Edited Transcript

Webinar with investors and analysts
National Development Bank PLC
Quarterly financial results – FY 2016

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YOURS

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Forward Looking Statements

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Investor Presentation

Dimantha Seneviratne

Opening Remarks

Good afternoon everyone, thank you very much for connecting to our investor webinar to discuss the financial performance of NDB Bank for the financial year 2016. I have two of my colleagues with me, the Group CFO and the Vice President Corporate Banking, and also a Team from Finance to answer any questions.

What I will do is, I will quickly take you through the presentation on key points and thereafter take any of the questions you have.

Slide 03 - Overview

On slide number 03, you can see the holding structure of the Bank, where the Bank holds 99.9 % of NDB Capital Holdings and there are basically four different companies in investment banking, wealth management, stock brokering and private equity management. This is a unique proposition that the Bank is offering to the Sri Lankan banking sector.

Slide 04 - Brief History - Milestones

This slide is on a brief history of how we have evolved over the years, from 1979 as a development financial institution, then the acquisition of the ABN AMRO Bank Colombo in 2001 and thereby commencing commercial banking operations, and now being retail banking oriented. Right now we are operating with 105 branches. About 50 of those branches have been added on to the network during the last five years.

Slide 05 - Macro Economy & Industry Overview

Moving on to the macro economy and the industry overview, the global economy grew by 3.1%, and China, the world's largest trading nation posted the lowest GDP growth in 26 years. So that was one key point. Also, the weak global demand continued throughout 2016.

When talking about the Sri Lankan economy, the GDP growth was also lower than what we expected, around 5% in 2016. A couple of key positive changes were also seen during the year such as enhanced currency flexibility which contributed towards short-term stability of the economy. The annual average inflation was around 4%. The regulator also initiated few key policy decisions, one of them being the revision of the statutory reserves requirement from 6% to 7.5%.

These were all signals given by the regulator in terms of curbing the interest rates hike. As a result, at the industry level, the overall credit growth was limited to around 17.5% in 2016, compared to the 21.5% in 2015. Deposits grew at about 16.5%. Margins remained at 3.6% despite the cost of funds going up. At an overall banking industry level, profitability improved mainly due to low credit losses. The overall industry NPL ratio is about 2.7%.

Slide 06 - Awards & Accolades

These are details of all the awards that we have won. One of the key awards was the CFA Sri Lanka Best Investor Relations award. This is in recognition of the interactive webinars, answering the investor questions and interacting with them on a regular basis. Euromoney recognized NDB Investment Bank for the fifth consecutive year as the best investment bank in Sri Lanka. NDB Capital Bangladesh also won the same title in Bangladesh. Talking about investment banking activities, last year NDB Investment Bank raised LKR 31.5 billion worth of debentures and enjoys about 40% market share.

Moving on to the financial performance of the Bank;

Slide 08 - 2016 Performance Summary

In terms of Profitability, the operating income grew by 8% to LKR 13.2 billion from LKR 12.2 billion. On the other side, operating expenses grew by 7%. Profit after tax however saw a 10% reduction to LKR 3.1 billion. This was mainly due to high impairment charges. We will discuss more about it in due course.

In terms of the Balance Sheet position, total assets have grown by 8% to LKR 335 billion. This roughly accounts for about 4.5% of the market share. Total loans grew at 9% from LKR 215 billion to LKR 234 billion. We also moved based on the direction given by the regulator last year. We were focusing on improving our margins and focusing on quality asset growth, in terms of volumes. So that was another challenge. In terms of deposits, same grew at 10% from LKR 185 billion to LKR 204 billion. So roughly about LKR 19 billion in terms of deposits.

The rate of growth in deposits, compared to the rate of growth in loans was high, and the Bank was conscious of these growth rates. Historically our LD ratio has been high. This is due to the development banking set up and the relatively young retail base, in terms of number of branches.

In terms of efficiency, the cost to income ratio has improved from 49.5% to 49.0 %, and this is an area that we have to do better. In terms of Net Interest Margin (NIM), despite the rates going up, we have managed to retain/ sustain the margins at 2.6%. So that I would say, on one side a satisfactory performance. But on the other hand, compared to industry, we are below the norm and we are working on improving this ratio. In terms of returns on average equity, this has come down from 15.6% to 13.4%. This is again an area that we will have to focus on going forward, which was mainly due to the drop in profitability last year.

Slide 09 – Income Statement

This shows more information on the net interest income and other income. So overall, the operating income has grown by 7.7%. LKR 942 million in terms of the variance. But as I mentioned, the major area that we encountered was the impairment charges which moved up from LKR 712 million to LKR 1,367 million. So it has almost doubled from what we have provided the previous year. So that is one of the concerns we have which we are also handling prudently.

In terms of operating profit, it has come down from LKR 5.4 billion to LKR 5.3 billion.

As appended in the graph on this slide, the contribution of NII of LKR 965 million has been affected by the impairment charges. Operating expenses have grown by 7% but this is reasonable compared to the inflation and the expansions we have gone through.

Slide 10 - Net Interest Income

This slide shows how NII has grown, with a detailed breakdown on a quarter basis. I do not want to spend much time on that but I would like to discuss Other Income.

Slide 11 - Other Income

This is one area that we are very keen on going forward. Fee and commission income has grown by 11.8% from LKR 2 billion to LKR 2.3 billion. So that would be one of the key areas that we focus. We have quite a good corporate banking portfolio. So this would be an area that will be able to capitalize on going forward. The other side of this is forex income. There is a lower contribution of LKR 1.1 billion. This was made difficult due to the lower ALM activities on the forex operations.

Slide 12 - Operating Expenses

Moving on to operating expenses, overall operating expenses increased by 7%. Within that personnel expenses grew by 7.2%. Depreciation is a small component. Other expenses grew by 4.2%. The overall cost to income ratio has improved from 49.5% to 49%. Cost to average asset ratio has improved from 2.12 to 2.00. One specific point that I want to highlight is the branch expansion. Last year we added 11 new branches to the network, so by the end of the year there were 104 branches and around 70 staff was added to the network. We have also made some technological advancements during 2016.

Slide 13 - Balance Sheet

Moving on to the Balance Sheet, assets grew by a modest 9%. Loan growth as I mentioned was curtailed, one due to the interest rate, the other due to the policy measures that took place.

The deposits growth was higher than the loan growth, but there again; most of these deposits came from fixed deposits. That is why our CASA ratio is at around 23%. This is a key focus area for us - to shift the deposits away from high cost deposits. The other issue was that the differential between the fixed and savings deposits were quite high, so in that scenario, there was a tendency for the entire banking industry to manage the cost of deposits.

Slide 14 - Loans and Advances

Loans and advances recorded a 9% year-on-year growth in 2016. The retail and SME sector contributed by 41% of the total mix. Corporate banking was 33% and project financing was 23%. Project financing is a key area where the Bank has funded several infrastructure projects. Corporate banking has consciously rationalized the portfolio.

Slide 15 - Asset Quality

Talking about asset quality, the portfolio mix, agriculture is 10%, a regulatory mandated area where we are meeting that requirement. Hotel sector is also 10%. This pie chart shows a well-diversified portfolio.

In terms of NPL ratio, we have given a sector wise break-up on this slide. One significant area is textile and garments. This is due to few specific customers. It is one of the historical NPLs and the exposure to the textile and garments sector has come down now, and as a result shows an increased NPL ratio.

In terms of Gross NPL ratio we are maintaining the ratio within industry average. The industry has also improved over the years, especially during last year.

Slide 16 - Customer Deposits

Moving on to deposits, we have grown our deposits by 10%. The pie chart shows the CASA composition of 23%. In that 23%, demand deposits are 8%. This is one area that we focus on. Our CASA ratio is below the industry average and also the larger banks. But it is also an area that we have a lot of opportunity in.

In terms of liquidity, we have maintained same well above the regulatory requirements.

Slide 17 - Capital Adequacy

In terms of capital adequacy ratios both Tier I and Tier II remain very much above the regulatory minimum requirement. The Tier I ratio is 9.3% and the Tier II ratio is 13.0%. We are quite comfortable there. But as we go on expanding the business and as per the Basel III requirements, we will need to improve our capital base and that is something we are currently working on, going forward this year.

Slide 18 - Investor Ratios

On investor ratios; EPS has come down, from 21.26 to 19.19. ROE has also moved in the same direction from 15.63% to 13.36% whilst book value per share has gone up from 137.4 to 149.8. The share price is trading near the book value; as such the price to book value is at 1.

Let's now move on to questions and answers.

Q & A Session

Q: Can you please give the reasons for the impairment charges in the last year.

The Bank had to make specific provisions for a few customers, based on the overall performance of the country, particularly due to the negative effect on the plantation sector.

Q: What is the Bank's expectation for the loan growth and the deposits growth for the next three years?

At the moment, we are working on our strategic plan in which we will look at ways to improve our growth. Since the strategy formulation is still under way, we cannot comment about what numbers we are looking at. But certainly, we target above market growth rate. To achieve our market share targets we have to have above industry growth rates. We will be able to share more details in the investor meeting for the following quarter.

Q: How many branches do you wish to open during 2017?

Again, that would be a part of the strategic plan. Last year 11 branches were added on. But for the time being, we have already received approval for 3-4 branches. We are working on those. We also look at branch relocations and branch renovations. We just relocated our Wennappuwa branch. It is not only the branch network that we are looking at, but also the facilities that we provide to the customers are looked at. There are also other channels to reach the customers. Digital channel is one area that we focus more.

Q: What do you expect the interest rates to be in 2017?

It is based on the investments/ foreign borrowings. The indications are that the rates will stabilize. But on the other hand, there are signals to indicate the increase in inflation. The credit growth remains higher than what the regulator is expecting. Given these situations it is quite difficult to predict. But for a bank, in terms of interest margins, we have to work on the margins because that is where we have enough scope. We will focus on what we can do well and what is within our control.

Q: With the increase in interest rates and the subsequent impact on interest income, how do you plan to maintain cost to income ratio?

Cost to income ratio is 49% and below 50%. But there is still room for us to improve. One reason, the cost to income ratio is within 49% despite adding several branches to the network. So we have managed to keep it below 50%. Another area is focusing on the fee based income. We have more opportunities here to improve on. The other important aspect is to improve the CASA base. We have a lot of room to improve on this line as well. This is where the investment in the branch network will help. We have 105 branches now.

Q: Which industries/ sectors do you expect the growth to come from?

Looking at the developments in the country, one main area would be construction. With the branch expansion, there are a lot more opportunities. We are at the right places. National Development Bank, functioning as a bank with a national orientation will help the development of the country not only in the Western province but other provinces as well.

Q: Currently are term loans given at fixed rates or floating rates? Will there be a further rate hike in the near future?

Actually we have both options, term loans at fixed and floating. Both options are there. It is up to the customers to choose which option. Majority of the loan book is variably rated. So even if there is a rate hike, the impact would be managed.

Q: What is your target LDR for 2017?

We are currently focusing on this area. We would naturally bring it down to below 100%.

Q: How much is your market share in credit cards?

I think we do not have full information as at December 2016. But in terms of the portion, our share is less than 2%. This again is an area where we can focus on; where more room to grow is available. Given our valid proposition, we should consider how we acquire customers and what services we offer. There is a lot more there that we can do.

Q: Given the weak macro-economic outlook at the moment, we expect the asset quality to worsen in 2017. Can you comment please?

I think Sri Lanka has gone through worse situations with the height of war. However the credit quality has improved. If the underlying standards are maintained at high levels, follows ups and recoveries are stable, I do not think that the industry will be affected. In terms of the Bank, the underlying standards have been very strong. How you manage the relationships, how proactive you are to what is happening in the industry and taking proactive measure are what matters and ensures good credit quality.

Q: How much is the capex per branch?

This varies from bank to bank. It is also not proper to disclose this type of information at a forum of this nature. Some banks have a minimum number of staff like 5, but some banks have a larger staff at branches. It also varies from branch to branch. What is more important is to expedite the break even.

We see some branches breaking even in 18 months. Some branches take more time. So the focus is more on breaking even.

Closing Remarks

Thank you very much for your attention and also for your questions. We are looking forward for similar kind of interactions. So thank you very much for the attention given.

End of edited transcript.