

Good morning, everyone. And thank you all for participating in our conference call. We are here today to provide you with all of the information you may need about our numbers. This is in line with our goal of always increasing the transparency of information disclosed to the market.

We have here today Mr. Marco Antonio Rossi, Chief Executive Officer of Bradesco Seguros Group and Bradesco Executive Vice President; Mr. Luiz Carlos Angelotti, Executive Managing Director and Director Investor Relations Officer; and Mr. Moacir Nachbar, Deputy Officer.

I will now turn to Mr. Luiz Carlos Angelotti, who will lead our conference call. After his presentation, we will be open to answer your questions. Mr. Angelotti, please go ahead.

Luiz Carlos Angelotti {BIO 4820535 <GO>}

Good morning, everyone. The Fourth Quarter of 2012 was marked by recovery of the global economy, even if very moderately. And between July and September, we saw the lowest level in terms of growth. Global (economic) risks remain mainly negative. But they are manageable. And are currently noted as lower than those seen during 2012.

With this scenario, the global economic outlook for Brazilian economy is positive from the commercial viewpoint. And also considering the lack of international pressures for (abrupt) reduction of international liquidity over the next months.

The recovery of Brazil's economy also continues moderate. But it is certain that the second half of 2012 was better than the first half.

In 2013, the normalization of supplying in (trading), in manufacturing, gives room to recover industrial production under a scenario where household consumption continues growing at solid pace, supported by employment and income growth. It is also worth mentioning the excellent outlook for domestic Agri business, as well as its positive effects on the economies of small and medium sized cities.

Brazil continues moving forward in institutional terms. And most recently policies concerning structural issues have been adopted, such as infrastructure and production cost savings.

Concerning the financial industry specifically, 2012 results are very challenging scenario. It is important to evaluate the changed scene in the system in view of the period that this industry has undergone over the past years. Therefore, financial institutions have been taking a very close look at the flow of operations. And at the same time, they have improved the scope of general services offered to their clients. It is, we think, this macroeconomic context that these Fourth Quarter results were inserted.

Slides 2 and slide three show our period highlights. I would particularly like to draw your attention to the slide two showing our adjusted net income for 2012, which reached to BRL11,523 million in 2012, 2.9% up on 2011. Total assets came to more than BRL879 billion, 15.4% up in the year; while our expanded loan portfolio increased by 11.5% in the same period, totaling BRL385 billion.

On slide 3, it's worth noting our assets under management, which ended the year at BRL1,225 billion, a 20% increase over December 2011. It is also worth mentioning the improvement in our efficiency ratio, which closed the Fourth Quarter at 41.5%, its lowest level for the past 10 quarters.

On slide 4, we show the reconciliation between our book net income and adjusted net income. This quarter, the main non-recurring items were the recording of tax credits and the full goodwill amortization, both from BERJ, totaling BRL1,389 million and BRL1,156 million respectively. And again of this, BRL793 million from the sale of Serasa shares. And the recognition of impairment losses amounting to BRL1,470 million, BRL527 million of which resulting from the return revaluation of Rights to Provide Banking Services. And BRL890 million relating to investments in shares, classified as available for sale due to the adjustment of the book value to their realization value.

Adjusting for these items, our Fourth Quarter adjusted net income came to BRL2,918 million. And our annual adjusted net income came to BRL11,523 million. You can see on this slide that our return on average assets came to 19.2%.

Slide five shows our historical (series) of our quarterly net income. Income growth in the Fourth Quarter was mainly due to the higher volume of operations and financial transactions. And the extended offer of products and services, both having a positive effect on fee income; and the net interest income growth from both non-interest and interest earning operations. And the reduction in the cost of the delinquency.

In the annual comparison, adjusted net income increased by (BRL325) million, or 2.9%, thanks to the upturn in net interest income, net of provisions for loan loss; the increase in fee income due to a higher volume of transactions as a result of the investments' organic growth; and the increased revenues from insurance operations.

Moving on to slide 6, I would especially like to draw your attention to our 12-month efficiency ratio, the red line, which improved for the fourth consecutive quarter, falling by 60 basis points. And closing the Fourth Quarter at 41.5%, its lowest level for the last 10 quarters. This important performance was due to our continuous efforts to control expenses, including the initiatives of our Efficiency Committee; and the maturation of our investments in organic growth; and the investments in information technology, which had a positive effect on the net interest income and fee income.

The Fourth Quarter ratio improved by (206) basis points over the same period last year. The blue line shows the efficiency ratio adjusted to the risk, which improved by 40 basis points over the previous quarter, due to the same aspects mentioned above.

On slide 7, as we have already seen, total assets came to BRL879 billion, BRL118 billion, or 15% up on the December 2011. The return on average assets remained at 1.4%, while the adjusted return on average assets stood at 19.2%.

The Basel ratio closed the quarter at 16.1%. And the slight variation was due to the increase in markets and (plus) risk-weighted assets, partially offset by the increase in our Tier 2 capital, which comprises the subordinated debt.

We highlight that Bradesco is the first and only Brazilian bank authorized by the Central Bank to use its own internally developed market risk management models to calculate regulatory capital as of January 2013.

Slide eight shows the relative share of our main operations in net income. In both the quarterly and annual comparisons, the highlight was the increase in the relative share of insurance activity, mainly due to a strong revenue growth in the life insurance and pension plan segments. The annual reduction in the share of loans was essentially due to the huge increase in delinquencies, as well as the pressure on average spreads and the change in the portfolio mix.

Let's look at slide 9. Unrealized gains totaled BRL24.9 billion in the Fourth Quarter, BRL3.8 billion up on the quarter before. This includes the two mark-to-market adjustments in our fixed income securities. These figures do not include the potential goodwill from our own profits in the total amount of BRL3.5 billion.

On slide 10, we show the evolution of our net interest income from both non-interest and interest-earning operations. The quarterly increase in total net interest income was basically due to the upturn in the interest-earning portion, especially in relation to the insurance and loan operation lines. And the non-interest portion, reflecting higher average trading gains.

The annual comparison, it is worth noting the 12% upturn -- in the 12% upturn in the interest-earning portion which was mainly due to the higher average business volumes, especially in regard to loans and securities operations.

Moving on to Slide 11. This quarter, the interest-earning portion of net interest income increased by 0.7%, basically due to the upturn in business volumes and the higher insurance margin, partially offset by the pressure on average spreads and impact of the change in the loan portfolio mix. As we expected, the (analyzed) (inaudible) (gross) margins narrowed by 10 basis points to (7.3%) in the period. We continue to expect nominal growth for the interest earning portion of the net interest income. But accompanied by a gradual decrease in the margin in the coming months.

Slide 12 gives a breakdown of the interest earning portion of the net interest income. In the quarter, it is worth noting the evolution in loans, whose volume of operations helped offset the reduction of the assets produced by the change in the portfolio mix and the decline in the interest rate and insurance, as we mentioned previously, due to the reduction in the (interest-earning), which resulted in lower expense from adjustment for inflation of the sum of the technical provisions in the period. These factors were offset by the lower gains from the securities margin.

The annual highlights were the loan and securities margins, thanks to the increased business volume. The reductions in the funding and insurance margins were due to the decline in the Selic and the upturn in the interest earning, respectively.

On Slide 12 (sic), we can see that this quarter ,the gross credit margin, the gray area, totaled BRL7,527 million sustained by the upturn in business volumes, although impacted by the pressure on average spreads and the changing the portfolio mix, as I have already mentioned. The red area shows the provision for loan loss which fell over the Third Quarter, as expected, helping push up the Fourth Quarter net credit margin. In the annual comparison, the net margin remains flat.

Look at the Slide 14. We see that our expanded loan portfolio totaled BRL385 billion in December 2012, 3.7% up in the quarter. And 11.5% up in the annual comparison. These increases were mainly due to increasing the loans to large corporates, which moved up by 4.6% in the quarter and 15% in the 12 months. And to SMEs which went up by 3.7% in the quarter and 10.6% in the year. In relation to the annual portfolio growth, if we exclude the acquired (loan) portfolio plus the (credit) portfolio, the remaining loans grew by around 15%.

Moving on to Slide 15. This quarter, I would like to emphasize the reduction in our delinquency ratio in the both enlarged corporates and SME segments. In the individual segment, the ratio remains flat. In the coming quarters, we expect a gradual decrease in the delinquencies in light of this short-term behavior. And this is the expected economic scenario for 2013.

The slide 16 shows our delinquent ratio for loans overdue by between 61 and 90 days, which presented a reduction this quarter, confirming our expectations and the trend of gradual decrease.

Slide 17 shows that our provisioning ratios remain strong. So much so that our provisions exceed the Central Bank requirement by BRL4 billion. Assuming the maintenance of the 12-month gross and net loss ratios, as from December 2011, we have booked provisions worth BRL7.6 billion above expected gross loss in the next 12 months, with a total budget of (inaudible), or even BRL11.1 billion in relation to losses net of recoveries, that's the dotted part of the purple line, also for the next 12 months.

On Slide 18, underlining what we mentioned in regard to the previous slide, we show the coverage ratio of the allowance for loan loss in relation to credits overdue by more than 90 and 60 days, which have remained at very comfortable levels. It is worth noting that the increase in the coverage ratio for loans overdue by more than 60 days reflected the reduction in the short-term delinquencies.

Looking at Slide 19, we see that the investments in organic growth as from the second half of 2011, such as increasing the number of branches and service points, led to an extension of our customer base and credit card footfall, which increased by almost 2 million cards in the period, in turn leading to a continuous upturn in transaction volumes as a result in fee income.

First quarter income totaled BRL4,675 million, 5.3% up on the previous quarter, mainly due to a higher return from cards, underwriting and financial advisor services and checking accounts. In the annual comparison, fee income increased by 15% led by underwriting and financial advisor services, which grew by 73.5%; credit cards, which moved up by 18.2% due to the aforementioned expansion of the credit card base and higher revenues from cards. And the income from checking accounts due to the expanded customer base.

Let's now look to the Slide 20. The growth in our operating expense was below 10%. In fact, it reached 7.7% for the year, which is below the lowest end of the guidance range, 8%, once again underlining our strong controls with its active improvement of our internal Efficiency Committee.

Fourth quarter operating expenses increased by 3.2% over the previous three months mainly due to the higher business volumes and the seasonal upturn in margin expense. The 7.10% annual increase was due to the impact of investments made in the period, offset by our strong cost control according to our search for higher efficiency.

The upturn in personnel expenses were mainly caused by salary increases in line with the 2011 and 2012 collective bargaining agreement and the expansion of workforce in the second half 2011.

Looking at the slide 21, we can see the 5.3% increase in Fourth Quarter. Again, such an expense was basically due to advertising expense and higher volume of business and services, partially offset by reduced expenses in third party services. The 5.6% increase in the annual comparison was mainly due to the higher expenses from the upturn in business and service volumes, the expansion of our distribution network and the contractual adjustments.

It is worth noting that in the last 12 months, the IPCA and the IGP-M recorded variations of 5.8% and 7.8% respectively.

Slide 22 shows revenues from our insurance pension plan and capitalization bond activities, which increased by 31% this quarter, primarily due to the strong upturn in the pension plan segment, boosted by the higher concentration of pension plan contributions in the period. In the annual comparison, there was a 17.7% increase. Our segment did well, once again recording double-digit growth.

Fourth quarter net income moved up by 15.2%, mainly due to higher revenues, the improved financial results, a claim ratio under control. And a greater administrative efficiency.

The 12.1% annual upturn was basically due to the 17.7% increase in revenues, in turn countered by stricter control over claims and the reduction in the general and administrative expenses.

Slide 23 shows some of the main figures of our insurance activities. The combine ratio came to 86.6% in the Fourth Quarter, nearly flat in comparison with the previous three months.

Financial assets totaled BRL142 billion, while technical provisions stood at BRL124 billion, BRL108 billion of which from life insurance and pension plan products.

Slide 24 shows our economic (department) GDP, interest rates, inflation and exchange rate estimates for 2013 through 2015. We believe the stimuli introduced through various economic policy channels and instruments which led to the recovery in Brazil's growth, even though few modest and concentrated in the second half of 2012, will become more apparent in the coming quarters, resulting in higher and more stable economic growth in the years ahead, with strict control over inflation and the maintenance of interest rates.

Slide 25 shows our guidance for 2013. In 2013, we believe the loan portfolio will continue to expand. growing by between 13% and 17%, mainly (divided) by loans to individuals and SMEs.

We expect to see a slowdown in our operating expenses, given our substantial investments, especially in information technology. And our cost cutting initiatives. And our continued search for improved efficiency.

In conclusion, we believe our results in 2012 were satisfactory, given the modest pace of economic activity throughout the year, not to mention the internal and external challenges we had to face.

The effect of our investments over the last few years in infrastructure, technology and new products and services, enabled us to increase the volume of transactions, helping us offset the pressure on margins.

The constant improvement in our efficiency ratio reflected a tighter control over the expenses. And we also had (the instant) contribution of the Insurance Group to annual results.

It is worth noting that these results confirm the correct positioning of our organic growth strategy and the strong synergy between the banking and insurance activities.

Finally, we are fully aware that business opportunities are likely to become more challenging in an increasingly demanding and competitive market. However, under its commitment of supporting the (country) development, Bradesco is (part of) this scenario, leveraging its banking and insurance activities, which is a responsible and sustainable approach.

Thank you, all very much for your attention. And we are now available to answer any questions you may have.

Questions And Answers

Operator

Ladies and gentlemen. we will now begin the question and answer session. (Operator Instructions) Daniel Abut, Citi.

Q - Daniel Abut {BIO 1505546 <GO>}

Luiz Carlos, a couple of questions. One, if I look at your loan loss provisions, last year, they ended up amounting to about BRL13 billion. That was a sharp increased compared to 2011 when you provisioned about BRL10 billion. My question is, given that you said that you think that the NPL ratio will continue to gradually improve over the next several quarters, as indicated by the trend that you are seeing in asset quality, do you see room for this -- your large level of provision that you did, particularly in 2012, to come down?

And I'm asking if you can give us some parameters, even though you are not providing guidance for loan loss provisions. I want to get a sense if there is room for that to become another driver of earnings next year, lower provisions. And some of your competitors have been guiding that way.

And question number two is on fee income. You're guiding 9% to 13%. Given that you grew 15% this year in challenging conditions. And in an economy that was growing very little, would you say that 9% to 13% is a rather conservative type of guidance for a year in which you expect economic growth to do much better than last year?

A - Luiz Carlos Angelotti {BIO 4820535 <GO>}

Thank you for your question, Daniel. About the loan provisions, we expect that the delinquency ratio will continue declining for 2013. It is (routine); is good movement in that decrease. But we consider the scenario that we have for 2013 and the lower interest rate. We expect that our delinquency ratio will decline during 2013.

The expense with the loan provision, since this is the Second Quarter, or the Second Quarter was our peak in 2012, in the Third Quarter and the Fourth Quarter, we continued decreasing our expenses.

We normally doesn't give a guidance. But we understand that the total expense that we will have in 2013 not to exceed the number that we have in 2012. Then we understand that probably will be a very similar number will be (delinquencies), considering that the decline in -- the decrease that's expected in the delinquency ratio.

About the fee income, our guidance is 9% to 13%. It's not a conservative guidance. But we understand that in 2012, we had this 15%. The number of transactions is growing very fast. We are working the same way for continuous improving our client -- improving the number of cards, working for our clients use more of the alternative channels for (do) transactions.

And we are very optimistic with our guidance in this. But now it is what we understand that is possible. It could be during the year, if you understand that we have a -- we can have an increase then, we will change the guidance. But now is what we -- that what we understand that is possible to have.

Q - Daniel Abut {BIO 1505546 <GO>}

Maybe if I can clarify the question. Was there anything unique in 2012 which was a challenging year for Brazil overall, that you were able to grow 15% fees and you think is going to be below that next year?

A - Luiz Carlos Angelotti {BIO 4820535 <GO>}

When you compare one year with the other, the number that we have to face is -- the number increase. And a continuous growth, 15% year after year, it's difficult.

We understand actually the guidance that we gave, 9% to 13%, is what is possible considering the targets that we have for the year. We expect -- we hope that to grow more now -- number that we gave you, the guidance. But we -- what is reasonable, what you have for this year, the guidance is 9% to 13%.

About 2012; what we had is that the effects of the investments in the organic growth; 1,000 new branches. We had in improvement in the client base. The number of credit cards improve as the clients will start to use more -- to do more transactions through the new channels; this growth that we are having, the effects that the investments that we did in improving our client base and the number of products that we offer for our clients.

Q - Daniel Abut {BIO 1505546 <GO>}

Thank you, Luiz Carlos. Very helpful.

Operator

Carlos Macedo, Goldman Sachs.

Q - Carlos Macedo {BIO 15158925 <GO>}

I have a couple of questions, both related to your margins. The first is related to your guidance. I was just trying to gauge how much confidence you have on the guidance you provided of 7% to 11% growth in net interest income from market sources -- from non-market sources, sorry; from interests.

The credit; if you look at your numbers, the average rate on your -- average yield on your loans has declined from 11.1% in the Fourth Quarter last year to 10.6% in the Fourth Quarter this year. But most of the decline was in the third and the Fourth Quarter, especially in the Fourth Quarter once the new rates on credit card loans. And etc., were put in place.

How -- given the amount of loan growth that you expect for next year, do you think this is realistic, 7% to 11%, particularly with the pressure the Government has been putting on pricing and on rates. And on the competitive pressure that the publically held banks are putting? Do you think 7% to 11%, is it going to be more towards the lower end of that or at the higher end?

Then I have a second question.

A - Luiz Carlos Angelotti {BIO 4820535 <GO>}

Our guidance for margins, 11% -- 7% to 11%, we are very confident with our guidance. This guidance is based in our internal discussions and is based in our budgets. We are very confident with the guidance now, not only in the net interest income but in the other lines.

We consider we -- the confidence that we have in the net interest income, we expect to grow, to have a good growth in the (credit) margin. And the insurance margin will be better than the margin that we had in 2012. We expect to have growth.

And the margins; we expect to have similar -- in securities and other, there is the line, we expect to have a stable growth; to grow a little more in this line. But when you -- in this total, we expect to grow at 7% to 11% in according our guidance.

Q - Carlos Macedo {BIO 15158925 <GO>}

Okay. But most of the growth -- in the credit margin, do you think you'll see a decline in the --?

A - Luiz Carlos Angelotti {BIO 4820535 <GO>}

There will be decline in the credit margin, yes. We will --

Q - Carlos Macedo {BIO 15158925 <GO>}

Do you think that the --?

A - Luiz Carlos Angelotti {BIO 4820535 <GO>}

(Multiple speakers) we expect to grow more considering our guidances that we have.

Q - Carlos Macedo {BIO 15158925 <GO>}

So just to follow up. On the credit yields that are now at 10.6% and closed the year 2012 at 10.4%, do you expect that to contribute to this growth? Or are the credit yields continuing to contract, as they have throughout 2012?

A - Luiz Carlos Angelotti {BIO 4820535 <GO>}

The credit growth that we expect is 13% to 17%. We expect to have the main contribution for the growing demand will come from the credit line. And we expect that in our -- considering only the credit margin that we have, we expect that probably, the effect that we'll have during 2012, we will (lose) something in our operations with credit card that we changed our rates.

But in the other lines, we expect to improve our -- we expect to maintain our spreads. So we will look to -- we will work to maintain our spreads. We understand that we will have high competition during 2011. But we will expect to have (compensation) improved -- have some compensation with more volume in the transactions.

And we will have some pressures in the spreads during the year. But we expect to have a compensation with the more volume in transactions.

And talking about the (mean) that we have, we finished the year with 7.3%. We expect too that we will continue to decline something in the mean for 2013. Probably during the year, we will finish the year with -- close 2012 with 7.3%.

We expect to finish 2013 with around 7%, considering the effects that we will have during the year. Then we understand that the main contribution will come from spreads. And we expect to maintain our guidance, to reaching our guidance that is 7% to 11%.

Q - Carlos Macedo {BIO 15158925 <GO>}

Okay. Thanks. The second question's also related to the spreads. And it's more related to the Fourth Quarter. The spread on interest for insurance operations increased by 50 basis points, which is a quite sizeable jump. I'm just wondering what the reason behind that increase was. And if there's any --. It says here that it was a decline in inflation in IGP-M that benefited reserves. If you could give us some color here as to what to expect going forward for yields and insurance.

A - Luiz Carlos Angelotti {BIO 4820535 <GO>}

The main effect is because in the Third Quarter, in the last quarter, was because IGP-M, that was small and the effect on provisions. We had our (loan extension with the funds) due to adjustment in inflation in the provision. Then the main effect that provides an increase in the insurance in the last quarter came from the IGP-M effect.

Q - Carlos Macedo {BIO 15158925 <GO>}

Okay. Thank you. Thank you, (Mr. Angelotti). Thank you, gentlemen.

Operator

Saul Martinez, JPMorgan.

Q - Saul Martinez {BIO 5811266 <GO>}

I also wanted to follow up on the questions on your net interest income guidance. And more specific -- and I guess I'll be even more specific. The securities and other line, you mentioned your expectation for securities and others will be more or less stable in 2013 versus 2012. And that is what is constituted or embedded in your guidance.

The securities and other line rose 75% in '12 versus 2011. And my understanding of that. And please correct me if I'm wrong, is that there was a benefit from the lower interest rates on your pre-fixed portfolio, your fixed rate portfolio.

If rates are to remain stable, I'm having a hard time understanding why that benefit from declining rates will continue to be there in 2012. Can you give us a little bit more color on why you're expecting that line item, securities and others, to remain stable in 2013?

A - Luiz Carlos Angelotti {BIO 4820535 <GO>}

In this line, we have the effect of pre-fixed portfolio. But we have effect from other assets, some assets that is -- which is credit risk and we're considering in this line.

During this year, we will continue to having effects from the pre-fixed portfolio in this line in another very similar -- little similar that we had a year before, in 2012. And we have the effects of other assets in this line. Then that is some assets that you have a credit risk in the (inventories) and the other assets. This is why we understand that for this year, we will have a stable effect in this line. And this is what to expect for this line, securities and other.

Q - Saul Martinez {BIO 5811266 <GO>}

Okay. In 2012, I'm sorry, these are somewhat technical questions. But in 2012, are these benefits valuation gains on these pre-fixed portfolios, or are they actual gains in the spreads that you're making on that portfolio?

A - Luiz Carlos Angelotti {BIO 4820535 <GO>}

The liquidity that we here is not only because it is pre-fixed portfolio, because the other assets that we are -- the liquidity in these other assets, our portfolio. Then one part of that this (huge growth) that we have in 2012 came from the pre-fixed portfolio. But we have the other assets that provided this growth during 2012, not only with the pre-fixed portfolio effect that we had.

Q - Saul Martinez {BIO 5811266 <GO>}

Okay. Maybe we can go a little bit offline as well.

Second question is related to your overall guidance. You mentioned on an earlier question that you think loan loss provisions will be at worst flat versus 2012. And if I look at your other guidance lines, 7% to 11% net interest income, low double-digit fees, operating efficiency improving, insurance 12% to 15%, you plug that into your model you're getting to pretty healthy earnings growth of the low teen to high teen range. Are you --? I know you don't give guidance for earnings and for ROEs. But is it fair to say that you're optimistic that earnings growth in 2013 is going to rebound versus what amounted to fairly challenging 2012?

A - Luiz Carlos Angelotti {BIO 4820535 <GO>}

We are working hard for to improve our efficiency, improve our growing in operations. Then we have a guidance; the normal guidance that we have for ROEs is 18% to 20% that we work for to maintain. And we understand that is reasonable, this level, for considering the scenario that we have in (part of) the economy.

We're working different fronts to maintain the ROE in the efficiency where we have internal committee of efficiency, where we look for opportunities for reduce costs or improve revenues. And then something that we -- is helping us to improve our efficiency. We have a strong -- we are -- (with very strong) investments in IT. And we expect to collect some benefits during 2013 and 2014 with the investment in IT. That will reduce our costs. And it will help us to improve some gains with the new system that we expect to start to run during this year.

Then for efficiency, we have target; that is to reach (39%) in 2014, at the end of 2014. But we have the other fronts. We have our Insurance business that represents around one-third of our costs. That is risk diversification. Then the Insurance business, the ROEs, the average ROEs are only 24%, 25%. And this is a piece that will help us to improve our profitability for the next years.

We expect that the delinquency ratio will continue to decline because considering the lower interest rate that we have, we understand that the delinquency ratio probably will adjust in a more -- will be adjusted in a more lower level. And we are working hard for improving the volume of transactions, offer more products for our clients considering the client base that we have, improving the profitability with these clients.

Consider the investments that we did in the segmentation, the opportunities that we have with the synergy between the Insurance and the Financial business.

Then we are working different fronts to improve our profitability. And this is another important revenue that we understand that we will have some compensation, it will help us to have some compensation for the pressures in the market.

Then we have the -- not -- we understand that the more reasonable ROE that we have for the next period is 18% to 20%.

Q - Saul Martinez {BIO 5811266 <GO>}

Okay. Great. Thank you. So much.

Operator

Mario Pierry, Deutsche Bank Research.

Q - Mario Pierry {BIO 1505554 <GO>}

Let me ask you also a couple of questions. The first one is related to your loan growth guidance of 13% to 17%. I was interested in hearing what is your expectation for market growth, because in 2012, we saw your loan book expand about 8%. But state-owned banks grew their loan books more than 20%. So I was wondering if you believe that the state-owned banks will be more rational or less aggressive in 2013 and then you expect to grow in line with the markets, or you still expect to lose market share.

And also, related to that question, I think some of your margin pressure that we saw in 2012 was related to this aggressive competition from the state-owned banks. Do you think that we could also see a more rational pricing environment in 2013 as the state-owned banks become less aggressive?

And finally -- there's two and a half questions. Then if you could provide us with any guidance with regards to your sensitivity of net interest margins to movements in the Selic rate. You do expect Selic rates to remain relative stable going forward. But can you provide us any guidance; what would happen to your net interest margins if the Selic was increased 100 basis points in 2013?

A - Luiz Carlos Angelotti {BIO 4820535 <GO>}

Okay, Mario, thank you for your questions. About the loan growth guidance, for the system, we expected -- for the total system, we expect to grow around 15%. Then our -- in our guidance, 15% to 17%; the (center) of the guidance is 15%. Then we expect to grow according to the market, to maintain our market share.

Then we work normally to increase our (participation) in the operations. But we expect, according our guidance, maintain our market share.

Talk about the margin pressure, about the competition, we had (competition) in 2012. But in (more), in two products, in credit cards and overdraft accounts. Then for 2013, we did adjustments in these two products. And for the -- considering the growth that we expect for the economy for 2013. And we understand that the (requirements) of the borrowers are with the -- more investments during the year. In the sense of the requirements of the borrowers, we will be there; we will help to improve the volume of transactions. And we expect to grow considering our guidance, to grow with (quality), maintain our credit policy.

And we understand that we will have strong competition. But we have capacity to compete in equal situation. We have a strong structure. We have scale. And we can do operations very (effective) considering our structure. And we understand that we have to compete and maintain a good margin in the operations.

And the guidance; your last question is about the Selic rate and the effect -- if we have liquidity in 100 basis points in the Selic rate. It's around 1%, or 100 point basis representative of BRL400 million before tax. Then if you will have an (equity for up) or go down, around the BRL400 million is the effect. But we expect that the Selic rate to be stable during 2013.

Q - Mario Pierry {BIO 1505554 <GO>}

Okay. So then to summarize what you said, or to make sure that I understood, is that you do expect then the state-owned banks to be more rational in 2013 for you to grow in line with the market rather than lose market share. Then we have already seen a significant impact of a lower interest rate environment already impacted your results in 2012, because this Selic rate fell by almost 500 basis points or -- during the year. Is that right? So you already felt a big negative impact from the drop in Selic rates in your results.

A - Luiz Carlos Angelotti {BIO 4820535 <GO>}

Yes. For 2013, we expect that Selic rate will be stable. Then we does expect too to have the main effect. But if you had an increase or one decrease around the 100 basis points, the effect would be around BRL400 million before tax, the -- what is the effect, the average of the effect. But we doesn't expect modification Selic rate for the year.

Q - Mario Pierry {BIO 1505554 <GO>}

Okay. Great. Thank you very much.

A - Luiz Carlos Angelotti {BIO 4820535 <GO>}

Thank you, Mario.

Operator

Jorge Kuri, Morgan Stanley.

Q - Jorge Kuri {BIO 3937764 <GO>}

Can you --? Just wanted a bit more specific on your expectation for NPLs. You did mention that you expect NPLs to go down. They're at 4.1% now. Do you have a specific number that you think they can reach by year end 2013? That's my first question.

Then the second question is if you can provide us a little bit more color on exactly what you're doing on the cost side. I do understand that you have a new IT system that is going allow you to operate with better costs. But what does that mean? Does the IT system allow you to fire people? How does it provide better cost?

And if I look at your expenses and your employees, your employee base is basically the same since the start of last year. I think it's probably down 1%. Some of your peers, actually your main competitor on the private side, their expenses are down; their employees are down around 10%.

So how do you really modify your cost structure, which is obviously what you need to do whilst you're moving into a lower rate environment and margins are going to come under significant pressure, without really changing your employee base?

So if you can just give us a little bit more color on how you're going to get to that efficiency levels.

Thank you.

A - Luiz Carlos Angelotti {BIO 4820535 <GO>}

Thank you, Jorge, for your questions. About the delinquency ratio. We finished the year with 4.1%. We expect that we'll continue to have a decrease with the delinquency ratio during 2013. Don't have a guidance, specific guidance. But probably to the end of the year, we will have the lower level in the delinquency ratio.

Looking what we had during 2011, the best moment that we had was the delinquency ratio was around 3.6%/3.7%. (Could be that) to the end of the year, we will reaching some level similar of that. But we don't have a specific guidance for the total delinquency ratio.

We understand that the decrease will be -- not to be fast, to be in a more slow movement. But it will be -- continue to -- during to the end of the year, we intend to have the best moment with a more lower level in the delinquency ratio.

About the cost side. We have our -- we have many fronts inside of Company. One of that is the Efficiency Committee. That is we have a group of directors between Vice President and directors that we discuss opportunities for reduced costs in our line, in third party services, communications, data processing, transport.

Then we are revising different process inside the Bank. Then this Committee, we have for around three years; then we start main process that will help us to get some benefits in the next period.

Then we have some actions that started, already started. And we expect to collect the benefits during the year, during this year and during the next year. Then it's a process that we have internally that we discuss our process. And we -- how departments inside the Bank are involved in this process.

And another front is about our investments in IT that we are now in the last (phase) of our IT (revitalization) plan. And we are now rewriting our systems. And we expect to collect some benefits. This year probably we will finish it to rewrite the system. And during 2014, we will finish the (test). Then probably some systems that we have now will help us to reduce the cost.

Some examples that we have is some systems that start to work in the branches that the employees will -- the cashiers, the cashiers will need less time for attend the clients. Then probably we will have now to improve the number of clients that we are branch, in the branch. And the cashiers will now have now to offer some products. Then the time that we reduce in this process will be around 25%, because that will help with the maintenance of the systems. We're reducing around 10% considering the new structure that we will have in the systems.

And these are some examples that we have that will -- intended to help us to reduce the cost.

Another thing is that we are working for to offer more channels for our clients uses. And not use only the branches. Then we offer the Internet and the mobile phone. And we have the Bradesco Expresso structure. And this structure is helping us to reduce the cost with the transactions. And the -- we are having an increase in the number of transactions that our clients are using in these alternative channels.

And these actions that we are doing, we understand that it will help us to reaching the targets that are in the guidance that we gave you for the next -- for 2013 about the operating expense. But the end of the line it's a process that we look for efficiencies; it's a continual process. And we are doing many investments in technology part helping us to reduce the operational costs.

Q - Jorge Kuri {BIO 3937764 <GO>}

All right. Many thanks for your response.

A - Luiz Carlos Angelotti {BIO 4820535 <GO>}

Thank you.

Operator

Regina Sanchez, Itau BBA

Q - Regina Sanchez {BIO 16404038 <GO>}

My first question is related to expenses. Actually, I like a lot the administrative and personal expenses. But our bottom line, the bottom line came slightly below our estimates because of other operating expenses that came higher than our estimates. But we read that the Bank improved the methodology for amortization of prepaid expenses.

If you could give more color what was this change. And how much this change impacted the other operating expenses in the Fourth Quarter. Had you not changed this methodology, how much less expense you would have in the quarter. And if you could provide a guidance for this line, even if not official, for 2013, is it going to be more correlated with NII growth, or with inflation? Or could expect even lower figure considering that you have already made some impairment of intangible assets, which I understand that the amortization of these intangible assets goes through this other operating expense line.

Then I have a second question. Thank you.

A - Luiz Carlos Angelotti {BIO 4820535 <GO>}

Okay. This modification that we did in the -- amortization in the process is an accounting -- we did an improvement in our accounting process. But the fact is -- the fact that we did -- we considered an extraordinary effect this is not reflecting in the -- because the modification that we did is not reflecting the results that we have this -- in the last quarter.

But it is a small number. And the fact that it's (taxed) for 2013, in the next year, is not significant. It is a small effect. It's only an improvement in the accounting process we did.

Q - Regina Sanchez {BIO 16404038 <GO>}

Okay. And what can we expect for this line in 2013 as a whole, especially considering that you made impairments of intangible assets? This could make this line to grow less in 2013?

A - Luiz Carlos Angelotti {BIO 4820535 <GO>}

We don't have the guidance for other operating expense. We have only the guidance for the non-operating expenses. We don't have to give that guidance for this other operating expense. You can consider stable compared with what we had in the last quarter. We believe that it will probably be stable.

Q - Regina Sanchez {BIO 16404038 <GO>}

Okay, fantastic. And my second question is related to Basel III. We saw in newspaper articles commenting on possible measures that the Government could take to reduce the impact of Basel III implementation in Brazil. I would like to know if you support these measures and when do you expect to see them implemented.

Do you believe --? I'm mentioning related to that a government warranty for deferred tax assets. Do you think this will be related to all deferred tax assets from (timing difference), or only the ones related to loan loss provisions?

Thank you.

A - Luiz Carlos Angelotti {BIO 4820535 <GO>}

Okay. Regina, we don't have the final -- we have some discussions. But considering the rules that we know that according -- that our Central Bank (publishes), we have now to implement Basel III in 2018. Without this -- we will have now to do the implementation. But if we have now some modification that we will -- one part of the tax that will be (offset) because if our (government) gives a (guarantee), it will reduce the effects of the Basel III implementation; will be favorable for the Bank.

But we don't have the final guidance, or the final rules. What -- the discussion that we have is about the portion related to the provisions for the (loan loss) spreads. That is the tax that is related to this part of the provisions could have a guarantee. And not will be to deducted for the future in the Basel III calculation.

But we don't have the final rules. We don't know how we'll do the implementation. But considering the whole scenario, we will have now to do the implementation. If we have some improvement in the rules, will be better. But we don't have the final (law) or the final rules.

Q - Regina Sanchez {BIO 16404038 <GO>}

Okay, fair enough. Thanks a lot.

Operator

Victor Galliano, HSBC.

Q - Victor Galliano {BIO 1517713 <GO>}

A couple of questions; just a follow-up, if you will allow me, on the margin side. I'm just looking here at the loan margin and the growth of that loan margin. So if you look at the 4Q interest income from loans and look at the annualized rate, that only grew at 5.1%; and you look at the average loan balance, that grew at 9.5%.

Now is it not clear that there's going to be a lot of margin pressure coming through in 2013 on the one hand from the fact that you've got the impact of the Selic and the loans re-pricing with a delay. And we're just beginning to see that in Q4? And also, the fact that you still have a lot of competition coming through from the public banks. And in particular from Banco do Brasil in areas like credit cards and overdrafts. And also increasingly in the SME space?

So I'm just trying to square the circle. And I just -- my sense is that 7% to 11%, plus (Saul's) earlier comment on the securities portfolio, it gives me some impression that that 7% to 11% loan growth -- sorry, net interest income growth, with the loan growth that you have, seem quite aggressive.

I know you've talked about this ad nauseam on this call. But for me it's a gorilla in the room and it won't go away.

A - Luiz Carlos Angelotti {BIO 4820535 <GO>}

Okay, Victor. About the margin, the guidance that we gave, the part that is related to prets, to loans, we understand that for 2013, the portion where we expect to grow more is in (the vehicles) and SMEs. And these kind of operations has better margins, or better spreads. And we understand that we will improve the mix of the portfolio, improving these operations. And we expect to have a better growth in this line if you compare with the 2012.

But we have other lines where we expect to have positive growth. That is in the Insurance margin. We expect to have a better growth compared with 2012.

Then we understand that we will have to reach this margin, this net margin that we gave, considering our structures for 2013 and the portfolio that we have in our -- that we have now, that we finish 2012. We understand that it will be possible to reach this level because with this guidance, considering our structure that we have now and our strategy for 2013.

Q - Victor Galliano {BIO 1517713 <GO>}

Okay. Just a quick follow-up there. The areas that you're growing in individuals is (inaudible) -- is relatively low risk. Am I right?

A - Luiz Carlos Angelotti {BIO 4820535 <GO>}

Yes.

Q - Victor Galliano {BIO 1517713 <GO>}

Okay. Just one quick follow-up. Renegotiated credits, they have been pretty stable at around 3.5% of the portfolio for the first three quarters of this year; picked up a bit to 3.6%. Is there anything we should worry about there, or not really?

A - Luiz Carlos Angelotti {BIO 4820535 <GO>}

The growth that we are having in this renegotiated portfolio is stable. We don't -- it's a similar behavior that we had for the total loan portfolio. Then probably during this year, 2013, probably the growth will be similar that we have in the -- at this total portfolio. We don't expect that we will have something different.

We have here one slide in the -- together in the presentation, that is number 36. For the renegotiated portfolio we have delinquency ratio stable around 28%, max 30%.

Then this is what we expect that will continue happening during 2013. Then we don't expect a modification, any significant modification for this portfolio during 2013. Probably the delinquency ratio will maintain stable in this level; and probably the growth that we will have in this portfolio will be similar that we will have in the loan portfolio.

Q - Victor Galliano {BIO 1517713 <GO>}

Okay. Thank you very much, Luiz Carlos.

Operator

Boris Molina, Santander.

Q - Boris Molina {BIO 1904979 <GO>}

I have a question regarding your -- the growth in the capital gains that you showed in the quarter was around BRL1.9 billion, after tax in your available for sale portfolio. Could you give us some color regarding whether this was driven by fixed income or by equity portfolios? And was this in the Bank portfolio or in the Insurance portfolio?

And whether you believe next year, given that rates are going to be flat, this is going to be something that might not perform as well; was there any reclassification of securities from portfolios? I think something occurred in the recent past on this front that you may help us.

A - Luiz Carlos Angelotti {BIO 4820535 <GO>}

Please, Boris, can you repeat the question?

Q - Boris Molina {BIO 1904979 <GO>}

Yes. The question was if you could provide some color for the BRL1.9 billion after-tax improvement in unrealized capital gains in your available for sale portfolio. And the question was a little bit to see whether it comes from the Banking portfolio, or whether it was in the Insurance portfolio? Was it related to fixed income, or have you increased your exposure to (equity) in the Fourth Quarter; that was pretty good for equities? A little bit of color just to help us understand this movement which was pretty large.

A - Luiz Carlos Angelotti {BIO 4820535 <GO>}

If the BRL1.9 million is --

Q - Boris Molina {BIO 1904979 <GO>}

Is the mark-to-market of available for sale securities. The growth in the --?

A - Luiz Carlos Angelotti {BIO 4820535 <GO>}

We have the slide in page nine where we have the -- these unrealized gains. The BRL12.9 billion that we have is in the securities. The majority is (inaudible) in available for sale. And it's related to our Insurance portfolio. And if you -- in our equity, we have a reserve around BRL5 billion/BRL6 billion that is related to these securities.

Then probably these revenues, these potential revenues, will be registered in the future according to the (accrual), maturity of the operations, or the securities.

Then we are having, growing this portfolio, because the valuation according to the market (volume) that we're having in the last three quarters. And every balance, or every quarter, we do the valuation according to the market (value). And the part that we have registered in the available for sale, we're increasing our equity, what we register in the equity.

Then for the future, probably these potential revenues will be registered in our (props), according to the maturity of these bonds, or these securities. Some of these bonds have 10 years or 20 years, then because related is a guarantee that we have for this provision in our Insurance business.

Q - Boris Molina {BIO 1904979 <GO>}

Okay. Excellent. Thank you. And the other question was regarding Basel III and this news that came out a couple of weeks ago. It would appear that the guarantee for deferred tax assets would be activated once the Bank becomes insolvent. So do you have any indication? It would appear that this improvement in the capital ratio would be -- should classify as Tier 2 capital, not as Tier 1, given that the guarantee is not activated as a going concern. But once the Bank is insolvent. So shareholders are not going to see anything.

So do you have any indication from the Central Bank whether this is going to be Tier 1 or Tier 2? Basically, we would like to see if this reform follows the spirit of Basel III, or if it's going to be a little bit different in Brazil than elsewhere.

A - Luiz Carlos Angelotti {BIO 4820535 <GO>}

Okay. These are discussions that we are having about it to do some adjustments in the Basel III calculation; and about the tax (spread).

Considering the rules that we have now related to the bulk of the tax spread from the Tier 1 capital. If we have some modification in this calculation where one part of the tax spread will be acceptable, not to be considered in the (discount), the effect will be in the Tier 1 capital.

In our case, the portion related to provisions for (credit) is around (50)% of our total tax spread. Then the number that we have is something around BRL12 billion or BRL13 billion is the number that we have.

But we don't have the final rules, or we don't have the -- how big the calculation, or how -- what we'll be considering in this rule if we have this modification. But --

Q - Boris Molina {BIO 1904979 <GO>}

But you expect it to be Tier 1?

A - Luiz Carlos Angelotti {BIO 4820535 <GO>}

The effect will be in Tier 1, yes.

Q - Boris Molina {BIO 1904979 <GO>}

Okay. Excellent. Thank you.

A - Luiz Carlos Angelotti {BIO 4820535 <GO>}

Sure.

Operator

Maclovio Pina, Morningstar Equity Research.

Q - Maclovio Pina {BIO 16236843 <GO>}

Two questions. And number one is I know you don't give specific numbers for credit quality in any of your particular business lines. But can you comment just on the improvement on NPLs for corporate and SMEs, both in 90-plus days and early delinquencies? Is there any particular industry that's showing more strength, that's driving the improvement, or is it just broad based?

A - Luiz Carlos Angelotti {BIO 4820535 <GO>}

The improvement in the (short) we --. Yes. We -- the costs for corporates and the SMEs, we had a declining delinquency ratio in the (90-plus) days. And for the short -- and for the -- in the short-term phase, the delinquency ratio was at 61 days and 90 days, we had a decrease in the same way.

We expect that the delinquency ratio, the total delinquency ratio will -- continue to decline. We don't have a specific sector of the economy where we had a better performance. But in the total portfolio, in the corporate side, we are having a decline. (The point is really) the last quarter was more stable delinquency ratio. But during 2013, we expect that we will have a decline in (inaudible).

The total portfolio expected during 2013 we will have a decline in the delinquency ratio. We don't have specific sectors or operations where we understand that we are having a decline, a specific decline. In the total portfolio, we are having an improvement in the quality of the portfolio.

Q - Maclovio Pina {BIO 16236843 <GO>}

Okay. And with regards to individual mortgages, do you expect that the rate that they are outgrowing the rest of the individual portfolio will continue into 2013 and '14? And can you just give us a sense of -- do you have any comment on the credit quality of these new mortgages that are coming online and if you have any visibility? And especially, how are you thinking about provisioning for these mortgages. And in terms of coverage?

A - Luiz Carlos Angelotti {BIO 4820535 <GO>}

Yes. We expect to continue growing in the mortgage portfolio, individuals and in the corporate side. It's (our one) important product. The delinquency ratio for this product is very small in our portfolio. And that is an important product where you have a long-term relation with the client and you can offer other products during this -- the period of the transaction.

Then we expect to continuously grow at a -- in this specific product. The delinquency ratio is very small and (inaudible). The (product) that we have in our portfolio is very good. And we expect to continuously grow.

Q - Maclovio Pina {BIO 16236843 <GO>}

Okay. And so it's -- just to recap. It's fair to say that you do expect it to keep outpacing the broad loan expansion at the rate it's been doing so?

A - Luiz Carlos Angelotti {BIO 4820535 <GO>}

Yes. For this product, we expect to continuous -- having the growth similar we have, we are having the last (few) years. And it's an important product.

And in Brazil, we have -- we expect that mortgage will be -- will continue growing very fast for the next years. And for us, it's an important product for the future.

Q - Maclovio Pina {BIO 16236843 <GO>}

Okay. Excellent. Thank you very much again.

A - Luiz Carlos Angelotti {BIO 4820535 <GO>}

Thank you.

Operator

This concludes today's question and answer session. I would like to invite Mr. Paulo Faustino da Costa to proceed with his closing statement.

A - Paulo Faustino da Costa {BIO 6436050 <GO>}

Thank you, all, for participating in this conference call. I would like to take this opportunity to remind you that our Market Relations department and our IR team are at your disposal. And that all the contents of our Fourth Quarter 2012 and other information concerning Bradesco, is in our website.

Thank you very much.

Operator

This concludes Banco Bradesco's audio conference for today. Thank you very much for your participation. Have a good day.