EMIRATES NBD Q4 2019 RESULTS ANALYSTS & INVESTOR CONFERENCE CALL & WEBCAST
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Operator

Ladies and gentlemen, welcome to the Emirates NBD 2019 Full Year Results Announcement Analyst and Investors Call and Webcast. If we're all ready to begin, I'll now pass the call over to our host Mr. Shayne Nelson, Group CEO of Emirates NBD. Please go ahead sir.

Shayne Nelson

Thank you operator and thank you all for participating in today's call. Joining me on this call are Surya, the outgoing Group CFO, who will cover the 2019 results and Patrick Sullivan, the incoming Group CFO, who will also comment on the results and talk about the 2020 guidance. Also on the call is Paddy, our Head of Investor Relations, not to be confused with Patrick, our new Group CFO.

We move to page 3 of the presentation, it contains a summary of the key results. We reported a strong set of results with net profit up 44% to 14.5 billion dirhams for 2019. We are also pleased with DenizBank's performance which contributed total income of 3.6 billion dirhams and a net profit of 609 million dirhams for the 5 months since acquisition. Excluding the gain from the Network International transaction the Bank's net profit grew marginally as a 29% increase in income more than offset higher expenses, taxation and impairment allowances. We will elaborate in more detail on the profit drivers in subsequent slides. The Bank's balance sheet remains solid with healthy liquidity and stable credit quality. Following the successful rights issue in November, the Common Equity Tier 1 ratio settled at 15.3%.

2019 was a momentous year for Emirates NBD. As well as growing the asset base to over 683 billion dirhams, we welcomed DenizBank into the Emirates NBD family. This expands the Bank's presence to 13 countries, servicing over 14 million customers. The $1.75 billion rights issue, which was 2.8 times oversubscribed, strengthened capital ratios to provide a strong foundation to embrace controlled growth in the coming years. The rights issue helped boost the capital base to over 80 billion dirhams and will propel Emirates NBD into the Banker's list of Top 100 global banks by capital.

The Bank raised its Foreign Ownership Limit to 20% and signalled its intention to further increase the limit to 40% in due course. Foreign ownership has grown from 5% to 8.5%, helped by over 62% foreign demand for the rights issue. The operating performance, coupled with strategic initiatives, helped generate significant shareholder value. We were granted permission to open a further 20 branches in the Kingdom of Saudi Arabia. This ongoing expansion in KSA and Egypt will help cement our position as a leading bank in the MENAT region.

We won numerous awards and were named 'Bank of the Year – UAE 2019' for the 4th time by The Banker, in recognition of its robust financial performance and pioneering approach to innovation in digital banking. Disability friendly access was extended to cover about half of the Bank's UAE network. 2020 promises to be an exciting year, filled with opportunities and challenges. As the official banking partner of Expo 2020 Dubai, we are excited about the economic opportunities that this event will generate for the UAE. This will further strengthen Emirates NBD's prominent position as a key banking partner.

We have recently completed the third chapter of our 1 billion dirham digital transformation and will conclude the final phase ahead of the UAE's 50th anniversary. We now operate a diversified business model across the MENAT region. This allows us to direct capital to the most attractive growth opportunities in the region. The Bank's Research team estimate that GDP growth in the UAE reached 2.0% in 2019. However, deeper oil production cuts announced by OPEC in December are likely to weigh on the UAE and the Research team expects GDP growth in the UAE to slow to 1.6% in 2020. Nevertheless, Dubai's economy is expected to gain momentum this year, with Expo 2020 providing a boost to activity in the Emirate. Research expects Dubai's GDP to grow 3% this year, up from an estimated 2% in 2019.

In summary, I am pleased with the Bank's operating performance and the many strategic initiatives which were positively received by all our shareholders. We will continue to drive efficiencies and capital optimisation across the Group. As Expo 2020 draws closer I am confident that we will be able to take advantage of growth opportunities across our MENAT network whilst delivering excellent customer service and superior value to our shareholders.

I'll now hand you over to Surya to go through more details of the presentation. Surya.

Surya Subramanian

Thank you, Shayne. This is my last full year presentation before Patrick takes over. I have immense pleasure in revealing a record set that will be among, if not, the best in the region.

Let me lead as usual through slides 4 and 5 of the presentation. As Shayne mentioned, the Group's net profit of 14.5 billion dirham in 2019 represents a 44% increase on the previous year. This includes a 3.2 billion dirham realized gain and 1.2 billion dirham unrealized gain from the Network International transaction. It also includes 609 million dirhams of net profit from DenizBank for the 5 months since acquisition date. Excluding the gain from Network International, net profit increased by 1% in 2019.

Core Operating Profit grew 4% year on year supported by 26% higher net interest income from loan growth and 38% higher non-interest income. Excluding DenizBank, Core Operating Profit declined 5%, mainly due to higher impairment allowances. The 28% increase in costs is due to a rise in staff costs, amortization of intangibles and higher depreciation due to IFRS 16 implementation. Excluding DenizBank, costs increased by 6%. The cost to income ratio at 32.1% is within guidance and the Bank remains firmly focused on cost controls.

Provisions of AED 4,818 million were 176% higher than in 2019, or 88% excluding DenizBank. We had given earlier guidance of an increase in the cost of risk reflecting the slowdown in regional and international markets. Net cost of risk rose to 117 basis points as a result of higher net impairment charges with lower writebacks and recoveries compared to 2018. Loans and Deposits grew by 7% each respectively during 2019 excluding DenizBank.

The Liquidity Coverage Ratio of 160.0% and the Advance to Deposit Ratio of 92.6% demonstrate the Group's healthy liquidity position. During 2019 the Impaired Loan Ratio settled at 5.6% as a result of acquisition of DenizBank's loans at fair value. The Bank's Capital ratios improved following the successful completion of the rights issue and remain comfortably above the minimum regulatory requirements.

Taking you now to slide 6 on net interest income we see that margins increased 7 basis point year-on-year to 2.89%, helped by higher margins from DenizBank. Excluding DenizBank, margins declined 12 basis points on higher average deposit costs for the year. As DenizBank benefited from a lower interest rate environment, it provided NIM diversification for the overall Group and the positive impact of DenizBank helped offset the effect of interest rate cuts flowing through to the UAE loan book.

In Q4, we saw a 28 basis points improvement in margins, as the 31 basis point impact from DenizBank's higher margins more than offset a 3 basis point margin contraction. These dynamics allow us to finish the full year at 2.89%.

Slide 7 on funding and liquidity, we see that the Liquidity Coverage Ratio remains healthy at 160% whilst the Advances to Deposits ratio strengthened to 92.6%, at the conservative end of the 90-100% target range and demonstrates the Bank's continuing healthy liquidity. Liquid assets are 109.3 billion dirhams or 18% of total liabilities. During 2019 we raised 13.3 billion dirhams of term funding in 9 different currencies with maturities out to 20 years. Debt and Sukuk represent 9% of total liabilities, down from 10% at the beginning of the year, due to a smaller relative contribution from DenizBank.

Since the acquisition, DenizBank has seen improved pricing and access to wholesale funding. In the 4th quarter of last year, DenizBank successfully returned to the syndicated loan market. This transaction saw good demand from a broad range of investors enabling DenizBank to issue a 2.8 billion dirham syndicated loan, whilst offering significant scale back. This loan included a 2 year tranche.

On slide 8 we share with you the loan and deposit trends and we see that gross loans grew 7% since start of the year with growth across all operating segments. Corporate lending grew 8% with demand coming from agriculture, manufacturing, services and the construction sectors. Consumer lending grew 4% due to growth in personal loans and credit cards. Islamic financing grew 5% due to growth in personal and trade sectors. CASA across the entire Group represents 43% of total deposits. The domestic CASA engine for Emirate NBD remains stable and represents 49% of domestic deposits.

We have a long composition slide 9, we thought it useful to show how the addition of Deniz Bank has helped diversify the loan book. A year ago the loan book was heavily concentrated with the UAE making up 93% of total loans. At the end of 2019, the UAE comprises 3 quarters of loans with International and GCC making up 25% of the loan book. This improvement in diversification also extends to sector level where 35% of loans are sovereign, down from 43% in 2018. Retail lending has grown from 12% to 17% whilst corporate has also grown from 30% to 35% of the loan book.

With that, I now hand you over to Paddy to take us through the next few slides.

Patrick Clerkin

Thank you Surya. Slide 10 shows that core fee income improved 32% year on year. This increase is driven by higher foreign exchange and credit card related income. Investment securities and other income also showed a year on year improvement due to a higher gain on trading securities as a result of changing interest rates. Property losses were smaller due to lower provisioning on the existing inventory.

On slide 11 we see that, excluding DenizBank, quarterly costs were higher due to a rise in staff and operating costs relating to international expansion, higher depreciation due to the implementation of IFRS 16, increased costs relating to the digital transformation and amortization of intangibles. The cost to income ratio in Q4, at 36.4%, increased partly due to redundancy costs. This ratio tends to be higher in the final quarter as the Bank invests in marketing initiatives and other revenue generating investments ahead of the new year. Excluding these one-off and seasonal costs, the cost to income ratio for Q4-19 was closer to guidance. The year to date cost to income ratio at 32.1% is within guidance and the Bank remains firmly focused on controlling costs.

On slide 12, as was mentioned earlier, we see that the NPL ratio settled at 5.6% as a result of the acquisition of DenizBank's loans at fair value. Provisions for 2019 of 4.8 billion dirhams increased 176% y-o-y, or 88% excluding DenizBank due to higher charges and lower writebacks and recoveries. In 2019 the Bank has 1.5 billion dirhams of write backs & recoveries compared with to 1.6 billion in 2018. The net cost of risk increased to 117 bps on higher provisions including the impact of DenizBank and reflecting the slowdown in regional and international markets. The coverage ratio declined to 112.3% as DenizBank had comparatively lower coverage on its NPL portfolio. Including collateral the coverage ratio is 210%.

Stage 1 & 2 ECL allowances amount to AED 8.3 billion or 2.2% of CRWA. Note 50 of the financial statements shows that, during 2019, stage 2 loans have increased from 9.4 billion dirhams to 20.3 billion dirhams. A large element of this relates to stage 2 loans at DenizBank and we will continue to monitor this closely. It is however worth noting that stage 2 coverage is high at 15.8%

Slide 13 shows that capital ratios strengthened in the final quarter of 2019 as the Rights Issue and retained earnings more than offset the impact of growth in risk weighted assets. Credit Risk Weighted Assets increased by 53% during the year as the Bank absorbed a 126 billion dirham increase in RWAs relating to DenizBank. Excluding the effect of the acquisition, RWAs grew by 8%. There was also an increase in Tier 2 capital on increased eligibility of reserves due to a larger credit risk weighted asset base.

On slide 14, we see that, in 2019, Retail Banking and Wealth Management income improved 8% year on year. Net interest income grew by 11% supported by growth in liabilities whilst fee income increased 5% due to an increase in cards, loans and foreign exchange transactions. Loan balances rose 4% and deposits also grew 4% supported by enhanced customer promotions and new product launches. Liv. has now a base of 350,000 customers as new products were extended to the Liv. offering. The bank launched E20, a digital business bank for entrepreneurs and SMEs.

Emirates Islamic delivered an 8% year on year increase in income to 2.7 billion dirhams on higher financing and investment activity. Total assets reached AED 64.8 billion at the end of 2019. Financing receivables grew 4% and Customer accounts increased by 9% during the year. CASA represents 63% of EI's customer accounts. EI's headline Financing to Deposit ratio stood at 83% and is comfortably within management's target range.

On slide 15 we see that Wholesale Banking income increased 2% year on year due to growth in fee income. Fee income of 1.3 billion dirhams increased 7% in 2019 due to higher lending fee revenue and increased investment banking activity. In terms of the balance sheet, Loans grew 8% during the year with strong momentum in lending activity and growth in the Bank's core and short term lending business. Deposit growth of 13% reflect the Bank's aim to maintain liquidity at an optimum level.

Global Markets &Treasury revenue declined 25% year on year as Net Interest Income decreased due to lower interest rates. The Rates and Foreign Exchange desks contributed significantly to a year-on-year increase in fee income by taking advantage of volatility in their respective markets. The Global Funding Desk raised AED 13.3 billion of term funding in 9 currencies through private placements with maturities out to 20 years in 9 currencies. The desk also successfully raised a US$ 1 billion Perpetual Tier 1 earlier in 2019.

With that I will pass you to Patrick for some comments on what we can expect in 2020.

Patrick Sullivan

Thank you, Paddy. Hello everyone. I am delighted to join the bank. Just looking back at its track record over recent years and the achievements of the last year, it was certainly an easy decision to join. And I'm looking forward to working in the Middle East and helping the bank to grow and also looking forward to meeting many of you in person in the coming year. Just turning to the guidance for the year ahead as set out on page 3 of the deck.

Firstly, with NIMs closing 2019 at 2.89%, just over the guidance range, we will maintain the expected range of 2.75 to 2.85% reflecting the softening NIMs in the UAE, as noted by Surya, as the effect of rate cuts in 2019 come through into 2020 along with the impact of a potential further federate rate cut later in 2020. This will be partly offset by relatively higher NIMs in Turkey.

For Costs we will continue to maintain strong control, as our track record shows in recent years, so guidance at 33% remains unchanged. Paddy noted the non-performing loan coverage ratio dropped to 112% with the addition of DenizBank and for 2020 we expect this to be stable. We expect the NPL ratio to increase slightly reflecting challenges from lower GDP growth across the region and we will continue to closely monitor the credit health of DenizBank's loan portfolio.

We will continue to maintain strong liquidity and keep the AD ratio between 90 and 100%. We expect mid-single digit loan growth across our regional network and retained earnings will continue to support healthy capital ratios in the coming year.

So I'll now just hand back over to Shayne for his closing remarks.

Shayne Nelson

Thanks Patrick. I am pleased with the Bank's operating performance and the many strategic initiatives which were positively received by all our shareholders. We will continue to drive efficiencies and capital optimisation across the Group. And as Expo 2020 gets closer, I am confident that we will be able to take advantage the global opportunities across our regional network.

And with that, Molly can we take some questions please? Surya, you had a couple already while she's lining them up?

Surya Subramanian

That came on the web and we can take it up. I'll read the first question that came off the web from Elena at TNI. She asks, what are the opportunities and challenges in the local banking sector for 2020? And specifically what are the drivers of Emirates NBDs growth and pressure points?

Shayne Nelson

Okay, I'll take that one. I think they start with challenges in the industry I think in the UAE; I suppose she's mainly focused on. I think the challenges not just for us, for the whole industry is, I don't think we're gonna see very a significant loan growth in 2020. Loan growth has been pretty muted in 2019 so I think that's certainly a challenge. I think NIMs for banks like us or which we've talked about that have especially high CASA balances as we get US rates being cut. It certainly has an impact on profitability for banks like ourselves with big CASA shares and we are quite interest rate sensitive when it comes to rights falling.

Conversely, if they go up it's actually very positive for us. I think one of the main challenges for the industry is around consolidation. We're just about through our digital transformation project. We're already now around 60% on private cloud, we're close to a 100% private cloud by the end of the year. So our full digital transformation is just about complete and the reason I mentioned that is that I think that the smaller banks are going to struggle to compete with the larger banks that are investing very heavily in digital.

And I think it remains a challenge for them as to where do they focus? One of the opportunities we are getting and drivers of our outgrowth is we're getting growth in market share across our retail products. And that's not because the market's growing, it's just us gaining market share from a pretty stagnant market. If those smaller banks also then try to compete in the larger ticket corporate side, capital is an issue for them and if they get losses that's an issue for them.

In the SME space obviously, whilst you know, important and can be attractive also has its problems as we've seen in previous years where, you know, the industry lost between 7 and 10 billion Dirhams in SME problem loans. So I think one of the challenges for the industry is going to be around the consolidation and where do they play as an industry. And you're seeing now that the 4 major banks, FAB, Abu Dhabi Commercial Bank, ourselves and DIB now are controlling more than 70% market share and yet you've got a market that has around 50 banks in it.

So I think, you know, where these small banks go, I think as for the market is gonna be difficult. Having said that, I think for us, we're out drivers of growth. I think one of the things that we've done as we saw the UAE slowing down the diversification that we've made into Turkey, diversification into Egypt and their growing share in Saudi certainly provides us with opportunities. We'll meet sometimes other costs, an example I'll give you in Saudi, yes, we've got approval to do another 20 branches, but there's a cost of doing that and a lag between cost and an income so it will take us a while to build those opportunities up.

So I think our diversification, geographical reach that we have now, our growing market share in profitable products puts us in a good position against the competition.

Surya Subramanian

Thank you Shayne, I'll take another question that came off the web. And this is probably a question that many of you have asked on the web and will probably ask on the call. Two questions in fact, the first relates to dividend, and there was a question whether a dividend will be announced? And if so, at what level will it be maintained? Or to seek clarity, is the board recommending zero or has the board yet to make a recommendation?

The simple answer to the dividend question is, the board has yet to make a recommendation for dividend for the year so wait for any further announcements on this particular subject. The other topic that was a common topic to many is the reason for increase in waterfall provisions, drivers of the provision, some breakdown between what's happening in Deniz Bank and the group. And I think I will take this first and my colleague Patrick will also add to it.

First of all, I will refer everybody to note 50 page 104 of the financial statements where you will find more detailed public disclosures. And it's fair to say, first of all, to clarify when we took Deniz Bank in quarter 3, we took their loans at fair value. Since then, some of those loans have obviously become 90 days past due and moved into the impaired loans category. So if you look at the slides on credit quality, we had impaired loans of 4.2 billion in quarter 4 against an allowance of about 1.2/1.3 billion.

Of these, 3 billion of these loans are disclosed in our financial statements as credit impaired on purchase POCI as we call it. Which means on the date of acquisition these were already taken in at fair value. So that already includes an element of valuation adjustment. The remaining movement which is about 1.2 billion has therefore an allowance of about 1.2 billion and it's 100% covered.

We do have other subsequent movements in the balance sheet which involves stage 2 movements. And primarily in the main UAE book year over year, there is clearly a change and a shift in expectations of economic indicators of what's happening in the real estate market. And each of these impact the models that drive the expected credit loss calculation for our book. And that also leads to a year over year increase but if you break it up and look at the operating segment disclosure also you would see when you look at year over year, there's almost 900 million of impairment coming from Deniz Bank in quarter 4 which didn't exist in quarter 4 of last year. And the rest of it is the stage 2 movement primarily in the domestic book, some effecting the corporate book, some effecting the retail book.

There's also some confusion relating to income year over year and I think we need to look. If you go to slide 5 you will see that the total income for the bank year over year is up 53% even though the costs are higher and we will talk about that for in relation to a separate question. The pre impairment operating profit is higher by 46%. It is this explanation of the impairment charges that bring down the operating profit almost flat.

The bottom line however is lower because of new things that have come into the P&L for the current year. Clearly in Deniz Bank we are subject to a higher level of taxation than the UAE GCC franchise where we were primarily operating. There's also a delta for the gain on bargain purchase, we had recorded a gain in quarter 3, we recorded a small loss in quarter 4 because we did a clean out of the remaining shares and took the company private for Deniz Bank that is.

And clearly since the sale of Network International, the major income we were deriving from share of profits of associates and for the full of last year doesn't flow through anymore. So there is some delta for all those miscellaneous lines as well which should normalize as we go forward. Patrick, you commented on some guidance for next year, do you want to touch upon the guidance for credit quality and impairment charges in the context of these questions?

Patrick Sullivan

Certainly, thanks Surya for that. And there are a couple of points to note here, like we do see that NPLs will be up slightly from the 5.6% as Deniz Bank NPLs start feeding through into the post consolidation results and the slightly weaker UAE environment. And we were also likely to see lower levels of recoveries in priors. So a combination of these factors, we do then expect the cost of risk to be in 2020 over a 100 basis points. And more likely to be at a level that we have been seeing overall in 2019 but perhaps with a different mix.

Shayne Nelson

Okay. Molly, can you open up the calls for any questions? We have I believe we have two, do we?

QUESTIONS AND ANSWERS

Operator

We will take our first question from Chiro Ghosh of SICO, please go ahead.

Chiro Ghosh - SICO

Hi. Thanks for hosting the call and for the presentation. So I have two quick questions. My first one is related to the operating expense, the cost. So I see that the operating expense is a bit higher this year so just wanted to get a sense why do you still believe that the cost to income ratio would remain at this level? Because this year included some redundancies and some digital transformation, so do you believe these things will again continue next year or is it related to the new branch network that you're planning to expand into Saudi? That's my first question.

And second question is, I don't know whether I understood you right or not. So the operate – the impairment charges went up by 78% in UAE, so that’s excluding Deniz Bank. So if you can throw some more light on why exactly had gone up in the UAE?

Surya Subramanian

Okay. Thank you Chiro. Just on the impairment since we had just talked about it, it's really the movement in the expected credit losses for stage 2 loans as there are changes in the economic indicators year over year. There are of course lower recoveries compared to previous years as well as collateral values also becomes subdued. So that's the dynamic for the impairment charges.

Shayne Nelson

But just remember the GDP models are largely driven by economic indicators, right? So it's what is your expected GDP going to be for the time? Where do you see – what are our regions rate gonna be? What are property processes gonna be? So in the expected loss calculation, it's very much a model on formulas. So if you are forecasting a weaker economic environment, then you will get a natural link for use in the ECL, yeah?

Surya Subramanian

Yeah

Chiro Ghosh - SICO

Sure, that make sense because the NPL number did not go up. Within UAE the NPL number did not go up, that's it.

Shayne Nelson

Yeah, that's what drives them not the number into the financials. And also if you think about what we do is if we restructure any loan that goes from stage 1 to stage 2, say we re profile it, maybe it was a loan that was say for 8 years as a property loan and we went to 12 because they got lower yields, we'd immediately move that to a stage 2, yeah? So even though we are – we've actually re profiled it and the cash flows may or can repay the loan, we for 12 months put into stage 2 and then migrate it back to stage 1 providing it's met all its obligations after the first 12 months. So you get a re – so you get a double whammy of the increased ECO calculation and the movement as you go from stage 1 to 2.

Surya Subramanian

I mean, is it fair to say that IFRS 9 has introduced some volatility in results because of expected credit losses? And they're just into the second year of the cycle, it'll take a few years for everybody to understand how these little bits and pieces interact with ECL.

Shayne Nelson

On – so we can just blame the accountant.

Surya Subramanian

They can blame the accountants. On your question of profits Chiro, I'll make two comments. One, while in certain quarters we have bust our management target of 33%, you'll notice that it has typically been in the 4th quarter when we do ramp up marketing spend. Under normal years, we ramp up Redding, the organization for growing income in the first quarter of the new year. And in this particular year, we talked a little bit more about right, about the redundancies, the amortization of intangibles on the acquisition. The impact of IFRS 16 on leases and so on.

But you'll recall that over all these past years, we have never missed our full year management guidance. So when we do give you guidance that will be coming back to 33, we know where we are taking the organization and what choices we have to make to get there. Clearly, Deniz Bank's own cost income ratio is higher than the Emirates NBD cost income ratio so there will be some averaging out there. But at the moment, year over year, they are a public entity until the last quarter of last year and year over year they have been improving their costs income ratio too.

Shayne Nelson

And there was a link question from Mohammed Al Badri about the redundancies related to Deniz Bank. The answer to that is largely no, the redundancies were the UAE. We're repositioning our cost base for a more difficult 2020 so it was largely out of the UAE that we – our costs. And one of the reasons why you see the increase in costs in the 4th quarter is that, those redundancies which are around 500 people that we took up in the last couple of months of the year.

Yep, I will comment on just like on costs would be that we do envisage we'll start to wind down some of our big IT spend hopefully I should say Inshallah into the 4th quarter as well. So we should start to see some drop in our IT spend as we complete our digital transformation.

Surya Subramanian

So Patrick we have a question for you on what's management's view of cost of risks for the ENBD group for 2020?

Patrick Sullivan

So, well, similar to the earlier comment actually. So we have seen that Deniz is carrying a higher cost to risk particularly in the 5 months since the acquisition. There will be a different change in the mix and we've already commented on some of the slowdown in the UAE as well. And so, and with slightly lower recoveries, we will see with combination of those factors that the cost of risk will be more likely around the level that we have seen for overall in 2019. So it will be a slightly different mix between Deniz Bank and the rest of the banks.

Surya Subramanian

And Shayne, we have one for you. What's management's M & A outlook for the next year?

Shayne Nelson

I think we've got enough to do at the moment Surya, with the getting the Deniz bedded down, dunning out Saudi. But having said that, you know, sometimes all the buses arrive at the same time after you've been waiting for a bus for a long time. We waited a long time for Deniz but we have – when it was nothing in the UAE or anywhere else at the moment though that we were in negotiation before. We would like to bid down what we've got, I mean, if it's a more strategic question, what I would say is we believe we have enough markets. You know, if you think about where we're pushing our growth outside of the UAE, they're in markets like Egypt, Turkey, Saudi with big populations.

So compared to the UAE, strong demographics and improving economics, and certainly Egypt for us in 2019 was a good year. Turkey has performed better than an initial, financial model and Saudi we certainly see huge opportunity there as we grow out at a network there and launch Livs and our digital offerings into that market. We can take some questions from the call please.

Operator

Our next phone question comes from Jagadishwar from Franklin Templeton. Please go ahead.

Jagadishwar Pasunoori - Franklin Templeton

My question going back on the provisions for 2019, I was looking at the note 40 of your annual report where I saw the corporates provision spend of 135 and retail 46% and Islamic 25%. So basically what you are saying was like, that stays to ECL calculations. Just for my understanding, these what are done just because you know, there was delay in payments from these loans?

Surya Subramanian

Yeah. So whenever there's a delay in payment, if it is more than 30 days anyway, you start getting into stage 2 and eventually beyond 90 days you're in stage 3 for sure. So these are definitely stage 2 for a lot of other reasons, mainly economic indicators.

Shayne Nelson

But there's an automatic migration, yeah?

Surya Subramanian

Yeah

Patrick Clerkin

If it's 30 days, this goes straight into stage 2

Shayne Nelson

But we also do have quite long blinds in there that are being restructured. So they're being re profiled, it might've been 8 year loans, gone to 12 year loans et cetera. That will stay there for 12 months.

Surya Subramanian

Yeah. But if it has gone past 90 days, it would be in stage 3.

Jagadishwar Pasunoori - Franklin Templeton

Okay. So can you tell me in the corporate segment, what are the specific sectors had impacted these higher stage 2 provisions? And when you said like collateral values have declined, how much have you declined in these models? As far as I understand their listed prices have declined by 25 to 30% in the last 3, 4 years. But how much did you do take care of that in these calculations?

And another question is, as far as I understand, these IFRS 9 implementation will reduce the volatility of the provisions. Is my understanding incorrect? I know, I mean, you got to this like only year back, you need more time to get into the stable part of this. Can you please explain that?

Shayne Nelson

I'll take the second question because I don't wanna let an accountant to answer it. Because There's no doubt in my mind that that IRFS 9 is credit volatility. You have one line that could be good reasons, moves into 30 days and bounces back. The volatility of that movement from stage 1 to stage 2 can be quite considerable, yeah? Yeah, maybe they couldn't make loan payments because they didn't get paid by someone else for example. Suddenly, you've got volatility that comes into your stage 2 very, very quickly so it's not smoothing out losses at all. If anything, to me it's just creating more volatility in the P & L.

Surya Subramanian

My comment on collateral values was specific collateral, which of course if say last year you had a collateral that was worth a hundred in the property sector, this year it's probably worth less than 85 for example, given what's happened in the property market. So that clearly flows through into your exposure at default as well. The broader movement is really the range of economic indicators.

Jagadishwar Pasunoori - Franklin Templeton

Okay. But have you corrected the collateral values as well when you're looking at this year’s expected assets recoveries? How much was it? Is it like 20%, 30% or in line with the market?

Surya Subramanian

These are specific collaterals also when you look at a loan by loan basis. Also, you had asked about which of the economic sectors that are flowing into the NPLS? I'm afraid we do not disclose that. However, there is some broad range of economic activity disclosed both in the financials. And about a month later when we announce our annual general meeting with the Basel II, Pillar 3 disclosures, there'll be some more information on a breakdown of the loan book by economic activity. You can get some more information there, but it wouldn't link back to the NPL formation via economic activity.

Shayne Nelson

And a corporate property line as supported by independent valuation. So as the valuations come down, obviously that's reflected in the models and loss given default.

Jagadishwar Pasunoori - Franklin Templeton

Okay, great. One last question from my end. Where are you in terms of increasing the FOL to 40%? Are you still on this path and is there a timeline that you guys are thinking?

Surya Subramanian

You'll have to wait for our AGM for that.

Shayne Nelson

Unfortunately, we can't disclose the AGM agenda before it's disclosed to the shareholders would be would be my answer on that. But we, I think we've been pretty clear as to what we want to do.

Operator

We will take our next question from Shabbir Malik of EFG Hermes research. Please go ahead.

Shabbir Malik - EFG Hermes

Just two quick questions from me. There was a lot of news flows which suggest that we're really is getting more active in terms of foreclosures. You know, Al Jaber Group and Infinite investments, there was some news flow around that. I was wondering, is there a reason why there's an increase in activity? Has there been a change in strategy or this is just BAU?

My second question is, Shayne, you talked about a room for consolidation in the market. What do you think is the end game for the smaller banks? How do you think they're likely to, you know, go about this changing landscape? Will they merge with each other or there will be targets for acquisitions from the larger banks? What do you think is the end game for the smaller banks?

Shayne Nelson

I think on the individual cases that are being in the press that have named us, I can't talk about them for obvious reasons, yeah? And you realize that but what I would say is that, you know, when we have Lombard lending to a client, if they hit triggers and they don't make their top pop, we just have an automated process.

On being more aggressive on recoveries, my view there is we always tried to do the best thing by the bank and the client, it's a combination of two. You know we're not in the business of selling out clients easily, we try to work through the problems with them wherever we can. Because in some regards us taking possession of any property, doesn't maximize the value as if the guy sold it on a non-distress basis. We will take action where we don't see a work out that is in the best interest of the bank in the medium to long term with a client. That's how we work, you know, we're here to do the best for all our stakeholders including our clients and we will act where we see it's in the best interest of all those stakeholders. But have we become more aggressive? The answer is no; we're acting as we normally would within our workout parameters.

Second part of this question is on consolidation. On that I think consolidation here from now on is somewhat more problematic just because of the ownership structures. I think the easier ones have been dealt with where you've had common ownerships. You know, Abu Dhabi is obviously consolidated into two or three, I suppose we've added and you know, Dubai, the last big one that they owned a significant stake of the north has gone to DIB. So now, I think the shareholdings become more problematic as to who will sell to who. And given the Emirates ownership of many of, you know, separate Emirates ownership of many of these banks, I think, you know, it's gonna be a bit more difficult for mergers to occur.

Do I think they should occur? Absolutely. You guys are analysts and investors, you know that size and this in especially in retail banking is really important. You need that size, you need that market shift, you need that investment capability. So yes, they should, the quicker they do it, the better. It's better to have a willing marriage than a shotgun wedding so I think, you know, that there should be more consolidation in the market. But I think it's gonna become more difficult now to refill that combination.

Surya Subramanian

Thank you, Shayne. There's a question on the web which I'll read out and between Patrick and Paddy, they will respond. This is further on the NPLS for Turkey, they say on asset quality, unlike other Turkish banks, NPL increased materially at Deniz Bank in 4th quarter. And I was wondering if you expect more and feel pressure there as you reclassify risk assets post-acquisition?

Also, can you provide us with the NPL ratio of the purchase originated credit impaired financial assets from Deniz Bank were added? There is a related question to this from Deepak Babu of the BNH group. Could you please provide some clarity on how provisioning for POCI efforts is carried out? Would it continue to be reported under NPL without requiring provisions against it? Patrick.

Patrick Sullivan

Okay, a couple of components there. I think just for the comparing us to the market and NPLs, I think that might be part of the earlier question where the 4.2 billion NPL stepping up from 0.2 includes 3 billion that was part of the acquisition share value NPLs. And as Surya said earlier, the 1.2 that's left over from that, with – had almost 100% provisioned against that. So that's the management team being very proactive in the provisioning. Nonetheless, we will of course keep an eye on the NPL formation in Turkey.

And the part about what would the ratio of the cover ratio look like if you adjusted for Turkey. Perhaps I can just look at that as a slightly different way. If you stripped out the 3 billion, so it's down, it went from 127% to 112%, and that is the effect of that 3 billion being recorded at share value. So if you strip that out and you can actually do that if you are looking in the notes to the accounts, and that would work out back at 127%. So broadly, a flat level of the coverage ratio if you exclude that 3 billion.

Patrick Clerkin

Okay. There was a couple of, part B and C of Ali bank of America's questions relating to the Deniz bank tier 2 loans and also XQLA risk with their assets for the central bank so I'll take those. Regarding Ali's, referring to the $1.2 billion of tier 2 debt that Deniz Bank had, we have taken over full ownership of that and we are in the process of looking to restructure that to make Deniz Bank's capital stack more efficient. So, approximately $400 million of that will be converted into a common equity tier 1 and we are looking because all the tier 2 is in amortization phase.

We are looking to restructure the remaining $800 million to make that more capital efficient. Regarding Ali's third part to his question. Yes, the cut of standards for government debt have been updated, there is a transition period, 7 year transition period from the 30th of June. And after that only government debt issued in local currency will continue to be 0% risk weighted. Risk weighting will be applied depending on the appropriate credits written for the relevant company.

Shayne Nelson

Just the question also was there around that the asset quality of Deniz's versus other Turkish banks and NPLs, I will just take that. Just in broad context and say you've all followed us long enough to know how conservative we are on risk and on provisioning. And the coverage ratios that we like and that we like to hit out our problems early and Deniz will be no exception to that. That, you know, we like to get in front of the problems and provision aggressively. And that's why, you know, historically we've had the gross coverage of over 125/127% last year and 250%, all over with security. So I think from our perspective, we want to be conservative and we will make sure that we be quite aggressive with the Deniz book as we have always been with our book.

Operator

Our next telephone question comes Vijay Raghavan of Arenco. Please go ahead.

Vijay Raghavan - ARENCO

One advantage of being called last is most of the questions have been asked and answered, especially the impairments have been completely dissected. Let's do questions on the Deniz Bank yes? I could see a 6 months, first half from the 5 months from the date you actually took over. So the full year profit can I say is about 1.2 if it is a rough estimate? That's a significant drop from 2018 full year, which has been disclosed.

Primarily, I guess coming out of the impairment do you see it as a one off or would you have any guidance for Deniz Bank let's say for the year ahead? And my second question will be around the dividends, you said the board is yet to take a call, any dates where the board or the AGM is going to be called for? Thank you.

Surya Subramanian

So Vijay as you know, whenever there's a board meeting, we will make a DFM announcement prior to that. So when the DFM announcement is made, you will know when the board meeting is being held and subsequently the update in the DFM on the minutes of that board meeting as well. So now, I'd say patience on that one.

On your earlier question on Deniz, you have to be a bit careful when you compare the 12 month results with the 5 months' results because Deniz's 12 months' results was prior to our ownership that's prepared under VRSA guidelines which is their local regulator. Whereas our results for 5 months are under IFRS but includes the purchase price adjustments on the acquisition as well. So I wouldn't straight normalize it, but it's fair to say that not just for Deniz but for the whole market, impairment provisions in 2019 are higher than the impairment provisions of 2018 because the crisis hit Turkey only midyear, 2018.

And in fact, I would say after the peak of the crisis, things have been in fact been improving. Interest rates that were at a peak of 24% have now become negative real interest rates. Some of the exchange rates volatility that we saw where at one point it was almost touching seven to the dollar. Now it's more stable at about 5.9 to the dollar in recent times. All of that is giving some comfort to the fact that the future is a lot brighter, although not yet totally out of the woods compared to you could say the latter half of 2018 and the early part of 2019.

Shayne Nelson

There was a question also I think related to that word. It was, I think it was the, around one of these massive lists of questions about the BRSA list of accounts wanting provisioning and how did we go with the due diligence of that? Because this acquisition took so long, we did 2 credit due diligences on the portfolio. On top of that as part of the sales and purchase agreement, as that process was going on, we looked at every large loan or a high risk loan in their book as normal flow. So all that lit a very large list of the VRSA gave banks.

We had 2 accounts that we hadn't picked up on each shoot and they were small that's why we didn't pick them out. They were below the sample size or quite small accounts. So we know the book well, we've had a very good look at it for now. Knowing each from when we've owned it 100%, but with the due diligence, the 2 due diligence plus the flows that seemed like it took forever. What was it? 18 months of flows that we looked at of the book so, you know, we know the book pretty well and we know where the provisions need to be taken.

Operator

Our next question comes from Naresh Bilandani of JP Morgan. Please go ahead,

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Naresh Bilandani - JP Morgan

Yeah. Thanks, just two quick questions, please. One is, could you share some insight into we – you shared the guidance with the group. Just wanted to get some insight on the outlook for Deniz into 2020. I mean, we have seen a pickup in growth and the NIM outlook that is coming from a banking guarantee is sounding much more optimistic for 2020. So any outlook you can provide on 4 key items, which is the volumes, NIMs, cost of risk and cost income ratio in Deniz? Where do you see these 4 key metrics evolving into the medium term? That will be very helpful.

And the second question is just again on Deniz, now that it's delisted, would you still be reporting the – will the bank still be reporting the quarterly financial statements so that we can maintain a separate model for Deniz Bank? Or should we just rely on the segmented information that you provide going forward? Thank you.

Surya Subramanian

Naresh. Let me take your second question first. Although they are delisted and therefore don't have any responsibility under the capital markets board disclosure requirements. Deniz does have public debt outstanding and there are some limited disclosure requirements under those public debt listing conditions. So you will see that and also the VRSA has some requirements although not quarterly around disclosure of financials. So you and everybody else will have access to a reasonable level of Deniz's financials because of these two reasons. However, one of the reasons we went into Deniz and you'd recall Shayne had said even in the early days that we are getting into a market that's counter cyclical to the UAE. We are oil producers, they are oil importers, we've seen in the interest rates cycle also they benefit from lower rates.

Because of our high CASA, we hurt marginally from lower rates and vice versa. So if we start giving you guidance at that segmental level and you run your models on an A plus B basis without looking at the synergies that come with this counter cyclical movement you will have some challenges. At the moment, whatever guidance Patrick gave you earlier was at a consolidated group level. Just one more caution on my earlier comment on Deniz's disclosure, they will be under VRSA basis, not on IFRS basis so you would have to make some adjustments between VRSA and IFRS financial statements.

Operator

We will take our next question from Aybek Islamov of HSBC. Please go ahead.

Aybek Islamov - HSBC

I think I just wanted to ask you about one point. Given now that you're present in Turkey, how are you planning to manage your capital let's put it a dividend policy given the volatility in Turkish Lira? So yeah, if you can sort of give us some light about your dividend policy post acquisition of Deniz Bank that will be very helpful. Thank you.

Surya Subramanian

Our dividends I think have always been a shareholder call at the AGM. So as management, we've never talked about a policy. I fully take on board your point that there will be some volatility in the Turkish later leading on to potential pluses and minuses on the group's equity through the translation. But you will notice that our capital ratios and our core equity is quite at an enhanced and high level. So there are buffers to support any dividend payouts, certainly the historic dividend payout.

Shayne Nelson

There's no escaping given that the Turkish market has significant amounts of foreign currency loans and that the core capital is in Turkish Lira that any large fluctuation in the Turkish Lira does translate into the consolidated capital numbers. So, you know, we are very mindful of that when we are modeling, when we made the acquisition and also the capital that we hold.

Operator

Our next question comes from Abdulla Al Tuwaijri of NCB capital. Please go ahead.

Abdulla Al Tuwaijri - NCB capital

A couple of questions from my side. First of all, are you expecting any regulatory changes in the coming 2 years? Secondly, if you can give us or shed a light on the real estate outlook in the UAE from your perspective? And if you can provide guidance on the targets at the LDL levels or the – and the targeted normalized cost of risk. Thank you.

Shayne Nelson

I think it depends which market we're talking about as opposed as to regulatory changes. The one thing I do know – – there's so many in every market that we operate in and may continue to evolve. For our main macro I suppose UAE, the one that is currently in drop form is around the real estate ratio. And, you know, that's an important one for our forecast both from a capital perspective and from a business perspective. So that might link into your question about what our outlook is for property. I'll give you my personal view, we don't have a bank view. We don't do property coverage as part of our research.

I'll give you my personal view, I think with – and I think this has been covered in the press quite a bit so there is considerable supply in 2020 coming on, there's supply coming in 2021. It's fair to say the government's doing a good job of now containing that supply coming in but the reality is that supply needs to be finished. You can't have a half complete residential tower so supply needs to be complete. I think we're gonna get some stabilization in prices once that supply pipe it comes through. I think it's probably going to be 2022 when we get that stabilization. I think we're gonna continue to get rental and property price pressures until we get that stabilization. And I think the government's doing a good job of doing things like long-term basis, attracting more people to invest here.

And also obviously managing that supply by restricting government linked company's development side. We've got some good positives, obviously we are hopeful that Expo 2020 will bring some more property investors into the country. But I think the overhang of supply I think is gonna dampen prices until we get through that pipeline.

Surya Subramanian

And, Patrick there was the final limb of the question for you, which I think it covered earlier but important to reassure again what is the outlook for NPLs and cost of risk?

Patrick Sullivan

And let's see, within the presentation you could see the ex Deniz Bank, the NPLs had been quite stable over the last 5 quarters. And we are guiding that there will be a slight increase in that given the slowdown in the economy and coupled with the risk that, you know, some of the stage 2 loans become NPLs as well. So I think, as I said before, we'll also make sure we're vigilant about the formation of the Deniz Bank nonperforming loans and the proactive provisioning that management's taken against that.

Surya Subramanian

Thank you. There are a number of questions on the web, which we haven't individually answered but they touched upon the themes of provisions in the UAE and Turkey. So if anybody feels that their specific questions has not been responded to, please write into us through investor relations.

Operator

We have no further questions on the line at this time.

Shayne Nelson

We thank you very much for joining us on today's call. Always a pleasure to get some good questions from you guys and we will talk to you next. But it'd be remissive of me not to thank Surya for 9 hard years …

Surya Subramanian

Thank you Shayne.

Shayne Nelson

Helping us through when it was pretty difficult times in Dubai to build the bank to where we are now. So thank you very much Surya for 9 years of hard service. We will miss you, but maybe not as much now that we've got Patrick. So we welcome Patrick and look forward to Patrick providing the same level of competency and transparency that we always have.

Surya Subramanian

I wish you and Patrick, Paddy and the team all the best, Shayne.

Shayne Nelson

Thank you, Surya. Thank you Ladies and gentlemen. Thank you for joining us.

Operator

Thank you. For any further questions, please contact our Investor Relations department whose contact details can be found on the Emirates NBD website and on the results press release. A replay of this call and webcast will also be available on the Emirates NBD website next week. Ladies and gentlemen, that concludes today’s conference call. Thank you for your participation.

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