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هاتف: ٨٠٠٠ ٢٢٩٨ ٩٦٥+
فاكس: ٨٤١٩ ٢٢٩٨ ٩٦٥+
رأس المال المصرح به ٤٠٠,٠٠٠,٠٠٠ د.ك
رأس المال المصدر والمدفوع ٣٢٨,٧٨١,٢٥٠ د.ك
سجل تجاري رقم ٢٤٠٦٧

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

Date: 14/05/2023
Ref: 349/2023

الكويت في: 2023/05/14
إشارتنا: 2023/349

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 2023

الموضوع: مؤتمر المحللين لبنك برقان ش.م.ك.ع. للربع الأول من عام 2023

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 02:00 pm, Wednesday, corresponding to 10/05/2023.

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 02:00 ظهرا من يوم الأربعاء، الموافق 2023/05/10.

وتفضلوا بقبول فائق الاحترام،،،

Best regards,

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

بنك برقان
011
Burgan Bank

BB/005-08/2022

Q1'23
Earnings Conference call Transcript
Wednesday, 10th May 2023

Q1' 23 Burgan Bank Earnings Call

Wednesday,10th May 2023

Transcript of Burgan Bank Earnings conference call on Wednesday 10th May 2023 at 14:00 Kuwait time (UTC+03:00)

<u>**Burgan Bank Participants:**</u>

Mr. Khalid Al Zouman	**Group Chief Financial Officer**
Mr. Naveen Kumar Rajanala	**Group Head of Strategy, Capital Management and Investor Relations**
Mr. Hamad Al Bader	**Manager – Group Strategy, Capital Management and Investor Relations**

Operator (Elena Sanchez):

Good afternoon everyone and welcome to the Burgan Bank Group Q1 2023 Earnings Call. Thank you very much for taking your time to attend this conference call. Today's conference is being recorded. With that, I would like to hand over to Mr. Hamad Al Bader from Burgan Bank to kick off the call.

Hamad Al Bader:

Thank you, Elena. Good afternoon everyone and welcome to the Burgan Bank Group Q1'23 earnings call. Thank you very much for taking the time to attend this call. Joining this call from Burgan are Mr. Khalid Al Zouman, Group Chief Financial Officer and Mr. Naveen Rajanala, Group Head of Strategy, Capital Management and Investor Relations and myself, Hamad Al Bader, Manager-Investor Relations. We shall cover the slides over the next 20 minutes and would welcome your questions at the end once the presentation has been covered. With that, let me hand over to Naveen to start the presentation with slide 8.

Naveen Rajanala:

Good Afternoon everyone and thank you for your time. Let me kick off the presentation with the key business updates.

1st Topic: Bank of Baghdad Sale

We have been talking about this over the last couple of years. We have now concluded the transaction. As discussed in the past, the transaction has boosted capital ratios by 70 bps for the bank, largely due to the release of RWAs of KD 342 mn.

Moving on to the 2nd topic: **BBT's performance**

We embarked on a "risk containment, restricted growth" strategy for our Turkish franchise since 2019 and this has now started paying off.

BBT has focused on a few strategic initiatives:

- Building a strong digital platform & leveraging it for "client acquisition" & "growing business from retail clients".
- Growing "non-asset-based business" away from "asset growth- led strategy".
- Improving asset quality by proactively engaging in restructuring &/ or recoveries.
- Lastly, implementing strong cost control measures across businesses.

Having done these, the results so far have been extremely encouraging:

- Its digital platform "ON" has been received very well in Turkey with strong user numbers & product take up, as highlighted in the slide.
- It also went on to win the prestigious "Best Digital Banking Platform" award by Global Finance.
- Significant growth in non-interest income levels.
- Cost to income ratio has been below 40% over the last 9-12 months.
- Most importantly, asset quality metrics have shown tremendous improvement with almost 80% decline in NPL stock from its peak.

Moving on to the 3rd topic **"ESG"**

- We have been focusing on progressing ESG priorities over the last 18 months.
- The reflection of these efforts can be seen in the improvement in MSCI ESG rating to "BB".

We are now progressing additional work streams with a view to further improve the MSCI ESG rating & deliver on our "sustainability" agenda.

Our 2022 sustainability report is out, please check our website when you get a chance.

With that, I will hand over to our Group CFO, Mr. Khalid to cover the key slides in the "financial review section".

Khalid Al Zouman:

Thank you, Naveen and good afternoon, to everyone. Let's move to slide 10;

- Before going through these details, I want to highlight that in 2021 and 2022 BoB's numbers were included in our P&L given that it was held in our books. Hence we have carved out BoB's numbers in "light blue color" to give a better understanding of the underlying numbers and make them comparable to Q1'23 figures.
- The Group's revenues increased to KD 55mn, driven by an increase in net interest income of 8% q-o-q.
- The Group's Operating Profit for Q1'23 is at KD 26mn; which is more or less flat compared to underlying Operating profit in Q1'22.
- The Group's Net Income fell to KD 7.6mn in Q1'23, which is largely due to IAS 29 impact of KD 6.5mn & we will cover the various moving parts affecting Q1'23 Net Income in detail in the next slide.
- Net Interest Margin remained stable at 2.1%, supported by improving margins in Kuwait.
- The Cost to Income Ratio increased to 52.9% for the Group, primarily due to increase in people costs in Turkey & Kuwait.
- Cost of credit continued to improve, down by 90bps at 0.40%.

Let's go to slide 11. I want to spend a little time on this slide to highlight some of the key drivers impacting Q1'23 Net Income. Our starting point is KD 11.4mn of underlying Net Income (excluding BoB) for Q1'22.

If we look at the key drivers that improved performance in Q1'23, they are primarily:

- Increase in Net Interest Income by KD 2.5mn.
- Reduction in cost of risk by KD 9.6mn.

But, these positive drivers have been offset to some extent by:

- Opex increase of 6.6 mn.

This brings us to the true underlying Net Income KD 14.1 mn. But if we add KD 3.4 mn of higher taxation (due to bigger contribution from BBT), the true underlying net Income levels are KD 17mn.

Unfortunately, IAS 29 impact of KD 6.5mn brings down the net income for Q1'23. Otherwise our bottom line performance for the quarter is quite decent.

Moving to slide 12, which reflects the Group's Asset Quality metrics:

- The Group's NPLs for Q1'23 decreased significantly over the past two years from a high of KD 284mn in Q1'21 down to KD 84mn this quarter. BBT is a big reason for this improvement.
- The Group's NPL ratio significantly reduced by 420bps over the past two years to 1.8% in Q1'23.
- The Provision charges have improved considerably down to KD 4mn for Q1'23.
- The Provision coverage ratio for the Group continues its upward trend with Q1'23 Provision coverage ratio of 219.3%.

Moving on to slide 13, the key messages on this slide are as follows:

- Firstly, the Group's underlying assets grew from KD 7.1 bn to KD 7.2 bn.
- The Group's loans continue to be well diversified & there is no major movement in the sector concentration.
- The bottom left chart shows the percentage of liquid assets in our balance sheet. As you can see. We hold healthy levels of liquid assets in our books.
- Lastly, the stage 2/stage 3 proportion continues to improve. As highlighted in the past, the staging criteria is as per CBK IFRS 9 guidelines which are quite stringent.

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

Naveen Rajanala:

Thank you, Mr. Khalid.

Moving on to slide 14, the key messages on liquidity are as follows:

- Our deposit levels are stables; we are obviously managing deposit volumes in line with planned asset growth & hence the decline.
- Also, we are continuing to proactively replace & reduce expensive deposits with other liquidity sources.
- Lastly, all the regulatory ratio requirements for liquidity are back to pre-pandemic levels from Q1'23 onwards.

- We continue to be well within the prescribed maximum Loan to Deposit ratio of 90%.
- Our Liquidity ratios, NFSR & LCR are also well above minimums.
- Our CASA balances continue to be at healthy levels. The CASA balances grew to 37% of total deposits.

Moving on to slide 15.

The key messages here are:

- Regulatory minimum levels for Capital Ratios have been reinstated back to pre-pandemic levels from this quarter onwards.
- Burgan's CET1 Ratio & CAR Ratio have improved largely due to the positive impact of sale of Bank of Baghdad. (as explained earlier in the presentation)

Moving on to slide 16, which provides details of performance by entity:

1. Kuwait
    - NIMs improved on the back of CBK discount rate hikes, especially in Q4'22 and the previous one in early Jan '22.
    - But NIMs will stabilize at this level with very limited upside if at all.
    - NPL ratio continues to be very low in Kuwait.
    - Cost of risk went up primarily due to a legacy account.

2. Turkey
    - We have already highlighted Turkey's all-round improvement & these KPIs reflect the same.

3. Algeria & Tunisia
    - KPI's across the 2 franchises are trending in the right direction.
    - Both remain solid and profitable.

With that, I will hand it back to Mr. Khalid to summarize and conclude the presentation.

Khalid Al Zouman:

Thanks Naveen.

So, in summary:

- Q1'23 was a good quarter if we look at underlying performance.
- Asset Quality continues to be stable & strong.
- International operations, especially Turkey, starting to contribute well to the Group's financial performance.

With that I will conclude our presentation and will hand it back to Ms. Elena to coordinate the Q&A session.

Elena Sanchez:
Thank you very much for the presentation. We'll move now to the Q&A session. If you have a question, you can either write it in the Q&A area and I will read it from there, or you can also click on the raise hand button or icon, and I will unmute your microphone. There are a few questions that have come already through the Q&A chart, so I will start reading some of them. Question on NIMs, could you talk a bit about the drivers behind the NIM decline on a quarter-on-quarter basis during Q1 2023?

Naveen Rajanala:
Primarily, in Q1 23, compared to previous quarter is because we had a very strong NIM in Turkey in Q4 22. But this year, Turkey's NIMs are a bit under pressure, given the recent monetary policy being adopted over the last couple of months. But if you look at Kuwait, the trend that we saw in the past in terms of the high increase in cost of funding is now slowing down and becoming more stable, etc. So, that's why we've seen quarter on quarter the Kuwait's NIMs improving, but the Group's NIM's are obviously impacted a little bit, by the Turkey NIM contraction.

Elena Sanchez:
Were funding costs affected by normalization of liquidity, regulatory liquidity ratios at the beginning of the year in Kuwait?

Naveen Rajanala:
So, though the forbearance measures were lifted from Q1 23 across the banking sector, every bank was well above the normal liquidity ratios. So, I don't think the move to a normal regulatory/liquidity metrics has impacted this. It is the usual cost of funding that went up quite

steeply in Q2 and Q3, and then started normalizing in Q4 and we are seeing that normalizing trend continuing.

Elena Sanchez:
How do you see the NIM outlook in Kuwait and Turkey for the rest of 2023?

Khalid Al-Zouman:
when we did our budget for the year 2023 we initially expected the cost of fund to rise, but we think now it's been normalized, and even recently, the Central Bank of Kuwait did not follow the Fed in regards to increasing rates and I don't think also CBK is asking to bid higher deposit prices for KDs. So, at this moment we don't expect anything to worsen.

As mentioned by my colleague Naveen, that Turkey is not making the same margins as they have been doing in the past couple of quarters and we expect it will not deteriorate. As everybody knows, we are waiting for the election results and we don't know what might happen after the elections. We are in close contact with the management in BBT and we are taking all the measures in terms of liquidity and other ratios.

Elena Sanchez:
A question on cost of risk. The presentation shows that there was no provisioning charge for Turkey in Q1 2023. What is the reason behind that, and can we take the Q1 cost of risk as the run rate for the full year?

Khalid Al-Zouman:
There was improvement in Q1 in some of the collaterals and that's why there were some write back of provisions. We hope that this continues and as I said, let's see what's going to happen after the elections in Turkey. So far, things are stable and the bank is progressing.

Elena Sanchez:
Question on loan growth, loan growth was soft for Q1 for the bank, as well as for the sector. How do you see the political environment as well as the interest rate environment impacting loan growth, and what is the outlook for the rest of the year? And also, specifically on corporate loan growth, what were the drivers of that loan growth during Q1? Was it driven by project awards?

Naveen Rajanala:
So, I think in terms of loan growth, the rate hikes have impacted credit demand in Kuwait. We've seen early trends in our retail loan growth, and the entire market has slumped a bit in terms of credit demand. But, as we've said in the past calls, retail transformation and growth remain our key focus area in Kuwait, our retail franchise is one of the few banks in Kuwait that has grown its portfolio in the first quarter. Obviously, retail still remains a smaller portion of Kuwait's pie, and they will continue to become larger as we go along, but we expect our retail franchise to grow close to double digits this year in spite of the credit contraction. Most of the corporate growth is obviously focused on government contracts.

Khalid Al-Zouman:
Furthermore, if you have a look at the government reports comparing Q1 of last year to Q1 2023, the Government's spending increased and we expect more contracts to be awarded. In terms of our budget and what we see, we are budgeting for a single digit growth in Burgan Bank Kuwait.

Elena Sanchez:
So single-digit loan growth for corporate only, or for Kuwait loan growth, total loan growth in Kuwait?

Naveen Rajanala:
Yes, for Kuwait. As we indicated, it would be around the 5 to 6% loan growth this year.

Elena Sanchez:
Question on OPEX, if you could elaborate on the drivers of the 30% year-on-year increase in OPEX despite muted volumes?

Khalid Al-Zouman:
Our Retail focus and transformation in terms of building market share in Kuwait requires increase spending mainly in staff costs, plus we are spending on our digital solutions along with some marketing initiatives being done in Kuwait. Additionally, in Turkey with the current inflation levels, we had an increase in staff costs also.

Elena Sanchez:
Thanks for that. And a related question, if you could provide guidance on cost-to-income ratio for 2023?

Khalid Al-Zouman:
Well, I think it will be more or less the same. But If you compare it to 2022, I expect a slight increase in cost to income ratio for 2023 year over year.

Elena Sanchez:
There are lots of questions on cost-of-risk guidance for 2023. I know that you have commented on this earlier and there is some uncertainty in Turkey, depending on what happens with the elections, etc., but I don't know if you could provide some broad indication for the group for 2023?

Naveen Rajanala:
In the past, we've said that there are a couple of things. In our planning and budgeting exercise, we typically budget for about 60 to 80 basis points of credit cost. So, the two things that could change that are any volatility post the Tukey elections and any deterioration in the credit environment there. The other thing is if there are any precautionary provisions that are added. But directionally we plan for about 60 to 80 basis points and might better it.

Elena Sanchez:

Thank you, that's very helpful. Questions on your retail strategy for Kuwait, which you spoke about in Q4, and your stronger focus now on retail in Kuwait. Does the plan include organic growth only, or is the bank also open to exploring inorganic growth plans, as well, in retail?

Naveen Rajanala:
As of now, as we've said in the past, obviously retail is a franchise that we started looking at since beginning of 2021. Early indicators both from 2021 and 2022 have been positive, and we've grown organically, we've grown market share, as well. Obviously, it's a long road ahead, it's early days, but our focus at the moment is completely on organic growth. There is nothing inorganic in terms of opportunity at the moment on the table.

Elena Sanchez:
Okay, thank you for that. A few questions raised on Capital adequacy ratio. Most of them are asking if you could provide more guidance on your internal capital ratio targets, and the outlook for this year, and also in the next few years.

Naveen Rajanala:
In the past, we've maintained that at a CET 1 level we always aim to have at least a buffer of about 100 basis points over CET 1, so at about 11.5% area. Obviously, during the year, intra-year, it takes a little bit of a dip due to non-inclusion of interim profit. But, having said that, one of the key things here is, when we look at IAS 29, we typically focus on the impact on P&L, but then IAS 29 also impacts equity positively. So, every time the P&L takes a hit, there's a positive impact on capital, as well. So, if we truly look at IAS 29 impact in its entirety, it still is shareholder value positive if you take the impact from Q2 22. So, that should help negate some of the net income impacts it's been having.

But, in terms of guidance, we should look at 11.5% levels. We're obviously working on some solutions on RWA optimization in the background as we've been working over the last few years. But as of now, I think we should plan for about 11.5% levels at CET 1 level. At a total capital level, between 17 and 18%.

Elena Sanchez:
Following the Credit Suisse AT1 event earlier this year, how are you thinking about your AT1 notes being called on the first call date?

Naveen Rajanala:
It's early days. Our AT1 call date is around July 24. So, we are good 13 to 14 months away. As I said, this is something that we need to discuss internally in terms of the next steps and strategy in terms of liability management, or whatever the route is and then go to the regulator. I think the right time to talk about this would be maybe in Q3 earnings call or Q4 earnings call. At the moment, we understand there's a lot of weakness in the market, a lot of volatility and nervousness around AT1. So, again, the hope is that the AT1 market starts normalizing in six months' time.

Elena Sanchez:

Thank you, Naveen. Question on Algeria, why did the NIM in Algeria fall by 160 basis points year-on-year?

Naveen Rajanala:
Well, if we look at Algeria's NIMs historically it's always hovered around the 6% mark. Last year, at the beginning, they were clocking at 7% due to some transactions and hence Q1 over Q1 is showing a massive dip. But if you look at normalized annual margins, they're usually around the 6.0% to 6.2% mark, so it's a major decline.

Elena Sanchez:
Questions also on hyper-inflation accounting from Turkey, how should we think about that number for full year 2023?

Khalid Al-Zouman:
We expect that it will be less and that's how we budgeted and that's how we see it. But again, let's see what's going to happen in the upcoming election and how will it impact on the currency. But as a forecast and upon talking to our counterparts there, we expect a lower impact this year.

Elena Sanchez:
Thank you. Question on stage 2 assets, a bit generic, but if you could give any color on your stage 2 loans or assets.

Naveen Rajanala:
As a trend, I think if you look at it, it sort of peaked in 2020 Q4 and then in early Q1 21, but since then it's been stable around the 14% mark.

Elena Sanchez:
A few questions on related party lending with KIPCO, are you considering reducing that? And if you could comment on the staging of related party loans.

Khalid Al-Zouman:
we are having some exercise through our board of directors to reduce RPTs, related-party transaction and you will see this reflected in the coming period. As you rightly said, KIPCO is a big company with diversified operations, but it looks like going forward they are restructuring even their holdings.

Naveen Rajanala:
Just to add, in terms of staging, they are all stage 1 barring one exposure, but that was because as per the guidelines when there was a rating decline. But in terms of the performance of the borrower, it's a regular account, and obviously we can't move it from stage 2 to stage 1 unless there's a passing of a curing period and approval from regulator. But performance-wise, the portfolio is performing well.

Elena Sanchez:

A question on interest rates, what is your house view on interest rates, policy rates in Kuwait going forward?

Naveen Rajanala:
I think as far as the CBK discount rate goes, our view is that it probably reached its peak, maybe 25 basis points, but that's an outlying scenario. We probably think 4% is the max for CBK. As far as dollar discount rate goes there may be another rate hike but we are again very close to the peak We potentially expect the rates to come off from Q4 onwards on the dollar side and then CBK would follow suit if such rate cut action happens from the Fed.

Elena Sanchez:
And the last question I see here in the chat, what is the contribution to group revenue from the franchises? I suppose it means international subsidiaries.

Naveen Rajanala:
So, if I look at Kuwait's contribution, it's about 27 million KD, so roughly at a top-line level between Kuwait and international it's 50/50.

Elena Sanchez:
Thank you, Naveen. I don't see any further questions. I will hand the call over to you for any closing remarks, please.

Hamad Al Bader:
Thank you, everyone, for joining us. Please feel free to reach out and send an email for any further queries. Thank you very much.