EMIRATES NBD Q2 2022 RESULTS ANALYSTS & INVESTOR CONFERENCE CALL & WEBCAST
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CORPORATE PARTICIPANTS

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Operator

Ladies and Gentlemen, welcome to the Emirates NBD 2022 second quarter results call and webcast for Analysts and Investors. Today's call is being recorded. Please note that this call is open to analysts and investors only. Any media personnel should disconnect immediately. I will now pass the call over to our host Mr. Shayne Nelson, Group CEO of Emirates NBD.

Shayne Nelson

Thank you, operator, you're all very welcome to our results call. First of all I'll touch on the operating environment within our footprint.

Over the last six months we have seen many economies return to a 'new normal', learning to live with Covid. Inflation has re-emerged, driven by pent-up human demand, with the conflict in Ukraine exacerbating the rise in food and energy costs. As inflation reached multi-decade highs, Central Banks have increased global interest rates at a faster pace than was expected even just a few months ago. The Federal Reserve has already raised rates by 225 basis points and is expected to increase rates by another 150 bp before the end of the year. Future rate rises are becoming a fine balancing act between fighting inflation and avoiding the risk of recession.

For the UAE and the GCC, higher oil prices will push budgets into surplus and reduce the need for sovereign debt issuance this year. Central Bank statistics show that the UAE's economy expanded by 8.2% year on year in the first quarter of 2022, led by higher oil production and strong 6% growth from the non-oil sector, as the country benefitted from increased travel & tourism, coupled with the positive impact of Expo 2020. Inflation in the UAE has increased but remains below the rates seen in many other economies. Egypt and Turkey have seen a strong surge in services inflow and tourism revenue as global travel resumed, which is offsetting some of the impact from rising energy costs on the current account deficit. Against this background I am very pleased to report that our profit jumped

50% to 7.2 billion dirhams before a new Turkey-related inflation adjustment. More on that from Patrick shortly.

Some of the key highlights during the first half are as follows:

All five business units delivered an increase in profit before tax, demonstrating that the Group's diversified business model continues to deliver. The fully digital IPO platform was rapidly delivered and provides a seamless, paperless solution from on-boarding to subscription and payment. This proved a great success in both the recent DEWA and TECOM IPOs and underlines our credentials and value add in the Equity Capital Markets.

Lending grew by 1% in the first half with new lending grow strong. Key sectors including Manufacturing, Trade, Transport & Communications, Utilities and Personal lending all delivered strong growth which more than offset in Sovereign lending. This retail and renewed commercial loan growth reflects the more optimistic economic confidence across a broad range of sectors. Higher interest rates are now feeding through to margins. Given the expectation of further rate hikes, coupled with widening margins at DenizBank, we raised our margin guidance by 50 basis points. This has enabled us to accelerate our investment in digital and our international operations.

Asset quality improved in the first half and a lower cost of risk reflects a stronger economic environment. We have seen a healthy level of writebacks and recoveries. It's particularly pleasing to see strong recoveries in Turkey helped by very strong demand for property. The Group's strong results and solid balance sheet helped secure a Moody's upgrade of the Group's short-term, long-term and baseline credit ratings. This upgrade is even more pleasing given the challenging global conditions. On the back of our digital transformation, we have significantly increased the number of customer interactions performed without any human intervention. 93% of new product or servicing requests are now fully automated, and this 5% improvement on last year has eliminated 4 million manual interventions annually.

I will now hand you over to Patrick to go through the results in more detail. Patrick

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Patrick Sullivan

Thank you, Shayne, and a very good afternoon to all of you. Let me start with the usual summary financials for H1 on page 4. On this page we thought it would be more helpful to present the Group results for H1 together with ENBD and Deniz on one page so you can more easily see the drivers of earnings. So just running down through the numbers.

Total H1 income of 14.2 billion dirhams was up 23% year on year. Within that, both NII and NFI are up. As you can see DenizBank was particularly strong relative to H1 last year, up 42% despite FX depreciation. Interest margins in both ENBD and Deniz have widened significantly and in a moment, I will update the NIM guidance. Non-funded income was up 40% year on year helped by strong customer FX and interest rate hedging, volume growth in both ENBD and Deniz, wider transaction margins in Turkey, and hedging gains on DenizBank's balance sheet.

Costs increased 8% year on year supporting very strong business volume growth, particularly in Retail and, as we accelerate our investment for the future including, as Shayne mentioned, our international network and our digital capabilities. The cost income ratio at just under 29% remains well within the 33% long-term guidance. Impairment allowances were down 28% year on year reflecting the improving operating environment and strong recoveries in the UAE as well as in Turkey, especially in the property sector, which is now in high demand in Turkey.

The Tax charge has stepped up on the back of strong earnings in Turkey however the effective tax rate remains fairly stable. This gives us a very strong H1 profit after tax of 7.2bn dirhams, up 50%. And finally, the new hyperinflation adjustment in Turkey takes 1.9bn off H1 earnings, but to be clear up front, this is a non-cash notional charge and is fully offset by a credit to equity via OCI, so capital neutral. That gives us a final profit number of 5.3 bn, up 11% for the first half.

Touching on the Q2 picture, particularly strong income – NII lifted from rate rises that started in Q1 coming through into Q2, and NFI growth from increased business volumes and 2021 Deniz mark to market gain reversals not recurring in Q2 2022. This has boosted the profit to 3.5bn, up by 42% year on year and 28% quarter on quarter, despite the new hyper-inflation charge in Turkey. In the bottom summary table you can see the balance sheet metrics are in good shape, with assets up 3%, deposits up 2%, capital and liquidity ratios strong, and the NPL ratio improving, supported by strong recoveries.

Turning to net interest income on slide 6. The bottom charts show that margins in Q2 improved by 65 bps year on year and the first half NIM up 41 bps year on year, helped by improving loan yields at Emirates NBD and strong core growth at DenizBank. As Shayne mentioned earlier, global interest rates have risen more quickly than was expected even a few months ago. As a result of this, and improving margins at DenizBank, we have revised our full-year NIM guidance up by 50bps to 3.2-3.3%. This includes a total rate raises of 375bps this full year, so 150 bps more after the FED announcement yesterday. This guidance also factors in some offset for tighter loan pricing, reflecting the competitive market landscape.

On slide 7 we see that gross lending increased 1% during the first half, with EI's lending growing by 5 billion dirhams or 11%, Retail also growing by 5 billion dirhams or 8% and DenizBank delivering 26% loan growth in local currency. We saw strong new lending in the first half with retail and renewed commercial loan growth across a broad range of key sectors, reflecting increased economic confidence, which more than offset a reduction in Sovereign lending.

We witnessed a small drop in CASA balances in Q2 with Retail CASA continuing to grow and partially offsetting a drop in Corporate CASA. This was expected and we had guided at the beginning of the year that some Corporate CASA may move to fixed deposits as interest rates increased. It also reflects encouraging signs that Corporates are rebuilding inventory and increasing investment. The transition to term deposits so far has been modest, reflecting strong liquidity in the UAE banking sector. And CASA remains at a healthy 62% of total Group deposits. The bottom right charts show the progress we are making in improving the diversification of the loan book across product and geography.

On slide 8, the NPL ratio improved by 0.3% to 6.1% helped by strong writeback and recoveries in both the UAE and Turkey. The annualised net cost of risk for H1 of 79 basis points is below guidance and well below the 124 bps cost for 2021, reflecting the improving economic environment. Coverage rose by 5% to just over 133%. The chart on the bottom left shows that, Stage 1 coverage is broadly stable, Stage 2 and 3 ECL allowances increased, increasing the stage 2 and 3 coverage to a very strong 23.5% and 95% respectively.

Now just before I hand over to Paddy, I thought I would provide some further detail on the Turkish hyperinflation adjustment. I have included a slide in the Appendix so let's jump to slide 14 for a moment. I guess there is a generation that has not really seen the higher levels of inflation that are being experienced in many parts of the world today, let alone hyper-inflation, but that is now today's reality in Turkey. Turkey has registered more than 100% inflation over the last three years and as such it triggers hyperinflation accounting for our Group IFRS accounts.

In super simple terms, there are two parts, firstly DenizBank non-monetary assets & liabilities, like property, are adjusted by index inflation rates, to the extent recoverable, to approximate what the current purchase cost would be in today's money. But for a bank this is a relatively small part of the Balance Sheet and the overall adjustment. Secondly, a bank has mostly monetary assets and liabilities. These are already at their current measuring unit, but they have lost purchasing power.

We don't adjust the monetary items on the balance sheet, but we do book a charge to P&L and a corresponding credit to equity via OCI – so it is really a notional non-cash representation of the loss of purchasing power of the net-monetary items. Given the offset in equity to this charge, it is capital neutral. The table on the right side shows DenizBank's profit movements year on year before and after the hyperinflation adjustment. Current earnings are covering this adjustment, but actually the reason they are down half on half is the FX translation from Turkish Lira to AED, which is down 49% year on year. Earnings would be around 0.9 bn if using the prior year rate.

I will now hand you over to Paddy to take you through the remaining slides.

Patrick Clerkin

Thanks very much, Patrick. If we got to slide 9 on non-funded income we see that fee and commission income was up 11% year on year in the second quarter, mainly from increased local and international retail card business at both ENBD and DenizBank, and strong investment banking revenue.

Other operating income was up significantly due to higher retail foreign exchange volumes, as customers took advantage of the strong dollar and increased remittance, a pick-up in SME activity, and increased flows due to the move to a Saturday-Sunday weekend. There were also strong gains from DenizBank's balance sheet hedging and there were some mark to market gain reversals for DenizBank in Q2 of last year that did not recur this quarter.

On slide 10 we see that costs increased 10% year on year. Staff costs are higher as we invest in software engineers, digital specialists and data scientists. As was mentioned previously, higher income enables us to accelerate investment in our international network and digital capabilities.

Moving to slide 11 on funding and liquidity. We see that the Group continues to operate with strong liquidity with an AD ratio of just under 91% and an LCR well over 150%. The small drop in LCR is a function of a greater deployment of liquidity in higher yielding interbank deposits this quarter. Debt capital market issuance globally has been quiet in the first half. We issued 3.7 billion dirhams of term debt in H1, with DenizBank successfully rolling over and upsizing its 1-year syndicated loan in June. We have 6.7 billion dirhams maturing in the remainder of 2022 and we remain comfortable with this, given the significant excess funding issued in both 2020 and 2021.

Moving to capital slide 12, we see that the common equity tier-1 ratio was stable at 15% during the first half. 4.8 billion of net earnings offset a 7% increase in risk weighted assets, as we experienced strong new loan growth in retail and a diverse range of corporate sectors. The common equity tier-1 ratio was 14.5% excluding the ECL regulatory add-back. As Patrick explained earlier, the hyperinflation adjustment is capital neutral.

Moving on Divisional performance on slide 13, we see that RBWM income improved 17% year on year. It was a record half-year for cards acquisitions, fee income and balance sheet growth helped by nearly 5 billion lending growth and over 15 billion CASA growth. ENBD and EI combined Retail have close to a 30% market share of debit and credit card spend within the UAE.

CIB income declined 6% year on year on lower lending balances. Profitability was boosted by higher fee income and lower provisions. EmCap remains very prominent in the capital markets and helped ENBD play a lead role in both the DEWA and TECOM IPOs. EI's income grew 16% year on year. Financing & investing receivables and deposits grew by 11% and 15% respectively.

Global Markets & Treasury net interest income jumped year on year on higher income from balance sheet positioning, hedging and an increase in banking book investment income. Non funded income was substantially higher on a strong Trading performance.

DenizBank's Income was up 42%, or 1.4bn dirhams, and impairment allowances were 0.6 billion dirhams lower on strong writebacks and recoveries. And these helped offset a 1.9 billion dirham hyperinflation adjustment.

With that I will pass you to Shayne for his closing remarks.

Shayne Nelson

Thanks Paddy. So to summarise, these strong results and ratings upgrade demonstrate the resilience of our diversified business model and the strength of our balance sheet. The positive outlook enables us to accelerate our investment for the future, supporting our next stage of growth.

With that I would like to open the call to your questions. Operator, please go ahead.

QUESTIONS AND ANSWERS

Operator

Our question comes from Waleed Mohsin from Goldman Sachs.

Waleed Mohsin - Goldman Sachs

Good afternoon. Three questions quickly from my side. The first one on Turkey and acknowledging a very strong performance in the second quarter with very strong NIMs, almost up 200 basis points quarter on quarter, a net writeback. But I was just wondering, the second half macro-outlook, at least for Turkey, looks very challenging given where inflation, spot deposit rates are less than 20%, and there are a number of dollar maturities for bonds falling due for different other banks in the sector.

I just want to get your thoughts on what you think is a more sustainable net interest margin for DenizBank as deposits continue to move up. What do you think would be a more sustainable cost of risk for DenizBank? Any comments on how you plan to navigate the more challenging second half macro in Turkey would be very useful. That was my first question.

Then, two very quick questions, one on cost to income ratio. We see that you haven't upgraded your guidance on that front, so just wanted to get your thoughts on if you're missing something in terms of the upgrade to your cost to income guidance. Then, lastly, loan growth. What opportunities do you see currently in the local market, especially on the corporate side? Thank you.

Patrick Sullivan

Just on Turkey, on the sustainability of margins and the cost of risk. First of all on the cost of risk, Turkey did benefit in Q2 from some quite strong recoveries. Their non-performing loans has dropped. If I had to pick out a sector in particular, it was the property sector where there has been a lot of strong international demand for property, so anything that was in the non-performing loan category and secured by property, we're seeing some good realisations there.

The overall cost of risk guidance hasn't changed but if we continue to see good progress as in Q2, I would hope cost of risk would be towards the lower end of that guidance. Obviously, quarter to quarter you have retail flow cost of risk coming through and then you have your corporate new non-performing loans, often offset by recoveries as well. So, it is never going to be perfectly linear. I think Q2 was particularly strong and it's more likely there would be something of a higher cost of risk in the following quarter, specifically for Turkey.

Just on sustainability of margins, we know that macro monetary policy is not as conventional as it might be and the rates in the current market, there are wider spreads in new lending, whether it is in Lira or foreign currency. So, that has seen a nice step up in the second quarter and that is partly also aligned to the global trend of the cost of funding as well.

So, NIMs have taken a nice step up. Will it go up more in the second half? Possibly, but I couldn't estimate at this point by exactly how much that would be. We have estimated that overall, for the full year margin guidance, you can run the maths that Turkey might contribute 20 basis points of that.

Shayne Nelson

I'll just elaborate slightly. I'd say we shouldn't underestimate how difficult the first half was for Turkey. Very difficult operating environment and they produced some very strong results. I think the management team are very good and agile at reacting to the market pretty quickly to maximise profitability and reduce problem lines there.

We haven't seen very much in the way of, especially on the corporate side, new problem loan information and I think I've made this comment many times to you. We went in early, we went in hard there and we are seeing recoveries from that conservative approach that we did early on in the piece. You can't underestimate that it is a difficult operating environment because it is, but we have a strong management team there that is very good at managing through these difficult circumstances.

On liquidity, I think from us, ourselves, when our loans mature I think there is certainly an element of our ownership helps with their liquidity and so far we're received no indication that their own liquidity is under any pressure at all. In fact, we monitor it as part of our normal group ALCO position.

Patrick Clerkin

That is underlined, Shayne, by the fact that they were able to upsize the syndicated loan that they did in June which, for a Turkish bank, was quite an achievement this quarter

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Patrick Sullivan

Cost to income ratio. Waleed, the 33% is a top end, long-term target. We operate within, under, lower than, whichever way to describe it. You may recall that for one year we increased it to 35%, more reflective of a significant loss of income after the rate cuts as we went into the pandemic. So, we've been able to restore that guidance back to your long-term 33% but we don't give a specific number. We give you some indicators on the income. You can see our trend on the costs page by quarter. So, that's where we are today.

Shayne Nelson

Let me start with the retail and then I flip to corporate. Retail has been super strong. The first half, both in Emirates Islamic and in ENBD, both engines are absolutely firing in the consumer space. We continue to take market share and we've been writing record new credit card numbers that we just haven't seen before. So, I think in that side it is very strong. On the corporate side, actually their growth has been super strong, offset by sovereign repayments. We still see opportunities in things like pre-IPO financing and stuff like that coming through. We're seeing new projects now come more to fruition than we have seen, some in property but a whole range of different areas we're seeing demand reemerge from our corporates which really started last quarter. I think I did say in the last quarter that the appetite was pretty low at the moment from our customers but we are seeing a return of demand from our corporate customers.

Patrick Clerkin

If you look at the financial statements, Waleed, you'll see the growth has been right across a range of sectors, utilities and services, transport, communication, personal, manufacturing, enterprise and management, real estate. So, it has been right across the board.

Waleed Mohsin - Goldman Sachs

That's very helpful. Just one last follow-up from my side. On the increases in rates, are you expecting or are you seeing any early signs of an impact on retail demand being tempered by higher rates?

Shayne Nelson

So far, no. In fact, the opposite. I've been pleasantly surprised, to be honest, but I think one of the things that we're seeing is there is population growth in UAE at the moment. We are getting new businesses opening. We are getting population movement and investment into the country. So, at the moment, no. We're not getting any pushback on loan growth because of rates.

Now, will that continue in the future? Obviously, there has got to be an inflection point but at this stage, no, it is not impacting our capacity to grow in the space. I think in the corporate side because of the liquidity in the system we are seeing margin pressure on new corporate loans. I don't think there's any doubt about that. The impact on the corporate side is more on the customer than it is on the banks, given the liquidity in the market.

Operator

Our next question comes from Waruna Kumarage, from SICO Bank.

Waruna Kumarage - SICO

I have three questions. The first question is on the loan mix. As you have mentioned, the sovereign payment has been offset by private sector and personal. I want to understand the margin improvement and even the guidance. Is that a factor in this considering that typically the rates on sovereign loans are low? That's my first question.

Shayne Nelson

Let's take that one before you get to your second. I think it is fair to say that the new corporate bookings, as I said just earlier, have lower margins generally than we've been experiencing historically. However, because of our 62% CASA, with the FED lifting rates and then followed by the central bank here, obviously we're getting high spreads out of that, just by our funding mix. I think one of the things that you need to remember. It's not like we accidentally found this CASA. We've been building this up and talking about it for many, many years now. It was a strategic objective for us to build CASA for the eventualities of higher interest rates. It hurts us when rates are going down but is a high pick-up on the way up.

Patrick Sullivan

There is one additional point there, Shayne, is the retail side, EI growing AED 5.0 billon, ENBD retail growing AED 5.0 billion. That new origination is also at a higher margin than you would see in corporate lending as well, so that is adding to the margin growth.

Shayne Nelson

So, I wouldn't like the participants on the call to think that our profitability is only driven by rate increases. That is not true. It's the volumes, also, that we've been driving through, especially in the retail space.

Waruna Kumarage - SICO

That what I was trying to get at, not necessarily rate increase but the mix change of loans, would that have helped the margin expansion to a certain extent? That was my question.

Shayne Nelson

Yes, it does. Obviously, the retail side has much better spreads than the corporate side.

Waruna Kumarage - SICO

Two more quick questions. The first one is on DenizBank. In this quarter you have seen significant hedging gains. I was wondering how do you see it going forward? Can we consistently see these kind of gains being made? The third one was to see whether there was any positive impact from CPI linkers that DenizBank was carrying that would have offset this net monetary loss? Thank you.

Patrick Sullivan

Okay. Just on the consistency of gains, the environment there, we're seeing strong, loan growth. The costs are being really well managed. There is an inflationary environment but inflation hasn't really come into the numbers, it being offset substantially by foreign exchange. But, on the income side, we do get some variability from quarter to quarter over the last two years. I think we've been articulating what some of the ups and downs are, including some of the hedge mark to market gains and losses that can come. That was a part of the increase of Deniz this quarter.

Some of that, if the curves were to settle down a bit, and with US rates going up, that might not be the fact into the next quarter. Some of that could reverse but underlying some of that mark to market variability, they do have really strong client flow increases, as well. Some of the customer spreads in foreign exchange, for example, have been widening over the last year, so that's helped contribute to it. How much further it grows, I couldn't say specifically right now.

On your point on the CPI linkers, I think the Turkish government issues, $4.5 billion of CPI linkers through February and March, so these are bonds that have 10 – 15 year maturities. They're zero coupon but are tagged to CPI increases. So, yes, part of the interest income has an element of an increase in that. It's not part of the book that we break out separately but that, indeed, amongst a number of other revenue streams, did help the earnings for DenizBank in this quarter.

Operator

Our next question comes from Aybek Islamov of from HSBC.

Aybek Islamov - HSBC

I wanted to ask about your monetary loss in the first half. How much of your monetary loss is due to the re-indexation of the P&L in Turkey and the balance sheet revaluation, so to speak? That's the first one. Obviously, I guess your core revenues have been impacted by this re-indexation of the P&L in Turkey, so it's very difficult to understand the real, underling core earnings trend in the group. So, that's what I'm asking this question. The second question is looking at your loans to the public sector, quite a steep decline in the second quarter. Why is that? And was there a reclassification of your corporate loans between the public sector and the private sector in the second quarter? Thanks.

Patrick Sullivan

Just on the monetary loss, we have set out in note 2 the impact of indexing in the P&L so that you can see. The net P&L before the inflation adjustment is just on 200 million. That then reverses in the hyperinflation row itself. So, you should be able to then see what an excluding indexing number is for Turkey, as well, so it does come back out. Just on your part on the public sector, I'm not sure where you're getting that from specifically….

Shayne Nelson

I think I understand what he's getting at. For example, if you looked at DEWA, once that is publicly listed that comes away from the central bank's classification of it being government once it is publicly listed. Is that what you're getting at?

Aybek Islamov - HSBC

I guess that could be it. You have your sectoral breakdown of your loan book and in there you have public sector loans which are 124 billion in the second quarter. In the previous quarter they were 139 billion. So, maybe that has to do with the listing of the companies.

Shayne Nelson

Some of the financing is pre-IPO financing. Any company that is going to list makes sure it has the right of leverage within the entity itself. So, some of it would be pre-IPO financing but not all.

Patrick Sullivan

Aybek, both private and public sector has been increasing. You can see in our note the GRE lending is up to 10%, so you know that 10% of 422 billion book is 42 billion, so you can see how much in total that has gone up. Corporate has gone up about 23 billion. So, three quarters GRE, one quarter private sector.

Aybek Islamov - HSBC

if I may, it looks like you were having provision writebacks in Turkey in the first quarter. Is that right? What's driving the provision writebacks, if that's the case?

Patrick Sullivan

Yes, indeed they did. In Q2 they saw some very strong recoveries, particularly with loans collateralised in the property sector, so very strong demand in that sector. Obviously, we don't have client-specific information for you, but they did. It was a very good quarter for them. In fact, their P&L had a small credit in the impairment line for Q2.

Operator

Thank you. Our next question comes from Alok Nawani, from Ghobash Trading and Investment.

Alok Nawani - Ghobash Trading and Investment

A couple of questions on Turkey. The first one for Deniz, if you could quantify the amount of any one-off impact that might be there in the non-funded income in the first half for Deniz alone, that would be helpful. The other question is would you be able to give us any colour on the NPL coverage levels that you have in Deniz and how close that might actually stand to ENDB consolidated levels? Generally, speaking we're looking to get some sort of a view on how you expect cost of risk to evolve for the next 12 months for Deniz. The second quarter can't really be reflective of reality with such high inflation. So, I just wanted to get a more balanced view from yourself.

Patrick Sullivan

Hi, Alok. It's Patrick here. Maybe, if I can just do that in reverse. The Stage 3 NPL coverage at the point of acquisition was around 50-55% and over the last 2.5 years or longer, has increased to the 70-75% level. So, we have been building up that provision and that's one of the drivers of the higher cost of risk within the 400s in our first year of acquisition, then to the 300s, now dropping down into the 200s.

As we've built their coverage and got comfortable with that, I think that level of cost of risk has been declining. I couldn't give you any specific guidance on what the longer-term rate will be other than the current year guidance that we give for the overall group of 120-125 basis points and, as I think I said a little bit earlier, if we see continued positive progress on recoveries in Turkey, and they were building up provisions over the last two years, then I would hope that tends to the lower end of that guidance.

Just on NFI one-offs, we don't give specifics on one-offs. You can see how much on the NFI on page 9 that we have gone up from 1,188 in Q1 to 1,552. That's not all DenizBank. DenizBank is a big part of that, yes, but not all of it is one-off as such because they've got strong underlying customer revenue also. So, it wouldn't be more than a few hundred million of mark to market type gains that may or may not reverse in future quarters.

Shayne Nelson

From memory, Patrick, DenizBank balance sheet and P&L is on their website. So, you could actually go and pull the whole thing off if you'd like. Q2 will be out very shortly.

Alok Nawani - Ghobash Trading and Investment

Can I just ask a general question on Deniz? What is driving the asset growth that we're seeing for Deniz in local currency terms at the moment? How sustainable are those kinds of numbers?

Shayne Nelson

It's widespread between their cards business, their SME business and their agricultural business. The corporate growth area has been negligible.

Operator

Our next question comes from Naresh Bilandani, from JP Morgan.

Naresh Bilandani - JP Morgan

Thank you. It would be very helpful if you could please give us some colour on how should we think of the quantum of the IAS 29 charge on the P&L going forward. I know it depends on the inflation rate but based on current expectations I would appreciate if you can offer some insight into how should we think of the quantum for the rest of the year. Also, it would be very helpful if you could please explain what should be the criteria for Turkey to shift out of IAS 29. For inclusion it was a cumulative inflation of 100% for the past 3 periods. It would be very helpful if you can tell us for how long can it stay and what makes move out.

It would be helpful if you can please reconfirm, did you include DenizBank Austria also for hyperinflation adjustment or was that not included at this stage? And a more generalised question. It would be very helpful if I can get some early thoughts from you on the impact to the franchise and the economy from the application of corporate tax next year. Is there any clarification on the application of 9% or 15% corporate tax for the UAE banks? Any thoughts you can provide, that would be great.

Finally, Shayne, if you can please, as always, throw some light on the operating metrics for Liv, especially the performance in Saudi Arabia. That would be great. Thank you.

Patrick Sullivan

Thanks, Naresh, as always. IAS 29 in H2, page 14 you can see it is based on the index. In the first half inflation went up 42%, so it is a rachet on the way up as the index increases. The central bank of Turkey put out a publication recently suggesting they have lifted their full year view to 60%. Research teams might indicate 70%. You could do a pretty good estimate of what our H2 number would be with a little bit of proportioning on that increase. So, 40% this half, 30% or 20% next half, you would expect it to be somewhat lower than the 1.9 billion that we've passed through for this half. On the criteria to shift out, it is similar as on the way in. You have to see less than 100% over a 3-year period before you stop hyperinflation accounting. So, it could be around for a couple of years to come.

And the third one on Austria. Is that included? No, it's not. We only index and apply the indexing to the Turkish Lira balances. Corporate tax, yes, it is either 9% or 15%. As a larger entity in the UAE, we would fall into the 15% bucket. This new corporate tax won't apply to us until January 2024. The actual rules and guidance has yet to be published, so we don't know exactly what an effective tax rate might be because you don't know what is assessable and what's deductible entirely at this point in time. So, that's one for us to think about through next year.

Shayne Nelson

Just a comment on corporate tax. Following the new OECD guidelines that there is a global 15%, I think it was only prudent for the country to adopt a 15% rule, because if you think about it, let's say it is Amazon, if they make a profit here and they don't pay the 15% here, they're going to pay the 15% somewhere else. So, profit generated in the country will now be tax that they would have been taxed in an offshore location. So, to me, it is absolutely right that the country should be earning its fair share of the tax base that would then be paid somewhere else. I think, from that perspective, it's a fair basis for the country to adopt this. Certainly, we have not seen any companies coming to the country and saying, oh, I don't know if we'll open here because the tax rate is too high because, if you look at it in global terms, 15% is extremely low. So, it is still a very low tax base. I've worked in many countries throughout the world and I'm sure most of you have. 15% is a very low corporate tax rate for anywhere in the world, and 9% is even lower.

On Liv. you asked particularly on Saudi. Saudi is picking up about 3,000 new clients a month. That's about where it is. It is out of the sandbox now. We've got the no objection certificate from the central bank now to bring it out of the sandbox. We are actually doing a strategy review on Liv at the moment, around the functionality build and the target clients. I'm hoping by next quarter we'll be able to sit down and talk to you in a bit more detail about Liv, as to where we see its future direction. We're doing a technology rebuild on it at the moment, moving it to the new stack versus the old stack. So, 'watch this space'. I think we've got some new exciting functionality and products that will come to Liv over the next 6 to 9 months, providing the digital guys get the build done.

One of the problems we have is our digital demand on our IT guys is huge. So, trying to slot everything in that we want to get completed is actually quite difficult and, as I'm sure all of you know, getting those resources in the UAE is not easy given the competition. However, there is light at the end of the tunnel for us, at least, from a crypto and a technology winter because we're now we're seeing jobs lost in those industries. That is now providing us with more talent than we would have had the capacity to attract historically. So, we are seeing an uptick in the capability to recruit.

Operator

Our next question comes from Shabbir Malik, from EFG Hermes.

Shabbir Malik - EFG Hermes

My first question is on in the repayment that you've seen from the sovereign. Do you have any visibility? Do you think this is a secular trend or this is just a one-off that we saw in the second quarter? Second question. We've seen one of your peers taking something called a CVA risk charge in their capital calculations. Does this apply to ENBD as well? And, finally, we've seen also some of the regional banks taking mark to market losses on AFS portfolios because of challenging market conditions. I don't believe it has been that material for ENBD. I was wondering what's the reason for that. Finally, there used to be a DenizBank business overview slide in your presentation. I didn't see it this time. Maybe if you can share that later, that would be great.

Patrick Sullivan

Maybe if I can just take those in reverse order. Just on the DenizBank page, what we did instead of that page was bring Deniz further up the deck to page 4 and for you to see the composition of the P&L of ENBD plus DenizBank to give the consolidated results. That's on page 4. I think there were a couple of other data points before that weren't necessarily useful or meaningful. So, we'll take that feedback but we thought it would be better to have that on page 4 in the consolidated results.

Just on the mark to market losses on liquidity book I presume, if you're looking at other banks' investment portfolios. The vast majority of our investment book, our liquidity management is held at amortised cost, so we are likely to have less going through the fair value OCI, let alone fair value P&L,

and I think you can see those on page 10, note 5 of the accounts as well and their respective classification to support that.

On CVA, yes, that was the finalisation of Basel 3 for the CVA RWA calculation. Yes, we have some of that. So, part of our increase in the RWA in the capital build for Q2 included some of that. It was less than AED 10 billion of RWAs, which would equate to 25 basis points or less, but you can see that we have easily been able to absorb that with our strong earnings for the quarter. As for repayments, yes, the government finances are in good shape and they have taken the opportunity to make repayments. They started those repayments through 2020 quarter by quarter. Yes, there have been more in this half. We wouldn't know specifically the future payment profile.

Shayne Nelson

And if we did know we wouldn't be able to comment because it is a client.

Operator

Our next question comes from Chiro Ghosh, of SICO.

Chiro Ghosh – SICO

Just a very quick one. The non-monetary asset calculation, does it apply also for the collaterals?

Patrick Sullivan

No. These are simply the non-monetary assets in Turkish Lira on DenizBank's balance sheet, so it's not any collateral. It's things like property and premises and non-banking financial instruments.

Chiro Ghosh – SICO

The income gain which made on the derivative side, I know you answered it but is there any counter exposure against that? So, as one thing stabilises, will you see a pick-up in earnings on the other side to balance it or it will only normalise or only decline?

Patrick Sullivan

So in DenizBank, they have been managing the interest rate risk in the liability side and looking ahead they were anticipating rate rises, so they were locking in lower rates and when you do that on a derivative basis then you are going to get a mark to market gain. So, that would really reverse if the yield curve came down at the longer end. With the monetary policy there at the moment and rising Dollar rates, we don't see that happening in the near term. It would be nice if it did.

Operator

Our final question for today comes from Edmond Christou, of Bloomberg Research.

Edmond Christou – Bloomberg Research

Just a quick question on the CET-1. The net earnings, you consider here, 4.8. If you just give me some highlight on how this has been calculated in terms of the net earnings compared to the one you reported on the income statement. I think there is an adjustment of IAS 29 here. The second one is on IAS 29. Is it possible to give what is the level of net monetary positions and what is the CPI linker portfolio there, just to be able to see what is the gap and how much you can add CPI linker to the portfolio? Thank you.

Patrick Sullivan

Just on your first one, on the CET-1 build. On page 10 you can see the net earnings, 4.8. The composition of that is the total comprehensive income that comes from page 4 of the accounts, so that's 5.2 billion. We take off from that the 1.1 of the hyperinflation adjustment. So, its 1.1 represents the non-monetary revaluation, so that doesn't count towards regulatory capital. Then, we get to add back 0.7 for the loss on cash flow hedges. So, 5.2 minus 1.1 plus 0.7 gives you the 4.8. And you asked what is net monetary position?

Edmond Christou - Bloomberg

Yes. I'm trying to establish what is the gap between your CPI portfolio and net monetary position because this has become important for ROE going forward.

Patrick Sullivan

CPIs, I think you'd be able to find that in the DenizBank financials which should be released shortly.

Patrick Clerkin

I'm conscious there's a few questions that we haven't been able to answer but we've run out of time. If you want to reach out to me, Paddy Clerkin, at Investor Relations, I'd be happy to answer those offline. Shayne.

Shayne Nelson

Thanks, Paddy, and I'd like to thank you all for joining the call today and I hope you recognise the very strong set of results that we have produced.

END