Peter Majeski
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Operator: Good morning, and welcome to the Intergroup Financial Services third quarter 2010 conference call. All lines have been placed 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 would like to ask a question. It is now my pleasure to turn the call over to Peter Majeski of I-Advize Corporate Communications. Sir, you may begin.

Peter Majeski: Thank you, Stephanie. Good morning, everyone. Welcome to Intergroup Financial Services third quarter 2010 earnings conference call on this, the third of November 2010.

We are very pleased to have up from Intergroup Mr. Jose Antonio Rosas, Chief Financial Officer and Ms. Claudia Valladares, Chief Financial Officer of Interseguro, as well as Gonzalo Basadre, Chief Investment Officer of Interseguro. They will be discussing Intergroup's results per the press release distributed yesterday.

If you have 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 212-406-3693. It is now my pleasure to turn the call over to Mr. Jose Antonio Rosas, Chief Financial Officer. Mr. Rosas, please begin.

Jose Antonio Rosas: Thank you, Pete. Good morning, everyone. Welcome to Intergroup's third quarter 2010 conference call. We will start with a brief discussion of the highlights of Intergroup's performance.

Looking at Intergroup's Profit and Loss Statement, we can see that recurring net earnings increased 20% quarter on quarter and 15% year on year, as a result of loan growth at Interbank and increased investment income at Interseguro. When including non-recurring items, such as a one-time investment gain and provision charges at Interbank, net earnings increased 8.5% quarter on quarter and decreased 19.8% year on year.

We look at Interbank's performance. Recurring net earnings increased 24% quarter on quarter and 16.5% year on year, driven by growth in interest on loans. When including non-recurring items, net earnings increased 38% quarter on quarter and 9.5% year on year. Loan growth continued to be very strong as a result of strong demand for credit. Dollar loans grew 6.1% quarter on quarter and 19.6% year on year. The ratio of recurring provisional expense to average external loans fell from 3.6% in the second quarter of 2010 to 3.1% this last quarter, as a result of strong asset quality.

At Interseguro, net earnings rose 60% quarter on quarter, and 64% year on year due to growth in investment income, partially offset by increases in reserves tied to very strong annuity sales. Annuity sales tripled quarter on quarter and quadrupled year on year to reach a record level. This significant growth was driven by Interseguro's leading position in the rapidly expanding early retirement segment.

Please turn to the following page for a discussion of Intergroup's Profit and Loss Statement. If you look at Interseguro's quarter on quarter performance, you can see that net earnings increased 8.5% quarter on quarter. When excluding non-recurring items, net earnings growth was 20%, driven by increases in gross financial margins and fee income. Financial margins rose 6.4%, as a result of increases in interest on loans and investment income. Growth in interest on loans was due to a 6% expansion in average loan volume, and the increase in investment income was due to higher returns from Interbank and Interseguro's investment portfolio. Provisional expenses increased 8% as a result of a one-time charge related to new regulatory requirements applicable since July 2010. Excluding this non-recurring item for recent expenses, would have decreased 8.8%.

Fees from financial services grew 8.5%, driven by strong business activity in Interbank's retail and commercial segments. Interseguro's loss from insurance underwriting almost doubled quarter on quarter, due an increase in reserves linked to significant growth in annuity sales.

Administrative expenses remained stable, despite significantly expanding commercial activity at Interseguro. Now, looking at the year on year performance of Intergroup, we can see that recurring net earnings increased 16.3% year on year, driven by financial margin growth, partially offset by increases in loans from insurance underwriting and administrative expense. When including non-recurring investment gains realized in the third quarter of 2009, reported net earnings decreased 9.8% year on year. Growth in financial income was driven by increases in interest on loans and investment income. Interest on loans increased 5.5% year on year, driven by 17% growth in average loan volume at Interbank.

Financial expenses increased 28% year on year, due to a higher average volume in deposits, bonds and bank loans. Interbank's average cost of funds remained unchanged at 2.7%. Administrative expenses increased 7.2% year on year, as a result of Interbank's network expansion and Interseguro's increased commercial activity.

Now, please turn to Page 5, and there we have a summary of net earnings for Intergroup and its two subsidiaries. We can see that recurring net earnings grew significantly at Interbank and Interseguro, leading to ROE ratios above 35% at both subsidiaries.

Now, let's turn to a little discussion of Interbank's performance, starting on Page 7. Interbank's net income increased 38% quarter on quarter. When excluding non-recurring items, recurring net earnings increased 24% quarter on quarter, driven by higher income loans, fee income from financial services and lower administrative expense. During the third quarter of 2010, two non-recurring items were recorded. The first one was realized gains from investments, totaling $29.8 million after taxes. The second item was one-time provision charge of $11 million after taxes, related to the application of a new regulation on loan classification, issued by the banking superintendent.

Now, we will look at Interbank's year on year performance. Net income grew 9.5% year on year. When excluding non-recurring items, net income grew 15.5% year on year. The annualized ROE was 38.5% in the third quarter of 2010, above the 30.1% reported in the previous quarter, but below the 43% reported in the third quarter of 2009.

On page 8, we have a breakdown of Interbank's loan portfolio. We can see that total loans increased 6.1% quarter on quarter, continuing the strong growth trend observed since the second quarter of 2010, when loans expanded by 6.8%. Loan growth during the last six months has been driven by expanding demand for credit in the retail and commercial segments, as a result of Peru's solid economic performance. Commercial loans grew 7.4% quarter on quarter, driven by strong demand for investment and trade financing among companies in Peru. In this context, Interbank's growth was boosted by an increase in market shares, from 8.1% in the second quarter of 2010, to 8.4% in the third quarter.

Retail loans grew 4.8% quarter on quarter, due mainly to an 8.3% increase in mortgages and a 5.3% increase in credit card financing. Interbank's mortgage portfolio has grown at consistently solid rates during the last four quarters, driven by strong demand for housing and successful commercial efforts at Interbank. As a result of these efforts, our market share has grown from 10.5% in the third quarter of 2009, to 11.4% in the third quarter of 2010, thus driving our total mortgage loan portfolio to expand by 31% year on year.

Credit card financing grew 5.3% quarter on quarter, and that is the highest growth reported by Interbank in the last several quarters in the credit card portfolio. As a consequence of the significant growth rates of the last two quarters, performing loans have grown almost 20% year on year, and our market share has expanded from 11% last year to 11.3% at the end of the third quarter of 2010.

On page 9, we have the composition of our funding mix. During the third quarter, there was a shift in our funding mix, as we used short-term bank loans, particularly short-term trade lines of credit to replace local institutional deposits. And, as a result of that the Central Bank started strengthening liquidity locally, and, as a result, going to correspondent banks for trade lines of credit was a lower cost of funding alternative than continuing to rely on institutional deposits locally. Total deposits decreased 7.9% quarter on quarter, due to 15.1% decline in commercial deposits, mainly from institutional clients. And those are the areas of what I mentioned earlier, about shifting from institutional deposits to short-term lines of credit as a funding strategy.

Retail deposits increased 4.1% during the same period. As a result of the sequence of events related to funding, in early October, Interbank issued $400 million in senior bonds, at a yield of 5.70%, and that is part of our strategy to strengthen our medium term funding at favorable rates.

Now, please turn to page 10 for a discussion of our financial margins. Gross financial margin grew 14.8% quarter on quarter, due to increases in investment income and interest on loans. Excluding non-recurring items, gross financial margins would have grown 4.2% quarter on quarter. In the third quarter of 2010, Interbank realized non-recurring gains on the sales of investments, totaling $44 million before tax. Interest on loans increased 4.3% quarter on quarter, as a result of 6.4% increase in our average loan volume, partially offset by a 30 basis point decrease in the average yield, from 14.2% in the second quarter 2010 to 13.9% in the third quarter. This decline was attributable to lower rates on commercial loans.

Investment income increased by $45 million quarter on quarter, as a result of the above mentioned investment gains, and an increase in the yield of Central Bank Certificates of Deposit held by Interbank. The average yield of interest earnings net assets was 11.7% in the third quarter of 2010, and 100 basis point increase from the second quarter of 2010, due to the much higher investment income, mentioned before. Financial expenses grew 8.4% quarter on quarter, due to increases on interest on deposits and bank loans. Interest on deposits grew 23.1% quarter on quarter, due to a 30 basis point increase in the average cost, from 1.1% in the second quarter of 2010, to 1.4% in the third quarter of 2010, with the average volume unchanged. The rise in the cost of deposits was a result of a 90 basis points increase in the average cost of institutional deposits, from 1.1% to 2% as a result of an environment of rising short-term interest rates, resulting from the Central Bank's tightening policies implemented during the first quarter.

Interest on bank loans grew 10% quarter on quarter, driven by a 34% increase in the average volume, and partially offset by a 70 basis point decline in the average cost. Gross financial margins grew 11.8% year on year, driven by increases in interest on loans, and investment income. Excluding non-recurring items, gross financial markets would have grown 8.1% year on year. Non-recurring items included the first quarter 2010 investment gains mentioned above, as well as a $27.5 sole in investment gains realized in the third quarter of 2009. Interest on loans grew 8% year on year, due to an increase of 17% in avaerage loan volume, partially offset by a

120 basis point decrease in the average yield, from 15.1%, last year, to 13.9% in the third quarter of 2010. This decline was due to lower rates on commercial loans, in line with a lower cost of funds, but also due to an increasingly competitive environment.

Financial expenses grew 16% year on year, due to significant increase in interest on bonds and bank loans, partially offset by a 25% decrease on interest on deposits. The year on year decline in interest on deposits was attributable to a 60 basis point decrease in the average cost, from 2% last year to 1.4% in the third quarter of 2010. The increase in interest on bonds was due $200 million Tier 1 bond issue, completed in April, which doubled Interbank's average volume of bonds outstanding. The increase on interest on bank loans was driven by 46.4% growth in the average volume, partially offset by a 30 basis points decline in the average cost. The bank's average cost of funds remained unchanged quarter on quarter, and year on year.

On page 11, we have a chart showing the evolution of our net interest margin, and we can see that our net interest margin increased 80 basis points quarter on quarter, from 8.3% to 9.1%, due to investment income growth. When excluding non-recurring items, net interest margin declined 10 basis points quarter on quarter, from 8.2% to 8.1%. Interbank's reported net interest margin of 8.1% remains significantly above the industry's average of 6.8%.

Please turn to page 12, now. There, we can see two charts related to our asset quality and provision expenses. Provision expenses increased 7.9% quarter on quarter, due to a non-recurring $16.2 million sole charge, related to obligations on new regulations on loan classification and provisioning applicable since July 2010. Excluding this charge, financial expenses would have decreased 8.8% quarter on quarter. Provisional expenses increased 33% year on year, as a result of the above-mentioned one-time charge, and also as a result of an increase in average loan volume. Excluding the non-recurring item, the ratio of provision expenses to average loans decreased by 3.5% in the third quarter of 2009 and 3.6% in the second quarter of 2010 to 3.1% in the last quarter. The ratio of past due loans to total loans remains stable at 1.6%, when compared to the second quarter of 2010 and the third quarter of 2009. The reserve coverage ratio increased from 253% in the second quarter to 264% in the third of quarter of 2010.

Please turn to the following page. In the first chart of page 13, we can see that the fee income from Financial Services grew 4.5% quarter on quarter and 10.7% year on year, due to increases in credit and debit card fees, fees from contingent operations and fees for collections and payment services. The increase in credit and debit card fees was a result of the growth in the number of active credit cards and the usage of such credit cards. The increase in fees from contingent operations was a result of a higher volume of guarantees and standby letters of credit, mostly related to trade finance.

Administrative expenses fell 2.3% quarter on quarter, as a result of lower project implementation costs, and a seasonal decline in provisions for vacations. Expenses grew 9% year on year, driven by the expansion of Interbank's distribution network. Between September 2009 and September 2010, Interbank added 12 branches and 117 ATMs to its network. The efficiency ratio improved from 51% in the second quarter to 45% in the third quarter of 2010, as a result of growth in revenues and the decrease in administrative expense.

On page 14, we show Interbank's capitalization. The ratio of regulatory capital to risk weighted assets was 15.4% as of the third quarter, slightly below the 16% reported in the second quarter, but above 12.2% recorded in third quarter of last year. This ratio is significantly above the 9.8% minimum required by the Peruvian banking regulations. The quarter on quarter change was a result of a 2.6% increase in risk weighted assets, coupled with a 2.9% decrease in regulatory capital. This decrease in regulatory capital has entirely to do with the appreciation of the local currency and its effects on our foreign currency denominated component of our regulatory capital. The year on year increase in our capitalization was due to growth rates of 37.4% in Tier 1 capital and 91% in Tier 2 capital. These increases were the result of the capitalization of earnings from the first quarter of 2010 and the $200 million Tier 1 bond issue completed in April.

And now, Claudia will discuss Interseguro's performance.

Claudia Valdivia: Thank you, Jose Antonio. Good morning to everyone. Please turn to page 16 of the presentation. The table shows a summary of the Interseguro's P&L performance, where we can see an increase from 15.5% quarter over quarter, and 54.3% year over year. ROE increased from 28.4% in the third quarter of 2009 to 36.5% in the third quarter of 2010. During the period, ROA grew from 3.8% to 5.3%. The increase in net income in both quarter over quarter and year over year is explained by high investment income, which will be discussed later in the presentation. This increase was partially offset by higher technical margin loss and higher administrative expenses.

Technical margin loss increased 31.8%, quarter over quarter and 34.9% year over year. This increase is primarily explained by higher reserves due to a strong growth in annuity premiums. The increased volume on annuity premiums is solid and accounting laws must be recognized in the financial statements, according to the Peruvian insurance regulations. On the other hand, increasing administrative expenses was due to higher commissions on increasing sales.

Please turn to the next page of the presentation. Page 13 shows some detail of the performance of investments over premiums. As shown in the table, premium sales more than doubled quarter over quarter and twofold year over year, driven by very strong growth in annuities. This significant expansion was a result of the new early retirement law, enacted earlier this year. Premiums sold under this early retirement law represented 33.6% of total annuity sales. As of September 30, 2010, Interseguro is by far the leading annuity provider to the early retirement segment, as well as the leading provider of annuities in the Peruvian market, with a 26.2 market share for the third quarter of 2010.

In addition to annuities, individual life saw important growth. Individual life premiums increased 21.5% quarter over quarter and 11.5% year over year. These was due to higher insurance sales. Group life premiums grew 4.7% quarter over quarter and 31.9% year over year, mainly due to an increase in life insurance premiums tied to mortgage credits, which represent 30% of group life premiums.

Finally, on page 18, there are some details on Interseguro's investment portfolio and investment income. Interseguro's investment income was $63.4 million soles in third quarter of 2010, a significant increase over both the second quarter of 2010 and the third quarter of 2009. This increase is explained by realized gains in fixed income securities and an increase in real estate income. The realized gains in fixed income securities are primarily explained by the sale of foreign bonds in order to take the opportunity to make profits and reinvest the proceeds in investment instruments with higher yields. The increase in real estate income was due to the opening of the Centro Civico Shopping Center, opened in December 2009, which represented 65% of real estate income in the third quarter of 2010, and to overall higher yield in Interseguro's investment in Interproperties, which yields $1.2 million soles in the third quarter of 2009 to $5.3 million soles in the third quarter of 2010.

Interseguro's investment portfolio increased 12.9% quarter over quarter and 19.1% year over year, totaling $2,151 million soles. This increase was tied to the growth in annuity sales. The additional funds response received were invested in both fixed income and real estate investments.

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

Operator: Thank you. At this time, we will open the floor for questions. If you would like to ask a question, please press Star 1 on your touchtone phones 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, that is Star 1, if you would like to ask a question.

Our first question is from Daniel Abut with Citi.

Daniel Abut: Jose Antonio, a couple of questions. In terms of loan growth, if you look at this quarter and year on year rate, you are already growing at 20% type of pay, but you explain in your remarks, most of it was driven by commercial and mortgage loans and much less so by credit card and consumer, given the natural position of the bank, should we expect consumer and credit card loans start to pick up going into next year and provide loan growth more in line with the portfolio as a whole, and 20% a good number to look at for the expansion of the loan growth next year? What are you looking, in terms of loan demand for next year? And second, on provisions, you explained that excluding this one time provision related to regulatory requirements, the number, as a percentage of loans came down in the quarter to 3.1%, significantly below the prior year's quarter, is that the level you think is sustainable, going forward next year? Or what type of provisions do you see for the 2011?

Jose Antonio Rosas: Good morning, Daniel. To answer your question, first, on consumer loans, we have indeed seen that consumer loan growth has been slower than mortgage loans and commercial loans, not only at Interbank, but for the market overall. Having said that, however, we have seen that credit card loans have started to pick up. As mentioned during the presentation, the 5.3% rate of growth that we saw for credit cards in the past quarter was the highest of the past seven quarters, so we do expect, and are already seeing a credit card loan growth starting to pick up. We have not seen that with payroll loans. We have been growing at a slower pace. And 20% is definitely a reasonable growth rate for our overall portfolio for next year and also for consumer loans.

Regarding provisions, excluding the one-time charge we mentioned, we did have a very positive quarter, with provision expenses at only 3.1% of total loans. We had a particularly strong quarter for our commercial loan book. We are being a bit more conservative in our projections and are expecting a total ratio of provisions to total loans slightly above the 3.1% that we reported in this quarter. We expect to be at between 3.3-3.5% as a sustainable level for next year.

Daniel Abut: Thank you, Jose Antonio.

Jose Antonio Rosas: You are welcome.

Operator: Thank you. As a reminder, if you would like to ask a question, you may Star 1 on your telephone keypad now.

Our next question is from Alonso Aramburu with BTG Pactual.

Alonso Aramburu: Yes, hi, good morning. Two questions; One is a follow-up from the previous one. Jose Antonio, do you include the pro-cyclical provisions that are going to start in the fourth quarter in the provision numbers and in the provision estimates that you are providing? And, second, can you give us a little more color on the consolidation adjustment of

$38 million soles, that negative adjustment that you had during the quarter, what triggered that, and what should we expect going forward? Do you expect something similar to happen again? I think that this is the first time that Intergroup has reported an adjustment as big as this one.

Jose Antonio Rosas: Good morning, Alonso. In terms of you first question, our expectations do include the pro-cyclical provisional requirements. They came into place in October of this year. We are already updating our total provisions to meet the new pro-cyclical risk regulations. We do not expect a big impact from that, however, so that 3.3-3.5% includes the pro-cyclical provisional requirements.

Your second question, the consolidation adjustment, as mentioned in the report, we had investment gains at Interbank and Interseguro, that when consolidated with Intergroup, this can be shown as part of that P & L statement in Interbank and Interseguro per accounting rules, but when consolidated with Intergroup, they must be taken out from the P & L and adjusted at the equity level, not shown on the P & L. However, dividends paid out by our subsidiaries will take into account those amounts, so that adjustment will not affect our dividend payout at a subsidiary level.

In terms of your question, it is to be expected in the future, definitely not. It was a very strong adjustment this time, but we would not expect to see something like that in the coming quarters.

Alonso Aramburu: Ok, thank you, Jose Antonio.

Jose Antonio Rosas: You're welcome.

Operator: Thank you. Again, if you would like to ask a question, you may press Star 1 on your telephone now. We have a follow-up question with Alonso Aramburu with BTG Pactual.

Alonso Aramburu: Yes, hi, good morning. Just to follow up also on the insurance side. Can you just give us a sense of what kind of growth should we expect on the annuities. It was obviously a very strong quarter this quarter. Is this something that you think will only happen for this quarter, or should we expect in future quarters, as well?

Claudia Valdivia: Good morning, Alonso. We do expect that the growth will be sustainable and indeed, we expect it to be much higher over the next years. On a regular basis, around 4,000 people are retiring every year. In addition, we have the early retirement laws that will be in effect until the end of 2012. Under this law, we expect around 26,000 people will retire over the period of 2010 and through 2012. So, we are really optimistic about the growth of the annuities market.

Alonso Aramburu: Great, thank you.

Operator: Thank you. Again, you may press Star 1 on your phone now. I'm sorry, no further questions, Mr. Jose Antonio Rosas, do you have any closing remarks?

Jose Antonio Rosas: Thank you, everyone, for participating in the call, and we expect to have you in our next quarterly conference call at the end of January 2011. Thank you very much.

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

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