EMIRATES NBD H1 2024 RESULTS ANALYSTS & INVESTOR CONFERENCE CALL & WEBCAST
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CORPORATE PARTICIPANTS

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Operator

Ladies and gentlemen, welcome to the Emirates NBD results call and webcast for the first half of 2024. Today's call is being recorded. Please note that this call is open to analysts and investors only. Any media personnel should now disconnect. I'll now pass the call over to our host, Mr Shayne Nelson, Group CEO of Emirates NBD.

Shayne Nelson

Thank you, Lydia, and welcome to our first half results call. We have built upon the very strong performance in the first quarter to deliver a record profit of AED 7.1 billion in the second quarter of 2024. This gives an overall first half profit of AED 13.8 billion, up 12% year-on-year. There are many highlights in these outstanding results. The record profit in the first half was driven by a 6% increase in lending, as our loan book reached the half a trillion dirham milestone and substantial impaired loan recoveries. Quarterly profits surpassed AED 7 billion for the first time ever, helped by the strongest-ever results from Emirates Islamic, improving margins in DenizBank and sizeable recoveries bolstered by a buoyant economy.

All business units achieved an outstanding performance in the first half. Retail grew its loan book by 16 billion in the first half, commands a one-third market share of UAE credit card spend, and grew assets under management by an incredible 41% over the last year. Corporate lending originated AED 48 billion of gross new loans in the first half, securing landmark deals across the network as it leverages the group's growing regional presence. Emirates Islamic delivered a record profit of 1.7 billion in the first half, as its balance sheet surpassed AED 100 billion and now serves over 700,000 customers.

Global markets and Treasury broadened investment opportunities for our customer base, offering fractional bonds and sukuks through ENBD X in accessible denominations. DenizBank delivered an AED 800 million profit, providing fresh funding to the Turkish economy, and the balance sheet grew to over AED 160 billion. We're now seeing real benefit from our branch operations in KSA, with a tremendous 33% loan growth in the first half, as the branch network doubled to 18, with several more branches scheduled to open in the coming months. Loan growth guidance has been revised upwards on strong regional demand, our cost of risk guidance was positively revised downwards on a healthy credit environment.

Net interest margin improved to 3.65% in the second quarter, as DenizBank's NIMS, increased on favourable loan pricing and stable funding costs. Moody's improved the outlook on Emirates NBD's credit rating to positive. Generative AI is being implemented across our businesses' operations in partnership with Microsoft. The advanced analytics initiative has now 50 use cases right through from the incubation to scaling phases, spanning every business unit and control function, with a focus on customer experience and improved efficiency.

We are the first UAE bank to publish our climate strategy through an assured TCFD report. Green fintech companies are being empowered to develop innovative solutions and support a climate resilient future through our Global SustainTech Accelerator Programme. Retained earnings have boosted capital ratios, and the rock-solid balance sheet, coupled with market-leading banking infrastructure, makes Emirates NBD a regional powerhouse to continue driving future growth.

In summary, the group continued its strong and consistent performance to deliver a record quarterly profit. We have excellent IT infrastructure and a regional presence, which position us very well to keep delivering profitable growth. I'll now hand you over to Patrick to go through the results in more detail. Patrick.

Patrick Sullivan

Thank you, Shayne. And a very good afternoon to all of you. Just to reiterate the strength of our results for this first half, all business and product lines continue performing very well. NIMs are improving in DenizBank, and we have seen strong impairment recoveries. And as such, we are upgrading two key guidance metrics, loan growth and cost of risk.

Let me first take you through the summary results table, then dive into a bit more detail by component. Starting with the performance summary there on page two, you can see our business momentum from the first quarter has continued into Q2. The group's ongoing investment in the UAE and the region is delivering at both the top and bottom lines. Total income of AED 21.4 billion in H1 is up year-on-year, and income is also up 1% quarter-on-quarter. Within that, net interest income increased 6% year-on-year on the back of a 15% increase in assets, which more than offset margin contraction.

Quarter-on-quarter, NII was up 7%, helped by loan growth and an improvement in margins in DenizBank. As usual, we've split out the contribution from ENBD and DenizBank in the appendix, that's on page 11. From a volumes perspective, retail lending grew very strongly, with 14% growth in the first half, and corporate delivered 7% loan growth, with 48 billion of new origination throughout the region.

Non-funded income is lower year-on-year, but client and trading flow income is growing steadily, and the decrease relates to more variable non-client income, which I'll go into in a bit more detail shortly. Costs have increased 12% year-on-year, supporting strong business volumes, particularly in retail. The accelerated investment in digital and our international network, in addition to the inflationary impact of DenizBank’s cost base.

The cost-to-income ratio at 28.6% however remains well within guidance. We have registered an impairment allowance credit in the first half of 2.2 billion dirhams on the back of cash repayments and recoveries. As a result of the strong credit performance, we have lowered our full-year cost of risk guidance to a 0 to 20 basis points credit. More detail on that shortly. This gives us a very strong profit before tax and hyperinflation of AED 17.5 billion dirhams and 13.8 billion bottom line profit, which is up 12% year-on-year.

In the bottom summary table, you can see the balance sheet metrics are in great shape, with total assets and deposits both growing by double digits year-on-year on strong underlying business momentum. Finally, capital and liquidity metrics remain robust.

Just turning to net interest margins, on slide three. The bottom left chart shows that margins tightened by 37 basis points year-on-year due to higher funding costs, increased cash reserve ratios, and competitive loan pricing at Emirates NBD. NIMs improved 13 basis points in the second quarter to 3.65%, as shown in the bottom right chart, and are now within the guidance range. There is a small net impact of ENBD's margin with the increase in the cash reserve requirement. But DenizBank is the primary driver for higher margins due to loan repricing feeding through and stabilisation in deposit costs following the sharp Turkish rate hikes.

We have maintained our guidance on margins at 3.6% to 3.8%, although ENBD's NIM was 6 basis points lower in Q2. We're not expecting it to drift too much lower, but will depend on CASA and Fed rates. We signalled last quarter that we expect DenizBank's NIMs to widen in the second half, averaging 4% to 5% this year, and we are now seeing signs of that. This remains our expectation. The two variables to keep in mind are, first, reduced access to cheap swap funding from the Central Bank in Türkiye, reflecting the country's improved cash reserve position, which could lead to higher funding costs. And secondly, the potential for rate cuts in Türkiye, given the favourable June inflation print, with inflation expected to fall further in the second half. Although we have not factored in rate cuts in Türkiye before year end, any such move would be positive for margins.

Moving on to slide four and non-funded income. Fee and commission income is up 64% year-on-year, and up 10% quarter-on-quarter, with a solid trend in quarterly growth across almost all of the group's customer driven businesses. The increase in fee income, as per the bottom left chart, is from substantially higher investment banking activity, increased loan volumes, higher retail card spend volumes at both ENBD and DenizBank, with the added impact of higher interchange rates in Türkiye.

Brokerage and asset management income increased in the second quarter, reflecting the growth in AUMs. Now, we have reconfigured the other operating income chart at the bottom right to make it easier to determine and emphasise the amount of client income. Other operating income has a stable client and trading flow income component of around AED 1 to 1.2 billion per quarter. Non-client related income was lower year-on-year and quarter-on-quarter due to higher swap funding costs in Türkiye. There was also higher mark-to-market gains in the second quarter of last year, coinciding with market volatility around the election time.

On slide five, we see that gross lending increased 6% during the first half. Retail had its strongest-ever half year, adding 16 billion in loans. Corporates also had a very strong half of 48 billion in gross lending. There was also strong financing demand in industry sectors, such as trade, transport, and communication, utilities, and conglomerates throughout the region, which more than offset sovereign real estate and other scheduled repayments. DenizBank has strong loan growth, up 20% in local currency terms, and 8% in AED, with regulations favouring a pivot toward sectors such as agriculture. KSA is benefiting from the network expansion, registering an excellent 33% loan growth in the first half of 2024.

Now we have revised up full-year loan growth guidance to high single digits following the strong loan growth in the first half, the continued positive economic outlook and further announcements on infrastructure investment. We are, however, mindful of a fair amount of loan refinancing in the second half, competitive loan pricing in the UAE, given the abundance of liquidity, and our disciplined approach to pricing for risk.

On the liability side, total deposits increased 39 million, up 7% in the first half. Within that, CASA and time deposits up by a roughly similar amount. In the second quarter, there was a clear preference to time deposits. We have been signalling for some time that we expect to see this shift. And as you can see, that since Q2 2023, that has been the overall trend. We have added 47 billion of term deposits against a net 8 billion of CASA in ENBD ex DenizBank since this time last year. Yet, CASA, as a percentage of total deposits, remains very healthy at 59% for the whole group.

On slide six, we see that the NPL ratio improved by 0.4% to 4.2% in the first half, reflecting the continued trend of strong recoveries that we've seen in recent quarters, and an increase in the lending denominator. On the bottom right, you can see that the stage 2 loans also improved by 0.9% to 4.4% during the first half, as a result of repayments and staging transfers. Overall, this has contributed to a 2.2 billion cost of risk credit. As ever, our recovery team works hard to clear legacy loans. There may be some further recoveries to come through in Q4, but the most substantial recoveries have already occurred.

As a result, we have revised our cost of risk guidance to a 0 to 20 basis points credit for the full year. Now, this implies a second half cost of risk charge of around 70 basis points, as we start to see normalisation of the cost of risk. Having said that, from time to time, we can get recoveries sooner than expected. Now, as I just mentioned, our NPL ratio is 4.2%, just drilling down by vintage. There is nothing over ten years old, and around 4 billion is five years or more. If we were to write these off, the NPL ratio would mathematically improve to around 3.6%, with no material P&L impact. Paddy will now take us through the remaining slides.

Patrick Clerkin

Thanks, Patrick. On slide seven we see that the cost-to-income ratio at 28.6% is comfortably within guidance, as continued acceleration of investment for growth is supported by existing income levels. Staff costs increased to drive strong business growth, invest in human capital for future growth in digital and international, including the branch expansion in KSA, coupled with an inflationary impact from DenizBank's cost base. IT costs increased year-on-year, as we continue to invest in our market-leading technology solutions. We expect this year's cost-to-income ratio to be closer to the 30% area.

Slide eight shows that the group maintains very strong liquidity, with an AD ratio of 76% and an LCR of 199%. We've refinanced AED 20 billion of term debt and sukuk in the first half, including a $2 billion syndicated loan and a $750 million debut Sustainability Sukuk from Emirates Islamic. DenizBank significantly upsized their one-year syndicated loan with 178% rollover to nearly $1 billion in June, attracting 20 new lenders and 42 participants. The bulk of the remaining maturities in 2024 is DenizBank's one-year syndicated loan in the second half of the year.

Slide nine shows that the Common Equity Tier 1 ratio strengthened in the first half to 15.4%, as retained earnings more than offset the 9% increase in RWAs. The increase in credit risk RWAs is from the strong retail and corporate loan growth. The group continues to operate with very comfortable capital buffers.

On slide ten, we see that RBWM income improved 12% year-on-year, with the highest ever revenue, strongest ever loan acquisition, and a substantial growth in balance sheet. We enjoy a one third market share of UAE credit card spend, as card spend grew 15% year-on-year. AUMs grew by an impressive 41% year-on-year, reflecting ongoing success of our wealth management strategy. CIB achieved an excellent 64% increase in profit before tax on higher income and increased recoveries.

Non-funded income grew 21% due to higher lending, a strong contribution from investment banking, and improved cross-sell. Corporate lending grew 7% in the first half, with strong growth in trade, transport, communication, utilities, and multinationals, which more than offset sovereign, real estate, and other scheduled repayments. CIB managed to continue to grow CASA, backed by group's market-leading and best-in-class digital escrow capabilities, including APIs and virtual accounts.

Global markets and Treasury delivered another solid performance, generating AED 1.3 billion of income in the first half. Net interest income continues to be strong at 1.4 billion, despite the general increase in cost of wholesale funding and term deposits due to higher interest rates. Sales delivered strong results, driven by an expanded product offering and new, innovative, structured solutions for clients. Fractional bonds and sukuk are now available through ENBD X, broadening investment opportunities for customers.

Global markets expanded the suite of commodities now actively available for customers. DenizBank delivered an impressive AED 800 million profit in the first half, providing fresh funding to the Turkish economy, as their balance sheet grew to over AED 160 billion. We do have a couple of extra slides in the appendix containing more granular detail and a dollar convenience translation. But with that, we can now open up the call for questions. Lydia, please go ahead.

QUESTIONS AND ANSWERS

Operator

Our first question today comes from Shabbir Malik with EFG Hermes.

Shabbir Malik – EFG Hermes

Hi. Thank you very much. I have a couple of questions, please. Your NIMs in the first half is currently around 3.59, 3.6%. Your guidance is pretty wide, about 3.6 to 3.8%. Where do you expect the bank to end the year in terms of NIMs? Do you expect it to be within somewhere in the middle of this range? And what are the variables that you think can change this outcome? That's one.

The other one is on fee income, and thanks very much for providing some extra colour on non-interest income between client related and non-recurring other income. But are there any elements of one-offs in fees this quarter? Because that was very strong in 2Q versus the previous quarter and even last year.

And thirdly, your NIM sensitivity to rate cuts is quite high. How do you plan to shield yourself from the headwinds of potential rate cuts this year and next year?

And finally, is there any update on the sale process of IDBI? Have you been given the green light from the central bank over there to participate in this bidding process? Thank you.

Patrick Sullivan

Shabbir, Patrick here, welcome. Thanks very much for joining the call. Thanks for those questions. Maybe I'll just take the first three and then hand over to Shayne for the last one.

Just on the NIMs, you're right, we're at 3.59% so far, so we're just right at the bottom end of the range. You may recall that we had to revise the range at Q1, after the sharp increase in the Turkish interest rates. Even at that point in time, I think our overall margin was about 3.52%, so we we're below the range. You can see that we've actually made some good progress through the second quarter with the NIM at 3.65% within that range.

The main variable is going to be what happens in DenizBank with the tightening of monetary policy. The rates are at 50% now. One thing that's been happening there is the cost of funding goes up a lot faster than the repricing of assets. We have started to see the repricing of assets, that just takes longer than the repricing of the deposit side.

And from the ENBD side of things, there are just a couple of variables that could affect us there. One being the Fed rates, depending on the timing, that story can change, but we have made the assumption of a rate cut in September and one in December. That really won't be so material for this year, more something for next year. The whole point in giving a range is, there are a number of variables where NIMs could go towards the higher end or stay nearer the lower end, and that will be more a function of what's happening within monetary policy tightening and the impact on Deniz.

The second one, asking if were there any one-offs? No. It was particularly strong quarter and a strong half. There's been a lot of activity in the market. Sometimes even if you have larger transactions that go into the overall P&L and there's nothing really there that we would call out as exceptional or lumpy that affects that overall good trend of growth of client income that we have there.

Just on the NIM sensitivity, have we done anything to protect ourselves from rates falling? Look, broadly, we are a floating rate bank. As rates go up and down, so does the income on the asset side. But with the strength of our CASA part of the portfolio and our low cost of funding, we are more sensitive, perhaps, than others. But in the meantime, we haven't left any shareholder value on the table because we optimise the earnings with that low cost of funding. There are certain things you can do, whether it's in the Treasury book of extending the tenor to lock in higher yields for longer. That's really just tinkering around the edges in many respects. We do provide quite a lot of information in past calls and in our annual accounts on what that rate sensitivity is, so you can model that quite well.

Shayne Nelson

I would add on to that, Shabbir, that you can see that loan growth where it is, and our guidance for loan growth. And one of the offsets, obviously, for us going into a lower rate environment is bulking up. We have been driving loan growth quite aggressively because we are taking market share, and that is as we position ourselves for lower rates in 25 and 26. And we've been doing this for quite a while, as you know, bulking up. And having to offset against the sovereign repayments that we've had, which, as you know, have been quite substantial. It has been a strategy for us to get loan growth up a bit.

On acquisitions that you mentioned, I won't mention any one name, but I would say there was another question on the dashboard similar to this. That one was around what are the attractive markets for M&A? And I'll just stick to what we've said many, many times. Our strategy with acquisitions is to go deeper, not wider. And that means for us, our existing territories, so Saudi, Türkiye, Egypt and India have been on the table for a long while now. All of those that at the moment we're growing organically. But inorganic, if the right deal comes up at the right price, we are interested and we have the capital and we have the liquidity. We are looking, but I would just reiterate, in 12 years, we've done two deals. So, it's not as if we're doing one every five seconds. For us, we look at a lot of transactions, we deliver very few, and that is largely because we walk away if we don't believe we can generate value to our shareholders in the medium to long term.

Shabbir Malik – EFG Hermes

Thank you. Just maybe a follow-up on the NIM response. The upper end of the guidance would require interest rates in Türkiye to start coming lower, or is that what's driving the upper end of the guidance?

Patrick Sullivan

To be in the mid of the range, the margin in Deniz would need to be within the 4 to 5% range. They were at 4.44% for Q2, so they're in the range, but I need that average for the full year, so I still need some more upside through the second half to get an average in that range of 4 to 5%, and then we'd be in the middle of the range. There are a number of variables that may mean it's either side of that midpoint.

Shabbir Malik – EFG Hermes

Got it. Thank you very much.

Operator

Our next question comes from Naresh Bilandani with JP Morgan.

Naresh Bilandani – JP Morgan

Thank you. It's Naresh Bilandani from JP Morgan. Congrats on a great set of results. Just a few questions, please. One is, could you please share some more insight into the strength in the Turkish NII? This is contrary to what the peers are seeing or guiding. Our recent meetings with the Turkish banks, and also from the results from some of peers, indicate that the NIM in Türkiye was expected to be under pressure in the second quarter and probably also going into the third quarter. I'm just keen to understand, how were you able to achieve the strength in the Turkish NII? Some more colour there would be very helpful. That's one.

The second is, could you please share what sectors or accounts are actually driving the provision reversals here? Am I right that these benefits are being accrued mainly from early repayments? And I guess there's no change in the impairment assumptions or changes in the outlook, which is leading to this benign impairment charge. Any further colour that you can share there would be extremely helpful.

And my third and final question is on the loan growth guidance, which, of course, now we've already seen 7% year-to-date. You're guiding high single digits. I'm just trying to get a sense, are you really forecasting any sizeable repayments to come through in the second half? Or is the pace going to materially slow down? I'm just trying to get a sense if this is just a conservative expectation and this space can easily move into double digits as we go into the second half of this year. Any thoughts there would be super helpful. Thank you.

Patrick Sullivan

Thanks Naresh, welcome. So just on the NIMs in Türkiye, it's mainly about the repricing of the loan book in Turkish Lira. When the rates went up to 50% the cost of funding went up to a range of 40-50% depending on timing. There is a preference for one and 3 month time deposit there so there is relatively little CASA. So that goes up very quickly and then you can actually reprice up asset. There are some limits on growing the portfolio so if you were able to grow the portfolio rapidly in an expanding economy, then you can get a faster repricing with that new origination. But with the lending limits that means that does take longer to reprice the book.

Shayne Nelson

There are macroprudential controls around loan growth in Türkiye, limiting growth of 2%, with some sectors that are actually exempt from it. Agri is one sector that we've always been big in, in Türkiye that is actually exempt from that growth.

Patrick Sullivan

That is one sector that has been growing. And when you grow that, you can actually reprice more quickly. I can't speak for the other banks. Another variable in there are the CPI linkers as well. The second quarter was a pretty high inflation level, that's topping out around that 70 to 75% level. With higher inflation, that just means you also get a higher yield on your CPI linkers, so that did help somewhat. That's just the overall trend we've been seeing month by month. And so, we do see that as a positive.

But there is one thing that is potentially slowing other banks down as well, and that is the sharp increase in the swap funding costs. When you swap euros or dollars into Lira with the Central Bank, the Central Bank has less need for foreign currency than they did before. There is not as much of that swapping to local currency going on. That was historically a good, cheap source of funding of Lira, and that might be something that's putting pressure on the other banks' margins as well. But that is not so much the case for us. It does impact us, but the others may be more affected by it. That's on the Turkish margin side.

Just on these factors for impairment, the actual collateral recovery that's being sold is substantially connected to realising property related collateral, in a very buoyant market. Now's the time to be able to realise that, and it's very realisable as well. It doesn't mean that is from all the property sectors. There are some legacy loans that were connected to the construction or property sector that it relates to, but not all of it.

Actually, around half of the net recoveries, and I think if you look at our notes, the accounts where we spell it out more clearly, around half the recoveries, and it's probably a net 3.3 billion or so for the half. About half of that is coming from stage two cash repayments, where customers or clients that have been in stage two have fully repaid or perhaps refinanced, and therefore, any provisions against that can be released, so that's a cash recovery as well.

Shayne Nelson

I just would add to that, Naresh, is that if you look at the stage two coverage that we've had, or we still have, some of that is specifically allocated to certain counterparties where we see the risk as higher than others. And our stage three coverage means that our stage three loans are just about an income generating asset now because of the coverage. And for stage two, we've had quite a lot of repayments and refinancing. And again, they've led to quite a lot of releases in that portfolio.

Our conservative provisioning that we've built up over many years is really coming into play. And I hear when I read some of the analysts, maybe it's not a great beat because suddenly a significant part of it's come out of the provisioning side. But, hey, we took the provisioning, right. No pain, no gain. And we took it all upfront, and now we're getting it back. We didn't get many kudos when we took it up front, and we don't get any kudos when we recover it, so we sort of can't win here.

Patrick Sullivan

Naresh, on your third point, just around loan growth, we are at 6% year-to-date, and we are guiding to high single digits. We are always quite cautious about that pace of loan growth. There are probably two components. One is DenizBank, just with the tightening monetary policy, there could be more of a slowdown in overall growth. They grew their loans by about 5 billion in AED equivalent in the first half. Whether we can repeat that, we need to manage risk, we're not going to put that all into agriculture. So, that's one factor. But also, we do have Government of Dubai and sovereign repayments that have been coming through. You may recall, there was around 30 billion repayments in Q4 last year, about 10 billion in the first half this year. And so, that can be factored in as well. The government's finances are in very good shape, so if they had surplus funding, that can, from time to time, be used to repay any of that debt. We're a little bit cautious on it. If it slips into double digits, it's not going to be massively higher double digit.

Naresh Bilandani – JP Morgan

Understood. Thank you, Patrick. Thank you, Shayne. Thanks a lot for the colour.

Operator

Our next question comes from Rahul Bajaj with Citi.

Rahul Bajaj – Citi Group

Hi, this is Rahul Bajaj from Citi. Thanks for taking my questions. Two questions, basically, from my side. Sorry, I'm repeating again on DenizBank margins. I just wanted to understand, if you could give us a sense of percentage of, for example, the loan book, which has been repriced and what is spending, to give it a sense of how much of that yield expansion can we expect, specifically in DenizBank, if rates do not change? Because my assumption is that cost of funding increases are already done in Türkiye, so if any margin expansion that would come in 3Q will come on the back of these loan repricing. If you could give us a sense of are we in the middle of the repricing, at the start of the repricing cycle, or just towards the end, something like that, that would be useful.

My second question is around provisions. There's been some chatter around this new regulatory rules on provisioning, which we could necessitate banks to amortise the collateral that they hold on NPL over a period of time. And eventually, basically lead to higher provisioning in the UAE over a longer term. Have you seen the graph? Have you had these discussions? What are your initial views on this kind of new regulation? Thank you.

Shayne Nelson

We certainly can't comment and pre-empt the regulator on regulations. We did, in the commentary, make some comments about that we have written off past ten-year NPLs, and we did make some comments that, if we wrote off everything over five years, that our NPLs would drop down to around 3.6%, and that the P&L effect would be immaterial. That's all we can say.

Patrick Sullivan

And then, Rahul, just to your Deniz margin part. It can take four to six months to reprice the asset book. The last rate hikes happened around March or April, including the unexpected extra 500 basis points. I would say we're maybe two-thirds to three-quarters of the way through the repricing on the asset book. Obviously, in a book you've got a range of tenors from three months repricing on the corporate side to, say, personal loans that might be three, four, or five years. It's a bit of a blend overall, but generically, you'll get most of your repricing through, with the biggest effect within six months. It's only been one quarter of that, so through Q3, we would see more of that repricing coming through. And there has been a stabilisation on the funding side as well, so we still see there's positive upside from that. Hopefully that answers that question for you.

Rahul Bajaj – Citi Group

Thank you. That's perfect. Thanks, Shayne, Thanks, Patrick.

Operator

The next question comes from Ashwath PT with Goldman Sachs.

Ashwath PT – Goldman Sachs

Thank you. Congratulations on your results. I've got two questions. The first is on the cost to income, some positive trends, it's quite below the 30% that you are expecting for the year. I just wanted to understand, in terms of that 30%, do you expect some more in terms of investment in the digitalisation front and/or inflationary pressure in Türkiye to lift that up towards the end of the year, towards that 30%? Or, put it in a different way, where do you see the cost to income settling over, say, the medium term for Emirates NBD?

The second question I have is on the capital allocation front. With the strong results, boosting internal capital generation for the business, and assuming, like you said, if there's nothing on the front of M&A, could we actually see more of this capital in terms of capital returns to the shareholders in terms of higher dividend payouts? I understand it's a board decision, but I wanted to understand your thoughts behind that as well. Thank you.

Patrick Sullivan

Ashwath, welcome. Just on the cost-to-income ratio, we're at 28.6. Our actual medium, long-term commitment is to keep the cost-to-income ratio lower than 33%. That's the actual guidance. But to be more helpful, we've given verbal guidance updates indicating that we'll be around the 30% mark for the year. We are continuing to invest, as we invest in CapEx, you get the amortisation starting to come through. We have been building out the branch network in Saudi Arabia, and that amortisation and the cost base of that starts coming in.

ENBD is actually relatively stable in that sense, and quite predictable. DenizBank does also have an inflationary element that we're seeing coming through, where Turkish Lira inflation is higher than the rate of FX depreciation that we're seeing. It's not been fully offset in AED terms by FX depreciation. That will increase the cost-to-income ratio a bit further in the latter part of the year. But stepping back, we still will be at or around that 30% mark. By any corporate metric for a bank, that is a very good, low cost-to-income ratio.

Shayne Nelson

On that one, for your model purposes, just take note of the cost base that we normally have in the fourth quarter as well for your model. Because traditionally fourth quarter for us, there's a lot of annual expenses that lands in the fourth quarter. And for modelling purposes, just remember that when you're actually modelling it.

Patrick Sullivan

And just on capital allocation, we are very capital generative. I think we generated about $1.3 billion in the first half, adding to the overall capital base. That just means we have a strong CET1 ratio, it does not mean we will go and spend all of that. I think, also, we have demonstrated in the past that we have listened around the dividend. And last year, the dividends was 100 fils plus 20 fils celebrating the 60th anniversary. That was a substantial increase on the 60 fil dividend that we had the year before, i.e., double.

And Shayne was talking about any corporate acquisition activity. These things don't happen overnight. Things aren't there on the supermarket shelf, these things take time. It would be premature, very much so, to be talking about capital returns, other than how we assess our dividend each year, which is an annual board decision.

Shayne Nelson

The other thing I would just add, Ashwath, I talked earlier about the question was about how do you keep earnings up in 25 and 26, as rates are falling? And we talked about one of the things that we've been doing is aggressively backfilling the sovereign repayments and aggressively going after loan growth and taking market share. Which is what we have been doing. Unfortunately, there's no free lunches, and that also has RWA implications. You will see that we've had quite a big RWA growth in the first half on the back of that loan growth. And also, you remember that the sovereign had zero risk weight, so it's backfilling with largely 100% RWA lending. There is an offset for us when it comes to capital as well and with the loan growth rates that we've been seeing, it has been eating quite a bit of capital, rather than it just being a free ride on capital that we had with sovereign lending.

Operator

Our next question comes from Chiro Ghosh with SICO Bank.

Chiro Ghosh – SICO Bank

Hi. This is Chiro Ghosh from SICO Bank. I have just one last question on Türkiye. I just want to get a sense on the four key parameters, and how would those get impacted if interest rate remains at 50% and inflation around 65 to 70? Net interest margin, asset quality costs and loans, so net interest margin, very clearly explained what will be the impact. I want to get a sense, how would the asset quality and the cost and the loan growth in Türkiye would remain going ahead if we assume that the interest rate remains at current level? That is my first question.

And second one, also, very quickly. How are you seeing your other international growth plan? Of course, you cannot comment much on the inorganic plan, but organically, how are you seeing those? These are my two questions.

Shayne Nelson

On organic growth, I think Egypt has been growing quite well in pounds, but obviously, the devaluation of the currency there has affected it. Now, I think the good thing about Egypt is we're not seeing the inflation impact that we thought we'd get from the devaluation, and we're getting a stabilisation of the currency there, so that's good from an organic growth perspective in Egypt going forward.

Saudi has been doing actually extremely well. And I think from a revenue perspective, that would be as big as Egypt, if not this year, certainly next year, from a top line perspective. We're quite happy with, as we said earlier, massive loan growth there. And it's not just corporate, retail's been doing very well as well. We're very happy with how Saudi’s doing, it's growing very well, and it's basically given us another Türkiye when it comes to revenue now. So, happy with that organic play. Obviously, the cost-to-income ratio in Saudi is not where it will be in the future, because it's still in the expansion phase, as we open more branches and headcount, and technology, etc., that needs to go into these new branches. But very happy with where we are in Saudi on organic growth.

I think India is still quite small for us, but India for us is as important when it comes to its contribution in the Gulf region, even our London office and our Singapore office. India, for us, feeds a lot of pieces of our network, so that's doing very well. And more organic growth in India, more branches, I'd be quite in favour of that for sure.

Patrick Clerkin

Thanks, Shayne. Chiro, just on the margins at DenizBank. If you look at the appendix, you'll see we do break out ENBD excluding DenizBank and DenizBank margin. And you will have seen that DenizBank's margins were quite high. In fact, they touched around 9% before interest rates started to rise. Then margins were down as low as 3.3%, and in Q2 have widened to 4.4, so 114 basis point widening in Q2. And Patrick explained that very clearly when he said that the loan pricing had effectively caught up with the rate raises.

And you were then asking about what happens if we stay at 50% interest rates and have high inflation? The guidance that we've given, we actually assume no further rate cuts this year. Any rate cuts that we get in Türkiye would actually be positive for DenizBank. But you can see that the Q2 margins was around 4.44%. And we had signalled that that's now in the range to meet our 3.6 to 3.8% guidance. And if there is rate cuts, then we will benefit more from those. If there's no rate cuts, then that will drive whether we trend towards the high or the low end of the guidance.

Chiro Ghosh – SICO Bank

The net interest margin part was very clear. I just wanted to know about other factors, like loan growth and asset quality. How do you see those?

Patrick Clerkin

Shayne mentioned that loan growth, there is restrictions on certain sectors. Most sectors where banks can only grow at 2% per quarter. There are exceptions to that, such as agriculture, and DenizBank is the second largest bank for agriculture in Türkiye, so they've been able to grow this part of the loan book. We mentioned they've grown 20% in local currency terms in the first half, and that's because there's been a pivot towards agriculture lending.

Chiro Ghosh – SICO Bank

Just one quick follow up on the previous answer, that all your international business operate on their own, or if, for example, you have higher liquidity in the UAE market, you can use that money to funnel growth in other economies.

Shayne Nelson

From a policy perspective, we expect our businesses to self-fund. Will we inject liquidity into a market where we see there's an arbitrage there between our funding and the market? Yes, but our policy is businesses offshore should self-fund. That's our policy. Just because we keep getting a lot of questions on Türkiye, we never hear too many positive comments on it, but I would just point out that if you look at the price to book multiples on Türkiye, where they are and some of the multiples you've heard about with potential acquisitions.

We bought this bank, which has grown very nicely and contributed nice profits, a number of years ago, at a price to book less than one. If you do the back of the envelope calculations on where the price to book is now in Türkiye, we've made a sizeable gain in potential value if we were to sell it, which we're not going to. You also need to bear in mind that there is considerable value in this franchise, which I know a lot of you don't seem to attribute a lot to, but there is a substantial amount of value in that franchise that we've bought, and we're very happy that we bought it.

Operator

The next question on the line is from Aybek Islamov with HSBC.

Aybek Islamov – HSBC

Thank you for the conference call and all the colour, very useful. I just had one question. What are your thoughts about your cost of risk in the longer term, as in normalised cost of risk, keeping in mind that your loan mix, there's a much lower contribution from the government sector, from the public sector, and also your incremental exposure to international is rising. And I think there's another factor that you might have to write off those NPLs which are more than four or five years old, more than five years old. What's your thought process around the normalised cost of risk? Thank you.

Patrick Sullivan

Hi, Aybek. Thanks for joining. Just on the cost of risk long term, it wasn't so long ago, more longer term guidance was 100 to 125 basis points. Just with the strength of the economy, recoveries, etc., I think we've typically seen it more around the 50 to 70 basis points, so that was earlier guidance before we started seeing a lot of these recoveries. I don't know what that full long term will look like, because we are in a cycle at the moment, so I can't give you what the long term is that we can actually look back with reference. Even in some of the downtimes of more recent times, during the pandemic, it wasn't so much more than the 100 to 125 basis points in a significant downturn.

Just on the NPL write off, I think I did say in the remarks that if we wrote off anything over five years, there would not be a material P&L impact.

Shayne Nelson

Just on the cost of risk, just remember when you're trying to do a medium or long-term view of our cost of risk, we're very heavy retail compared to a lot of banks in the country. And therefore, the risk-reward equation normally means that you're going to have a higher percentage of NPLs in that retail portfolio. If you're big in revolver credit cards, obviously it's extremely profitable business for us. But the cost of risk on that portion of the business is much higher than a corporate would be. I think again when you're doing your model for a medium or long term on us, you've also got to look at the mix we have, and which we do disclose.

Patrick Clerkin

Thanks, Shayne. And there's a few questions just come in. I'm aware I've got two minutes left. I'm very quickly going to go through those. Some people have asked not to be named, so I'll not name anybody asking the questions. And we've already answered quite a lot of the questions posted.

Is NFI sustainable? Again, if you look at slide four, you can see the fee and commission income and the new display that we have for other operating income, and we've split out the client flow income, which tends to be more persistent, as opposed to the non-client flow income.

A question on why the loan growth guidance has not been revised up again, given the geography, increased talk about infrastructure, the buoyant economy and the region? We have already addressed this question.

We talked about the DenizBank loan growth. A question about tax rate nine versus 15. There's nothing been formally published by the UAE, but our working assumption is that implementation in the EU would trigger other countries to implement the 15% tax rate.

Why the growth in interest expense? Again, that's the flow through coming from the cost of higher deposits, given a higher rate environment and increases over the last year.

What percentage of the loan book is variable? Again, the majority of our loan book is floating rate, and if you look at our annual financial statements, you'll see the split of that in terms of the reset, the profile of both loans and deposits.

And then finally, last question on hyperinflation adjustment. Our hyperinflation adjustment for Q2 was down 16%. Compared to QNB's, that was down 33%. Is there room for a big improvement in hyperinflation adjustment? Again, we've said in the past that if you look at the movement, it's quite proportionate. If you take the move in inflation, you can pro rata it from one quarter to the next. Whatever you want to make your assumption about hyperinflation, as I say, you can pro rata to the adjustments that we have been making.

Shayne Nelson

Just on that one, Paddy, just be cautious if you're doing that in your model, but also have a look at the CPI linkers, because that's also then offset by the income line versus the hyperinflation deduction at the bottom line. That'll correlate.

Patrick Clerkin

That is all the questions on the web. And we are exactly at 3 o'clock UAE time. If there are no further questions.

Shayne Nelson

Thanks, Paddy. As you can see, we've continued our strong growth and our consistent performance, delivering another record quarterly profit. Our solid balance sheet makes us a powerhouse in this region. And we have a really good platform for future growth. And I'll hand you back to Lydia in case you've got any further follow-up questions. But thank you all very much for attending the call. Those that are going away for the summer, which has really hit us now, please have a good break, and I look forward to talking to you all on the next quarter's call. Thank you all.

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