

ADIB 1Q 2022 Earnings Presentation

Thursday, 28 April 2022

Janany Vamadeva Hello everyone and thank you for joining us today. This is Janany Vamadeva and on behalf of Arqaam Capital, I'm pleased to welcome you to Abu Dhabi Islamic Bank's Q1 2022 early conference call. I have with me here today from ADIB management, Mr. Mohamed Abdel Bary, Chief Financial Officer, Mr. Ahsan Akhtar, Group Financial Controller, and Lamia Khaled Hariz, the Head of Public Affairs and Investor Relations. Thank you [inaudible] now [inaudible] to the head of investor relations, Lamia Khaled Hariz. Lamia, over to you.

Lamia Khaled Hariz Thank you, Janany. Good afternoon to everyone on the call and thank you for joining us today. Before we get started, just a quick reminder that today's presentation and all our financial disclosures are currently available on the IR section of our corporate website and on our dedicated IR app. As Janany mentioned, Mr. Mohamed Abdel Bary, our group CFO, is here with us in the room and he will be taking over this call and Mr. Ahsan Akhtar, our Group Financial Controller. Basically, just to recap on the agenda of today, we will go over the financial highlights and give a quick progress on our strategy, followed by a more detailed analysis of the financial performance of this quarter. Mohamed will then provide an outlook and guidance for the rest of the year, after which, we'll open it as usual for Q&A. With that now, I will hand it over to Mohamed, who will take you through this presentation. Mohamed, over to you.

Mohammed Abdel Barry Yes. Thank you, Lamia, and good afternoon, everyone. And thank you for joining us on today's call. We are very pleased to report a very good start for the year. So from a net profit perspective, we are reporting an 18% growth year-on-year, which has resulted in a return equity of 17%. We've done that by growing revenues by 6%, predominantly driven by growth in non-funded income to the tune of 19%. We've also managed to reduce cost by 2%, which has led to an improvement in our cost to income ratio by 3.4 percentage points, taking us to 40.1%. From a balance sheet perspective, we've shown also healthy growth by growing our financing assets by 9%. And we've also seen a healthy growth on the deposit side, which has grown 8%. The growth has been predominantly also driven by a healthy contribution from current accounts and saving accounts. And accordingly, we are still showing a healthy mix of 76% coming from our current account and saving accounts. From a capital perspective, our C81 remains to be healthy at 12.7%.

Moving on to the next section, just a brief update on the strategy. As you all know, our strategy is informed by our renewed purpose as a lifelong partner for our customers, colleagues, and community, and our vision to be the world's most innovative Islamic bank. On slide six, we are seeing the main four pillars of the strategy, which is continuous innovation, segment focus, this and excellence and sustainable future. I'll just call out a few sound bites under each of these four pillars. Under continuous innovation, we have done good progress. And as an example, we launched a digital platform for our wealth management clients, which has allowed them to track their investment products and provide them some sophisticated and useful tools for their saving and retirement plans. Also, we have managed to add more clients to our Amwali platform. We've added 4,600 new joiners or clients to the Amwali family.

Under segment focus, we've attracted 28 new clients to the bank, of which 10,000 are in the first quarter of this year. We've also enhanced our cost ratio, and we've also managed to continue growing our corporate book in year to date, 2.5%, but year-on-year, it's in the double digits. From a digital excellence perspective, we remain to enjoy a leading position whereby 99% of all our transfers are coming through our digital platforms. And we've seen a healthy pickup in our straight-through processing initiatives. Our app remains to be rated very highly on the app, so on Google Play, with a 4.5% rating. From a robotics perspective, we've added 68 new robotics to our process to ensure

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that we continue enhancing our end-to-end digitization journey, which is not only front end to client, but takes the journey all the way from point of origination till the transaction is complete.

Our fourth pillar is addressing sustainability or ESG, and we've maintained our position as an A rating on the MSCI ESG rating. We've also continued to enhance our employment engagement and index, and our net promoter score has continued to evolve year-on-year. Moving on to slide eight, again, as a reminder, we've seen this before, but just reminding everyone what are we trying to solve for? We are making good progress toward achieving our ROE of 20% by 2025. We are still on track to deliver a double profit from where we started, enhancing our cost to income ratio to the sub 36%, and continue to digitise our bank. With that, let's move into the financial section of our results. As mentioned in my opening remarks, I'm very happy to see the growth in net profit by 18% to 715 million. And the comfort, which is really quite obvious to us is that the delivery of this performance has been by growing revenues, reducing cost, as well as seeing normalisation in our cost of risk.

And in terms of our operating profit, I think we are reporting probably one of the highest operating profit margins growth year-on-year in the market at 12%. Moving forward, let's talk a bit about our income statement, as you can see on the top right chart, all components of the EPNL are contributing positively to the performance year-on-year. From a segment perspective, we've seen contributions from all our key segments. Retail has contributed 20% ,with private and others contributing 31% year-on-year. In wholesale bank, net income declined 32% year-on-year, but that's predominantly driven by provisions we have taken in the first quarter of this year, which are more legacy portfolio related. So not very name specific, but we felt there was a need to enhance the provision level at the portfolio level. Moving on to slide 12, which talks about the non-funded income, which has again been a key driver for our strong performance year-on-year. If one would look at what has driven the 12% growth, the 12% growth has been coming from predominantly fees and commission, which is again, a reflection of really, we recover in the economy.

The increase in fees and commission has been in the retail bank, as well as in the corporate bank. In the retail bank, it's been driven by cars fees and cars income, and that reflection of the improvement in the external environment as clients and just people in general start to travel more and post the sentiment is reflected in their spending habits. Moving forward in terms of our funded income, the only point I would like us to maybe talk about that is if you see while we have a decline in our net profit margins to 2.92%, that's predominantly driven by market pressures in terms of competitive credit environment.

However, as emphasis starts to go up, we should start seeing this number normalising, society picking up, especially because our cost of fund remains to be resilient and effective, trending at around the 30 basis point. Not expecting to see that significantly changing in the near future. From a cost perspective, the 2% reduction year-on-year I think again, quite unique given what we've seen in the market in the first quarter in other institutions, but our journey has really yielded fruited in terms of where we started in terms of our digital journey.

It is paying off, we are seeing efficiencies trickling to the system, and we are able to provide more service, better service, faster service, but at a much more efficient pace. And that's also reflected in the fact that our digital spend, again, has not reduced as compared to other items in the expense line. From a digital banking perspective, we had made excellent progress digital journey as its reflects in the UAE's highest customer ratings and other key digital metrics highlighted on the slide. Digitally active customers now represent 65% of our customer base up from 57% only two years ago.

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I've spoken about our digital activity and again, the success we've seen in our payments process were almost 99.8% going through completely digital channels. From an impairment perspective, again, a few points to call out here. Our cost of risk for the first quarter is at 44 basis points. That is probably I would call an underlying cost of risk for the bank, but it's expected to go up as we go into the next few quarters of the year, and we talk about our guidance in a second. But as we are opening new segment, that number is likely to stabilise anywhere between maybe 60 to 70 basis points.

In terms of our non-performing or NPA ratio, our NPA has remained stable at 8.8% and our coverage ratios have improved to 68%. Maybe it's better we talk about it on this slide. Yes, correct, Lamia. Thank you. So 8.8% NPA ratio has been stable and that's driven also by a bit of uptick in our non-performing assets. However, our loan growth has kept the ratio at Q4 levels, and we are expecting to see that ratio to continue improving as we go throughout the year. Our coverage ratio as mentioned, has improved to say 68.7%. We're making good progress. Only one year ago, we were 60% and our coverage ratio, including [inaudible], stands at a healthy 121%

From a balance sheet perspective, again, solid growth of approximately 6% during the last 12 months of the year. On a quarter-on-quarter basis, the balance sheet below 1% as financing and investment growth was partially offset by lower cash, central bank, and interbank balances. The 25% quarterly growth in the investment portfolio is one point to call out, which is part of a purpose study to deploy more of our liquidity, which we are enjoying ADIB. Even with that deployment, we remain fairly liquid and have ample liquidity to invest in whether it's [inaudible] or financing portfolio without creating any pressure on the funding side. From a financing perspective, again, we are seeing the healthy growth year-on-year. We have grown the portfolio, as I mentioned in my opening remarks by almost 9%. That's probably one of the highest again in the market. We've seen healthy growth both in corporate and retail side. And this trend is likely to continue. Now with rising interest rates, there might be some slow down in that area, but the mid-single digit between anywhere to 5%, 7% for the full year still remain.

Next one [inaudible]. Yeah, let's talk about on my presentation before I go to the outlook on the capital position. C81, as I mentioned, 12.7% remains quite robust and healthy with a total cap [inaudible] of 18.1. The main reason of why the ratio has slightly come off from our fully year 2021 position is that the number one, avenue has grown from a 104 to 110. The growth is predominantly driven by our increase in the investment portfolio, the Sukuk portfolio, as well as starting to consolidate some of our associates into that number. But again, it remains to be healthy and robust and it will continue to grow as we goes through the remainder of the year. Okay. With that, I'll just talk briefly about the guidance we have. So from a financing perspective, the mid-single digit 5%, 7% still holds our net profit margins between 2.9 to 3.1. Very much achievable, will all depend on the competitive environment and the decision the banks including us will have to make, how fast to pass on the interest rate hikes into the client pricing.

We need to be mindful of that as well. We don't want to push clients into a sad situation if they cannot absorb these hikes so quickly. Cost of risk, 60, 70 basis points, remains to be on track. Cost to income ratio 38 to 40, very much on track as well. The growth in net income, 15% to 20%. That's our aspiration, as we speak, we might be able to even [inaudible] on the upside, given our strong entry point into Q1. And our return equity of 17% comfortably within our full year guidance as well. So with that, I'm proposing we open up for any Q&A.

Operator Thank you. If you would like to ask a question, you can press star, followed by one on your telephone keypad, or the flag icon if you've joined online. And you can also type your question in the chat box if you're viewing the presentation. We'll take our first question from Shabbir Malik of EFG Hermes. Shabbir, over to you.

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Shabbir Malik Thank you very much for this presentation. A question on [inaudible] if I remember from the previous call, I think you said you've taken about 80% coverage for this exposure. Given that there has been a restructuring that has been completed and there is an exit instrument that has been handed out to creditors, is that something that can potentially have a favourable outcome for you in terms of provision release? Is that something that we can expect going forward? Second question is on your name outlook, I think you've cut your name outlook and you've cited some competitive pressure there and the reason for that. Do you think that despite this name cut, you will be able to achieve your profit growth outlook for this year? And my final question is on your CA SA mix, you stated in your MDA CA SA mix of 92%. In your presentation, I think it's closer to 75%. I just want to understand what is the difference between the two numbers and what should we take in our models? Thank you.

Mohammed Abdel Barry Sure. Thanks, Shabbir. So I think let me start with the first question on NMC. By the end of 2021, we had provided up to 85% of the total exposure we have. Yes, you are absolutely correct, the news and the exit instruments are indeed good news. We will watch the situation very carefully and yes, it will probably likely lead to an upside or relief once we have really reached that stage of comfort to be able to make this decision. I will not rush into that too soon, but it is fair to say that yes, there will be an upside on that in the near future. Given that you we been very prudent in our current provisioning levels by 2021. On the second point on net profit margins, 2.9%. Yes, the main pressure points we have seen is that given that the market really has not grown that much in terms of financing.

So look at it from a retail perspective, retail market is around 350 billion or so, that hasn't really grown that much. And accordingly, banks and institutions have been fighting over the same pie, which have led to yield pressures and which have triggered all the bank. And that's the reason why we have seen this compression coming also to ADIB. We still have probably one of the highest net profit margins, but it is not where probably we would have liked to see it if the market would not have been that competitive.

Having said that, as rates are starting to go up, our book reprises 50% in three months and 68% to 70% in one year. So we have the optionality and advantage to make decisions on how fast we pass on these rates to the client. And accordingly, we are still fairly comfortable that our full year target is within reach. And in fact, I am also hopeful that we can actually outperform that target. The third question was on STI and CA SA. So CA SA proposition of our total deposit is 67%. I think- 76, sorry. [inaudible]. 76, but including STI, it is 67. That's what they're saying, right? Yeah. So maybe [inaudible].

So our CA SA percentage strictly is 76%, but when we include STI balances, that percentage actually increases to 92%, which we have disclosed as part of our NDA. Yeah. Shabbir, is that-

Shabbir Malik What do you mean by STI?

Mohammed Abdel Barry These are short-term investment accounts [inaudible] CA SA balances, mainly in wholesale banking, where you have some escrow balances and some other corporate customers who keep short-term investments with us.

Shabbir Malik Sure. Thanks for that. Maybe if I can ask one follow-up question. We saw strong growth in your investment portfolio. Is this a deliberate strategy from the bank or to deploy liquidity into Sukuk?

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Mohammed Abdel Barry Indeed. So for a very long time, I think we have been trending at a certain level at Sukuk level. The bank has ample liquidity to deploy, and the bank strategy has always been that we will build our investment book in the investment grade issuances, which we are comfortable with. And accordingly, that's where you see the increase going to close to 17 billion by the first quarter of 2022.

Shabbir Malik Great, thank you.

Operator Thank you. I'd now like to remind everyone to ask a question, it's star followed by one, a flag icon, or you can type your questions in the chat box. We do have a question registered from Vikram Vis of Invicta Capital, who's asked costs are high in first quarter, and then start dropping in subsequent quarters. What's the reason for this?

Mohammed Abdel Barry Sorry, can you repeat the question again? What is that [inaudible]?

Operator Of course. So Vikram Vis has asked, costs are high in the first quarter, and then start dropping in subsequent quarters. What is the reason for this?

Mohammed Abdel Barry Okay, I think, and Vikram if you're on the call, maybe you can elaborate as well, you're probably talking about last year's trend where the last quarter was probably on the lower side, and then it started to pick up again, and then it normalises. Now, the quarter four is not a usual quarter for us. So I think we reported 531 in the quarter, which had some releases for provisions, which were not required by year end. Right? So that is a... And I think in the full year, in our announcement call for 2021, we also clarified that this is not a number which needs to be annualised. Our underlying [inaudible] currently sits around 570 to 577 for the quarter. And as we continue on our efficiency journey, there would be an expectancy this number coming off as well in a normalised level. But Q4 of last year is not a benchmark for where the underlying cost for the bank sits.

Operator Okay. Thank you. We don't have any further questions, so I'll hand back to the management team.

Lamia Khaled Hariz So Janany, if no more questions, we can conclude this call.

Mohammed Abdel Barry Give them one minute.

Operator Janany's dropped off the call. We'll put her back in.

Lamia Khaled Hariz Okay. That's okay. If no more questions you're having, we can conclude this call. Consider Ramadan timing now. So if you have no more question, we can conclude. And as usual, you can always email us or call us and we can answer them offline.

Operator We do have a question registered from Vikram Vis Invitca. Vikram, your line's open.

Vikram Vis Yeah. Thank you. Thank you, Mohamed for the presentation. Just to follow up on my question on the cost, so last year, if we look at the cost transition, the first quarter was 592 million, and then second quarter was 570 and third quarter was 567. Is that because... So in the first quarter, you have some special expenses like bonuses and some accruals. So this is the question I wanted to ask, I understand that Q4 was exceptional in

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nature, but even if you look at the first three quarter, the first quarter is high, and then the second and third quarter, there was a drop. Or maybe this was very exceptional for last year. So I'm not sure.

Mohammed Abdel Barry No, it is a trend. Yeah. I see where you're coming from because it is a trend you would expect to see. It's cyclical for us a little bit. In the first quarter, we have a bit of more expenses. Last year, if you notice, there was a reduction quarter-on-quarter. The one thing we need to also to keep in mind is that as we continue our investments in digital, and as more projects are being delivered, your depreciation elements will start to kick in. And by the time you start creating efficiencies to absorb that, then the full year number starts to normalise. And that's why you see sometimes a spike as projects are being delivered. And at the same time, the delivery of the efficiencies to combat some of this task is not coming in the same quarter. And that's what happened last year and probably will happen this year as well.

Vikram Vis Always. Excellent. Thank you. Thank you, Mohamed.

Operator Thank you. We have a question from Andrew Brudenell of Ashmore. Andrew, please go ahead.

Andrew Brudenell Hi there. Great. Thanks very much. Yes. I just wanted to get a little bit more colour or maybe just remind me of the NIM guidance that you've given, and then lowered here. Within this 2.9% to 3.1% guidance that you are now stating, what are we assuming in terms of rate hikes in that? And then I think you said in the past, you think most of the NIM improvement from rate hikes might end up coming in 2023. So I wonder if you could also give us a sense, everything else being equal. I know it's difficult, but what might look like. Because on the face, it looks a little disappointing.

Mohammed Abdel Barry Yeah. So I think that the expectations on rate hikes is changing by the minute, right? So we started the year with certain assumptions. Last month was something, and even today that completely... A few you different views on what's going to happen. So we had one hike happening already. I think there's another expectation for next month and then in June and then onwards. And we are talking about 50 basis points hikes. So now we could, if you look at the [inaudible] rate for the full year outlook, we are talking anywhere between 2% to 2.5%, which implies that there could be seven to nine of hikes of 25% now 25 basis point. Now, by the time the impact of the rate hikes trickles into the system and gives you an uplift, this will take time, not only because the repricing of the portfolio, because in fact, ADIB is in quite in strong position where it comes to repricing.

And let me just maybe repeat the earlier statement I made is that 50% reprices in three months and close to 68% to 70% of the book reprices in one year. And that's between one and three years. So our repricing cycle is fairly quick, but the main challenge which we are mindful of is that how fast you are pricing the uplift or uptake into your [inaudible] yields to the client, given the competitive advantage and the competition you are seeing in the market. You don't want to lose market share, you don't want to lose volumes and you don't want to be out of the market. So it's a very sensitive play in how you incorporate these changes into your pricing model.

Having said that, the increase will happen, but it'll have to happen gradually. And I repeat the earlier point which the call I made is that the biggest impact will really happen in 2023. This year, we will have benefits because rate hikes have happened, but the full year impact really happens only next year. And if we have a 2% hike by the end of this year, we could easily be looking at anywhere between 400 and 500 million dirham of uplift to our net profits on a like for like basis by the beginning of '23.

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Andrew Brudenell Okay. And to be clear, that's therefore not within that 2.9 to 3.1 guidance, the 200 bits rate hikes?

Mohammed Abdel Barry No, we assume that a lot of it will have to be pacing it out, given this market environment, right? So we are very, very sensible. And also if I may add, not only the market environment, we don't want to shock our clients too fast, right? So you don't want to push them. I don't want to even call the word... Say the word default, right? But you don't want to suddenly change their pricing pattern too quickly and accordingly, while you might gain a bit more, you create a bigger problem for you in the future.

Andrew Brudenell Yeah. Okay. All right. Thank you.

Operator Thank you. We do have a typed question from Chin Soen. Hi, on your 2025 medium term 20% ROE target, can you expand on the key levers you see to getting there?

Mohammed Abdel Barry So happy to. So we are already at 17%, so that's a very encouraging start. We have a few more years to come to our 20% by 2025. We are mindful as that as also your business grows, your capital will be growing as well. And accordingly, you have to be mindful of what kind of business you're writing. So there are a few elements which will get as there. Number one, the element, obviously, we spoke about interest rate hikes, that's straight-through half a billion impact for one year, starting from next year. We are very much focused on growing our non-funded income. So whether it's in the asset management space, whether it's in wealth management, just capital light product, which will get us there.

And we have clear line of sight how to reach the 20%. From an avenue perspective, we are also mindful that as we assume more risk, avenue will grow faster. But our strategy is that we are not doing either or in terms of low avenue or higher avenue] intensive business. But we are doing a very sensible mix of both, whereby capital creative business will support some of the other transaction, which might not be that avenue efficient. So all this put together, we have very clear line of sight of how to get to our 20% ROE by 2025 and possibly maybe a bit earlier.

Operator Perfect. We have no further questions registered, so I'll hand back to the management team. Thank you.

Mohammed Abdel Barry So thank you everyone for today's call and we remain available for any follow-up questions you might have. And Lamia, if you want to make any closing remarks.

Lamia Khaled Hariz Thank you. And as I said earlier, if you have any further questions, you can always email us. Thank you and Eid Mubarak to all.