



SICO Bank – BBK Conference Call

Monday, 23rd May 2022

Introduction

Sumaya AlJazeerai

Assistant Vice President, Financial Institutions, Research, SICO Bank

– good morning, ladies and gentlemen, as-salaam-alaikum. This is Sumaya AlJazeerai from SICO and I would like to welcome you all to the BBK Group's First Quarter 2022 Results Conference Call. It is my pleasure to host BBK Group's senior management today. We have here with us Dr. AbdulRahman Saif, Group CE; Mohammed Abdulla, Group CFO; Ahmed Abdul Qudoos, Head of Group Corporate Secretariat; and Hussain Toorani, Head of Treasury. By now you should have received the company's presentation and earnings release and detailed financials for the first quarter of 2022, which have been disclosed on Bahrain Bourse and the Bank's website. You can also view this on the webcast as well. The presentation will be followed by a Q&A session and management will be taking your questions. You can either queue via dial-in for the Q&A or send each of your questions separately via the webcast link. Instead of clubbing them together, I do request you to enter each question separately.

Now, without further delay I will hand over the call to Dr. AbdulRahman Saif to commence the conference call. Thank you very much.

Q1 Highlights

Dr. AbdulRahman Ali Saif

Group Chief Executive, BBK Group

Thank you, Sumaya. Good morning, ladies and gentlemen. **Dr. AbdulRahman Ali Saif:** Welcome to this investor's conference call. This is now an established event. We have been doing this over the last two years or so and we have decided to continue with this on a quarterly basis, and we will look at possible enhancements to this event, meeting. We usually start with highlights of major developments, any specific strategic initiatives and then more focus on the financials, and we leave the end for interaction, Q&A.

Three-year Strategic Cycles

In terms of major events that took place so far during the quarter, as you may know BBK has a tradition of developing three-years strategy cycles. So 2021 was the end to the last strategy cycle, and by the end of 2021 we have introduced to our board our new strategy cycle that will cover 2022 to 2024. That was approved and we are now in the implementation mode. We will share with you the main themes of the new strategy cycle. Now, this year marks the 50-years anniversary for the operation of BBK and we have announced the start of the celebrations in February; which was the month when BBK started its operations in Bahrain in 1972. So, we are marking this anniversary with special celebrations which will continue until February 2023.

Community initiatives

We have announced a number of initiatives to support the community and we have some more to announce. For those who are interested, we have announced 50 scholarships at national universities. We have announced the write off 50 loans – these are happening on a

monthly basis through DROs – and we have announced what is called 'Sahm Al-Gharimeen.' These are for financially-strapped p

ersons, to support them and take them out of their stress. These are all initiatives to show our strong support for the community. We have further announcements to make during the coming month.

As you may know, in the second half of last year we have closed the first transaction of US\$150 million two-year club facility for BBK and during the first quarter we have closed an increment to this by US\$50 million. The same terms apply to the US\$150 million, so in total we have closed US\$200 million of bilateral facility. Four domestic and regional banks have participated in this transaction.

In terms of rating, recently Moody's has affirmed the rating of BBK as B2 and the outlook was changed from negative to stable. This mirrors the update on the sovereign rating of the Kingdom of Bahrain.

Last on this, and to demonstrate our support to strategic business importance of the SME sector, we have signed an agreement with Tamkeen, this is the Labor Fund, to support the growth and development of SMEs in Bahrain.

Now, as I mentioned, we have approved the three-year strategy for BBK that will cover 2022 to 2024. In the new strategy cycle we are focusing mainly on five themes. We will continue with digital transformation. This is a journey we have started back in 2019. We have covered many milestones so far and this will continue with us for the current 3 years cycle. We have identified specific milestones on digital transformation and we are committed to transforming the whole bank; the front end, the back end, the culture, helping the transformation of our clients. So we are addressing digital transformation in a very comprehensive manner.

Our customers are a priority for us and so customer centricity will be one of the main themes of our current strategy. We have identified a number of milestones on this, and customer centricity is linked to our ESG as well because it's an integral pillar of the ESG. Corporate growth through M&A also is one of the strategic themes, and that continues with us from the last strategy cycle. The other two are operational excellence and bank ecosystem. We look – along with digital transformation, we are looking to revise our policies, procedures, organizational structure, and many other things to enhance our efficiency and really complement what we're doing on the digital transformation aspect. So, the main idea is corporate efficiency and, again here, we are looking at it in a comprehensive manner.

ESG

Briefly on ESG, we have approved the framework back in 2020. 2021, we have identified the main pillars of our ESG framework; we have identified all the KPIs and the milestones; we have an approved setup to govern the ESG development and compliance, starting with board, management and teams. So, this is the setup to ensure efficient implementation of our ESG framework and plan. We will issue our first ESG report this year, that will relate to 2021.

So that's it from me on the main developments and highlights on the strategy. On key governance and investor relations, can I invite Ahmed Abdul Qudoos, please?

Key Governance Initiatives

Ahmed Abdul Qudoos

Head of Group Corporate Secretariat, BBK Group

New sustainability framework

Thank you very much, Dr. Abdulrahman Saif, for the introduction. And I will cover only few of the key governance initiatives. Starting with the Board who actually is the governing body for ESG, so now the Board has adopted a new sustainability framework and management committee, and that committee has been formed to develop, review the relevant statements and KPIs for the sustainability framework. The nomination, remuneration and governance committee was delegated to follow up on this issue. So the Board has taken full ownership of ESG because it's one of the main priorities for the Bank.

Compliance with regulatory requirements

The other issue is compliance with regulatory requirements, three layers of compliance with regulatory requirements concerning corporate governance, were performed to ensure full compliance with these requirements. And we are one of the institutions that are proud that we do not only ensure compliance with regulatory requirements regarding corporate governance, but corporate governance is a philosophy embedded within the Bank's culture.

Enhanced use of technology

The third issue is the enhanced use of technology by having fully paperless functions for the Board and Board committees. We had started the process back in 2011. Now we have improved it to cover the majority of the functions of the Board and Board committees. The Bank looks at paperless operation as part of the sustainability framework adopted by the Bank.

Investor Relations unit

An Investor Relations unit within the corporate secretariat was developed and the Bank launched a revamped platform for investor relations, taking into consideration international good practice to keep all investors abreast of all relevant disclosures. And we're also keen to improve our practices by holding these kind of meetings with the investors to listen to them and answer their questions and queries and try to improve on our efforts and endeavors regarding investor relations.

Financial Performance

Mohammed Abdulla

Group Chief Financial Officer, BBK Group

Net Profit Growth

Thank you, Ahmed. On the financial performance, which has been published. The bank has achieved a growth in net profit of around 5% and we have witnessed a growth in all lines of income, with a total revenue growth of around 12% year-on-year. Operating expense has slightly grown from BD 14 to BD 15 million, mainly because of certain strategic initiatives that have been undertaken and the 50th anniversary initiatives that were explained.

Moving to the balance sheet, the balance sheet has slightly grown over December 2021, mainly on loans, advances around 1.4% and total assets around 1%, and the customer deposits almost flat compared to December. This is part of the balance sheet optimization, where we grow our liabilities whenever needed without competing on the pricing of our customer deposits. We continue to be a net lender to the market, as we used to be, with more than BD 300 million long in terms of money market.

Moving to the key financial indicators. Annualised Return on average equity and return on average assets, have improved over December 2021. . Earnings per share around 37 fils, while cost to income ratio improved to 49%. The asset quality indicators shows an improvement over December 2021, as well as the regulatory ratios, being CAR, NSFR and LCR, at a very comfortable level as of end of first quarter of 2022. This is, in summary, the performance of the bank. Further details has been published in the newspapers and the website. Thank you.

Sumaya AlJazeera: I'd like to thank BBK's senior management. We can now transfer to the Q&A session. We'll give you a few moments to log in your questions or dial in for further questions.

Q&A

Operator: Dear participants, as a reminder, if you wish to ask a question over the phone, please press star and one on your telephone keypad. Alternatively, you can submit questions via the webcast. Dear speakers, there are no questions over the phone.

Sumaya AlJazeera: The first question we have is directed to Dr. AbdulRahman Saif. Good afternoon, Dr. AbdulRahman and everyone. Thank you for having the call and, at the outset, let's congratulate BBK Group on the financial results for the first quarter and the Golden Jubilee. The three questions go as follows. Can you let us know, please, how much is your cost of funds in Q1 2022 and, as comparison, on a quarter-on-quarter and year-on-year basis?

The second question, I would appreciate if you can let us know what is the gap between your cost of funds with these benchmarks; the three-month LIBOR and average three-month BIBOR? The following question, what is the asset yield percentage in first quarter 2022?

Dr. AbdulRahman Ali Saif: I would answer this question in a broad manner. Now, starting 2020, after the outbreak of the pandemic and the following sharp reduction in global and

domestic interest rates, we, like other financial institutions, suffered because of this. So, in the second quarter of 2020, we have embarked on a very thorough exercise of balance-sheet optimization where we have done a full review of our liability, cost of liabilities, our assets and our yield.

And we have restructured our balance sheet in a way to really preserve our margin at that time and then put our balance sheet on a path that would benefit from the subsequent development and the rest of 2020-2021.

Now, I can confirm that starting with the fourth quarter, we have seen a reversal of the trend in our net interest margin. We have seen reduction in our costs, cost of liabilities. And so, we managed to really stabilize and grow our net interest margin.

Now 2021, we have seen a kind of stabilization. and we had better visibility. Markets started to absorb COVID and the impact of COVID. So we have seen a kind of stabilization and that also allowed us to look at our balance sheet and possibly restructure our balance sheet.

Global fundamentals were more on the positive side. We have seen better growth, we have seen developments, better on supply chain, opening up of markets and so on. So, by end 2021, the main concern moved from recession to inflation, with possible reversal of interest rates. And quarter one 2022, we have witnessed a kind of aggressive interest rates hike. In fact, the second was at 50 basis points was unusual in the recent history of monetary policy in the United States. And that shows the extent of really reversal in outflow.

Through the restructuring of our balance sheet, in particular, liabilities that we refinanced in 2020 and 2021, we stand in a good position to benefit from these developments in monetary policy, globally and domestically. And we are seeing the benefits already.

Now, I have to close by saying we are not traders on interest rates. We maintain a sound risk limits on markets, including interest rates. So while we adjust our balance sheet and adjust our financial – our positions based on global and domestic fundamentals, we would always comply with our risk limits and we would take a kind of balanced approach to really maintain sustainable operations.

This outlook is, in my personal opinion, by no means a fully established. We are aware of the global risks and vulnerabilities, including the possibility of stagflation. So, we are not leaning heavily on any economic outcome, but we are looking at a balanced approach here. So, I hope I have answered all these three questions comprehensively and beyond the question in terms of our position and our output.

Sumaya AlJazeera: Thank you, Dr. AbdulRahman. One more question from the same entrant. Are there any plans regarding organic and inorganic growth acquisitions? Is BBK eyeing BCFC at the moment?

Dr. AbdulRahman Saif: As I said, M&A is an integral part of our strategy, and we are taking it seriously. As our audience may know, last year we have embarked on a specific opportunity looking at specific assets of Ithmaar Holdings, and we have gone through all the stages. We have created an organization structure to implement this. So we have a Board Committee and a Management Committee to ensure that we pursue this as per our strategy.

So, this year, we are looking at a number of opportunities. We are still in the assessment stage and hopefully, through this assessment, we will reach to some specific assets, I would

say, be it in Bahrain or outside Bahrain, be it in banking or outside banking related sectors. So we are serious about it and we will pursue that. I cannot comment on any particular opportunity now. So that is our position.

Sumaya AlJazeeri: Thank you. The following question is regarding the return on assets. We have noticed that ROA for the retail segment of the Group stood at 80 basis points in the first quarter versus 150 basis points year-end. Similarly, corporate segments of the Group results in a negative ROA in the first quarter of 2022 versus a marginal one. What are the main drivers to improve these indicators?

Dr. AbdulRahman Saif: I don't think the question is very clear. And I would ask the analysts or the readers of our financials to be very careful in assessing this. What we do for each segment, for each segment we do the operational performance, but then we apply a methodology that is internally used for transfer price and we adjust our transfer pricing based on our strategy, market conditions and based on different products.

So, really what I see the numbers quoted may not reflect the exact position of the segments mentioned. What I can confirm is that all our segments are profitable. All our segments contribute significantly to our income and bottom line.

BBK today maintains a fine balance in terms of its revenue and net income. So, retail, corporate, treasury, investment and international fully contributes and in a balanced way to our income, total income and net income. So that I can confirm.

Sumaya AlJazeeri: Thank you, Dr AbdulRahman. The following question is regarding NIMs, which we have touched upon, but we can shed light on this briefly. BBK's NIMs have remained stable at 2.8% for the first quarter, in line with the average for 2021. What is the basis point average increases expected this year amid the reversal of the interest rate cycle in an upward direction?

Dr. AbdulRahman Saif: As I said earlier, we have stabilized our NIMs and actually we have grown it since second half of 2020. Now, we want to maintain this and possibly continue the upward trend. This is achieved through our control over liabilities. On this, we have done major refinancing in 2020 and 2021. Given the environment then, we managed to lock in wholesale liabilities at a very competitive cost. We have also kind of managed our cost of customer deposits and not at the expense of the size of customer deposits. Customer deposits still constitute the bulk of our liabilities. So we had adjustments to really make.

On the asset side, we also have done comprehensive review. We have exited certain assets, where we thought we are not well compensated and we have redirected our loan and investment portfolio towards better yielding assets.

Now, I have to say we are not fully driven by it. There is a balancing act here also. We had since 2020 to balance our capital ratio, our asset quality and the yield.

Now, if you notice, even with the sharp deterioration in the global and regional markets for the first four months of the year, our capital is still resilient, as of end march towards an excess of 23%. And that is one of the fruits of the optimization work we have done. So these are all the steps we have taken to defend and grow our margin and efficiency.

Sumaya AlJazeera: Thank you very much. We have a couple of questions on dividend payments. Any guidance on dividend payments? Any interim dividends expected? And is the bank going to adopt the cash bonus share dynamic going forward?

Dr. AbdulRahman Saif: Back in 2019, we were, I think, the first bank in Bahrain to have approved an interim dividend. And at that time, when we introduced it, our conviction was that this is a new tradition and culture of BBK. So, it was not introduced as a one-off measure.

Our Board has deliberated this in 2020-2021 when discussing the interim financials. We had also discussion with the Central Bank of Bahrain on possible interim dividends in 2021. I can summarize our position as BBK, why we want to adhere to this and continue with paying interim dividends. The circumstances, the high uncertainty caused by COVID in 2020 and 2021 were the justifications for not paying dividends.

But I think as BBK, we are committed to our new direction on paying interim dividends. And should the situation become more conducive and stable, I think BBK will consider paying interim dividend. So that would be the common direction for us.

Sumaya AlJazeera: Thank you very much. We have a question on the loan balance. How do you evaluate the growth in loan balance this year in the first quarter and going forward? Could we expect the growth in the commercial loan book this year?

Dr. AbdulRahman Saif: All right. I mean, this is natural when we go through a major slow down, as we witnessed in 2020 and '21, that with all the uncertainties in the market and the escalating risk, it is natural that we would be highly selective about booking assets. So, as I said earlier, we had balancing to do between growth, asset quality, yield and capital.

We were highly selective in terms of certain asset classes, in terms of certain markets. As you may know, we have positions in different markets, Bahrain, the rest of the GCC, the wider Middle East. And our investment portfolio is a kind of a global portfolio. So even when it comes to markets, we had to assess them.

Now let's say mainly starting second half 2021, we have started seeing certain opportunities in terms of financing, mainly in Bahrain. And we have started to look seriously at these opportunities to grow our loan portfolio. We managed to book high ticket transactions with government entities like Bahrain Tourism Authority, Electricity and Water Authority and others. That has helped to sustain our loan portfolio.

As we speak now, we are looking at a number of good ticket transactions also. So, we have started showing growth in our loan portfolio in the region of 2-3%. And we would look now to increase the growth in our loan portfolio this year.

Sumaya AlJazeera: The next question is regarding the ECL coverage ratio. Could you give a breakdown for the ECL coverage? I suppose it refers to the total coverage ratio.

Dr. AbdulRahman Saif: I would answer this also. It is important, and therefore, I appreciate sharing more details with our investors.

Now, first, I would like to mention that we have continuously assessed our assets, even in 2020-2021 during the height of the pandemic and we have revised credit grades. So revising

credit grades in these environments would naturally entail more provisions, both general and specific. So we have done that exercise.

We have also, at the request of the Central Bank of Bahrain 2020 revised our ECL model to reflect the operating environment at that time, and that entailed more ECL. So, we have been doing this constantly. As we stand today, we, in terms of our coverage, in terms of our ECL all stages, we compare favorably with all banks in the region. We have a detailed comparison. We look at the ratio of Stage 1 and we compare highly favorably. I would say that we are conservative. And we look and compare our coverage by a stage, we rank favorably and highly conservative compared to banks in Bahrain and in the region.

So we are comfortable in terms of our ECL and coverage. We stand on the more conservative side.

Sumaya AlJazeeri: Thank you very much. The next question is also regarding provisioning. We have seen BBK's cost of risk, loan loss provisioning to average loans declined to 0.2% in the first quarter. Shall we expect this to be maintained for the rest of the year?

Dr. AbdulRahman Saif: This is one of our objectives, to enhance asset quality, to contain and control any deterioration in our loan portfolio. In the last two years, we managed to avoid any major stress in the portfolio and any major failure. So we managed to control. Our stage migration was mainly within the performing stages. In fact, we managed to resolve a number of stress accounts. And that reflected positively on our net provision.

We managed to achieve good recovery, we managed to achieve reversals of stress account into performing. And that's why you will notice our net provision was relatively low. We will continue on this on resolving pending cases, reaching settlements, reaching work out with those clients who are impacted by the pandemic and continue to be impacted.

On this, I'm happy to share that we have set up a committee to proactively identify those clients who haven't recovered, as much as others and who may need further assistance going forward. We have established communication with them and we are ready to help should the deferral come to an end-by-end June 2022.

Some of them will need a different course of action apart from the blanket deferral. They will need more specific restructuring or rescheduling that will be based on their cash flow. So, we are also looking at this. We will continue our responsibility to show our support to those at this unusual time. I believe most of our clients have shown recovery.

One good signal of this, we have financials or interim financials, and also those who have availed the deferral on all the occasions, they are on the minority, not majority. So that – this give us good comfort signals that our clients are recovering well, that we can continue our efforts to maintain good asset quality work and to contain our NPL. Our NPL, we managed to reduce it from over 6% to 5%. We believe we are able to further maintain this downward trend going through 2022.

Sumaya AlJazeeri: Thank you. We have a question regarding the fee income. The bank's earnings were boosted by strong fee income in line with loan growth. However, to what extent do you believe this fee income growth level is sustainable in the upcoming quarters? And what is your guidance for the full year?

Dr. AbdulRahman Saif: Our fee income in the last two years, like other banks, were impacted by certain measures. Some are temporary, timely, and some are permanent. The permanent ones are the caps introduced by the Central Bank of Bahrain, and these are permanent caps. So that had negative implication on our fee income relate to loan fees and other fees.

The other, which was only temporary, was part of COVID or anti-COVID measures to put a cap on the merchant commission. This is on the more acquisition side. So, on the retail fee, I think now stabilizing, in line with post COVID costs in new CBB caps.

The acquisition fee is now back to normal and we expect to see more growth there. Where we are also focusing is on other fees, like advisory, management fee. And we expect to achieve some growth there. So, we are – a part of our strategy is to enhance the proportion of our income – the fee proportion of our income.

Sumaya AlJazeeri: Thank you very much. The next question is segmental breakdown shows a slight decline in net interest income in the retail segment versus an increase in the corporate segment. Is this due to the repricing of corporate loans, which is floating rated versus the fixed rates? I think we touched upon this but we can go over it briefly.

Dr. AbdulRahman Saif: I think the main challenge in Bahrain is, I would say, competition has intensified. With this slowdown in the market and with the ability of the banks in general to address their liquidity, we have seen a heightened level of competition. So, that has reflected in the margins and pricing on both retail and corporate. So that will reflect on all banks, not only BBK.

We are looking carefully. We have to stay competitive. We have to defend our market share. We have to grow our market share in both retail and corporate, and we have to adjust when our pricing is justified. We are part of the markets. And given the number of banks in Bahrain, I believe we are all price takers. No one bank can dictate the pricing in Bahrain with around 25 to 26 commercial banks competing. So we have to be realistic in our pricing.

I believe there is another aspect to this. Competition is not driven by pricing alone. We recognize that our customer value service, value the quality of service. Now, on this, we were one of the early banks in Bahrain to have launched onboarding. In summer 2020, we have launched the onboarding platform for application, for liability accounts.

I'm happy to report that we have seen very encouraging response from our clients. And now two years into this, our onboarding platform is very stable and attract a lot of business. So accounts can be opened within three minutes.

Now, in summer 2021, we have launched our onboarding for consumer loans. I'm happy to report that we are the only bank in Bahrain who offers this service, onboarding for personal loan. And this has attracted better-than-expected response from our clients. So these are signs that our clients wants pricing but also quality service.

Sumaya AlJazeeri: Thank you, Dr AbdulRahman. I think this would wrap up the questions for the day. I would like to thank everyone for the participation in this conference call of BBK Group discussing the first quarter 2022 financial results, and would like to hand over to Dr AbdulRahman for just one final remark.

Abdulrahman Saif: No, this was, as usual, a fascinating meeting with our investors and clients. As I said, now, we will continue with this conference call and we will enhance it, hopefully into more interactive into video rather than audio. We value the interaction. We are developing our Investors Relation platform.

And thank you for the questions. I think that the value of this meeting to have as many questions as possible. And we keep very open in answering and providing detailed information. Thank you.

[END OF TRANSCRIPT]