Millennium bcp Q4 2012 Earnings Call

Company Participants

• Nuno Amado (CEO)

• Miguel de Campos Pereira de Bragança (CFO)

• Rui Pedro da Conceição Coimbra Fernandes (IRO)

Other Participants

• Carlos Peixoto (BPI)

• Antonio Ramirez (KBW)

• Ignacio Ulargui (BBVA)

• Juan Pablo López (Espírito Santo)

• Jaime Hernández (Nomura)

MANAGEMENT DISCUSSION SECTION

Operator

Good day, and welcome to the Millennium bcp Full Year 2012 Earnings Conference Call. Today's conference is being recorded. At this time, I would like to turn the conference over to Nuno Amado. Please go ahead, sir.

Nuno Amado

Okay. Good afternoon, everybody. I am CEO of BCP, Millennium bcp and this is my first annual result presentation as CEO of the Bank. First of all, I would like to bring to mind that the results that we are to going to present right now or to review right now are the outcome of a particular, difficult and efficient year, as you know, for both our Bank and the Portuguese economy, which is the core of our asset. Despite the negative results that we got, I would like to recall you that they were expected. They are more or less in line with our funding and capital plan because, as it was mentioned before, we have three main levers of priorities, three main priorities – liquidity, capital and profitability. And the first two were in 2012 much more relevant than the third one. Liquidity and capital were critical for the reasons that you understand. We took less than one year to reinforce our financial position, namely in capital and in liquidity, as I mentioned. Two or three figures, we have consistently deleveraged and we reduced our commercial gap and we reached a loan-to-deposit ratio of 129%. This 129% is according to the Bank of Portugal criteria, but if we divide deposits by customer funds on the balance sheet, our ratio is already 112%. And our commercial gap decrease was more than €7 billion as you'll see later on. In terms of capital, we have now a Core Tier 1 of 12.4% according to the Bank of Portugal criteria, and 9.8% according to EBA. However, in EBA if we make the mark-to-market of our sovereign debt position, at December 31, last year prices, our EBA ratio is not 9.8%, it would be 11.4%, which is, in my opinion, very strong for both criteria, Bank of Portugal or EBA. I also would like to recall that we have concluded a very difficult, but very successful capital increase process in September, a very difficult month for every purpose and we got it over subscribed, very large investor base, it was really I think an achievement of the year. We also did some important things internally. I would like to mention, for instance, the improvement of the credit recovery process, and credit risk control. Right now we have a credit area, risk area, which is totally separated from our commercial area that's totally independent approach to the portfolio into the new loans and recoveries of the existing portfolio. We've restructured our organization making it lighter and promoting efficiency gains. We've decreased last year around 1,000 staff, but we did a decrease of 800 staff only in the last quarter. So in one quarter we did a strong effort that will have impact on future years. I'll say that we're now better prepared to support our customers and to support the development of the economies where we're present, not only in Portugal, but the main market that we have, which are in Europe, Poland, and in Africa, Mozambique and Angola. These are the four strategic markets that we've right now. For the detailed presentation, I'll pass the word to the CFO, Miguel Bragança, who will present these results in more detail. Miguel?

Miguel de Campos Pereira de Bragança

Good afternoon, ladies and gentlemen. I'll go through the main highlights of the Group and the general financials of the Group, and then in terms of the specific operations, our Investor Relations will comment a little bit on them. So, as you may see in page four, so the liquidity was significantly reinforced with consistent closing of the commercial gap this time by €7 billion year-on-year. The balance sheet customer funds grew 5.1% this year and the loans to customer reduced by 6.5% so this enabled us to reach a ratio of net loans to balance sheet customer fund of 112% by every mean a very conservative ratio. In terms of capital, capital stands comfortable above requirements and this is not by chance because the results and the profitability that we are presenting now was already to a large extent expected so that we created the capital buffer Exactly to accommodate our plan. So our core tier 1 reached 12.4% according to the Bank of Portugal, which is significantly higher than the 9.3% by the end of 2011. And our Core Tier 1 according to EBA is 9.8%, and as Mr. Nuno Amado was just commenting, adjusting by the mark to-market of our sovereign buffer, it would have been 11.4%, basically our sovereign portfolio now has net gains and not net losses. The consolidated net income was €1.2 billion, penalized by the results associated to our Greek operation of around €700 million, and by impairment losses in Portugal. On the other hand, our other three geographies, besides Portugal, where we are focusing represented a consistent result of €236 million. However, right now, exactly as expected in plan, we see the conditions of reversing trend. So, the net interest income, if you look at the last quarter compared with previous quarters, is already showing a reversal. We have implemented very, very tough restructuring program, anticipating our objectives and what we had communicated to the market with a future annual savings above €30 million and the past due entries are lower than in the previous quarter. In the meantime, as was communicated to the market, we are pursuing our strategy of de-risking vis-à-vis our Greek operations and we have signed an exclusivity agreement with Piraeus. However, everything right now in terms of the deal is still non-binding. So we are still in a negotiating phase. What you see in page five and is six basically a graphical exposure of what I just commented. However, I would highlight in page six, exactly the reversal of the net income trend and also the good trend in terms of the net new entries in terms of past due in page six. Going to page eight, in terms of liquidity, what we see is our 5% growth in terms of balance sheet customer funds, which was achieved with a total growth of 4.6% in terms of total customer funds. So, we are growing in terms of our commercial activity and our client based activity. And this is not only internationally, where we have grown around 12.5%, but also nationally, so in Portugal where we were able to show a 2.2% growth in terms of balance sheet customer funds.In terms of loans, we see here a deleverage in consolidated terms of around 6.5% in spite of a growth in the international portfolio as it should be of 1.8%. Okay. And we are engaged to decrease somewhat also our mortgage loans in spite of the long maturity of these loans, which have decreased 5% as has been in the previous quarter. In page 10, you see that it is the implication of all these efforts in terms of credit of deposits was a closing of the commercial gap of around €7.3 billion. And this closing of the commercial gap has made it possible to repay medium, long-term debt around €5.5 billion, and still reduce the net usage of the ECB by €2.2 billion. In page 11, what you see is that we are with a very, very comfortable liquidity position mainly taking in mind what we have done in the recent past. So you see here in 2009, 2010, 2011, 2012, a significant amount that has been repaid with consistent closing of commercial gaps between €7 billion and €8 billion a year. And when you look at our maturities going forward you see that it's not an issue. We have a very conservative liquidity profile. And if you take a look, of course, at our funding structure, you also see that most of our assets are being funded either by long-term funding or by customer deposits.Turning to capital, in page 13, you see here a significant growth of the capital ratio by 3.1 percentage points in terms of Core Tier 1, and this of course was made possible through the issue of the CoCo's and through also our capital increase, but also through our consistent deleverage and management of the risk weighted asset. And if you take a look here at page 14 what you see we have here a bi-annual view of what was achieved. So, we came from levels of around 5% of Core Tier 1 during – until would say 2007, so pre-crisis 5% and this has been consistently grown to the level of 12.4% that we see right now. And this, of course, is also a very good level when you compare it with other Eurozone banks with as you see below. So, we, in terms of capital, in terms of basic capital, we are in a comfortable position. Of course, we have access to [state debt], but the reason why we have so much capital is exactly to cope with this transformation and with the turnaround adjustment that we're implementing. In terms of the pension funds, there was also decrease of the pension fund – I'm sorry, a decreasing – de-risking of the pension fund with in spite of the loan maturity of the pension fund that we have around 17 years our exposure to shares is only 28% and the coverage of the pension liability was increased to 120%. The fund profitability was not that high, was only 1.6% basically explained by the specific strategies in stock picking in which it was invested. In terms of the actuarial assumption, what you see is that we have decreased the discount rate by one percentage point and simultaneously adjusted the salary growth rate and the pension growth rate to the new environment.

Moving to the income statement, in page 17 we're trying here to understand a little bit the dynamics of the income statement. We have here aggregated the lines so as to exclude from some line, but not from the bottom line, the CoCo impact and the net impact of Greece. What you see here is that in terms of net income before income tax 2012, and before income tax and Greece and CoCo's now, on a like-for-like basis adjusting by these effects, 2012 is already showing some degrees of turnaround with a better net income before income tax than 2011. And the operating profit before impairment and provisions, of course, also shows a positive impact. It is when one adjust these for the costs related to the CoCo's that are somehow of equity nature, if they were designed differently, they could probably have even had another type of accounting treatment. And items related to Greece that we see this final impact in terms of net income. But the main lesson that I would here like to show in page 17, and then by the way also in page 18 is that, in terms of the fundamentals, in terms of the core earnings there are already some signs of turnaround.

In page 18, this is also made a little bit more explicit. In the left you see an aggregation of the items that are very specific and not that much comparable to what competitors have done, namely, the items related to Greece, the cost of the CoCo's and the 2011 liability management exchanges where securities with low interest rates were exchanged for securities with higher interest rate at the end of the day. You see that these – if you aggregate these three impacts, you see positive impact in terms of the core operational income that increased in terms of the operational cost that decreased significantly and in terms of impairment and provisions that have also decreased, okay.

I would now go to page 20 and commenting on the different lines of the income statement. In terms of the net interest income, as you see there is an important decrease. This decrease is explained on the right-hand side. There are several effects here. One is the effect of the CoCo's alone and the other is the effect of the liability management of 2011 that I just commented, but the largest one was the country risk issue of the de-coupling of the deposit rate vis-à-vis the Euribor to which most of the mortgages are indexed. As you know, Portugal is facing difficulties and associated to these financial difficulties there was a total de-coupling between the deposit rates on retail deposits and of the Euribor, and the fact that these rates became totally uncorrelated basically explains the decrease in terms of the net interest income. And why is the impact for us particularly big, it is because more mortgages. We're a genuine retail bank for the better or for the worse, so we have – so the quality of our deposit, I would say is better the quality – the diversification of our franchise is higher, but, on the other hand, we have more mortgages also, so in this scenario of de-coupling of interest we face a higher impact. Page 21, in terms of fees, I would say that the fees are resisting quite well in this scenario. The pure banking fees and commissions are quite stable, whereas these other fees and commissions, which are mostly retail fees links to current accounts, to packages and so on, paid accounts are performing well.

The markets related fees due to the situation of course decreased vis-à-vis last year, but the big impact as you say here is the negative fee that is the cost of the state guarantee for the bonds that we issued with state guarantee.

On page 22, you see our net trading income. You see here a couple of impacts. You see on one hand that the repurchase of our own debt has generated this year less than the year before, so the quality of the net trading income for this reason is somewhat better because this is more or less than kind of mark-to-market of our own debt, and is less – I would say is less recurrent.

You see also that last year we have gains on Portuguese government debt or last year, I mean, 2012 we have gains of Portuguese government debt of €106 million and the year before, 2011, we had lost €128 million. And this explains the main impact on our net trading income. As you may see, so the other, so to say more client-driven net trading income is around €50 million and this is quite consistent on a year-by-year basis.

Going to page 23, the operating cost. I would say that when you compare this with the Portuguese environment what was then qualitative terms at the end of the year, was very material, but this is not – we will see this now – the impact, the financial impact of this now in 2013 and not as much in 2012. In 2012, we had the restructuring cost that we see here. You see here that the restructuring program and early retirements have cost us around €70 million, which was more or less the impact of the legal change in terms of the mortality allowance, so one pays more or less for the other. You see that in terms of the above-the-line number of staff cost, they have decreased 14.5%, but to be totally transparent, so the core evolution of the staff cost was around 2% nominal, which is not best, but you will see now in 2013 a better number exactly because of the restructuring effort that we have implemented now at the end of the year.

In terms of the credit quality and provisioning, you see a decrease in the velocity at which the credit at risk was increasing and you see in page 24 also quite constant coverage ratios. And in page 25, what you see is that our mortgage portfolio, which is the core of our business – of our retail business, is performing very well in terms of non-performing loans and in terms of impairment charges. Most of the impairment charges that we have was linked to I would say big loans to companies that explain exactly the evolution, which on one hand is quite positive because this shows that we have – a part of our business, or our core business that is profitable and that is healthy.

In page 26, you see the structure of our collateral. You see that our LTVs of the mortgage portfolio in Portugal is quite conservative, which on the other hand is what explains its good performance. But, in general, our loan portfolio is collateralized. The problem of all collaterals in the company loans and mainly in the big company loans is the value of the collateral when they are indexed to shares and they are indexed to real estate. Of course, as the market evolves, this creates impairment evolution that we see and this in general terms is what we see in terms of the bank.

I would pass now to our Investor Relations to comment on our operations.

Rui Pedro da Conceição Coimbra Fernandes

Thank you. So, let's go in some more detail for Portugal. Both these numbers with you already customer funds, the increase of 1.6% that with a rather stable amount for deposit, and on the loan side a decrease of more than 9%. If we go for P&L now, net income for Portugal, there is a decrease – the deterioration of more than €250 million, which is coming from a decrease on the banking income on one side compensated by this lower cost that was already mentioned, especially on the staff, but this one-off item related to 2011. And the difference for the composite is still with – in a way a one-off tax treatment of last year of €133 million, so which explain the worse result.

In terms of banking income, the decrease is both on net interest income and commission explained by some other improvement. On the net interest income, the decrease in Portugal on the last year comparing to this year it was already presented, it is very much related to market rates that really affect our P&L. And we can see here the difference between last year and this year on the Euribor three months that is the main one that explains this evolution.

Although the good news is when we compare fourth quarter with third quarter where we see a big increase of €80 million, although not all of them should be considered recurrent in terms of forecasting for the future, but there is an important movement on the deposit repricing that represents €10 million out of this €80 million. And last quarter is always a good quarter in terms of recoveries, so some non-accrual that become accruals again coming from recovery efforts. This is normal, although it was very good this quarter, but we should not expect going forward in every quarter to have positive numbers here, it should be as it was during the year, a negative number what we expect and it was already mentioned, is that the new entries being less amount than previously we should expect this negative number affecting net interest income to be smaller in the future compared to the past.

In terms of spread, the evolution of spread, it was very good during the year in terms of the loan spread that increased 53 basis points, in terms of deposit we saw during the fourth quarter the beginning of this turnaround even though it was for the full year it was a big decrease in the spread.

On the loan side, it is mainly on the companies where from the 3.95%, last year at the end of the year compared to the fourth quarter of 2012 is a gain of 35 basis points and loans to companies represent 50% of the portfolio.

For the other 50%, it is more or less the same number, as you can imagine it is very difficult to re-price mortgage especially when the customers are paying. And this is what is happening, we have very well NPL rates there in the mortgage.

For the time deposits, the picture there shows exactly what we were doing, although up to now it is an effort for the full year, but up to now it didn't appear really on our P&L since Euribor was decreasing so much that the decrease of the rate didn't appear as an improvement in the spread. The last quarter we managed for this to start to appear and we hope it will continue quarter on quarter. So, new production, for example, now is at 2.5% compared to numbers at 4% one year ago, and before that, 2% portfolio now we've had 3% and one year ago it was 4.5%, so an important difference.

In terms of commissions, it was mentioned already. The good news is that again apparently the fourth quarter we can see already a recovery here, which means that third quarter was the bottom of the evolution of commissions as well.

On the operating cost, it was mentioned already, there is a lot of specific items that it was present. Now, the restructuring program that happened on the last quarter at the end appear as a decrease on the head count of 977, and this is placed in the three parts, mutual agreement at 626, early retirement 120, and the natural reductions of more than 200, and this is the number, type of the number that we should expect for the next couple of years to have this natural reduction.

The overall cost, it was €69 million and as we mentioned when we were in road show for the capital increase, we said that this program should be done in two years, and we did it in two months, and the effect should be of more than €30 million starting by 2011, and at the end it was better than expected in the sense that we did it in a very quick way. And all the cost that appear upfront in 2012 and now going forward we will have the €30 million savings immediately this year to appear, but when we compare to the 2011, we should consider a higher number if more than €50 million. So, higher than the one we present when we were – for the capital increase and when we present our Strategic Plan.

Now, on credit quality, and we have the main numbers that it was shown already for the consolidated coming from Portugal. We see that the dynamics, actually we have better ratios now compared to September, but it is normal, as we said, for the fourth quarter to always to – these ratios to appear slightly better. We always said that we expect all these ratios to continue to increase up to 2015. The topic and the way it will affect our numbers is that the trend of the increases here it will be lower than in the past. And this is as the – it will be the kind of the slope of the curve that is the one that generates the cost of risk that will be now from something that was exponential up to now, that is turning to a more low rate one, which means that we should expect lower cost of risk for the future compared to 2011 and 2012.In terms – we see this here on the last two quarters. What it shows as well the fourth quarter is that although the net increase in past due 2012 was higher than 2011, we see that although there is a typical trend of the second half to be better than the first, the difference here is important and it shows really that some of the measures taken in the past during the first six months of the year of improving the management of the past due loans in a way we start to see some numbers here and we should expect then that the new entries not to be exactly at this type of numbers, because again the fourth quarter is always better than the previous one, but we should expect really something better than 2012 overall.

Now moving to the international side, the main numbers Poland, Mozambique and Angola all together with €236 million, which is slightly above the numbers of last year. The overall numbers for the international operations was very much affected by the numbers from Greece.

Let's go now in some detail for Poland now. There was an important growth in terms of customer funds and deposits as well, it was the growth of 11% for deposits. And in terms of loans, rather stable, because this 2.5% decrease has an effect of an appreciation of the zloty against Swiss franc. Without this effect, the growth will be at 1% and more here on mortgage than on the other, the decrease it is strategically important as we mentioned before in September that the focus for the Polish subsidiary is much more from now going forward in – for company loans than for mortgage and this is a key part of the new plan.

Now, in terms of net income and rather stable with an increase on the banking income with €15 million, stable operating costs, the income is both on the net interest income we'll see why and from FX gains as well from trade.

On the net interest income, this increase is important because actually the interest rates, the market interest rates were dropping during the year and a strong competition on the deposit side. Even though – and we see that the spreads of deposits deteriorate, still it's positive, so we still make money having more deposits. But on the loan side, we're managing the spread to compensate and not to allow the decrease of market rate to affect our spread. On the net commissions a slight increase, not very important.

Operating costs a stable member, on the staff costs though there was an increase coming mainly from an increase of the social security tax rate on the employer side from 4.5% to 6.5% that represents a big part of this increase.

On the credit quality front, it's rather stable, the number is lower now, the 90-plus from 2.8% – it was 3.1% in September, so we see a decrease here. The increase compared to previous year is mainly due to companies, individuals is rather calm here the increase. And for companies, as it is very well known, the construction sector is suffering a little bit in Poland. Our exposures there is less than 4% of the full balance sheet. So it's really, it's not the big topic, but it was important this year to increase even the cost of risk that was higher than forecasted at least at the beginning of the year.

We should expect for 2013 lower cost of risk compared to 58 basis points that we are presenting now. Even with this increase from 2.3% to 2.8% in terms of 90-plus, it is almost half compared to the numbers of the system.

So, there is no topic there in terms of credit quality now in this period. Just a reminder, we present the strategic target some three months ago, just to remind that we are at 10% return on equity now. The top five banks are more around 14%, 15%, and so is our target for 2015.

The way to go to these numbers, as we present at that time, it is a balanced growth of our balance sheet, balanced, I mean, both in deposits and in credit; but credit more focused on consumer and companies, and deposits more focused on cheap deposits and not so much the expensive time deposits. So it is this type of growth that will make a better net interest income and the increase of return.

Core Tier 1, and so both capital and liquidity very comfortable situation in our Polish subsidiary. They're completely independent from BCP, from the mother. They do not need funding from Millennium bcp. They don't need capitals for this expansion, at least Strategic Plan that we are presenting. In terms of capital, as it was announced, it was approved through IRB for the most part of the retail portfolio. There it was approved that the full impact is around €1.6 billion, and it was approved in a way that this year 2012 around €300 million appear as a decrease of risk weighted. The next €300 million it will be in 2013 and then €1 billion in 2014. So this is something – a proof that you can consider in your calculations.

Moving to Mozambique, in terms of volume, deposits and the customer funds increased 5%. If we see this in local currency, the increase is 19%. In terms of loans there is this decrease, but in local currency there's an increase of 12%, so an important dynamics here on the volume side. On the net income not so well, this decrease is coming mainly from the decrease on the net interest income. Of course we are still on an expansion plan there so we'll have increase in costs.

And the reason why net interest income decreased we can see on the next page. This decrease of 7% is definitely given the market rates that are decreasing there. I remind you that last year the market rates on average were at 15% and now they're at 5%. So this affects the loan side and on the other side because the position of liquidity is very comfortable, we use the excess for public debt as well and of course the rates there decreased as well. So, this affects net interest income, and even having a positive effect from commission, it was not enough to compensate.

We are, as we mentioned before, we continue our expansion plan. We opened 13 branches during this year and hired 67 more employees, so this naturally has an impact on the operating costs. And, as we promised previous time, when we present the Polish target, we said that this time will be the time for both Mozambique and Angola. So, the challenge here for Mozambique is in a way to – as you know, and it is very important to remind you, we have more than 30% market share, so we are the bank in Mozambique.

The challenge now is to maintain this leadership, but at the same time to maintain this type of return on equities above 20%. The way we will do this is to continue our branch expansion, but to reinforce the topic of – and the growth of volumes both for corporate on the loan side and to pay particular attention to the Prestige segment on the deposit side.

We continue to expect for the future to grow more than the country, so that is a country that is expected to grow at 8% per year. We continue to expect to grow at this pace. But it will be more a volume oriented growth here that will generate more net interest income and of course the net income that we expect will be an important contribution for the repayment of the CoCo's.

Some note on page 49, two or three things that I believe nowadays everyone knows very well, but – which is the potential growth for Mozambique. It was already like this based on the coal production that is expected for the future. But recently with the new gas reserve, oil discoveries made this country really to have an amazing potential, which is very comfortable to be in a country like this with 35% market share.

Moving to the last topic, Angola, here we grew in terms of deposits and loans at around 3%. If we do this in local currency and the growth is around 6%. For net income, net income increased around €4 million, coming from a nice dynamic on the banking income everywhere, net interest income, net commissions and even for FX as well that was more than enough to compensate the increasing costs due to the expansion plan that we are doing. Again, in Angola we opened 15 branches and we hired more than 130 employees.

Here the dynamics of the net interest income although market rates went down, here we completely compensate by the volume effect that we show before and we manage as well to maintain more or less the same net interest margin. So it was the volume that generates this growth. In terms of commissions, transfers and credit and guarantees were the main responsible for this growth.

And again the strategy for Angola, obviously the two countries and the two banks are quite different, but more or less

the same target we have. So, the challenge here is to continue to grow to gain market share with return on equities on top of 20% and this should appear not only with an aggressive expansion plan, but again looking to the corporate side and the affluent customers as well. It is supposed for us to grow above GDP, well above GDP and to gain market share, but this, again, is through volumes that we expect to increase net interest income and net income as well and to move the return on equity to this type of number.

As a conclusion, this is the table that we presented already and we bring here every quarter and we present the medium-term, as you remember medium term is 2015, we present this target and the target for more long-term 2017 when we were in the road show. It is important for us every quarter to come here and to compare with this target. What we can see is that very comfortable capital and liquidity position today. And, of course, especially Portugal, the next years will be important to improve our cost to income and of course, the cost of risk as well. That cost to income as we said at the time it will be we mainly through the repricing of the time deposit. We've reduced a lot the time deposits rate, but we didn't manage yet during 2012 to improve the spread, even the decrease of market rate.

Operating costs, we did it one shot at the end of the year so we'll have immediately the decrease in costs immediately this year. Cost of risk, we decreased already comparing 2012 with 2011, but going forward, it will continue the trends for numbers more close to 100%.

And we are still on the first stage of our Strategic Plan, which is the stage of looking to balance sheet and it will the year 2013 to continue like this, although to create or raise the conditions for the future profitability, both in Portugal and on the other countries that we consider core.

Overall, what we are presenting here, it was in line with the Strategic Plan that we presented some six months ago.

Q&A

Operator

Thank you, Our first question comes from Carlos Peixoto of BPI. Please go ahead.

<Q - Carlos Peixoto>: Hi, good afternoon. First of all, just a small couple of detailed questions. Basically I was wondering if you could provide us some data on the evolution of foreclosed assets and its coverage. And at that same time – and, well, similar to what happened in other Portuguese banks, I was wondering if you could give us some data on assets being transferred to the real estate and construction or restructuring fund? What was the amount of loads that were transferred to these funds and whether there were any provisions related with this in this quarter, and also what might we expect on this front going forward? Thank you.

<A - Miguel de Campos Pereira de Bragança>: Carlos, so, in terms of the amount that's over the full year was transferred to the recovery funds, let me just here give you in one minute the amount that was transferred in the year, it was €690 million and the impact that this had in our income statement was €130 million of provision. Okay.

And in terms of the foreclosed assets, the total foreclosed assets evolved to €1.41 billion compared with around €1.3 billion and the stock of provisions is at around €320 million, so we have now a coverage of 22.6%. Okay. Hope this answers your question, Carlos.

<Q - Carlos Peixoto>: Yes. Thanks.

Operator

Our next question comes from Antonio Ramirez of KBW. Please go ahead.

<Q - Antonio Ramirez>: Hello. Good afternoon. Couple of questions from me. First on the net interest income performance in Portugal in the fourth quarter. You explained basically three impacts, one from deposit repricing, then funding and then the accrual of interest on the past due loans that were recovered, and that's the one – is the one you claim seasonality in the fourth quarter. So, if we think about 2013 – and you expect further a positive impact on margins coming from the continued re-pricing of deposits – how much do you think is the potential impact from that?

Should we annualize what we saw this quarter or – and then forget about the past due. So how you see the net interesting income in Portugal evolving? And on these main impacts you described for this quarter, what should we be considering in 2013 as recurrent? So that's my first question.

Then second question is regarding Greece, if you can – I know there is nothing agreed yet on the negotiations you've started with Piraeus, but if we would assume a transaction similar to the ones we saw for the French banks where they were selling their Greek operations for €1 after re-capitalizing them, so what could be the impact? So can you remind us the risk weighted assets you have in Greece that you will be deconsolidating in case of selling the company or the Bank?

And also, can you remind us how much is left of the generic provision that you booked in the third quarter. So, how much is still available in case you need to take more losses or increase the provisioning level in Greece. So, what would be the impact if you deconsolidate the Bank in Greece tomorrow and you get €1 for that, would be my question.

And also related to that – I'm sorry, there's three questions not two, can you explain the move we had in the fourth quarter on the provisions different to loan losses, it looks like you did a massive recovery of around €280 million, that then seems to have been booked as more lending provision and I would assume this is related to the generic provision in Greece, but if you can explain please. Thank you.

<A - Miguel de Campos Pereira de Bragança>: In terms of the net interest income, as you know, what we have presented in our Strategic Plan, and in terms of our road show, is that over the medium term we would convert to cost of deposit – to a negative cost of deposit of around 165 basis points, assuming that the Euribor will stabilize at more normal level than what it is right now. And our net interest income is very sensitive. It's very sensitive to, of course, the Euribor rate. We do expect that before CoCo's, we will have a positive evolution of the net interest income in Portugal. However, after CoCo's, we think this will be more or less compensated, but a lot of it will depend on the Euribor and we give you enough information in terms of interest rate sensitivity for you based on your Euribor estimations to, I should say, estimate our net interest margin.

But, in terms of core, yes, after CoCo's, the impact is less straightforward, okay. In terms of Greece, so what I can tell you is that we have around €4 billion risk weighted assets in Greece and we still have around €430 million of the provision left. In terms of what would be the impact if we sold this for €1 or not, I mean you can do the numbers. I would prefer not to do it myself, in order not be quoted saying it is in the middle of a negotiation, okay. The numbers are easy to do, so you can do different assumptions. I won't give any guideline because anything that I may say may even be put in question due to confidentiality reason.

The last question, I did not totally hear, we will answer it. Rui will answer it.

<A - Rui Pedro da Conceição Coimbra Fernandes>: I believe you are referring to the increase on the provisions – on the other provisions and the main one on the fourth quarter is related to the transfer to the recovery fund, which is more than – around €100 million, I believe this was the question.

<Q - Antonio Ramirez>: Well, more specifically, it looks like in the fourth quarter you had a recovery, so a positive on other provisions of around €280 million. But, then you have a very elevated loan provision, so it looks like there is a transfer there or a reclassification, so apart from the €100 million you mentioned on the fund for construction, is there other moves as well or that's all?

<A - Rui Pedro da Conceição Coimbra Fernandes>: Look, because definitely I cannot find this decrease on provisions that you're mentioning, do you mind if we discuss this after?

<Q - Antonio Ramirez>: Yes, okay. No problem. Thank you.

<A - Rui Pedro da Conceição Coimbra Fernandes>: No, Miguel, just a brief explanation. In the fourth quarter basically, we didn't decrease our provisions, we increased our provisions, and we didn't use the Greek provision, basically that is the key line. We've some compensation of provisions, but all in all it was – we increased our provisions for other assets, for loans and we didn't decrease our provisions for risk. Okay?

<Q - Antonio Ramirez>: Okay, thank you.

Operator

Our next question comes from Ignacio Ulargui of BBVA. Please go ahead.

<Q - Ignacio Ulargui>: Hi, gentleman. I have two questions the first one is regarding the on-site inspection and the €206 million that you booked in 2012, whether you expect further provisions as of these incoming quarters? And the second question is, if you could just provide us with some light on the

capital gains, long term capital gains that you could have in your sovereign bond portfolio at this stage? Thank you.

<A - Miguel de Campos Pereira de Bragança>: Okay. In terms of further provisions, you know the size of our credit portfolio. So, we have a credit portfolio of around €67 billion in terms of these on-site inspection programs. Of course, our models, our strategical models have always performed very well in the SIP and – in the on-site inspection program.

So, the issue here is the assessment of the large loans sometimes. And as you know, it is almost impossible to – this is not totally a science, so when you discuss with an external auditor whether it's necessary to provide 20% or 21% or 23%, or I mean, when you speak about a large loan, it is not as scientific as when you do the general provisions. What you also see is – so is that the amount that has been implied by these inspections programs relatively to our credit portfolio of €67 billion is relatively small, so – and even if you compare it with the loans to company, which is half of our portfolio of €33 billion, it's relatively small. So, it is – I think that we are well provided for or that we are provided for in accordance with Generally Accepted Accounting Principle. This is already the second inspection.

According to the macroeconomic evolution, whether a specific macroeconomic evolution will have a higher impact in one loan or a lower impact in another loan, I cannot promise anything. The only thing that I can promise is that we are provided for according to General Accepted Accounting Principle and that we have already had two inspections and that these inspections, in spite of the numbers that seem large, are not that large when you compare it with the size of our portfolio.

So, in terms of the capital gains implicit in our Portuguese sovereign portfolio, the total capital gain, so, netting, netting the positives and the negatives is €70 million. I can – I have to stress that this comes from a capital loss at the time of the EBA, in excess of €860 million. So, this is a very important evolution in terms of the mark-to-market of our portfolio. I also would like to say that from our portfolio, only one quarter has more than three years. So, the price volatility and the conservativeness of the portfolio in terms of duration is important.

<Q - Ignacio Ulargui>: Thank you very much.

Operator

Our next question comes from Jaime Hernández of Nomura. Please go ahead. Our next question comes from Juan López of Banco Espirito Santo. Please go ahead.

<Q - Juan Pablo López>: Yes, thank you for taking my question. Actually, I have three questions. First one is very straightforward question and this is regarding Romania. It looks the losses are accelerating in the quarter and getting where I calculate €14 million losses in this quarter. I was wondering if there is any specific reason for that, €14 million loses.

The second question is regarding the NPL entries. I was very positively surprised that looking to the recent trends, I was wondering if you could elaborate a little bit more on that. What's the impact of the transfer of the loans to the recovery fund that you mentioned, I don't know if that explains part of this fall, or what you're seeing in terms of NPL entries, in terms of corporate loans, recoveries, just some color on that and potential trend as well.

Lastly, regarding the recovery fund, you mentioned the amount that you transferred, do you expect to transfer more to the recovery fund? Did you book these loans as nonperforming before they transferred to the recovery fund?

And I'm sorry, one last question, this is more a strategic question, it's regarding Poland. I don't know if you could give us also additional color regarding Poland, regarding the timing, and the potential negotiation power that you have regarding the recent rumors that the European Union could force you to sell Poland, so if you could give us some details regarding the timing there that will be great. Thank you.

<A - Miguel de Campos Pereira de Bragança>: Okay. Starting with the last question, okay. In terms of Poland, what came out in the paper were pure rumors, so we have had absolutely no negotiations up

until now with DG Comp and we don't have any guidance from DG Comp in terms of the sale of any specific asset. Okay, they are pure rumors. And what we – and we expect – of course we cannot assure it, but we expect that potential remedies that will be imposed upon the Portuguese system will be consistent with the program that was developed at the national level. So contrary to two other countries, Portugal has a program. In this program of €78 billion, €12 billion were earmarked for the capitalization of the banking sector and together with the capitalization of the banking sector, every bank was suggested or forced to present a funding and capital plan that is part of the strategy of each bank and that is consistent with the adaptation of the country and that is consistent with the macroeconomic evolution of the country. We have presented this funding and capital plan and the sale of Poland is not a part of this funding and capital plan. So this is what would seem fair to us, but on the other hand the negotiations haven't started. So I cannot comment on something that has not started and I cannot comment too much on rumors. What I can tell you is that we have had absolutely no negotiations with DG Comp in terms of sale of assets. Okay.

In terms of the transfers to the restructuring fund, to give you a little bit more of highlights in terms of restructure. First, we do think that the transfer to this restructuring fund has economic value, it's not a pure transfer, it basically a way for the different creditors of one bank, of one institution that is in financial distress to sell their credit at market price to specific fund that are only allowed to buy it at market price and they have the incentives to buy it at market price. And based on this they are able to coordinate so to say the strategies of different borrowers and they are able – they are in a much better situation to implement the turnaround of this company. So, the credits are sold at market price and in change for it we receive so to say units, participating units in the fund. As the different banks that sell credits to these funds have asymmetric positions, there is, so to say – there are enough incentives and controls to assure that the credits are brought at market price, and effectively when we sell our credit at market price, we have losses and it exactly these losses and the provisions that I commented right now in terms of the income statement. Okay.

In terms of the transfer to the recovery funds, the impact in terms of NPLs of the transfer of the recovery funds, the full year impact is around €160 million. So, I cannot comment, I don't have here the number of the quarter.

And in terms of Romania, the numbers that I have a loss of €24 million, which is not very relevant in terms of the evolution of the Bank. So, Romania is a start-up, is a company, is performing according to plan, but as a new management team are very much focused on priorities. So up until now our key priorities had to do with the capitalization of the Bank, with liquidity, with the turnaround in the main geographies, and to be totally transparent. So, up until now Romania and the issue of Romania due to its size has not been top of our priorities, so no decision has been taken yet. But what we can say is that is evolving more or less according to plan, €5 million more or €5 million less, so it's not very relevant.

<A - Nuno Amado>: This is Nuno Amado. That's correct what Miguel mentioned, it's totally correct, but I want to add on one point and the point that I would like to add on is the following on Romania. The result of last quarter was not the normal result, the normal loss because we canceled a tax, deferred asset that we have in our book. So, you cannot multiply by four the result of the fourth quarter of Romania. That's clear because there was an extraordinary item on it.

That's the only small adjustment that they would like to do.

<Q - Juan Pablo López>: Okay. Thank you very much.

Operator: Our next question is a follow-up question from Carlos Peixoto of BPI. Please go ahead.

<Q - Carlos Peixoto>: Hi, again. Good afternoon. I was wondering if you could also shed some light on the impacts of the pension fund, namely, what was the impact from the change on pension fund that drove the differences vis-à-vis the total impact of the pension fund in the quarter. And also, what was the amount of write-offs done this quarter? Thank you.

<A - Miguel de Campos Pereira de Bragança>: In terms of the pension fund, as you know we have here a different impact. So, one impact that we have that is a negative impact is the return of the pension

fund vis-à-vis the assumptions. As you know, our actuarial assumption was a return of the pension funds over 5.5%. As we had 1.6%, this had an impact of €91 million in terms of difference. Then we had a positive performance in terms of wage and pension versus assumption. So, this positive performance has a positive impact of around €17 million, so one-seven. And then we have here the change in actuarial assumptions that is the reduction of the discount rate, which is negative in terms of the present value of the liabilities and the reduction of the wages and pensions growth rate, which is positive. The impact of these actuarial assumption difference is €90 million. Okay. Thank you.

<Q - Carlos Peixoto>: Thank you.

<A - Miguel de Campos Pereira de Bragança>: I'm sorry, the write-offs were €280 million; this was your other question.

Operator: Our next question comes from Jaime Hernández of Nomura. Please go ahead.

<Q - Jaime Hernández>: Hi. Hello. Thank you very much. I apologize because when I was going to ask before, I had

a problem with the telephone, and I've been disconnected for a while, so I don't if the – I'm sure that some of my questions were already answered. But I would like to ask you, please, regarding the recoveries of the quarter. You just provided the write-offs together with the recoveries that in some way implies that the gross entries were still high. I will like to know of course if there is a kind of seasonality in this fourth quarter with recoveries. If there was something, I don't know, punctual and if you can elaborate a little bit more on the recovery levels because we saw that this explains also a big part of the increase in the fourth quarter of the domestic net interest income.

And also if you can please provide the approximate level of the residual loans. Thank you very much?

<A - Rui Pedro da Conceição Coimbra Fernandes>: Hi. It's Rui. Let me answer to the first question. If you see the picture on page 36, on the new entries, for the second half this decrease, this €203 million is really already taking into consideration both write-offs and transfers for the real estate funds. Because actually if we do not take this into consideration, the new entries are negative and that's why we mentioned that it was really a good semester although with some seasonality there.

Let me tell you, first, if we just make the gross difference on the new entries is minus €335 million, then you should sum-up the write-offs of the second semester, which is €381 million and then sum please the transfer to real estate funds, which is €157 million. And this is the three parts that gives the €203 million, okay?

<Q - Jaime Hernández>: Yes, but, on the level of recoveries of the quarter, I mean, the gross entries without considering the recoveries, I am trying to see how big the net – the recoveries were in the quarter, it looks like that they were really high and if there is someone, if there was kind of one-off in the quarter? That's why I also asked you regarding the residual loans, just to be sure that there was – that it's not being because of higher level of residual loans.

<A - Rui Pedro da Conceição Coimbra Fernandes>: Look, the number I mentioned, the negative variation, the minus €335 million is already net of recovery.

<Q - Jaime Hernández>: Of the recoveries?

<A - Rui Pedro da Conceição Coimbra Fernandes>: I'll give you then the two parts of the entries and the recoveries after, okay, but the main one is less entries this time...

<Q - Jaime Hernández>: Yes, okay. Thank you.

Operator: Our next question is a follow up question from Juan López of Banco Espírito Santo. Please go ahead.

<Q - Juan Pablo López>: Hi, thank you. My question has already been answered. Thank you.

Operator: Our next question is a follow-up question from Carlos Peixoto of BPI. Please go ahead.

<Q - Carlos Peixoto>: Hi, again. As a final question, I would like to ask you what's your view on or what's your expectations on the evolution of cost of risk for next year? You already mentioned that you're expecting a stabilization or a mild increase – or a mild improvement in terms of NPL's, net new entries if I understood correctly. I was wondering what's your expectation for the level of cost of risk for next year. And also in terms of NII, what do you expect to see at the Group level for next year, bearing in mind it's – if I recall correctly next year – I'm referring to next year, but I'm referring to 2014, sorry for that – bearing in mind that if I recall correctly this year you'll have the full impact from the CoCo's cost in NII, whereas in 2012, we only had half of this impact. I was wondering how you see this playing out with the improvement in deposits cost that we saw this quarter.

Thank you.

<A - Miguel de Campos Pereira de Bragança>: Carlos, it's Miguel Bragança. As you probably – probably you were not listening, but in terms of the NII, I have also already given the answer probably. If you need any additional information, maybe we can take it later, but just not to repeat it to the other people because I had already given the answer to this question. In terms of the cost of risk, what you know, and if you take a look at here at page 55, is that we're expecting a progressive convergence to more normal levels, assuming that the situation in Portugal stabilizes as we all are hoping in our basic scenario to a level of around 100 basis points in 2015. So, right now, we're at around 180 basis points if I would have to – I mean make here an estimation, we would expect to be quite linear in terms of the evolution from 2012 to 2015.

<Q - Carlos Peixoto>: Okay

<A - Nuno Amado>: This is Nuno Amado. I just want to add one or two things. The first thing is that we still estimate this year as a tough year for obvious reasons. If you see our Strategic Plan, 2012 and 2013 are years of preparation, let's put things like that, for the profitability and for future growth, so this year, we estimate clearly a tough year. What meant, we estimate that the net interest margin will keep on going. The management of it on a very precise way in such a way that what we call the commercial margin will improve. However, there are other factors that will affect it, as Miguel mentioned, which is the interest rate, the Euribor level, it's very important for us. And the second is obviously the full impact of the CoCo's this year. So, we are positive on the commercial side. We have some impact that we cannot totally anticipate as the Euribor issue.

On the impairment charge, we think that, as Miguel mentioned, we estimate a lower level than in last two years, but still high level, that's clear – that's obvious. We also think that our strategic presence in other markets will add on as they did this year, and we'll have not the impact or the same impact as we had on Greece this year, and we've not –probably much smaller, but the impact of Romania as we had this year because we also had done extraordinary items there.

So, all in all we think difficult year, 2013 year, but better prepared than we were one year ago, that's for sure, so we are better prepared, we cannot be – we are conservative, but more optimistic than we were in March last year. That's I think my overall view.

Operator

That will conclude today's question-and-answer session. I'd now like to hand back to Mr. Amado for any closing or additional remarks.

Nuno Amado

I just did it, so it was my pleasure to hear all the questions, and I hope that we were transparent in regard to the answers right, if not we will send to you some more details on the next days.

Thank you very much, everybody.