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PRESENTATION

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

Good morning, everyone. Thank you for joining. I'm Tomas Lozano, Head of Corporate Development, Investor Relations and ESG. Welcome to Grupo Financiero Banorte's second quarter earnings call. In today's call, our CEO, Marcos Ramirez, will comment on the effects of rates, inflation and nearshoring for Banorte followed by the main results for the quarter, including loan growth, inflation related effects on the margin and the evolution of asset quality. He will also provide the key highlights related to our progress in ESG. Then Rafael Arana, our COO and CFO, will guide you through the financial results and walk you through the updated guidance for the remainder of the year.

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

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

Thank you, Tomas. Good morning, everyone. Thank you for joining our call today. The first half of the year was marked by a sense of macroeconomic stability, extending the positive inertia observed since last year, driven by strong investment, external demand and private consumption, mainly supported by a sound labor market, higher lending activity and strong remittances levels.

The resilience depicted in the U.S. economy is also supporting Mexico's momentum. The latter has resulted in an upward revision of our 2023 GDP forecast, reaching 2.7% from our initial estimate of approximately 1.5% at the beginning of the year. Inflationary pressures in Mexico continue to fade away, although we see signs of a delay start of the easing cycle as core inflation dynamics remain challenging, our economic analysis team has revised its forecast for annual inflation of 4.5% from 4.8%. Therefore, we are expecting tight monetary conditions for the remainder of the year, with the reference rate stable at 11.25% until the first meeting of 2024.

Mexico's performance will still be supported by positive tailwinds. We expect the Mexican currency to remain stable in 2023, with a year-end estimate of MXN 17.90 per dollar, supported by high interest rates, strong macroeconomic fundamentals, and more recently, the materialization of nearshoring investments in the country. Regarding this nearshoring effect in the last 6 months, we have seen increasing demand for credit from both foreign companies recently established in Mexico as well as from companies already established but expanding their operations and production capacity.

There has been increased activity from industrial spaces and higher demand for financial opportunities for construction, industrial warehouses, transportation companies, mostly in the north and center of our country, where we have a strong footprint.

Moving now to Slide #3. The business operations of the first half of the year continues to portray sound margin performance, supported by great origination volume and mix, although already pressured by higher cost of funds aligned with market conditions. Structurally, we continue to reduce our margin sensitivity with an active asset liability management already reaching MXN 860 million of additional NII for every 100 basis points increase in rates down from MXN 1.1 billion last quarter. Rafael Arana will provide additional details in the following slides.

Moreover, we continue to see solid NIM dynamics together with very positive expansion of lending activity, boosted by strong internal demand and some importance levels. All this with a strict focus on asset quality, which continues to show better-than-expected results.

Starting off with profitability, Slide #4, ROE improved more than 250 basis points compared with the first half of the year, driven by the expanding performance across most of the business lines, which is also reflected in a solid return on assets.

Moving on to the top line results of the group, Slide #5, despite solid growth in the loan portfolio, NII went down 10% in the quarter, mostly driven by a negative valuation effect of inflation index securities in the annuities business amounting to around MXN 4 billion. In the quarter, inflation-related instruments (inaudible) dropped [10%]. It is worth mentioning that net income from the annuities business was not impact whatsoever at this negative inflation valuation was practically offset by lower technical reserves in the order time of the business.

Another fact that this pressured NII is the influence of higher rates in our funding costs despite our ongoing strategies to maintain our collection efforts and the funding mix. Rafael Arana will provide more details on this. Noninterest income expanded MXN 3 billion in the quarter on the back of lower technical reserves constitutions in the annuities business, driven by lower inflation along with higher trading income.

Fees, Slide #6, remained flat in the quarter on higher interchange fees derived from the hot sale event, which accelerated online purchases during the quarter, with accumulated figures, fees grew 9%, led by stronger electronic banking fees, higher advisory and structuring fees in commercial and government portfolios and more dynamic transaction volumes in consumer products, driven by the strength of private consumption. Digital transactions keep growing in tandem with the increased adoption of our digital channels. As of the second quarter of the year, the number of customers who conducted mobile banking transactions grew from 5 million to 6 million people, up 20% versus the second quarter 2022.

Loan growth, Slide #7, continues to accelerate with a strong focus on asset quality. Loan expansion posted a double-digit annual growth across most of the portfolio. During the quarter, the commercial book was one of the key drivers for growth as the strategic focus on low-risk SME lending continues to materialize. We still have a long way to go in this segment. But as we increase our capabilities to provide comprehensive and tailored-value propositions, we will be gradually regaining our fair market share and generating more profitable relationships in the long run.

Corporate loans had a relevant performance in the first half of the year, although affected by both repayments and FX valuations. Opportunities to increase our dollar loan portfolio continued to grow currently representing 11.3% of our loan book. The government book went down 9% in the quarter, driven by the maturity of some short-term revolving operations.

The consumer portfolio, Slide #8, displays double-digit annual increase across all products, reflecting the stability of the labor market and a strong internal demand. Growth in the mortgage book stood as one of the main drivers within the consumer portfolio, consistently growing over MXN 2 billion per month reflecting the results of our strategic approach to gather high-value customers, focusing on a low leverage, high (inaudible).

Payroll loans and credit cards continue to show accelerated demand driven by good employment levels as well as by the convenient offering of our digital banking channels. Auto loans have increased demand and there has been a recovery of supply shortages and also driven by our commercial partnerships with strategic dealerships. Mortgages and auto loans account for approximately 29% of the total loans.

Slide #9. As I have mentioned before, asset quality continues to perform ahead of our expectations. NPLs remain practically unchanged quarter-over-quarter, despite higher value volume growth in consumer and commercial books. Risky products, such as SME and credit cards continue to outperform their historical levels, mostly explained by favorable changes in our customers' approach to credit, along with more precise origination models enable us to grow without sacrificing quality.

Payroll loans continued the (inaudible) normalization process but growing with solid risk strategies. The annual increase in cost of risk is well aligned with origination volume and mix. So far, we do not foresee deterioration in any sector or any geographies.

Analyzing the quarterly results by subsidiary, Slide #10. The bank shows some core banking operations, boosted by a more dynamic and higher-quality lending activity as well as better market-related income, although slightly offset by higher cost of funds. Altogether, these results yielded a solid 26.6% return on equity for the bank with accumulated figures ROE stood at 27.2%.

The insurance business had a quarterly reduction driven mainly by the seasonal effect of the first quarter of the year, which concentrates most premium greening ones. On an accumulated basis, the insurance business is already operating at the normal levels, with some business generation. It is worth noting these results were affected by the upward adjustment in the intercompany (inaudible) between the insurance company and the bank, for insurance products hard to the bancassurance model effective as of last quarter.

The broker sector increase was mainly driven by higher business operations. The Annuities business, as mentioned before, has relevant inflation-related movements with the P&L, but with neutral impact on the net income. The quarterly reductions responds mainly to lower business generation derived on the market compression. With accumulative figures, the expansion was driven by higher technical results on the back of lower constitutions of reserves for inflation updates. As for the pension funds, it displays a solid evolution with higher yield of financial products.

Slide #11, we provide greater detail into the insurance business performance, showing the seasonal effect in premium origination during the first quarter, along with normalized trends. On an annual basis, it presents a business expansion, especially for light and auto portfolios with higher claims resulting from the mix of the portfolio. Moreover, the acquisition cost line is affected by the bancassurance fee increase mentioned earlier.

Shifting gears to ESG, Slide #12. Throughout the first half of this year, we have completed the measurement of carbon emissions and decarbonization targets for the most relevant sectors of our portfolio. We are now implementing different projects that will enable us to reach these targets through the joint efforts of all areas within the financial group. We will keep you updated on their growth. Moreover, during the quarter, we were proud to receive AA rating by MSCI from the third consecutive year as well as different recognitions from reputable organizations, such as the World Finance, who recognized Banorte as the best retail bank, best corporate governance and best pension fund in Mexico, among other recognitions.

Finally, I would like to stress our commitment to focus on organic business generation. We will prioritize investments related to the hyper personalization efforts in the bank and the expansion of our digital capabilities, placing the customers at the core of our product design.

Moreover, we will focus on improving the efficiency of our (inaudible) network, providing either digital interfaces or human interactions based on our customers' requirements. Increase our infrastructure footprint in the country through our ATM and new branch model networks and continuing to strengthen our human capital.

Nevertheless, internal capital generation has been consistently strong. Therefore, we will call for a shareholders' meeting in the upcoming months to propose the payment of one extraordinary dividend amounting to MXN 15 billion in the last quarter of the year. This payment will be on top of our dividend policy, which recently had a 50% payout ratio last June, totaling approximately 9% dividend yield for the year with totals -- with today's price. Now I will leave you Rafael Arana, who will provide additional details about this and will walk you to the financial results of the second quarter of the year. Rafa, please go ahead.

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

Thank you. Thank you, Marcos, and thank you for attending the conference. On the slide that you can see and going in the term of what Marcos just mentioned, the balance sheet continues to be in an extremely positive situation.

The return on equity continued to move in the right direction. As you know, we have committed from '20 to '21 for the group, we are a bit above the 21% for the group. The bank is around 26.6% on that. Obviously, the question is what's the recurring number that you can have for the bank, and what we have seen based upon all the movements that we see in the -- basically in the book, in the consumer book and the evolution of all the parts of the business we really think that from '22 to '24 will be a recurrent return on equity for the bank.

The transformation continues to be quite strong. We continue to be, if you look at the NPS, that is public information in Mexico. We continue to evolve positively in comparative what appears in everything that is related to the mobile banking to the interfaces on digital and human.(inaudible) the group, Marcos already explained the effect that we have on the annuities side, that is totally compensated by the technical reserves.

So no effect of the net income, strong return on equity for the business on the annuities business of 20%, so we continue to see pretty good evolution on that business. And the effect, as Marcos showed on the slide, the effect that the inflation had on the valuation of the positions is really what is causing that reduction on the NIM for the annuities fully compensated by the technical reserves.

The bank continues at 6.5% is slowing the pace of growth and the expansion of the NIM still a very, very positive expansion on the NIM for the bank based is upon two things, the consumer books continues to go pretty strong and the variable rate part of the group that is basically the corporate, the commercial and the government part of the group continues to go in a very positive way, aligned with the hike in the interest rates.

The other thing is in the funding cost. The funding cost has been some question about the evolution of the funding cost. As you remember during the conference call on the Investor Day, we remind that last year, we were very positive on the growth on the time deposits around 3%, and demand deposits were around close to 14%, So it was a very positive funding mix. We continue to have a very positive funding mix, 72% demand deposits and 28% are term deposits, but term deposits are obviously asking for better returns that we -- we used to have last year. So term deposits this year are growing around 8%, and that is causing an effect on the funding cost that we advised during the Investor Day. That number is currently of 43% of (inaudible) the funding costs, but fully compensated by the spread and the evolution of the margin on the loan book against the liability book.

If you see the spread continues to expand and the liabilities against the assets part of the group. So we are in a good position, good growth in the loan book, more expenses on the funding cost because of the growth on the funding mix on the term deposits, but very positive because the type and the kind of clients that we are attracting to the bank. So the funding cost, I think, is on a (inaudible).

We will see that funding cost coming down on the following months and really going back to the 41.5% at the end of the year, that was our expectation for the -- when we set up for the project. So that's the effect on the funding costs. If you see the funding costs, some people are we say, well, the funding cost is growing 90% on the funding side and 60% on the asset side, yes, but you have to take into consideration that 90% is basically the 28% part of the funding mix that is cost driven. The other part that is basically demand deposits close to that 72%, those 72%, 60% are with no cost.

So that part what is really funding basically the fixed rate part of the group. So it's completely positive on that mix, and the effect that is really creating the increase in the funding cost is coming from the time deposits growth that we are growing nicely in that part of the book and attracting good clients for us, but it has an effect on the funding cost. But overall, if you see the expansion of the margin, the 24% expansion on the margin and when you go to the NII and you go to the loan and deposits, you will see that 25% is the growth. So we are balancing that pretty well.

Remember that we are the largest term deposit bank in the market, so we have a market power in that part. But the growth and the ask for better returns for our clients is causing that growth in the funding cost, but pretty manageable based upon the 24% expansion on the

NIM and on the NII -- 25% expansion on the NII.

On the expenses, expenses continue to be under control. As you know, we are basically funding two new data centers that has moved the expense line a bit on that part that will be fully integrated on the second month of the next year. So the cost-to-income ratio continues to go in the right direction, now it's reaching at 34.1%. This is a record low for us, and we would like to be looking at that number as a possible number going forward. So when you -- when Marcos present the cost/income ratio, and you see the difference on the revenue side and the cost side, we will make more efforts on the cost side to continue to move around the 34%, 35% cost income ratio.

Capital, as Marcos mentioned, we continue to be net positive generation on the capital numbers. Core Tier 1 is at 15.4%. Now that Marcos advised of the dividend that will be paid in the -- once we get they go from the assembly to be paid in the month of October on that front. So that eventually will put us very close to the same number by the month of October on that front. So moving to the next one, the recent one on a more detailed basis, we already described the return on assets, return on assets continue to be a pretty good story on that part. We are growing 39 basis points on a year-to-year basis on that part. So based upon the mix that we currently are improving.

Remember that we are pushing the fixed rate part of the book in a very positive way. That is basically the mortgage book and the car loans. And you also can consider basically because it's a portfolio of the credit card book and also the payroll book. So we are pushing that number up. We are very close to the 44%, 45% on the total mix of the book that will be a natural hedge when the interest rates go down. So that has been very positive for us, we are attracting the clients that we like, high (inaudible) very positive. Sometimes we are sacrificing a bit on the margin in order to get the clients that we can build our relationship with them.

The return on equity for the bank continued to be very strong. If you look at on a yearly basis, 294 basis points growth on return on equity, taking into account very sound capital numbers. So the least -- and the least leverage fund in the market. So that is a very positive balance sheet and a very positive solvency numbers that we run the bank with.

If we go to the next one and get into the net interest income that I already described that basically, net interest income, very positive 25% on the loan and deposit book. The net fees of the bank, very positive 19% growth of the net fees of the bank. Every single channel is pretty active from mobile ATMs, transaction, cash management, everything is moving on that part. So the bank is breaking records numbers on transaction on a monthly basis.

So the bank is in full motion and in a very profitable motion on that part. So NIM very positive for the bank, very positive on the fees, 90% and also the net interest income for the bank on the loan to deposit is 24%. So I think we are managing pretty well the potential return to a more normal level of rates. We will see in a minute the sensitivity on that part. But I think we are very well positioned on the upward trend and very well positioned on the (inaudible). Next, please.

This is in a detail because there have been some questions about what was the fact on the annuities. This is basically the way that business has to be run because we cannot take any risk on the money of the pensioners. So when the inflation goes down and Marcos showed in the graph and inflation was negative for two consecutive months. That basically affects the valuation part of the positions, but it's fully compensated by the payment reserves. So there is no effect on the net income. And the net income, as I mentioned before, is pretty sound for the business, high returns on equity above 20%.

You see on the graph to the right on the colors on how we segregated the effect of the annuities, the bank very sound on the net interest income. As you can see, the insurance business, very, very strong again and fully recovered from the pandemia. And you see the effect on the annuities from MXN 6 billion to MXN 2.3 billion. That's the effect on the valuation. It doesn't have any effect of the net income. It has an effect of the net interest margin of the group that will be compensated as inflation that arises in the coming months, okay?

If we move to the next one, the asset quality continues to be a very good story. The MXN 1.7 million that you see on the cost of risk is right on the guidance that we provided to you at the beginning of the year. And basically, that uptick on the cost of risk has to do with the high volumes that Marcos referred at the beginning of the conference, where you see car loans, 30% growth, our payroll loans and credit card pretty close to the 20% very positive commercial loans. But if you see the write-off rate that is really a sound measure of how do we manage risk. You see a very stable number on the write-off rate that doesn't go up and down, up and down, as some of our other banks jumps up and down and up and down.

This has to do a lot of how we manage the business because if you look on a risk-adjusted basis, the margin, the margin grew 88 basis points on a year-to-year basis. So we are really penetrating the market with the clients that we like with the risk that we like and building a strong relationship with those clients. You see the number of trade provisions and is relevant to mention that we still carry MXN 540 million of the extraordinary provisions that we haven't used from that part. We move to the next one.

The next one, and this will be fully explained by Gerardo in a minute, so I will not take a lot of time on this, but we already start to unwind the positions to be ready for the lowering of the interest rate cycle. As Marcos mentioned, our economy expects the first part of the year to start the easing cycle on that part. On pesos and dollars, we also have reduced our sensitivity. I think that is a very positive news for the market.

And if you put that into the dimension of the net interest income of the bank, you can see that the group will suffer 0.6% of the total NII for each 100 basis points that interest rates brought down. So I think when you see that into the dimension of the NII, you see that we are extremely well positioned for that part.

The bank NII is 0.7 NII per 100 basis points of lower number rates on that front. So you see that if you go aggressive of the 6.5 or 400 basis points lower on the interest rate, it will cost us 2.4% on the group and it will cost 2.8% of the NII of the bank that will be fully compensated by the way, by the dynamic of growth that we have on the loan book.

If we move into the next one. Here, you see what already mentioned, the cost-to-income ratio that is very positive. And what I would like to mention is the graph to the right on the bottom part of the page, when you see a very strong pickup on the revenue side and a very stable cost line on the cost side. That cost line is the one that we want to keep pushing lower based upon what Marcos mentioned, a new format on the branch networks and expansion on the branch network, but with much more automated processes on that part, because we understand that the revenue side will lose a bit of momentum on that part, and we have to compensate that on the cost side. Okay.

The capital numbers, as Marcos mentioned to you and the liquidity, liquidity is around 170%, very strong liquidity. Gerardo will also explain a little bit more on that position that we have on the funding side, but we are very well positioned on that part. The capital adequacy ratio is at 21.7%, 50.4% the core Tier 1, fully compliant with a (inaudible) number that we require. And you see the leverage ratio that is really a very, very positive numbers on that part. So moving into the next one, I would like Gerardo to go in detail of a graph that he presented at the Investor Day, and that he has updated based upon the latest news.

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

Thank you. Thanks, Rafa. At the Banorte Investor Day last March, we provided investors with a better understanding of (inaudible) Banorte financial position and the potential risk we are facing. We strongly believe that balance sheet risk helps investors make informed decisions and assess Banaforte's ability to manage risk.

So risk-wise, here is an update on six fronts. In front number one, (inaudible) at the left upper side of the slide, regarding interest rate risk, you can see that in the fixed interest rate portion of the balance sheet, liabilities more than cover assets measured by outstanding balances by 103%. But notice that the duration provides the same excess, a remarkable 146%.

In addition, 49% of the loan portfolio has a probing interest rate regime with 41% variable interest rate funding. Remember that the variable portion of our balance sheet, asset duration exceeds liabilities range. That means that we are exposed to a risk in the case that interest rates are coming down. But that is going to be compensated by the fixed rate portion or gap between assets and liabilities in the fixed rate portion because asset duration is less than liabilities duration in that part.

In order to accommodate our balance sheet, we are using among others 6 strategies. Strategy #1, we use diversification, spreading investments across various assets, classes, industries and maturities. Strategy #2, duration management and NII sensitivity management, that is we adjust the portfolio overall duration based on our outlook for interest rates. For example, you have seen NII sensitivity cut by 1/3 in the first half of this year. We are preparing our balance sheet for the imminent interest rate decrease.

Strategy #3, we practiced bond laddering, which involves investing in bonds with stagger maturities. Strategy #4, we use interest rate drops. Strategy #5, we perform active monitoring and analysis, keeping a close eye on economic indicators, central bank policies and global macroeconomic trends. And Strategy #6, we continue to use hedging strategies to protect our portfolios from adverse interest rate movements.

All in all, our strategy will depend on our risk tolerance, investment goals and market outlook. That's regarding the first front. The second front, which is (inaudible) deposit stickiness, you will see that although cost of funds have gone up in relative terms, we expect it will normalize before the end of the year. Demand deposits represent 73% of total deposits and 96% of total deposits are considered sticky due to several reasons. Some of those reasons could be listed in the following.

First of all, we have increased up to 1 point of interest rates. Second, we are using hyper personalization to promote customer loyalty, building trust to personalized services, excellent customer support, tailored financial solutions in that regard. Number three, our product offerings remain attractive in the liability side of our balance sheet. Number four, we continue to invest in our market reputation to inflows to influence deposit stickiness. Also, we regularly check on economic stability and consumer confidence to detect a trend of our depositors regarding their behavior.

Number six, we comply strictly with regulatory standards to build trust. Number seven, we are very sensitive to customer needs and lifetime events like specific financial goals for life milestones, which could alter the behavior in our depositors. Number eight, we remain competitive in the profile of our deposit offerings, making them attractive all the time. And number nine, we provide and offer accessibility and convenience to our online banking services, mobile apps, and wide ATM and corresponding banking network. That is very important to make our deposit sticky in that regard.

We decided to provide you with this color, not just with the numbers that you can see at the low portion in the left-hand side of the business line. Front #3, Letter C, for AT1s, we use cash flow matching. We constantly use and make LDIs decisions, that is liability-driven investments.

You will see that this cash flow matching provides us with an investment in treasuries in order to have those cash flows dedicated to that event at the time of the call of the AT1s. So we manage and match AT1s future cash flow requirements with corresponding cash inflows from our securities portfolio. Front #4, letter D at the middle and low side of the slide, you will see that Banorte is the less leveraged banking institution among peers with a leverage ratio of 12.12%.

This Basel III leverage ratio is an essential regulatory tool to ensure that banks maintain sufficient capital to absorb losses and promote financial stability, which for us is paramount. Front #5, at the upper right-hand side of the slide, you will see that, as you might recall, in the context of Basel III Financial assets are classified into different levels based on their liquidity and how quickly they can be converted into cash.

Banorte has a 96.1% Level 1 assets that is high-quality liquid assets. And I will remind you that the most liquid and highest quality assets can be readily converted into cash in times of stress. And that's very important for us because you will see that the Basel III framework sets strict criteria for Level 1 assets requiring them to be highly liquid, low risk and readily available in the market. The composition of Level 1 assets includes cash on hand, qualifying government and central bank securities and deposits among others. In Front #6, letter F, our balance sheet has already had an adverse, but low severity capital impact of 20 basis points in the available for sale securities portfolio.

At the close of June 2023, if we were to impact our capital with the unrealized losses of the held-to-maturity portfolio, the theoretical impact will be of only 45 basis points, which is equivalent to a 50% consumption of our variability buffer. All in all, confirm this number with our capital volatility buffer that will be 83% because -- 83 basis points because by the end of June 2023, we had 33 basis points consumption. So this 45 basis points impact on capital is equivalent to 50% of the buffer. All in all, the consumption will be 83%. So absorbing these very unlikely scenario is thoroughly workable and sustainable in the case of Banorte.

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

There has been some questions about the guidance. I would like to go for the guidance as we start. Now the guidance, we moved the loan growth from 6% to 8% to now to 10% to 12%. Net interest margin that was basically supposed to be at 6.8%, now we are -- for the group at 6.2% to 6.4% as we have just mentioned what happened on the annuities side. The net interest margin of the bank that was at a point in time expected to reach 7%. Now we are lowering that to 6.5% to 6.7% based upon the cost that has happened on the interest rate side but still very positive on the number that it will be very close to the 6.6%, 6.65%.

The recurring expense growth, 7% to 8% and the total expense growth 11% to 13%, we are considering that the (inaudible) startup that it will be account for 2% of that expansion of the expense line. On the efficiency, 35% to 37%. We would like to have that a little below that, but I think that's a conservative number. Cost of risk, 1.6% to 1.8% remains the same, tax rate remains the same. Net income, now we moved the lower part of the guidance to MXN 51.5 billion to MXN 53 billion.

Remember that on this part, you have to take into consideration two things, we have been affected on two sides. The effect of the peso that is extremely strong has had an effect on the dollar position that we have and also the foregoing interest that we are giving away by paying the dividend is also taken into consideration that number.

If that was not the case, that number of MNX 53 billion would be easily above the MXN 53 billion. If there's any change coming in the next 3 months, we will advise the market and we have adjusted our guidance, I think, in a positive way.

Return on equity for the group 20.5% to 21.5%; and for the bank, 26.5% to 28.5%; the return on assets 22.3% to 22.5% with the numbers that you see on the economic arena 2.9% on the GDP; inflation rate from 4% to 5% and the reference rate still at 11.25% but who knows if things can happen before year-end. So that's the adjustment on the guidance that we would like to present to the market.

QUESTIONS AND ANSWERS

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

Thank you, Marcos and Rafael. Now we will continue with our Q&A session. (Operator Instructions) We will start with Gustavo Schroden from Bradesco.

Gustavo Schroden ***Banco Bradesco BBI S.A., Research Division - Research Analyst***

Good morning, everybody, and I have a couple of questions, and the first one is related to NII and NIM. First of all, I'd like to congrat you as you presented a very good explanation about the impact on NII due to the impact on annuities. But I'd like to clarify with you if it is correct, we mentioned that is correct, we understand that this volatility is much more related to accounting rules from IFRS or would have anything that the bank or management could do here to reduce this volatility.

Because if I understood, it is much more related to inflation trends. which in turn impact the annuit valuation -- assets and liabilities sides. So I'd like to clarify if this volatility is much more related to accounting rules or would be -- or would have anything that you could or if you have any way to manage this volatility in NII? And my second question is regarding the dividend policy, dividend distribution.

You mentioned that you were planning to announce or to propose an extra dividend in the amount of MXN 15 billion. I need to say that it's a very welcome from our side. But I'd like to understand that you still have a strong capital position, and we understand that in the past, there was an option of a potential deal, especially regarding the Betamax, but now it is no longer in the radar.

Would you think or are you saving capital for a potential new acquisition? Maybe it would be great if you share with us how do you -- or how are you planning the -- what is the growth plan of the bank? Maybe it would be great if you share with us how you should -- we should think in terms of growth plans of the bank. If we should consider a potential acquisition or if the main growth revenue would be through organic or would be an inorganic way.

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

Gustavo, I will start with the second one. We are not saving any more of the capital. But having said that, as I have said, we will prioritize investment related to the hyper personalization efforts in the bank, the expansion of our digital capabilities, and we will focus on improving the efficiency in our branch network, providing digital interfaces of human iterations in our customers' requirements.

We have a nice infrastructure footprint in the country, but we're -- with this new sharing strategy, (inaudible) maybe we'll move some pieces and all this, we will grow in ATMs, we are hoping to have 2,000 more in the next months, in the next year. And all these regarding to strengthen our infrastructure and our human capital. But so far, we don't see any big buy or anything. Maybe as you know, we are -- part of our job is to see what's in the market. And if we see a good opportunity for us to go to the assembly and then we will, in this case, raise money because so far, we are not saving it. But the strategy so far is to grow organically and in the right direction, and we have a lot of things to do, we have a lot of things in our hands, and that's a strategy.

And going to the #1, the NIM, that's correct. Before the IFRS, these movements were in another place. And now you have it there, but I would like to see that they are perfectly matched. If they go one way, they go down in the other side of the equation, so that's the (inaudible) you have the investment of all these reserves in (inaudible). And if they go up, they go up, and then you lose money, you lose money in both ways because that's not our money. That's the money that is there, but with this IFRS principles, now it's there and it moves and we need to show it and we need to spend it, because it's in the group, not in the bank. But the way I see it, you don't have a worry at all because it's perfectly matched.

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

All this that Marcos is mentioning is all a matter of accounting geolocation. Where do you want to register each and every item will make a difference in NII. But in the financial results and the P&L statement you will see the same effect on the bottom line. So where you put the item is the only difference and that's the distortion in terms of financial analysis.

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

And let me just stop on, if we were not doing this under IFRS, if we take risk on the positions, we will not be compliant with our fiduciary duty that is to protect the pensioners' money in a complete and relevant way. That is the law, that's the way we have to manage the money of the pensioners and the effect of the IFRS is exactly what Marcos mentioned and Gerardo.

In the past, it was completely matched, you didn't see movement at all, now you're seeing 2 different spots, and that's the case. But if we will play with the money of the pensioners, I think we will not comply with the law and with our fiduciary duty with the pensioners. So it will go up and down. I mean inflation went down pretty fast, so that's a result of that. Now you will see a much more stable number. You see a big reduction from one year to the other on the position on the margin on the annuities, but it's completely matched with the technical reserves. So it's no material on the net income accounting-wise and fiduciary-wise is the way that we have to manage the position.

Just to remember one thing on the dividends, I think we advised the market that the world was not quiet, and we needed to be careful with the dividends on the capital. We understand the buildup of capital and if we continue to see a much -- the pace that is becoming more and more normal there, what is going all over the place, not just in Mexico but over the place. We will continue to see a more aggressive flow to the shareholders in 2024. That's for sure. We are not saving money for anything. But as Marcos mentioned, for organic growth, but there will be enough money to keep on building more benefits for the shareholders.

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

Just to give some detail on Page 5, you can see exactly how what just Marcos (inaudible), it was basically compensated in the past with IFRS in the NII. And now we're disclosing the technical reserves of annuities that was MXN 4 billion, and that was the change from the margins to the net technical reserves down in the income statement.

Gustavo Schroden ***Banco Bradesco BBI S.A., Research Division - Research Analyst***

Super clear, super clear and thanks for the answers. And yes, super clear.

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

Thank you, Gustavo.

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

Thank you. We'll now take the next question from Geoffrey Elliott from Autonomous.

Geoffrey Elliott

Can you hear me okay? It's a question on the deposit side. First of all, you said on the previous call that you were expecting funding costs to come down from May onwards. That's not obvious in the numbers. Did that happen? Or is that delayed? And then related to that, deposits grew quite a bit faster than loans. So is there a deliberate strategy of kind of prefunding now? Or why are you growing deposits faster than loans in the quarter when deposits are obviously more expensive than they have been previously?

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

Yes. Geoffrey, it has seen a delay on that, but I think we already saw a dipping point in the month of July on the funding side. We always like to gather deposits, the more that we can. In this case, there's an opportunity in the market to bring the clients that we like to bring and some of them are asking for more return on the funding side, especially on the time deposit side. As I mentioned, last year, we were extremely fortunate on only 2% growth on demand on time deposits and 40% on demand deposits.

If you see demand deposit this year growing very close to 12% percent but it's matching the loan growth basically 1:1 on that part. So we are not having like an excess funding of that because the dynamic of the book is becoming really very, very strong. And with the clients that we like. So we don't want to lose any opportunity on that part. We are paying more on the funding side, but it's fully compensated, as you saw on the margin side and the spread, if you see the liability on the asset side, the spread continues to move up not at the same pace, but still expanding month-to-month. So I think it has been a balancing act, but a good balance act for the group.

Geoffrey Elliott

Great. Thanks very much.

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

Thank you.

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

Now we will continue with Tito Labarta from Goldman.

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

A couple of questions. One, maybe a little bit more of a modeling question, but just on the NII and the technical reserves from the annuities. Just -- is this a one-time adjustment? Or I mean I can understand maybe some volatility there, but as inflation maybe stabilizes or does it move as much -- should like next quarter, should we get a spike in net interest income from the Annuities business and then the reserves go back to where they were prior quarter? Just to help us kind of forecast how that can evolve from here? Or should we just think about the NII and the technical insurance results kind of combined as a better way to model.

And then my second question, more a little bit on your ROE outlook for the group, and thanks for the updated guidance and everything. But if we look like on -- think it was Slide 11 in your presentation where you have like the ROEs by the different subsidiaries, right? The bank ROE, as you mentioned, will probably come down to that 22% to 24%. Look insurance is above 50%, annuity at 20%, but then maybe (inaudible) and the broker dealer, which is 10 out of 11.

Can you help us think about to sustain that ROE, the 20% to 21%. And I think the dividend payment helps as well. what will offset some of the pressure that you see on the bank ROE as rates come down? So what's going to keep it above 20% to 21% if we think of the other subsidiaries?

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

Thank you. On the first one, it's very rare to see negative inflation in (inaudible). Everybody is expecting when you have the (inaudible) how much is inflation and how much they have to pay you and sometimes is low, sometimes is high. Sometimes you're happy, sometimes you're not happy, but negative inflation is rare to see, and that's what happened. I cannot say that we will have more events like this, but I would say that is going to be rare to see this case. But again, it doesn't move anything one way and go to the other.

The only problem is that according to the area for us, it goes to this part in. From my point of view, it was better before the IFRS, it was more clear. But that's the rules, accounting books. But goes one way, it goes to the other. We shouldn't worry about that though. That's my (inaudible) and the second one, the ROE, Rafa?.

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

Yes, Tito. If you look at the activity of the bank and if you look at the rate of growth that you'll have on the book, on the consumer book and going back, how do we expect to maintain the ROE of the 22% to 24% on that part. When you see the interest rates go down and based upon the high funding capabilities that the bank has that we have 72% of demand deposits and 28% on time deposits. You will see also a drop on the cost of funds that will very -- that will sustain a very strong fixed rate part of the group that is also will be fully compensated by that drop in the funding on the interest rates.

So that was one point, the other thing is that we continue to see that the bank is now really in full motion in every part of the business: commercial, corporate, consumer, the branch network, the mobile channel. So I think after the pandemia, the bank took some time to really fully recover the activity on that part. If you see SMEs, SMEs are growing in a very strong pace with a very strong credit risk numbers because we knew a lot about those clients during the pandemia, and we have evolved a lot on that.

We hire a lot of people to support the SMEs the same on the commercial side. So the bank is in full motion, is fully prepared to capture the activity at the time, the country, in the tourism side, in the near assuring side, in the SMEs, in the consumer side. So I would say that this, if you look at the pace of growth and when you see the numbers coming from the CNBV, you will see that the bank is really topping most of the consumer numbers in the market but credit cards because we like to be prudent about our great products. But that shows really that the bank is now reaching a potential to grow at a very fast pace with a very strong risk number. So we are not going to use capital to pay for unexpected losses on that part. So that's what really allows us to project the 22% to 24% for the bank and the 21% to 22% for the group.

So if you see, as you mentioned, above 50% return on equity on the insurance business, the bank 26%, 27%, we know the for -- why the -- I mean, the (inaudible) at the most will reach the 14% if you don't go to tangible and -- but everything else will be above the 20%. I mean what is going with the drop dealer and that part will fully compensate and it's a very small portion of the group. So we don't see any drag really to keep pushing the bank at 22% to 24%. And the bank is already taking into account the drag on the pension -- on the Afore business. So everything is going up from now. And as Gerardo mentioned, we are fully prepared for the easing cycle on the interest rates. The funding is in the right way, the consumer book is moving a lot more to the fixed rate part of the book.

We are having very strong relationships with our clients, and the fees -- the banking fees are growing at 19% and we don't see any reason why we shouldn't be able to keep that pace because the amount of money that we're investing in the channels, in the distribution, in the way we are setting up our branches and really the NPS is another very important thing that you should take into consideration. The NPS for the bank is at record levels, so the appetite for the clients to do business with the bank are a very good turns based upon everything that we have been investing in. So that's our confidence. I think it's not coming out of the rule. It's based upon the numbers that we are seeing and how we are managing the risks and how we are managing the price.

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

Okay. Great. No, that's helpful. So I mean, yes, I think the bank is pretty clear, but it sounds like even the insurance ROE you think might be sustainable above that 50% level and then you get some upside from the (inaudible) and maybe even a little bit in the annuities, is that correct?

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

Yes.

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

Okay. Perfect. And sorry to go back to my prior question and Marcos, thanks for the call there. I understand the difficulty in forecasting that and the bottom line doesn't really matter, right? But just to help us think about the individual line items between NII and the technical results. And so we don't see negative inflation again, right, which as you said, is not common. Would we expect sort of a normalization to where we were before this quarter? So kind of can look at this, what happened this quarter was a little bit of a one-off? And then it kind of normalizes to where we were before. Is that the right way to think about it, for both NII and insurance?

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

Yes. I think you will see a more normal number on that. I mean, if you see at the drop, the MXN 4 billion drop...

Unidentified Company Representative

Yes. (inaudible) mentioned that it would be a good idea to look at the two items together. That would be the financial products that you get from the investment side, and the compromises the annuity company on the technical reserves. If you look at the combined ratio, not the combined ratio, the combined items, then you will see that those things offset each other. We do not control the volatility of inflation. So looking -- going forward, we may take higher inflation, lower inflation. What is important is what was mentioned by both Marcos and Rafa that the two things are offset to each other because that's the way it's built because remember that we have to guarantee a real rate of return whenever we sell an annuity. And therefore, we match the assets and the liabilities.

That's why we invest only in (inaudible), which is the instruments issued by the Mexican government, which are linked to inflation. So it's not the way to start your question, you have to look at those items together, which was the way it was seen before the changes introduced by IFRS. But that, I think, would be the way to look at into the future because we cannot control the volatility of inflation. So that way, you will see that always these things will be offset one to each other.

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

Okay. Perfect. That's very clear.

Alejandro Padilla

Can I add something as well, please? -- chief economist. You have to also bear in mind that there is seasonality in Mexican inflation every year. You have subsidies to electricity tariffs during the second quarter of the year. And the contrary effect, you will observe it in the -- between the third and the fourth quarter when all the subsidies are completely off and you see higher inflation. So in Mexico, there's a seasonality in which you have deflationary numbers in April and May, and then also in a seasonal basis in October and November, you have higher inflation rates. Just to add to the answer.

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

Thanks Alejandro for the color.

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

And I think what Fernando mentioned is very important. That we don't play the game of positions and taking advantage of the money of the pensioners, that's not the way we want to start that business. So what you see is exactly, and it's very easily explained on the NII that we present, what Fernando mentioned, you match one with the other in a perfect way. And it's very clear explained on the Slide #5.

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

Yes. Okay. Perfect. That's very clear. Thank Rafa.

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

Now we go with Daniel [Vass] from Credit Suisse.

Unidentified Analyst

Congrats on the results, I would like to switch a bit to the commercial part of the business. I saw a good credit growth and also good asset quality on NPL. So I would like to take a bit of a sense what's the amount of debt you attribute already to the near-shoring effect if it's there already or not. And going forward, do you expect that to, I don't know, keep this growth on track or you didn't have a higher growth due to the near-shoring effect or so? So that's my question.

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

Thank you, Daniel. Rafa?

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

Daniel, if you look at the numbers of the bank on the prior years, you see commercial growing around 6% to 8%. So if you see commercial now growing at 12%, is basically all what is going on with infrastructure, building industrial parks, everything that is related to the supply chain. So you can add a very important number to that based upon the nearshoring that is at least of the 12% at least, 5%, 6% is related to the nearshore...

Unidentified Analyst

So very clear. So going forward, do you expect that to even go higher, right? So this could even rise?

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

Yes. That's why we set up close to 1,000 new bankers to capture the opportunity.

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

Thank you. Now we will continue with Yuri Fernandes from JPMorgan.

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

I had a question regarding earnings sensitivity and congrats on reducing this, I guess this is the big concern of the market, right, like there is any -- congrats, I think this has been maybe faster than we expected and you put out a soft guidance of the sensitivity reaching about MXN 700 million, right? Every [100 bps] change on rates. My question is, why not lower? In the past, I know your balance sheet was smaller, but you had around MXN 500 million, and as you said during the presentation, right, you are growing more fixed rate consumer loans, you are trying to grow your time deposit franchise that should also help reducing the sensitivity. So my question is, when should we see the MXN 700 million that you guided there? And why not lower? Why shouldn't we not expect like you'll be able to reduce even more your rate sensitivity and then I can have a second question.

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

It's a dynamic process because if you lower right now, you are losing the opportunity, the margin that is there right now. So yes, you need to be prepared and with good assets. And it's some other of the clients, they produce the good assets and to be very dynamic because yes, I would like to (inaudible), but not now, I want to have it when the rates go down. So we should calibrate when to do it and how to do it. The idea, Yuri, is to go down a little more in the future, good assets in the long term. And in the (inaudible), we have some ideas there to reduce it. So in the next future, when you say what did you do when we did a lot of things. But right now, it's not a good idea. We need also to take advantage of the rates right now. So we chose both -- but my answer is we should be dynamic that we will be post how we move on that sensitivity.

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

No, super clear. And a second one, if I may, regarding funding, there were questions about this already. But checking them and deposits, they are growing actually faster on a quarter-over-quarter basis, right? And your funding cost moved up. So what is happening with them in deposits? I guess it increased 7% quarter-over-quarter, faster than time deposits. And in this higher rate environment, I would expect maybe timing deposits to grow faster, right? So my question is, what's happened there? Because, again, you have a very good quality funding, and this was somewhat a surprise for us here.

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

I think it's part of the offer that the bank has. If you look at the growth that we have been having on the payable part of the business, that is basically demand deposit with no cost we continue to grow pretty strong on the payable side. Also, the SME side that has been an extremely good surprise for us because of the pace of growth, not just on the loan book, but also on the funding side is basically also a demand deposits with no cost, a considerable part of that. So I think those 2 are the ones that are basically sustaining the high growth on the demand deposit base, those two parts.

And also the activity that we are spacing at the bank with the digital offering that we have, the digital opening of accounts that you don't see very high balances opening in the digital but a lot of new accounts coming into digital. And that's when you add everything up is an important number on the funding side. So those 3 are the ones that are pushing up. Obviously, you have the time deposit, the big transactional banking movements that we have from the commercial and the corporate, I think, but on the low end of the cost side, those are the ones that are balancing the cost.

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

No, super clear [Raf]. And you have like new players, team techs trying to grow on-demand deposits, sometimes offering higher yields. I guess it's too early, but are you seeing any pressure on that front or not a big deal?

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

Not at all.

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

The next question is from Ernesto Gabilondo from Bank of America.

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

My first question is a follow-up on NIMs, so if keeping the MXN 4 billion reclassification at the NII level, I think you were guiding before NIM expansion between 20 to 50 basis points. So if keeping again the MXN 4 billion at NII, how should we be the NIM expansion this year? And given that you are reducing the sensitivity to interest rates, how should we think about the NIMs next year? Could they be stable or with modest NIM pressure? Any insight will be very helpful. And then my second question is on your new digital bank. We have seen that the regulator has approved, the digital banking license for [Hey Bank] and for Openbank, so when do you expect (inaudible) to be open to the market? And what would be (inaudible) key differentiators against the new digital banks?

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

Ernesto, the first one would be 10 basis points more. That would be the effect of the MXN 4 billion on that part. What you will see on the margin next year, I think it will be a very stable situation from the margin, maybe from -- if you ask me what would be a conservative view, it will be around 6.3% to 6.5% for the bank because everything that we have been building up on the fixed rate part of the group, we will protect us on that part. And also the funding side as Yuri just mentioned, continue to really move into the -- a nice pace on that part. So I think the reduction in the funding cost plus the fixed-rate part of the group that will continue to deliver pretty good returns, I think, allow us to have a margin from 6.3% to 6.5%. But I think most part of the year will be more around the 6.4% net interest margin for the bank on that part.

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

Excellent. And in the digital bank?

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

The digital bank, I would love to give you a lot of information about the digital bank, but I think it will be a very positive surprise when we launch into the market. Everything is being set up ready as soon as we get the go from the authorities. And now we are seeing when will be the best time to launch once we get the approval. But by the way it has been very helpful there, the authorities going into this process. So basically, I will compromise most of the strategy if I open the book now. So sorry for being a little bit closed on that.

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

Thank you. Now we will continue with Luis Yance.

Luis Yance ***Compass Group PLC - CIO of Compass Mexico & Portfolio Manager of The Local Equity Strategies***

I'd like to go back to the change in guidance on the NIM for the bank specifically, and I appreciate all the color around, the annuities. But help us understand what were the assumptions back then to think initially, you thought perhaps at the high end, you could have gotten to a 7% NIM, right? And right now, we're at 6.5%. So just trying to understand what were the assumptions that could have gotten you to 7% on the bank name that perhaps you're no longer expecting, were you sort of thinking that the funding cost pressure was not going to be as big or something trying to understand that because it looks like the average rate that you're assuming for this year is higher than the previous guidance, therefore, that's supposed to be good. You're growing faster on the right segments, so the mix should be helping you. So trying to reconcile the negative changing guidance on the NIM of the bank specifically for this year?

And perhaps a bigger question there is I would have thought that as rates peak, which we could argue perhaps the peak is this quarter with TA still going up this quarter sequentially. And if rates don't walk anymore, this is kind of the peak, so if that's the case, I would have thought perhaps a quarter or 2 after that, we would have seen the peak in the bank profitability. However, it looks like NIMs may have peaked in the fourth quarter, ROEs may have picked in the first quarter. And based on your guidance, it looks like that was kind of the case. It's actually the opposite which surprised me. Did that surprise you or not? Or how are you thinking about that? That will be my first question.

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

I think the first thing that you have to see is that we never expect to have the loan growth that we have. And also if you look at the guidance, basically was 5% to 7% loan growth. And that was with a very sound funding mix on the cost side that was very close to 38.5%, 39.5% we said this. Then the movement started to peak on the lending side and also the demand for more returns on the time deposit side. Even though you have pretty strong growth on time deposits and more than strong growth in the commercial part and the consumer part of the group.

You have to fund those and the competition for funding in the market, obviously went off on that part. Even if we still a very strong funding mix, but I mean to move from 38.5% to 41% was a big jump, to move to 43% was another jump. Then you will start to see that number coming back from the 43% back again close to the 41% at the end of the year. But that was difficult really to provide based upon the pace of growth on the lending side and also the competition for the funding side. And we saw a big opportunity on the market to bring clients that would demand more returns on the funding, but give us a much better relationship.

That's as simple as that, it's simple math, 38.5%. Now if you look at 43%, based upon the pace of the loan growth and the funding growth and the cost of the funding on the time deposits from 3% growth on time deposits to 8% growth on time deposits that is explained. But if you go to NII, and you at loan-to-deposits is growing 25%, the NIM is growing 24%, but the NII on loan-to-deposits is 24%, and the spread on the book still is very positive.

Obviously, when you see the number, just the margin on the number from -- we're very close to 7%, that it was very positive, very possible based upon the initial guidance that we have. Now based upon, I think we are in a much better position with a much important loan book with a very profitable loan book and we are very rich clients that we like to have in our book in order to build up relationships. So it's a game theory in this part. I mean, it's not a zero-sum game on this part. So we balance this based upon the pace of growth on the loan book and the demand of the funding side. We went up to 43% cost of funds, yes, we will go down, but we already have the loans. So that was the -- I think that was the strategy on this part.

Luis Yance ***Compass Group PLC - CIO of Compass Mexico & Portfolio Manager of The Local Equity Strategies***

Understood. Thanks for the detail estimation.

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

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

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

My first question is on your AT1 capital. And of course, you do have a lot of capital, we are going to agree on that. But if I look at the -- I mean, the AT1 capital, the purpose have been in dollar terms, fixed the $3.2 billion over the last 4 quarters, $3.2 billion. But yet, the contribution to capital has declined by about 180 basis points to 600 basis points as of the end of this quarter, which for almost any other bank, that would be kind of a huge deal losing 180 basis points of capital.

I wanted to ask you, and clearly, this has been driven by the appreciation of the peso versus the dollar, have you hedged that FX exposure on your dollar purpose? So that's my first question. And then second question, kind of a follow-up on the question, the first question that I think Gustavo was asking. In the past, you have kind of highlighted a potential extraordinary dividend payment before the end of this year. Wanted to ask if there's an update on that. And more importantly, what would be your target of common equity Tier 1 by the end of this year after paying that extraordinary dividend?

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

I will start for the second one. We already are paying this extraordinary dividend of MXN 15 billion and so far, that's it, we don't have anything nice to give, until the next year, I don't know. The first one, yes, we have some kind of hedge and...

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

Yes. I think what you mentioned is correct. That really shows you the capability of the bank to be. And I think it's very important what you mentioned because sometimes people thinks about -- that the AT1, we are very dependent on the -- no, I think the AT1s are very instrumental for us to compete in the market on the dollar group. We hedge to call those on day 1. Obviously, there has been an effect on the currency rate that we have. But as you mentioned, if you see the strength of the capital numbers of this bank and the capacity to manage this it really shows how careful we are with the balance sheet in this part. The numbers that you will see once we pay the dividend by the end of the year, we basically the same numbers that you are looking now at this part. And what will be a [EDL] number for the core Tier 1 and we have adjusted this to 13%, we will convert to that in the coming months and year.

We will like to be at around the 13%. We hope the world will become more easy, more peaceful and then we can really understand a lot of the economic things that are moving around. And now that you asked about the AT1s. The other day, people were asking that if we -- and you know by law, we cannot say we honor the call or not. But let me just give you one note to some people that aren't concerned about that. The only source that we have for capital -- regulatory capital instruments are the AT1s or the AT2. We are not playing in any game to sacrifice our entrance to that market in any way. That's the only thing that I would say about the AT1s.

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

Very clear, Rafa. Maybe just one follow-up there. So if I take out MXN 15 billion from your common equity Tier 1, I get to roughly 13.8% CET1. You are saying by the end of this year, you expect to go back to the number you reported -- roughly the number you reported at the end of June because of organic capital generation or...

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

Yes, very close to the 15%.

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

Not only the bank that provides dividend, the group has cash and receive money from the subsidiaries. So yes, as Rafa mentioned is 15% with the mid part of the guidance.

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

Okay. And one last question then. If the peso continues appreciating versus the dollar, we should expect that AT1 contribution to continue declining EBIT just because of that FX translation.

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

Yes.

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

We'll continue with Olavo Arthuzo from UBS.

Olavo Arthuzo Duarte ***UBS Investment Bank, Research Division - Research Analyst***

Actually, I just have one and sorry, because I wasn't able to hear the entire call. But I just want to follow up on your digital bank initiative, the bineo, and thank you for disclosing our new guidance. But basically, I wanted to have another date on this because you guys have been mentioning in the press the target of 3 million customers. And if I'm not wrong, the bank stated at the beginning of this year, the expectation for this initiative to represent something like 5% through 7% of the bank's income in less than 5 years. So I'm just trying to understand the potential here, is that 5% through 7% still valid? And in terms of credit portfolio, I understand the focus should be on consumer loans, but how much big the portfolio could be? This would help us a lot. Thank you.

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

Thank you, Yes, we will start the operations of bineo as soon as the first quarter of next year. We are in the final details and the strategy and all this, and it should move a little bit, the numbers. Rafa, you...

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

I think if you look at 7% of the net income of the group, you are looking at a pretty high number. I mean you are looking at our net income at that point in time that we want to reach that -- the 3 million clients on that part. You're really looking at a very, very high number. I think it will be a very positive surprise, the digital bank because we will really like to run that with a cost-of-income ratio very low, 25%, a full segmentation bank that could reach any segment of the Mexican population or financial inclusion will be very present. And based upon everything that we have on the risk models and everything, I think it will be a pretty good story about that, not just on the cost side and the cost-income side, but I mean 7% of our group that will be delivered at that point in time, a pretty high number will be, I think, more bigger than most of the medium banks that you currently have in Mexico.

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

Thank you. Now we will continue with Jose (inaudible) from Citi.

Unidentified Analyst

Just a quick follow-up. If I understood correctly, one of the means for cost of funds, which is 43% offset to go down would be based in your lower needs for funding as you have already like secured, so to speak, some of that funding in it. So that would be one of the mechanism, I just wanted to confirm if that's correct. And also, just wanted to kind of like tie or link the dots with the bank's NIM guidance. So if I'm understanding it correctly, despite that improvement in cost of funds and despite stronger loan growth, potentially better mix, that would still not be enough to offset what I would believe are still funding cost pressures and hence, the slight trim in NIM of the bank. Would that be the correct way to think about it?

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

No, I think part of the question is right. I think the funding will go down faster than the assets part of the book. But the variable rate part of the book will start trending down because on contractual terms follow the drop in the interest rates. Remember that we have 56%, 57% of the book in variable rates. So even though we have a very strong mix now on the consumer, and it will be a balance in that. How fast we can lower the funding cost of the overall portfolio, I think that will be the key to see how fast we can really improve or sustain the margin the way we are.

We don't know exactly, we are playing all the levers in order to be ready for that. But I think it would be a play in the market. It will be something that the market will follow how fast the funding rates on the market start to go down. I think that will be the key part.

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

Before we continue, I think we need to limit to one question because we are receiving more and more questions and people on the line. If somebody needs to disconnect, you send us an email, I'm happy to connect after the call with you. Also we're receiving a lot of chats for clarification on the dividend. So I would just like to give the details that have been discussed earlier is MXN 15 billion we proposed to the assembly. The payout ratio for the full year is around 83% and is around MXN 5.2 per share. So these are questions we're receiving, so we hope we can clarify that. Thank you.

Now we'll go with Carlos Gomez from HSBC.

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

Thank you also for the updated guidance and for the dividend. So quickly, because it's getting too late. Can you give us an idea of what you expect for Mexico and for the bank, not for this year, but for the next 5 or 6 years? You say that you are already growing very strongly. Do you expect that growth to continue for the next 2, 3 years? What can we realistically expect not in terms of ROE, but in terms of loan growth and earnings growth for the coming 6 years for Mexico and for Banorte?

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

I think ROE, as we mentioned, loan growth, I think 10% to 20% is very feasible for us to continue to grow in that part. And net income, as we promised on the Investor Day, that will be double-digit number for net income.

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

We'll now go with [Kiran Nagesh] from WhiteOak Capital.

Unidentified Analyst

I wanted to get a bit more color on the loan growth. We've been printing more than 10% Y-o-Y loan growth for at least 3 quarters now. I wanted to understand, especially from the consumer side, is it coming from customers who are new to the bank? Or is it coming from increased lending to the existing customers of the bank. And on the side of commercial loans, are they more into working capital loans or fixed investment loans?

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

The first one is coming from both, from new to the bank and also to increasing the relationship that we currently have with the current banks based upon the hyper personalization process that we are moving on that front. On the commercial side, in both ways, you take the capital part and also the -- to increase your stock for working capital lines. So I would not say that is one or the other is all over on that part.

Unidentified Analyst

On the consumer side, just following up, among the customers who are new to the bank, what percentage might be new to the financial system itself? I mean are we doing any loans to customers that it might be the first formal loan they are taking?

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

I think the way we manage that is through the payroll. The payroll is for many -- the first relationship that they have with the bank. Once they get into the bank with the payroll, we start looking at the behavior of the accounts and things and then we start originating the lending side. So that's the most healthy way to financial inclusion into the credit cycle of the clients.

We also take our launch on the personnel side. But if you look at the numbers on the personal loans, are very small on that part. We rather graduate the clients through the payroll and then the payroll loan and then continue to go through a cycle on the car loans and then the credit cards and things so that's the way we manage the risk, and that's the way we manage the clients through the risk cycle in the bank.

Unidentified Analyst

And one last quick question about asset quality, if I may. So we have seen a very stable NPL ratios and write-offs. Now should we adjust for any restructuring or refinancing or portfolio sales among these NPLs or are they all baked into the NPL numbers that we see in the presentation? That's my last question.

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

What you see is what you get, nothing out of the ordinary. It's exactly what it is.

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

Now we'll continue with Natalia (inaudible) from JPMorgan.

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

Natalia can you hear us?

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

Maybe not, we can come back and we will continue to...

Unidentified Analyst

Can you hear me now?

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

Yes, I can.

Unidentified Analyst

Okay. Sorry. So I'll be quick. Just going back to your AT1s and Tier 2s. Another way to build capital is through the issuance of Tier 2. So how are you thinking about -- if you're like replacing your AT1s, how are you thinking about this? Are you planning to replenish with AT1s? Or are you thinking about Tier 2s? And how are you thinking about issuance in general?

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

We do not plan to replace AT1s. They have been very effective for us. And that's why we take care of lot -- we are saying that it's very important for us to take care of that. So far that's it, Rafa?

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

Yes, Natalia. And as we mentioned before, if there's an opportunity in the market for the Tier 2s or anything else that we see that is potentially beneficial for us on the structure of the balance sheet, we are not close to anything. We look at opportunities in the market. We raised the AT1s, prepare AT2. If it's a green bond that we are actively looking into those. Also senior, we look at every single opportunity and we take the best one for the group.

Unidentified Analyst

Right. But would you be open for Tier 2 because I remember that in the past you didn't like the structure too much?

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

Yes. I think honestly, the AT1s are much more efficient for us. But the AT2, if there's a window of opportunity for AT2, we will use it.

Unidentified Analyst

Right. And then you could reduce your AT1 stock with perhaps a little bit more of Tier 2s.

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

Yes. We have two more. So please let's focus on one question per individual and happy to connect after the call.

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

Yes, we'll go with Edson Murguia from (inaudible).

Edson Murguia

My question is regarding on the loan book growth, just trying to understand how do you manage the process of origination change? Because on an annual basis, basically to grow on a double digit, mostly in every segment, but the NPL is staying the same. It's 1.7% NPL. So I was wondering what changed. How do you manage this? Because for me, my reason, it doesn't match the loan growth and the NPL in the same stage.

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

Mr. Salazar.

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

Yes. I will tell you that we did make a change for the better. We are getting more selective in the wholesale side of the bank and more selective in the retail side of the bank. So contrary to popular belief, we are not playing a trade-off between credit or loan growth versus credit quality. We're forbidden to do that, and you can see those in any graph that you want to see, like [Imara] and our NPLs, you will see loan growth without jeopardizing credit quality.

Edson Murguia

But on a fundamental level, you did not change the process? It's the same, but your remarks (inaudible).

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

(inaudible) process from origination to collection, all the phases remain the same. They have been optimized in order to hyper-personalize and contain a better attention and service to our customers, but there is no any risk variable involved in that process or that redesign or reengineering credit process.

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

Thank you and we'll take our last question from [Federico Galassi].

Unidentified Analyst

Just a quick question, Marcos and Rafa. How do you balance the loan growth and capital ratio growing at this level, is some level that affects the capital ratio for this year or next year or you can continue to grow faster than we are seeing now?

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

It's a dynamic process.

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

Yes, at this level and with this level of loan book we need to grow around 17% or 18% to start consuming capital. So that's why the number we projected for CET1 is around 15% with increase in the loan growth guidance.

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

Thank you, everyone, for your interest in Banorte. With this, we conclude our presentation. Thank you very much.

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