

IFS 1Q10 Conference Call
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Operator: This is a recording of the Peter Majeski conference call with i-advice on Wednesday, May 5, 2010 at 10 a.m. Eastern Time. Good morning and welcome to the Intergroup Financial Services First Quarter 2010 Conference Call. All lines have been placed on mute to prevent any background noise. After this presentation, we will open the floor for questions. At that time, instructions will be given as to the procedure to follow if you'd like to ask a question. It is now my pleasure to turn the call over to Peter Majeski of i-advice Corporate Communications. Sir, you may begin.

Peter Majeski: Thank you, Stephanie, and good morning, everyone. Welcome to Intergroup Financial Services First Quarter 2010 Earnings Conference Call on this the 5th of May, 2010. We are very pleased to have with us from Intergroup, Mr. Jose Antonio Rosas, Chief Financial Officer and Mr. Gonzalo Basadre, Investor Manager of Interseguro. They will be discussing Intergroup's results per the press release distributed yesterday. If you had not yet received a copy of the presentation or earnings release, please visit us at www.ifs.com.pe to download a copy or call us in New York at 212-406-3694. Before we begin, I would like to remind you that any forward-looking statements made today by Intergroup's management are based on information and data currently available and are subject to various conditions that may differ materially. It is now my pleasure to turn the call over to Mr. Jose Antonio Rosas. Mr. Rosas, you may begin.

Jose Antonio Rosas: Thank you, Pete. Good morning to everyone and welcome to our First Quarter 2010 Conference Call. We posted a very strong performance in the first quarter of 2010 with net earnings at Intergroup nearly doubling the earnings reported in the first quarter of '09. This significant increase was driven by growth in the gross financial margin and lower provisioning expenses at Interbank and increased investment returns and premium sales at Interseguro.

Interbank posted a very strong performance as well with a 69% year-on-year increase in net earnings. Total loans remain stable quarter-on-quarter, but retail loans increased 2.9% as demand for retail credit starts to pick up, particularly in the credit card and mortgage segments and we continue to win market share in those segments. Interbank's net interest margin was 8.5% in the first quarter of 2010, significantly above the industry's average of 6.9% and 80 basis points above our own first quarter of '09 NIM. Asset quality remained strong, with a past-due loan ratio of 1.6% and a reserve coverage ratio of 255%. As a result, write-offs declined and provisioning expenses decreased 12% quarter-on-quarter and 14% year-on-year. At Interbank, capitalization was strengthened as the BIS ratio rose from 11.5% in the fourth quarter of '09 to 12.8% in the first quarter of 2010. Additionally, in April 2010, we placed a \$200 million in Tier I bond issue, which will further strengthen our capital.

Interseguro also continued to post a strong performance, with a fivefold year-on-year increase in net earnings. Premiums increased 20% quarter-on-quarter and 10% year-on-year, driven by higher annuity sales. And investment returns increased significantly both year-on-year and quarter-on-quarter when excluding a one-time gain in the fourth quarter of '09.

Please turn to page four for a quick review of Intergroup's earnings. As shown in the chart in page four, Interbank and Interseguro posted strong year-on-year earnings growth and made significant positive contributions to Intergroup's performance. Both subsidiaries' earnings also declined from record high levels in the 4th quarter of '09, a quarter during which posted it one-time items, where we project at both companies. There are no significant non-recurring items in the 1st quarter 2010 earnings. Intergroup's return on equity was 29.7% in the 1st quarter of 2010, above the 19.3% reported in the first quarter of '09 and below the 36.8% reported in the 4th quarter of '09.

Please turn to page five for a review of Intergrupo's P&L statement. There, we can see that net earnings increased 97.4% year-on-year, driven mainly by 33% growth in the gross financial margin and a 14% decline in provision expenses. Growth in the gross financial margin was due to lower funding costs at Interbank, higher investment income at Interseguro, and moderate growth in interest on loans. Provision expenses declined 14% year-on-year, as stable asset quality and less stringent regulations led to lower provisioning requirements. Fee income from financial services grew 10% year-on-year, mainly as a result of higher fees from services and indirect loans at Interbank. Interseguro's loss from insurance underwriting totaled 4.9 million, a 35% improvement year-on-year as a result of a 6 million Soles increase in premiums. As a result of this factor, income before taxes and profit sharing increased 109% year-on-year and net earnings increased 97%.

Now, if we look at the quarter-on-quarter performance, we can see that net earnings decreased 13% quarter-on-quarter from a record-high level in the fourth quarter of '09. Net operating margin increased 7%, but was offset by a 29 million Sole decrease in other income and a 3 million Sole increase in income tax. Gross financial margin decreased 0.6% quarter-on-quarter, mainly as a result of a 2% increase in financial expenses. Also, Interseguro has posted a one-time 27 million Sole gain in the 4th quarter of '09, and we had no one-time gains in the 1st quarter of 2010. Provision expenses decreased 12% quarter-on-quarter as a result of lower write-offs and higher recoveries at Interbank. Fee income decreased 13% quarter-on-quarter due to seasonally lower commercial banking fees. Interseguro's loss from insurance underwriting was half the loss reported in the 4th quarter of '09 as a result of an 11 million Sole increase in premiums. Administrative expenses decreased 7% quarter-on-quarter as a result of seasonal decline in Interbank sales expenses. As a result of the above-mentioned factors, net-operating margin increased 7% quarter-on-quarter. However, a 62% decline in other income led to a 5% reversal in income before taxes. Other income had been unusually high in the 4th quarter of '09 due to provision reversals at Interbank totaling 25.5 million Nuevo Soles. Despite the decline in earnings, income taxes rose 19% as the effective tax rate rose from 26% in 4th quarter of '09 to 30% in the 1st quarter of 2010. As a result, net earnings decreased 13% quarter-on-quarter.

Please turn to page seven now for a discussion of Interbank's performance. In the P&L summary in page seven, we can see that Interbank's net earnings were 115 million Nuevo Soles in the 1st quarter of 2010, a 69% increase year-on-year and an 11% decrease quarter-on-quarter. The ROE was 34% in the 1st quarter of 2010, higher than the 29% reported in the 1st quarter of '09 and lower than the 39% reported in the 4th quarter of '09. The year-on-year increase in net earnings was due to a higher gross financial margin, a decrease in provision expenses and an increase in fee income from financial services. The quarter-on-quarter decline was due to a significant decrease in other income, which offset an 18.7% increase in net operating margin.

Please turn to page 8 now. There we can see that the current loans at Interbank grew 4.3% year-on-year, and only 0.6% quarter-on-quarter. Year-on-year growth was due to a 9.2% increase in retail loans driven by 14% growth in mortgages and 13% growth in our consumer loans. Growth in commercial loans remained stable year-on-year. During the first quarter of 2009, demand among retail clients increased from previous quarters' levels, particularly in the mortgage and credit card segments, leading to a 2.9% quarter-on-quarter increase in total retail loans. Commercial loans, on the other hand, decreased 1.7% quarter-on-quarter as demand among corporate clients remain moderate and competition intensifies. The chart on the bottom right of page 8, we can see that Interbank has continued to gain market share in retail loans. As a result of total industry growth in every retail-banking segment, our share of total retail loans in the banking system has grown from 16.7% in the fourth quarter of 2009 to 17.5% in the first quarter of 2010.

Please turn to page 9. On the first table on page 9, we can see the breakdown of Interbank's funding structure. During the first quarter of 2010, the use of Interbank's funds declined by roughly S/.200 million and was replaced by a similar increase in bank loans, mainly attributable to higher use of trade lines of credit. Total deposits remained stable quarter-on-quarter despite a decline of 2.4% increase of deposits.

Following a trend observed during 2009, retail time deposits declined 12% quarter-on-quarter as lowering rates have led consumers to seek higher yielding investment alternatives such as mutual funds. As a result of this trend, retail time deposits have decreased 32% year-on-year, leading to an 8.2% year-on-year decrease in total retail deposits. Commercial deposits, on the other hand, grew 8% year-on-year. Given stability in loan deposits, we have funded our 12-month growth mainly with a 17.4% increase in bank loans, attributable mainly to S/.384 million Nuevo Soles medium-term notes received in June of 2009.

Please turn to page 10 for a discussion of Interbank's gross financial margin. We can see that gross financial margin increased 3% quarter-on-quarter and 23% year-on-year. The quarter-on-quarter increase was a result of 3% growth in financial income, attributable to a higher investment income and exchange gains. The year-on-year increase in gross financial margin was due to a significant improvement in net interest margin driven by a lower cost of funds and a relatively stable yield on the loan portfolio. Financial income increased 3% quarter-on-quarter as a result of a 37% increase in exchange and derivatives gains and a 13% increase in investment income. The increase in exchange and derivative gains was a result of higher trading activity with clients. The increase in investment income was a result of 1.9% growth in average volume and a 60 basis point rise in the average yield from 5.3% in the fourth quarter of 2009 to 5.9% in the first quarter of 2010. Interest and commissions on loans, on the other hand, decreased 1.1% quarter-on-quarter as a result of a 60 basis points decrease in the average yield, from 14.1% in the fourth quarter of 2009 to 13.5% in the first quarter of 2010, partially offset by a 2.7% increase in average volume. As a result of a lower yield on loans, the average return on interest earning assets declined 40 basis points quarter-on-quarter, from 11.2% in the fourth quarter of '09 to 10.8% in the first quarter of 2010. Financial income increased 1.9% year-on-year as a result of a 5% increase in interest on loans, partially offset by a 78% decrease in interest on cash. The growth in interest on loans was attributable to a 6% increase in average volume, and partially offset by a 30 basis point decrease in yield, from 13.8% in the first quarter of '09 to 13.5% in the first quarter of 2010. The decline in interest on cash was a result of a 40 basis point decrease in yield, from a low 0.5% in the first quarter of '09 to an even lower 0.1% in the first quarter of 2010. The average yield on interest earning assets decreased 60 basis points year-on-year due mainly to a higher proportion of cash and investments in our assets. Financial expenses increased 2.7% quarter-on-quarter as a result of 13 million Soles increase in other financial expenses, partially offset by a 3.5% decrease in interest on deposits. The increase in our financial expenses was attributable to valuation losses on interest rate swap contracts. The decline in interest on deposits was due to a 30 basis point decrease in the average cost of funds, from 1.5% in the fourth quarter of '09 to 1.2% in the first quarter of 2010. Financial expenses decreased 40% year-on-year as a result of a 62% decrease in interest on deposits. The sharp decline in interest on deposits was achieved despite a 9% increase in the average volume due to a significant decrease in the average cost, from 3.5% in the first quarter of '09 to 1.2% in the first quarter of 2010. This decline in the average cost of funds is related to lower reference rates both in U.S. dollar and Nuevo Sol. As a result, Interbank's average cost of funds decreased by 190 basis points, from 4.4% in the first quarter of '09 to 2.5% in the first quarter of 2010.

On page 11, we can see we have the evolution of our net interest margin. You can see that net interest margin decreased 30 basis points quarter-on-quarter, from 8.8% to 8.5%, as a result of the above-mentioned decrease in the loan portfolio yield. Nonetheless, it remains 80 basis points above the NIM report in the first quarter of '09 as a result of a lower cost of funds. It also remains 160 basis points above the industry's average net interest margins of 6.9%.

Please turn to page 12. You can see that provision expenses have decreased 12% quarter-on-quarter and 10% year-on-year. The quarter-on-quarter decline was a result of lower write-offs and higher recoveries at Interbank. The year-on-year decrease was a result of unusually high provisioning requirements in the first quarter of '09 as a result of a pro-cyclical provisioning regulation enacted in December 2008. This regulation is no longer applicable since September 2009. The annualized ratio of provision expenses to average loans have decreased from 4.2% in the first quarter of '09 to 3.7% in the fourth quarter of '09

and 3.2% in the first quarter of 2010. Asset quality and coverage remained strong. The ratio of past due loans to total loans has increased slightly, from 1.5% in the fourth quarter of '09 to 1.6% in the first quarter of 2010, a level similar to the banking industry's average. The reverse coverage ratio decreased from 267% to 255% in the first quarter of 2010 and remains above the industry's average of 224%.

Please turn to page 13. Fee income decreased 8% quarter-on-quarter from a seasonally high fourth quarter of '09, mainly as a result of lower fees from corporate finance advisory attributable to a lower number of transactions closed during the first quarter. Fee income rose 11% year-on-year as a result of a 37% increase in fees from services, related to savings accounts, ATM use, and other items. On the chart to the right, we can see that administrative expenses decreased 8% quarter-on-quarter as a result of an 18% service decline in terms of received from third parties, mainly related to sales expenses, consulting services and TI expenses. Expenses increased 6% year-on-year, mainly due to a 13% increase in personnel expenses, related to a headcount growth from 5,500 employees as of January 2009 to 6,400 employees as of January 2010. This is mainly due to growth in the credit card sales. The efficiency ratio improved from 54% in the first quarter of '09 and 52% in the fourth quarter of '09 to 48.5% in the first quarter of 2010, as a result of significantly higher growth in revenues than in expenses.

Please turn to page 14. The ratio of regulatory capital to risk-weighted assets at Interbank was 12.8% in the first quarter of 2010, above the 11.5% reported in the previous quarter and 10.9% reported in the previous year. The ratio was also significantly above the minimum 9.5% required by the Peruvian banking regulations. The quarter-on-quarter increase in our regulatory capital ratio was driven by an 18% growth in Tier I capital due to incorporation into regulatory capital of 182 million in capitalized earnings and legal reserves, from earnings posted during 2009 and the first quarter of 2010. Additionally, on April 16, 2010, we issued \$200 million in non-cumulative junior subordinated notes, which will be considered as part of our Tier I and Tier II capital and will significantly strengthen our capital base. A pro forma calculation of our first quarter 2010 capitalization ratio incorporating these notes results in a total regulatory capital ratio of 17.5% and a Tier I capital ratio of 11.8%. Now, Gonzalo Basadre will discuss Interseguro's performance.

Gonzalo Basadre: Thanks, Jose Antonio. Good morning to everyone. Please turn to page 17 of the presentation. The table shows the summary of Interseguro's P&L performance, showing a fivefold yearly growth in net income and an decrease of 42.8 quarter-over-quarter. The increase of net income year-over-year is mainly explained by higher investment income, which will be discussed later in the presentation. The quarter-over-quarter decrease is a result of a one-time gain of 27.1 million arising from the application of a new accounting regulation of credit-linked notes. Excluding the effect of this gain, investment income will have increased 37.8 quarter-over-quarter.

Page 18 shows in detail the performance of Interseguro Premiums. Premiums increased 20.1 quarter-over-quarter and 10.3% year-over-year. The increase is explained by annuities premiums, which grew 24.2 quarter-over-quarter and 12.2% year-over-year. The quarter-over-quarter growth was the result of share market share gains of 2.3%, 18.3 as of December 2009 and 20.6 as of March 2010. On the other hand, Group Life premiums grew 16.6 quarter-over-quarter and 8.8 year-over-year, mainly due to an increase of life insurance premiums tied to mortgage credits, which represents 78% of Group Life premium.

Finally, on page 19, there are some details on Interseguro's investment portfolio and investment income. Interseguro's investment income was 35.9 million Soles in the first quarter of 2010, a significant increase over the first quarter of '09. The year-over-year increase is explained by the reversal of an exchange loss, an increase in real estate revenues and the recovery in financial markets, which led to higher gains in fixed income and equities. A quarter-over-quarter decrease is a result of the application in the fourth quarter of '09 of a new accounting regulation on credit linked notes. As mentioned earlier, excluding this effect, investment income would have increased 37.8% quarter-over-quarter. Finally, Interseguro's

investment portfolio increased 2.5% quarter-over-quarter and 5% year-over-year, totaling 1,916 million. Additional funds received were mainly investments in real estate project.

Jose Antonio Rosas: This completes our presentation and now we are open for the question and answer session.

Operator: Thank you. If you would like to ask a question, you may press star (*) 1 on your touch tone phone now. Questions will be taken in the order which they are received. If at any time you would like to remove yourself from the questioning queue, press star (*) 2. Again, if you'd like to ask a question, press star (*) 1 on your phone now.

Our first question is from Marcelo Telles with Credit Suisse.

Marcelo Telles: Hello, good morning, gentlemen. Congratulations for the good results. I have two questions. The first one, there was a very strong reduction in provision expenses versus the fourth quarter. How should we look at this going forward? Will you be able to maintain in order that the provision expenses that kind of levels or do you think there's room for the improvement? And my second question is regarding the performance of the large corporation's portfolio, which is still quite weak in the quarter despite the good performance on the retail side. When do you see, or do you see that segment recovering in the coming quarters? Thank you.

Jose Antonio Rosas: Good morning, Marcelo. First, before regarding your question on provisions, in this we've seen a significant decline in provisioning requirements, particularly in the retail portfolio, and this has been better than our expectations. We've seen our recoveries in asset quality which has been faster than we anticipated initially, and we are seeing that each increase brings gradual improvement in our provisioning requirements and in our asset quality. So we definitely should soon expect a gradual improvement throughout the year. We're being conservative on budgeting and provisioning requirements will remain similar to the first quarter's level, but there's obviously a very conservative assumption at the moment.

Second, regarding the corporate portfolio, indeed, we had a first quarter of very slow growth or negative growth in our commercial loan book. As mentioned during the presentation, it was due to moderate demand and also very intense competition. However, we've seen demand gradually pick up for the first month of the year. In fact, March was a better month than January and February. And we've seen also a much better performance during April. So, we definitely should see an increase in commercial lending as the year goes on.

Marcelo Telles: Thank you.

Operator: Thank you. Our next question is from Daniel Abut with Citi.

Daniel Abut: Good morning, Jose Antonio. First, a follow up question on the loan growth, you addressed the weak demand on the commercial side and said that you're seeing better numbers already in April. But, what about retail? I mean, retail clearly was stronger than commercial, but still, for your participation in that business and the strength of a recovery in Peru of economic activity, I would say that 9% year-on-year is nothing to write home about, and probably, you've seen better than that four years ago. You've seen a pick up in retail loans as well. And what is good guidance for retail loan growth for 2010 as a total? That's question one.

And question two, just to give you credit, you had said in prior conference calls that you expected a 30% flat ROE to be sustained for a few more quarters, and you reported four consecutive quarters with an ROE of 30% or more. Where do we go from here? Do you still think you can sustain a few more quarters

at this level or will this be the last quarter of that level of ROE? And what level is a more realistic, sustainable one going forward?

Jose Antonio Rosas: Good morning, Daniel. Regarding your first question, retail lending, indeed, was slower in the last 12 months than it had been in the previous years, but we are seeing a pick up in demand. And definitely we're seeing much stronger demand for mortgage loans now than in the last year. We're seeing our monthly disbursements in mortgages have been higher than at any other period for Interbank. And also, we're seeing consumers coming back into the market and credit card use is increasing as well. I think commercial credit cards had a very good month in March. It has also had a very good month in April. And we expect growth to start growing at more significant rates throughout the year. So those should be the two drivers of growth in retail lending, credit cards and mortgages. And it should drive us to a year-end growth rate of between 15% and 23%.

Now, regarding your second question on the ROE, in this we have had a run of very good quarters with ROE close or about 30%. And as mentioned always during our management presentations, our long-term expectation for ROE at Intergroup is 25%. However, we do see that this quarter, the second quarter of 2010, will probably remain strong in the 30 level, and then we'll probably start seeing a gradual decrease as the cost of funds start to increase and margins get compressed. When reach 25%, that's probably a gradual decline as mentioned throughout three or four quarters.

Daniel Abut: Very good, Jose Antonio.

Operator: Thank you. As a reminder, if you would like to ask a question, you may press "star" one (*1) on your touch-tone phones now. Our next question is from Alonso Aramburu with BTG Pactual.

Alonso Aramburu: Hi, good morning, Jose Antonio, two questions. The first one, can you elaborate a little bit on the investment returns that you had at the holding level. How you've had an average \$94.1 million return and also an ROE income of 2.4 million? So can you remind us what investments you have there and what is the mix of those investments?

And my second question is regarding efficiency which is gradually improving and what are your expectations for the rest of the year?

Jose Antonio Rosas: Good morning, Alonso. Regarding your first question on Intergroup's investment returns; at Intergroup, will have an investment portfolio totaling a close to \$19 million at the moment. And it's composed of Peruvian sovereign bonds, some real estate investments that compliment Interseguro's real estate investment strategies, and also structured notes. All of the returns that we have seen in the 1st quarter of '09 are interest only. We don't have any market gains on any of those investments during the 1st quarter of 2010.

Second, regarding the efficiency ratio, we definitely expect to remain below 50% throughout the year. Our long-term goal or medium-term goal is to get to 45% at Interbank and we definitely expect to remain below 50 and around 48% throughout this year.

Alonso Aramburu: Okay, thank you. And to just follow up on the second question, how do you expect your distribution network able to grow this year now that the economy is recovering? Do you expect to accelerate maybe up in the branches or should it be a close to the levels that you have now?

Jose Antonio Rosas: Some of user networks, we already have 227 branches and more than 1,600 ATMs. We have the largest ATM network in the country and the share of total branches that is higher than our share of deposits and loans. In addition, we already feel that we have a very comprehensive and wide distribution network. Having said that, we do anticipate that we will continue to expand our network certainly not at the pace we did during 2007 and 2008, the couple of years during which we

doubled our network. We will continue to grow organically, going to places in which we are not present at the moment or high at traffic locations. And also, continue to join Supermercados Peruanos in their expansion strategy throughout Peru. So, as a result of that, we expect our network to grow by around 10% this year, and probably 10% the following year as well.

Alonso Aramburu: Great. Thank you, Jose Antonio.

Operator: Thank you. Again, if you would like to ask a question, you may press star-1 on your touch tone phones now. Our next question is from Luis Guzman with Santander.

Luis Guzman: Good morning. I have two questions, First, what do you see, or how do you think the impact is going to be with the regulation of payroll that is in discussion and is happening in the last two months and the second one is regarding annuities. Where do you see that they are going in the coming quarters?

Jose Antonio Rosas: Okay. Good morning, Luis. Regarding your first question on the regulation of payrolls, that's a subject that has been in the media, has been touched by Congress and it's difficult to predict an outcome at the moment highly politicized thing. What we can say is that it is not a subject that affects us directly at Interbank. Since most of our retail clients are credit card and mortgage clients that are not payroll clients for us, we do not discount money from the payroll accounts to pay for a credit card or mortgage late payments. As a result of that, it is not something that has a significant impact for Interbank. And Gonzalo will discuss the annuities.

Gonzalo Basadre: Yeah. Good morning Luis. Can you repeat the question on annuities? Were you interested in loans?

Luis Guzman: Okay. Annuities grew more of this quarter? Just would like to know, what's the guidance in the coming quarters?

Gonzalo Basadre: Okay. First of all, the growth, the increasing growth in annuities, especially year over year, this was due to market growth. What we saw last year was that because of a couple of market prices, many individual accounts have lost a lot of values, so people deferred their decision to retire or to buy annuities or from other players in the market. And as the market has recovered, these people have started buying annuities again. They just postponed their decision.

Quarter over quarter, this is from year over year? We had market share gains of 50% which increased 10% of our sales in annuity screening. Going forward, I think the market's gonna present significant changes. As you know, there's a new regulation on early retirement called REJA. This will make the market grow significantly in the following 24 months. Even though that the regulation has already been enacted, we have only seen 16 million solid sales of REJA in the first quarter. But in the following quarters, we expect the whole market to grow by at least \$400 million per year for the whole market.

Luis Guzman: Okay. Thank you very much.

Operator: I'm sorry, no more questions at this time? Mr. Rosas, do you have any closing remarks?

Jose Antonio Rosas: No. No concluding remarks. Just thank you to everyone for participating in this call and we expect to have you in our second quarter 2010 conference call.

Operator: Thank you, ladies and gentlemen. This concludes today's conference. You may now disconnect. Have a great week.

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