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M/s Bursa Kuwait

السادة / شركة بورصة الكويت المحترمين،،،

Dear Sirs

تحية طيبة وبعد،،،

Sub: Burgan Bank K.P.S.C. Analyst Conference transcript for the Financial year 2021

الموضوع: محضر مؤتمر المحللين لبنك برفان ش.م.ك.ع. للسنة المالية 2021

Reference is made to the above subject and in compliance with the provisions of clause (4) of article (8-4-2) of Bursa Rule Book; attached is the transcript of the Analyst conference that was held via phone at 02:00 pm, Thursday, corresponding to 10/02/2022.

بالإشارة إلى الموضوع أعلاه، والتزاماً بأحكام البند (4) من المادة (8-4-2) من كتاب قواعد البورصة، مرفق لكم طيه محضر مؤتمر المحللين والذي تم عقده عبر الهاتف في تمام الساعة 02:00 من بعد ظهر يوم الخميس، الموافق 2022/02/10.

Best regards,

وتفضلوا بقبول فائق الاحترام،،،



خالد فهد الزومان

Khaled Fahad Al-Zouman
رئيس المدراء الماليين للمجموعة
Group Chief Financial Officer



بنك بروگان
BURGAN BANK

FY'21

Earnings Conference call Transcript

Thursday, 10th February 2022

FY' 21 Burgan Bank Earnings Call

Thursday, 10th February 2022

Pre-Transcript of Burgan Bank Earnings conference call that took place on Thursday, 10th February 2022 at 14:00 Kuwait time (UTC+03:00)

Burgan Bank Participants:

Mr. Khalid Al Zouman

Group Chief Financial Officer

Mr. Naveen Kumar Rajanala

**Group Head of Group Strategy, Capital Management
and Investor Relations**

Operator (Elena Sanchez):

Good afternoon everyone and welcome to the Burgan Bank Group FY 2021 Earnings Call. Thank you very much for taking your time to attend this conference call. Today's conference is being recorded. For today's call, we have Mr. Khalid Al Zouman, Chief Financial Officer and Mr. Naveen Rajanala, Group Head of Strategy, Capital Management and Investor relations. At this time, I would like to handover the call to Mr. Khalid.

Khalid Al Zouman:

Good afternoon everyone and welcome to the Burgan Bank Group earnings Call. Thank you very much for taking the time to attend this conference call.

Let me start with Slide 3 which captures the key points of FY21 performance.

- We have seen a strong rebound from FY20 revenue levels with economic activity picking up in key sectors.
- Revenues: Burgan Bank Group's Revenues increased by +10.3% y-o-y to reach KD 235mn.
- Net income: Burgan Bank generated a strong Net income increasing by 34.8% y-o-y to reach KD 45mn.
- We have also improved our asset quality significantly largely through write-offs. Group's NPL Ratio decreased to 1.7% & NPL Coverage Ratio improved significantly by 94.2bps to reach 227%
- As highlighted in the past, we have taken many actions to optimize our expenses. As a result, the Group showed positive efficiency indicators with Cost-to-Income of 40.4% improvement of 530bps y-o-y & JAWs ratio of 12.8%

Slide 4 reflects the key messages of the year. 2021 has been busy year and some of the key initiatives delivered are:

Rights Issue:

- Burgan Bank Group successfully executed the rights issue in Q4'21 and raised KD 71.25mn to support the long-term growth of the bank
- The rights issue had an Oversubscription of 2.25 times and a high percentage of Rights was subscribed (93.09%).
- The impact of this rights issue of the regulatory capital (CET1) is +120bps

Digital:

- We have been making lots of progresss in Digital & we have started seeing results of these efforts
- Transactions executed through digital channels grew by 3 times.
- Burgan maintained a High App rating of 4.5 (Apple & Android)
- Burgan won awards from "Global Finance" for its digital platform under 4 categories in 2021

BoB Sale:

- In terms of Bank of Baghdad (BOB) sale, the Group achieved a much-improved offer and due diligence is in the last phase
- We hope that the sale transaction is concluded in Q2'22, upon completion of due diligence and all regulatory approvals

Containment of Pandemic Impact:

- In terms of the pandemic impact, we feel that in 2021 especially since Q3'21 in Kuwait it's been largely contained and for our international operations also, the impact on business has subsided especially in the second half of 2021.
- We are witnessing a pick up in execution of key projects in Kuwait
- In addition, individual customer activities almost back to normal levels in the second half of 2021

Moving on to Slide 5, highlighting performance on Revenue and Operating Expense:

- Burgan Bank Group's Revenues grew by 10.3% y-o-y to reach KD 235mn, mainly driven by growth in non-interest income & strong performance by Kuwait.
- Margins are stabilizing at 2.1%
- As highlighted earlier, the reduction in the Group's operating expense continues in 2021, the operating expense decreased by 2.5% y-o-y to KD 95mn.
- Burgan remains efficient with a significant improvement in Cost-to-income ratio to 40.4%

Moving to slide number 6, which highlights Burgan's Operating Profit and Net Income:

- Burgan delivered a robust operating profit of KD 140mn, increasing by 21.1% y-o-y
- As a result, Net Income for FY'21 increased significantly by 34.8% y-o-y to reach KD 45mn

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

Naveen Rajanala:

Thank you, Mr. Khalid. As highlighted earlier, we have made significant progress in improving asset quality

- The first chart shows the drop in NPLs from last year by almost 60% to KD 81mn in FY'21. The drop is largely driven by write-offs where the bank utilized excess provision buffers to do the exercise.
- As a result, Group and Kuwait's NPL ratios dropped to 1.7% and 0.7% respectively
- Second important point is the coverage ratio, the bottom left chart shows the strong Coverage ratio that Burgan has both at the Group level and Kuwait. NPL coverage ratio for the Group and Kuwait increased to 226.6% and 532.9% respectively in FY'21. Please note that we have collaterals on top of these provisions which adds further comfort.

Moving on to next slide which captures the asset details.

- The Group's total Assets remain stable at KD 7bn
- The loan growth focus still remains in Kuwait with lower/no growth in the international loan book.
- The loan book composition continues to be similar to the previous year with no major movement.

Moving on to Slide 9 on Deposits and Liquidity metrics. The key messages here are:

- Access to liquidity via customer deposits and international markets remains solid.
- Customer deposits in Kuwait grew to KD 3bn in FY'21 with international operations maintaining stable levels of deposits with stable CASA balances of around 32% of total deposits

- We have also included Cost of Funds details. As you can see we have reduced COF's by 50% over the last 2years in Kuwait to largely offset drop in yields due to rate cuts
- Group COF at similar levels due to higher COF in Algeria & Turkey.
- Burgan maintains strong liquidity metrics and remains well above the regulatory minimums. The Group's Liquidity coverage ratio is at 125.3% and Net stable funding ratio is reported at 106.9%

Moving on to slide 10 that captures Burgan's Capita Levels:

- The CET 1 Ratio increased to 11.4%. This of course is due to the recent rights issue and higher retained earnings
- Please note that in time with CBK's gradual rollback of forbearance measures, the min CET1 will increase to 9% from Q1'22 & to 10.5% from Q1'23.

Moving on to slide 11 which provides details of performance by entity.

- Kuwait had a strong year. CoC was high due to couple of large a/c's but we expect the credit cost to improve.

International Operations:

- The international operations performed well and their metrics continue to improve.
- The NIMs continue to be healthy in these markets
- Turkey: continued reduction in balance sheet size in this market as per our strategy which now only contributes 13% of Group's assets. Turkey balance sheet shrunk due to the dual impact of devaluation & our strategy of highly cautious growth. NIM's were impacted given the rates volatility in that market. NPLs have been reducing and has fallen by 550bps largely on the back of recoveries & debt asset swaps.
- Algeria: Profitable franchise with continued high margins. Though there is slight increase in NPL ratio, the NPLs are well provided for.
- Tunisia: continues to be stable.

With that, I will now hand it back to Mr. Khalid to cover the last slide and conclude the presentation.

Khalid Al Zouman:

Thank you, Mr. Naveen

On slide 12, to conclude:

- Given the successful rights issue & sufficient capital buffers, we expect to grow in Kuwait & opportunistically in our subsidiaries market.
- We expect credit costs, especially Kuwait, to start normalizing unless there are any surprises.
- The general view has changed quite a bit on rate hikes over the last couple of months. So, if rate hikes happen as expected, we expect it to boost our margins.

Thank you. I will now hand it back to Ms Elena.

Elena Sanchez:

Thank you, Mr. Khalid and Mr. Naveen for the presentation, we will move now to the Q&A session. If you would like to ask a question, you can either click on the “raise hand” button and I will unmute your microphone, or you can write your question in the Q&A designated area. We'll pause for a minute to allow you to send your questions. Thank you.

Elena Sanchez:

Okay. We'll take a few questions from the chat now. One of them is, what is the normalized dividend pay-out that you see for the bank? Is there scope for a significant change compared to the full year 2021 level?

Naveen Rajanala:

Yes, I think as we've said in the past, we don't have a set dividend policy, but obviously our dividend payment is dependent on our discussion with the regulators and capital levels, but we wouldn't necessarily conclude from the dividend levels in 2021 that its dividend payout is future direction. We expect the dividend levels to improve as we go along with the business activity and the bank's growth outlook picking up. So short answer is, I don't think 2021 is a signal of the dividend levels to come in the future.

Khalid Al Zouman:

Also, I want to add that the Central Bank recently issued a new instruction to the banks for interim dividends. So that's also an improvement.

Elena Sanchez:

Thank you. We'll take now another question from Divya Poojari. How should we think about related party exposure given its significant portion of the total loan book? How comfortable would you be given that KIPCO investment companies are still not out of the woods completely?

Khalid Al Zouman:

Today we need to understand that KIPCO are in different industries and they are a holding company. Yes, maybe there is a related party from IFRS point of view, but there is no interference or related party within the lending. Each credit has its own assessment and its own cash flow and there is a viability analysis of that lending. So, in terms of related party, we know KIPCO and how they are the biggest holding company in Kuwait. But in terms of, inherent risk, we don't see it as very significant.

Naveen Rajanala:

Yeah, I think you've covered it all. And if you look at it, there's not been any increase in the exposure in the last couple of years. So, we expect that to remain stable and sort of slowly go down as we go in future. But the critical point here is, and as Mr. Khalid said, this is a profitable business for the bank as well. This is being done at arms' length, and then we've not lost any money on this exposure ever. So, we have to keep that in context.

Elena Sanchez:

We'll take a few more questions from the chat. Is the current CET1 ratio something that you are comfortable with? What are the other catalysts that you are looking at towards the CET1, given that it will be very close to the minimum requirement from Q1 2023?

Naveen Rajanala:

Yes. So, two things, one is we expect the earnings to reach normalized levels going forward, obviously given the current expectations around the pandemic's future direction. So that should help our capital levels. Secondly, as Mr. Khalid alluded to, there's the proposed Bank of Baghdad sale, which should add around 45 basis points to the capital. So, I think with these two, and based on our planning exercise that we do for the next four to five years, I think we are pretty self-sufficient in terms of capital for the medium to long term.

Elena Sanchez:

Another question on NPLs. In terms of NPLs, as well as stage two, how much of the exposure is coming from Turkey, and how much of the exposure is coming from the related party lending?

Naveen Rajanala:

There is no NPL from related party. From Turkey, the stock of NPLs is 42 million KD out of a total of, the international stock of KD 53 million. But again, as highlighted earlier, this has gone down over the last 12 months, and we expect that to slowly fall from these levels going forward. We don't expect any spikes as we see things at the moment in Turkey.

Elena Sanchez:

Thank you, Mr. Naveen. Question on ESG, are you looking for any tangible ESG indicators or publishing of reports? And also, any tangible ESG targets that you are focusing on?

Naveen Rajanala:

Yes, so we've made quite a bit of progress on the ESG front. So, we have published a sustainability report on 2019 and 2020. We expect to publish the 2021 report, along with the annual report in Q1'22.

We have communicated some of the critical tangible targets, in the document and that's something that we will be more vocal around in 2022. The obvious one is to increase our lending & investing in this space. We expect this as one of the key focus areas for the bank over the next two to three years, obviously, depending on the kind of projects that are available for financing.

We also are internally focused on improving our ESG MSCI rating, and there are many elements that the bank has worked on over the last couple of years. So, we expect our MSCI ESG rating to get a bit of a boost in the future.

Elena Sanchez:

Okay. There are a couple of questions on margins and interest rates. Do you expect the Central Bank of Kuwait to follow the Fed rate cycle in 2022? And how many rate hikes are you expecting?

Khalid Al Zouman:

As stated in the last slide, we mentioned this. During our budget process for 2022, the rate hikes was not considered. But what we see in recent times, our economist team are saying that there might be an interest rate hike from Q1 of 2022. So, coming back to your question,

historically CBK always maintained the corridor or the level between the rates on KD and the Fed's USD interest rates.

In terms of the second question, whether our NIMs are going to be affected, yes. We see it as an opportunity for our NIMs. If there is a rate hike, for every 25 basis points we expect an impact of 4 KD million.

Elena Sanchez:

Okay, thank you Mr. Khalid.

Naveen Rajanala:

I think there is one more question on mortgage law, right?

Elena Sanchez:

On the mortgage law, yes.

Naveen Rajanala:

So, I think the last update that we had given, it was in discussion and I don't think there's been much of an update. Again, there is an expectation that this should be sorted in a quarter or two, but unfortunately there is not tangible or concrete piece of news that it's going to happen now or later.

Khalid Al Zouman:

Unfortunately, it is not within the coming period as it's under the parliament discussions. But we as a bank, see it as an opportunity for us. It's not only Kuwait, even in advanced markets and globally this law is there. So, for us it's going to be opportunity, definitely.

Elena Sanchez:

Thanks for that. We have another question on NPLs. I think it has been partly answered. How much of the NPL recent decline was driven by write-offs and how much by recoveries? And a little bit of color of what happened in terms of countries.

Khalid Al Zouman:

Yes. To be honest around 140 KD million has been written off, mainly coming in Kuwait. And there are also recoveries, we saw some recoveries in Turkey during 2021.

Naveen Rajanala:

So, just to add to Mr. Khalid. So, the write-offs are largely in Kuwait because we had a massive provision buffer which we used. In terms of the capitalization in Turkey, as you might be aware, BRSA announced a regulation at the end of the year that they would be using a certain fixed rate for the capital calculation. I think it's about USD/TRY of 8.90. Based on that, the capital levels of our entity in Turkey is sufficient and above minimum regulatory requirements. But we, are ready to put in another \$50 million or so if needed. But as of now, their capitalization level is sufficient.

Elena Sanchez :

And the question of senior transactions, are you looking to revive your senior transactions soon, given your tight NSFR?

Naveen Rajanala:

I don't think we are under any liquidity pressure. So, I think NSFR requirement, as you would have seen, is 80%. We are maintaining it around 106%. And the question of tapping in the senior market is purely economic driven. So, if we see that there is a low rate that we can achieve, then we will target it. Otherwise, we have enough liquidity onshore and with other international market avenues. And again, as I said, we don't see the need to load up on liquidity at this stage. We will do it as and when it's needed.

Elena Sanchez:

A question on NPL coverage ratios in Turkey and Algeria?

Khalid Al Zouman:

It's more than 100%.

Elena Sanchez:

Okay. A question on Bank of Baghdad sale, have you approached the regulators for a preliminary approval to avoid any potential delays in the transaction?

Naveen Rajanala:

So, one of the critical things is, last time, one of the feedbacks from the regulator in Iraq was they would prefer that the buyer is a financial institution than a corporate or a family-owned

enterprise. So, we are dealing specifically with the financial institution who has applied for approval in their own jurisdiction. We have obviously intimated a Central Bank of Kuwait and they're aware of this transaction. But once the price consideration is agreed, which as Mr. Khalid said, it's in its final stages, we expect the formal dialogue with the regulators to start. But again, we don't expect too much issue from the regulators in terms of the approval.

Elena Sanchez:

A question on NPLs, but a bit from a different angle, was there any significant formation of NPLs during 2021, particularly in Turkey?

Naveen Rajanala:

No. In fact, as we had shown in our chart, so we've not had any immediate blow back because of the currency drop that we saw in Q4. So, no new NPL formation that we've seen.

Elena Sanchez:

Okay. A question on 2022 growth outlook. Can you please comment on growth ambitions for this year and which regions will drive loan growth? Would you retain a conservative stance with no growth objectives in their national operations?

Naveen Rajanala:

Yes, I think as we said, growth will be driven by Kuwait. We expect Kuwait's growth to be in the 5% to 6% mark. And obviously, if there are opportunities to push that number higher we will do, depending on the availability of good transactions. On the international side, I think our focus is that Algeria might grow, opportunistically, if there are any good transactions. We don't expect Turkey to grow. If there is any growth in Turkey, it will be around 1% or so.

Khalid Al Zouman:

Very selective in Turkey.

Naveen Rajanala:

Yes, very selective. But Kuwait is what will drive growth at a group level. Growth at group would be around 5%.

Elena Sanchez:

A question on non-interest income. Could you please provide more information on the increase of income from net gain in FX, foreign currencies, net investment income and other income which helped to increase total revenue?

Khalid Al Zouman:

Yes. I can give some highlights. For example, in terms of FX gains, there are two aspects, one is related to the improved activities of treasury in Kuwait, plus Bank of Baghdad (BOB). BOB has been doing very good FX business in 2021. In terms of other income, other income is mostly because of some net recoveries, recoveries in NPLs that were written off and now has been recovered. These recoveries appear in other income. I think I said earlier also that in Turkey, they have a lot of good recoveries in '21.

For the securities gain, these are our investments, direct investments. These are funds which we are holding in long term position, and the performance was well diversified in the international market, between US and some Europe.

Elena Sanchez:

Okay. A question on the FX translation losses of 43.1 million Kuwaiti Dinar; is it because of Turkey? Do you have a plan to manage it in the future with further the Turkish leader depreciation?

Khalid Al Zouman:

Unfortunately, you will see only the bad side, which is the foreign currency translation, but we have another side, the gains coming from our hedge also. We are hedging our investments and the gains also comes in equity.

Naveen Rajanala:

I was just going to say the same thing. So, KD 43.1mn is a gross number. And if you net it off against the hedging gains, it's lower. Yes, given the quantum of the movement of Turkish Lira, it's largely attributable to the Lira. But given that we are hedging, the impact has been lower, which as Mr. Khalid said, please put that figure in context with after netting off against the hedging gains, which is there in the equity.

Elena Sanchez:

A Question on guidance for full year 2022. If you could provide some guidance on cost of risk, NPL ratios, earnings growth.

Naveen Rajanala:

See, on the cost of risk, as we've said in the past, it's something that as Mr. Khalid said, we expect that to normalize. But again, these things that are out of control and hence cannot be predicted, for example, the precautionary. So, it's a little difficult to say it's going to be around this figure. But we expect CoR to improve given the overall improvement and what we are seeing in terms of client activity, expectations, etc.

Khalid Al Zouman:

Yes, also on one of the slides, I mentioned that now we are post pandemic, so we expect things to improve going forward particularly in Kuwait, definitely.

Elena Sanchez:

Okay. A question on Turkey. When should we expect Turkey to return to profitability and what will be the drivers for that? And what is your outlook for NIMs in Turkey?

Khalid Al Zouman:

According to BRSA rules, the bank is profitable by the way. However, the difference between central bank rules in terms of provisions, makes the difference between our reporting & local reporting.

Naveen Rajanala:

Yes, and then we expect margin to, again, improve a little bit. In the past, there have been well north of 3%, but I don't think it'll be those levels, but we expect margins to improve and stabilize.

Elena Sanchez:

Another question, will the minimum requirements from LCR and NSFR be raised to 90% from 80% in January 22 and to 100% in January, 2023?

Naveen Rajanala:

Yes, that's correct.

Khalid Al Zouman:

Yes. These were instructions from the central bank actually.

Elena Sanchez:

Thanks. There is a question also on your view or comments on the possibility of interim dividends announced by the CBK recently. You commented briefly on that before, but I don't know if you want to add any further comments.

Khalid Al Zouman:

The instructions are clear, they opened a window for that, but the central bank also said it's going to be under study. So, each bank will submit, thorough studies on that.

Elena Sanchez:

Okay. Thanks. There is also a question on whether you expect any pressure on asset quality metrics in full year 2022.

Naveen Rajanala:

No, I don't think we, I mean, obviously we've seen a spike in 2020 and 2021. We don't expect the levels to rise significantly not to the levels that were there in 2020. There might be a little bit of one-off spike here and there, but as of now, we don't see any increase.

Elena Sanchez:

There is another question on stage two. If you can provide any insights on the nature sectors of stage two loans.

Naveen Rajanala:

Yeah, so in terms of stage two, in terms of levels had, if I look at the loan book, it's about 750 million KD of loans in stage two. But we need to put that in context that these are based on CBK's IFRS 9 guidelines. So, this is not comparable with the international IFRS 9 guidelines. The other critical thing here is that as per the local guidelines, we have to apply to the regulator before we can move someone from stage three to stage two or stage two to stage one. So, the negative movement happens automatically, but any positive movement, it has to go through the curing period of 12 months before it can be reflected as a positive staging. In terms of the industry concentration for the stage two specifically, I don't have it to hand.

I can give a quick snapshot of stage three if that helps. So, in terms of stage three, 22% or so of the current NPL is in real estate sector. And some 12% is in personal. When I say personal, these are largely private banking exposures. And around 17% in trade and commerce. But again, these numbers percentage wise looks high, but let's also remember that the NPL stock itself has gone down. So, I'm talking about 18 million KD in real estate, 30 million KD in trade and commerce and in personal 9 million KD in of stage three.

Elena Sanchez:

Okay. Thanks for that. I can see two more questions. One is whether you can comment on the weakness in trading in your subordinated bond.

Naveen Rajanala:

Again, unfortunately, obviously it's not just our tier two, I think a lot of those tier twos, which were issued in those low rate environments, are struggling and a lot of these fixed income instruments are struggling with the rate expectations. We don't get into market making of our bonds, but yeah, obviously we would've hoped for the price to sort of recover, not sure that's going to happen under current market expectations.

Elena Sanchez:

And the final question on deposits. Can you comment if there has been any unusual withdrawal or activity in deposits at the bank and what would be the deposit growth outlook for 2022?

Naveen Rajanala:

No, I don't think we expect any weakness in our deposit collection activities. We've not seen any early signs or so, so deposit wise, we are comfortable. As we've said in the past, we are not relying on the big K companies for our deposits. We have reduced our concentration. So don't see any imminent issue with our deposit collection. Typically, we ramp up the deposit collection depending on our growth plans. But as of now our access to deposits continues to be strong.

Elena Sanchez:

All right. So, I think we can conclude the call at this point as there are no new questions or new topics being raised. I'll hand it over to you for any closing remarks that you may want to make.

Khalid Al Zouman:

I would like to thank you, Elena, and I would like to thank all the attendees, and we hope to see 2022 a better year than 2021, and we'll see you on the next calls hopefully.

Naveen Rajanala:

Thank you everyone for your time and we are available if you have any other questions, please drop us line at ir@burgan.com. Thank you so much.

Elena Sanchez:

Thank you very much. This concludes the call.