



1Q23 Results

Thursday, 11th May 2023

Introduction

Sirish Patel

Head of Investor Relations, SAB

Welcome

Hello and welcome to our Results Call for the First Quarter of 2023. As mentioned by the phone operator, we have our CEO and Managing Director, Tony Cripps, and our CFO, Lama Ghazzaoui, with us on the call today. As usual, Tony will kick off the call summarising the key updates for the quarter, followed by Lama, who will provide the usual summary of our financial performance. We aim for the presentation element to be approximately 15 minutes, and then we shall open up the floor for Q&A, which will take place over the phones.

Slides are available for download from our website, and our webcast.

So, without further ado, I'll hand you over to Tony to start the presentation.

Overview

Tony Cripps

Managing Director and Chief Executive Officer, SAB

1Q23 Key Messages

Thanks, Sirish, and good afternoon, to all of you on the call. Thanks for joining.

First, just a, a comment on the new brand that many of you will have seen. This sort of brings an end, I guess, to the merger story. But at the same time, the idea behind the new brand is to demonstrate our strategy, our growth strategy, and from here on in, we expect the returns that we are seeing now to continue. And with the new brand and of course our new building, which we are moving into soon, it underscores our ambition in supporting the Kingdom's transformation program. The formal name still needs to go through its process of being approved, but this will happen fairly shortly we understand.

So, to performance, Q1 was pleasing. We obviously had been guiding that higher interest rates would support NIM expansion for us, but we also demonstrated good volume growth across all of our businesses, which continues the returns on the investment we've been making in the last 12 months, in better systems, better products, greater online capacity, and all of that has paid off.

It's fair to say that the global macro uncertainty is probably the highest in a long time, in a decade or so, but it ebbs and flows between pessimism and optimism. That has continued in Q1. But the strength of the Saudi economy has been very good and has not really been impacted overly by this volatility, and it remains robust. And in our view, 2023 is going to be another solid year for the economy. The recent external indicators such as the IMF and the World Bank forecasts are stable, and the outlook from the credit ratings agencies have actually, improved. The price of oil is obviously very important, has been volatile, but relatively in the ranges of expectation and therefore the economy is well-supported.

Our underlying planning assumption on interest rates haven't changed. Where we started the year was we expected interest rates, the US interest rates to be at 5% or a bit higher, and possibly coming down later in the year or though that story again, ebbs and flows depending on, which week and which month you look at it. But an average rate throughout the year as we guided before of about 5% or 5.25% is still the expectation. But things are a little uncertain, and therefore we remain vigilant in managing the business week-to-week and month to month, but at the moment it's steady as she goes, and we expect the growth that we've seen in the Q1 results to continue.

On to slide one.

Our strategy remains on track. As I said, we've built out our digital capabilities, our online penetration levels are up significantly, our customer satisfaction surveys, independent surveys are very strong. And our staff internally have done a great job in setting our growth strategy and the enthusiasm for which that's being delivered is also very visible, in the culture of growth and innovation that we have developed in the last 12 months and longer. Initiatives such as developing online mortgage products, retail tools in order to track your spending, SAB360. Our international capability through Global View Global Transfer, which links your SAB account, your retail account to your HSBC account anywhere in the world and allows instant transfer, is a unique proposition for our affluent segment.

We've grown the loan book by SAR8 billion this quarter, or 4%. The first quarter can typically be strong. It was last year as well. And it's built up from a strong corporate growth of SAR6bn, and solid growth of SAR2bn in retail. Corporate growth is from a wide range of customers and some of the bigger ticket wins in the energy sector. In the retail space, growth was mainly driven by mortgages, which is about half of our retail lending. The outlook in mortgages has softened a bit, and that's visible in the market numbers, some of it because of changes in the subsidy program. The Q1 numbers are not really materially affected by this. Q2 possibly could be, with some seasonality. We may not have the best indication actually until Q3, but in our own numbers, we are marketing our proposition. It's very good, and we are seeing growth across our lending in mortgages.

Revenues grew, and we achieved SAR3.2 billion this quarter, which is a record for SAB. And this comes from increased net special commission income as our NIM continued to expand to 3.1% in the first quarter. We also saw an increase in fee income, higher FX, and higher trading gains, an excellent start in our markets business, and gains from our investment portfolio. Asset quality remains solid, with our NPL ratio falling to 2% on SAB-originated loans. As a result of the strong growth in loans, quarterly cost of risk remains at Q4 levels, but this largely reflects updates to our modelling, which as I said earlier, the outlook has become possibly a little more volatile, and we've built that into our modelling and therefore taken some provisioning. And we haven't seen any deterioration in the portfolios as a result, but it's a conservative approach which we've taken.

All of this – all of these results have led to a ROTE of 15.9% for the quarter, which is an excellent improvement on the fourth quarter of 2022, and we continue to enjoy very healthy capital levels.

Our liquidity and funding is very strong, and we have a 17.2% CET1 ratio and 207% LCR ratio. And our NIBs ratio has remained pretty steady, at around 66%. And this is a welcome respite

to the gradual decline that we saw through 2022, as customers naturally responded to higher rates and higher returns.

So, all in all, we're ahead on a number of our metrics and the momentum on the balance sheet has been very good, and the expansion in returns. Our commitment to spending on digital with the expectations that our revenue profile would be strong is paying off. And the automation of our services, our propositions, as I said, both within retail and significantly our growth in the middle market and our investment in our SME proposition is yielding very good growth. We launched the entirely new platform for the SME proposition last year, digital, and the onboarding and progress there has been really good.

So, with that, I will pass you over to Lama, who will as usual give you some further detail on our financials. Lama over to you.

Thank you, Tony. And, good afternoon, everyone.

We start at slide three.

We generated SAR2 billion of net income before Zakat and income tax and SAR1.8 billion post Zakat and income tax. This is a record achievement for SAB and up 76% year-on-year and 27% quarter-on-quarter on a post Zakat and income tax basis.

On a year-on-year basis, net income was up from higher revenue, which was partly offset by increased operating expenses and higher expected credit losses. I'll explain the main drivers over the next few slides, but again, it's been very pleasing to see the consistent build in the revenue since the end of 2021. Comparing to the fourth quarter of last year, net income was up from higher revenue together with lower operating expenses as the prior quarter included some costs that are one-off in nature related to the rebranding.

NIM expanded further in line with our expectations to 3.1% for the first quarter. Non-funds income also performed well, supported by higher fee and exchange income, together with trading gains from our fair value through statement of income investment portfolio, which were higher than prior year. This is part of our strategy to position the investment portfolio and expectation of downward movement in benchmark rates.

Cost efficiency improved greatly to 31% as a result of the strong revenue performance. Absolute cost expenditure is in line with the plan.

Cost of risk of 47 basis points was higher than the first quarter of last year, but broadly in line with the fourth quarter of 2022, this was largely driven by macro modelling updates. Asset quality remains strong and there are no indicators of additional stress in the portfolio. All this, of course, leads to an annualised first quarter return on tangible equity of 15.9%, and of course, we're very pleased with the build-up in the returns.

Moving on to the balance sheet, loans were up 4% and the quarter, driven by strong performance across both corporate and retail. Comments we've been making for quite some time on the lumpiness of our portfolio remain. However, we expect to build on this position for the second quarter and into the second half. Our customer deposits were up 5% in the quarter, and it was particularly pleasing to see our NIBs ratio remain at 66%. Lastly, capital levels remain robust and we've adopted Basel III reforms in this reporting period, which had around

50 basis points punitive effect on SAB, largely driven by our corporate skew. Our CET1 closed at 17.2%, which still places us at the top end of the sector on CET1 basis.

On to slide four.

The left-hand chart shows the quarterly revenue build by segment. All our three main businesses are driving the performance, with our corporate business benefiting from the increased rates and higher volumes, and our retail business also benefiting from improving loan volumes, particularly in mortgages. Our treasury business also improved quarterly revenue through higher trading revenues, which was in part supported by the repositioning of the investment portfolio, as we've locked in current rates and extended durations.

The top right-hand chart shows our NSCI build, which reached SAR2.5 billion for the first quarter – another record – and this comes from volume growth as well as the repricing in our corporate portfolio. NIM, of course, reached 3.1% with gross yield of 4.7% and the cost of funds of 2%.

On slide five, we show the performance in our non-funds income, which is up 14% on the first quarter of 2022. All the key lines showed a strong improvement with fee income up 9%, exchange income up 15%, and all other lines in aggregate up 22%. Exchange income was up primarily from increased customer flows, and the other lines were largely driven by higher trading income, as mentioned earlier. Fee income was up 9%, as I mentioned. A breakdown of our fee income from its main contributors is shown on the right-hand side of the slide. And also it is pleasing to see that these businesses are showing signs of good growth in the first quarter.

On to expenses.

Costs increase 20% year-on-year, but were down 7% quarter-on-quarter. The year-on-year movement largely reflects the shift to our investment phase, and mostly in our people, and also absorbing a 100% of the SAB Invest business, formerly known as Alawwal Invest. The quarter-on-quarter reduction largely represents a drop as the prior period included, as I said, some one-off expenses relating to the rebranding exercise and other invest-related activities. Cost efficiency improved further, but this was mainly driven by the improved revenue position, and we are at 31% cost efficiency ratio for the quarter.

Credit quality. The cost of risk for the quarter was 47 basis points, and as mentioned earlier, cost of risk was higher than first quarter of 2022, but broadly in line with the fourth quarter of last year, this was largely driven by continued macro modelling updates. While asset quality remains strong, there are no indicators of stress.

Following the strong growth in loans, our NPL ratio fell to 2% on the SAB-originated basis, and 4% on total basis. As a reminder, this is a significant improvement since the merger, where we peaked at 6.1% following the conclusion of the merger accounting.

Our coverage ratio for the quarter improved to 146%. As always, we continue to monitor the portfolio for any signs of or indications of increased pressure or risk, but we are well provided for and always remain vigilant to the changing macroeconomic landscape.

On to customer lending, on slide eight.

Our gross loans have grown 4% this quarter, which is broadly in line with the market. Growth comes from both corporate and the retail businesses, and is a continuation of the strong

performance achieved since the launch of our strategy. And as can be seen, on the right-hand chart, corporate originations have again been strong, and as Tony mentioned earlier, have come from a wide range of customers, but with a skew towards the energy sector this quarter. Activity on the other giga-project remain pleasing and the pipeline for the remainder of the year looks promising.

Retail momentum continues with a closing portfolio of SAR48 billion, and our mortgage portfolio is now SAR23.4 billion. Mortgage growth continues to be pleasing, and our market share of originations has grown to 9.2% for the first quarter, which is nearly two times our market share of stock. Roughly half of the mortgage originations in the first quarter are from REDF, and therefore half are non-REDF, and our current stock of mortgages is roughly 30% REDF.

We did not expect the changes in the mortgage subsidies to have an impact in the first quarter, particularly giving the timing of when these changes were announced, but we expect it to impact Q2 across the market. Given our share of sales of private non-REDF mortgages, we still feel that we can deliver mid-teens growth in mortgages.

The personal lending businesses faced competitive pressures towards the end of last year and into the first quarter, and we don't see that changing in the near term. Our cards business continues to do well, and we remain number one with respect to spend per card and overall business remains a highly profitable business.

On to slide nine.

Funding and liquidity, as usual, remain competitive strengths for SAB. NIBs of 66% was stable versus year-end, and remains well ahead of the market, and we have the capacity, of course, to support our customers' borrowing aspirations.

Moving on to returns and capital, on slide 10.

With a continued strong financial performance, our returns have continued to build with an annualised quarter-to-date ROTE of 15.9%. Our capital ratios are now on a Basel III reform basis, and we closed the quarter with a CET1 ratio of 17.2%. The closing of December 2022 CET1 on a Basel III reform basis would have been around 50 basis points lower than what we published at the end of the year. The reforms are generally more punitive to a corporate bank. However, on an underlying basis, CET1 is up around 0.10 percentage points from profit, fair value movements on OCI, partly offset by loan growth. And capital, of course, remains a fundamental strength, always ready to be deployed for the opportunities that lie ahead.

Finally, a few words of conclusion before we move to Q&A.

As Tony said, our strategy is still on track, the investment plan is on track, and the growth agenda is also on track. We continue to demonstrate delivery of strong financials, strong revenue, net income, and balance sheet growth. Our NIM expanded to 3.1%, and our returns, as we said, expanded to 15.9%. Our loan origination continues at pace with 4% quarter-to-date growth, in line with our plans. The macro environment, which continues to shift, still has the ingredients for a prosperous banking sector and the wider economy.

For 2023 guidance, we are making no changes to the guidance. Our loan growth remains on track to deliver low-double-digit growth. Our NIM for the first quarter, as I said, was 3.1%, which is the floor of our guidance. This is undoubtedly the most sensitive to external factors,

but as a reminder, was based on two 25 basis point hikes, which we have now seen, followed by a period of stabilisation, and then potential cuts in the fourth quarter of 2023.

Clearly, this can change very quickly and therefore, therefore, we remind you of our sensitivity to the 4-6 basis points for every 25 basis point shift to policy rates. This will feed into our cost efficiency ratio, where despite the great performance in Q1, we would expect this to increase slightly in the second half of the year. And therefore, we feel it's prudent that we maintain the 33-35% level.

No change to the cost of risk guidance, as we're not witnessing any notable incremental stress in the portfolio. And finally, given that there are no changes to the above, our ROTE guidance also remains at low to mid-teens.

Now clear, the Q1 results are at the upper end of most of the guidance ranges, and all things being equal, we should hopefully hit the upper end of some of the ranges we've given on 2023 guidance. However, given the planning assumption was the expectation of cuts to take place in the second half, after the two rate hikes we've had, we feel prudence should prevail, and therefore, we will revisit the guidance at Q2.

That concludes the presentation element. Thank you. And operator, we can start the Q&A.

Q&A

Operator: Thank you. As a reminder to ask a question, please press star one-one on your keypad and wait for your name to be announced. To withdraw your question, please press star one-one again. Stand by your first question. Your first question comes from Waleed Mohsin at GS. Waleed, your line is open. Please go ahead.

Waleed Mohsin (Goldman Sachs): Yes. Good afternoon. Thank you much for the presentation. Three quick questions from my side.

First, you talked about, you know, a positive or good strong pipeline on the mega projects for the remainder of the year. If you could, please, elaborate a little bit further. I mean, where are we in terms of progress? I think, I believe that, some part of the first quarter, corporate growth was driven by drawdowns on some of the projects. So, if you could just talk about the second half, what are you seeing, where are we in terms of further drawdowns, that would be very helpful.

Secondly, if we look at your loan to deposit ratio, clearly the most comfortable in the sector, but then again, your deposits outpaced loan growth during the quarter. I mean, conscious that you don't run the bank on a quarterly basis, but would be great to hear, on how you're thinking about deposit gathering, you know, going into the remainder of the year, given that, cost of funding does remain elevated for the market.

And third, just on your net interest margin. You laid out your assumptions for the remainder of the year. But if you could please, highlight when you expect net interest margin to peak? And just to confirm that I heard it correctly, that you are factoring in rate cuts at the back end of the year, which are factored into your guidance? Thank you.

Tony Cripps: Hi. I'll take the first one. So, yes, there is momentum across the giga-projects, we have started to see in the fourth quarter and Q1 this year, further drawdowns as those projects accelerate, and we expect for the rest of the year, that will continue. So, the corporate outlook on that basis remains strong, but it's the effect that cascades from these projects through the supply chains, you know, into the middle market also, that's really important for the growth outlook. And as those big projects are driving growth in the middle market as well, which is part of our strategy, we're quite optimistic on seeing that growth continue.

On the deposit gathering side, Lama?

Lama Ghazzaoui: Hi, Waleed. On the cost of funds, of course, as price goes up, we would still expect our yields to follow. So, we expect some margin erosion, of course, as customers would generally not be happy just to have the rates passed on. And the cost of funds, we expect, of course, to continue to rise in the short term, in line with the trend seen. But we still have one of the highest NIBs ratio in the Kingdom. So, we are closing at 66% for quarter one. However, you know, competition remains and as time passes, you would expect that there will be more opportunity for customers to renegotiate margins or ask for higher deposit rates.

On your question, on when NIM would peak, the – you know, we currently feel that the NIM will peak towards the middle of the year, and then they will plateau, and then a lot depends on any potential rate cuts at the back of end of 2023. So, this is all factored within the guidance, yes.

Tony Cripps: Yeah. And when we used 5% for our reference rate for the planning process, it was ahead of the rate rise that we've seen already this year. We just assumed in Q4, in the planning, that you would get rate rises in Q1, and that was in line with the market. And the market also had priced in, that there could be cuts at the back end of the year. And of course, that changed very dramatically in Q1, at a point in time, when suddenly that disappeared, and then now it's flipped back again. So, we've just taken a conservative approach, really. We're not going to change our forecast based on week-to-week movements in the market, and we're just assuming that rates will stay according to the Fed guidance higher for longer, and therefore perhaps not as aggressively coming down as the market is currently forecasting, and just taking guidance from the Fed themselves. So, to Lama's point, we expect that our NIMs will continue to be strong, into the back half of the year.

Waleed Mohsin: Got it. Thank you much. And just one follow-up. So, on the – on the deposit gathering, I mean you, if I get it correctly, so you are quite optimistic on the pipeline for the remainder of the year, and, as a result, the deposit gathering during quarter kind of supports your line-of-site on drawdowns further than the year because, you know, you, you could have actually let go of certain expensive deposits and further optimise your loan to deposit ratio.

Tony Cripps: We haven't really chased deposits. In general, we are, of course, strategic in talking with our large customers, but on average, we haven't been chasing deposits at all. We have a very strong corporate business, which accounts for half of our deposits, and a lot of that is deeply integrated into our transaction banking services. So, that is a significant advantage for us. And on the retail side, you know, our strong brand attracts customers, particularly expat customers. Over 40% of our client base are expats, and again, that tends to provide a stickier deposit base potentially.

So, yeah, we expect that there will be, as always, funding our growth in – and, yeah, we know that we attract liabilities. We're a very strong brand, and in a more volatile world, that's probably even more important. So, we're quite happy and confident about our liability growth in the second half or in the rest of the year. Thank you.

Waleed Mohsin: Got it. Thank you, Tony. Thank you, Lama, very helpful.

Operator: Thank you. Please stand by for your next question. Your next question comes from Rahul Bajaj at City. Rahul, your line is open. Please go ahead.

Rahul Bajaj (Citi): Thanks for taking my question, Rahul Bajaj from Citi here. I have three quick questions.

The first one is regarding your rebranding to SAB. Just wanted to understand, is this to do with any change in your relationship with HSBC? Also, in terms of any cost related to rebranding, should we be baking in any one-off cost down the line in 2023 for your rebranding exercise, and how sizeable could that be? So, that's my first question.

The second question is on the investment cycle, we have seen, two quarters of slightly elevated cost OPEX. As you said, you continue to invest in the business. Now, where are we in that cycle? I mean, should we expect the current run rate to be the run rate we should use for our forecast going forward? Or you think, this is a phase which would end after two, three, four quarters? Any thought there would be useful.

And finally, if you could please help me with your regulatory LDR, that would be very useful. Thank you.

Tony Cripps: Great. Thanks for the questions. I'll take the first one, on the brand. The short answer is absolutely not. It doesn't change in any way the relationship that SAB has with HSBC. As you know, we have a technical service-level agreement and therefore, the branding conversation was a conversation that SAB had with its own board, of course, in its management, but equally, with the HSBC Group. You've obviously have noticed that the hexagon remains, as it always has been. And the change in the name is something we're registering now and seeking final approval of. Again, it's – I don't think it's all that surprising when you put two banks together, you reference both of those banks if you can in a sensible way. And so, I think we've done that with the brand and, and also the name itself in Arabic says something about the history of the bank. And so, there'll be more to come in explaining, perhaps, more about how and why we branded the way we did. But we're very happy with it, and we know the market feedback so far has been very good. But no, the relationship is stronger than ever with the HSBC Group, and I'm sure you know that the board of the HSBC Group visited in November last year. The management team from the Group also visited in January, as a team going around the Kingdom, looking at all the giga-projects and leaving with a sense of optimism. So, nothing changes here.

The next questions I'll pass to Lama. Thanks.

Lama Ghazzaoui: Yes. Hi, Rahul. On your next question, on, I think the cost-income ratio or the cost base, we are expecting a fair cost increase in 2023, as we start seeing more of the investment costs hitting the P&L, and we fully now absorb the asset management brokerage and margin lending business cost from our hundred-percent-owned subsidiary. And you know, we are targeting cost-income ratio of 33-35%. As we said, this allows us to be bit more flexible

and gives us the opportunity and optionality for investing further. But on your question, whether the current base, or the first quarter base, yes, you can consider this as a base for the remainder of the year.

On regulatory LDR, we are in the low 70s. We closed the quarter at 72%.

Tony Cripps: And also just to finish on the brand, the costs associated with rebranding were – have been built into the existing plan. So, no surprises on cost resulting from additional spend on the brand change itself.

Rahul Bajaj: Understood. Thank you so much, Tony. Lama, thanks so much.

Tony Cripps: Welcome.

Operator: Thank you. Please stand by for your next question. Next question comes from Naresh Bilandani at JP Morgan. Naresh, your line is open. Please go ahead.

Naresh Bilandani (JP Morgan): Thank you. Hi, good afternoon. It's Naresh Bilandani from JP Morgan. Thank you. Three questions, please – and congrats on the set of results.

Just, firstly, if you could please throw some light again on the strong fee income that we have seen? Lama, if you can just please throw some colour on what areas contributed to the strength in the first quarter? Clearly the volumes were strong, but, on an underlying basis, what drove the fee income in the first quarter, that would be extremely helpful.

The second is, Lama too, in your presentation during the guidance, when you were discussing the 33-35% cost-income ratio, could you please kindly highlight again the function of this being was there a rate cut assumption built in, or should we see the pickup of the cost base further from the current levels, and that's what's going to drive the cost-income ratio higher from what we are seeing in Q1? If you can please just clarify that function again, that would be very, very helpful.

And just a third question for both of you. In light of the strength of the results, and clearly, have you had some chance to take a look at the – reassess your longer-term ROTE, which in the past you had kindly guided to the market of for being over 13%. In light of the current environment, have you had a chance to delve into it further? And if you can please throw some light, whether that stays or not, or if you anticipate some change from that level in the future, that would be super appreciated. Thanks a lot.

Lama Ghazzaoui: Hi, Naresh. On fee income, as we said, it's up 14%. The first-quarter number is a fairly clean number with no material one-offs. We were always transparent on what one-offs came into the quarter. But this quarter was a clean figure. And again, the tidy-up we did the last quarter involved moving some fee expenses that used to sit in operating expenses into income and also some VAT-related expenses. But this quarter was, as I said, a clean quarter.

Our card business continues to perform well. Again, you know, the – as we said last quarter, the fee income from the cards is fairly small. But overall, it is a very profitable business. The main line items in the fee income were trade payments, cash management, brokerage, and lending fees, and they're all showing double-digit levels of growth with respect to revenue. And again, just as a reminder, our trade business is number one in the Kingdom, and it constitutes around 50% of our fee business.

On your next question on the cost-income ratio. We did assume within the plan one cut that could happen towards the end of the year, towards Q4. This would not have a material impact on the revenue side. But it was taken into the plan, into the 33-35%. But yes, the pickup and the cost, as I said, is from the investments that we did in the last two years that will start showing more visible impact into the P&L.

On the longer-term ROTE, we are now giving one-year guidance of ROTE. But we are now in a re-strategising and refreshing actually our strategy, that we built a couple of years ago. So if there is any change in the longer-term ROTE, of course, in light of the macro and in light of all the dynamic changes, we will communicate those.

Naresh Bilandani: Thank you very much.

Operator: Thank you. Please stand by for your next question. Your next question comes from Nida Iqbal at Morgan Stanley. Nida, your line is open. Please go ahead.

Nida Iqbal (Morgan Stanley): Hi, thank you very much for the presentation and congratulations on the results. I have one question, as we look beyond this year, of course, you know, the rate hikes have been excellent for SAB and the margins. But as we look into a rate-cutting cycle potentially next year, how is management thinking about the leverage that can be pulled to offset some of the pressure from rate cuts, given the high sensitivity for SAB? Thank you.

Tony Cripps: Yeah. We've been thinking very hard about that for well over a year. You know, even in 2022, as we saw the yield curve start to invert in the US, and we started to assume that within 6-12 months rates would peak, we took a strategy through the investment book run within our treasury business, to increase the size of our investments, to put significantly more into fixed rates at longer maturities, at the highest credit. And therefore, we built a position in the investment book which will act, if you like, as an offset to any interest rate reduction affecting other parts of the bank's income. And it's something we continually focus on. Again, we've increased the size of that position in Q1 when rates backed up, the rate went back up to nearly 4% at one point. It's now backed down to 3.5% or thereabout. And we'll continue to do that so that we have a very different position going into the next cycle than we did in 2020.

In addition to that, obviously the growth in our mortgage business will also act as a buffer to rates coming down because the mortgage market in Saudi is obviously almost all fixed. And as we grow volume there in the retail business, that acts as well to diversify the income into less floating and more fixed. So, they're the two ways in which we're managing, I guess, the forecast that ultimately, at some point later in this year, or in '24 or through '24, the rate cycle will have turned. So, hopefully, that answers your question.

Nida Iqbal: Thank you very much. That's really helpful. Just to follow up on that. As we think about the rate cuts, then taking these factors into account, would you be able to share your NIM sensitivity to rate cuts?

Lama Ghazzaoui: Hi, Nida. It's for every 25, we said 4-6 basis points. So if it's plus or minus, it's for now 4-6 basis points of sensitivity.

Nida Iqbal: Thank you.

Sirish Patel: Nida, to some degree, we'll be looking and monitoring this quite closely and, when rates do turn, we'll get more information and more data to understand how our customers are, you know, how they're operating. So, we'll get more information, and then we'll be able to give you an update on our NIM sensitivity, but for the time being, 4-6 holds for on the way up, and on the way down.

Nida Iqbal: Great. Thank you very much.

Operator: Thank you. Please stand by for your next question. Your next question comes from Shabbir Malik at EFG Hermes. Shabbir, your line is open. Please go ahead.

Shabbir Malik (EFG Hermes Research): Thank you. I just wanted a clarification. I think, Tony mentioned something about the retail expat composition. I think you said 40%, just wanted to double-check that.

Secondly, I think if I look at your CASA mix, it's a quite impressive trend. We haven't seen a lot of CASA migration on time deposits. Maybe if you can comment on that, what's enabled you to maintain such a good level of CASA despite the high-interest rates, and what are your thoughts about the coming quarters? That will be my second question.

Thirdly, in – if I'm not mistaken, in terms of your segmental provisions, the retail segment has released – you saw a release in provision reserves in retail. If you can maybe comment on that, the drivers of that, and if it's something that we can expect in the coming quarters.

And maybe if you can also give a comment generally on asset quality on the corporate side? With higher interest rates, is that something that's putting pressure on the sector, or are there any early warning indicators on that front? Thank you.

Tony Cripps: Thanks. So, I said before that our client base in retail, 1.3 million, or there about – a bit over 40% of that client base are expats, and it's one of the reasons we prioritised the integration of SAB's retail bank accounts with the HSBC Group. So, because obviously many of our SAB customers also have bank accounts with the HSBC Group in various places, and creating that connectivity is quite unique, and it's a useful proposition.

Lama, I'll pass to you, to the next question.

Lama Ghazzaoui: Yes. Hi, Shabbir. On – I think your second question was on the customer migration, the customer deposits. So, we do cater on a customer by customer basis, and so there will be some instances where customers will negotiate a time facility to move their NIBs across. But this has been the trend that we've seen from the middle of last year. However, at the end of this quarter, we had a period of stabilisation, and we build up NIB balances, again. And ending, as we said, 66% NIBs ratio. As we always say, you know, we are the bank of choice for liabilities and, you know, our skew towards multinational, large corporates, and the institutional business, it's our strength, also, in payments and cash management that gives us this edge.

I think your third question was retail release in cost of risk. This was not that material in this quarter, but this is a continuous exercise that we do across our models. And we actually had a small – you know, for cost of risk in general, we had a smaller set of recoveries this quarter than the other maybe recent quarters. But for the retail release specifically, it wasn't that material.

And I think on asset quality for corporate, we are not noticing any stress in asset quality. And we continued to stress test the portfolio on a very continuous basis. We said in quarter four, we did take some overlays for interest rate movements on a part of our portfolio that is sensitive to interest rate, and we were prudent and proactive in that. But this is not an indication of any asset quality issues.

Shabbir Malik: Great. Thank you.

Operator: Thank you. Please stand by for your next question. Your next question comes from Gabor Kemeny at Autonomous Research. Gabor, your line is open. Please go ahead.

Gabor Kemeny (Autonomous Research): Hi, thank you. Can I just pick up on your last point, Lama, please? Can you quantify the macro-overlay provision you created for the higher interest rate assumption?

Lama Ghazzaoui: Yes. Hi, Gabor. Q4 provision was largely this overlay that we took, it was around SAR170-175 million in Q4.

Gabor Kemeny: And in Q1, have you created any overlay provision?

Lama Ghazzaoui: No.

Gabor Kemeny: Okay. So, why do you think you were a bit above the guided range?

Lama Ghazzaoui: For Q1, you mean?

Gabor Kemeny: Yes.

Lama Ghazzaoui: Look, you know, it is, again, in line with our plans and our projections. As I said, we did have a smaller set of recoveries in Q1, than the other quarters. And these are based off settlements, so we have a reasonable view of when these would happen. It's just a timing factor. And, you know, again, there's no particular indicators of incremental stress in the portfolio. It's just the timing of the recoveries that did not take place in the first quarter.

Gabor Kemeny: Okay. Very clear.

Lama Ghazzaoui: And just to add to that, some of the provision in the first quarter included modelling impact, but not overlay, but a modelling part of some modelling across the corporate.

Gabor Kemeny: Got it. Thank you. My other question is about corporate lending and the link to the state bond project. Sorry, if I missed – I had to miss the start of the call, but can you talk a bit about whether the Q1 growth, which was pretty impressive, driven by a broader set of projects or just projects or just one project? And are we talking about – when it comes to the pipeline, are we talking about just a few individual projects or a broader range of state projects? And finally, how much? We read into the fact that I think you dropped one of the giga-projects from your slide in the presentation – discussing this opportunity.

Lama Ghazzaoui: So, during quarter one, you know, majority of the corporate growth was driven by a range of areas, some skewed toward the energy sector. But the activities in giga-project of course continues, but the drawdowns were not a theme of Q1 in the giga-project. And of course, the activity and the work behind the scenes is very strong, and this is what provides us with the comfort for the future pipeline. You know, activities, for example, on NEOM have really gathered pace, and we expect further drawdowns on the Red Sea, for example, project to happen throughout the remainder of this year.

Gabor Kemeny: Okay. Thank you.

Operator: Thank you. Please stand by for your next question. Your next question comes from Mohammed Al-Rasheed at Ashmore Saudi. Mohammed. Your line is open. Please go ahead.

Mohammed Al-Rasheed (Ashmore Saudi): Thank you for the call. I have, three questions if I may?

The first one is regarding the Basel reforms impact on the risk-weight for the corporates, if you can please provide more details on that? What specific area of the corporate is with higher risk weight? Is it the loan maturity or project finance segment or other segments?

My second question, you mentioned that you have updated the macro variables into the ECL during the first quarter. So if you can provide a direction of that because your oil price assumption by then end of 2022 was like \$96, and now oil price is already at around below \$80 level. So, was that already revised lower during the first quarter?

And my final question is regarding your provisioning. I noticed that majority of your provisions during last year, or net provision during last year and this quarter is related to your POCI book. So, was this because of updating the model, or are you witnessing, any credit quality in the asset quality of your POCI? Thank you.

Lama Ghazzaoui: Yes, Mohammed. Thank you. So, for the first question on the Basel III reform, you know, again, as we said, from what we've seen, Basel reforms are more punitive towards corporate banks rather than retail banks. For SAB, it's meant an increase in RWAs, mainly from credit risk and market risk. So, credit risk is also due to the introduction of the capital charge on revocable commitments, which now incur a 10% CCF. I know this is too technical, but, you know, just to break it down. And previously, it was nil, for example. Market risk RWA was due to introduction of the FRTB, which compared to the previous adopted standardised approach. So, this is fundamentally the breakdown.

Your second question on the macro, we factored an average of all prices of around the \$80s. So, yes, it has dropped from last year, and hence, the impact on the modelling provision that took place in Q1. And whatever relates to POCI is now business as usual. So, if we see any need for additional provision on performing POCI – don't forget that we do have POCIs that are performing – we do cover for those.

Mohammed Al-Rasheed: Okay. So, most of the incremental provisions on POCIs was on the performing part?

Lama Ghazzaoui: Yes because the non-performing POCI were written down to their lowest value back then, and hence they're not performing then. They have already been written down.

Sirish Patel: Yeah, I think as Lama said earlier, you know, the main theme in our first quarter ECL charge is probably the lower recoveries, which, you know, similar to our corporate originations are lumpy. You know, we have a similar profile with corporate when it comes to loan originations as it does to ECL. You that we generally also have a good outlook and forecast of those recoveries as well. And that's what kind of gives us that kind of comfort that will stay within the guidance range for ECL,

Mohammed Al-Rasheed: It's very clear. Thank you.

Operator: Thank you. Please stand by for your next question. Your next question comes from Chiro Ghosh at SICO. Chiro, your line is open. Please go ahead.

Chiro Ghosh (SICO): Hi, this is Chiro Ghosh from SICO Bank. I have two questions. The first one is related to the deposits again.

So, can you give some kind of idea like what is the duration of this deposit? I just want to get a sense how will it behave once the interest rates starts to go down. So don't need an accurate number, but say six months, one year. I mean, a rough duration would quite help me a lot. Also in this quarter, the deposit inflow was quite strong. So, was there any kind of government deposits inflow, and if yes, what was the magnitude?

And then my second question is related to the asset quality. So, what we see that overall the asset quality has continued to improve, which is very counterintuitive in a rising interest rate environment. So, are you doing something different? I mean, if you can give – shed some light on that part?

Lama Ghazzaoui: Yes. Thank you for the questions. So, on average, duration of our deposit is around three months. So, it's short in duration.

On the last question, I think the asset quality, it has improved. One, the base has improved. The growth in the portfolio is a factor. Two, we've been very prudent before in classifying assets as NPL and hence, the recoveries and the activities that took place on these assets throughout the last two years, on restructuring through our SAM team, the Special Asset Management team, has been very rewarding. And, we have been planning to write off some assets. And so, this is a combination of the improvement in the asset quality.

On the second session, I think on government deposits, inflow, did I hear right?

Chiro Ghosh: Yes.

Lama Ghazzaoui: So, yes, we did see that the money supplies, you know, supply improved towards the end of Q1. You know, the sector liquidity is mainly driven of course, you know, by some government spending and various government, and semi-government institutions injecting some liquidity into the market. So, as the various projects get underway, these institutions will definitely get their liquidity in readiness, and this also enters into the system, eventually.

Chiro Ghosh: Is it fair to assume it's mostly indirect inflow, not any direct infusion into the banking system?

Lama Ghazzaoui: Sorry, what do you mean by direct or indirect?

Chiro Ghosh: So, did the government entities park money directly into the banking system or they were spending, and so eventually the money flew into the – came into the banking systems?

Lama Ghazzaoui: Yes. This is the second one.

Chiro Ghosh: Second one. Okay. That's all from me. Thank you very much.

Operator: Thank you. There are no further questions.

Tony Cripps: Thanks very much for joining the call, and thank you for the questions as well. So, as I said in the beginning, it was a solid start. Q1 was a good start for us, and we've exceeded our earlier guidance. But I also made comments earlier that we are seeing a lot of

volatility in the global economy. And we are going to, at this point, stick to the guidance we gave at the beginning of the year, which was an assumption around interest rates being around 5%, up initially and perhaps down in the fourth quarter.

But as Q2 unfolds, we will update guidance appropriately. We are positive for the rest of the year our income levels will remain strong on volume growth, and NIM sensitivity will mean that our NIM will continue to be robust well into the second half. And then it depends somewhat on what happens in the market. But even if we do get rate cuts in the fourth quarter, there will be a delayed effect. And as I also said earlier, our balance sheet's in a different position than it was going into the last cycle in 2020. We have been very mindful of the risks in a rate cycle that is heading down. And given our sensitivity, Sirish has guided currently that our sensitivity is lower at around 4-6 basis points. And again, we will update that guidance as more information comes through in Q2.

And finally, I just say that what we are seeing amongst our customers in growth and optimism in Saudi is something that is still very clear to us. And as Lama said, we haven't seen any stress yet in the system itself, and we'll keep an eye on that. But for the moment, the guidance for the economy is strong, and therefore our own outlook is also strong, built on the foundations of our Q1 results.

With that, again, just thank you very much for joining the call.

[END OF TRANSCRIPT]