

Banco ABC Brasil | Investor Relations
Transcription of 4Q19 and Full Year 2019 Earnings Conference Call
February 07, 2020

[Anis Chacur – CEO]

Good afternoon ladies and gentlemen and thank you for joining our conference call for the fourth quarter and year of 2019.

On slide 2, the main highlights of the quarter and of the full year of 2019:

The Expanded Credit Portfolio ended December 2019 with a balance of 30.1 billion reais, presenting an increase of 6.8% in the quarter and 14.9% when compared to the same period in 2018.

The Loan Portfolio once more presented a solid performance in the quarter, growing 13.2% in relation to the previous quarter, and 32.5% when compared to the same period in 2018.

The Accounting Net Income reached 145.6 million in the quarter, an increase of 11.6% versus the previous quarter, and 78.1% when compared to the same period in 2018. In 2019, the Accounting Net Income grew 26.4% when compared to 2018.

The Recurring Net Income reached 119.7 million Reais in the fourth quarter of 2019, a reduction of 2.7% versus the previous quarter, and of 1.5% in relation to the last quarter of 2018. In the year, the recurring net income increased 6.8% when compared to 2018.

The Accounting Annualized Return on Equity reached 14.6% in the quarter and 13.7% in the full year of 2019. The Recurring Annualized Return on Equity reached 12.0% in the quarter and 12.6% in 2019.

The Investment Banking presented record revenues in the fourth quarter and in the full year of 2019, reaching 46.2 million Reais and 113.5 Reais, respectively. On an annual basis, revenues grew 27.8%.

On slide 3, we compare 2019 actual figures with the Guidance for the year:

In February 2019 we announced a guidance for the Expanded Credit Portfolio annual growth between 11% and 15%

With the first half of 2019 presenting economic activity below initial expectations, and with the demand for credit still timid, we decided to announce in August 2019 a revised guidance for the year, with an annual growth between 6% to 10%.

As mentioned in our third Quarter Earnings Conference Call, in that quarter we started to experience a significant change in the overall market demand for credit. This trend continued during the fourth quarter, resulting in a annual Expanded Credit Portfolio growth for the year of 14.9%, very close to the top of our initial guidance.

Regarding the guidance for Personal and Other Administrative Expenses, we indicated in February 2019 an annual increase between 4 to 6%:

We closed 2019 with an increase of 7.4%, slightly above the top of our guidance.

This expense growth above the guidance was influenced by the anticipation of some of our new initiatives, including: the offering of new products and services, such as the Equity Capital Markets, Project Finance, Energy Trading, Writs of Payment Trading and mainly, the anticipation of our expansion in the Middle Segment, both in the geographic expansion to other cities, as well as in the expansion of our target market, with the inclusion of clients with annual sales starting from 30 million reais.

All those initiatives resulted in higher personnel, technology and marketing expenses, as compared to our initial estimates in the beginning of 2019.

On slide 4 we present the evolution of the expanded credit portfolio.

We would like to highlight once more the positive performance of the Loan Portfolio, which grew 13.2% in the quarter, and 32.5% in the year. This performance was a result of a relative improvement in the credit market environment.

Even considering the reduction in Guarantees issued, the strong growth in the Loan Portfolio contributed for a solid performance of the Expanded Credit Portfolio, which grew 6.8% in the quarter, and 14.9% in the year.

This performance was above the revised guidance announced in August 2019, of a annual growth between 6 to 10%, and close to the top of the range announced in the guidance announce in the beginning of the year, of between 11 to 15%.

We also present the performance of the Expanded Credit Portfolio broken down by segment:

In the Large Corporate segment, the Expanded Credit Portfolio grew 3.7% in the quarter, and 3.4% in 12 months.

In the Corporate segment, growth was 10% in the quarter and 30.8% in 12 months.

Finally, the Middle segment grew 12.2% in the quarter and 17.1% in 12 months.

On Slide 5, we show a comparison between Banco ABC Brasil and the Brazilian Financial System in terms of the Corporate Loan Portfolio growth on a quarterly basis.

We observe that, starting in March 2019, the Bank started to present a loan growth rate considerably above that of the Brazilian Financial System, and that, from September 2019 onwards, we started to experience an improvement in the demand for credit on all segments in which we operate.

On slide 6, we discuss the evolution of the Middle Segment:

We launched the Middle Segment in May 2019, initially restricted to the São Paulo Metropolitan Area, with the support of 10 newly hired officers.

After confirming positive initial results, we decided to anticipate in October 2019, the second expansion wave, moving in two fronts:

expanding geographically, by entering into 7 new cities – including the interior of São Paulo, Rio de Janeiro, Belo Horizonte and the South of Brazil – and

by expanding our target client base, starting to serve clients with annual sales from 30 million reais, down from the previous lower limit of 100 million Reais

This second expansion wave included hiring 16 new officers.

During the first half of 2020 we expect to launch the third expansion wave, which will cover additional cities, and shall include hiring additional 25 officers.

We closed 2019 in the Middle Segment with a total of 166 clients, out of which 82 with credit exposure, and an Expanded Credit Portfolio of 785 million Reais.

We believe that the Middle Segment will significantly contribute, not only in terms of loan growth, but mainly in terms of a positive impact in the financial margin for the coming years.

On slide 7, some highlights on each segment.

In the Large Corporate Segment, we ended December with 414 clients, out of which 237 with credit exposure, resulting in an average ticket of 58 million Reais per client. The Large Corporate portfolio ended the quarter with an average term of 361 days.

In the Corporate Segment, we ended December with 1,097 clients, out of which 793 with credit exposure, resulting in an average ticket of 15 million Reais per client. The Corporate portfolio ended the quarter with an average term of 480 days.

Finally, in the Middle Segment, we ended December with 381 clients, out of which 255 with credit exposure, resulting in an average ticket of 3 million Reais per client. The Middle portfolio ended the quarter with an average term of 270 days.

On slide 8, we discuss asset quality:

The first chart shows Credit Transactions Overdue 90 days, which ended December accounting for 1.0% of the portfolio, a reduction of 0.2 percentage point in relation to the previous quarter, confirming the strong asset quality of the credit portfolio

The second chart shows Loan Loss Provisions Balance, which ended December 2019 accounting for 2.5% of the loan portfolio, a reduction of 0.1 percentage point compared with the previous quarter.

On slide 9, we continue with the discussion on asset quality:

In the first chart, Loan Loss Provisions Expenses reached 47 million reais, equivalent to an annualized cost of credit of 1.2% in the quarter.

It is important to highlight that the increase in provisions versus the previous quarter is mainly resulted from the growth of 2 billion Reais in the loan portfolio. Moreover, the cost of credit continues close to 1% and is in-line with the figures observed throughout 2018 and 2019.

In this sense, the increase in Loan Loss Provisions does not indicate a deterioration in the quality of the loan portfolio, fact that can be confirmed (i) with the improvement in the NPL ratio, as observed in the previous slide, as well as (ii) with the decrease in loans rated between D to H, which we will discuss now. Therefore, this is a provision of credit growth.

In the second chart, the evolution of Loans rated D and E-H:

Loans Rated D ended December at 1.6% of the portfolio, while the balance of Loans Rated E-H ended at 2.6%.

Both the portfolio rated D as well as the portfolio rated E-H improved in the quarter, as a result of the maintenance of a high quality credit portfolio.

On slide 10 the evolution of our funding.

By the end of December, our total funding balance reached 30.1 billion reais, an increase of 2.3% in the quarter, and of 8.1% in 12 months.

Liquidity remained high and properly priced. The quality of funding continues to be one of the cornerstones of our business.

There is no asset-liability mismatch. The bank presents a positive liquidity gap in all future terms.

On slide 11, the evolution of the Shareholders' Equity and BIS Ratio.

We ended December 2019 with a Reference Equity of 5.4 billion Reais and a Shareholders' Equity of more than 4.0 billion Reais.

The reduction of Common Equity in the quarter is a result of the growth in the Loan Portfolio, which was more significant when compared to previous quarters.

We closed the quarter with a BIS Ratio of 16.89%, comprised of 14.04% of Tier 1 capital – broken down into 12.53% of Common Equity and 1.51% of Additional Capital – and 2.85% of Tier 2 capital.

We highlight that 100% of the capital is Basel 3 compliant.

On slide 12, we present the evolution of the Net Interest Income:

The Net Interest Income reached 258 million reais in the quarter, a decrease of 1.6% quarter-over-quarter and an increase 7.9% year-over-year.

Comparing quarter-over-quarter, the impact of two SELIC rate cuts on the Remuneration of the Shareholders' Equity was partially offset by the solid Loan Portfolio growth. On a year-over-year basis, there was an increase of 3.8% in relation to 2018.

The Shareholders' Equity Remunerated at CDI rate reached 44 million reais in the quarter, a decrease of 20% quarter-over-quarter, and 6.5% year-over-year. Comparing 2019 with 2018, there was an increase of 12.6%.

The Financial Margin with Clients reached 164 million reais, an increase of 4.5% quarter-over-quarter and 6.1% when compared to the same period of 2018. On a year-over-year basis, there was an increase of 3% in relation to 2018.

The Financial Margin with Market reached 50 million reais in the quarter, flat quarter-over-quarter, and an increase of 33.4% in relation to the same period in 2018. Comparing 2019 with 2018, there was a decrease of 1.9%.

The fourth quarter of 2019 had an Annualized Net Interest Margin of 3.4%, a reduction of 0.2 percentage point in relation to the previous quarter, and stable in relation to the same

period of 2018. In 2019, the NIM reached 3.4%, a 0.2 percentage point reduction in relation to 2018.

On slide 13, the evolution of the Financial Margin with Clients and Spreads:

Regarding the Margin with Clients, we can observe that the increase in the margin was mainly driven by the increase in the average volume of the Loan Portfolio in the quarter.

In the second Chart, the evolution of Spreads with Clients. The healthier credit environment experienced throughout 2019 impacted the level of spreads. However, this movement was offset with a higher volume of credit.

On slide 14, the Service Revenues.

Service Revenues reached 96 million in the fourth quarter of 2019, an increase of 22.1% quarter-over-quarter, and of 5.1% year-over-year. On an annual basis, there was a reduction of 3.7% in 2019 versus 2018, resulted from the Guarantees Issued, which was partially offset by stronger revenues from the Investment Banking.

In the second Chart, the share of Service Revenues as percentage of the Total Revenues. In the fourth quarter of 2019, Service Revenues accounted for 28.7% of Total Revenues.

In relation to our Investment Banking, we would like to highlight the growth in Capital Markets origination volume, which in 2019 increased 84% when compared to 2018.

On slide 15, the expenses and efficiency ratio.

Personnel and Other Administrative Expenses experienced an increase of 6.5% quarter-over-quarter and 9.4% year-over-year.

When comparing 2019 with 2018, there was an increase of 7.4%.

The Efficiency Ratio reached 36.6% in the fourth quarter of 2019, stable in relation to the previous quarter, and an increase of 1 percentage point when compared to the third quarter of 2018.

In 2019, the efficiency ratio reached 37%, an increase of 1.2 percentage points in relation to 2018.

On slide 16, the profitability.

Recurring Net Income was 120 million in the fourth quarter of 2019, a decrease of 2.7% quarter-over-quarter and of 1.5% when compared to the same period of 2018.

In 2019, the Recurring Net Income increased 6.8% in relation to 2018

The Annualized Recurring Return on Equity reached 12.0% in the fourth quarter, a reduction of 0.5 percentage point in relation to the previous quarter and 1.3 percentage point in relation to the same period of 2018.

In 2019, the Recurring Return on Equity reached 12.6%

On Slide 17, our guidance for 2020 e 2021.

Looking now on our future, we decided to disclose a guidance both for 2020, as well as for 2021, in a way to provide the market a 2-year horizon that captures the evolution of our initiative, especially, the Middle Segment.

Regarding the Expanded Credit Portfolio Growth, our guidance for both 2020 and 2021 are of an annual growth from 11% to 15%. This view results from a business environment more prone to asset growth. It is importante to state that the pace of growth in Loan should be stronger than the pace of growth of the Guarantees Issued.

We have also decided to provide a guidance related to the size of the Expanded Credit Portfolio of the Middle Segment, reaching between 1.4 billion and 1.6 billion by the end of 2020 and between 2.2 billion and 2.5 billion by the end of 2021, resulting in a composed annual growth rate of 67% to 78%.

Regarding the guidance for Expenses - including Personnel, Other Administrative Expenses and Profit Sharing – our guidance for 2020 is of an annual increase from 14% to 18%, and for 2021 of an annual increase from 6% to 9%, resulting in a composed annual growth rate from 10% to 13%.

These figures already capture the increase in expenses related to our new initiatives, in addition to the Middle Segment, which include: Equity Capital Markets, Project Finance, Energy Trading and Writs of Payments Trading.

In summary, we are confident in our business model, in the new initiatives and in the healthy credit environment which fosters growth. Thus, we should continue to generate positive results to our shareholders.

These were the main figures to be presented. Now we remain at your disposal to answer possible questions you may have.

Thank you!

[Q&A]

[JP MORGAN]

Hi Anis, thanks very much for the opportunity of making questions. I have two questions. The first one regarding NII for 2020, I know you don't have a Guidance for NII but, should we expect NII growing ahead of loan volumes, loan loss volumes... My point is, as you said credit should grow more than guarantees, so that should help a little bit more in the NII, and also you have the mix shift towards Middle that should also benefit NII. But on the negative side, we have also have low interest rate in Brazil, and some spread pressure, so just trying to see how the moving parts will hit your top line, that's the first one. And a second question is regarding your ROE, again, I know you don't have a guidance for ROE, but just a trend, should we expect given the high investments maybe your cost to income and ROE coming down in 2020, and maybe accelerating back in 2021. That should be a trend that the management is expecting? Just to get a qualitative color would be nice.

[ANIS]

Hi Yuri, how are you, thank you very much for your question, here is Anis. First of all, regarding the NII, we don't have a guidance for NII, but I can give some color regarding this issue. As we mentioned, we are expecting higher growth in the loan book than in the guarantee book, as a consequence, this should represent an improvement in the NII with clients, and a reduction in the income with guarantees. So, the NII with clients should be benefited by the growth of the loan book and also by the growth of the Middle market, which is more aggressive than the average loan of the total loan portfolio of the Bank. Regarding the low interest rates, the only aspect that we are affected in terms of the reduction of the Selic rate, is the remuneration of the Equity of the Bank, this is the main point. So this is totally representative in the NII of the remuneration of the Equity of fourth quarter 2019. And for 2020 we are expecting the Selic rate in the level that was announced around 4.25%, so this should be the effect. But apart from the remuneration of the Equity there isn't any specific major influence in our results. Regarding the ROE, with the initiatives of the Middle market, this is something that will make some impact in the return of the Bank for 2020, 2021 mostly. In 2020, we will be having some initial costs as we are having now, but more intensive to develop the initiative, either in terms of technology, in terms of back office, and in hiring of officers. As the portfolio grows, the income will come, but this growth of portfolio will take a while to achieve its mature size. In a way that profitability should be reduced or negatively impacted in 2020 because of this, and should be positively affected showing the outcome of the business provided that you have a good execution. Where in 2021, where you'll reach a visible size of the portfolio, with the spreads that you're seeing in controlling the level of the cost risk, having all the costs in terms of OpEx and CapEx in the activity. Then we should expect for 2021 a better profitability because of the initiative of the Middle market being concluded. So, summarizing your two questions, better NII should be seen because of the fact that we are growing the loan book in a higher speed than we are doing with the guarantee book. ROE, not so brilliant for 2020, but much better for 2021 when you'll have finished all of this starting process of the Middle market.

[HSBC]

Hi, good morning. First of all thank you very much for providing a good us a good guidance for 2020 and 2021, it's very useful. I have two questions, one is regarding tax rate that you expect for the coming two years I don't think that's part of the guidance. Second, in terms of asset quality in the Middle market you actually have 0% NPL, isn't that too little? Are you not taking more risk in the segment? Thank you so much.

[ANIS]

Hi Carlos, here is Anis, regarding the tax rate, I'm here with Borejo our CFO, he can explain to you.

[BOREJO]

Hi Carlos, thanks for your question. Regarding tax rate, probably, I mean, of course it's not a Guidance, it's hard to say but I would say is an increment the Social Contribution rate, should be probably ten or twenty bps higher than our historical rate, okay?

[ANIS]

And the second question, regarding the NPL for the Middle market so far, so far it's a new portfolio, and as a new portfolio, and also in a benign credit scenario that we are living, puts this outcome. For sure, the NPL should increase but the Middle market that we are expecting in terms of cost of risk, for sure is as higher cost than the Corporate or even the Large Corporate. But we are not thinking about having a Middle market with high spreads and high cost of risk, our spread are around 6% to 10% per year, the cost of risk so far is good because the environment for credit is benign. Time will pass, we'll have some deterioration but no too high. It should be higher than the 1% per loan that we see in our Corporate segment. But everything totally controlled and giving a substantial improvement in terms of profitability iof the Bank, in case we manage to conclude the way we are expecting.

[HSBC]

Thank you Anis, a little follow on, on the tax have you said only 20 or 20 basis points higher or...

[BOREJO]

I said a 100 to 200 basis points, sorry.

[HSBC]

Okay. Alright, thank you so much.