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CORPORATE PARTICIPANTS

Carlos Eduardo Martínez González *Grupo Financiero Banorte, S.A.B. de C.V. - MD of Retail Banking & General Director Retail Banking*

Fernando Solís Soberón *Grupo Financiero Banorte, S.A.B. de C.V. - Md of Long Term Savings & General Director of Long Term Savings*

Gabriel Casillas Olvera *Grupo Financiero Banorte, S.A.B. de C.V. - Deputy Director General of Economic Analysis*

José Marcos Ramírez Miguel *Grupo Financiero Banorte, S.A.B. de C.V. - CEO & Proprietary Director*

Manuel Antonio Romo Villafuerte *Grupo Financiero Banorte, S.A.B. de C.V. - MD for Methods of Payment*

Rafael Victorio Arana de la Garza *Grupo Financiero Banorte, S.A.B. de C.V. - COO & CFO*

Unidentified Company Representative -

Úrsula Margarete Wilhelm Nieto *Grupo Financiero Banorte, S.A.B. de C.V. - Executive Director of IR*

CONFERENCE CALL PARTICIPANTS

Carlos G. Macedo *Goldman Sachs Group Inc., Research Division - VP*

Carlos Rivera *Citigroup Inc, Research Division - Senior Associate*

Claudia Benavente *Santander Investment Securities Inc., Research Division - Research Analyst*

Daer Labarta *Deutsche Bank AG, Research Division - Senior Analyst*

Domingos De Toledo Piza Falavina *JP Morgan Chase & Co, Research Division - Head of Latin America Financials*

Eduardo Nishio *Brasil Plural Corretora de Cambio, Titulose Valores Mobiliários S.A., Research Division - Financial Sector Analyst*

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

Jorge Kuri *Morgan Stanley, Research Division - MD*

Mark T. H. Lien *Lazard Asset Management Limited - Portfolio Manager*

Natalia Corfield de Melo Monteiro -

PRESENTATION

Operator

Good day, and welcome to the Banorte Fourth Quarter 2017 Earnings Conference Call. Today's conference is being recorded. At this time, I would like to turn the conference over to Ursula Wilhelm. Please go ahead.

Úrsula Margarete Wilhelm Nieto *Grupo Financiero Banorte, S.A.B. de C.V. - Executive Director of IR*

Thank you, Kathy. Good morning, ladies and gentlemen. Welcome to Grupo Financiero Banorte's Fourth Quarter and Full Year 2017 Earnings Call.

Today's presentation may include forward-looking statements that are subject to risks and uncertainties

that may cause actual results to differ materially. Marcos Ramírez, Chief Executive Officer, will provide an overview of the quarter.

Thank you, and I'll leave you with Marcos.

José Marcos Ramírez Miguel *Grupo Financiero Banorte, S.A.B. de C.V. - CEO & Proprietary Director*

Good morning, everybody. First of all, I want to wish you a very successful year 2018. Thanks for listening to the conference call.

Last year, at the same time, I was telling you that we were leaving interesting times. A cloud of pessimism hung over Mexico so markets and companies were expecting a pretty negative turn of events. Economists, for the most part, varies on the economy mainly due to the potential effects on the highly uncertain scenario on corporate investment decisions.

A day like today, but a year ago, the exchange rate was trading about MXN 21 per dollar. Nevertheless, even under these difficult circumstances, we did not provide a conservative guidance. Moreover, we had to revise it later in the year to a more aggressive one. And we delivered. With a clear plan, our management team has been developing the right strategies to succeed, and each link of the chain of command has been working to achieve the 2020 directives with the right sets of incentives.

For Grupo Financiero Banorte, 2017 was an exceptional year. Let me refer to the fourth quarter first on Slide 2. It was the strongest quarter in the year, both in terms of growth and metrics. Net income was MXN 6.5 billion, growing 4%, both in return on equity of 18.1%, marking the first time since 2008 that Banorte achieved this level of return on equity.

The net interest margin expanded an additional 10 basis points to 5.6%. Fees grew 8%. Trading income came in a low MXN 331 million, affected by mark-to-market valuations. Expenses grew 7%. We registered some legal and advisory fees from the relevant transaction. Personnel expenses were up on a portion of year-end pay. The loan book was up 2%, while the consumer book alone grew 3%. Repayments on the corporate book explain the difference in growth.

Credit quality in the quarter was mixed. The NPL ratio increased 20 basis points to 2%, mainly on the corporate exposure of MXN 1.4 billion that went in arrears. We are in the workup process with the customers and also with other banks.

Credit card collections improved. While we have some deterioration in payroll loans on higher employment to another, cost of risk stabilized at 2.6% in line with guidance. The insurance company posted premium growth of 8.5%. It registered a provision of MXN 205 million related to reinsurance, therefore bringing the earnings down 3% to MXN 588 million.

So 2017 was a strong year for Banorte. I want to highlight the exceptional quality of the results with high recurrence, quality of pricing and underpin on client volumes.

Net income reached MXN 23,908,000,000, growing 24%. Earnings per share reached MXN 8.62. Return on equity was 17% for the year, up 284 basis points. Business growth was good with overall loan growth at 9%, deposits at 12% and insurance premiums at 18%. Subsidiaries' results were strong also. Among the most relevant was the bank with earnings growth at 30%, annuities at 57%. The pension fund company grew 3%. The insurance company had a modest expansion in earnings of 6%, given higher losses on the ALCO group and extraordinary provision of MXN 290 million on reinsurance. The group's financial results were overall better than the guidance for the year.

Moving to Slide 3. I want to share with you the progress that we have achieved at the bank. The bank is the largest subsidiary of the financial group. The improvements are underpinned by structural changes in the balance sheet and the business that go far beyond higher interest rates. I want to focus on growth rates and profitability indicators.

The bank achieved higher-than-industry growth in consumer loans, supported by capabilities from technology and analytics. The growth advantage of Banorte versus the system was 10.3 percentage points with Banorte growing at 18.5% versus the banking system at 8.2%. In the P&L, the bank also surpassed the market. Net interest income grew 23.1% at Banorte, versus 13.7% for the system, while the total revenue grew 20% versus 15% for the market. And lastly, expenses grew 9.4% for Banorte versus 10.7% for the system.

On profitability, the bank achieved record metrics. ROE expanded 577 basis points to 19.9% versus 241 basis points to 14.9% for the system. Return on assets expanded 21 basis points versus 25 basis points for the banking system, while the efficiency ratio of Banorte declined 386 basis points versus a smaller drop of 236 basis points in the efficiency ratio of the banking system. So overall, results speak for themselves. You can see the details on the conference call presentation.

Now I want to move to our outlook for the year 2018, which seems less challenging than what it looked like this time last year. Market expects GDP to grow 2.2%, while inflation should come down to 4%. Public spending will be active all the way through election day, supporting the economy. Also, we expect salaries to grow above inflation. But interest rates will increase at least by an additional 25 basis points.

Noise and volatility will be high and will affect our financial markets, especially the exchange rate. On one hand, the usual uncertainties that stem from a general electoral process and on the other, the still open NAFTA negotiation. We assume a contentious election with 2 front runners. The official electoral process will kick off in March, and it will conclude in July 1, which is the election day. The theme of the election, as you know, is centered on corruption.

On NAFTA, the position of the United States has lacked flexibility for both Canada and Mexico in some elements of the treaty. In this context, and given the electoral calendar, we do not rule out that the final agreement may be approved, if any, until next year. We expect the private sector to remain cautious and investment subdued, translating into moderate grave demand.

Banorte is in a privileged position to withstand this environment. The financial group enjoys healthy finances, a strong capital position, a diverse business architecture and a solid franchise. Investments made in the state of their technological platform and distribution network will continue to support efficiency gains and help us expand the share of wallet with our customers.

On Page 11, we have set reasonable business growth targets. Asset quality will be the fundamental and group's financial metrics will continue to work our 2020 targets. Growth in deposits and control of the funding costs are key drivers this year. The insurance company should remain performing well, achieving double-digit growth -- earnings growth.

Therefore, the goal metrics that we commit to achieve this year are as follows: overall loan growth between 8% and 10%, with the Consumer growing at faster rate, 14%; the group's net income should be between MXN 27.5 billion and MXN 28.5 billion; the net interest margin should stand between 20 and 30 basis points.

Therefore, the goal metrics that we commit to achieve this year are as follows. The cost to income ratio will decline to a level of 39% and 40%. The tax rate will remain similar to last year between 27% and 29%. ROE should range between 18.2% and 18.6%. All of these metrics are for Banorte only -- for Grupo Financiero Banorte only. Once the Interacciones merger takes place, we will update our guidance.

And talking about Interacciones. The process stands as follows. The acquisition and merger was approved by shareholders on December 5. We kicked off the deep due diligence process immediately after. Regulatory approvals have already been requested to the Minister of Finance and also to the Mexican (inaudible) agency. We expect them well into the second quarter. Therefore, the legal merger will take place around the third quarter of this year. We will update you as we advance.

With this, I conclude my remarks and thank you, everybody. And now I open to all the questions. Thanks for listening.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) And we'll take our first question from Carlos Macedo with Goldman Sachs.

Carlos G. Macedo *Goldman Sachs Group Inc., Research Division - VP*

First question actually on your guidance. On the expense growth, you're guiding for 8% to 9% after doing something similar this year. And yet inflation, as you said, you expect to be much lower. Is there any room for some improvement there with expenses coming in low. Of course, you're going to revise this with Interacciones. But just trying to understand where the growth is coming from that would lead you to outpace inflation by that much. Second question, you talked about your guidance has 20 to 30 basis

points improvement in margin in 2018. And you said that you might -- you expect to see rates go up another 25 basis points. Where do you see rates by the end of the year? Do you think they're going to start going down? I think consensus now has them going down starting in the second half. And if they do, by how much? And how does that affect your margins and your guidance for margins going forward?

José Marcos Ramírez Miguel *Grupo Financiero Banorte, S.A.B. de C.V. - CEO & Proprietary Director*

Thank you, Carlos. Yes, we have some room, you are right, in the expense. We are cautious, but let's see how the market develops. And you are right. I will ask Rafa to go deeper on this. And also remember that, yes, we will have at least an increase 25 basis points and maybe 50 basis points but it's a lack, so we need to wait until that happens and only 6 months after we receive the upside of all these. Rafa, can you give us more color on this?

Rafael Victorio Arana de la Garza *Grupo Financiero Banorte, S.A.B. de C.V. - COO & CFO*

Yes, Carlos. Good morning. About the inflation, you're completely right. It seems that inflation is coming down already on the first month of January. But the fact is that when you do all the budgets and you start looking at -- the prices doesn't fall immediately on the expenses that we run at the banks. And also, you have to consider that we also included on the budget additional costs related to the transaction that is ongoing that we put under -- above or close to MXN 700 million on that buffer. So if you strip those numbers out, and you can be a run rate of the cost of the bank around 6.8% to 7%. This year -- last year, we committed to 8.8% of -- to achieve on the cost line. And we have been always guiding the inflation plus 150 basis points. The problem about inflation as it comes down as fast as it's coming down is that not all the prices immediately that affect the banks goes at the same pace, lots of the restructuring costs that I'm telling you. So if you strip those issues down, you could be run rate of cost around 6.5%. That will be in line with the expected drop in inflation around 4% to 4.5% so it will be around the 150 basis points that we have been running the bank for. So that's the reason why.

José Marcos Ramírez Miguel *Grupo Financiero Banorte, S.A.B. de C.V. - CEO & Proprietary Director*

And also, Carlos, yes, the rates will have a -- is going to be a roller coaster in the year. They will go up and then maybe they will go down at the end of the year. So -- and how much, I don't know. I will ask Gabriel here to explain a little bit that. But it's going to be both sides, the up and the down.

Gabriel Casillas Olvera *Grupo Financiero Banorte, S.A.B. de C.V. - Deputy Director General of Economic Analysis*

Thanks, Marcos. This is Gabriel Casillas. To the economy, the 2 things here just to complement what Marcos and Rafa has already -- have already said. On the one hand, on inflation, the other thing is inflation, yes, will trend downwards, but it's not going to be just like that's going downwards all the time. Actually, we expect the inflation to start to reflect the driving season in gasoline prices for the first time ever. Remember, gasoline prices were managed and now they are liberalized. So in this context, actually, our official forecast for inflation is 4.3% for year-end. But average inflation for the year is 5.1%. So I think that's one important thing to highlight. And secondly, what Marcos was saying on interest rates, yes, even though we have been conservative in what -- in our assumptions for the guidance, we're assuming only 25 basis points of an increase. Actually, on the economics department, what we are expecting is

actually 3 hikes: the 75 basis points of hikes between now and July; and then a space for cuts -- 2 cuts of 25 basis points in the second half of the year. So as Marcos is saying, quite a roller coaster, a quite dynamic central bank. And at the end, we expect the interest rate -- multiple interest rate to be at 7.50%. So that's our call from the economic side.

Rafael Victorio Arana de la Garza *Grupo Financiero Banorte, S.A.B. de C.V. - COO & CFO*

And Carlos, just another thing that you have -- you can look on the numbers that we presented, we commit also to the market at the end of the fourth quarter that the cost of funds will go down drastically in the fourth quarter. If you can look at the numbers in the third quarter, we were running the cost of funds around 48 to reference rate. And we dropped down the number to 35% -- 35 basis points at the end of the year. So I think also an additional expansion in the margin will come from the good management of the cost of funds that we achieved at the end of the year will continue to happen through the year. Even though the hike that Gabriel mentioned that can possibly happen, 3 hikes, we only budget only 25 basis points. And remember that once you get the hike, you get penalized on the funding side for 6 months, and then you get the benefit after 6 months right on the asset groups. On the corporate commercial and SME, you get the benefit also in the government loans immediately. So it's a balance that we have been managed pretty well last year. We really end the year at a very good cost of funds that will support the expansion on the margin that we set up on the guidance I think and that number sits really on the low end.

Carlos G. Macedo *Goldman Sachs Group Inc., Research Division - VP*

So -- just to be clear, you expect margins to go up 25 -- sorry, the benchmarks, they go up 25 basis points and stay flat through the end of the year at that level. That's what's in your guidance and not...

Rafael Victorio Arana de la Garza *Grupo Financiero Banorte, S.A.B. de C.V. - COO & CFO*

Exactly right.

José Marcos Ramírez Miguel *Grupo Financiero Banorte, S.A.B. de C.V. - CEO & Proprietary Director*

That's it.

Rafael Victorio Arana de la Garza *Grupo Financiero Banorte, S.A.B. de C.V. - COO & CFO*

Exactly right, Carlos.

Operator

We'll now take our next question from Jason Mollin with Scotiabank.

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

I wanted to understand how management is thinking about profitability, return on -- in particular, return on equity, in the context of this very high or at least since the beginning of the -- I would say, 2001 inflation and interest rate environment. I mean, if we looked just year-over-year, the ROE is now at 18.1% up from the 15.1%. But TA has gone up dramatically as well or the overnight interest rates. And

the spread has increased slightly, but you're earning about 10.5% more than the TA, the 28 day TA, and it was about 10% a year ago. How should investors or how does management think about the cost of money and the kind of returns that you can generate? How important -- clearly, you're showing operating leverage and that it's not all rates showing this improvement. But how should we think about that?

José Marcos Ramírez Miguel *Grupo Financiero Banorte, S.A.B. de C.V. - CEO & Proprietary Director*

Thank you, Jason. As I started, we see less volatility than last year. We see volatility, but maybe less than and we manage already with that kind of volatility. So I will ask Rafa to go into the numbers, but it's not so difficult. We know the inflation is going to be down, which is good. The rate will be up, that's good. And we will manage whatever happens next. Go ahead, Rafa.

Rafael Victorio Arana de la Garza *Grupo Financiero Banorte, S.A.B. de C.V. - COO & CFO*

Yes, Jason, thank you for the question. I think the key element of what you mentioned in addition of what's going on the run rates that you get on the effect on the hikes on the reduction inflation is, to be honest, how well we have been able to manage the cost of funds. Our cost of funds, as I told Carlos, is sitting now at 38 -- 35 basis points -- 35 percentage of reference rate. And the reason that we had a hike on the past year on the cost of funds is that we fund in the extraordinary growth on the Consumer with time deposits. But we have been able already to balance out again with demand deposits. So one key element to really sustain and be able to manage the volatility that goes -- and is aligned to the books that we have is really to manage the cost of funds. As you saw on the guidance, deposits have grown around 12% and loans will be around 8% to 9%. And the mix will again be beneficial to the demand deposits. So the key element, when you see the type of environment that we see now in Mexico, there's just going to be some volatility and also some concerns about potential risk on the election and things like that, is to really concentrate on the cost of funds, manage your books pretty solid. Last year, we were able to really outpace the market. So now we are sitting in very profitable books that we can fund them with a very much efficient cost of funds than past years. So that will allow us really to continue to keep the expansion on the margin and the profitability of the books in the same -- in a better trend that we have from last year. So I think basically -- yes...

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

That makes sense. Sorry, continue. I was just going to ask. I mean, I -- I mean, my question is more to -- we used to talk about this in the past about the spread of ROE over the policy rate or over the TA rate. And my question in one way is, is 10 -- should we think of it this way? Is it a 10%? Is it 10 -- 1,000 basis points or 10 percentage points higher? Is that kind of a way to think about the profitability of the bank? Because the cost of money has gone up dramatically. As you're saying, on the cost of funding directly, you're trying to improve that. And I think there is upside, but I also think there's competition on that front. But how do you think about that spread of profitability versus the cost of money? Whether you want to use a TA or the long bond, it's now up, I think, 7.7% in Mexico, is another way to think about it, the inputs to your cost of equity. Because on my numbers, the cost of equity really hurts the valuations that we're looking at for all Mexican companies in particular banks.

Rafael Victorio Arana de la Garza *Grupo Financiero Banorte, S.A.B. de C.V. - COO & CFO*

Yes, the numbers that you're looking at, the 10%, if you look at historically, that number has been up more than double in the past. So I think what you will be looking at this year is around 16%. That will be the number that you should be looking at instead of the 10%.

Úrsula Margarete Wilhelm Nieto *Grupo Financiero Banorte, S.A.B. de C.V. - Executive Director of IR*

And Jason, this is Ursula. The other thing to remember is that I'd say from 2013 to today, another fundamental change has taken place, which is the business architecture of the group. And while in the past, all of the burden on the ROE was just really left to the bank, today, the architecture of the business, you have a portion of the profits that are coming from the nonbank subsidiaries that are less dependent upon interest rates. And this is just something that is still growing. And it's going to support also the ROE. So that is why the margin between the ROE and the policy rate for Banorte has expanded versus the past.

José Marcos Ramírez Miguel *Grupo Financiero Banorte, S.A.B. de C.V. - CEO & Proprietary Director*

Yes, you can see that very fast. You can look at returns on equity on the annuities company, 50%; on the insurance company, 40%; brokerage house, 30%. The bank is already at above 20%. So I think what Ursula mentioned, the mix and the way we are managing the business allow us to be -- I mean, we ask -- we are very disciplined in how we ask the business to provide the return on equity of the capital that we lend to them, and the return has to be well above the cost of capital and well aligned to the 2020 return on equity that we are seeking. We know competition is out there, but it's not only price. I mean, all the services that we provide and the way that we do the services and the interaction with the client has allowed us to also have a premium sometimes on the relationship with them.

Operator

We'll now take our next question from Tito Labarta with Deutsche Bank.

Daer Labarta *Deutsche Bank AG, Research Division - Senior Analyst*

A couple of questions also. First, following up a little bit on expenses, and I guess, efficiency. Just to understand, the increase in the professional fees, which we saw, go up a lot. Is that mostly related to the acquisition? Just want to confirm that. And then to reach the efficiency targets, which you expect to improve more than 200 basis points potentially, what kind of fee income growth do you expect? I mean, we saw good growth in fees last year. Can that continue? Can you maybe give some guidance for fees? And then my second question is on asset quality. We saw a little deterioration. Given just the uncertainty and volatility, any other risks that you could see in terms of asset quality for this year?

José Marcos Ramírez Miguel *Grupo Financiero Banorte, S.A.B. de C.V. - CEO & Proprietary Director*

Thank you, Tito. The first one, yes, is professional fees. We are aiming to MXN 200 million around that level. And the second one, Rafa is going to -- is 14%?

Rafael Victorio Arana de la Garza *Grupo Financiero Banorte, S.A.B. de C.V. - COO & CFO*

Yes, the fees will continue to be, Tito, around the 14% to 16% that we have seen. The fees related to the banking business continue to grow and outpace the other fees. Also the corporate entities and the commercial bankers are a lot related to services. So you can see that the rate of growth of the program the Commercial has been also exceptional. So we don't see any limitations to keep on growing the fees at a very, very steady level numbers. On the asset quality, we know that there's concern about the quality of the consumer, especially on the credit card business. But it's very important to remember that even though we had some issues around July, that has to do with some origination processes that were not as efficient as they needed to be and that we've closed them and now the roll rates are improving. After the earthquake, we almost missed a completely -- a complete cycle on the collection for the credit card. That's going to stay for us until May next year. But you already saw at the end of the year that there are -- that NPLs went down from 6.3% to 6.1% for the end of the quarter. We think this number will continue to go down. No -- and it will be steady around 5.8%. I think we are now comfortable with the way we are originating the credit card business. We are mainly devoted to pre-authorized credits. And I'm sure that Manuel can also provide you, the head of the product, with some additional guidance on that.

Manuel Antonio Romo Villafuerte *Grupo Financiero Banorte, S.A.B. de C.V. - MD for Methods of Payment*

Yes. Hi, Tito, this is Manuel. Thank you, Rafa. On credit cards, I think that Rafa covered it all. I think that you can see even in the numbers that we are reducing a little bit the speed of growth. We started with preventive actions in the first quarter of this year as we have mentioned in these calls. And we are really -- what we are doing is preventing the cross-held privileging campaign for existing customers of the bank. We are really, really getting out of any out-of-branch walk-ins, new segments and all of that campaign and all that. So if you see the year-on-year expectation of growth of the portfolio of credit cards, for example, in June, July, it was around 20%, 23%. Right now, it's closer to 17%, 18% and that is really a reduction of fees on specific segments. Regarding, Tito, payroll, 2018 specifically is a year that is -- we're already preparing for it because there is -- it is the highest number of state and municipalities elections: federal, states and municipalities. And we have a very good penetration of government payrolls. So what we are doing is taking preventive action with all the analytic tools. And it's the risk that we have right now and being very cautious regarding those changes in administration.

Gabriel Casillas Olvera *Grupo Financiero Banorte, S.A.B. de C.V. - Deputy Director General of Economic Analysis*

Just one extra thing I want to complement. This is Gabriel Casillas, Tito. Just from a macro side, obviously, on election year despite all the uncertainty that there will be that Marcos highlighted, one important thing is that usually actually growth rates are higher. And this year, I don't think we'll be an exception. Actually as Marcos said at the beginning, the market is expecting growth rates of around 2%, 2.1%. On the economics team, we're expecting 2.5%. This is not what we use in our guidance. We use the Marcos (inaudible) number. Nevertheless, there are 3 important things to highlight on growth this year. Number 1 is that the uncertainty will be absorbed by exchange rates, not by employment or by growth. Number 2, we are expecting oil production to stop contributing on the negative side on GDP. As you know, since 2006, it has contributed on the negative side. And number 3, electoral year. As Manuel

was saying, it will be the largest election we have ever had in Mexico. Actually, it will be 3,406 positions that will be elected, so imagine that. And usually, electoral expense is very high without jeopardizing public finance. So I think that that's important to highlight not for our bank only but for all the banking industry in Mexico.

Operator

(Operator Instructions) We'll now take our next question from Carlos Rivera with Citi.

Carlos Rivera Citigroup Inc, Research Division - Senior Associate

My first question is regarding the outlook for loan growth for companies. What do you expect in terms of seasonality? I mean, this part of the portfolio is the one that we've seen decelerating fastest throughout the year. Would it be reasonable to assume that it will continue to do so until we have a resolution on the elections? Or what are your thoughts particularly first half versus second half of the commercial loan book specifically but also probably on the entire portfolio? And my second question is related to asset quality. On the corporate side, you mentioned a specific case, MXN 1.4 billion. So I'm not sure if you could share a little bit more color on this exposure. How much is provision? Will it still require additional provisions in 2018? I assume that's part of the guidance. And just to confirm, that is very focused on 1 case and it is not expandable to the entire industry which this company is in.

José Marcos Ramírez Miguel Grupo Financiero Banorte, S.A.B. de C.V. - CEO & Proprietary Director

Thank you, Carlos. Yes, this year, we will have to use the first semester. And then the second semester, it's going to be like interesting times. But what we expect in terms of seasonality, Ursula can give us some color and also about the provision for the year 2018. Go ahead, Ursula.

Úrsula Margarete Wilhelm Nieto Grupo Financiero Banorte, S.A.B. de C.V. - Executive Director of IR

Yes, thank you. Hi, Carlos. Exactly as Marcos said, it's going to be on the nonconsumer books, there is going to be a little bit more volatility in the growth. Probably the first half of the year as lower growth, as our expectation is that companies -- I mean, you have seen investments. Private investment has been coming down, and we expect companies to continue holding on investment decisions until the electoral process is cleared out. So we expect that demand because of that. And then probably in the second half of the year, we should see some more larger growth rates in those books. The other thing that we have seen is because of interest rates, companies have been using a lot more liquidity than debt in their operations and in their -- in the financing of projects that they have. And part of that is what -- why you have seen that we've had a higher...

Operator

Please standby.

(technical difficulty)

José Marcos Ramírez Miguel Grupo Financiero Banorte, S.A.B. de C.V. - CEO & Proprietary Director

Okay. Ursula, go ahead. Sorry about that.

Úrsula Margarete Wilhelm Nieto *Grupo Financiero Banorte, S.A.B. de C.V. - Executive Director of IR*

I don't know if -- I was saying -- if you were able to get my answer or not so I will make it a brief repetition. Growth in nonconsumer, we expect a slow first half and more vigorous growth in the second half because of election, because of interest rates and because the investment has been slowing down. And on the corporate exposure that we transferred to NPLs, a portion of that is already provisioned. We will make an additional provision in the first quarter, but it's already included in the cost of risk guidance that we provided. So it should not be above, let's say, in the overall cost of risk for the year. That's all.

Carlos Rivera *Citigroup Inc, Research Division - Senior Associate*

Okay. And just if I may, a quick follow-up on the Nonconsumer portion. How long do you think it could decelerate in the first half just to set expectations right and to not have significant concerns that things are going out of plan?

Unidentified Company Representative -

If I may jump on that. The Consumer, as Gabriel mentioned, labor continue to be quite strong. So we see a healthy consumer in Mexico. We don't see any issues on that. The fact that we are providing a less aggressive guidance than last year, that we are staying consumer around 14%. But you still see pretty good growth on the car loans around 19%. Mortgages will be running around 11% to 12%, credit cards around 14% and payables in the same number. So still, we see a very pretty healthy consumer. We will not be as aggressive as last year because I think we're already pretty comfortable with the size of the books that we are getting, and we can be very selective on the type of clients that we can bring into the book.

Operator

We'll now take our next question from Jorge Kuri with Morgan Stanley.

Jorge Kuri *Morgan Stanley, Research Division - MD*

One question, if I may, on what's left to do on the IBM project. What are the milestones or initiatives that are going to be implemented this year? And to what extent the results and guidance that you provided for 2018 reap the benefit of things that were implemented over the last year or 2? And just the 2020, what exactly does that mean in terms of ROE? Are you expecting the fourth quarter ROE of 2020 to be 20%? Are you expecting the full year to be 20%? Because obviously, the run rate that you need in order to get that from here would imply that there's still a lot of upsides from IBM. So just wanted to get a little bit more color on that.

José Marcos Ramírez Miguel *Grupo Financiero Banorte, S.A.B. de C.V. - CEO & Proprietary Director*

Thank you, Jorge. I will start with the second one. 20% is a good objective for us for 2020 so we will keep that. Moving to the IBM project, as you know, now we have the foundation. We have all the data. We have all the clients in the right place. And we will work in 2 ways. One is with the customers, when they arrive to the branches, they will notice that something happened because everything will be easy to handle. And they will notice that. We have a program for that. And in the other hand also, we will work

with the analytics and all these, and we'll know how to sell to all the clients. So you will see that we will increase the share of wallet of the clients. You will see they will be happier. And the cross-selling ratio of the (inaudible) one will start to increase. So that's our goal and we are aiming to that, and everything is under control. And we are very happy with how things are managed. I don't know what else to say because the competitors are there. But we are happy with that and you will see the results going forward in 2020. And again, talking about the ROE for 2020, 20% is a good objective, and we will keep on track to do it. That's it.

Operator

And I'll take our next question from Domingos Falavina with JPMorgan.

Domingos De Toledo Piza Falavina JP Morgan Chase & Co, Research Division - Head of Latin America Financials

My question is more on the deal, if I may. Like it seems on your first remarks that things are on track, and you're hopeful that this will be concluded in the third Q. And I've noticed like despite sort of it widened a little bit in the last couple of days, I've seen in other regions, banks or the companies that acquires, once approved taking the initiatives to add already the shares and basically buy the company for cheaper. So my question is why don't you start using your treasury and others to start acquiring direction in shares, and once you get the approval, you can finish the process. But at least you know you cannot betray the spread.

José Marcos Ramírez Miguel Grupo Financiero Banorte, S.A.B. de C.V. - CEO & Proprietary Director

We don't want to do that. We are a bank and we don't want to mess with all that, and we will leave the market to respond to that market and be efficient. And we don't want to be involved on that because everybody will take a point of view. So the market will be effective, I assure you that because nobody is full. And we will be out of these trading positions that we can take. We don't want to do it.

Domingos De Toledo Piza Falavina JP Morgan Chase & Co, Research Division - Head of Latin America Financials

Okay, okay. And the second one is just like your growth on the consumer side has been notably higher than the industry average. My question is on your origination, what percentage of those loans are going to existing clients versus new clients?

José Marcos Ramírez Miguel Grupo Financiero Banorte, S.A.B. de C.V. - CEO & Proprietary Director

That's right. We're growing faster than the peers, talking about Consumer. Remember that our natural quarter should be like 15% or 16% and we are below that. So we need to increase with our customers and we are working on that. Maybe Manuel Romo can give us how much is the new ones and...

Manuel Antonio Romo Villafuerte Grupo Financiero Banorte, S.A.B. de C.V. - MD for Methods of Payment

Thank you. We estimate around 60% to 70% of all the consumer new origination coming from existing customers. As we open new channels of origination, ATMs and digital channels and all of that, we expect

that number to even grow a little bit more on the Consumer book.

Operator

(Operator Instructions) And we'll take our next question from Claudia Benavente with Santander.

Claudia Benavente Santander Investment Securities Inc., Research Division - Research Analyst

I was wondering about on the insurance revenue. We've -- I believe there will be like at least comparison base considering 2017 was affected by the earthquake. Historically, you had shown us 20% growth on the revenue so I was wondering if we could expect an above 20% growth in 2018. And then I have a second question.

José Marcos Ramírez Miguel Grupo Financiero Banorte, S.A.B. de C.V. - CEO & Proprietary Director

Thank you, Claudia. I will ask Fernando Solís, who is here with us, but on another side of the room. So he wants to talk.

Fernando Solís Soberón Grupo Financiero Banorte, S.A.B. de C.V. - Md of Long Term Savings & General Director of Long Term Savings

Well, yes. First of all, yes, we were hit by the insurance by the quake. But mainly, as was pointed out in the report, it was that we have to write down an account that was payable that we will not be able to collect from an insurer. That's what mainly drives down the growth in the earnings this year. If you take out that effect plus the extraordinary realization of our reserve last year due to the new solvency regulation, which was more or less MXN 200 million, the company would have been growing at a rate of more or less 24% this year. So what I want to highlight is that if you do not take into account these nonrecurring events, actually the insurance company was performing quite well. Having said that, our guidance for next year for the insurance company -- this year, sorry, for this year, not next year, for this year, will be somewhere around 16% to 20%, having said that. Of course, hopefully, we will be able to grow at a higher pace. But that's more or less our view.

José Marcos Ramírez Miguel Grupo Financiero Banorte, S.A.B. de C.V. - CEO & Proprietary Director

So on that, actually it's not structural. And we will return to a very good pace in the future. That's the rest.

Claudia Benavente Santander Investment Securities Inc., Research Division - Research Analyst

Okay. And my second question is about SMEs. You have been showing an above-industry growth. So I was wondering what we can expect for that line. And if you see any competition in the sector because growth for the industry now has been pretty weak, and if you have any competitive advantage that you see in that segment.

José Marcos Ramírez Miguel Grupo Financiero Banorte, S.A.B. de C.V. - CEO & Proprietary Director

I will ask Carlos Martínez to talk about SMEs and thank you.

Carlos Eduardo Martínez González Grupo Financiero Banorte, S.A.B. de C.V. - MD of Retail Banking &

General Director Retail Banking

Thank you. We work this year -- we will work in growing in a more stable pace. We will expect to grow in a very high level this year. We will assess credit quality, first thing. Another thing is time-to-market. We've been addressing time-to-market in order to have a better credit recognition, to have the better credits. And we expect to have growth this year about -- between 10% and 12%, only with good quality in order to grow later in the year and maybe next year, 16%, 20% but this year, we expect to grow in a moderate basis.

Claudia Benavente Santander Investment Securities Inc., Research Division - Research Analyst

Sorry, do you expect them to grow between 10% to 12% this year?

Carlos Eduardo Martínez González Grupo Financiero Banorte, S.A.B. de C.V. - MD of Retail Banking & General Director Retail Banking

Yes, that's correct.

Claudia Benavente Santander Investment Securities Inc., Research Division - Research Analyst

Okay, sorry. And I have 1 final question. I remember you have said in the past that the fixed interest rate asset position has yet repriced to the high interest rate environment. However, if we take a look to the industry's numbers, we can see that the interest rate -- the charge interest rate for almost consumer products, of course, with the exception of credit cards, have not incorporated high rate. For me, it could be maybe due to the competition. So even if this part of the portfolio has not repriced to this higher interest rate, probably we're not going to see any benefit from that position.

Carlos Eduardo Martínez González Grupo Financiero Banorte, S.A.B. de C.V. - MD of Retail Banking & General Director Retail Banking

Yes. Regarding SMEs, we are pricing our portfolio. Our whole portfolio can be repriced in less than a year so we expect to have a good reprice about 150 basis points during the year, more or less. I think you can expect a better ROE in this portfolio.

Rafael Victorio Arana de la Garza Grupo Financiero Banorte, S.A.B. de C.V. - COO & CFO

So, if you look at the risk-adjusted margin for SMEs, the risk-adjusted margin for SMEs really grew pretty nice last year as what Carlos just mentioned. We are contemplating a pretty good quality of assets. The NPLs of the SMEs are running at around 5.1% close to record levels for a market like that. And this year, when you see 12% maybe it's not so much. But yes, we're really concentrating a lot in the cross-sell, the funding side, the fee side and providing all the elements to the already existing clients that we have. We are very happy with the SME performance. It's getting record levels on the NPLs. And also the penetration in our client base have allowed us to really increase the risk-adjusted margin well above the other loan books that we have seen in the market.

Claudia Benavente Santander Investment Securities Inc., Research Division - Research Analyst

And I totally agree. Sorry, I meant about the consumer products that -- the position that it's linked to a fixed interest rate that hasn't yet repriced to the overnight hikes. I was saying that competition has been

stronger, excluding credit cards, and the interest rates have not incorporated these overnight increases. So I was wondering that despite of the fact that it could reprice to a high interest rate it's not going to happen due to competition because I remembered that you said in the past that there could be this positive position that could contribute to the growth of the net interest margin.

Rafael Victorio Arana de la Garza *Grupo Financiero Banorte, S.A.B. de C.V. - COO & CFO*

Yes. And let me just give you a very good example about that. If you look at the car loans market, our NPLs on the car loans are around 1%. We outpaced the market by a lot. I mean, we are now really closing the gap with the largest provider that is BBVA. But the very important thing is that we are looking at NPLs on our side around 1% and competition is around 2.4% to 3%. So we are really able to keep the right clients, the good clients, because we have not been able, because as you mentioned this competition, to really reprice the full interest rate hike. But what we have been able to do is to keep the expected loss very, very low record levels.

Operator

(Operator Instructions) And we'll now take the next question from Mark Lien with Lazard Asset Management.

Mark T. H. Lien *Lazard Asset Management Limited - Portfolio Manager*

Could you provide us -- give us the progress on your cross-selling, maybe update us on where the cross-selling ratio was at year-end? And perhaps just give us your commentary on how this would evolve against the backdrop of a decelerating consumer loan book, albeit from very high growth rates currently?

José Marcos Ramírez Miguel *Grupo Financiero Banorte, S.A.B. de C.V. - CEO & Proprietary Director*

As you remember, Martin (sic) [Mark Lien], we are aiming to 2.2% in the year 2020. At the beginning, it was very difficult because we didn't have the tools so it was our target. And now that we have the tools, it will not -- you will see how it increase each year in a dramatical way, let's say that. The numbers are here with Rafa and let me give the numbers.

Rafael Victorio Arana de la Garza *Grupo Financiero Banorte, S.A.B. de C.V. - COO & CFO*

Yes, the number that we reached at the end of the year is 1.9%. As you know, we are coming down from 1.7%. It was really 1.6%, 1.7%. We're reaching 1.9%. It seems like a very slow pace, but the results of the returns of achieving those and reaching the 2.2% that Marcos mentioned on the 2020, we are right on track on achieving those. And it has to do with what Manuel was saying that now that you have the mobile with all the full capabilities of selling and the ATM, the web and also the related channels besides the branch, you will see that based upon all the analytics and the best option and best opportunity that we present to the client, if you now go to any of our branches, not only on the web or the mobile, that is very easy to give you the right offer. But if you go to the branches, immediately when you start interacting with our executives, you will get the right offers, the best offers for you based upon the quality of the client and the possibilities. So now the full distribution capabilities are loaded with the cross-sell opportunities for the client. So that has to continue to increase at a different rate than has

been in the past. There was a lot of building blocks in the past. Now they are fully functional. And we will continue to make more -- those more efficient through the year.

Operator

(Operator Instructions) And we'll take our next question from Natalia Corfield with JPMorgan.

Natalia Corfield de Melo Monteiro -

Just to follow-up on Interacciones. If you could remind us how much impact are you expecting in your capitalization coming from the merger with Interacciones?

José Marcos Ramírez Miguel *Grupo Financiero Banorte, S.A.B. de C.V. - CEO & Proprietary Director*

Can you repeat, how much what? What was your question? Sorry.

Natalia Corfield de Melo Monteiro -

The impact in your capitalization from the acquisition of Interacciones.

José Marcos Ramírez Miguel *Grupo Financiero Banorte, S.A.B. de C.V. - CEO & Proprietary Director*

The capitalization. Thank you. Rafa?

Rafael Victorio Arana de la Garza *Grupo Financiero Banorte, S.A.B. de C.V. - COO & CFO*

Yes. As we mentioned on the roadshow, if you apply today the integration of Interacciones, the tier -- Core Tier 1 that is sitting around 11.9% will go down to 10.8%. But as you know, since this is expected to happen until June, July, the numbers when the Interacciones integration happens, the Core Tier 1 will be around 11.7%, 11.8%. So we are not worried at all with the capital Core Tier 1 that we have. And the evolution of the bank allow us to really build up capital at a very fast pace.

Natalia Corfield de Melo Monteiro -

All right. But I can assume around like 100 basis points?

Rafael Victorio Arana de la Garza *Grupo Financiero Banorte, S.A.B. de C.V. - COO & CFO*

Yes. I think yes, but that will be reduced through the year. By the end of the year, you will see again, the 12% Core Tier 1 once the full year of the integration happens.

Operator

And we'll take our next question from Eduardo Nishio with Brasil Plural.

Eduardo Nishio *Brasil Plural Corretora de Cambio, Titulose Valores Mobiliários S.A., Research Division - Financial Sector Analyst*

My first question is regarding Interacciones. And any plans to reduce the dividend so you can make this acquisition with a more -- a stronger capital? And then I will make my second question later.

José Marcos Ramírez Miguel *Grupo Financiero Banorte, S.A.B. de C.V. - CEO & Proprietary Director*

No, Eduardo. There is no plan to reduce. We will keep the stronger capital. There is no plan for that.

Rafael Victorio Arana de la Garza *Grupo Financiero Banorte, S.A.B. de C.V. - COO & CFO*

And as Marcos said, it's very important to notice also that the dividend for the 2017 has already been provided at the group level. So the policy of 40% continues to be. And any additional capital that we can return to the market, we will do on a tactical basis. But no, there's no effect at all on the dividend policy that we have. We -- the capital generation at the bank allow us to be -- to feel very comfortable with the operation with Interacciones and keep the dividend policy fixed. And if there's an additional capital to return to the market, we will advise so on a tactical basis.

Eduardo Nishio *Brasil Plural Corretora de Cambio, Titulose Valores Mobiliários S.A., Research Division - Financial Sector Analyst*

My second question regards to the consumer loan. And as a follow-up on that, you've been growing very fast. And as much as you can, I know there is competitors in the line. But as much as you can, can you give us a little bit more color on what you're doing in analytics and whatnot, if there is any digital initiatives here, technology and big data and BI?

José Marcos Ramírez Miguel *Grupo Financiero Banorte, S.A.B. de C.V. - CEO & Proprietary Director*

Yes, Manuel will get that. Yes, Manuel Romo can help with that.

Manuel Antonio Romo Villafuerte *Grupo Financiero Banorte, S.A.B. de C.V. - MD for Methods of Payment*

Yes, Eduardo. The strategy that we have been following is basically using all the expanded capabilities of channels, coupled with analytics to better and more efficiently cross-sell to our existing customers, mostly from payroll and debit accounts. With regards to the existing portfolio growth, that's for new customers. With regards to existing portfolio growth, what we're doing is basically relying on very traditional point-of-sale usage and very traditional, very well-aimed personal and payroll loans for this kind of customers. We will continue with the strategy to be very vigilant on the growth, risk-adjusted margins of the portfolio for 2018. And we are going to privilege good quality growth. So in 2018, we are going to be very, I would say, conservative regarding cash. For example, cash incentives or going to new segments or being very aggressive on portfolio growth if we are not very certain about risk-adjusted margins impact on our portfolio.

Eduardo Nishio *Brasil Plural Corretora de Cambio, Titulose Valores Mobiliários S.A., Research Division - Financial Sector Analyst*

All right. And the vintage are coming with good delinquency rates. How do you see the new vintages coming?

Manuel Antonio Romo Villafuerte *Grupo Financiero Banorte, S.A.B. de C.V. - MD for Methods of Payment*

Again, I think that if you separate the vintages for -- from existing customers, you're going to see very good behavior, really very good behavior, risk-adjusted margin-wise, because also the interest rate that

we're offering for good quality is -- continues to be very attractive and we're doing a lot of refaced pricing. If you separate the vintages from the existing customers to the new ones, new segments that are not existing customers, we can see some concern in certain segments of the population, and that's why we are cutting back on those segments of origination.

Operator

(Operator Instructions) It appears we're showing no further questions at this time. I'd like to turn the conference back to your hosts for any additional or closing remarks.

José Marcos Ramírez Miguel *Grupo Financiero Banorte, S.A.B. de C.V. - CEO & Proprietary Director*

Thank you very much and see you next quarter. Thank you.

Operator

That concludes today's conference. Thank you for your participation. You may now disconnect.

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