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بنك برقان
BURGAN BANK
K.P.S.C. | ش.م.ك.ع

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الكويت في: 2022/05/08
إشارتنا : 2022/277

M/s Boursa Kuwait

السادة / شركة بورصة الكويت المحترمين،،،

Dear Sirs

تحية طيبة وبعد،،

Sub: Burgan Bank K.P.S.C. Analyst Conference for the 1st Quarter 2022

الموضوع: مؤتمر المحللين لبنك برقان ش.م.ك.ع. للربع الأول من عام 2022

Reference is made to the above subject and in compliance with the provisions of clause (4) of article (8-4-2) of Boursa Rule Book; attached is the transcript of the Analyst conference that was held via phone at 12:00 pm, Wednesday, corresponding to 27/04/2022.

بالإشارة إلى الموضوع أعلاه، والتزاماً بأحكام البند (4) من المادة (8-4-2) من كتاب قواعد البورصة، مرفق لكم طيه محضر مؤتمر المحللين والذي تم عقده عبر الهاتف في تمام الساعة 12:00 ظهرا من يوم الأربعاء، الموافق 2022/04/27.

Best regards,

وتفضلوا بقبول فائق الاحترام،،،

خالد فهد الزومان
Khalid Fahad Al-Zouman
رئيس المدراء الماليين للمجموعة
Group Chief Financial Officer

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بنك برقان
BURGAN BANK

Q1'22

Earnings Conference call Q/A

Wednesday, 27th April 2022

Q1' 22 Burgan Bank Earnings Call

Wednesday, 27th April 2022

Burgan Bank Participants:

Mr. Raed Al Haqhaq	**Deputy Group CEO & CEO-Kuwait**
Mr. Khalid Al Zouman	**Group Chief Financial Officer**
Mr. Naveen Kumar Rajanala	**Group Head of Group Strategy, Capital Management and Investor Relations**

Operator (Elena Sanchez):

Good afternoon everyone and welcome to the Burgan Bank Group Q1 2022 Earnings Call. Thank you very much for taking your time to attend this conference call. Today's conference is being recorded. For today's call, we have Mr. Raed Al Haqhaq, Deputy Group CEO and CEO-Kuwait and Mr. Khalid Al Zouman, Chief Financial Officer and Mr. Naveen Rajanala, Group Head of Strategy, Capital Management and Investor relations. At this time, I would like to handover the call to Mr. Raed.

Raed Al Hahqhaq:

Thank you, Elena and good afternoon, everyone and welcome to the Burgan Bank Group Q1'22 earnings call. Thank you very much for taking the time to attend this call.

Let me start with Slide 3 which captures the key highlights of Q1'22 performance.

- Markets are normalizing post a difficult 2021.
- We have seen higher loan and deposits volumes, mainly driven by Kuwait operations.
- Margins are improving, supported by lower CoF and the recent rate hike in Kuwait; margins in Turkey are also trending positively
- Cost of Credit is lower, reflecting the improving operating environment
- Liquidity levels remain strong as reflected in our regulatory ratios

Moving on to Slide 4, highlighting performance on Revenue and Operating Expense:

- Burgan Bank Group's Revenues grew by 10% y-o-y to reach KD 53mn for Q1'22, mainly driven by growth in Net-interest income which increased by 22% y-o-y.
- Net interest margins improved by 30bps y-o-y to reach 2.1% in Q1'22, largely driven by lower Cost of Funds.

- The Group's operating expenses continue to remain stable at KD 22mn, which is within the run rate seen over the last 3 years or so
- As a result, the cost-to-income ratio improved to 42.6% in Q1'22.

Moving to slide number 5, which highlights Burgan's Operating Profit and Net Income:

- The Group's operating profit increased by 11% y-o-y to reach KD 30mn for Q1'22.
- The Group delivered a robust Net Income for Q1'22 reaching KD 12mn, increasing significantly by 140% y-o-y

I will now hand over to Mr. Khalid who will cover the next few slides.

Khalid Al Zouman:

Thank you, Mr. Raed. Slide 6 reflects the significant progress in improving asset quality and we continue to make more efforts.

- The first chart shows significant decline in provisions by 31% y-o-y to stand at KD 14mn for Q1'22.
- The bottom left chart shows the significant drop in NPL's y-o-y by 58% to KD 120mn and the strong Coverage ratio that Burgan has both at the Group level and Kuwait. Coverage ratio for the Group increased to 236% and for Kuwait, it increased to 284% in Q1'22.
- The Cost of Credit decreased both at Group level and Kuwait to stand at 1.3% and 0.7% respectively for Q1'22.
- The Group and Kuwait's NPL ratios dropped to 2.5% and 1.9% respectively.

Moving on to next slide which captures the asset details.

- The Group's total assets increased by 7% y-o-y to reach KD 7.4bn in Q1'22 with the growth driven by 9% increase in Kuwait's assets.
- The Group's loan book grew by 2% driven by 4% growth in its core market
- The Asset and loan book compositions continues to be similar to the previous quarters with no major change.

Moving on to Slide 8 on Deposits and Liquidity metrics. The key messages here are:

- Access to liquidity via customer deposits and international markets still remains solid.

- Customer deposits in Kuwait grew by 8% y-o-y to KD 3.3bn in Q1'22 with international operations maintaining stable levels of deposits with stable CASA balances of around 33% of total deposits.
- The bottom left chart shows that the Cost of Funds has reduced both at Group level and Kuwait to 2.1% and 1.0% respectively in Q1'22.
- Burgan continues to maintain strong liquidity metrics and remains well above the regulatory minimums. The Group's Liquidity coverage ratio is at 120.3% and Net stable funding ratio is reported at 107.6%

I will now hand over to Mr. Naveen who will cover the next few slides.

Naveen Rajanala:

Thank you, Mr. Khalid. Let's go to slide 9 that captures Burgan's Capital Levels:

- Firstly, I want to highlight that the forbearance measures for capital requirements are being wound down starting Q1'22
- Capital requirements have gone up by 1% across CET1, Tier 1 and CAR and you can see this on the chart with the doitted lines going up
- The Group's CET 1 Ratio increased to 11.0% for Q1'21, compared to 10.5% in Q1'21.
- CAR Ratio increased to 17.0%. All Capital metrics well above regulatory requirements.

Moving on to slide 10 which provides details of performance by entity.

Kuwait Operations:

- Kuwait had a good Quarter with consistent improvement across metrics. The Kuwait entity's contribution to the Group is consistently increasing with 78% of the Group's Assets and 70% of the Group's Net Income.

International Operations:

- The international operations metrics are stable.
- The NIMs continue to be high in these markets
- Turkey: continued reduction in balance sheet size in this market as per our strategy and hence contributes only 12% of Group's assets. Turkey has shown strong overall improvement in all its metrics.

- Algeria: Continues to be Profitable franchise with continued high margins and though there is slight deterioration in some metrics, there are no red flags.
- Tunisia: continues to be stable.

Moving to slide 11, to conclude:

- Q1'22 results signal a good start to the year with positive indicators from all franchises
- Topline growth is expected to be driven by growth in interest income on the back of expected loan growth momentum supplemented by likely rate hikes
- Credit costs are normalizing and we expect this trend to continue.

With that, I conclude the presentation and will now hand it back to Ms. Elena.

Elena Sanchez:

Thank you for the presentation. We can move now to the Q&A session. If you have a question, you can write it in the Q&A designated area, or you can also click on the raise hand option, and I will unmute your microphone. We have a few questions that came in the chat already. One of them is, what is the reason behind the strong growth in deposits during the quarter? Is this an anticipation of some long growth in the coming quarters?

Raed Al Hahqhaq:

I can cover that. Basically, there is an expectation that higher interest rates are coming, and due to the availability of liquidity at reasonable prices, we have chosen to book large amount of deposits during this time to capitalize on the future interest rate expected increases, of which we have already seen one. And we are expecting two, or three more to come.

Elena Sanchez:

Thank you, another question: Could you please provide some color on the rise in Kuwait NPLs to 1.9% from 0.7%?

Khalid Al Zouman:

It is due to one client with syndication facility. We are now establishing the condition for the restructuring, with the lead syndicate. We expect this account to be normalized soon.

Elena Sanchez:

Thank you. Another question: any update on the Bank of Baghdad disposal? And are you still looking to complete the transaction by end of June?

Naveen Rajanala:

Exactly. The target continues to be end of June. We are in the final stages now, the price has been established, and now we are in the documentation process and then we would be approaching the regulators. But, the target date still continues to be the second quarter.

Elena Sanchez:

Thank you. What is driving the current improving trends in Turkey? And do you think this is sustainable?

Naveen Rajanala:

Again, I think obviously, they've gone through difficult 2020 and 2021, but as we've said in Q3 and Q4 last year, we started to see some improvements, businesses stabilizing. Obviously, the interest rate movement and the currency devaluation aside, the franchise is focusing more on improving their efficiency, trying to build their digital platform, leveraging the digital platform to gather liquidity. They're also focused on growing non-interest income streams by building wealth management platform. They're also slowly exploring the retail portfolio, from a lending point of view. As we've said earlier, we have also communicated to the franchise, that they should be reducing the proportion of foreign currency loans and that have come down. So, all these efforts are being reflected in these metrics now.

And obviously, our expectation is this should continue and based on our budget and planning, they are going in the right track.

Elena Sanchez:

Thank you, Naveen. Another question from the chat. In which country, or sectors have you seen asset growth during Q1 2022?

Naveen Rajanala:

Largely, the growth is being driven in Kuwait. So, Kuwait, as a franchise grew and we saw some small growth in Algeria as well. As we said in the past, we are trying to ensure that Turkey's growth is minimal and that trend continues. So, as far as this particular quarter goes, the loan growth, is largely from our Kuwait operations.

Elena Sanchez:

How do you plan to boost capital buffers given that they look very thin, considering the complete removal of pandemic relaxation by early next year?

Naveen Rajanala:

Two things, one as pointed out BOB sale is expected to go through soon. So, that would add about 45 basis points of buffer. And I think this year, obviously we expect our earnings generation to start going back to normal-ish levels, or close to pre-pandemic levels. That should also help boost capital levels. Again, this is something that we monitor closely, but we don't expect growth to be impaired due to our capital levels. And we are already doing a lot of planning exercise knowing fully that the earlier required capital levels will be back from Q1'23. So, we are fully prepared from that perspective.

Elena Sanchez:

Can you please go into more details behind the sharp decline in NPLs for Turkey?

Khalid Al Zouman:

Actually, it's a combination of write-offs, plus recoveries. We have good recoveries in 2021 and that would continue in 2022. I think that's what Mr. Naveen touched in his answer about what's improving the trends in Turkey.

Elena Sanchez:

Thank you, Mr. Khalid. Few other questions. Do you have plans to re-enter the Eurodollar bond market this year?

Naveen Rajanala:

I mean, again, it'll be opportunistic. So, if there are good opportunities at the right price, we could potentially look at it. So, we have the EMTN program up and running. So, as in, when there's a good opportunity, we will look at it, but we are not hungry for funding at the moment. We are very liquid, as you can see in our ratios, but if we do tap the market, it'll be very opportunistic.

Elena Sanchez:

Thank you, Naveen. Another question related to Turkey. You already touched on loan growth, but the question is more referring to how do you plan to manage FX volatility from LIRA's depreciation?

Naveen Rajanala:

As we've been saying over the last few years, we are effectively hedged, which means that we ensure that due to any depreciation in LIRA, the impact on group capital, or group common equity of one ratio is minimal – which is typically in the range of one, or two basis points. We, as a group, have taken the position, that it's better to hedge, rather than assuming significant volatility on the capital due to fluctuation in LIRA. And, we expect to continue do this going forward also.

Elena Sanchez:

Thank you, Naveen. Another question from the chat. Can you provide us with an update on the progress of your work on the ESG front?

Naveen Rajanala:

This is something that we've made quite a bit of progress over the last 12 months, or so.

A couple of things, one is what we've done so far, the ESG reporting framework is in place. We've released the first two sustainability reports 2019, 2020. We expect that 2021 report to be out shortly. On top of this, internally we've put together a structure whereby a lot of these initiatives get visibility and are driven to ensure that the group moves towards its targets. We will be a lot more vocal about what we are doing, and communicating both activities, as well as targets to the street more from the second half of this year. We've also been engaging with rating agencies to ensure that all the work that the group does this year also is reflected in our rating and the MSCI rating. So that also should receive a boost or a pickup by the end of this year.

Elena Sanchez:

Thank you, Naveen. We'll try to take some questions now from Dmitry.

Dmitry Ivanov:

Thank you for the presentation and for updating us with recent developments. I have two questions on the capital ratios, and situation in Turkey. So, if I understand correctly, there was some decrease in ratios. Can you maybe give us some color, maybe some general breakdown what happened with the ratios? And maybe sub question here, you mentioned that the minimum requirements, for instance, for CET ratio is 9%. I just want to double check with you, if it includes all their applicable buffers? or 9% is just a global minimum?

Naveen Rajanala:

Let me start with the regulatory requirements. So basically, what happened when the pandemic started was the regulator suspended the capital conservation buffer of 2.5%. So, for us, the minimum was nine and a half. It dropped to 7%. But as a D-SIB, or Domestic systemically important bank, we had a 1% charge. So, our minimum dropped from 10.5% to 8%. Then the regulator came out with a notification mid last year, saying that the capital conservation buffer of 2.5%, which was suspended will be brought back gradually over two years. 1% will be brought back in Q1 '22, and 1.5% will be brought back in Q1 '23. So, this 9% that you see as minimum will go back to 10.5% from Q1 '23 onwards.

Second, going to your earlier question of why there's been a drop in CET1 from Q4 to Q1, it's largely two reasons. One is obviously there's a slight increase in balance sheet, given that the regulator does not allow interim profits to be included in the capital. There is a natural dip in capital when there is growth. Secondly, the depreciation of LIRA largely has caused some capital to drop through the OCI movement

Dmitry Ivanov:

Understood. So just maybe to clarify this drop in LIRA, because you mentioned that you tried to hedge it. If I understand correctly, LIRA depreciated by approximately 7% to 10%, end of Q4 to end of Q1. Do you have any kind of maybe some framework for us on how to approach this? For instance, if we see additional 10% LIRA depreciation, how will it impact CET ratios of Burgan's global Banks? Is it possible just to give us some guidance on this? Because I think expectations that LIRA might continue to depreciate.

Naveen Rajanala:

So, at the end of the day, we also have to keep in mind that hedging LIRA is an expensive affair. We continue to hedge, so what happens is if there is a devaluation, which is lower than expected, or at cost, then it'll still show as a reduction through OCI. So, in quarters where you see a massive devaluation, that's when the hedging benefit kicks in, because even though it costs us, we also get the hedge gain. So irrespective of that, there is an amount of cost that the bank incurs through its OCI when we hedge this exposure.

Dmitry Ivanov:

CET requirements as you've mentioned are 9% from Q1'22 and 10.5% from Q1'23, so including all buffers, right?

Naveen Rajanala:

Yes.

Dmitry Ivanov:

And in terms of the capital ratios in Turkey, are they well above minimum requirements? Can you give us any kind of color on the capital ratios in Turkey?

Naveen Rajanala:

Turkey also is under Basal III but obviously BRSA requirements are different there. There, the minimum requirement is 7%, and they are operating around 100-125 basis points over that. And that's, again, a design by choice. So, the total capital requirement is 12%, and their CAR is about 18%. So as of now, we do not see the need for recapitalizing, but in the past whenever there was any requirement, we've always been supportive of the franchise. And even now if they do need some capital for regulatory requirements, we were there to support the franchise.

Dmitry Ivanov:

Thank you very much.

Naveen Rajanala:

Thank you.

Elena Sanchez:

Couple of questions from the chat. Any update on the mortgage law? Do you expect it will be passed this year?

Khalid Al Zouman:

We believe that the banks will benefit from the mortgage law if it's passed, but still it is unclear at the moment on any progress on this subject and seems as it's not a priority in the parliamentary agenda at the moment.

Elena Sanchez:

Thank you, Mr. Khalid. Another question, what is the reason for the top line or revenue decline, quarter on quarter?

Naveen Rajanala:

So, it's largely driven by drop in the non-interest income, which was due to decline in investment income. As we know that the equity markets and the fixed income markets are struggling, especially in the first quarter. So that's being reflected in the drop in non-interest income.

Elena Sanchez:

Thank you, Naveen. Given that Bank of Baghdad sale has faced challenges in the past, what are the other options into consideration to boost capital buffers, considering that earnings alone may not be fully sufficient?

Naveen Rajanala:

I think the challenge to BOB sale earlier was when we went to almost the end of the transaction, Central Bank of Iraq was not comfortable with those specific buyers. But then when they said that, they also told us what are the kind of buyers they would be comfortable with. So, like they said, they have to be a financial institution, ideally well capitalized, etc. So, we've taken all that into account. And this time, we have been only dealing with financial institutions. As I said in the past, there are a number of institutions that are interested in buying this franchise. But we've taken a conversation with this particular financial institution to this stage. And we are quite confident, given the background of that institution, we're quite confident of a regulatory approval. We do not foresee any risk, but obviously we can never say that with 100% certainty. But our expectation is regulatory approval will not be a challenge once we've shaken hands with them on the price, which is almost at the last stage now.

Elena Sanchez:

Thank you, Naveen. A few questions are just coming through - The sensitivity of interest margin to changes in interest rates?

Khalid Al Zouman:

It's definitely a positive effect. Each time we have interest hikes, definitely our revenues will improve and our bottom line will improve accordingly.

Naveen Rajanala:

And just to add to what Mr. Khalid said, every 25 basis points, as we said in the past, gives us a top line boost of about 4 to 4.5 million KD.

Elena Sanchez:

Thank you, Naveen. And just a related question to that, I believe that after the recent rate hike by the CBK, the discount rate was raised. But in terms of repo rates that are used for the pricing of deposits, the increase was not linear across all maturities. Since it was a bit higher for longer tenures than shorter tenures, do you expect that to drive any pressure on funding costs?

Naveen Rajanala:

No. Obviously, the deposit rates would go up, but again, there is a time lag and obviously the balances also provide us with some buffer to ensure that the increased cost is not passed on to us. And then as we've said in the past, we've proactively diversified our funding profile, where we have the EMTN funding, the club loan funding, etc. so it offsets some of the risks. So as of now, we've not seen that there's an impact on our interest rate margin due to the repo rate being higher.

Elena Sanchez:

Okay. Thank you. Last question that I can see if you can give any insights or an explanation on stage two loans,

Naveen Kumar:

So, as we've covered this many time in the past now, the stage two that we look at is firstly for the group and all these stage two loans are recast as per CBK guidelines, which as we've said in the past, is relatively a bit strict. So hence that perspective needs to be kept. And for some franchises that number is high, but it does not mean that these are due to any stress in the portfolio. An example is rating movement, so if there is a one notch downward movement, we have to move from stage one to stage two, which is a bit stricter than standard global guidelines. Secondly, any positive movement from stage three to two or two to one requires a curing period of one year and CBK's approval.

Elena Sanchez:

Thank you. I see no further questions. I'll just hand it over to you for any closing remarks.

Raed Al Haqhaq:

Thank you, Elena, and thank you everybody for joining us, looking forward to the next investor call in the second quarter. If you have any queries or you would like to know more information, we are always available through emails and calls.

Elena Sanchez:

Thank you. This concludes the call. Thanks.