

# Q2 2019 Earnings Call

## Company Participants

- Carlos Wagner Firetti, Market Relations Departmental Director
- Nianda Miranda, Executive Director and Investor Relations Officer

## Other Participants

- Jason Mollin, Analyst
- Nicolas Riva, Analyst
- Tito Labarta, Analyst

## Presentation

### Operator

Good morning, ladies and gentlemen, and thank you for waiting. We would like to welcome everyone to Bradesco's Second Quarter 2019 Earnings Conference Call. This call is being broadcasted simultaneously through the Internet in the Investor Relations website, [banco.bradesco/ir-en](http://banco.bradesco/ir-en). In that address, you can also find the presentation available for download. We inform that all participants will only be able to listen to the conference call during the company's presentation. After the presentation, there will be a question-and-answer session, when further instructions will be given. (Operator Instructions)

Before proceeding, let me mention that forward-looking statements are based on the beliefs and assumptions of Banco Bradesco's management and on information currently available to the company. They involve risks, uncertainties and assumptions because they relate to future events and, therefore, depend on circumstances that may or may not occur in the future. Investors should understand that general economic conditions, industry conditions and other operating factors could also affect the future results of Banco Bradesco and could cause results to differ materially from those expressed in such forward-looking statements.

Now, I will turn the conference over to Mr. Carlos Firetti, Market Relations Director.

### Carlos Wagner Firetti {BIO 2489005 <GO>}

Good afternoon, everybody. Welcome to Bradesco's second Q '19 conference call. We have today, with us, for the call our CEO, Octavio de Lazari; our Executive Vice President and CFO, Andre Cano; Bradesco Seguros' CEO, Vinicius Albernaz; and our Executive Director and Investor Relations Officer, Nianda Miranda.

For starting the call, I turn now the floor to Nianda.

### Nianda Miranda

Hello, everyone. Thank you all for joining our second quarter 2019 earnings review conference call. We are very pleased to continue presenting solid consolidated results, despite the many challenges facing the economy. Our business model and the team have shown flexibility and excellence to thrive every single market that we play in. We are proud of our accomplishments and confident that we shall keep this path as we accelerate our investments in people, technology and services. We would like to thank all of our employees for this outstanding performance and

continuous focus on serving our clients and communities. In addition, we have a special thanks to our clients who have elected Bradesco as their bank of choice.

The economy was far weaker than expected what led us to lower than our 2019 GDP growth expectation, increased volatility jeopardized, the confidence level of consumption and investment results in tough environment for banking. Despite the challenging short-term scenario, we are optimistic about the future.

The pension reform does seem to be on track in the Congress and it has already been voted and approved with major support in the fourth round in the Lower House, which may allow companies to finally focus on their long-term goals without being blurred by the lack of fiscal uncertainty. Therefore, we believe that investments in growth are likely to resume over the following months.

Our solid performance this quarter came as a consequence of several changes that we have been implementing for quite a while, which allowed us to grow the credit portfolio, despite the economic scenario. With excellent credit quality, we're maintaining our costs under control and with a great performance of our insurance operations.

On Page 3, we bring some of our financial highlights. First of all, an all-time high net income of BRL6.5 billion, a growth higher than 25% year-on-year. The operational results grew 11.1% in the annual comparison. Our ROE reached 20.6% in the quarter, an expansion of 220 bps even with a strong expansion of our shareholders' equity in the quarter that grew 18.2% year-on-year to BRL133.6 billion. Our expanded credit portfolio grew 2.2% this quarter and 8.7% comparing to the same quarter last year and the individuals portfolio is a highlight through the strong growth of 14.8% year-on-year. As expected credit quality continues to improve with the over 90 days delinquency ratio falling 4 bps confirming our view of the Bradesco optimal position for lending. Finally, our Tier 1 capital ratio reached strong 15%, a growth of 50 bps this quarter and 360 bps in the annual comparison.

Moving to Page 4 we bring the other highlights of the quarter. The first one is a strong growth in individuals loan portfolio. It expanded 14.8% in the annual comparison. We are gaining market share in different lines such as personal loans, payroll loans, mortgage and out financing. We are achieving this growth with excellent credit quality, as shown. By delivering this growth is a reflect of the commitment and motivation of our teams as well as the evolution our process and models.

The second highlight is the acquisition by \$500 million of BAC Florida that we have announced in the beginning of the quarter. Our objective with this move is to the strength our positioning in the high income segments, pretty much wealth management offering to our customers checking accounts, cards, mortgage financing and other sources in US. With the conclusion of the deal is pending regulatory approval, but we are very confident that it shall come in a very near future.

The third highlight is in the MEI segment, which we were the first bank to launch the digital account. Credit origination through digital channels, mobile and internet has an expansion in the first half 2019 growing 53% in the individual segment, and 44% in the company segment. Our checking account customer base continues to expand.

In the annual comparison we grew 1.1 million customers and this last quarter 400,000 customers.

Finally, NEXT reached 1.1 million accounts in the quarter and we are confident that they shall exceed their target of 1.5 million customers by year-end. On page 5 and on the next page we bring some numbers of our operations in the digital arena. As mentioned in the previous slide, NEXT reached 1.1 million clients and 77% were not Bradesco's clients. We aim to reach more than 1.5 million by the year end and our CEO is very confident that we shall reach even 2 million clients by year-end.

In Bradesco Group, we closed this quarter with 16.4 million digital checking account clients an expansion of 1.9 million in 12 months. As you can see on the next page BIA, Bradesco Inteligencia Artificial is our artificial intelligence had more than 144 million interactions and 1.1 million customers through WhatsApp. Credit origination through digital channels in individuals segment totaled BRL11.8 billion in the first half a growth of 53% in the annual comparison.

In the companies segment it totaled BRL14 billion, a growth of 44%. These numbers show that our traditional banking clients are quickly adopting the digital channels, even for credit products. Turning to page 7 a great pride of ours Bradesco Foundation is one of the largest educational projects in the world. The Foundation, has a budget of approximately BRL650 million bringing benefits to more than 92,000 students with base education of high quality

On page 8, we show the value that we add to the Brazilian society. In terms of value added out of BRL33 billion 30% was paid to governments, and 29% to the compensation of our employees. Moving to the financial results of the second quarter we see here on page 10, the growth of the financial margin in the annual comparison was 7.1% and in the first half it was 5.6% close to the center of our guidance. Expanded loan loss provision reduced 3.2% in the quarter to BRL3.5 billion remaining on the upper part of our guidance

We are doing really well in insurance operations with expansion in the operational result of 16.9% in the first half. Our net income grew 23.7% in the first half and the operational result 13.3% show a solid performance of the organization as a whole. And we will go into more details on the following page.

Moving to Page 11 our ROAE grew again to 20.6%. This is the fourth quarter in a row with the expansion in our return, even with our shareholders' equity presenting a significant expansion of 18.2% year-on-year. We understand that ROAE may remain at these levels or even expand a little for some time as our CEO has pointed out. Our ROAA was 1.85%.

On page 12, we may see that our credit portfolio grew 2.2% this quarter and 8.7% when compared to the same quarter last year. The deceleration of the annual comparison is mainly due to a larger comparison base in the second quarter 2018. I would like to remind you that, in the second quarter 2018, there was a large expansion in the corporate portfolio mainly due to the valuation of our currency by 16% and also due to a large transaction of BRL5 billion that quarter with a great Brazilian company.

As highlighted earlier in this call the individuals portfolio presents a growth of 14.8% in the annual comparison with highlights to personal loans which is growing 29.2% payroll loans growing 22%, car financing growing 17.5% and mortgage growing 15.9% it's been an incredible year so far. The good performance of the individuals segment is a consequence of our market positioning, improvement in credit operations, evolution of credit models with intensive use of data and our highly motivated sales force.

In the companies segments, in addition to the effect of the comparison base that we have already mentioned, the operation suffers from low level of investments by companies and we understand this line to pick up with improvements in the economy.

In the SMEs segments the growth is also affected by reallocation. In the first quarter of '19 approximately BRL6.7 billion in loans from the SMEs segments to the corporate segment as part of Bradesco's new segmentation in companies, which increased the growth in the corporate portfolio and reduced in the SME portfolio.

Turning to page 13, credit origination per business day continued to have a good evolution. In the individuals segment, the growth was 17.3% in the quarter and 39% year-on-year. In the companies segment, the growth was also good 15.4% in the quarter and 21.9% in the annual comparison.

On page 14, we present our NII which grew 2.7% in the quarter and 7.1% in the annual comparison. The highlight is on the NII from market operations that presented a growth of 7.3% in the quarter and 25.9% in the annual comparison. The annual comparison is also impacted by the weak comparison base in 2000 -- in the second quarter of 2018. The NII from client operations grew 1.9% in the quarter and 4.2% in the annual comparison. It benefit from the credit portfolio expansion, changing product mix and quantity of days in the quarter offsetting the reduction in the average spread. We understand that this alignment continued to present positive performance as a consequence of the growth in the credit portfolio, despite the trend of spreads contraction. We are expect an acceleration in this line during the second half.

Turning to delinquency ratios on page 15 you can see that it continued to have a positive evolutions in all segments in line with what we have been pointing out in previous quarters. We still see the possibility of further improvement, but we are approaching the end of the normalization process of the credit cycle. We hope that it comes by the year end. The strong loan growth in the individuals segment reduced room for improvements. As you can see on page 16, NPL creation increased in this quarter, impacted mainly by individuals and corporate segments. In the individuals segments the impact is related to the growth of the portfolio.

Expanded loan loss provision improved to BRL3.5 billion this quarter representing 2.5% of the expanded credit portfolio the best level ever in our historical series. We still see room for reduction in the provision levels in the coming quarters. However, the expansion in the individuals credit portfolio reduces space for reductions, but should be compensated somehow by a positive impact of the financial margin.

Fees are presented on page 17. The growth in the quarter was 2.6% and the annual comparison 1.3%. The checking accounts line has a positive evolution growing 9.5% in the annual comparison due to the growth in the customer base and evolution of our segmentation. The pressure on fee income was related to cards revenue which are pressured by the competitive environment on the acquiring business and the reduction on debt cards interchange fees.

Asset management revenues which are pressured by the reduction of management fees, loan operations revenues pressured by a reduction in the volumes of sureties and guarantees. We understand that 2019 is a year of adjustments in this line and we may resume growth in fee income by 2020 with a stronger economy and with an adjusted revenue base. We are possibly positive with Brazil.

On Page 18 we bring the table with our operational expense, which are both the guidance presenting a growth of 6.2% in the first half. We had a maximum performance on administrative expenses, which grew 3.3% in the first half and 2.2% in the second quarter on an year basis. Below the inflation the performance would be even better haven't we made anticipation of payments to discounts of the pending negotiation of concept store is very positive for the bank as a whole.

In personal expenses we had a growth of 9.1% in the first half. The main pressure comes from the non-structural portion, mainly from higher profit sharing provisions related to extraordinary performance program as we continue to make provisions assuming maximum performance and from higher provisions for labor claims.

Expenses would be growing by 4.6% if we were to exclude the effects of this payment anticipation, higher profit sharing provisions related to this extraordinary performance program. So pretty much we believe that we shall keep them below inflation as time goes by.

Moving to page 19, insurance results we have again this quarter a very good result, with operational results growing 16.9% in the first half and 11.6% in the annual comparison.

Bradesco Seguros net income was BRL1.83 billion, a growth of 1% this quarter and 15.9% in the annual comparison. Insurance premiums grew 3.3% year-on-year, with highlight to health insurance segment, which presented growth in number of customers. Technical provisions totaled BRL265 billion expanding, 5.2% year-on-year. A few more topics on insurance are presented on page 20. In the annual comparison, net profit in the first half grew 16% and ROAE reached 23.6%.

In the second quarter, overall claims ratio had an increase and reached 72.5%, but it's still lower than the same figure in the second quarter of 2018. The best way to see it is on a semi-annual basis. The main impact on the ratio was caused by health segment, mainly due to the lower impact in the first quarter as a consequence of Carnival in the end of quarter and due to the higher quantity of business days in the second quarter.

For a better comparison, as I have pointed out, we should consider that first half total claims ratio is reduced from 74.4% in the first half 2018 to 70.5% in the first half 2019. We are confident that claims ratio will have a better performance in '19 than in 2018.

Turning to page 21, our capital ratios continue to evolve, as you can see, organically through retained profits. Core equity Tier 1 and Tier 1 both expanded 60 bps in the quarter.

And finally, on page 22, we bring our guidance, which had no changes. We understand that considering the full year we will be within the guidance range on credit portfolio growth, total NII, expanded credit provision expenses and fees. Our insurance operational results will be better than the top of guidance range, which is 9% growth. We shall increase it by far. In the line of operating expenses, we'll also be slightly above the range, with expenses growing a little bit more than 4% due to legal claims and also the compensation program that we have pointed out. In general terms, the current performance does not change the return targets implied in the guidance initially released in January.

Therefore, we now conclude the presentation; we are open for your questions. Thank you very much for your attention.

## Questions And Answers

### Operator

We'll now initiate the question-and-answer section. (Operator Instructions) Our first question is coming from Mr. Tito Labarta with Goldman Sachs. You may proceed.

### Q - Tito Labarta {BIO 20837559 <GO>}

Hi, good afternoon, thanks for the call. A couple of questions. Firstly, in terms of your asset quality, it continued to improve and cost of risk improving. You said it can improve a little bit further, although you did mention that NPL creation increased a bit in the quarter. So just trying to understand the dynamics there, a little bit, if you do see some further improvements, how much and when does it revert? So when we think about like the cost of risk, how much lower can you get it and what's a more normalized level as the year progresses?

And then my second question is in terms of fee income, the continuous fee pressure in the cards and asset management and also the collections. Just curious particularly I guess in the card income there, we did see a slight pickup in the quarter. Do you think most of the pressure has subsided from the acquiring business? I mean we saw Cielo volumes were up a bit yesterday. Do you think the pricing pressure has now subsided, to, it makes it more comfortable than the card fee income business there? Thank you.

### A - Nianda Miranda

Tito, thank you very much for your questions. Firstly, on the asset quality, we are pretty much pleased with the growth that we have had in individuals and SMEs. That pretty much represents the healthier possible portfolio that we could have. And when you compare our provisions level, you're going to see that pretty much we are decreasing the provisions either in relative or absolute terms. That means that the new vintages are by far better than the old ones. So we believe that the asset quality is improving and shall continue this way at least for until year-end.

Regarding to NPL creation, we see that the provisions for an amount that is higher than 90 days, it's going, it's improving dramatically and the volumes -- we do not see them growing in the individuals and SMEs when you compare to a relative analysis. And so, therefore, we understand that we shall get more and more alpha when you compare the return of these two portfolios when compared to the provisions. So we understand that this spread is pretty much there to stay.

Regarding to fees, we can make some sort of split here between -- among the three issues that you have pointed out, Cielo, asset management, and underwriting. First of all, on asset management, we had an adjustment in the management performance fee, but mainly on management fees, due to the decrease in the base rate of the country, right? So pretty much -- most of the portfolio was comprised of fixed income funds and, therefore, the management fees should be adjusted to the new reality of interest rate in the country.

Now, we are changing the mix more and more into equity funds, to Fundos Multimercados that are hybrid funds, including debt and equity, and we expect the management fees to stay there in fixed income and to have an improvement in management fees to those new asset classes. And as the environment in the country is getting a lower returns in interest rates, we understand that clients will get eager to get higher returns and that new base of investments.

For underwriting, we also benefit from a stable economy, as we shall see more and more IPOs, more and more equity and debt offerings.

And, again, on Cielo, they understand that we have the right strategy, we understand what they have said that they are there for dominance, they are willing to keep their market positioning, and therefore they made sacrifices and they are increasing their sales force. We are positive with their strategy to provide full support to the senior management.

**Q - Tito Labarta** {BIO 20837559 <GO>}

Okay. Thank you, it is helpful. Just I guess one follow-up on the asset management fees, with the expected further reduction in interest rates this year that's already priced in, you think, or could there be a little bit more pressure?

**A - Nianda Miranda**

We do not see more pressure, pretty much the pressure that we have had in the last couple of years was due to the decrease in the basic interest rates and most of the funds are mutual funds or fixed income funds, so (inaudible) they have to make adjustments. From this point on, we have pretty much reached a balance in the economy, the balance in the industry and we expect this to get stable in the mutual and fixed income funds and to have a higher and wider offering of equity and hybrid funds what shall increase the management fees and we hope the performance fees, as we do our job properly.

**Q - Tito Labarta** {BIO 20837559 <GO>}

Okay. Thank you.

**Operator**

(Operator Instructions) Our next question is coming from Mr. Jason Mollin with Scotiabank. You may proceed.

**Q - Jason Mollin** {BIO 1888181 <GO>}

My first question is a follow-up on fees. So I get that lower rates put pressure on asset management fees, but can you talk about competition and new entrance for asset management, and could that be another leg of pressure on fees? And we've seen your checking account fees actually grow for the first half of '19 versus first half of '18 by almost 8%. We've seen some new entrants cutting -- offering free accounts. Do you think that we could see pressure there as well, that's been actually one of the saviors to get to this 2% growth after the first half '19, almost 2% first half '19 versus first half of '18? And then maybe also talk about, it's a smaller number, but what's driving the growth in the consortium management fees? Thank you.

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

Thank you, Jason, for the questions. Well, let's start from -- the first one that is regarding to the asset management fees, right? We believe that we had some pressure from our competition in the last two years, pretty much because we were one of the leaders in this industry, so they presented new funds with adjusted management fees. We were in the process of making the adjustments. Right now, we have made all the adjustments when compared to the whole competition. We have this database and this intelligence, and we do it on a weekly basis, so we do not see that we are lacking in sort of competitiveness features right now. We believe that we are ready to grow and our management fees shall not decrease any longer. We expect that we shall have an inflow of funds to be managed by Bram, especially because of the interest rates scenario we have in the country; we have seen how much domestic investors are active and how much retail has been coming more and more important, especially when you see the brokerage houses movements bringing high net worth individuals to this game.

Regarding to checking accounts, Octavio has made this point earlier that the way we see it is that we shall present competitive packages to every single client of ours but always take into account their profile, their needs. So we believe that those fintechs or new competitors when they enter into the market, they are not providing all the full service, all the full package that we present. So in this sort of market we have been more and more competitive and a very good example of that is that for the first year in a row we have been able to grow in the traditional platform, the number of net accounts, so pretty much we are having more and more clients in our branches in our traditional bank as well as in our native digital bank.

If we are willing to -- if we are prepared to lose clients for any native digital bank we shall be losing to NEXT, but our experience is not showing that. Our experience is showing that we are growing in both. Both platforms are very strong and they are trying to serve better and better our clients. That's the reason why we are confident that we shall keep on growing. Regarding to pressure on growth, we believe that as economy gets back on track, we shall see clients get more and more banking services and we are very well-positioned as you could see in the first semester, not only to get market share from state-owned banks, but also from the other private-held banks. So we are positive with this scenario and as Brazil gets the level of growth that everybody is expecting we shall be there on a very leading position.

**Q - Jason Mollin** {BIO 1888181 <GO>}

That's helpful. And in terms of your digital strategy, and thank you for the update on the digital customers and initiatives, can you tell us what Bradesco expects to see where Bradesco expect to see the greatest impact of the digital transformation in the next year or two? Is it in costs or revenues. And can you help us quantify the impact? Thank you.

**A - Nianda Miranda**

Okay. First of all, we all used to think that technology would eliminate jobs, and experience has proven the other way around. Technology allows us to have different jobs, different revenue

streams and allow us to serve our clients even better and that's what our focus on. Our focus is on our clients. So digital channels have allowed us to grow our clients base even faster have allowed us to grow to serve our clients with better products and are creating leverage to the managers in our branches to be focused more and more on investments and on new business. That's where we think that the technology will drive us. The technology will not only drive us to reduce our fixed costs, but mainly to improve revenues and to get more and more competitive.

**Q - Jason Mollin** {BIO 1888181 <GO>}

That's helpful. Thank you.

**A - Nianda Miranda**

Thank you.

## Operator

(Operator Instructions) Our next question comes from Mr. Nicolas Riva with Bank of America. You may proceed.

**Q - Nicolas Riva** {BIO 20589225 <GO>}

Yeah. Thanks a lot for taking my question. One question on income taxes, if you can remind us where we are in terms of the approval in Congress of increasing income taxes for the banks. When do you think this will go into effect? And also what would be the impact on your capital from the one-time adjustment of your net deferred tax assets? Thanks.

**A - Nianda Miranda**

Thank you. Thank you, Nicolas for the question. We know that it's under discussions, but there's nothing on track or in process right now. The information we get so far is that the government is willing to increase activity and if they decide to increase income tax on dividends, they will reduce our tax brackets. So, their willingness is to keep the money inside the bank and to allow us to be more and more productive to the country to our clients. So by the end of the day it's going to be a good benefit for society as a whole and for investors, because you do not need to get dividends, you can get capital gains and you can sell your stock in the secondary market you're going to be much better off.

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

On top of what Leandro said, the discussion on the social contribution, as you know, is part of the pension reform. It was already approved in the first round in the Lower House, it should be voted probably early August in the Lower House. So the approval if they keep it should be maybe, September or October, the increase in the social contribution.

**Q - Nicolas Riva** {BIO 20589225 <GO>}

Okay, thanks. Carlos. And one thing in terms of the amount because there was some reference in Bloomberg I guess, from your Portuguese call about BRL6 billion and...

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

Oh, yes. Basically from the increase -- sorry -- from the increase in the social contribution, if it happens from 40 to 45 there is a revaluation of tax credit, and the value of this revaluation will be BRL6.4 billion, Our amount of tax credit increase BRL6.4 billion. There is no impact on BIS from this revaluation.

**Q - Nicolas Riva** {BIO 20589225 <GO>}

Thanks very much, Carlos.



**A - Nianda Miranda**

Thank you all. We are finishing the call.

**Operator**

Excuse me. And ladies and gentlemen, since there are no further questions, I would like to invite the speakers for the closing remarks.

**A - Nianda Miranda**

Well, thank you, all. We'd like to thank you once more for making the time to be with us and we are going to be open for questions and discussions afterwards, as our Investor Relations department is here to provide you on the information as they have always done. Thank you so much. Have a great day.

**Operator**

Thank you. That does conclude Banco Bradesco's conference call for today. Thank you very much for your participation. Have a good day.

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