Itaú Unibanco - International Conference Call
Second Quarter 2019 Earnings Results
July 30th, 2019

Operator: Good morning ladies and gentlemen, welcome to Itaú Unibanco Holding conference call to discuss 2019 Second Quarter Result.

At this time, all participants are in a listen-only mode. Later, we will conduct a question and answer session and instructions will be given at that time. If you should require assistance during the call, please press the star key followed by zero. As a reminder, this conference is being recorded and broadcasted live on the investor relations website at www.itau.com.br/investor-relations. A slide presentation is also available on this site.

Before proceeding, let me mention that forward-looking statements are being made under the safe harbor of the Securities Litigation Reform Act of 1996. Actual performance could differ materially from that anticipated in any forward-looking comments as a result of macroeconomic conditions, market risks and other factors.

With us today in this conference call in São Paulo are **Mr. Candido Bracher**, President and CEO; **Mr. Milton Maluhy Filho**, Executive Vice-President, CFO and CRO, and **Mr. Alexsandro Broedel**, Group Executive Finance Director and Head of Investor Relations.

First, **Mr. Candido Bracher** will comment on 2019 second quarter result. Afterwards, management will be available for a question and answer session.

It is now my pleasure to turn the call over to **Mr. Candido Bracher**.

Candido Bracher: Good morning everybody, welcome to our second quarter 2019 earnings conference call. I will start the presentation on slide 2, where we show the main highlights of our performance for the quarter.

Recurrent net income was R$7 billion, which represented a 2.3% growth when compared with the previous quarter and resulted in a 23.5% ROE. The key drivers of this performance were the acceleration of our financial margin, both with clients and with the market; as well as a stronger fee revenue generation. These effects were partially offset by two expected events: Seasonally higher noninterest expenses and a higher cost of credit. The letter is the result of a continuous growth of the origination of credit to individuals.

Lastly, our effective tax rate increased 70 basis points as a result of the lower TJLP, long-term interest rate, in the period, which is used to calculate the tax shield from our interest on capital. In the next slide we will provide a more in-depth view of these figures.

On slide 3 we show that our value creation increased 9% in the second quarter and reached R$3.2 billion, a record figure. This was a result of our performance in the quarter as well as due to a lower cost of equity.

Moving now to slide 4, we show that our Brazilian credit portfolio grew 7.9% over the last 12 months driven by individuals and SMEs, which have grown 14% and 19% respectively. Origination continues to accelerate in both portfolios, resulting in a richer credit mix, as will be shown in the next slide. On the other hand, our credit portfolio in Latin America remained practically stable compared to the previous year. This is a consequence of the appreciation of the Real against other currencies in the region.

If we discount this effect, the portfolio would've grown 7% when compared to the same period in 2018, the portfolio LATAM, and the portfolio as a whole would have grown 7.7%.

Now I want to draw your attention to slide 5, which portrays a crucial element of our results dynamics – it is in the bottom of slide 5. Financial margin with clients is composed by two distinct elements. One is related to working capital, which is mainly affected by its own volume and the SELIC rate, and the other which is the core element of NII and emanates from spread-sensitive operations.

The spread-sensitive NII grew around R$800 million as a result of the credit portfolio expansion and continuous change of mix towards higher spread-bearing products. This amount was partially offset by a lower working capital NII, which was a result of two effects: one, lower average balance after dividends payment; and two, lower interest rate. Consequently, we are observing a robust increase in the spread-sensitive NII.

On slide 6 we show that our financial margins with the market increased 26.4% this quarter. This performance was largely attributed to higher accruals in the foreign investment, overhead strategy, and in our insurance reserves management. We consider those gains to be structural as they are an integral part of our core banking activities.

Turning to slide 7 now, we show our credit quality. Short-term delinquency remained stable in the quarter, while the NPL 90-day ratio decrease 10 basis points. The letter was a result of loans written-off from specific large corporate clients and a further improvement in the SMEs NPL ratio, which reached 2.5%, the lowest level since the merger between Itaú and Unibanco.

The NPL 90-day coverage ratio remained stable at 208%, and the cost of credit ratio increased 10 basis points, as would be expected, given the acceleration of the change in credit mix in the period.

Slide 8 shows that our revenues from services and insurance grew 5% in the quarter. This performance was mainly driven by asset management and investment banking fees. It is worth to highlight the growth of almost 50% in the year of the funds from our open platform initiative, which reached R$155 billion. Also of note is our credit and debit card issuer fees, which continues to grow consistently.

Lastly, the acquiring business fee revenues declined 12.8% in the quarter mainly as a result of the new commercial initiative, which consists in a charge interest rates on the prepayment of credit card transactions, which are now paid in T+2. In the next page we examine in more details the initial results of these initiative.

On slide 9 now, we show that after the T+2 initiative, our acquiring operation had an upsurge of demand. New client acquisition increased 73%, while new clients choosing Itaú Unibanco as a bank domiciled more than doubled in the same period. More importantly, net promoter score increased 8 points in the year. These KPIs reinforce our perception that this was the right move.

Now turning to slide 10, we show that our non-interest expenses grew 4.3% in the quarter. This growth was largely expected as expenses in the first quarter are seasonally lower than the rest of the year, but it is important to highlight that the growth was more subdued this year than in 2018, when our expenses grew 5% in the same period. It is worth pointing out that the quarter concentrated the closure of almost 200 branches just in Brazil, which added further pressure in our immediate Opex, that will positively impact our efficiency from now on.

Finally, our first half expenses grew 3.7% when compared to the same period in 2018, roughly in line with inflation for the period. Another important message: yesterday we announced a voluntary severance program. This program effects a potential population of 6.9 thousand employees, potentially. They will have, from first to 31 August, to decide whether they will join or not the program. As we have more information about this, more confirmed information about this, we will inform the market.

Now slide 11 illustrates the organic capital generation of the bank as we finish this quarter with a Tier 1 ratio of 14.9%, an increase of 30 basis points compared to March 19. It is worth mentioning that we announced the distribution of R$7.7 billion as a complementary dividend to be paid in August 23rd, 2019.

Finally, now I want to discuss our expectations for the remainder of the year. On slide 12 we show that the actual performance of the economy so far makes it clear that the original forecast for economic growth was too optimistic, with the interest rate forecasted in a higher level than the one we foresee now. Lastly, it is worth mentioning the appreciation of the Brazilian Real against the Chilean and Colombian pesos.

So bearing these effects in mind, I now want to comment on our guidance and go item by item here. So we still abide by our guidance for the year, but it continues to situate our base scenario for each line.

Total credit is well within the interval within Brazil, but the changes in exchange rate for LATAM places our base scenario around the lower end of the range for the consolidated portfolio. The forecast of a lower SELIC rate and a narrower future yield curve have a negative impact in the expectations for our liabilities margin and for our working capital NII. Therefore, we anticipate our financial margins with clients to finish the year close to the lower end of the guidance.

We expect our financial margin with the market and our cost of credit to be around the midpoint of their respective ranges.

As for the commissions and fees, we anticipate to finish the year between the mid and lower point of the guidance. And finally, we expect our non-interest expenses to finish the year around the lower end of the guidance.

With this, we conclude this presentation and are now open to any questions you may have.

Question-and-Answer Session

Operator: Ladies and gentlemen, we will now begin the question-and-answer session. The questions will be limited to two per participant.

Our first question comes from your Jorg Friedman, Citibank.

Jorg Friedman: Thank you for the opportunity. I have two questions. The first question, thank you very much for sharing your impression, Candido, on where you should be in terms of the guidance by each line, but here I just want to understand a bit better why you are so conservative in terms of the financial margin with the market, because if you look into the run rate so far you are already above the upper end of the range. So just wondering if there is anything that might, you know, negatively impact the results for the coming quarter that you are already aware, or it is just a matter of being really conservative there.

And the second question, I understand that you are still, you know, looking for additional clarity about the early dismissal program, but just a couple of points there: First, I understand that the 6.9 thousand employees that are eligible for the program are all based in Brazil, so it is approximately 7,000 out of the 85,000 that you have. Is that correct or this could be also extrapolated to other regions?

And the second point, just wondering if you had already contemplated such early dismissal program when you put together the Opex guidance and how the potential effects of, you know, such a program will be contemplated in the guidance. You mentioned that you believe that you are going to be in the midpoint of the Opex guidance here. This is already contemplating or not the potential effects of the layoffs for this year? Thank you very much.

Candido Bracher: Hi Jorg, thank you very much for your questions. First on guidance. On guidance I must say, I think you are right; the financial margin with the market is probably the line more difficult to forecast and, I mean, we had a positive semester, two positive quarters in the beginning of the year, above our initial guidance, so we were relatively conservative when forecasting the end of the year. I think it can be better, but I cannot be certain about it.

Now concerning the early dismissal programs. First, you are right, it only concerns Brazil. So it is 6.9, the eligible population is 6.9 thousand employees in Brazil. The costs of this program they, of course, they fall into the nonrecurrent costs, so do not affect our guidance. As to the benefits, we will wait until we have a clear figure of how much adherence to the program there is. So far, we have not included any of these impacts when we guide the noninterest expenses to the lowest point of the guidance.

Jorg. Friedman: Okay, that's perfect. And, by the way, could you just give us some kind of initial ideas about, you know, what could be the impact, if you have like, I don't know, 20% or 50% adherence, or are you still working on the numbers? Thank you very much.

Candido Bracher: You know, Jorg, last time we made a program like this was 10 years ago, so we really have no statistic evidence to make any kind of forecast here, it depends very much on the adherence, in which level this adherence will happen. So it is too soon to tell about our expectations.

Jorg Friedman: Okay, thank you for the answers, and congratulations on the results. Thank you.

Candido Bracher: Thank you.

Operator: The next question comes from Otávio Tanganelli, Credit Suisse.

Otávio Tanganelli: Hi, good morning and thanks for taking my question. I have only one question, if I may. I wanted to ask about the asset management fees. We saw an acceleration from previous quarters, it was growing at about 5% year on year, and this quarter it accelerated up until almost 15%. I wanted to get a little more color on what's driving this, because the assets under management continue to grow at similar pace than what we saw in the previous quarter, but the average rate, if you divide the revenues by the assets under management, they increase as a percentage of the AUM. So I wanted to understand a little better. Thanks.

Candido Bracher: Thank you Otávio for your question. I have a very direct answer, I mean, what drove this improvement in the margin were the performances, I mean, we had a good quarter in terms of performance of the more sophisticated funds, and this improved this line on our balance sheet.

Operator: The next question comes from Mario Pierry, Bank of America Merrill Lynch.

Mario Pierry: Good morning everybody. Let me ask you two questions as well. The first one is related, Candido, to the 6,900 employees that you think are eligible for dismissal. If you can give us some color, what kind of assumptions are you targeting, what kind of job these people have?

And related to your costs also, this quarter you closed 200 branches and laid-off 1,000 people. Can you disclose to us the costs that you had related to this branch closing and lay-off of people? And then I'll ask a second question related to something else.

Candido Bracher: Okay Mario, thanks for your question. So this 6.9 thousand employees they are above 55 years of age - and they must become 55 before the end of this year -, and they are people who enjoy ("or" not "and")… so above 55 years or people who enjoy some kind of stability, which according to Brazilian legislation happens when you have a health life and is member of syndicate or director of syndicate or things like this. So they are not divided by functions specifically, so they cover all the spectrum of functions in the bank.

As to the 200 branches we closed, I do not have a figure of the cost involved, but of course there is some cost involved, and there always is when you have to lay off people, and we could expect the benefits to come along the time.

You said you had another question?

Mario Pierry: Yes, so just one follow-up on this 6,900 people. So it's fair to assume then these are people that have an above-average salary at the bank? Is just that I'm trying to understand here what could be the potential benefits of this plan, so if you look at average salary, but it seems to me that this would be people earning well above the average salary.

Candido Bracher: Yes, I think this is a reasonable assumption Mario.

Mario Pierry: Okay. And then second question is related to your net interest margins. If you are on page 5, the ability of the bank to maintain net interest margins relatively stable over the last few years even though the SELIC has contracted quite a bit, can you discuss… I understand a big chunk of this is related to improved mix, but can you discuss a little bit the type of pressure that you see on credit spreads, especially in specific segments, if you are already seeing spreads coming down? Looking at Central Bank data, we see mortgage rates are down, pretty much every interest rate that you're charging on your loans have been coming down. So, you know, the question becomes about your ability to maintain your financial margin with clients stable for the foreseeable future.

Candido Bracher: Well, you know Mario, the Central Bank divulges an item, an index called ICC (*índice de custo de crédito*) which is a compound weighted average of all financings in the bank. During the past year our ICC dropped 0.1%, but the mix made it increase 0.6%. So, spreads alone had a negative impact of 0.7%, and I see this as a continuous trend, especially with the improvement in the economy that we expect from the pension reform and so on. I think that competition will increase and there will be pressure on spreads. This may still be somehow offset by a richer mix in terms of portfolio, but there is a limit to where you can go in terms of mix. So I think that the general trend is for more pressure on spreads.

Mario Pierry: Okay, that's very clear Candido. Thank you very much.

Candido Bracher: Thank you Mario.

Operator: The next question comes from Andrew Brosky, Goldman Sachs.

Andrew Brosky: Hello? Is that for Tito?

Candido Bracher: Hello?

Andrew Brosky: Hello. Hi! Not sure if that was for Tito Labarta of Goldman, or is that somebody else from Goldman on? Can you hear me?

Candido Bracher: Yes, I hear you.

Tito Labarta: Sorry, I'm not sure why they got Andrew, but this is Tito Labarta, from Goldman Sachs. I'm sorry for that.

Candido Bracher: Hi Tito, how are you?

Tito Labarta: Good, thanks! Thanks for the call. A couple of questions also. I guess first just a little bit of color on Rede. We saw the volumes only grew about 0.9% in the quarter despite the price reductions and the free prepayment of receivables. Just curious why it looks like you're still losing market share in Rede despite the price reduction. And then I have a follow-up question on expenses after that.

Candido Bracher: Okay. Tito, thank you for a very good question. If you pay attention, our T+2 offer targeted the market with net revenues up to R$30 million a year. We think that this is the richer segment of the market, where there is more profit to be made. But this is not the segment that makes the most of the market share. Most of the market share is made by the large corporations, well above R$30 million a year, and in this segment we have been losing market share for quite some time already, and so this is why, despite our offer and despite our improvement in this segment up to R$30 million, in the overall figure we grow very little in our total volume.

Tito Labarta: Okay, that's helpful. So do you think you will continue to lose share over all given these trends that you're seeing?

Candido Bracher: No, it depends on the willingness of our competitors to grow below cost on the larger corporation segment, because that's something we are not doing.

Tito Labarta: Okay, got it, makes sense. Great. And then a follow-up question on expenses. I know you gave us some color there, but maybe just thinking a bit longer-term, do you think the expense growth can remain around the 3% to 5% guidance that you're giving for this year, particularly with some of the initiatives that you are announcing? So, you know, around inflation, is that a good level of cost growth for the next years? And are this sort of initiatives, is it because of the pressure you're seeing on spreads and competitions sort of forcing you to reduce costs, or is it something else?

Candido Bracher: Well, Tito, as I said, I mean, I see non-interest expenses in the bottom of the range this year and we will certainly keep a strong hand on that in the time coming ahead.

I don't see this as a result of pressure, I see this as an opportunity. As you remember, we started the year with a much higher guidance, 5% to 8%, then when we saw that the economy would have a weaker performance we decided to make the big corporate effort around efficiency and costs. And we are happy with what we are discovering, with the opportunities we are seeing, and we certainly think they do not finish this year, I mean, that this will be a trend.

Tito Labarta: Okay, great, thank you Candido.

Candido Bracher: Thank you Tito.

Operator: The next question comes from Eduardo Nishio, Banco Plural.

Eduardo Nishio: Thank you for the opportunity. Good morning Candido. Two questions as well. First on the guidance, if you can go back again. I think there is two items that I either missed or you didn't talk about. Cost of credit, if you can give us your views on that and also effective taxes, I will appreciate it. Then I have my second question. Thank you.

Candido Bracher: Okay. Thank you Nishio. Cost of credit will be in the middle of the range as it's going very well along the lines we had forecasted. Effective tax rate will also be in the middle of the range this year.

Eduardo Nishio: So for cost of credit, the 4 billion posted this quarter, a little bit more than that, and then last quarter it was 3.8, so more or less the same level, no changes probably to reach the 16 billion, right?

Then my second question is concerning your digitalization, your digital transformation, if I will. You've been reducing staff, this quarter was about quite a lot - is 1,200 people -, reducing branches and we cross-checked here across all regions. What would be the ideal size, what is your ideal bank size in this digital transformation? And by when do you expect to reach it? And by the way, you've been hiring IT folks as well, so what would be the ideal mix of people and if you can give us some color on the future of your digital transformation, I appreciate it. Thank you.

Candido Bracher: Okay, thanks Nishio. Here we have two conflicting forces. In one hand, we expect growth in the economy coming after the pension reform approval to put some pressure in growth, in terms of absolute growth, and this also implies people. On the other hand, digital transformation has been enabling us to reduce people in a faster pace. When you combine both movements, I would think that reduction will still more than compensate the economic growth factor, but not quite sure about it.

In terms of digital transformation, I mean, we are increasing, I mean, the opening up accounts totally digitally, we are now using facial recognition in many aspects including vehicle financing. So there are many progresses being made and that will be made in the future.

In the closing of branches, it is not only the digital, I mean, of course it is an effect of digital transformation, but the digital transformation is driving less people to our branches. But we are not closing branches which are isolated geographically, we are only closing branches so for that are very close to one another. So when two branches are very close - less than 500 m distance - and one of them is capable of absorbing the population of both branches, this is the case when we are closing. We still have some room for that in our portfolio.

Eduardo Nishio: Thank you.

Candido Bracher: You are welcome.

Operator: The next question comes from Domingos Falavina, J.P. Morgan.

Domingos Falavina: Good morning Candido and everyone. Thanks also for taking the question. Candido, my question is a bit more structural. When we look at the fee composition this quarter, it looks very good to us like the evolution based in investment banking and broker growing 40+ percent, and above all, it seems to us that the bank is not really pushing hard current account fees, which, in our review here at least, seems like a smart decision given the competitive threats.

So. my question is, when we look at these fees, is this kind of reading correct or basically do you also share this view that current account fees are unlikely going to grow, you know, substantially? And it makes sense to hold back on some of these adjustments? Or not, is that something we are reading in a wrong way? And then I'll ask the second question.

Candido Bracher: We take these decisions on a decentralized manner Domingos, but I think you're reading is right, we are preferring to grow in the areas where we can grow volumes more significantly, as in investment banking and asset management, and we are not pressing on the fee level, we are valuing more in growing volumes than the level of fees, which we tend to keep as slow growth as we can.

Domingos Falavina: Understood. And second question is on Rede, and I'm sorry if I missed any specific comments there, but, I mean, volumes came in… at first, it seems some additional deceleration, but when we look at the industry in general, I mean, Getnet decelerated massively to 6%, Cielo grew 9, so versus the big players, Itaú is still bid well, but it kind of left us with the question here, like, “what's happening to volumes”, like, are we not seeing one big player, I'm not sure if it's Safra Pay or someone else, growing and taking away volumes? Did you guys notice an overall industry deceleration, maybe, in credit and debit volumes? And what kind of effect the T+2 have in NII, in fees? Like, if you could comment a little bit like even in a quarter has passed?

Candido Bracher: So, in relation to T+2, the effects are those I have described to you, so 73% increase in new accounts, more than doubled the increase in companies choosing us to be the bank where they receive their commissions and so on.

I'm not sure I understood your doubt about the total volume, different from what I explained in the last question, I mean, it's really linked to the large corporations, I mean, this is where we are losing market share. There are some competitors which are very aggressive in this segment, I mean, looking specifically for market share, but at prices which, in our experience, leave a negative margin. So this is why we are not going there, and I am not worried about it either.

Domingos Falavina: My question was more like: Do you believe you are losing share? Because when we look at Getnet, it grew 6, we look at Cielo, it grew 9. So you grew more than those two. So my question was more like, do you believe you are losing share, or do you believe the industry in general is growing below 14%?

Candido Bracher: I am not sure about the answer here. Sorry Domingos.

Domingos Falavina: Thank you.

Operator: The next question comes from Olavo Arthuzo, Santander.

Olavo Arthuzo: Hi everybody. Candido, good morning and thank you for taking my question. Actually, I wanted to shift a little bit the discussion to other topic that has been calling the attention of the market. I would like to understand the bank’s digital strategy, so in other words, I just wanted to have a clear view on Itaú's approach as a digital bank, because Bradesco has their own feature called Next, that has few services free of charges and others that the clients must pay a fee, and Banco do Brasil has another digital solution that is free of charges for some services, but different from Bradesco, it is within the bank and we know it as Conta Fácil.

So my two questions are, first, what is exactly the Itaú perception on these approaches from your main competitors in light of a lot of other initiatives and digital banks that target the total customer base? And the second question is, in few words, what is the main focus of Itaú digital strategy? Thank you Candido.

Candido Bracher: Thank you Olavo, very good question. So, answering your first question, I think I can come back to something I've been saying for some time, which is, there is a basic decision to be made in terms of digital strategy, which is: do you separate a new bank from an old bank and you concentrate your digital efforts in a new venture or do your work, I mean, to transform the existing bank, the legacy systems and so on and to modernize the incumbent bank, to say? And here our strategy is clearly the second one.

So we are working hard in order to digitalize Itaú as a whole and not a new bank. We have new initiatives, like: ITI for instance, which is quite a new product, it is a platform, but it is integrated into Itaú; we have, as you know, Cubo, which is a hub of co-working and joining companies, it is the largest in Latin America, and we learned a lot from them there; we are leaders in digital wallet in Brazil, Apple Pay, Samsung Pay, and all the others; we have now just launched and app for people who buy foreign exchange in the app; we are opening more than 200,000 accounts a quarter exclusively by… So we are digitalizing the bank as a whole and not in some separate initiative.

Our digital strategy here – I mentioned this in an interview recently – I like that phrase that “incumbents must find innovation before innovators find distribution”, and I thought as an incumbent, using to think as an incumbent, that finding innovation was basically being fast in replicating the initiatives of Fintechs and so on. I have changed my view in this point, I think it's simply not replicating what they do, but it's learning to do it differently, it is producing technology in an integrated way between the technology area and the business area, which by the way, I think that in a few years from now we will not be talking anymore about technology and business area, this will be one only thing. I mean, this is the path we are trading, and I think we are making consistent progress there.

Olavo Arthuzo: Okay, that's very interesting. Thank you Candido.

Candido Bracher: Thank you Olavo.

Operator: Excuse me, as a reminder, if you would like to pose a question, please press the star key followed by the 1 key on your touchtone phone now.

Our next question comes from Marcelo Telles, Credit Suisse.

Marcelo Telles: Hi, good morning Candido. Thanks for your time. I have two questions. My first one is a follow-up on your comment about credit spreads. I think you mentioned earlier that you expect some pressure in credit spreads down the road. And my question to you is, you know, in which segments, you know, you think that this should happen? Because when you look at the credit spreads evolution, at least as per the Brazilian Central Bank data, we actually see spreads fairly resilient, particularly on the retail side. So if you could elaborate what would be, you know, the timing, which segments, you know, what would be driving that, maybe is more the Fintechs or the competition should come, you know, from among the big banks? Just to understand, you know, what would cause that spread compression to take place.

And my other question is with regarding cost. I think it's very good, you know, to see the banks so, you know, so much focused, you know, on reducing costs, you know, through the severance program. My question to you is, you know, going forward, if you think from 2020 and on, does the bank, you know, have some sort of goal of not growing, you know, operating expenses at all and, you know, trying to, you know, become more competitive, you know, allow for some fee decline or use Opex as, you know, an operating leverage to, you know, leverage earnings growth down the road? Because with this program it could be that maybe your Opex next year could not grow at all or even decline. Is that a reasonable assumption you think considering the efforts that you've been undertaking? Thank you.

Candido Bracher: Thank you Marcelo. First, on the spreads, I am expecting the competition to come more from traditional competitors, and it is usually the case, I mean, when the economy starts to perform well, you have more appetite also from foreign banks in the local markets, I mean, the corporate sector faces quiet significant pressure in this situation. So, I am not seeing the pressure on spreads coming in any specific segment, I'm just thinking that, with a better economic environment, there will be more people willing to take credit risk, and this will possibly, I mean, generate some extra pressure on spreads. But, I mean, spreads have already been under pressure for quite some time, not too much pressure, but some pressure and I think this may increase.

In what relates to costs, I mean, we certainly intend to keep very strong focus on that. I think that cost reduction is a fundamental tool in order to enable the bank to be more competitive in pricing, and I think we will need to be more competitive in pricing, everybody will need to be more competitive in pricing going forward, therefore a strong activity in costs is fundamental there.

Marcelo Telles: And Candido, just one follow-up on your answer. Being very competitive on costs and being able to have better pricing, does that mean, you know, that you think you could sustain your current ROE levels, you know, where they are today? Do you think that they are sustainable, let’s say, in the short to medium-term at least with all these efforts that you are undertaking?

Candido Bracher: As you know, we guide our efforts very much in the bank on value creation, and so, I mean, I look at the ROE always in relation to the average cost of capital. I see a clear trend of decline in the cost of capital in Brazil, so I think that there may be some pressure also on ROE.

Marcelo Telles: Okay, that's very clear. Thank you Candido.

Candido Bracher: Thank you very much Marcelo.

Operator: Our next question comes from Neha Agarwala, HSBC.

Neha Agarwala: Hi, thank you Candido for taking my question. I wanted to understand that for your Rede business, the acquiring business, you made recently cuts in prices, but apart from competing in pricing, any other changes that you are making, structural changes that you are making in Rede which improves its competition given that it involves dynamic of the sector?

And my second question is, can we have any update on ITI? Is the platform operational, how is that behaving, how do you see it integrating with the bank? Any update there would be very helpful. Thank you so much.

Candido Bracher: Thank you Naha. So on the acquiring business, I think you are right, I mean, it's not only at pricing that we are looking, I mean, we have been investing a lot in improving the quality of our services, I mean, the quality of our machines, of our support service to the client and so on, and we are seeing improvements in the levels of satisfaction, which are not only derived from the pricing activity. As I have mentioned in another question in relation to competitors, I think we have really good examples here looking at the competition and, I mean, it keeps us under pressure to improve more the quality of our services.

In relation to ITI, I would tell, I mean, it's too soon to say more about this product, I mean, it is just being opened to some groups of clients, smaller groups of clients. I think we will know more next quarter and the quarter after that.

Neha Agarwala: If I can follow up on the acquiring business, have you adopted any other distribution model apart from the bank’s channels, especially for the micro-merchant segment? I believe you've been spending a little bit more on the marketing and advertising, but any other specific changes in your model or the way you reach clients that has been made for Rede? Thank you.

Candido Bracher: We have been focusing also more on the segment of the non-current account holders and we are investing a lot in the support for these clients.

Neha Agarwala: Okay, thank you so much.

Candido Bracher: You are welcome.

Operator: As a reminder, if you want to pose a question, please, press start 1.

The next question comes from Luiz Fernando Azevedo, Banco Safra.

Luiz Fernando Azevedo: Hi Candido, good morning everybody. My question is a follow-up on the ROE dynamics. Looking ahead, if you look at the appendix there is a breakdown of ROE per segment, that's a very good chart, and we can see a big improvement in the ROE of the credit operation. On the other hand, the service has been under pressure. I'd like to know, Candido, how do you see the ROE per segment moving ahead? And of course, the idea is… do you think that the consolidated ROE is already in a peak this 23.6%? And if you could open how is the assumption of the cost of capital that you are assuming now? Thank you.

Candido Bracher: Thank you Luiz Fernando. I think this chart that you refer to the business model, it shows the conveniences, the advantages of having a wide portfolio of products, I mean, services and credit, and over time we have seen services performing better and now we're seeing credit improving in the past one year and so on. And I make no specific forecasts here for these areas as even within the groups of insurance and services and credits, you have products which improve during the time and others which face more competition. As to the general, I'd just say that, I mean, I feel comfortable in having such a wide portfolio of products when one tends to compensate the other.

In terms of the ROE, what I can tell you is that the distance now between ROE and cost of credit is probably the widest in our historical series. So, let's see if we can keep the spread in levels.

You asked me what is my take is on how cost of capital is going to evolve. Here I am a bit appalled, let's say, because I see our cost of capital in 13 and with a reducing trend. On the other hand, I see the cost of capital used in developed economies be mainly around 10, way above the interest rate in these markets. I would expect some moment in time there would be a convergence, I mean, not that they would go to the same level, but that this wide margin would reduce in the developed economies. That's not what we are seeing so far. While we don't see a reduction in the cost of credit of 10% in the developed economies, it is difficult to imagine that Brazil will have a cost of capital which is only 2% above what you have in developed economies. So, I see this as a resistance for a drop in the cost of capital in Brazil.

Luiz Fernando Azevedo: Sorry, so you think that we are going to… we are already stabilizing the cost of capital?

Candido Bracher: Unless we see a drop in cost of capital in developed economies, I think, yes, that we are already around the bottom, around the narrowest margin, reasonable margin, between cost of capital in developed economies and in Brazil.

Luiz Fernando Azevedo: Okay, great. Thank you Candido.

Candido Bracher: Thank you Luiz Fernando.

Operator: This concludes today's question-and-answer session. Mr. Candido Bracher, at this time you may proceed with your closing statement.

Candido Bracher: Okay, just to thank you all for the very good questions and for the interest in our results. Thank you and have a good day.

Operator: That does conclude our Itaú Unibanco Holding earnings conference for today. Thank you very much for your participation. You may now disconnect.