Q3 2013 Earnings Call

Company Participants

- Alfredo Egydio Setubal, EVP and IR Officer
- Rogerio Calderon, Corporate Controller and Head of IR

Other Participants

- Boris Molina, Analyst
- Carlos Macedo, Analyst
- Daniel Abut, Analyst
- Jorge Kuri, Analyst
- Marcelo Telles, Latin America
- Mariel Santiago, Analyst
- Mario Pierry, Analyst
- Saul Martinez, Analyst

Presentation

Operator

Good morning, ladies and gentlemen. Welcome to Itau Unibanco Holding conference call to discuss Third Quarter 2013 earnings results. (Operator Instructions)

As a reminder, this conference is being recorded and broadcast live on the investor relations website, at www.itau-unibanco.com/ir. A slide presentation is also available on this site. The replay facility of this conference call will be available by phone on (55 11) 4688-6312, access code 8549644#.

Before proceeding, let me mention that forward-looking statements are being made under the safe harbor of the Securities Litigation Reform Act of 1996. Actual performance could differ materially from that anticipated in any forward-looking comments as a result of macroeconomic conditions, market risk. And other factors.

With us today in this conference call in Sao Paulo are Mr. Alfredo Egydio Setubal, Executive Vice President and Investor Relations Officer; Mr. Caio Ibrahim David, Chief Financial Officer; and Mr. Rogerio Calderon, Corporate Controller and Head of Investor Relations.

First, Mr. Alfredo Setubal will comment on Third Quarter 2013 earnings conference. After, management will be available for a question-and-answer session. It is now my pleasure to turn the call over to Mr. Alfredo Setubal.

Alfredo Egydio Setubal {BIO 1528623 <GO>}

Good morning, everyone. It is a pleasure for us to be here again for the Third Quarter conference call. (I think these are the best results that we have seen) since the merger between Itau and Unibanco. It's the best quarter. I think in all lines, the trends are very good. And we were able to confirm that our strategy, especially the strategy that we took the last two years reducing the risk of the Company and controlling much better the costs and reducing costs, paying off now with these Third Quarter numbers.

For those who are following through the internet, we are starting on the slide number 2, the highlights for the quarter. Of course, the first one is the recurring net income of a little bit over R$4 billion, a growth of 11% when we compare to the Second Quarter of 2013. And the total net income for the year, R$11.2 billion.

This result implies in a recurring ROE of 20.9%, an increase of 160 basis points when we compare to the Second Quarter and 240 basis points when we compare to the Third Quarter. Year to date, the ROE is almost 20% -- 19.8%.

Other highlights. On the loan portfolio, the growth of 2.9%. And 10% when we compare to the last year. If we don't consider the decrease of the vehicle portfolio that reduced 20.9% in these 12 months, the increase of the total credit portfolio would have been 14.3%. So much in line with the growth of the (system inventory).

Financial margin with clients, an increase of 1.7%. The total, R$11.5 billion in the quarter, R$33.7 billion year to date. It is a good trend that the margin with clients for this quarter again increased. And we expect that this line to continue to increase after some quarters in the past that reduced due to the new strategy of reducing the cost and changing the credit portfolio. Now, we are in a trend, even though it is not very high, the growth of this line. But at least we're starting to grow, what is important for the trend and for the future of our revenues.

Financial margin with the market, this quarter is still below the average that we used to have in this line. But better than the Second Quarter. The Second Quarter was our worst result in terms of financial margin with market. And this quarter, R$340 million. The average, when we consider (the past two years), is around R$500 million. In the past, the average was close to R$800 million. We don't see these numbers going back to the same level. But we expect that we can have better numbers, more close to the average, in the coming quarters.

Financial margin of credit, net of loan loss provision expenses, an increase of 5.5%, the fourth consecutive quarter that we show a better number in this line. And the total was R$6.6 billion.

Good news continues to come from credit quality. We improved the 90-days NPL ratio to below 4%. We achieved 3.9%. It was a reduction of 30 basis points in the quarter and 120 basis points in 12 months.

Another good news is that the delays between 15 and 90 days continue also to improve to a better number, the ratio this quarter finishing 3%. So it's the lowest level that we ever have, an improvement of 40 basis points in this quarter when we compare to Second Quarter. So it's important because the delays that we have today if they are reducing show us for the past experience that the 90-days will continue to reduce in the coming quarters.

Loan loss provision expenses also reduced, again in this quarter, when we compare to the Second Quarter. The total was R$4.5 billion and R$14.4 billion when we compare 12 months.

Commissions and fees also in a good trend, better than we expected at the beginning of the year. We are in a trend of almost 24% in this line, including the results from the insurance, pension plans. And capitalization business. But anyway and considering Redecard 100% in this line, the growth was very strong and sustainable. So it also is a very good news for our Third Quarter results.

Non-interest expenses continue to be a main objective and a main focus of the bank. It's part of our strategy to reduce the costs to increase the ROE, through this better control of expenses. And in this quarter, the growth was 0.9%, also a good number. And when we adjust the Redecard numbers, full consolidation. And adjust the basis of last year to compare to 2013 when we already had 100% of Redecard, the growth was 4.4%, in line with the guidance that we showed at the beginning of the year.

Considering all these revenues and losses and expenses and everything compounded, the risk-adjusted efficiency ratio improved 370 basis points in this quarter and 340 basis points when we compare nine months, in line with we were expecting here in the risk-adjusted considering the NPLs and the claims for insurance.

On slide number 3, we see the result of the bank for this Third Quarter, with much better numbers, as I mentioned, in terms of financial margin with clients and loan losses provision expenses. We continue to expect both lines to improve in the coming quarters, margin with clients increasing, showing growth again. And some more reduction in the loan losses expense. And also, a better and continuing to control the operational expenses too, as I said, as part of our strategy to continue to grow the results of the bank in the coming quarters.

On slide number 4, we can see banking and insurance operations splitted. We can see that from our recurrent net income of R$4.022 billion, R$3.27 billion came from what we consider the banking operations and R$618 million came from our insurance operations. Insurance continues to be a very good business. We continue to increase (our banking and insurance) business and products. And with a very good efficiency ratio and ROE of 36.5% for the insurance business and efficiency ratio of 32.3%. So this is a good business. And we will continue to pay a lot of attention to these (banking and insurance) products.

On slide 5, we see the net interest margin that continued to reduce in this quarter, achieving 10.9%. Good news came from the net credit spread, the green solid line, that continues to improve. We achieved 6.9% one year ago. And now it's 7.4%. So we are in a much better position. And of course it's helping us in terms of results.

On slide 6, we see how the margin increased in this quarter. We finished Second Quarter 2013 with R$11.3 billion. The loan volume improved revenues in R$280 million. The impact of the Selic rate is almost R$200 million in terms of financial margin. More calendar days, two days more, in this quarter. And also, we were able to appropriate more revenues. That is the positive lines of this financial margin.

And now, the negative. We continue to have some impact in the product mix, of R$108 million, reducing the margin; R$220 million related to client mix, as we are changing the mix of the portfolio and product; and other small numbers, totalizing R$85 million. So that will explain how was the components of these R$11.5 billion in terms of net financial margin with declines in this quarter.

In the bottom of this slide, we can see how the loan portfolio mix changed that explains, as I mentioned, part of this impact in the financial margin in decline. We continue to increase large companies. We continue to increase the payroll business and mortgages as part of the strategy of reducing the risk of the credit portfolio. And of course, this has some impacts in terms of revenues, because we are operating with lower-risk clients and products.

On slide 7, financial margin of credit and loan loss provision expenses. We see the split. The total was R$9.8 billion. R$3.2 billion was related to loan loss provision expenses, net of the recoveries that we achieved in the quarter.

On slide 8, we see the financial margin with the market. As I said, these numbers are reducing in the last quarters. Much more difficult in terms of playing the market in terms of results. The average of these periods since the Fourth Quarter of 2011, the average of this line was almost R$500 million. As I said, it was almost R$800 million some quarters ago. And this quarter, better than Second Quarter. We achieved R$340 million. But below the recent average and the mid-term average for this line. So let's see how we will be able to play in the market, both in terms of proprietary trading and the structural positions of the bank in terms of hedging, funding. And liability.

On slide number 9, we see commissions and fees and results from our insurance business. As I said, we are very happy with this line. The numbers are much better. Clients are using more services of the bank. We are able to sell better and more (inaudible) products for clients. And also the insurance business that continues to represent an important part of the (picture).

As we can see on page 10, the insurance operations, remembering that we sold to Porto Seguro all the vehicles and residential insurance. What we have here is mainly the life insurance that we sell through our branches. But the result continues to be important and growing in terms of importance. And we believe that this (bank and insurance) business will be important part of our strategy.

Remembering also that we continue to be out of the health insurance, due to the level of interference that we're seeing in this business. Even last week, the government showed new regulations in this health insurance, obliging the companies to pay more medicine and treatments related to cancer. So this will impact probably more these products. So we continue to be out of this and concentrating what we consider to be the bank and insurance business.

But anyway, we have this business and a recurrent of R$618 million, here including the 30% of participation that we have in the Porto Seguro total business, total company, that we are shareholders in the last (four years).

Payroll loans, on slide 11, continue to be important and continue to grow. We achieved R$20.5 billion in portfolio for this product. We continue to grow, especially through the joint venture Itau BMG. We are growing through BMG into the public employees and retired people. And we continue to be very active through our customer-side branches with the private corporate employees. So we are growing faster and recovering market share that we should have in this product through the size of the bank in Brazil.

So payroll loans already represent 43% of the total personal loans of the bank. We came from 31% last year.

Mortgage, we achieved R$32 billion. We continue to use our branches, the brokers. And our partnerships. And (inaudible) to originate the business. It's a business that we like. It's growing, with very good loan to value collateral, in average and in recent vintage. For example, (we can see) the market vintage of June, 71%. So we are very comfortable with the collateral.

And delinquencies rate, six months after the origination, very, very low, much lower than the market, as you can see here in this slide. Our number is 0.17%. And the market is 0.73%. So we are in a much better position in the mortgage business.

Credit quality, on slide 13. We finish with 3.9%, the lowest level that we always have here in the last years, with an improvement both in individuals, that achieved 6%. The peak was in June of 2009 -- 8.1%. So much lower than the peak in the last years. And the same for companies -- 2.3%. And the peak was 4.1% four years ago.

The coverage ratio for 90-days NPL continued to improve and achieved 170% in this quarter.

Credit quality, we can see also in this slide 14 that the trend continues to be very good in terms of ratios from when we consider the loan loss with the loan portfolio. I think the level of provisions continue to be very good and very comfortable. We continue to maintain complementary provision of R$5.1 billion in this quarter. Of course, this R$5.1 billion is losing importance as we go growing the portfolio and what is happening in the last quarters.

Credit quality, when we look in terms of delays 15 to 90 days, the numbers also are improving. We finish with 3%, came in from 3.4% last quarter. So we can expect less provisions in the coming quarters when we look at these as the first sign for delinquencies. We see that the numbers continues to improve and reduce. So we continue to expect lower level of NPLs over 90 days in the coming quarters.

On slide 16, using 100 as a basis in our March 2011 when we started to change the strategy of reducing the risk of the credit portfolio, we can see that in all lines with the exception of vehicles that we continued to improve the quality of the credit portfolio of the bank.

On slide 17, non-interest expenses continue to be a very focused objective of the bank to control as much as possible below the inflation level. And we will continue to target these in the coming periods. But anyway, this quarter the improve was 0.9%. And when we compare to last year considering Redecard full consolidation 2012 and 2013 they include the growth of expenses was also below inflation, at 4.4%.

Efficiency ratio and risk-adjusted efficiency ratio, on slide 18. We continue to improve the efficiency ratio adjusted. Adjusted here means that we include here the claims for insurance and also the NPL over 90 days. We are in the trend of reducing this ratio to the level that we expected this year in terms of guidance. We have some work to do of course in the traditional efficiency ratio, both in terms of revenues and (inaudible) expenses that we see some room (at least) to cut more expenses in the coming quarters.

On slide 19, the total assets of the bank finishing at R$1.082 trillion and the stockholders' equity, R$78.2 billion.

On slide 20, we see the composition of our loan portfolio. As I mentioned, we continue to focus the growth on payroll loans and mortgage and corporate.

We did see a reduction in the car financing profit. We expected this reduction to continue until probably middle of next year.

And we still see some reductions in the very small and small (inaudible) that we are continuing to reduce. And when we look at the middle-market typical company, this portfolio is growing slowly. But it's growing. What is making the reduction in this line of 4.1% in 12 months is more related to very small and small corporate.

We still have corporate private securities of R$24 billion and also endorsements and sureties. So if we consider all these of credit, the total credit portfolio, the total exposure for credit in our numbers achieved R$481 billion, what means a growth of 10% when we compare to last year. If we exclude the vehicle financing that we have been reducing a lot this portfolio, the growth is 14.3% and what is in line with the growth of the credit portfolio, the (financial system has numbers released by the central bank).

Funding and assets under management and capital of the bank total R$1.5 trillion, very comfortable position in terms of money from our clients and assets and funding.

We can see on page 22 that loan-to-funding ratio is 94%. So very comfortable. We don't see funding as an issue if we decide to grow more the credit portfolio in the coming quarters.

On slide 23, we see the changes in the quarter in our stockholders' equity. We start off R$75.8 billion. The profit of the period is R$4 billion. Interest and dividend that we paid for shareholders, R$800 million, reducing the stockholders' equity. Asset valuation of the long positions public securities impacted R$200 million in this quarter, very low compared to other quarters. And we bought back shares in the period of R$400 million, reducing also the portfolio. Other things, R$100 million. So that explains the growth of 3.3% of the stockholders' equity in the quarter, when we finish with R$78.3 billion of stockholders' equity.

It is important to mention that we've bought back this year 23.5 million shares, non-voting shares. And the average price for this acquisition was R$28.18.

Now, on page 24, the BIS ratio, 17.5%. We have a very comfortable position. We have here to face the growth of the bank and the present portfolio. We see here a good opportunity in terms of acquisition. And also to face the new adjustment that we will need to do in the coming years in terms of Basel III implementation. So we consider these levels very comfortable for the coming years.

On slide 25, recurrent (ROAE). If we take off the market numbers, Treasury, we see that the client business ROAE, let's put it this way, achieved 22.7%. It's growing since the Second Quarter of 2012. So I think it's important to separate the clients business from the market operations. So we see a very solid business in terms of client-oriented products and services, what is important in terms of sustainability of our returns for the coming years.

Markets capitalization achieved R$171 billion. It is important to notice that this year the level of transactions, the liquidity of Itau shares, is very well balanced between the BOVESPA and the New York Stock Exchange, our ADRs that are traded there, this year, different from other years when the liquidity was more in the NYSE. This year, it is very well balanced between BOVESPA and NYSE.

On page 27, we see the split of our numbers between the four traditional segments that we are used to show in these conference calls. Of the R$4 billion in terms of net income, R$1.8 billion came from the commercial banking; R$428 million came from the retail consumer credit; wholesale banking Itau BBA, R$1 billion; and market and the (excess) of capital, R$737 million.

On page 28, we show the IFRS numbers that we are releasing to (attend) the demands from (Itau users); that is, (we like to have) the numbers of the holding company in these accounting. And it is interesting to see that in IFRS our profit is R$4.3 billion. And our ROAE increased from 20.9% to 21.9%. So we have some different numbers when we analyze through the IFRS.

On slide 29, some information about our credit card numbers and merchant service. We announced some changes in the Hipercard business. We reduced the brand to Hiper. So this is a new brand. And we will start to really be more active in this brand. And we will continue to have the Hipercard brand for the customers of Walmart that remain with the Hipercard brand to use their card. But we are expanding the business of this new brand because in the credit card business in Brazil it's a brand that has almost 5% of market share and we want to increase this brand also to all the country. Today, it's very concentrated in the northeast area and the south of Brazil.

We changed the name of Redecard as part of the new strategy of the company and to start to be more active and more aggressive in terms of the business that we have 100% now. We also launched new products. And we are really starting from now on to be more active with (rede), as we mentioned. And it was our strategy when we announced the intention last year to buy the minority shareholders of Redecard. So now we are in the trend of being more active in the company with new products, new technology, new brand. So it is important. And use the synergies between rede and Itau Holding.

Itaucard is our brand in terms of credit card. Just to give you some numbers, we are totally focused on Itaucard 2.0. That is the card that charges clients that use the credit from the day of the use of the credit card, not from the day of the statement. And we have around 1.5 million cards. We consider this product a very good success and a very good acception from the client. Low claims. And we are only selling this card, not the traditional one that other banks and companies still sell. So we are very happy. And we will continue in this trend.

On slide 30, the outlook for 2013. We are not changing any of this guidance. We continue to expect the loan portfolio to grow between 8% and 11%. The growth now is almost 10% -- 9.9%.

Loan loss provisions, again it was R$19 billion to R$22 billion. We continue to expect. And now, very close to the R$19 billion, maybe a little bit below that (figure) Fourth Quarter.

The commission and fees that we expect in 15% to 18% is growing above these numbers. Probably the level that we already have is the level that we will finish the year. So this will be above our expectations. (This is more useful clients and also from Redecard and other people.)

Non-interest expenses is a growth of 4% to 6%. When we adjust the Redecard numbers last year and this year, the growth is 4.4%. So in line with our expectation.

And also, the risk-adjusted efficiency ratio, we were expecting an improvement of 200 to 400 basis points. We are 340. So we are in line also with this risk-adjusted efficiency ratio.

And to finish, on slide 31, we have a public presentation of the bank here in Sao Paulo for those who will be here on November 12 at 2.00 pm for the (inaudible). We are having this public presentation with the presence of our chairman, Pedro Moreira Salles. And our CEO, Roberto Setubal.

So we finish now our presentation. And we are here open to questions that you probably 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>}

Good morning, Alfredo. A couple of questions. Number one, on the insurance business. As you explain in one of the slides, this business which is posting ROEs of 35%, 36% contributes about 15% of the bottom line of the entire Group. That's about half of the contribution in your closest peer. So do you have a target of where do you see that evolving and what type of contribution to the Group the insurance business should have over the next few years?

And second. And somewhat related to this, the question is on your ROE. As you correctly explain, your ROE has been 20% for the first nine months of the year, 21% in this quarter alone excluding non-recurring items. Where do you see the ROE being sustained? Because if I consider some of the things that you said -- that your contribution from the market related business is still below par and will probably trend towards the R$500 million contribution that is the average historical; that insurance probably is a high ROE business and will continue to lower its participation; that the lending business in terms of volume growth is still below par should probably trend up; and finally, that you have excess capital at the bank level and that is a drag on the ROE and that should probably improve as you improve the allocation of capital -- where do you imagine your ROE being sustainable once you consider all these factors if the floor now seems to be 20%, 21%?

A - Alfredo Egydio Setubal {BIO 1528623 <GO>}

Hello, Daniel. Well we see the trends. When we analyze the trend of the last quarters and what we see in the coming quarters and the strategies that we have are showing in terms of expenses and credit portfolio and so on, we are very confident that the level of around 20% will be sustainable in terms of ROE for the bank.

Of course, we have to follow close all the numbers and everything, the environment, the local economy, international and so on. But the trend seems for us very positive. And I think we are showing that our strategy both in terms of banking and insurance was correct. Porto Seguro also shows good results in this quarter. (Bank insurance) continued to grow in our numbers. The strategy of reducing the risk of the portfolio was correct.

So we are not seeing anything in the short term at least that will move the kind of returns that we are showing in the last quarters. And especially this quarter. We think that it is quite sustainable, this level that we show this quarter.

A - Rogerio Calderon

Regarding the first portion of your question, Daniel -- Rogerio speaking -- we see insurance business outgrowing other business in the bank, what should account for this proportion to increase. However, when you consider that it's perhaps at a first glance only 15%, you also should consider that the other portion in the bank is actually very strong. We operate much more lines than most of our competitors. So when you look at the full pie, our pie is much bigger and probably better if you look at the performance.

But we do believe that this proportion is going to increase as time goes by. And when you consider the insurance business itself, it's actually very similar in size when you compare the industries that we operate. Remember that we don't like and we don't operate one of the most important industries in insurance, when you consider only revenues. And I am referring to health insurance of course.

But the size of the insurance business is going to outgrow the other portion and probably this percentage that you mentioned is going to increase. But not to reach the same 30% level, or whatever, because the other businesses are actually also growing.

Q - Daniel Abut {BIO 1505546 <GO>}

Rogerio, I appreciate the answer. I was not suggesting that the goal should be to try (and deliver) 30%, just to have an idea if you have a number or a target. If you look at Banco do Brasil, for example, as part of the (BB Seguri flotation), they are currently about 15% contribution, like you. And they have clearly targeted to grow that towards the 20%, 25% levels. Do you have a target and a timing for that target?

A - Rogerio Calderon

No. We don't have any targets on this.

Q - Daniel Abut {BIO 1505546 <GO>}

Okay. And just a follow-up on the first, Alfredo. I hear what you said. It seems to me that the 20% should be a floor, given all the trends that you indicated. If you are already at 20%, 21% and if most things can only get better, more likely that 20%, 21% should be more a floor and have room to be above that. So when you say it's sustainable at 20%, it seems that you are putting the bar too low.

A - Alfredo Egydio Setubal {BIO 1528623 <GO>}

I think it is good to say today that is a floor. I think it's sustainable around these numbers. We are confident about that. But I think we have to follow the environment, Daniel. It's difficult to be very assertive that this level will be a floor. We expect it, yes. But --.

Q - Daniel Abut {BIO 1505546 <GO>}

On the environment that could potentially be a drag, what are the things that still worry you? Spreads, for example? Or, what other things are still you want to monitor before you commit to a higher number?

A - Alfredo Egydio Setubal {BIO 1528623 <GO>}

Daniel, could you repeat these last words?

Q - Daniel Abut {BIO 1505546 <GO>}

I understand that Alfredo said that there's still too many moving pieces that need to be watched before you are willing to call a higher number. So what are the things that still worry you in that environment? Is it spreads? What are the things that are still too early to say?

A - Rogerio Calderon

I think the international environment is an issue. Probably at a certain point the Fed in the US will start to increase interest rates. So this we saw some months ago the impact that this can have in the economy of an emerging market like Brazil, for example.

In terms of spreads, no. I think that it seems at least that the worst in terms of reduction of spreads are gone. We are not seeing today the banks fighting for gaining market share through prices, through reduction of spreads. So we can even see in some lines in the mix some improvement in terms of the spreads in the coming quarters.

But we have to follow closely the economy and employment in Brazil, inflation. We have a lot of year left in (inaudible). So I think there are some things that can impact the environment, even though we consider all these not very high probability. But we have to consider all these in the scenario that we are working.

Q - Daniel Abut {BIO 1505546 <GO>}

Thank you, Alfredo.

Operator

Marcelo Telles, Credit Suisse.

Q - Marcelo Telles {BIO 3560829 <GO>}

Hello, everyone. Thanks for the opportunity. I have two questions. The first one, of course we are seeing that there seems to be a change in the way, in the aggressiveness of public banks, I would say, in several segments of their credit portfolio. But my question to you is, since I think that your delinquency numbers were very good and were very bullish for the improvement down the road, do you see any risk particularly in the SME segment that a pull-back from public banks could actually trigger some deterioration in your portfolio. And of course in the other portfolio, the other private sector banks? I think this has been kind of a recurring theme that investors have been asking about. Do you think there is any significant overlap between your SME portfolio and, let's say, the SME portfolio of Banco do Brasil or some of the other public banks?

And my second question is regarding NII, net interest income, growth next year. I was wondering if you could share with us what you think would be kind of a worst-case scenario for NII growth in 2014? I understand there are many variables that would definitely have an influence on that. And of course, part of that would be what your expectations are for your Treasury results, because we saw still a relatively low number versus the number you used to say, about R$800 million. So I don't know in what time frame you would expect that number to convert, at least to, let's say, around R$500 million to R$600 million, if you could convert to that number?

Those would be my questions. Thank you.

A - Rogerio Calderon

Marcelo, Rogerio speaking. Regarding your first question, when we look at our portfolio, as a results of this much more selective approach that we have been applying, what we've seen in our portfolio for companies, SMEs, is now much stronger and as a consequence much more resilient than what we had in the past.

So it's now based on operations fully collateralized or, importantly, partially collateralized. So we really don't think that we would be affected by any event what would change in the system as a whole. We don't know -- of course we are not sure about the quality of the portfolio of other banks. But we don't think that it should be a matter of a systematic risk or anything like this. And definitely it's not going to affect our credit portfolio.

Your second question is of course a bit more complex. When we look at net interest income, there are several different parts accounting for this evolution. Talking specifically on each one of them, we see volumes slightly growing. So what should stimulate NII growth.

We think (Selic) to be a little bit higher than today. And eventually (inaudible). As a consequence, higher in average next year than this year. So again contributing for a higher line.

And we see a still presence net interest margin compression because of the change in our mix of portfolios and asset quality.

So all together, we see conditions of a slight increase in net interest income line when talking about clients.

When talking about this same line regarding what we say margin with the markets, that's much more difficult to forecast anything. I think it's important to highlight that we don't see (various) conditions of being back to our historical level. So we believe we can perform better than what we are posting this quarter and last quarter as well. But not back to our usual level of R$800 million. This is far from what we have now, because of the stricter positions that we have built up in the past on a lower interest rate level.

So looking forward, even performing better we should not expect for a higher than, let's say, R$500 million, something like this, in the coming quarters. This is of course a big guess. But qualitatively saying it's not difficult to make two different statements here. Yes. We can deliver better than today. And it's very difficult to believe that we will be back to our historical level.

Q - Marcelo Telles {BIO 3560829 <GO>}

Thank you. So much, Rogerio.

Operator

Mario Pierry, Deutsche Bank.

Q - Mario Pierry {BIO 1505554 <GO>}

Hi. Good morning. Let me ask you two questions as well. The first one is related to your provisions. You had recently guided for provision charges of R$19 billion to R$22 billion for this year. The number for the first nine months is running at R$14 billion. So clearly you're running below your guidance. I'm just wondering if you think --? You chose not to change any of your guidance. But I was wondering if you see room for provisions to come at the lower end or even below your guidance for R$19 billion to R$22 billion?

A - Rogerio Calderon

Yes. It's possible that it comes below R$19 billion. If we just repeat the Third Quarter in the Fourth Quarter, it's going to be lower than R$19 billion. And we believe that we can do even better than this. So at the end of the day, it's possible, if not likely, that is going to be below R$19 billion.

The reason we are not changing anything in terms of guidance is, first of all, because it's not meaningful and, second, because we don't think that changing guidance, as the year-end is so close, we don't think that makes sense.

Q - Mario Pierry {BIO 1505554 <GO>}

And what about 2014? Should we expect provisions to be lower than 2013?

A - Rogerio Calderon

Could you repeat, Mario?

Q - Mario Pierry {BIO 1505554 <GO>}

Just your outlook for provision charges next year, 2014?

A - Rogerio Calderon

So we still have our asset quality improving. So chances are that it comes in a lower level than today. On the other hand, we have acceleration growth. So looking at the same figure with a slightly potential downwards is possible. Under the current risk environment on our portfolio, we don't see provisions growing in nominal amounts.

Q - Mario Pierry {BIO 1505554 <GO>}

Okay. So my second question then is with regards to loan growth. As you're saying, it seems like asset quality is completely under control. Also, Alfredo's remarks earlier that we're not seeing banks fighting for market share. It seems like you have a rational pricing environment. So what is your appetite for taking on more credit risk, especially as you're able to better price the risk? It seems like with the public sector banks being less present that you could probably see better spreads on your products. So I was just wondering what kind of loan growth can we see next year, given that asset quality is under control, when state-owned banks seem to be less aggressive?

A - Rogerio Calderon

We should be closer to the system growth, because the portion that is preventing us of following the markets, that is the auto loans, (inaudible) one or two quarters more. Then, only we're starting to grow (strong) from the second half of next year.

So as this is going to be better than this year, marginally saying, which we should be closer to the market's growth next year. What means that is implied some marginal acceleration, some slight acceleration. And this acceleration I think is very important to highlight that we are not accelerating because we are changing the risk appetite. We didn't change -- we are changing nothing regarding our risk appetite, because that with the improvement that we see clearly now in our portfolio is not so clear when we look at the market. So we don't see conditions of being less selective than what we are doing right now.

Q - Mario Pierry {BIO 1505554 <GO>}

Okay. Thank you very much.

Operator

Carlos Macedo, Goldman Sachs.

Q - Carlos Macedo {BIO 15158925 <GO>}

Good morning, gentlemen. Congratulations on the strong set of results. A couple of questions, somewhat follow-ups to the ones that have already been asked, both having to do with loan mix. We've seen the loan mix change significantly, with payroll loans increasing materially as a part of your overall loan mix and the addition of other less-risky loans. When you look at the progression of the 90-day NPLs, this is the lowest ratio since the merger. But also the portfolio you have is completely different than what you had in the merger. What is your expectation for --? And how low can this NPL ratio get, given the mix of the portfolio? In other words, if you adjust that NPL ratio to where it was during the merger and you put in the current mix of the portfolio, is it reasonable that we go to 3%? Or, is 3% completely out of the question, assuming that the underlying economic conditions don't change that materially going into next year?

Then, I have another question.

A - Rogerio Calderon

Okay, Carlos. Well clearly it's possible that it goes below the current level. How fast is a very difficult question to answer. (Figures) are getting better every single new vintage. We have better quality in collaterals, et cetera. So it's possible that we deliver 50, 60 basis points lower than today. More than this, we should be closer to this moment to reassess the question.

Q - Carlos Macedo {BIO 15158925 <GO>}

But just for instance, in your individuals' portfolio, in 2010 when you had a 5.7% NPL ratio, you probably had something like 40% of that portfolio in auto loans. And now, you have 40% in payroll loans plus mortgages. Going from 6% to below 5.8%, which is what you had then, is a reasonable expectation. Would you agree with that statement?

A - Rogerio Calderon

Even if we use equal portfolios in terms of products, we have today a better mix of clients, quality of clients, than what we had by that time. So we have today a better level of delinquency than any other moments in our history.

Q - Carlos Macedo {BIO 15158925 <GO>}

Okay. So you're saying that still part of the reason why the NPLs haven't come down even further is still cyclical?

A - Rogerio Calderon

Cyclical? Well the cyclicality is (now) in our favor, since we are having better vintages every new month.

Q - Carlos Macedo {BIO 15158925 <GO>}

Okay. Thank you, Calderon. The second question is the flip side of that is margins. And if it weren't for the additional working days in the quarter, your NII would have been essentially flat sequentially, despite some loan growth. Next quarter, we won't have additional working days. I think in fact we go back. And so, given what we saw there is the possibility that unless loan growth is very significant, the NII does remain flat, or even comes back, because of the change in mix. How strong is this change in mix? And how should we look at it affecting your NII going forward? It's a continuation of Marcelo's question from before. But is that something that will continue to have this negative impact? And will the provision expenses from the lower NPLs be able to offset most of the damage there?

A - Rogerio Calderon

You are right on your analysis. But considering everything, we see some room for increasing NII in the Fourth Quarter and beyond. It's not going to be an exciting growth. But it's going to be a positive evolution.

Q - Carlos Macedo {BIO 15158925 <GO>}

Okay. Thank you, Rogerio.

Operator

Saul Martinez, J.P. Morgan.

Q - Saul Martinez {BIO 5811266 <GO>}

Hi, everybody. I have two questions, as well. The first question is really a follow-up to a number of questions that deal with your financial margin and provisioning levels. In turning to slide, this is the fifth slide, you give your net interest margin evolution over time, both before provisions and after provisions. And what it shows obviously, as Alfredo highlighted, was that your risk-adjusted NII and NIMs have been expanding. It seems like you continue to think that that will continue. Can you give us some more color though on how you see this evolving in the next few quarters? How much more room is there for your credit risk-adjusted net interest margin to expand, say, over the next four to six quarters, because you're still relatively far below where you were in 2011 it seems?

Second question is on your capital strategy. You seem to me to have a very comfortable capital position even factoring in Basel III implementation, especially when you consider your ROEs, your current payout ratio. And the fact that your growth is coming from products that have very low risk weightings. Can you just comment on how you are looking at capital deployment between dividends, non-organic growth, because it seems like you're generating more capital than you need to sustain your organic growth?

A - Rogerio Calderon

Well regarding the evolution of our spreads on net interest margin, we are still finishing our business plans for next year. And we should get back to you guys. We know that you want to anticipate everything that is going to happen next year. But we think that we will be in a better position to talk on this in the next conference call.

But we do believe that there is some room for a still increase our net interest margin, adjusted by risk. We believe that the compression we see in the net interest margin pre-provision is going to be lower in the coming quarters because of the change in the portfolio mix to be less impacted than today. Then, although the improvements in the loan loss provision is going to be as well lower than today, this tradeoff should be still positive.

So this is what I can say qualitatively. Then, maybe we can go further in figures in the next quarter.

Regarding your question, Saul, in relation to our capital deployment, I think it's pretty clear our intention of being back to a normal level of growth when this restructuring of the auto loans portfolio is finished. Probably we will be back to that around 15% growth in our credit portfolio.

If we consider that the 20% is a sustainable level, by keeping the current dividend payout and growing 15%, we should be more or less with capital stabilization. However, I know that your question is a little bit different. So in case we have another (inaudible) -- so not possible to grow at the same level our credit portfolio -- we're still delivering higher ROEs. Then eventually we're getting to a position of excess of capital. At this point in time, we should have a couple of different measures to take. One, it's of course increasing dividend payout. But we also look at the strategical opportunities of moving internationally, as you know.

So at the point that we have this decision to take, then eventually we will be dependent on the circumstance at that specific point in time.

Q - Saul Martinez {BIO 5811266 <GO>}

Okay. Do you feel like you have excess capital today?

A - Rogerio Calderon

If you look at the full implementation of BIS, our total capital is 15%. But the core capital, the common equity Tier I, would be around 10%. The last figure we calculate precisely in this case is 9.7%. So eventually it (makes sense of) capital but not a big one.

Q - Saul Martinez {BIO 5811266 <GO>}

Okay. Great. Thanks a lot, Rogerio.

Operator

Mariel Santiago, HSBC.

Q - Mariel Santiago {BIO 16478669 <GO>}

Hi. All my questions have been answered. Thank you. And congratulations on the strong results.

A - Rogerio Calderon

Thank you, Mariel.

Operator

Jorge Kuri, Morgan Stanley.

Q - Jorge Kuri {BIO 3937764 <GO>}

Hi, everyone. Your asset quality indicators have done very well, especially in the consumer segment. Now, the labor market in Brazil has shown some signs of deceleration this year. Actually, unemployment rate went up 10 bps in September. Have you done any sensitivity about unemployment and your NPL ratio for consumer loans? Let's say if unemployment goes by 100 basis points in one year, by how much the consumer NPL ratio should increase? Thank you.

A - Rogerio Calderon

Hi, Jorge. This is Rogerio speaking. Yes. We do and we have in our base scenario for next year actually an unemployment rate to go up from the current level, up to 6.4%. So considering 6.4%, the (picture) in Brazil would still show job creation, not enough to fully absorb the demographic bonus. But creating jobs.

So if we go beyond 7.5%, around 7.5%, then this implies real job reduction. And then it could impact differently and strongerly this system as a whole. When we look at Itau, then it's a different picture, because our portfolio is actually much more collateralized now. And this, even with a stress negative scenario on unemployment, we don't see any problems beyond 8%, 9%. Lower than this, we don't see any important impacts in our credit portfolio because of the quality, the type of products that we are growing by (inaudible).

Q - Jorge Kuri {BIO 3937764 <GO>}

Okay. Thank you very much.

Operator

Boris Molina, Santander.

Q - Boris Molina {BIO 1904979 <GO>}

Good morning. I have a question regarding your investment plans on IT. We've noticed how the intangible assets related to software development and software acquisition has been accelerating in terms of growth. This obviously has an impact on your capital ratio. So what is the quarterly rate of additions to these intangibles that you expect to see? In the Third Quarter, it was around R$450 million, pretax. Is it going to go up to R$550 million, R$600 million on a quarterly basis? How could we expect this evolution in terms of your quarterly outlays in IT? And what is the amortization calendar for this type of intangibles, because as these intangibles grow they consume capital. But then the amortization hurts reported earnings. So I would like to get an idea of how this is going to evolve.

A - Rogerio Calderon

We are trying to conclude on how to address the points. I think we have some points to make here. The first and most important is the investments that we are doing, the IT. This amounts to more than R$10 billion -- R$10.4 billion. (It's now through a fast, speedy implementation.) This is going to impact our capitalization in both 2014 and 2015. So increase of course. Then, depreciation to increase especially as from 2015.

However, we have a very important efficiency to capture out of this investment here. So we don't think that this should imply any further pressure on our profitability. This should be matched.

In terms of capital, the portion on non-tangible I think --. Could you develop a little bit more on this, if this is the way we should address the points?

Q - Boris Molina {BIO 1904979 <GO>}

Yes, I was just trying to get an idea if quarterly additions to your software development acquisition intangible, which are right now they are almost double in the Third Quarter. So it's R$450 million. So is this the steady-state level of investment on a quarterly basis? Or, could it go up to R$600 million?

A - Rogerio Calderon

No. No. It's actually in a higher level today than our normal level, because parts of this package, the full package of R$10.4 billion, is related to the software.

Q - Boris Molina {BIO 1904979 <GO>}

Yes, Okay. So you would expect it to go a little bit higher from current levels? Or, this is the level that you think is going to be recurring?

A - Rogerio Calderon

I should look at the figures in the budget to be more precise on this. But (inaudible) short term. But then coming back to a lower level. We are now in a --. I don't know if we are at the top peak of the disbursements in this project. But we are in a higher level than usual.

Q - Boris Molina {BIO 1904979 <GO>}

Sure. Sure. I understand. Okay. Thank you.

Operator

This concludes today's question-and-answer session. Mr. Alfredo Setubal, at this time you may proceed with your closing statements.

A - Alfredo Egydio Setubal {BIO 1528623 <GO>}

Thank you, all, for the participation. We have a very good result. We expect to continue on this trend in the coming quarters.

So thank you for your time here with us. I expect to be together again in the Fourth Quarter conference call. Thank you.

Operator

That does conclude our Itau Unibanco Holding earnings conference for today. Thank you very much for your participation. And have a good day.