Edited Transcript

Webinar with investors and analysts
National Development Bank PLC
NDB.N0000

Quarterly financial results – Q1 2018
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Best Bank in Sri Lanka 2018

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Forward Looking Statements

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Investor Presentation

Dimantha Seneviratne

Opening Remarks

Good afternoon ladies and gentlemen, and a warm welcome to the Investor Webinar to discuss the financial performance of the NDB Bank for the first quarter ended 31 March 2018.

Slide 04 - Agenda

The Agenda of today's webinar would be; let's start with the discussion with an overview of the Bank, we will then move on to the discussion on the financial performance of the Bank. At the end of these discussions, let's open the forum for questions and answers.

Slide 06 – Business Overview

You can get an overview about NDB as per the points presented on this slide.

On the awards we are quite satisfied with the awards that we won in 2018 so far. Our biggest feat was being recognized as the Best Bank in Sri Lanka 2018 by the prestigious Global Finance Magazine of USA. We also won three more titles from Global Banking & Finance Magazine of UK for the Best SME Bank, Best Retail Banking Product (Personal loans category for Dream Maker Loans) and the Best Bank for Credit Cards in 2018.

We were also recognized with a silver award for best celebrity endorsement for NDB Araliya Women's Saving Product, at the 7th Global Customer Engagement Awards at the Asian Customer Engagement Forum (ACEF) held in Mumbai.

Slide 07 – Business Overview – Strategic Focus

Last year we launched the Transformation 2020 strategic plan, which is our strategy spanning up to 2020. We had professional inputs in this strategy from the International Finance Corporation (IFC) Advisory Team. The ultimate goal of this strategy is to convert NDB Bank as a systematically important private commercial Bank by 2020 with an asset base of around 20% growth. We also have a liability driven strategy where we would have our own funding to support our assets growth. Our business focus will be more on retail and the business banking areas while also growing Project and Corporate Banking Books of the Bank.

Our strategy is well on track. We have made the investments in IT and also in developing staff by aligning the entire staff into One NDB Team, which has progressed quite well. Some of the results especially the 1st quarter results were achieved by the strategic initiatives that we have already launched in 2nd half last year.

Slide 09 -Key Performance Indicators [Bank]

Moving on to the financial performance, the KPIs for 1st Quarter 2018 are mainly driven into 4 quadrants, Profitability Indicators, Balance Sheet Indicators, Efficiency & Return Indicators and Business Capacity Indicators. In terms of Profitability we will be discussing more in detail later.

For now, NII was up by 44% compared to similar period last year to LKR 3.4 billion. Net fee and commission income grew by 28% to LKR 710 million. Total operating income grew by 44% and total operating expenses were quite well managed at a 12% increase despite the VAT increase. Profit after Tax has grown by 35% year on year to LKR 1.561 billion. Group Profit Attributable to Share Holders was up by 56% to LKR 1.152 billion.

In terms of the Balance Sheet, the total asset growth for the three months was 3% and total assets touched LKR 396 billion. The Net Loans recorded a 3% growth to LKR 282 billion. Deposits recorded a 4% growth to LKR 284 billion, this is the first time we have outgrown deposits. Deposits figure is now above the advances figure. Total Assets of the group level crossed LKR 400 billion. In terms of the efficiency, the cost to income ratio improved quite well to 35.8% from 45.5%. Net Interest Margin which we were working very hard on improved to 3.49% from 3.0% last year.

Return on Equity which has also improved from 16.2% to 16.8% and the Return on Average Assets have improved from 1.21% to 1.26%. In Business Capacity ratios, Loans to Deposits as I mentioned has now improved to almost 100%. Tier I and Tier II capital levels are well above the Statutory Minimum Requirements, Tier I at 8.73 % and Tier II at 13.35%. The Liquidity Coverage Ratios are also well above the minimum statutory requirements.

Slide 10 -Income Statement (Bank)

Moving on to Income Statement in detail, as I mentioned earlier, Gross Income had a 20% growth quarter to quarter where we ended up with a LKR 1.9 billion increase per quarter or a 20% growth. Total Gross Income was LKR 11.9 billion.

Net Interest Income that has the highest percentage growth of 44% reflecting the improvements in the margins. In the beginning of last year, 2017 the NIM was 2.6% and we have moved up to 3.49%, so almost 90 basis point improvement at NIM level.

Fee & Commission income again reflected a 28% quarter to quarter growth to cross LKR 700 million. So overall Operating Income has grown by 44% to LKR 5.4 billion. Of course there is a sizable impairment charge compared to 1st quarter last year. One was on prudence basis that we made certain impairments and also there is a trend in the industry where NPLS are gradually picking up. Of course we are relatively better than the industry but we were prudent in providing some impairment and also the SLFRS 9 impact was also taken into consideration in making provisions .Accordingly, net of impairment, the Net Operating Income has grown by 27% from LKR 3.6 billion to LKR 4.6 billion. This is an almost LKR 1 billion increase at the Net Operating income level.

The total operating expenses increase as I mentioned was 12% from LKR 1.7 billion to LKR 1.9 billion. We have been curtailing the expenses where ever possible, as a very good cost management discipline has been introduced. Cost champions are appointed to ensure controllable costs are managed and that exercises will continue to progress and will ensure our Cost Income Ratios are maintained well within the requirements that we have. Operating profits have grown by 40% from LKR 1.9 billion to LKR 2.6 billion. Of course tax component is quite sizable, one is that tax rate has gone up. So that has a 48% increase in taxes so the 1st quarter we have made provisions for LKR 1.1 billion. Profit after Tax we had a 35% growth from LKR 1.1 billion to LKR 1.56 billion. The Group Profit Attributable to Shareholders also had a 56% growth from LKR 738 million last quarter 2017 to LKR 1.1 billion in the 1st quarter 2018.

Slide 11 - Revenue Analysis - Fund Based Income

Further analysis of revenue is available on fund based income. Interest Income grew by 16% from LKR 8.5 billion to LKR 9.9 billion while the interest expenses grew by only 5% from LKR 6.2 billion to LKR 6.5 billion, which shows the improvement in the NII growth of 44% that also resulted in 71 basis points increase in NIM from 2.78% to 3.49%. It is mainly coming from interest income side. On interest expenses, although our deposit portfolio had a highest growth last year, i.e. we had almost LKR 70 billion in new deposits that came in, this shows that the deposits have come at a reasonably good cost. We should also take into account the CASA contribution last year which was at around LKR 12 billion. So all of these have contributed to improve our NIM in this manner.

Slide 12 - Other Income

Further analysis of Other Income is available in this slide. Net fee and commission income recorded a growth of 28% to LKR 710 million. Net gain from trading had a 30% growth from LKR 273 million to LKR 355 million and there is a Net gain of LKR 310 million in the Financial Investments mainly on the Treasury Bonds. Other operating income grew by 13% from LKR 603 million to LKR 683 million. So total non-interest income growth was 44% from LKR 1.4 billion to LKR 2 billion.

The good thing of all this is that the revenue has come from all Business Segments, Corporate, Retail , Business Banking where all segments have contributed equally for the growth and we would continue to focus more on the Retail and Middle Market side where we see the opportunities, given our presence in 107 branches. Of course the comparatively high gain from ALM also contributed to this net gain from financial investments due to the favorable movement in interest rates.

Slide 13 - Operating Expenses [Bank]

We had an overall increase of 12% in operating expenses, with 11% growth in personal expenses from LKR 918 million LKR 1 billion. Naturally one is the staff increase, we roughly had about 100 staff members increase from last year to this year quarter and apart from that we had salary increments. Other expenses had a 16% growth and cover the VAT and other administrative expenses.

Still I would say the 12% increase in operating expenses is commendable but I think we are still working on further improving on the cost management side. Why I am saying the increase in the cost levels is commendable is because, we had some big investments where we had new 3 Privilege Banking centers (for HNW clients) that were opened. Additional 4 branches were opened last year, we relocated branches where there cost elements were quite high. All this contributed to 1st quarter 2018 cost. Also we introduced Cash recycling machines. Despite that 12% increase in cost, I would say it is well managed so far but of course going forward with the salary increments we might see slightly more increase in this cost segment. We are working on controlling the controllable costs using costs champions.

Slide 14 - Balance Sheet [Bank]

On the Balance Sheet; I would say we had a moderate growth in 1st quarter. Of course when we are comparing from the 2017 December Balance Sheet where we had an exceptional performance, in particular from the latter part of the year. So overall the growth in Balance Sheet is 3.3% from LKR 383 billion to LKR 396 billion, about LKR 13 billion growth. Of that; the loan growth was almost 3% and deposits 3.8%. In terms of the quantum LKR 10.8 billion in deposits and 8 billion in loans. At the Group level the total assets crossed LKR 400 billion as at March 2018 from 389 billion last year. That again is about a 3% growth.

Slide 15 - Loans & Receivables [Bank]

The 1st quarter 2018 reflects a moderate growth in loans, coming from Trade Financing, Consumer and also Term Loans. Corporate Banking accounted for the highest portion of the growth but we have seen the Retail and middle market also contributing. In terms of the currency composition the local currency to foreign currency mix has improved now to more towards local currency at a 78:22 ratio. You may recall at the beginning of the last year this was roughly 75% to 25%. That is one our strategic imperative to move towards a more LKR base lending book.

Slide 16 -Asset Quality

NPL ratio has slightly deteriorated from December figure but still remains below the Industry average. Our NPL ratio has gone up to 2.46% whereas the industry average is around 3.0% as at March 2018. Of course we have seen certain pressure on some of the portfolios which is seen across the industry and they are not limited to any specific client. We have seen some collection issues which are the case in the industry as well. Naturally with a low growth rate in the country there is a stress level that will reflect in any bank's portfolio. But we are bringing our standards especially at the monitoring level; our underwriting standards are quite good, but basically following up on general delays and where ever we can help our clients we help them and also enhance our monitoring and collection arrangements to ensure that we manage this properly.

Our portfolio is quite diversified; there is no concentration risk in any particular area. But with these more monitoring proactive measures, we expect the NPL ratio to improve as we move along towards the latter part of the year.

Slide 17 -Customer Deposits

Quite a good growth of LKR 10.8 billion in deposits. In terms of the composition, 82% of deposits have come in LKR terms whilst 18% is in foreign currency. CASA ratio is at 22%. In an environment where savings capacity is also getting limited maintaining a CASA ratio is a challenge for any Financial Institution but we will be working hard on improving this to ensure our cost of funds are managed further down. Of course we have a couple of products and CASA driven strategies that we have launched recently so we will be looking at reaping the benefits of such arrangements in the coming month.

Slide 18 - Capital Ratios

In terms of the Capital Ratios we are quite well in terms of the minimum capital requirements. Tier I – Bank at 8.73% and at Group level 10.1%. Tier II – Bank is 13.35% when the minimum requirement is 11.875%. So we have roughly about 150 basis points above the minimum requirement. At Group level it is 14.44% so we are well within the Risk Parameters in meeting the capital requirements. However, looking at our growth opportunities and impact of SLFRS 9, we will be looking at capital infusion in future/ during this year.

Slide 19 - Investor Ratios

Share price remains almost at the same range compared to last year which closed at LKR 136/40 and now at LKR 133/10. This is hovering around LKR 134/-. Earnings per Share have improved from LKR 24/52 to LKR 27/62 on an annualized basis. ROE has improved from 16.27% to 16.78% and ROA from 1.21% to 1.26%. Book Value per share remains at higher LKR 167/31 and also the Price Earnings ratio at 4.82 times. We would be focusing on ROE. The 16.78% ROE compares quite well with the industry ROE of 17.1%. We are comfortable that we should be able to cross these industry level averages as we move along, especially on the profitability side. I would say NDB share continues to be an attractive buy since it is trading below the Book Value.

These are basically the industry ratios that are been shared with you. I am sure you'll have enough questions. We are happy to answer any questions. Clarifications that you may have.

Questions and answers session

(Answered by the CEO, unless specifically mentioned)

Q1: What are your plans to sustain CASA at tolerable levels?

Sanjaya Perera: With our Transformation 2020 strategy, we have specially focused on growing CASA deposits and if you have noticed last year we have come out with many new products promoting CASA. Also we had promotions throughout the year and in the 1st quarter of this year as well we had very successful promotions for promoting CASA. I am sure with this and with the expansion of the Branch Network and focus on Retail and SME and the segmentation of Current Account segments of our Business Clients we are hopeful that our ratios will improve. Although we have shown a significant growth in CASA, rest of the deposits have grown at much faster pace so you will not notice an improvement in the ratio. We will sustain and improve the CASA growth in future as well.

CEO: I think apart from the product launches that we had I think we have been addressing staff mindset to move towards more liability driven strategy and in that the growth in CASA is one of the prime goals in the targets given to them. So as Sanjaya mentioned one is the product strategy and the other is the incentives and to ensure that we maintain that momentum specially the contribution for Business Banking clients is also high because for any Business banking client brought in, they would be required to open a current account and also to open their ancillary accounts opened with us. With this we are looking forward to improve our CASA ratio further.

Q2 - There is a LKR 2 billion increase in NPL in the quarter. Would you be able to give a sense of which segments and sectors this has come from?

Buwenaka Perera: By and large it has come from the manufacturing sector where we have seen certain areas in manufacturing sector due to poor collections in the market but I believe we would get this improved as time moves on.

Indika Ranaweera: Apart from that, in middle market side due to poor collections we are experiencing the same but as a Bank we always help by restructuring to overcome this situation.

Q3 - Private Sector Credit growth is very high at 4.6% year to date and NDB had a loan growth of 3%. What is your target loan growth for 2018 and 2019?

Of course in 2018 we will naturally grow more than the market rate. Rather than commenting on our figure I would say it will be above average growth rates. So we will be working hard to ensure that the next three quarters provide more than what we achieved in Q1 in terms of the loan growth. But that doesn't mean that we are bringing down our underwriting standards. Still there are opportunities in retail markets and also in corporate side as well.

While maintaining our high credit standards there are quite a lot of opportunities where we will look at the higher growth in the advances side in coming three quarters.

Q4 - What's your view on Interest rates going forward and whether there is any pressure on NIM considering the decline of policy rates by 25 basis points in April 2018?

Niran Mahawatte: After the rate cut , Central Bank has also clearly stated that the tightening cycle is over , so we think at least for this quarter and in the next quarter the rates will remain stable at the current levels. This will put the Bank actually in a much better wicket because the way our Assets and Liabilities are structured, we are in a very good position to expand our NIMs further.

Q5- Corporate segmentation is currently 57% of the loan book. Do you expect this to be continued for the next 3 years from now on? How would you be targeting more on Retail and SME?

Of course the 57% is Corporate including commercial banking and project financing. In this Project Finance has got certain middle market clients as well. Of course the focus would be while growing the corporate portfolio to concentrate more on Retail and SME side and Business Banking. That's why we set the new Business Banking segment with special strategies to grow this segment, working hand in hand with the branch network and making use of the present 107 branches we have in our hand for us to approach those customers at SME and Middle Market level.

We also have a very good personal banking portfolio i.e. Dream Maker loan. It is the best Personal Banking portfolio plus, we have quite a good leasing portfolio. The Credit Cards are progressing quite well. So we put our resources more into growing these sectors. As I mentioned in previous presentations like this, one way to improve our Risk Profile is by spreading our risks and that's where there is a better margin plus touching a customer base of a larger community and they would also be part of our clients and will have our normal other operating accounts. This will have lot more cross selling opportunities when we grow in retail and SME space.

Naturally with all of the above the mix of the Balance Sheet is expected to shift more towards Retail and Business Banking segments by 2020. The target is almost like 50:50 or slightly higher contribution coming from Retail and SME space compared to where they are.

Q6: Can you elaborate further on the LKR 310 billion Financial Investment Gain?

Niran Mahawatte: This was mainly derived from our Bond Portfolio where we managed to derive some of the investments gains from the favorable movement of the interest rates.

Q7: Is there any update on the Debt Repayment Levy? Is it implemented or scrapped?

Lalith T Fernando: We have not received any communication from the IRD about that so far. There is no update which we can provide.

Q8: Is the impact of SLFRS 9 included in the quarter? Can you please some further analysis in impairment?

Lalith T Fernando: SLFRS 9 impact is actually disclosed in the quarterly publications, the impact to what extend it is going to be at the year-end - it's about 30% to 35% and up to 40% on the opening provision. For capital requirements, Central Bank has given a verbal indication that it will be over 3 year time horizon but in the books we will be adjusting it at the year-end which the other banks also have followed, and will not reflect in the quarterly financial statements in the Balance Sheet, It's only a disclosure.

Q9: What will be the increase in annual provision of IFRS 9? Is it same as 35% to 40%?

Certainly not. I think this is the first day impact. This is the first day impact based on IFRS 9 and when you stress your portfolio, now under IFRS 9 entire 30 days + arrears portfolios have to be discounted at the cash flows. The impact is assessed based on that.

So the first day impact is around 35% to 40%, but that doesn't mean the entire provision level would go up by that percentage. Under IFRS 9 we need to account and impair the entire portfolio, looking at the full tenor of their credit cycle there will be an increase in the provisions. It is an industry wide increase and the indications that we have received from Audit Firms is that there will be roughly around 10% increase in general provisions. So it's not unique to a particular bank and industry wide we can expect roughly 10%-15% provision in overall provisioning because of IFRS 9 Accounting treatment.

Q10: What is your strategy on Digital Banking side?

Sanjaya Perera: I think we already have the best mobile banking application which we want to further enhance on. Also for the Business segment we have the E-Windows platform which is used heavily by the Corporate and as well as SME sector. You would have noticed that we have launched cash recycling machines in certain strategic locations, facilitating deposits as well as withdrawals and also the tab banking which was launched across the branch network going into door steps and collecting cash. Those are the digital channels which we have started now and we are working on more initiatives.

CEO: We have setup a separate Digital Banking Business Unit itself, there is a team working quite hard on that area so as Sanjaya mentioned we have some good head starts in terms of the mobile app, branchless banking is at about 25 of our branch network, which will be launched to the entire branch network. Apart from cash recycling machines we are looking at few digital focused branches in going forward because rather than a brick and motor branch expansion itself; we are looking at a digital avenue as a major contributor going forward to grow our Balance Sheet. So already it's taking progress with some professional input on this so we are working on the digital strategy quite well.

Q11 – Is there a specific advantage of the current LKR depreciation given your higher exposure to foreign loan segment?

Niran Mahawatte: Actually what happens is when both Assets and Liabilities get revalued, it basically get netted off. From Balance Sheet point of view there is no much of a difference but it will reflect only in Off- Shore profit component which is in USD term, which will get revalued and will show a slightly higher profits. We have been getting this income in our normal business but this time it's a bit of a steep revaluation during the two months which will be reflected in June numbers.

Q12 How is the Macro Economic growth during the year and do you expect continuous stress on NPLs at the industry level?

It's an industry wide phenomenal, and it's not fair for me to comment. But in generally I can comment as this is a natural cycle we have seen over the years. Whenever the growth rate is low naturally there will be a lag effect and NPLs are going to pick up.

So we are going through the same cycle and last year we came up only with a low growth rate and naturally we can expect some stress levels in our portfolios so I would say that at Industry level which NPLs are picking up to 3% which was somewhere around 1.8 % at the beginning of last year so there can be a trend. I think the Banking and Financial Institutes have to rise for this kind of situation, improve your monitoring mechanisms and wherever the real situation is there we should also help our clients and improve our standards of monitoring.

End of Q&A.

Closing remarks

Thank you ladies and gentlemen for your participation and the very active engagement in the Q&A session.

If you have any more questions, please feel free to reach us through our email investor.relations@ndbbank.com and from our contact numbers given.

The NDB Team, I, the Management and all of the Team is working as One NDB in continuing this tremendous performance in to the future.

End of edited transcript.