Abu Dhabi Commercial Bank PJSC
Q2/H1 2020 Earnings Call Transcript

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ADCB Speakers

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Kevin Taylor - Group Treasurer
Monica Malik - Chief Economist
Denise Caouki - Head of Investor Relations
Naresh Bilandani Good day everyone, it’s Naresh Bilandani from J.P. Morgan. I’m pleased to welcome you all to this call with Abu Dhabi Commercial Bank management to discuss their second quarter 2020 results. We have the full management team here with us, and I’m going to pass the call now onto Denise, who is the Head of IR, to kick this off. Denise, all yours.

Denise Caouki Thank you Naresh. Ladies and gentlemen, thank you for joining us to discuss our second quarter financial results which were announced today. On this call we will be giving you an overview of the Bank’s financial performance, our continued response to COVID-19, as well as an update on merger related synergies, following completion of integration in April. Finally, we will finish by taking any questions. We have provided a detailed presentation which has been shared with you and can be found on our website.

Today, I am joined by Deepak Khullar, Group CFO, Kevin Taylor, Group Treasurer, and Monica Malik, our Chief Economist. I will now hand over to Deepak to begin the presentation.

Deepak Khullar Thank you Denise and thank you everyone for taking the time to join us. I trust you all are keeping safe and well. I would like to invite you to turn to slide five of the investor presentation deck, for an overview of what we will discuss today. The Bank continues to support its key stakeholders through the COVID-19 situation since responding quickly in Q1 to roll out a comprehensive package of measures to support our major stakeholders.

I am pleased to report that despite the tough environment, ADCB continues to make good operational progress in the first half.

As a result of the successful process of integrating systems and migrating former UNB customers in April, we increased our synergy target to AED 1 billion. And introduced a series of bank wide cost initiatives to enhance efficiencies further. In the second quarter, we reported a sequential increase in net profit due to lower impairment charges and an improvement in operating expenses, demonstrating that our underlying business remains resilient.

We continue to take a prudent approach to risk management in light of the prevailing macroeconomic environment and ADCB is focusing its efforts in building sustainable shareholder value. I will go now into more detail on our response to COVID-19 on slide six. ADCB’s reaction to the challenges of COVID-19 highlights the strong culture of our organisation. The bank is leveraging its financial strength and expertise to support customers, employees, business partners and communities in line with the directives and initiatives of the government.

We continue to support the decisive measures taken by the UAE Central Bank to cushion the impact of COVID-19 on the economy through an extensive package announced in March. As the Central Bank launched its Targeted Economic Support Scheme, or TESS, ADCB was the first lender to offer relief measures for customers, including instalment deferment, fee reductions and waivers, temporary interest rate reductions and rescheduling of working capital facilities. As at 30th June, the Bank has provided deferment of loan instalments, totalling AED 8.3 billion to over 53,000 customers.
We rapidly created an effective remote working framework and we are now implementing a gradual return to the workplace plan with all the necessary precautions in place. Throughout this period we have maintained continuity in service through enhanced digital capabilities. Since lockdown measures began to ease in April, we have steadily reopened branches, and over 50 are now operational. To further support our communities, ADCB has invested AED 9 billion to support distance learning for students and to express gratitude to frontline healthcare professionals.

Slide seven shows how branch and ATM transactions have rebounded since April, as stay at home measures were relaxed. Branch interactions are approaching levels seen in February. On slide eight you will see how ADCB’s focus on digital channels delivered impressive results during the first half, seamlessly serving our customers through a period of considerable disruption to daily lives. Mobile banking has seen particularly strong uptake. I would also like to update you on the development in our digital transformation journey.

On slide nine you will see that the Bank has successfully completed 39 digital releases in the first half of 2020, more than three times the same period of 2019. This has not only enhanced service, but also facilitated the onboarding of new customers. By June, over half of new-to-bank customers at ADCB were enrolled digitally, compared to 35% in 2019. As for Al Hilal Bank, a new strategy was launched last year, which focuses on offering retail customers Sharia-compliant products and services through digital channels.

This approach is gaining strong traction. The number of new customers joining through Al Hilal Bank’s app in the second quarter was triple the quarter four 2019 total. Meanwhile the cash management and trade finance digital platforms offered by ADCB’s Wholesale Banking Group continue to prove highly popular with our clients. The transaction processed through ProCash increased to 93% of the total in the first half and ProTrade accounted for 61% of total trade finance transactions, up from 48% in 2019.

The trend towards digital banking at ADCB has accelerated significantly in just three months and will continue as we execute our digital transformation programme. You can find further information on our digital progress on slides 10 and 11. Please turn to slide 13 for an update on the successful completion of integration following the combination with UNB and Al Hilal Bank. To recap, our fast track process was completed within only eleven months of the legal merger - less than half the time originally foreseen - and the integration programme was formally closed down on April 15th.

There’s still some work left to be done, that will carry on in the second half of this year. But the programme has formally closed down. Due to the effective execution of integration, we upgraded our run-rate synergy target to AED 1 billion from the previous target of AED 840 million. This is materially higher than our original target of AED 650 million. We are fully on track to achieve 75% of this new target in 2020 and to reach the full target in 2021.

On slide 14 you will see that we realised AED 411 million of synergy in the first half, with AED 185 million achieved in quarter one, which increased by another AED 226 million in quarter two. Cost efficiency gains have been derived across the board, including from productivity enhancements, branch optimisation and economies of scale.

Furthermore, integration related costs are tapering off and remain well below budget, with quarter two costs only at AED 22 million, bringing total integration costs incurred so far to AED 557 million, excluding capex. I will now hand over to Kevin, who will discuss developments in the operating environment this year.
Kevin Taylor: Thank you Deepak. Slide 16 and 17 show the key indicators of economic activity in the UAE in the first half of 2020. We are forecasting that the macroeconomic headwinds from the COVID-19 pandemic and the decline in oil output will result in a 6.5% contraction in real GDP in 2020. Before a partial recovery in 2021, when we are forecasting a 2% growth in real GDP. Global oil prices have seen some recovery from April lows, supported by production cuts and improved demand.

Nevertheless, the current global climate continues to severely impact activity in key sectors of the UAE economy. External headwinds are expected to put further pressure on economic output for the remainder of 2020. The combination of COVID-19 and lower oil prices will continue to weigh on consumer sentiment and the businesses of our customers for the foreseeable future.

Aviation, logistics, retail, tourism and hospitality have been particularly impacted by the reduction in the global travel and trade. On slide 18 you will see that despite the tough operating environment, banking sector liquidity remains robust. Following the measures taken by the UAE Central Bank, including a relaxation in LCR and reserve requirements. The Central Bank’s measures, and a rise in government deposits from April, is helping to make up for the higher GRE funding demand.

During the first half, there was a sharp drop in benchmark rates as the US Federal Reserve took monetary action to cushion the economy from the impact of COVID-19. Turning to slide 19, you can see that the contraction in Abu Dhabi and Dubai real estate sales and rental prices in April and May remain broadly in line with the declining trends seen in the first quarter. However, we see downward pressure in the real estate market increasing going forward.

On slide 20, consumption indicators reflect the challenging economic environment in the first half. However, there was a notable rebound in credit card and debit card spending in May as restrictions on the retail, leisure, hospitality and food & beverage sectors were eased. I will now hand back to Deepak to take you through the bank’s Q2 financial results on slide 24.

Deepak Khullar: Thank you Kevin. I would like to give you a quick overview of our financial results before going into further detail. We have reported a second quarter net profit of AED 1.2 billion, which equates to a return on average tangible equity of 13.2%. This robust performance reflects ADCB’s strong fundamentals despite the multiple challenges faced by the banking sector, including the economic impact of COVID-19, lower oil prices and declining benchmark rates.

One of the key achievements of the Bank over the last 12 months has been the substantial improvement in our cost to income ratio, driven by the capture of significant merger synergies and a disciplined approach to cost management. In the second quarter, the cost to income ratio stood at 34.9%, a decrease of 710 basis points from a year earlier. Our impairment charges were significantly lower on a quarterly basis due to lower provisions on NMC, Finablr and associated companies.

Meanwhile, our balance sheet remains robust, with capital and liquidity ratios comfortably above minimum regulatory requirements. We will now move on to the balance sheet, starting on slide 24. The Bank’s asset base remains stable at AED 406 billion as at end of June. On the whole, our loan book has held up very well this year with average loan balances steady, in line with the UAE banking sector, at an average of AED 248 billion through the first half.
However, total loans ended the second quarter down 3% from the end of 2019 due to large corporate repayments at the end of June 2020. As we continue to execute a strategy of rebalancing our deposit base, total customer deposits ended the first half 5% lower at AED 250 billion. The average customer deposit balance during the six-month period was AED 259 billion.

Total shareholders’ equity stood at AED 53 billion at the end of the first half, 5% lower than at the end of 2019, but up from the end of the first quarter. The decrease was partly due to the AED 2.6 billion dividend pay-out in the first quarter and an AED 1.3 billion decrease in the net fair value of reserves on debt instruments to go through other comprehensive income. It is worth pointing out that a significant mark to market adjustment was taken in the first quarter due to the increased market volatility, and this was partially reversed in the second quarter as credit markets recovered.

For more detail on our first half income statement, please turn to slide 25. Our first half net profit of AED 1.4 billion was lower year on year primarily due to the higher impairment allowances, which included just over AED 1.2 billion of provisions for NMC, Finablr and associated companies. In a tough macroeconomic environment, declining benchmark rates and a contraction in the loan book had an impact on the top line.

Net interest and income from Islamic financing was 2% lower year on year at AED 5.1 billion. However, higher merger-related synergies and other cost reduction measures, resulted in a 12% decrease in operating expenses to AED 2.4 billion, and there was a 15% reduction when integration costs were excluded. As a result, we reported a 2% increase in operating profit to AED 4 billion.

The impairment allowances of AED 2.6 billion reflect the increasingly difficult economic backdrop and include significant provisions taken for NMC, Finablr and associated companies. In quarter one, we booked impairments on 25% of our exposure to these companies and in quarter two we raised our provisions on Finablr and associated companies to 50% of exposure.

This approach is in line with international accounting standards and based on current information, including detailed data on revenue generation, cash flows and asset values received from the joint administrators of NMC and our advisors. We continue to monitor developments very closely and will make appropriate adjustments if required. I would like to remind you that the Bank continues to take a proactive approach to resolving this issue and is pursuing a range of avenues and legal routes to ensure repayment of debt.

If I can invite you to turn to slide 26 please, I will run you through the income statement highlights for the second quarter. We reported a net profit of AED 1.2 billion in the period, significantly higher than in the first quarter, but 15% lower year on year, due to higher impairment allowances. Our successful fast-tracked completion of integration has allowed us to achieve a rapid drop in operating expenses and a reduction in our cost to income ratio.

During quarter two, the improvement in operating expenses continued as we realised further synergies in the quarter and launched a new programme of cost control measures. Operating expenses were down 25% year on year at AED 1 billion or 23% lower when excluding integration-related costs. Consequently, operating profit came in at AED 1.9 billion, a 2% increase from the previous year.

During the quarter, we reported impairment allowances of AED 668 million, up 56% year on year, to take into account the post-COVID environment and increased provisioning for Finablr and associated companies. For
more detail on our balance sheet metrics, kindly turn to slide 28. Following our merger, our exposure is diversified across economic sectors and well balanced between Wholesale and Consumer Banking.

Over the first six months of the year, Wholesale Banking loans have declined 3% and Consumer Banking loans have reduced by 4% as economic activity slowed. As a UAE-centric bank, 94% of our loans are domestic and weighted towards Abu Dhabi, which accounts for 57% of total loans. I will now hand over to Kevin who will take you through the next few slides.

Kevin Taylor

Thank you Deepak. You will find a breakdown of our deposits on slide 29. We continue to focus on increasing our CASA deposits, which in combination with lower benchmark rates have contributed to a decrease in our cost of funds over the last year. In the second half we saw a continuation of this theme, with CASA deposits reaching AED 114 billion up 12% in six months. They now account for 46% of total customer deposits, compared to 39% at the end of 2019.

In parallel, expensive time deposits declined 15%, in line with the Bank’s strategy to reprice and rebalance its deposit base. Turning to slide 30, you can see that the degree of diversification and stability in our liability base remains high, with customer deposits accounting for 71% of total liabilities. We have also maintained a healthy wholesale funding mix, which totalled AED 62 billion at the end of the second quarter, with maturities well distributed over the coming years. We continue to be a net lender in the interbank market to the tune of AED 11 billion.

Our main insurances in 2020 include a five-year US $300 million issue and a forty-year US $390 million note issue. If you now turn to slide 31, you will see that our liquidity position has strengthened. Our liquidity coverage ratio at the end of June was at 129.1%, comfortably above the regulatory minimum, which was reduced to 70% by the UAE Central Bank as a part of its measures to support the economy. The Bank continues to take a prudent approach to management of its liquid assets, which were at AED 110 billion at the end of the second quarter.

On slide 33, you will find a snapshot of our capital ratios at the end of the second quarter. Our CAR and CET1 ratios improved to 16.31% and 12.95% respectively, from 14.13% and 10.82% at the end of March. This was due to an increase in shareholders’ equity that we spoke about earlier, driven by an increase in the fair value of FVTOCI designated assets during the second quarter, as well as the additional retained earnings. Both ratios are comfortably above the regulatory minimum levels set by the UAE Central Bank.

Deepak will now discuss the asset quality.

Deepak Khullar

Thank you Kevin. On slide 34, you will see the evolution of our asset quality during the first half.

We have taken a conservative approach to provisioning, given the prevailing difficult economic conditions. Impairments taken this year therefore include a prudent overlay for expected credit loss given the current environment. In the first half, total impairment charges were AED 2.6 billion, compared to nearly AED 1.2 billion a year earlier. This includes the 1.2 billion provisioning taken for NMC, Finablr and associated companies.

As a result, the annualised cost of risk increased to 165 basis points in the first half, from 70 basis points in the first half of 2019. Excluding impairments related to NMC and Finablr, the cost of risk in the first half would
have been 91 basis points. On slide 35 you can see that the NPL ratio was 5.16% as at 30 June, up from 4.65% as at 31 March 2020, driven by a few corporate customers. Including POCI or purchase or originated credit impaired assets, the NPL ratio was 6.62% at the end of the second quarter.

Our coverage ratio remains comfortable at 101.8% at the end of June. I would now like to go into a little more detail on our income statement on slide 37. As mentioned earlier, we have seen an improvement in cost of funds due to our continuous strategy to grow CASA deposits, in combination with lower benchmark rates. Our cost of funds decreased to 1.47% in the second quarter. An improvement of 106 basis points from a year earlier. The sequential improvement was 51 basis points.

However, Q2 net interest margin of 2.66%, decreased 52 basis points sequentially due to lower benchmark rates and volumes, with asset yields declining on account of fair value adjustments and interest releases reported in quarter one 2020, which were not repeated in quarter two 2020. Net interest income in the second quarter decreased 10% year on year and 16% quarter on quarter. On the next slide you will see that non-interest income in the second quarter was down 9% year on year and 14% quarter on quarter at AED 594 million. This was due to a decrease in net fees and commission income. With card-related fees, loan-processing fees and trade finance commission impacted due to COVID-19. Meanwhile, quarter two trading income increased 47% from the previous year and 12% quarter on quarter due to gains on foreign exchange and securities trading.

I would like to turn now to an analysis of operating expenses on slide 39. As you can see the Bank’s cost to income ratio has improved consistently over the last year as we realise significant merger-related synergies. In the second quarter, we launched a further programme of cost initiatives, which included enhancing procurement efficiencies, process optimisation and reduction or elimination of discretionary spending. As a result, ADCB’s cost to income ratio, excluding one-off integration related costs, decreased to 34.1% in the second quarter, an improvement of 570 basis points over 12 months.

I would now like to briefly summarise our performance in the second quarter. The Bank delivered a solid performance, despite a weak macroeconomic environment caused by the COVID-19 pandemic.

Our key achievements include realisation of substantial merger synergies, and we are on track to reach 75% of our AED 1 billion run-rate synergy target this year, and the full target in 2021. This has resulted in sizable improvement in our cost to income ratio. The Bank’s balance sheet remains strong, with enhanced capital and liquidity ratios, which comfortably meet regulatory requirements. We are also stepping up our digital transformation programme in tune with changing customer behaviour.

The sustained increase in usage of ADCB’s digital channels, even as lockdown restrictions were eased, points to a long-term shift. Meanwhile, given that COVID-19 will continue to impact the economy for some time, we are focusing on increasing institutional resilience through prudent provisioning and by taking proactive measures to maximise efficiencies across the Bank.

We believe that ADCB remains in a position of strength to support stakeholders through COVID-19 challenges and to contribute to economic recovery. I would now like to open the floor to any questions you may have. Thank you.
Operator    Ladies and gentlemen, if you would like to ask a question, please press star followed by one on your telephone keypad now. If you are joining us via the web, please click the request to speak flag icon. If you change your mind, please press star followed by 2.

When preparing to ask your question, please ensure your phone is unmuted locally. We have a question from Deniz Gasimli of Goldman Sachs, your line is now open, please go ahead.

Deniz Gasimli    Hi, good evening, thank you for the presentation. Two questions from my side. Obviously, a lot of moving parts in cost of risk given the current backdrop and the different aspects to it. So, for the first half, as you mentioned, cost to risk was around 170 basis points, but around 90 basis points when excluding NMC, Finablr impact. When you look forward at coming quarters and maybe coming year as well, do you have any sense of where you would like to see a sustainable cost of risk through the current backdrop or is it too early? Any thoughts that you can share in that regard would be much appreciated.

And a second question on capital, this quarter strong performance in terms of capital ratios and CET1. Given where we are now, six months into the year, do you have any thoughts on the dividend pay-out for ADCB or is it too early to think about at this moment? Thank you very much.

Deepak Khullar    Thank you for those questions, let me pick up on the cost of risk, yes, excluding NMC and Finablr, they were at 91 basis points. There is still a lot of uncertainty surrounding the provisioning in terms of the impact of COVID-19; how quickly will the economy recover and the impact on our customer base.

We think, based on what we see so far, we are seeing some green shoots in terms of pickup, in terms of spending etc. and hopefully that will translate then into the economy. But the cost of risk will remain elevated at these levels of what we have seen in quarter two. Probably see a little uptick in quarter three and quarter four as well, depending on how the economy recovers.

Capital, yes, we are in a strong capital position right now, CET1 of 12.95%, total capital above 16%. It’s a bit early to talk about dividend pay-out but you’ve seen the Bank’s past performance in terms of dividend pay-out being consistent around the 50% pay-out ratio. So, we will see how we prepare for the balance in the second half of this year.

Deniz Gasimli    Thank you. As a follow up, when you talk about uptick in terms of [unclear] from Q2 levels.

Deepak Khullar    I’m sorry, I can’t hear you clearly, your voice is very faint.

Deniz Gasimli    Sorry about that, maybe this helps. I want to ask, when you talk about uptick in cost of risk, from Q2 levels, do you mean ex NMC and Finablr impact? Or both headline and adjusted cost of risk?

Deepak Khullar    No, I was talking about ex NMC and Finablr.

Deniz Gasimli    Understood, thank you very much.

Operator    We have a question from Alok Nawani of Ghobash Trading & Investments, your line is now open, please go ahead.

Alok Nawani    Good afternoon gentlemen, and thank you very much for the call, just two questions from my side. Would you kindly clarify how much of NMC, Finablr have you provided for? By my calculation,
the 1.2 billion on the 4.3 billion exposure, implies 29%, I’m not sure if I heard 50% so that’s one. And the other question is to do with your operating expenses. I understand there has been recent news articles about additional layoffs, 400 odd employees.

I’m wondering if this is over and above your integration and synergies plan that you have communicated; the 1 billion synergies target? Or is this well within the same remit?

Kevin Taylor Thank you Alok, just off the top of my head, our NMC exposure was roughly about $981 million and Finablr was $200 million odd. So, on Finablr we’ve taken up 50% provision coverage, as of the end of second quarter. For NMC, 25%. That’s how you’ll be able to work out these numbers. And in terms of operating expenses, for the last decade ADCB has implemented global best practice in managing our lowest underachievers following regular performance reviews; so this continues.

And any reduction in the cost base as a result will be over and above the synergy target.

Alok Nawani I see. Just two follow up questions, if I may. One is can tell us your current headcount before the 400 reduction that was talked about. And on NMC and Finablr, I would have expected perhaps that ADCB book slightly more aggressive provisions when it comes to NMC, considering you already took about 25%, if I’m not mistaken, last quarter. So, I’m trying to understand, has there been any material positive development on that front which has led you to be not all that aggressive on provisioning? Just to hear some of your thoughts on that please, thank you.

Deepak Khullar So, on the total headcount, as at last year end, roughly around 7,000 people across the group. And in terms of the provision on NMC, when we took the provision in quarter one, it was just announced and things were just breaking out. But since then, based on additional information received from various parties, the Bank’s assessment is that the current impairment allowance against the debt is adequate as of 30th June.

We will, however, continue to reassess this provision level every reporting period in light of new information that will be made available as the recovery process proceeds. The number of key inputs that go into determining expected credit loss on stage three accounts, and this factors in a number of things such as forecast of future cash flows from the borrower’s business. Other sources of recoverability, cash flows from sale of assets, realisation of collateral, seniority of claims, cost of realisation, time of recovery, etc, and a range of probabilities. And the Bank is working very closely with the court appointed joint administrators, who are managing the UAE and the overseas assets as a going concern operation. And they are taking actions to maximise enterprise value. So, we have come across more information in the past, 90 to 100 days, so we feel that this level of provisioning is adequate at this stage.

Alok Nawani Thank you very much.

Deepak Khullar And in terms of how we approach our provisioning, further details can be found in note 42 of our full year financial statements as well, very detailed analysis there.

Alok Nawani Appreciate it, thank you.
Shabbir Malik: Hi, thank you very much for this presentation. In terms of your margins, there was quite a steep contraction this quarter relative to the previous one. And you’ve indicated it’s because of the low rates as well as lower fair value unwind. I wanted to understand in terms of the fair value unwind, do you expect this to be more of a volatile number? And is there something that we could expect in the next two, three quarters which could prop up the NIM again? If it’s more chunky or bigger in the next quarter. And my second question is on your loan book. Which sectors do you think are probably at a higher risk and what percentage of your loan book makes up those sectors?

Deepak Khullar: Sorry Shabbir, could you kindly repeat the second question? Which percentage of the loan book if you can kindly repeat that please.

Shabbir Malik: Which sectors do you think are at a higher risk because of COVID-19 and how much of your loan book do those factors constitute or make up?

Deepak Khullar: If you remember in the quarter one results, we did say we saw an uptick in our overall NIM across the 3% mark and I have at that stage mentioned we would see this come down more to the 2.75 levels in quarter two. So, we had number of fair value unwinds in that quarter and some interest in suspense as well. Fair value unwinds, some of them will be a regular phenomenon, but at a much lower level, depending on the performance of the accounts as well.

And the only time you’ll get some chunky movements would be either when there are chunkier repayments or refinancing to another bank etc, then you’d see probably a chunky unwind of that fair value that they have taken. So, that’s where you could see some movements. Other than that, if the loan continues in our books and continues to perform then there will be a gradual unwind of that over the tenure of the loan. So, that’s the two variations.

In terms of your second question, percentage of loans which are at high risk. So far what we have seen in terms of deferrals that we’ve seen coming, requests for deferrals coming through to us, primarily from the trading sector, which is AED 2.4 billion, real estate and investment about 2.8 billion, hospitality roughly 0.6 billion, retail 0.8, manufacturing a much lower number at 300 million and services at 200 million. So, that’s the major component of that 8.3 billion deferrals that we’ve had so far in June of this year.

These are the areas that are most impacted. Aviation as well, so trading is right on top and followed by real estate and investment. Real estate investment is roughly 29% of our overall book and trading is a much smaller number, I’ll come back to that in a moment. But it’s a much smaller composition of a loan book.

Shabbir Malik: Thank you, if I may ask one follow up question, if I look at your loan growth, your loan book’s shrank this quarter, I would imagine that client demand for credit is much higher now, what has been your strategy in terms of lending?

Deepak Khullar: We are actively in the marketplace, we haven’t seen a decline in our overall market share and that’s why we said these repayments that came through, came through virtually at the end of the second quarter. And we feel confident that we will fill that up in the third quarter and fourth quarter. That’s
why we mentioned that the average loan book was a much higher number than the period end number that you saw. And what impacts the income statement is the average loan book, which was very healthy at AED 248 billion odd.

Shabbir Malik Thank you.

Deepak Khullar And sorry, to your earlier question, trading comprises about 4% of the overall loan book for the Bank.

Shabbir Malik That’s helpful.

Operator We have a question from Aybek Islamov, your line is now open, please go ahead.

Aybek Islamov Thank you, this is Aybek from HSBC. I wanted to ask you about your loan under TESS programme which you disclosed, I think the total amount is roughly AED 79 billion, so pretty much one third of your loan book. By far that’s the highest ratio, perhaps ENBD is also high if we take out sovereign loans out of the total loans. So, their TESS loans are also quite high. So, the question is really, what does it mean for your longer-term cost of risk? Given that such a high ratio of loans under TESS. The majority of TESS loans, it looks like according to your disclosures, these are loans with temporary liquidity problem. Do you expect these loans with temporary liquidity problems will become loans with structural credit risk. How are you positioning your provisioning policy given such a high ratio of loans under TESS?

Deepak Khullar Okay, so thank you Aybek. A couple of things there. So, overall deferrals are about AED 8.3 billion on a total exposure of 78, 79 billion of exposures. So, that’s roughly 10%.

But you’re right, of the total number if you calculate it’s about a third. We’ve got much larger value loans compared to other banks where the deferrals have been offered and that’s why you see a different ratio. But what needs to be considered is what you’ve got in Group One and Group Two of these loans. The UAE Central Bank has requested banks to group the deferrals into Group One and Group Two. Group One is customers that are temporarily and mildly impacted by the COVID-19 crisis.

And Group Two customers are those that are expected to face substantial changes in their credit worthiness. Most of our deferrals fall in the Group One category, roughly 6 billion in Wholesale Banking and half a billion or so in Retail Banking. So, 6.5 billion roughly is in Group One and only about 1.8 billion is in Group Two, which is where you could see some more pressure coming in.

Aybek Islamov Okay, and implications for long-term cost of risk, perhaps this is not that easy to handle, I mean this assessment.

Deepak Khullar Yes, there’s a lot of uncertainty in these times, we are taking into account guidance issued by the IASB and regulatory bodies in the UAE who determines staging and ECL calculations. And we will look at forecast conditions, but both in terms of what impact it would have on the clients and also, the government support measures that have been undertaken which will lessen that impact. So, that’s why we have taken both into account, we mentioned that he might see a slight uptick in cost of risk in the following quarters.
But it depends on how the economy works with that.

**Aybek Islamov**  Okay, and one clarification question, it’s technical. How much of the interest free deposit zero cost funding facility have you received? I was going through your footnotes, I couldn’t find it, [unclear]

**Deepak Khullar**  Sorry, what was the question? How much of the interest free deposit?

**Aybek Islamov**  No, how much of zero cost funding have you received from the Central Bank? I couldn’t find it in your footnotes.

**Deepak Khullar**  Overall, as at 30th June, it was AED 8.8 billion, and to date while we are in July, still those were numbers as of 30th June, we’ve utilised our entire 8.9 billion allocation that is due to us and have moved that across to the customer base as well.

**Aybek Islamov**  And just a final one, is there any indication that Central Bank may expand the zero cost funding? Beyond AED 50 billion, can they go to 70? 100?

**Deepak Khullar**  I’m not aware of anything so far.

**Aybek Islamov**  Okay, thank you, that’s all.

**Naresh Bilandan**  Ruby, can we go to the next question please?

**Operator**  Hello, it seems as though we have disconnected from Divya, so I will hand back to you Naresh.

**Naresh Bilandan**  Okay, Ruby, do we have any more questions on the line?

**Operator**  We have no questions remaining.

**Naresh Bilandan**  Okay, well, if there are no questions then let’s end the call here in the interest of time. Thank you everyone, I appreciate everyone’s participation of this call. Thanks a lot to you, Deepak, Kevin, Denise and Monica for the time today, have a good day everyone. Thank you.

**Kevin Taylor**  Thank you.

**Deepak Khullar**  Thank you.

**Denise Caouki**  Thank you.