

## Y 2018 Earnings Call

### Company Participants

- Bernardo de Azevedo Silva Rothe, Chief Executive Officer
- Rafael Sperendio, Head of FP&A, Accounting, Treasury and Investor Relations

### Other Participants

- Eduardo Nishio, Analyst
- Mario Pierry, Analyst
- Thiago Batista, Analyst

### Presentation

#### Operator

Good morning, everyone, and thank you for waiting. Welcome to BB Seguridade's Fourth Quarter 2018 Earnings Conference Call. This event is being recorded and all participants will be in a listen-only mode during the company's presentation. After this, there will be a question-and-answer session. At that time, further instructions will be given. (Operator Instructions) The presentation is available in the Financial Information Presentation section of BB Seguridade's IR website at [www.bbseguridaderi.com.br/en](http://www.bbseguridaderi.com.br/en).

Before proceeding, let me mention that forward-looking statements that may be made during this conference call regarding expectations, growth estimates, projections and future strategies of BB Seguridade are based on management's current expectations, projections of future events and financial trends that may affect the business of the Group and do not guarantee future performance since these projections involve risks and uncertainties that could extrapolate the control of management. For more information on the statements of the company, please check on the MD&A.

With us today are Mr. Bernardo Rothe, BB Seguridade's CEO; Mr. Werner Suffert, BB Seguridade's CFO; and Mr. Rafael Sperendio, Head of FP&A, Accounting and IR. Please, Mr. Rothe. You may now begin.

#### **Bernardo de Azevedo Silva Rothe** {BIO 18059993 <GO>}

Thank you, everyone, for participating in our conference call. I just want to make a few remarks before I give the floor to Rafael to make the presentation. It's a big honor to be the CEO of BB Seguridade, one of the best and the biggest and leader in the market, it's a company that went through a big transformational year. We are now a different company from what we were at the start of last year after a great job done by my predecessors.

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We have a new team including in our companies and the insurance companies. We are very much invasive to deliver better results in 2019 and 2020. We have big challenges ahead of us, but we are pretty sure that we can deliver and we are going to return to an increase in profitability throughout these next years. We are the leader, as I mentioned, in the market, and that makes us a big target in terms of the competition that tried to replicate what we have, our competitive advantages or even this cut short what we have in place. That means that we need to keep it rolling all the time, changing the way we do our business, changing the products that we have to be able to compete and keep the leadership that we have. And we are going to focus in more -- in transact section and with capitalization of our sales force and counting on the network of Banco do Brasil, that's very strong capacity in terms of selling insurance and our product in general. So we are very, as I said, motivated, keep delivering better results throughout 2019, 2020.

With that, I would like to now pass the floor to Rafael for the presentation. So thank you.

### **Rafael Sperendio** {BIO 18963159 <GO>}

Thanks, Bernardo. Good morning, everyone. I'm going to take you through the presentation now. So let's start on Page 2, where we have the main highlights of Q4 a recurring stocks of BRL 840 million in the fourth quarter, down 10.7% year-on-year, driven by the 40% decline in financial results partially offset by the 4.1% improvement in the operating results as you can see in the chart on the lower left hand side. The financial results posted (ph) a lot in this quarter due to the spike in the IGP-M inflation rate in the period from September to November last year, which substantial increase in the cost of our financial liabilities of our refinance benefit pension plan, which are no longer sold, but are still impacting our financial, so -- financial results (inaudible) that a big hit in Q4. We expect that was eventually Brexit. It might reverse. It's already reversing. In December, the IGP-M showed some deflation, but the main point is that it does not impact the income statement. Now it's going to help the P&L just in some -- the first quarter 2019.

In terms of dividend, our payout which is BRL 2.9 billion in 2018, we added to the extraordinary dividend paid of BRL 2.7 billion with regards to the restructuring of our insurance partnership we have with MAPFRE. It amounts to something around 10% dividend to considering the current price of the stock. So we return to shareholders. Our annualized return on equity Q4, reached 41.4%, down 80 bps. Something that is worth mentioning here that despite the decline, we had a net income of almost 11%, we haven't seen the same proportion of declining in return on equity, which shows that when considering the moves related to the restructuring, it shows the more efficient capital allocation we have. So by restructuring our insurance company, we freed up some capital that was not really efficiently allocated. So it helped to hold the return on equity at a high level (inaudible), and we expect that it can be even higher from now on considering a lower level of capital allocated in this operation.

Another highlight we have in the quarter is the growing in the management fees of 8.5% at Brasilprev, driven by the 9.5% increase in the assets under management and the pension segment. In premium bonds, the main highlight was related to the increase in the net interest margin about 90 bps. It helped financial results to grow 25.7% year-on-year in

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Q4, driven mostly by the yield curve which flattened throughout the quarter. So it helped a lot the financial results as a premium bond company.

And lastly here we have the accounting of BRL 276 million recorded as an additional commission at the broker. We pushed through the new agreement that we have in our insurance company related to our commercial performance of credit life and credit life for farmers. So in case we exceed the targets, the commercial targets for these products, the bancassurance channel to receive an additional commission at the end of the year. So it is BRL 276 million refers to the commercial performance from April to December. It was only recorded in December because we got the late approval from the regulators of this reorganization only in November. So those will be book in December. From 2019 on this volatility we do not exist anymore. We've done book on a monthly basis according to our estimates related to how much we expect to receive as an additional anything the end of the year. So from 2019 on, it's going to be different, we will not see this at the end of the year and more.

Moving on to financial results on Page 3. Your lower right-hand side, you can see that financial results fell 43%, as I mentioned in the beginning of the presentation, accounting for 20% of the company's net income. Well, among the main factor that led financial results to post such a decline, we have the most straightforward ones with the lower steady rates, as you can see on the upper left hand side. But despite the IGP-M inflation index was the main drag on financial result in Q4. So this sort of led Brazil (inaudible) financial losses in Q4 for the first time in the history. So recalling that most part of the liabilities that Brazil (inaudible) the project benefit pension plans, they are back to IGP-M, while the assets there are back and these liabilities have a growing share of securities back to the IPCA with inflation index in Brazil. So although in Q4, another thing that's important to highlight here, as you can see on the lower left hand side, in Q4, IGP-M was lower than the IPCA. But it does not really reflect the performance of the financial results in the P&L because when we look at the way that interest is compounded on the liability, it's worth mentioning that there's a lag effect here of one to two months. So the period from September to November is the one that's responsible for this spike in the cost curve of our liabilities. So it's worth highlighting here that September and October (inaudible) with it being the for highest inflation index of the year. That's important, as I mentioned, (inaudible) that it wasn't a one-time effect, we can consider it as a one-time. It hits the financial results in Q4, but it's already showing some improvement that we might expect from the first part of 2019 on because of the deflation of the IGP-M in December.

What we've been talking about the post this slide we having in financial results, I mean the most important one is the move seeing in the forward yield curve. As you can see, the light colors represent the beginning of the quarter, and the dark colors represent the end of the quarter. So we can see that of the gray lines that the yield curve flattened in the fourth quarter 2018. It helped a lot Brasilcap with mark-to-market gains in view of coupons and inflation-protected securities in the end of the year.

Now on Page 4. We have a brief review of the performance, the commercial performance of our life and rural operation, which also began to operate with the home insurance and commercial lines from December on. We observed here that the lines that are more correlated to the credit origination posted a very strong performance in 2018 and net

premium should grow 7% in the year with a spotlight on credit life, which grew 20% and a very strong performance as well in credit life, and in mortgage life, and in rural.

Now on Page 5. In terms of the operating performance of our business, because we are still in a transition period from the old formation to the new formation from a December on we have last year, I hope you find it useful pro forma analysis, as we stated, we assume the information that it has been for -- since the beginning of 2017. So the blue lines show the numbers as reported, while the yellow line shows the pro forma figures. Another adjustment we have here is related to the commission ratio to normalize this commission effect that was only recorded in December. So the lean year when we look at the dashed line here it shows the normalization of this commission paid as it has been paid since April not only in December. Well, it's something that's worth highlighting here in terms of our performance as reported that the loss ratio increased by 4.8 percentage points. And it was mainly driven by the increase in the treatment of claims we having in rural mostly related to the drought, we had in the Midwest and excess rain we had in the south part of the country. And in addition to that, we also saw some increase in the loss ratio related to the Life segment due to a specific claim we had in a coinsurance of group life call it, we have in another insurance company. So we think that it's something that was may be in (inaudible) Q4 talking about life specifically and should not repeat going forward.

The commission ratio increased. There is a straightforward effect coming from the renegotiation we had with MAPFRE related to this commercial performance fee that we received. It's a function of our commercial performance and credit life and credit life for farmers.

And lastly when we look at the outcome of all these movements, in the combined ratio we can see that it rose by 4.6 percentage points and it's totally related to their increase in commission trend and increase in the loss ratio.

On Page 6, we have a brief explanation of our financial results, which fell 32% year-on-year due to a lower average SELIC rate in the quarter and also the base effect here. It's worth reminding that in the fourth quarter 2017, we booked some capital gains on spot market transactions. So this wasn't repeated in the fourth quarter 2018. So these gains amounted to BRL 82 million and this basic (inaudible) also dragged down the financial results comparison in fourth quarter 2018.

So the net income fell 53% year-on-year and so mostly related to this increase in the loss ratio, the performance fee paid to BB Corretora and also the decline in financial results. Let's say were the main drags to earnings up as a (inaudible) in Q4.

On Page 7, we bring here our performance in the Pension segment. So in terms of growth deposit with the decline of 7% year-on-year in Q4 greatly reducing the rate have decline, but we have been observing due to the third quarter of the year net inflows fell 36%, while redemption rate reduced it 20 bps year-on-year. Our pension reserves grew 9% and reached BRL 257 billion in 2018, helping management fees to grow 8% year-on-year in the fourth quarter and 10% growth in 2018.

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On the other hand, we can see that performance of net income of the company it was down 37% year-on-year in the fourth quarter and was totally driven by the financial loss we had related to the higher cost of our liabilities, as I mentioned in the beginning was driven by despite the IGP-M inflation rate.

On Page 8, we have our performance of our premium bonds operation. So collections fell by 29% year-on-year being Q4, the best quarter of the year. So this decline was mostly related to the hardest (inaudible) selections should be global trends that were (inaudible) at the beginning of the year so until September. So this growth trend was resource as a state-of-the-art comp in 4Q 2017. Financial results was the main highlight here in this company with a year-on-year increase of 26% in the fourth quarter and the net interest margin expanding 90 bps due to the mark-to-market gains we had (inaudible) securities in the fourth quarter. And due to the strong performance in information growth in fourth quarter, the net income grew 7% year-on-year, reaching a 40% annualized return on equity in the quarter.

On Page 9, we have BB Corretora. So commissions grew 26% fourth quarter year-on-year basically due to the BRL 276 million recorded as additional commission that we have received due to this performance related to credit life and credit life for farmers. By adjusting these effects of the light blue bars in chart on the upper left hand side, it shows that an analysis, but it is due to the additional commission linear range throughout the year from the April to December, and we did the same for 2017. You might remember that we had a write-down of commission receivable, which was fully concentrated in the fourth quarter 2017. So we also made a kind of adjustment here on revenues by splitting linear lead throughout 2017. And by making these two adjustments, you can see that the brokerage income on an adjusted basis declined 8% year-on-year and directed by soft performance -- commercial performance we have in the pension plans and premium bonds in 2018.

The EBIT margin increased at 540 bps also adjusted by the impact that reached 81.3%. The decline is 200 bps in 2018 enforced fully driven by the strategy that we had. In the middle figure, when we focus more on the lower ticket products, and by doing that we have some contraction in the EBIT margin. It's already reversing in the third quarter of the year. And we expect it's going to normalize to the average we have until 2017.

On Page 10, we have our accountability to our 2018 guidance. We ended 2018 with net income down 9.3% falling below our revised guidance range of decline 6% to 4%. We can assign here two-thirds of the deviation to two events. So the first is something that completely escaped our control, was very difficult to predict with the spike in the IGP-M inflation index during the election period, which ended impacting a very significant way because of our liability related to the decline in benefit pension plan at Brasilprev.

And the second was also in the Pension segment, which was the expansion of the low fees. So it was something that we were already expecting. We have been incurring these fees a long time, but we were doing it more gradually, but it was not the way that market responded, which led us to cut this fee more appropriately in the end of September because of our two dealers (ph). And the remaining a third of the deviation was assigned to the declining -- the premium bonds collection, which ended up impacting the big

(inaudible) result along with the increasing frequency of claim in life and rural in the end of the year. So these were the main drag on earnings.

And to wrap up the presentation on Page 11, we have here our estimates for 2019. As you can see, we have introduced two more guidance for this year. And for net income, we expect a growth of 5% to 10%. For insurance premiums, we are working here on pro forma analysis that is replicating the post corporate reorganization structural of our package with MAPFRE for the full year of 2018, and we are also excluding the DPVAT, we submitted (inaudible) government insurance. It doesn't depend on us (inaudible) its performance. So we are excluding it from our comparable. And so with regards to this pro forma analysis, we expect premiums to grow from 7% to 10% in 2019. And in terms of the reserves at Brasilprev, we expect it to grow from 7% to 10%.

So with this presentation over, we can now move on to the Q&A session.

## Questions And Answers

### Operator

Ladies and gentlemen, we will now be begin the question-and-answer session. (Operator Instructions) Ladies and gentlemen, our first question comes from Thiago Batista with Itau BBA.

### Q - Thiago Batista {BIO 15398695 <GO>}

Hi, guys. Thanks for the opportunity. I have one question about the possible impact that pension reform on the (inaudible) business. We saw in '16 material increase in the pension inflows during the discussion for the pension reform. Do you believe you can see something similar now? And also, what are the main impacts that you believe the potential approval of the pension reform should have in the (inaudible) business?

### A - Bernardo de Azevedo Silva Rothe {BIO 18059993 <GO>}

Thank you, Thiago, for the questions. Bernard speaking here. We consider that the pension reforms which are bigger policy for the country as a whole, for our pension business, it's a more medium to long-term impact. You may see some people running to do something this year, but it's not something that we expect putting out in numbers. But it's a very positive change in the long run, right, because it's going to increase the need for a pension plan and so on. So it's positive in the long run, medium to long run, maybe next year more than this year. And that's how we see it. Although, again, we consider the pension reform should be approved this year. That's the impact that's going to come over time. But the pension reform also can increase confidence in the market and so on and so forth. And that can impact unemployment in Brazil, and the decrease in unemployment and increase in available income, exposure of income by Brazilians overall is very positive for any insurance group. So we see that as a positive impact in other parts of the business overall.

### Q - Thiago Batista {BIO 15398695 <GO>}

Perfect. Thanks, Bernardo.

## Operator

Our next question comes from Mario Pierry with Bank of America.

### Q - Mario Pierry {BIO 1505554 <GO>}

(inaudible) mostly two questions. First one I'm trying to reconcile your guidance for 2019 of growth of 5% to 10% in net income. Just when we look at your operating results in 2018 excluding financial results, they increased 3%. So I would imagine that under a better economic environment that this should be growing faster. And then on the other hand, when we think about the financial results that declined 40% in '18, I would imagine it has to be much higher in '19 because interest rates aren't likely to be much lower in Brazil. So I'm trying to understand why the 5% to 10% seems conservative to me. If maybe you can give us a breakdown of what are you're expecting in terms of operating results and financial results and what is the significant rates that you have embedded on your guidance? Similarly, when I look at the premium growth that you're guiding for the SH1 segment of 7% to 12%, it is not much higher than what you reported in '18 of 7%. Also when you talk about growth in reserves at Brasilprev of 7% to 10%, it's actually lower than the 10% you've delivered in '18. So I'm just trying to understand why do these forecasts seem so conservative? Thank you.

### A - Rafael Sperendio {BIO 18963159 <GO>}

Hi, Mario. Rafael speaking. So first of all, with my assumption that we have in guidance for the SELIC rate, we expected to remain flat for the full year. So we don't expect any increase or decrease in interest rates throughout 2018. In terms of the operating performance, it's worth mentioning that we expect it to increase. If we were to break it down, the guidance in terms of operational performance and financial results, I would tell you that we expect the operational performance to be more closer to the top of this guidance, while in terms of financial results, our expectation for 2018 is that it can post even a decline and why? It's worth mentioning that part of the contribution of financial results which come from SH2, it's not part of our conglomerate anymore. So because of the exit of SH2, we can expect a decline on financial results. If we were to compare apples to apples, of course, it might pose an increase, but not that we are looking, we need to compare the numbers with the ones reported in 2018. Because of this effect, financial results might decline. But related to the expectation we have in premium growth, we are very optimistic with the performance in the lines that are correlated to credit origination. So credit life and mortgage life, these ones might be the main drivers for premium growth in 2019. Of course, there are different banks use credit life use to grow until last year more concentrated on individual segment. We expect that the SME segment might show some recovery in 2019, but overall, these are the main drivers. But with regards to the performance in term life, of course, it's something that accounts for 40% of the premium we had in SH1. So it's hard for such a big portfolio to grow in a such fast pace. So that's why when we analyze our performance in 2018, net premiums grew 7% in 2018. We are now using this 7% as the bottom of the new guided range. So we are expecting a very good performance, but it might be gradual, of course, according to the improvement in the activity in the economy, what we believe is going to show some more I'll say, material improvement from second half, that's why what was embedded in our guided range for

net income. And the thing for reserves as a Pension segment, one the main track we have is related to lower SELIC rate. Of course, it's not a big decline as we had in '17 and '18, but it's still a decline. So the 7% to 10%, that's a lower SELIC rate considering that we are assuming that we will offset part of it with some recovery in pension inflows, but it's still a significant impact that we have in line rate.

**Q - Mario Pierry** {BIO 1505554 <GO>}

Okay. Just a quick follow-up. On your management fees at Brasilprev, it stayed flat on a quarter-over-quarter basis, I think for the first time in a while 1.08%. I think we're used to seeing this decline at least 1 basis point per quarter. Does it mean that the pressure on asset management fees are over? And then we should expect them flat? Or is there some seasonality in this figure?

**A - Rafael Sperendio** {BIO 18963159 <GO>}

There are no seasonality. The main thing is that it declined quarter-on-quarter, but you can see because of decline rounding. So that's something that's important to note. Of course, the SELIC stage at 6.5% for longer, this competition might increase. Of course, we need to respond to it by providing more financial advisory services to clients in order to improve their capital allocation and then increase their exposure to private securities and to the stock market itself. But we expect if we were to consider a trend for management fee is that it will keep declining, but at a lower base a great quarter. Remember, it used to be 300, 200 bps per quarter, reduced it to 200, 100 bps per quarter. Now it's more close to 100 bps per quarter.

**A - Bernardo de Azevedo Silva Rothe** {BIO 18059993 <GO>}

Just to add, it's part of our job to offer new set of products to our clients in the integration plan. So we can have funds that carry a high fee. So it's part of what we've been doing. That's going to be a positive impact on one side. But on the other side, we want to increase the participation also of lower income, middle income people with pension plan. They tend to be more conservative in terms of what they do. They want to compare more to savings than anything else. So fixed income funds tends to grow, although we have higher management fee in this middle income type of clients than what we charge. In private banking clients, for example, they tend to be lower than the (inaudible) funds and the equity funds and so on and so forth. So the trend over time tends to grow the participation, the total management funds through these type of higher management fees type of fund, okay?

**Q - Mario Pierry** {BIO 1505554 <GO>}

Okay. Thank you very much.

**Operator**

(Operator Instructions) Ladies and gentlemen, our next question comes from Eduardo with Banco Plural.

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## **Q - Eduardo Nishio** {BIO 15333200 <GO>}

Hi, everyone, thank you for the opportunities you show here. Question to Bernardo. Bernardo, congratulations for the new post. Just wondering, if you -- a few days, you've been in charge as a CEO, just wondering your views and what you can do, any changes you can do to make BB Seguridade growing a little bit faster than it has been for the past few years. If you can give us your impression what strategy to boost earnings? I would appreciate it. Thank you.

## **A - Bernardo de Azevedo Silva Rothe** {BIO 18059993 <GO>}

Thank you, Nishio, for the question. Let me tell you that's a -- the first two quarters of the year is pretty much right. Because we have a lot of remeasures in what we do. So we are going to see the good job done last year that's going to start reflect and the results that we're going to see this year. What I'll try to do here to focus on private sections to make things more sustainable over time even that increase in competition, insured (ph) tax coming to the market and so on and so forth. So we have to increase quite substantially with our products. We have to increase the Banco do Brasil employee satisfaction in selling our products. So we are going to focus pretty much in improving our products, improving the process of selling our products throughout the different channels, right? The difficult journey has to improve and we are going to do a lot of things in terms of that because we have also a new broker, right? The additional brokerage (inaudible). So we have to improve the portfolio of products in sequence to grow. So we have several measures that we're going to focus from now on to make results improve and improve sustainably over time, right, not only thinking about the company. It seems that also 2020 and so on. So focus on client satisfaction, improvements of products and the process of selling our product, that's the main drivers of our strategy in this year.

## **Q - Eduardo Nishio** {BIO 15333200 <GO>}

Okay. Thank you so much.

## **Operator**

Ladies and gentlemen, this concludes today's question-and-answer session. I'd like to invite Mr. Bernardo Rothe to proceed with his closing statements. Please Mr. Rothe, go ahead.

## **A - Bernardo de Azevedo Silva Rothe** {BIO 18059993 <GO>}

I just want to thank everyone for participating in our conference call, and you have all our IR team at your disposal to clarify any doubts that you may have in terms of our performance last year and what we expect for this year. So thank you very much and see you next conference -- in the next conference call. Bye.

## **Operator**

With this, we conclude BB Seguridade's conference call for today. As a reminder, the material used in this conference call is available on BB Seguridade's Investor Relations

website. Thank you very much for your participation and have a nice day. You may now disconnect.

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