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Q3 2022 Grupo Financiero Banorte SAB de CV Earnings Call

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### PRESENTATION

**Tomas Lozano Derbez** *Grupo Financiero Banorte, S.A.B. de C.V. - Head of Corporate Development, IR, Financial Intelligence, M&A and Sustainability*

Good morning. Sorry for the delay. I'm Tomas Lozano, Head of Corporate Development, Investor Relations and ESG. Welcome to Grupo Financiero Banorte third quarter's earnings call. Our CEO, Marcos Ramirez, will provide an overview of the inflation and its effect on the right environment year-to-date as well as the main results for the group, including the positive trend in loan growth and NII, controlled asset quality and the continuous recovery on insurance claims.

On the ESG side, we want to thank you all of you for your valuable feedback and comments, which have held Banorte to be rank in top positions in 2 well-regarded rankings. Most socially responsible bank according to Newsweek and Statista and Most Honored Bank in Mexico according to Institutional Investor. You will find our quarterly update in the earnings call there. After our CEO's presentation, Rafael Arana, our COO and CFO, will provide details of the main financial results of the group, including the ongoing impact of high reference rates, continued cost control and capital ratios. We will then proceed with the Q&A session.

Please note that today's presentation may include forward-looking statements that are subject to risks and uncertainties, which may cause actual results to differ materially. On Page 2 of our conference call deck, you will find our full disclaimer regarding forward-looking statements. Thank you.

Marcos, please go ahead.

**Jose Marcos Ramirez Miguel** *Grupo Financiero Banorte, S.A.B. de C.V. - CEO & Proprietary Board Member*

Thank you, Tomas. Good morning, everyone. Thank you for joining our call today. The third quarter of the year presented resilient results for the financial group, navigating through a challenging global economic environment. Nevertheless, economic activity in Mexico continues to show good performance and is expected to continue for the remainder of 2022. GDP in Mexico has been driven by the recovery in private consumption, supported by greater mobility, remittances at historically high levels, better employment conditions, along with increasing export activities, despite the potential disruptions in the global supply chains.

Our economic analysis team is holding its annual growth estimate of 2.1% for the year 2022, although recognizing a more challenging

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scenario towards the end of the year and the next, driven by the potential global recessions, including that of the United States as well as persistent inflationary pressures and a more restrictive global monetary policy. However, it is safe to assume a soft landing for the Mexican economy considering that it has not yet reached pre-pandemic levels. In this sense, we believe that Mexico could grow around 1% in 2023, despite a moderate recession in the United States, supported by increasing new shoring activity.

Inflation remains as one of the most important challenges for most of the economies with annual inflation in Mexico, reaching 8.7% in September. Our economic analysis team has revised upwards its forecast to 9% from 8.1% for the year 2022, anticipating a turning point by January to end 2023 at 5.4%. With this background, we expect further tightening of monetary policy. Thus, we recently adjusted our forecast of Banxico's reference rate, expecting it to end 2022 at 10.4%, with a terminal rate of the current restricted cycle up 11% in the first quarter of 2023, suggesting more tightening monetary conditions for at least the next 12 months. On the political front, Congress is expected to continue to focus on economic package for 2023. On the legislative agenda, attention is still on the initiative to reorganize the National Guard under the Ministry of Defense.

Moving now to the bank's operation. During this quarter, we have strengthened our commercial teams to increase our presence and competitiveness to attract potential customers. Banorte is constantly searching for ways to attend the needs of the Mexican market, and these times are ours to take, always with a responsible approach towards risk and profitability. Moreover, as you might have heard, Banorte was recently granted the banking license for the constitution of its digital bank.

This is an important milestone into fulfilling our vision for the year 2023, which is to be the #1 financial group in Mexico doing banking in a digital role. We are aiming to capitalize on all the strengths that we have consolidated in more than 120 years of banking and provide Mexican users with a 100% digital, personnel, easy and secure solution. We will continue to work with the financial authorities to comply with the regulatory process and certifications until it starts operating in the market.

In the upcoming months, you will receive an invitation for our Investor Day, where we will go through our current corporate strategy and as one part of its 3 pillars, we will share all the details about the digital bank. We are working on the general business plan and different scenarios with all the product lines. The operation will be at a fully digital native bank with a competitive cost structure that will enable us to transfer benefits to our customers. Additionally, it's important, the focus of the business will be on profitability, although we will have [KPIs] related to digital bank, we will be basically focused on ROE, ROA and net profits.

In the same line and aligned with our strategy of promoting hyper personalization, innovation in the digital field and the search for alliances that approach us to different customers. During the quarter, our [BanorTec] digital ecosystem was launched for the Tec de Monterrey, University community of around 89,000 individuals in 25 campuses across the country. This app exclusively for Tec students, staff and alunite allows an easy and secure access to highly transacting financial products and services, along with availability of the campus ecosystem within the app. Lastly, the adoption rate of our digital channels continues to rise. And most importantly, customer satisfaction in the use of these channels has had relevant improvements. Our mobile banking reached an NPS of [82.7 in the quarter, 9.1] points higher yearly.

Turning into the financial results for the quarter on Slide #3. The resilient performance of the group was supported by a dynamic credit demand, some funding mix, a strong reactivity contained expense below inflation, still better-than-expected risk metrics and achieved balance sheet.

Starting off with profitability on Slide #4, ROE improved more than 400 basis points on a year-on-year basis on the back of a solid performance across most of the business lines. Nevertheless, it continues to be pressured by insurance results, which are gradually reaching pre-pandemic levels.

On Slide #5, NII from the loan portfolio increased 8% quarter-over-quarter, partially incorporating the effects of reference rate increases during the first 9 months of the year. Noninterest income decreased in the quarter as a result of extraordinary expenses from the insurance company registered in other income, [discount] expenses and lower trading income.

Zooming into this Slide #6, they remain flattish in the quarter on higher credit origination through the external sales force. With

accumulated figures, we continue to grow fees at double digits, driven by a strong electronic banking fees, higher advisory and structuring fees in commercial and government portfolios and more dynamic transactions in consumer products, aligned with the recovery in private consumption. POS transactions had a seasonal effect during the quarter due to the hot sale in May, [by they] present a steady growing trend to digital and physical means.

Moving on to Slide #7, we see a very healthy expansion in the loan book. Corporate loans were partially affected by prepayments, but the yearly comparison is expected to continue growing from the market at [6 and 19 in dollars], which is already around [12%, 13%] of our loan book. Commercial loans are gaining traction, and this trend is expected to continue for the rest of the year as we benefit from the new shoring operations, especially for the manufacturing industry and increase our exposure in low-risk profile as a mix. The government book was also impacted by prepayments from different states in the quarter, but we are not expecting deceleration in the book for the year 2022.

The consumer portfolio, Slide #8, displays a strong quarterly expansion and a record annual volume increase in the portfolio. The evolution of payroll and credit card loans rely on good consumption dynamics driven by higher mobility unemployment conditions. Auto loans are recovering as supply shortages, they start to normalize, and we expect good performance in this segment going forward.

Mortgages presented on a remarkable annual growth during the quarter of 10.2%, held by business approach we have had during the origination process where we [prioritize] customer lifetime value over short-term margin base. Going forward, this segment is expected to be resilient during the rising rate cycle as we increased our personalized [operation]. However, we might experience some moderation in credit demand at sustained rates above, let's say, 10%.

On Slide #9, asset quality continues to perform better than expected. NPLs remained resilient during the quarter with delinquency indicators for each product within the expected levels. Currently, we don't foresee deterioration that can represent the trend mainly industry or geography. However, we do expect a normalization of risk metrics as we increase our share in [risk area] segments, such as the consumer products.

Analyzing the results by subsidiary in Slide #10, during the quarter, the bank was slightly impacted by higher operational expenses and provisions. Nevertheless, with accumulated figures, it continues to expand on the back of solid NII asset quality, expanded management below inflation levels and expanding loan book, showing significantly high levels of ROE, above 24%. As people who mentioned, we are constantly analyzing different alternatives to optimize capital and maximize value to our shareholders. The insurance business results are gradually recovering with good premium expansion and COVID-related claims decreasing with almost pre-pandemic levels. Operating results show continued growth, especially in bancassurance.

The brokerage sector showed a quarterly reduction driven by lower transactionality. [The weakness] business increased during the quarter driven by business expansion offsetting higher reserves from inflationary adjustments. As for pension funds, the business was still impacted during the quarter by the pickup imposed by the regulator, along with the valuation impact of higher rates in the Forex long-term investments. Nevertheless, different initiatives to control expenses started during the quarter and will continue for the rest of the year, aiming to partially mitigate these extraordinary affectations.

On to Slide #11, we provide greater depending to insurance, showing an increasing business trending to normalization by the first quarter of [2022] and lower claims. COVID-related claims have almost reached normalization in all portfolios. Health and life claims continue to cease, while auto and damages are increasing hand-in-hand with mobility.

Moving on to Slide #12, we continue to see good operating and profitability metrics at joint venture with Rappi. We are enhancing our unit economics and increasing the number of cards issued along with credit activity for corporate users.

Shifting gears to ESG, Slide #13, I would like to highlight that among many other initiatives, we have been working on mentioning our Scope 1, 2 and 3 carbon emissions as we intend to align with fragment initiatives such as the Net-Zero Banking Alliance. I also want to express our gratitude to all our stakeholders for the valuable guidance, which has been key in the design of our corporate strategy in which ESG partners are at the core. This has given us the opportunity to be recognized by relevant international publications where

Banorte has been awarded top-tier positions among several well-regarded bankings.

As a final note, regarding the material event released earlier today, Banorte is no longer participating in the bidding process organized by [Citigroup]. I would also like to inform that we will call for a shareholders' meeting seeking approval to pay dividends and/or buybacks. As I have mentioned in the past, we are always looking to maximize our shareholders' value. Banorte has a life of its own, and we will be taking the most out of the opportunities ahead for us.

With this, I conclude my remarks, and now Rafa Arana will walk you through the financial results for the third quarter of the year. Rafa, Please go ahead.

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**Rafael Victorio Arana de la Garza *Grupo Financiero Banorte, S.A.B. de C.V. - Chief Financial & Operational Officer***

Thank you, Marcos, and welcome all, and thank you for the interest in Banorte. So we will be proceeding to go for the different issues that we think are relevant on the financial road map. I think the best one is that Banorte continues to have a very strong balance sheet. As you can see, we have seen in the capital numbers and on the liquidity side. We are really happy with the way we have been controlling inflation. Inflation, as you know, is speaking now close to 9%, the cost that we have been able to manage is around 8%, [8.1%], maybe at the end of the year, we will be having 8.2%.

Just note that the digital transformation ongoing in Banorte at a very fast pace. We have a motto now in Banorte, as you know that Banorte is the Bank in Minutes, because you can onboard and do transactions and relationships at bank in a very efficient and in a very fast pace. Marcos as just mentioned the JV with Rappi and the Digital Bank is already on the move. So all the basic path that we defined in 2018 that Banorte was to pursue on the evolution of the bank is now fully in motion.

The next parts of the slide, what you can see is there a very strong net interest margin, 6.7% for the Group, and the bank for 6.3%, with a very, very strong expansion from 1 quarter to the other and compared to last year. And what is also relevant is that the cost of funds continue to be something relevant for us. We know we still have room to improve on that. But if you look at the base of growth on the funding side, we will see slide a bit ahead of the presentation. We are experiencing a very strong growth in the main deposits and the mix continued to improve to [73] demand deposits and 27 time deposits.

[This is] we've been providing notes a very strong growth on the margin side. But the most important thing, taking into account that we have a very good tailwind on the rates. The fact is that we are getting the margin because the inventory of loans that we have has been performing extremely well. So by applying the new marketing and the funding costs to a very, very strong dollar group, sorry, dollar group and peso group, we are really having a continuous expansion in the margin, and we expect that to continue for the remainder of the year.

If we talk about the capital numbers is already reaching the 23% and the core Tier 1, 14.7%, well above the requirements of the TLAC and that needs to be -- to be reached by the regulator and by the banks, but not this already in full compliance of that platform.

If we move to the next slide, we will go in the different elements of what we just mentioned. The name of the bank, as you can see, continued to expand at a very, very fast pace. The same goes for the NII. Sequentially, you can see that 30% is growing the NII on a year-to-year basis. The expansion for the quarter for the net interest margin was 71 basis points and the net income that you can see this is slightly down from the past quarter is basically conserved by the trading group. That is getting to a more normal rate of pace and not at a really extraordinary numbers that we have in the second quarter.

The return of equity of the bank that is already reaching the 27% for the month, continues to be a very positive surprise for the market. I think it's based upon all the elements that we just mentioned about the loan book, the funding, the services, the expense control, all the elements are really pushing the return on equity of the bank at a very fast pace. And you have to take into consideration that the numbers that we want to run the bank from [21 from 12% to 12.5%], and we are well above that number. So that, in addition, would also benefit when we start moving dividend from the banks to the group the return on equity of the bank will continue to expand. The return on assets also continues to grow into the right direction. This is, as you have seen, the expansion on the consumer growth continues to be a very, very strong lever for this number. And the return on equity for the group, that is already for the quarter above the 19% will end the

year above [19% overview].

If we move to the next slide, that describes in a much severe way, the evolution of the NIM for the bank and for the group, you see already that the pace of change has completely accelerate on that based upon what we just mentioned, the funding, the good returns on the book and a very good control on the expense side.

Let me move to the next slide. The asset quality continues, as Marcos mentioned, to be a result of all the things that we have been doing in the past about the modeling, the recovery unit. And what you have seen is that now it's trending at 1.4%. When we describe exactly the elements that moved out extraordinary elements, not really recurrent ones. Some of them are basically related to commercial loans that are really on the process to be sorted out. So that number should also start to trend again to a better number than we've seen in this quarter.

The provisions that you see a slight pickup on the provisions and then I also will ask Gerardo to go on this a bit. This has to do with, obviously, the rate of -- and the pace of growth of the consumer book and -- but nothing that we think is trend or anything that is related to any part of the group. Our exceptional parts are on the rate of solving the commercial loans and the pace of building the consumer group is requiring a bit more provision than expected because, as you have seen on the growth, the consumer book is growing at double-digit to the all the consumer book, but say, the car loans that by the end of the year, will be also in double-digit.

Gerardo, could you (technical difficulty)

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**Gerardo Cuitlahuac Salazar Viezca *Grupo Financiero Banorte, S.A.B. de C.V. - Chief Risk Management & Credit Officer***

Sure, Rafa. Good morning to everyone. I will tell you that I'd remind you that payroll loans at Banorte held at 20.8% market share, increasing 33 basis points in the first 3 quarters of 2022, that ranks us as the second largest vendor in this grade prototype on the Mexican banking system. And I will tell you and assure you that the main reason that the provisions are going higher in payroll loans are due to growth.

We still have very good sound practices basing 4 principles: The first one is establishing an appropriate credit risk environment for this type of product and everything else in the loan book; second, operating under a sound credit granting process; third, maintaining an appropriate trade administration, measurement and monitoring process; and last, the fourth one is ensuring adequate controls over credit risk. So we feel very comfortable with these provisions and with the growth that payer loans is -- has been experiencing on all the consumer loan book.

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**Rafael Victorio Arana de la Garza *Grupo Financiero Banorte, S.A.B. de C.V. - Chief Financial & Operational Officer***

Thank you, Gerardo. And then as you can see, the write-off rates, and there's also a question that always comes, how much you still hold on the extraordinary provisions are close to [MXN 1 billion] that are still on the book to be used as needed in the coming months or quarters [as continuing].

If we move to the next one, the funding cost that it has been also something that we have been looking very closely to improve. As you can see, the trend is a good trend for Banorte, but we still have, as I mentioned before going to improve. The mix is on the right direction. Also the growth in demand deposits that I mentioned to you are 16% for the year, 2% for the time deposits. So we think -- we are expecting these numbers to go down the cost of funds for the remainder of the year because the large inflow of deposits come at the end of the year. So that will also push the cost of funds down.

If me move to the next one, please. The sensitivity on the book, that's always been something that they are responding very closely. We are still at [MXN 1.21 billion] in the peso book and MXN 896 million on the dollar book. So basically, we are reaching a steady state on both of them.

Expenses is a good story in a very challenging environment. We are below inflation. And we're also advancing as many expenses for next year look -- try to look as much as we can on prices for the next year. We expect inflation -- we expect the growth rate of the expense line with the low inflation. That is obviously helping us on the cost-to-income ratio that is now reaching 37.1%.

We understand that the cost-to-income ratio has to do because of the acceleration on the revenue side because of the margin expansion that we have and all the other good revenue sources that we just described, but the controlling expenses has been extraordinary time for the bank. At the same time that we increased substantially the potential on the sales side for the commercial, for the SMEs and for the branch metric. So we are managing to be ready for expanding the growth, controlling costs based upon the good returns that we're getting on the revenue side.

The bank and capital ratio, as you see, continue to expand, even though the pace of growth of the book has accelerated, but we are still in lower limits to continue to provide capital for the bank. So we are in a very good position on the capital numbers. As I mentioned to you, we initially like to run the bank from 12% to 12.5% on the [21]. We are well above that, and the total cap is [20%] after the call that we did on the AT1 in the past months.

The liquidity ratio is now trending to the normal number that we have is around 160%. Remember that we usually manage the liquidity ratio from 135% to 150%. We are reaching these numbers now. I think we are becoming much more efficient on the management on the liquidity side. And the leverage ratio, as you know, we are the least leveraged bank in the market.

So I also would like to guide you to an adjustment that we just announced for the guidance. The loan growth. Now we see the loan growth moving instead of 5% to 7% to 7% to 9%. The NIM expansion from 25 basis points to 35 basis points. Now we are putting a number range from 85 basis points to 100 basis points. The NIM of bank expansion, the same [115] basis points. The expense growth 7.9% to 8.4%. The efficiency ratio from 37.5% to 38.5%.

I think there's room to improvement in that, but that's at this point in time that's the room that we have. The cost of risk trending to the normal rates because of the rate of growth and pace of the consumer group to 1.3% to 1.5%. Tax rate, the same numbers. Basically, the net income, now we're moving from MXN 40.5 billion to MXN 42 billion to MXN 44 million to MXN 45.4 billion. And the return on equity for the group from 18.7% to 19.2%, and the return on assets to 2.2% to 2.3%. This is now the guidance that we commit to the market, it implied by the end of the year.

With this, I'll conclude my remarks.

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**Tomas Lozano Derbez Grupo Financiero Banorte, S.A.B. de C.V. - Head of Corporate Development, IR, Financial Intelligence, M&A and Sustainability**

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

Before beginning the Q&A, I would like to remark that as it was disclosed to the public through a natural event, I'm not saying no longer participating in the process organized at Banorte Group. In light of the foregoing and in view of our confidentiality of undertakings, no further information in connection with such transactions will be provided. And therefore, we will not be responding to any questions in such regard. We are now ready to start the Q&A session. Thank you.

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## QUESTIONS AND ANSWERS

**Tomas Lozano Derbez Grupo Financiero Banorte, S.A.B. de C.V. - Head of Corporate Development, IR, Financial Intelligence, M&A and Sustainability**

We will start with Ernesto Gabilondo from BofA. I think Ernesto has connection issues. We'll move to Geoffrey from Autonomous.

**Geoffrey Elliott Bernstein Autonomous LLP - Partner of Regional and Trust Banks**

Great. You finally got the digital banking license, which I know is something that you've been working on for a long time. Can you give some detail around the investment that is going to be needed to build out the digital bank? Does that flow into OpEx? Does it flow into CapEx? And clearly, the long-term goal is to get the efficiency ratio down. But is there a possibility that the efficiency ratio has to go up in the near term to facilitate some of that's investment?

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**Jose Marcos Ramirez Miguel *Grupo Financiero Banorte, S.A.B. de C.V. - CEO & Proprietary Board Member***

Geoffrey, we are saving that for the next month. We will (inaudible) to our Banorte Day, and you will see everything, but let's see what we can say, Rafa.

**Rafael Victorio Arana de la Garza *Grupo Financiero Banorte, S.A.B. de C.V. - Chief Financial & Operational Officer***

No, Geoffrey, and follow on, on what Marcos said, as you know, we have just getting the license on that. And I think it's -- we are really refining all the numbers to be ready for that. Obviously, there's already the capital meeting [into it]. We'd rather please wait for when we go to the Investor Day, when you will have a full view of exactly how the bank is going to be funded, the capital is going to be working, what do we expect about our cost income ratio, how the evolution of the bank. So it has been very recent that the license, and we are working all the issues to finalize the process. And remember that we are still on the review of the last part of the authorities to grant to finally say the growth for the bank. So we'd rather wait for that on the Investor Day.

**Geoffrey Elliott Bernstein Autonomous LLP - Partner of Regional and Trust Banks**

Understood. I mean is there any color you could give around what you're doing right now? Are you hiring people? Are you moving people out of Banorte into the new entity. What sort of activity is going on right now? I guess more on the commercial side so that you're ready to launch this as soon as you'd like.

**Jose Marcos Ramirez Miguel *Grupo Financiero Banorte, S.A.B. de C.V. - CEO & Proprietary Board Member***

Okay. I will pass this question to Francisco Martha.

**Jose Francisco Martha Gonzalez *Grupo Financiero Banorte, S.A.B. de C.V. - MD of Digital Businesses***

Geoffrey, yes. We have -- in the process that we have been through and the authorization that we received at the end of last month implies that we have all the processes and all the regulation for the new bank documented. So we already have a platform that is a platform, I mean, technology and operations and processes in place. That will give us the efficiency that you were mentioning, and we will show you later in the Banorte Day.

We have all the strategy based on data, all the platforms that we're going to use and all the data, obviously, the repositories are empty, but all the data that we are going to use and the engines, the risk engine, the personalization engine, the empowerment [banks] that we are creating. And we also have an app, a mobile app and a complete customer service application. So all of that is ready, people is in place. So it's not that we are launching a paper bank, but it's everything that it's needed, it's in place. Now we are going to certify that what is in the binders is really operating. So that's the next steps with the authorities.

**Geoffrey Elliott Bernstein Autonomous LLP - Partner of Regional and Trust Banks**

Great. And look forward to the Banorte Day next year.

**Tomas Lozano Derbez *Grupo Financiero Banorte, S.A.B. de C.V. - Head of Corporate Development, IR, Financial Intelligence, M&A and Sustainability***

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

**Ernesto Maria Gabilondo Márquez *BofA Securities, Research Division - Associate***

Congratulations on your results. My first question is on dividends. We ran some numbers, and we see around MXN 27 billion in excess capital at bank level. If you normalize a common equity Tier 1 ratio to 11.4%, that was your internal minimum, and we see around MXN 29 billion to MXN 30 billion at group level. So the combined in dollars is around [\$2.8 billion]. So I just wanted to check with you is those numbers are reasonable? And if paying dividends, when should we expect them? Is this something that could take place this year or next year or maybe a portion this year and most of it next year.

And then my second question is on the regionalization and resharing opportunities. We started to see several companies moving part of their production to Mexico. I understand that banks will not be financing directly the expansion of the corporate plans, but more the

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supply chain related to semiconductors, computer and electric components, out of par, electrical equipment, agro industry, plastic sectors, among others. So just wondering how is Banorte preparing to take advantage of those opportunities that could be taking place in the next years?

### **Jose Marcos Ramirez Miguel *Grupo Financiero Banorte, S.A.B. de C.V. - CEO & Proprietary Board Member***

Ernesto, I think that you have run through your numbers and you have some color, right. Remember, winter is coming and remember the TLAC is coming in some days. So let's be not so enthusiastic. Rafa, please.

### **Rafael Victorio Arana de la Garza *Grupo Financiero Banorte, S.A.B. de C.V. - Chief Financial & Operational Officer***

Yes. No. So remember, the 11.4% was what we mentioned that if we go to any M&A, that will be the minimum capital level that we put on the Core Tier 1. But the number that we like to run the bank with and especially at these times is from 12% to 12.5% Core Tier 1. And I think we will stick to that. The numbers that you run on that is our right numbers, but you'll have to develop that part of them, 11.4% to the 12% to 12.5%.

The other part that is relevant about the numbers that you say is that the dividends will be called once we hold for the assembly, we have already granted the go for go-to the assembly. And once we call and the assembly is that we have 30 days for that. And after 30 days will be announced the dividend or the buyback policy for the shareholders. And we really appreciate the patience of our shareholders during this process because we know we understand always that the money is money of the shareholders. We retain that in a way that we try to guarantee any possibility that we can turmoil for the shareholders.

So thank you for your patience, and we are now in full motion for the dividends on the payback, as is the customary processing in Banorte. But the numbers is not 11.4%. The number you should be looking is 12% to 12.5%.

### **Ernesto María Gabilondo Márquez *BofA Securities, Research Division - Associate***

And maybe Rafa...

### **Jose Marcos Ramirez Miguel *Grupo Financiero Banorte, S.A.B. de C.V. - CEO & Proprietary Board Member***

Hey, Alex, you have to talk a little bit about...

### **Alejandro Padilla**

Sure, Marcos. I will tell you regarding the second part of your question, Ernesto, that Banorte is very well positioned in taking advantage to this trend of new shoring, [front] shoring whatever you want to call it. I will tell you that the approach is that we are currently using are by geography, by market segments and also by banking, product and service. Currently, everything related to USMCA, that accounts for around 11.5% of the total loan book. I would tell you that around our insight almost 11.5% of the loan book, manufacturing accounts for 41%; tourism, 35%; distribution and logistics, 11%; transportation and auto parts, 9%; and real estate talking about industrial parts and (inaudible) 5%. So we are trying to take advantage of this very important strategic trend for the country and all our corporate banking, commercial banking, fees charged on services, trust services are very well aligned, trying to take advantage of that.

### **Tomas Lozano Derbez *Grupo Financiero Banorte, S.A.B. de C.V. - Head of Corporate Development, IR, Financial Intelligence, M&A and Sustainability***

We will now take the next question from Thiago Batista from UBS.

### **Thiago Bovolenta Batista *UBS Investment Bank, Research Division - LatAm Equity Research Analyst of Banks***

Yes. Congratulations for the results. I have one question about the profitability of the bank. We saw the ROE achieving 20% for the group, even considering with very low leverage that we discussed. So when the bank optimized their capital, what's the level of ROE that we can see for Banorte in the coming years? So is it possible to believe in the, let's say, new to any (inaudible) goes that?

And my second question is about asset quality. Delinquency ratio is to be close or a bit below 2% in the past, now we are significantly

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close to 1%. What do you believe will be the normal level of delinquency ratio going forward? You mentioned that you are expecting a rate normalization of the delinquency ratio. But do we have a new normal now or no, is it possible to see delinquency ratio returning to close to 2% as in the past?

### **Jose Marcos Ramirez Miguel *Grupo Financiero Banorte, S.A.B. de C.V. - CEO & Proprietary Board Member***

Let's start for the first one, the ROE the rates would increase and the ROE will increase, but this is -- I don't think this is not a great question, but what are we going to do to maintain the NII and be here for the next 100 years. And the idea is to work in all the things that we are doing and to open all the answer we have in order to maintain a good ROE in the future.

Right now, for the next year, it seems that the rates will go [11%], and this is a very good asset quality. And the idea is to keep in mind that it's not for sure and forever. So we need to be strengthening to continue to the cost control, continue with digital (inaudible), continue with the analyzation, and then we will (inaudible). I don't know, Rafael, go ahead...

### **Rafael Victorio Arana de la Garza *Grupo Financiero Banorte, S.A.B. de C.V. - Chief Financial & Operational Officer***

No. I think Marcos chimed perfectly. I mean if you look at numbers, I agree with you. I mean, that the number of the (inaudible) is already there, but the fact is that what Marcos mentioned, if you look at exactly what we're doing is we're investing -- continuing to investing aggressively in the digitalization of the Banorte and the spin-offs that we have on the digital bank. But I think the most important thing is that we are strengthening all the commercial lines of the bank at the same time in order to be able to maintain whatever the rates are a very reasonable return on equity for the shareholders.

So yes, eventually, you will see a very close number to the very at the bank level. We are pretty sure of that. But I think what you have to see is how that return on equity is really obtained and it's obtained exactly as Marcos mentioned has to do with a very good cost of fund that needs and continue to improve a good expansion on the consumer and the commercial books. And the most important thing is that the fact the decline relates to Banorte more and more at NPS, very, very close to the [80s, 82, 87] in most of the services that we provide.

So if the client like us, we have a very good cost control with the asset book is as clean as it is, and all the processes that we are delivering to the market are improving by the day based upon the customer centricity that we have. I think the general equity will not be depending on the future of accelerating trend all the way. It will be more and more based upon what the bank can really diluted based upon this huge transformation that is ongoing and is already delivering with [splendid] results.

### **Jose Marcos Ramirez Miguel *Grupo Financiero Banorte, S.A.B. de C.V. - CEO & Proprietary Board Member***

And Thiago, regarding the second question that you have regarding asset quality, I will tell you that credit risk ratios are well under control or even better than COVID levels as you have seen. As quality ratios remain at historic low levels. And looking forward and to the close of 2022, I would tell you that we expect NPL ratios to be ranging from 1% to 1.5%, and cost of risk ranging from 1.4% to 1.6%. We have been running risk scenarios trying to measure expected losses -- expected losses and even catastrophic losses. In this modeling, we have been measuring the impacts and within a changing economic financial market and behavioral assumptions. So we remain confident, but very expectant to purchase might arise given some of the [credit] risk that you have all seen like geopolitical and so many other types. So asset quality, you can rest assure that for the short term, it is guaranteed to be ranging from those levels that I mentioned.

### **Tomas Lozano Derbez *Grupo Financiero Banorte, S.A.B. de C.V. - Head of Corporate Development, IR, Financial Intelligence, M&A and Sustainability***

Now we will continue with Rafael Frade from Citi.

### **Rafael Berger Frade *Citigroup Inc., Research Division - Research Analyst***

I have 2 questions here. The first one is related to the guidance for the updated guidance for 2022. So with this updated guidance, it implies that earnings should go down in the fourth quarter versus the third quarter. I would like just to understand if you are being conservative here, if there's any line that potentially can impact the fourth quarter?

And the second question is related to insurance results, insurance and pension results. So you show a very strong improvement in the

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operational side. But in terms of [premium] issue, in fact, it fell year-on-year. So just want to understand here, where we are in the insurance operation, as you mentioned, it's normalizing. I would like to understand if it's already almost normalized or is still there are some lags here. Just trying to understand where we are.

### **Jose Marcos Ramirez Miguel *Grupo Financiero Banorte, S.A.B. de C.V. - CEO & Proprietary Board Member***

Rafael, the first one, no. This quarter is going to be at least the same or maybe a little bit up. That's what we are expecting as a guidance. So I don't know what's your number, but no, we are going up or at least, we think that the same amount. So you can run through the numbers on that and come with the final numbers.

And the second one, insurance, the premiums, yes, we have some information that we'll need to give you. Go ahead, Rafael.

### **Rafael Victorio Arana de la Garza *Grupo Financiero Banorte, S.A.B. de C.V. - Chief Financial & Operational Officer***

Yes. The fact is that, yes, the insurance business is going to normal now. You will see that fully in motion in the first quarter next year, but it's already happening. And also I would like to clarify something that was a concern of some of the analysts that in the other income, there was an additional provision for the insurance business and for the annuities business. This has to do for 2 specific related issues on VAT potential claims.

That is not just for Banorte, but for the whole system that we are anticipating that in order to be prudent on that. And on the annuity side, also some plans on the tax-related issue that is ongoing. By the way, we already gained the first claim for that. So I think we are in a good position, but we would like to point on that. So that's I think is -- I think it's -- everything is trending in the right direction in the insurance business as you saw on the slides projected to do that the premiums are going up and the penetration on our client base and we go and moving on the right direction.

### **Tomas Lozano Derbez *Grupo Financiero Banorte, S.A.B. de C.V. - Head of Corporate Development, IR, Financial Intelligence, M&A and Sustainability***

We now go with Jason Mollin from Scotiabank.

### **Jason Barrett Mollin *Scotiabank Global Banking and Markets, Research Division - MD of LatAm Financial Services***

Great. Congratulations on the good quarter. I have a follow-up on the cost of risk and provisionings. If I heard correctly, I believe there's still MXN 1 billion in excess or additional provisions that could be used going forward. I believe that number was MXN 1.3 billion in the prior quarter. So is it that you consumed that MXN 300 million of the prior amount that you had? And maybe if you can give us a little more color on the statements of an increase in provisions in payroll, maybe to talk a little bit about that product. It's a great market share, 21%, if you can tell us a little bit about the clients and what they're facing and what are the risks in that portfolio? I'm imagining they should be low, but if you can help us understand where delinquency could come from or has come from in the past and could come from in the future.

And the second theme, I thought maybe you could provide some color on is competition. We've seen new entrants growing credit card plastics issued at a rapid pace. If you're seeing that as a risk for the market in general and if there are segments that you think that Banorte should stay away from.

### **Jose Marcos Ramirez Miguel *Grupo Financiero Banorte, S.A.B. de C.V. - CEO & Proprietary Board Member***

Let's start for the second one, the competition in the (inaudible).

### **Jose Francisco Martha Gonzalez *Grupo Financiero Banorte, S.A.B. de C.V. - MD of Digital Businesses***

Jason, Francisco Martha. I agree. We -- as Banorte -- the Banorte vehicle, we are being very careful with the segments that can enter into a highly risk or a nonperforming loan. So we are being very careful growing the portfolio as much as we can, but with -- but being careful. And -- but we have the other vehicle, at least in our case, that it's [Lapicar]. As we mentioned a quarter ago, we have been slowing the pace of growth because of the situation, but we are still growing very carefully. We think as your -- as you imply in the question that, that something can be complicated for the new entrants that are giving that kind of cards or kind of credit without reviewing credit bureau or not being as preventive as we are.

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### **Rafael Victorio Arana de la Garza *Grupo Financiero Banorte, S.A.B. de C.V. - Chief Financial & Operational Officer***

Regarding your first question, Jason, COVID provisions were 1 year ago, MXN 2.97 billion, that was September 2022. As of now, they are MXN 1.038 billion. You are right, it is not MXN 1.3 billion, but MXN 1.038 billion. And going forward, we are still expectant of this winter and see if this same risk factor behaves in a better way or more favorable way to our business. Regarding the payroll behavior, the payroll loan portfolio, I would tell you that there are 2 main key risk factors. One of these being the cash management services of the payer with companies that distribute with payrolls. Once you lose that service, the credit risk activates we've seen each individual loan in this product. We are always monitoring what the behavior is regarding that.

And the second big credit risk factor is customer payroll, mobility. So once it is easy to each customer to change the bank that the account receives the payroll, that is a secondary factor, but it is also in our risk greater all the time. Regarding the behavior of provisions, I would tell you that [there are some far] most factories growth. I underline that is growth. I emphasize that factor. And the second one is that we did open credit standards and lower them within our risk appetite. So you can expect to see cost of risk growing in that product for -- in the near term. So those are the 2 biggest things that explain this increase in provisioning.

### **Jason Barrett Mollin *Scotiabank Global Banking and Markets, Research Division - MD of LatAm Financial Services***

Just to follow up on the excess provisions. I understand. I think -- I don't know if you misheard me, but I think I was referring to the quarter-on-quarter change. In the excess provisions that I believe that from the second quarter presentation, we had MXN 1.3 billion and now as you're suggesting we're at MXN 1.038 billion.

### **Rafael Victorio Arana de la Garza *Grupo Financiero Banorte, S.A.B. de C.V. - Chief Financial & Operational Officer***

You're right, Jason, it is MXN 1.298 billion, MXN 1.3 billion like you said.

### **Tomas Lozano Derbez *Grupo Financiero Banorte, S.A.B. de C.V. - Head of Corporate Development, IR, Financial Intelligence, M&A and Sustainability***

Now we will continue with Alonso Garcia from Credit Suisse.

### **Ricardo Alonso Garcia *Crédit Suisse AG, Research Division - Research Analyst***

So the first one is a follow-up on capital. I would just like to touch base on how front loaded or gradual, do you think this process of optimizing capital would be from this 14.7% CET1 ratio to the 12% to 12.5% where you would like to run the bank, plus the excess capital you have at the group. I mean do you think -- I mean you already mentioned that you are going to call for our shareholders, for an assembly and then announce on dividends. So do you think you will optimize your capital position already released with this dividend announcement?

Or do you think this would be instead a more gradual process, I don't know, for the next 1, 2 years until you finally optimize your capital structure. And historically, I mean, your returns to shareholders have been much more skewed towards dividends as opposed to share buybacks. So I don't know if you could provide some color on how the split going forward should be?

And second, I have a follow-up question on your retail strategy, specifically on the mortgage product. I mean we have seen an acceleration to 10% year-over-year growth from 6% in the previous quarter with 5% growth in 3Q alone. So my question is, how are you competing in this segment? Is it group pricing? How is your pricing strategy relative to your competitors? That will be my question.

### **Rafael Victorio Arana de la Garza *Grupo Financiero Banorte, S.A.B. de C.V. - Chief Financial & Operational Officer***

Let me start with the mortgage one, Alonso. The mortgage, as you know, we have the best risk numbers in the market. The second one towards is double that we have in the mortgage loan. So if you look at the expected loss of the book, it's really, really, really low, because the quality of the brands that we're going to try. So we have been very careful in managing the price hike, because we continue to see an acquisition process that is bringing the best clients in the market. So by taking into account the expected loss that is extremely low, we can really manage and still be very competitive on a risk-adjusted margin, even though you see that we have been slow in the hiking of the prices.

The other thing that you have to take into account is that usually, the mortgage comes with a lot of other products at the same time. So

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the lifetime value of the client is exactly what we are really looking at. And that lifetime value continues to expand. So don't be surprised that if you see that we are sometimes the lowest in the market on the price, but you have to take into account all the issues of our risk adjusted margin, how do we manage the risk and exactly at what position in the time line we have compared to our competitors. And remember that we basically do the mid to the high end on the mortgage loan.

On the second question, the related -- the normalization of the capital ratios, I think you described it pretty well. It will go from 1 to 3 years to normalize that to the 12.5%. Taking into account that times are a little bit hectic right now. So be prudent on that part, not overly prudent but being prudent is something that we would like to -- you have always seen that in the Banorte behavior. But you will see a trend toward that number in the coming months along so. So I think those are the 2 questions.

And on a competitive basis take into account that I think Banorte is now able to compete in any space with any brand in any product. So that is why it's really pushing up all the numbers. And the good thing is that we are coming from a very low end on the credit numbers that allow us to be -- I would not use the word picky, but picky about the type of lines that we would like to have in our book.

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**Tomas Lozano Derbez Grupo Financiero Banorte, S.A.B. de C.V. - Head of Corporate Development, IR, Financial Intelligence, M&A and Sustainability**

Now we'll go with Nicolas Riva from Bank of America.

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**Nicolas Alejandro Riva BofA Securities, Research Division - VP in Credit Research & Research Analyst**

So my question is on capital once again, and then I see a lot of questions on excess capital year towards paying back -- paying some extraordinary larger dividends. But if I look at the capital structure, the excess capital is really concentrated particularly on the AT1 bucket. So you have roughly 800 basis points of AT1. The optimal level would be around 50 basis points. So now given that you already announced, we are not going to be buying Banamex. How should we think about this AT1? I mean do you agree you have a lot more AT1 than you need? Does it make it more likely that you're going to be calling the AT1s without even the need to issue more AT1s? And if you would even think about buying back some of these AT1s ahead of time. So that's my first question.

And then the second question, and potentially, you cannot discuss this at all. But on Banamex, my only question is, if you can share with us the main factors that led to you no longer been in the running to buy Banamex, if it was more Banorte's decision or [CET] rejecting the offer.

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**Jose Marcos Ramirez Miguel Grupo Financiero Banorte, S.A.B. de C.V. - CEO & Proprietary Board Member**

We start with the end. As anticipated by Tomas, we are unable to share any further information in connection with the [CETI dynamics] transaction per our confidentiality undertakings. And let's work the good question about the capital -- excess capital (inaudible). Rafael?

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**Rafael Victorio Arana de la Garza Grupo Financiero Banorte, S.A.B. de C.V. - Chief Financial & Operational Officer**

Nicolas, I think you have to understand that the AT1s for us is not just issue that we would like to have for the sake of have a more expensive type of instrument that the (inaudible) because it allow us to change. On liquidity purposes allow us to have a very stable liquidity base. As you know, the perps characteristic of the AT1s, we don't have to build up liquidity a year before that to go. So that's one thing that proves to be very efficient in the convenient.

The second one is that Banorte now is extremely active on the dollar. I think we are reaching levels that Banorte was never outplayed on the dollar group. And now we have a very strong play in the dollar book in the market. So we have -- we are now to have a midterm funding for those loans. So the AT1 strategic for us in a way to build up the balance sheet on the Dollar group and also to provide -- and there's with a question that people say, why don't you call -- why did you call that the AT1, if it was not financially wise. The fact is that we honor the calls because that's what we said, and we want to be one of the calls.

We will not call the -- because some people say, well, why don't you call your bonds you are well below par? Well, the fact is that for us, it's part of the structure of the balance sheet is not important. And the way that we manage the balance sheet is in a very conservative way. We don't go up and down based upon opportunistic issues. We look at always the structure of the balance sheet. So that's the reason for the AT1s. If you ask me, if we want to issue more AT1s, it depends on the -- as you know, Banorte has always been very

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opportunistically going to the market. We never go when we need -- we know when we want the instrument.

And I think at this point in time, the market is extremely volatile about prices. So we are concentrated on what we have. I think we have a strong capital base. And as I mentioned to you, the ATI is a very important part of how do we compete on the dollar form, [dollar funding] for the group and has been extremely positive for us. And remember that when some people has always tell me in the past, where were you taking the equity -- benefit from the equity line and providing them to the fixed rate part, yes, we are returning 24% on equity. So I think that's a very good investment.

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### **Tomas Lozano Derbez *Grupo Financiero Banorte, S.A.B. de C.V. - Head of Corporate Development, IR, Financial Intelligence, M&A and Sustainability***

Now we will continue with Tito Labarta from Goldman Sachs.

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### **Daer Labarta *Goldman Sachs Group, Inc., Research Division - VP***

A couple of questions also. Maybe first on your margin. I know you have the guidance. But just want to think a little bit longer term on the sustainability of it, once rates come down, I guess, first, when do you think rates could come down? Any color on, I guess, inflation and when that may start to come down and what that could mean for rates maybe towards the end of next year. And I know you have the sensitivity of MXN 1.2 billion for every 100 bps increase in rates. Should we consider the same sensitivity on the way down? Or is there something that you could do to reduce maybe the sensitivity on the way down?

And then my second question is on your loan growth. You mentioned your GDP growth slowing into next year. I think you said consumer loans may moderate closer to double digits. Any color, how should we think about loan growth for next year? And should we expect a slowdown as GDP growth slows?

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### **Jose Marcos Ramirez Miguel *Grupo Financiero Banorte, S.A.B. de C.V. - CEO & Proprietary Board Member***

Let's first see how we see the rates and then we (inaudible) [Alejandro], please.

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### **Alejandro Padilla**

This is Alejandro Padilla, Chief Economist. Well, what we expect is that [banking] might keep the repo rates at 11% for several months during 2023. However, we are forecasting that they can start cutting rates by the end of next year, maybe decoupling from the Federal Reserve, but at a very mild and cautious pace, indeed, from that 11% that Marcos was talking about that we expect in the first quarter, we think that by year-end, the repo rate might reach [10 and 1 a] quarter. On the other hand, going forward, I think that taking into account inflation dynamics for 2023 and maybe 2024, I think that it's going to be more a story of 2024 in which [Makiko] can cut rates at a faster pace. But I think at least in 2023, we might think of higher rates for longer.

From the growth side, Marcos was mentioned before, we are confident in our 2.1% increase of GDP for this year. However, we think that with several headwinds in the global economy, these risks of a global recession and taking into account that mainly the US will be more resilient than other regions. We think that Mexico can grow around 1% in 2023. However, we have to take into account that we might see a very different pace of growth in Mexico from these states in the central and northern part of the country that are more integrated with trade dynamics to the US from those states that are in the southeast part of the country. But overall, we are forecasting 1% for the GDP of next year.

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### **Daer Labarta *Goldman Sachs Group, Inc., Research Division - VP***

Maybe follow-up on the NIM and the loan growth.

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### **Jose Marcos Ramirez Miguel *Grupo Financiero Banorte, S.A.B. de C.V. - CEO & Proprietary Board Member***

Yes. We will say in the next conference, the final numbers of the guidance. But for now, let's keep in mind between [5% and 7%] around the loan growth over the next year on that.

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### **Rafael Victorio Arana de la Garza *Grupo Financiero Banorte, S.A.B. de C.V. - Chief Financial & Operational Officer***

And the NIM, I think recurring -- we have Banorte have been proved that on the -- when the rates were low and things that an attainable sustainable NIM should be around from 6% to 6.3%.

### **Tomas Lozano Derbez *Grupo Financiero Banorte, S.A.B. de C.V. - Head of Corporate Development, IR, Financial Intelligence, M&A and Sustainability***

Now take the next question from Carlos Gomez-Lopez from HSBC.

### **Carlos Gomez-Lopez *HSBC, Research Division - Senior Analyst, Latin America Financials***

Congratulations on the results and congratulations on never having to answer a question about Banamex again. Specific questions. Going back to your expectation for the year. Again, for the fourth quarter, you essentially have a one-off provision in this third quarter regarding the annuities and the pensions. Rates continue to be up. The average rate is going to be higher in the fourth quarter than in the third. Why wouldn't earnings continue to grow? I know you have increased your guidance by 8%. But as mentioned earlier, you're still implying that we will have a lower fourth quarter. I wonder if there is something that we are not seeing there.

Second, your tax rate for the year, I think we are coming out at around 26%, which is higher than last year, despite higher inflation is that where we should expect it for the rest of the year and for next year?

### **Jose Marcos Ramirez Miguel *Grupo Financiero Banorte, S.A.B. de C.V. - CEO & Proprietary Board Member***

Yes, the tax rate should be around 26%. And yes, there are issues (technical difficulty) we are cautious. That's what we're talking about. (technical difficulty)

### **Carlos Gomez-Lopez *HSBC, Research Division - Senior Analyst, Latin America Financials***

Okay. So pure caution. No specific reason.

### **Jose Marcos Ramirez Miguel *Grupo Financiero Banorte, S.A.B. de C.V. - CEO & Proprietary Board Member***

No, we don't see any (technical difficulty) so far.

### **Rafael Victorio Arana de la Garza *Grupo Financiero Banorte, S.A.B. de C.V. - Chief Financial & Operational Officer***

[And that's why we have] the range going through.

### **Tomas Lozano Derbez *Grupo Financiero Banorte, S.A.B. de C.V. - Head of Corporate Development, IR, Financial Intelligence, M&A and Sustainability***

Now we will continue with Andres Soto from Santander.

### **Andres Soto *Santander Investment Securities Inc., Research Division - Head of Andean Research***

My first question is regarding your decision not to participate in this deal. But actually, this is more related to your strategic plans ahead. Now how these decision changes? Are you willing to grow organically on a more accelerated way? And if that's the case, what is going to be the role of the digital banking in this part of the strategy?

### **Jose Marcos Ramirez Miguel *Grupo Financiero Banorte, S.A.B. de C.V. - CEO & Proprietary Board Member***

As I said, Banorte has a life of some, and we will be taking the most of the opportunities ahead of us. And when I say that, I mean all we are not a bank. We are a financial group. All the financial groups that we have in Mexico. In Mexico, you know we need to -- [bank arise a lot] in Mexico. We have a lot of things to do. We are hoping for our future. And it's coming for the guys that are prepared, and we want to be prepared. So everything is on the table.

### **Rafael Victorio Arana de la Garza *Grupo Financiero Banorte, S.A.B. de C.V. - Chief Financial & Operational Officer***

If I may add to what Marcos says, remember, in 2018, it's not that Banorte is planning the future now. In 2018, we define the path of growth for Banorte for the coming years. We short term the planning process to the -- in 2023. But really it's for the ongoing future. And I think it's very, very, very clear is that the fact that Banorte, the traditional bank is now almost fully digital. You can do whatever you want.

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You can go to the branches, you can do everything on digital. So that transformation is almost complete and will continue to be ongoing on that part. The Rappi is already in place, so that has a space on its own.

The digital bank would have a very specific part that we are multi segment banks that could approach the high end and the low end at a much better cost base and benefits for the client. But what you see is an organization that has all the capabilities in place and in fully and in full motion. And also the businesses that we have the annuities business, the insurance business, the broker, dealer, the mutual funds, all of whom have been part of this deep transformation of Banorte. So when we say that we have a rise on loan is that we're constantly evolving from that, strong base that Banorte has. We're never going to be still or anything like that. We will see a continuous evolution of Banorte, but the most important thing to consider about Banorte is Banorte is fully a creator of its own future. We don't need anything else to build up on the future that will be for them.

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### **Andres Soto Santander Investment Securities Inc., Research Division - Head of Andean Research**

And my second question is regarding the excess capital that you have at the holding company level. As my large look, that was about \$1 billion. I would like to confirm if that's still the figure or what is the new number? And also if the full purpose of this will be to return to shareholders or you are going to keep some of this money for pursuing any other opportunities that you may have?

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### **Jose Marcos Ramirez Miguel Grupo Financiero Banorte, S.A.B. de C.V. - CEO & Proprietary Board Member**

The number is MXN 29 Billion.

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### **Andres Soto Santander Investment Securities Inc., Research Division - Head of Andean Research**

And the purpose is that, that will be available to return to shareholders?

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### **Rafael Victorio Arana de la Garza Grupo Financiero Banorte, S.A.B. de C.V. - Chief Financial & Operational Officer**

That will pump up, yes.

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### **Tomas Lozano Derbez Grupo Financiero Banorte, S.A.B. de C.V. - Head of Corporate Development, IR, Financial Intelligence, M&A and Sustainability**

We'll now take the next question from Guillermo Delgadillo from Santander.

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### **Guillermo Diego Delgadillo SAM Asset Management, S.A. de C.V., Sociedad Operadora de Sociedades de Inversión - Co-Portfolio Manager of Mexican Equities**

Maybe just on the capital allocation side, we have seen the stock having a normal correlation with the markets, with the U.S. banks. This correlation obviously in the last month was broken, the stock outperformed close to 11% versus the benchmark. You have other players that were also bidding in the Banamex process like, Grupo Mexico, and they're performing like 14% considering that copper is like flat minus 1%. So it seems like the stock has discounted.

Obviously, a certain part of you taking out of the transaction right along the financial calls that we have seen with this rally in the stock, obviously, the price is close to the higher range of the multiple levels in the last 10 years, 20 years. So from a treasury perspective -- and maybe this question goes more for Rafael, but obviously, for Marcos. From a treasury perspective, what's going to be the structural axis for deciding the capital allocation?

Today, as you said, with the rally, if you divide the return on equity between the book value, it seems that you are investing your money close to 10%, 11%. If you do a dividend, the Mexican overnight rate is close to 9.25% and the set is when you spend 88%. So it seems for the people or investors looking for yield, the short-term treasury or the overnight seems like a pretty fair alternative. So it seems you are in a tough decision, either from the dividend side given the funding levels or either from the buyback given the return on equity divided by book value. So what are going to be the structural axis to return to the shareholders this MXN 29 billion that Marcos already said? That's maybe the first question.

And the second question is, as we had the conference call, the President was talking about the transaction. It mentioned that the Chairman, Carlos Hank tried to look for him in the night just for a quick call, he wasn't available, but he was going to be talking with him

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after the President's morning call. So is this just a courtesy call, just to inform about the return from the process or should we expect something from this President, Carlos Hank call?

### **Jose Marcos Ramirez Miguel *Grupo Financiero Banorte, S.A.B. de C.V. - CEO & Proprietary Board Member***

On second one, they have a relationship and they talk about a lot of business. So I don't know that we are here in the meeting. And regarding the first one, it's a tough one, because as I said, I used the word approval to pay dividends and/or buybacks. We want to maintain both because we need to see what's going in the future and vice versa for the bank and what are the opportunities there. So we want to maintain open around that.

I don't know, Rafael, if you want to...

### **Rafael Vitorio Arana de la Garza *Grupo Financiero Banorte, S.A.B. de C.V. - Chief Financial & Operational Officer***

No, and I talk to agree with you. I mean, all the time that you see the EPS accretion for the shareholder, you see dividends. At this point in time, we have dividend and the buybacks. But on a long-term basis, what's the best deal for the shareholders. The fact is that Banorte will continue to be a strong provider of capital for the shareholders. And also that allows us to be very opportunistic in the market where we see that something could be of additional value for the shareholders. I mean, the credit ratings of Banorte are very strong. And we don't have an issue on that if we see something that we might want in that quarter.

I think, as you mentioned, we always balance out what's the best deal for the shareholders. And we understand that we have our shareholders that are basically based upon growth, probably ones that are basically on the dividend payout and other ones are on a fixed rate basis. So we have to balance all those out. And as you mentioned, we always do all those calculations that we use in order to maximize each of one of those in the best way that we can.

### **Guillermo Diego Delgadillo *SAM Asset Management, S.A. de C.V., Sociedad Operadora de Sociedades de Inversión - Co-Portfolio Manager of Mexican Equities***

And just finally, a quick question. Jason, you have already discussed the provision side, you have already mentioned that on the first quarter, second quarter, the yearly comparison, the quarterly comparison was beneficial, and this third quarter, there was a quarter-on-quarter jump of 30%. But Marcos said something important about the risk factor. So throughout COVID, throughout 2020, Banorte was one of the state of the art banks to forecast the provisions. So considering this platform, this state of the art platform and what Marcos said about the risk factor to continue monitoring, would you say that throughout October, which is practically done, this risk factor has improved? Should we expect the provision that we saw in this quarter to start decreasing or are we still on a wait and see mode?

### **Jose Marcos Ramirez Miguel *Grupo Financiero Banorte, S.A.B. de C.V. - CEO & Proprietary Board Member***

The answer is steady, but I'll ask Gerardo Salazar to put some color on that.

### **Gerardo Cuitlahuac Salazar Viezca *Grupo Financiero Banorte, S.A.B. de C.V. - Chief Risk Management & Credit Officer***

We're still stagnant and our job is to be prudent. So there is no change. There is no improvement. From this time on, we are just stagnant of what the environment could present to us.

### **Tomas Lozano Derbez *Grupo Financiero Banorte, S.A.B. de C.V. - Head of Corporate Development, IR, Financial Intelligence, M&A and Sustainability***

Now we will continue with Jose Luis Cuenca from Citi.

### **Jose Luis Cuenca Gonzalez *Citigroup Inc., Research Division - Assistant VP & Senior Associate***

Just a very quick one. I'm sorry if you already answered it. I got disconnected somewhere along the call. Just wanted to ask if you could please remind us what is your long-term sustainable ROE?

**Jose Marcos Ramirez Miguel *Grupo Financiero Banorte, S.A.B. de C.V. - CEO & Proprietary Board Member***

First, let's define long-term. We're aiming, let's say, for the 20s and that's like our model now is to have it, let's say, forever. Obviously, you will see I expect the 30s and then maybe 18 something. But I think a nice sustainable worldwide recognized ROE should be that 20s and that's our goal, let's say, in the near and long-term.

**Tomas Lozano Derbez *Grupo Financiero Banorte, S.A.B. de C.V. - Head of Corporate Development, IR, Financial Intelligence, M&A and Sustainability***

We'll now take Edson Murguia from SummaCap.

**Edson Murguia**

I have 2 questions. The first one is related to the guidance of expense growth. Just trying to figure out this is related that you expressed in the press release, which is about traveling and all the type of even increasing the number of personnel in the commercial force. And so looking ahead, at the end of 2022, it might be in the same sense or it's going to adjust because of the dynamics of the economics? That will be the first one. The second one is related about BanorTec. It's interesting, the initiative. So I was wondering if this type of initiative we can see with other universities in Mexico?

**Jose Marcos Ramirez Miguel *Grupo Financiero Banorte, S.A.B. de C.V. - CEO & Proprietary Board Member***

We'll start with the BanorTec with Francisco Martha.

**Jose Francisco Martha Gonzalez *Grupo Financiero Banorte, S.A.B. de C.V. - MD of Digital Businesses***

Edson, yes, you can expect that. We are already reviewing with some other universities and some other institutions where we can create such kind of ecosystems.

**Edson Murguia**

And just a follow-up on this. Do you have any specific target of number of accounts or type of different products in other universities or even with BanorTec type of launch or origination or what will be the goal?

**Jose Francisco Martha Gonzalez *Grupo Financiero Banorte, S.A.B. de C.V. - MD of Digital Businesses***

The same way that we are planning for the bank and for the 3 pillars of the strategy. We are not talking about products, but more than products, we're talking about experiences. So the students can have an account where they can save money or they can use their money for payments and they can have a credit card. And we will be launching some type of credits.

And depending on -- if you talk about students, the credit can be for different use and if you talk about the teachers or the alumni. We have now close to 1,600 accounts from a number of 7,000 students. So we're targeting -- not exactly -- we don't have a target, a specific target of accounts, but we are trying to move away the cash and create ecosystems. So more than market share, we are talking about a share of trends because we have talked about this before.

**Rafael Victorio Arana de la Garza *Grupo Financiero Banorte, S.A.B. de C.V. - Chief Financial & Operational Officer***

On the expense line, as you can see, there's a lot of moving parts. If you look at the results, personnel expenses are growing only just 1%. So that's an incredible number, but you have also -- have to take into account the PTU part that is part of the personnel expenses. What we can tell you is that being in the situation that we are on a bank that is growing and very active and creating more commercial capabilities, I think we are managing expenses extremely low. And because to be able to contain the expense growth and at the same time grow the commercial capabilities and still invest in IT is I think something that we are good at.

**Tomas Lozano Derbez *Grupo Financiero Banorte, S.A.B. de C.V. - Head of Corporate Development, IR, Financial Intelligence, M&A and Sustainability***

Now we'll continue with Yuri Fernandes from JPMorgan.

**Yuri R. Fernandes *JPMorgan Chase & Co, Research Division - Analyst***

Congrats on the results. I have just one regarding our non-bank business, you already discussed this during the call sometimes. But if you can provide more color on how you see the insurance, the annuities, the broker-dealer, I guess the Afore. This is 25% of your earnings, ROEs on an aggregated basis has been below the bank. So my view here is what you expect for 2023, '24?

Like, are you seeing what can help those units to improve the operations? I guess, Afore, we had a lot of regulation and you already saw a better quarter, but which one could surprise us here? Like do you see more room for insurance to surprise? Like can we still continue to see better results on insurance? Like just a general view on ROEs and growth for those units that we don't discuss a lot in details usually?

**Jose Marcos Ramirez Miguel *Grupo Financiero Banorte, S.A.B. de C.V. - CEO & Proprietary Board Member***

Yes, they are in different boxes and different lights now. Let's go for a broker-dealer, it's a little bit complicated because there's a lot of volatility, but we expect to have a very good ROE, better than the bank you stated. The same happens with insurance, and we will have good news there. Remember that (inaudible) and now they need to go back to their business and then this happens to be a very good business and we know how to do it.

And now let's talk about the Afore, about the regulator, and this is another deal totally. It's a deal of heavy loss of more clients and cost control. And I think the work is over because the rates will not have the impact -- the investments of Afore. So it's going to be another story, but at the end in the future it's going to be also a good part of the financial group. Remember as I always say we are a financial group and we have counter cycle the insurance and then this is one of them, therefore it should be one when the rates slow down. And so we feel very comfortable of the business that we have.

I don't know, Rafael, you want to say something.

**Rafael Victorio Arana de la Garza *Grupo Financiero Banorte, S.A.B. de C.V. - Chief Financial & Operational Officer***

No, I think, Yuri, the fact -- in fact, if you look at the returns on equity, you're looking at a very efficient use of capital in those businesses. All of them are above 20% for the Afore. We know the Afore has a lot of goodwill included (inaudible). The fact that Afore is going to take, as you know, to double the assets under management based upon the new mission structure that happened and will also increase substantially (inaudible) have difficulty on their accounts. So that's going to take 4, 5 years.

So you will start to see some relief after the (inaudible) on that part, but there will be benefits coming from the management of the investment that we have on that part. So Afore is a long-term issue. It's a good source of dividend for us. It will become pretty active on the net income side after 3 years that we start to balance out the amount of money that flows into the accounts and balance out that with optimum ease. So at this point in time, the Afore, as you can see on the numbers, is something that is very good thing.

**Yuri R. Fernandes *JPMorgan Chase & Co, Research Division - Analyst***

So what I understood is basically the annuities and the broker, they may run and they are running very close to the ROE of the bank unit around those 27, right? Insurance is not there yet. But I guess, the message is that you see this going to kind of that level and the Afore is the only one that ROEs are more in line with cost of capital, like it's a more specific unit, right? Like is this summary okay, Rafael? Did you understand correctly?

**Rafael Victorio Arana de la Garza *Grupo Financiero Banorte, S.A.B. de C.V. - Chief Financial & Operational Officer***

No, if you look at the -- business is about 40%. So the return on equity of the insurance business is extremely high. It's about 40%. The annuities is about the 20%. I think the issue that we have on the Afore business is that you have to look on tangible, you will see a more reasonable one. At this point in time, the return on equity, including the goodwill, is very positive. But the annuities and the insurance business are well above the general equity of the bank, especially the insurance business and this is more aligned with the return on equity of the bank.

**Unidentified Company Representative**

May I jump in?

**Rafael Victorio Arana de la Garza *Grupo Financiero Banorte, S.A.B. de C.V. - Chief Financial & Operational Officer***

Yes, go ahead, (inaudible)

**Unidentified Company Representative**

I want to give you some flavor or more flavor on what you asked. I mean, that we have a lot of opportunity to grow in all the lines of businesses. Let me start with insurance. I think insurance -- I mean, the most profitable products that we sell are related to Bancassurance and those are products linked to credit, but also we sell products which are not linked to credit. So as long as the bank keeps growing, as it has been, we will see there definitely a very nice growth in our mix in the future because what happened in the past was related to COVID, but that's something that is about to be gone quite recently, I mean, very recently.

And we are very confident that we will keep growing there. And we are also developing some other distribution channels for the insurance products in the digital world. So I think we will see there some perfect product. And actually, the return on equity for these lines of businesses is about 50% in the insurance business. So it is quite -- it's much higher than what you see in the bank level.

Now let me go to the annuity firm. The annuity firm has been performing very well. And as you know, there are 2 lines of businesses which are related because it depends on how many pensioners you have. But the first business is to, of course, sell annuities. And we have been the leader in the market with 46%, 47% of the market share. It depends on how the market grows. But as you may know, we expect that this market will be growing steadily in the future, mainly because the transition generation that is those workers that were -- that started after -- it will finish for all those workers that started contributing to a system in 1997. So they will not have the right to be pensioners according to the previous law. So this market will keep growing. And of course, eventually, this will be a very, very large number and we're the main player.

And the other line of business is that we sell credit loans to -- which are payroll loans, but with very low risk because we pay the payroll. So we have a very -- we don't have delinquency rates there because we pay us first and then we put the money into the pensioners' accounts. So it's a very, very, very healthy business. And also the ROE has been performing quite well. And I should tell -- or I should mention that we expect that market to keep growing.

Now regarding to Afore, I mean, as you know, we have a reduction in the short-term of 28% in the commission that we charge on the assets under management, but we also face this market stability that reduced the assets under management with respect to review in our budget, more or less 13%. That's why -- and that's why we are -- due to those facts, I mean, we are having like one -- I would say, like MXN 1,640 million less in terms of commissions with respect to previous year, but also because we have to invest the capital of the Afore in the funds, according to special reserve, we have a mark-to-market hit for that money of around MXN 870 million. So what I will tell you is that, taking out those effects, the result would have been double for the Afore. And I'm talking here, of course, 100% because we only own 50% of the Afore. So we will have, at this point, the double of the earnings that we are observing.

Now for the future, of course, given the dramatic production last year, hopefully, we will not see such reductions in the commissions. And therefore, we expect that eventually, as the asset management recover, and also it depends, of course, on the growth on employment and also on wages, but we do foresee in the future that the assets under management will keep growing and also the reduction in the commissions. And also something that is coming next year, start to come next year is that remember that the contributions will rise steadily -- will rise for the next 10 years more or less 1% on the payroll contributions per year.

So taking those facts into consideration, I think that there will be better news for the Afore business as well. And hopefully, as you know, we spend a lot on the transfer of accounts. Hopefully, those will also be lower in the future and more concentration in the industry. And that will also help for better performance of these assets. That's what I would mention.

**Tomas Lozano Derbez *Grupo Financiero Banorte, S.A.B. de C.V. - Head of Corporate Development, IR, Financial Intelligence, M&A and Sustainability***

We will end with the final question from Federico (inaudible)

**Unidentified Analyst**

Congrats for the numbers. Just 3 questions. The first one, just to check the -- in your guidance of ROE, you are not including for this year any additional payment of dividends. This is the first one. The second one is, in the fees continue to grow stronger, in particular, electronic banking, what do you expect for the second part for the fourth quarter? And the last one, when we see the loans breakdown in the portfolio, mortgage and consumer have been growing faster than commercial. What do we expect for the next year? These 2 lines growing more than commercial and corporate as was the last years?

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**Rafael Victorio Arana de la Garza *Grupo Financiero Banorte, S.A.B. de C.V. - Chief Financial & Operational Officer***

The first one, Federico, the guidance for return on equity does not include any dividend payments.

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**Jose Marcos Ramirez Miguel *Grupo Financiero Banorte, S.A.B. de C.V. - CEO & Proprietary Board Member***

The other question, I think the mortgage and the consumer has been outstanding growth. You asked next year, we will see a moderation on the growth on the mortgage group because, as you know, the increase in rates, mortgages in Mexico are fixed rate. So eventually, you will see that there are low (inaudible) credit for 15 years. At a high rate, we would not be very (inaudible) for our clients, even though we have been managing the price pretty well. But I think that there will be a moderation on the mortgage product for the next year.

The other thing is that in some parts of the country the properties also have been having some discounts. So one is balancing the other. That's not the case all over the country because in other parts prices are growing fast, pretty high. But I think it will be a moderation compared to this year, Federico.

And the last one is set around the commercial fees. Fee will continue to expand well above loan growth. And you will see that the fourth quarter usually is a very high quarter of fees. So that will continue to be the number more of the 13% maybe 14% for the fee growth. But I think it will continue to outpace the loan growth.

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**Tomas Lozano Derbez *Grupo Financiero Banorte, S.A.B. de C.V. - Head of Corporate Development, IR, Financial Intelligence, M&A and Sustainability***

With this, we conclude our presentation. Thank you very much.

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**Jose Marcos Ramirez Miguel *Grupo Financiero Banorte, S.A.B. de C.V. - CEO & Proprietary Board Member***

Thank you, all.

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