Transcript of the Conference Call
English
2Q19 Results
July 25th, 2019

Announcer:

Good morning, ladies and gentlemen, and thank you for waiting. We would like to welcome everyone to Bradesco's second quarter 2019 earnings conference call.

This call is being broadcasted simultaneously through the Internet in the investor relations website banco.bradesco/ir-en. In that address, you can also find the presentation available for download. We inform that all participants will only be able to listen to the conference call during the company's presentation. After the presentation, there will be a Question & Answer session, when further instructions will be given. Should any participant need assistance during this call, please press *0 to reach the operator.

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

Carlos Firetti:

Good afternoon, everybody. Welcome to Bradesco's 2Q19 conference call. We have today with us for the call our CEO, Octavio de Lazari, our Executive Vice-President and CFO, André Cano, Bradesco Seguros CEO, Vinicius Albernaz, and our Executive Director and Investor Relations Officer, Leandro Miranda. For starting the call, I turn now the floor to Leandro.

Leandro Miranda:

Hello, everyone. Thank you all for joining our second quarter 2019 earnings review conference call. We are very pleased to continue presenting solid results, despite the many challenges facing the economy. Our business model and team have shown flexibility and excellence to thrive in every single market that we play. We are proud of our accomplishments, and confident that we shall keep this path, as we accelerate our investments in people, technology and services. We would like to thank all of our employees for this outstanding performance and continuous focus on serving our clients and communities. In addition, we have special thanks to our clients who have elected Bradesco as their bank of choice. The economy was far weaker than expected, what led us to lower again our 2019 GDP growth expectation, the increased volatility jeopardize the confidence level of consumption and investment, resulting in tough environment for banking.

Despite the challenging shortage scenario, we are optimist about the future. The pension reform does seem to be on track in the Congress, as it has already been voted and approved with major support in the first round in the Lower House, which may allow companies to finally focus on their long-term goals without being blurred by the micro fiscal uncertainty. Therefore, we believe that investments and growth are likely to resume over the following months. Our astounding performance this quarter came as a consequence of several changes that we have been implementing for quite a while, which allowed us to grow the credit portfolio despite the economic scenario, with excellent credit quality, while maintaining our cost under control, and with a great performance of our insurance operation.

On page 3, we bring some of our financial highlights. First of all, an all-time high net income of 6.5 billion Reais, a growth higher than 25% year-on-year. The operational results grew 11.1% in the annual comparison. Our ROE reached 20.6% in the quarter, an expansion of 220 bps, even with the strong expansion of our shareholders' equity in the quarter that grew 18.2% year-on-year to 133.6 billion Reais. Our expanded credit portfolio grew 2.2% this quarter and 8.7 comparing to the same quarter last year. And the individual's portfolio is a highlight, with a strong growth of 14.8% year-on-year. As expected, credit quality continued to improve, with the over 90 day's delinquency ratio falling 4 bps, confirming our view of Bradesco optimum position for lending. Finally, our Tier 1 capital ratio reached strong 15%, a growth of 60 bps this quarter and 360 bps in the annual comparison.

Moving to page 4, we bring other highlights of the quarter. The first one is the strong growth in the individual's credit portfolio, with expanded 14.8% in the annual comparison. We are gaining market share in different lines, such as personal loans, payroll loans, mortgage and auto financing. We are achieving this growth with excellent credit policy as shown by the new vintages. This growth is a reflex of the commitment and motivation of our teams, as well as the evolution in our processes and models. The second highlight is the acquisition by 500 million dollars of BAC Florida that we have announced in the beginning of the quarter. Our objective with this move is to strength our positioning in the high-income segments, pretty much wealth management, offering to our customer's checking accounts, cards, mortgage, financing and other sources in US. The conclusion of the deal is pending regulatory approval, but we are very confident that it shall come in a very near future. The third highlight is in the MEI segment, which we were the first bank to launch the digital account. Credit origination through digital channels, mobile and internet has an expansion in the first half 2019 growing 53% in individuals segments, and 44% in the company segments. Our checking account customer base continues to expand. In the annual comparison, we grew 1.1 million customers, and this last quarter, 400 thousand customers. Finally, Next reached 1.1 million accounts in the quarter, and we are confident that they shall exceed their target of 1.5 million customers by year-end.

On page 5 and on the next page, we bring some numbers of our operations in the digital arena. As mentioned in the previous slide, Next reached 1.1 million clients and 77% were not Bradesco's clients. We aim to reach more than 1.5 million by the year-end and our CEO is very confident that we shall reach even two million clients by year-end. In Bradesco group, we closed this quarter with 16.4 million digital checking accounts clients, an expansion of 1.9 million in 12 months. As you can see on the next page, BIA - Bradesco Inteligência Artificial, is our artificial intelligence, had more than 144 million interactions and 1.1 million customers through WhatsApp. Credit origination through digital channels in the individuals segment totaled 11.8 billion Reais in the first half, a growth of 53% in the annual comparison. In the companies segment, it totaled 14 billion Reais, a growth of 44%. These numbers show that our traditional banking clients are quickly adopting the digital channels even for credit products.

Turning to page 7, a great pride of ours, Bradesco Foundation is one of the largest educational projects in the world. The Foundation has a budget of approximately 650 million Reais, bringing benefits to more than 92 thousand students with basic education of high quality.

On page 8, we show the value that we add to the Brazilian society. In terms of value added, out of 33 billion Reais, 30% was paid to governments, and 29% to the compensation of our employees. Moving to the financial results of the second quarter, we see here on page 10, the growth of the financial margin in the annual comparison, it was 7.1%, and in the first half, it was 5.6%, close to the center of our guidance. Expanded loan loss provision reduced 3.2% in the quarter to 3.5 billion Reais, remaining on the upper part of our guidance. We are doing really well in insurance operations, with expansion in the operational result of 16.9% in the first half. Our net income grew 23.7% in the first half and the operational result, 13.3%, shows a solid performance of the organization as a whole. We will go into more details on the following pages.

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

On page 12, we may see that our credit portfolio grew 2.2% this quarter, and 8.7% when compared to the same quarter last year. The deceleration of the annual comparisons is mainly due to a larger comparison based in the second quarter 2018. I would like to remind you that, in the second quarter 2018, there was a large expansion in the corporate portfolio, mainly due to the valuation of our currency by 16% and also due to a large transaction of 5 billion Reais that quarter with a great Brazilian company. As highlighted earlier in this call, the individuals portfolio presents a growth of 14.8% in the annual comparison, with highlights to personal loans, which is growing 29.2%, payroll loans growing 22%, car financing growing 17.5%, and mortgage growing 15.9%. It is really an incredible year so far. The good performance of the individuals segment is a consequence of our market positioning, improvement in credit operations, evolution of credit models, with intensive use of data, and our highly motivated sales force. In the companies segments, in addition to the effect of the comparison base that we have already mentioned, the operation suffers from low level of investments by companies, and we understand this line to pick up with improvements in the economy. In the SMEs segments, the growth is also affected by relocation. In the first quarter 19, of approximately 6.7 billion Reais in loans from the SMEs segments, to the corporate segment, as part of Bradesco's new segmentation in companies, which increased the growth in the corporate portfolio and reduced in the SMEs portfolio.

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

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

Turning to delinquency ratios on page 15, you can see that it continued to have positive evolutions in all segments, in line with what we have been pointing out in previous quarters. We still see the possibility of further improvements, but we are approaching the end of the normalization process of the credit cycle. We hope this comes by the year-end. The strong loan growth in the individuals segment reduced room for improvements.

As you can see on page 16, NPL creation increased this quarter, impacted mainly by individuals and corporate segments. In the individuals segments, the impact is related to the growth of the portfolio. Expanded loan loss provision improved to a 3.5 billion Reais this quarter, representing 2.5% of the expanded credit portfolio, the best level ever in our historical series. We still see room for reduction in the provision levels in the coming quarters. However, the expansion in the individual's credit portfolio reduces space for reductions, but should be compensated somehow by a positive impact of the financial margin.

Fees are presented on page 17. The growth in the quarter was 2.6%, and the annual comparison, 1.3%. The checking accounts line has a positive evolution, growing 9.5% in the annual comparison due to the growth in the customer base and evolution of our segmentation. The pressure in fee income is related to cards revenue, which are pressured by the competitive environment on the acquiring business and the reduction on debt cards interchange fees. Asset management revenues, which are pressured by the reduction on management fees, loan operations revenues pressured by a reduction in the volumes of sureties and guarantees. We understand that 2019 is a year of adjustments in this line and we may resume growth in fee income by 2020 with a stronger economy and with an adjusted revenue base. We are positive with Brazil.

On page 18, we bring a table with our operational expenses, which are above the guidance, presenting a growth of 6.2% in the first half. We had an excellent performance on administrative expenses, which grew 3.3% in the first half and 2.2% in the second quarter on a year basis, below the inflation. The performance would be even better if we had not made an anticipation of payments due to discounts, obtained in the negotiation of contracts. It was very positive for the bank as a whole. In personal expenses, we had a growth of 9.1% in the first half. The main pressure comes from the non structure portion, mainly from higher profit sharing provisions related to extraordinary performance program as we continue to make provisions assuming maximum performance and from higher provisions for labor claims. Expenses would be growing by 4.6% if we were to exclude the effects of this payment anticipation, higher profit sharing provisions related to this extraordinary performance program. So, pretty much we believe that we shall keep them below inflation as time goes by.

Moving to page 19, insurance results. We had again this quarter a very good result, with operational results growing 16.9% in the first half and 11.6% in the annual comparison. Bradesco Seguros net income was 1.83 billion Reais, a growth of 1% this quarter and 15.9% in the annual comparison. Insurance premiums grew 3.3% year-on-year, with highlight to health insurance segment, which presented growth in number of customers. Technical provisions totaled 265 billion Reais, expanding 5.2% year-on-year. A few more topics on insurance are presented on page 20. In the annual comparison, net profit in the first half grew 16%, and ROE reached 23.6%. In the second quarter, overall claims ratio had an increase and reached 72.5%, but still lower than the same figure in the second quarter of 2018. The best way to see it is on a semi-annual basis. The main impact on the ratio was caused by health segment, mainly due to the lower impact in the first quarter as a consequence of Carnival in the end of quarter and due to the higher quantity of business days in the second quarter. For a better comparison, as I have pointed out, we should consider that first half total claims ratio is reduced from 74.4% in the first half 2018 to 70.5% in the first half 2019. We are confident that claims ratio will have a better performance in 19 than in 2018.

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

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

Announcer:

We will now initiate the question and answer session. If you would like to ask a question, please dial *1. If at any point your question has been answered, you may remove your question from the queue by pressing *2. Our first question is coming from Mr. Tito Labarta, with Goldman Sachs. You may proceed.

Tito Labarta:

Hi, good afternoon, thanks for the call. A couple of questions… first, in terms of your asset quality… it continued to improve and cost of risk improving. You said you can improve a little bit further. You did mention that NPL creation increased a bit in the quarter, so I am just trying to understand the dynamics there a little bit… you know, if you do see some further improvements, how much and when does it revert? So, what you think about the cost of risk, you know. How much lower can you get it and what some more normalized level as a year progresses? And then, my second question is in terms of fee income. You know, the continuous fee pressure in the clients and asset management, and also the collections. Just curious… particularly I guess in the card income that we did see as slight pick up in the quarter… do you think most of the pressure has subsided from the acquiring business? I mean, we saw Cielo volumes were up a bit yesterday… do you think the pricing pressure has now subsided to… it makes it more comfortable than the card fee income business? Thank you.

Leandro Miranda:

Tito, thank you very much for your questions. First, on the asset quality, we are pretty much pleased with the growth that we have had in individuals and SMEs. That pretty much represents the healthier possible portfolio that we could have. And when you compare our provisions levels, you're going to see that pretty much we are decreasing the provisions either in relative or absolute terms. That means that the new vintages are by far better than the old ones. So, we believe that the asset quality is improving and it shall continue this way at least for until year-end. Regarding to NPL creation, we see that the provisions for an amount higher than the 90 days is going… it's improving dramatically, and the volumes, we do not see them growing in the individuals and SMEs when you compare to a relative analysis. And so, therefore, we understand that we shall get more and more alpha when you compare the return of these two portfolios, when you compare to the provisions. So, we understand that this spread is pretty much there to stay. Regarding to fees, we can make some sort of split here among the three issues that you have pointed out: Cielo, asset management, and underwriting. First of all, on asset management, we had an adjustment in the management performance fee, but mainly on management fees due to the decrease in the base rates of the country, right? So, pretty much, most of the portfolio was comprised of fixed income funds, and therefore, the management fees should be adjusted to the new reality of interest rates in the country. Now, we are changing the mix more and more into equity funds, to "Fundos Multimercados" that are hybrid funds, including debt and equity, and we expect the management fees to stay there, in fixed income, and to have an improvement in management fees to those new asset classes. And, as the environment in the country is getting a lower return in interest rates, we understand that clients will get eager to get higher returns and that new base of investments. With underwriting, we also benefit from a stable economy, as we shall see more and more IPOs, more and more equity and debt offering. And again on Cielo, we understand that they have the right strategy, we understand that they have said that they are there for dominance, they are willing to keep their market positioning, and therefore, they have made sacrifices and they are increasing their sales force. We are positive with their strategy and we provide full support to the senior management.

Tito Labarta:

Ok, thank you, it is helpful. Just a second follow up on the asset management fees, would be expected further reduction in interest rates, that's already priced in you think or it could be a little bit more pressure?

Leandro Miranda:

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

Tito Labarta:

Ok, thank you.

Announcer:

I would like to remind you that, to ask a question, you just have to dial *1. Our next question is coming from Mr. Jason Mollin, with Scotiabank. You may proceed.

Jason Mollin:

My first question is a follow up on fees. So, I get that the lower rates to put pressure on asset management fees. But can you talk about competition and new entrance for asset management, and could that be another leg of pressure on fees? And we´ve see your checking account fees actually growing in the first half of 19 versus first half of 18 by almost 8%. We´ve (27:41) seen some new entrants cutting, offering free accounts. Do you think that we could see pressure there as that has been one of the saviors to get to this 2% growth after the first half 19, almost 2%, first half 19 versus first half 18? And then maybe we also talk about… it is a smaller number, but what is driving the growth in the consortium management fees? Thank you.

Leandro Miranda:

Thank you, Jason, for the questions. Well, let us start from your first one that is regarding to the asset management fees, right? We believe that we had some pressure from our competition the last two years, pretty much because we were one of the leaders in this industry, so they presented new funds with adjusted management fees. We were in the process of making the adjustments. Right now, we have made all the adjustments when compared to the whole competition. We have this database and this intelligence, and we do it on a weekly basis, so we do not see that we are lacking in sort of that competitive features right now. We believe that we are ready to grow, and our management fees shall not decrease any longer. We expect that we shall have a new flow of funds to be managed by Bram, especially because of the interest rates scenario that we have in the country; we have seen how much domestic investors are active and how much retail has been coming more and more important, especially when you see the brokerage houses movements bringing high networth individuals to this game. Regarding to checking accounts, Octavio has made this point earlier that the way we see it is that we shall present competitive packages to every single client of ours, but always taking into account their profile, their needs. So, we believe that those fintechs, or new competitors… when they enter into the market, they are not providing all the full service, all the full package that we present. So, in this sort of market, we have been more competitive. And a very good example of that is that, for the first year in a row, we have been able to grow in the traditional platform the number of net accounts, so pretty much we are having more and more clients in our branches, in our traditional bank, as well as in our native digital bank. If we are prepared to loose clients for any native digital bank, we shall be losing to Next, but our experience is not showing that. Our experience is showing that we are growing in both. Both platforms are very strong, and they are trying to serve better and better our clients; that is the reason why we are confident that we shall keep on growing. Regarding to pressure on growth, we believe that, as the economy gets back on track, we shall see clients get more and more banking services, and we are very well positioned, as you could see in the first semester, not only to get market share from state-owned banks, but also from the other private-held banks. So, we are positive with this scenario and, as Brazil gets the level of growth that everybody is expecting, we shall be there on a very leading position.

Jason Mollin:

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

Leandro Miranda:

Ok. First of all, we all used to think that technology would eliminate jobs, and experience has proven the other way around. Technology allows us to have different jobs, different revenue streams, and allows us to serve our clients even better. And that is what our focus is; our focus is on our client. So, digital channels have allowed us to grow our clients base even faster, have allowed us to grow to serve our clients with better products and in creating leverage to the managers in our branches to be focused more and more on investments and on new businesses. That is where we think the technology will drive us. Technology will not only drive us to reduce our fixed cost, but mainly to improve revenues and to get more and more competitive.

Jason Mollin:

That's helpful, thank you.

Leandro Miranda:

Thank you.

Announcer:

Once again, if you would like to ask a question, please dial *1. Our next question comes from Mr. Nicolas Riva with Bank of America. You may proceed.

Nicolas Riva:

Thank you for taking my question. One question on income taxes, if you can remind us where we are in terms of the approvall in Congress including income taxes of the banks. When do you think this is going to be into effect, and also, what would be the impact on your capital from the one-time adjustment of your net deffered tax assets? Thanks.

Leandro Miranda:

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

Carlos Firetti:

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

Nicolas Riva:

Ok, thanks, Carlos. I want to understand the amount…because there was some reference in Bloomberg I guess from your Portuguese call, about 6 Billion Reais, and…

Carlos Firetti:

Oh, yes. Basically from the increase… sorry… from the increase in the social contribution, if it happens from 40 to 45, there is a revaluation of tax credit, and the value of this revaluation will be 6.4 billion Reais. Our amount of tax credit increases 6.4 billion Reais. There is no impact on BIS from this revaluation.

Nicolas Riva:

Thanks very much, Carlos.

Leandro Miranda:

Thank you all… we are finishing the call.

Announcer:

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

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

Announcer:
Thank you. Then, that concludes Banco Bradesco's conference call for today. Thank you very much for your participation. Have a good day.