Conference Call Transcript

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PRESENTATION

Operator

Good afternoon, ladies and gentlemen, and welcome to the Millennium bcp First Half 2009 Earnings Conference Call, which will be hosted by Carlos Santos Ferreira, Chairman and CEO, followed by Sofia Raposo, Investor Relations. My name is Mattie and I will be your coordinator for today's conference. For the duration of the call, you will be on listen-only. However, at the end of the call, you will have the opportunity to ask questions. (Operator Instructions).

I am now handing you over to Mr. Carlos Santos Ferreira to begin today's conference. Thank you.

Carlos Santos Ferreira - ***Millennium bcp - Chairman and CEO***

Good afternoon, ladies and gentlemen, and welcome and thank you for attending this conference call. Let me start by telling you that during second quarter of 2009, the main focus of the Executive Board of Directors was on measures to reinforce our capital ratios and implement structural changes to our pension fund. The Tier I capital ratio increased to 8% as of the 30th of June 2009, a level in line with the recommendation of the Bank of Portugal for September. Core Tier I ratio increased to 6.2% and the total solvency ratio to 11.1%.

The ratios reflect the positive impact of the full subscription of the public offer of the Millennium "Value Capital 2009" issue for a total of EUR300 million as well as the positive impact related to the pension fund, the result of a change of the actuarial assumptions and, I should stress, of structural change in the benefits associated with the pension plans. These ratios do not yet include any future private placement designs for institutional investors of Millennium "Value Capital 2009" issue.

We expect to have the first of our private placement of EUR200 million more fully subscribed within the next week. This should add a further 30 basis points to the Tier I ratio. And we will keep issuing "Millennium Value Capital" as much as we consider necessary to give us a very comfortable Tier I ratio. I hope that the ones that are taking this into consideration for their own judgments can have this data, actual data, and not old ones into consideration.

After -- and this is, in my opinion, less important -- net income was up to EUR147 million. And despite the interference in Portugal, business volumes continue to grow, with loans increasing 5.1% and deposits increasing 6.9%. Net operating revenues increased by 10%. Let me say that total costs decreased in the same two quarters by 5.2%. In fact, in the scope of the Bank's strategic priorities for 2009, we have developed a series of transformational initiatives with increasing visible results. The evolution of the Bank's cost base is one good example.

Net income has been influenced by the lower contribution of our international operations. As you know, the effects of the global economic and financial environment have been more pronounced in Poland. But I would like to stress that directed implementation of an adjusted strategy has already had positive impacts. This is not what some have forecasted in the past, but Poland has not assisted disaster. The Polish economy, in our opinion, will not enter a recession and the zloty has increased in comparison with euro and the Swiss franc.

During these six, almost seven or eight months of turnaround, our costs have decreased in a very sharp way in Poland. If we compare the first two quarters of 2009 with the last net figures of 2008, costs have decreased more than 15%. In these two quarters, almost 10% of the staff has been dismissed. The levels of Core and Tier I and solvency ratio have increased and the Bank has achieved to keep the market shares they have in deposits and loans.

Speaking about international operations, in Mozambique, -- net income increased to EU27.9 million. And in Angola, with two quarters, we have already almost done the results that we have forecasted in our budget for the year. Regarding one point that today is quite important -- the credit quality and cost of risk -- what we have in our hands is what we have forecasted in our budget.

If we are talking about impairments, impairment charge stood at 75 basis points in first half of 2009, comparing with 74 basis points in 2008. If we are talking about non-performing loans, the ratio increased to 2% and this is in line with our peers in Portugal and, as you know better than me for sure, slower than what we have in the Portuguese market. Anyway, it's in accordance with what we have forecasted in the budget.

May I try to sum up? The Bank has reinforced its capital ratios and, as you will notice, Tier I is the highest of this decade. We have a quite more solid liquidity position. Cost reduction efforts are consistent, as you have recognized, and are showing the results of more than one year of work. Repricing is underway. The impairment levels and non-performing loan levels are in accordance with our budget and the international portfolio. Regarding the international portfolio, we are happy with our operations in Africa and we believe that the operation in Poland has started already the turnaround.

I now ask our new Investor Relations, Mrs. Sofia Raposo, to start the presentations with the details of the Bank's performance in the first half of 2009. Thank you very much.

Sofia Raposo - ***Millennium bcp - Head, IR***

Thank you, Mr. Chairman. Good afternoon to all. I would like to start with a presentation, with the highlights for the first half 2009 results. Basically, as the Chairman has said, we have strengthened the capital ratios with Tier I increasing to 8% and Core Tier I rising to 6.2% in June 2009. Our net income grew by 45.5%, reaching EUR147.5 million.

The banking income increased by 10% and costs declined by 5.2%. In Portugal, we would highlight costs and risk control in a context of economic recession and especially with interest rate's steep decline, while international operations were affected and continue to be affected pretty much like the first quarter, also by the impact of the current crisis.

Loans and deposits and on balance sheet customer funds continue to grow despite the unfavorable economic environment. And we believe we have a solid and prudent liquidity position. Our new debt issues of EUR3.8 billion until June 2009 were completed. We have a stable commercial gap in the last few quarters. Highly liquid assets improved to EUR7.2 billion and we still maintain the possibility to use up to EUR3.5 billion in State guarantee.

With regards to the net income and moving into slide four, the net income increased by 45.5% to EUR147.5 million and basically reflects and was affected by the 93.6% decline in international operations, while results in Portugal were benefited from the fact that there were no capital losses in BPI this year as we sold the operation in December 2008.

We have also the benefit of lower costs, as you already know. And basically, we were penalized in some way by the increasing impairment and lower net interest income and commissions, which were affected by the economic environment and net interest income affected by the decline in interest rates. This is partially offset by trading profits, mainly resulting from gains in interest rates.

Moving into volumes, and even though the economic environment is not favorable at this point, business volumes continue to increase with loans (Company corrected after the conference call) up by 5.1%. We would highlight the increase in mortgage loans by 7.2% and corporate loans by 3.6%. With regards to customer funds, they remain broadly flat with on balance sheet customer funds rising by 3.6% and with a notable growth of deposits by 6.9%.

With regards to the capital ratios, we have strengthened them during the first half of 2009. Tier I improved from 6.8% to 8% in June 2009, while Core Tier I increased from 5.5% to 6.2%. And total ratio increased from 9.9% in the first quarter to 11.1% in June 2009. The Core Tier I benefited from the EUR371 million actuarial gains from the change in the pension fund assumptions as we will see later on. And Tier I further benefited from the issue of EUR300 million of perpetual subordinated debts.

These ratios do not include the positive impact of the approval IRB advance that is pending on the Bank of Portugal. A conservative estimate for an IRB foundation adjusted would improve our Core Tier I to 7.2% and our Tier 1 to 8.4%. We would expect that the approval by the Bank of Portugal should occur during the second half of 2009. We, as the Chairman has said, would also expect to complete the private placement of EUR200 million of perpetual subordinated debt within the next week.

As you can see in slide seven, the current capital ratios - of Tier I 8% and Core Tier I of 6.2% are one of the highest of the last decade.

And with regards to the pension fund, I would like to note that we have material and structural changes to the pension fund and to the pension liability.

So, starting with the first issue and following the agreement with the unions for 1.5% salary increase in 2009 and considering that inflation expectations going forward are fairly subdued, we believe that the assumptions we had for the salary and pension growth were clearly excessive and thus we have reduced the salary and pension growth rates by 50 basis points from 3.25% and 2.25% to 2.75% and 1.75%, respectively. This represented an actuarial gain of EUR371 million that positively affected the Core Tier I.

Second place, we have also changed the financing conditions of the defined contribution funds for employees hired from July 2009 onward. We believe it will improve the value of the Bank in the future. Before, the Bank contributed with 4% and employees with 0%. From now onwards, the Bank will contribute with 1.5% and the employees with 1.5% as well. This aligns the pension benefits for new employees with market practices.

Another important change for the future and that has been decided by the Executive Board of Directors is the change in conditions for the benefit attribution of the Defined Benefit Fund. First of all, the Bank will only contribute to the funds if the return on equity will be higher than government bonds plus 5%, but with a minimum of 10%. Second, although employees will retain previous benefits, there will be changes in the pension calculation formulas that represent a split of benefits between employees and the Bank.

The value of this responsibility on the overall stands at around EUR400 million and the change in the conditions will reduce this amount to around EUR15 million (Company corrected after the conference call). So basically, as we are talking about the Defined Benefits Fund, this has no impact on Tier I or pension liabilities, but will indeed reduce the personnel costs from 2010 onward by an estimated EUR15 million. And this represents a net present value of around EUR250 million to the Bank. Therefore, we believe we made some very significant and structural changes in the pension liabilities and pension fund.

With regards to the pension responsibility, I would like to note that the pension liabilities are 107% covered, following the contribution we made last year and the fund's performance. The pension fund has had a positive performance of 4% and total actuarial gains amounted to EUR450 million, including the EUR371 million impact from the changes in the pension fund. Also, we would like to note that the equity exposure of the pension fund has reduced quite significantly in the past year and now it stands at only 22%.

With regards to liquidity, we have completed our EUR3.8 billion of this year's debt issues and basically have almost completed the funding plan for 2009. Further, we have improved the eligible assets portfolio to EUR7.2 billion during the past year and we still have EUR3.5 billion available to issue with State guaranty in a total of EUR14.5 billion that more than covers all the refinancing needs we have for the next three years.

Moving onto slide 12, I would like to highlight that the banking income improved by 10%, as I said, mostly due by the fact that we do not have capital losses and BPI during the year, while operating costs declined by 5%. If we exclude the specific items that we had, both in 2008 and 2009, nonetheless, the banking income would have declined by 7.4%, but is matched by a decline of 7.2% of costs as well.

The results in the banking income, basically reflect the decline in banking income of international operations while in Portugal, excluding extraordinary items and -- sorry, specific items, banking income declined by 2.8% only.

With regards to the net interest income, it declined by 19.8% to EUR675.6 million and basically was affected by a strong decline in international operations and also by the decline of 14.2% in the Portuguese net interest income.

Commissions are still declining year-on-year, but mostly relates to the decline in market-related commissions. If you look into the core banking commissions in the first half of 2009, you see that there is already a slight increase on a year-on-year comparison and that is much more visible in terms of quarterly performance with the second quarter commissions growing by 9.1% in terms of banking commissions and, on the overall, rising by 5.5%.

With regards to costs, we have declined costs by 5.2% in Portugal, where costs have declined by 2% and international operations where costs have declined by 10.8%. This is reflected in the decline on personnel costs of 1.6%, decline in admin costs by 10.6% and decline in depreciation by 3.4%. This is a significant decline that happens in spite of the 79% increase in pension costs and if you were to exclude the pension costs, operating costs would have declined by 10.2%.

With regards to staff costs, we would like to highlight that there has been significant containment in all operations with the exception of Africa and we believe this is very visible in the slide 17. In Portugal, total personnel costs rose by 7.3%, but this basically includes the pension costs which rose 78.6% and if we were to exclude that, remunerations declined by 5.9%. And this happens --without a significant decline in the number of personnel, which basically happened only in Poland.

With regards to admin costs, they have declined by 10.6% and I would like to show a detail of the main changes that happened during the year. You can see that there are very significant declines in outsourcing, maintenance, consumables, consulting, insurance, independent work and that shows the efforts that we have been making over the past year.

The cost to income has declined from 55.9% to 54.5% in the first half of 2009 and it's continuing to show significant and material declines since 2004.

With regards to impairment, the impairment levels are still 75 basis points of loans, but have decreased quite significantly when compared to previous quarters.

With regards to credit quality, we would like to note that overdue loans of 90 days reached 2%, which is an increase from 0.8% last year. But we would like to note that this includes the change in the write-off policy, which had an impact of 0.4pp (Company corrected after the conference call). The coverage ratio is 132.3% and, as I said before, the impairment charges stood at 75 basis points of loans. We would also like to note that BCP presents some of the best provisioning levels among the Iberian banks. And with overdue loans coverage of 111% and on balance sheet total provisions as percent of loans of 2.59%.

With regards to Portugal, we would like to highlight that loans' rise was 4.3%, mortgage growing by 5.4% and corporate loans growing by 3.3%, while on balance sheet grew by 2.4% and deposits growing by 6.9%. The banking income obviously rose quite significantly and operating costs fell by 2%. Excluding the impact of specific items, nonetheless, banking income would have declined by 2.8% while costs reduced by more than 5.3%. And thus, cost to income in Portugal declined from 55.9% to 54.5%.

The net interest income in Portugal declined by 14.2% to EUR506.3 million and was mainly affected by the impact that the sharp decline in interest rates had on deposit margins. The speed of the decline in interest rates was unable to be compensated by the repricing impact in course and we expect should continue and proceed in the next two years.

As you know and as the majority of retail banks, BCP has a positive sensitivity to the interest rates. As a trend, the net interest income would increase when interest rates increase and decline when interest rates fall. This basically happens because the margin in demand deposits declines as interest rates reduce.

Considering that the Euribor 3 months rate and short-term rates have come down very fast and sharply from 5% levels to 1% levels during the past 12 months, with an average decline of 3 percentage points when compared to the first half of 2008, our deposit margin has been clearly penalized. And repricing, although quite material in terms of new production, was unable to compensate the size of the decline in the deposit margins as only a third of the corporate portfolio reprices every year.

I would like to note that only the corporate's portfolio, large corporates and SMEs, can be fully repriced and at the mortgage portfolio which represents 36% of the loan book, Portugal cannot be repriced. Thus, only new production can have higher spreads than before and are now being booked at an average of 1.6 percentage points in the second quarter. However, as the new production in mortgage is low, the impact on the portfolio of mortgage loans is limited.

But with regards to corporates, however, new production is actually being booked with significantly higher spreads, which have increased by 1.6 percentage points on average since the first half of 2008. And we would like to note, however, that only a third of the portfolio is repriced every year. And even those spreads of new production are being booked at around 4%, the repricing still means that the whole portfolio spread rose only by 35 basis points (Company corrected after the conference call). It also means that the repricing efforts should continue to show results for the next two years.

The increase in the net interest income in corporates and companies during the first half of 2009 illustrates the impact that one year of repricing can have on the net interest income. So going forward, we would expect to have also a small decline in terms of net interest income in the third quarter, but should recover quite considerably from 2010 onwards.

With regards to commissions, it is pretty much the same low growth levels that we would see in consolidated figures, but there is a much more significant increase in core banking commissions and it is very visible that there is an improvement on a quarter-on-quarter basis.

With regards to the cost reduction in Portugal, which declined by 2%, we would like to note and highlight the decline of 15.3% in admin costs and 9.5% in depreciation whilst remunerations and salaries in Portugal declined by 5.9% excluding the pension costs. Slide 33 gives you an idea of the dimension of the efforts that we have been pursuing over the past 12 months.

With regards to credit quality overdue ratio over 90 days stood at 1.9 percentage points and I would like to note that the write-off policy had an impact of 0.4pp (Company corrected after the conference call) when compared to last year. The impairment charge as a percent of total loans stood at 70 basis points of the portfolio and declined in the second quarter when compared to the first quarter.

Slide 35 illustrates that our past due loans ratio is well below the sector which has also increased over the past 12 months even though it's only stands at 3% and BCP is fairly below the average, which goes to show the correctness of the credits revision analysis of the Group. We would also like to note that our client satisfaction indexes have continued to increase during the first half of the year and are at their highest levels since 2006. And continuity with the Bank is fairly high. This has allowed for the Bank to continue to improve its cross-selling, its sales and maintain very high retention levels.

Also, we would like to note that Millennium BCP is the bank that most invests in innovation in Portugal and that we believe partly explains the satisfaction of levels of our clients. Also, we would like to note that our market share is exclusively in Portuguese activity and even though there was a lot of turbulence within the banking sector during the past two years, the market shares in Portugal, both in loans and customer funds have managed to increase during the last three years.

With regards to international operations, there was a significant decline, as we said before, of 93.6% mostly influenced by our Polish operation. Here, we would like to highlight the performance of Mozambique and Angola, our African subsidiaries. And Mozambique increased its profits by 14.3% to EUR27.2 million while Angola improved its profits quite substantially to EUR6.3 million.

With regards to Poland, net profit declined by 92% to EUR4.6 million and it basically -- total operating income declined by 22.5%, but costs also declined by 9.6%. The net income was influenced by the continuation of the price war on deposits and high costs of FX swaps used to fund the loan portfolio denominated in foreign currency. But was also partially offset by further achievements in cost reduction and stabilization of the provisioning efforts.

The deposit war in the market resulted in a deterioration of Bank Millennium deposit spreads to minus 74 basis points. However, we would like to note that there is an already visible spread recovery from previous months of minus 0.8% to minus 0.6% as a result of the repricing. The net interest income has thus declined by 44% year on year.

The average cost of FX funding grew during the second quarter, but current prices are already lower than the peak we had between November and February. And as a result of these effects, the net interest margin decreased in the second quarter to 1.1%. But nonetheless, we believe that the majority of the negative effects are fading away and the worst seems to be over.

With regards to commissions, they continue to decline, but basically are mainly due to the drop in commissions from investment, products and brokerage. Trading-wise, it grew by 26% supported by better results in the fixed income portfolio and the compound impacts of the FX derivatives on trading income was not material during the first half of 2009.

Operating costs declined by 10% in local currency with very strong declines in staff costs by 21% and a reduction in the number of employees by 347 year-on-year, which nonetheless the number of employees was somewhat higher in December 2008. If you compare it to that level, the reduction was over 600 people. This happened while the number of branches continued to increase year-on-year by 39 to 484.

With regards to loans to customers, our loans to customers continued to increase by 38% in local currency and deposits grew by 29%. Credit quality stands at 4.8% in terms of impairment ratio with coverage of 54%. And impairment charges continue to be relatively high at 1.06 percentage points.

With regards to Greece. Earnings fell by 69.2% to EUR3.3 million and were negatively influenced by the increase in impairment year-on-year. The operating income recovery was visible in the second quarter of 2009, with margin recovering to EUR31.6 million, which is 0.4% above the quarterly average 2008 and 17.5% above the first quarter margin.

The operation continued to have controlled costs even through 13 branches were opened since 2007. The loans to clients increased by 12% and customer deposits increased very significantly to 26.7%. The overdue ratios over 90 days increased somewhat in line with the expectations we had for the operation and coverage ratios stood at 43%.

With regards to Mozambique, we would like to highlight the 14.3% increase in net profit. The GDP growth in Mozambique remains fairly high and is expected to stand at 4% to 5% in 2009 and 2010. High profitability levels and net income growth are very significant and the bank has continued its ongoing expansion plans with branches that have reached 103. It continues to have and shows very strong volume increases and has a positive commercial gap with loans to deposit ratio standing at 65.6%. Loans to customers rose by 32.9% in Mozambique while customer deposits grew to EUR801 million.

With regards to Angola, we would like to note that we completed during the first half the partnership between Sonangol and BPA. The operation continued to expand its network and continued to post very strong loan and deposit growth and despite the continuous expansion, profitability levels remain very high.

So, to sum up the key initiatives in the framework of our 2009 priorities, I would like to highlight that the capital ratios were strengthened. Tier I improved 8%, Core Tier I to 6.2%, before IRB advanced. We would like to highlight also EUR300 million debt issue in subordinated perpetual securities during the first half. And we continue to monitor the approval processes for the advanced methods of Basel II while improving the internal control and risk management systems.

With regards to liquidity, we believe we had a very good performance during the first half, long-term debt issues of EUR3.5 billion, consolidated commercial gaps is quite in control with reasonable and very controlled performance in Portugal and the majority of the operations, and highly liquid assets rising to EUR7.2 billion.

Also, we would like to note that in terms of performance, we completed a faster cost reduction program and organizational streamlining with costs clearly subdued while we have maintained our commitment to customers with the repricing progress ongoing and an expected impact over the next few years. And we have also begun the leakage management process in the second quarter of 2009. We maintained very high service levels and we continue our efforts to capture on balance sheet funds.

With regards to sustainability and value, we would like to note that we continue our business model adjustments with Poland, Romania and private banking. We have completed the Angola partnership and continue our expansion on Mozambique. We have maintained very strict capital allocation discipline and are refocusing more in the African operations and we have introduced several structural measures in the pension fund.

So, in terms of our strategy and how we see ourselves, we believe that Millennium bcp is transforming itself, that we are institutionally stable, commercially resilient, focused on risk control, efficiency innovation and customer service. And basically, the bank is more solid. The capital ratios are strengthened. We have a prudent liquidity position. And even though the adverse economic environment is decreasing, our international operations profitability levels and pressuring operating profits in the very short term, we believe that the Bank is more efficient. We believe that the repricing efforts keep its pace and should have a much more visible impact over the next few years. And even though impairment levels are higher, they are basically in line with our expectations at this point of the economic cycle. So basically, we feel that we are changing what we believe must change and we are adjusting with discipline to what we cannot modify.

So, that would conclude my presentation and we have here our chairman, our CFO, and CFO of our Polish operations and we are ready to take your questions.

QUESTION AND ANSWER

Operator

Thank you. (Operator Instructions).

And the first question comes from the line of Matthew Gilbert from KBW. Please go ahead.

Matthew Gilbert - ***Keefe, Bruyette & Woods - Analyst***

Good afternoon. I just have one question. This is on asset quality. The provisioning charge in the second quarter seemed relatively low given the pick up in NPLs. Can you give us anymore color on your provisioning policy going forward. And specifically, do you have a minimum coverage ratio that you'd not be willing to [give away]? Thank you.

Sofia Raposo - ***Millennium bcp - Head, IR***

Very good. Thank you for your question. With regards to the provisioning policy, as you know, the net entries for the portfolio for bad loans have continued and are maintaining their pace, but they are basically in line with our expectations at this point in the cycle. And thus, we believe that the provisioning levels for the full year, the guidance that we have been saying for the past year of 70 to 80 basis points of loans should be adequate for 2009.

Matthew Gilbert - ***Keefe, Bruyette & Woods - Analyst***

Okay. Thank you.

Operator

Thank you. The next question comes from the line of Tiago DionÃ-sio from BES. Please go ahead.

Tiago Dionísio - ***BES - Analyst***

Hi. Good afternoon. Two questions. The first is regarding banking commissions. Could you provide some more detail as to what these other commissions relate to? There was a strong improvement in the quarter and if you could provide some more details on this, please. And the second question is regarding costs. Do you see further room to cut costs in Portugal? What kind of decrease by the end of the year should we expect in the first half? You had about 5% decline on a yearly basis. At the end of the year, what kind of drop should we expect? Thank you.

Sofia Raposo - ***Millennium bcp - Head, IR***

Thank you very much for your questions, Tiago. With regards to the commissioning levels and it is indeed -- there has been some improvement in terms of commissions. Basically, with regards to commissions in Portugal, what we have seen over the past few years, and actually bcp has a reputation has a reputation for having fairly high commissioning levels and also very good service levels.

And what we see when we compare the reality is actually that we do have a very high service level, but the commissions are somewhat below markets competitors. So basically, what we are is correcting some inefficiencies, reducing some leakage in commissions and correcting our pricing list that we believe we can have a lot of leeway to improve the commissioning on your role for -- in Portugal. So basically, that's the first.Second quarter shows the very first signs of the commission leakage management that we began in the second quarter of 2009.

With regards to costs, yes, we still believe that there is room for improvement. The current growth rates are very important during this year. We very likely will maintain the decline and going forward, we expect to continue to have declines in the future.

Tiago Dionísio - ***BES - Analyst***

Okay. Thank you.

Operator

Thank you. The next question comes from the line of Inigo Lecubarri from Abaco. Please go ahead.

Inigo Lecubarri - ***Abaco - Analyst***

Hi. I want to get some granularity on the net interest income issue. 20% growth of net interest income, 2Q versus 1Q, is probably one of the biggest drops I've even come across in a retail bank. It's a very significant one. And not only that, but also 3Q and 4Q are probably going to be recurring because you have some mortgage repricing to absorb here and there. The cost of risk has come down relative to the previous couple of quarters, so here's there a risk of that number, that cost going up. So, bottom line is the profitability of the P&L has no room for error and is very close to no profits whatsoever.

Obviously, very happy to see the pattern going up. But you will agree with me that a lot of these has to do with accounting and to extract EUR371 million from pensions is by reducing assumptions establish risk because we're going on with mortality tables that are probably out of date anyway. So, it is very counterintuitive to be able to produce equity gains in this kind of environment.

Net-net, I'd like to see how can we square these? I think the P&L, the profitability of the Bank is impacted and will continue to be more impacted by the kind of hangs and the repricing of the mortgages so on and so forth. We are at a level where it is very difficult to see how we can produce equity internally. And then, we have managed to put up the equity by the accounting means, but I would suspect that this is A, accounting, and B, difficult to repeat. I'd like to ask the CEO how can we run this forward with such a weak P&L?

Sofia Raposo - ***Millennium bcp - Head, IR***

Well, thank you very much for your questions. I would just like to make a very specific note with regards to the net interest income. As you know, you're probably saying that we are -- have one of the highest declines that you have encountered so far. But probably there hasn't been, in your experience, such a sharp decline in terms of interest rates in one given year. Actually, they have declined by 3 percentage points during the last 12 months on average. And that, indeed, has been quite significant for our portfolio.

We would also like to note that we cannot -- we did not have any specific direction of coverage in terms of ALCO and therefore the decline we had basically shows a very straight and clean commercial margin. Going forward, we would expect this to continue to decline during the first quarter, but definitely we would see some very positive effects for the year of 2010 with the continuance of repricing. And depending on what your expectations are for interest rates, we believe that they have reached their minimum. So eventually, you may have different views on how much and when they are going to increase.

But we have a positive sensitivity to that particular item and any 25 basis points of interest rates increase would translate into EUR15 million to EUR20 million increase in net interest income going forward. So, that gives you an idea of how much we could improve further beyond what we expect to have in terms of repricing where we believe it could have a positive effect of over 10% for the next year. So, on the overall, that is what we expect to see in terms of net interest income.

With regards to the cost of risk -- and as I said before, we are maintaining our estimates for 70 to 80 basis points of loans. And with regards to capital, we do not believe that our improvement is only related to any accounting changes. Basically we have issued EUR300 million subordinated perpetual debt and that is significant.

And also, we would like to note that our pension fund is 107% covered. Last year, we made a contribution of almost EUR800 million to the fund, so basically that's also affected our net interest income and it is only fair and reasonable and very much in line with what we believe is acceptable to have some of the impact back in our capital base.

Carlos Santos Ferreira - *Millennium bcp - Chairman and CEO*

Okay. Thank you very much. May I add some points? First of all, in what regard the non-performance loans and impairments. As you know, the worst situation has been in the last quarter of last year. And again, the quality of our assets, they have not been deteriorating as some people used to say and what we have is really exactly as I told you, the same basis points for impairments and the same percentage that we have forecasted.

And the point is that if we go with our forecasts, in our opinion, we go well. And if we have forecasted in accordance with the markets and our peers, we go very well. And the figures that we have are in accordance with the figures of our peers. We believe that this part of the situation is, for us, it's clear.

Two more points. First of all, commissions. As you have noticed, commissions have also started a turnaround in the second quarter. And as you have noticed also, commissions in loans are flat. This means that we have space to increase. And the general command through all the organization is to push on. So, we will push on commissions and we will have space.

I will also like to say that the increase of Tier I is not an accounting question-. It is -- it will be the easy thing -- the easiest thing to do, but we are not dealing with people that don't know what goes on. We are dealing with you and yourselves, you know what is going on. We have, in these two quarters, a positive impact related with the pension fund.

But we have also a positive impact related with the subscription of EUR300 million of "Capital 2009." As I have already told you, we expect to have fully subscribed EUR200 million more in the next week related with first range of private placements and we are ready and we will continue to issue more capital related with "Capital 2009". We are going to finish next quarter and the end of the year with a very comfortable margin on top of the figures given by the Central Bank of Portugal.

Relative also with margin. If we are talking about consolidated margin, we have been suffering a negative impact of Poland. Anyway, the impact has been better or less impact than we had forecasted in accordance with some of opinions in the markets. And also in Poland, we are, in our opinion, clear opinion in the turnaround. You will have interesting, may I say, news in the future relative with Poland. Thank you.

Operator

Thank you. We currently have no further questions coming through. (Operator Instructions). And we have no further questions coming through, so I'll hand you back to your host to conclude today's conference. Thank you.

Carlos Santos Ferreira - *Millennium bcp - Chairman and CEO*

Well, ladies and gentlemen, let me end this presentation with one final remark. We feel that we have started to turn a page in our past performance. We believe that we are more stable, more solid, more efficient and more focused. And we will keep going on and pushing on. Customer service and innovation will drive our future action.

Thank you very much to all of you and I hope at least to be in touch in three months time. Thank you very much and have a nice holidays. Thank you.

Operator

Thank you, ladies and gentlemen, for joining in today's conference. You may now replace your handsets. Thank you.