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رأس المال المصرح به ٤٠٠,٠٠٠,٠٠٠ د.ك
رأس المال المصدر والمدفوع ٣٤٥,٢٢٠,٣١٢ د.ك
سجل تجاري رقم ٢٤٠٦٧

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

Date: 06/08/2023
Ref: 532/2023

الكويت في: 2023/08/06
إشارتنا : 2023/ 532

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 first half of 2023

الموضوع: مؤتمر المحللين لبنك برقان ش.م.ك.ع. للنصف 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 02/08/2023.

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 2023/08/02.

Best regards,

وتفضلوا بقبول فائق الاحترام،،،

خالد فهد الزومان
Khalid Fahad Al-Zouman
رئيس الجهاز التنفيذي للمجموعة بالوكالة
Acting Group Chief Executive Officer

بنك برقان
Burgan Bank

BB/005-06/2023

بنك برقان
BURGAN BANK

H1'23
Earnings Conference call Transcript
Wednesday, 2nd August 2023

H1' 23 Burgan Bank Earnings Call

Wednesday, 2nd August 2023

Transcript of Burgan Bank Earnings conference call on Wednesday 2nd August 2023 at 14:00 Kuwait time (UTC+03:00)

Burgan Bank Participants:

Mr. Khalid Al Zouman	**Chief Financial Officer**
Mr. Naveen Kumar Rajanala	**Deputy General Manager – Finance Group**
Mr. Hamad Al Bader	**Manager – Investor Relations**

Operator (Ahmed El-Shazly):

Good afternoon everyone and welcome to the Burgan Bank Group H1 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, Ahmed. Good afternoon everyone and welcome to the Burgan Bank Group H1'23 earnings call. Thank you very much for taking the time to attend this call. Joining this call from Burgan are Mr. Khalid Al Zouman, Chief Financial Officer and Mr. Naveen Rajanala, Deputy General Manager – Finance Group and myself, Hamad Al Bader, Manager-Investor Relations. We shall cover the slides over the next 20 minutes or so 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 updates on the Digital front:

a) **Burgan Bank Kuwait**

- BBK's continuous digital investments and enhancements are still yielding with great results with around 90,000 of total customers onboarded digitally.
- Digital activities increased by around 50% in H1'23 vs H1'22, with around 94% of transactions being executed via mobile app.
- We are also seeing the business volumes pickup through digital channels rather than mere transactional volumes.
- We have seen higher CASA volumes; more than 1.1K accounts opened via Digital Channels in the first 6 months of '23.

- Burgan's app continues to be rated highly on both IOS and Android platform; well rated at 4.6 and is consistently amongst the top 2 banks in Kuwait.

b) Burgan Bank Turkey

We have talked about BBT's digital platform over the last few quarters:

- BBT's award winning platform "ON" continues to outperform and gain traction, with around 157,000 clients onboarded during H1'23.
- Deposit volumes for Q2'23 at TRY 6.3bn, 4% increase q-o-q.
- Loan volumes for Q2'23 at TRY 3.3bn, 30% increase q-o-q.
- Some exciting new features such as FX & overdraft have been added to the platform, these features will drive new revenue streams for the bank.

This was a quick summary of the progress we have made on the Digital front.

With that, I will hand over to our 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 as it was classified as an "Asset Held for Sale". Hence, we have carved out BoB's numbers in "light blue color" to give a better understanding of the underlying numbers and provide an accurate comparison of H1'23 financials with prior period figures. Accordingly, for comparisons with prior year, we would be referring to BoB adjusted numbers throughout this presentation.
- The Group's revenues increased by 8% y-o-y to KD 108mn, driven by strong Non-Interest Income of KD 47 million (up 28% y-o-y) and Net-Interest Income of KD 61 million.
- The Group's Operating Profit for H1'23 was at KD 54mn; in line with levels seen last year.
- The Group's Net Income stood at KD 18mn in H1'23. Group's bottom-line results were impacted primarily due to IAS 29 impact, higher expenses and proactive provisioning. Adjusted for these factors, our normalized profits are in the KD 28mn to KD 30mn levels.
- In terms of KPIs, Net Interest Margin remained stable at 1.9% despite low interest rates situation in Turkey during H1'23.

- The Cost to Income Ratio is higher for the Group in H1'23, largely attributable to higher staff expenses mainly in Kuwait and Turkey. We are focused on optimizing expenses over the coming period.
- The Credit Costs were slightly higher in H1'23 at 90bps primarily due to proactive provisioning by the bank on certain exposures.

Moving to slide 11, which reflects the Group's Asset Quality metrics:

- The Group's NPLs for H1'23 decreased significantly over the past two years from a high of KD 214mn in H1'21 down to KD 91mn in H1'23. BBT is a big reason for this improvement.
- The Group's NPL ratio reduced by 250bps over the past two years and is stable at 2.0% over the past few quarters.
- As discussed earlier, Provision charge is higher in H1'23 due to proactive provisioning.
- The Provision coverage ratio for the Group continued its upward trajectory with H1'23 Provision coverage ratio standing strong at 200%+.

Moving on to slide 12, the key messages on this slide are as follows:

- Group's assets grew y-o-y to KD 7.1 bn in H1'23 The Group's loans were at KD 4bn for H1'23 and continue to be well diversified. Also, importantly, there was no major movement in the sector concentration Y-o-Y or Q-o-Q.
- We continue to hold healthy levels of liquid assets in our books as reflected in the bottom chart. Liquid assets to total assets ratio stood at 25% for H1'23.
- 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 and are quite conservative.

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

Naveen Rajanala:

Thank you, Mr. Khalid.
Moving on to slide 13, the key messages on liquidity are as follows:

- Our deposit levels have increased by 5% y-o-y to reach KD 4.3bn and remains well-diversified
- We continue to be well within the prescribed maximum Loan to Deposit ratio of 90%.
- Our Liquidity ratios, NFSR & LCR are also well above regulatory minimums.
- Our CASA balances continue to be at healthy levels. The CASA balances are around 32% of total deposits.

Moving on to slide 14.

- Burgan's CET1 Ratio & CAR Ratio continue to trend positively and are higher than the past two years. Our CET1 Ratio is at 11.5% and CAR Ratio at 17.8%, both well above regulatory requirements. The reduction in RWAs during H1'23 is largely attributable to the sale of BoB in Feb'23

Moving on to slide 15, which provides details of performance by entity:

1. Kuwait
    - Slightly difficult first half for Kuwait:
        - Largely due to higher expenses and Credit Costs.
        - But NIMs are stable and expected to be at the same levels, while NPL ratio continues to improve.
2. Turkey
    - Turkish business continues its outperformance. The interest rate situation for local currency in Turkey had a bearing on the bank's NIMs. However, the bank has demonstrated strong improvement across other KPIs such as cross sell, efficiency & asset quality. The Bank continues to generate strong returns for the Group.
3. Algeria & Tunisia
    - Both of these franchises 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.

In summary:

- Group's Asset quality, Capital position & Liquidity levels continues to be healthy.
- Going forward, we anticipate that the Kuwait performance would improve especially in light of the recent rate hike in Kuwait.

- Also, the actions from the Turkish Central Bank & other agencies post-election who are committed in ensuring further stability in Turkey are expected to contribute positively to Turkey's performance.

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

Ahmed El-Shazly:
Thank you, gentlemen, for the presentation. We will now open the floor for your questions, so if you'd like to ask a question you can either type it in the question box on your screen, or you can click on the Raise Hand button and I will unmute your microphone. We already received a few questions, so we'll start with reading the first one. Are you planning to call the AT1 bond next July? And if so, how can you replace it given Burgan's relatively weak Tier 1 ratio?

Khalid Zouman:
It is too early to decide. Still, we have another year but there are discussions within management, and I think maybe in the coming quarters we'll make up our mind.

Naveen Rajanala:
As Mr. Khalid stated, Basically it's a little too early. As per Basel III guidelines, we cannot communicate something that creates expectations around these instruments, but once the decision is made at the bank, and post-discussion with the regulators, we will communicate. But as you can see from our capital structure, the bank needs the Tier 1 instrument. But beyond that, it's too early to comment on this.

Ahmed El-Shazly:
All right, thank you. Another question. At what interest rate did Burgan raise their $800 million syndicated facility from regional and international banks in late April?

Naveen Rajanala:
All in, the pricing was SOFR plus 120 basis points.

Ahmed El-Shazly:
Okay, thank you. A few other questions. Can you please share some color on the drivers of the decline in Stage 2? Is it because of the BoB sale or other factors?

Naveen Rajanala:
The decline in Stage 2, it's not due to BoB but it's been a continuous improvement since the pandemic, the receding of the impact of the pandemic. Also, in Kuwait, there's a little bit of a time lag with Stage 2/ stage 3 reclassification improvements, because these exposures have to go through a curing period and central bank approval before reclassification. But the drivers are also the improvement in our portfolio.

Ahmed El-Shazly:

Thank you. Another question. Can you please share your strategy or approach to boosting CET1 buffers, and what is your target? Is it 150 basis points or less?

Khalid Zouman:
We always wanted to have 100 basis points above the regulatory requirement. We have been successful in the past in doing some optimization measures and actions, so that's our target.

Ahmed El-Shazly:
Can you comment on how the related-party exposure changed, Q-o-Q?

Naveen Rajanala:
At a total level, as we've communicated earlier, quarter-on-quarter, there would be some minor movements, but I think as we communicated earlier, there is a broad overall plan where over time we expect related-party exposure to come down. I don't think we should read too much into quarter-on-quarter movement. But definitely there's a plan whereby year on year you would start seeing some tangible reduction in these exposures.

Ahmed El-Shazly:
Thank you. I see we have a few raised hands. We'll take the first question from Rakesh Tripathi. Please go ahead.

Rakesh Tripathi:
I had a few questions, so I'll start one by one. My first question was around your loan growth basically in H1. The contraction that we've seen, I understand that Kuwait has seen little credit growth overall in the first half of the year, but we've seen most banks doing a lot better in the corporate segment, It's the retail where growth has been muted and still you've had on average about 1.5% kind of Credit growth for the sector as a whole. So, what is driving the contraction at Burgan and what do you expect basically going forward?

Khalid Zouman:
Overall there is a growth in Kuwait. However, as you mentioned, the contraction is coming from Turkey, and as for Turkey the devaluation of the currency is something out of the hand. secondly, recently we saw that there are some negative spreads in the TRY loans. So, we opted to close certain loans. So, the combination of closing some loans and the devaluation, but there was growth in Kuwait.

Rakesh Tripathi:
I believe up until sometime last year you used to provide the breakdown of what used to be the loans and deposits and international overall. If you start disclosing that information again, it'll be helpful for us to see what the domestic business is doing compared to how the rest of the business is doing.

Naveen Rajanala:
sure, noted. I think we can look at start disclosing those specifics.

Rakesh Tripathi:
My second question was around the increase in Kuwait NPL ratio. So, just Kuwait, overall, it was 10bps increase in NPL ratio from year end to end of H1. So, not significant, but just talking about Kuwait, the NPL ratio increased about 50 bps, from close to 1.5% to now 1.9% and this is something that we've been noticing for the last couple of years, two to three years in fact, that every year Q1, Q2 we see spike and then it levels out either by end of the year or the first quarter of the next year. So, what's driving this increase? Why the deterioration in Kuwait? Is it just one account? I know that's been the case in the past couple of years that it's been one or two, a handful of corporate accounts that have deteriorated. But this is sort of a consistent thing that's happening every year, so I just wanted to understand what's happened here.

Khalid Zouman:
As you rightly said, it's not a significant amount, it is one customer. The business unit decided to classify this customer, but to clarify that this customer is paying his interest. He has some collateral, but the decision was based after the management of the bank had asked the customer to fulfill certain actions and basically the customer didn't fulfill, so the business unit under the management's approval decided to be hard on this customer. This customer is fully collateralized.

Rakesh Tripathi:
I understand this is a trend across Kuwait, across the rest of GCC as well. In fact, most places right now because of the high interest rates that there's a migration from CASA to Time Deposits. I believe in your case there has been sizeable deposit growth and CASA ratio at the same time has come down to 32% now, from close to 36% I believe from end of the year. So, the growth predominantly is being driven by time deposits. With that happening as it is, how do you plan to manage NIMs, manage your overall ROE. Also, considering that your cost to income ratio is significantly up now, 50% of you operating income being consumed by OPEX that the business needs. So that significantly hinders your capital generation as well.

Naveen Rajanala:
Yes, fair point. I think there are two things. One is let me cover the CASA piece, as we would expect in a rising interest rate environment, there would be some impact on CASA balance. As a result, there has been some 400 basis points drop off in the CASA proportion. But I don't think it's reached a stage where it is alarming. I think it's a natural and we've planned for it. At the same time, if you remember sometime last year and also in Q2, Q3 last year when there was a lot of pressure on Cost of Funds, that pressure has gone away. So, when the interest rate hike happened now, which is the very recent one, we don't expect that to impact the cost of fund too much. So, I think we would still expect to capture some positive spread there. Though as the migration from CASA to Time Deposit happens, it's going to impact our overall cost. But we are very mindful of that, as we said our margins should be around the 2% level. The pickup at a group level on the margins is going to come from the expected positive movements that's happening in Turkey. So, Turkey margins, historically, were 3.5%+, it's come down to the low 2s.

We expect that to start migrating towards the 3% by the end of the year and move up from there. That should provide the much-needed margin pickup.

Rakesh Tripathi:
If I may just ask one thing regarding Turkey margins. I've been on other bank calls, UAE banks calls, the ones that have subsidiaries in Turkey. Some of them have the precise opposite view that they expect the regulatory pressures in Turkey to have a negative impact on the overall group NIMs, while you expect the opposite effect to happen. Can you walk me a little bit through what changes you expect in Turkey that might help the NIMs really pick up there another 7,200 basis points in H2?

Naveen Rajanala:
If we look at in the first half or if you look at Q1 of this year, most of the Lira Loans were running a negative gap of about 17 to 20%. So, effectively, it was costing the bank on deposits close to 40%. We were lending at about 15% because these were prescribed rates. That's one of the reasons why Mr. Khaled said that we had to reduce our Lira proportion. And so, again, from a bank to bank, the FC and Lira proportion changes. In our case, the foreign currency loan proportion is about 60% and it's going up, it used to be about 50/50 and now it's going up. On the foreign currency piece, the margins continue to be very healthy and is going up, while the negative pressure on our Lira proportion seems to be easing off. It's still in negative territory but it's easing off and it's not as bad as Q1. That's the rationale behind our thinking of the margins improving in Turkey for us.

Rakesh Tripathi:
The Central Bank basically is allowing now to price loans higher than the 15% rate, that's what is going to help?

Naveen Rajanala:
Correct. And also, the pressure on Funding Cost in Lira also is not as steep as it was in Q1.

Rakesh Tripathi:
That makes sense. Thank you. And second part, as you were going to address.

Naveen Rajanala:
Yes, so coming back to OPEX. So, obviously the bank has spent on digital and also there was increased personnel expenses in Kuwait, as Mr. Khalid alluded to. If you look at it truly, the cost to income ratio is largely impacted because of the drop in top line. We expect our interest income to sort of go up. But having said that, there are internal work streams to start looking at expense optimization. These things take a little bit of time, but I think we should start seeing the impact of this in three to four quarters from now.

RakeshTripathi:

Fair enough. So, right now, overall picture for Burgan, right now at least this quarter wasn't looking that great. The loan book contracted a little bit, incomes are down, CASA is going down, NIMs supposed to improve now, but have been under pressure so far. NPL ratio slightly up. But what we understand is that these things are expected to improve and by year end we should see better overall performance from the bank. Could you also confirm to me the Kuwait loan growth, what was the loan growth percentage actual year to date? Last question from my side.

Naveen Rajanala:
In terms of exact number, it's about 2%. We wrote off some exposure at the end of the year that reduced the loan book, but if I compare from last H1'22 to H1'23 the growth is 2%.

RakeshTripathi:
Fair enough. Thank you very much.

AhmedEl-Shazly:
Thank you, Rakesh. We have a question from Rami Qumri. Please go ahead.

Rami Qumri:
I want to understand the banks flexibility towards the dividends. What I'm trying to understand is given the increased cost to income ratio, lowering NIMs and potentially a little bit of contraction in the economies moving towards more uncertainty in the coming quarters. I'm trying to understand what tools the bank use will to reserve the capital ratios. I mean, how flexible are you with regards to cutting dividends if need be and increasing your retained earnings to boost your capital ratios? I mean, just the bank's capital allocation strategy and how flexible are you on dividend if need be?

Naveen Rajanala:
Sure. On capital, we've ended the first half at about 11.5%. As I've said in the past, this does not include our profits generated so far. So, if I look at a view at the end of the year, we are fairly confident that we would be around these levels, net of any potential dividend payment. We don't have a set dividend policy, but it is governed by mix of availability of sufficient capital buffers, as well as guided by what the market expects. But if there is a situation where capital is under pressure and a dividend non-payment is on the table, we will look at it as well. But at the end of the day, all dividend payment decisions are agreed with the regulator.

AhmedEl-Shazly:
Our next question comes from Essa Buheji. Please go ahead.

Essa Buheji:
One question on the Cost of Risk. We've seen a spike during the quarter. Is that driven by the account that you spoke about in Kuwait or are you trying to be more prudent in the sense increasing your allowance? And going forward, what is the guidance basically for Cost of Risk?

My other question is on the top line, so I understand what happened in Turkey, but the drop is really sharp quarter on quarter, this is the lowest I think in in the recent past that we've seen for the bank in terms of top line. Will this be reversed in the coming quarter, or it will take time until we go back to normalized levels in terms of net interest income? That's all from my side.

Khalid Zouman:
In regards to Cost of Credit, we mentioned earlier in our previous calls that historically it's 1%. Recently we saw some reduction lower than 1%. However, this quarter, we increased our provisions and we took proactive provisions. We have some good recoveries in Q2. So, we said why don't we invest in terms of booking some provisions in our P&L. So, in other words this is like a one-off item which has been asked after discussion among the senior management here. Please go ahead, Naveen.

Naveen Rajanala:
So, on the top line, obviously, one of the things we want to look is growing our interest income. So, you're right, I don't think the migration of those back to the previous levels of topline is going to be immediate. There are two things, one is obviously if you look at it in the past, Turkey was a much bigger franchise, we had BOB, etc. So, all these things impact our absolute topline level. But to get back to the previous levels, it's going to take some time. We obviously want to grow our book as well. But we're looking at about three to four quarters before that true growth starts kicking in at a topline level.

AhmedEl-Shazly:
Thank you, Essa. We have our next question from Constantine Rosenthal. Please go ahead.

Konstantin Rozantsev:
Thank you very much for the presentation and for taking my questions. I had three questions that I wanted to ask, and apologies if some of these have been already answered in the past. I missed part of the call. So, the first question on the Cost of Credit or Cost of Risk, could you please share your guidance? What's the outlook for Cost of Risk for the second half of this year and for the full of next year? What's your guidance? The second question. Over the next year or so, should we expect any capital contributions from shareholders towards the bank or any more asset transfers like in the case of BoB to related parties? Any activity, any transactions of that type?

And the third question. I think in the previous earnings call there was reference to the fact that the management is considering some exercise to reduce the related party transactions or exposures. Could you please update us on that? Has there been any work done on that? And if there's anything that we should expect around this year in the near term? Thank you.

Naveen Rajanala:
Sure. So, let me start with your first question in terms of guidance for Credit Cost. So, our credit cost is around the 90 basis points for the first half. We expect it to be around these levels. Again, it's a difficult exercise to hazard a guess on this, because I mean if we have any

precautionary, etc., it's difficult to sort of guess that number. But from our internal planning point of view, we expect this to be south of 1%. Guidance for next year is an extremely difficult exercise and I don't think it will be fair to give you a number. Our budgeting process etc. is going to happen towards the Q4 of this year. I think after that we'll be in a better position to give you some sort of color on that.

Coming to your next question in terms of is there any plan for new capital infusion from shareholders etc. As we undertake our capital planning etc., we do not foresee the need for any new rights issue or capital requirement, I'm talking about equity capital. As I mentioned, and as Mr. Khaled also highlighted, we are looking at certain optimization initiatives and if that comes to fruition, we will add some capital to our regulatory capital levels. So, as I mentioned earlier, related party exposure reduction is more long-term in nature. But as we've said this in the past, given that KIPCO is a large entity with many operating entities across MENA, it makes sense for us to do business with them.

But at the same time, there are efforts to reduce this over time. It cannot be reduced in one shot. But as we've said in the past, these are transactions which are done commercially at arm's length and as far as cost of Risk on any of these exposures, the bank has not lost a single Cent in Credit Costs over the last 15 to 20 years since this relationship started.

Konstantin Rozantsev:
Thank you very much.

AhmedEl-Shazly:
Thank you. We have a few more questions from the chat. Most of these have already been answered. So, what is your NPL coverage in Turkey following all these reversals there? What is your outlook on asset quality in Turkey of FX loans following the devaluation?

Naveen Rajanala:
The NPL coverage ratio in Turkey is about 150%. We've had a devaluation in the first half of last year and the general expectation was that it will translate into credit quality slipping up, but that never happened. So, we're not seeing any signs that the recent devaluation is going to lead to slippage in credit quality.

AhmedEl-Shazly:
All right. Thank you for that. I believe we have no more questions. I'd like to hand over the call back to management for any closing remarks.

Khalid Zouman:
Well, I would like to thank you for attending this call. For any further queries, please drop us a line or reach out to ir@burgan.com. Many thanks.

AhmedEl-Shazly:
Thank you so much have. A good day.