

Q3 2013 Earnings Call

Company Participants

- Ivan de Souza Monteiro, CFO
- Leonardo Loyola, Head of IR
- Unidentified Speaker, Unknown

Other Participants

- Carlos Macedo, Analyst
- Jorg Friedemann, Analyst
- Marcelo Telles, Analyst
- Mario Pierry, Analyst
- Natalia Corfield, Analyst
- Philip Platt, Analyst
- Regina Sanchez, Analyst

Presentation

Operator

Good morning, everyone. And thank you for waiting. Welcome to Banco do Brasil's Third Quarter 2013 earnings conference call. (Operator Instructions)

Before proceeding, let me mention that this presentation may include references and statements, planned synergies, estimates, projections and forward-looking strategy concerning Banco do Brasil, its associated and affiliated companies and subsidiaries. These expectations are highly dependent on market conditions and on the performance of domestic and international markets, the Brazilian economy and banking system.

Banco do Brasil is not responsible for updating any estimates in this presentation.

With us today we have Mr. Ivan de Souza Monteiro, CFO; and Mr. Leonardo Loyola, Head of Investor Relations. Mr. Leonardo, you may now begin.

Leonardo Loyola {BIO 16193219 <GO>}

Good morning, everyone and thank you for joining our Third Quarter earnings conference call. I'd like to start the presentation on slide number 3. On this slide we show some highlights of Banco do Brasil's performance in the period. We posted a net income of BRL12.7 billion in the first nine months of 2013. In the adjusted view, this amount was

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BRL7.9 billion. In the quarter adjusted net income was of BRL2.6 billion, while the net income reached BRL2.7 billion.

Our loan portfolio in the broad concept grew 22.5% in 12 months, we will detail this performance in later slides.

Our delinquency ratings remained at the best in the industry closing September 2013 at 1.97%. The following pages will illustrate the resilience of our credit methodologies in terms of average risk and the stability in the ratio between the provision expenses and the loan portfolio.

I also would like to emphasize that the cards billings grew by 23.7% year over year and BB Seguridade value reached 23.8% market share. Our administrative expenses remained under control growing less than inflation.

Moving to next slide, on the slide number 4, we present some of the earnings highlight starting with interest income that grew 0.6% quarter on quarter and 2.3% for nine months year on year. In fee income we grew 9.9% over the past nine months feeding the low end of the guidance range.

Provision expenses dropped 7.2% quarter on quarter, over the past nine months these expenses increased by 3.6%. We posted an adjusted net income of BRL2.6 billion in the quarter corresponding to an adjusted return on equity of 15.7%.

Moving to the next page, in slide number 5, we show our sources and uses where we observed relative stability in our funding mix. Between June and September 2013, as you know BB has promoted a migration of time deposits to other instruments over the last several period; notably to agribusiness and real estate letters of credit. This has allowed us to realize huge savings in funding costs. These instruments' balance grew by 44.2% compared to last June 2013. You can see that Banco do Brasil's loan portfolio represents 84.6% of the Bank's uses.

I'd like to highlight here the adjusted loan-to-deposit ratio that showed an improvement of 87% in September 2013, which illustrates that BB's loan portfolio is appropriate to its level of commercial funding.

Moving to the next page, to slide number 6, we show Banco do Brasil's net interest income performance. In the upper left-hand side graph you can see the behavior of our global spread that was relatively stable in this quarter, reaching 4.5%. The performance was mainly impacted by higher funding costs due to the increase in SELIC rate. And also we have a mix effect due to the growth of the loan portfolio in line with lower risk.

In the graph on the right-hand side we show the credit spreads by segment. We highlight here the behavior of the spreads for the individual segment that reflected the growth of the loan portfolio with a safer [ph] credit line. In the table below we show a breakdown of our NII that grew by 2.3% on a 9 month year-on-year basis.

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I want to emphasize here both the loan operations income growth and treasury income that performed at levels similar to 2012. On the other hand, funding costs reflected the recent increase in the SELIC rate. We will see at the end of the presentation the adjustment that was made in the NII guidance.

Moving to the next page, to slide number 7, we have the evolution of the loan portfolio in what we called the broad concept. We see an increase of 22.5% compared to September last year, highlighting the growth of 32% in agribusiness portfolio and 25% in loans to companies, which accounted respectively for 19.9% and 47.1% of the loan portfolio of Banco do Brasil.

Our loan portfolio to individuals also in the broad concept grew 14.1% in 12 months and ended the quarter representing 25.1% of the BB's loan portfolio. We will see at the end of this presentation the adjustments we made in the credit guidance for 2013.

Moving on, on the next slide we have the portfolio with individuals in what we call the organic view. In this view we excluded proportional consolidation of Banco Votorantim and the acquisition of portfolios of other banks. On the basis, the portfolio grew 20.4% in 12 months and 3.4% in the quarter. As you can see, 74.9% of this portfolio is concentrated in lines of lower risk such as payroll loans, salary loans, auto loans and mortgages.

On slide number 9 we detail a bit more about risk lines. On the upper graph we observe the comparison of BB's payroll loans balanced with our peers. We see that balance of this portfolio in September 2013 is much higher than all other banks and allows Banco do Brasil to hand [ph] the peers with 28.4% market share.

If we consider the organic portfolio, 87.2% of this portfolio is customers who are civil servants, 8.4% relates to INSS retirees and 4.4% to private sector employees.

BB's mortgage portfolio posted a balance of BRL20.1 billion at the end of September 2013 an increase of 87% in 12 months. This slide has been bringing a lot of importance in our portfolio and that vigorous growth is explained by our recent entry in this market.

The Bank has granted mortgage loans since 2007 and today we are positioned in the fifth place among the financial institutions that operate in the sector. This product is extremely important to the Bank. Since it promotes a long-term relationship with the client and creates an opportunity for increasing (inaudible) by offering products that add value to the relationship.

Finally, the bottom right-hand-side graph shows the growth in the auto loans portfolio. As you know, we show the strategy (inaudible) to our customer and our branch network. First, in September 2013 more than 80% of auto loans was taken by customers with (inaudible) for over five years.

Moving on to the next page, in page 10, we show you the Company's loan portfolio. Over BRL307 billion that we highlight the growth in the credit for investments in capital loan.

The next page in slide 11 we present the breakdown of the loan portfolio with companies considering their size. SMEs and medium and large companies. The SME portfolio (inaudible) September 2013 a balance of BRL94.4 billion, up 0.4% quarter over quarter. I'd like to emphasize here that we categorize as SME companies that have annual gross revenues of up to BRL25 million. BRL16.8 billion of the SME loan portfolio was covered by the Operations Guarantee Fund, the FGO.

It's important to note that that from this BRL94.4 billion portfolio approximately two thirds is contracted with clients who have been with the Bank for more than five years. On the other hand the stake of clients with less than a year with the Bank its only 2.1%.

Moving on to the next page on the slide 12, we can see our agribusiness loan portfolio. This is the portfolio with the lowest delinquency across the Bank's different types of credit. As you know, agribusiness has driven the growth of Brazilian GDP and following these trends this agribusiness loan portfolio grew 2.4% quarter over quarter and 32.2% year on year.

As you can see from the chart on the right-hand side, more than 65% of the loan (inaudible) to working capital for people purchase on the 13/14 crop are protected with insurance options offered to our customers.

Moving onto the next page on slide 13, there are some important metrics that explain the low delinquency of Banco do Brasil's loan portfolio. You can see in the chart at the top of the page the average risk of our portfolio, which is the ratio between the required provision and the classified loan portfolio is lower than the ratio seen in the industry. We closed September 2013 with a ratio of 3.57% while the industry posted 5.08%. This confirms the resilience of our credit methodologies.

On the bottom left-hand-side graph we see the write-off ratio of Banco do Brasil. We take last operations for (inaudible) and when that happens we recovered the most as you can see on the right-hand-side chart. These factors influence BB's low delinquency as we will see in the next slide.

As you can see here at the top of slide 14 our current provision levels enable us to record a coverage ratio of 191.9%, a much better ratio compared to the industry. At the bottom of this slide you may notice that the delinquency ratio ended September at 1.97%, much better than what we saw in the industry, which was 3.3%. If we exclude Banco Votorantim's delinquency this ratio improves to 1.78%.

Moving to the next slide, slide 15 where we present the breakdown of BB's delinquency per segment. After we reached the very low level in our delinquency in the Second Quarter of 2013 we can observe that the non-performing loans have been stable compared to that observed in 2012. We emphasize that Banco do Brasil's consolidated delinquency as well as the NPLs for loans overdue for more than 90 days of all portfolios remains at levels significantly lower than those reported by the industry. BB has quite robust credit methodologies that guarantee the quality of our loan portfolio.

Moving on to the next slide we see the breakdown of Banco do Brasil's delinquency per segment after we reached the very low level in our delinquency in the Second Quarter 2013. You can observe that the non performing loans has been stable compared to that observed in 2012.

We emphasize that BB's consolidated delinquency as well as NPL for loans overdue for more than 90 days of all portfolio remains at levels significantly lower than those reported by the industry. BB has quite robust credit methodologies that guarantee the quality of loan portfolio.

On slide number 17 we make the comparison of our credit provision expenses to the total loan portfolio. The result achieved with the risk management of the credit portfolio, the very low historic rates of delinquency and the wide historic rates of the coverage ratio have allowed the continuous improvement of methodologies for this classification of our loans.

On the first graph, upper left-hand side, we have the ratio between provision expenses and the loan portfolio on a 12 month view. This is a guidance (inaudible) and you can see that this ratio has decreased and at the end of September reached to 2.80% which enable us to reduce the guidance range from this guidance as we will see later on.

On the second graph on the upper right-hand side we see the same relationship but now on a quarterly view where we also see an improvement in this ratio. In the graph at the bottom we show that 21.7% growth of the loan portfolio between September 2012 and September 2013 has been occurring in (inaudible) mainly between AA and C.

Moving to the slide number 18. So we promoted a revision in our criteria and parameters for credit rating. This migration was done mainly between the AA and C level. It has had target clients with the best risk profile with indebtedness exceeding BRL50,000 and with whom we saw the rating verified after the credit concession was better than the rating posted in the beginning of the credit concession.

Considering criteria, we observed the specific criteria such as category of transaction, purpose, warranties and terms.

Moving on to slide 19, we show a breakdown of this provision expenses in the quarter. We had a worsening of BRL183 million regarding the anticipation of Pronaf transactions and BRL280 million (sic-see slide 19 "BRL208 million") regarding changes in the portfolio and we also had a revision amount of BRL695 million we offered to the revision of criteria for risks made. The net effect between provisions between our revision and Pronaf event was BRL512 million pretax. We still maintain our additional provision amounting to BRL1.2 billion. I would like to emphasize that even with these adjustments our coverage ratio remains well above the level of the industry.

Moving on, on the next slide, we have information regarding the origination fees for light vehicles from Banco Votorantim. We can see that the delinquency in this portfolio has shown a significant improvement.

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And moving on to slide number 21, we addressed the asset quality of loans originated in Banco Votorantim. The top graph shows that provision expenses and looking only at the credit provision expenses for the auto loan books when we compare the Third Quarter of this year to the Third Quarter of 2012 we see an improvement of 46%.

On the bottom left-hand-side chart we also see an increase in Banco Votorantim's coverage ratio now at 120% and the NPL ratio reaching 5.7%. In the bottom right-hand-side we see that the share of the portfolio with high delinquency originated between July 2010 and September 2011 has decreased its share in Banco Votorantim's auto portfolio.

The new car contract, actually the new vintage contract after September 2011 already occupies 59% of the total auto loans granted by Banco Votorantim.

Moving on slide 22, we show our performance in fees. This item increased by 9.9% over the past nine months in comparison and now we are very close to reaching our guidance for fee income. As you know the Bank has focused on diversifying values.

I would like to highlight here the card values which grew by 17.5% over the past nine months compared to the same period last year. We will see more details about cards on the next slide.

Fees from insurance pension plan and premium bonds as well as those from capital markets also performed very well during this period. You could see fees from loan operations growing 16.6%.

Moving on to slide number 23, we show some information about our card business. As you know, in the last quarter we brought more information about this business in our MD&A. I would like to draw your attention to the chart on the left-hand side where you can see what we call operational results of card services.

We can observe in the nine months accumulated comparison between 2013 and 2012 an increase of 26.5% in those results which is completely in line with what we see on the graph on the right. The intense use of cards as payment instrument as well as an alternative access to traditional credit lines has increased the revenues from the cards. Banco do Brasil has -- is steadily increasing its market share over time reaching 24.4% of this market.

Moving on to slide number 24, you can see the performance of our administrative expenses. These expenses amounted to BRL21.8 billion in the nine months of 2013, accumulated an amount that is 5.3% higher than in the same period of last year. This low growth demonstrates the strong commitment of Banco do Brasil to cost control and operational efficiency. I would like to highlight here that this figure is lower than inflation accumulated in the same period.

Moving on, on the next slide as a result which you can see in slide number 25 the relative stability in our adjusted income ratio with improvements in the (inaudible) over the last 12

months.

And the next slide, moving to slide 26, we show that our BIS ratio was 15.17% end of September 2013, a quite comfortable ratio even in a period of strong growth of the loan portfolio. It grew 22.5% in 12 months. If we consider the full implementation of Basel III rules adjustment calculated on September 13 the BIS ratio would be estimated on 13.47% and Tier I on 8.55%.

Moving on slide 27 we close this presentation with our guidance. We demonstrate our 2013 performance against what we projected throughout the year and also the revision of some items. We achieved 15.8% adjusted return on equity in the middle of the range for 2013. We revised the NII guidance to a range between 2% and 5% as well as our estimates for commercial funding now in the range between 12% and 16%. The credit items of individuals and agribusiness were also adjusted, the first one down and the second one up. And finally, the allowance for loan losses that decreased to a range between 2.7% and 3%.

Thank you for your attention and let's now open the Q&A session.

Questions And Answers

Operator

(Operator Instructions) Philip Platt, UBS.

Q - Philip Platt {BIO 19772677 <GO>}

First question just on the risk classifications of low income, could you explain the rationale for doing this and the timing of it, please?

And secondly, in terms of new NPLs, we saw a pickup which you presented in your slides earlier, can you explain where this is coming from, which sectors are seeing problems, how are newer vintages doing? Thank you.

A - Ivan de Souza Monteiro {BIO 16420543 <GO>}

So thank you Philip for your questions. I am going to start answering first one and then I will pass to Gustavo for the second one. So basically this is something that we do -- actually the way that we handle this, we see -- we provide a range for the credits in the beginning and then we after a while we see the actual performance of this credit and then we adjust according to the actual performance of the credit.

This is something that we do on a regular basis and something that we did now. So there is a no particular motive. We see this as a natural procedure that we do on a regular basis. Then I would like to pass to Gustavo to answer the second.

A - Unidentified Speaker

Yes, Philip, could you repeat your second question please.

Q - Philip Platt {BIO 19772677 <GO>}

Yes. Absolutely, it's to do with the pickup in new NPLs, I think saw a 26% rise year on year, I appreciate your loan growth has been pretty strong as well but really the question was where are we seeing the problems in new NPLs coming from and can you also give us an update on the behavior of these new vintages of loan that you have been giving. Thank you.

A - Unidentified Speaker

Yes. Well yes, you see the slight increase in new NPLs in the Third Quarter, bear in mind that in the Third Quarter we had a strike that -- in a period that was longer than what we anticipated and there is no denying there are some impacts related to that. There is no signal in any of Banco do Brasil's portfolios individuals, companies or agribusiness of credit deterioration, what we forecast is a relative stability for the upcoming periods.

If you look at the performance of the newer vintages across the portfolios because of general improvements in the credit methodology what you will always see is a newer vintage still performing better than the older ones so it's a continuation of what you have seen in the last quarters.

Q - Philip Platt {BIO 19772677 <GO>}

Okay. Great, can I just have a follow-up question on the risk classification? In the Third Quarter AA classified loans were around 54% of your total portfolio, which is well above the industry average which was around 25%, 30%. Can you explain why there is this discrepancy between you and the industry, please?

A - Unidentified Speaker

Well first of all when we do our internal credit assessments we are looking at our portfolio. And our portfolio follows a different strategy, specifically for individuals, the Bank has prioritized growth in lower-risk segment for a few years now. And the most important of those products is credit on payroll, both payroll and salary loan. If you get these two items together they are more than 50% of Banco do Brasil's organic portfolio with individuals.

The strategy for the other segment is quite similar. The credit with SMEs, for example, heavily based on guarantee funds or receivables. Our credit methodology with large corporations prove even through recent events that Banco do Brasil has a very strong methodology. And if we look at the agribusiness segment. And that's 20% of our portfolio, this is the segment with the lowest NPLs, with the lowest delinquency across our portfolios. We think our number is very adequate.

But if you look at the banking industry and you extract the largest banks you will see a concentration more closer than ours. So don't look at the banking industry as a whole, look at our peers and you will see a concentration in the best [ph] risk as well.

Operator

Marcelo Telles, Credit Suisse.

Q - Marcelo Telles {BIO 3560829 <GO>}

I have some follow-up questions on the -- based on the Portuguese call. My question is on the Pronaf. As you mentioned there was, this is definitely an offsetting factor regarding the part of the provisions right that you -- regarding the positive impact of the reclassification of risk criteria.

But my question here is the Pronaf, did that change have any impact on your NPL as well or the only impact was on provisions, that's my first question. And the second question is I mean you've done a remarkable job on operating expenses in the quarter. So I was wondering if this is the type of behavior you should expect also for the quarters to come and the next year?

I know for you guys it's little more difficult to contain costs being like a public bank but if you could comment on the initiatives you are doing to try to grow OpEx at a lower amount, thank you.

A - Unidentified Speaker

Thank you, Marcelo, Gustavo here. On your first question about the events related to Pronaf, the impact is on both sides, both on our credit provision expenses and also on NPLs. So as this was implemented you do have an increase in NPLs for this segment. If we were to look at the delinquency level of the agrobusiness portfolio extracting, discounting this effect, the NPL ratio will be closer to the one we had on the Second Quarter.

Moving to OpEx growth, yes, the Bank is heavily committed to growing OpEx below the inflation rate, it is hard, as you said because of some characteristics specific to Banco do Brasil but we don't stop there. So we have serious initiatives related to efficiency gains that are taken both at the head office level with the different goals that we implement across the different managers for Banco do Brasil but also at the branch network level.

Next year every branch from Banco do Brasil will see their bottom-line number in a very objective and very easy-to-navigate system. So it will be an instrument for them to aid Banco do Brasil in this pursuit of efficiency.

Q - Marcelo Telles {BIO 3560829 <GO>}

That's great, thank you. Thank you, Gustavo. Just a follow up on your first answer regarding Pronaf impact. If I just apply what you mentioned about flat -- delinquency on the agricultural portfolio to have been flat basically the impact would be around BRL260 million on your NPL, does that sound about right?

A - Unidentified Speaker

I don't have the information of the balance with me but I can definitely check that and our IR team will send that to you.

Q - Marcelo Telles {BIO 3560829 <GO>}

Okay. And I say because if that is the case, I mean if it's more or less BRL260 million or BRL300 million, that's more than like about 40% of your increase in new NPLs would actually be explained by Pronaf, right, which I think it might indicate maybe a better performance (inaudible) than what the numbers you would show?

A - Unidentified Speaker

You are correct on the fact I just have to double-check the numbers.

A - Ivan de Souza Monteiro {BIO 16420543 <GO>}

Yes. So we are going to check the numbers on balance so we will get back to you. So early I mean today in the afternoon.

Operator

Jorg Friedemann, Merrill Lynch.

Q - Jorg Friedemann {BIO 15405752 <GO>}

I would like to discuss some subjects that were not discussed in the Portuguese call. The first one, if you could just give us an up-to-date on the slide 26 that you showed. What would be the core Tier 1 as calculated for September 2013, you show there Tier 1 of 8.55% but what would be the core Tier 1, please?

A - Unidentified Speaker

Thank you, Jorg, for your question. But informally we do not disclose this information. This is the first approach and the first figure that we bring to the market, we are bringing right now but we don't go further on this figure.

Q - Jorg Friedemann {BIO 15405752 <GO>}

And would you have, at least for Tier 1, an estimate of fully loaded basis of Basel III or not yet?

A - Unidentified Speaker

Jorg, the number that you have on slide 26, on that comment there where we show Tier 1 of 8.55%, that is the fully loaded Basel III number. So we are basically taking all off all the capital deduction for the next five years and fully loading them now. So this is the full implementation number for Basel III on total, the BIS ratio and Tier 1. As Leonardo said, we are not disclosing the core capital in this number.

Q - Jorg Friedemann {BIO 15405752 <GO>}

Perfect. And my second question would be in terms of the (inaudible) surplus adjustments that you usually do on the annual basis, just still wondering given that value has appreciated and your mark-to-market in this values by the end of the year if you could offset these gains also with an order up to date of the discount rate to calculate the actual abilities or if probably you will have an increase of the surplus flowing into the balance sheet, thank you.

A - Unidentified Speaker

Jorg, unfortunately, we don't have an objective answer for you. So I'm going to try to make some subjective comments. Yes, one thing that helps the valuation of the fair value of the plant's assets is the recent performance of Vali [ph], that is a plus in our calculations. We don't have the discount rate yet, that is something that we calculate, that we will calculate at the end of December. So at this point it's very hard to estimate what the final impact will be even though one of the main drivers of that number, of that impact in our shareholders equity is the performance of Vali which is positive at this moment.

Operator

Carlos Macedo, Goldman Sachs.

Q - Carlos Macedo {BIO 15158925 <GO>}

I have one question only. Looking at the profitability that you reported this quarter if you exclude the BRL500 million pretax positive impact from provisions your ROA for the quarter would have been somewhere around 0.7%. Now, that's the lowest recurring ROA that I have for you I think going back more than 10 years. If you could talk qualitatively. And we heard a little bit about the operating side for expenses, if you could talk qualitatively about where do you think the ROA can go and what efforts are you making in order to get the ROA to be higher potentially so it could also let your ROE return to the 17% level that you reported last year it will be great, thank you.

A - Unidentified Speaker

Well I'm going to have to provide, as you said, a qualitative answer because we don't have an objective guidance for ROA. So the initiative of course if we look at the revenue side first is the Bank's continued focus on growing in the lower risk segment. So even though we will likely capture because of the mix effect lower spreads will also likely have a smaller impact of credit risk provisions. And that's because if we look at the individual portfolio the most profitable portfolio, the high-growth item in there is mortgages.

The strategy for agribusiness and companies is the same that we have been implementing. So it is always to grow in lines that are backed by collaterals, receivables and guarantee funds. So on the revenue front on the credit side it's the usual strategy from Banco do Brasil. One important driver of the Bank's profitability for the upcoming years of course is fee generation and as we always say we are not talking about adjusting prices on fees we are talking about increasing the -- what we make of touch points with the different clients, that you have more products per client.

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One of the most important items there which is the number one fee generator for Banco do Brasil today is revenues from cards, debit cards, credit cards, the Bank already has the leadership in debit cards and has been gaining market share in credit cards. Specifically using credit cards as an instrument to access traditional credit lines with companies. So card is a clear priority for Banco do Brasil.

Another priority for the Bank on the fee generation front of course insurance. And that's a segment where the Bank has several leadership positions and plans, plans to expand market share in those items. We don't have the guidance for 2014 yet. But we know that we are going to have a strong growth number in our projections for insurance in the next year.

Naturally the other fee generators for Banco do Brasil are asset management and capital market. Specifically in capital markets Banco do Brasil today has, if I'm not mistaken, four out of the five important leadership items in the local league tables.

Moving to the efficiency front, we have many initiatives targeted at containing the OpEx growth number at below inflation. And they are related to process review. As I said answering a previous question, having the branch managers working with us we will provide them better information on how they can control their costs on every front; administrative expenses, risk management, as well in terms of operating losses. So we want to have the branch managers as our partners in this initiative to contain OpEx growth.

So if we look at all of that, Carlos, this is what we think will drive the Bank's profitability and will expand the Bank's profitability in terms of return on assets. What we are seeing now is the impact of a period of contracting spreads with our initiative of efficiency gains not fully loaded yet. But what we foresee for the upcoming years is these types of initiatives gaining traction and then a recovery of profitability.

Q - Carlos Macedo {BIO 15158925 <GO>}

So just a follow-up question, Gustavo, how -- you're not fully loaded on your efficiency push yet. When do you gauge you are going to be fully loaded? Is it something that we should expect for some point in the middle of the next year and as a result we could have this top line pressure for spreads not being offset by the efficiency and therefore we should look for that -- the profitability to resume to the higher level at some point next year rather than in the short term?

A - Unidentified Speaker

Unfortunately I have to give you another qualitative answer, okay, because we don't have the OpEx growth number approved in our budget for 2014 yet. But what I can tell you is that part of the gains, of the efficiency gains will be seen in 2014. But we are confident that throughout 2015 and 2016 you will see a bigger impact of that. At this moment we have a number of initiatives that are being analyzed so that we are able to provide -- to declare internal projects, internal guidance numbers for several items related to efficiency?

Operator

Natalia Corfield, JPMorgan.

Q - Natalia Corfield {BIO 6421991 <GO>}

My question is a follow up on the capital. I understood that you did not disclose the CTI. And is that correct or in am I mistaken?

A - Unidentified Speaker

You are correct, that is not disclosed yet, this is not -- at this moment this is not part of the required regulatory reporting. You will see that on the next quarter, the number we tried to disclose was a number that is in line with the level of disclosure of our peers, that is why we disclosed this number in this fashion.

Q - Natalia Corfield {BIO 6421991 <GO>}

All right. Thank you. Just to make a comment on that. You have your perpetual note that has a trigger that's linked to this CTI. So regardless if our peers -- your peers are reporting or not I think that should be a number that -- numbers you should be disclosing going forward since it's an important measure for your perpetual notes.

A - Unidentified Speaker

You are correct.

Q - Natalia Corfield {BIO 6421991 <GO>}

(Multiple speakers) would appreciate that.

A - Unidentified Speaker

You are correct, the number you are referring to is the 5.125 trigger that we have in our hybrid perp, what I can tell you is that we are not close to this number. And the reason why we're not disclosing this yet is because we wanted to be in line with our peers in terms of disclosure levels.

But you will see this number in the next quarter since this will be a regulatory requirement. So you will see this number and then you can make the comparison. You will be able to make the comparison with the trigger and have the necessary comfort for our bondholders.

One other thing that I have to tell you is that the number that we have on page 26 is the fully loaded number. So once we report the fully loaded number in the next quarter, the fully loaded number should not be compared to the trigger. Even though the fully loaded number will show you a good level of comfort, still that is not the number to be compared with the trigger because most of the adjustments to Basel III are implemented over the next five years.

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Operator

Regina Sanchez, Itau BBA.

Q - Regina Sanchez {BIO 16404038 <GO>}

I have a question in terms of NII, I mean that we saw a sequential increase in the last two quarters. But net interest margin is still slightly compressing, do you believe that with higher SELIC rate and the recent increase in interest rates of some loan portfolios we might be able to see some increasing NIMs during 2014. Then in the short-term or maybe the impact of higher SELIC rate is not necessarily positive as it is in the long-term because most deposits had their cost increasing immediately given that they are indexed to the benchmark rate. But it takes longer for loans to be renewed at the higher rate.

And also if you could give a sense of how much in terms of loan mix I mean growing faster in mortgage and (inaudible) portfolio might also affect net interest margins in 2014. In other words maybe -- do you think we should focus more on net interest margins after provisions risk adjusted NIMs? Thank you

A - Unidentified Speaker

Regina, you're right on the money, once the SELIC, the SELIC rate comes up the immediate effect that you have is the re-pricing of your significant portion of your funding cost, while this effect is translated into higher rates on the credit side over time. Some of the products have a longer duration and it takes a while for that to be re-priced in the portfolio specifically in the fixed installment products like consumer credit. So, yes, there is a delay on the recovery of NIMs on the credit side.

So even though we can't point out to in which quarter we'll see this impact but we think that in the first half of 2014 we're likely to see a recovery of NIMs because of this effect. It is also hard to gauge, Regina, how much of the change in mix will offset that. So looking at the next year when you see products flowing with an adjusted SELIC number as a NIM-positive you will have the change in mix as a NIM negative. It's hard to say what the next effect -- what the net effect will be. But we believe that the net effect will be positive.

Q - Regina Sanchez {BIO 16404038 <GO>}

Okay, perfect. Thanks, Gustavo, for the answer. My second question regarding the expenses, I mean that I really like the evolution in the Third Quarter, especially the decline in personnel expense. But considering the guidance range for 2013 of 5% to 8% growth in administrative expenses we expect that is likely to be more towards the bottom of this range, at least below the mid of this range. And in general terms, what can we expect for 2014, is there any internal goal to grow expenses below or in line with inflation next year?

A - Unidentified Speaker

Well for this year what I can tell you is that it's not going to be as the top but it's likely going to be somewhere around the midpoint, okay?

And for 2014, even though we don't have a stated number yet, we don't have the approved budget for 2014, I can tell you that it is our internal goal to grow below inflation.

Operator

Mario Pierry, Deutsche Bank.

Q - Mario Pierry {BIO 1505554 <GO>}

Let me ask you two questions as well. The first one is related to your loan growth, we saw a sharp deceleration in the growth rates from above 7% in previous quarter to close to 2% this quarter, does this reflect a new growth rate that we should expect from the Bank? Does it mean a change in the strategy of the Bank? And if this is at all related also to your - drop in your Tier 1 ratio.

So my second question is related to your Tier 1, I know there were a couple of questions on this. But last time we saw your Tier 1 ratio below 10% was in 2010 and the Bank proceeded to do an equity offering. If you could then discuss how comfortable are you of your capital ratios, what or if you think that this could limit your growth potential and what measures could you take to improve your capital ratio? Thank you

A - Unidentified Speaker

In terms of capital ratios, yes, we are comfortable with the current level that we are operating at. We have no change in our strategy. What we are seeing is that the projections for our credit growth for 2014 have been revised downwards by the industry and that effect that impacts every bank in this country. In terms of, just to finalize on capital, Mario, at this moment we aren't negotiating, we aren't preparing, we aren't planning any type of capital increase, that you have our best estimate of a Basel III number there on our slide 26 and this a comfortable number for us.

In terms of this recent credit growth, this number was lower than what you saw in the previous quarters because of two effects, first, there is a lower demand for credit in the economy. And second, we are seeing stronger competition, specifically from private sector banks targeting credit with individuals very heavily, most importantly on the payroll items.

Q - Mario Pierry {BIO 1505554 <GO>}

Okay. So let me follow up then. When you say you have no plans for, to do an equity offering. But there are other ways that you could, other transactions that you could do to boost your capital ratio, maybe selling more of BB Seguridade, maybe IPO in the credit card, the card business, or even reducing your payout ratio, are any of those strategies being considered right now?

A - Unidentified Speaker

No, Mario, we have our capital projections, of course. We know of the several initiatives that we may take over the next years but we're not considering reducing our stake at BB

Seguridade, we don't have a plan to IPO our credit card business, our cards business. And we are not considering a reduction in payout.

Q - Mario Pierry {BIO 1505554 <GO>}

Okay. Then just a follow-up on what you mentioned earlier, you said that the 2014 credit growth forecast for the industry have been revised down. But we -- we saw the Bank this year growing above industry trends, should we expect the loan growth next year from Banco do Brasil to be more in line with the industry or should we continue to see the Bank growing at a faster pace?

A - Unidentified Speaker

Mario, because of this changing status of credit projections for next year we don't have a clear answer for you at this moment. We're still discussing what the growth strategy will be for the next year. But of course we are taking these revisions under consideration.

Operator

This concludes today's question-and-answer session. I would like to invite Mr. Leonardo Loyola to proceed with his closing statements. Please go ahead, sir.

A - Leonardo Loyola {BIO 16193219 <GO>}

Thank you for joining us (inaudible) everybody a nice day. Thank you.

Operator

That does conclude Banco do Brasil's conference call for today. As a reminder, the material used in this conference call is available on Banco do Brasil's Investor Relations website. Thank you very much for your participation and have a nice day. You may now disconnect.

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