

IFS
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2Q17 IFS Conference Call

Operator: Good morning and welcome to the Intercorp Financial Services second quarter 2017 conference call. All lines have been placed on mute to prevent any background noise. After the presentation, we will open the floor for questions. At that time, instructions will be given as to the procedure to follow if you would like to ask a question. It is now my pleasure to turn the call over to Rafael Borja of i-advize Corporate Communications. Sir, please begin.

Rafael Borja: Thank you and good morning to everyone, on today's call Intercorp financial services will discuss its second quarter of 2017 earnings. We are very pleased to have with us Mr. Luis Felipe Castellanos, Chief Executive Officer of Intercorp Financial Services, Ms. Michela Casassa, Chief Financial Officer of Intercorp Financial Services, Mr. Gonzalo Basadre, Chief Executive Officer of Interseguro, and Mr. Reynaldo Roisenvit, Chief Executive Officer of Inteligo Group.

They will be discussing the results of what was distributed yesterday. There is also a presentation to accompany these results. If you didn't receive a copy of the presentation or the earnings report, it is now available on the company's website, ifs.com.pe to download a copy. Otherwise for any reason, if you need any assistance today, please call I-advize in New York at 212-406-3693.

I would like to remind you that today's call is for investors and analysts only. Therefore, questions from the media will not be taken. It is now my pleasure to turn the call over to Mr. Luis Felipe Castellanos, Intercorp's Chief Executive Officer for his presentation. Mr. Castellanos, please go ahead.

Luis Felipe Castellanos: Okay. Thank you. Good morning to everyone and thanks for joining our earnings call to review our second quarter results. Let me start on the macro side. GDP growth expectations for the year stand now at around 2.5%. We have not yet seen a recovery in internal consumption nor in private or public investment.

However, we are optimistic and believe that the second half of the year will be better than the first half. Peru's macro fundamentals continue to be solid with low debt levels, high level of international reserves, low inflation and a relatively stable currency. Moreover, the investments for the reconstruction of the areas affected by El Niño, the unlocking of certain infrastructure projects like the Linea Dos of the Metro in Lima, the airport expansion, Talara and other announced projects, the easing of monetary policy by the Central Bank, and the increase of key commodity prices like copper, together with a better political scenario should lead to a recovery of public and private investment. All this should improve second half perspectives and result in a better growth scenario for 2018. The

financial system in the country continues with low growth and low activity, but it will remain solid, profitable, and very well capitalized.

Under this scenario, Interbank was able to slightly grow its loan portfolio during the quarter, mainly as a result of a pick-up in our retail business. This growth was partially offset by a decrease of the commercial portfolio. We continue focused in managing credit risk as the effect of the internal consumption deceleration and the impact of El Niño in our customers continue to put pressure in our asset quality.

We continue to invest in our digital transformation centered in providing new solutions for our customers, while managing adequate levels of operating efficiency. Interseguro had a good quarter with premiums increasing strongly. Since the impact of the changes in regulation are being left behind and the launching of new products start having a positive effect.

During this quarter we announced the acquisition of Sura's life insurance business in Peru, which will consolidate IFS' leadership in retirement annuities and life insurance. We will provide an update of the transaction later in the call. Inteligo had another very solid quarter achieving strong earnings growth.

Inteligo continues to provide IFS with a good level of earnings diversification with a strong fee income and with very profitable and efficient operations. Adding all this up, this quarter resulted in a solid quarter for IFS and our platform is well positioned to benefit from the expected recovery of the economy in the coming months. Now, let me pass it onto Michela to continue with our report.

Michela Casassa:

Thank you, Luis Felipe. Let me add some few comments related to the developments of the impact of El Niño on IFS, and particularly on Interbank before we start looking at the numbers.

During the second quarter of this year, we have seen the total amount of loans potentially affected by El Niño coming down from the 1 billion soles we reported during the first quarter to around 800 million soles.

The main reasons for the decrease in such amount is a fine-tuning of the figures by a more detailed analysis by geographical area of the impact in our retail portfolio as well as some repayments of loans in our commercial portfolio, which decreased the original estimate. The total amount of loans under the restructuring scheme approved by the SBS as of the end of June is around 390 million, up from the 300 million announced during the first quarter.

Thirty percent of which is commercial and SMEs, and 70% of which is retail loans, mainly in credit cards. We estimate the total impact of provisions for the year not to be substantial; and actually, not more than an additional 5% of the total growth provision for the year, which is between 40 and 50 million of which 15% has already been registered in the second quarter. No impacts on Interseguro and Inteligo as previously mentioned.

Now, let me start the discussion of the quarterly performance by referring to pages two, three, four, and five of the presentation. The main highlights are: first, at Interbank, loan portfolio continued to grow faster than the banking industry. The second quarter earnings were up 7.5% on a quarterly basis due to higher interest income and lower provisions, and stable costs.

NIM was up 40 basis points in the quarter with NIM after provisions up 50 basis points, and reaching 3.8%. While NIM on loans was up also 10 basis points. At Interseguro net premiums grew 8.4% on a quarterly basis, and 12.3% when compared to the previous year, with annuity premiums growing 12.4% on a quarterly basis showing that the launch of new annuity products has started to compensate the decreasing premiums after the regulatory changes of last year.

Strong quarter at Inteligo, with revenues and profitability growing substantially. IFS second quarter 2017 net profit reached 215 million soles, a 36% increase quarter on quarter and 21% year on year; and 2.8% and 4.6%, respectively, when excluding the discount rate impact on technical reserves that has been negative, but to a lower extent than in the previous quarter. Relevant net income for dividend payments, which includes local accounting for Interbank and Interseguro, and IFRS accounting for Inteligo show earnings growing on a quarterly basis by 8.1%, 37.8%, and 13.9% respectively.

When looking at figures at IFS level, NIM decreases ten basis points during the quarter, but both NIM and NIM on loans improve at Interbank mainly due to higher yield portfolio mix. PDLs increased ten basis points reaching 2.7% on a quarterly basis at IFS level.

Cost of risk improved 20 basis points quarterly down to 3% mainly due to an improvement in credit cards. Efficiency continued to improve down 60 basis points on a quarterly basis to 38.9% when excluding the impact of discount rates on technical reserves at Interseguro. Capitalization ratio for Interbank remains strong at 16.6%.

Please turn to the following pages for a brief overview of the quarterly net earnings of IFS three segments.

On page eight, performing loans grew 0.7% on a quarterly basis, as a result of a 2.2% increase in retail loans partially offset by a 1% contraction in commercial loans. Growth in retail loans was due to increases of 2.8% in other consumer loans, 2.4% in mortgages, and 1.3% in credit cards. The growth in other consumer loans was a result of higher payroll loans, while the increase mortgages was due to a higher dynamism in the traditional segment.

It is worth mentioning that the credit card portfolio has started to grow again; and we expect this trend to continue in the following quarters. The quarterly reduction in commercial loans was a result of lower short and

medium term lending associated with certain prepayments in the corporate segment.

Performing loans grew 3.3% year on year, due to increases of 3.6% in retail loans, and 2.9% in commercial loans. Retail loans grew mainly due to increases of 5.6% in mortgages, 5.5% in other consumer loans, partially offset by still a contraction of 1.2 in credit cards when looking at yearly figures.

In this context of low growth in the market, we have been able to increase our market share on total loans by ten basis points on a quarterly and yearly basis.

On page nine, deposits grew 3.4% on a quarterly basis with a stronger growth in commercial deposits of 5.6% compared to the 1% growth in retail. This strong growth has led to an increase of 30 basis points in market share in the quarter. It is worth to mention that deposits now represent 72% of total funding.

On page ten, when looking at SBS comparable figures to the system. Interbank's past due loan ratio increased ten basis points on a quarterly basis reaching 2.8% and below the system average of 3.1%, which increased also 10 basis points in the same period. The coverage ratio remains strong at 172% and the same trends are valid for the IFRS PDL figures.

When looking at the PDLs breakdown, we can see within retail that the overall consumer credit PDL has improved ten basis points on a quarterly basis down to 3.8%; and is slightly above the system average. Credit cards PDL has remained stable in the quarter at 5.5%, still above the system average of 5.1%, mainly due to both increases of past due loans and to a low growth of the credit cards portfolio of 1% in the quarter.

Within the commercial portfolio, PDLs increased in corporate by 30 basis points, but improved in both medium and small and micro companies, where we remained well below the system average. The annualized ratio of provision expense to average loans has improved 20 basis points down to 3.1% in this quarter. This ratio remains above the system average of 2.3% mainly due to the mix of the portfolio with a higher incidence of retail and credit cards when compared to the system and to the other big three banks.

Normalizing the effect of our portfolio mix, our ratio would be 2.1%, slightly below the system average. The weight of our credit card portfolio is roughly 16% of our total portfolio compared to 8% of the system. When looking at IFRS cost of risk figures, the trends remain the same.

On page 12, as of the second quarter, Interbank capital ratio of 16.6% was 460 basis points above its risk adjusted minimum capital ratio requirement established at 12% for the quarter, and above the system average of 15.8%.

The minimum regulatory capital ratio requirement was 10% while the additional capital requirement for Interbank was 2%. Core equity Tier 1 ratio was 9.1% in the quarter.

Please turn to the following pages to discuss Interseguro's results.

On page 14, net premiums in the second quarter increased 8.4% on a quarterly basis and 12.3 % on a yearly basis. The quarterly growth was explained by an increase of 12.4% in annuities, coupled with an increase of 5.4% in retail insurance highly explained by higher premiums in card protection. The yearly growth was also explained by increases of 13.2% in annuities, 11.8% in retail insurance, and 9% in individual life.

Annuities net premiums in the second quarter increased 12.4% on a quarterly basis and 13.2% on a yearly basis. The quarterly and annual increases were mainly explained by the rapid growth in volume of premiums of the private annuity launch in October of 2016, which largely offset the decreases of 16.1% on a quarterly basis, and 57% year on year of regular retirement premiums affected by the law which allows retirees withdraw a significant portion of their pension funds since the second quarter of last year.

On page 15, net premiums were 146 billion in the second quarter, increases of 11 million on a quarterly basis, and 16 million on a yearly basis. The quarterly growth was mainly explained by increases of 9 million in annuities after the market stabilization and 3 million in retail insurance. The annual increase was also explained by increases of 9 million in annuities, 6 million in retail insurance coupled with an increase of 1 million in individual life. Annuities market share in the second quarter was 23.2%.

Adjustment of technical reserves in the second quarter was 101 million compared to 177 million in the first quarter and 135 million in the second quarter of the previous year. The quarterly reduction was mainly due to different discount ratings impacts in annuities. This rate decreased by 16 basis points in the first quarter, and decreased by 6 basis points in the second quarter.

The yearly decrease was also a result of different discount rates impacts in annuities. This rate decreased by nine basis points in the second quarter of 2016. Net claims and benefits incurred in the second quarter were 88 million, increasing 4 million on a quarterly basis, and 13 million year on year. The quarterly growth was mainly due to a higher number of pensioners in annuities; and the yearly growth was mostly explained by higher annuity pensions and higher claims in retail insurance. Considering the factors previously explained, total premiums earned less claims and benefits resulted in minus 43 million in the second quarter, increasing 83 million versus the previous quarter, and 37 million versus the previous year.

On page 16, in the second quarter, Interseguro investment portfolio reached 5,900 million, increasing 5.4% in the quarter, and 10.9% year on year. Results from investments in the second quarter were 76 million, which represented a 5.3 return on Interseguro's investment portfolio before the

6.3 reported in the first quarter; but above the 5.1 registered in the previous year.

The quarterly decrease was explained by 30 million decreasing net interest and similar income partially offset by increases of 8 million in valuation gain from investment property, and 6 million in net gain of securities coupled with a decrease of 5 million in impairment loss available for sale investments.

On page 18, we will start the discussion on Inteligo's Group results.

As previously mentioned, Inteligo had a very positive result in the second quarter with a solid quarter in activity, revenues, and profitability. Inteligo's second quarter net profit reached 56 million soles a 13.9 increase quarter-on-quarter and 3.5% year-on-year. Inteligo's net interest and similar income in the second quarter was 25 million, a 3% decrease when compared with the first quarter. The quarterly results were mainly explained by lower income and dividends on investments available for sale, and higher expenses related to the deposits and obligations.

Net fee income for financial services was 29 million and remained relatively flat versus the previously quarter. Inteligo's other income reached 21 million in the second quarter, an 11 million increase on a quarterly basis, mainly explained by a more than a two fold increase in net gain of sales of security partially offset by net trading loss.

Other income increased by 30% year-on-year when compared to the second quarter of 2016, a result that was mainly attributable to 8 million growth in net gain of sale of securities, partially compensated by a negative result in net trading gain. Other expenses grew 4.5% on a quarterly basis mainly explained by a slight increase in administrative expenses due to higher third-party related services.

On page 19, assets under management plus deposits reached 14,684 million in the second quarter, a 1.1% increase when compared to the previous quarter, and 6.5% increase when compared to the previous year. Loan portfolio reached 1,650 million in the second quarter, and remained relatively flat. Revenues generated by Inteligo were 75 million, a 10.8% increase on a quarterly basis, and 0.7% increase on a yearly basis.

Inteligo's bank fee income divided by assets under management decreased to 0.9% in the second quarter. Inteligo's net profit in the second quarter was 56 million while annualized ROAE was 32.8%, higher than the 28.2% reported in the first quarter.

On page 23, we also wanted to give you an update on the Sura acquisition which we announced on May 31st.

As we have already communicated, the main rationale of the transaction includes: first, the consolidation of IFS leadership in life insurance business, being number one in asset under management for life, number one in retirement annuities, and number three in overall life insurance. Second,

an increased size and scale in an underpenetrated insurance market. And third, the potential to capture synergies through efficiency gains, and economies of scale, as well as from improved investment performance.

With this acquisition, Interseguro doubles its asset size reaching roughly 10 billion soles. As an update on the process, we have already filed all necessary documentation with the SBS at the beginning of Jun; and are expecting the SBS approval during the third quarter of this year in order to be able to close the transaction before year-end.

As a final remark, as you might have seen, we announced to the market that we have ended our share repurchase program yesterday. Under the share repurchase program, we have bought 2.4 million shares, or 2.1% of the total outstanding shares, which together with the previously held shares reach a total of 6.7 million shares, or 5.9% of total IFS outstanding shares. Now, we welcome any questions you may have.

Operator: And at this time, if you would like to ask a question, please press a star and one on your touch tone phone. You may remove yourself from the queue at any time by pressing the pound key. Once again, that's star and one to ask a question. We'll take our first question from Carlos Rivera with Citi Bank. Your line is open.

Carlos Rivera: Hi. Good morning everyone. Thanks for taking questions. My first question is regarding the macroeconomic outlook for Peru. Luis Felipe, you mentioned several factors to be optimistic about the outlook. What makes you confident that we can see finally all the infrastructure projects moving forward, and the political gridlock easing?

And do you think the positive impact of these is something we can see this year, or we will have to wait until 2018? And what does this mean for your strategy in terms of loan growth? Do you think you can grow faster now in terms of your risk appetite? And I'll ask my second question after. Thank you.

Luis Felipe Castellanos: Hi. Well, yes. We're optimistic, because we've seen already some things being announced, just a strong push from the government to resolve some of the pending issues: the metro 2 has been announced, the airport, the Lima airport has already been resolved in terms of the issues it was facing. We've seen Petroperu tapping into the markets and raising the funds needed for Talara which was also a point of concern. And like that there is a number of projects that are in line, and we expect them to get in line this year during the coming months. That itself should bring a boost to growth.

The second factor that makes me optimistic is that I guess lots of the issues around the political gridlock that we've had are really being resolved in terms of dialogue being open, and a clear view on the investments required to move our country. So although I don't like to give opinions on the political front itself, I guess there's a – my sentiment and the sentiment of the Group which I represent is that investments should start flowing

based on certain clear lines of action by the government established with the opposition on the dialogue that is going on right now.

As a testament of this optimistic view, is what the Intercorp Group itself is doing. We've announced transactions, and investments in the recent months between 400 and 500 million, including the acquisition of Sura. We've announced that we want to move forward with our Puruchuco project in the center of Lima. We've done an acquisition also of our own universities, so that's a sentiment that I'm reflecting throughout the expectations for the second half. And that should flow into 2018 as well.

And I also mentioned the easing of the Central Bank will help the cost of credit to go down in order to boost that growth of corporate and commercial credit. And also, the international environment for certain commodities that affect the Peruvian economy and exports, and it's also been better than we expected at the beginning of the year. So, if you add up all these factors, really, it's hard not to be cautiously optimistic at least.

Carlos Rivera:

Okay. And if you could just quantify a little bit now what you expect for in terms of loan growth given this optimistic outlook. And if this will translate probably into a little bit more of a risk appetite from you guys?

Michela Casassa:

Let me just jump into this. I mean, we have seen this low growth of 0.7% in this quarter. Okay. Which actually now, it's a mix growth, because we are seeing the retail growth recovering as credit cards have started to grow. Actually, this is the first quarter in which we registered a positive growth for credit cards of 1.3%, but still, the yearly figure is negative. But as we expect this trend of credit cards to continue in the forthcoming months, we expect that this will, I mean, not boost, but improve a little bit the figure of growth in retail.

If you look at the total retail loans growth for the year, it's still 3.6% which is 5.5% in other consumer, 5.6 in mortgages, but a negative number, 1.2 in credit cards. So if we continue with the trend that we have seen this quarter, and credit cards continues to have a positive figure, this is going to at least make this 3.6% of retail loans to be more closer to the 5% that the other products are growing.

And on the commercial side, I mean, we have been growing. If you look at the yearly figure, 2.9%, when we look at it on the yearly basis. What is impacting this figure, and what has impacted this figure in this quarter has been some prepayments of large commercial clients. We've had some clients going to the capital markets, big transactions and those are some of the prepayments we are talking about.

We could see some of those also in the second half year, but we also expect a little bit of recovery. We are seeing for example our mid-corporate segment growing faster than in the past. So that should also help. So putting and adding it all up together, when you look at our yearly growth, which stands at 3.3%, we should expect something above that.

Not, again, a boost in loan growth, but for sure adding up all the different segments, we should have a second half of the year that grows, I don't know, a couple or three points more than the growth that we have had in the first half of the year.

Carlos Rivera: Okay. Great. And my second question now moving to asset quality, we saw the past due loan going up a little bit, particularly on the corporate side, 30 basis points up. But still the provisions declined so a positive trend there. So just wondering if you could help us a little bit understand and reconcile these two moving pieces, for one side the NPL is going a little bit up, but provisions are going down. And on the press you particular say that the decline in provisioning, that got to the P&L is because of lower provisions on corporate. So any color there would be greatly appreciated. Thank you.

Michela Casassa: Yeah. The figure that you're referring to in terms of the increasing PDLs in corporate is actually not this 0.5% that turns into 0.8%. Actually, that is referring to one single client, and it's one client that is fully covered by a guarantee, and that have not been reflected in additional provisions. So this is, if you want the specific reason why you see an increase in the PDL of corporate, and you don't see a high increase in provisions in the overall commercial portfolio. And actually, when you look at the medium corporates, and the small, and micro companies, you see that there is also an improvement in the PDL figures. Now, medium corporates are going down from 3.7% to 3.6, and the small companies are going down from 7.7% to 7%, so this is why you don't see an impact in the levels of provisions. And moreover, I think it's important to take into account that when you look at the total provision expense, the incidence of retail, and particularly of credit cards on the total provision expense, it's roughly about 80% of the total provisions.

So it is much more linked to the PDL trend of the retail portfolio and not on the corporate side. And there, you see that when you look at the total consumer portfolio, the PDL has improved from 3.9% to 3.8%. So when you put these two things together, this is the reason why at the end of the day, the loan provision expense goes down from the 3.4% in the IFRS figures to the 3.2%.

Carlos Rivera: Okay. Very clear. Thank you very much, Luis Felipe and Michela for the answers.

Luis Felipe Castellanos: Thank you.

Operator: And then, we'll take our next question from Guilherme Costa with Itau BBA. Your line is open.

Guilherme Costa: Good morning, guys, and thank you for the opportunity. I have two questions. The first one, could you tell us again the amount of provisions you have already booked for El Niño phenomenon, and how much do you expect to book in the coming quarters? And could you remind us about your expectations for the cost of risk for the year? And then, my second question is regarding the low margins. Could you give us some

indication on the low margins evolution, both for 2017 and 2018? Thank you.

Michela Casassa:

Okay. First in terms of the El Niño impact, I mentioned at the beginning of the call that the impact is going to be something around 40 million, or not more than that, and actually, we have booked already in the second quarter roughly six million. You know that under the restructuring scheme approved by the SBS, we were able to let's say to change the dates for the clients. And basically, what we did was that we took a group of clients, the ones that we felt that were more riskier, or that have more problems, and actually, we contacted a big portion of these clients. And we gave them like, I don't know, on average, 90 days. So basically, a portion of those clients, actually, will have to pay their loans during the third quarter. So that's why we're expecting the bigger impact of this total amount during the second half of the year. And what we have registered already is related to the clients that already have shown that they will not be able to pay. And that is referring to the 6 million. So this is related to El Niño.

In terms of yields, you have seen that the NIM on loans has improved ten basis points. This is mainly due to the mix of the portfolio. With credit cards resuming growth being the product with the higher yield in the portfolio, this is for sure helping. And also, due to the fact that the commercial loan book has decreased 1% now versus retail, this is also something that has helped.

Then when you look at the total NIM there are a number of other factors that have a strong impact, which have nothing to do with the NIM on loans, but that have to do with for example, with the investments, with the portion of the reserve requirements that have helped us this year, because there have been several decreases in the reserve requirements for dollars. So this is also one of the reasons why when you look at total NIM, it improves from year to year. And going forward, I mean, I think we're going to have figures that would be relatively in stable levels to this year. Why? Because you will have positive effects now with credit cards being, I mean, resuming growth; but also, the commercial portfolio, we are expecting it to grow back again. So, that will offset a little bit of positive effects that the credit card growth could have on NIM. Another thing to mention is that the NIM net of provisions has improved, because the ratio of provisions has improved. So for 2018, that is a number that might improve as we see the cost of risk improving during this year.

Guilherme Costa:

And the cost of risk, do you expect both for 2017 and 2018, if you could give us some indication?

Michela Casassa:

What we're expecting for this year is, I mean, to be in similar levels to this year, because still as I was mentioning before, we've seen an improvement of 20 basis points this quarter, but we might see something that is, I don't know, similar to this quarter, or to the previous one due to the points we have discussed related to the El Niño impact. And for next year, yes, we should expect an improvement in cost of risk, and be more in the line of roughly 3%.

Guilherme Costa: Very clear, thank you.

Operator: And we'll take our next question from Jason Mollin with Scotiabank. Your line is open.

Jason Mollin: Hello. Thank you for the opportunity to ask a question. Perhaps on the banking sector level, you can talk a little bit about the competitive environment. One of your large competitors was saying, was using the term, due to aggressive competition, they've seen some pressure on spreads, particularly in the commercial side. And another competitor, actually, the same competitor, was talking about increasing their push into the consumer side where they have been holding back. If you can give us an update on what you're seeing in competition and if you would agree that there is a so called aggressive competitive environment. Thanks.

Luis Felipe Castellanos: Hi, Jason. This is Luis Felipe. Thanks for your question. Well, yeah. I agree with it. Given the lack of growth, we're seeing lots of aggressiveness towards, especially the commercial portfolio. Mainly, big corporates, and I would say maybe that's one of the reasons that we've seen our portfolio decrease. You usually do not play the size game. We're very focused on profitability as you all know.

So we've let some transactions just to pass by because of that reason. But we do see search for growth at nil margins from competitors, and that's something that is not in our appetite. And we do expect that to continue, although if the economy resumes growth, probably more sense we'll come into the competitive environment on that front.

And then on the retail side, yeah, I guess the same concept, if the economy starts to recoup as we expect given actual internal consumption growth, then we'll be able to be a bit more aggressive in our portfolio. As you know, we've taken many measures in order to restrict credit given what is going on in terms of the increase of the PDL. But we need to witness that before really turning into a more aggressive stance. So we still see that our growth is coming from good customer segments in terms of risk. However, in terms of risk appetite being increased for us, we'll need to really see internal consumption picking up before opening new sources of customer segments.

Jason Mollin: Thank you very much.

Operator: And we'll take our next question from Isaac Nontel with Prima AFP. Your line is open.

Isaac Nontel: Thank you for taking my question, a couple of questions. Considering that the impact on your net interest margin in the context of lower interest rate, how do you see that impact on your margins?

Michela Casassa: Okay. Let me see if I have understood. Now, you're asking me about the impact on net interest margin with lower interest rates, right?

Isaac Nontel: Yes. Yes.

Michela Casassa: Okay. I mean, the impact actually is different when you analyze the retail portfolio than when you analyze the commercial portfolio. Of course, on the commercial portfolio, especially in the corporate segments, clients think about spreads, so with lower rates your interest income is going to be lower. Luckily for us, on the retail portfolio, it doesn't work that way.

So basically, lower interest rates translate into lower cost of funds; and that lower interest rate not necessarily translates directly and straight ahead to the clients. So, the fact that the interest rates in soles have decreased, for example, has improved a little bit the cost of funds, and improved margins and spreads in the retail segment. So basically putting the two things together, we see more or less, they offset, but we see a small, but positive effect of this decrease in the soles interest rates.

Luis Felipe Castellanos: Yeah. It should be a marginal improvement in our NIM.

Isaac Nontel: Thank you.

Luis Felipe Castellanos: You're welcome.

Operator: And we'll take our next question from Alonso Aramburu with BTG Pactual. Your line is open.

Alonso Aramburu: Hi. Good morning and thank you for the call. A couple of questions, just to follow up on yields and the NIM. The press release mentions lower yields in credit cards. Can you give us some color as to what's driving that? Are you focusing on higher income clients? So what's driving that decline?

And in the case of Interseguro, also what explains the lower yield and the fixed income portfolio this quarter, and also if you can talk a little bit about the growth of your private annuity business, which you saw nice growth this quarter, and what do you expect for the second half of the year and into 2018?

Michela Casassa: Hi, Alonso. Let me answer the first question, then I'll pass it to Gonzalo for Interseguro.

In terms of the yield of credit cards, what's happening is it has to do with the mix of the portfolio mainly. Okay. Basically what has happened is that the, let's say that the *Consumo* part of the portfolio, so the one that is related to new billing is growing less than the other products like, for example, *Compra de deuda* or debt buying, which has lower yield. So there is a portion of that impact that is coming related to the mix of the portfolio. It's not that we are lowering the rates for each specific sub products. It's just that the sub products with the lower yields are growing more than the others. And let me pass it to Gonzalo. Maybe he can comment a little bit on the Interseguro part.

Gonzalo Basadre: Sure. Two questions. First, regarding the yield in the investment portfolio, the change has to do with what happened with inflation during the year. In the first quarter, inflation was very high, especially for the El Niño effects. So, all our inflation-adjusted securities gained on that, for that reason. And that has been reversed in the second quarter where inflation in several months was even negative. So, that impacted the yield of our inflation-linked securities.

Regarding the growth of private annuities, this is a product we launched last year. It was a reaction because of the new law, the liberalization of the retirement of the funds. We were the first insurance company that launched this type of product, and we think that we are leaders in this segment, which is basically an annuity but with several characteristics that make it more attractive for customers. We believe that any, most of our customers should choose a private annuity over a traditional annuity. In fact, most of the growth of private annuity comes from our pension clients that before will choose a normal annuity, and they choose a private annuity.

Alonso Aramburu: Great. Thank you. And what are your expectations as far as growth for these private annuity segment? I mean, quarter over quarter it grew like 50% in 2Q17. Do you expect this to continue to grow very aggressively, or do you think this can grow, I don't know, single digits? What kind of rate do you think these annuities can grow at?

Gonzalo Basadre: Right now, we're seeing it around the monthly sales of around 10 to 12 million sales per month.

Alonso Aramburu: Okay. So the round rate of 2Q should be roughly sustained where you have 30 million?

Gonzalo Basadre: Yeah. A little bit higher than that in the following quarters. Definitely not less.

Alonso Aramburu: Okay. Thank you.

Operator: And once again, if you would like to ask a question, please press the star and one on your touch tone phone. We'll take our next question from Joswilb Vega with Integra. Your line is open.

Joswilb Vega: Hi. Good morning and thank you for taking my question. I have just one question. Given that you are optimistic on the economy this year and the next year, how much of credit growth should we expect for 2018? And if you have any guidance for the ROE over the next two years or at least for next year? Thank you.

Luis Felipe Castellanos: Thank you. Before I pass it onto Michela, let me say cautiously optimistic. That's the word. Now, let me pass it onto Michela.

Michela Casassa: Okay. I mean, of course, there is a level of uncertainty now of what's going to happen in the second half. But if you see that our yearly growth of the loan portfolio has been 3.3%, when we look at this quarter, and

there are certain positive effects now as credit cards resuming growth. We should expect year end now with a growth that is, I don't know, something above 4%. If we can get closer to 5%, we will all be very happy. But for sure, it has to be something that is higher that we have seen up to June. Okay. So this is what we see in terms of loan growth.

In terms of ROE, when we look at the figures for the bank, the bank ROE stands at roughly 21%, and we expect this figure to be more or less in the same trend. And when we look at the figures for IFS, IFS ROE, when excluding the impact of the discount rate on the technical reserves of Interseguro, stands at around 18%. The second quarter of last year was 19.5% and now we are at 18.4%, so we should be in levels between this 18 and 20%.

Joswilb Vega: Okay. And about the credit growth for the next year, how much should we expect?

Luis Felipe Castellanos: I guess if we do, like, 4 or 5% this year, and the economy recovers, we should be around 8% next year.

Joswilb Vega: Okay. Thank you.

Operator: And we'll take our next question from Sebastian Gallego with Credicorp Capital. Your line is open.

Sebastian Gallego: Hi. Good morning. Thanks for the presentation. I have two questions. The first one regarding a contingency in the other expense line that you recorded. Can you provide some more disclosure on what was this about? And the second question is regarding regulatory capital and the implementation of Basel III standards. Can you provide some more color on what you're expecting regarding buffers, and probably regarding also the, on risk-weighted assets density, what could be the main changes here, or if there are no changes at all? Thank you.

Luis Felipe Castellanos: Okay. Thank you. On your first question, that's a generic provision we've booked, there are some changes that are being discussed, under the MiVivienda program. Depending on the outcome of that, there are some changes to the coverage that the program could grant to such loans. So we've booked this generic provision that could translate into a specific provision in the second half of the year. So we've already taken that into account. So not to affect the ultimate P&L results coming forward. So basically, that's the first part of your question. The number two . . .

Michela Casassa: In terms of capital, we always say that in Peru, we stand at something that is Basel 2.5 or something like that, because we have not fully implemented Basel III, but the superintendence has already now in two different points in time implemented many of the different definitions of Basel III. Actually, I think it was three years ago, the superintendence implemented many changes to the weights of the risk weighted assets of the different products in order to try to align to Basel III.

So when talking specifically about the risk weighted assets, we are not expecting further changes. We now have products that have really up to 300% weight of risk weighted assets versus loans, like, when we're talking about some consumer loans, so the risk weighted assets are already, I would say even much more than what Basel III is actually asking.

In terms of the requirement of capital and of the different components of capital, what the superintendence is currently regulating is the total capital ratio. It is not still regulating the Core equity Tier 1 ratio. So basically, today, we are being asked to have a 10% minimum total capital ratio plus an additional capital ratio that is calculated on a bank by bank basis, and that for Interbank as of the second quarter was the 2% that I previously mentioned and we stand in the 16.6% in this figure. Of course, we also internally measure and communicate to the market Core equity Tier 1, because it's a number that you all analysts see and the rating agencies see, and this number for June was 9.1%, and as this number builds up during the year, now we are expecting to end up the year with a number that is around 9.5%. Going forward, we expect that in some point in time, the superintendence will start to regulate Core equity Tier 1 and this is why we have been working in order to improve this ratio over time. Actually, this ratio one year ago was 70 basis points below the 9.1 that I'm reflecting in the figures of June. And we will continue to do so in the future.

Operator: Thank you. And there are no more questions at this time. I would like to turn the program back to Mrs. Casassa for any closing remarks.

Michela Casassa: Okay. Just to thank everybody for doing the call and we will listen each other on the next quarterly call. Thanks a lot.