



WORLD RECORD. NOW WHAT?

SANTANDER, OF SPAIN, ISSUES THE LARGEST PUBLIC STOCK OFFERING IN THE WORLD THIS YEAR AND SHOWS THAT BRAZIL HAS BECOME ONE OF THE MAIN STAGES FOR COMPETITION AMONG BANKS IN THE GLOBAL MARKET.

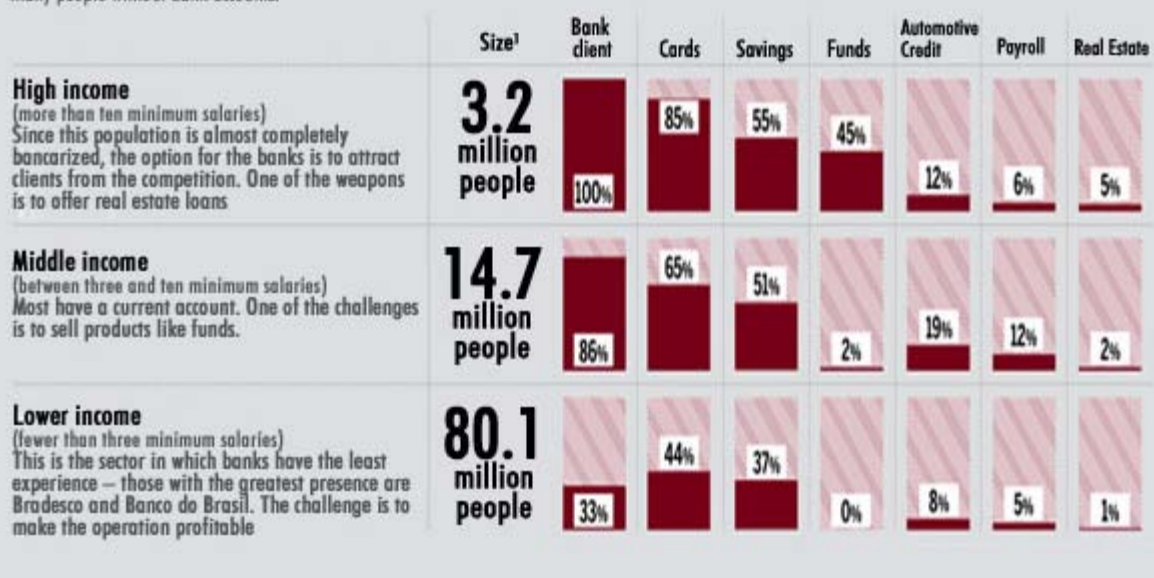
Fabio Barbosa, president of Santander in Brazil: the hard part now is to deliver on the promises to shareholders

Exactly one year ago, Fabio Barbosa, president of Santander's Brazilian operations, was in a corner. His boss, the Spaniard Emilio Botín, Santander's controller, did not hide his irritation. At a press conference organized at Hotel Grand Hyatt, in Sao Paulo's south zone, in October 2008, Botín declared, with all possible pomp, that his objective was to transform Santander into the "largest private bank in Brazil". In one of those historical coincidences filled with irony, three days later Itaú and Unibanco announced the largest banking merger in the Brazilian financial system and they took the lead and were all alone at the top. Extremely upset, Botín made it very clear to the highest echelons of Santander in Brazil that they should have found out about the negotiations in time to avoid the fiasco of the press conference - in the market, the Grand Hyatt announcement became a joke. But on the 7th, the initial public stock offering by Santander's Brazilian operations, issued simultaneously on Bovespa and the New York stock exchange, reminded everyone it was prudent to not make fun of the Spanish bank. After capturing 14.1 billion reais, the largest initial public stock offering of all time on Bovespa and the largest in world this year, Santander showed it was strong and ready to fight for space on the Brazilian market.

Why the banks are getting ready

Today, Brazil is one of the most promising markets for banks in the world. A study by the consulting firm Bain & Company shows that in the lower and middle classes there are still many people without bank accounts.

IN the upper classes, everyone has a relationship with at least one institution, but they use few of the available products



Even if the old plan to take over first place in the ranking of private banks now seems nearly impossible - the leader Itaú Unibanco has almost twice the assets - today Santander has size, geographical presence and money to at least bother the three in front of it: Banco do Brasil, Itaú Unibanco and Bradesco.

With going public behind him, Barbosa, 54 years old and from Sao Paulo, now faces the pressure of thousands of shareholders avid to know how Santander will invest its 14.1 billion reais and how it will transform them into even greater wealth. Over the weeks that preceded the public offering, Barbosa participated in a marathon of meetings with investors in Brazil, the United States and Europe. He made it clear that his goal is to grab at least 2 percentage points of market share in the main segments in which the bank operates in five years - including real estate credit and credit for small and mid-sized



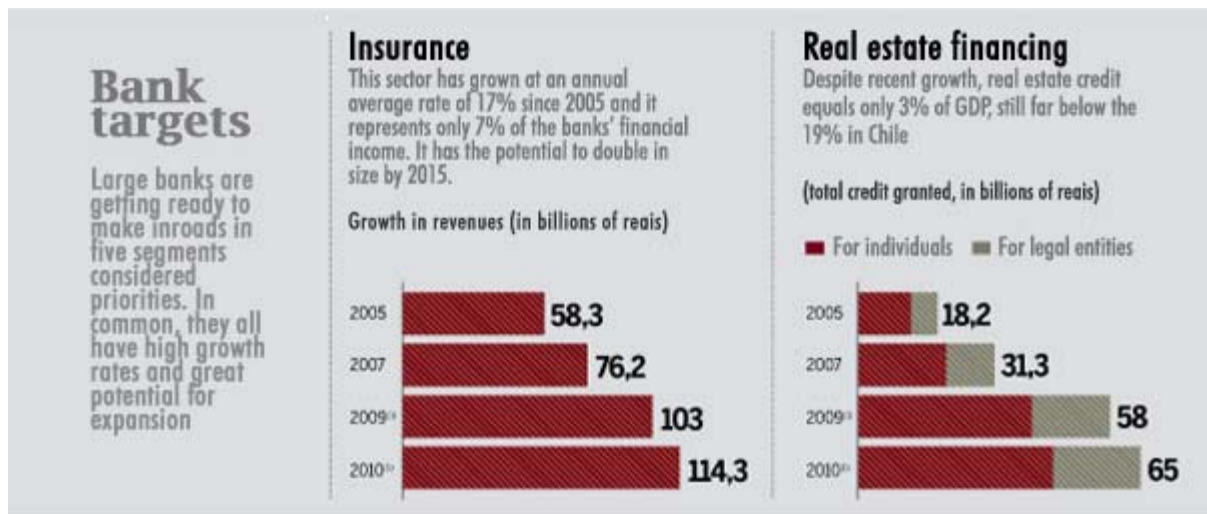
Queiroz, employee at São Paulo's subway: every day, 53,000 new accounts in the country

companies. The message was that the bank did not intend to merely benefit from the country's expected growth. He promises to do that while also taking clients from the competition. It also became clear that Santander was not selling its shares based on past performance - the history of the bank's profitability in Brazil, about half that of its rivals in 2008, is not impressive. The price of its shares reflects promises of growth. Now Barbosa and his team have the commitment to deliver.

Even in a sector full of mastodontic egos, part of the competition recognizes a professional with rare skills in Barbosa - he was lifted to Santander's top position even after the bank he was running, ABN Amro Real, had been bought out by the Spanish, something very rare in any market. Today he commands Santander's second largest operation in the world. But his adversaries also say his biggest test is only just beginning. The competition is about to begin. Over recent times, Brazilian banks have adopted the law of the strongest to perfection - in a few words; the big have gobbled up the weak. For example, Banco do

Brasil is the result of adding Votorantim and Nossa Caixa. Besides the two banks that comprise it, Itaú Unibanco also added BankBoston, BBA and Nacional. And so on. The result was a concentration unprecedented in the history of the financial system. The ten largest banks in the country are currently responsible for 94% of all bank agencies. Ten years ago that participation was 76%. The sum of assets for the top four banks in the ranking has almost doubled since 2007 - in the middle, it is always good to remember, of the largest international banking crisis in seven decades. By 2007, no Brazilian bank was on the list of the world's top 20 in market value. At the beginning of October, Itaú Unibanco was 11th and Bradesco 17th. "The large financial institutions are looking forward and getting ready for the Brazil of the future," says Aldemir Bendini, president of Banco do Brasil, which began an expansionist marathon over recent months. Driven the government's anti-cyclical policy and with uncommon aggressiveness, public banks have increased their market share from 34% to 40% over the past 12 months. "Everyone wants to hold on to what they have and conquer new spaces."

But that is getting more and more difficult every day. Due to a lack of new targets, the strategy of growing by buying out competitors is running dry. Now the predators are directing their guns against each other. "The only way to grow is to compete directly to win over clients and grant credit," says Rodrigo Dantas, director responsible for the financial area of the consulting firm Roland Berger. It may seem like a paradox, but this concentration has served to stimulate, and not restrain, competition. This fact is in line with the top economic research results. In the past, classic economic theory affirmed that competition grew as the number of competitors increased. The ideal world for economists was that of "perfect competition", comprised of thousands of small producers. In practice, some of the most competitive markets are made up of a reduced number of large companies willing to do anything to seduce the consumer. "In many cases, concentration has stimulated innovation," says Elizabeth Farina, former president of Cade, the entity that watches over competition in the country.



The first signs of stiff competition can already be felt. With the tendency for a reduction in interest rates and lower yields of public securities, in recent years the banks have begun to increase loan volumes. Of the five areas considered priorities by most large banks - insurance, real estate loans, consumer credit, credit for small and mid-sized companies and credit cards - four are in all out growth (the exception is credit for mid-sized companies, which is still crawling). According to data from Instituto Assaf, of Sao Paulo, the granting of credit represented 49% of the banks' financial income ten years ago. In 2008, that index reached 63% and the perspective is for it to continue rising. This more aggressive attitude can be seen in the reduction of spreads. According to data from the Sao Paulo consulting firm Tendencias, the difference between what the bank pays to capture money and how much it charges in loans to individuals should finish 2010 at 22.6% - a very high percentage, but still the lowest this decade. "The banks have grown accustomed to earn more from the rate than from volume. We have now entered the era where gains will come from scale," says Alexandre Assaf Neto, professor of finance at the University of Sao Paulo.

Consumer credit²

Consumer credit has doubled over the past four years, but still only represents 4% of GDP, compared to 18% in the United States

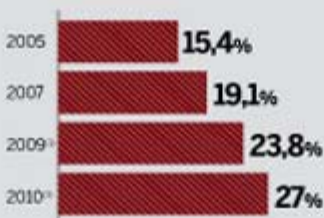
(in billions of reais)



Cards

The number of credit cards has grown, but use is still low compared with abroad. In England, for example, 57% of all purchases are made with cards

Card use in total purchases



Mid-sized companies

In Brazil, the participation of small and mid-sized companies in the total credit portfolio is 20.6%, still low compared to the international average, which is around 35%.

Participation of small and mid-sized companies in the banks' total credit portfolio



¹ Projection ² Balance at the end of each year. Includes automotive and cards
Sources: Abecs, Accenture, Banco Central, Cnseg and FGV



Restaurant in São Paulo: more than 20 million credit cards issued in Brazil in 2008

This scale will be driven by the good moment being experienced by the Brazilian economy. This is a surprising situation for any Brazilian over 30. The scenario many banks work with projects that the economy will grow about 5% per year until the 2016 Olympics (that's right reader, you are not dreaming) - a rate few countries expect to achieve. This expectation is imbedded in the banks' share prices - this in part explains the 80% appreciation in securities from the three largest institutions this year. "Brazil has already had several periods of euphoria, followed by deception. In the 1970s, there was a feeling that no one could hold the country back. Today it's different. The euphoria also exists, but it is deserved. Brazil is viewed according to its opportunities," says American economist Thomas Trebat, director of the Latin American Studies Institute at Columbia University.

It is this promising environment that is inducing the growing dispute among large banks. In their search for grabbing those opportunities Trebat mentions, each institution is reinforcing its own



Civil construction worker: the Brazilian real estate market is still below the international average

growth strategy. "Each bank's ambition and culture are what determine the level of the dispute," says Rodolfo Spielmann, partner at the consulting firm Bain & Company. Even its main competitors recognize that Santander does not lack in aggressive instinct. In the mid 1980s, it was the sixth largest bank in Spain. After a series of acquisitions, it reached the top of the Spanish ranking, and in the world, it now occupies eighth place on the list of largest by market value. In informative material distributed to Bovespa investors, Botin's bank promises to direct 70% of captured funds, about 10 billion reais, towards expanding its network in Brazil, which includes opening 600 new agencies by 2013. If this plan is carried out that means an average of 150 units being inaugurated per year. For purposes of comparison, since the beginning of 2009, 96 agencies have been opened in the country by all of the banks. Opening an agency costs on average about 1 million reais - not counting expenses in information technology. Once open, it takes two years before it begins to cover its costs. Botin says this will all be done without reducing the current number of agencies. "There's no problem in having two on the same street, so long as both are profitable," says a Santander executive who asked not to be identified.

From the banks' perspective, the economic growth projected for Brazil highlights two great challenges: one is to explore the potential of people and companies already part of their portfolios, and the other is to reel in the enormous contingent of "bancarizables" - a neologism of doubtful taste used to describe a group comprised of 75% of the small and mid-sized companies that still do not have a strong relationship with a financial institution and the 56 million members of the middle and lower classes still without a bank account. Few countries have such a large contingent of potential clients, which makes Brazil one of the most promising markets in the world. Every day, 53,000 new accounts are opened by people and companies in the country.



Emilio Botín, world president of Santander: he became enchanted with São Paulo's traffic



Among the private banks, Bradesco is the most present at the base of the pyramid. The Bradesco agency that opens most accounts in Brazil is in Montes Claros, Minas Gerais, but it is through the Banco Postal and its correspondents that the bank is able to keep costs under control and reach the enviable mark of 16 new, low-income clients per minute. Of the 8 million accounts opened by Bradesco since the start of the decade, 5 million are active, most in the northeast and southeast regions. One belongs to Pedro José de Queiroz, 28 years of age. Queiroz is from Bocaiúva, Minas Gerais, and he moved to Sao Paulo seven months ago. He got a job as a helper on the works for the subway's Yellow Line, and he opened his first account in the beginning of October. "I only asked for the debit card. For now, I'm just going to withdraw my money," he said, adding he has already learned how to operate the ATM.

Bradesco's objective in investing in those at the base of the pyramid is not to obtain high rates of return in the short term - low profitability is a notable characteristic in this segment. "Our goal is to wed, not woo. We want to accompany the rise of those classified today as lower class, to the middle class," says Odair Rebelato, vice-president of Bradesco responsible for retail. According to data from the Getulio Vargas Foundation, for every 100 people in class D, 30 move up to class C every year. This upward movement also occurs among those already in class C: for every 100 people, five move up to class B. Bradesco and Banco do Brasil, the two most aggressive in this segment, believe that is the time to reel in that client. "Proof of social mobility is that 65% of the bank's loans are for clients who borrowed before," says Domingos Abreu, vice-president of Bradesco responsible for controllership. A survey by Data Popular Institute, at the request of the McCann Erickson agency, reveals the low-income population relates very little with banks. Less than one-third of those who have an account use it like Queiroz, the subway employee: just to receive their salary and withdraw the money.

A lesson Santander learned well in Spain is that the long-term relationship between banks and clients is closely tied to real estate credit. In March of this year, Santander signed a deal with the real estate consultant firm Sotheby's to offer financing for high standard properties. In order to expand the number of high-income clients, the bank run by Barbosa eliminated the ceiling it had for loans. Despite initiatives such as that and their accumulated experience, Santander executives know it won't be easy. There are Itaú Unibanco employees at every branch of Coelho da Fonseca, one of the largest real estate consulting firms in Sao Paulo, to provide information and close contracts. The bank has also signed an exclusivity agreement until 2027 with Lopes, the largest real estate consulting firm in Brazil, for offering loans.

Financing real estate is not an extremely advantageous operation per se. The spread - difference between what the bank pays to capture money and how much it charges in interest - is, on average, around 1% per year, much lower than for other operations, like overdraft protection, where the difference can reach 150% per year. However, for the banks, real estate loans are seen as an anchor that avoids client migration and permits cross selling other products over the long term. According to data from the consulting firm AT Kearney, one year after contracting loans, clients begin to generate an average income of 200 reais per month for banks through other products like insurance and credit cards. "The impact this has throughout a 30-year loan is enormous," says Silvana Machado, vice-president of the consulting firm AT Kearney.

It is in this extremely competitive, but opportunity-laden, environment that Botín's and Barbosa's Santander will have to grab market share from the competition. Despite the challenges, those who have recently been with Botín say the Spaniard is enchanted with Brazil. After arriving in Sao Paulo recently, Botín got stuck in one of those endless traffic jams faced by the city's residents. Rather than complain, he spent his time observing the cranes at construction sites, store fronts and new cars. Botín, revealing good humor with the executives who were with him, said all that chaos also meant prosperity - and opportunities. It was not mentioned whether he passed in from of the Grand Hyatt.

The strength of those at the top

See the weapons of Banco do Brasil, Itaú Unibanco and Bradesco, the country's top three, to take advantage of Brazil's economic expansion



Roberto Setubal
PRESIDENT OF ITAÚ UNIBANCO

The bank has one of the best groups of executives. The well-defined hierarchical model facilitates the decision process. BBA, its investment bank, is one of the most active on the market



Aldemir Bendini
PRESIDENT OF BANCO DO BRASIL

With more than 12,000 banking stations, the bank is strong in the small and mid-sized company market. Its objective is to reinforce the insurance area, which is responsible for 12% of its results. The goal is to reach 25% by 2014



Luiz Carlos Trabuco
PRESIDENT OF BRADESCO

With the greatest capillarity among private banks, it is the leader in the low-income market. It uses its agency structure well to expand the efficient insurance division