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SUPV - Q2 2019 Grupo Supervielle SA Earnings Call

EVENT DATE/TIME: AUGUST 13, 2019 / 1:00PM GMT

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PRESENTATION

Operator

Good morning, and welcome to the Grupo Supervielle Second Quarter 2019 Earnings Call. A slide presentation will accompany today's webcast, which is available in the Investors section of Grupo Supervielle's Investor Relations website, www.gruposupervielle.com. (Operator Instructions) As a reminder, today's conference call is being recorded.

At this time, I would like to turn the call over to Ana Bartesaghi, Treasurer and IRO. Please go ahead.

Ana Bartesaghi - *Grupo Supervielle S.A. - IR Officer & Treasurer*

Thank you. Good morning, everyone, and thank you for joining us today. Speaking during today's call will be Patricio Supervielle, our Chairman of the Board of Directors, who will discuss the overall macro environment; and Jorge Ramirez, our Chief Executive Officer and Vice Chairman of the Board, who will review our results for the quarter. Also joining us is Alejandra Naughton, Chief Financial Officer; and Alejandro Stengel, Chief Operating Officer of the bank. All will be available for the Q&A session.

Before we proceed, I would like to make the following safe harbor statement. Today's call will contain forward-looking statements, and I refer you to the forward-looking statement section of our earnings release and recent filings with the SEC. We assume no obligation to update or revise any forward-looking statements to reflect new or changed events or circumstances.

I'd now like to turn the call over to our Chairman, Patricio Supervielle.

Julio Patricio Supervielle - *Grupo Supervielle S.A. - Chairman of the Board*

Thank you, Ana. Good morning, everyone. Thank you for joining us today. If you're following the presentation, please turn to Slide 3. I will begin my presentation this morning touching on the key highlights of the second quarter results. We have planned to spend time updating you on our digital initiatives on this call.

But given recent political events, we will focus on our performance and leave more time for Q&A. The resiliency and flexibility of our business model was evidenced in results for the quarter. Overall credit demand remains weak as we are conducting business in an ongoing challenging macro environment. Against this backdrop, pretax income more than doubled. Additionally, we delivered good revenue generation and increased our NPL coverage to almost 108%.

Becoming a leaner and more efficient organization is a key strategic focus for us -- of ours. And although we are making progress, some of this has been offset by weaker performance in Consumer Finance and wage inflation. Jorge will discuss this in greater detail in a moment.

We delivered solid results in the quarter, but we remain cautious as to the remainder of the year as interest rates remain consistently high and weak economic activity has been impacting several key industry sectors. As a result, we continue to closely monitor our loan portfolio. While we are facing challenging times in the near term, we do have a long track record of operating in uncertain environments. It is important for us to continue to make the necessary investments to operate in a changing customer banking world and to do so efficiently.

Moving on to the macro on Slide 4. Macroeconomic imbalances have been trending towards normalization over the past quarters. While historically, Argentina has been characterized by chronic government overspending and consequent deficits, we are currently observing a drop in aggregate spending equivalent to over 10 percentage points of GDP. Moreover, economic activity hit bottom in November. And since then, we observed a shy, improving trend. The stabilization in the -- in the FX led to 3 consecutive months of lower inflation rate. Consequently, the monetary policy or Leliq rate declined for 4 consecutive months. Following Sunday's primary election results, it is still too soon to establish which is the new baseline.

Now looking at the Argentine financial sector on Slide 5. The system remains highly liquid, with total industry deposits up nearly 7% quarter-on-quarter. Measured in currency of origin, industry deposits were up nearly 10% in pesos and 4% in U.S. dollars. As of May, the most recent Central Bank publicly available data, system liquidity in pesos as well as in dollars stood at almost [60%] of total deposits. Moreover, the inventory of total industry U.S. dollar deposits as of last week was at the highest level observed over the past 16 years.

Reflecting weak macro and high interest rates, loans were flat sequentially in nominal terms. This was the case of Argentinian-denominated loans and dollar-denominated loans in currency of origin. We experienced a relatively similar trend in loans this quarter and a slightly lower growth in deposits as we continue to focus on liquidity management.

I will now turn to Jorge, who will review our financial performance and outlook. Please Jorge, go ahead.

Jorge Oscar Ramírez - *Grupo Supervielle S.A. - First Vice-Chairman & CEO*

Thank you, Patricio. Good day, everyone. Turning to Slide 6, total assets were up nearly 38% year-on-year, growing above loan growth and relatively stable sequentially. The share of high-margin 7-day Leliq securities issued by the Central Bank accounted for close to 24% of total assets at quarter end compared to 20% in the first Q '19.

Now on to Slide 7. Our loan portfolio remained flat as we maintain a cautious approach in a recessionary environment. In this context, we continue to reduce our exposure to the Consumer Finance segment, which now represents 8% of our total portfolio, down from 9% in the first Q '19 and 11% a year ago. Overall, Consumer Finance loans declined 10% sequentially and nearly 22% year-on-year. The share of corporate loans remained stable at 50% of total loans and increasing 2% sequentially. Retail loan growth remained soft, growing slightly over 2% sequentially, reflecting ongoing weak consumer sentiment.

Please turn to Slide 8. We saw a slowdown in deposit growth rates this quarter as we continue to focus on liability managements as spreads from investments in high-margin 7-day Central Bank Leliqs declined towards the end of the quarter, we reduced our exposure to wholesale and institutional deposits. The combination of these factors continued to weigh on our loan-to-deposits and loan-to-assets ratios, which decreased by 170 and 50 basis points to nearly 73% and slightly over 49%, respectively.

Our liquidity ratio in pesos and dollars remained healthy at 65% and 56% of total deposits as of June 30 respectively, compared with [60%] for the overall financial system. At the same time, while in currency of origin, foreign exchange deposits rose nearly 4% sequentially. The share of foreign exchange deposits over total deposits declined 30 basis points sequentially to slightly over 32%, mainly reflecting the peso appreciation in the quarter.

Moving on to funding on Slide 9. As we've been discussing over the past quarters, we're actively managing our wholesale and institutional deposit base to maximize spreads. With Leliq interest rate declining towards the end of the quarter, we reduce our exposure to wholesale and institutional deposits to 35% of total deposits from 40% in the first Q '19. At the same time, the share of retail and senior citizens deposits increased by 400 basis points to 46% at quarter end, while corporate deposits increased 160 basis points to 19%. Therefore, while the share of non- or low-interest-bearing deposit balances accounted for 35% of total deposits compared with 33% in the prior quarter, the average balance of these deposits increased to nearly 44% in the quarter from 41% in the prior quarter.

Now on to the P&L on Slide 10. We delivered strong net financial income growth this quarter, up nearly 20% Q-on-Q; larger average volumes of assets and deposits, together with higher market interest rates, were the main drivers behind this good performance. Total NIM, in turn, was up 300 basis points sequentially, reaching 22% in the quarter, up from 19% in the prior quarter. This was principally driven by higher average Leliq yield in the quarter together with a lower share of nonremunerated reserve requirements. Our Argentine peso loans portfolio also contributed to this performance with a 60 basis point increase in NIM as we continue to experience repricing in retail loans.

Turning to Slide 11. Net service fee income remained stable sequentially. We saw a good growth in fees charged, driven by the full repricing on the fees on bundled services, credit card commissions and in noncredit-related insurance products. This good performance however was largely offset by weak loan origination and higher commissions paid mainly to debit and credit card processors. Income from insurance activities was up mid-single digits sequentially. Written premiums rose up 15% Q-on-Q supported primarily by strong growth in mortgage and Home Insurance as well as Technology Insurance supported by growth across all other insurance products. We also saw lower claims paid as we implemented the annual rebalancing of the seasonal accident rates curve.

Looking at asset quality on Slide 10 -- pardon me, Slide 12. We delivered sequential improvement in loan loss provisions, cost of risk and the overall NPL ratio. Loan loss provisions were down 36% sequentially after fully provisioning a commercial loan that became delinquent in the prior quarter in excess of the 25% regulatory requirement. Cost of risk declined to 6%. And the total NPL ratio was down 20 basis points to 5.1%. Keeping a cautious approach given the persistently high interest rates and weak activity levels observed across several economic sectors, this quarter we increased NPL coverage to nearly 108%.

Finally, the NPL ratio declined 20 basis points sequentially to 5.1%, reflecting stable corporate loan NPL ratios and a lower incidence of the Consumer Finance segment. And while Retail and Consumer Finance loan NPL ratios increased slightly sequentially, this was mainly due to lower loan origination while we observed a decline in NPL creation.

Turning to Slide 13. We remain focused on protecting asset quality on the Consumer Finance lending business. This business, which has been the most impacted by the high inflationary environment, continued to post improved asset quality since we implemented more stringent credit scoring standards early last year. We experienced sustained, good performance in 3-month vintages following the peak observed in February of last year and the slight deterioration in the fourth quarter of last year. Most importantly, Consumer Finance NPL creation declined for the second consecutive quarter and stood well below peak levels reported in the first half of 2018.

Moving on to expenses on Slide 14. We experienced a sequential deterioration in the efficiency ratio. Excluding nonrecurring severance charges of ARS 273 million this quarter and ARS 91 million in first quarter '19 from streamlining of operations, comparable efficiency was nearly 59% this quarter compared with 58% in the prior quarter. While improving operating efficiency range is one of our key strategic objectives, efficiency remains impacted by higher personnel expenses mainly driven by mandatory salary increases to adjust to the inflationary environment.

Moving down to the bottom line on Slide 15. Profit before taxes doubled sequentially, underscoring the strength of our franchise and our revenue generation capability. This was so even after increasing NPL coverage to nearly 108% and despite nonrecurring expenses from the bank's reorganization earlier in the quarter. Year-on-year, pretax income more than tripled, reflecting easier comps as second Q '18 was a particularly weak quarter. Return on average equity for the quarter increased sequentially to 42.2% from 13.6% in the prior quarter while return on average assets improved to 4.7% from 1.5% in first Q '19.

Note that starting this quarter, we're recognizing inflation adjustment in the income tax provision as inflation for the current year based on market consensus is likely to surpass the 30% threshold established by the tax reform passed by Congress in 2017. As a result, net income in the second quarter includes the benefit of ARS 664 million corresponding to inflation impact from the first half of the year. Roughly half of this positive impact was generated in the first quarter and the other half in the second quarter.

At the same time, our Consumer Finance lending business remained impacted by higher market interest rates in its wholesale funding structure while asset quality continued to show improvement after tightening of its underwriting policies and reduced exposure. Normalized return on average equity for Grupo Supervielle excluding the Consumer Finance lending business would have been 48.5% in the second Q '19.

Please turn to capitalization on Slide 16. As we explained in more detail in our earnings report, this quarter the Central Bank clarified an interpretation with respect to deductions on Tier 1 capital in connection with deferred taxes. Until first quarter '19 and following the IFRS and Basel frameworks, deferred taxes were deducted from regulatory Tier 1 capital on a net basis.

Starting second Q '19, we are required to deduct deferred tax assets without offsetting deferred tax liabilities, which resulted in high deductions on Tier 1 capital. If this criterion had been adopted in first Q '19, the Tier 1 capital ratio for the first quarter would have been 11.8% instead of 12.1% as reported. Importantly, capital creation contributed with a 90 basis point increase in Q1, exceeding the 50 basis points consumed by our weighted asset increases in the period. During the quarter, we made capital injections of ARS 500 million in our finance company. We also paid ARS 303 million in dividends and received ARS 353 million in dividends from our subsidiaries. A total of ARS 442 million remain at the holdco for future capital injections.

Moving to the outlook on Slide 17. When looking at our first half results, we're tracking ahead of full year net income guidance provided earlier in the year. And we are cautious about the back half of the year. It has always been our intention to provide guidance of the key drivers to help you understand the business. This quarter, we're taking the unusual and temporary step of placing our prior guidance under revision while we continue to navigate a challenging environment compounded by increased volatility surrounding the presidential election. This makes it more challenging to calibrate guidance around many of our key business drivers for the back half of the year. We expect to update the investment community on the key metrics when volatility recedes.

This concludes our prepared remarks. Operator, now please open the call for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question comes from the line of Gabriel Nóbrega with Citi.

Gabriel da Nóbrega - *Citigroup Inc, Research Division - Research Analyst*

I would just like to know how has the bank prepared itself ahead of the elections on Sunday. And while I know it might be too early to understand the impacts from the market movements that we saw yesterday, could you just remind us if you were net long or short dollars? And also making it in parallel with the peso depreciation that we saw in 2018, what could be a possible read-through for your net financial margin in the coming quarters? And I'll ask a second question afterwards.

Jorge Oscar Ramírez - *Grupo Supervielle S.A. - First Vice-Chairman & CEO*

Regarding your -- the first part of your question, we had a neutral position. We closed all of our positions on Friday. We took advantage of the Friday upward market and closed down. So we remain neutral for the election weekend, which was in hindsight the right thing to do given the high uncertainty we had on Friday. No pollster anticipated the results of -- this Sunday and definitely not the difference between the 2 candidates. So we decided the more cautious approach. Given the uncertainty, was to remain neutral.

In terms of the second part of your question, it's a very different environment, 2019 and the second half of the year to what we experienced in 2018, essentially because when we had the major devaluations at the beginning of last year, second quarter of last year, we still had the LEBACs in place. And the Central Bank had several problems in terms of renewing the LEBACs every 35 days. So clearly, we're facing a very different balance sheet in which loans to assets is 49% of total assets. So it's substantially lower than what it was last year. We have a -- even though we retained -- we had a lot of liquidity impact last year, we have a substantially higher level of liquidity now. So I don't think that we can use the experience of last year in terms of predicting the impact or the pass-through that this might have on our NIMs going forward. And it's still too early in the game after the results of the presidential election to be able to give you a meaningful forecast. By the way, that's the reason why, as I just explained, we suspended guidance for the time being until we have a clearer picture in terms of what we see coming ahead.

Gabriel da Nóbrega - *Citigroup Inc, Research Division - Research Analyst*

All right. That was very clear. And as for my second question, I know that it might be too early to say but have you begun to experience any type of a deposit run? And in this case, could you just remind us how are your liquidity ratios and if you are worried on any parts of this?

Jorge Oscar Ramírez - *Grupo Supervielle S.A. - First Vice-Chairman & CEO*

We haven't seen any runs in the deposits. And as I explained in the presentation, our liquidity levels as of the end of the quarter and even today stand at 65% for peso deposits and 56% -- or around 56% for dollar deposits. So we're extremely liquid. The whole system is extremely liquid and very well prepared to face any systemic run. So personally and collectively, we as a team, we don't foresee that, that's going to be a major problem. We might see the mutual fund industry facing some withdrawals and of people changing portfolios. And that might impact the prices of some securities and maybe some sell-offs. But I think that everything, the whole system, including the mutual fund industry as well, I think they're in a much better position than what they were last year when we had this run against the peso.

Operator

Our next question comes from the line of Jason Mollin with Scotiabank.

Jason Barrett Mollin - *Scotiabank Perú S.A.A., Research Division - Analyst*

You talk about your liquidity and the asset composition with loans decreasing in importance. We've seen, on the other hand, a very substantial increase in the exposure to Leliq and government securities, which at the end of the second quarter represented about 27% of assets. If we look last year, taking into consideration the LEBACs and the government securities, I think it was probably about half of that or about 14% of assets. How do you feel about your exposure to government securities and the Central Bank notes? And is that something that you would consider adjusting given the current environment?

Jorge Oscar Ramírez - *Grupo Supervielle S.A. - First Vice-Chairman & CEO*

I think -- I mean this is part of the [flexibilization] strategy that we've been putting in place. And it was discussed a couple of weeks ago in New York that clearly loan demand has been particularly nonexistent. And overall loans in pesos have been flat year-on-year with a cumulative inflation rate over 50%, closer to 60%, for that same period.

So we have had a sharp increase in liquidity. The whole industry has had that as a result of the unwinding of the whole LEBACs programs. And the big difference we have now is that the Leliqs are -- only banks can invest in Leliqs. So these are tools that the Central Bank uses for -- to maintain and manage liquidity for the overall system. So unless there is a massive run in deposits systematically against the peso deposits, there is no place banks can go with the LEBACs -- with the Leliqs.

So we don't feel worried about it. If even mentioned in dollar terms, the percentage of the Leliqs is substantially lower than what the LEBACs were at their peak. Yesterday, the valuation has even further [liquidated] the outstanding measured in U.S. dollars. The Central Bank still has plenty of reserves and is being very cautious and is showing to be very cautious in terms of how they're using them. So clearly, this is not the type of business we'd like to run. But this is the right kind of asset composition and balance sheet composition we need to have given the current circumstances and the current environment that we're facing.

Jason Barrett Mollin - *Scotiabank Perú S.A.A., Research Division - Analyst*

That's helpful. Maybe just some comments on the FX and what you're seeing, the intervention on behalf of the Central Bank and how your bank is managing FX for clients? What kind of spreads are you offering them for buying and selling pesos in the current environment?

Jorge Oscar Ramírez - *Grupo Supervielle S.A. - First Vice-Chairman & CEO*

Well, the bid and offer yesterday were really very, very wide because it was a highly uncertain day and highly volatile day. So it's only [logical] that it has been in line with what the rest of the banking industry has been doing. In terms of our overall exposure, we're neutral as I explained earlier. And we've been using our dollar loan portfolio measured in its original currency, especially with corporates. So we don't expect to have a major impact coming from that.

Operator

(Operator Instructions) Our next question comes from the line of Yuri Fernandes with JPMorgan.

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

I have a question regarding Alberto Fernández. If you can comment any kind of proposal he has for banks like if you had heard anything in particular that is worth flagging? I recall he was a critic of Leliqs in the past of this high real interest rate. So if you can also discuss what would be the impact for your bank? And I think like this could be a concern for the market, right? As the previous questions, you have a big exposure to government secured. (sic) [securities.] And what would happen if there is a material change there? So if you can comment on the whole of public banks, the whole of Leliqs, any kind of past regulations such as subsidizing loans for SMEs? I don't know. Anything you can provide colors that maybe Fernández had been commenting, would be nice.

Jorge Oscar Ramírez - *Grupo Supervielle S.A. - First Vice-Chairman & CEO*

Yes. I mean Alberto Fernández and the Frente para Todos hasn't been still very outspoken in terms of what they're going -- in terms of economic policies. Yesterday, he's starting to -- or started to try to bring some calm to the market, saying that they're not thinking in terms of any foreign exchange controls, that they don't -- that they want to -- that they will honor Argentina's debts, that they might sit down with the IMF to renegotiate terms and conditions, but that they will -- that they have the willingness to meet all of Argentina's obligations. And they haven't been any more specific than that so far. I think we're going to have a little more clarity in the next couple of weeks or in the next month or 1.5 months.

Regarding his comments about Leliqs, I think that was part of -- I mean that was in the middle of the campaign. One of his chief economic advisers, Guillermo Nielsen, came out and explained that, well, he cannot just simply not pay the Leliqs and use the to money to pay other things. So I think that was more a thing -- or more an expression used in the heat of the campaign to chastise the government because of the current level of interest rates rather than an actual threat in terms of what they're planning on doing with the Leliqs going forward. So again, summing up, just a more moderate tone after Sunday but not yet enough clarity in terms of specifics in terms of what they're planning on doing.

Just one -- let me add just one thing. And I think we -- some of you that we met in New York a couple of weeks ago, we had this exact same discussion, but for the benefit for the rest of the audience. Our bank, our group grew a lot, I mean probably 2/3 of our market share. We grew under the years of -- when Cristina was in power. Essentially, if -- traditionally, they have been of the mind of -- that consumption brings growth to the economy. If they want to do and go ahead with that kind of policies, our franchise is very well prepared to take advantage of that because of our Consumer Finance business plus our Retail business in the bank.

So in a sense, what I'm trying to -- I think the message I'm trying to relay here is that if you've worked many years in the Argentine financial system as most of our team has had, we've seen our fair share of this, unfortunately if I may add. We would like things to be different. But we sort of are used to being at the helm under stormy weather. And we've been able to weather through different storms throughout our professional careers. This is the mood and this is the way or the spirit under which we're facing this challenging scenario.

It's very difficult to plan ahead long term. But we're going to focus on things that we know that will not change irrespectively of who wins the elections and remain very flexible for the rest. And I think that we have prepared the company and the different companies of the group in order to face this challenging scenario. And we're trying to keep as flexible as possible in terms of trying to apply the right strategy at the different moments that we have to face.

Operator

We have no further questions at this time. Ms. Bartesaghi, I would now like to turn the floor back over to you for closing comments.

Ana Bartesaghi - *Grupo Supervielle S.A. - IR Officer & Treasurer*

Joining us today, we appreciate your interest in our company. We look forward to meeting more of you over the coming months and providing financial and business updates next quarter. In the interim, we remain available to answer any questions that you may have. Thank you, and enjoy the rest of your day.

Operator

Ladies and gentlemen, this does conclude today's teleconference. You may disconnect your lines at this time. Thank you for your participation, and have a wonderful day.
