Intercorp Financial Services

2Q23 Earnings

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CORPORATE PARTICIPANTS

Luis Felipe Castellanos – *Chief Executive Officer*

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Carlos Tori – *Executive Vice President of Payments, Intercorp Financial Services*

Natalia Nirenberg – *InspIR Group*

PRESENTATION

Operator
Good morning and welcome to Intercorp Financial Services Second Quarter 2023 conference call. All lines have been placed on mute to prevent any background noise. Please be advised that today's conference is being recorded.

After the 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. Also, you can submit online questions at any time today using the window on the webcast, and they will be answered after the presentation during the Q&A session. Simply type your question in the box and click "Submit Question".

It is now my pleasure to turn the call over to Natalia Nirenberg of InspIR Group. You may begin.

Natalia Nirenberg
Thank you and good morning, everyone. On today's call, Intercorp Financial Services will discuss its second quarter 2023 earnings. We are very pleased to have with us:

Mr. Luis Felipe Castellanos, Chief Executive Officer, Intercorp Financial Services;
Ms. Michela Casassa, Chief Financial Officer, Intercorp Financial Services;
Mr. Gonzalo Basadre, Chief Executive Officer, Interseguro;
Mr. Bruno Ferreccio, Chief Executive Officer, Inteligo; and
Mr. Carlos Tori, Executive Vice President and Payments at Intercorp Financial Services.

They will be discussing the results that were distributed by the company yesterday. There is also a webcast video presentation to accompany the discussion during this call. If you didn't receive a copy of the presentation or the earnings report, they are now available on the company's website ifs.com.pe to download a copy. Otherwise, for any reason if you need any assistance today, please call InspIR Group in New York at 646-940-8843. I would like to remind you that today's call is for investors and analysts only therefore questions from the media will not be taken.

Please be advised that forward-looking statements may be made during this conference call. These do not account for future economic circumstances, industry conditions, the company's future performance or financial results. As such, statements made are based on several assumptions and factors that could change causing actual results to materially differ from the current expectations. For a complete note on forward-looking statements please refer to the earnings presentation and report issued yesterday.

It is now my pleasure to turn the call over to Mr. Luis Felipe Castellanos, Chief Executive Officer of Intercorp Financial Services, for his opening remarks. Mr. Castellanos, please go ahead, sir.

Luis Felipe Castellanos
Okay, thank you. Good morning, everyone, and welcome to our second quarter 2023 earnings call. Thank you all very much for attending our call today.

I will start, as always, by assessing the macro situation in Peru. We expect a mild improvement in some of the key indicators for the second half of the year, but we continue to operate on a challenging environment. As you know, the country got off on the wrong foot with social unrest and inclement weather in early 2023. Peru had a first half of the year with negative GDP growth. This has taken a toll in the numbers for the full year and now GDP growth expectations have trimmed down to between 1% and 2% range.

In the meantime, inflation has moderated and hopefully begun its journey towards the Central Bank's target. The currency, the Nuevo Sol, has recovered some of its value, and that has helped alleviate pressure on prices. Interest rates in Peru have probably peaked and at some point in the second half of the year, we would expect the Central Bank to start lowering them again. The potential impact of an El Niño phenomenon for later in the year or early 2024 is still uncertain. So, as you know, as you've heard, it's a challenging environment.

Moving to our business, IFS continues to grow in terms of number of customers and expanding market shares across key business lines. This has fostered a 15% revenue increase this quarter and 47% earnings growth compared to the same quarter of last year, when market conditions impacted investment results in our wealth management business. Paired with only 5% year-over-year growth in expenses, below inflation, this has led IFS to register a sound efficiency level of 35% in the quarter.

At Interbank, we have been able to sustain growth across revenue lines despite the moderation in banking activity. NIM has expanded further to 5.6%. However, provisions continue to increase in retail banking as we are digesting the impact in the Peruvian consumer of slower economic growth, high inflation, and especially, the effect of the social and weather dislocations previously mentioned. We expect growth moderation of our consumer book in the second half of the year to continue.

At Interseguro, we see good investment returns with a well-hedged and predominantly fixed income portfolio. The company remains market leader in the annuity business, while gearing to higher growth segments such as individual life and retail insurance, which have importantly increased the contribution to total premiums in the last year.

Inteligo has managed to grow AUM in dollar terms and shows resilience as investment results start to normalize. Finally, we continue to strengthen our payments ecosystem with Izipay, which represents a growing and profitable operation for us that has started to provide new income streams to our business through better customer engagement, larger float, increased fees, and net interest income.

Going back to what I first mentioned, the macro backdrop has temporarily put pressure on risk profile and profitability at IFS, and we have adjusted our guidance for cost of risk and ROE accordingly, as Michela will explain in detail further on. On the first topic, confidently, loan loss allowances provide strong coverage. And, on the profitability outlook, we are confident that once we move towards the next credit cycle, we will be on track to achieve our mid-term target of around 18% sustainable ROE.

As such, we remain optimistic about Peru and about IFS outlook going forward and continue to build on our key strategic priorities, which are growth, digital, and focus in key businesses.

Now let me pass it on to Michela for further explanation of our figures in the quarter. Thank you.

Michela Casassa
Thanks, Luis Felipe. Good morning, and welcome everyone, again. Today, I will review four sections of our earnings presentation, starting with an introduction to our results on slides two to four.

On slide 2, the macro-outlook is slightly improving as shown by the decrease in inflation of the last quarter and the stabilization of the soles rates, together with a relatively stable exchange rate, as Luis Felipe mentioned. The new estimate of the Central Bank for reaching the inflation target of 3% is the first quarter 2024. Still, economic growth represents a challenge as evidenced by the negative trend registered in the last months considered to be the worst semester in a long time, and the new expectation of GDP for year-end is below 2%.

On slide 3, financial performance at IFS continues to post growth, with ROE impacted by high cost of risk of consumer finance and soft investment results. Six key messages in this slide. There has been a moderation in year-over-year loan growth from 15% in the first quarter to less than 12% this quarter with a stronger moderation in commercial banking loans. Good top-line year-over-year growth continues at 15% this quarter, and NIM continues to increase, but with a lower pace, reaching 5.6% at Interbank. There has been a further increase in cost of risk coming from consumer lending, pushing the bank cost of risk in the quarter to 3.6% and the retail cost of risk to 6%. The high risk of the consumer portfolio is the result of sustained and consistent high inflation as seen in many other countries, a negative GDP growth in the first semester of this year in the Peruvian economy and the social and climate disruptions of the first quarter. We have seen a deterioration in the consumer payment behavior during the last quarter. Nonetheless, coverage ratios remain healthy. We continue to see good efficiency levels both at IFS and at the bank level, as we are strictly monitoring and managing costs, especially at the bank, which has reached a cost-income ratio of 37% in the quarter, a strong improvement versus last year, mainly due to the good operating leverage. IFS ROE of 14.3% this quarter has been impacted by cost of risk at Interbank and soft investment results at Inteligo. Finally, we continue to register sound capital levels with core equity tier 1 ratio up 30 basis points in the quarter, reaching 11.4% and total capital ratio at 15.2%.

On slide 4, we continue to build on our three key strategic priorities, which are: First, growth reaching 5.8 million clients at Interbank and growing earnings 47% year-over-year. Digital, with a digital retail banking NPS of 46 and 73% of our retail clients being digital. Third, focus on our key businesses with growing market shares in consumer finance at 21.2%, acquiring business at 44%, and annuities at 28%.

Now, first on pages 6 to 10, let's talk about our growing customer base and sustainable earnings. On slide 6, we see a continuous growth of customer base at IFS or 15% year-over-year in banking, 17% in insurance, 10% in wealth management and 53% in payment merchants.

On slide 7, IFS 2Q reported earnings of 331 million soles are up 24%, or 7% on a quarterly basis adjusted, and 47% year-over-year with an ROE of 14.3%. The quarterly and yearly increases in earnings are mainly due to a recovery in the investment results in wealth management and strong results coming from Interseguro. Payments has performed nicely despite the decrease in earnings as EBITDA continues to grow, and most KPIs grow at double digit.

On slide 8, good news is top line as total revenues continue to grow double digit or 15% year-over-year, mainly due to the growth registered in banking of 18%, wealth management recovering from negative territory one year ago and payments of 8%.

On slide 9, another positive is our fee income which constitutes a source of incremental and diversified revenues, growing almost 10% year-over-year in banking, which represents 63% of IFS fees, and payments which represents 27%.

On slide 10, sound efficiency levels at IFS at 34.9% in the quarter and 37.3% for banking with both ratios being very good, mainly thanks to the operating leverage of the bank which was very strong in the quarter, with revenues growing 18% year-over-year and costs growing only 3%. This has helped the efficiency ratio of the bank to improve 500 basis points year-over-year.

On digital, I would like to start this part of the presentation by reinforcing and highlighting that we are building 100% digital solutions for our customer journey, which includes day-to-day banking, savings, financial planning, financing, insurance, wealth management and acquiring for merchants through Izi and IzipayYa.

On slides 13 and 14, positive news in our digital indicators, which continue to show nice trends when compared to the previous year. Still, we believe there is a way to go in moving these indicators further. As of June 2023, digital customers reached 73% of retail customers who interact with the bank during the last 30 days, up 5 points in the past year. Digital sales reached 65%, up 2% from last year and our digital self-service indicator has improved sharply from 75% to 83%.

NPS for digital customers continues its path to become a top NPS in the next years reaching 46 points this quarter, relatively stable versus previous quarters.

We continue to see an important number of new digital accounts being opened for both individuals and businesses. As of the end of June, 95% of new businesses accounts were opened digitally.

Insurance and wealth management digital indicators show positive developments as well with digital premiums still small, but reaching 9.4%, digital self-service reaching 54% and digital transactions for fund management reaching 43%.

Now let's move to the performance of our four key segments on slides 16 to 24. Starting with banking and in line with our focused strategy, we continued increasing market shares, reaching 22.7% in consumer loans as of June 2023, 19.4% in retail loans, 15.1% in retail deposits and 9.4% in commercial loans. However, in line with the increased riskiness of the portfolio, we have further tightened our credit underwriting standards in consumer loans and small businesses, which has already had an impact on new disbursements.

On slide 18, sustained growth came across all revenue lines in banking in the second quarter with 18% year-over-year growth in top line, with net interest income growing 20%, coming mainly from increased volume and yield on loans, fee income increased 9%, mainly explained by increase in fees from credit and debit cards, and other income increased 11%, coming mainly from FX trading.

On slide 19, interest-earning assets mix and continuous repricing efforts pushed yield on loans upwards 60 basis points in the quarter and 240 basis points in the year, reaching 11.5%, and NIM 10 basis points in the quarter and 70 basis points in the year, reaching 5.6%. Risk-adjusted NIM stabilized in the quarter as the increase in yields has been offset by an increase in cost of risk of consumer loans.

Good news in yields has been partially offset by rising funding costs. Cost of funds reached 4% in the quarter, up 40 basis points on a quarterly basis and 180 basis points year-over-year. Cost of funds has been rising as market level mainly due to two reasons: a continuous migration of retail deposits to more expensive term deposits, both in soles and dollars, and the higher remuneration to commercial and institutional deposits in soles as rates continue to be high and in dollars as rates have continued to increase.

During the month of July, we have started to see a first correction of the overnight deposits rate in soles which constitutes the first turning point in cost of funds.

Our loan-to-deposit ratio of 102% continues to be better than the industry's average of 105%. Deposits continue to increase its share in total funding and retail deposits market share has continued to increase.

On slide 21, we have seen a pick-up in cost of risk up to 3.6%, mainly due to the impact from the retail portfolio which has reached a cost of risk of 6%. This increase is mainly focused on credit cards and personal loans as payroll loans to the public sector employees and mortgages have performed relatively better.

As previously mentioned, the high risk of the consumer portfolio is the result of sustained and consistent high inflation in the country, as seen also in many other countries, a negative GDP growth in the first semester of this year in the Peruvian economy and the social and climate disruptions of the first quarter.

During the first quarter, we granted some credit cards customers rescheduling programs in line with the Superintendency guidelines for the social disruption and El Niño phenomenon. Those reschedulings, which had a large component of unilateral solutions due to the social and climate impacts, are in the process of maturing, impacting cost of risk already this quarter.

NPL coverage ratio continues to be high at the bank at 173% and even more in retail banking at 258%, much higher than the 179% level pre-COVID.

On slide 22, moving on to our insurance business, there has been a decrease in annuities due to a normalization of the market to pre-COVID levels and our market share has recovered and is up at 28%. Both individual life and retail insurance business lines, which constitute high profitability business lines continued to grow nicely year-over-year, or 28% for life insurance and 9% for retail insurance, increasing their contribution to total premiums.

On slide 23, the quarterly return on the investment portfolio came at 6.4%, below the extraordinary high second quarter of 7.8%. The insurance portfolio is composed of 85% fixed income, 9% real estate, and 6% equity and mutual funds as of the end of June.

On slide 24, wealth management is 6% up in terms of assets under management. Returns remain in positive territory but are not fully recovered yet.

On slide 25, we want to give you a summary of the developments in our payment ecosystem which we have continued strengthening. After the acquisition of the remaining 50% of Izipay in April 2022, we launched the first value-added service Arisale, an integrated solution for billing and inventory management for merchants.

This second quarter has already seen nice adoption of our solution, reaching more than 7,000 merchants as of the end of July paying monthly fees. Moreover, during May this year, Tunki plus Izipay combined to launch IzipayYa, a solution targeting micro merchants with interoperable QR codes and same-day availability of cash.

Growth in merchants and volumes continues. Izipay merchants increased 53% year-over-year, reaching 1.2 million, transactional volumes grew 16% year-over-year, and moreover, e-commerce transactions are gaining share within our transactional volumes reaching 16% as of the end of June.

Izipay represents a growing and profitable operation. Revenues continued to grow nicely, 8% year-over-year, supported by the increase in the transactional volumes and merchants with some pressure on MDRs coming from increased competition. EBITDA continues to increase as well, or 9% year-over-year, reaching 30 million soles in the quarter.

We have been working to accelerate the growth of our payments ecosystem by having all our assets work towards a common strategy. We are focusing on increasing transactional volumes, offering merchants additional services, continue to pilot low-risk loans to merchants, and use Izipay as a distribution network for Interbank products as well as a source to increase float. As shown on slide 28, we are starting to provide new sources of revenue coming from increased float in Interbank accounts from Izipay flows, which have increased 32% year-over-year, as well as from greater transactional volumes from micro merchants, which have grown 2 times year-over-year, thanks to IzipayYa.

On slide 29, Plin has been accelerated by the new landscape of interoperable P2P system. Plin reached almost 12 million users as of the end of June, with Interbank participation at 46%. Number of merchants continue to increase as well at a pace of 84% year-over-year for Plin with Interbank participation at 56%. And the volume of transactions has continued its strong growth, reaching twice the volume registered in the same quarter one year ago.

Plin and Yape interoperability has started in April. This has been an important development for financial inclusion in the country, which the Central Bank has encouraged, and which should help to bring more Peruvians into the financial system, reducing the use of cash, which continues to be high in the country. Number of transactions for Interbank have increased 82% from April to June.

On slide 31, let me give you an update on our operating results for the second quarter and a revised guidance for ROE and cost of risk. First, total capital ratio of 15.2% and core equity Tier 1 ratio of 11.4% as of the end of June are above our guidance. ROE of 13.7% in the first semester has confirmed the trend in cost of risk and investment results, thus, we are revising our guidance downwards to around 14% ROE. 11.6% total loan growth and 18% consumer lending growth is above our guidance, though we expect further moderation in the coming months. NIM for Interbank was 5.6% in the first semester, in line with guidance. Cost of risk for banking was 3.4% in the first semester and 3.6% in the quarter, above the higher end of the guidance. Following quarters might continue to be challenging depending on the behavior of the consumer portfolio. We are revising our guidance upward to 3.2% to 3.6% for the yearly cost of risk. Efficiency levels for IFS and Interbank continue to be good at 34.2% and 37.1%, respectively, for the first semester and within guidance.

On slide 32, we have continued to strengthen our sustainability strategy upon our focus areas. Our latest developments on the environmental front include a co-hosted event on climate risk with Peru Sostenible. In addition, our target for sustainable financing for 2023 has been set to 500 million soles, aiming to build more sustainable business. On the social front, our financial services education platform, Aprendemas, as well as the launch of IzipayYa are solutions that are contributing with financial inclusion. Moreover, Interbank has been recognized as #1 in the Merco Talento ranking for talent attraction and retention, and was certified by Aequales as a company committed to equality and diversity. Finally, on our governance front, Interseguro released its first sustainability report in line with the GRI framework and Inteligo Group companies approved the Responsible Investment Policy aligned to the Principles for Responsible Investments.

On slide 33, let me finalize the presentation with some key takeaways. First, we have seen a first half of 2023 with a challenging macro scenario aggravated by the social unrest and climate factors. Second, we have a growing customer base, 15% revenue increase year-over-year, and market share expansions in our key areas of focus. Third, further NIM expansion to 5.6% in banking due to increased yield on loans. Retail cost of risk continues to increase on the back of macro scenario, strong coverage at retail banking. Five, investment results are normalizing on insurance and wealth management, driving IFS earnings up 47% year-over-year in the second quarter. Six, we have sound efficiency levels, IFS cost income ratio at 34.9% and banking at 33.3% are benchmarks in Latin America. Seven, we continue to strengthen our payment ecosystem and Izipay represents a growing and profitable operation. Finally, we are revising our guidance for cost of risk and ROE for this year. However, after the current credit cycle, around 18% sustainable ROE remains our midterm target.

Thank you very much. Now we welcome any questions you might have.

QUESTIONS AND ANSWERS

Operator
Thank you. At this time, we will open the floor for your questions. First, we will take the questions from the conference call and then the webcast questions. If you would like to ask a question, please press the star key followed by the one key on your touch tone phone now. Questions will be taken in the order in which they are received. If at any time you would like to remove yourself

from the questioning queue, just press star then two. Again, to ask a question, please press star one now. For the webcast viewers, simply type in your question in the box and click submit question. We will pause momentarily to compile a list of questioners.

The first audio question comes from Ernesto Gabilondo with Bank of America. Please go ahead.

Ernesto Gabilondo
Thank you. Hi, good morning, Luis Felipe and Michela. Morning to all your team. Thanks for the opportunity to ask questions. My first question will be on Peru's outlook. Can you provide us like an update on what could be the impact on El Niño? I don't know if you have been looking to weather institutions to understand what could be the expectations. I don't know if it could be between low to moderate. And, also, at the end the floods in Peru tend to materialize early next year. So, I wanted to double check that with you. And then, we have seen some demonstrations that took place in the country a couple of weeks ago. They wanted to remove the president and to call for early elections. I believe at the end, it didn't have a material impact. But are you hearing about the possibility of new demonstrations? So again, any color on El Niño and the potential outlook will be appreciated.

Then on my second question is on your ROE guidance. So, you are lowering it for this year, and you are maintaining it medium-term at 18%. But I would like to understand when you expect to reach the 14%. Do you think it could be achievable next year? And what could be the drivers behind it? Would it be a normalization of the cost of risk and probably a more normalized coverage ratio? What are your expectations on that? Thank you.

Luis Felipe Castellanos
Okay, Ernesto. Thanks very much for your questions. On El Niño, we are following it very closely. Unfortunately, it's not clear yet. Based on what we've been reading, the people we've been meeting, the think tanks and the agencies that follow this phenomenon, would say there's a 50-50 chance, probabilities of being a strong or extreme Niño are not that high. It's probably going to be a 50% probability of it being a low to moderate El Niño. But again, every week, we get new information. Some of them collide with each other, some let's see the U.S. agencies, probably they see more probabilities, then next week we get something from the Australian agency, and they see less likelihood. So, it's pretty unclear.

The fact is that temperatures in the country and in the region are higher than expected. So, we are preparing to have something. That's another one of the reasons why we are moderating our growth just to, because we are moderating growth in two fronts, probably Michela will elaborate on it later. But for one in some segments, higher risk segments, where we are moderating growth, but also we are starting to prepare in some regional zones that usually get affected by El Niño. If something happens, it's unlikely that it will happen by the end of the year, which is not discarded, but that's not the number 1 scenario. It's probably, as you mentioned, going to happen in terms of heavy rains and floods, if they come, early next year, more likely late January or February, which is the usual date.

So again, there's not lots of update there, we are again like you and probably everybody, following the news. Not very concrete things yet, just getting prepared, similar to what the government is doing. The government is putting lots of funds in order to reinforce certain infrastructure to make sure that the phenomenon is not as bad as we've seen. But again, we have to play by ear once we get new information.

In terms of the social unrest and political turmoil that we saw at the beginning of the year, that has come down significantly. There has been some announcement of continued people trying to do things that were not very successful. Those happened in July, specifically the 19th of July. At the end, I think the report was that there was about 20,000 to 25,000 people actually going to those demonstrations. So, it has not had an impact. Personally, I think that the level of these things has come down significantly. I do not expect them to pick up. However, again, it's going to be news dependent. If something comes around the government that makes some people push again, something could happen. But our scenario is that that’s very low probability so far. So, I think that’s water under the bridge with the news that we have right now in front of us, and hopefully that will continue to be the case.

And then in the ROE, cost of risk front, just briefly. Again, we haven’t worked in detail on the numbers for next year. There are lots of things moving around. Obviously, we will come back to you and the market when we have more clarity. What we are seeing in terms of increased cost of risk has to do with two things, as Michela mentioned. First, slower economy, that’s a fact, high inflation impacting for so many months the consumer, that’s also a fact. So, what would change there, probably the impact that we had in the first semester because of these dislocations of the social unrest and the Yaku phenomenon will not repeat. Let’s see what happens with El Niño. So, that was kind of what we see as an external factor that affected our already slow-growing economy. So, it’s going to be probably negative growth or – sorry, moderate growth, not negative, but starting this quarter and hopefully for next year, mediocre growth of around 1% to 2%, hopefully picking up at some point of next year, but it’s not going, the basics there is not to continue going negatively. And hopefully, next year will be also the same. Inflation should start to come down, that should put some relief.

So, again, I don’t want to project next year, but there are many macro conditions that should turn to the positive. Let’s see how they evolve, but not negative growth and lower inflation should have positive headwinds for our operation. Again, as we mentioned, midterm, we are very confident that the 18% is achievable given the nature of our businesses, the stage where they are, the investments that we’re doing, the efficiency that we’re running. The higher cost of risk of this quarter, it’s not only explained by the slow growth and the inflation. It has an important factor coming from the first quarter dislocations that were mentioned.

That should pass and hopefully, let’s say, I’m not trying to project, but certainly, for the last quarter of this year, that should be also water under the bridge in terms of those impacts that happened in the first quarter which our models captured partially because we closed very soon the quarter to the events in the 1Q. It has captured a significant portion this quarter, probably there’s something left there for the next quarter, but we expect normalization for the latter part of the year and hopefully, next year, we’ll see probably not as good as pre-COVID levels, but obviously not as bad as we’ve seen in the first semester of this year.

Ernesto Gabilondo
Perfect. Very helpful, Luis Felipe. Thank you very much.

Luis Felipe Castellanos
You're welcome, Ernesto. Thank you.

Operator
The next question comes from Juan Recalde with Scotiabank. Please go ahead.

Juan Recalde
Hi, good morning. And thank you for taking my question. So, the economic growth expectations have weakened, and cost of risk has been higher than anticipated. However, we are still seeing the consumer loan book expanding almost 4% quarter-on-quarter. So, can you talk about how you are balancing the cost of risk with growth in the consumer portfolio? And what type of products and clients are driving the growth in the consumer portfolio?

Luis Felipe Castellanos
Sure. Thank you very much. Well, as you know, our portfolio is very geared towards consumer, that's not a surprise. So, we're not afraid or we are familiar with the credit cycle. We know this happens. That's the credit cycle as is. As mentioned, it's been exacerbated by certain external factors, but our book reflects our strategy and we're leaders in consumer. We want to continue being leaders in consumer, and we're building all our strategic pillars to make sure that it is sustainable.

Obviously, we have to be very tactical depending on the situations. So, what we're doing is we continue to growth, while gearing towards lower risk segments presents some challenges, of growth and your value proposition has to come there. To put the brakes in growth, is not something automatic. You have your credit card customers; they have their lines, they use them in certain tough situations, and we have to be there for them. Obviously, we have to be very responsible in terms of what we do. But part of the growth is our existing customers using the lines they already had. Consumer direct, like cash consumer loans is easier to put the brakes on.

So that's what we've seen, like, we've seen the collateral structure of our portfolio still growing during the second half. It has already started to decelerate, and probably will continue doing so because, again, we've been able to manage the portfolio we have, and we are gearing towards lower risk segments. We are also boosting our payroll deductible loans efforts. That will probably have a toll in terms of risk reward profitability. But again, it's part of what we've been doing for the last 25 years. We've gone through these cycles. And what is good is that the drivers of the engagement and relationship with customers remain healthy. It's just a matter of helping them to go through this tough situation, and we're ready to do that, moderating our risk appetite in the quarters to come.

Juan Recalde
That's very helpful. Thank you for the comments.

Luis Felipe Castellanos
You're welcome.

Operator
As a reminder, if you would like to ask a question, please press star then one to be joined into the question queue.

The next question comes from Alonso Aramburú with BTG. Please go ahead.

Alonso Aramburú
Yes. Hi. Good morning. And thank you for the call. I have three questions. The first one is on your holding expenses, which were a little bit larger than usual. Can you just comment as to what exactly happened there? Second, also, when it comes to Inteligo, which reported better numbers, but it continues to show some mark-to-market losses. Can you just comment as to what exactly is being marked down. Has that been already fully marked down, so we can see better numbers in the next couple of quarters? And, finally, regarding your margins, which have continued to move higher, which is good news. But now as the rate cycle likely continues to, or will start to decline in a couple of months or so, do you expect a similar sensitivity on the way down? Or do you think your margins can be more resilient as rates decline? Thank you.

Luis Felipe Castellanos
Thank you, Alonso. On the holding expenses, yes, it's been a particular month. Basically, that structure is very simple. Basically, we don't have like lots of overhead expenses. There're only like the regular ones. So, what is impacting is a small portfolio that we have there. As you remember, I've talked to you about this many times in the past, part of our strategy is not to just like invest directly, in local fintechs or related companies, we do have a small portfolio at the Holdco level. We have deployed funds. It's not that big, it's only like the investment with them there, among five or six different names is no more than $30 million out of a total asset base of $34.5 billion. It is small.

However, what has happened in the last quarter is that some of those investments, which are payments companies or credit-related fintechs in the U.S. mainly, had also a valuation actualization. So basically, that's it. So, in our portfolio of capital deployed of $25 billion at some point during early last year because the valuations don't come frequently, that went up, and we marked it up at that moment. With all what happened late last year and early this year when the new valuations came in, they're reflecting the actual value of tech companies and the fintech companies. So that basically gave us a hit of around 30 plus million soles. So that's basically the impact there.

All the valuations are still above the capital deployed. However, it had gone up because of the frenziness of what we saw in terms of fintech valuations, and it went down because of the frenziness that we saw on fintech valuations in the last quarter. And so, again, $28 million deployed among 5 to 6 names that went up at some point in the last two years and went down this quarter, reflecting market conditions. So basically, that's it. We hope that it will not repeat in the future. And if it goes up because something happens, we will report it as well as we have done in the past.

In terms of Inteligo, let me pass it on to Bruno so he can give us a better view on terms of what's going on there, and then I'll come back with the margin question with Michela.

Bruno Ferreccio
Yes. So, in terms of Inteligo’s portfolio, there’s one effect that is similar or the same as Luis Felipe just mentioned. We have a portion of the portfolio that is invested in some funds, private equity funds, and the effects that we’ve seen this year, which we would expect to be completely marked are, in some sense, due to some of the effects that were felt last year. Now, the majority of the portfolio is mark-to-market. And so, on the fixed income and equity side, it’s, if I would say, very hard to predict whether this is going to move a lot up or down. It depends on the market because, again, it’s marked-to-market, and so it would be largely dependent on what the market prices are going to do.

The fixed income portfolio has been rebalanced. There is a good portion now that is going through equity as opposed to P&L. But then the equity portion, so the stocks that we hold in portfolio are going to fluctuate as market valuations go for the rest of the year. So hard to say how much more, but we have seen, like we've been saying, we've seen much better performance this year, and we would expect that to be much more stable going forward for us in the portfolio.

Luis Felipe Castellanos
Thank you Bruno and Alonso, I forgot to say something, actually, because the portfolio we have at the Holdco that created these expenses, it's not just investments, different to what we do in the insurance company or the wealth management company. These are fintechs where we get access to know-how, we get access to observer rights in their boards. We get access to their management to learn what they're doing in terms of credit underwriting, in terms of the building of their payment solution. So, it's very strategic for us to have them. Again, it’s the way we're learning. Instead of building something local in Peru, which we believe the market is very limited, and we have our own, digital solutions coming from the bank, we do those investments again in the order of 5 million each, but we do them only if we get access to a special know-how that we feel we can then transfer in order to put to work into our strategic deployment of our initiatives, okay? So that's the rationale behind those investments there.

And then your last question was in terms of margins. Let me pass it on to Michela, so she can help me with that.

Michela Casassa
Good morning, Alonso, how are you? In terms of rates, I'd like to go a little bit on the different lines because, it's not evident yet what is going to be the net impact of the different trends. If you see what has happened in context were rates have been increasing both in soles and in dollars at a very high pace, we saw a very big increase in yield on loans. And then we have also seen that in terms of cost of funds. So, if you see like the last 18 months, cost of funds has catch up with yield on loans, and that is why NIM has continued to increase, but this quarter only 10 basis points.

So going forward, we have different trends actually for soles and dollars because at some point, before year-end, we should start to see soles rates decreasing, which should have some positive impacts in terms of our cost of funding, especially the short-term and overnight institutional deposits, which are still an important part of funding. So those should decrease sharply. And actually, in July, I mentioned a little bit about that, we have already start to see an inflection point there.

And our asset book, more focused on retail, should be a little bit less sensitive. We should try to stick as much as we can with the higher rates. In the commercial book, it's a little different because there you reason in terms of spreads, so we should see rates decreasing there even in soles.

Now when we talk about dollar rates, the dollar rate has continued to increase, even recently, and we still need to see what happens until year-end. So, in terms of dollars, next year, we could still see an increase in cost of funds because the full effect of the increasing rates of this year still will impact the cost of funds next year. And, if then there is an inflection point next year and the rates in dollars start to decrease, in the commercial loan book, where we have the biggest part of dollar loans, we could see there also a decrease in yields.

So, putting everything together, I am not yet completely sure what is going to happen with NIM. We are just running the estimates now, and it will depend also of a third component, which is the portfolio mix because this year, portfolio mix has also helped improve the yield on loans. And, depending on the growth of next year, that could continue to be the case. So, I'm sorry, if it is not a straightforward answer, but I think there are different trends moving in different directions now.

Alonso Aramburú
Okay, thank you for the color, Luis Felipe, Michela and Bruno. Thank you.

Operator
The next question comes from Marlon Medina with JPMorgan. Please go ahead.

Marlon Medina
Hello, everyone. Thanks for the opportunity to ask questions. Actually, most of my questions have been answered, but just a quick follow-up on margins. And I understand it is different for the dollar portion than for the soles portion. But can you provide the sensitivity for every 100 basis points that rates move?

Michela Casassa
Yes. Listen, we have provided this sensitivity in the past. And the sensitivity has been neutral to positive when the rates were going up. And that was like the theoretic sensitivity of 100 basis points move. But what has happened in reality has been a little different from that because of the cumulative effects of many increases in rates. So, at the end of the day, it ended up being more positive than what we estimated at the time. So let me come back to you for the sensitivity now with the decreasing rates for soles and dollars because we are still working on that one.

Luis Felipe Castellanos
Yes, bottom line there, and I think that Michela mentioned it before, the consumer book should be less sensitive, especially it's mainly soles and pricing there does not correlate to the cost of funds really, it's more related to risk appetite, actually. So shouldn't be on the downturn of the rates as sensitive as the commercial book.

Michela Casassa
Yes. And maybe one additional comment is that the speed of the movements in rates have also been impacted by competitive dynamics and liquidity. So, for example, this year, we've seen soles

rates in the market being higher than the reference rate because of a decrease in liquidity of the financial system overall. So, we will have to see also what happens with the liquidity in the market.

Marlon Medina
Perfect. Thank you very much.

Luis Felipe Castellanos
You're welcome.

Operator
The next question comes from Andres Soto with Santander. Please go ahead.

Andres Soto
Good morning and thank you for the presentation. I have two questions. The first one is related to the payments business. We see results still under pressure due to the customer acquisition cost. And I would like to understand based on what you have seen so far, have your expectations for the ROE in this business changed in any way, positive or negative? And when do you expect this business to be accretive in terms of ROE for the overall portfolio?

Luis Felipe Castellanos
Okay. Thanks, Andres. I'm going to pass it on to Carlos Tori so he can help me with the question. But basically, here, this business, like the payments business, specifically Izipay, we don't see that as opposed to the universal banking or even insurance company. ROE is not an obsession for us in payments or Izipay. It's more EBITDA what we're looking at because we're growing and we're depleting lots of Capex there in order to do the expansion. But Carlos could probably provide a little bit more clarity on the specifics of the numbers.

Carlos Tori
Okay, so hello, Andres. As Luis Felipe said, some of the pressure that you've seen comes from the growth that we've had in the last couple of quarters. We will continue to look for that growth and... sorry, can you hear me? I think I've lost connection.

Michela Casassa
No, it's okay.

Bruno Ferreccio
It's okay, Carlos.

Luis Felipe Castellanos
Yes, Carlos, we can hear you.

Carlos Tori
So, you've seen that we will continue to follow that growth. There has been some pressure on the margins due to increased competition, but we expected that. What we are trying to do is to maintain our share in physical POSs, increase the float or the flow to Interbank, and add services to those clients that will increase fees, both at the bank and at Izipay. And we would like to increase our share in the e-commerce business, which in POS, we have somewhere around 50%, probably

a little bit higher than 50%. And then in e-commerce, we have probably somewhere around 25%, 26% of market share. So, we will focus on growing in e-commerce. We will continue to follow that growth and build the aggregated services that are starting to bring in more income. So that's kind of how we look at it. I don't know if that answers your question, Andres.

Andres Soto
Yes, that's very clear. Thank you, Carlos, for the additional insights. My second question is related to a follow-up on the El Niño question and your cost of risk outlook. I would like to understand to what extent your new guidance for cost of risk already incorporates the risk of El Niño or if indeed El Niño materializes, we should see additional cost of risk pressure this year? Or is this more of an event for 2024?

Luis Felipe Castellanos
No, I would say that the cost of risk is for 2023, as I mentioned in the guidance. The effects of El Niño will probably come, if they come, early next year, as we've seen in the past, we've seen usually in late January, February. However, part of the growth outlook that we are providing is incorporating some restrictions in some areas that could be heavily affected by El Niño. So, we're preparing the portfolio for that, but in terms of growth.

One thing that has not come across is that our enterprises and commercial portfolio is behaving very well despite some of the temperature issues that we're seeing. As you know, we have good exposure on fishing, exposure on agriculture. That's behaving very well. Our PDLs there and the relationship we have with the companies. We work with the most solid ones. So, we are also working with them in order to make sure they are ready for an El Niño as they've done in the past, and we are confident that they will be able to go through that process with no issues or with limited issues. So, whatever comes from El Niño will be mostly related to any impact on the consumers around the area impacted by El Niño, but our commercial book exposure, we're very happy with it, even in this downturn of the economy, it's proven to be very resilient. Our delinquency rates are very low, and that's the way we manage the bank. A little bit more aggressive on the commercial -- sorry, on the retail loan book and more conservative in the commercial book so we have a more balanced portfolio.

Andres Soto
Thank you, Luis Felipe. So, if I understood correctly, you are including the effect of El Niño in your guidance, mostly in terms of loan growth, not as much in terms of cost of risk. But if we look to past El Niño events, five years ago or so, what was the historical impact of this type of events on your cost of risk? And when should we see that being reflected, I mean in terms of it is at fourth quarter of this year or, in terms of provisioning, I mean, or it's going to be once the event is in full swing?

Luis Felipe Castellanos
Yes, it should be between the first, but mostly in the second quarter of next year, similar to what we've seen in Yaku, which is very different because that was a very different phenomenon that we have not seen for many years. So yes, it's not included this year. It's probably, if it hits, it's going to be incorporated in the first quarter or second quarter of next year, and that should be it basically because the phenomenon does not last the whole year. What we've seen in the past is a similar thing. 2017 was very strong in the north of Peru and some portion of Lima. I would say

there you'll see probably 1% increase in PDLs related specifically to El Niño and very specific in certain areas. It does not affect the whole of the country in the same way […] we expect.

Andres Soto
Perfect. That's very clear. Thank you so much.

Luis Felipe Castellanos
Thank you.

Operator
At this time, we will take the webcast questions. I will now turn the call over to Natalia from the InspIR Group.

Natalia Nirenberg
Thank you. The first question comes from Daniel Mora Ardila from Credicorp Capital. And the question is, what is the expectation for asset quality indicators considering the growth in the consumer segment and the challenging outlook ahead? When do you believe the bank could reach the peak of NPLs? Can this change the appetite of growing in the consumer segment?

Luis Felipe Castellanos
Hi Daniel, thanks again for your question. Let's see. What is the expectation for growth when you believe the bank could reach the peak? Well, we think we've reached the peak this quarter. There are probably some leftovers for next quarter. But based on what we see going through the book, we're going through the peak. It all depends -- like in terms of what we already have in, okay? And again, a big portion is what's happened with Yaku and the social unrest of early in the year and the reprogramming of those that have been maturing in the last months. So, that's I would say, the most important portion of what we are seeing this quarter. There might be a leftover for next quarter, but probably next quarter will be worse, similar or better than this. I don't want to anticipate numbers. Obviously, we cannot predict exactly, but what I am seeing is that. And the change in the appetite, again, we are different to our competitors, like we have like 55%, 56% towards retail. This is what we've been doing in the last 25 years or 30 years, and we'll continue to do so. Obviously, there we will go through the credit cycles. We will shine when things go all up, and we'll suffer a bit when the credit cycle is in the down period, which is what we're seeing right now.

We are moderating growth. We're looking to go in lower risk segments. Based on what we're seeing in the economy, that change is not going to be radical, but you will see moderation, which already has started. We've seen some in this quarter. We've seen that in July and probably will continue during the latter part of the year. We're always looking for new pockets where we can grow. We are looking to reinforce our models. As you know, the model got like messed up in the whole world because of what happened to COVID and the liquidity that was put into the systems overall. So, we're working to refine our models and be able to grow again, targeting a moderation in growth and lower risk segments. And once the situation stabilizes, obviously, we're going to go to the emerging middle class, as we've been doing in the past.

Natalia Nirenberg
The following question comes from Alexandra Ramos from La Positiva. And the question is, I would like to know more details about the Insurances' ROIP. Why has it gone down in this quarter?

Luis Felipe Castellanos
Okay. I think that's a great question, Alexandra from La Positiva. Let me pass it on to Gonzalo, who can help you with that answer.

Gonzalo, you're in mute, I think. We cannot hear you.

Let's do something. Let's go to the next question. And while Gonzalo solves his technical issues, we'll come back to him. So, I don't know, moderator, do you have a third question?

Natalia Nirenberg
Yes. Okay. The next question comes from Greg Mitchell from AVP Ventures. Can you please remind us how the digital strategy is improving cross selling both within each IFS business, for example, multiple products within banking system and across IFS business segments, for example, between banking and payments? And how significant will the impact be on overall performance?

Luis Felipe Castellanos
Okay. Thanks, Greg, for your question. Let me pass it on to Michela, so she can help me with that. I think she has already been looking at that.

Michela Casassa
Okay. Let me go a little bit into detail of the value that is being generated by the digital strategy, which is something that we try to reflect across the whole presentation, but I would like to make it very clear. So, the first point is that the digital strategy is helping us to increase customer base on an accelerated pace. So, you have seen that across all business lines: double-digit growth in banking, insurance, wealth management, and also payments.

Now, how do we monetize this increased customer base? First of all, more float, and this is specifically happening already in the different customer segments. So, in retail, we are seeing an increase in market share of the retail deposits, which is sustained in time. And this is mainly thanks to digital, creating more engagement, Plin this helps with this. More engagement means being more principal or being the main bank of these clients, so they bring more volumes to us.

The third point is more cross selling. And here, we can see a lot of things being cross companies. So, we are working very hard in bank assurance. So, for example, now we have all the Interseguro retail insurance products being cross sell to our client base through the app. We also see the turnover of credit and debit cards, and this is also being used through the app growing double digit. We are also seeing the growth in market share in consumer loans, and this has a strong impact coming from digital.

And the last point, which talks about what is the impact or the relevance of this on the numbers and also the synergies with payments. I think some of this is already showing in our numbers. First of all, fees are growing almost 10% for banking and for payments. And this is related, due to the specific focus on payments, both for customers, but also for merchants. We also have seen the increase in net interest income coming from the increase in volumes, not only in yields.

And another thing which I think is very important to consider coming from the digital strategy is that IFS has been able to grow client base and revenues, improving the efficiency, so the marginal acquisition cost of digital for sure is lower. And what we are seeing is a growing client base and top line with an improving cost income. And now the improvement in cost income does not come only because margins are high and the net interest income is growing a lot, but because we're being able to manage this growth with a little increase in costs. You have seen the numbers this quarter are less than 5% increase in cost. So, I think this is something that differentiate us from our peers in the region. And I think it's something that constitutes the core of how we intend to continue extracting value from our digital strategy in the future.

Luis Felipe Castellanos
Okay. And now I think Gonzalo is back, so we can go back to question number two of this section.

Gonzalo Basadre
Yes. Thanks, Alexandra. Regarding your question, first of all, there's a small reduction in earned interest basically for two reasons. One is exchange rate came down. So, our dollar holdings produce less interest in soles terms. And the second is, that line also includes some dividends received. We received a smaller amount of dividends during the period. So that explains that part. The other line that has also reduced is, we made a loss of 30 billion soles on real estate valuation and those two lines explains most of the reduction.

Luis Felipe Castellanos
Okay. Thank you, Gonzalo. I don't know if we have any more questions from the moderator?

Natalia Nirenberg
As there are no further questions, I will return the call to the operator.

Operator
And there appear to be no further questions on the audio side at this time. I would like to turn the floor back over to Ms. Casassa for any closing remarks.

Michela Casassa
Okay. Thank you very much. Thank you, everybody, for all the questions and for attending our conference call. We'll see everybody again back when we report our third quarter results. Bye. Thanks.

Operator
This concludes today's conference call. You may now disconnect.