Itaú Unibanco - International Conference Call
First Quarter 2019 Earnings Results
May 3rd, 2019

Operator: Good morning ladies and gentlemen, welcome to Itaú Unibanco Holding conference call to discuss 2019 First 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, **Mr. Alexsandro Broedel**, Group Executive Finance Director and Head of Investor Relations, and **Mr. Marcos Magalhães,** CFO of Rede.

First, **Mr. Candido Bracher** will comment on 2019 first 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: Well, good morning everybody. Welcome to our first quarter 2019 earnings conference call.

We will start the presentation on **slide 2**, where we show the main highlights of our performance for the quarter. You see that our recurring net income was R$6.9 billion, which represented a 7.1% growth when compared to the same period in 2018, resulting in a ROE of 23.6%. This performance was mainly related to an improvement in our financial margin with clients, which was partially offset by a lower financial margin with the market. Our cost of credits remains relatively stable and non-interest expenses were up by 4.1%, below the inflation for the period. In the next slides we will provide further details on these figures.

On **slide 3** we show the value created by the bank, which amounted to 2.9 billion in the quarter, in line with our focus on creating value for our more than 1.2 million individual shareholders. Actually, you see that the 2.9 billion is a record figure in our history.

Page 4 we show that our total credit portfolio grew 7.7% over the last 12 months driven by individuals and SMEs, which have grown 12.7% and 17.6%, respectively. Origination continues strong in both portfolios, resulting on richer credit mix, which will be shown in the next slide. In addition, we observed in this quarter an upsurge on the corporate origination at 18% growth, while corporate bonds issuance remained solid.

On **slide 5**, the 1.1 billion increase in NII was mainly due to the change in the mix of our credit portfolio, as shown in the previous slide, and superior average balances. This NII performance resulted on an NIM of 10% for the quarter.

On **slide 6** we show our financial margin with the market, which amounted to 1.2 billion, well in line with our expectations and guidance.

Turning to **slide 7** now, we show our credit quality information. Short-term delinquency increased 13 basis points in the quarter due to seasonal effects on individuals' portfolio related to a higher concentration of expenses for households, such as cars and housing taxes, among others. It is important to mention that despite this increase and the change of the credit mix towards higher interest-bearing loans, short-term delinquency ratio is below the level seen in the same period in 2018.

The 90-day delinquency ratio increased 11 basis points in the quarter, but it is also below the level seen on the same period in 2018. The increase in the quarter is due to a couple of cases on the wholesale portfolio that were already fully provisioned. This event led to the decrease of our NPL 90-day coverage ratio, as we have been anticipating. It is important to highlight that the coverage ratio for the retail NPL 90-day continues to show stability despite the change in mix towards higher risk and interest-bearing loans.

Lastly, the cost of credit ratio increased 30 basis points in the quarter as would be expected given the credit portfolio growth and the acceleration of the change in credit mix in the period.

Slide 8 shows our revenues from services and insurance, which grew 1% when compared to the same period in 2018. This small growth is a direct result of the competitive environment, especially related to the acquiring business. Also of note is the impact of the regulatory cap on the interchange fees from debit transactions, which started to impact our operations on the 4Q last year.

Turning now to **slide 9**, we show that our non-interest expenses grew 4.1% when compared to the first quarter 2018. Our cost to income ratio improved 240 basis points on the quarter, but it is still above the same period of last year. We intend to continue to work tirelessly to keep costs under control and improve operational efficiency.

Slide 10 now illustrates the strong organic capital generation of the bank as we finished this quarter with a Tier I ratio of 14.6, coming from 13.5 in the end of 2018. The main driver of this growth was our profitability in the quarter, as well as the lower density of our risk-rated assets. Also of note was the approval by the Central Bank of Brazil of the additional Tier I instrumental we issued on the local market in the beginning of the year, which added 30 bps to our capital ratio.

Slide 11 talks about our new initiative on the acquiring business. Rede will no longer charge interest on the prepayment of credit card transactions, which will be paid in T+2. This is valid for credit card purchases with no installments and to clients with Itaú domicile and annual revenue up to R$30 million, which covers about 98% of the market. We see this as a way to better serve our clients and harmonize practices with international standards.

Now on **slide 12**, we present our revised guidance for the year. We revised the guidance as a consequence of two management initiatives: First, the new acquiring payment arrangement with Rede previously mentioned; and second, a more rigorous revision of our cost structure motivated by our perception of a more modest macroeconomic growth for 2019.

As a matter of fact, in the beginning of the year we estimated GDP growth at 2.5% when we gave the initial guidance, and now our economic team estimates GDP growth at 1.3%. Therefore, we revised downwardly our expectations for financial margin with clients and also fees and insurance.

Additionally, we reduced our expectation for non-interest expenses growth for the year. When seeing in aggregate, these changes do not have a significant impact in the guidance implied net income.

With this, we conclude this presentation and are now open to any questions 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 1 key on your touchtone phone now. The questions will be limited to two per participants.

If at any time you would like to remove yourself from the questioning queue, press star 2.

Our first question comes from Jorg Friedman, Citibank.

Jorg Friedman: Thank you very much for the opportunity, gentlemen. I have two questions. The first, it became evident in this quarter – and according to what Candido just mentioned – that the environment is tougher for revenue growth and the bank is trying to curb costs to same profitability. However, I'm surprised by the significant cut in the Opex guidance. So I was just wondering if you could provide a bit more color on the reasons behind lower cost growth for this year. Are you reducing investments in any specific areas or trying to simply optimize costs through enhancement of process? And this is the first question.

The second question, I know that you have that methodology that takes into consideration profitability and, you know, the expansion of risk-rated assets to come up with your payout. In this quarter, in particular, we saw an optimization of risk-rated assets, I believe that this is related to stronger growth in the retail portfolio that demands lower RWA, and at the same time your profitability continues to be very solid. You added 8 basis points in terms of your common equity Tier I, and just with internal capital generation, and in addition you also had a bit more AT1. So, taking into consideration all of these dynamics and where you are in terms of common equity Tier I, do you believe that you could have, you know, how much of payout this year? Thank you very much.

Candido Bracher: Thank you, Jorg. So, let me take your two questions. First, on our cost and the change of the guidance and costs, I mean, all the actions we've taken since the beginning of the year in order to control and reduce cost expansion in the bank.

Actually, they were not costs by the perception of higher competition in the market, of a more competitive environment, the main reason was the perception of slower economic growth. As I mentioned, we began the year estimating GDP growth of 2.5% and now we are estimating it at 1.3%. So, we had early on the game the perception that the economic growth in the year would not accommodate a cost growth as we had anticipated.

And the measures we've taken they involve virtually every sector of the bank. We have gone in details through costs in every executive director area and there were cost reductions across the Board in the bank. They did not affect a sector specifically nor did they affect investments specifically.

Second, the payout. The payout is not a target itself, the payout is a consequence of the level I capital that we want to have. The Board establishes that by the beginning of the year we should have a level-1 capital of 13.5%, taking into consideration the expected portfolio growth for the year, expected RWA growth for the year, possible investments and possible changes by the regulator, which may require more or less capital.

So, taking all this in consideration, the board tells us in the beginning of the year that 13.5 level I capital. This is what we will continue to do, I mean, we are, in terms of date, we are still following year that we will make these calculations and, seeing from today, they point to a significant payout again for the year of 2019.

Jorg Friedman: Yes, that is perfect. I really appreciated, Candido. Just following up very quickly on the first point, if I understood it correct, you are not, you know, curbing any investments, you know, in technology and, you know, the plans that you had in terms of restructuring some business areas, such as insurance, for instance. So, everything continues as before, you know, the result of the lower cost guidance is more related to enhancement of processes. Is that correct?

Candido Bracher: We are certainly not cutting any investment in technology, and to be very transparent with you in insurance we are not cutting any investment as well, but we are lengthening the profile of the investment. Not because we wanted to save money with that, but because we found out that it takes a little longer to train the workforce that we hire, so the rhythm of hiring is going to be a little slower than we had originally anticipated, Jorg.

Jorg Friedman: That's perfect. Thank you very much for the clarifications.

Candido Bracher: Thank you.

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. First question, Candido, you mentioned that you now expect weaker economic recovery in Brazil this year, you've reduced your GDP forecast, but at the same time you're maintaining your loan growth guidance unchanged. So, I was wondering, how do you expect loan growth to be throughout the year, especially if the economy is to be decelerating? If you can talk about how you are seeing demand from large corporates, the large corporate segment continues to contract while consumer lending has been growing at a double-digit pace. So if you can just give us some color here with, you know, your appetite for lending, what kind of trends you are seeing and why you maintain your guidance for loan growth unchanged even though you expect a weaker economy?

The second question is related to the strategy at Rede. It seems like, you know, some of this change in your guidance is self-inflicted, right, your lower fee income generation and some of your margin, as well as because of the actions you are taking at Rede. However, you started to be more aggressive in prices in the second quarter last year, so it seems to me that even though you are reducing prices, you are not seeing the benefits either in volume or in revenues. When do you expect that to change? And if you can give us some color as well with regards to the profitability of Rede on a standalone basis, you know, if you are already operating over a return on invested capital below your cost capital or, you know, if you still are being profitable in the business. Thank you.

Candido Bracher: Mario, thank you very much for the two good questions. First, the guidance for loan growth. Despite the fact that we see the economic growth by half of what you saw in the beginning of the year. There is one factor which is that, despite expecting the economy to grow less this year, we expect the pension reform to be approved in the second half of the year, and the loan growth is measured by the figure at year-end, so this plays a role in there.

But the main factor, I would say, is that we are feeling encouraged by the loan growth we are experiencing, not only in individuals and SME, but mainly in March and more recently we saw an upsurge in the demand for corporate loans at prices which are compatible with our cost of capital. So, I mean, we remain confident that, I mean, given these expectations we will finish the year within the limits of our guidance for loan growth.

Now, in relation to Rede. It is difficult to make precise forecasts in the market which is changing so fast as the acquiring market in Brazil, to be honest with you. Last year, as a matter of fact, we have started to lower our rates in the second quarter and, as a consequence, we leveled our market share and we stopped losing market share.

But I must say that, in last year movements, we were mainly followers, I mean, we reduced our margins following the market. With this recent movement, we anticipated what we saw as an unavoidable trend in the market. To paying in T+2 is what markets in the whole world do, it didn't do in Brazil because of our historic very high interest rate, volatile inflation and so on, and, I mean, the recent stability in interest rates and inflation under control I think will drive the market inevitably to the T2 standard. So here we are basically anticipating this move.

And you are correct in saying that the change in guidance was mainly provoked by self-inflicted measures, be it the measures related to Rede and the T+2, be it the additional cost controls and cost savings that we have implemented.

Mario Pierry: Thanks. Candido, just a follow-up. It seems that your competitors now then are following you in reducing prices in the acquiring business as well. So, where do you think this stops? Because it seems like, ok, last year you were – like you mentioned – being a follower, now you're being a leader, but then someone else might want to be a follower. How do you see the profitability of this business then over the long term?

Candido Bracher: I think the profitability of this business will suffer if you don't take into consideration increases in volume and if you don't take into consideration innovations, which I think is inevitable in this market. But certainly, I mean, it's not a market where you can give yourself the luxury of protecting our margins and seeing our market share be washed away very fast. So, you have to play along, I mean, that’s competition.

Mario Pierry: Okay, thank you.

Candido Bracher: Mario, wait. I will ask Marcos Magalhães, CEO from Rede, to complement.

Marcos Magalhães: Just one thing that I think it's important to stress is that, despite competition being very fierce on pricing, it is not being irrational competition, so we are going towards maybe what Candido said in terms of what this standard international practice is, I think that the margins of this business in Brazil will also converge to international standards, and as of now, it is still a couple of inches above international benchmark. So, we believe that we will go and, again, it’s not, at this point, we don't see it's irrational competition.

Mario Pierry: Okay, thank you. Just to take the opportunity, when you mentioned that the profitability of margins is in line with international standards, international standards don't have prepayment. Are you talking about… what kind of margins are you talking about?

Marcos Magalhães: Just talking about overall margins. So if you get the ratios for pretax profit over revenues, that's a good figure where mathematics should go to.

Mario Pierry: Okay. Thank you.

Operator: The next question comes from Eduardo Rossman, Banco BTG.

Eduardo Rossman: Hi, good morning everyone. I have two questions. The first one is on fee income, because even if we exclude Rede and the credit card business, actually the performance overall is still weak. I know that we are seeing kind of a pressure, you know, across the Board, you know, on asset management business, investment banking, you know, credit cards and etc. So, I just wanted to get your thoughts about, you know, how should we think about growth in the fee income business, you know, going forward. Should we expect, you know, growing in line with inflation now as the new normal or not? So, this is the first question.

Second question is on your value creation. When we look at your slide number 3, we can see that your value creation is probably, you know, reaching record high levels. So I wanted to ask how you think about this natural trend, if you believe, if it is still possible to improve the gap of the ROE to the cost of equity, if you think this is going to be more like the ROE going up or cost of equity to move down, how much can move down. So, if you can talk about that as well it would be interesting. Thank you very much.

Candido Bracher: Thank you, Eduardo. So, in your first question, how do we see the growth in the fee income, if we see it growing along with inflation, if this is the new normal. No, I don't. I think we are living a special situation this year and next year with the pressures from the acquiring business and, it is important to add, the interchange cap, which was established by the regulator and the effects started to be felt in the last quarter of last year, but I see them more combined between inflation and GDP growth. I think that as GDP starts to grow again, we will have an increase in demand of this business, which generates fee income. So, for this year we have provided the guidance – 2% to 5% -, but I expect these figures to improve and to be better as the economy starts to grow.

On your second question, on value creation, I don't see this gap widening, the gap between ROE and cost of capital. I think it is historically high level, I see the cost of capital reducing as the pension reform gets approved and so on. So, yet, despite not seeing this gap widening, I see value creation improving through volumes. So, the value creation is not only the result of the gap, but is also the result of how much capital you apply to the business, how much results you generate, and I think that a more healthier way of growing value creation will be to grow portfolio and to grow business in general, which we expect to have, as the economy starts growing again.

Eduardo Rossman: Perfect, thank you very much Candido.

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

Jason Mollin: Hello, thank you for the opportunity to ask a question. Candido, my first question is a follow-up on cost. We've seen Itaú's focus on cost efficiency in the past, of course, obviously an accelerated fashion after the merger with Unibanco, but it seems as if that's always been a focus for the Group. What drove the timing for this renewed focus now in the first quarter versus the end of last year and what I guess you referred to as self-inflicted pain and this change in guidance? And could we see this again, is there more room to really tighten down more? I guess if you look at Brazil globally, costs, assets for the bank are on the high side.

So how low can we go? And of course, you just mentioned – I mean, this was related to my first question – I was going to ask in terms of value creation, it really is I think important to talk about revenues and not just cutting costs. So if really you are thinking that where we are now at record value creation, very high earnings and it's not going to come… when can we expect this volume? Is it really next year, the year after? Where can we go to in terms of that volume growth, loan growth? Can we get back to 15% loan growth in Brazil? Where is the long-term kind of recovery in loan growth rates for you guys? Thank you.

Candido Bracher: Thank you Jason. So, you first question on costs, I mean, what drove the timing of these measures of cost controls. What drove it was the perception that the economy would not grow as expected this year. So, when we looked at the difficulties we would have in growing fees and etc. this year, that we wouldn't get a tailwind from economic growth, we decided to be much more austere in cost management in the Bank.

Is there more room to control costs? Yes, there is. I think there always is, but especially with the investments we are making in technology. So we expect that over the next years we will have a significant improvement in costs in the Bank. You may say also that maybe all these innovations will also bring a reduction in fees in general, I mean, in margins in general. We have our efficiency ratio now at 26.3, but I believe there is room to improve more, I mean, taking your observation in view, I mean, what concerns the timing, we are not working on costs way beyond the end of this year, so we are already projecting the same austerity for the periods ahead.

The second question concerning volumes and when we can expect them to come back. I don't have the precise figure with me now, Jason, but I have seen it recently, I am sure that, I mean, in corporates we are still below the level of the end of 2015. In individuals, we are more or less about the same level of growth, but taking inflation into consideration. So I believe there must be room for growth, significant room for growth in assets and in income in the years to come. And I think what we depend on is economic growth, and economic growth depends on fiscal stability, and fiscal stability depends on pension reform. This is more or less how we see it. So, the perspective of approving a good pension reform in the second half of this year I think opens very constructive perspectives for 2020 and beyond.

Jason Mollin: Thank you very much.

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

Nicholas Riva: Thanks very much, Candido, for taking my question. Just two questions. The first one on capital, we did see the decline in the CT1 because you paid the additional dividends and the interest on capital. Right now it is at 13.3%. I think you said earlier in the call you gave a target of 13.5, was 13.5 the target for the CT1 or actually for the Tier I? So, just to have an idea if you are done basically with this process of optimizing the capital structure.

And then the second question on the guidance, so you changed the guidance for net interest income, but you didn't change the guidance for loan growth. Was the reason for this basically more competition from other banks in terms of pricing, or a different assumption for the SELIC rate? Thanks.

Candido Bracher: Thank you, Nicholas. On the first question, you are right, for Tier I capital, 13.5 is the level we want to have every beginning of year for Tier I capital. Our core equity Tier I now is at 14.6 at the end of this… sorry, our Tier I now is at 14.6 at the end of this quarter. The core equity, Core Tier I is 13.3, you are right.

The second question, I mean, why did we are just the guidance for financial margin with clients and for fee income and not for total credit portfolio. One reason is because we look mainly at self-inflicted factors, which were the measures we had in Rede when adjusting the guidance, but the main factor is that we feel encouraged by the growth we are witnessing in credit demand. We are seeing a healthy demand from individuals and SMEs and, starting at the end of last quarter, we are seeing an upsurge also in the demand for corporate loan. So we feel encouraged that we will be able to meet this goal established in our guidance for loan growth, also because we do expect the approval of the pension reform in the second half of the year, and I and this will drive demand for loans especially in the corporate sector even further.

Nicholas Riva: Okay, thanks Candido. One follow-up there. The revenues on the prepayment business from Rede, they are all booked in the fee income line or also on the NII line? Because you mentioned Rede as a also what happened in the change of guidance for net interest income, but I wasn't sure if it is booked in NII or just in fee income, the prepayment business of Rede.

Operator: Our next question comes from Otavio Tanganelli, Credit Suisse.

Marcelo. Telles: Hi, good morning everyone. Marcelo Telles from Credit Suisse. Thanks, Candido, for your time. I have a couple of questions. The first one, regarding your NII guidance for the year, I mean, particularly the client NII, you know, even though you brought it down to 9% to 12%, you know, it seems, you know, somewhat, you know, like a challenging target, you know, considering that you are like, you know, 7% year on year, so you probably have to grow, you know, 4.5% per quarter, you know, over the next three quarters in order to reach that target, which to me, you know, sounds too optimistic…

Candido Bracher: Sorry…

Marcelo Telles: Hello?

Candido Bracher: Otavio, sorry. We were cut. Could you please start your question again since I didn't hear it from the beginning? Sorry.

Marcelo Telles: Of course, Candido. Marcelo Telles here from Credit Suisse. Thanks for your time. So I have two questions. The first one, you know, regarding your clients NII growth targets of 9% to 12%, even though your trend versus your previous guidance for a little bit, it does seem, you know, somewhat optimistic considering that, you know, you grew, you know, a little over 7%, you know, year on year, and it seems you would have to grow, you know, 4.5% per quarter over the next three quarters in order for you to reach that target. So, my question to you is, you know, what makes you, you know, comfortable that you can achieve this target, especially considering, you know, that you mentioned that the economy, you know, is a little bit lower than you expected and perhaps, you know, probably the growth could me more, you know, skewed towards, you know, the second part of the year? So, if you could elaborate on that, I would appreciate.

And my second question is: you did mention, you know, that this ongoing cost effort that, you know, Itaú is making is something that, you know, is probably not just a one-year thing, but it is, you know, an ongoing effort maybe you can, you know, see that going forward. So, considering that, you know, the fee growth, you know, has slowed down but that you are being able, you know, to really control your costs very well and you mentioned that, you know, you do not expect your ROE, you know, gap to your cost of capital to widen, is it fair to say that, you know, on the positive side, you know, you can continue to, you know, keep, you know, your excess return as it is today because you still see room, you know, to offset, let's say, some potential pressure, revenue pressure, particularly on the fee side, with more, you know, cost cutting down the road? And I'm trying to look a little bit beyond 2019 in that question. Thank you.

Candido Bracher: Okay, thank you Marcelo. First, concerning NII growth, which we are guiding between 9% and 12% for the year, I mean, we are confident that we will be able to deliver this growth in NII and the reasons are the following: one is that we expect some economic, some more economic activity now, we expect the pension reform approval in the second half and so on.

The main reason, though, is average portfolio growth. I mean, average portfolio growth between 2019 and 2018 is much higher than we had between 2018 and 2017, and, as you know, the NII is made on the average portfolio, not at the portfolio on the end of the period. So, this gives us also confidence to being able to reach this NII target.

And the other very important point is the change in mix that we are experiencing. We are really experiencing a much more intensive growth in individuals and SMEs portfolio, which have a higher margin than corporates and so on. So this change in mix, as you can see, by the way, in the presentation, I mean, this change in mix is the main explanation for the growth in NII.

In what concerns costs. Yes, I see our cost control going beyond 2019 and 2020. I think we are keeping this more and more under control, I think that technology will enable a structural cost transformation in the Bank going forward, but it's also something that will always require investments, and I think that there is a limit to the ability to improve profitability based on cost reduction. So, we expect profits in the future to come mainly from growth in assets, some growth in income and economic growth in general although, I mean, we intend to keep costs strictly under control going forward.

Marcelo Telles: Thanks, Candido. Just one follow-up on your second answer. So is it fair to say, you know, that, you know, even though you may have like some competitive pressure, you know, some of your revenue lines that you can actually – because, you know, you continue to control costs and, you know, you'll probably have like a very positive credit cycle ahead – that you can maintain, you know, your, you know, excess return, you know, similar to the levels, you know, that you have today, you know, at least in the shorter to medium term? Is it a fair assumption?

Candido Bracher: It is certainly in this direction that all our efforts here go, Marcelo. But as the example in Rede has shown well, competition must be taken into consideration when building the scenarios ahead.

Marcelo Telles: Excellent. Thank you very much, I appreciate it.

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

Domingos Falavina: Thank you very much for taking the questions, and good morning to all. Also, two quick questions. The first one is just again on Rede provisioning. So, when we look at kind of like the medium-term history of Rede, one of the market share loses, I think, given the growth of and Santander. All the way, growing 0% to 1% with industry growing 10% year on year, all the way up to the 4Q of 17, 1Q of 18, and what we hear, you know, on the grounds, is basically that change, and sort of, and even in your management speech, yourself, changed your speech drastically as far as, you know, the profitability of the industry and decided to change the attitude I should say in pricing as well. And we started seeing volume growing basically 5% year on year, 8%, 14%, 18% in the 4Q, which is above industry growth, industry was growing 15%.

In this 1Q we saw basically growth decelerating to 14%, which implies maybe in line, maybe a little bit below industry growth, potentially market share losses, and then we noticed this second round of aggressive measures as far as the plus 2. So, my question is: at what level of growth – assuming the industry growth is 15% - will you be okay within the cost print growth? And is it like market growth, or is it plus 1%, plus 2%, you want to be a gainer? And at what point you're going to revisit price and say: "we have to want a second round"? So that's the first question.

The second question is on tokpag. You have a very good like for transferring, it's been removed from the Apple Store, we can no longer download it, and, you know, some of the rumors are heard that you may be launching some kind of digital initiative, digital banking around that software. I am just curious to see why exactly was it removed, is this just rumor or do you have actually something in mind for more the low income portion of the population on the digital side? Thank you.

Candido Bracher: Hi Domingos, thank you for the questions. I will ask Marcos Magalhães to help me with the first answer, but the first part of your first question, on why have we changed our stands in Rede in regards competition, so I think we changed it twice, as I mentioned. First, during 2017 and so on, we tried to protect margins, this evidently didn't work. So there was a moment, at the beginning of 2018, when we would play along with the market and protect our market share, and this worked in the sense of protecting the market share at the expense of compressing margins, which is what happens in highly-competitive markets. And now we have, so to say, taken a lead, leading the industry towards this initiative.

We are exercising and we are in constant discussions here in how to cope with this much more competitive environment, and there is a learning process and we feel that we are doing better now. But I will pass to Marcos to complete the answer.

Marcos Magalhães: So, two points to add to that, Domingos. First is the difference evolved between the first quarter of this year and the fourth of last year, there is a seasonality involved in terms of our client portfolio mix, so that pretty much explains the variance of growth in fourth to the first quarter.

Domingos Falavina: Magalhães, I am comparing year on year growth. So if you could explain it. The seasonality shouldn't impact year on year, right?

Marcos Magalhães: No, it does impact because the portfolio mix change in that period, so when you look at fourth quarter, we are year over year and the first quarter year over year the reason in the change in growth rate is related to that.

Second point is, our long-term pursue here is to level market share, so we intend to…, we don't have a goal to be the largest acquiring in the market in terms of market share, we do have a goal to keep our operations relevant in the market share in the market, and that means for us to sustain our share on the long-term.

Domingos Falavina: Right, so the goal is to grow in line with the market, at least?

Marcos Magalhães: Yes.

Domingos Falavina: Clear, thank you. And on the tokpag?

Candido Bracher: On your second question, on the tokpag. Well, the tokpag, I think, was an excellent product. I agree with you. I got some criticism at home because we have discontinued it. But the fact is that the market did not seem to think it was such a great product and adoption was not to the standards that we demand from our new products. So, this was the simple reason why it has been discontinued.

In what concerns new initiatives, I mean, we are always thinking about it and we are always working on new products to satisfy our customers, but there is nothing to be advanced right now in this field.

Domingos Falavina: Thank you very much, Candido.

Operator: The next question comes from Jorge Kuri, Morgan Stanley.

Mr. Jorge Kuri, you may proceed.

Jorge Kuri: Hi, good morning everyone. I have two questions if I may, one on the bank and another one on acquiring. Can you walk us through what happened with the delinquency? In the first quarter we did see a meaningful uptake in most of the metrics whether NPLs, renegotiated loans, cost of risk, all of them moved in the wrong direction, I guess. Is this mostly seasonal, is this mostly because the economy has been weaker than expected? Are you seeing similar trends so far in the second quarter? What is your expectation of how this is going to shape out?

And my second question, I guess taking advantage of Mr. Marcos Magalhães is on the call, it is about rather overall from a strategic perspective. So, I'm guessing some people would disagree that the main disadvantage was pricing at Rede, some people would argue that – and certainly your competitors argue that – the difference between themselves and the incumbents they provide much better products, services, customer experience and that's what merchants really value. So, are you only going on the pricing routes and how sustainable is that strategy? Everyone moves to free D2 tomorrow and then you are still the same company, with the same disadvantage on prices, products… sorry, product, service quality, etc., or is there, in addition to prices, effort at the company to try to provide a much better customer experience enhance in a more sustainable competitive advantage?

And here I just may ask a third question, sorry. You did mention that you thought that profitability had to converge to international standards because there is no reason why Brazil should have higher profitability in the payments base. I'm not sure I understand that. I mean, the bank generates 23% return on equity, and I don't see banks globally generating 23% return on equity. So, does that mean that we should also expect the bank to have single-digit ROEs like every other bank in the world? Or how do we reconcile this comment? Thank you.

Candido Bracher: Hi Jorge, thanks for your very provocative questions as usual. So, let me start by the first one here, on credit.

First, what is happening on credit is totally within our expectations, we are not surprised by anything that has happened. It is the result of three movements - and please remind me if I forget something. The first is what we show in our product mix. We are moving from credit mix towards assets where margins are higher, but also where delinquency is higher: individuals and SMEs. So this change in mix and the portfolio growth itself commenced higher provisions. The second effect is a seasonal effect in the first quarter of the year, that always happens in the first quarter of the year. Last year it had been weaker, it had been only 20 basis points, this year it came to 40 basis points again, as it has been in the previous years. So, no surprise here. And the third aspect is more to do with the corporate world, which is the decline in the coverage ratio. I mean, this decline in the coverage ratio, you will remember, I have been announcing for over one year now, and we make provisions which are precautionary, we have made quite a few of them during the years of crisis and after, because there were companies which had not defaulted yet, but which probability of default. The probability of default we saw increasing in the period.

With these companies, two things may happen. One is that they actually do default, we had this case in this semester, when two companies did default, did pass the 15 to 90 days to the over 90 days, and these two companies were already 100% provisioned for a long time. What happened is just what we expected. And the other thing that may happen is that companies may improve simply, and their probability of default may improve and we may deem that provision is no longer necessary for these companies. This also happened in this quarter. We had a couple or three companies which fit in this description.

So, when you combine all this, you'll see that the expected losses, in general, are exactly according to what we have forecasted and, I mean, you can see that this is perfectly in line with the guidance we have provided for cost of credit. So, I mean, here we had absolutely no surprises in the credit front.

I will answer the third question and then pass to Marcos to answer the second question. When I mentioned that, in the payment arena profitability could go to international levels, I am just recognizing the factual situation which…

Operator: Ladies and gentlemen, please, hold.

Speakers, you may proceed.

Candido Bracher: Jorge, sorry, we got cut. I don't know when did you stop hearing me.

Jorge Kuri: Thanks, Candido. You were actually starting explaining the question I asked about profitability converging for payments. You were just starting the answer to that.

Candido Bracher: Okay. So, let me resume this. So, this comment I made it derives from witnessing the very strong competition in this sector and the enormous margin compression that we've been experiencing there for three years now probably. And the market is changing here, I mean, this is a market where innovation and technology are making a big difference, as well as the normalization of the interest rates in Brazil. So all this is leading to this compression which I see in this market, and measures, as the ones we have taken this week, they are designed to grant us a lead in the industry and enabling us to keep on serving these clients as broadly as we can in the Bank. We certainly do intend to maintain the differentiated returns on equity that we have, and we think that we will be able to make it, not by avoiding competition, on the contrary, by facing competition directly.

I'll pass now to Marcos.

Marcos Magalhães: Okay, just adding a few points to what Candido said, when talking about conversions, remember that also the product the way it works in Brazil is converging also to international practices. For example, rent is something very typical of our market, it is inexistent in other markets, and that's going down towards the sale of the POS, for example. We talk about the settlement period, which is also shortening by stronger competition and by also strengthen of the regulation. So, these conversions are making the product to converge to international practice, that’s where we infer it will convert to profitability on that segment as well.

Talking about a better service or user experience, that's a very good question, Jorge, thanks for bringing that up, certainly we are focusing on that, we have many fronts, we are working on improving our customer service or the user experience, and we have goals to increase our NPS, all of our employees have goals on that respect. But linking to what we did in terms of pricing change, this debt by our measure, half of the gap in the NPS towards our competitors is by virtue of pricing. So NPS measures satisfaction, but part of the satisfaction comes also from pricing. So half of the difference, half of the gap is for pricing, that's why we decided to level that.

Jorge Kuri: All right, thanks everyone for your thoughtful answers. Thanks a lot.

Candido Bracher: Thank you, Jorge.

Operator: The next question comes from Olavo Arthuzo Santander.

Olavo Arthuzo: Hi Candido. Thank you for taking my question. It is just one, it is related to the guidance for the year. There were two main revisions, one on the revenue side, and the other on expenses. So, sorry for my insistence on this topic, but my point here is that, given that the competitive scenario in the acquiring industry is becoming day by day more challenging, we do understand the recent change on Rede strategy, thus, the change in the guidance of the year. But on the other side, since the management of operating expenses relies basically on in-house initiatives, why this change in so short period of time? So, would I be wrong to assume the bank is perceiving a more scenario for top line growth to rebalance or offset this weaker-than-expected performance of revenues and deliver a high profitability, they are shifting their minds and are starting to cut costs? But more important than this, are you seeing this movement in your competitors too, or only Itaú is shifting the strategy from products and growth to cost management after these four months of the year? Thank you.

Candido Bracher: Hi Olavo, thanks for your question. Yes, it is true, we decided to be much more aggressive in dealing with costs once we realized that the economy would not grow as we had expected when we supplied the guidance. As we mentioned already, our expectation for GDP growth was cut by half, from 2.5% to 1.3%, and this is what led us to be much more active on cost control than we were initially.

We normally don't talk about competitors here, and you referred to the competition, but I should just observe, and you know that our main competitors' guidance for costs is already very low. Ours was the highest guidance for costs.

Olavo Arthuzo: Okay, thank you very much, Candido.

Candido Bracher: Thank you, Olavo.

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

Jason Mollin: Thank you. Just a quick follow-up on the comment that the outlook for the economy is positive getting a pension reform in the second half of the year. What is the downside risk if we don't get this pension reform? What is the outlook, how is Itaú Unibanco preparing for this? What could that scenario look like? Thank you.

Candido Bracher: Thanks, Jason. The scenario is not good, so if the pension reform does not get approved, we will have the relation public debt over GDP, if you keep on increasing, this will cast doubts on the stability of inflation, probably interest rates will have to rise, we may see some pressure on the exchange rate also due to that, I mean, the level of confidence as a whole in the economy is going to drop.

Unfortunately, this is not a scenario we are unaccustomed to. We have lived this scenario very frequently in the past and, I mean, we know what to do in this situation. I just hope and expect that we will not have to use this toolkit this time.

Jason Mollin: Thank you very much.

Operator: Next question, Carlos Gomes, HSBC.

Carlos Gomes: Thank you and good morning. I'm not going to ask about the acquiring business, for a change. My two questions are the following. Number 1, on the tax rate, your tax rate is now at 32%, in our calculation your peers are 30% or 29%, part of it only has to do with your international operations, but is there anything more structural or is there something temporary that you expect to converge with your peers at some point?

And the second refers to the guidance, but in a different way. I'm not really surprised that you have reduced your NII guidance by only 0.5%. When I look at your economic forecast, six months ago you were expecting SELIC at 8% for this year. Three months ago, you were expecting 6.5%. Now you are expecting 5.75%, and it seems to us that what you expect your NII to do has not really moved a lot in line with interest rates. We know that you are slightly sensitive, but still, the impact seems quite minor. Could you comment on that? Thank you.

Candido Bracher: Thanks, Carlos. I will comment on your second question and then I will ask Alexsandro Broedel to comment on the tax rate issue.

You are right, when you observe that we had a SELIC rate… and we must adjust point out that it is end-of-the-year SELIC rate. But we had the number of the year SELIC rate of 8.5% at our first forecast, and now we have 5.75%, and in the middle, we had 6.5%.

What changed is – I am not in the economic team making the economic forecasts, but as I understand for the economic team – what changes the perception of when the pension reform would be approved. We started the year, the end of last year we believed that the pension reform could be approved early this year. If it were the case, then we expected economic pickup derived from that, from the levels we had, and this would drive the need for higher interest rates in order to keep inflation under control.

As we've seen, inflation is well-behaved, now in recent months it has shown a couple of higher indexes, but our economic team believes it is well under control, and the expectation for the pension reform has moved to the second half of the year. And it is widely expected in the market now that if it were not for the fiscal weakness, structural weakness of Brazil, interest rates could be lower. And this scenario has been building, it is consensus, it has been building in the economy. So, now the expectation is that immediately after the approval of the reform, there could and there should be a drop in the SELIC rate. Afterwards, as the plan unfolds and the economy starts growing and so on, the question of raising interest rates may come again and take place.

But why is the effect in our NII reasonably limited is because in both cases, be it when it was 8.5%, be it now when it's 5.75%, we are only referring, maybe to the last couple of months in the year, so the effect of this is rather limited.

I'll pass the Broedel now.

Alexandro Broedel: Carlos, two main reasons to reconcile our effective tax rate with this competitor of us that you mentioned: The first one is goodwill amortization, our level of goodwill amortization at the moment is much lower than this case that you mentioned, so that affects our effective tax rate. The second reason is ROE, so, higher ROE, higher effective tax rate because the benefit of interest on capital is pretty much fixed over the year because that depends on the amount of your book value of equity and the amount of the TJLP, so the rate that applies to book value of equity. So, these are the two main reasons that reconcile our number with the theirs.

Carlos Gomes: Thank you. And if I can follow-up on interest rates. Do you expect interest rates to be lower than? Would that have an implication of your NII for 2020?

Candido Bracher: Lower interest rate in 2020, yes, I mean, a lower interest rate has… I mean, yes, if you look at the chart we show in page 5, in page 5 we show our NII, how it has evolved as the SELIC rate dropped from 10.9% to…, here it is 6.4% because it is the interbank rate. So it has dropped 4.5 points, and as you see from our NII level, it has kept well around 12% or high 11%.

So it is not that the interest rate, does not affect our NII, but it affects in different manners and quite often in compensating manners. Volumes tend to grow, there are many compensating factors, and this is what explains that our NII was virtually unchanged as the interest rates suffered this drop which we have seen. I expect this to remain the same way and should rates drop for the next year.

Carlos Gomes: Thank you very much.

Candido Bracher: You're welcome.

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

Candido Bracher: Now just to thank everybody for your attention and your interest in our results and the very good questions. Thank you.

Operator: That does conclude our Itaú Unibanco Holding earnings conference for today. Thank you very much for your participation. We would like to invite you to join the conference in Portuguese at 11:30 AM. You may now disconnect.