Y 2021 Earnings Call

Company Participants

- Jose Marcos Ramirez Miguel, CEO & Proprietary Board Member
- Rafael Victorio Arana de la Garza, Chief Financial & Operational Officer
- Rene Gerardo Pimentel Ibarrola, Deputy MD of Corporate Banking
- Tomas Lozano Derbez, Head of Corporate Development, IR, Financial Intelligence, M&A and Sustainability
- Unidentified Speaker, Unknown

Other Participants

- Brian Flores, Analyst
- Carlos Gomez-Lopez, Analyst
- Daer Labarta, Analyst
- Ernesto Gabilondo, Analyst
- Geoffrey Elliott, Analyst
- Gilberto Garcia, Analyst
- Gustavo Schroden, Analyst
- Jason Barrett Mollin, Analyst
- Jorg Friedemann, Analyst
- Jorge Henderson Cubillas, Analyst
- Nicolas Riva, Analyst
- Olavo Arthuzo Duarte, Analyst
- Ricardo Alonso Garcia, Analyst
- Rodrigo Ortega, Analyst
- Unidentified Participant, Analyst
- Yuri Fernandes, Analyst

Presentation

Tomas Lozano Derbez {BIO 20387400 <GO>}

Good morning. I'm Tomas Lozano, Head of Corporate Development, Investor Relations and ESG. My best wishes to everyone in this New Year. Welcome to Grupo Financiero Banorte Fourth Quarter Earnings Call.

Our CEO, Marcos Ramirez, will provide a brief macro overview followed by the main highlights of the quarter, including the performance of the loan portfolio and positive evolution of asset quality, an update on the COVID-19 impact for our insurance business as well as a quick review of what to expect in our next annual report that will be published in March.

I would like to take this opportunity to mention that this year, we will launch an additional document, a shorter and hopefully convenient reference for our analysts and investors that will provide a brief summary of our ESG strategy, including progress under each ESG topic, main key performance indicators, as well as the short and medium-term milestones that will lead to our long-term objectives.

You will receive more information regarding this release date soon.

After our CEO's presentation, Rafael Arana, our COO and CFO, will provide further detail on our updated sensitivity to rates, improvements to our cost of funds, details on some extraordinary expenses during the quarter as well as the results of our JV with Rappi as we concluded the first year of operations.

We will then proceed with the Q&A session.

Please note that today's presentation may include forward-looking statements that are subject to risks and uncertainties, which may cause actual results to differ materially.

Thank you.

Marcos, please go ahead.

Jose Marcos Ramirez Miguel {BIO 1967010 <GO>}

Thank you, Tomas. Also, I would like to take this opportunity to wish everyone a healthy and successful New Year. Thank you for joining us today.

The last quarter of 2021 ended with continued signs of recovery for the Mexican economy. However they were somewhat shadowed by the rapid effect of the new Omicron variant of the COVID-19 virus. Its higher contagion rates have been partially offset by less severe health complications. More than 57% of the Mexican population has been fully vaccinated, and close to 8% has had a booster dose, thus significantly reducing hospital occupancy and mortality rates.

Although these surge in contagion many still caused some headwinds for the country's economic activity, we expect progress on supply chain issues and resilience in consumption to offset this effect. GDP growth for 2021 totaled 5.7% and our expectations came to approximately 3% growth for 2022, fueled by relevant employment gains, which have already offset the job losses broken by the pandemic as well as by solid remittances, which are likely to continue sorting in 2022 after reaching a MXN 51 billion record in 2021.

Inflation remains as one of the most important issues for the economy, reaching 7.4% in 2021. However it is expected to gradually decline during the second half of 2022, to end the year around 4.5%, supported by a more restricted monetary policy from the Central Bank. The most recent decision in December took the reference rate 50 basis points higher during the year at 5.5%.

Our economic analysis team expects another similar hike in February, followed by a steady 25 basis increases at the end of each quarter or end at 7% in 2022. We believe this rate levels will contribute to a solid margin evolution at the bank. Rafa will provide deeper insight into this in a moment.

On the political front, we expect to see active campaigns from parties and candidates at six state governorship will be up for election in June. On the legislative agenda, attention will be centered on the constitutional reform to the electric sector, and the potential introduction of a reform to reorganize the National Guard under the Ministry of Defense.

Key projects for the current administration will likely be inaugurated such as the Dos Bocas refinery and Santa Lucia Airport.

Moving on to the bank's operation. After nearly two years of remote work for most of our corporate office personnel, we are convinced that a permanent hybrid-working scheme is the new way to work.

Banorte's strength relies in our human capital. Therefore, we have implemented important changes to provide a convenient, attractive and flexible work environment that maximizes productivity while fostering talent retention and attraction. Depending on the nature of their job functions, some people will return to the office full time, while some others will follow a hybrid mode, working remotely between two or three days on average.

To accommodate business team, we have remodeled offices based in our corporate offices with convenient layouts that adapt well to the new mobility requirements. Less frequent commutes, which also had a positive impact for the environment, which is also a key priority in our strategy. Meanwhile, in an effort to ensure the safety and wellbeing of all our teams, we will continue working from home until contagion rates are down.

Now let me highlight the main quarterly results, which show a solid performance of the group, supported by an improving margin, a strong fee activity, healthy asset quality, and a shielded balance sheet, which points for a stronger start of 2022.

Starting off with profitability. Slide 4. ROE for the group is still impacted by unpaid dividends and high COVID-19-related claims in our insurance business. However claims are expected to gradually return to pre-pandemic levels during the second half of the year. As we will see later on, ROE of the bank unaffected by these factors is already above 19%, driven by better NII, solid asset quality, and growth in fees.

On Slide 5, NII is already incorporated the effects of earlier reference rate increases despite still being pressured by high insurance claims. Noninterest income had a favorable result, driven by strong key activity during the quarter, led by higher credit card activity from the holiday shopping sector -- season and a strong core banking fees.

Looking in greater detail, Slide 6. Net fees show a relevant increase during the quarter and the year, already showing the effects of the economic recovery and higher mobility. The accounting reclassification of these based on external sales forces into the same plan had a more evident effect on net fees during the quarter.

Loan growth on Slide seven shows better trends in corporate and commercial portfolio during the quarter. While mortgages and consumer were clear growth leaders throughout the whole year. A last few couple of the years for corporate and government loans was further impacted by large prepayments during the quarter, which results slightly lower-than-expected total loan growth for the year.

Asset quality, Slide eight was one of the most positive results throughout the year with NPLs standing the year below the pandemic average. During the quarter, some specific cases were written up, paving the way for a clean track in 2022.

Analyzing the results by subsidiary, Slide 9, the insurance business continues to stand out among the rest. We built high claims from COVID-19 cases in the life and medical expenses portfolios and are returned to normality in the current insurance sector, resulting from higher mobility in the country. Therefore the business had a good performance during the quarter. And as previously announced, it will be impacted in 2022 by the fee reduction initiatives implemented by the regulator.

Slide 10, we provide greater detail into the insurance business, showing a steady quarterly growth in premium origination. However the impact of the size in claims, which are expected to gradually recover the pre-pandemic level during the second half of the year, as I said.

Switching gears to ESG. I would like to mention that we have gathered comments and suggestions from our investor base and following the best international practices, we will be including additional disclosures in various ESG topics in this year's annual report, which will be published at the end of March.

Among other updates on the disclosure of information on the governance side, you will find many of details regarding our work composition. I still make (inaudible) rated insights into each member's professional background, the value contributions to the Board, and how this aligned with the group's corporate strategy.

On the environmental side, we will show short-, medium- and long-term goals that will mark the path towards achieving a net zero alliance rate (inaudible) . On the social pillar, we will disclose our diversity targets, as well as short and medium-term plans to reach them. In particular, you will see milestones to increase the number of women in senior management positions and to promote salary equality.

We will also provide metric to show our progress in nondiscrimination practices and diversify training through our personnel. Furthermore, we will reveal our financial inclusion results for 2021 and what we expect ahead. In addition to this, we will publish our first TCFD report. And going forward, we will keep reporting our climate risk exposure and a strategy using this TCFD recommendations.

On the sustainable finance pillar, we are currently working on a sustainable product rollout on the consumer, corporate, and SME segments that will align to sustainable development KPIs.

As a final note, many investors have been inquiring about our reaction to the announcement regarding the sale of Citibanamex' retail operations in Mexico. At this point, I can tell you that it's our duty to make a full assessment of this opportunity. If we find that the potential transaction could be additional value for our shareholders then it will be for them to decide.

With this, I conclude my remarks. And now Rafael Arana will provide further details in our bank sensitivity to rate increases, as well as efficiencies in cost of funds and asset quality. He will also provide us an update in our JV with Rappi, and will walk you through our 2022 guidance, which shows double-digit net income growth for the year. Rafa, please, go ahead.

Rafael Victorio Arana de la Garza {BIO 1982204 <GO>}

Thank you. Thank you, Marcos. I would like to go -- as Marcos mentioning some of the elements of the -- that we will be trying to achieve and are already included on the guidance.

As Marcos mentioned, we are -- we continue to protect the balance sheet the best as we can. I think we have been doing a good job on the balance sheet, on the capital side, on the liquidity and everything on the key metrics that really allow us to have a very comfortable position on the capital base and also on the liquidity.

As Marcos mentioned, on the fact about the expenses because there have been some comments because we commit to the market that our guidance wasn't going to be 4% to 4.6% on the expense line. And basically, we ended up well above that even though we ended up below inflation. There's a reason for that, and it's a reason because we consider because the inflation ended the year above 7.4%, that we needed to protect the expense line for '22.

So we've decided to advance basically on the severance payment side because we are reducing 2% cost on the personnel expenses. We decided to front load that in December, and also based upon the guidance that we have on the inflation, I'm talking with several providers. We also anticipate payments to them in order to secure prices in that part. So what you will see in this year because obviously the lagging effect of inflation will still -- the pressure in the cost line is that we -- that will be basically be on a downward trend through the year.

For the year, we will be having a 7.2%, 7.4% for the expense growth, but trending down on at the latest part of the year. We needed to do that because of the lagging effect of the inflation side. So basically taking that into account, we also see that there are several improvements on the basic metrics of the bank and also at the group. If we follow the, as Marcos mentioned, the return on equity for the bank as we guide the market last year, 3.25% [ph] to basically end the year above the 19% return on equity for the bank.

We ended up 19.2%. If you go to a current and take away the expense line that we anticipated that number should have reached the 22.4% for the year. As Marcos mentioned, the net interest income of the bank continues to grow quite nicely in every single part of the line. So we continue to see a very good trend on that part. The return on assets also is a good story. We are already above the 2%, 2.1%. If you exclude the extraordinary payments that we did in December, the bank ended the year at 2.5% on return on assets. So a good story on the return on equity and the trend that we -- that we promised the market.

The net interest income closing a good recovery trend. The return on assets also is now above the 2% for the -- that we will -- when we go to the guidance, what we expect for the year. The new expansion for the year for the bank has been on a constant basis above 6%, and now we ended the year at 6.4% for the NIM of the bank.

This is the effect of a much better mix, reduced cost of funds that we will talk about that in a minute, and also the impact of the repricing on the portfolio. So what we expect for that the number that we ended the year will be basically the number that we will be anticipated as an average for the full year, which peaks around 6.5%, 6.6% in some of the months of this year.

The net interest margin of the group, as Marcos mentioned also, we continue to see the effect of the claims on the insurance business, but also we have seen a much better trend on the Third Quarter and the Fourth Quarter on the buildup of technical provisions that allow us to pave that, as Marcos mentioned, we will get to a more normal number by the end of the Second Quarter. The growth in sales and premiums as we saw continues to be quite strong. So structurally, the business is in a very good trend, and the technical reserves and claims are now starting to level off.

If we move to the asset quality piece, that I think has been a very good story and has to do with how do we have managed the process during the pandemia, things that are relevant to that is that there has been many questions about the cost of risk that we are looking at 1.3%, what would be the normalized cost of risk. And as you know, Banorte has always been running the cost of risk as the number is around 2%. We think that we are reaching a new normal on that part because all the efficiency in the models on the onboarding models and every on the collection process on -- so we now are looking at numbers more on the 1.6% to 1.7% on a recurring basis. And also the NPLs that we have been also reaching very good levels on the -- during the year.

We also see that, that also will be a reduction in the usual trend that the bank loans that part of the portfolio through numbers more on the range is around 1.7%, 1.8% [ph]. So asset quality, a very good story, and it's relevant to say it here that we've decided not to release provisions as we have talked to many of you during the several meetings. So MXN 1.8 billion are still on the balance sheet because we haven't decided to release those provisions because of the new variant that came in place, that's the Omicron.

So we still have MXN 1.8 billion provisions that are ready to be released as we need through the year and also relevant to mention that we've decided to also clean up part of the commercial portfolio during the Fourth Quarter. So we decided also to use around MXN 700 million of those provisions to clean up part of the commercial portfolio. So we faced the year with a very strong asset quality portfolio that is ready to grow. We have seen some good trends as you saw on the numbers of the growth in the loan book that show us that the trend that we saw in the third and Fourth Quarter will continue into the first and Second Quarter of the year, and a much improved for the third and the Fourth Quarter.

The coverage ratio that we have is also reaching record limits around 191%. As you know, that number usually we won [ph] the bank around 135% and 140%. So that also will be a downward trend, but a very, very slow downward trend in that part. Another commitment that we guide the market also is that we needed to accelerate the reduction in the cost of funds. We started the year around 38% of cost of funds considered and set as the reference rate, and we ended up 38%. So it was basically the result of a much improved mix on the demand deposits, the non-bearing demand deposits really reach record also record levels.

So now we have a mix of 72% of demand deposits and 28% of time deposits. For the cost of funds, will continue to be a priority for us in '22. So we are aiming to reach as you see on the graph, our benchmark competitors [ph] are still below us. But now we are in an accelerated trend to reach those numbers. There also have been many questions about the sensitivity on the balance sheet. As you can see in the graph, that number in the Fourth Quarter reached the MXN 1.1 billion [ph]. That number will eventually reach the MXN 1.3 billion [ph] in the local currency. And also you see the effect on the foreign currency that we have on the balance sheet.

So -- so this is also the resources of very active ALCO that is protecting the balance sheet, and we are as sensitive, and we have a positive gap in the -- in the increase in rates that we have seen in this part. Now I turn to the line that has got many of the questions about investors and analysts, what happened with the expense line. Basically, as I mentioned before, is the result of what we've decided to front load in December to basically the severance payment that we knew we needed to pay in '22, we anticipate those that is really 2% of the personnel expenses. The other thing that also was basically, as I mentioned before, everything related to -- provide us that we needed to also lock the prices in those goods.

And we think that we need the right thing in order to balance out the living effect of inflation. So that's the result of that 7%. If you strip that, we will be right on target for the 4.2% as we mentioned to the market. But we decided to front load those and that had the effect, as we saw in that we do not comply with the guidance that we gave you at the beginning of the year. Those are the reasons that we didn't comply for that.

The other thing that has been also be quite important is everything that is related to the capital ratio and dividends. As you see on the graph, we are reaching 24.7% of total CAR and core Tier 1 at 15.3%. Those numbers are well above our commitments to the market that is 12.5 and 41 [ph] well above any requirements concerning TLAC or anything that is related to any buffer that regulatory pieces.

So I anticipate the question, so when the dividends are going to be paid out or whatever. There's also -- we are waiting for the latest results of the stress test, and we hope to have an answer for you. I know this has been a recurrent -- we don't know. We don't know. Sorry, but that's what everything that I can tell you at this point in time that we are doing anything -- everything that we can in order to provide all the information required by the regulator to allow us to comply with the payments that are pending to the market on that part.

And also, I would like to anticipate another question that is going to be present on this is anything, anything on the possibility, and I'm just taking exactly the word that Marcos mentioned that after looking everything that we see on a potential interest in the transaction on everything, then is for the shareholders to decide also what could happen on the dividends concerning a potential transaction.

So we don't have, at this point in time, anything that we can clear you, because we don't have any information related to when we're going to be able to pay the dividends or what's going to happen with that information that has been running around the market around the Banamex potential transaction. So if I just report to you the Rappi information, and I would like also (inaudible) mention anything of this is -- on Rappi, we are right on target what we promised the market, the 400,000 active cards on that part. So we are where we want it to be, and we have learned a lot from that business.

We feel confident that for this year, we will evolve a lot more in the acquisition cost and a lot of metrics that we can present to you. We expect to present to you those metrics at the end of the First Quarter, much more clear metrics about platform Rappi. What we can tell you at this point in time that everything that we commit to market about the 400,000 cards and are now on five and active as we -- as we promised with you and we decided to go to the joint venture on this. I don't know, (inaudible), if you want to add anything in there. So that has been a good story, and we hope that will continue to be a good story. We are learning a lot about managing those type of operations that are basically digital operations.

So now I jump to the guidance. The guidance, as you see, we are expecting a loan growth of 7% to 9%, and this is based upon the trend that we saw in the third and the Fourth Quarter. NIM expansion, we expect 30 to 40 basis points. The expansion at the bank level, we hope to have 45 to 65 basis points. The expense growth will be 7% to 7.6%. Even this inflation now is aiming to be -- to end the year around 4.4%. We think that the lagging effect of inflation will still be present through the year.

Several efforts will be put into the expense line to control that as much as we can. But at this point in time, this is the number that we can provide to you. We will see a change in that. We will immediately guide the market of changes for the expense growth. The efficiency will trend again more to the 40%. That is the number that we want to be, 40% or below 40%.

Cost of risk, as we mentioned, we think we reached a new normal. So we are guiding 1.6% to 1.9%, but we think that the normal will be more than the 1.6%. Tax rate, 26% to 27%. In this point, I also want to clarify that there was a -- and because of inflation accounting principles, there was a result that we put into the group on the net income results because we have an effect of inflation that would reduce the payment on taxes for the month of December.

That not just happened for Banorte, it happened for all the banks because of inflation accounting principles on that part. So most of that benefit was that we anticipated on the cost line. The other thing that we would like to guide is the net income. We expect net income to go to MXN 39.5 billion to MXN 41.1 billion [ph]. I know it's a wide range, but at this point in time, is what we see because there's some -- during the release of provisions from insurance will happen and also the Omicron will stay a bit. So we need to release provisions at a faster pace.

Also, I would like to go to the return on equity for the group. The return on equity for the group will be reaching the 17% to 18% in that part. This is considering that we are able to pay the dividends that are pending. The return on equity for the bank will reach 21% for the year. Return on assets for the group, 2.2%, and return on assets for the bank will be above 2.2%.

GDP, we expect GDP to be at the top of 3%. I think it would be a little below that, but that's the GDP that we have from an economic area. So inflation rate from 4.2% to 6%, I think the lagging effect will be an issue for the year. That's why we are anticipating that expense growth. The reference rate on average that we are using for the budget is 6.4% for the year.

With this, I conclude my remarks, and I pass the word to Marcos.

Questions And Answers

A - Tomas Lozano Derbez {BIO 20387400 <GO>}

Thank you, Marcos and Rafael. Now we will continue with our Q&A session. (Operator Instructions)

We are now ready to start the Q&A session. We will take our first question from Jorg Friedemann.

Q - Jorg Friedemann {BIO 15405752 <GO>}

Thank you very much for the presentation, Marcos, Rafa. I have two questions. Let me start with the first one, with the first one. I know that you are in a position that it's very difficult to anticipate anything, but I think it's the most important theme for discussion with investors, which related to your interest that already stated on the acquisition of the available assets in the market. I understand also that you cannot give too much ideas. But let's talk about just a plan of ideas. In case you already stated that you have the interest. So how we should proceed in terms of dividends if the government authorizes you, the regulator authorize you to pay off higher dividends? It's fair to assume that we're going to be more conservative in terms of dividends until you have a decision about the potential transaction. This is the first related question to the team.

And also related to that, if you anticipate any issues in terms of antitrust, I know that in terms of loans, you would be probably -- they're aligned with the market leader, but there are also other segments that I think might be of consideration of the authorities such as the IFRS [ph] for instance.

And the last one in terms of the guidance, just wondering what you already considered at the end of the day to come up with the guidance in terms of the GDP growth because as Rafa anticipated in the question, you believe that it could be a bit lower. In our case here at Citi, we work with less than 2%. So just wondering how much accommodation we could have in the guidance for lower GDP. We are particularly concerned here in the potential impact that could have in terms of loan growth and also in terms of expenses. Expenses, actually, we did not understand that much. Why so high if you already front-loaded a bit of the expenses, but just a consideration here.

A - Jose Marcos Ramirez Miguel {BIO 1967010 <GO>}

Jorg, thank you very much for your questions. I will start with the first one. We will continue talking with the authority, with the CNBV and (inaudible) all these, we want to be ready to pay the dividend. So as soon as we can do it, we will do it. We want to continue with the business as usual. Then we will evaluate the other assets that you call it in due time. That's what we are going to do.

Now we will continue to work fast and nothing is going to stop us. The second place, antitrust, I don't know. We still don't know the asset that we will, don' know anything. So if we are responsible to answer that.

And the third one, yes, you're right, we were discussing before is not (inaudible) is to come true because this is let's all it done all that in the last week. I believe like that but the guidance, we will keep it the same. So don't you worry about the that number, we know about that we use and our guidance remains the same.

A - Rafael Victorio Arana de la Garza {BIO 1982204 <GO>}

And if I may add, Jorg, to what you mentioned about expenses. The rents that you see in the loan growth from 7% to 9%, assumes that if you have a push down on the GDP, it will be more around the 7% down than on the 9%. But based upon the dynamics that we are seeing in the market, and also the opportunity to have been presented, as you saw, we have been gaining market share on a permanent basis. On that part, and we continue to do so now because the market is growing faster, but we can achieve a better growth than the market based upon how we can really tending to the clients, and how we can really serve the clients with the capital base that we have. And now we are -- we're very present also in the (inaudible) group but it's also giving us additional growth.

On the expense line, you're right on that, but you have to take into consideration that even we anticipate a reduction of 2% on personnel expenses. The main effect of the inflation will be basically in wages. So that will hit you at the beginning of the year and stay with you for the year. So many other efforts will come from many other parts, even if we already front-load the severance payment on that part and part of the growth in some of the suppliers.

We also anticipate that other parts of the cost line will also move. We are really putting this number around the 7%, taking into consideration that as we see the lagging effect of the inflation will continue but we also are looking to many ways to try to reduce this. So I agree with you based upon all the efforts that we did, that number should go down. But once we get that, we will communicate to the market that we are already in a downward trend on a much faster pace than we anticipated, Jorg.

Q - Jorg Friedemann {BIO 15405752 <GO>}

Perfect. With lower GDP, I think probably it would also make sense to work in the lower range of this OpEx guide as now?

A - Jose Marcos Ramirez Miguel {BIO 1967010 <GO>}

Yes. I agree with you.

A - Tomas Lozano Derbez {BIO 20387400 <GO>}

We will now take the next question from Ernesto Gabilondo from Bank of America.

Q - Ernesto Gabilondo {BIO 16384492 <GO>}

My first question is on the potential acquisition of Citibanamex. As you mentioned, you are analyzing the potential transaction for your shareholders. However at first glance, where do you see the key operating and funding cost synergies?

Then my second question is also related to the potential Citibanamex transaction and dividends. Can you remind us what is the excess capital level at the group and at the bank is reducing it to an internal minimum of 12%, 12.5%. I just want to double check if this excess capital is around $2.1 billion?

Then finally, my last question is on the Afore Banamex. Citigroup's press release is not mentioning to sell Afore Banamex. However if it is in the package, would you like to analyze it? Or do you think it's too big for you considering that you already own the largest Afore in Mexico? If analyzing it, don't you think it could delay the approval of the COFECE, the antitrust commission for the Citibanamex retail business? Any touch on this will be very helpful.

A - Jose Marcos Ramirez Miguel {BIO 1967010 <GO>}

Ernesto, thank you. I will start with the second question, which is the excess capital at the group. It's around MXN 52 billion should be around that level that's our excess capital. And again the number one and number three, you know better than we do. We are talking about this concentration about the approval of the regulator of COFECE, the synergies. We are still here in the step 1, which is trying to analyze if we are going to analyze to see it. So it's too early to say anything about that. Sorry, but that's the right question, the right answer. Thank you.

Q - Ernesto Gabilondo {BIO 16384492 <GO>}

So let me just make another question about your guidance in terms of the provision charges. You mentioned that you have a stock of provisions of around MXN 1.8 billion that you can be relating during 2022. But your new cost of risk guidance, is it considering it or not?

A - Rafael Victorio Arana de la Garza {BIO 1982204 <GO>}

Yes. We are considering that we will start to flow some of these provisions. We don't know exactly how much, but that's why the range goes from steady 9.5 to 41 on that. So that Ernesto is not fully depending on what part of the range you are. But we think that we -- based on what we saw on the -- we have seen on the Omicron, we think we will start to release those provisions through the year, and that will put us on the high end of the range.

A - Tomas Lozano Derbez {BIO 20387400 <GO>}

We will now go with Tito Labarta from Goldman.

Q - Daer Labarta

A couple of questions also. First, following up on the cost of risk and provisions. Thinking about in terms of what kind of assumptions do you -- are implies for like NPLs. Do you expect some deterioration from here? Do you expect to go back to pre-COVID levels? When does that begin to happen if it does? Just some color on the asset quality that you're assuming for the cost of risk guidance that you gave?

Then second question, if you can give any color on expectations for fees, good quarter for fees there. Do you expect that trend to continue in 2022?

A - Jose Marcos Ramirez Miguel {BIO 1967010 <GO>}

Thank you, Tito. (inaudible).

A - Rafael Victorio Arana de la Garza {BIO 1982204 <GO>}

Yes. I will start and I would jump to Jose [ph] to complement on this. As we mentioned, the cost of risk, we think we reach normal on the cost of risk. So the number should be more on the 1.6% based upon all the origination processes and collection improvements that we have put in place. So now we feel more confident around the 1.6%.

That I think will be the new normal on the -- for the banks. Some months, you will have a lower and upper. But that I would -- I think that should be our goal, and I will in a minute as (inaudible) to complement on that.

On the fee side, you should expect double-digit growth on fee side. But if you saw what happened on the trend on fees, I think we have been achieving a pretty good rate of growth on that.

So we feel confident to go into double-digit growth on the fee side based upon all the growth that we have and not just on the digital is that -- that's very important because we are also becoming extremely active also at the branch level, on the opening of new accounts, and things on those type of services and also an improvement in the number of services that we can provide for the SME. So we feel confident to have double-digit growth also on the fee side.

A - Jose Marcos Ramirez Miguel {BIO 1967010 <GO>}

On my behalf, Tito, I will add just that asset quality ratios are well under control, better than originally forecasted in our budget and way better than our stressing scenarios for 2022, they have converged to pre-COVID levels or even better, as you have seen on annualized, but to loan ratio decreased from 1.2% to 1% during the Fourth Quarter '21, and still below 1.7% pre-COVID on the First Quarter of 2020. I will also add that we maintain available that MXN 1.8 billion that Rafael was talking about, provisions built up on were MXN 5 billion, as you remember. By 2021 year-end, we have used just MXN 2.1 billion of those provisions and significantly below our original projections.

Due to new COVID variants, we decided to keep MXN 1.8 billion because pandemic dynamics will have us very expectant to analyze vaccination rates, infection rates, COVID-19 virus in patients and so forth. We entered this dynamic that is very well known for all of us. But at the end, at the bottom line, I would say that sooner or later, the credit process quality equals asset quality, and that's -- that's the reason behind was Rafael was commenting on reaching about a new normal of cost of risk.

We remain very confident that we can maintain the cost of risk below previous historic levels based on what we have experienced in the last two years.

A - Tomas Lozano Derbez {BIO 20387400 <GO>}

If I could have just a quick follow-up. And first, just on the NPL. So I mean at that 1% NPL level, I mean it seems -- how long can it stay there? Do you expect to see some deterioration? I mean I get the cost of risk will be below historical levels, which makes a lot of sense in these NPLs. But any color in terms of the deterioration that you could see? Do you go back to historical levels? Or the NPL ratio also remains fairly low given the levels that we see now? Then -- and I have one more follow-up on this fees, if I can? Yes. Yes. I guess I see it's more kind of related -- because a lot of the growth in fees that came from the electronic banking. I don't know if the JV with Rappi is contributing at all to that. Do you expect sort of like the digital initiatives to help also the fee income growth? Now that Ubank [ph] is public, they're growing quickly in Mexico, I think they've mentioned close to maybe 1 million cards in Mexico. How do you see sort of that competitive dynamic and then your ability to grow your digital initiatives and potential benefits to fees from that?

A - Rafael Victorio Arana de la Garza {BIO 1982204 <GO>}

On the NPLs, as (inaudible) mentioned, we reached a new normal also to don't expect us to go to the 2%, 2.1% pre-pandemic levels. So I think we will also be in the range of 1.6% to 1.8%. Note that we speak deterioration, but we expect growth basically on the consumer lines. As you know, the credit cards and all those products demand initially a lot of buildup on provisions and things, but we don't expect and we are extremely happy with the performance of the portfolio and the quality of the portfolio that we have at the bank.

So we now know exactly how to manage those acquisition and onboarding process that are much better level that we had before because all the buildup and information that we have put in place for the internal models that the bank has.

So that's have a very important characteristic of Banorte that the (inaudible) models that we have on the onboarding side are proved to be extremely, extremely predictable and also the recovery unit that Banorte has, and I think has always been a benchmark in the industry is also a point a lot more analytic techniques to prevent any deterioration and tailored solutions for the clients. So that's the reason, the reason for that.

On the other thing, no, Rappi hasn't put any on the fee side at all. If you see the -- I think the game with Rappi, and (inaudible) complement on that is how do we manage the acquisition cost and how we improve that acquisition cost in order to reach the breakeven as soon as we can. We think that we have a pretty good handle on the business right now, and we can project that. But I think (inaudible) can also add more to that.

A - Unidentified Speaker

So thank you, too. We have not -- the Rappi deal is not providing any feet to this -- to the numbers that you have seen. And as Rafael is saying, the way we see it is as much as we can control our expenses and we can translate that efficiency to the customer, we can be able to grow the number of customers and to reduce the customer acquisition cost and the cost to serve.

As you know, Rappi has in Mexico, close to 9 million customers transacting. So there's plenty of information that we can reach. Although as you can -- as you saw in the numbers that Rafa presented previously 1/3 of our customers are new to a credit card. So it's good news for both sides.

A - Tomas Lozano Derbez {BIO 20387400 <GO>}

We will now take the next question from Jorge Henderson from Santander.

Q - Jorge Henderson Cubillas

My question is related to the Rappi joint venture. I was wondering if you could share with us the NPL ratio and the loan portfolio size of the Rappi JV and RappiCard. And also if you have any updates or color you could share with us regarding the launch of your new digital bank, that would be highly appreciated.

A - Jose Marcos Ramirez Miguel {BIO 1967010 <GO>}

Thank you, Jorge. Rafa?

A - Rafael Victorio Arana de la Garza {BIO 1982204 <GO>}

Look, Jorge, as we mentioned, we -- I think we need to wait for the First Quarter to go to the numbers on NPL. You know that the roll rates, and the curves of acquisition, and risk needs to stabilize. I think we have a much better view by at the end of the First Quarter on that part. But what I can assure you is that the first three months were challenging for the venture. Then we took control of collections and took control of risk origination and things. And now we feel quite at ease of what we see on the trends on the risk side, but we will rather wait for the First Quarter to provide to you. Then the second one, the digital bank.

A - Unidentified Speaker

Thank you, Jorge. On the digital bank, we are already running tests, pilot tests with friends and family. Obviously we cannot move any kind of money until we have a final approval from the authorities. So we are expecting that process, as you know, the process implies two steps.

The first step is the license in paper and then a certification process. So we're expecting that to happen the first part in the First Quarter. But as far as it concerns to us, we are close to be ready and with the application and all the products that are going to be served in the first minimum viable product.

A - Tomas Lozano Derbez {BIO 20387400 <GO>}

Thank you, Jorge. Now we will go with Nicolas. I'm assuming is Nicolas Riva. Nicolas, can you confirm your last name. Nicolas?

Okay. We will then go with Jason Mollin from Scotia.

Q - Jason Barrett Mollin {BIO 1888181 <GO>}

Yes. Can you hear me?

A - Tomas Lozano Derbez {BIO 20387400 <GO>}

Yes. Perfect.

Q - Jason Barrett Mollin {BIO 1888181 <GO>}

I have two follow-up questions. First, on the guidance for the 2022 ROE outlook. If you can talk and I think Rafa, you mentioned that this assumes the dividend payments. But can you just again clarify what are those dividend assumptions?

Then my second question is also a follow-up on the Rappi JV. You mentioned, you learned a lot, and I think you mentioned certain points here and there, but maybe you can just be more explicit on what have you learned from the JV at Rappi? Is it really the cost focus that you're mentioning? Or is there anything else on both the positive or not so positive side?

A - Jose Marcos Ramirez Miguel {BIO 1967010 <GO>}

Close to Rafa and second (inaudible).

A - Rafael Victorio Arana de la Garza {BIO 1982204 <GO>}

Yes. The -- what we are implying for the return on equity of the -- of the group, Jason, is that we're going to be able to pay MNX 34 billion of dividends to the shareholders.

Q - Jason Barrett Mollin {BIO 1888181 <GO>}

Very clear.

A - Rafael Victorio Arana de la Garza {BIO 1982204 <GO>}

Thank you.

A - Unidentified Speaker

Thank you, Jason. On the Rappi side, plenty of things that we have learned personally, I can tell you that I keep learning every day on how this business moves different than the traditional credit card in the bank. But I will highlight a couple of them. First, on the risk side, the different models that we are using, and we're implementing and moving forward with loan and growth strategy has been very useful also for the bank. I mean it's something that we are learning in Rappi and it's improving, and then we can implement it also here in the bank.

And the second one is how the customers -- remember, when we started this, we were telling you that we can connect the three flows, the information flow, the financial flow, but also the physical, the product flow. We are learning and if the customer leaves a tip, then he's a better payer.

If the customer acquires such products then he prefers to be communicated in different ways. So we are learning -- we are testing and learning how to contact better with our customers and moving towards a personalized offering.

A - Jose Marcos Ramirez Miguel {BIO 1967010 <GO>}

Let me add just something you have to because I think it's also relevant because of many questions that we have received. Also, I think when you find this type of organizations, everybody is like very (inaudible), they feel very attractive to the -- what the fintech was --

but when you try to match those with the banking principles like collections, accounting, shock prevention, risk metrics and things, you think in addition of what (inaudible) mentioned that you need to have a very, very stable and solid back-office operations and very flexible front office operations. That combination is what makes these joint ventures feasible to succeed.

If you don't apply all the regulatory processes and all the discipline in the back office process, you lose a lot of money in the front office. So when you do that in combination, very flexible, very customer-oriented very, very innovative front office but with a very, very, I would say solid back-office operations, then you really start learning that that's the way to go into the market and the client appreciates that a lot.

Q - Jason Barrett Mollin {BIO 1888181 <GO>}

Very helpful. Rafa, just -- I mean is it -- in the MXN 34 billion dividend that you mentioned to be paid, is that -- is the assumption that, that's paid on average throughout the year? Like would you say just that will be paid in the middle of the year to calculate that? Or how are you forecasting?

A - Rafael Victorio Arana de la Garza {BIO 1982204 <GO>}

I think to anticipate that would be before the middle of the year will be that we have information about the regulator that we don't have. So we are looking at least at the middle of the year and then start paying at the middle of the year, the dividend.

A - Tomas Lozano Derbez {BIO 20387400 <GO>}

We'll take the next question from Nicolas Riva from Bank of America.

Q - Nicolas Riva {BIO 20589225 <GO>}

Can you hear me well?

A - Tomas Lozano Derbez {BIO 20387400 <GO>}

Yes.

Q - Nicolas Riva {BIO 20589225 <GO>}

Okay. Great. I apologize for that. So I have three questions. The first one on Banamex. Can you tell us in the case that you were to acquire the retail business of Banamex? I would assume, of course you would do an equity offering. Is there a minimum level of CET1 and total capital that you would like to run the bank with after a potential acquisition of this business? That's my first question.

Second question, completely different topic. IFRS-9, I understand it will begin to be implemented in Mexico starting January 1. It's going to apply to all the banks. Can you tell us what would be the impact on capital at the time of adoption? And also the impact on provisions for loan losses on a quarterly basis going forward?

And more generally, I mean so far, you have been reporting, of course the NPL ratios as any bank. I understand, now you will have to report the loans in three different buckets, Stage 1, 2 and 3. How should we think about that new reporting compared to the NPL ratio that's been reported so far?

Then the third question on your AT1 bonds, you have perp, which is callable in July. I assume this has already been prefunded with your most recent provisions back in November, but if you can confirm that?

A - Jose Marcos Ramirez Miguel {BIO 1967010 <GO>}

Thank you, Nicolas. I will start for the third one, the perp one, is callable in July.

Yes. We can confirm you that we are planning to pay it in July. The first one, of any assets that we could buy anyone, at least we should have a minimum level of 11% to 11.14% [ph] our duty is a strong Banorte and that is I cannot tell you anymore because I don't know when. I can tell you that we have this line or any asset (inaudible)

And the second one, Rafa is what?

A - Rafael Victorio Arana de la Garza {BIO 1982204 <GO>}

That's the second one. (inaudible) It doesn't have a -- but please, (inaudible), go ahead.

A - Unidentified Speaker

Yes. IFRS 9, we have been measuring each and every month in the last half year of what the impact is going to be. I can tell you that as of now, at the close of December is -- everything remains equal, the impact will be MXN 746 million. As you know, lifetime horizon provisions for credit on Stage 2 will take place. And not given default will change also.

So the total impact of loan provisions will be charged to capital, not profit and loss. That's very important for you to know. We will make our numbers by the end of January. But we have been considering the impact of the credit portfolio, the derivatives portfolio, and the leasing operations. So we have -- we remain very confident that this is not going to be a big impact for Banorte.

A - Rafael Victorio Arana de la Garza {BIO 1982204 <GO>}

And also (inaudible) that we are on our way. While we said 11.4%. If you remember when we did the acquisition of Interacciones, we reduced the capital numbers to that number.

Then immediately rebound to the 12.5%. That is the number that we like to have. But as Marcos mentioned, we are willing to go as low as 11.4% for any asset on that part.

Q - Nicolas Riva {BIO 20589225 <GO>}

And Rafa, one thing, when Marcos before said excess capital we have right now is MXN 52 billion, which were like $2.6 million. In that case, are you using the minimum level of 11.4% or the 12.5% for CET1?

A - Rafael Victorio Arana de la Garza {BIO 1982204 <GO>}

The 11.4%, Nicolas.

Q - Nicolas Riva {BIO 20589225 <GO>}

And one last follow-up for Gerardo. You said the impact of IFRS 9, did you say MXN 746 million. Did I hear that correctly?

A - Rene Gerardo Pimentel Ibarrola {BIO 18270892 <GO>}

Yes. That's in the current portfolio. But if you add the impact on leasing operations and also derivatives, the number will go up to MXN 1.4 billion.

Q - Nicolas Riva {BIO 20589225 <GO>}

Okay. That will be a positive impact on capital to be taken directly a positive impact on capital?

A - Rene Gerardo Pimentel Ibarrola {BIO 18270892 <GO>}

It will be a capital deduction.

Q - Nicolas Riva {BIO 20589225 <GO>}

A capital deduction. Okay. All right.

A - Rene Gerardo Pimentel Ibarrola {BIO 18270892 <GO>}

Yes. Yes.

A - Tomas Lozano Derbez {BIO 20387400 <GO>}

Thank you. Now we will go with Alonso Garcia from Credit Suisse.

Q - Ricardo Alonso Garcia {BIO 20354965 <GO>}

I actually have two questions. My first -- if you could provide some details on your loan growth. I mean how are you seeing growth for the year by segment. And just to clarify there, if you are -- if this includes some credit card loans from your RappiCard JV? Or I mean just to understand how this JV is going to be accounted in your growth?

And my second question on the insurance side. I mean is it possible for you to quantify the impact on insurance claim in 2021 from the pandemic? And how much is embedded in your 2022 guidance? I mean I know it's hard to estimate how much you will have this year because it's hard to know how the pandemic will evolve. So just to understand how much is embedded currently in your guidance, and your guidance for margin expansion.

A - Jose Marcos Ramirez Miguel {BIO 1967010 <GO>}

Thank you, Alonso. Let's see the first one. The mortgages around 8% to 9%, payable accelerating to 5% to 6%, our loans rate 7% to 8%. Credit cards still gone around 5%. Commercial more aggressive in customers were like 5% to 6%; SME still cautious, 2% to 3%; government 2% to 3%; (inaudible) continue to participate in this, and on corporate we will see should be around this level. So all this because we have a lot of (inaudible) this deal should be around 7% to 9% loan growth around that.

And talking about the impact of insurance claims from COVID, I will ask (inaudible) around there.

A - Unidentified Speaker

Yes. Marcos, thank you. Well first of all let me tell you that the trend is good in the insurance sector. For instance, let me just mention some things. I will go to the question. But for instance, the retail products that we sell to the branches, last year grew 13%, and also those -- also the insurance, which is embedded in the credit products grew 12%. So the fundamental and the more profitable products. I think the business is doing well, as (inaudible) mentioned in the introduction.

I should mention that the reduction in this year, net earnings with respect to the previous one, which was 43% was due mainly, of course because of COVID, but also we had an impact in insurance business due to the interest rates because, as you know, we fell mainly short-term products, and therefore, we had an impact because of reduction in interest rates during the year.

And that impact was around net earnings around MXN 500 million. The difference to explain the result was due to COVID. Now let me mention, first, how was the behavior of the number of claims and also of the losses within the year. To explain this, what we did -- and we took the average of the claims and of the losses previous to the pandemic. Then we compare to what we observe in 2020 and 2021. Let me just refer to 2021. We're not taking that much time. But for instance, in terms of claims in the First Quarter, we have a 25.2% more claims than the average previously to this pandemic.

In the Second Quarter, it do a little bit -- well, let me go by quarter, 25.2%, and then we have -- in terms of losses, 48% more losses and with the average of previously to the pandemic. In the Second Quarter, in terms of claims, it was a little bit higher, 25.9%. And -- but the -- since the average claim was lower, we had a reduction in the losses and it was only above previous to the pandemic at 47%. By the Third Quarter, we had a reduction in this number from almost 26% of the previous quarter to 22.4%, and also a reduction in the losses with these numbers of -- it went down from almost 47% to 40%.

And by the Fourth Quarter, we observed that the number of claims above the average of the previous recovery levels was at 16%, but the loss -- and the loss ratio had also a very important reduction in respect to the previous quarter because it was only above the normal levels by 28%. So the trend is good. So far, what we have seen, of course it's more volume. But so far, what we have seen in these weeks of January, which is, of course very soon to tell. And remember that we're in the mid of the peaks of the number of people that have COVID in the country. So we will be perhaps be affected a little bit because of the volume because it's a very high volume, more infectious than previously.

But on the other side, if you look at some leading indicators that is the number of claims, and also looking at what happened in the -- in the line of business, which is the health part of the business, we do not see that much increment in serious cases due to COVID. So of course there's a lot of uncertainty, but we are projecting that we will keep going down with a number of claims and at the (inaudible) level, we will go a level down to the previous ones. But as Rafa mentioned, I mean we are making a conservative assumption, and we're making a reduction which is not very (inaudible) because we have a lot of uncertainty.

So I think we will have more to say next quarter. And certainly, I think that what has been mentioned is that very likely and everything else the same, of course. And Marcos has been mentioning in some other places, if nothing else so that is not -- hopefully, we will not see another variant or something that will change fees. So I think that we will level up by the second -- Second Quarter of this year.

A - Jose Marcos Ramirez Miguel {BIO 1967010 <GO>}

And Also, if I just add to what I think Fernando perfectly the good evolution of what we see. If you go to the budget on the insurance side, we are assuming a very conservative net income growth that you saw last year that we have a reduction to close to 50% in net income. For this year, we are only considering at a 40% growth on the issuance side. So we are still, as Fernando mentioned, very conservative about this. If we see a much better trend we will guide you the evolution of that. But that's -- at this point in time, we are being conservative with the insurance business, but very confident in the evolution of business on the sales side.

Q - Ricardo Alonso Garcia {BIO 20354965 <GO>}

Perfect. And just a last follow-up on the RappiCard loans, will they be booked in your balance sheet or maybe book aside?

A - Rafael Victorio Arana de la Garza {BIO 1982204 <GO>}

No. They will be on an independent booking. Once we decide exactly how the joint venture is going to act if we will have -- as you know, now it's 50-50, so we don't -- we don't consolidate that, but we will present that as a part of the investments in place that we have. We receive some e-mails asking us to repeat the guidance by product. So mortgage is around 9%; payroll, 6% or better than that; auto [ph] (inaudible), around 8%; credit cards still recovering above 5%; commercial, around 6%; and in the corporate and government, we will see recovery this year, and we are not giving a specific guidance, but we should continue to see recovery as we continue.

And the other question is that, yes, just to be clear, this is even considering a lower GDP. We just received these two questions, and I want to be very clear about that.

A - Tomas Lozano Derbez {BIO 20387400 <GO>}

Now we will go with a start from Gustavo Schroden from Bradesco.

Q - Gustavo Schroden {BIO 17051676 <GO>}

Can you hear me?

A - Jose Marcos Ramirez Miguel {BIO 1967010 <GO>}

Yes. Perfectly.

Q - Gustavo Schroden {BIO 17051676 <GO>}

Okay. Well I have two questions then. The first one is still related to your guidance. Can you give us any color regarding which lines are you more comfortable? Then do you think that we should work at the high end of the guidance and which lines you are less comfortable? Then we should work at the low end of guidance. Any color on that would be great.

And my second question is as a follow-up on this potential lower GDP. I'm asking that because we have received many questions from investors regarding this potential weaker GDP. Here at Bradesco BBI, we're already working with a 2% GDP. So we are below your numbers.

And you are very comfortable saying that in your guidance, although you showed 3%. You think that the bottom line and the evolution of the business would be at the same even considering the lower GDP. So my question is definitely lower GDP, we should see some impact on the loan growth, and asset quality, operating expenses, and fee income. I mean so which lines do you think could be impacted at most in a lower GDP, and which lines could offset these negatives from a lower GDP. That at the end of the day we should continue to work with this guidance range you provided. So those are my two questions.

A - Jose Marcos Ramirez Miguel {BIO 1967010 <GO>}

I'll start with the second one. Why we are so comfortable because we went in with the number three consistent, let's call it, an old number, but we are working all the other data. We -- it's going to move down. So that's why we feel after working. I don't know, saying 3, but in the reality of the internal number that we are working is around 2. That's not since the beginning, we knew that this number is going to change a lot and we don't want to depend on that. That's why it doesn't move our middle tier. That's (inaudible). I'm sorry that the softened, but this will the reason.

And the first one, we're talking about the guidance. Rafa, the most comfortable (inaudible).

A - Rafael Victorio Arana de la Garza {BIO 1982204 <GO>}

No. I think Gustavo. If you look at the margin side, we are confident in the margin because of the interest rates and mix the sensitivity that we have on the balance sheet. So we are pretty confident on the margin side. The second one is the fee side. The fee continues to be trending in a good way. If we survive the process during the pandemia that we don't have data, the physical but adjusted EBITDA digital, we also see a very good trend on the fee side. On the loan growth, also, we continue to see based upon the third and the Fourth Quarter, good expansion, and that will benefit also the margin. The funding costs that is also related to the margin continue to expand well above our deposit growth above the loan growth.

So that also will be a good source for the margin. Trading will be in balance what we always see. So we don't see any -- we are very well -- I think we have been positioned pretty well for the downward trend and also for the upward trend. So we don't see an impact on that part. The expense line is the one that we have to really look hard into the expense line to reduce that 7% that we are giving you in that part of that.

That's the risk part, but it's in our control now that we anticipate a lot in the Fourth Quarter. I think we have more control on that, and we have to look at and ways to reduce that. NPLs and cost of risk, we feel confident because of what we saw so during the high levels of the pandemia, everything was locked down and how we manage the client. We also feel confident in that, and we have that MXN 1.8 billion ceiling there to protect also any deviation that we see on that. We also see a potential benefit is what Fernando mentioned, improved faster than we anticipate. We also see that part.

On GDP, I think that you have to understand that Mexico is like three Mexico. You see the center on the north, pretty active by exports and moving forward on manufacturing and most part of the business. And a part of tourism also moving quite nicely in the Baja part. And also on the tourism side, the Cancun and also pretty active in that. The center to the south is basically nothing. So when you look at GDP, you also have to look at local GDP from state to state. That's a completely different. That's why we see that we can manage that number that we've given you on the loan growth, even though the GDP going to fall down for sure, below 3%.

But in some parts of the country, the local GDP will be high above the 3%, and that's what basically we are doing business in that part of the country in the south (inaudible), the center and the north with the manufacturing, that's where Banorte is basically very active.

A - Jose Marcos Ramirez Miguel {BIO 1967010 <GO>}

I would like to (inaudible) value at 2.5% GDP. (inaudible)

A - Unidentified Speaker

Thank you. Thank you, is Alejandro del Rio, Chief Economist. Well Marcos and Rafa mentioned before, the guidance is hovering around 3%. Right now, market consensus is at 2.5%. I think that Rafa was quite accurate to outline our expectations about several sectors in the economy because as in the world, GDPs are recovering at a different pace. It's going to be the same thing in Mexico. We think that we will observe different the (inaudible) in terms of growth, for example, in external demand or anything that had to do with manufacturing or the exporting sector. Why? Because we are confident that we will continue benefiting from growth in the U.S. from nearshoring, from all these strategies that Mexico has been achieving in the last years to strengthen trade between the U.S. and Mexico.

So I think we are confident in that part. Also in terms of domestic demand, we have to stress out that consumption can be resilient now that we have vaccination program that will allow consumers to keep on with their activities. Remittances are at all-time highs and remittances are basically focusing on consumption. And also, we have been observing improvement in terms of employment. So exactly what Rafael was saying that despite the consensus, it's around 2.5% for GDP this year. We have to take into account that Mexico has different regions, different sectors. I think that he accurately said in which sectors Banorte has several strengths.

Q - Ricardo Alonso Garcia {BIO 20354965 <GO>}

Yes. Yes. No. Very good. Very clear.

Just if I could, if I may just to do one follow-up on the guidance, especially on the NII. I consider that you are comfortable with the line and you are more optimist. And according to your answer, regarding the insurance business in the previous question from my colleague, if I understood correctly, you are adopting a more conservative approach for insurance in this year, right?

So any positive surprise from insurance business could represent a potential upside in your NII estimates? Is that correct?

A - Unidentified Speaker

Yes. It is correct. Hopefully.

A - Jose Marcos Ramirez Miguel {BIO 1967010 <GO>}

Thank you very much. Thank you. We have received different comments now regarding the duration of this call. So if anyone needs to leave, please send us an e-mail, and we can arrange a call later on. And also, please, if you -- your question has been already answered, please, we can connect now later to go into other details.

We will continue with Geoff Elliott, please go ahead.

Q - Geoffrey Elliott {BIO 15944940 <GO>}

I know you want -- you don't want to get into the specifics of Banamex, and clearly, that's completely understandable. So maybe let's broaden it out. And could you talk about the criteria that you generally look at when you're considering a significant M&A transaction, how that evaluation works. You guys have got lots of experience doing this with other deals in the past, most recently with Interacciones.

So what are the criteria that you look at when you're thinking about a significant deal?

A - Jose Marcos Ramirez Miguel {BIO 1967010 <GO>}

Well It's a holistic approach. It's not so easy to say if -- we see all the pieces and then we (inaudible) most important, the acquisition for our investors. But obviously we see in an ESG, we see everything. As you said, we have a -- that's for fees requirement here that (inaudible) all this, we see all the opportunities.

So everything that is moving in the market is not accurate. We have the ability to look at it. So we are seeing is a different part. I would say that we cannot answer so directly because it's obviously (inaudible) that we made. But as soon as we have some color, we will obviously with -- in this case, our Board of directors, and then we move on and doing that so that somebody know. We know that real, we know everything, but we look everything. The acquisition is the most important, I would say.

A - Tomas Lozano Derbez {BIO 20387400 <GO>}

We'll now go with Carlos Gomez-Lopez from HSBC.

Q - Carlos Gomez-Lopez {BIO 18107094 <GO>}

I would ask about the Afore business. You mentioned that now we know that's fee, which is going to be charged. In the previous conference call, you mentioned the impact that the reduction in fees would have on your business without mitigating measures now that you have all the information, what are your expectations for the Afore business. This year, you made about MXN 4 billion, about a 2% increase, it's 5.5% of the business. Where do you realistically expect it to be next year?

And the second, and again I know that you cannot say too much about any possible transaction. But I would wonder -- It would seem to me that one of the most valuable things of Banamex is actually the brand. But you have your own, does the brand have any value for Banorte when you consider a possible combination for them?

A - Jose Marcos Ramirez Miguel {BIO 1967010 <GO>}

I will start with the first one, (inaudible) on the line and (inaudible). Go ahead, please.

A - Unidentified Speaker

Something I can answer that. Yes. Well the Afore (inaudible) because, as you know, I mean certainly, the reduction in the fees was materialized. What I mentioned in previous conference call, the impact in net income without any -- without doing anything else, it was quite significant because it was a reduction of 23 basis points. Therefore, in terms of net income without doing anything else, the impact was somewhere between the MXN 1,400 million to MXN 1,500 million.

As of today we are continuing, of course reducing the expenses in the commercial side. We are considering there that perhaps we will able to reduce the expenses, perhaps MXN 300 million. What is the challenge for the other expenses is that there are some regulations they are trying to change within the next quarter. Therefore, it's very hard for us to know exactly how those regulations will impact for good or bad in some other expenses. Let me give you an example. For instance, they are considering, the regulator is considering that perhaps the Afore, we will not be able to pay commissions to the sales force. Well if that happens, and they go to transform the sales persons moving to advisers. Therefore, you cannot pay them commissions, you have to pay them a fixed salary without commissions in the total compensation.

So that might be a positive to say one thing. Some other things that will -- it's likely that will happen because is that the regulatory is trying to reduce, given that they reduced the commission so much, they are trying to come up with some offset measures like, for instance, reducing some regulations, perhaps relying more in separate relation within the Afore to reduce that, also to concentrate the files, so on and so forth. But those are under discussion. Most of them are positive.

So there are some others, which may not be positive in terms that they are perhaps also planning to enhance some services that we have to be provided to the clients. So the cost of that is we have some uncertainty. Also something that is on a discussion which will be positive for us is that they are discussing that we can reduce the level of the reserves that we have to keep according to the assets under management. We have -- that will also be a positive.

So there are going to be minuses and pluses. So I would say so far, that's what we have seen. The only thing concludes, and we will have more on the call, hopefully, by the First Quarter is that we have this impact in due to the reduction in our income. This offset, the reduction of around -- so far at this point, but hopefully, it could go higher, but we have to wait and see of MXN 300 million.

I'm not sure if I (inaudible).

Q - Carlos Gomez-Lopez {BIO 18107094 <GO>}

Sorry if I understand correctly, first, the reduction in the fee was, if I recall correctly from 0.8 to 0.57, could you confirm?

A - Unidentified Speaker

That's correct. That's correct.

Q - Carlos Gomez-Lopez {BIO 18107094 <GO>}

Then you mentioned your previous calculation was a reduction in net income of 1.4 to 1.5? You said that you could mitigate it by about MXN 300 million with the reduction in the sales expenses. Is that correct?

A - Unidentified Speaker

Yes. But I have really careful to tell you that there are some things that are happening, as I mentioned, some regulatory changes. Some things were beneficial, some others will not. So that's why we have to wait and see this quarter to give you more color about what we expect for the end of the year.

A - Rafael Victorio Arana de la Garza {BIO 1982204 <GO>}

So Carlos, just a quick clarification. That's the amount for the impact of the full Afore. Remember, we only have 50% so you need to divide that. So you get to around MXN 750 million [ph]. Then MXN 300 million [ph] now.

A - Unidentified Speaker

Yes. I always think of the numbers of the party in terms as a whole. But as you know, the impact for us is only 50% (inaudible).

A - Jose Marcos Ramirez Miguel {BIO 1967010 <GO>}

And regarding the second question. Well (inaudible) we are doing that in each case, our holistic approach. One of the business is the brand. This is one of the multiple agents that we see, and that is we see a lot of things, a 100 things (inaudible).

A - Unidentified Speaker

As, if you look at the (inaudible). That is put the value on the ground. You will see they are not on the ground, have more value than the Banamex brand. As we speak. That's for the sight.

Q - Carlos Gomez-Lopez {BIO 18107094 <GO>}

Okay. No. I don't doubt that. But as a fact, you have -- you already have a valuable brand. Therefore, if you were to acquire that asset, that would not bring a brand, it may bring it to somebody else, but (inaudible).

A - Jose Marcos Ramirez Miguel {BIO 1967010 <GO>}

(inaudible).

A - Tomas Lozano Derbez {BIO 20387400 <GO>}

Okay. We'll now move into Yuri Fernandes from JPMorgan.

Q - Yuri Fernandes

A lot of questions. I have one on margin sensitivity. There is this nice chart here showing like the sensitivity to rates increasing over time. It seems pretty good now at MXN 1.1 billion per 100 bps change in rates.

My question is how much more can we see this moving forward? Because I guess Rafa mentioned that he believes, this sensitivity may continue to increase. So my question is, how much more can we see this for the mid of the year for the year-end, where this can be the sensitivity?

And I have a second question and sorry for returning for this topic on Banamex, dividends, and capital. Looking to your Tier 1 and core equity [ph] Tier 1, it's pretty solid. Like you have a lot of capital. And my point here is more on the core equity than the Tier 1 because on the core, I guess it's tougher for you to generate this kind of capital. You mentioned MXN 52 billion of with excess capital. My question is if you pay those MXN 34 billion, your excess capital will decrease materially, right? Like if the MXN 34 billion is not calculated as part of those MXN 52 billion.

In addition to that, again we don't know about the acquisition. We don't know the price. We don't know like who do you be generated, the RWA calculation. There are many, many moving parts. But considering the dividends, and the prices we are seeing people discussing around. My question is, can you keep the 11.4 capital with such material acquisition? Or would you need to increase capital or finance this with debt in the holding because I know also that in Mexico, the Basel III regulation, it's not a financial conglomerate, right?

So one thing is looking for the capital at the bank level, and other things thinking about the holdings. So my question is thinking about dividends you pay as you said, the excess capital would reduce and it's a super big acquisition, right? So I don't know how to fit the 11.4, correction that you mentioned with all those moving parts here. I would like to understand this a little bit better.

A - Jose Marcos Ramirez Miguel {BIO 1967010 <GO>}

Thank you. Yuri, I can (inaudible).

A - Unidentified Speaker

Sure. First of all, the sensitivity.

Yes. As you mentioned, Yuri, we have been increasing that in the local currency balance sheet is around 1.1. We are expecting an expansion level of around 200 million.

On the foreign currency balance sheet, we're at around 900 [ph], and we also expect some expansion in that regard. Then I think that your question about the core equity Tier 1 is what's the excess capital given the correct one that we're going to maintain in the MXN 52 billion that Rafa discussed.

Q - Yuri Fernandes

Okay. We can take -- we can discuss this later because it's many moving parts here, and I'm not getting like the MXN 52 billion -- like the MXN 52 billion includes the MXN 34 billion payments because MXN 52 billion less MXN 34 billion, it would decrease materially right after the dividend payments.

A - Jose Marcos Ramirez Miguel {BIO 1967010 <GO>}

Does that MXN 52 billion include those MXN 34 billion?

A - Rafael Victorio Arana de la Garza {BIO 1982204 <GO>}

I think we need to define what is material because you're looking at a 15.4% core Tier 1, okay? And that for Tier 1 is only taking into account 50% of the net income of '21. Everything else is already at the group. So that will not be a reduction on the capital numbers, what is already at the group, that is MXN 16 billion that is ceiling at the group. So what we are talking about is another MXN 16 billion that will be put down and the MXN 54 billion that we say the MXN 54 billion [ph] is if we won't like to decrease the level of core Tier 1 to levels of 11.4%, 11.6% that Marcos mentioned, that is the basic metrics that we run when we want to reduce the capital for any assets that we need to acquire.

I think that distinction needs to be made that MXN 16 billion are already ceiling at the group. So when you're talking about materials, we're only talking about MXN 16 billion will be the effect on the 15.4% of core Tier 1 that we have. So it's really not material. Obviously it's important for it doesn't move -- it will still well above the 12.5% that is the number that we would like to run the bank.

Q - Yuri Fernandes

Yes. I'm not concerned about the dividends. You have a lot of capital to pay out the dividends. I'm thinking about the acquisition, the capital for the acquisition.

A - Rafael Victorio Arana de la Garza {BIO 1982204 <GO>}

Yes. The acquisition. That's the tricky one is we're taking into account to paying the dividend as you take in account of the dividend part of the acquisition. That's the key part that we can (inaudible).

Q - Yuri Fernandes

That's the key part. That's the key part. Like if you keep the dividend aside or you pay the dividend and acquire something else? That's the question.

A - Rafael Victorio Arana de la Garza {BIO 1982204 <GO>}

Definitely.

A - Tomas Lozano Derbez {BIO 20387400 <GO>}

Now we will go with Gilberto Garcia from Barclays.

Q - Gilberto Garcia {BIO 17390216 <GO>}

Not to try to sneak in another question about potential M&A. But given that you already have a sizable branch network. How do you think about this physical questions, especially as you continue to learn about the people business through the Rappi JV?

A - Jose Marcos Ramirez Miguel {BIO 1967010 <GO>}

I want to (inaudible).

A - Rafael Victorio Arana de la Garza {BIO 1982204 <GO>}

If you look at the sector, I think you have to see that the largest number of branches belongs to the DDA [ph] that's not close to close to 500 branches more than that and the same number than Banamex because the branches of Banorte and Banamex are basically the same. So I think whatever happens in the market, there will be, I think more branches than needed, that's why you move into this acquisition.

So we have to -- as you know, Banorte has got the branch network in the past three [ph] years, but what we are doing is remodeling the branch network to a better layout and a better orientation for the service. So that's why we can tell you about that. We have to go and look at the value of branches, what the potential we grow things and also the potential cost savings based upon the digital. It's a potential balance in that (inaudible).

Q - Gilberto Garcia {BIO 17390216 <GO>}

Very clear. And a follow-up on the insurance business, if I may. Thinking longer term, you mentioned that you've seen strong demand for insurance products at the branches. Do you believe, this could be sustained, leading to wider adoption of private insurance, particularly considering how low insurance penetration is in Mexico?

A - Jose Marcos Ramirez Miguel {BIO 1967010 <GO>}

Firstly, (inaudible).

A - Unidentified Speaker

(inaudible) Yes. I do believe so. I mean precisely because of that. I think -- and I think that the resolution through the -- I mean for this call bancassurance is a very -- a very, very strong distribution channel.

Also in the digital world, I think there is also something that we have to keep looking at. I think there are also very good opportunities. But what we just mentioned about the -- for instance, everything else the same, of course we cross-sell products, as you know, in the credit products, but also in the -- in the other parts of the balance sheet, I mean the deposits.

So I think we have very good opportunities. So I mean even for -- also for existing clients, I think we have some room to improve the cross-sell as well and also to upgrade, not only we sell a (inaudible) they buy a quasi [ph] product or for a credit product, but also to offer some upgrades as they do that. So I'm optimistic about this line of business certainly.

A - Tomas Lozano Derbez {BIO 20387400 <GO>}

Now we will take the next question from Eduardo Miller. We don't have the company work that you represent, if you could state the company, please?

Q - Unidentified Participant

I am an independent individual. Giving a follow-up on Jorge question and your comments on the product (inaudible) quality, I would like to ask constituting the reported provision levels by our current local macroeconomic view to have diminished it from previous levels. Are you expecting to allocate more resources?

And following this line of thought, are you anticipating to increase available credit lines from the banking counterparts and banking -- I'm sorry, and (inaudible) from the reported levels. And finally, regarding derivatives, at what point of the year can we expect to see a full transition of the underlining to suffer from (inaudible)?

A - Jose Marcos Ramirez Miguel {BIO 1967010 <GO>}

I don't want to feel good about this, but I think those questions require a deep answers on that. If you allow us to go on a one-to-one with you, happy to show you because there's a lot of regulatory issues that we have to show in that part, everything related to credit lines. There's some secrecy about who are the counterparts and things like that, as you know, by regulation. So I'm happy to take off-line, but happy to answer each one of those.

A - Tomas Lozano Derbez {BIO 20387400 <GO>}

Now we will go with Olavo Arthuzo from UBS.

Q - Olavo Arthuzo Duarte

Can you hear me well?

A - Tomas Lozano Derbez {BIO 20387400 <GO>}

Yes.

Q - Olavo Arthuzo Duarte

Okay. I wanted to explore one single topic here. Actually, I wanted to understand the bank strategy for the credit card portfolio of the bank for this year. In this 4Q, it was one of the highlights within the contract portfolio. And as you mentioned early in this call, the growth rate for this year should be something above 5%. Correct me if I'm wrong.

So could you share with us the rationale of this growth rate? I mean really this supported by a more aggressive pricing approach or supported by the expected demand for the year? And what I thinks here on this topic that it is all the pipeline for this product to launch some new features like new reward programs, partnerships with other annual financial companies, or on the other side, around some other initiatives to force the use of your credit card through that transaction. If you could add the card strategy, through the partnership with (inaudible) to which it would be great.

A - Jose Marcos Ramirez Miguel {BIO 1967010 <GO>}

Thank you, Olavo. Remember that we are, let's call a big bank and our natural quarter should be around (inaudible), I don't know, in other products, and we don't have it here. So we have a good of improvements and a lot of good here. So we're optimistic, and we know what to do. (inaudible).

A - Unidentified Speaker

Yes. Thank you, Olavo. On the credit card, we are planning to grow that percentage considering the capabilities and all the infrastructure that we have already in place. As you may be aware, we have a complete set of products. We have alliances with (inaudible), with United, with AT&T, with some advertising group here in Mexico. So we believe that in the basket of the products, which are products that can cover all the needs for all the customers.

On the process side, we have been working during these two years in making the -- what we call the bank in a minute. So you can open a credit card in a minute -- in five minutes, 10 minutes in the digital channels.

So that's -- and also, you can -- the customer can serve almost all the transactions that they want, using the mobile banking, they can claim some nonrecognized charge or a statement of payments, obviously. We also have the digital card, and we have more than that additional to that, we have the rewards platform that you can use it in three different ways. You can buy in the shop. You can pay in a commerce with your points, or you can raise your transaction using again your mobile banking.

So we believe that we are in a very good position to serve the customers and to attract more and more customers. And additional to that, as you can imagine, the portfolio is very clean. We have -- we're confident that the customers that we have there are going to be saved properly in this new post-pandemic or post two years of pandemia season.

A - Tomas Lozano Derbez {BIO 20387400 <GO>}

Thank you. Now we will go with Brian Flores.

Q - Brian Flores {BIO 19197169 <GO>}

Can you hear me well?

A - Tomas Lozano Derbez {BIO 20387400 <GO>}

Yes. Perfectly.

Q - Brian Flores {BIO 19197169 <GO>}

Great. I just wanted to know if you can detail how would the process of M&A relation goals internally, let's say your team analyzes an idea, likes it. How long does it take for it to be approved internally, and then to be taken to the shareholders' meeting, which you already have mentioned?

A - Jose Marcos Ramirez Miguel {BIO 1967010 <GO>}

(inaudible).

A - Rafael Victorio Arana de la Garza {BIO 1982204 <GO>}

Brian, the process is, as you know, we have an M&A area that is always valuing assets in the market on a permanent basis, not because something comes and appears at the market. We do this exercise on a monthly basis, we update the values and everything that is in the market, even if it's for sale or not for sale on that part.

So that's one set that is panel. Once we find that if something is worth it to take into the Board, we take it to the Board, how long it takes? It's really based upon the availability of the information that the potential assets allow us to look at. But on valuation processes, we are on a permanent basis, looking at every single asset that is in the market, even if it's for sale or not for sale.

And how fast the acquisitions are internally at Banorte are pretty tough. I mean compared to anybody else is pretty fast because we -- the decision process is local, and the Board is local, and then we call for the assembly that is obviously global, but the internal process go very smooth and very fast. And -- but it's worth mentioning that permanently, every single month, we update the value of any potential asset that is in the market.

Q - Brian Flores {BIO 19197169 <GO>}

So Rafa, just a quick follow-up. Assuming you have this availability of data. So how quick are we talking around? Are we talking three, six months? Just to have an idea.

A - Rafael Victorio Arana de la Garza {BIO 1982204 <GO>}

I think at the most, three months.

A - Tomas Lozano Derbez {BIO 20387400 <GO>}

Now we will take our final question from Rodrigo Ortega from BBVA.

Q - Rodrigo Ortega {BIO 7474614 <GO>}

I was thinking about looking long term, and the substantial funding improvements that you have achieved. I wanted to know how much of loan growth do you think that (inaudible) support before this funding improvements start to erode. I think it would be reasonable to think that if our loan growth materially points, we start to consume their excess savings. So how should we think about this balance in the midterm between growth and funding efficiencies?

And the second one, a follow-up on credit card. What are you expecting regarding the evolution of clients making full payment, which continues strength to trend upwards listed data as of October from CNBV? And also about the average revolving balance with these clients.

A - Jose Marcos Ramirez Miguel {BIO 1967010 <GO>}

(inaudible), we start with the second one.

A - Unidentified Speaker

Thank you, Rodrigo. We are expecting, as you know, we have more customers now pay the, paying all the debt more than revolving. But we are expecting that to start moving towards as our previous numbers, pre pandemia numbers, by the Third Quarter of this year. And again as I was saying previously considering what we are doing in personalized offers, we believe that we can pull that earlier in the year.

A - Jose Marcos Ramirez Miguel {BIO 1967010 <GO>}

Yes. Rodrigo, if you look at the history of Banorte, there's two things that we have to take in consideration about loan growth. The capital consumption and so the deposit availability for growth. Basically, if we're still in the range from 10% to 12%, on the funding side, we don't have an issue about the cost not because of the availability because the variability there on the cost is the 10% to 12%. If we go to 15% loan growth, we start consuming capital.

A - Tomas Lozano Derbez {BIO 20387400 <GO>}

Thank you very much.

A - Jose Marcos Ramirez Miguel {BIO 1967010 <GO>}

Thank you.