IR Call Transcript (Edited Version)
QNB Group Q2 2023 Results

CORPORATE PARTICIPANTS

Noor Mohammad Al-Naimi *Senior Executive Vice President, Group Treasury*

Mark Abrahams *Qatar National Bank (Q.P.S.C.) – Executive Vice President - Group Treasury*

Durraiz Khan *Qatar National Bank (Q.P.S.C.) – Senior Vice President, Group Financial Consolidation (acting on behalf of* **Ramzi Talat A. Mari** *Qatar National Bank (Q.P.S.C.) - Group Chief Financial Officer)*

CONFERENCE CALL PARTICIPANTS

Waleed Mohsin *Goldman Sachs*

Edmond Christo *Bloomberg Intelligence*

Aybek Islamov *HSBC*

Elena Sanchez *EFG Hermes*

PRESENTATION

Operator

Hello, everyone, and welcome to the QNB Group's Second Quarter 2023 Results Conference Call. My name is Nadia and I'll be coordinating the call today.

I will now hand over to your host, Elena Sanchez, from EFG Hermes to begin. Elena, please go ahead.

Elena Sanchez *EFG Hermes*

Thank you, Nadia. Good afternoon and good morning, everyone. This is Elena Sanchez from EFG Hermes. I would like to welcome you all to QNB Group's Q2 2023 results call. It's a pleasure to have with us in the call the following speakers from QNB Group: Ms. Noor Mohammad Al-Naimi, SEVP, Group Treasury and Financial Institutions; Mr. Mark Abrahams, EVP, Group Treasury Trading; and Mr. Durraiz Khan, SVP, Financial Consolidation.

The call will begin with a presentation from management on the key highlights of Q2 2023 results and then we can move on to the Q&A. I would like to hand over the call now to Mr. Mark Abrahams. Please go ahead.

Mark Abrahams *Qatar National Bank (Q.P.S.C.) – Executive Vice President – Group Treasury*

Thank you very much indeed, Elena and EFG Hermes for hosting our Q2 call today. Before we begin, it is customary to remind everyone that this earnings call is for investors and analysts only and any media personnel should disconnect now, please. I will begin by giving an overview on the macroeconomic environment. Then I will cover QNB's financial results for the six months ended 30th of June 2023, and finally open the floor to Q&A.

The global environment continues to be affected by the consequences of excessive post - pandemic policy stimulus and geopolitical tensions. Higher inflationary and monetary tightening has resulted in a slowdown of global growth and uncertainty in some advanced economies. The conflict in Eastern Europe has added further uncertainty and volatility to the global growth outlook. Furthermore, despite a correction in oil and gas prices, fiscal and external revenues remain robust in Qatar and the wider GCC region. This is adding momentum to the strong domestic macroeconomic backdrop. As a result, the economic expansion continues, while the banking sector is resilient and healthy, presenting significant growth, ample liquidity, adequate levels of capitalization, higher set quality and robust profitability.

Qatar continues to lay the foundations for GDP growth over the medium and long term through investment, diversification, and stronger private sector engagement. On the non- hydrocarbon front, following the successful preparation and organization of the 2022 FIFA World Cup Qatar, the country has further consolidated its position as a regional and international hub for business, investments, commerce, tourism, and culture. This has accelerated the execution of the Qatar National Vision 2030 and assisted in the ongoing transition towards a knowledge-based economy.

On the hydrocarbon front, tailwinds from investments and increasing gas production will drive economic growth, with six new LNG trains planned under the flagship Northfield Expansion Project, one of the largest capital expenditure projects in the region and industrial engineering projects in the world. This investment is expected to increase Qatar's LNG production by 64% to 126 million tons per annum, contributing to almost a third of global LNG demand. The project will include an equivalent expansion of Qatar's refining, downstream, and petrochemical capacity. Positive spillovers from these projects will combine with diversification efforts and structural reforms to boost economic activity and spending in the broader manufacturing and services sectors.

We expect domestic activity to remain strong with a GDP growth of 2.4% in 2023 and 2.5% in 2024, according to consensus estimates. Importantly, Qatar is set to continue to benefit from major twin surpluses on its current and fiscal balances, while inflation will moderate further to around 3% this year and 2.5% next year.

I will now move on to QNB's financial results for the six months ended 30th of June 2023. Net profit was QAR7.6 billion or $2.1 billion, a robust growth of 8% compared to last year. Solid revenue growth resulted in an increase in operating income to QAR18.5 billion or $5.1 billion, up 14%, demonstrating QNB Group's success in maintaining growth across the range of revenue sources. QNB's cost-to-income ratio remained strong at 20.4%, which remains - considered to be one of the best ratios among large financial institutions in the EMEA region.

Total assets are at QAR1.202 trillion or $330 billion, up by 7% from the same period last year. Loans and advances reached QAR819 billion or $225 billion. QNB Group remained successful in attracting deposits, which resulted in an increase in customer funding by 5% from June 2022 to reach QAR836 billion or $230 billion.

The Group's loan-to-deposit ratio remained stable at 97.9%. QNB Group's ratio of non- performing loans to gross loans stood at 3%, reflecting the high quality of the group's loan book and the effective management of credit risk. In addition, the coverage ratio on stage three loans is at 99%. Total equity increased to QAR104 billion, up by 1% from June 2022. The bank's capital adequacy ratio at 19% is comfortably higher than both QCB and Basel III requirements.

We will now turn to questions and answers. Thank you.

Operator

Our first question today go Waleed Mohsin of Goldman Sachs. Waleed, please go ahead. Your line is open.

QUESTIONS AND ANSWERS

Q - Waleed Mohsin *Goldman Sachs*

Yes, good afternoon. Thank you much for the presentation. Three areas I wanted to discuss. Firstly, if you could provide an update on the loan demand domestically, if you're seeing any changes there? Any green shoots on that front and how that is factoring into your guidance for this year? Are you revising your guidance? So, any color on that would be very helpful.

Secondly, on net interest margin. It seems that Turkiye was the big or the large detractor this quarter. You had a significant contraction. And given the data we're seeing in Turkiye, it seems that third quarter and fourth quarter will be also weak given the increase in funding costs. So if you could put this into context for the group net interest margin, that will be helpful.

And third and final question on asset quality. If you could share some details in terms of how the conversations with the regulator are progressing and if a peak credit loss is in sight and if you would see certain level where your credit losses will peak and then we start seeing an improvement. Those would be the three questions. And then finally, if you could update us on your guidance that would be very helpful. Thank you.

A - Durraiz Khan *Qatar National Bank (Q.P.S.C.) – SVP, Group Financial Consolidation*

Thank you so much, Waleed. This is Durraiz Khan filling in for Ramzi.

In terms of loan demand domestically, what you'd notice is that, despite significant devaluations in our Turkiye and both Egypt, our loan growth has still held up and that is driven by private sector loan growth in Qatar. We had approximately, compared to December, loans were up 3% in private sector while the government continue to repay the loans. So the domestic credit demand has continued to stay robust, which has helped us in making sure that we have continued to post quarter-on-quarter sequentially as well as versus last year loan growth.

We will go to the guidance first so that your question is answered. From a balance sheet perspective, we expect total balance sheet growth will be around 4% to 5%. Profit and loss will be the same at 7% to 9%. The cost of risk for the full year we expect it at around 90 to 95 basis points and the margin for the full year will be around 250 to 252 basis points.

Your second question in terms of net interest margin and Turkiye, of course, what has happened in Turkiye in Q2 was significant contraction in margin by approximately 300 basis points, principally coming from the cost of funds. Central Bank has taken a lot more actions towards the end of Q2 in reducing some of the reasons why -- which the cost of fund was going up significantly higher. At the same time, the benchmark rates have been raised as well and we expect that the trend of raising the benchmark rates would continue. We slightly differ in this view that Q2 and -- Q3 and Q4 are going to be further weak. No. It will -- hopefully, it will be an improvement from the compression that we saw in Q2 towards late Q3 and Q4.

In terms of your third question, in terms of asset quality, we -- as you're aware, as long as our operating income growth is robust, which has held up in the first half of the year, we will be very proactively provisioning and providing for the cost of risk. This in -- particularly in first half of the year we have front-loaded a lot of ECL, resulting in our cost of risk at around 113 basis points for first half on an annualized basis. We expect that for the full year the cost of risk would come around 95 bps, which would be - 90 to 95 bps, which would be lower than what was last year. So there is expectation that it will be -- the peak cost of risk was actually the year 2022. That's our view right now.

Q - Waleed Mohsin *Goldman Sachs*

Thank you much, Durraiz. That's very helpful. Just on the net interest margin point. I mean, so it's more a question about there's something different in your balance sheet versus the local Turkish banks, because when we look at the data for the Central Bank data, I mean, weekly data, it continues to show that margins on Turkish lira loans continue to be negative, especially on the commercial side and deposit rates have continued to go up.

So is there something that you're doing on the Turkish balance sheet which is helping you offset those cost of funding pressures? Are you doing more in terms of SMEs, which are not capped in terms of rates?

A - Durraiz Khan *Qatar National Bank (Q.P.S.C.) – SVP, Group Financial Consolidation*

In terms of overall balance sheet size, from a lending side, it's corporate-driven. It is our view that since the benchmark rates have risen and the loan cap - the cap on interest rates have been removed, this will help us in improving the margin towards, but it will not be sudden. We expect in late Q2 it will help us in actually making sure that the margin erosion which happened, significant margin erosion, which happened in Q2, part of it goes away in late Q3 and Q4.

It's still early days in terms of the new policy transmission. So I think, looking at the data, immediately after the policy action, which have been taken, might not give the right sense of direction. Let's wait for certain more data to come in, at least a month should fully pass before we can make different judgments as to how the margin would work out, but our view is it would be an improvement versus Q2 definitely.

Q - Waleed Mohsin *Goldman Sachs*

Perfect. And just to wrap it up, so then in that context, your Group NIM, as you said between 250 to 252, which kind of implies from first half levels that they will be marginally down, but generally stable, right. So the rest of the group, you expect Egypt to continue to remain high NIMs and then Qatar to be -- domestic business to remain stable in terms of NIMs?

A - Durraiz Khan *Qatar National Bank (Q.P.S.C.) – SVP, Group Financial Consolidation*

Yes, this is our expectation that for the rest of the year, we have put in one rate hike which almost is priced in. As long as that's the case, we expect the group -- Qatar NIMs and other business NIMs to be stable compared to what was in first half.

Q - Waleed Mohsin *Goldman Sachs*

Perfect. Thank you so much, Durraiz. Thank you.

Operator

Thank you. Our next question go to Edmond Christou of Bloomberg. Edmond, please go ahead. Your line is open

---

Q - Edmond Christo *Bloomberg Intelligence*

Hello. Hi, it's Edmond Christou from Bloomberg Intelligence. Thanks for the call today. So the question has been already answered, but just probably to put some light on the asset quality, if possible. It seems to me that Qatar asset quality is more stable in 2Q compared to 1Q. How should we think about it going into the second half of this year and going into next year, especially with the oversupplied property market, which I think is yet to be seen as a downgrade into the books? If you can give some light on this.

And the second one on Turkiye. Do you expect (inaudible) of credit quality pressure going into next year and if you had seen any pressure on the migration in the second quarter?

The last one is, if I understand correctly, it's reasonable to assume that the margin for the Qatari riyal lending is stabilizing into the second half of the year where you are able to price better on the asset side compared to the cost of deposit and if you can give some color on the cost of deposit in the local currency. I know there has been a competition on certain maturities amid the Central Bank requirement on SSR et cetera. So is there any update on this? Thank you.

A - Durraiz Khan *Qatar National Bank (Q.P.S.C.) – SVP, Group Financial Consolidation*

In terms of asset quality guidance for Qatar, we have actually taken - frontloaded some provisions in first quarter, just to ensure that we are adequately covered for whatever scenarios that are there for the rest of the year. In terms of your question as to whether the overhang of property sector and that is not yet reflected in the local -- in the sector. We wouldn't comment because QNB is a very differently structured bank compared to the rest of the market and our loan profile is very different from everyone else. We very proactively provision any loan, which we think is going to cause us issue down the line and that is why we don't believe that that is going to world - especially World Cup related overhang is going to be a major issue for us. Yet, we remain cautious and we try to - as soon as we identify something, we'll proactively cover it.

In terms of Turkish asset quality, interest rates are still deeply negative in real terms, resulting in the lowest-ever NPLs in Turkish banking franchise that we have seen in the longest of time at around 1.3%. As interest rates will rise and will come closer to inflation rates, there is a natural expectation that there will be problems in asset quality, but we have been building provisions in Turkiye just for this purpose. Our stage one provision in Turkiye is around 3%, stage two is around 18%, and stage three is 1.68% [ph] just to ensure that this is the best-in-class provision that you would find at any -- or potentially any other financial institution. So we are covering for our asset quality risks in Turkiye, which may come down the line, but it would be more of 2024 issue, not a 2023 issue.

In terms of your third question on Qatari riyal lending, see, from QNB perspective, even when we talk about margin stabilization in Qatar, it's more of a dollar-based balance sheet that we have. Qatari riyal is there, but dollar has a more significance and we think that whatever loan deposit repricing that was there, has been done. And even if there is one more rate hike, which almost is priced in, our margin would remain stable for the rest of the year.

Q - Edmond Christo *Bloomberg Intelligence*

Very helpful. Thank you very much. Good luck.

Operator

Our next question go to Aybek Islamov HSBC. Aybek, please go ahead. Your line is open.

Q - Aybek Islamov *HSBC*

Yes, thank you for the conference call. Couple of questions from me, please. Well, first is operating costs. You've done pretty well in the second quarter. Obviously, your revenue line was a bit under pressure and yet your operating cost was quite good. What are your thoughts on the operating costs for the rest of the year, how do you see them evolving? That's my first question.

And I think secondly what I wanted to ask you is the changes in regulations about funding by the Qatar Central Bank. Does it somehow impact your net interest margin sensitivity to change the interest rate going forward? And if it does, in what way? So would you expect more margin compression when rates fall, for example?

A - Durraiz Khan *Qatar National Bank (Q.P.S.C.) – SVP, Group Financial Consolidation*

In terms of operating cost, absolute decline principally is happening from the devaluation in our two key markets. If you go back to our discussions, which we were having in Q3 and Q4 when absolute operating costs significantly increased was -- the reason was that, our two large subsidiaries had certain adjustments primarily in the staff cost and other lines because of very high inflation in both markets, but since exchange rates was stable, it was resulting in a like-for-like increase also in dollar amounts. But since both of these countries have had devaluation, almost a fifth in both of these markets, so absolute levels are coming down. We expect similar trends going forward in second half of the year as well.

In terms of Central Bank regulations, no, it doesn't change any sensitivity. As such, the only thing the Central Bank is trying to do is, asking the banks to go slightly longer term to ensure that stability of the deposits or stability of the funding in the system is more robust compared to what market thinks and this can be demonstrated by the data. But we don't think that our sensitivity changes because of these actions.

Q - Aybek Islamov *HSBC*

Thank you. Just one follow-up question. On your capital ratios, can you remind us what's your minimum capital requirements in Turkiye? How much capital buffer you have there at the moment and also in Qatar, right? So obviously there's a lot of consumption in quarter one on back of the FX translation losses, which accelerated in 2021, so, yeah, can you remind us the capital ratios.

A - Durraiz Khan *Qatar National Bank (Q.P.S.C.) – SVP, Group Financial Consolidation*

In Turkiye, minimal requirement is 12%, whereas locally reported capital over there is 13.8% - this is disclosed in our Finansbank slide, in our investor relations pack. And in Qatar as well, we are much higher than the local requirements. The minimum requirement, if you give me a minute to get to the page, Slide 23, 11% on CET1, we are at 13.9%. On a total capital, we are approximately 300 bps higher. 16% is the minimum requirement versus 19% on an overall basis. We are very comfortable and we are higher -- at a Group level, we are much higher than the buffers that are - that we have internally set for ourselves.

Q - Aybek Islamov *HSBC*

And just to clarify, on your Group core Tier 1 quarterly numbers, you do not add your net income? Do you retain any...

A - Durraiz Khan *Qatar National Bank (Q.P.S.C.) – SVP, Group Financial Consolidation*

Not yet.

Q - Aybek Islamov *HSBC*

In quarterly results. Not yet?

A - Durraiz Khan *Qatar National Bank (Q.P.S.C.) – SVP, Group Financial Consolidation*

Not yet. This might - this we are expecting may change in 2024.

Q - Aybek Islamov *HSBC*

All right. Thank you. Yeah. Very clear.

Operator

It looks like we have no further questions. I will now hand back to Elena of any closing comments.

Q - Elena Sanchez *EFG Hermes*

Thank you, Nadia. Yes, I can see some questions here that have been sent in a written form that have not been asked before. There's one on the - asking about the nature of the big write-offs this quarter. And can you provide color on the high income from FX operations?

A - Durraiz Khan *Qatar National Bank (Q.P.S.C.) – SVP, Group Financial Consolidation*

Yes, Elena. In terms of the write-off, this - as we have said that we have been following up for a very long time to get certain approvals for write-offs for loans, which had been provided many years ago and some of the approvals came in, which has resulted in the write-off that we are seeing this quarter. In terms of high income from FX operations, it's principally coming from our Turkish operations and the reason is that volatility in between the dollar and lira was significant in late Q2 that resulted in much higher FX income.

Q - Elena Sanchez *EFG Hermes*

Okay. Thanks, Durraiz. There is another one on non-resident deposits. What is the share of non-resident deposits now for QNB? The (Technical Difficulty) mentioning that deposit growth has mainly come from (Technical Difficulty) and how that affects cost of funding in the company?

A - Durraiz Khan *Qatar National Bank (Q.P.S.C.) – SVP, Group Financial Consolidation*

In terms of our deposit break down, we provide detail breakdown in our investor presentation as to what are the geographies from where deposits are coming in. The question which usually gets asked is around whether the non-resident deposits would continue to slow down. No, they have broadly stabilized. Between the December and the June levels, they are broadly very similar. They wouldn't - I wouldn't expect them to continue to come downward this year as well. Now we are trying to change the composition of deposits to try to ensure that we meet the regulatory requirements of Central Bank and try to increase our diversification efforts. So far, besides -- obviously, when we are trying to go slightly longer, it will have some cost impact, but on an overall basis, the impact on NIM has been manageable.

Q - Elena Sanchez *EFG Hermes*

Okay, thanks. Couple of other questions that I can see here. One is asking about the outlook for operating expenses growth this year and also asking if staff cost inflation has eased in Turkiye, slowed down in Turkey and Egypt.

A - Durraiz Khan *Qatar National Bank (Q.P.S.C.) – SVP, Group Financial Consolidation*

See, in terms of expenses in Turkiye and Egypt, both countries continue to be under a much high inflation. That has been for a long time. And we expect that, that is going to drive the cost higher. Having said it, in usual circumstances, whenever these countries generally have devaluations, so when the numbers are eventually translated to dollars or riyals, the absolute number is much lower than what has been given in the local markets. So that is our view, that would continue to be the case.

Q - Elena Sanchez *EFG Hermes*

Thanks, Durraiz. Question on taxes. Tax expense last quarter in Q1 '23, there was a tax write-back of QAR21 million, asking about the change in or the increase in the tax rate in Q2 2023 compared to Q1.

A - Durraiz Khan *Qatar National Bank (Q.P.S.C.) – SVP, Group Financial Consolidation*

Elena, we have a detailed note in the financials that last we -- last quarter we had a one- off from Turkiye because of change in tax law regarding certain properties. That drove the one-off tax write-back. That is no longer there. So that's why now the Q2 tax number is more normalized.

Q - Elena Sanchez *EFG Hermes*

Okay, thanks for that. And then lastly, a question on credit quality in Egypt, if you can comment on the dynamics there and expectation?

A - Durraiz Khan *Qatar National Bank (Q.P.S.C.) – SVP, Group Financial Consolidation*

Our view is that, in our Egyptian franchise, the credit quality continues to be high on the agenda. We are trying to make sure that the NPLs are creeping up slowly and gradually and we expect because of high inflation in that market an exchange rate volatility. This trend will continue. It's our job to ensure that we take much more than adequate cost of risk provisions against those. At least for the second half of the year, our view is that credit quality - credit costs would continue to trend higher and the NPLs would also continue to trend higher.

Q - Elena Sanchez *EFG Hermes*

Another question (inaudible) Qatar's business backdrop on loan growth. Can you speak a bit -- can you please speak more about the loan performance outlook within Qatar? Do you expect most of the non-performance to be cleared from the Qatari system? And I don't understand the second part of the question. If you can perhaps answer the first part of the question, the loan outlook within Qatar for the rest of the year.

A - Durraiz Khan *Qatar National Bank (Q.P.S.C.) – SVP, Group Financial Consolidation*

We covered it in our first question that we expect the private sector loan growth has continued to remain robust. For QNB, it is approximately 3% up versus December - June versus December numbers. And we expect pickup actually in second half of the year, so that we are able to achieve the targets that we have announced for the full Group.

Second question is looking at the Qatar PMI data, business is high. What early indicators would you love to - at the turn of a cycle, see, PMI is - we have to go slightly back. PMI was low recently because the World Cup had just ended and there had been a lot of inventory buildup. Now that that has been cleared, the PMI indicator, of course, has improved.

What does major CapEx kick-off for NFP 2024 we expect from this year onwards? It would not be something which will happen all of a sudden. It would be a momentum, which will gradually build up, but we expect initial things to start coming in from second half of this year.

Q - Elena Sanchez *EFG Hermes*

Yes, hi. I see no further questions in the queue. I think we have covered most of the questions that have been sent in written form. In this case, I think perhaps we can close with the call. I would like to thank QNB's management for their time today and everyone for participating in the call. And I hand it over to you, Durraiz and Mark for any closing remarks that you may have. Thank you.

Q - Mark Abrahams *Qatar National Bank (Q.P.S.C.) – Executive Vice President – Group Treasury*

Thank you all very much for your time today and we'll speak again in three months. Have a good day. Thank you.

Operator
Thank you. This now concludes today's call. Thank you so much for joining. You may now disconnect your lines.