

Q2 2020 Earnings Call

Company Participants

- Inacio Reis Caminha, IR Superintendent
- Mauro Dutra, CFO & IRO

Presentation

Operator

Good afternoon ladies and gentlemen, and welcome to Banco Pan's Conference Call to Discuss the Second Quarter of 2020 Results. This event is also being broadcasted simultaneously on the Internet both audio and slide show, which can be assessed on the Company's IR website www.bancopan.com.br/ir, and MZiQ platform with the respective presentation.

We would like to inform you that in this event, all participants will be in listen-only mode during the Company's presentation. After the Company's remarks are completed, there will be a question-and-answer section. At that time, instructions will be given (Operator Instructions).

Forward-looking statements are subject to known and unknown risks and uncertainties that could cause the Company's actual results to differ from those in forward-looking statements. Such statements speaks only on the date they are made and the Company is under no obligation to update them in light of future developments.

With us here today, we have Mr. Mauro Dutra, Banco Pan's CFO and IRO. Now I will turn the conference over to Mr. Mauro, who will begin the presentation. Mr. Mauro, you may begin your conference.

Mauro Dutra {BIO 21792010 <GO>}

(Technical Difficulty) second quarter 2020 earnings release. We have here besides me, our CEO, Mr. Carlos Eduardo Guimaraes and our Head of IR and Funding Mr. Inacio Caminha. This was a challenging quarter in which our digital profile allowed us to operate normally. We managed the bank very conservatively and we can see, we are very satisfied with the results obtained.

Starting on Slide 3, we see that the credit portfolio of the bank remained stable in the quarter with BRL24.7 billion in the end of June, growing 10% in 12 months. Regarding credit production, we originated on average BRL2 billion per month in this quarter, 11% higher than in the first quarter and 22% above 2019 with a significant growth in digital formalization, leveraging both our B2B and B2C channels. We advanced to 5.7 million customers under management, growing 24% in 12 months. We also achieved an earnings

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before taxes of BRL207 million in the quarter, in line with the past quarter and 26% above 2019. And for the first half of the year, we reached BRL417 million in our earnings before tax, which is an important growth of more than 40% when compared to 2019.

Net income for the period was BRL144 million, and BRL314 million for the first half of 2020, also improving significantly compared to 2019. These results generated an annualized ROE of 11.4% in the quarter and 12.5% in the semester. Regarding our adjusted ROE, we had 19.9% in the quarter and 21.5% in the semester, maintaining consistent levels of returns here in the bank. We ended June with BRL5.1 billion of net equity and 15.9% of Basel ratio, reinforcing our conservative strategy during this pandemic period.

Then moving to Slide 4, due to this -- due to the current scenario, we decided to initiate our presentation with an overview of the quality of our credit portfolio. First of all, talking about loan postponements, as you can see in this slide, we had a very conservative approach to loan deferral. Only two installments of around 11,000 customers were postponed or deferred. And following the payment evolution of these installments, 87% and of what was due in June was already paid. We had 5,000 installments due in June, from which 87% were already paid. The amount of these loans -- of these deferred loans represent less than 1% of our portfolio. And all the contracts involved in disposed [ph] ones have collateral as they are part of our vehicle financing portfolio. As a result, we saw a controlled increase in our over 90 days deferration [ph] from 5.7% in March to 7% in the end of June, which reflects the real impact of the crisis on our portfolio. Another information we released this quarter is the shorter default indicator from 15 to 90 days. This indicator increased to a peak of 10.8% in April, decreasing since then, up to 8.3% in the end of July. It is worth to mention that this is an early indicator to the ninth [ph] day deferration, which we expect to have a better performance looking forward.

Moving to Slide 5, we can see the evolution of our loans for losses and credit recovery. Here we show the effect of the restricted credit (inaudible) approach on credit provision expenses, which increased to BRL414 million in this quarter. The expense, net of credit recovery, reached 5.9% of the portfolio. The financial increase of such expense -- of the net expense was BRL133 million, of which BRL37 million come from a smaller recovery in the wholesale portfolio, which is already 100% provisioned, as we explained in the past quarters. The resilience of our portfolio is very important to mention, especially because we have 95% of payroll deductible loans and collateralized transactions, as we are going to explain in details when we talk about the credit portfolio during the presentation.

In the vehicle financing business, which accounts -- which portfolio accounts for 38% of our total portfolio, we saw a significant positive movement. The provision expenses in this business in June reverted to the pre-crisis level, showing an important improvement in payments. Even so, we continued to manage credit, capital and liquidity conservatively here in the bank. So just to finish this credit session, I'd like to tell you two key messages regarding this matter. The first one is both our balance sheet and our results already reflect the real impact of the crisis in our business. And the second key message is that the indicators, as you could see in the slide, show that looking forward, (inaudible) seems better than in the past, although we are still managing the bank conservatively because maybe a second wave of the virus or its economic impact can still hurt some figures, but we are very satisfied up to now.

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We can then move to Slide 6. Here, I'd like to initiate remembering you what we have said in the last quarter. Our long-term view for our business and for the bank hasn't changed with the crisis. We made some adjustments to our business, to our activity, but we keep focused on the evolution of our digital strategy. In this context, on the left side of the slide, you can see our digital formalization has evolved significantly in this quarter. We reached 66% of our payroll operations digitally formalized in June. And for the vehicles business, the figure was even higher with 94%. Our digital bank continues to grow in line with our expectations, and we are very satisfied with what is happening. In the second quarter, new features were launched. And in the coming months, we will add self contracting in payroll loans, which is very important, investments in fixed income assets and also financial education tools.

On the right side of the slide, you can see some partnerships we announced on this quarter with different companies from different sectors, which have a great fit with our target client base and can add new services to our clients. We highlight them, the partnerships with Claro and the fintechs Mobills and Celcoin. We see these channels as a relevant tool to engage customers and partners -- both customers and partners, optimizing cross-sell and upsell opportunities in addition to increasing the portfolio of services and products of Banco Pan.

I would then let Inacio explain you about the figures and the financial performance of the bank.

Inacio Reis Caminha {BIO 19326001 <GO>}

Thank you. So moving on to Slide 7, we present some of the main numbers and indicators for the quarter. The upper left chart shows the increase in the net interest margin, reaching BRL1.2 billion and 19.1%. This shows -- this slight increase reflects the volumes of credit assignment and also the robust level of spreads in our operations. Allowances for losses, we have already talked about it in the previous slides. And going forward, the expenses -- administrative and personnel and also with origination, they dropped to BRL592 million, basically because of the mix of originations that we had in this quarter. So all these together, they combined BRL207 million earnings before tax and a net income of BRL144 million, slightly below what we saw in previous quarter, mainly because of an effective higher income tax rate following the changes in the regulatory system in Brazil. The adjusted ROE, which also reflects the performance of the bank and the margin ended the quarter at 19.9%.

In the next slide, we have the half year earnings. So, when we look at all the same figures, we see a 30% increase in the NIM, reaching 18.5%. Allowances for losses went up 19%, reaching BRL736 million. And the other expenses also increased 19%. And these other expenses, they reflect the bank change that we had in this last year, also having higher margin, but more investments in technology and the digital bank didn't have any impact in the first half of '19. So still, we see an important evolution in the earnings before tax, reaching BRL417 million in the semester, 43% above what we saw in the first half of '19, resulting in a net profit of BRL314 million and the adjusted ROE of 21.5%, very strong figures in our view [ph].

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On Slide 9, we see the composition of that -- these adjustments that we make to get to the adjusted ROE. So basically, we are adjusting or excluding the excess of financial expenses related to fixed rate time deposits that we had issued in the past between 2005 and 2008. And without that, the net income would be BRL199 million in the quarter, above the BRL144 million that we see in the accounting figure. The other adjustment relates to the size of the shareholders' equity, we also exclude the excess of DTA that we have related to also losses in the past in the previous management. So when we get the BRL4 billion equity and the BRL199 million net income, we reach the 19.9% adjusted ROE and coming from the 11.4% in the accounting ROE. The same dynamics runs in the first half of the year. So we get to the 21.5%. And it's important to mention that these are two simple adjustments to make easy to understand. And this year, we have a significant maturity in this time deposits, BRL971 [ph] million will mature in December. So 30% will be gone by year-end.

On the next page, we have the details of our credit origination. We have granted BRL2 billion per month in the quarter, reaching BRL6 billion in the first three months, increasing 23% in 12 months. Payroll led this increase, reaching BRL1.2 billion per month. And this increase basically relates to the changes that we had in the interim and cap rates for the social security program. And in April alone, we saw the -- our record in terms of origination, BRL1.4 billion in one given month.

Vehicle financing had an average origination of BRL355 million, decreasing 26% from the past quarter. And still, we had a better performance than the market that we will show further on. Credit cards remain stable, practically with BRL385 million per month in terms of transactions. Also in this quarter, we had 180,000 new clients per month, reaching 5.7 million managed clients by the end of the quarter.

On Slide 11, we present the composition of credit portfolio. The portfolio mix remained practically stable. Also the overall balance, BRL24.7 billion, but also growing 10% in 12 months. When we see the breakdown, payroll remains as a main product with BRL13 billion and 52% of portfolio mix. Vehicle financing ended the quarter at BRL9.3 billion, with 38% of the portfolio and credit card BRL1.2 billion with 5%. The other runoff products kept reduced their balance. And with that, we get to the BRL24.7 billion portfolio. It's very important to mention that within those BRL24.7 billion portfolio, 95% of them are either collateralized loans or payroll loans. So this gives a very significant value for our portfolio. And also when we look at renegotiated loans, they only account for 0.6% of the entire portfolio. So when you look at the originated portfolio, we ended the portfolio -- we ended the quarter at 32.5% -- BRL32.5 billion.

In payroll, we remained as a relevant player focused on federal codes, figuring among the top originators for the social security market. We have granted BRL3.7 billion in new credits in this quarter, out of those, 95% comprised by loans and 6% in credit cards. And as Dutra mentioned, we had 60% of all these loans originated digitally. And June alone, it was 66%. This technology brings much more efficiency to the operation, especially in this time of lockdown and all the partners and clients are very, very satisfied. The concentration remains very relevant in federal codes. We saw an increase to 95%, explained by the increase to 89% in the INSS. The loan portfolio balance declined due to

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the credit assignments, but the credit card portfolio continued to grow. Together, they reached BRL13 billion.

On vehicle financing, on Slide 13, we see that the portfolio remains stable at BRL9.3 billion with an adequate level of loan-to-value and also the term of the operations. In the table, we see the drop to BRL355 million per month in the quarter, but it's important to look that the movements that occurred both in the market and also in our numbers. So to help to visualize that, we included these two charts in the -- over right side. And then we can see that in the used vehicles market, it reached the lowest level in April and then recovered month after month. And when we see our performance, we didn't fall that much. And now we are -- we have originated in June more than what we have originated in February also with a very conservative approach in terms of credit concession. In new motorcycles, we had the same trend. So the market felt the effects of the crisis, of the pandemic, but we had a better performance than the market. And here in vehicle financing, it's very important to mention that all of this digital formalization platform has improved significantly. And with that, we became more closer to our business partners, all the dealerships. And then -- and also helping the clients to acquire the loans, acquire the cars in these times.

Moving on to the next slide, we have the credit card data. We maintained a stable level in terms of transactions, and we issued fewer cards because of our more conservative approach. We have expanded the origination channels, and then we see month after month, our clients are becoming more digital. So not only in the way that they purchase the credit cards, but also in the way that they serve themselves using chat and WhatsApp and also receiving digital invoice. So all these environments, not only brings more efficiency to the transaction, but it also helps to enhance the clients' experience, while using our products.

In the next slide, we have the insurance premiums detail. We saw a decrease pretty much related to what we saw in the vehicle financing because they are very connected. And we see that the digital bank has a leverage tool to help to increase a lot of these insurance sales, not only the products that we already have, but also bringing new type of insurance.

Talking about funding on Slide 16, we ended the quarter at BRL24.2 billion. Time deposits increased their share, contributing to the diversification of our funding, not only through direct clients, but also through distribution platforms. In April, we settled the subordinate bonds that matured \$567 million, sorry. It was fully hedged and even after that, we continue with a very comfortable liquidity position, operating very conservatively.

And to conclude the presentation on Slide 17, we have our Basel ratio, which ended the quarter at 15.9%, entirely composed by CET1, showing a very strong level of capital. And we remain steady in our digital strategy in diversifying products for the low-income individuals, with a focus on credit through B2C and B2B channels and also with our strong origination capacity. Obviously, considering the moment, we will maintain a conservative posture until the scenario becomes more clear.

And then with that, I conclude the presentation and open the line for questions.

Bloomberg Transcript

Questions And Answers

Operator

Ladies and gentlemen we will now begin the Q&A section. (Operator Instructions) And there seems to be no further questions, I would like to turn the floor over to Mr. Mauro for his final remarks.

A - Mauro Dutra {BIO 21792010 <GO>}

So thank you very much for you all being here with us. We reinforced our view that our balance sheet and our results already reflect the real impact of the crisis in our activity, and we are very satisfied with the results of this quarter. See you next quarter, thank you very much.

Operator

This concludes Banco Pan's conference call. You may now disconnect, and have a good day.

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