Q3 2024 Earnings Call

Company Participants

- Alejandro Padilla, Chief Economist and Managing Director of Research
- Gerardo C. Salazar Viezca, Chief Credit and Risk Officer
- Jose Francisco Martha Gonzalez, MD of Digital Businesses
- Jose Marcos Ramirez Miguel, Chief Executive Officer
- Rafael Arana de la Garza, Chief Operating Officer & Chief Financial Officer
- Tomas Lozano, Head of investor relation

Other Participants

- Andres Soto, Analyst, Santander
- Carlos Gomez-Lopez, Analyst, HSBC
- Eduardo Rosman, Analyst, BTG
- Ernesto Gabilondo, Analyst, Bank of America
- Jorge Kuri, Analyst, Morgan Stanley
- Nicolas Riva, Analyst, Bank of America
- Olavo Arthuzo, Analyst, UBS
- Renato Meloni, Analyst, Autonomous
- Thiago Batista, Analyst, UBS
- Tito Labarta, Analyst, Goldman Sachs
- Unidentified Participant

Presentation

Operator

(Starts Abruptly). We'll move to the Earnings. Moving to the presentation with our CEO, Marco Ramirez, who will provide an update of the political and macroeconomic events that surrounded our third quarter's operation, followed by an overview of the Group's main results, our quarterly update on sustainability, as well as details on our capital and an update on the shares we bought through the buyback program.

Then Rafael Arana, our COO, will walk us through the evolution of the margin and balance sheet sensitivity as well as details on asset quality and efficiency, among other relevant updates. 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 two 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 {BIO 4413879 <GO>}

Thank you, Tomas. Good morning, everyone. Thank you for joining us today. The third quarter of the year showed a sound evolution for Banorte regardless of the current operation -- operating environment. High-frequency economic data continued to show signs of a slowdown, thus bringing us to adjust our GDP growth expectation for 2024 to 1.3%. Nevertheless, we still perceive a strong inertia in domestic demand driven by resilient consumer fundamentals. For 2025, we forecast GDP growth of 1% given the current global headwinds despite the Mexican resilience derived from its high dependence to the US. Annual headline inflation continues to trend down, yet it is still above the central bank's target of 3%. Nevertheless, core inflation decreased for the 20th consecutive month and it's already within Banxico variability range. We estimate inflation to end the year at 4.7% and 4.4% in 2025. Regarding monetary policy, we expect, we expect two additional cuts this year, reaching 10% by December and 200 basis point or basis points cut throughout 2025, reaching 8% by the end of next year. Volatility in the Mexican currency is expected to persist mostly given the uncertainty regarding the upcoming US elections in November.

As a result, we forecast MXN0.909 per dollar by the end of 2024 and MXN20.9 in, in 2025. On the political front, Claudia Sheinbaum took office at the beginning of October. And during her initial speech, the President reinforced the importance of, one, sustaining healthy fiscal policies. Two, enhancing and protecting local and foreign investments in the country. Three, collaborating with the private sector and infrastructure projects through public, private associations. Four, preserving the strong relationship with the United States and Canada to boost nearshoring. And five, maintaining the autonomy of the Central Bank. So far, her administration has held discussions with both Mexican and foreign business leaders to foster trust-based relationships among the different stakeholders.

Moreover, the unveiling of the economic package of 2025 on November 15 [ph] should provide for an insight about the investments and fiscal priorities of her administration. Let's focus now on the result of the quarter on slide number three. The sound performance of the Group was driven by expansion in the loan portfolio, resilient margins and larger net fees. Notably, despite greater loan origination in our consumer book, asset quality remained solid with NPLs stable at 1% and cost of risk slightly down to 1.6%, evolving better than expected, given healthy behavior of new vintages in our different portfolios and the calibration of our internal movements.

NII sensitivity in the local currency balance sheet have become almost neutral to monetary cycles, decreasing to MXN36 million for every 100 basis-point change in the reference rate and reaching MXN531 million in the foreign currency book, further shielding our balance sheet from the easing cycle and increasing our reliance in selective lending and stable deposit volumes. Raf Arana will provide more details on this. Our strong capital adequacy ratio stood at 19.2%. Later in the call, I will go deeper into our strategy for capital optimization.

Slide number 4, net income continues to grow, showing a 7% year-on-year increase to MXN14.2 billion. Additionally, accumulated net income for 2024 reached MXN42.5 billion, 8% higher versus the same period of last year, driven by the expansion across most business lines, reflected on a 150 basis-point increase in ROE to 22.7%.

On slide number five, the quarter results by subsidiary show relevant contributions for all sectors. The bank's net income remained relatively flat in the quarter, mostly related to lower non-interest income despite good core banking dynamics. With accumulated figures, net income from the bank grew 7%, driven by loan volume and mix as well as positive evolution of net fees. Operating expenses grew in line with our expectations for the year. Altogether, these results yielded a sound 29.5% ROE for the bank, up 180 basis points versus the same period of last year. Our insurance business grew 28% in the cumulative comparison, driven by greater premium growth in the corporate and government sectors.

Annuities expanded 11% in the quarter, normalizing the effect of inflation-related movements observed during the second quarter. With accumulated figures, it showed 17% growth, given its greater participation in social security allocations. The brokerage sector's quarterly and annual increases were mostly explained by securities valuation and larger business operations. As for the Afore business, its performance was driven by higher yields from financial products.

Slide number 6, the loan portfolio continues to expand, reporting double-digit growth. The corporate book had a remarkable 24% year-on-year growth followed by commercial with 10%, driven by greater business activity across multiple sectors as well as our ongoing efforts to strengthen relationships with SMEs, which are starting to capitalize from our investments in the segment. During the quarter, FX variation had a positive impact for the dollar loan book, representing 14% of our total portfolio. Our government book grew 2% in the year, impacted by some prepayments. The consumer portfolio on slide number seven continues to show double-digit growth. Credit cards were up 26% in the year due to greater transactionality. It is worth mentioning that during the third quarter, we were launching two new products addressing the revolving credit needs for our payroll holders as well as those of younger demographics. These products are expected to help us develop comprehensive relationships with these clientele -- clients. Nevertheless, nevertheless, we maintain our cautious approach in credit cards to avoid compromising our asset quality metrics. The Auto portfolio held a similar pace, increasing 23% year on year, mainly driven by our current commercial alliances with different dealerships and ongoing positive dynamics in that sector.

Payroll loans grew 9% in the year despite our prudent approach to clients in government entities with administration changes related to elections. Finally, mortgage loans showed a 7% annual expansion, keeping our focus on building a stronger high lifetime value clientele.

On slide number 8, asset quality remained solid in the quarter with NPLs relatively stable at 1% despite our higher growth in the consumer segment. It is noteworthy that cost of risk has gone down driven by the assertiveness of our internal models and our hyper personalization efforts to engage with high-value customers with better risk profiles that limit unexpected losses.

Fees on slide number nine grew 7% in the quarter, mainly due to greater core banking fees and transactionality in investment funds. With accumulated figures, net fees grew 20%, led by higher activity in consumer products and related businesses, supported by a still strong private consumption. Furthermore, we continue to increase our digital transactions. As of the third quarter of the year, the number of digital active clients grew 11% versus the third quarter of 2023.

Turning to slide number 10. We are proud of our NPS, Net Promoter score evolution, which remains on track to achieve a 90 point NPS score. The enhancement of our digital capabilities, which enable us to operate as a digital bank with branches, together with the strength of our human digital interactions is what differentiates us holding that competitive advantage in the market. Our self-service capabilities are driving value added in personal experiences, reflected in the high NPS score in all our interactions through different channels. Once again, this demonstrates that our investments in technology and hyper personalization are trading off, creating a differentiated engagement with our customers. This was recognized by The Banker granting us its Most Innovative Bank in Latin America who are -- in 2024 and many other worldwide acknowledgments emphasizing the innovation, usefulness and transformation in our -- in the digital initiatives. Shifting gears to ESG. On slide number 11, I would like to highlight Banorte's participation in the 17th Annual Financial Education week, where we have the chance to share financial education essentials and interact with a diverse audience of more than 2,700 students and young professionals, highlighting the importance of creating a budget, the benefits of starting a savings culture and the relevance of keeping a healthy credit score among other topics.

On the environmental front, we continue with our efforts to grow our sustainable finance book using the proceeds of the green and social bonds issued earlier this year. Regarding the operation of our buyback program, we have already bought back MXN10.7 billion out of the available MXN (inaudible) billion, representing an approximate 70.3 billion shares. This morning, we called for a shareholders meeting to propose their cancellation. Our capital allocation strategy focuses on providing the highest possible total return to our shareholders, considering the best balance between buybacks and extraordinary dividends.

Last but not least, I'm proud to share with you that Grupo Financiero Banorte is celebrating 125 years of operation in the market, 125 years of transforming, strengthening and committing to our country, growing together with Mexico, most importantly with you, our stakeholders. What started as a small bank in Monterrey in 1899 has now become one of the leading financial groups in Mexico. Our business participation, our transformation through technological and digital developments, our customer-centric model and most importantly, the flexibility of that differentiated working culture have been among our strongest assets to move forward in both gray and blue skies alike.

Looking ahead, our focus on hyper personalization, diligence, and risk management, strict operational efficiency together with our continuous investment in technology and human capital will keep Banorte as a strong and competitive franchise to face both traditional and digital players in the market. I would like to thank you for your support and trust throughout this journey, and we look forward to many more years of development and growth. Now, I will leave you with Raf Arana, who will walk in to detail of the financial results of the quarter. Rafa, please go ahead.

Rafael Arana de la Garza {BIO 22681143 <GO>}

Thank you, Marcos, and thank you all for attending the conference. As Marcos mentioned, and I will just provide the most important metrics about the bank and also some of the metrics about the group. The balance sheet continues to be our main strength on how we have built the balance sheet in order to support and be able to take advantage of the downward trend on the rates as you can see and there's something important to notice about this. Some people has questioned that if we were not so fast in a -- in really positioning the balance sheet on the, on downward trend, I will say that it's difficult to put the right timeframe to do that, but what we can see now is that the direction and the strategy was exactly the right one.

That -- and this is also quite important. This has cost us around MXN2 billion to position the balance sheet. But if you project the already benefit of that positioning for the next year, we're already at the rates as is today is giving us close to MXN1.8 billion in additional margin for the next year. So it's like we pay for one year and we will get the benefit for the next five years based upon the tenure that we have on the -- on the fixed-rate part of the book. So that's important to notice about the balance sheet.

The second one is that the Group continues to deliver pretty strong return on equity, 22.9 and that's not on a, on a tangible basis. If you go on tangible and you take out the goodwill of the -- on the, on the Afore business, the goodwill of the Group will, will jump very close to 2024 return on equity. The bank is producing 31.1% as Marcos mentioned, 2022, it was close to 228 basis points compared to the last year. This is also considering that we are still holding 13.9 on the core tier 1. So that really shows the efficiency of how do we manage the capital base and the, and the balance sheet and all the results that provide that benefit for the, for the bank. The transformation for the bank as Marcos mentioned is a day -- it's, it's a day, day-to-day operation of the bank.

We are in a continuous transformation. Marcos showed the, the graph that shows the banking menus, that shows that Banorte is really a digital bank that can compete with anyone that comes into the -- into the digital space. And that, that position ourselves that the NPS continues to grow in the right direction. The clients like the way they, they, they deal with the bank and the branches. The branches continue to keep -- improving the, the NPS on a daily basis. And the digital operations and the digital self-serve capacity of the bank also continues to improve the NPS on a channel-by-channel basis. The net interest margin of the Group is at 6.5%, pretty strong, if you look 77 basis points compared to last year. And what is also remarkable is the Banorte Bank, that is at 6.7%. Some people is, is, is concerned about how we can continue to expand the margin even when the interest rates go down.

And it has to do with the position of the balance sheet and the fixed rate part of the book and also the good trending, funding costs that we now are experiencing based upon how we are managing the funding base of the bank that I will go in a minute how the, the funding base is, is producing pretty strong returns on the margin side, but also giving us a pretty strong foundation on non-interest bearing deposits, interest-bearing deposits, time deposits and also if we need to go to the market for specific reasons, also we go to the market with our very strong benefit for Banorte. So, the funding base, liquidity funding is trending in the right direction and is going to continue to improve the margin as we, as we, as we go towards the end of this year and on the next year.

The capital, the capital base has already been explained, 13.9 at core tier 1 after -- and this is, this is quite important after we or on the call that we that, we did on the, on the, on the core, on the tier 1 and also by funding the dividends of the group, most of those dividends. So, that continues to be a very strong core tier 1. Obviously, there's concern that it's too much and that we should return the money on the, on the, on the balance sheet for the, for the investors. Obviously, we're always looking to really return the most value to our investors. And that could be on a buyback basis or also it could eventually potentially be an extraordinary dividend, but we have to wait to see how the macroeconomics and the US elections really happens.

So, so, Banorte is a position to manage either way on, on that part. And that's, that's quite important because that flexibility, we have achieved that flexibility by managing the bank in a very conservative way, but also in a very high growth, growth pace. When you go to the net interest income of the bank, of the Group, we will go in a minute for the bank, but you could see on the, on the, on the non-interest income growing. The annuity effects continues to confuse some of our investors, but I think there's a very detailed explanation on the, on the pages, on the report. But what is, is worth mentioning is that our net, net NII of loans and deposits increased on a quarter-to-quarter basis, 4% and that's a very, very strong number to have on the, on the loans, on deposits. So, I would say that NII is trending in the right direction, and everything concerning the revenue side. Also, next, we will see in a minute how the fees are evolving. But what we can really say is that we have a very productive loan base and a very, very sound funding base that is continuously trending in the right direction to our lower cost on the funding side.

If, if you go to the ratios of the bank, it will show you basically, as we mentioned, the margin of the bank at 6.7% coming from 6.4%. That, that really shows all this management that we have been doing on the funding, on the, on the loan growth and how we position ourselves in the market. And this is quite important, when you look at how Banorte is positioned in the market, we are never on the high end of the price base. We are always on the mid to the low end of the price. We never compete on price. We compete on the service and on the risks that we like to serve the clients. The NII of the, of the Banorte Bank, as you can see, 7% on a year-to-year basis is a quite good trend and that trend will continue as we go through the end of the year and on, on the next year.

Net fees are very, very strong numbers. And it shows exactly why the bank continues to evolve in the right direction because we are transforming more and more, the activity of the bank in a very productive way, opening of new accounts, transactional banking, services fees from the commercial, for the corporate, for the government base. All the bank is, is performing this activity every single day in a much more productive activity. Not just activity, but really activity that is profitable for us and serving our clients in the right, in the right way. It's not that we are increasing the cost of the fee on the price of the fees, it's really the activity that the bank is producing in the market. We are gaining market, we are gaining clients.

The clients like the way they, they interact with the, with the bank and that is giving us a pretty strong growth on the, on the fees. It's not because we, we increase the price on the, on the fees. If we go to the -- I would say -- and this has to do with a lot of work for many people at the bank, the treasury, the risk, accounting, everyone looking at how to really position ourselves in the right direction for the downward trend on the rates. You can see now that the sensitivity on the peso book is only at 36 -- MXN36 million that basically we are on a neutral basis on the, on the sensitivity. So, the balance sheet has been managed on the way up of the rates, in the right direction, and the downward trend of the rates also in the right direction. So to position the bank on a neutral basis has cost us some money, but it will give us money for the next five years at least.

On the, on the, on the foreign currency, we will start to also be more aggressive on, on reducing the sensitivity. There are more tools to use on the, on the foreign currency balance sheet. I don't -- we start -- we need still to see how aggressive the Fed is going to be, if it's going to be 25 or 50 basis points downward trend. But when you look at the sensitivity on the NII, we almost erased the sensitivity on the NII. And that's, that's not easy to do and that's, that's something that, that is, is the result of very, very intelligent work of many people at Banorte.

The next one really shows some of the key metrics, the, the return on assets, 2.6 is a very strong number, 2.6. The net income of the bank, 7% on a year-to-year basis, and also, I will also try to address that the net income of the bank is already being affected by the foregone interest that -- and not just the, the bank, the Group for the foregone interest on the buyback program that is close to MXN570 million and will by the end of the year reach around MXN650 million on a, on a, on a reduction on the margin base.

The return on equity of the bank as well, as we mentioned before, 31.1% with a very strong capital base. So that really gives, gives you the idea the -- that how efficient are the management of I would say how do we use the capital to, to improve the return, the returns of the bank in every single space of the, of the bank. If we move to the next one, the managerial NIM, that's, that's in order too because some of you has asked us to extract the annuities effect on the, on the NIM. And you can see on the, on the graph the NIM with ex-insurance and annuities in order to have a much more rational number that is not depending on the, on the inflation base and affection of the -- and the effect on the annuities. The cost of funds and this is a -- even if you will see that even if you will, you will see that -- it shows that -- it, it seems that the cost of funds jump to 49.3, but that has to do with the pace of reduction of the, of the sectors compared to tier. The centers, most of the time deposits are linked to the center space. So when the center starts to, to go down, we have to wait for -- some people put the time deposit to 30 days, other people to 60 days or to 90 days or 120 days. So, you need to get all the process ongoing. So you will see a continuous downward trend that will -- the PA will eventually chase the, the center. And the center will erase the lagging effect that it has on this renewal of the, of the time deposit base because every time that you, you basically go on a fixed rate on the time deposit, you have to wait for the renewal at 90, 20 or 30 days or 45 days.

So, that's what you, you see as, as a small pickup on the, on the funding cost. But when you look at the margin base and improving the margin, that really shows exactly how we are managing the asset side and funding side that give us a better margin than, than expected. Another very important thing is that non-interest bearing deposits are growing 8% on a year-to-year basis because there has been some questions about the effect of the -- of some of the announcement of the new bank or other -- of the new banks or try to be banks in, in the market. What's the effect? As you can see, we continue to, to gather non-interest bearing deposit at a very good pace, 8% on a year-to-year basis.

And time deposits are growing close to 20% and time deposits are well below the rates that, that some of those players are playing in the market. Why? Because we base our -- on a, on a relationship base, not on a product by product base. So, when the when a client comes to the bank, it gets a full suite of products that he can monetize and see that they get a much better deal when they monetize on their relationship with us. Okay. So funding is pretty, pretty strong, growing in the right direction at a good pace, at the right cost. So now we will move to one of --

what some people are -- are of quite, I would say concerned about how sustainable these, these numbers you know on the, on the risk side.

And when you look at the graph on the cost of risk, and I will ask Gerardo in a minute to, to please join us on the conversation. Cost of risk continues to go down in a very important way and in a steady way. And at the same time, you see that loan growth is exactly what we produced on the guidance to be 13% ex, ex-government. So we have very sound loan growth and the cost of risk continues to go in the right direction. Write-off rates is very steady. We are not a bank that jumps and cleans the book on a, on a, on a, I would say on non-program basis. So, we are very steady on the on write-off rates and credit provisions are right on line what we expect, below what we expected at the beginning of the year. And so these numbers also take into account that if you take away Banorte Futuro [ph] we're at 1.5, and then at Banorte Futuro [ph] we're at 1.7.

So on the cost of risk, I will not say more because I will let, let Gerardo say it, but this is, this is something that Banorte has shown that it's not just you know one, one, one-time effect. It's a continuous effect of how do we manage the bank. Please, Gerardo.

Gerardo C. Salazar Viezca {BIO 16248253 <GO>}

Yes. Thank you, Rafael. Good morning, everyone. Over the past several years, our commitment to the loan quality has yielded, as you can see such exceptional results demonstrating the strength and resilience of our portfolio. Through prudent underwriting and robust risk management, we have successfully maintained a high standard of performance even amidst changing economic conditions. I will say that this success reinforces our confidence in our approach, not only for current stability, but as a sustainable model for the future. And we remain focused on long-term growth, ensuring our lending practices continue to deliver value to our stakeholders as well as supporting the broader financial well-being of our -- of the communities we are serving.

Together, we look forward for building on this strong foundation for years to come. And additionally, let me emphasize the importance of regulator-approved internal risk -- great risk models. Their contribution has been very relevant because, regarding loan origination, portfolio management and loan recovery processes, this contribution has been substantial. These models have been providing structured, reliable and compliant frameworks for, for managing credit risk, operational efficiency and portfolio performance. They support profitability, stability and risk mitigation. And I will say that after years of work, our loan quality metrics are very stable, as Rafa was telling, telling you and also have been predictable and better than ever.

Rafael Arana de la Garza {BIO 22681143 <GO>}

And I would like also to, to say that our, our model of hyper personalization is, is -- the, the foundation is the risk by, by client, not by product anymore. And that will give us a very, a very, very I would say, a big difference in the market when you address by client and not by product, the, the, the risk base. So everything on the bank, the foundation of the bank that we deliver to the client is based upon sound risk metrics. If we like the risk, we like the client and we can even be very aggressive on how we can and sometimes sacrifice some margin in order to, to bring the clients that we would like to have at the bank.

On the expense -- on the expense side, as you can see, we are at 35.5% cost-to-income ratio. Some people has asked us, we had a meeting yesterday and said, what would be the cost-to-income ratio if you go to recurrent basis and, and, and ex targets at Futuro and Vinoyo [ph], the cost-to-income ratio will be 33.7. That will be the cost-to-income ratio that we will have.

So the recurring expenses is 7.3 and 5.2 is the extraordinary expenses coming from Vinoyo and (inaudible) Futuro. So the, the, the operating leverage continues to be very positive and we will continue to have that operating leverage in a positive way. So the cost-to-income ratio, I think we are peaking at a cost-to-income ratio cost. We will continue to push that number down for the next, for the next year. The bank's regulatory capital, as you can see, it's at 13.9% at core tier-1, 19.2% overall capital ratio, well above the TLAC requirements and this is the -- this is really shows, as I mentioned at the beginning after the AT1 call.

So, that really shows you the capacity of the bank to generate our capital. I will address now the issue about dividends and buybacks. We have been, as Marcos mentioned, at very, I would say active on the, on the buyback program. And some people say, why you don't activate more the buyback program. The buyback program allow us to go up to MXN32billion. We have used around MXN10.7 billion and that's a strategic tool for us to try to -- to defend the value of, of the share. At this point in time, there are several I would say, issues that needs to come clear for us in the next month, and in the next month. One is the US elections, another one is the presentation of the budget in, in, in Mexico.

What exactly will be the, the, the programs that the President has announced that we think will allow the market to become much more confident about Mexico in the, in the coming, in the coming weeks. But we have all the tools to manage the best return for the, for the shareholders. If we see a space after these events to go for an extraordinary dividend, we will do that. If we need to reactivate and activate the, the, the buyback program, we will activate the buyback program.

So, we have all the tools in our hands. So don't -- don't think that we are being, I would say, not looking at the market in a, in a very, in a very close, close way. We are very, very attentive of how the market behaves, but we also understand that there are many issues that are not under control that needs to be clarified in the next weeks, weeks, not months, weeks. And I will be very, very clear about, about that. So now let me move into the, into the guidance because there have been some questions about the guidance.

The guidance, basically the loan growth as we mentioned ex-government will be very close to the 13%. The net interest margin of the bank as you can see now is at 6.5%. So we are right on track. The, the recurring expenses is where we, we are even below the, the expense growth. The efficiency ratio shows a better number, but we have to wait for the end of the, of, of the year. Cost of risk, now we adjust the cost of risk because the cost of risk is trending better than expected.

Tax rate is where we are and the net income shows already the effect of the reduction of the foregone interest of the -- of the buyback program that we have to use. And, and so that's, that's, that's where you see the reduction of that. I will not say that that's a final number. If we, we, we continue to see very strong loan growth on, on October, especially on the, on the consumer side, and, and a, a very good trend on the funding side. So that could give us a pickup still on the, on the net income. The return of equity of the bank is, is online with the guidance, a pretty sound number, the same for the group. And the ROA is showing a much better number than expected at the beginning of the year. Another very important issue is that when we project all the numbers of the bank, the GDP was expected to be very close to 3%. We are delivering this number with a GDP of 1.1 to 1.5. This is important to, to, notice because there have been some concerns about what's going to happen with next year, okay.

We will have been able to manage the bank at a, at a GDP trend of around 1.1. And we continue to see extreme strong loan demand on the consumer and also on the corporate basis on, on that part. And SMEs also showing some resilience on that part. That allow us that if the GDP for the next year is around 1 to 1.1, we could still see reasonable loan growth close to low double-digit numbers or very close to double-digit numbers. But we will see that as we continue to see when the guidance comes goes in place in the -- in January.

But it's important to notice that as we speak today, we continue to see reasonable performance of the loan book at a GDP of 1.1. So I would say that the other thing is that the interest rate that we expect by the end of the year will be around 10, 10% for the, for the, for the full year. So with that, I conclude my, my remarks. Thank you, Rafa.

Questions And Answers

A - Tomas Lozano {BIO 20758923 <GO>}

Thank you, Rafael. Now we will continue with our Q&A session. (Operator Instructions). We'll take the first question from Tito Labarta from Goldman Sachs. Tito, please go ahead.

Q - Tito Labarta {BIO 20837559 <GO>}

Hi, good morning, everyone. Thank you for the call and taking my questions. And you know, thanks for some of the points on you know the uncertainty that's going on and that you still expect a pretty healthy loan growth for next year. But maybe just to hone in a little bit on that point. As you mentioned, Rafael, yeah, even with 1% GDP growth, you're delivering double-digit loan growth and could maybe even do that again next year. Just you know what could be the downside or where could the downside come from? Like in what environment would loans grow single digits? Would asset quality be deteriorating? Is there anything that you're hearing or seeing? I know there's a lot of uncertainty where you could see that type of scenario. And if that scenario were to arise and you're growing your loan book, let's say, 0% to 5%, would you be more aggressive in returning capital given the strong capital you have? Thank you.

A - Jose Marcos Ramirez Miguel {BIO 4413879 <GO>}

Thank you, Tito. Rafa, please go ahead.

A - Rafael Arana de la Garza {BIO 22681143 <GO>}

Tito, let's -- what I'm saying that based upon the number that we have today, we could achieve very close to double-digit growth or almost double-digit growth. But let me just give you one, one very important question, one very important issue. If employment continues to hold, that's, that's the foundation of where we think that we could achieve that number. If employment start to weaken, then that will affect and then you will see loan growth from 7% to 9%. So that's, that's, that's the way we see it.

A - Jose Marcos Ramirez Miguel {BIO 4413879 <GO>}

Alex, do you want to add something?

A - Alejandro Padilla {BIO 6837329 <GO>}

Yeah, sure. Thank you. Alejandro Padilla, Chief Economist. Well, as Rafa was mentioning before, when you analyze GDP dynamics in Mexico, the main driver of the economy has been product consumption. Indeed this morning, the third quarter GDP was released and it was on the upside. It surprised in a positive way, especially going from domestic demand and the domestic demand is mainly driven by labor market that Rafa was saying and also by strong remittances and a better position of, of Mexican households.

And in this regard, as we are waiting for the economic package in 2025, the most likely outcome is that in terms of government spending, they will continue to, to deliver strong social programs that will benefit households' income. So, that's why we think that at least from the domestic side, it's going to be positive. And thinking about risks, well, we are contemplating this 1% GDP growth for next year with one condition that the US will continue without any recession.

We don't think that the US will, will get into a recession. Indeed, also today's first quarter GDP of the US was quite strong. The labor market has been also very resilient in the US, so we are forecasting that the US will grow around 1.7% next year and that's going to be a positive for Mexico because 56% of the economy, we have calculated that is highly dependent on the US.

Q - Tito Labarta {BIO 20837559 <GO>}

That's very helpful. Thanks, Alex and Rafael. And on the second point, would you consider returning more capital in a slower growth environment?

A - Jose Marcos Ramirez Miguel {BIO 4413879 <GO>}

It depends. As Rafa said, we want to keep all the tools here and we want to bring you the best for you. So, if that's the solution for you, then we expect to invest it. Where we don't have to work to invest, we will return more capital, the answer is yes.

Q - Tito Labarta {BIO 20837559 <GO>}

Great. Thank you, Marcos. And if just one quick follow up, I forgot to ask. Has there been any other talks of earlier in the -- before the elections, there were talks about reducing some tax benefits for the banks? Have you heard anything else from the government about any potential impacts on the banks?

A - Jose Marcos Ramirez Miguel {BIO 4413879 <GO>}

Not so far, nothing at all.

Q - Tito Labarta {BIO 20837559 <GO>}

Yeah, okay. Perfect. Thank you, Marcos.

A - Jose Marcos Ramirez Miguel {BIO 4413879 <GO>}

Thank you, Tito.

Operator

Now we'll go with Ernesto Gabilondo from Bank of America.

Q - Ernesto Gabilondo {BIO 16384492 <GO>}

Yeah. Hi, good morning. Thank you. Thank you. Hi, good morning, Marcos and Rafael. Thanks for the opportunity to ask questions. My question will be only one in terms of Vinoyo. So we saw it had a loss of MXN247 million. It was around 1.7% of the consolidated earnings. So today is working as friends and family, probably you will launch it to the open market next year. So, we just want to understand what could be the size of the loss for every quarter in Vinoyo. I don't know if at the beginning could be a little bit higher of the 2% of the net income or that should be the level we should be expecting going forward. Thank you.

A - Jose Marcos Ramirez Miguel {BIO 4413879 <GO>}

Yeah, thank you. That's a good question because maybe we should say that in the business plan, we saw that we're going to lose money for one, two years, you know. So, we need to, to explain this because it's a way to do with that business. Rafa, please go ahead.

A - Rafael Arana de la Garza {BIO 22681143 <GO>}

If you look at the total expense numbers, as you mentioned, this is around MXN1.2 billion [ph] a year. We don't expect that number to, to grow from, from that because as you know, we, we are using most of the scale of the bank in order to produce the economics of scale on the, on the cost side. So, that number should stay as is and maybe even improve a bit on that part. So, so you will not see an, an expansion on the cost, on the cost line. I think we reached the limit on the cost side and, and, and you shouldn't expect more cost coming from that, from that line.

A - Jose Marcos Ramirez Miguel {BIO 4413879 <GO>}

Thank you, Rafa. Is that okay, Ernesto?

A - Tomas Lozano {BIO 20758923 <GO>}

Ernesto, I think you have a mute on your microphone. Okay, we'll go for the, for the next question with Eduardo Rosman from BTG. Eduardo, please go ahead.

Q - Eduardo Rosman {BIO 16314825 <GO>}

Hi, hi everyone. One question here regarding the results from the other subsidiaries, right. You mentioned that the, the bank is delivering a 31% ROE, which is very strong, right. And that you, you -- with the hedges you know that you did, you're very likely going to, to be able to protect you know the ROE from a bigger decline, right, once interest rates go down, right. So can you please elaborate on the other subs you know that the, the ROE there, I still see room for improvement. So, if you can discuss a little bit where do you see room you know for improvements, in which one you know can that be relevant? Thank you.

A - Jose Marcos Ramirez Miguel {BIO 4413879 <GO>}

Thank you, Eduardo. Rafa, please go ahead.

A - Rafael Arana de la Garza {BIO 22681143 <GO>}

If you go to the, the return on equity, you see that I think we have opportunities to grow the business on the insurance side. I think we, we still have low penetration on our customer base on the bank insurance side. I think we can, we can still do, do more on that. I think there, there are more -- there are more insurance products coming to the market to address the new issues or the new services that the insurance company need to deliver to our clients. The annuities business continued to be quite, quite solid in that on that, on that part.

There have been some, some questions about trading. And since trading had a good quarter, there was like a -- it was a big jump on the quarter. But if you look at trading for us, it has always been around -- now if you look at total revenue against trading is 5% and it has been a very steady line as -- for many years. So, I think the bank will continue to, to push forward. And remember that the bank is the main distribution -- distributor of the insurance business. So the, the -- as long as the bank continues to grow and expands as in has been the case in the mortgage side, in the car loans, in, in credit cards, in, in payrolls, in bank, the, the insurance business will continue to grow.

And in addition, there will be some in the, in the open-market. The annuities business, we are very close to the leaders in that market. So this pretty good returns is a pretty sound business, so, so, so no issues on that. So what we have to protect is basically the Afore, the pension company that as, as, as we move forward to the -- to the coming years, the effect of the reduction on the fees starts to normalize more. But you will see return on equity of the, of the, of the Afore not on a tangible basis, maybe reaching the 14%. If you go to tangible, then that number will be very close to 10%. So, so I think that the, the way the return on equity has been set up, the leasing, the leasing company could also improve the company could also improve the the return on equity on that. We can see a lot more activity on the leasing and factoring company. So that could also improve some of the returns for the Group. But that's overall, we don't see any weakness really on any of the businesses.

Q - Eduardo Rosman {BIO 16314825 <GO>}

Oh, great. Thanks a lot for the detailed answer. If I could just follow up on, on, on, Ernesto's question on Vinoyo, right? I still -- I know that we're still in a work in progress, but do you think that this will be like the entity or the brand that will kind of compete with the new entrants like Nubank and (inaudible) or do you think that competition will take place kind of across the board you know including the, the Banorte brand, right? So how should we think about it? It's a different entity, a different brand, you know, or, or, or we should think about like, look, it's just -- it's the whole thing that will be competing?

A - Rafael Arana de la Garza {BIO 22681143 <GO>}

The first thing that you have to notice is if you are competing against bank or fintechs. When the fintechs become banks, then the competition becomes among banks and it will be a much more fair play because capital numbers, liquidity, compliance, everything will be on the same, on the same level, you know. That's the first question. So if you see competition that banks against fintechs, I think the, the, the slide that Marco presents that Banorte is a bank and lender, you see the, the, the power of Banorte in the digital bank. But obviously, Banorte has an issue on the cost structure that is delivering the 34%, 33% cost-to-income ratio for the next, for the next years.

So that, that could be seen for some people that is a disadvantage to compete in the market. But when you see that the combination of human and digital that Banorte, Banorte has and not only, but it also had the same that give us an edge where you see the balances that we open at the, at the, at the branches and the services that we provide on the overall, on the overall.

So when we launch a full value proposition for Vinoyo, that will be open for any customer on the banking side and also on the fintech side. And some of the banks of -- some of the clients of Banorte could choose to go for that if they like to live only on digital and that will be okay for us on that part. But we will compete with every single one in the market for the clients. The only thing that we will not compete is on a product-driven basis. We will always compete in a relationship basis by providing all the services and needs that a client needs. We are not just, you know, a product-driven bank. That hasn't worked for us in the, in the past and I don't think that's the way forward for us.

A - Jose Marcos Ramirez Miguel {BIO 4413879 <GO>}

Thank you, Rafael.

Q - Eduardo Rosman {BIO 16314825 <GO>}

Yeah, thank you very much.

A - Jose Marcos Ramirez Miguel {BIO 4413879 <GO>}

Thank you.

Operator

Now we take Meloni from Autonomous. Please, Renato, go ahead.

Q - Renato Meloni {BIO 19012073 <GO>}

Hi, everyone. Thanks for taking my questions here. So first, I would like you to give a bit more clarity on the balance sheet optimizations that led to this bank NIM increase to 6.7%. Just trying to understand here if this is a sustainable level or if this is going to revert back to lower levels going forward, especially because the lower yield or the NIM on the loans, it was still stable this quarter. And then just secondly, a quick question here on provisions. Just trying to understand the reduction in the commercial and corporate and government book, if there were some reversals there or if it was just a change in the model that, that you mentioned and trying to also gauge what's a normalized level here? Thank you.

A - Jose Marcos Ramirez Miguel {BIO 4413879 <GO>}

Thank you, Renato. We will start with the second one, the provisions, the product, so Rafa, please.

A - Rafael Arana de la Garza {BIO 22681143 <GO>}

Yes. As one can see, if you take a look and you take a deep dive into our commercial lending business, you will see that what we have is that the commercial portfolio registered less (inaudible) versus the first half of 2024. As in the third quarter of '24, the portfolio rose 5% quarter over quarter and 16.2% year over year, driven by (inaudible) in tourist areas such as (inaudible) Los Cabos. Currently, what you can see is that regarding provisions and the increase in the commercial side of the loan book, we are not detecting a pattern either by a sectorial view or by a geographic view.

So, our provisions are no sign of credit deterioration or asset quality deterioration in the commercial side of the, of the business. If you take a look at the corporate side, during the third quarter of 2024, we saw a mild slowdown versus the growth pace of certainty in the first half of 2024. As the portfolio, the corporate loan portfolio grew 7.8% quarter over quarter and 23.6% year over year, driven by great demand in sectors such as real estate, financial sector, transportation, logistics, and manufacturing. And in the other hand, we saw a slower pace in sectors such as oil and gas as well as in infrastructure projects. So that's the loan dynamics in these two parts of the loan portfolio. And the asset quality, the corporate side, it has been superb. It has been excellent and we are -- we remain very confident that in the commercial side and in the corporate side, the wholesale loan book is going to remain very predictable and stable.

A - Jose Marcos Ramirez Miguel {BIO 4413879 <GO>}

Thank you, Gerardo. Rafa, the NIM, are we maintaining that?

A - Rafael Arana de la Garza {BIO 22681143 <GO>}

Yeah, as you know, Renato, the, the, the projection for the guidance was that -- or it was below where the NIM is. So I think a sustainable NIM and one thing that is worth mentioning is that when you look at the mix on the portfolio, 57% of the portfolio now, now is at fixed rate. So that will more than compensate the reduction on the rates. That positioning of the book is what really cost us MXN2 billion last, last year, but that we'll get a benefit for the next five years. And the variable rate part of the book will be always moving as when the tier goes down, that variable rate part of the book will go down. But that's the advantage of Banorte.

The variable rate part of the book, when the rates were going up, we were very asset sensitive on that part. And it was the one who was really delivering the push on the margin side. And, and let's say that the, the fixed rate part of the book was mostly neutral. Now the fixed rate part of the book is picking, picking up on the margin side with 57% of the book in fixed rate and the variable rate part of the book will follow the, the, the tier, tier trend. But that's already been compensated on one to the other. Remember that the variable rate part of the book is 43% of the, of the, of the total book. So, so we feel very confident that 6.4% is a very, very steady margin for us on the coming, on the coming years.

A - Jose Marcos Ramirez Miguel {BIO 4413879 <GO>}

Thank you, Rafa.

Q - Renato Meloni {BIO 19012073 <GO>}

Great. Thank you. It's clear. So the message is that the bank NIM will converge here to the guidance then?

A - Rafael Arana de la Garza {BIO 22681143 <GO>}

Exactly when -- if you see on, maybe on the next two to three years, it will converge to the guidance because you, you will continue to see a pickup on the margin for the next year and for the end of this year.

Q - Renato Meloni {BIO 19012073 <GO>}

Great. Thank you.

A - Rafael Arana de la Garza {BIO 22681143 <GO>}

Thank you.

A - Tomas Lozano {BIO 20758923 <GO>}

Thank you. Now we will continue with Olavo Arthuzo from UBS. Olavo, please go ahead.

Q - Olavo Arthuzo {BIO 19964942 <GO>}

Yes. Thank you, Jose Marcos, Rafa. I have a question on Vinoyo, but it's a kind of different approach because I just wanted to understand how relevant has been the launch of the money pockets or money boxes. I mean, at the current customer base, what is the percentage of clients that has invested into it? And if you could just also please give us the amount and pesos that has been already invested in pockets at Vinoyo, that would also be great. Thank you. Then I'll go to my second question.

A - Rafael Arana de la Garza {BIO 22681143 <GO>}

Remember that we haven't advertised any on that. So basically, it's on the friends and family. So, the numbers that you still see is quite low on, on, on that. But what is good that we have a full activation on the opex [ph] side and we can really provide a client what they want. But you need to wait when we really do, do the big launch on the, on the Vinoyo part to really understand the dynamics of the clients. The number of clients right now is non relevant compared to the potential of the, of the Vinoyo brand honestly. That's what I can say.

Q - Olavo Arthuzo {BIO 19964942 <GO>}

Okay, so just a follow up. When do you expect this to gain any traction, so?

A - Rafael Arana de la Garza {BIO 22681143 <GO>}

We are aiming to have the full value proposition in place in the first quarter of next year. On that, from that, we'll get the full traction because you will get the payroll, you will get the mortgages, you will get the car loans, you will get mutual funds, you will get the credit cards, you will get the debit that is already the pockets, the funding. So you get the full because Banorte needs to compete on a relationship basis, not on a product-driven basis. So and that has to happen in the first quarter next year.

Q - Olavo Arthuzo {BIO 19964942 <GO>}

Okay. No, that's great, Rafa. And also a, a follow-up question on this topic, but more broadly related to (inaudible). Is there anything to share with us about the benefits of adopting that technology as kind of a payment in Mexico, Rafa? Because I just wanted to understand what are the collective thoughts on, on that? And I think customers are transacting using demo? Any update on this regard will also be greatly appreciated.

A - Jose Marcos Ramirez Miguel {BIO 4413879 <GO>}

Go ahead, Rafa.

A - Rafael Arana de la Garza {BIO 22681143 <GO>}

The technology is good. I think it's a good technology. It is, but we have a structural problem here that is the informality of the market. So we need to move to a much more formalized market in order to have the advantage that (inaudible) or things like that, like that. So, clients still are heavy on cash, even if they -- the technology is pretty good, honestly, it's pretty good. So, I think the more benefits are given into the labor force, the more employment continues to grow and benefits, you are moving much more into financial inclusion. Even on the remittances side, we are playing a very hard game on remittances to, to really move the financial inclusion on remittances and build up accounts and, and that on that part of the market. But I think more on the regulatory side, what needs to happen like, let me just give you an example. Right now, every single public service needs to be paid from an account, a digital account with no cost, but that will really allow those type of technologies to be quite useful for the clients.

Q - Olavo Arthuzo {BIO 19964942 <GO>}

Okay. So the top of mostly be marginal accretive for the bank, right?

A - Jose Marcos Ramirez Miguel {BIO 4413879 <GO>}

Right.

A - Rafael Arana de la Garza {BIO 22681143 <GO>}

Right.

Q - Olavo Arthuzo {BIO 19964942 <GO>}

Okay. Well, thank you very much, Rafa. Thank you very much, Marcos.

A - Jose Marcos Ramirez Miguel {BIO 4413879 <GO>}

You too.

Operator

Now we'll go with Yuri Fernandes from JPMorgan. Please, Yuri, go ahead.

A - Tomas Lozano {BIO 20758923 <GO>}

I think, Yuri disconnected, so we can follow with Jorge Kuri from Morgan Stanley. Jorge, please go ahead.

Q - Jorge Kuri {BIO 3937764 <GO>}

Hi, everyone. Good morning and thanks for taking my question. I wanted to ask about deposits. Your deposit growth rate decelerated a lot during the year. You started the year growing at 17%, 18% and now this quarter, your deposit growth rate was 8% year on year. That's slower than your credit growth, which is 11%. I'm wondering if there is something to be read about competition for deposits from the digital banks. You know, Nubank, just looking at the CBM disclosure, Nubank has gone from $0 billion to $4 billion in deposits over the last 12 months, which is no longer a small number, right. I mean, that would be like equivalent to around 7% of your deposits. And then you also have many more competitors, (inaudible) etc, etc.

So what do you think explains the slowdown in deposit and just the absolute level of growth in deposits below your credit growth and to what extent do you think that if these platforms continue to overpay for deposits for long, it will start to change the competitive dynamics for deposits in the system? Thank you.

A - Jose Marcos Ramirez Miguel {BIO 4413879 <GO>}

Thank you, Jorge. That's a good question because here deposits, deposits, deposits is the name of the game, we agree on that. And well, the rates are going down and that's going to be good for, for, for everybody. But -- and the war is there if you compare with the, the other peers and the, the new competitors. I will ask Rafa, to give you some numbers, please.

A - Rafael Arana de la Garza {BIO 22681143 <GO>}

Jorge, one number that, that you should be looking is the non-interest bearing deposit that have been growing at 8% for the year. And we based upon the dynamics that we see on that part, that is the, the tough part to, to fund. You will see that by the end of the year, that number will be very close, very close to loan growth, the non-interest bearing deposits. So, that's the, that's the key issue for us to really see how powerful the, the, the service proposition that we deliver to the market could bring non-interest bearing deposits that has to do a lot with payroll service to the companies and, and, and individuals.

So, that's what's the big number. The, the other big number is of time deposits. Time deposits are growing 20% for the year. So when you add everything up, you can really fund the growth on the, on the book based upon, upon this. But the time deposit base, what is good about the time deposit base is not just the growth, is that the time deposit base is converging to a much lower funding cost than we needed to put in place when rates were around 11.15.

So, if you ask me, if there's pressure in the market for the, for the Nubank, for the (inaudible) on that, of course, it is for some of the people that likes to take advantage of that. And usually what happens and we can see that because you can see where the transfer money comes -- goes from Banorte to Nubank to the others. That is basically money that moves, take advantage of the rates and then comes back to pay the services and loans that they have with the bank.

That number is around MXN3 billion that compared to the, to the other -- to the big number that we have on the funding side is really a very, very small number. It's not that we are not very attentive to that. But what we have seen and we are very, very pleased is that the non-interest bearing part of the book is really growing at a very, very good pace.

And you will see that the numbers of non-interest bearing by the end of the (inaudible) question.

Q - Jorge Kuri {BIO 3937764 <GO>}

Hi. Thank you, Rafa. If I can just squeeze one additional question? I thought this was going to come out earlier, but it, but it hasn't. And since your last quarterly earnings, the, the big development in Mexico, obviously is the judicial reform. Given how much banks in general rely on the courts for reprocessing assets, executing guarantees, you know, deal with labor and civil lawsuits that are normal in your world. To, to what extent this changes your ability to lend your appetite to lend, the pricing, the provisions? You know, how does this new judicial reform potentially impact the loan side of the business? Thank you.

A - Jose Marcos Ramirez Miguel {BIO 4413879 <GO>}

Thank you. I will pass this to Gerardo Salazar. Please go ahead.

A - Gerardo C. Salazar Viezca {BIO 16248253 <GO>}

Well, hello, Jorge. I will say that we've been working in very important contractual risk mitigants in order to deal with the effects of this constitutional reform of the judiciary system. We, we can protect our rights through contractual mitigants that minimize credit risk. If we look at several key ingredients, which I'm going to give you an example. The first ingredient is going to be collateralization and secure lending. We are more than ever looking for those credit structures like asset-backed collaterals. The pledging of receivables is one example. Also, when there is the opportunity, we will work with cash collaterals. Also, the second main ingredient in dealing with the potential effects of this judiciary reform is to look for third-party guarantees in order to protect our sources of payment.

I will add a third front in which we have been working which are the modification of some covenants like the financial covenants, look at the pledges and more information covenants to be closer than ever to our customers, to see their performance, to see what arises and to take proactive actions in an early manner. Fourth ingredient in which we consider we have some mitigants is a more intensive use of SPVs, special-purpose vehicles and using bankruptcy remote structures to, to see how we -- how can we deal with this type of, of deterioration or potential deterioration, which we have not seen as of yet, but we are preparing for that kind of a scenario. We are intensifying, intensifying the use of escrow accounts and also control agreements with dedicated escrow accounts and, and some deposit and control agreements in that regard. And also, we are using more than ever cross-default clauses in order to, to deal with the potential impact of these. Another thing that our team is working in is trying to analyze and change whenever it is possible, jurisdiction and arbitration clauses. That's going to become and it is still very important. We have had some experience in the past regarding that front, but we will deal with it in that manner whenever it is possible. We know that in the commercial side and the corporate side of the business and the wholesale loan book, there is big possibilities to protect ourselves regarding this, this ingredient.

And also we, we have been looking for political risk mitigation, working hand in hand with local investors, local entities and also the development banks whenever it is possible regarding any, any, any size of, of, of the loan book. That's the actions that we have been taking previously trying to foresee the, the, the effects of this judiciary reform, which obviously we are trying to protect our rights, and also to make our customers feel comfortable in a reasonable manner because of these effects.

Q - Jorge Kuri {BIO 3937764 <GO>}

Thank you. That's very clear. Thank you.

A - Tomas Lozano {BIO 20758923 <GO>}

Thank you, Jorge. Now, we'll continue with Carlos Gomez-Lopez from HSBC. Carlos, please go ahead.

A - Jose Marcos Ramirez Miguel {BIO 4413879 <GO>}

I can hear you, Carlos.

A - Rafael Arana de la Garza {BIO 22681143 <GO>}

I think Carlos is, Carlos.

Q - Carlos Gomez-Lopez {BIO 18107094 <GO>}

Now you can hear me.

A - Rafael Arana de la Garza {BIO 22681143 <GO>}

Yeah.

A - Jose Marcos Ramirez Miguel {BIO 4413879 <GO>}

Yeah, thank you.

Q - Carlos Gomez-Lopez {BIO 18107094 <GO>}

Okay. No, no, thank you. Thank you so much. So I actually wanted to follow up on the judicial reform. And again, I understand the mitigants that you're going to introduce and that's of course what, what you have to do. When do you expect that the changes in the judges and the structure of the courts will start to affect operationally what you do on a day-to-day basis? Is that something that you expect already in the beginning of next year, end of next year, 2025, etc? And if, if I can follow up totally unrelated, can you give us some more information about the Rappi joint venture, (inaudible) Futuro? Thank you.

A - Jose Marcos Ramirez Miguel {BIO 4413879 <GO>}

Yes. First one is a good question because it's not going to be immediately. Our lawyers think that two or three years, so it's going to be a long way to work and, and to see how we, we adapt to that, you know. And the Rappi one, I will ask Paco Martha is right here with us on the call. Paco?

A - Jose Francisco Martha Gonzalez {BIO 19073751 <GO>}

Thank you, Carlos. We keep working with the, with Rappi and the joint venture, we have more than 1 million cards, 75% of them active month over month. We already crossed the MXN5,000 million on the, on the portfolio. And, and as we mentioned in the previous call three months ago, we are now in, in black numbers, reaching the, the black numbers starting on April of this year. So the business is moving forward. The, the, the loans are well managed. The users are heavily using the card. We have more or less the same, the same transactions per month in the, in the credit card, in the RappiCards as we have in, in Banorte's card. So in a nutshell, that's what's happening in the, in the RappiCard business.

Q - Carlos Gomez-Lopez {BIO 18107094 <GO>}

Do you see any potential cannibalization between Vinoyo and Rappi?

A - Jose Marcos Ramirez Miguel {BIO 4413879 <GO>}

You know that only 6% of the customers that we have in RappiCard are also customers on Banorte, not only in credit card, in general, no. And you can see that RappiCard has 75%, 76% of the customers below 36 years and that numbers in Banorte is 30%. So we don't see really a cannibalization, but more than an, an additional credit card that people is using. You know that in Mexico, it's frequently to have one, two, three or more credit cards. So it's, it's not that moving towards there. It's leading Banorte.

Q - Carlos Gomez-Lopez {BIO 18107094 <GO>}

Thank you so much.

A - Jose Marcos Ramirez Miguel {BIO 4413879 <GO>}

Thank you, Carlos.

A - Jose Francisco Martha Gonzalez {BIO 19073751 <GO>}

Thank you.

A - Tomas Lozano {BIO 20758923 <GO>}

Thank you. Now we'll continue with Andres Soto from Santander.

Q - Andres Soto {BIO 15822388 <GO>}

Perfect. Good morning to all. Thank you for the presentation. I have just a couple of questions. The first one is regarding cost of risk. You are improving a little bit your guidance for this year based on a very positive performance that we have seen so far. And it is interesting that this happens at the same time that you downgrade your GDP expectations. So I would like to understand, you know, regarding your risk model, if the GDP is not the key parameter that we should look at or is it rather employment, as you mentioned before, and it will require for employment to deteriorate for you guys to need to make an adjustment to every small level and for that to be reflected as additional provisions? And more broadly speaking, when I look at Banorte prior 2018, the cost of rates was about 2%. Now you are running at, let's say 1.8% and this is despite a significant shift in your loan mix. So, I would like to understand what can we expect over the medium term, also considering this deteriorated Mexico growth outlook.

A - Jose Marcos Ramirez Miguel {BIO 4413879 <GO>}

Thanks, Andres. The first one, the cost of risk, Gerardo Salazar, please go ahead.

A - Gerardo C. Salazar Viezca {BIO 16248253 <GO>}

Thank you. Thank you. Thank you, Marcos. I will say, first of all, that regarding the growth drivers of the loan book. At the same time that we are considering a lower GDP growth, we are also considering a lower interest rate. And that's very important for you to consider because that's the income effect and the substitution effect to take into consideration regarding the, the, the parameters that we have announced in this call. Also, I will try to complement some other growth drivers in which they are not only the macroeconomic drivers of growth for the loan book. Obviously, those drivers are very important. As Rafael Arana was saying, the, the, the unemployment rate is key for our models and also it is key trying to, to deliver some, some performance because our loan book is dependent on economic growth, consumer confidence and income levels. And the unemployment rate is going to be one very important indicator of that.

But we have to add some other drivers, which are more endogenous, which are under our control in order to provide growth of the loan book. I will say that there is a market and customer demand drivers will see loans at a lower price if the interest rates continue to, to, to go down. Also, we consider ourselves to have better products for the hyper personalization Rafael Arana and Marcos was, was mentioning. And also we have low pricing drivers. We are willing to price our loans in low levels because we have the structure and the cost of risk is low as you can see. And in order to do that, we have been transforming that key element in the Banorte strategy into a competitive advantage regarding our peers. Also, I would have to add that regarding growth of the loan book, you have to take into consideration the capital and risk management drivers that we possess. The capital strength of Banorte in which we account for sufficient capital to support growth is one key ingredient to support that growth. And also our liquidity position makes funds available for loan disbursements. So we are in pace of trying to provide a, a, a healthy loan growth for the next years.

Q - Andres Soto {BIO 15822388 <GO>}

Thank you so much. And then if also, the medium term cost-of-risk expectations?

A - Jose Marcos Ramirez Miguel {BIO 4413879 <GO>}

Yeah, the cost of risk expectations for the medium-term, I will, I will say, Andres, will be between 1.8 till 2.2. That's going to be the range. We know that we are below that for the moment, 1.66 is the cost of risk as of now, but we, we're taking a very conservative view on the, on the, on the potential behavior of this indicator.

A - Gerardo C. Salazar Viezca {BIO 16248253 <GO>}

And we will move to consumer products.

A - Jose Marcos Ramirez Miguel {BIO 4413879 <GO>}

Yeah, yeah.

Q - Andres Soto {BIO 15822388 <GO>}

So, understood. So it will be similar to the pre-COVID level, but with a better loan mix, I would say.

A - Jose Marcos Ramirez Miguel {BIO 4413879 <GO>}

That's correct. Yes. The, the retail book is going to be more important throughout the years, in a way.

Q - Andres Soto {BIO 15822388 <GO>}

Right. And then finally on expenses, do you guys have any -- when we started the year, we, we had very positive expectations for the Mexican economy, a lot of investment coming up and you guys also reflected that in terms of your expansion and growth, expense growth that you're forecasting. When you look at 2025, should we looking at the expense growth, double digit, high single digit, what level will be reasonable for you guys next year?

A - Jose Marcos Ramirez Miguel {BIO 4413879 <GO>}

Rafa?

A - Rafael Arana de la Garza {BIO 22681143 <GO>}

I mean, I will -- we will really push to, to, to, single, single-digit expense growth. That's our goal. And we are doing everything in our hands to do that. What we're doing, basically integrating everything on the operational side, on the HR side, accounting side. All the back office's functions are being integrated into one for the, for the group. That is going to give us a very reasonable reduction in expenses. And also, you have to consider that most of the, of the big spending cycle about hiring the bankers, 1.2 -- a 1,200 bankers that we hire for the, for the nearshoring SME and commercial and corporate now has -- is already in full production. So that also will increase the, the revenue side and we don't need to add more cost on that, on that base. Vinoyo and, and Rappi will continue to wait on that. So we have to, to lower the recurrent base of the, of the cost base that is now at sitting at 7.3, but -- and that's the one that we are working to do that and not allow the entities Vinoyo and Rappi to increase the expense side. So I think it's a long shot, but we are aiming to have a reduction to, to a single-digit expense growth next year. I know it's a long shot, but we are fully working on that.

Q - Andres Soto {BIO 15822388 <GO>}

Perfect. Thank you so much. So just to summarize, you are expecting some, I would say, some efficiency improvement next year, better margins, some deterioration in cost of risk. It will be hard to say that you will be targeting similar levels of ROE to this year or it's too early to tell?

A - Rafael Arana de la Garza {BIO 22681143 <GO>}

No, I think, ROE will be -- will continue to be very close to the number that we have. I think our, our goal on the bank level is around 28%. We are around at 31.1% right now. But I think 28% is where we are aiming to have on that part. Why? Because there's still a potential to manage the capital base on a, on a much more efficient way. Why we haven't done that because the world isn't quiet. So but we have a -- if you, if you go to a number that we have promised the market to be from 13% to 13.5%, you will see an immediate jump on the, on the return on equity with basically the same numbers that the bank produces at the -- on that today. So, we have many levers, but we would like to keep a sound capital base and still deliver very strong return on equity. And I think we have been able to do that in the past years.

Q - Andres Soto {BIO 15822388 <GO>}

Absolutely. That's very clear. Thank you so much.

A - Rafael Arana de la Garza {BIO 22681143 <GO>}

Thank you.

Operator

Thank you. Now we'll go with Nicolas Riva from Bank of America. Please, Nicolas, go ahead.

Q - Nicolas Riva {BIO 20589225 <GO>}

Thanks very much. Thank you, Rafa and Marcos for the chance to ask questions. So, my question is on capital. So this quarter, at the end of September, you called the $600 million outstanding in the six and three quarters. So with that, let's see, your CET1 is at 13.9%, so let's call it roughly 14% CET1. The message I get from your comments in this call is that you are not going to be accumulating more, more capital, more CET1. If anything, this number is going to be stable or really decline a bit. You pretty much don't have any tier-2 outstanding. I think there's less than a $100 million outstanding on the 2031s. That's only, I think 20 basis points of tier-2 capital. And then you have the AT1s, but you just called the six and three quarters without a capital replacement. So, you know, capital requirements in Mexico are very-high with TLAC implementation. So by the end of next year, you're going to need to have 17.9% total capital. And again, doing the math roughly, 14% CET1, which is going to be probably stable or going down. You got 500 basis points of AT1, but you have another 5 calls and again, you just called the six and three quarters without a capital replacement. So my question would be, if you are thinking of raising more tier-2 or AT1 as you call the next calls, again to meet that very high capital requirement of 17.9% total capital by the end of next year. Thanks.

A - Jose Marcos Ramirez Miguel {BIO 4413879 <GO>}

Nicolas, you have the big, big picture. You are totally right. And what else we can say? Yes, we are planning to raise more capital. It -- the problem is the market, no. We don't need it, but it's good to have it, no. So we will be there and we will see how the market reacts. And if we see the window, yes, we will issue more, more to or whatever is good for the bank, no. And you have the whole picture. So you know what are we going to with this.

Q - Nicolas Riva {BIO 20589225 <GO>}

So, Marcos, a follow up there. Then in that case, in the past, you have shown a preference to raise AT1 compared to tier 2 despite theoretically a lower cost of issuing tier 2. Is that necessarily going to be the case going forward, a preference to replace AT1s with new AT1 capital, as you call the AT1s?

A - Jose Marcos Ramirez Miguel {BIO 4413879 <GO>}

Yes, we prefer the AT1s because for us, it work better and, and it's a matter of what's better for the -- for our balance sheet. So we prefer the AT1s, yes.

Q - Nicolas Riva {BIO 20589225 <GO>}

Okay. Thanks very much, Marcos.

A - Jose Marcos Ramirez Miguel {BIO 4413879 <GO>}

Thank you.

A - Tomas Lozano {BIO 20758923 <GO>}

Thank you. We'll continue with Thiago Batista from UBS. Thiago, please go ahead. Thiago, yeah, please unmute, yeah. Now we'll hear you.

Q - Thiago Batista {BIO 15398695 <GO>}

Hi. Yes, guys. Thanks for the opportunity. I had a question on the government lending book. We saw a decline of almost 2% q-on-q. The year is mentioned, about, let's say, 2%. So my question is, this, this is and simply a weak performance of this portfolio was more a decision of the bank decided to be more conservative on the credit for, for government lending or lower demand because of all the changes? And also trying to understand how dilutive is this business for the ROE of the bank? We know that the cost of risk is probably close to zero and interest rates are much smaller, but how dilutive is this business for the ROE of the bank?

A - Jose Marcos Ramirez Miguel {BIO 4413879 <GO>}

Thank you, Thiago. Yes, we saw some prepayments last year. Remember that we are changing the cycle with the new present, but it's a good business for us. Remember, it's not -- it's only -- it's not only the lending part. We work with the governments with a lot of pieces. So for, for us, it's very important to, to be with them and to -- and it's good for the country too. So it's a win-win situation. We want to be there. You will see in this year that we will start to be on track again and we see a lot of things to do. Rafa wants to say something here. Rafa?

A - Rafael Arana de la Garza {BIO 22681143 <GO>}

On, on the dilution side, there is no dilution for us, a very simple reason. The use of capital is very, very low for the government book, because remember that we -- when we lend to the government entities, we set up on a trust that we control the trust. So we get the funds coming from the federal budget into the trust. So as you can see, NPLs are zero and the usage of, of capital is very low. Obviously, the margin, the margin is what I think. The margin in this loans is thinner than on the margin on the corporate side, but the return on equity usually is, is higher than the, than the corporate on the commercial side.

So and as Marco said, the, the advantage of the, of the, of the government book is the ancillary business that you receive from, from that relationship. So no, there is no dilution on the, on the ROE from the government book.

Q - Thiago Batista {BIO 15398695 <GO>}

Very clear. Thanks.

A - Jose Marcos Ramirez Miguel {BIO 4413879 <GO>}

Thank you, Thiago. We're almost over on time. We have two final questions. Please, we ask you to only present one, one question. We will continue with Igor (Inaudible). Thiago, please mute your microphone. Thiago. Yeah, thank you.

Q - Unidentified Participant

Hi, everyone.

A - Jose Marcos Ramirez Miguel {BIO 4413879 <GO>}

Hi, Igor.

Q - Unidentified Participant

Hi. Can you hear me?

A - Jose Marcos Ramirez Miguel {BIO 4413879 <GO>}

Yes, perfectly.

Q - Unidentified Participant

Yes. So thank you for the call and taking my question. Regarding on cost of funding, we were expecting a continuous decrease. However, we saw a jump from 47.8 to 49.3, so I kindly would like to understand the main reasons for -- that contributed for this? And just confirm how you are seeing the evolution of design considering the Banxico cuts on policy rates, please?

A - Jose Marcos Ramirez Miguel {BIO 4413879 <GO>}

Thank you, Igor. Let's go, Rafa.

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A - Rafael Arana de la Garza {BIO 22681143 <GO>}

Igor, we, we said at the beginning of the call that you have a, a different pace on the on the centers and on the tier, tier related to the asset side and set is more related to the funding side. Remember that on the funding side, on the, on the time deposit base, those get renewed on a, 30, 45, 90 days. So, when you see a disconnect about the pace of how fast the set is going down compared to the tier, you have to wait for the renewal of the time deposits to get adjusted to the, to the new rate. That's what you see a 49.8 jump, but you will see that, that lag closes by the end of the year that you, you should see those numbers very close to 47 something at the end of the year. And then the pace of the, of the, of the tier and the set will be much more aligned. That's the reason for that jump, not that the funding costs overall because you saw a jump on the margin side, on that, on that part. That's the reason.

Q - Unidentified Participant

Okay. That's super clear. Thank you.

A - Rafael Arana de la Garza {BIO 22681143 <GO>}

Thank you.

Operator

Now we'll have our last question for Edson Mohia [ph] from (inaudible). Please Edson, go ahead.

Q - Unidentified Participant

Hi, good afternoon and thank you for taking my questions. I know I have to go for one. And my question is a follow up on what Dr. [ph] Salazar said about the risk mitigation that you are doing or you will do for the following months, weeks for years. Cash, collateral, third-party guarantees, modification of covenants, and the SVPs, how those risk mitigation regarding on the judicial reform will affect the loan growth portfolio for the following quarters?

A - Jose Marcos Ramirez Miguel {BIO 4413879 <GO>}

Gerardo Salazar, please.

A - Gerardo C. Salazar Viezca {BIO 16248253 <GO>}

Sure. Thank you. Thank you, Edson. I will say that the growth dynamics have not been affected as of yet. That's the main reason that we are providing a, a range of growth of 10% to 12%. So these risk mitigants providing that we are still seeing GDP growth, a tight labor market with a low unemployment rate that makes us, makes us, makes us confident that looking forward, we will see a growth happening with the same quality standards that we have provided as of now.

Q - Unidentified Participant

Okay. Well, thank you so much and happy 125th [ph] year.

A - Rafael Arana de la Garza {BIO 22681143 <GO>}

Thank you, the anniversary.

A - Jose Marcos Ramirez Miguel {BIO 4413879 <GO>}

Yes. That's right. Thank you very much.

A - Tomas Lozano {BIO 20758923 <GO>}

Thank you. With this, we conclude our presentation. Thank you very much for the interest in Banorte. Bye, bye.