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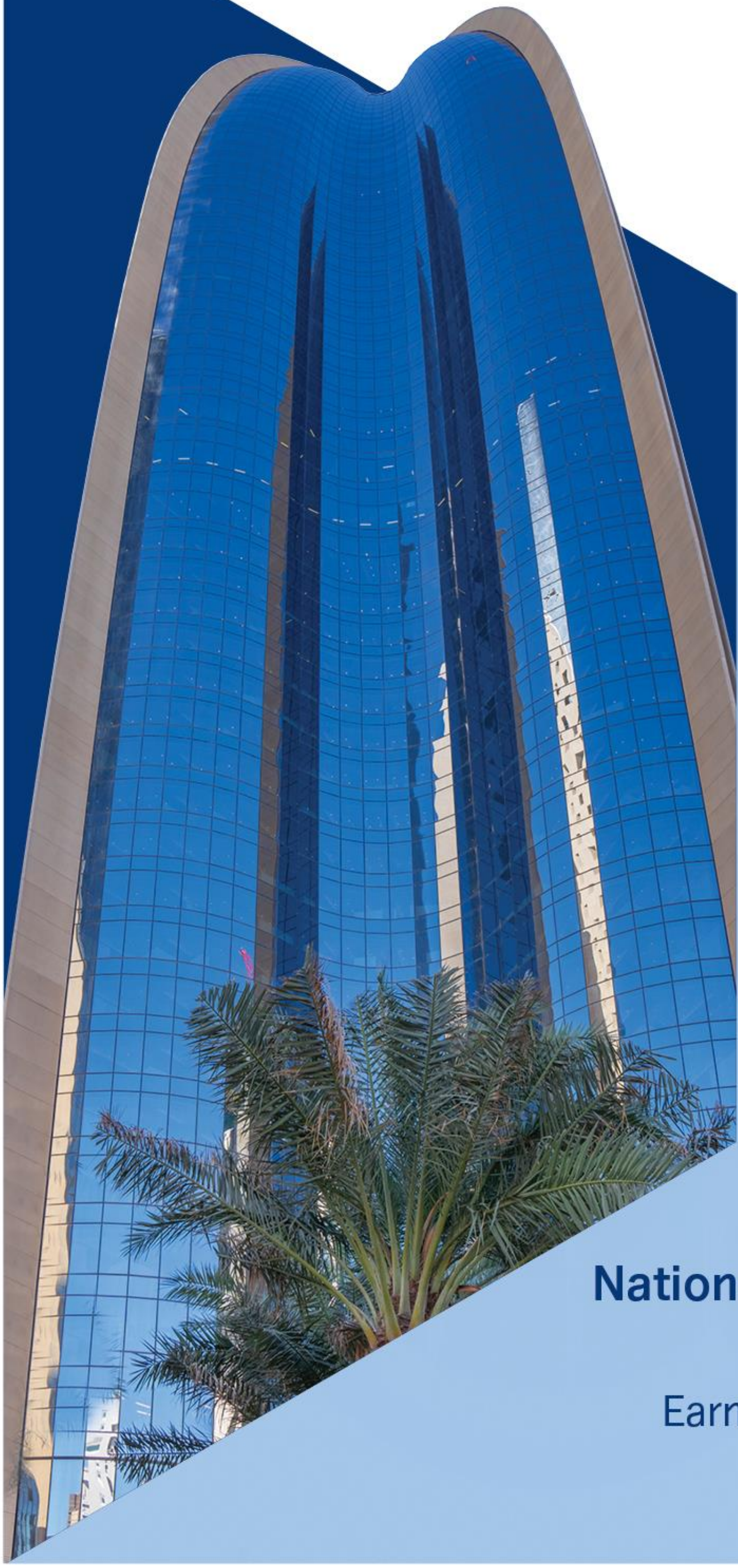

National Bank of Kuwait

3Q 2024

Earnings Conference Call

17 October 2024

3Q/9M 2024 National Bank of Kuwait Earnings Call

Sunday, 20 October 2024

Edited transcript of National Bank of Kuwait earnings conference call that took place on Thursday, 17 October 2024 at 3:00 pm Kuwait time.

Corporate participants:

Mr. Isam Al-Sager – Vice-Chairman and Group CEO, NBK

Mr. Sujit Ronghe – Group CFO, NBK

Mr. Amir Hanna – Head of Investor Relations and Communications, NBK

Chairperson:

Elena Sanchez – EFG Hermes

Elena Sanchez: Good afternoon everyone. This is Elena Sanchez and on behalf of EFG Hermes, I would like to welcome you all to the National Bank of Kuwait third quarter and nine-months earnings call for the year 2024. It is a pleasure to have with us in the call today Mr. Isam Al-Sager, NBK Vice Chairman and Group CEO, Mr. Sujit Ronghe, NBK Group CFO and Mr. Amir Hanna, Head of Investor Relations and Communications at NBK.

At this time, I would like to handover the call now to Mr. Amir Hanna.

Please go ahead Amir.

Amir Hanna: Thank you Elena.

Good afternoon everyone. Thank you for joining us for today's webcast.

We will start the call with our usual disclaimer as I would like to bring to your attention that certain comments in this presentation may constitute forward-looking statements. These comments reflect the Bank's expectations and are subject to risks and uncertainties that may cause actual results to differ materially and may adversely affect the outcome and financial effects of the plans described herein. The Bank does not assume any obligation to update its view of such risks and uncertainties or to publicly announce the result of any revisions to the forward-looking statements made herein. Please also refer to the full disclaimer in our presentation for today's call.

Today's call will follow our usual agenda. Our Vice Chairman and Group CEO, Mr. Isam Al-Sager, will start the call by giving some opening remarks on the operating environment and the highlights of the reporting period. Then Mr. Sujit Ronghe, our Group CFO will go through the financials in more details. Following our presentation, there will be a Q&A session through Webex platform. If you have any follow-up questions after the call please direct it all to our Investor Relations email address and we will answer them at the earliest. Today's presentation is available on our website for your convenience.

Now let me hand over the call to Mr. Isam Al-Sager for his opening remarks.

Isam Al-Sager: Thank you Amir.

Good afternoon everyone.

I am pleased to join you today for our third quarter and nine-months earnings call for the year 2024.

On a global scale, uncertainty continues to shadow the economic outlook as major central banks shift their attention from rising prices and inflation towards potential recession challenges. The sluggish demand and increased geopolitical tensions added to the uncertainty of the outlook.

In the GCC region, performance across markets witnessed relatively positive economic developments with strong non-oil growth amid looming uncertainties. On the other hand, the challenging geopolitical scene and oil price volatility will continue to have an economic impact on GCC economies.

Likewise, in Kuwait, economic indicators point to a subdued pace of growth but not far from a rebound. Inflation on the other hand softened marginally to 2.9% as of August-2024 and expected to continue to trend lower to remain on track for an average annual rate of 3.0% compared to 3.6% recorded in 2023.

Similarly, latest provisional data showed that non-oil GDP grew modestly in 2Q-2024. Meanwhile, oil GDP contracted on lower crude production.

On a positive note, Project activity maintained its momentum and remained solid in 3Q 2024 with the power and water sector constituting three quarters of the value awarded during the period. Activity is likely to pick up for the remainder of the year, in line with government development plan priorities with around KD 3.3 billion worth of awards penciled for next couple of quarters.

In the face of uncertain economic cycles, NBK continues to prove its resilience against shifting operating conditions, its prudent approach to risk management and its ability to sustain growth from diversified income streams. We reported net profits of KD 457 million for the nine-months of the year; growing by 6% on an annual basis. As for the three-months ended September 2024, net profits reached KD 164.6 million; posting a growth of 5.7% year-on-year.

Our diversified business portfolio across geographies and business segments has further driven growth while capturing opportunities even in volatile market conditions. We achieved growth of 7.8% year-on-year in net operating income to reach KD 931.0 million for the nine-months period.

In line with the evolving needs of our clients, we continue to excel in digital innovation and deliver a holistic banking experience that reflects positively on operational efficiency while reinforcing our commitment towards long-term value creation to both stakeholders and customer. Accordingly, our return on average assets for the reporting period reached 1.60% whereas our return on average equity reached 15.4%.

Our strategic initiatives continue to contribute to the leadership position that the Bank is recognized for in Kuwait. We will continue advancing our technological and digital investments and growing our products and services portfolio in the market. Furthermore, by deepening the relationships with existing clients and actively seeking new business opportunities, we will endorse the Group as a trusted financial partner.

Moreover, we will remain focused on leveraging our unique competitive advantage domestically, as the only bank in Kuwait with access to both conventional and Islamic banking markets. Our subsidiary Bobuyan Bank continues to support the Group in diversifying our client base and income streams. Meanwhile, NBK wealth will solidify its proposition and offering best-in-class wealth management experience in the market. Similarly, our international operations remains vital for the Bank's stability and growth prospects.

At NBK, ESG principles remain a cornerstone of our operations and lending philosophy. Our robust governance framework is central to every strategic decision that we continue or intend to make. This affirms our dedication to ESG stewardship, our commitment to transition to a low-carbon economy and our carbon neutrality pledge.

With that, I will conclude my comments and leave you with my colleague Sujit Ronghe, our Group CFO, to cover quarterly and nine-months results in more details.

Please go ahead Sujit.

Sujit Ronghe: Thank you Mr. Isam.

Hello everyone and welcome.

I am very pleased for the opportunity to take you through the financial results in respect of nine months of 2024.

We have announced a net profit of KD457m for 9M24, a 6% increase over the corresponding period of 2023. These results stem from a strong operating performance by the Group and demonstrate the continued growth in our business.

Before going on to details of our financial results, a few words regarding the overall operating environment during the current reporting period.

The higher interest rate regime for a significant part of the reporting period and an overall stable operating environment in Kuwait have generally benefitted the Bank. Last month's bench-mark interest rates cut appears to have set the tone for upcoming quarters. At the same time, recent geo-political events in the region and beyond continue to adversely affect the global operating environment.

Now turning to the financial results for 9M24.

As shown at the top left of this slide, net profit at KD457m reflects a yoy growth of KD25.9m i.e. 6%. Underlying drivers for the robust bottom-line performance are a combination of yoy growth in business volumes, relatively higher interest rates, culminating in a strong operating performance. Group loans and advances grew year on year by 6.2%. Investment securities also contributed strongly to Group assets with a growth of 17.3% v Sep 23.

The top right chart reflects operating surplus i.e. profit before provisions and taxes for the current nine months at KD588.5m, a growth of KD34.9m, +6.3% over 9M23. Net operating income increased by KD67.3m, +7.8% whilst operating expenses grew by KD32.3m, +10.4% over last year.

3Q24 net profit at KD164.6m was 12.9% more than previous quarter driven by a stronger operating performance and lower provisions.

The operating income mix profiled at the bottom right hand continues to show a healthy mix with 21% coming from non-interest income sources.

I will go into the main drivers behind movements in income, margins and costs shortly.

Moving on now to the next slide.

We now will look at net interest income and drivers behind its performance.

The chart at top left reflects the net interest income of KD733.7m for 9M24, a growth of 10.2% over 2023. NII largely benefited from higher average interest rates compared to 9M23 and growth in loans and investment securities across geographies and segments. You would also note from the chart at the top right that Average earning assets grew by KD1.8bn i.e. 5.2% over Sep 23, to reach KD36.4bn.

We see from the chart at the bottom left, that average NIM for 9M24 at 2.69% reflects an improvement of 12bps over 9M23, driven by a higher yield, despite increased funding cost. Group yield and funding cost for the current nine months were 6.23% and 3.99% respectively. The higher funding cost relative to 9M23 results from the repricing of deposits at increased market rates and a limited migration of lower cost deposits to time deposits. However, an overall sticky and stable base of retail customer deposits continues to benefit the Group.

At the bottom right of this slide, we can see drivers behind the 12bps yoy increase in NIM from 2.57% in 9M23 to 2.69% in 9M24. Loans and others backed by a strong year on year growth in volumes and relatively higher average interest rates, contributed net 54bps to the NIM. Higher funding cost negatively affected the NIM by 42bps.

Moving on now to the next slide.

As we can see at the top left of this slide, total non-interest income of KD197.3m was similar to the last year. Fees and commissions income was strong at KD151.7m, reflecting robust contributions across different lines of business and geographies. Fx income at KD24.8m, was lower than 9M23 despite a stronger underlying performance mainly due to the negative swing of currency movement on assets related to our $AT1 bond issuances. Other non-interest income sources at KD20.8m was slightly higher than the previous year.

Our fees and commissions income are from a well-diversified pool of geographies and lines of business. Also, major sources of non-interest income are core banking activities in respect of business-related factors.

Turning now to operating expenses reflected in the top right-hand side of this slide. Total operating expenses for 9M24 at KD342.5m, were 10.4% higher than the previous year. The cost growth reflects increasing activity levels across the Group's network and investments in key businesses initiatives, digital technologies, resources etc. This enables the Group to offer best-in-class service to its customers and optimize resources to improve operational efficiency.

NBK's focus on digital channels and product offerings continues to play a vital role in attracting and servicing customers, with increased volume of electronic transactions. We also continue to press ahead with selective product offerings in certain geographies e.g. through our global wealth management business i.e. NBK Wealth, Islamic banking through Boubyan Bank and by further leveraging our overseas network.

As a result, the 9M24 cost to income ratio was at 36.8%, compared to 35.9%, for 9M23 and 36.6% for the full year 2023.

Moving on to provisions and impairments profiled on the bottom right-hand side of the slide.

Total credit provisions and impairment losses for 9M24 were KD56.3m, a decrease of KD9.5m over the last year. Specific provision of KD44.8m was in course of normal business activities at Kuwait and overseas locations. KD15.4m was towards general provisions, which included a component of precautionary provisions. The Group remains committed to its conservative approach in managing credit exposures.

The Group wrote back a net amount of KD3.8m towards ECL and other impairment losses, due to lower net provisions requirement towards non-credit financial assets.

The cost of risk for 9M24 was 34bps compared to 40bps in 9M23.

It is worth noting that the Group's Balance Sheet remains strong with a stable credit quality. NBK's capital base along with the ability to generate healthy operating profits provides a strong credit loss-absorption capacity.

Moving now to the next slide.

On this slide, I would like to elaborate on the matter of earnings diversification of the Group through different lines of business.

NBK Group continues to benefit from its unique position amongst Kuwaiti banks in terms of geographical spread through International Banking and the ability to conduct business in both Conventional and Islamic Banking.

NBK's business segments serve as main pillars of diversification, providing a strong competitive advantage and a significant degree of resilience to Group earnings.

You would note that NBK's Consumer Banking contributed 20% and 17% to the Group's net operating income and profit respectively. Similarly, Corporate Banking contributed 13% and 19% to the Group's net operating income and profit.

International Banking contributed 24% to net operating income and 23% to the Group's profit, reflecting a strong operating performance.

The Group's Islamic banking subsidiary Boubyan Bank delivered a net profit of KD73.5m, up 20.3% on 9M23, boosted by a strong growth of 10.2% in operating surplus and lower provisions for credit losses.

NBK Wealth contributed to 10% and 11% of the Group operating income and profit respectively. NBK Wealth provides asset management, brokerage, lending, deposits and other customized and innovative offerings to high-net-worth individuals and institutional clients, further advancing the Group's diversification agenda.

Finally, chart at the bottom right corner, you will note that International Banking and Boubyan Bank contributed 42% and 23% respectively to Group's total assets enforcing the diversification agenda of the Group.

Moving to the next slide.

Here we will look at some of the movements in key volumes during the year.

As profiled on the chart at top left, the Group total assets reached KD39.2bn as of Sep 24. The 6.3% year on year net growth, includes adverse effect of EGP devaluation in March 24.

Group loans and advances at KD23.2bn registered a growth of KD1.4bn i.e. 6.2% from September 23 and 3.9% during the current year. Loan growth was achieved at Kuwait and International locations, in both - conventional and Islamic banking. Similarly, investment securities reflected a yoy growth of 17.3%, to reach KD7.4bn.

Customer Deposits, i.e. non-bank and non-FI deposits at KD22.4bn, reflect a yoy growth of 7.1%. As can be expected in a higher interest rates scenario, some low-cost deposits moved to relatively higher cost time deposits. However, CASA deposits at end of the current quarter are at a level similar to Dec 23. The Group continues to benefit from a strong base of core, franchise retail deposits.

NBK's stable deposit and the fuller funding base reflects a sustained focus on the deposit gathering aspects of our business, the Group's strong brand, customer appeal and credit ratings.

Customer deposits comprise a healthy 68% of total funding mix of the Group.

I want to highlight that the Group continues to maintain healthy liquidity levels & comfortably exceeds the minimum requirements of Basel III ratios.

Moving now to the next slide.

We will now look at the impact 9M24 financial results had on certain key performance metrics.

The Return on Average Equity for 9M24 remained steady at 15.4%. Similarly, Return on Average Assets increased to 1.60% compared to 1.58% in 9M23.

At 16.5%, the total capital adequacy ratio remained strong and stable, well above the regulatory minimum with CET1 and Tier1 ratios at 12.2% and 14.2% respectively. It is important to note that regulatory capital does not include interim profits, but the interim dividend of KD83m (at 10 fils / share) is deducted for capital adequacy ratio calculations.

As regards asset quality, NPL ratio remains stable at 1.39%, similar to Dec 23 level. Loan loss coverage ratio is at 263%, reflecting conservative provisioning policy of the Group.

Moving to the next slide.

On this slide, I would like to discuss Expected Credit Losses (ECL) on credit facilities as per IFRS 9 calculated in accordance with CBK Guidelines. As per the regime adopted by CBK, Banks calculate the credit provisions required (i.e. the amount in the balance sheet) as per CBK instructions and compare it with the ECL on credit facilities as per IFRS 9 in accordance with CBK guidelines. Consequently, the charge to income statement is based on the higher of the two balance-sheet amounts.

It is important to note here that CBK guidelines for calculating ECL on credit facilities as per IFRS 9 are on a more conservative basis compared to the original accounting standard.

The key chart on this slide at the bottom right reflects that ECL provision required as of Sep 24 was KD600m, slightly lower than Dec 23.

Although IFRS 9 ECL and CBK provisions are two different regimes and should not be compared as such, currently the balance sheet provision as per CBK instructions exceeds the ECL by KD326m. This provides ample cushion for the Group to withstand any possible adverse effect of prevailing uncertainties on ECL provision requirements.

Now to the final slide in this section.

Before concluding, allow me to summarize our financial performance in 9M24.

NBK's strong operating performance with a healthy balance sheet, comfortable liquidity and a strong capital base continued in 9M24.

In light of the ongoing regional and international geo-politics we remain cautiously optimistic that the overall operating environment, although challenging, will remain generally stable in the coming quarter.

Now turning to the guidance for the remainder of the year.

As regards loan growth - Given the current geo-political and the general macroeconomic situation, we continue to expect the overall loan growth for 2024 to be in the mid-single digit range.

Now turning to the NIM. The expectation at large is that benchmark interest rates, especially the US Fed, would continue to decrease in coming months and quarters. The 9M24 NIM of 2.69% benefited from stronger volumes and higher interest rates. Interest rate cuts in 4Q24 will have a limited impact on the full year 2024 NIM and we expect to close the year similar to 9M24 level.

As regards operating expenses, the 9M24 yoy cost growth was 10.4%. As the Group continues to invest in human resources and digital technologies, we expect the annual cost growth to be below 10% and the cost to income ratio to be in high thirties.

The cost of risk was 34bps during 9M24. We are cautiously optimistic of an overall stable operating environment and expect full year cost of risk to be in the 35-40 bps range.

However, given the overall geopolitical and macroeconomic uncertainties, it would not be prudent to give specific guidance on earnings / capital adequacy. We are hopeful of maintaining capital adequacy ratios in line with our internal targets above the regulatory minimum.

That ends my presentation.

Thank you very much for your time.

Back to Amir.

Amir Hanna: Thank you, gentlemen.

We will break for a while as questions are being received through the Q&A platform.

We will resume to respond on according to topic.

Margins improved quarter on quarter in 2Q and Q3 but with rate cuts how do you see the trend? What percent of your book is USD? Can you remind us of the impact on the NII from a 25-basis point rate cut?

Sujit Ronghe: You are right, margins did improve between the second and the third quarter resulting in a Group NIM of 2.69% for the nine-month period. Going forward, we generally expect that benchmark interest rates would continue to decrease in coming months, although at this stage, the size of each rate cut remains uncertain both in Kuwait and International context.

That said, we do not expect a significant impact on the NIM in the fourth quarter and the full year NIM is expected to be similar to that of the nine-months.

On the sensitivity side, I would expect that the annualized impact of a parallel shift (that is both on assets and liabilities) of 25 basis points in CBK rate and international benchmark rates would be in the range of 3-4 basis points. The impact on net interest income can accordingly be forecasted depending on the frequency and size of rate cuts.

Amir Hanna: How do you see loan growth evolving in Q4 into next year against the backdrop of government initiatives and lower rates, and where do you see growth coming from, and when do you expect the projects spend to accelerate in line with government priorities? How do the indicators in Kuwait translate into loan growth outlook for next year and in the medium-term?

Sujit Ronghe: The loan growth in last nine months was achieved in both Kuwait and our International network. Credit growth was more on the corporate side because of the rather muted demand for consumer loans in Kuwait. We expect this to change in the coming year when interest rates decline.

As regards the growth related to Government projects- historically, given the project life cycle, loan growth has translated on the book, 4-6 quarters after the projects are awarded. We would first expect some growth in the trade finance related activities followed by on-balance sheet loan growth. Hence, we are a bit far away from projects related loan growth in the immediate few quarters. At the same time, we remain very optimistic that the significant project activity expected, would lead to first non-cash in the business i.e. guarantees, LC's, etc. and later translate into loan growth.

Our base case scenario guidance is for next year's loan growth to remain in mid-single digit. However, as project activity progresses, we could see loan growth increasing to a high-single digit, of course depending on the timing of projects and drawdowns by corporates.

Amir Hanna: Question on corporate tax and how should we model that going forward?

Sujit Ronghe: As we know, the Pillar 2 or 15% Global Minimum Tax is applicable for companies with a turnover of more than Euro 750 million and is expected to be levied from the next year. NBK Group is already paying tax in most of the countries where we operate. Recently, Bahrain has declared a 15% Minimum Domestic Top-up Tax for qualifying entities. We are similarly expecting a tax law to be enacted in Kuwait before the beginning of next year.

Although specific details regarding the Kuwait tax law are not yet available, it would be fair to estimate that the tax charge to double and reach the level of 15-17% of pre-tax profits.

Amir Hanna: Another question on asset quality, the bank reported a very healthy asset quality improvement, can you shed some light on the sector and region?

Sujit Ronghe: The improvement in asset quality has not come from any one specific sector or region. We have seen an overall improvement in the NPL classified previously. The asset quality remains sound with NPL well within the range of 1.5-2.0%, which is considered a normal level for the Group.

Amir Hanna: Question on trading income, third quarter 2024 was high, how much of it are one-off in nature?

Sujit Ronghe: Typically the bank does not have a lot of activity in the trading book. Most of the trading income was a result of better valuations in the third quarter compared to the second with no particular one-off instances in the trading book.

Amir Hanna: On Saudi, have you been placing deposits in the Saudi Arabian banking system at SIBOR? Can you comment on your Saudi strategy if it part of syndicated loans to the corporate or GRE sector?

Sujit Ronghe: Saudi Arabia or any other international branch or subsidiary that we operate are mainly self-funded. Deposits that have been placed in SIBOR are funded from local operations.

Our strategy in Saudi Arabia since the last few years, is to increase our presence in the wealth management business through NBK Wealth. This is in line with the focus on increasing wealth management offerings to private banking customers beyond Kuwait and Saudi is a key growth market for us.

With respect to corporate banking, we continue to provide credit facilities and other trade finance services to different companies in Saudi Arabia - some GREs while others are high quality corporates. We of course maintain our conservative approach to credit, which has resulted in a sound credit quality and lower NPLs for the Group.

Amir Hanna: A couple of questions on the mortgage law, the increase in the backlog of housing applications and government plans?

Isam Al-Sager: This has been the case for a long time concerning the mortgage law. The previous parliament penciled various housing-related laws and initiatives that position the law closer to getting passed; minding that the political scene have changed in the meantime.

Given the growing number of housing applications which reached 97.6 thousand as of Sep-24, there is an increased likelihood that the law will be passed to address this financing mechanism issue going forward.

Looking at the political scene recently in Kuwait, there is no solution other than passing the law and the sooner it does the better.

Amir Hanna: Are financial institutions deposits very different in nature from customer deposits? Why are they disclosed separately? Are financial institutions deposits of a shorter term and from outside of Kuwait?

Sujit Ronghe: Our acceptances and deposits, they come from 3 main sources - interbank acceptances, customer deposits and deposits from financial institutions i.e. non-bank financial institutions. Customer deposits base comprises of retail, GREs and private corporates across our network. Financial institutions deposits are shown separately in the balance sheet for better disclosure purposes, as some readers want to see the same separately from inter-bank acceptances. Hence, we follow the best practice by disclosing due from banks, deposits from other FIs and customer deposits separately.

Deposits from financial institutions are typically medium-to-long-term in nature and comprise of both Kuwaiti and overseas financial institutions.

Amir Hanna: More questions on loan growth this year and expectations for next year; I believe we covered this area comprehensively.

Could you please add some color on what segments are driving the increase in credit demand and what do you see in the coming quarters that makes you think that the momentum will continue?

With the exception of the sectors, we covered that as well.

Sujit Ronghe: From a sector point of view, demand for loans in the last nine-months of this year mainly came from corporate relationships in Kuwait and across our international network, be it the middle east region or Europe, US, UK etc.

Amir Hanna: Can you please comment on how you think to approach the AT1 call option that is coming in Aug-2025?

Sujit Ronghe: The AT1 call option would be in the second half of next year and it is too early to give a definite answer. However, it is important to note that the Bank has historically been market friendly when it comes to such decisions. At this stage, we don't foresee any reason to change this practice in the future.

Amir Hanna: A question on capital, is your buffer over CET 1 by year-end 2024 of approximately 150 bps a comfortable level? Considering that credit demand could improve in 2025.

Sujit Ronghe: In line with our risk appetite, we aim to maintain an internal buffer of minimum 150 bps over the minimum CET1 requirement at the year-end. This buffer of course is reviewed periodically and for now the Bank is comfortable with minimum 150 bps.

Amir Hanna: A question on mortgage law that is covered.

Can we expect opex to grow at the current rate in 2025 as well?

Sujit Ronghe: Yes, given our continued investments in digital banking and the resources that are required to roll-out different offerings, we would expect a circa 10% increase in costs for the coming year as well.

Amir Hanna: Last question we have on the list. Can you maintain the current cost of risk level next year too?

Sujit Ronghe: We expect the cost of risk to range between 35-40 bps for the current year. As things stand, there is a lot of uncertainty with respect to the geopolitical situation and macro-economic environment. From a 2025 guidance point of view, we currently expect the cost of risk to be in the region of 40 bps.

Amir Hanna: Another question came in. What is the impact roughly of your interim profits on your CET 1 ratio in the nine months?

Sujit Ronghe: Current year profits are not included in the capital adequacy calculations for interim periods, but interim dividend is deducted from the capital base. To answer the question slightly differently, at the year-end, we expect the CET 1 ratio going back towards the 13% level after including full year profits and deducting dividend.

Amir Hanna: These are all the questions that we received for today.

Thank you so much for attending the call.

Back to Elena.

Elena Sanchez: I would like to thank NBK's management team for the presentation and responses provided today.

Thanks to all participants for joining us today.