Q3 2019 Earnings Call

Company Participants

- Andre Rodrigues Cano, Chief Financial Officer, Executive Vice President
- Carlos Wagner Firetti, Market Relations Officer - Head of IR
- Octavio de Lazari Jr., Chief Executive Officer
- Vinicius Almeida Albernaz, Chief Executive Officer

Other Participants

- Eduardo Nishio, Analyst
- Eduardo Rosman, Analyst
- Giovanna Rosa, Analyst
- Jorg Friedemann, Analyst
- Thiago Batista, Analyst
- Tiago Binsfeld, Analyst
- Unidentified Participant
- Yuri Fernandes, Analyst

Presentation

Operator

Good morning, ladies and gentlemen, and thank you for waiting. We would like to welcome everyone to Banco Bradesco's Third Quarter of 2019 Earnings Conference Call. This call is being broadcasted simultaneously on the Internet at the Investor Relations website of Bradesco at banco.bradesco/ir, where you may find the presentation available for download as well.

We would like to inform you that there is simultaneous translation into English. All participants will be in listen-only mode during the Company's presentation. Afterwards there will be a question-and-answer session when further instructions will be given. (Operator Instructions).

Before proceeding, we would like to mention that forward-looking statements that we make during this call in relation to the Company's business perspective and operating and financial projections and targets are beliefs and assumptions of Bradesco's management as well as information currently available to the Company.

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

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

Now we would like to turn the conference over to Mr. Carlos Wagner Firetti, Market Relations Officer.

Carlos Wagner Firetti {BIO 2489005 <GO>}

Good morning, everyone, and thank you for participating in our call about the third quarter results. Today we have our CEO, Octavio de Lazari, Jr.; the Vice President and CFO, Andre Cano; the CEO of Bradesco Seguros, Vinicius Albernaz; our Executive Officer and Investor Relations Officer, Leandro de Miranda. And now, I would like to turn the floor over to Octavio.

Octavio de Lazari Jr. {BIO 17539074 <GO>}

Thank you, Firetti. Good morning, everybody, and thank you very much for participating in our call about the results of the third quarter.

There is a positive feeling regarding the moment that Brazil is looking so that we may achieve gradual, consistent and healthy growth and inflation under control. In the current published period, we consolidated the reform of the social security, a fundamental point for the sustainability of public finances in Brazil, and also for the preservation of our positive agenda for the Brazilian economy.

This combination of the fiscal and monetary policies, adequate and clear policies, in order to alleviate us from the very low economic growth allowed us to control inflation. And with a consistent drop in interest rate, we see a lower risk scenario that motivates more and more investments to operation and consumptions by the private economic agencies with a gradual recovery of the economic activity.

And this is very important for us as an organization because we prepared ourselves, and we are positioned to capture the benefits of a more positive economic cycle. On Page 3, we bring you our highlights. Expanded credit portfolio continues to grow in a healthy and well-diversified manner in the higher growth and return segments, as individuals and SMEs, the new venture -- new vintages [ph] are still improving 3.2% increase growth in the quarter at 10.5% in an annual comparison.

We especially highlight the performance of individual segments growing 19% in 12 months. Our fee revenue, which were under pressure, were adjusted in the previous quarters and already show signs of improvement with growth in the most important lines. We believe that from now on, they should continue to recover.

Our expenses, which were presented in a relatively strong increase due to planned strategy, they have already started to go back to their regular phase after a stringent and comprehensive program for expense reductions and controls that we will be detailing ahead. We are determined to keep them in line under control. And now that we have made the necessary adjustments, we have been able once again to present a strong quarter with a new record in our net income growing by 19.6% on annual comparison in the nine months of '19. Our net income was 22.3%, higher operating income to 11.6%. As a result, our ROE, nine months, remained higher than 20%. Our Tier 1 BIS ratio reached 14.7%, a 250 bps growth in the last 12 months.

And finally, it is worth highlighting the extraordinary event of R$8 billion recently announced, and we will keep an asset management of our capital considering growth opportunities and our projection of the optimal capital structure given the economic momentum that we will be leaving.

And starting to present details of our figures, let's go to slide number 5. Our net interest income grew 5.7% in the nine months year-on-year, and 5.9% a year in the quarter. The performance in this line indicates that we can stay at the center of the guidance. The risk profile of the new loan vintages continue to be very good. Our expanded loan loss provision expenses decreased by 4.3% in the quarter, accumulating a reduction of 4.9% considering a nine-month comparison. As a result, our net income recorded a 19.6% increase year-on-year in the third quarter of '19 and 22.3% year-to-date.

On slide number 6, we show you the indicator of our ROAE reaching 20.2%, considering the 3Q. Nevertheless, for analysis purposes, adjusting our equity by the R$8 billion extraordinary dividend, ROE would have been 21.5%. ROAA was 1.9%.

As we have been saying in the last quarters, we believe that we can keep the ROE higher than 20%. And in spite of the impacts of low interest rates and spreads slightly decreased, we would have had our future return benefits from a stronger loan volume growth, a more favorable portfolio mix and scale as well.

And looking at the longer term, considering the maintenance of low interest rates and falling spread scenario, we could see a reduction in returns, but we believe they will still remain at a high level, especially because of the lower level of risk of the demand loss provision.

Now going to page number 7. Growth in our loan portfolio accelerating again, as we have said, it would happen close in Q3 at 10.5%. The highlights for the individual segment, which recorded a 5.5% growth in the quarter, 19% year-on-year, with all lines showing a good performance. And it is worth highlighting, personal loans, which improvement in the product journey, mainly in the digital channels, growing by 62% together with more competitive rates and longer tenure and increases of analytics led to portfolio to have a 9.7% growth in the quarter and 36.2% in an annual comparison. Payroll loan, we grew by 24.1% year-on-year. And we have a unique position in this product due to our distribution network, public sector, payroll agreement and also public pension system processing, where we are the leading bank.

It's important to say that 78% of our origination of payroll loans is carried out at our branches, therefore, without paying any commissions whatsoever. And we had a good performance in mortgages as well growing by 16% with good perspective, and vehicle financing, 21%. It is also worth noting the growth of cards, which accelerated now to 2.5% [ph] year-on-year.

And in the Company's portfolio, there was an acceleration in SMEs, which grew by 8.3% year-on-year, but adjusting for the migration of customers between segments and the slowdown in corporate will be increased 12.9% and we already expected this. And the increase is stronger in small companies than in mid-sized companies.

Now let's go to Page number 8 where we show our credit origination, which continues to have a good performance, both for individuals and companies and with a good perspective for a longer term growing by 35.5% year-on-year for individuals and 40.8% for corporations. On Slide number 9, we discuss our net interest income.

Total NII grew 5.9% year-on-year, accelerating the credit margin growth to 5.2%, while the margin with the market remained actually flat in the quarter. The positive effect of the mix and the volume growth during the quarter have outrated the negative effect of the following spreads. We believe that the effects of the positive mix and volume growth should continue to offset the book spread reduction and the renewal of the loan book.

On Slide 10, we talk about the delinquency. Delinquency remained flat in individuals with an increase in SMEs and a higher increase in large caps as a result of few specific cases. Nevertheless, this has not affected the loan loss provision expense as the cases were totally provisioned, most of them. Overall, we see delinquency under control and aligned with our product mix strategy.

On Slide 11, we talk about NPL creation. We maintained a good performance in terms of provision expenses with a reduction in the quarterly nominal terms. And the cases have led to the increase in NPL creation were already provisioned for. And the cost of risk ratio dropped 20 bps, going to 2.3%.

On Page number 12, we show the NPL creation per segment, and we can see the increase in the quarter is concentrated in specific corporate status [ph] . On Page 13, we talk about fee income. We had a better performance in the third quarter with 3.7% increase year-on-year and 2.5% year-to-date, that is to say accelerating in the third quarter.

And it's worth noting the good performance of the annual comparison of cost study and brokerage consortium, checking accounts and loan operations. In the quarter, 4.8% increase in asset management, despite a reduction in private pension administration fees that happened in the first quarter. We have additional initiatives in this area being implemented in wealth management, which should certainly produce increased results in the coming months.

On Page 14, operating expenses. The increase in cost above the guidance was mainly due to important decisions made earlier this year, such as the implementation of the new branch network compensation program. The increase in the number of labor lawsuit settlement because of costs and reinforcement and something such as the next team and the hiring of a more robust team of data scientists. And we understand that we have to improve our performance in expenses, and we have already taken all the necessary measures in order to reach this target.

On Page 15, on Slide number 15, we highlight the measures which should allow us to have a much better performance in costs in 2020. You can see that we should close -- we expect to close the total of 150 branches in 2019. Therefore, 100 more per year up to the year-end 2019. And we have plans to close another 300 branches in 2020, at least an additional 300 branches.

In future periods, we should have a lower number of employees as a result of the new voluntary redundancy program and continued adjustments in addition to our productivity gains from digitalization. Just to give an idea, so far, we had over 3,000 employees joining our voluntary redundancy program, and this figure is higher than our plan. And finally, we believe that the labor lawsuit expenses in 2020 will be lower than this year.

Now going to Slide number 16, talking about our insurance company. The net income of the Insurance group was R$1.880 billion [ph] at 2.8% growth in the quarter and 28.9% year-on-year. And ROE reaching 24.1% in Q3. We should note that the acceleration of premium growth would reach 12.3% year-on-year, highlighting the strong performance in life and pension, which grew 8.3% in the quarter and 18.2% year-on-year.

On the next slide, number 17, we highlight the 20.1% evolution. Year-to-date, the net income with a 23.6% ROE, health and P&C segment, stood out in terms of earnings performance. In the three months -- in the nine months comparison, which eliminate seasonality, which is better for the insurance company purposes, we recorded improvements in the group's consolidated combined and claims ratios.

Going to Slide 18, we closed the quarter with the cost of BIS ratio of 14.7% and the impact on the BIS ratio of R$8 billion extraordinary dividend distribution will partially be mitigated by the reallocation of the group's insurance is also via dividend. As you can see, this pro forma bar here, the last one on the slide. And the -- only 60 bps of this drop will be mitigated, additionally, by what we will be accumulating in the fourth quarter.

Now talking about capital management on Page 19. On October 7, we announced extraordinary dividend of R$8 billion, representing a yield for a distribution of approximately 3%. And we will define our distribution of the excess capital generated in our operations figuring the following assets, business opportunities, the risk -- the environment risk level and the view of an optimal capital structure for the economic moment that we will be leaving.

And on the last page, on Page 20, in relation to our guidance for 2019. What we can say about our guidance is that we should remain in the middle of the guidance in the extended portfolio, 11%, may be a little bit more. In the middle of the guidance for the net interest margin, 6%. In the lower part of the guidance for fee revenues, between 3% to

4%. Above the guidance in operating expenses, it should go down from the level that we have today and above the guidance in earnings from Insurance operations at 13.7% going to 5.9% [ph] .

And on the -- above the guidance in earnings from the Insurance operations -- in the upper part of the guidance is the extended loan loss provisions, R$13 billion to R$14 billion. So these are the data that we wanted to inform to you. Thank you very much for your attention.

Now we're going to go to our Q&A session.

Questions And Answers

Operator

Thank you very much. Now, we will start our Q&A session. Questions in Portuguese may be asked and the other participants, could you please remain in listen-only mode?

(Operator Instructions). (inaudible) from Credit Suisse. You may proceed.

Q - Unidentified Participant

Good morning everybody and thank you for the opportunity. I have two very quick questions, if you allow me. The first one has to do with the spreads. We see a drop that you show of about R$300 million per quarter in this quarter in this waterfall chart.

And I understand that part of that is a repricing of your back book of corporate. So my question is the following, from now on, are you going to reprice a loss? The negative R$300 million, should we continue to see this in the next few quarters? And the second question is about the OpEx. It seems to me that you will be above the guidance for this year but could you share with us an internal estimate about the cost reduction coming from the closing of these 300 branches may be --

A - Andre Rodrigues Cano {BIO 17254737 <GO>}

Thank you very much for your question. And with relation of the spreads, the answer is no. There will be a spread reduction. This is only natural with the reduction of the Selic rate that yesterday dropped to 5 and already contracted for the (inaudible) And as of February, it should -- they should more carefully measuring this by the (inaudible) the economic activity, etc.

But this should be followed by a higher growth in the economy. This is what we believe will happen, and this will allow us to monitor the spread levels. But we grow in the portfolios that have different spreads, like to the individual and the SMEs portfolios.

But for large caps, this is a fact that we have already been living since the beginning of this year. We have different costs for our commercial portfolio. We were talking about an

IOF of 2% and there is a natural migration to the capital market.

So I'm not going to repeat the R$300 million, as you repeated. And regarding the branches, this is an important homework that we are doing, closing 300 branches is our expectations, at least 300 for next year. It is difficult to talk about numbers or figures because there are many factors that come into play besides the physical structure and the rent and personnel, but the cost reduction is very significant as we digitalize. The company costs 70% lower or when you transform these branches into mini-branches only for businesses.

Then you no longer have cost. However, you have -- you still have net revenue. It's very difficult to quantify this. But what I can say is that it will be very big. In relation to the back book, most of the pricing should come in one single quarter or one additional quarter only. Thank you very much.

I would like to remind you that 300 branches represent 6.5% of the whole branch network of the bank. It's a very considerable figure.

Operator

Eduardo Rosman from BTG Pactual.

Q - Eduardo Rosman {BIO 16314825 <GO>}

Good morning, everybody. I have two questions. The first one is the following. I would like to know how you see the excess AOL. We saw that this offers some reasons for the excess. AOL continues to be stable. So are you going to review your policy of never reverting your provisions because recently you decided to review your dividend policy.

And the second question, would you like to give us more color for next year, the most important lines. And you mentioned during the call that next year, expenses will have a better performance than this year. And do you see room for fees going up more than in 2019? It would be interesting to know why you feel so comfortable with that?

And could you give us an idea about your loan portfolio may be going up, maybe more than in 2019 NII. Does it make sense to imagine that it will be growing more? I know that you don't have a guidance to give us, but can you give us some indication regarding what you expect in terms of the bank's results for next year because you mentioned that the ROE should be close to more than 20% in 2020.

A - Andre Rodrigues Cano {BIO 17254737 <GO>}

Thank you for your question. In relation to the excess NPL, as we have been repeating, there is a practice that we have not been using. That is to say regarding the nonperforming loan, we consider this as a buffer.

And we believe that there is room to consider the excess NPL not any longer as a buffer, but looking at it, within the process of migration for the migration towards IFRS 9. Although it could still be discussed for 2021, 2022, we should start to run this regarding the positioning and doing this even more in advance. So all the provisions would be included in this both, so as you say and -- well, this is what I can say regarding the excess allowance for loan losses.

Regarding the outlook for 2020, I will try to answer this and I will try to avoid giving you a guidance. And -- but I think some of the discussions are already underway in the credit scenario, we believe that the credit scenario will be quite good especially in lines that brings higher margin, individuals and SMEs. And also, the back book will be repriced.

Obviously, there is a consistent gradual repricing, but we got a period of very high spreads, 2016, 2017. So we still have part of that in our book. But we believe that for 2020, the evolution of credit margins considering the effect of spreads and mix will be better than in 2019.

And maybe with a slight reduction, but allowing the average price of the volume that we expect to be quite big, expecting this to play a more important role of the -- then the NII as a credit and NII as a whole. You have the market NII part, where we put our -- well, we believe there will be a positive effect.

But of course, this will happen over time. But we believe that the scenario for NII for next year is constructive. In relation to expenses based on the work that we have been doing and what Octavio has already mentioned during his presentation, we believe that the performance will be much better as far as costs are concerned.

And we intend to achieve this as fast as possible. And the fee line improving. I would say that this year, it is close to the bottom of the guidance, around 3%. And it will be better next year. And you have to keep in mind that this year, there were some stronger impacts of acquiring and the debt (inaudible) , started in October last year.

So we believe that net of these effects and the volume growing more strongly, we will be able to have a better performance in this line. Insurance, maybe Vinicius would like to talk.

A - Vinicius Almeida Albernaz {BIO 17958985 <GO>}

Well, about the Insurance scenario. Well, we see a gradual rebound of the economy. So we are experiencing a good top line growth in the insurance line. And with lower interest rates, I think this should be offset by the divisional growth. I think this is the landscape that we envision looking forward.

A - Andre Rodrigues Cano {BIO 17254737 <GO>}

Just to add, in terms of expenses. I think it has to do with what we talked about in terms of reducing the number of branches allows for loan losses that is higher than 2,000 [ph] , 3,000 employees, and that was our initial expectation. And even in the actions related to expediting labor agreement even before the labor reform, this helped boost the economy and it will help us towards 2020.

I think we should envision a better day because we are increasing the customer base by 1.5 million clients. And in 2019, we will have 2 million clients. Once you break this down, in addition to all of the payment means that we are acquiring, 74% of payrolls is now in the hands of Bradesco. So with all of that, we have fees, we have credit cards, in addition to that, we also have other products, services, loans, payroll, deductible loans.

And all of that can give us a better outlook for next year. Right?

Q - Eduardo Rosman {BIO 16314825 <GO>}

Right. That's great. Thank you. Thank you very much.

Operator

Our next question from Gabriel Nobrega from Citi. You may proceed. Mr. Gabriel Nobrega, you may proceed.

Q - Jorg Friedemann {BIO 15405752 <GO>}

This is Jorg Friedemann. I have two questions. The first is about write-offs. I noticed that this quarter your write-off was down by 20% vis-a-vis the previous quarter. It's the lowest one since 2017. And I don't know whether this should be seen as a new normal because it was -- it appeared in several lines, not only in corporate, SMEs, et cetera.

So I would just like you to elaborate a bit more on right-off evolution. And my second question is with the approval of the pension reform and the likely increase in the banking sector. We hope that this will have a positive impact on the part of the banks in terms of the evaluation of tax credits.

And given the inventories you reported on the third quarter and according to my evaluation should be over R$6 billion. So how do you intend to approach that in terms of destination? I just want to understand what you would do with that?

A - Andre Rodrigues Cano {BIO 17254737 <GO>}

In terms of write-offs, there is nothing new, It's just a cycle. If you look at the provisioning cycle, considering all the provision in ten years in terms of (inaudible) , considering collateral. So in a way, this dropping write-offs is just a consequence, stemming from the facts that the credit quality has improved. So after some time, this is just a natural consequence.

So it was just expected that right-off would attain this level. Now in terms of tax credits, our expectation is that the reassessment of these credits should generate something like R$6 billion. And then, we will still have to evaluate and think about what we will do because it's possible that something will go into provisions, but this is yet to be decided.

Q - Jorg Friedemann {BIO 15405752 <GO>}

Okay. Perfect. Just add something else in regards to taxes and whether you could give me an idea of how the effective tax should evolve in terms of the bank. I understand that this does not cover all of the businesses of the organization. So maybe this shouldn't have a full impact. But if you can give me an idea, it will help me out.

A - Andre Rodrigues Cano {BIO 17254737 <GO>}

What we've been saying is that this year's taxes, according to what we have been talking about, should be close to 28. And if the new tax rate of (inaudible) as you indicated, taking only the bank and not all of the other businesses it should have an impact of 2% or 2.5% in addition -- percentage points.

Q - Jorg Friedemann {BIO 15405752 <GO>}

Thank you.

Operator

Next question from Giovanna Rosa from Bank of America. You may proceed.

Q - Giovanna Rosa {BIO 21036371 <GO>}

Hello, good morning and thank you for taking my question. I would like to revisit the issue of cost. You talked about adding 3,000 employees to your voluntary severance program. And I would like to know what is your outlook for next year? When I look at cost per employee, I arrive at an economy savings of about R$630 million for next year.

I mean, I know that these employees have joined the program, they are older employees so maybe those numbers could be higher. If you can give us some idea of your savings -- your figure regarding savings in this regard, I would appreciate it.

A - Andre Rodrigues Cano {BIO 17254737 <GO>}

I think that your assessment that looking at the tenure of the employees and the average cost is higher, it's true. But we don't have yet any numbers to share with you at the moment. This has and will have a relevant impact. This is almost 3% of the employee base of the bank, but we don't have yet any number to share with you.

In fact, this program, the voluntary severance program ends today. So this number of 3,000 refers to day before yesterday. So we feel you may have some variation. Moreover, it also depends on who is joining the program because we have people from different job descriptions, different positions in the company. So we still have to run a more thorough analysis. But your calculation makes sense.

Q - Giovanna Rosa {BIO 21036371 <GO>}

Okay, thank you. My second question is more related to credit quality and provision. When we look at the next quarters looking forward, a part of that will be used when the IFRS 9 is implemented. But should we expect that ALL should grow below that portfolio? Or from now on they will be moving hand-in-hand?

A - Andre Rodrigues Cano {BIO 17254737 <GO>}

Well, basically, we think that we still have a positive effect of the loan vintages until the end of the year, and I think that the numbers should be lower when compared to the loan portfolio that we've been posting. But as for next year, we should see growth more in keeping with the growth of the portfolio.

We are well-positioned, and we are growing in the individual segment and the segment of micro, small and mid-sized companies. And we are experiencing a unique environment in Brazil. Therefore, we believe that there shouldn't be any pressure in terms of provisions.

That's at least what we've been experiencing, looking at the natural growth of the segment. Now this quarter, we don't believe that levels will deteriorate. On the contrary, with the growth of the economy and all of the controls, increasing consumption, lower interest rates, I mean, NPLs should go down.

Q - Giovanna Rosa {BIO 21036371 <GO>}

That's very clear. If you could give me just a follow-up of your answer. You are growing significantly in the individual and SME segment. I would just like to understand whether there is still room to sustain this growth? Or you reached the top of growth for both lines?

A - Andre Rodrigues Cano {BIO 17254737 <GO>}

No, we still see further growth in both lines because unemployment is still quite high in Brazil, in particular in regions where we have absolute leadership and market share. Therefore, we should see growth in individuals and also, particularly in macro and small companies, we should see some economic growth.

Therefore, as we manage our credit models and our algorithms, we are now more comfortable to understand the profile of our customer and we feel comfortable when expanding our portfolio. So we haven't reached the top yet. There's still room for growth.

Q - Giovanna Rosa {BIO 21036371 <GO>}

That's clear. Given the fact that provisions for these portfolios tend to be lower when compared to a large corporate, it's just natural that the provision levels looking forward should be better than the current levels, right?

A - Andre Rodrigues Cano {BIO 17254737 <GO>}

Yes, you're right. Because we are seeing a reduction on the side of large corporates. And so your reading is right. If we don't have growth in the same level, if we were to grow the same way individuals in SMEs, that would be different. So if we reduce large corporates -- I mean, the fact that we have new operations, these are operations on the individual segment. I mean, this is still very healthy because these are new operations and they are performing well. And with the advent of new things to be adopted next year, like IFRS 9, our position should be even more stable and this performance should be even better.

Giovanna, I think you should look at the next spread because the size -- the pressure on spreads in several segments, when you look at next spread, you'll see growth and we've been growing. And in this segment, we can keep the bulk of our current revenues because we are seeing now the entrance of new consumers and new clients.

Q - Giovanna Rosa {BIO 21036371 <GO>}

Yeah, that's very clear. Thank you very much.

Operator

Our next question is from the Thiago Batista. You may proceed.

Q - Thiago Batista {BIO 15398695 <GO>}

Good morning. I have a few questions on the insurance side. The first has to do with cost reallocation because you said you will generate substantial gains. And my question is whether it is only this capital line? Or we should see any other activity similar to that in the coming years?

A - Andre Rodrigues Cano {BIO 17254737 <GO>}

This quarter, as Octavio said, when we look at nine months, we see some leadership positions, but when we look quarter-on-quarter, there was a worsening scenario.

Q - Thiago Batista {BIO 15398695 <GO>}

I mean, you are above in some quarters today than where we are in previous quarters. What should we expect looking forward? Are we going to see improvements? Or maybe the opposite?

A - Andre Rodrigues Cano {BIO 17254737 <GO>}

Let me give the floor to Vinicius now.

A - Vinicius Almeida Albernaz {BIO 17958985 <GO>}

Let me first refer to the claims ratio. In fact, if you look at the nine-month period, we see a very favorable period for individual income (inaudible). When we look at quarterly figures, what we see is a seasonal effect. This quarter was affected by the health claims ratio and this affected our overall claims ratio.

In terms of frequency, this is common due to seasonality reasons. And at the same time, we have an additional effect, which is a larger number of business days. We had a few more days during this quarter when compared to the previous quarters, and even more days compared to the second quarter of this year, and this affects frequency.

If you look at combined figures, there are some good news because despite this worsening in claims ratio, we have been putting good efforts to control cost, et cetera. And to control our assets have been an adequate move to maintain the combined effect and to maintain things stable.

Now this effect, the seasonal effect, has to be analyzed because there are some peculiarities here. We had a third quarter which was very positive. We see a growing trend coming -- still coming from the first and second quarters. We are monitoring the situation. We've been looking at the performance of the insurance line.

So we still see some room for improvement and we are monitoring and also see when we should resume to normal figures. This is not the case at the moment. The average cost of these procedures, everything is under control, it is way below inflation and in keeping with what we've been doing in the past. So in relation to the average cost, we are very comfortable. And this effect is an effect of frequency. It has also included seasonal effect. When we talk about claims ratio, it's also -- claims is also important to talk about premiums earned and job generation, the market -- the health care market is very competitive.

And we've seen payers with lower capacity to transfer prices. We had to increase our portfolio. I mean, in this quarter we didn't see any positive effects from that increase in our portfolio and so this will have a positive effect looking forward.

A - Andre Rodrigues Cano {BIO 17254737 <GO>}

Now talking about dividend. I'll now give the floor to Firetti to comment on that, our capital management.

A - Carlos Wagner Firetti {BIO 2489005 <GO>}

In terms of solvency and the insurance company in our holdings, we can say that this was not an impact to capital. And so, management is just normal. Every month we -- depending on the provision levels, we manage that in a monthly basis. And we study that on a monthly basis in order for us to maintain an optimum level of capital in the insurance company. But we also have to look at the optimum level of capital because we don't want that to reach the BIS ratio. Or to affect the BIS ratio.

Q - Jorg Friedemann {BIO 15405752 <GO>}

Thank you.

Operator

Our next question from Tiago Binsfeld from Itau BBA.

Q - Tiago Binsfeld {BIO 19874107 <GO>}

Good morning and thank you for taking my question. I have two questions. Going back to the number of current account holders, you have 1.5 million that you add to your base every year. How much of that is due to your strategy in terms of payroll?

And Octavio said that Bradesco has 74% of all payroll accounts. I want to know whether that only refers to civil servants or also servants from the private sector? I just want to know what generally increases in the operating risk this quarter? And whether we should expect additional effects looking forward.

A - Octavio de Lazari Jr. {BIO 17539074 <GO>}

Tiago, this is Octavio. In terms of our current account holders, and the fact that we are adding 1.5 million accounts to our network of branches, I would say that 40% of these accounts come from payrolls that we acquired, and the remaining comes from our own internal work and some agreements that we have, like with Avon and other companies, that helps make up that two numbers. So it is mostly related to payroll accounts and also our own internal work to procure customers, clients.

It's also important to say that our focus in terms of payroll accounts is mainly in the public sector. We work in the relationship with bankers. And about RWA, in terms of the market, I think we have to look at the volatility of the market and we have to factor that in the cost of the business and in terms of capital, and this could vary up or down.

And you should recall the landscape in the third quarter. But now talking about operating risk, a periodic review, so we don't see any frequent variation. In terms of the market -- on the market side, the number should be lower because the volatility in the environment is lower.

Q - Tiago Binsfeld {BIO 19874107 <GO>}

Okay, thank you.

Operator

Next question from Eduardo Nishio from Banco Plural. You may proceed.

Q - Eduardo Nishio {BIO 15333200 <GO>}

Thank you for this opportunity. Good morning, everyone. My question, it's a bit long but it's a follow on to Jorg's question in relation to the outlook looking forward. We are now going through structural changes. I mean, yesterday we had another cut in the civic rate, minus 5% now. And so now we're probably heading towards even lower number than years ago, we couldn't even think that something like that would happen.

So my question to you is how do you see the landscape looking forward? Or maybe if we focus on loans, fees, costs and on the insurance side, how do you see this scenario when interest rates are structurally lower? And how does it impact your businesses, whether you grow or whether you would not grow? And if you could also mention about competition in the market, it will be interesting.

A - Andre Rodrigues Cano {BIO 17254737 <GO>}

We see the growth of FinTechs and they are hardly charging any fees for their services.

Q - Eduardo Nishio {BIO 15333200 <GO>}

And as a consequence, whether -- I want to know whether you could maintain ROE around 20%. I think even more important to that, your bottom line in two digits because maybe we could utilize capital. But also I want to know whether you can grow your net income or your earnings in the next coming years?

A - Octavio de Lazari Jr. {BIO 17539074 <GO>}

Eduardo, thank you for your question. This is Octavio. I think you are very right in what you're saying. We are looking at a shorter term period and that's why we said that we will be able to maintain that return of around 15% to 20% or even slightly above. But we are experiencing a structural change and this will be the new normal. If we think in terms of an interest rate that is now 5% or may be 4.5%, depending on whether it will be lower with inflation rate at around 2%, 3% or even 5%, we will be talking about an actual rate of 1%. And this will lead us to believe that in the longer term, it could even be lower or it grows as you put it quite well, can no longer be a two-digit growth. On the other hand, we have the opportunity to capture business and this is a very unique opportunity for (inaudible) Brazil, because we usually started and we will sail with good wins for one or two years and then things will go backward.

So if we think about the investment that Bradesco did, particularly with the purchase of a few banks and all of the new payrolls that we're adding to our base and new non-payroll clients, considering the fact that there we still have a lot of unemployment and people that are misplaced.

Once they return to the labor market, I mean, we are well positioned to capture payroll accounts, current accounts, to capture more clients in the health care segment because we're not losing our clients to the competition, just clients left because they were unemployed.

Therefore, we were able to grow despite all of these fact. Therefore, I believe we still have a lot of opportunities on the table. And they will allow us to look for what we want, an economy with low interest rates. So if you don't manage to get scale, you won't be able to keep growing around two digits or at a high one digit.

When we look at all the possibilities we have -- of course, there are FinTechs, there's a lot of competition. And we are not even FinTechs. When we talk about investments and you have a lot of large companies. When we talk about acquiring, you have a lot of companies already operating in these segments.

This is all true. But the growth that can be expected in the market, considering a higher capacity for the Brazilian economy to grow, we still have a lot of people that are not part of the market. And once they return, things have changed. Look at what happened to the real estate market seven years ago.

And the growth we had, once we reached the level of full employment -- of almost full employment. But unfortunately, it didn't last very long, almost just one year, and then we had to go backwards and the banks had to step on the brakes. But that level of growth was the new normal with the low interest rates and good unemployment rates.

There are many challenges, but I think there are more opportunities than challenges, and we will be able to grow and observe all that labor force, especially because of the growth of Bradesco.

Q - Eduardo Nishio {BIO 15333200 <GO>}

Thank you very much.

Operator

Next question from Yuri Fernandes from J.P. Morgan. You may proceed.

Q - Yuri Fernandes

Thank you for taking my question. I have a question on funding. Looking at numbers of the quarter, and I know the situation maybe volatile, but that is very low. Deposits were about 4%, whereas the loan portfolio grew more. I know that the bank is very liquid. But how do you see competition for liability? Will that be a problem in the future? I mean, there are digital banks and some independent organizations. Do you think that this could be a problem for you in terms of the cost of the banks?

The second question is about assets under management. We took a look at your assets under management, AUM, and there was a drop and this is something that has been happening in the last few years. Maybe you could tell us whether you have any plans to improve performance in this line of AUM? Or whether this is related to any specific case or any specific client that left your customer base? Thank you.

A - Octavio de Lazari Jr. {BIO 17539074 <GO>}

This is Octavio. Very good remark. Your remark is extremely timely. And this is the job that we have been doing for a long time, and the bank that has a network such as the one that we have. And with the level of unemployment in Brazil, it gives you the impression that you do not have the same performance of the economy. But just to give you an idea, all the wealth management area of the bank was changed, how we are training 230 people in our organization, experts in investments.

We are not concerned with that right now because when the economy gets better, if you have a lower unemployment rate. Of course, we will have a much better situation for growth management, coming from the different types of funding, from the different sources, digital bank and our branches, etc.

So this is something that we are studying very thoroughly, mainly in our prime clients who are very important clients when you talk about investments. And then the other funding lies [ph] from our retail clients because funding of the wholesale bank, you can do this whenever you want.

So we do not need investments in this kind of funding, and we do not have a big reliance on that. And the funding that is cheaper for us is in prime and retail bank as a whole. But your question, your remark is very good and we have taken all the measures regarding that. And your other question has to do with brand, the Bradesco asset management that suffered the more aggressive competition, mainly from the new entrants in the market and other that are not so new.

With an interest rate at levels that they are today and going down, people will have more clarity about financial investments when the investment they are looking for other types of investments and not only fixed income, in order to try to obtain some more eggs in this basket and with a better income. But this is the challenge for all the asset management companies. Of course, we've had many portfolios under management and I believe that brand was able to have an excellent learning curve.

And as of the third quarter, we will be seeing this, that is to say from now on. Sometimes you don't have -- you increase your participation but you do not increase your profitability, and this is not our focus.

Q - Unidentified Participant

Very clear. Thank you very much.

Operator

Daniel (inaudible) from Santander.

Q - Unidentified Participant

I would like to refer to what was said here, with SG&A higher because of the branches, et cetera. And Next, how do you project the breakeven for that? Where do you believe this will leave your liabilities line and you start to have a return on these lines? So this is my question.

A - Andre Rodrigues Cano {BIO 17254737 <GO>}

Daniel, good morning. For Next, we already have the defined strategy. Next will have a separate structure. It has already moved, and will be transferred to their own facilities with an IT area, with a different CEO, with a different human resources area. And this is the phase of building up your muscles, that is to say in a few years, we believe that Next -- well, we do not expect any good results yet because the investment is high. But with the increase in SG&A, we might have to stop this line of liabilities. So to say and having Next bringing revenue before schedule, and this is a strategy that we are establishing for the future.

Digitalization is a crucial point. It means a decrease in the back office in the branches and this is what we're seeking, but mainly for businesses. So doing that we can tap into the commercial strength of our team and not be concerned at the end of the day of doing the most bureaucratic part. So this is the process that we have already accelerated with our IT area and it is already on track in terms of digitalization and also the decrease in our back office at the branches, and focusing on the commercial area, the business area.

Q - Unidentified Participant

Thank you very much.

Operator

As there are no further questions, I would like to turn the floor back to the speakers for their final remarks.

A - Carlos Wagner Firetti {BIO 2489005 <GO>}

Thank you all very much for participating. Any additional questions, please contact our IR team and we'll promptly answer your question. Thank you very much.

A - Octavio de Lazari Jr. {BIO 17539074 <GO>}

Thank you, have a nice afternoon.

Operator

Bradesco's conference call is now concluded. Thank you very much for participating and have a very nice afternoon.