

Q3 2014 Earnings Call

Company Participants

- Ivan de Souza Monteiro, Chief Financial Officer
- Leonardo Loyola, Head of Investor Relations

Other Participants

- Boris Molina, Analyst
- Carlos Macedo, Analyst
- Marcelo Telles, Analyst
- Saul Martinez, Analyst
- Tito Labarta, Analyst
- Unidentified Participant

Presentation

Operator

Good morning, everyone, and thank you for waiting. Welcome to Banco do Brasil's Third Quarter 2014 Earnings Conference Call. This event is being recorded and all participants will be in a listen-only mode during the company's presentation. After this, there will be a question-and-answer session. At that time, further instructions will be given. (Operator Instructions) This event is also being broadcasted live via webcast in Banco do Brasil's website at www.bb.com.br/ir where the presentation is also available. Participants may view these slides in any order they wish.

Before proceeding, let me mention that this presentation may include references and statements, planned synergies, estimates, projections and forward-looking strategy concerning Banco do Brasil, its associated and affiliated companies and subsidiaries. These expectations are highly dependent on market conditions and on the performance of domestic and international markets, the Brazilian economy and banking system. Banco do Brasil is not responsible for updating any estimates in this presentation.

With us today, we have Mr. Ivan de Souza Monteiro, CFO; and Mr. Leonardo Loyola, Head of Investor Relations. Mr. Leonardo, you may now begin.

Leonardo Loyola {BIO 16193219 <GO>}

Good morning, everyone, and thank you for joining us for our third quarter earnings conference call. I'd like to start the presentation on slide three, where we show the main highlights of Banco do Brasil's performance in the period.

We posted an adjusted net income of R\$2.9 billion in the third quarter of 2014 and net interest income grew 7.3% compared to the first nine months of 2013. Our loan portfolio in the Broad Concept grew 12.3% in 12 months reaching a total balance of R\$732.7 billion. Our delinquency ratio remain the best in the banking industry, closing the quarter at 2.09%. Finally, we highlight our BIS ratio that reached 16.04% this quarter, rising almost 200 bps on the quarter.

Moving on to slide four, we present some earnings highlights. NII grew by 7.6%, compared to the third quarter of 2013, and 7.3% compared to the first nine months of 2013. Fee income reached 6.7% year-on-year hitting the guidance.

The main income generators were cards, asset management and account fees. We posted an adjusted net income of more than R\$2.9 billion in the third quarter of 2014, corresponding to an adjusted return on equity of 16.1%.

On slide five, we show our sources and uses where we call your attention to agribusiness letters of credit and real estate letters of credit that together grew 61.9% in 12 months, reaching R\$113.5 billion in September 2014. We also highlight corporate bond repos which grew 60.6% year-on-year. You can see that Banco do Brasil's loan portfolio represents 89.5% on the Bank's funding usage.

On slide six, we displace BB's net interest income performance. In the upper left-hand side graph, you can see our global spread behavior reaching 4.2% in this quarter. On the right-hand side, we show the credit spread by segments that showed recovery in agribusiness and company segments. In the third quarter of 2014, NII reached R\$12.5 billion, a 7.6% growth compared to the third quarter of 2013.

Comparing the first nine months of 2013 and 2014, NII grew by 7.3%, reaching R\$26.7 billion. We also highlight the increase in loan operations income that reached R\$60.8 billion in the period, 18.7% growth due mainly to increase in the volume of loans and the portfolio turnover.

In the next slide, we have the evolution of loan portfolio in the Broad Concept reaching R\$732.7 billion in September 2014, representing 12.3% growth in 12 months. In the same period, the individual's portfolio grew by 6.9%, representing 23.9% of the total loan portfolio. The company's portfolio grew by 12.8%, representing 46.7% of the total loan portfolio and the agribusiness portfolio grew by 21.8%, representing 21.6% of Banco do Brasil's total loan portfolio.

Considering the classified loan portfolio, BB's market share was 21.1% in September 2014. The guidance for the loan portfolio was reviewed as we will see further.

On slide eight, we have the loan portfolio in the classified concept, which does not include BV operations considering the contracts by period. By the end of September 2014, we can see that contracts from 2013 on represent almost 60% of the total portfolio.

On slide nine, we have the organic portfolio with individuals. On this basis, the portfolio grew 12% in 12 months and 2.3% in the quarter. The full lower risk lines, I mean payroll, salary loans, mortgage and auto loans represent together 76.1% of this portfolio against 75% in September 2013.

On the upper graph of slide 10, we observe the comparison of BB's payroll loan balance with our peers. The balance of this portfolio in September 2014 was R\$63.1 billion, a growth of 2.3% year-on-year, allowing BB to end the period with 25.8% market share.

If we consider the organic portfolio 88.2% of this portfolio is customers who are civil servants, 7.8% relates to INSS retirees and 4% of private-sector employees.

We highlight BB's mortgage portfolio that posted a balance of R\$35 billion by the end of September 2014, an increase of 73.1% in 12 months, which allowed Banco do Brasil to be the second largest financial institution in this segment.

For individuals, the growth was of 63.2% reaching R\$25.7 billion, while for companies the increase was 108% with a balance of R\$9.3 billion.

The bottom right-hand side graph shows the auto loans portfolio, credit offered exclusively to our customers within our branch network. In September 2014, more than 83% of auto loans were taken by customers with relationships of over five years with Banco do Brasil.

Moving on to the next slide, we present the company's loan portfolio totaling over R\$342 billion, representing a 12.8% growth in 12 months, highlighting the increase of 108% in mortgage and 23.6% in credit for investments.

On slide 12, we present the breakdown of loan portfolio with companies by size. SME, medium and large companies. The SME portfolio ended September 2014 with a balance of R\$101.5 billion, up 7.5% year-on-year. The medium and large companies portfolio reached 15.2% growth for the same period.

In the upper right-hand side graph, 19.9 billion of the SME loan portfolio was covered by the Operations Guarantee Fund, the FGO, and 3.6 billion of this portfolio is covered by Fampe, an SME Guarantee Fund. This amount covered by these funds are growing by 15% year-on-year, a higher pace than the total portfolio.

Finally, on the bottom graph we displayed that more than 70% of the SME portfolio that is contracted by clients with relationship of over five years with Banco do Brasil.

On the next slide, we can see our agribusiness loan portfolio that grew 21.8%, compared to September 2013, remaining with the best delinquency ratio in BB's portfolio with a 0.59% ratio. As we can see from the chart on the right-hand side, 64% of loans destinate for working capital for input purchase on the '14-'15 crop are protected with insurance options offered to our customers.

The 2014, '15 crop sorted during July 2014 had an estimate of R\$81.5 billion disbursement through June 2015 and up to September 2014 the disbursement was R\$20.6 billion.

On slide 14, we detail BB's asset quality showing average risk of our loan portfolio evolution which remains below the banking industry. We ended September 2014 with a ratio of 3.66%, while the industry posted 4.83%. In September 2014, we posted 185.9% coverage ratio, much better ratio compared to the industry, as shown on the bottom graph.

Our current provision levels enable us to remain below the industry, even with a scenario change, such as an increase in delinquency.

On the upper graph on the next slide in September 2014, the NPL 90 days ratio was 2.09%, remaining considerably below the banking industry average. On the bottom graph, we presented BB's NPL 15 and NPL 19 in the three largest segments of the loan portfolio, individuals, companies and agribusiness.

On slide 16, we see the NPL formation index, with a better ratio compared to the last quarter and new NPLs slightly lower than the previous quarter with a substantial decrease in write-offs. The index remains stable and in line with historical curve.

On slide 17, we can observe our credit provision expenses considering the average classified loan portfolio. The first graph on the upper left-hand side we have a ratio between provision expenses and the loan portfolio on a 12 months view. By the end of September 2014, we reached 2.79% according to our estimate.

On the second graph, on the right-hand side, we see stability on a quarterly view. In the bottom graph, we see that the 13.2% growth of the loan portfolio between September 2013 and September 2014 has been contracted in the best risks, mainly between AA and C levels.

On slide 18, we present Banco Votorantim net income in the third quarter of 2014 that reached a total of R\$135 million, completing one year of positive results. On the left-hand side bottom graph we have an information regarding the origination figures for light vehicles from Banco Votorantim,

where we can observe a decrease of 0.6% on the NPL 90 days, when compared to September 2013.

The right-hand side bottom graph shows the new vintage contracted after September 11, that already occupies 83% of BV's managerial auto loans portfolio.

In the following slide, we show our performance in fees. Considering the first nine months of 2014, fee income reached R\$18.3 billion, growing 6.7% compared to the same period in 2013, converging to the guidance.

We highlight that 13.3% growth in card operations compared to the first nine months in 2013. And insurance, pension and premium line we achieved growth of 15.7%, asset management growth of 8.9% and 16.9% growth in fiduciary services due to the recent investments in this business.

On slide 20, we present BB Seguridade's performance, a company that leads in several segments such as life, pension plans and premium bonds. It's important to notice the increase of 49.1% in the adjusted net income in the first nine months of 2014, compared to the same period in 2013.

On slide 21, we display the organization chart of the main card businesses in which Banco do Brasil holds a direct or indirect equity interest. We highlight that Livelio has been recently authorized by CADE to start its operations. We will detail the card business performance on the next slide.

On the top graph on the slide 22, we see the card business net income, which reached almost R\$1.5 billion in the first nine months of 2014, corresponding to a 38.5% growth compared to the same period in 2013.

On the right, we show the total turnover that increased by 12.7% in 12 months. On the left-hand bottom graph, we see the increase in Elo Cards issued by Banco do Brasil that grew from 6.2 million in September 2013 to 7.2 million in September 2014 and the turnover with these cards increased by 10.1% (Technical Difficulty)

Operator

Excuse me. Banco do Brasil conference call has been interrupted for technical reasons. Please hold on and we'll soon resume the conference call. Please, sir, you may now proceed.

Leonardo Loyola {BIO 16193219 <GO>}

Sorry, we've been cut off. So just coming back to where we were, on slide 22. On the top graph on the slide 22, we see the card business net income, which reached almost R\$1.5 billion on the first nine months of 2014, corresponding to a 38.5% growth compared to the same period in 2013.

On the right, we showed a total turnover that increased 12.7% in 12 months. On the left-hand side graph, we see the increase in Elo Cards issued by Banco do Brasil, that grew from 6.2 million in September of 2013 to 7.2 million in September 2014 and the turnover with these cards increased by 10.1% year-on-year, reaching a balance of R\$4.2 billion.

We also call your attention to the turnover increase with benefit cards issued by Alelo, a growth of 37.3% year-on-year.

On slide 23, we can see the performance of our admin expenses. These expenses amounted to R\$23.6 billion in the first nine months of 2014, corresponding to an 8.5% increase compared to the same period in 2013.

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The growth in this line was driven primarily by the adjustments in salaries and benefits from the Collective Bargaining Agreements 2014-15 and contract renegotiation, such as surveillance and transportation that occurred in the third quarter. We expect to hear the guidance for this item by the end of the year.

Regarding our cost to income ratio on slide 24, we can observe relative stabilities throughout the presented quarters. On slide 25, we show the BIS ratio of Banco do Brasil that ended September 2014 at 16.04%.

Regarding the Central Bank authorizations for the Hybrid Capital instrument of R\$8.1 billion to incorporate into our core capital, we can observe an increase compared to the last quarter. This increase on the total ratio is due to the recent Central Bank macro prudential measures operations. This metric already considers the Basel III rules and if we consider the fully implemented measured over June 2014, the estimate BIS ratio would reach 14.69% and Tier 1, 10.6%.

In the core capital, there was an addition of 98 bps due to the authorization for the Hybrid Capital instruments and 55 basis points due to the Central Bank macro prudential measures operations.

On the slide 27, we close this presentation with our guidance. Considering the results of third and fourth quarter of 2014, some estimates were revised.

Regarding the portfolio management strategy, the commercial funding estimates was revised to 12% and 16%. The guidance for domestic loan portfolio Broad Concept was impacted by a lower demand and for the reason we've revised to 12% and 16%.

The estimates for individuals portfolio were revised to 8% and 12% due to a decrease on the acquired portfolio and vehicles credit, partially compensated by mortgages in the period.

Company's portfolio went to 12% and 16% due to a lower growth in private securities operations. Regarding the agribusiness, we also revised estimates to 16% and 20% considering the crop dislocation due to drought and a lower performance expected for the fourth quarter of 2014, compared to the fourth quarter of 2013 when we achieved a record disbursement.

Finally, we posted an adjusted net income of 15.2%. The net interest income reached 7.3% and fee income grew by 6.7% in the third quarter of 2014. Allowance for loan losses closed September 2014 with a stable ratio of 2.8%.

Thank you for your attention, and let's now open to the Q&A session.

Questions And Answers

Operator

Ladies and gentlemen, we will now begin the question-and-answer session. (Operator Instructions) Our first question comes from Tito Labarta of Deutsche Bank.

Q - Tito Labarta {BIO 20837559 <GO>}

Hi. Good morning, and thanks for the call and for taking my question. My question is just regarding asset quality and we did see some deterioration in the quarter. Specifically in the corporate portfolio, NPLs went up around 30 basis points. I'm assuming if you can give a little bit more color of anything specific happening there? And also how you see this evolving? And also you mentioned in the agricultural portfolio, even the asset quality has been under control, but you said

in the outlook it may be a little bit weaker because of the drought indeed, any concerns about asset quality in that portfolio as well, so we can get some color on that? I appreciate it. Thank you.

A - Ivan de Souza Monteiro {BIO 16420543 <GO>}

Thanks for your question. We expect a stable trend and even a slightest decrease for the next quarter, it's hard to say right now. But the overall portfolio is performing well. We keep the delinquency ratio well below the system in Brasil and the trend is, as I mentioned before, we expect a stable or a slightest decrease on the NPLs in the Bank.

Talking specific about the agricultural portfolio, you know that we have a historic low level on the NPL in this segment. We expect to see the same performance for the next crop.

Q - Tito Labarta {BIO 20837559 <GO>}

Okay. And then -- so then in the quarter and at least in the corporate portfolio, was there anything specific with the NPLs went up 30 basis points, and why you expect that to improve?

A - Ivan de Souza Monteiro {BIO 16420543 <GO>}

There is small and middle-sized companies, it's a more fragile segment in the whole economy as a whole, in the whole economy, I'm sorry. We don't expect any further increase in these delinquency, we're working hard to do that. But again, in the environment that's a little -- there is a lot of volatility, this is the segment that is that we have to be cautious about.

Q - Tito Labarta {BIO 20837559 <GO>}

Okay. Great. And then maybe just one follow-up on the back of that, did loan growth items with asset quality have any issuances on that, you mentioned it was more lower demand, but any -- the lower loan growth that has come because of any concerns about asset quality?

A - Ivan de Souza Monteiro {BIO 16420543 <GO>}

No, it was not related to the asset quality, it's only related to the lower demand estimation.

Q - Tito Labarta {BIO 20837559 <GO>}

Okay. Great. Thank you very much.

A - Ivan de Souza Monteiro {BIO 16420543 <GO>}

Thank you very much for your question.

Operator

Our next question comes from Gustav Shredding [ph] of Bank of America.

Q - Unidentified Participant

Thank you for taking my question again. I have one question regarding the administrative expenses, because we saw it's growing at 90% in the first nine months of the year. And this is above the high-end of the guidance range of 5% to 80%. My question is that, why have you reiterated the guidance? I mean, do you expect lower expenses in the next quarter to maintain the guidance of 5% to 80%? Thanks.

A - Leonardo Loyola {BIO 16193219 <GO>}

Yep. So, thank you, Gustav, this is Leonardo speaking. Basically, as you know, every September we have negotiations with the unions. There are two things to be considered here. The first one, the last year the negotiation took longer and that's why there was no impact on the third quarter

figures, which was not the case for this year. So there is -- it's not -- we are not comparing apples-to-apples, just taking this fact alone.

And on the other hand, the negotiations came a little bit higher than expected. That's why we are negotiating -- we are working hard on the other topics apart from personnel expenses, just to drive down and to perform within the guidance by the end of the year.

Q - Unidentified Participant

Okay. Okay. Thank you very much.

Operator

Our next question comes from Saul Martinez of JPMorgan.

Q - Saul Martinez {BIO 5811266 <GO>}

Hi, good morning. Hope, I guess new for you guys, but how are you? I have a couple of questions. First, when did I ask about your risk adjusted net interest margin, it was 2.6 this quarter, this is on Table 7 of your MD&A and it come down considerably since fourth quarter of 2012 from 3.5 to 2.6, that's a pretty meaningful reduction. As you look out going forward, how -- when are we going to start to see an improvement there, because obviously the investment story for Banco do Brasil is that as the back book reprices that margin start to expand and asset quality remains contained, you could see an improvement in risk adjusted margins and hence earnings in crop stability.

Can you talk about how you see that playing out? Because that number has been stable for three quarters now in spite of what seems like a better competitive backdrop.

And the related question there is just why funding costs rose so much this quarter? Could you give a little bit more color and with the Selic rate increasing, is there risk that in the coming quarters you're still going to continue to see funding cost pressures for your margin expansion prospects?

A - Leonardo Loyola {BIO 16193219 <GO>}

Hi, Saul. Leonardo speaking. Thank you for your question. So let me start from the second question, and then move to the first one. Basically, what we have is -- in the funding, so the funding volume increased by 15% in nine months, while the Selic rate increased by 39%.

The interest expenses could have increased more than it really did. The main reason why it didn't go higher is because the use of instruments like LCAs and LCIs that pushed down the cost of funding for the Bank.

On the other hand, we have been focusing on low risk credits which are very helpful, you know about this, for our cap customers within the bank, with us, for longer, but they do not help much spreads. This is one thing just taking the fan.

On the other hand, so the risk-adjusted NIM, as you mentioned, so it's true. I mean it's coming down since 2012, but just drawing your attention to NIM on the same Table 7, so you can see that despite the fact that it was going down over this year's, over this quarter's in a row, so you could see that net interest margin, it start to going up in the same way, I mean, from 4.1 to 4.2 from the second quarter to the third quarter.

And on the other hand, you can see on the Table 6, the annualized managerial NIM, you can see that it touched the bottom in the end of 2013 and it's now going up, it reached 7% backend of fourth quarter of 2013 and now we are seeing an increase over the quarters in a row. That's why -- so we expect some sort of recovery just following the trend.

Q - Saul Martinez {BIO 5811266 <GO>}

How, when should we -- I understand lending NIM seem to have increased, but your overall NIMs are not increasing and presumably as NIMs come down, because in part because it make shift in part because of pricing, as we've seen at the other banks your cost of risk comes down, your cost of risk has been kind of stable, hence your risk adjusted net is flat. Do you -- I understand the 50 basis points improvement, but it's not translating into better financial margins, when should we -- when do you think we start to see that take place, because that's obviously the critical factor, one of the critical factors that tends to why profitability levels. What will drive profitability levels higher from the current ways?

A - Leonardo Loyola {BIO 16193219 <GO>}

One think that you must consider, Saul, it's -- which is important to mention is the mix effect. As you know, so we are growing faster in credit lines like mortgage in our growth. I mean, they are good credit lines for delinquencies for NPLs, but on the other hand they tend not to help much NIMs.

That's why it's very hard to say, because you could see that our mortgage for instance is still growing very fast. So it's pushing up, it's main responsible for pushing up the growth in the individuals. That's why it's very hard to predict exactly when we're going to start seeing this trend.

Q - Saul Martinez {BIO 5811266 <GO>}

Okay. And I hated playing devils ask a little bit, but presumably the mix shift should be lower NIMs, but lower credit costs and lower provisions, and that hasn't happened, provisions have been stable in the percentage of loans even as the mix shift has occurred yet, NIMs have fallen. So it really is dependent, if you see that kind of stay in that relationships remaining NIM, credit costs remaining stable as percentage of your loan book that does imply that you're absolutely NIMs really have to start increasing and I guess that's what we're waiting for and what the market is I think a lot of the market is waiting for?

A - Ivan de Souza Monteiro {BIO 16420543 <GO>}

Saul, this is Ivan, thanks for your question. We need to take in consideration that when we have an environment to do business that is more volatile, we're tightening the credit methodology and we're tightening all the measures in the credit portfolio as a whole. One of the most important one is the rating of the company, individual or the companies.

During this process, we downgraded some companies and downgraded some ratings, why? To be more conservative on the approach to do the credit business, that's why it's not a disc relation that, we are using more and more, we are changing the mix of the portfolio and need to be consider -- need to consider that we are tightening the credit methodology as a whole.

Q - Saul Martinez {BIO 5811266 <GO>}

Okay. So that, so you think you're being somewhat conservative there on the terms of your rating actions on commercial borrowers?

A - Ivan de Souza Monteiro {BIO 16420543 <GO>}

It always depend on what is the segment that we are working, what is the macroeconomical conditions. It's a lot of measures that we are taking consideration, when we providing a certain rating for a company. But as a whole the portfolio and as a whole the methodology becoming, we are tightening these.

Q - Saul Martinez {BIO 5811266 <GO>}

Okay. All right. That's very helpful. Thank you very much.

A - Ivan de Souza Monteiro {BIO 16420543 <GO>}

And always there is a consequence on the provisions. And as you know, that in Brasil deposits, the provisions (inaudible).

Q - Saul Martinez {BIO 5811266 <GO>}

Got it. Understood. Thank you very much.

A - Ivan de Souza Monteiro {BIO 16420543 <GO>}

Okay? Thank you very much.

Operator

Our next question comes from Boris Molina of Santander.

Q - Boris Molina {BIO 1904979 <GO>}

Yes, good morning. Thanks for the opportunity to ask. And I had a question regarding the Hybrid debt capital instrument that was included now in your core capital. I would like to get an idea of what are the conditions for that remuneration for this capital, if it's based on TJLP, whether this is going to -- the remuneration for this capital is going to be included in your payout ratio?

And whether do you foresee that you might be increasing the share of these type of instruments in your capital structure going forward, as the migration to be Basel III proceeds?

A - Leonardo Loyola {BIO 16193219 <GO>}

Thank you, Boris. Basically just going through the instrument, as you remember, the remuneration, it's the dividends of the year one, divided by the shareholders' equity of year 0, times the payout of the bank. So it's -- that's why -- I mean the TJLP plus 50 bps is the cap for the instrument. So the estimates -- we have seen some estimates, it's obviously not -- it's far from the cap in the instrument.

Sorry, I didn't get your first question. Could you repeat, please?

Q - Boris Molina {BIO 1904979 <GO>}

No, it was, one question, this instrument has no retained earnings account, right? This is more likely a debt instrument, it has a dividend payment with a cap.

A - Leonardo Loyola {BIO 16193219 <GO>}

One important thing, so it takes -- we take the shareholders' equity of the (inaudible) minus one just to pay the instrument. This is pretty much the structure of the bonds. This is a structure that we put on, but the new structure that was approved by the Central Bank to be considered as core equity Tier 1.

And we are going to see, I mean, this is the first time, just highlighting here, you can see on the financials, how it is considered there in this quarter particularly, as you know.

So it was approved by the Central Bank to be considered as core equity Tier 1 back in 28th of August. That's why in this quarter particularly, you're going to see parts of the cost of this instrument being considered as a core instrument.

And on the other hand, just from 28th August onwards, you're going to see in the new version, probably, you're going to see -- an important thing to highlight as well, it's not going to be paid

semi-annually any more, it's going to be paid on annual basis. This is another difference from the new version.

Q - Boris Molina {BIO 1904979 <GO>}

I know, so it's going to be paid every fourth quarter?

A - Leonardo Loyola {BIO 16193219 <GO>}

Sorry, Boris, I don't have this information right now. But I can -- I mean, we can do the follow-up with the IR team in Sao Paulo. They are going to come back to you with the exact month in which we are going to pay this instrument. Okay?

Q - Boris Molina {BIO 1904979 <GO>}

Wonderful. Excellent. Thank you so much.

A - Leonardo Loyola {BIO 16193219 <GO>}

Thank you, Boris.

Operator

Our next question comes from Carlos Macedo of Goldman Sachs.

Q - Carlos Macedo {BIO 15158925 <GO>}

Thanks. Good afternoon, gentlemen. A couple of questions. First, could you comment a bit on your effective tax rate? It was very low this quarter, just want to know, what we can think about going forward. It's generally been below your peers. Should we consider the levels that we've seen before or what should we think about this quarter in terms of the effective tax rate?

Second, this is a more general question, kind of following up on Saul's question earlier, looking into next year GDP growth being fairly weak, rates going up, your loan growth this year, you pulled your guidance down, it doesn't look like a loan growth next year should be that strong, all your peers have been talking about single digits or maybe very meekly into double digits in terms of loan growth margins, probably being flat despite the higher rates. What should we expect in this scenario, I mean given the amount of, I know you presented your capital situation, it is much better after the Hybrid Capital. But if you are unable to really deliver strong ROE and strong earnings growth and you still distribute 40% of your earnings as dividends, the likelihood that you rode your capital position going into next year is not insubstantial. Is that the correct reading or is there something more that we should consider?

A - Leonardo Loyola {BIO 16193219 <GO>}

Thank you, Macedo. Just starting from the second, that's -- it is okay. So it's -- this is pretty much the view. So, you know that we came with a much stronger capital base on the third quarter. One important thing to mention, that during the Portuguese conference call, I mean we are discussing the numbers for 2015 right now with the Board, that's why it's very hard to make assumptions for 2015 in a broad view, you are right. I mean it's going to an year of adjustment, but on the other hand there are many opportunities. That's why I wouldn't like to touch the 2015 forecast right now. So we are going to come with the guidance and the view for 2015 when we release the fourth quarter figures.

On the tax side, as you know, so we follow a strategy of hedging the assets abroad against the fluctuations in the FX. Particularly in the third quarter, we observed the movement in the FX that ended up in causing FX gains over the assets abroad, which was offset by the losses in hedge. The FX loss is deductible from the tax base. I mean, it reduced the effective tax of this quarter particularly.

Q - Carlos Macedo {BIO 15158925 <GO>}

Thank you. But this is something that all your peers also do and they were unable to report the effective tax rates quite this low, is there anything that should we consider this 20%, 22% effective tax rate is something that you will -- that will be recurring going forward or it was -- and you're saying that the FX variation kind of drove that this quarter. But when should we consider it as a recurring tax rate for the year, to put it that way?

A - Leonardo Loyola {BIO 16193219 <GO>}

Macedo, every quarter is a quarter, so we have to see quarter-by-quarter, it's very hard to predict. I mean, in this case it was caused particularly by the fluctuations in FX. So it's very hard to say exactly what is going to happen to the FX, just taking FX alone in the fourth quarter, that's why it's very hard to predict.

Q - Carlos Macedo {BIO 15158925 <GO>}

Okay. But just so -- it's just hard to insist, if we were to forecast a year, would the year at 22% make more sense or year at 28% make more sense?

A - Leonardo Loyola {BIO 16193219 <GO>}

It's a range, it's hard to say. So sorry for not being precise. But again, so you put the right range that it's reasonable to work inside within this range.

Q - Carlos Macedo {BIO 15158925 <GO>}

Okay. Thank you. Thank you, there.

A - Ivan de Souza Monteiro {BIO 16420543 <GO>}

Thank you, Macedo.

Operator

Our next question comes from Marcelo Telles of Credit Suisse.

Q - Marcelo Telles {BIO 3560829 <GO>}

Hello, gentlemen. Thanks again for your time. I have some questions. The first one still following up on Carlos question on the tax rate. I mean, when we look at the tax rate, we look at your, usually your managerial number which already adjust for the fiscal hedge that you do, right, and still you have a very low effective tax rate. So I think your explanation in that regard is actually on the accounting side, but if you already considered managerial where you already considered the fiscal hedge, there was some something in the tax rate that may have been lower, right.

So the question is, were you fully hedged or is there something that or you're under hedged in that case that might have caused to have a little bit more of an impact there. I think that will be one of the questions.

The other question would be, I mean, if you normalize for, let's say a lower, for a higher effective tax rate similar to what you had in the past about like 25%, your ROE would be, let's say below 15%. So we see your peers actually increasing ROE and you have reduced ROE, so the ROE gap has increased. So how should we think about your profitability next year? Do you think is there room for you to increase the ROE in the next year? And in your view what could be the drivers for that increase in ROE?

And finally, just one last question, if I may. Regarding your SME portfolio, you make an interesting disclosure of the loans that had been renegotiated, but loans there are, but loans that are not

overdue, but are in current status, but loans that you actually changed the terms, right. So if I look at your SME portfolio, do you have a sense whether this loans or this type of renegotiations pre-delinquency whether they have increased in the quarter or not? And how they have been behaving versus previous quarter? Thank you.

A - Leonardo Loyola {BIO 16193219 <GO>}

Thank you, Marcelo. Just taking the -- from the last one. So, it's stable. This is pretty much, we don't see any sort of change in this just taking the renegotiation alone. Just moving back to, just a second.

A - Ivan de Souza Monteiro {BIO 16420543 <GO>}

Marcelo, this is Ivan, we didn't discuss as I mentioned before, we didn't discuss with the Board about our budget for 2015. But I can tell you that we will focus on efficiency and we will focus on three basic business. As we mentioned before, the environment, it's a tough environment and there is a lot of volatility not only in Brazil but abroad. That's why we will be focused on increasing and trying to improve the ROE of the Bank and the main purpose of -- for us is to do increasing the fee business, the insurance, the card business, the fiduciary service, asset management, capital markets that you will know that 2014 was not a bright year for this.

And to try to diversify a lot, what we can do? I believe that the postal bank to be a very important source of new customers of the bank and very important source of the efficiency of the bank. We can -- probably, we are finalizing the business plan of the business and we can give more color in one or probably in one month or 45 days, but the main purpose of our work today is to increase the ROE based on this increase in the fee-based business and increasing the efficiency of the Bank, reducing the cost of the Bank overall.

A - Leonardo Loyola {BIO 16193219 <GO>}

Marcelo, just taking the first one, you mentioned if we hedge or if we under hedge, actually we over hedge the position.

Q - Marcelo Telles {BIO 3560829 <GO>}

No, I understand that. My point is that, you know that impact is already included in your managerial adjustment, so the low impact tax rate must be explained by something else, not because of depreciation, so that's my point.

A - Leonardo Loyola {BIO 16193219 <GO>}

There is nothing -- anything particular to that case, maybe we should follow-up with the IR team in Sao Paulo, just -- maybe go for the calculations if you need.

Q - Marcelo Telles {BIO 3560829 <GO>}

Sure. That will be great. And just as a suggestion, you guys have a very good, very good disclosure regarding this renegotiated credit that are still -- there are current on their payments, but you only release the flow of this credit. I think it would be very interesting to see if you could disclose in the future the balance of this credit, so that we can see the evolution of that line, that will be great.

A - Leonardo Loyola {BIO 16193219 <GO>}

Great, Marcelo. So suggestions from analysts here are very welcome. So as you know, we are always trying to bring more transparency to our MD&A and information like -- things like vintages of SMEs and credits for SMEs and things like that. So we are going to discuss internally and probably we're going to see if we can come up with something like this. Thank you very much for your suggestion.

Q - Marcelo Telles {BIO 3560829 <GO>}

That's great. Thank you, again.

Operator

(Technical Difficulty) Investor Relations website. Thank you very much for your participation, and have a nice day. You may now disconnect.

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