Itaú Unibanco
International Conference Call
Third Quarter 2018 Earnings Results - October 30th, 2018

Operator: Good morning ladies and gentlemen, welcome to Itaú Unibanco Holding conference call to discuss 2018 third 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. Caio Ibrahim David**, Executive Vice President, CFO and CRO, **Mr. Alexsandro Broedel**, Group Executive Finance Director and Head of Investor Relations; and **Mr. Milton Maluhi Filho**, Itaú CorpBanca CEO. Mr. Milton is participating in this conference call as the future CFO and CRO of Itaú Unibanco.

First, **Mr. Candido Bracher** will comment on 2018 Third quarter result. Afterwards, management will be available for a questions and answers session.

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

Candido Bracher: Thank you. Good morning and welcome to our third quarter 2018 earnings conference call.

Starting our presentation on **slide 2**, we had another solid quarter with our recurring net income reaching R$6.5 billion and a consolidated ROE of 21.3% and of 22.4% in our Brazilian operation.

You can see that the growth of 1.2% of our financial margin with clients and the reduction of 9.4% of the cost of credit were the main drivers of the third quarter results. This positive performance was partially offset by the 2.1% decrease of our fees and result from insurance and by the 3.1% increase in our non-interest expenses.

The higher expenses were mainly influenced by Forex variation and by the collective agreement with the bank employees' union. Nevertheless, our expenses from Brazilian operations, excluding the impact from Citibank retail business, grew 0.9% over the past 12 months, well below inflation from the period.

Additionally, the credit portfolio grew 10.6% over the last year, while the nonperforming loans over 90 days improved 30 basis points at the same time. It is important to note that a 10-basis-points deterioration of the NPL ratio in the quarter was mainly due to a few corporate cases that were already properly provisioned.

Lastly, our capital ratios continued to improve despite the credit growth in 2018. The Tier I capital ratio reached 14.8%, which already considers the fully loaded Basel III capital requirement and also the impact of XP Investimentos minority interest acquisition.

On **slide 3** we present our income statement. You can see that our accumulated performance over the first nine months of 2018 generated a 10.1% growth in income before tax and minority interests. This performance was partially offset by a temporary higher effective tax rate in the period. The higher tax burden is caused by the accounting of our tax credits at a 40% rate, while we take current taxes at a 45% rate in accordance with current regulations, which should expire at the end of the year.

On **slide 4**, the financial performance reported on slide 3 is an essential element of our value creation process. Here, on slide 4, we show that our value creation reached R$7.2 billion in 2018, an increase of 36% on the last four years, which confirms our focus on capital discipline.

Also essential to our value creation process is our investment in technology, which, as shown on **page 5**, has increased 67% since 2014. This investment is of foremost importance to generate both cost efficiency and product quality.

This investment has promoted the constant evolution of our digital platform, including the user experience of our clients. This led to a constant growth in the adoption of our digital channels by our clients as they already amount to almost 11 million individuals by the end of September. Through our app, we opened more than 160,000 new current accounts in the third quarter, a 30% growth compared to the previous quarter.

Our digital branches represent more than 30% of the operating revenues in the retail business with an efficiency ratio that is more than 4,000 basis points better than a brick-and-mortar branch. This are some of the important KPIs tracking during our digital transformation journey.

Now on **slide 6**, we see our business model with a breakdown of our income statement between credits, trading, insurance, services and excess capital. We evaluate our business allocating capital to each and every transaction in the bank, creating a more critical capital management approach. This process allowed us to enforce our value creation in each area of the bank, linking it to each manager compensation.

As previously shown in this presentation, our value creation increased R$1 billion during the first nine months of the year, as it has been the case in recent years. Our insurance and service operations continue to account for the bulk of the value created, but it is important to point out that credit transactions have consistently created value throughout 2018.

Turning to **slide 7**, our credit origination remains strong, mainly in our individuals and SMEs credit portfolio. As mentioned in the past quarter, this growth is driven by credit demand from our clients, and not by the loosening of our risk appetite and credit standards.

On the corporate portfolio, the origination remains subdued due to lower demand from our clients and our minimum value creation requirements. However, this does not implicate in a reduced relationship with our large corporate clients, as we continue to advise and help them to access the debt capital market, in which we play a leading role, both in the distribution and in the origination of corporate debt.

Now, turning to our credit portfolio on **slide 8**, you can observe a growth rate of 2.1% in the quarter and of 10.6% over the last 12 months. This performance is concentrated in our individuals and SMEs portfolios, which in aggregate grew 11.9% over the last 12 months. Our portfolio in Latin America continues to be affected by Forex variation, especially when compared to last year. If we strip out this effect, the portfolio would have grown by 5.2% in the last 12 months, instead of the 27.4, as the table shows.

That brings us to **slide 9**, where we show our financial margin with clients growing by 1.2%, primarily because of the continuing change in the credit portfolio mix towards products with higher spreads, as shown on the previous slide.

Our risk-adjusted NIM increased 10 basis points in the quarter, also in line with the improvement of the credit quality of our portfolio. Also of note is the fact that, before the easing cycle of the SELIC rate, we were constantly questioned about the negative impact that a lower SELIC would have in our financial margin. Now, two quarters after the stabilization of the SELIC, the figures shown here indicate that our NIM is less sensitive to market volatility than people originally thought.

Slide 10 shows our financial margin with the market. This revenue, as you know, includes not only our trading gains, but also our asset and liability management, and it remained relatively stable in this quarter, despite the market volatility in the period.

Turning now to **slide 11**, we will take a look at our credit quality indicators. Our nonperforming loans over 90 days include 30 basis points over the year, consistent with our risk appetite and strategy. In this quarter, the 10-basis-points increase is caused by the corporate book and refers to the delinquency of a few companies that were properly provisioned and did not cause any negative effect in our PNL.

The NPL over 90 days of our SMEs portfolio reached 3.4% this quarter, which represents 150 basis points improvement over the past year. In addition, the delinquency of the individuals' portfolio, which remained stable in this quarter, shrunk 60 basis points over the last 12 months, both portfolios are at the lowest delinquency ratios since the Itaú and Unibanco merger.

Moving on to **slide 12**, we can see that our cost of capital has reached 2.1%, once again, the lowest point since the merger between Itaú and Unibanco.

Now on **slide 13** we show our coverage ratio, which has declined 1,300 basis points in the quarter. As mentioned previously, this indicator was likely to decline either due to the default of exposures for which provisions already existed, or due to the upgrade of the credit ratings from clients whose financial health improved. During this quarter, both factors contributed to the decline seen.

Slide 14 gives a breakdown of our revenues from services and insurance and, as you can see, these revenues were down by 2.1% in the quarter. Commissions and fees declined 1.1% in the quarter, mainly due to the advisory services and brokerage. This line was naturally impacted by the pre-election instability. Despite the higher competition in our fees and services business, its revenues still show a good performance growing 6.8% in 2018. It is fair to say that without the effects from the Citibank retail business, revenues grew 5.2% in the same period.

As for the lower result on our insurance operation in the quarter, it is related to the liability adequacy test revenue recognized in the second quarter. Since this test is held once every six months, we had no impact this quarter.

Now, turning to our non-interest expenses on **slide 15**, we had an increase of 3.1% in the quarter. This growth was mainly related to the effect of Forex variation in our expenses in Latin

America, as well as the impacts of the collective agreement with the bank employees' union. We note that our expenses from the Brazilian operation, excluding the impact of the Citibank retail operation, grew 0.9% over the past 12 months, well below inflation for the period.

On **slide 16** now, we show our Basel III Tier I capital ratios, which increased 60 basis points in the quarter, reaching 14.8%, already accounting the 19-bps impact on the acquisition of XP Investimentos. This evolution was due to our net income in the period, as well as to the effect of Resolution 4680, which changed the treatment of deferred tax assets originated from hedging strategies of international investments.

Now on **slide 17**, we are glad to announce that we have received the final approval from the Brazilian Regulators to acquire the minority interest of 49.9% in XP Investimentos. The total transaction value was R$6.7 billion and the financial settlement took place at the end of August. This acquisition reflects our strategy to diversify our net income towards less volatile revenues.

With this, now we conclude this presentation and we are open for the questions which you may have. Thank you.

Question-and-Answer Session

Operator: Ladies and gentlemen, we will now begin the question-and-answer session. If you have a question, please press the star key followed by the one key on your touchtone phone now. If at any time you would like to remove yourself from the questioning queue, press star 2.

Our first question comes from Eduardo Rossman, Banco BTG Pactual.

Eduardo Rossman: Hi, good morning everyone. I have a couple of questions on the acquiring segment. The first one is regarding the competitive environment in the industry where we can see that your prices declined a lot in the third quarter when compared to the previous ones. We did some calculation here and we can see here that the yield calculated as revenues divided by the card volumes declined 13 basis points quarter on quarter, to 1.08. So, I wanted to understand, you know, what drove, you know, let's say, the lower price in this quarter, if this was something, you know, more proactive, you know, from you. Also, what do you think we can expect if these prices should continue moving down, or if you believe, you know, that from now on, you know, this should be a more, you know, stable level? So, if you can elaborate a little bit, we would be grateful.

And the second question is also, let's say, on the industry. We saw Cielo announcing recently, it is leaving the banking lock agreements, so I wanted to know if it makes sense for Rede, you know, to remain in the agreement or not, or if it makes sense, you know, to have the agreement at all from now on.

I think clearly some of the new entrants they have been able to be very aggressive on prices because they do a lot more prepayment than incumbents, so I wanted to understand here the view of the bank. For the bank, I understand that the end of this agreement is bad, right, because it increases the risk on the loans that have car receivables as collaterals, but on the other hand, this could help, you know, Rede to become more competitive, you know, when compared to the other ones. So, if you can talk a little bit about this as well, I would be thankful as well. Thanks.

Candido Bracher: Good morning Eduardo, thank you for your questions. So, first, on the acquiring business and the competitive environment in the acquiring business. I think it's no secret, everybody is witnessing how competitive this business has become in the past two years, and it's becoming increasingly more competitive. In this scenario, we have first lost some market share due to competition, but we have restructured our activity in many ways, with investments, and we have been able now to stop this loss in market share.

As to the prices, I mean, we don't make the prices. The competition makes the prices, the market makes the prices, so I can't tell you if they will keep on falling or not. But I could say that I see nothing in the market that indicates that the competition will ease in the near future. So, as you know, I mean, we have created Pop Credicard in order to compete in another segment, we have increased significantly our direct sales force, and we will keep on competing in this market expecting to bring a better service to our clients and to be a strong competitor in the segment.

About the SEG, I mean, the agreement. Cielo has announced that it will leave the SEG, we have announced as well that we are leaving the SEG. Yet, I expect this should not happen, neither for Cielo nor for us. I believe that the end of this agreement is first and foremost a loss to the system, not to the bank. Especially a loss to the client. The clients today have access to this type of credit that in Portuguese we call “fumaça” (smoke), which is the ability to discount revenues which are still to be… of sales which are still to be made. And, I mean, this SEG enables this credit to be made, it is a safer credit and first it has a lower interest rate, which is very beneficial to clients. Without this agreement, without the SEG, such credits – “crédito fumaça” - cannot be made.

There is an effort led by the Central Bank to establish a way in which this could continue being made. An agreement has already been reached on how this market should function in the future, but it takes some time, it takes about two years for all the technical evolution to be made, and then, when this is done and ready, all the participants will have access to discount in receivables in the market, thus improving the rates for the companies. And what's being worked upon now is a solution meanwhile, I mean, between now and two years from now.

I trust that the efforts of the Central Bank and of the banks will succeed and we will be able to find some way of functioning that will enable this “crédito fumaça” to keep on being made so we won't have to leave the agreement.

Eduardo Rossman: Perfect. Very clear, Candido. Just a small follow-up on the “fumaça” question. Do you expect any increase in provisions because, you know, of the, let's say, of the deterioration of these collaterals, or you don't think that this is going to happen?

Candido Bracher: I don't think nothing significant can happen there, Eduardo.

Eduardo Rossman: Okay, thank you very much.

Operator: The next question comes from Carlos Macedo, Goldman Sachs.

Carlos Macedo: Yes, good morning Candido, gentlemen, thanks for taking questions. A couple of questions more on the banking side. First, you mentioned during your presentation that much of the growth that you've been seeing so far, the acceleration at least, has been driven by demand and not by appetite. I think I asked this question on last couple of quarters. You know, now that the elections in Brazil are done, we have an outcome, of course you still need to see the new president come to power and govern, but what will it take for the risk appetite of the bank to improve? I mean, on the asset quality side, NPLs are at the lowest level they've been, as you said, since the merger, and cost of risk has been pretty much flat. What does it take for your risk appetite to increase and what would that mean for loan growth if it did?

And I have a second question that's on asset quality specifically on the consumer side, you know, volatility on the corporate, but the consumer side has been pretty steady. Do you see any room for further improvement there given where you are? The cost of the risk there hasn't really declined that much, it's actually been going, trending a little bit upwards, at least on the retail side. How do you think about that going forward in terms of the cost of risk of that specific segment? Thank you.

Candido Bracher: Thanks for your question, Carlos. You said you've been making these questions for the past two quarters, making the same question. This time, I may give you a different answer.

So, as to risk appetite, first, just to be precise on what is risk appetite and what is not risk appetite. Risk appetite for us means that we don't lend to companies or to individuals with risk or probability of default above a certain level, which stablishes different levels for different segments. So, how have we then been able to increase our portfolio and to increase our credit activity? Because companies get better when the economy gets better and their probability of default decreases. So, companies which were out of the risk appetite they get in the risk appetite as the economy improves and as they improve.

So, changing the risk appetite would mean accepting lending to companies and individuals with a higher probability of default. We think that the steadiness we had seen in the improvement of companies and the perspectives we have ahead may encourage us to review these levels of probability of default below which we do not land. I mean, we are studying this as we speak, and we may submit to our Board some measure in this direction over the cost of this next quarter.

So, this is your first question. Your second question, if I understood well, was about the perspectives of cost of risk on the consumer side. It has really improved very significantly, at some moment it should stabilize. We do not see the signs of it yet, I mean, so far it continues to improve or be at a slower pace, but it continues to improve.

Carlos Macedo: Okay, thank you Candido. Just a follow-up on the first question, I don't want to flatten around your guidance for next year, but a stronger risk appetite, I mean, you are already growing at 13% per year. Would that mean loan growth potentially staying in the mid-teens next year if the risk appetite doesn't really go up, or is that a little bit too aggressive for the size of the market as it is now and the prospects that we have for GDP growth?

Candido Bracher: Carlos, I cannot right now estimate what the loan growth will look like for next year, but what seems safe to say is that the growth for next year will lean more upon credit than it has been this year.

Carlos Macedo: Okay perfect, thank you Candido.

Candido Bracher: You're welcome.

Operator: The next question comes from Jason Mollin, Scotia Bank.

Jason Mollin: Hello. Thank you for the opportunity to ask questions. My first question is again on loan loss provisions and the declines we've seen, and I would call "normalization", I guess, the cost of credit as well as loan loss provisions to loans we've seen in the chart you showed for all the history there, we are at the lowest levels. Should we expect levels to increase as loan growth accelerates, or can they continue to decline? Would be my first question.

Candido Bracher: Thank you Jason. As loan growth accelerates you have a natural tendency for these levels to increase because you have to make provisions for the new loans. However, given the very high level of the coverage ratio that we present, as I have been saying over the past quarters, I mean, this level tends to decrease over time. It will decrease because some companies will default, they were added to the denominator, or it will increase because some companies will improve, and their provisions will be reversed.

I think this is still a trend, but normalization, as you named it, I mean, which we should see still for one or two years ahead. And this trend, of course, tends to reduce the cost of credit. I mean, what will be the balance between both trends, I mean, one of increase because of the total portfolio and one of decreasing because of the decreasing of the coverage ratio, I don't know.

Jason Mollin: Okay, thank you for that. Let me ask you a second question on the credit card business. So, cards now represent about 35% of the loan book, around R$69 billion, only less than 9% are revolving credit. We know… I think you reported about 83% are transactional charges including installments without interest. So, I just wanted to understand how you see these potential changes in this market, specifically the use of interest-free installments, and we've seen some push to reduce the use of interesting installments and move to installment payments and charge in interest rates. How do you think about this issue and what are the implications for Itaú and the credit card market in general?

Candido Bracher: Okay, Jason. Well, as you know, interest-free installment is embedded in the culture of Brazil, it's something that every retailer sells on interest-free installments. Just recently - one year ago - the retailers have been allowed to have a discount when the sale is not made in interest-free installments. As this habit becomes more widespread, then there tends to be a tendency to increase the interest-bearing credit, which is where we place our efforts.

So, our main efforts in the credit card area is to increase interest-bearing portfolio. I think we are being successful there, I think this is a trend which should increase as we go forward, but

I don't think interest-free installments will ever be excluded, will ever be finished. There are too much of a traditional already in the market, a lot of the retail market depends upon it. But as we create alternatives for it, and the alternatives, I mean, are discounted value and then bearing interest in the financing, I think we would be able to grow our credit card portfolio that bears interest.

Jason Mollin: Can you share a little bit of this 83% that you call - I would call - “transactional charges”? What portion of that is the interest-free installment versus just the usage when the card payment is due by the client paying it off in full? What percentage of that is actually due to this interest-free installment product?

Candido Bracher: Jason, I don't have this figure right now with me. I will have to ask Gustavo to call you back with this.

Jason Mollin: Great, thank you very much.

Candido Bracher: You're welcome.

Operator: The next question comes from Jorg Friedman, Citibank.

Jorg Friedman: Thank you very much for the opportunity. I have also two questions. The first is related to your fee income business. I was particularly intrigued by the performance of the asset management in your fees. So, just wondering if you could describe a bit what drove the performance in this quarter, if you could attribute that only to competition, or it could also be, you know, the initial signs of the effect of, you know, Itaú opening its platform and migrating a bit from the pure asset management fees to distribution fees, something that will be accommodated over time.

And my second question is related to costs. Of course, it became very clear to us in your presentation that the bulk of, you know, the increase has been related to the LATAM unit, given the depreciation of the real during the quarter as well, but you also had this impact of the labor agreement. So, just wondering, you know, if you strip out the FX impact, what we could, you know, think about structural growth? The question is more related if the LATAM units will continue pushing, you know, costs above the inflation for the foreseeable future? Thank you very much.

Candido Bracher: Thank you your Jorg. First, your question on the asset management. No, the decrease in fees in asset management is not related toward change in spend or distributing more third-party products or so. It’s very specific in this quarter, it's due to smaller performances, I mean, we have most of our funds this year, in the first quarter, after yield in the industry and so performance fees were very strong in the first semester and was a bit less or so in this third quarter. So, this was the reason for the impact in the asset management fees.

As to costs, I mean, what relates Latin American costs, if they will be above or below our inflation in Brazil is related essentially to the exchange rate variation. We cannot forecast that.

Locally, their costs tend to increase below inflation, as it is the case in Brazil and as we intend to continue to do so in Brazil.

Jorg Friedman: Very good point. Just a brief follow-up on that part of Latin America, you know, some of the units, particularly Chile and hopefully Colombia soon, are recovering and the question is more related to if this growth observed abroad could continue pressuring expenses, you know, in the quarters ahead, or if you believe that at some point we will converge to the guidance this year and the lower levels for next year? That was a bit more of my point. Sorry if I was not clear.

Candido Bracher: I think that's the improvement in performance, especially in Chile in Argentina, they have more to do with the way management is evolving and with the way new managing guidelines are being implemented in these banks than with investments in itself. So, I think, I mean, we will be able to keep on improving the performance there, keeping expenses below inflation in these countries.

Jorg Friedman: That's perfect, very clear. Thank you very much.

Operator: The next question comes from Rafael Frade, Bradesco.

Rafael Frade: Hi good morning all. My question is really to the guidance you… on the press release you reaffirm the guidance, but you don't mention anything on the… during your initial presentation. I would just like to get a sense of how you are seeing the guidance for the year. A few lines now seem to be looking for credit, it seems that probably it will be above your guidance, in fess maybe we can be more in the low end of the guidance. So, I would like to hear your thoughts about it.

Candido Bracher: Okay, thanks for the question, Rafael. As you know, I mean, we provide guidance for these various lines and we know that you make your calculations and you end up with a guidance for final results. We do the same thing here, and when we look at this calculation we think that we will be well within the guidance, the result that you have calculated for final results.

As to the individual lines, you are right, I mean, there are some cases where we will be around the extremes of the guidance, either positive or negative.

Rafael Frade: Okay, thank you.

Operator: Next question comes from Domingos Falavina, JP Morgan.

Domingos Falavina: Thank you Candido and team for taking the question as well. Only two quick questions. One is on headcount. We notice about 1,000 employees increases Q-on-Q, and I believe, in addition to the FX and also the salaries, one of the reasons for the Opex increase, according to the release, was the efforts or the focus on the commercial efforts on the acquire as well as on the insurance. So, if you could provide a little bit of detail of this headcount increase, what percentage points you acquired, how many people or actually didn't increase your acquire sales effort by, and as well as your insurance. And then I'll go for the second question.

Candido Bracher: Thank you for your question, Domingos. Yes, I mean, you are right, there has been a headcount increase and there will continue to be investments in people in these two areas, I mean, insurance and the acquiring business. I think that this past quarter our figures, they were around 300 for the acquiring business and 400 for the insurance.

We expect to have, of course, efficiency gains in any other areas of the bank, which will offset the impact on costs created by this investment in these areas.

Domingos Falavina: Super clear, thank you. And one additional, one on the acquiring. It seems that the POS rental is sort of the most commonly used negotiation tool to retain clients, and it seems Itaú is very focused in keeping this client relationships as seen by the number of clients as well as by the volume growth. So, my question is, when you look at this POS rental revenue stream, do you see that decreasing or becoming irrelevant in how long? Is that something that you believe will continue to be a relevant stream, or it seems to be important in the short term?

Candido Bracher: You are right in saying that we are trying to adapt our products and our offer to customer needs, to clients' needs, and one of the main victims of it is the POS rental, and apparently it will continue to do so, POS rental tends to continue to decrease.

Domingos Falavina: Okay, very clear. Thank you very much.

Candido Bracher: You're welcome.

Operator: The next question comes from Marcelo Telles, Credit Suisse.

Marcelo Telles: Hi good morning Candido, good morning everyone, thanks for your time. I have two questions. The first one, it's more of a broad question regarding fintechs. How do you see the threat of fintechs to your business, particularly, you knos, considering your expectation of probably like accelerating your loan portfolio, you know, down the road? So where do you see the biggest threats, you know, from fintechs, you know, for you? If that is something that could perhaps change the dynamics a little bit in terms of this loan growth acceleration into the future?

And my second question is regarding costs, you know, kind of a follow-up on Falavina's question. Considering that you expect to accelerate your loan growth, you know, going forward, how should we think about your operating, you know, cost base down the road? Can you still continue to deliver, you know, the strong cost control you've delivered, you know, in recent years, or you think because of higher learning growth, you know, you might start to see an acceleration on your operating expense base? Thank you.

Candido Bracher: Thank you Marcelo. So, first you question on fintechs. I must tell you that I see the fintechs activity much more challenging for us in the service side than on the credit side, at least for the near future. Most of the activity we see in fintechs and new competition, I mean, they come on investments, they come on the acquiring business, mainly they come on services.

In credit, we do not see yet such an intense activity by fintechs, and we see the quality of our credit operation improving very consistently with the use of artificial intelligence, with the use of technology, the way our credit models are improving. So here we have the impression that we can compete on a more even basis using technology to compete against fintechs. So, my expectation is that the credit portfolio will experience good growth ahead of us.

And going to your second question, I don't see a huge impact in costs, in the growth of the portfolio. I think we have an established structure and within this structure, I mean, we will be able to grow the portfolio without adding much cost to it, these are part of the scale gains. It is a completely different scenario than in the acquiring business or in the insurance business, where we need more people to increase sales. I mean, we don't need more people to increase our credit activity.

Marcelo Telles: Thank you Candido, very clear. Just one additional question, if I may. Regarding Rede, where do you think you are from a technology, you know, standpoint, you know, from a service standpoint, you know, compared, you know, to newcomers in that business, you know? Do you think you still have to do with a lot of like legacy issues, you know, that have been, you know, potentially impacting your business? If you could just elaborate a little bit on the service, you know, and technological strategy of Rede, that would be great.

Candido Bracher: Okay. Marcelo, I think we have still quite a way to go in our acquiring business, I think we can improve much more there. It is not the case of Pop Credicard. Pop Credicard is already born and is a new platform. But in the traditional Rede, I see a lot of room for improvements in the quality of our offer to our clients, and, I mean, we are following up all the aspects of this offer and we are following closely, I mean, the improvement in each of them, and we think we will be able to improve much more and offer much more competition to the market.

Marcelo Telles: Thank you very much.

Candido Bracher: You're welcome.

Operator: Our next question comes from Philip Finch, UBS.

Philip Finch: Thank you, Candido Bracher for the presentation. Couple of questions also from me. First, a follow-up to Marcelo's question on disruption risk. We've seen a few new digital players coming into the market in the last year or so offering free banking, free checking accounts and transfers. Is that putting pressure on you? Are you seeing any customers switching to this new startups or digital players? And are you planning to also reduce your fees as well related to this? So, I guess ultimately, you are benefiting from cost reduction as result of technology and digital banking. Is there a risk that these cost benefits are going to be passed through to your customers partially or fully via lower fees?

And the second question is regarding your digital… sorry, your dividend payment or payout outlook. So, in previous calls you've mentioned the potential for a higher dividend payment given that, well, at not least how you've issued some additional Tier I capital. Now loan growth clearly has picked up much faster than anticipated. Does this in any way reduce the potential for dividend payments going forward? Thank you.

Candido Bracher: Thank you for your questions, both very good. First question deserves a little longer answer. Of course, these fintechs and all this new competition is a threat to the business. I have no illusion that this will not somehow affect our margins. I think margins will suffer, as they always suffer when there is petition, when there is increased competition.

As to the way we compete, I have seen this phrase written somewhere, which made sense for me, which is that "incumbents must find innovation before innovators find distribution". I think this is more or less the race that is established. So, we as incumbents must find innovation, must be able to compete with the products offered by this new competition. And this is what we are doing, I mean, this is why I have shown here our investments in technology, I mean, we could go on much longer about investments in technology, we could mention that, I mean, we have traveled the number of data scientists in the bank, and many other progresses which we are seeing in order to keep improving our efforts as new competitors appear in the market.

So, I think that in this game we can compete very well, but margins will be compressed. I think it will be more so in services than in credit. I think in credit our condition to compete and our gains of scale and, really, I mean, the accumulated knowledge on credit evaluation that we have, I mean, presents and enables us to compete even more strongly in credit than in services. But, I mean, I think this is the name of the game going forward, is to face this competition in every market. We mentioned here the acquiring business, the insurance business, we have the cash management business, there are many businesses like this.

I believe we offer the benefit of a complex offer of structured financial products, the possibility of being a one-stop-shop and so on. And we think that, if we are able to constantly improve the quality of our products, to constantly improve the user experience of our products, which is our main focus now, I mean, we will succeed in this competition and we will keep the high levels of returns that we have been offering to our investors.

Second question on dividend payout. Yes, I mean, as you know, our risk appetite states that we should have, by the beginning of the year, 13.5% Basel III Tier I ratio, and what is above it and will not be consumed by acquisitions or by expected changes in regulation, will be distributed as dividends. So, as I look to next year, I think that we will have a fair level of dividend distribution. If portfolio grows much faster than we expect, then, of course, we will distribute a little less dividends because more capital will be required to keep the 13.5% level.

Philip Finch: Okay, perfect. Thank you very much Mr. Bracher.

Candido Bracher: You are welcome.

Operator: The next question comes from Felipe Salomão, Citibank.

Felipe Salomão: Hi Candido and team, good morning, thanks for the question. I have a few questions about Credicard Pop. Is it possible to share more details about the recent performance of this business? For instance, what is the current POS base of Credicard Pop, how many clients are, I mean, Credicard Pop has been able to add to its portfolio on a monthly basis? And if you could also, if possible, of course, share with us some numbers about estimated market share in the macro segment? Both the current market share and the market share of net additions, that would be great.

And the last question that I have is why Itaú decided to use the systems of First Data to do the processing of Credicard Pop transactions instead of using Rede? These are my questions. Thank you.

Candido Bracher: Thanks Felipe, for the questions. Concerning Credicard Pop, we are not disclosing many information on this, but I think the information I can give you is that we are on track to reaching our goal of 120,000 clients by the end of the year. Why did we decide to use First Data and not Rede as the platform supplier for Credicard Pop? Because we are experimenting with different alternatives. I mean, this is part of our striving to offer our customers a better user experience and we are challenging our own internal platform to collect this and we expect to have both improving like this.

Also, I could have answered this in another way too, and it would also be through, Felipe, this question about First Data. You know that, I mean, in every company and in every bank, there is a competition for IT resources. We have a high competition for IT resources in the bank, we have a very clear and established method of measuring net present value of each investment that we propose to technology. So, when a new product comes, which has a longer rump-up, it is easier for them, it is easier to calculate the results and the prospects of this investment if you do not rely on our internal IT, but if you can hire it externally.

Felipe Salomão: Okay Candido, thank you very much for the answers.

Candido Bracher: Thank you, Felipe.

Operator: The next question comes from Nicholas Riva, Bank of America.

Nicholas Riva: Yes, thanks very much, Candido, for letting me ask questions. I have two questions. The first one, on the level of NPL creation, so we did see an increase in this level in the quarter, about R$5 billion. You did mention the rollover of some overdue loans, which were 15 to 90 days overdue, and now they are more than 90 days overdue, but if you can comment on this increase in the NPL creation, if it's something that concerns you for the coming quarters.

And then my second question, on your guidance for loan growth. So, in the call, you seemed to be more positive on credit growth going forward, but if I look at the guidance for loan growth, you didn't change it for this year, the 4% to 7%. And if I look at what implies for the fourth quarter, it seems to imply basically zero growth quarter on quarter for the 4Q. So, my question there is, the acceleration that you are seeing in loan growth will be more of a 2019 story rather than for the quarter story? Thanks.

Candido Bracher: Hi Nicholas, thank you for your questions. Concerning the NPL creation, I mean, these companies that went in arrears over 90 days in this quarter, I mean, these are cases that date back to 15 or 16. I mean, in 15 or 16 we identified companies which were much weaker due to the huge crisis that we went through, we have made precautionary provisions for these clients and we follow up these clients very closely in a different area of the bank that we created especially to follow up clients like these since.

So that, I mean, when these clients they eventually default, as it was the case with these companies now, the level of provisioning is very high, and in this case, it was above 80%, in the case of both. And we expect we will not lose 80% of this credit eventually going forward. So, this does not present any special concern to me going forward.

And as I look into our book of similar situations, we see some companies improving, and others still deserving a closer attention. Expect that if the economy as a whole improves, we may have more positive than negative surprises in this portfolio going forward. And we have not seen new companies being added to this portfolio. So, we are not… during this year it has not been significant the number of new cases added to these cases of bigger concern.

Guidance for loan growth. We are reaffirming the guidances in general with this, this disclaimer that I mentioned in the previous question, I mean, in some lines we may be around the top or the bottom of the guidance.

Nicholas Riva: Okay, thanks very much Candido.

Candido Bracher: You're welcome Nicholas.

Operator: The next question comes from Carlos Gomez, HSBC.

Carlos Gomez: Good morning gentlemen, thank you for taking the call. I have a question about two products. When I look at page 69 of your presentation, I want to ask you about legal financing and mortgages. And obviously you are much smaller than you were before, but you are regaining ground. What would be your aspiration? Do you want to have a loan portfolio as large as you had in the past? Do you think it would be a particular percentage of your total individual portfolio, or do you have a market share target as an institution?

And on mortgages, which are now 21% of your legal loans, at what point is funding going to become an issue and would you need deeper instruments than the credit accounts? Thank you.

Candido Bracher: Okay, thank you Carlos for your questions. About vehicles, I mean, this is a market which we think we will grow and where our presence will grow. As you know, I mean, we have restructured completely our activity in this market, we were once market leaders, now we are a much smaller participant in the market, and we want to regain terrain here and we have invested a lot in the quality of our products, in the processing, in technology in order to give better user experience, a quicker turn time to customers and we think we will be growing this portfolio consistently above inflation going forward.

And sorry, your second question, Carlos?

Carlos Gomez: About the funding for the mortgage portfolio.

Candido Bracher: Okay. Funding for the mortgage portfolio does not present a special concern right now. As you know, the mortgage portfolio is funded fundamentally by what we call “Caderneta de Poupança”, I mean, the savings deposits of the bank and we have a very comfortable margin to fund the expected growth of this mortgage portfolio.

Carlos Gomez: So, you guys don’t expect any problem in the next, let’s say, two or three years, as you already?

Candido Bracher: I expect the portfolio to grow, but I don't expect problems in funding it.

Carlos Gomez: Thank you very much.

Candido Bracher: Thank you, Carlos.

Operator: Ladies and gentlemen, as a reminder, if you would like to pose a question, please press the star key followed by the one key on your touchtone phone.

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

Candido Bracher: Well, just to thank you very much for the interest in our call, excellent questions you made. And we are confident that we will continue to show, I mean, strong results going forward. Thank you very much.

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