

Q3 2012 Earnings Call

Company Participants

- Alfredo Egydio Setubal, EVP and IRO
- Rogerio Calderon, Corporate Controller and Head of IR
- Sergio Ribeiro da Costa Werlang, EVP of Risk Control and Finance

Other Participants

- Boris Molina, Analyst
- Carlos Macedo, Analyst
- Eduardo Nishio, Analyst
- Fabio Zagatti, Analyst
- Jorg Friedman, Analyst
- Marcelo Telles, Analyst
- Mario Pierry, Analyst
- Philip Finch, Analyst
- Saul Martinez, Analyst
- Victor Galliano, Analyst

Presentation

Operator

Ladies and gentlemen. thank you for standing by. We inform you that this conference call aims exclusively to discuss the earnings results of Itau Unibanco Holding regarding the Third Quarter of 2012. At this time, all lines are in a listen-only mode. Later, there will be a question-and-answer session and instructions to participate will be given at that time. (Operator Instructions) As a reminder, this conference is being recorded and broadcast live on www.itau-unibanco.com/ir. A slide presentation is also available on the site.

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 those anticipated in any forward-looking comments as a result of macroeconomic conditions, market risks and other factors.

With us today in this conference call in Sao Paulo are Alfredo Egydio Setubal, Executive Vice President and Investor Relations Officer; Sergio Ribeiro da Costa Werlang, Executive Vice President of Risk Control and Finance; Caio Ibrahim David, Chief Financial Officer; and Rogerio Calderon, Corporate Controller and Head of Investor Relations.

First, Mr. Alfredo Setubal will comment on the Third Quarter 2012 results. Afterwards, management will be available for a question-and-answer session. It is now my pleasure to turn the call over to Mr. Setubal.

Alfredo Egydio Setubal {BIO 1528623 <GO>}

Hello. Good morning, for those who are in the US. Good afternoon for those who are in Europe. We have a presentation here for the Third Quarter. It's a pleasure to be back. For those who are following through the slides, we are starting with slide number 2, the highlights for the results. The first one is the result itself.

We achieved a recurring net income of BRL3.4 billion in the quarter. This means unrealized ROE of 17.7% and also a decrease when we compare to the Second Quarter of 2012 of 4.8%. When we look for the nine months period of 2012 the recurring result reached BRL10.5 billion, with an annualized ROE of 19% and a decrease compared to last year of 3.2%.

The second highlight is the loan portfolio growth. Here we are showing the numbers with all the endorsements, sureties and private securities that we held in our treasury portfolio. And these total number achieved BRL437 billion, with a growth of 1.1% when we compare to June of this year. We are going to go much more in detail in the coming slides when we talk about the credit.

Third highlight is the financial margin with clients. The total was BRL12 billion in the Third Quarter with a 3% reduction when we compare to the Second Quarter of this year. The net interest margin with clients reached 10.6% in this quarter, with a decrease of 30 basis points when we compare to the Second Quarter -- essentially because of the reduction on the SELIC rate during this period and also because of the higher growth in the loan portfolio of lower risk and spread clients in this period. And the strategy that we are following of reducing the risk of the credit portfolio of the Bank in the coming quarters.

The spread reduced -- decreased 60 basis points, achieving to 12.8% and the risk adjusted credit spread, net spread, what we consider net spread, showed a 50 basis point decrease, achieving 7%.

Fourth highlight is banking fees and the result from the insurance business and pension plans and capitalization. The banking fees and in insurance the revenues achieved BRL5.7 billion in this quarter. The first nine months of this year this revenue increased 8.7% when we compare to the 17 -- achieving BRL17.2 billion in this 2012 nine months.

Fifth highlight is the non-performing loan ratio and loan losses. Expenses achieved -- net of the credits recovery in the quarter total of BRL4.8 billion with a decrease of 1.7% to the previous quarter. The 90-day NPL achieved 5.1%, with a decrease of 10 basis points. And what is good is the 15-90 day NPL ratio that reduced 30 basis points, that maybe is showing -- indicating a downward trend in this ratio for the coming quarters of course. For the next two quarters we expect loan losses, expenses to achieve something between BRL5.5 billion and BRL6 billion.

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Number 6 is the non-interest expense. We show a decrease of 3.1%, a nominal decrease in this quarter when we compare to the previous quarter. And when we compare 12 months, September over September, we show increase of 2.7%, what is much below the inflationary levels.

The seventh highlight is the efficiency ratio that achieved 45.5 -- increased when we compare to the last quarter mainly because we are not increasing the revenues in the pace that we were planning because of the strategy in reducing the credits -- the risk of the credit portfolio. When we analyze 12 months we see a better number of 45% and a decrease of 240 basis points in the ratio when we compare to last year.

Unrealized gains, the last highlight. We showed BRL6.9 billion with an increase of 19.9% in the quarter and also we have unrealized gains in our available for sale portfolio, secured portfolio of BRL2.4 billion.

If you go in more detail about all these highlights, that's the first slide that we showed, we go into page 4, we see our results -- so going back to the margin with clients, we saw the decrease of 3%, mainly because we are reducing our credit portfolio related to cars financing and we continue to be very conservative in the small companies. So this also reduced our margin with clients with lower volumes as we continued to -- in this pace of reducing the risk of our portfolio.

Of course we have also -- the competition that is more active and this means less spreads in some of our credit line and also because we are reducing the risk of the credit portfolio. Of course we are operating with lower spreads, with better quality clients. So all these together represented the reduction in this quarter of 3%.

When we see the line of financial margin with the market we see also reduction in this quarter, an important reduction of almost 25%. But just to remember, in the last conference call when we showed the Second Quarter, we said that the number of the Second Quarter was higher than the average of the quarters and this Third Quarter is much more in line what we can expect in terms of performance for our operations in the market through our treasury department. We see also that the results from insurance business, an increase of 2.1% in the quarter and a good number, almost 16% when we analyze 12 months.

In terms of loan losses, I think the expenses for the loan losses we stay in the same level of the Second Quarter, around BRL6 billion and also the same level of recovery of credit written off almost in the same level of the Second Quarter. So we continue to be very confident that the expenses for loan losses will continue to reduce. And as I said before, we expect at this coming quarter, the Fourth Quarter, to be something between BRL5.5 billion and BRL6 billion in terms of expense.

In terms of non-interest expenses, this was a good number. We continue to be very focused on controlling expenses and we were able to show a 3.1% reduction, nominal reduction in the quarter, even with a BRL145 million that was the impact that we had in the quarter because of the annual negotiation with the union in terms of salaries negotiations.

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So 3.1% reduction was a very good number. And when we analyze 12 months, we see also 2.7. That's very good because inflation level is around 5.2%. So we continue to be delivering good numbers in terms of expense.

And these all together -- so we show this BRL3.4 billion in terms of recurrence result, with a decrease of almost 5% in the quarter and 3.2% when we compare the whole year of 2012 when -- with nine months of 2012 and nine months of 2011.

On page 5, the highlights, we can see here in a more visual way. Our revenues with a growth of 12 months of 8.2%. Loan losses provisions we achieved almost BRL18 billion. So it continues to be a very high number that we are working hard to reduce. Non-interest expenses of almost BRL25 billion, which is increase of only 2.7% and the recurring net income with a decrease of 3.2% of BRL10.5 billion by the end of September.

On page 6, net interest margin. We can see here the reduction with the margin with clients of 70 basis points when we compare nine months with last year and 30 basis points when we compare to the Second Quarter of this year.

Banking fees and the result from the insurance business, an increase of 8.7% (in terms of) fees for these segments. So the recurring ROE of 17.7% is among the -- in the quarter among the lowest of the Bank, in the history of the Bank in the recent years. But we show 19% when we annualize the results for the nine months of this year.

On page seven we can see the financial margin. The gross and the net and the SELIC rate, the CDI is showing that we have been following the reduction of the gross spreads achieved, 12.8% in this quarter, when we compare to 13.4% for the Second Quarter of this year. As I said, the main reason here is the lower pace of our growth in terms of private portfolio. We are reducing substantially the car financing portfolio. So we are losing market share and also being much more selective in terms of car financing. And also because of the reduction of the SELIC rate and the new mix of credit with better clients. Of course, we are operating in a lower spread environment to achieve better quality client in this new mix of credit portfolio that we want to have in the coming quarter.

So these of course impacted the financial margin which declined and the trends both for the gross credit spread and the net credit spread. The net credit spread reduced from 7.5% to 7%. And also the same trend that we are seeing in the margin.

On page 8, we see that we finished with BRL960 billion in terms of total assets, with a growth of 8%. Stock holders equity of almost BRL79 billion, a growth of 4.4%. The loan portfolio with the endorsements and sureties. But not with the private securities, of 417% (sic-see slide eight "BRL417,603 million") here is a low growth because of these reduction and the strategy that we adopted in the credit portfolio. And funding, (inaudible) money, total including the assets under management of BRL965 billion.

So going in more detail in the credit portfolio, on page 9, we can see here the reduction on the car financing, vehicles. We were at BRL60 billion level by the end of the year and we finished this portfolio with BRL44 billion by the end of September. And we will

continue to reduce in the coming quarters this portfolio and probably this year we will finish something in between BRL50 and BRL52 billion. And probably we are going to see a reduction yet in the First Quarter of 2013.

So these of course will impact the growth of our total portfolio. Even though we are growing in other credit lines. But the impact of the car financing in terms of growth of the portfolio we will continue in -- at least in the last two coming quarters.

Mortgage continued to be a good business and we are showing good growth, 6% in the quarter, 32% in 12 months. In terms of companies, I think we continue to reduce and to be much more -- much less active in terms of very small and small companies. That's the reason our credit portfolio in this segment is not growing and decreased in this quarter, 2.4%. And the growth was only 1.1%.

We continue to grow our middle companies portfolio. But when we analyze very small and small we are much more conservative and reducing the portfolio. And this is compensated by a much bigger growth in terms of corporate, large companies that show a growth of 3.7% in this quarter and 12 -- and 16.4% in the 12 months.

And going to page 10, we can see the NPL ratio for over 90 days. We see a small reduction in this quarter from 5.2% to 5.1%. We see reduction in the Company's portfolio, reducing from 3.5% to 3.3%. And an increase in the portfolio in the ratio of the individual's portfolio. And this increase, one of the reason. So that is that we are still making provisions for the car financing portfolio and we are reducing the portfolio.

So the NPL ratio in this portfolio is increasing even though the quality of our new contracts are much better, as I will show in the next slide, than in the past. So this is one of the reasons.

When we analyze the NPL from 15 to 90 days, we continue to see the Third Quarter in a row with much better numbers. Even for companies and for individuals, the average of the Bank reduced from 4.8% to 4.2%. So this gives us confidence that we are in the correct way to reduce the risk of our credit portfolio and reduce the level of expenses for loan loss. The total allowance for loan losses is BRL27.7 billion by the end of September.

On page 11, we can see the 90 days NPL ratio by vintage when we compare four and six months after the origination. Let's focus on the four months that will show the NPL over 90 days, we can see that by the end of 2009 our numbers in the market without Itau Unibanco was almost the same, 0.47%, 0.48%.

We had a worse performance when we compare to the market, almost all these period and to the First Quarter of 2011 when we took some measures to reduce the risk of these portfolio. And we today are in a much better position because we anticipate these decisions when we compare to the market and today our portfolio is showing much better ratios than the portfolio when we compare to the market.

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So I think also we show the trend that we are in the correct trend to reduce the risk of the portfolio and to operate with clients that show this better quality for the portfolio.

On page 12 we can see that in 2010 we operated with three months in this portfolio and in the Third Quarter we are operating in 42 months in the portfolio. We are not anymore financing 100% of the vehicle. So the client has to put 20%, 30% to get the financing for the rest of the car cost and this also brings better quality and better clients to our portfolio.

In the Third Quarter the credit portfolio of vehicles we made BRL971 million in terms of loan losses provisions and we expected a reduction in this coming quarter to something around BRL800 million in these level of businesses.

On page 13, show here all the funding and assets under management and working capital of the Bank and so, that we achieved BRL1.2 trillion, what is a very comfortable position in terms of deposits and clients money.

On page 14, we continue to be very confident in terms of -- the deposits are very good in terms of funding level for the credit portfolio, especially in this moment that we are growing in a lower pace because of the strategy of reducing the risk of our portfolio.

On page 15 we can see more details of our service fees. We can see that the main reason when we -- not achieving the guidance in terms of the growth of tariffs and service fees for this year is located especially in the fees that we collect from the lower operations and guarantees that we provided to client that show a reduction of almost 20% when we compare 12 months and 6.5% in this quarter. So I think that's the main reason.

When we analyze other lines, asset management, current accounting -- the accounting -- checking account service is good in terms of volumes. They are not suffering any kind of pressure here. And also another point of attention when we compare is that we sold Orbitall processing service during this year and this impacts our service fees when you compare to last year. So I think in general we are not achieving the guidance, especially because we are reducing our credit portfolio but also provide less tariffs in these service related to the loan.

When we go page 16, we see non-interest expenses and efficiency ratio. Here is a very good number of nominal reduction of 3.1% in the quarter when we compare to the Second Quarter and only increase of 2.7% when we compare to last year. So we continue to be very focused in this strategy of reducing the cost of the Bank to compensate the reduction on spread due to the much higher level of competition in the market and also a reduction in our spread related to the strategy of reducing the risk of our credit portfolio that brings a different mix of products and also different clients, much better clients in terms of quality of credits that also operate with a lower spread.

Here it is important to say that we are controlling much more the cost of the Bank in the areas that don't put any risk in terms of quality of our services and also in terms of

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technology. We continue to invest in new branches. We continue to invest a lot in terms of technology, in terms of quality of our services. We are not cutting costs in these areas.

On page 17 we can see the distribution of our recurring result, our composition in a managerial way to see it. We can see in the Third Quarter that the commercial bank was responsible for 30% of the result; Itau BBA 16%; insurance 13%; consumer credit 9%; and activities with market and the excess of capital was 32%

In terms of BIS ratio on page 18, we are very comfortable with 17.5%. And of course in these moments, in these quarters that we are growing less with the credit portfolio we need less funding and of course less capital.

On page 19, our daily trading continues to be good, BRL742 million, in line with the other quarters and giving opportunities to all kind of investors to buy and sell our shares.

The last 3 slides, important message. The first one on page 20 is Redecard that we were successful in the tender offer that we made to buyback -- to buy the shares of Redecard. And CVM also delisted the company last week. So we are in the process of making all the necessary corporate transactions to maximize the value of the company; that we intend to do by --- during this Third Quarter till the end of the year.

On page 21, as I said, we announced a huge amount of investment in technology in the last two weeks -- last two weeks ago and BRL10.4 billion between 2012 and 2015. This means BRL2.7 billion in data processing systems from third parties; BRL0.8 billion in software acquisition and BRL4.6 billion internal develop of softwares.

And also we are -- we started this year the construction of a new data center for the Bank. The first phase will be completed by the end of next year. So in 2015 we will already start to use these new data center and this infrastructure we can grow in the coming years. The Bank needs more capacity to do all the transaction in terms of technology and profit. So it's a very important investment looking 20-30 years on the Bank systems.

On page 22, we announced yesterday when we released the Third Quarter result that we sold to Experian our shares in the Company, (inaudible). And these 16.34% that we had in the Company that was sold -- and the result before taxes that will appear in our non-recurrent result in the Fourth Quarter is BRL1.5 billion.

So this finish our presentation and we are open up here that we are -- in the conference call to answer the questions that you will probably have.

Questions And Answers

Operator

(Operator Instructions)

Mario Pierry, Deutsche Bank.

Q - Mario Pierry {BIO 1505554 <GO>}

Let me ask you two questions, Alfredo. The first one is related to your provision charges. As you made your case throughout the presentation that your spreads have been under pressure from a change in the loan mix. But provisions have not yet reflected this change in the loan mix. But when you gave your guidance for provision charges in the Fourth Quarter and First Quarter -- Fourth Quarter of this year and First Quarter next year, you are pretty much guiding for provision charges to remain relatively flat. So I was wondering why do you think provisions should be flat in Fourth Quarter -- in First Quarter next year, especially also as you showed that some NPL ratios are already improving?

Then my second question is related to your tax rate, your effective tax rate next year. As you show the acquisition of Redecard created goodwill of about BRL10 billion. So I was wondering if you expect any improvements in your effective tax rate next year?

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

Mario, this is Alfredo. (Relate) to your first question about the mix and the provision. We expect in the coming quarter to show a reduction in the nominal levels of our provisions and we show in the last two quarters that it was around 5.9%. We are seeing something between 5.5% and 6%. It is probably conservative, I agree. We expect a lower number when we compare to the two previous quarters.

In the next year probably we are going to increase our portfolio, our credit portfolio again in a more normal pace when we compare to the market. So we will also need more provisions in these -- related to this growth of the portfolio. And also, the mix. I think the mix will take us with a lower level of provision because we are in a lower -- we are changing the mix of the credit portfolio, especially cars, as I showed some slides, also reducing the very small and small portfolio of companies. That also will bring lower provisions. But also we are operating with lower strength.

So the reduction in the margin is also related to the mix and I think today represents most of the reduction of the margin is the mix. And of course part is the spread because the competition is much more active. Everybody wants to make more revenues. So the competition of course is much higher. So we expect a nominal reduction in the coming quarter in terms of loan losses, provisions. And also, in 2014, even growing the portfolio we expect a good reduction in the loan losses and provisions.

Q - Mario Pierry {BIO 1505554 <GO>}

Thank you, Alfredo. But just to get a better idea, when you say a good reduction in provisions what does that mean? Does it mean double-digit reduction or is it single-digits?

A - Rogerio Calderon

Mario, it is Rogerio speaking. We actually don't have the first level of precision to give you right now. But we expect the level of reduction to be actually bigger than the one we are presenting regarding the First Quarter. Because you should remember that in the First Quarter we have seasonality against us and then it should improve even better in the following quarters. If you also consider that some level of recoveries should increase, it's a good sign of a sizeable improvement. We don't have the figure to give you. But we are pretty positive on this.

Q - Mario Pierry {BIO 1505554 <GO>}

Okay.

A - Rogerio Calderon

Let me address the second question. You mentioned goodwill. We are finishing our analysis. The goodwill matter is under analysis. We are -- we need to finish the separations in order to separate what is tangible from non-tangible et cetera. But it may cause a positive impact on our results next year -- yes, it may cause.

Q - Mario Pierry {BIO 1505554 <GO>}

Okay. And just to understand also, once you separate what is tangible and what is intangible, is there a guideline on how many years you have to amortize this goodwill?

A - Rogerio Calderon

We are still finishing this. But it's probably around 6-8 years or close to that. But not -- we have not finished yet.

Q - Mario Pierry {BIO 1505554 <GO>}

Sure. When do you expect, Rogerio, to have more information on this?

A - Rogerio Calderon

Probably next call we should have this information to give to all of you.

Q - Mario Pierry {BIO 1505554 <GO>}

Okay. Great. Thank you.

A - Rogerio Calderon

No. Thank you.

Operator

Carlos Macedo, Goldman Sachs.

Q - Carlos Macedo {BIO 15158925 <GO>}

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I actually have a couple of questions. The first one is related to your expenses. You had a very impressive performance in the expense line this quarter with reduction in admin expenses and flat personnel expenses. I realize that you still have severance expenses there inside that personnel expense. I was just wondering if -- when do we rebase. In other words, when do we reach a period at -- where expenses are growing again at inflation or maybe at slightly higher level? Do we still have more efficiencies to come from this expense number?

And the second question is related to your tax line. We did see a fairly low effective tax rate. Of course there might have been some changes in accounting in the quarter. I was just wondering what should we expect in terms of effective taxes? Are there more tax credits that you can take advantage of over the following periods or should we expect the tax line to increase?

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

Okay, Carlos, I will answer the first question and Rogerio will answer the second one. I think the -- we continue to be very focused on the reducing the expenses of the Bank. We expect the next year also to -- the growth of the expenses to be below the inflation levels. We are working hard to be the lowest as possible in terms of expenses.

We continued to get some synergies and changing process and putting new system in place. And all these together working very well in terms of reducing process and cost for the Bank.

As I said before, we are not reducing expenses, putting quality and important investments in risk. We have a very strong brand and a very good level of clients and we don't want to put our franchise in risk when we are saying that we are controlling the expenses. So we continue to be very focused on clients and quality of relationship. We are making all these investments in terms of technologies that we announced. So -- and we continue to see opportunities as we dig. We continued to see the opportunities in terms of process, in terms of getting more efficiency.

So next year we'll continue to be very focused on this level of growing below inflation. I think we have some synergies to capture yet and probably in 2014 we are going to see the same trend. Let's see the evolution of next year. But our expectation is that in the coming two years we will be very -- continue to be very tough in terms of controlling the expenses, not only personnel. But all the other expenses like trips -- like use of telephone. Everything is under analysis in this period and we will continue.

We continue to renegotiate with our providers and we continue to be very focused in this equation. We see a scenario of lower spreads with the economy not performing so good like years in the past. So we have to compensate all these with a much better and a much efficiency -- efficient bank to keep the level of returns that we expect. I think this quarter, in our view, the ROE was a point off out of the line. I think we expect to increase ROE next year to a more stable level that we showed in the last 12 months. That's the way we are working in terms of expenses and also in this strategy of reducing the risk of our credit portfolio.

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A - Rogerio Calderon

Addressing the second question, Carlos, our current normal level of effective tax rate is 27%, 28%. Of course we have some volatility in this figure to recognize eventual increase in tax credit here or there or because of the different composition between the different tax rates we have in different entities. Remember that we have some entities that are on 34%, not on 40%. So when you blend the mix there are some volatility on this. We don't expect movements on this effective tax rates up to the Third Quarter next year. We still have the social contribution credits to fulfill our effective tax rates up to the Third Quarter next year.

As from the Third Quarter next year our effective tax rate should go up to around 31%, 32%. Remember that we are giving all these informations ex any eventual benefit from the Redecard goodwill, as I addressed Mario in the previous question.

Q - Carlos Macedo {BIO 15158925 <GO>}

Okay, perfect. So you still have tax credits that will last more or less one year?

A - Rogerio Calderon

Three quarters next year, yes. As from the Third Quarter next year, we will have this increasing impacts ex Redecard benefits.

Q - Carlos Macedo {BIO 15158925 <GO>}

Okay, prefect. Thank you, Rogerio, Thank you, Alfredo.

Operator

Philip Finch, UBS.

Q - Philip Finch {BIO 3252809 <GO>}

Thank you for hosting the call and offering the opportunity to ask some questions. I have two questions, please. The first is regarding your loan growth expectations going forward. We have clearly seen the rate of growth slowdown in previous quarters. The question is when could we start to see this start to reaccelerate and bearing in mind that you have indicated earlier in the presentation that you are planning to continue to shrink your vehicle portfolio?

And the second question is related to with the ROE performance of your Bank, which came in the Third Quarter at a low level. What is a level that you think that the Bank should be able to achieve? Is this a one-off what we saw in the Third Quarter or are we likely to see structurally lower ROEs going forward? Thank you.

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

Philip, it is Alfredo. Regarding to the loan growth expectation. So we are -- if you take off the car financing and the reduction in small and very small companies, the pace of the

other lines are good, are around 14%, 15% when we take off these two lines. So the issue is these two credit lines. As I said, we will continue to reduce. And we expect it by the end of this year the car financing portfolio to finish something between BRL50 billion and BRL52 billion.

In the First Quarter of next year probably this portfolio will reduce BRL2 billion more or BRL3 billion more I think so. When we consider the car financing, we see probably two quarters of reduction of these portfolio. So we have around BRL7 billion of reduction of our total portfolio coming from these lines. And also, you probably see one quarter more of reduction on the credit portfolio related to small and very small companies.

So answering your question, probably that by the Second Quarter of 2013 our credit portfolio will start to grow in the pace of the market or depending on the market -- the economic conditions and the scenario that we foresee. At that moment we believe even higher than the market. But I see Second Quarter and ahead as the time that the portfolio will grow at least in the same level of the market.

In terms of ROE it's difficult to measure. We don't like to give numbers in this arena. But we expect to have ROEs, normalized ROEs in terms of our result due to all these efforts that we are doing in terms of reducing the risk of the portfolio that of course will give us a positive impact in terms of the level of provisions, loan losses provisions that we will need to make in the coming quarters. All these efforts in terms of reducing --- (reducing) the expenses of the Bank, non-interest expenses, of these compounded. We see, let's say, something a little bit higher of the average that we have in the first nine months of these quarters, what we target in terms of ROE for the coming years.

Q - Philip Finch {BIO 3252809 <GO>}

That's very helpful. Thank you very much.

Operator

Saul Martinez, JP Morgan.

Q - Saul Martinez {BIO 5811266 <GO>}

I know you are going to give guidance on --- official guidance on 2013 after the Fourth Quarter results. But can you just comment a little bit about what your initial views are for net interest margins and NII growth next year given all the trends that you are talking about the -- still a couple more quarters of decline in some of your higher margin lending segments followed by increases? Can you give us a sense for how you are seeing NII evolve next year?

Then, secondly, on --- kind of a related question I suppose, just on your overdraft rate. It seems like the public banks have really reduced rates aggressively, private banks have not. Do you see any pressure from reduction in your overdrafts? Obviously, it is a small portfolio but the yields are extremely high. So reductions do have some impact on your NII evolution. Just curious to see whether you have any thoughts on that?

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A - Rogerio Calderon

Saul, Rogerio. We expect the credit growth to be --- next year to be more accelerated than this year. So you should expect --- and we -- maybe I should start saying that we have not finished all the exercise for the budget for next year. But we have and most of the players in the markets and agents and analysts are pointing to around 15% credit growth for next year. If we consider credit growth at this level probably our net interest income before the debt should be growing low single-digits, positive but low single-digit.

And definitely considering the adjustments we are doing in our mix of the portfolio, we expect an additional growth leveraged by lower level of better provisions. So looking at the net interest income adjusted by better provision, then this growth should be much or bigger than what I am saying, high single-digits or even low double-digits. But when you are looking before the debt probably low single-digit, since we are adjusting the mix of the portfolio.

Q - Saul Martinez {BIO 5811266 <GO>}

Okay, fair enough. And on overdrafts?

A - Rogerio Calderon

Could you repeat? We didn't --

Q - Saul Martinez {BIO 5811266 <GO>}

Yes, I am just curious if you have any thoughts. Obviously, the --- it seems like overdraft rates or saque a descoberto rates on -- from public banks have been reduced quite a bit. Private banks have been slower to reduce that. Do you see any pressure on your margin coming from reductions in rates on saque a descoberto?

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

Saul, this is Alfredo. I think in terms of this overdraft tariffs, I think it is important to say that this is a very convenient product for the client, is a product the client should use one day, two days, five days. But it is not a credit that the client should remain a long period. So we have mechanism to -- when we see that the client is using in a wrong way this credit line we provide and offer the client a different product more adjusted to the needs that he has.

So I think the difference between the banks looking from this perspective of convenience for the client is not very important, because the client should use this for a very few days and not for a long period of time.

But I would like to use your question to make some comments on tariffs in general and service that we provide. I think the competition of course, is in the newspaper, is very aggressive and is growing. But you have to analyze in the case of Itau Unibanco we are a very segmented bank. Itau was before and Unibanco also was. And we increased the segmentation of channels in our strategy in the last years. So we have a very strong

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commercial area in the Bank to serve all these different channels and different kind of clients and profile of clients that we have.

And it is very important to say that, because our prices in terms of investment products, in terms of tariffs, in terms of credit, everything has been and always has been adjusted to each profile and each channel of the Bank. So the (inaudible) use all these distribution it has, all these service that we provide to the private bank and to large companies. We have different strategies and different managers and different products and services.

So when we see competition more aggressive and we analyze our prices, we think the prices that we have are very competitive. Because most of the banks that are reducing the tariffs and the service fees they do not operate in a multi-channel strategy like we do and other banks do.

So we make some adjustments in terms of prices of tariffs, in terms of prices of some investment products. But we don't need to make much reductions or change in the strategy because our prices are according to the profiles of the client and not the same price for all the clients. That is the way some banks operate.

So it is important to analyze that the impact of all these in our case because of the segmentation and products and prices. We have hundreds and thousands of clients of personality, for example -- that is one of the channels that I am mentioning -- that they don't pay tariffs, any tariff. They don't pay for any service, because the volume of the investments, the volume of transactions that they do with us we don't charge anything from that.

So it is important to understand that what is happening in the market is affecting of course. I am not minimizing the impact of the competition and so on. Of course this will bring less revenues from service, less revenues from tariffs, of course less spreads, not only because of competition in our case but because we are changing the mix of the credit portfolio. But the impact is lower, because we have this multi-channel strategy than in other banks.

Q - Saul Martinez {BIO 5811266 <GO>}

Okay. That is fair enough. I appreciate the thoughtful response.

Operator

Victor Galliano, HSBC.

Q - Victor Galliano {BIO 1517713 <GO>}

Just on what you were saying about provisions earlier. I mean looking at the guidance that you are giving for just the vehicles portfolio loan, I mean that comes down --- should come down by around close to BRL200 million quarter-on-quarter and yet the guidance seems very conservative. I mean is this a case of just being conservative given what has happened during the course of the year and giving yourselves some scope there to be

conservative on your estimates? Or is there -- is there actually some other area outside of vehicles that in the consumer or in the very small SME portfolio that is still being a little bit problematic in terms of credit quality? That is my first question.

And my second question really relates to the kind of de-risking and re-pricing of the loan portfolio. You put a very good chart in here on page 16 of the MD&A. How do you feel this will continue to progress? Judging by what Rogerio said about the growth of NII -- we are going to see quite a lot of margin and spread pressure still coming through into Q4 and Q1.

My question is, did you feel the kind of the full impact in the quarter of re-pricing and de-risking of portfolios in Q3 or was this just a partial effect and we are going to see much more of it in Q4 and Q1 of '13?

A - Rogerio Calderon

Starting from the end, Victor. No. We still see the coming quarters being adjusted because of the mix of the portfolio. What is going to happen, however, in the favor of the better results is the fact that delinquency should improve much strongly as from the Second Quarter the next year. Why not in the First Quarter? Because First Quarter normally is impacted by some level of seasonality that goes against the delinquency improvement.

And maybe I should link to the first part of your question. We still have some impacts on the auto loans portfolio to be reported in the Fourth Quarter, slightly in the First Quarter next year and then vehicles should contribute much strongly to the improvement in the bad debt provisions, as I mentioned before.

And what we should expect is the auto loans portfolio to be back to its normality since we are not originating the same credits without first or very low first down payments that caused this increasing delinquency.

I understand what you said, next quarter and First Quarter -- I think next quarter we still have some impacts from the auto loans and First Quarter; except for seasonality, the improvement should be even bigger. Seasonality will prevent this benefit to be noticed in the first quarter but Second Quarter on we should see much stronger benefits out of this.

Q - Victor Galliano {BIO 1517713 <GO>}

Okay. Thank you.

Operator

Marcelo Telles, Credit Suisse.

Q - Marcelo Telles {BIO 3560829 <GO>}

I have two questions. One is a follow-up on asset quality. I know there is the seasonality, (inaudible) seasonality in the First Quarter of the year and so on. But what would you expect in terms of reduction in the NPL ratio -- if you want to say 60 day or 90 day NPL ratio by the end of 2013; I don't know if you are able to share that with us.

And the other question is on the improvement that you posted on your commercial delinquency. I think that there was a 20 basis points decline quarter-on-quarter. What was the driver there? Was it like the improvement in the SME segment or there was some improvement in the larger corporations?

A - Rogerio Calderon

Okay. Marcello, what is driving the improvement in delinquency is a long list actually. We have all the vintage without any exception, the recent origination in better quality, asset quality than what we had before. So with the maturity of the portfolios you should expect for improvement in all without any exception, all the lines of our credit portfolio. And signs are actually already appearing.

If you look -- not only the over 90 days. And I should highlight the point that even though we had some increase in the over 90 days for individuals, we should remember that we still have some statistical impacts from the reduction of the auto loans portfolios.

So what we have in the auto loans is NPL ratio increasing despite of better origination and better delinquency because of the reduction of the total portfolio. So this is actually not a deterioration in the delinquency. But a statistical impact. If you remove that even individuals would be improving in the Third Quarter.

So corporate is already improving. We have the early delinquency 50 to 90 days. Improving other lines, 30 basis points if you look at the data in September (credit). Remembering that we had strikes and strike impact, particularly impacting early delinquency. Coverage is increasing in other lines, new vintage improving in all the segments. NPL creation is reducing. Total overdue reducing in nominal terms. So any overdue more than 15 days is actually lower in September than what we posted in June. So all the signs are positive and we should see continuously these benefits.

Regarding the first part of your question on any guidance on NPL, you know we have been trying not to give any NPL ratio guidance. We tend to guide on the total bad debt expenses. However, at the beginning of the year, we announced our NPL ratio guidance saying that NPL ratio should increase in the beginning of the year in the First Quarter of the year and then it starts to decrease to be back to the more or less to the same level at the beginning of the year.

So we guided the market for stability in the NPL ratio when comparing beginning of the year with the end of the year with some increasing in first part of the year and then decreasing. We think it is going to happen exactly like what we said in the beginning of the year. It should be back to the same level of the beginning of the year and then further improvement next year since we are going to collect more benefits out of this change in our portfolio mix.

Q - Marcelo Telles {BIO 3560829 <GO>}

Thank you, Rogerio. One final question if I may, just regarding the -- I don't know if you could tell us what the status of the negotiation is regarding the potential changes in the treatment of tax credits for the purpose of Basel -- Basel III? Is there anything you should -- can we expect maybe, let's say, a softer regulation in that regard? Thank you.

A - Sergio Ribeiro da Costa Werlang {BIO 2384657 <GO>}

We are positive that there is going to be at least for the deferred tax assets generated by the provision for loan losses that there will be some changes. But -- we are following closely. But we are still positive of that. Specifically, on the loan losses part.

Q - Marcelo Telles {BIO 3560829 <GO>}

Thank you.

Operator

Boris Molina, Santander.

Q - Boris Molina {BIO 1904979 <GO>}

I had a question regarding your IT investment plan. It's a sizeable project and so I was wondering how could you expect us to see how this is going to eventually be impacting cost in terms of how you are going to account for this? Are you going to capitalize the software investments or are you going to extend it because it could have medium term implications in May 2014 in terms of efficiency and cost?

And the second part of the question is, there is certain amount of investment in new software development. So I would like to know what are the modules or if it's a complete rewrite of your IT software platform? What are the enhancements that you plan to make and what type of your efficiency gains could we expect, particularly because Itau still works with a relatively high ratio of employees per branch and how could we see this overall efficiency improving in the medium to long-term? It gives the impression that this is a transformational IT project that we should keep an eye on. So I would like to see if you have more color on this?

A - Rogerio Calderon

Boris, Rogerio speaking. We -- of course those investments are going to impact our total expenses mainly as a consequence of the increase in depreciations since the investments are going to be done since now up to 2015. But when we supplied you with a guidance of the total expenses growing below inflation in the years 2013 and '14, this is also encompassed in that calculation.

So despite of this growing or increasing depreciation over time, we still have gains in efficiency to offset and to be positive on this growing below inflation over the next two years. We have not the figures for the other years before that -- after that. But we expect --

theoretically saying we expect our improvements, our efficiency gains to be enough to compensate this.

In terms of the total investments, what we are doing -- IT platforms they scale up in different steps. We -- last time we had strong investments on this area was to prepare the Bank for 20-30 years. This is what we are doing now. So you should expect really this big investment to prepare the Bank for the next 30 years. What it means that the Bank is going to gain -- to make a lot of or to collect a lot of benefit out of these investments. We have some technical date on this that we could supply to you. But gains in electricity, for instance. And also in processing. It's almost 10 times the processing per second that we have today is going to be in the future. We need to tackle the future challenges for the Bank in a growing environment.

Q - Boris Molina {BIO 1904979 <GO>}

Thank you very much.

Operator

Fabio Zagatti, Barclays.

Q - Fabio Zagatti {BIO 3846027 <GO>}

Just to make sure we all got this correct. So would you expect net interest income, pre provision, to grow in the single-digits in 2013; actually, I guess, because you mentioned low single-digits assuming 15% credit growth? Then on a (inaudible) loan loss provision basis, did you mean NII growth could be in the low double-digits? And if this is indeed right, I mean even if you don't provide an ROE guidance for 2013 but based on very simple math of the other assumptions that we have for OpEx mainly, is it fair to say that the risks are that ROEs should remain below, let's say, on 18% level? So below the historical levels as you previously suggested in this call? Then I'll have a second question. Thanks.

A - Rogerio Calderon

So Fabio, your understanding is correct on what I have said. It is probably to grow NII for bad debt, probably to grow low single-digits and probably after that that to be around high single-digits or low double-digits.

Regarding ROE, it is always very important to remember what we constantly say to you guys is that what -- we manage the Bank based on creating spread over the cost of capital. So every time we talk on return on equity, it is very important to remember that these figures could move depending on the cost of equity, depending on the cost of capital.

So if we consider stability on the current levels, we think that the nominal level on ROE that we have reported in the Third Quarter is below our potential because of this abnormal level of delinquency.

So from this level we are posting today we expect improvement in the ROE. I think we will be able to give you more precision on this in the next quarter. But definitely we expect improvement from the current level to post in line with the average we have on the last 12 months.

Q - Fabio Zagatti {BIO 3846027 <GO>}

Okay thanks, Rogerio. Then I would like to ask one more thoughtful and related question. What do you think could be a trigger for improvement in market sentiment towards the banking sector in Brazil after all that we have been through? With all the risk of continued government intervention I believe we have reached a point where a news article like this warning is published today, reading that banks profitability fell to the lowest levels since 90s ends up paradoxically being a positive. Because it somehow shows that the government initiatives have had some impact so far. So I would really like to hear from you whether you guys believe that we are in the cycle of ROE compression risks being priced in? Thank you.

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

Fabio, this is Alfredo. Your question of course is very difficult to give a precise answer. We, looking around the world, look in other countries like Australia, like Chile, like Canada and so on, we see that in this environment they are much more stable and much more -- they are operating with a much lower spread and so on. The returns of the banks in these countries are much higher -- is around 20%, 18%.

So we are very confident that in Brazil the level of returns will be close to the historical levels of the last years. We are operating the Bank in these -- with this strategy and targeting these levels of ROEs. And we think that is possible. We are seeing that it is possible to operate and bring different kind of clients in different environment.

All this that is happening here in Brazil is interesting to show that the demand is elastically recording -- according to the price. In the past the banks, in general, the systems were operating in the feeling that the clients don't need money. They have their own savings and investments. They were not even considering using credit in their life.

And what we are seeing is a different scenario. We are seeing clients with investments using part of these investments and savings to pay part of the mortgage and financing the rest-- car is the same. So we think that all these really will bring more clients and will bring more volumes to the system. And we are seeing that probably all of these will bring NPL levels and provision for loan losses to a much lower level in the coming year.

So these all altogether in our view give us confidence that the returns will continue to be in a good level for the investors and for the soundness of the system in the transition period.

You asked in what part of the curve we are in this transition period. I really don't know exactly. But I think the worst pressure is past. It doesn't mean that we are not going to see more pressure. I think probably we will continue to see more pressure because all the

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banks need some more volumes, all the banks need more revenues to compensate the pressure in spreads and so on. So -- but looking ahead we are very calm; we are very confident that this is part of the transition period.

I think the economy of Brazil will continue to grow and this will bring new clients, new opportunities, a better environment in terms of growth for the economy that is fundamental for a sound financial system. So I don't know exactly in what part of the curve we are. But looking some years ahead I think we are very confident the financial system will continue to serve well in a lower spread environment but providing good returns of capital for the (inaudible).

And of course in all this scenario you continue to be in a good direction. Of course the cost of capital that Rogerio was talking in the previous answer will reduce also. And I think it's important that this system will continue to be able to provide a premium over the cost of capital. And we are very confident that we are -- we will continue to provide a premium over the cost of capital because -- and probably the cost of capital will continue to reduce in Brazil. Probably the interest rate all around Europe and US and Japan and many countries will continue to be lower for many, many years still.

So I think it's a new environment. We have to adjust our strategy. We have to adjust our target for this new environment of lower interest rate, lower cost of capital in the world and Brazil is a part of this, for the coming years. It's a transition period and we are confident looking ahead.

Q - Fabio Zagatti {BIO 3846027 <GO>}

Thanks, Alfredo. It seems very helpful.

Operator

Eduardo Nishio, Brasil Plural.

Q - Eduardo Nishio {BIO 15333200 <GO>}

I have two questions, first regarding Redecard. I would like to know what will be the strategy after delisting the company in terms of pricing, in particular MDRs? And also regarding this topic giving the latest news flow on MDRs and particularly relating to some regulatory pressure to reduce MDRs and maybe brand sharing, what do you see coming up in this firm -- and that's on Redecard -- on loan? And I would like to know in the auto segment what do you see? If you still see some leftovers in terms of provisions for 2013?

And on the SME segment why are you not growing at a faster pace now given that SME has a lower duration and all -- probably the worst in terms of provision you have already has gone for now and therefore you would be in a better position to go back and grab market share in that segment as well? Thank you.

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

This is Alfredo. I will start answering the second question. I think when you analyze the credit portfolio for SMEs, what we are doing in this direction of reducing the risk of our portfolio is to reduce the risk of the current portfolio for very small and small companies. If you analyze the pure middle company, middle market company, our portfolio is growing in a very good pace. But this is offset by the reduction of this small and very small portfolio, credit portfolio.

And why we are doing that? Because it's very difficult to increase the quality of the portfolio in this segment. I think we are increasing the collaterals. We are doing something. But there is a limit that what kind of collateral and guarantee these kind of companies can provide to us. So we are reducing very small and small companies to the limits where we think the collateral and the guarantee is good. This is different in the middle -- the traditional middle market companies that we are growing and continue to grow. So these I think we have -- still are one quarter yet to adjust these small and mid-sized -- small and very small portfolio.

A - Rogerio Calderon

Nishio, Rogerio addressing the first part regarding Redecard. I think what is important to highlight here is then when we brought Redecard to our (technical difficulty) we were targeting, as you all know, to have a better ability to scale up the business in Redecard by gathering different products. So with a new -- actually, I think in summary we should say that we have designed a new model to operate at Redecard in which we should be able to capture growing volume with gains in synergy both for the administrative side and particularly on different revenue stream lines since we will be to supply Redecard with a much broader list of products.

That's the reason for this strategically movement and this is what is going to happen over the coming periods. Particularly when you addressed the MDRs, there are lots of change in the dynamics of the business and it maybe -- we may see some additional pressure on MDR. But the whole strategy that we are addressing at Redecard is actually to offset this to compensate with a much broader volumes and products, looking at Redecard from a different perspective.

And always you should remember that when we look at the credit card business, we are looking at the market at a segment that is growing on average 20% year-on-year for 3 or four years on a roll. So it's really plenty of opportunities to come and we are trying to collect all the benefits of this growing environment.

Q - Eduardo Nishio {BIO 15333200 <GO>}

Okay. So no -- and not really a strong pressure are you seeing for 2013 and '14, right?

A - Rogerio Calderon

From the perspective of Redecard we will be able to overcome with any marginal pressure on MDRs with the strategy as a whole.

Q - Eduardo Nishio {BIO 15333200 <GO>}

And on the auto segment, any leftovers for -- in terms of provision for 2013 or it will be clean in 2013?

A - Rogerio Calderon

It's going to be clean and strong -- actually, we may have some residual in the beginning of the year but it's not really worthwhile.

Q - Eduardo Nishio {BIO 15333200 <GO>}

Okay. Thank you.

A - Rogerio Calderon

Thank you, Nishio. We still have a question I think.

Operator

Jorg Friedman, Bank of America.

Q - Jorg Friedman

Thank you very much for taking my question. Actually, it's a follow-up on the Redecard issue. I just like to hear your opinion about the recent turmoil on the sector, more regards with the potential regulatory scrutiny in the business? So any chances that -- to you to classify as more likely in the business model and to change going forward, to have a new regulatory body that will be in-charge of the sector and so on and so forth? Thank you.

A - Rogerio Calderon

Actually, we have been preparing our business in credit cards and Redecard and InterCard actually from the last two years to face the change in the business environment. And of course this is -- when we look at the future it's possible that we had some additional movements.

Well I think we should not deny this possibility. But it does not mean that it is likely to happen. It is possible. And what we have been doing is actually to do all that is possible for us to be able to be in good shape despite of any additional pressure.

Remember that even with pressure this is a very good market with a very attractive growing prospective, profitability. Now we have a new opportunity to enhance the business here inside Itau. It is really very positive for us.

Q - Jorg Friedman

So just to clarify, Rogerio --

A - Rogerio Calderon

And maybe the best example on this is the fact that even under this turmoil, as you said, we never changed the offering, the price offering that we have offered since the beginning of this transaction. Despite of this additional pressure, we still had the confidence that the future cash flows, et cetera of the business could be defended.

Q - Jorg Friedman

Yes, I think that the biggest concern that the market have at the moment is of potential political interference. So my question is more according to the recent discussions that we -- I am pretty sure that you guys have with government officials. You do not feel anything disruptive to be coming on?

A - Rogerio Calderon

We have no further comments on this, Jorg. It will be speculative to say if we believe the government is going to do one thing or another thing. It is possible.

We should be prepared to do -- to take the best from our business, not to be concerned with any other thing. The business model was designed to protect our ability to keep posting good results on this business. That is what I could add.

Q - Jorg Friedman

Okay -- no, perfect. And taking that into consideration would it be fair to assume that even though NII will be under pressure, as you commented already, fee income would still be in a good position next year potentially flirting with the double-digit?

A - Rogerio Calderon

Perfect. Actually, when we mentioned that our strategy is actually converting into reality when you look at the figures, with revenues -- spreads reducing but the mix changing, et cetera. And loan loss provision should be lower in the future, efficiency should be collected. We also should add that we have a very positive view on fee income to grow. And Redecard is a very important part and parcel of this strategy.

Q - Jorg Friedman

Okay. Thank you very much.

A - Rogerio Calderon

Thank you.

Operator

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

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

Thank you, everybody, for participating in this conference call. And just to add that we continue to be very confident in the strategy of reducing the risk of our credit portfolio, controlling expenses to provide good returns in the coming years for our shareholders.

Thank you. And we are here for any question that you have. And going to be together again in the beginning of next year with the results of the First Quarter. Thank you.

Operator

That does conclude our Itau Unibanco Holding earnings conference call for today. Thank you very much for your participation. You may now disconnect.

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