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Alinma Bank Q4-22 Earnings Conference Webcast Transcript **Thursday, 09 February 2023**

Operator: Good day and welcome to today's conference. I'll now turn the call over to Waleed Mohsin. Please go ahead.

Waleed Mohsin: Thank you much. Good day, everyone, and thank you for joining us today for Alinma Bank's FY2022 Earnings Call hosted by Goldman Sachs. It's my pleasure to welcome the Alinma management team represented by the CEO, Mr Abdullah AlAlKhalifa, the Deputy CEO and Head of Retail and Digital Banking, Mr Saleh Abdullah Alzumaie, the Chief Financial Officer, Mr Adel Saleh Abalkhail and the Head of Investor Relations, Mr Ahmed Sager.

Please note that today's call is being recorded. The call is intended for investors and analysts only, and any media personnel should hang up at this moment. So without any further delays, I will pass on the call to Alinma Bank CEO, Mr Abdullah AlKhalifa.

Abdullah AlKhalifa: Thank you, Waleed. Welcome, everyone. We will, as usual, will take you through a quick presentation and then later on, we'll open the floor for your question. The presentation starts with page four, which gives you an overview of the market share, financial position, stock highlights and digital snapshots.

Page six talks about the overall view of the financial performance. Adel following my presentation will give you a detailed presentation on the financial performance of Q4. But our loan growth rates increased by 16% to reach 146.5, slightly lower than our guidance of high teens. The reason for this is we had a few loans that totalled about 1.4 billion that was highly expected to take place and booked before the year-end.

Unfortunately, due to maybe documentation issues and so on, it was actually booked after the new year, after the end of the year, as well as an unexpected repayment of 100 million received in the last few days of before the year-end, that a swing of 1.5. If we add this 1.5 to the portfolio, we would have increased our loan by 17.2, which was in line with our guidance.

We had a strong growth in total assets, 16%, 20% increase in our operating income to reach 7 billion and 163 while our net income increased by 33% to reach 3.6 billion. Our NPA ratio increased to 1.94 and our coverage ratio declined to 136. And maybe that's an opportunity to talk also about the cost of risk, which is not this slide. It will be coming later, but we were – our guidance for cost of risk was 65 to 75 basis points. We closed the year at 85 basis point. And the reason behind this mess is that we were fairly confident about full recovery of stage three exposure, a sizable stage three exposure through the sale of collaterals.

Auction was set up towards 27th of December with the most conservative valuation enough to fully cover our exposure. So naturally, we put a reserve price. Unfortunately, due to the short time in terms of marketing campaigns on this auction, we didn't get the right price. So it seems like now 2023 story rather than 2022 recovery. The same time there was an exposure within stage two that was under discussion for restructuring and due to the slow progress on the

discussion, it was decided to be prudent and move that exposure to stage three. As a result, we ended up with higher cost of risk and higher NPL ratio.

Our customer deposits increased by 20% to reach 145 billion. But more importantly, the growth on CASA we managed despite the high interest rates, which, as you know always means a migration from current into time. We managed to increase this by 4%. I think today I saw the two largest banks published financials and both of them show a decline in current accounts. So we don't see the industry yet, but I would imagine that industry will see a similar trend.

Our cost of income came in line with our guidance. Our guidance was to be below 35%. We closed the year at 34.7. Our NIMs expanded by 20 basis points to reach 362. 20 basis point was the lower end of our guidance. Our guidance was 20 to 25 basis points. Later on, you'll see on page 17 how cyber moved since August and the big growth in cyber was around 3%. But towards the end of September, start picking up, end of October reaches close to 5%. And as you appreciate, when interest rate goes up, the first thing that can happen to you is your cost of funding goes up faster than the benefit of repricing your assets as it takes longer to reprice.

Our CASA, obviously, is at 50 diluted when I mentioned in Q2 that because of the expected growth in loans, we will have to take more time deposits and a result that's been diluted to 56.8. But with this current interest rate, I think it's a good rate in a way. Our CARR reached 19.8, so I guess we have better efficient capital now.

Now in terms of the strategy, which starts at page eight. Just a quick reminder of our current 2025 strategy. One of the headlines is obviously we want to be the fast and most convenient bank in the country. We want to be the best service provider by being number one net promoter score and as well as being number one employer of choice. On page nine, gives you more details on [inaudible] business. But Bank wise, we want to build a digital factory. We want to enhance our analytics capabilities and also achieve a culture transformation that will allow us not only to attract, but also retain the talent, the top talent in the country.

In retail, we're focused on building our affluent and high net worth franchise. Want to focus on the youth segment and be the best customer service provider through best NPS, Net Promoter Score. In corporate, we want to be the main bank not only for large corporates but also for mid-corporates. We want to develop our high quality SME franchise and as well as growing our cash and trade businesses. In Treasury, the top priority was obviously in addition obvious to margin liquidity and ensure sufficient funding in terms of assets. But we wanted to be also the main provider for all our customer needs, whether it's hedging their interest risk or FX risk.

On page ten, talk about some progress. We already achieved 54 initiatives out of total initiative 76, so very good progress. Some of the activity that took place in Q4 as an example, I'm not going to go one by one. But we launched

auto loans, auto lease, which we didn't have before. We're leveraging now our branch networks through offering point of sale on a smaller scale, smaller merchants, the main point of sale businesses within the semi. But as you know around the country, the smaller merchants that there is need for such products and we're progressing very well.

We're also bundled products and start selling bundled product for SMEs rather than individual products. We achieved 270% growth in assets, mid corporates and even higher growth in 467% growth in unfunded, 108% growth in point of sale and 46% growth on Kafalah. And we installed and we went live with our new treasury system and we started selling more derivatives. And the story I think will be given bigger in terms of the size of profit rates, for example, in Q1, as we did the sizable deals in this month.

Some of the things that we will be working on during 2023 will be 2022 initiatives will be starting in 2023, and some of them will obviously finish in 2023. Some will extend to the year later. So in terms of bank-wide, we want to continue to expand the utilisation usage of robotics or improve the efficiency and the turnaround time for all our products. We want to improve the retail app. Finalising now, we're going to go live with a new retail app as well as by end of this quarter, we're going to launch our well anticipated youth app that I talked before.

On retail, I want to enhance the family ecosystem. We want to launch and implement a new loan origination system for corporates. We want to digitise mortgage journey for our customers. We already digitised personal finance, the auto lease and credit card, but we now continue to digitise also the mortgage business while we continue to develop our regional distribute model, and we want to build an integrated portal for all corporate segments to include the semi and mid and large. In Treasury, we're developing more structured deposits. We want to increase the duration of the liability, so we diversify the funding options through inter banks and through our customers.

That is a quick presentation on the overall financial performance as well as strategy. And now I give the floor to Adel to give a detailed presentation on the slides.

Adel Abalkhail: Thank you, [inaudible]. Very good afternoon to you all and thank you for again joining us on our end-year call for the FY2022. I'll be running you through the financial performance in a bit of more details. I'll try to do this as usual in a quick way so that we will allow more time for the Q&A session.

On slide number 13, on the overall balance sheet trends, we have seen a year-on-year 16% growth on the balance sheet and this was mainly driven by 16% growth in the financing and also a 16% growth on the investment portfolio year on year. On the total liability movement, we have seen an 18% growth, which is mainly driven by 20% growth on the customer deposits, and 8% growth in due to [inaudible] and banks and other financial institutions.

And on next slide, slide number 14 on the P&L trend, net profit after the cut for the full year, we closed at 3.6 billion. That's a 33% growth year on year was mainly driven by growth in the total operating income of 20%, which as you can see in the top right-hand graph, this 33% was basically an 18% growth from funded income and 25% growth in the non-funded income. Despite the increase by 17% and the total operating expenses, there was slightly lower impairment charges year on year by 6%. And the graph on the same slide on the bottom right graph, the overall operating income composition, 76% is from the funded income and the remaining 24% is denominated income between the other income and exchange income and also the fees from banking services.

On the next slide, slide number 15 on the financing, as mentioned earlier, we have 16% growth on the financing that, as you can see in the bottom left graft, the growth basically was a 32% growth in the financing for home financing and also a 34% growth in the personal and other retail products. Other retail products would be the revolving credit card that was launched last year and also the auto lease financing that was launched in Q4 in 2022. A 10% growth in corporate that includes the mid-corporate and also large corporate and project finance and 27% year-on-year growth on SME business. The overall financing composition is corporate plus SMEs represent 75% and the remaining 25% is the retail financing outstanding as of December.

On the next slide, slide number 16 on the deposits as mentioned by the CEO earlier, despite the challenges of increasing interest rates, we managed to grow CASA by 4% year on year. And obviously, with the growth in the financing, time deposits has grown 51% year on year. If you can see on the center of the page, the CASA as a percentage of total deposits as we have been expecting, this percentage and the CASA's percentage of total deposits to dilute. We have reached the peak in Q2 last year where we reached around 71%. But with the increase of time deposits as of December, CASA stands as 56.8% of the total deposits.

On the next page on the yield income or income from financing and investments year on year, the total funded income has increased 34%, and that's a representation of 33% growth in funded income for financing and also 40% growth in income from investment. If you see the graph in the center where the YTD NIMs has moved, we start to see the pick up on the NIMs as an expansion. We have seen 11% up to the end of the first half 2022, then another 17 basis point growth expansion in the nine months YTD. And we closed the NIMs at 3.62, which is 20 basis point expansion, as mentioned earlier by the CEO, which is at the lower end of the guidance, within the guidance that we gave, which is 20 to 25.

This is just to remind ourselves of what happened in Q4. And if we look at the graph on the bottom left, which is the movement of three-month cycle. And clearly, if we see the movement from July to December, we start to see the big shift from the 3% level of three-month cyber up to slightly more than 5% level in late September and early October. And

as mentioned by the CEO earlier, this has impacted the cost of funding in a way that the repricing on the shorter-term deposits take place. And this will be part of the explanation on the overall NIMs expansion during Q4.

The next slide, slide number 18 on the fee and other income, we have managed to grow the non-funded income by 25%. Fees upon banking services has grown 13%. We have a very good growth also on a fixed income year on year, which is 56%, and also the investment gains and also the valuations and investments and also dividends and other income has grown as well. As fees from banking services composition as usual, 34% on the card services, 33% is from the fund management, 10% will be the trade-related services and 7% will be the brokerage and other income 16%.

On the next slide, slide number 19, on the operating expenses, we have had the growth on the expenses 17% year on year. As you can see on the top right hand graph, the 19% growth in salaries and employee-related expenses, D&A, depreciation and amortization has increased 11% and other G&A has grown up by 17% year on year. The positive jobs that we have achieved around 230 basis points positive jobs in the year-end has resulted on seven points per thousand improvements on the cost to income. So the cost-to-income ratio has decreased from 55.4% in December 2021 to reach 54.7% by end of 2022.

The next slide, slide number 20. As mentioned by the CEO earlier on the environment, we have seen a 60% jump on environment. Also the overall year on year, 60% sequential basis, but year-on-year was lower by 4%. And that's why you can see the graph in the center of the page, cost of risk, it's reduced year on year by 70 basis points. Yet the 85 basis point cost of risk was 10% more than the high end of the guidance. And this was explained earlier on what happened during Q4.

The next slide, slide number 21 on the NPL and NPL coverage. So the non-performing loans, as mentioned again is also – some accounts moved – the accounts mentioned by the CEO that's been under discussion for restructuring. We have been prudently moving that, and that has increased NPL in Q4 in a sequential basis by 22%. NPL ratio we're closing at 1.94. That's almost 19 basis points above December 2021 level. Coverage ratio, as we always mentioned and we kept that during the first quarter and second quarters this quarter within the 150% range. However, was explained earlier on those expected settlement that has kept or reduced the coverage ratio by year-end to be 136.3%.

On the next slide, on the capitalization and also liquidity the bank remains healthy in all ratios. We can see from the capital adequacy by the year-end capital adequacy ratio stands at 19.8%. We have also a very good improvement on the ROE moving from 10.8% to be 15.7% by December 2022. And also that's also an improvement in the ROE from reaching 1.9% from 1.6% level. All the liquidity ratios are looking at to LCR well above the regulatory minimum. And also there are some LDR standing at 82.8% by end of the year, which is also well below the regulatory maximum. And it's about as well 106.1 by December, which is again well above the regulatory minimum.

In the next section, we will be talking about the outlook and the guidance for 2023 financial year. Just to remind ourselves of the guidance given for some of the financials, the financing growth as mentioned earlier by the CEO, the guidance was high teens and some expectation of last-minute booking that looks like slipped into Q1. This would have been within the guidance. For next year with the expectation of the continuation of the growth and the execution of the strategy, the focus of most corporate and SMEs, and also the continuous pickup in retail business the guidance for 2023 is mid-teens. And its profit margin 20 basis points year on year. That's within the 20 to 25 guidance. We are guiding for the NIMs expansion from the 3.62 year-end NIMs at 55 to 45 basis points.

On cost to income ratio, we managed to close 34.7%. That is within the guidance which given before, which is below 35. The guidance for cost to income ratio for the year 2023 is below 32. On the return on equity, the guidance was above 15%. The actual return on equity on December 2022 was 13.7. The guidance for 2023 on ROE is above 17. Cost of risk, as mentioned earlier, 10 bips above the high-end guidance. But this would be back as a reason to what was discussed on these some settlements that were expected to be happening and did not take place during the last days of the year.

The guidance for cost of risk in 2023 is 60 to 70 basis points. And also on the CARR below one we closed at 19.8%. And obviously with the expected increase in risk-weighted assets from the mid-teen growth expected on the asset side, the financing side. The guidance is between 17 to 18%. We have been asked by investors for long to guide on the long-term ROE and as part of the ongoing activities, we are guiding for the 2025 return on equity to be above 18%.

Thank you all for listening. And just before maybe hand this to the Q&A session, there are a couple of slides in the back of the presentation on the latest updates and progress and what we are doing on the ESG side. So it's for information. So with that, I'll pass it to Q&A session.

Waleed Mohsin: Perfect. Thank you much. I think we can open up for Q&A. But before we do that, maybe a couple of questions quickly from my side. Firstly, on NIM, your guidance for 2023 applies 3.75 to 3.85, which is above your exit NIM for fourth quarter, which we calculate to be around 3.7. So I was wondering what do you expect to be the key driver of net interest margin expansion into 2023, and when do you expect NIMs to peak on a sequential basis? That would be the first question.

And secondly, on liquidity, how do you see the liquidity situation so far in the first quarter? And how concerning is a combination of tight liquidity and higher rates from an asset quality perspective? And given your read of the market, what do you think resolves this liquidity tightness in the market? Thank you.

Abdullah AlKhalifa: Thank you, Waleed. Now, on the NIMs, the way we look at it and forecast it is basically if you look at the expected and changes in rates and cyber, we have witnessed, remember we started the year at roughly cyber was three months that was like 70, 80 basis points and closed the year at 550. So there's a big swing in terms of cost of funding because of this big movement. The outlook for cyber is potentially may be some growth. Some increase in cyber is not anywhere close to what we see in terms of magnitude of the change.

So in terms of cost of funding, we're not expecting significant or material I mean, significant impact coming from great changes on the cost of funding. Yes, there could be volume because obviously, we're increasing our loan and we have to take [inaudible] deposits. But as far as rates, there's not a significant impact. On the other hand, though, all our assets, even three months' assets that was booked or repriced, sorry, maybe early October, late September now will come to reprice in full for next year at higher rates towards the six months' related assets that we're booking. Again, with recovery pricing, we also have one-year cyber-related corporate loans that now will come for the repricing and that will even be a significant shift.

In terms of repricing of liability, yes, there will be some repricing, but as you may appreciate, liability tends to be short term. So majority has already reflective of the current rate. In addition to that, you have also the business growth. The loans come in booked. The new loan booked, whether it's project finance, mid corporates, SME, large corporates or retail that also will come at prices close to the markets, similar to the market rates that we see. So on all these combination, we believe the NIM expansion is the guidance that we gave.

On liquidity, it is a challenge I have to say. We've seen already some action taken by central bank replacing government deposits with the banks. There's so much obviously money outside the country that the central bank can manage and we believe that could be easily if the market needs they can provide this. I think we collectively as Saudi banks, we may be now more encouraged to go internationally to issue whether it's senior tier one or tier two. That can also help. The investment and the increase in FDI coming to the country that will help support liquidity. Loans themselves also create liquidity. So all in all, yes, it's a bit concerning, but we don't lose sleep over liquidity in a nutshell.

Waleed Mohsin: Perfect. Thank you much. Operator, we can open up for Q&A, please.

Operator: Yes. As a reminder, that's star one for questions. And we'll go first to Naresh Bilandani with JP Morgan.

Naresh Bilandani: Yes. Hi. Thank you. It's Naresh Bilandani from JP Morgan. Thanks for the presentation. Three questions for me, please. Just to be sure, are you –actually, you know what? Thanks also for a good guidance. It's a very much-needed respite to the selloff that we've seen across in the sector. So congrats on that. So now my first question is

just to be sure, are you expecting any rate cuts that are implied in your guidance? I'm just trying to also get a better view on what is the sensitivity for any rate change that you have for this year.

And also I think just on that line, if you do get a rate cut, as is implied in the consensus expectations, would the first impact be actually positive just consistently with the impact that we saw last year, that liquidity repriced up first before assets did. So we initially saw NIM pressure and now you seem to be a lot more confident the net interest margin coming through this year. So how should we think of the NIM assuming those changes from this point on? That's the first question.

Second is some of the banks that have already reported the guidance, your larger peers are guiding a somewhat of a lower loan growth than your guidance at this stage. Is that because their retail mix is higher and that is expected to slow more than the corporate or is this a base impact or what is the other reason that you think you'll be growing much faster than the peers at this stage?

And my final question is, thanks for publishing the medium-term ROE, actually 18%. That's quite helpful. Could you kindly guide on how should we think of the medium-term cost of risk and broad-based like the medium-term fair dividend payout because both of these will have had a bearing on how you are thinking about the ROE at this stage? Thanks very much.

Abdullah AlKhalifa: Thank you, Naresh. In terms of rates, Adel.

Adel Abalkhail: So, yeah, thank you, Naresh, for the question. On the commission sensitivity, again, if you recall what we have communicated in the year-end 2021 when we have been talking about the ten basis points expansion for every 25 bips, increased rate. That's now above the 20 bips that we had for the full year as an expansion really proved that this static NIMs sensitivity remains theoretical, so it's subject to many things. And also again, sometimes really hard to forecast the behaviour or the impact of the transition that happened on CASA and also the repayment behaviour that happens when it comes to the increasing rates.

So are we forecasting any rate cuts during 2023 within this guidance? No, no cuts is expected. And the average cyber that is being incorporated in this guidance is around 5.5%. So expecting a couple of more hikes to happen during 2023, including the one we have seen in February. So, again, you'll also see from the financials that our net commissions sensitivity gap in the balance sheet for the one year.

It used to be a 60 billion during the end of 2021. Now it's reaching 45 billion. So this explains the impact on the NIMs this year and how we are optimistic for the next year because some of the deposits now are on the time deposits that is becoming within the 12-month maturity and more into the 1 to 3 months. So this also, as we said quickly, when cyber increases, as we mentioned for Q4 that starts immediately to eat into the NIMs. So the guidance is also, as mentioned by CEO earlier, is also what you expect to have a repricing for the remaining back book in the corporate. And this would have a major positive impact.

Abdullah AlKhalifa: Okay. On the loan growth, Naresh, obviously when you look at our main strength, one of the important measurement that we have is a strong project finance. If you look at 2030 and the amounts of projects in the pipeline and the amount of financing and expected to finance is significant and that plays in our hand because that's the natural strength that we have. There could be – there's some estimates that maybe in 2023 as much as at least 80 billion worth of projects certain that will be launched in the country. Not saying all of them will be financed by us, but it tells you the size of project finance demand coming to the market in 2023 and that is not expected also to – that demand or that credit for project finance is expected to reduce even 2024 or 2025, I think. The levels would be high in the next three years.

Also as you know in our strategy, we really focus on building and developing our mid-corporates and we are achieving a very strong growth and we continue to attract more customers and continue to grow in that segment. SME we introduced so far already have six programme-based lending, so that will help us to accelerate the growth on SME. And in corporate and retail, we started with this new strategy that we build. We build the growth in the team. We will introduce incentives. We have the KPIs and the monitoring. So I think we achieved the growth faster than the market growth. And Saleh, maybe you can comment on the potential growth in retail also there for next year.

Saleh Alzumaie: Thank you for the question again. Yes, last year we had a very good growth, almost 34% growth in our retail financing, and we are expecting this growth to continue. For next year, we are expecting high teen digit for next year, especially in the more than as mentioned by the CEO. We just introduced the auto lease and the credit card. We are building in our portfolio quicker than we expected. So there is great demand.

The market share of the mortgage we managed to increase it last year from 2% to 5%, and we expect this year to continue focusing on the mortgage and the back order. So we still believe that there is a huge potential, especially that we onboarded so many customers last year, around 700,000 customers in 2022. Those customers are potential customers for taking loans this year, inshallah.

Abdullah AlKhalifa: And I think the third question on the cost of risk throughout in the mid-term. Cost of risk, I've mentioned a couple of times, I think in some of the either earnings calls or conferences that I believe throughout the

cycles cost of risk should be in the range of 50 to 60 to be prudent, to be more cautious than going very aggressively low. If you look at economic activities, what's happening in the country and even on the retail side, the unemployment is declining. More bank of our customers forming businesses for SMEs and mid-corporates and suppliers and vendors. It's not really expected to see a significant or a decline in the credit quality. To the contrary, I think this is supportive of a much better outlook for cost of risk.

But for us, the guidance for next year is 60 to 70, who knows? In 2024 and 2025, probably we put in our assumptions for the outlook and ROE may be close to that range in terms of cost of risk as well as I think you said what kind of dividends payout built into our assumptions, as we always have been trying to be obviously higher in payout. However, I think it's safe to say that it's close to the range that we have already and maybe higher to 60%. I would say that in our model.

Naresh Bilandani: Thank you. These were very helpful. Thanks a lot.

Operator: We'll go next to Rahul Bajaj with Citi.

Rahul Bajaj: Hi. Thanks for taking my question. This is Rahul Bajaj from Citi. Two questions from my side, actually. The first one is on cost. Very good outlook statement actually, and a very solid CIO reduction I see in 2023 or 2022. So just wanted to understand, I understand a large part of that CIO reduction would be coming from revenue improving and margins going up. But from a cost perspective, how much of your investment is now done and how much of that kind of large, big investment that you are planning to do is now still ahead of us? So what I'm going to basically come to is should I expect cost growth to decline also meaningfully going forward or cost will continue to grow and it's just that the revenue line, which is helping the CIO. So that's my first question.

The second question is on the youth app. I recall Abdullah mentioned youth app and has mentioned youth app before as well on calls and conferences. Just wanted to understand now that you are close to launching the app, what kind of tangible may be benefits in terms of numbers should we expect from the app over the next six, 12, 18 months? Or do you think that this is still early phase and maybe it's better to break in any upside from the app only in 2024-2025? So those two will be my questions. Thank you.

Abdullah AlKhalifa: Thank you, Rahul. In terms of cost, we mentioned multiple times that when we embarked on our journey on the new strategy, we fully realised we need to invest a lot, really, in terms of people training. Remember, also one of the strategic goals to be employer of choice. And in order to do all this and be the best customer service provider and be the fastest and most convenient, it also requires building a new franchise whether it's an affluent and private, whether it's a mid-corporate, whether cash and trade, sales specialist, product specialists.

As a result, you've seen double-digit growth somewhere around 17%, I think year on year between 2021 and 2020 and also 2022 we had also 17% growth in operating cost and that is not expected to continue. We've done the bulk of our investments. We're going to continue to invest. But the level of investment compared to the base year, let's say 2020 is going to be much less.

So when you look at our outlook for cost of income to be below 32, that's a combination. Obviously, a stronger growth in the top line, whether it's the repricing, the impact of repricing of the assets that will come in at higher rates, as well as the growth of the loans are coming at close to the market rate and not much significant impact as far as rates impact on the cost of funding. Yes, it'd be volume but not rate backed. So a combination of this plus obviously slower growth of OPEX going forward.

On the youth app, obviously, we'll focus on the youth, our intention is more on long-term strategic. We already have a very good market share in terms of achieving or gaining customers in the youth segment. However, we knew that we need to be much more proactive. It's a very young population, those clients who are college students now may not very profitable day one, but when they get a good job, they have a net source of income. Then you start building more and more and sell more and more products, and that will secure a strong future for the bank. So in 2023, we'll not have high expectations as financial impact, except obviously the volume is large. You're going to have some NIBs coming in, but not much of asset sales.

Rahul Bajaj: [Inaudible]. Thanks, Abdullah.

Operator: We'll go next to Shabbir Malik with EFG Hermes.

Shabbir Malik: Yes. Hi. Thank you very much. I have a question on your cost of risk guidance, two points, actually. One, if I look at your NPL coverage that has come off in the fourth quarter to 1.36%, which if I look at recent history, is a bit on the lower side. And secondly, if I look at your loan growth outlook for 2023, it's being driven by some more higher risk segments, such as SME and retail compared to corporate. So I just wanted to check with you that 60 to 70 basis points cost of risk guidance compared to 65 to 75. It looks a bit light to me. Maybe I'm missing something, considering that your NPL coverage has slipped a little bit and you're looking at higher risk segments. So if any comments on that would be very useful.

And secondly, in terms of your spending, do you expect your cost, the investment spending that you're doing, do you expect that to dissipate or normalise in the second half of 2023? And maybe in terms of loan growth, do you expect this mid-teen growth to be second half biased or is there – or you think this to be evenly split between the first half and second half, the mid-teen loan growth outlook for 2022? Thank you.

Abdullah AlKhalifa: Thank you. As far as the cost of risk I just mentioned in my introductory presentation is that we're expecting a sizable stage three, i.e., NPLs to be fully recovered, fully settled, fully settled without any losses. And I mentioned the story about the auction and I said this is going to be next year or just 2023. We also are expecting another good settlement coming from another stage three that was linked to their ability to do rights issue, which I believe is approved so most likely is going to happen within the first half.

So all these combination will help. Plus, if you recall, we've got, let's say we'll say in mid-teen growth and loans and everything being equal, the growth in loans will dilute the cost of risk if we take the same amount, dilute the customers. So I think 60 to 70 is a good conservative number. Fairly confident about our coverage ratio, will pick up again, maybe well beyond 150 in 2023. I think the other question is about the –

Adel Abalkhail: The spending, as well as the earlier answer around the OPEX growth. And yes, we had seen the high teens growth in the OPEX overall. But as mentioned by the CEO, let's remind ourselves, the 2021 and also throughout 2022, the bank was running through an investment cycle and we are going into 2023. And as you can see from our guidance on the cost to income, part of the guidance to be below 32 is around the efficiency and also the progress that we have seen and we will continue doing in the digitalisation.

But also there will be some, of course, impact not to the same extent, but for those investments that has been done mid-year or maybe toward the year-end of 2022, that will have a full impact during the 2023. But as an overall, I think it's in line with the previous answer, which is we're not expecting to see those growth levels in OPEX in general.

Shabbir Malik: Thanks. And maybe if you can give some colour on the phasing of the loan growth, is it going to be done equally throughout the year or do you think there is going to be some biases towards maybe the second half or maybe in the first half of this year?

Abdullah AlKhalifa: We give guidance for the full year. We don't give very clear guidance about the – by half. But project finance is something that come whenever the deal is finalised and not necessarily smooth flow throughout the 12 months of the year. However, retail is possibly is closer to the smooth sales going throughout the year is and not going to be big spikes. But project finance itself, the nature of it, the major deal comes in utilisation, maybe high utilisation spike the loan at that month. But we have obviously our own business plan, which you see it month by month. But typically, we give guidance for the year. We don't give guidance for the halves.

Shabbir Malik: Okay. Thank you.

Operator: We'll go next to Edmond Christou with Bloomberg.

Edmond Christou: Hello. Good afternoon. It's Edmond from Bloomberg Intelligence. I just want to ask on the credit growth guidance of mid-teens so we hear from banks, as they are a bit cautious on the TBR impact from rising interest rates and appetite for the corporate to borrow and even the retail. So within the mid-teens clearly are taking market share from the market. So I just want to understand what's your view on the overall market growth when it comes to lending this year. Do you expect it to be in the mid-single digit, high single digits and you are taking market on the back of it? And taking market share usually come with competitive pricing so the margin growing 35 to 45 basis points. Just find it hard to understand how this will happen. And do you have any information you can give me on terms of how percentage of your loan is yet to be subject to repricing on the five-plus cyber compared to a year ago? Thank you.

Abdullah AlKhalifa: Thank you, Edmond. Now, what I can see and we can scan in the market and knowing what's coming in terms of projects whether it's in the green project, whether it's neon projects, let's see we have also water treatment projects, not to mention obviously the mid-core but in SME. To me the market is expected to grow in double digit in the next 2 to 3 years easily, in my view, that's my own personal view. I was surprised by some of the guidance that I've seen. I don't know of the focus. Obviously, there's some kind of slowdown in terms of mortgage growth, for sure. The base is getting much bigger, but for us, it's as I said, the strength, the inherent strength that we have, which is the project finance, which tend to be very sizable deals as well as much less competition.

I think you mentioned the point about taking market share on the expense of margins. We never played a price game. We demonstrated that clearly in the first half of 2022 when we had literally no growth in corporates because we didn't want to go very aggressive on pricing. Somebody did. But in our case, we never did this and we never will. In fact, pricing on some of those deals is attractive because during construction is perceived as higher risk than a normal loan. And then they come for repricing after one or two years of operations.

In terms of the other question is about retail. We were not very active selling retail in previous years. When we build the team now we build the process, we build the KPIs, the mastering, the culture of sales, the incentives and so on. We start really picking up and as Adel mentioned we grow much faster than the market. We're going to continue. We are not the biggest player in the market, so it's very hard to achieve sizable growth in terms of ratios. But with certainly smaller base and we build this franchise very quickly by the combination of more products and much more focus now on customer acquisition and sales. I hope I covered your point.

Edmond Christou: Yeah. Can I follow up on the green and water plan and the other project that are low carbon emissions? I mean, this is opportunity for the banks in Saudi to issue green bonds and be able to access the markets probably at cheaper cost of funding. Is there any issue in terms of funding eligible projects or eligible assets? Probably this project are green, but are they eligible? Is it easy to verify it's eligible rating agency to agree on it? Because you do

have excellent opportunity on infrastructure and the green assets and financing is probably cheaper if you go through the route of green finance and green bonds, etc.

Abdullah AlKhalifa: Yeah, it's true. I think the opportunity for green projects in the country is very high. If you take renewables, whether it's solar or wind there is a significant a number of projects coming to the country. The country needs about 58 gigawatt of electricity generated from both solar and wind by 2030 to meet its commitment of 50% of electricity generated by renewables. Then you add the water treatments or sewage treatment. You have green hydrogen, maybe blue hydrogen. There could be a variety of green projects, which we're very much interested in.

Also I mentioned that we would develop in our originate to distribute. So that also could be another idea to improve the yield on the retained portion and we can underwrite more and offload to other international interested parties potentially can also do it in domestic to offer access to corporates and private bank customers to gain on this business. Issue on green bonds or green sukuk in our case, it's on the table. We'll continue to assess all potential options to improve liquidity or improve the funding structure and improve asset-liability mismatch. So that's not rolled out, but we haven't made a final decision on that.

Edmond Christou: Very helpful. Thank you.

Operator: We'll go next to Aybek Islamov with HSBC.

Aybek Islamov: Yeah. Thank you for the conference call. Excuse me. Excuse my voice. I had a couple of questions. First one is NIM guidance. Definitely quite good. I appreciate that. Can you elaborate what Alinma Bank can do differently about its funding this year compared to other peers? For example, are you looking into raising foreign currency long-term funding in 2023? Is that a potential move that you're exploring? And I think also I wanted to find out regarding the tier one debt. You already have quite a bit of tier one instruments outstanding. How much more tier one debt can you issue? And I believe you haven't issued tier one in 2022. Can you also elaborate why you didn't issue tier one in 2022? So these are my funding questions.

Secondly, on the ROE guidance, the improvement that you expect to see through 2023, how much of that improvement do you expect to see on the back of rising balance sheet leverage? And does that ROE guidance imply that you expect loan growth to be mostly driven by retail products, in particular mortgages? So is that the way to understand your ROE guidance? That's my second question.

And I think, thirdly, a very impressive performance in the mortgage market. The way you raise your market share, quite impressive. That mortgage loans that you've originated last year, how much of them are off-plan mortgages? How big is the share of off-plan in new originations in 2022? That's my last question.

Abdullah AlKhalifa: Thank you, Aybek. In terms of funding, I think it's even our strategy to explore other types of funding, long-term funding through interbank multi-year repo. We're discussing this with some of the international names or through structured deposits and with longer-term such a deposit with institutional investors, institutional depositors, as well as affluent customers. We're also exploring the potential of issuing senior sukuk or potentially fulfil the need. We can actually think about capital instruments.

You mentioned tier one. We did issue 5 billion riyal tier one. We don't see a need for another issuance immediately. That could be – we continue to assess and forecast on like almost a three-year cycle, how much loan growth, how much is expected CARR, and so on with the assumption that we continue to pay dividends. So we fulfil the need, that's always on the table and we have very good appetite for that. In terms of the ROE, you've asked about the ROE in terms of

Speaker: Include the average rate.

Abdullah AlKhalifa: Yeah. Obviously, ROE is impacted by multiple factors. If you improve, for example, your cost of income, if you improve your NIMs, if you improve, obviously your leverage. All these combinations will obviously and the cost of risk and others, all of this supportive of growth in ROE. So, yes, obviously, you saw how our CARR reduced by almost 300 basis points from a year before. That means a better efficiency and better leverage. And that also supportive of the ROE expansion. In terms of mortgage, I'll leave it to Saleh.

Saleh Alzumaie: Yeah, I think your question is about the planned percentage of the total portfolio. Currently, almost we stand around 25% of our portfolio. Our new sales are in of planned projects. Given the fact that some of the cities still not yet having projects that fulfill our criteria to finance customers. As I mentioned, we had a very good growth in the mortgage and again, we emphasise on the quality and we didn't go on this war price with other competitors. We compete and the customer experience and journeys, we are one of the most efficient in terms of reducing the loan in a very short time to the customers. And this is what we give off very good competitive advantage. Plus the things that the CEO mentioned, that we are building the sales culture, we're acquiring more customers and we are also building a very good incentive scheme to our sales agents.

Aybek Islamov: Thank you. And just a follow-up question. When you talk about your loan growth expectations for 2023, how much of that do you expect to be driven by retail, specifically mortgages? Would you say two-thirds of the growth would be driven by mortgages? Is that how you see this year? Or do you expect corporate contribution to increase materially?

Abdullah AlKhalifa: We don't give a specific guidance as far as where the growth is going to come in exactly as a percentage of the growth. However, as I mentioned in my introductory, we're expecting continued health, very healthy growth rates on mortgage, on retail. Not necessarily, the whole market growth, but the way we're doing it, we're focused on customer service, customer experience, as Saleh mentioned, that allow us to increase our market share, not pricing. It's a quality of service that we provide. It's the focus of sales. I mentioned one of the large contributor of the growth are going to be also project finance. Project finance amounts a large. And this is the area of strength that we have. So it's a combination of all of those plus obviously the mid-corporates and semi.

Aybek Islamov: Thank you. That's all for me.

Operator: We'll go next to [inaudible].

Speaker: Hello? Can you hear me?

Abdullah AlKhalifa: Yes, we can hear you.

Speaker: Yeah. My questions were answered already but I just want to go back on the NIM. So I understand that part of the [inaudible] is going to be repriced from the back end of some of the corporate loans. But then again, as you're saying the project finance and the other activities in the loans, don't you have any fear that with the high-interest rate that those projects might be delayed to 2024? And do you expect any savings from the liability side, from the consumer? Thank you very much.

Abdullah AlKhalifa: Thank you. Now, as far as project finance and the new company, as you know, the PPP is obviously a bidding process. Contractors or companies bid based on their expected costs that they will incur during building or operating the projects, which they will include assumptions about interest rate costs and so on. So that will be reflective on the price that they bid for. Maybe the project owner, theoretically, when interest rate is much higher than the expected offtake sale or offtake lease theoretically would have been higher than if the interest rate was very low and expected to be lower naturally.

But it does not jeopardise the projects to be deployed and I think the country's focus on the long-term strategy. It's called 2030. There's so many initiatives to be delivered and the progress of these projects are happening significantly now. The other question was about the potential delay. So we covered that. What was the other one? Did I cover your questions or is something that I missed?

Speaker: Yeah, just on the cost of funding. Since you're like [inaudible] 30 to 40 bips almost NIM improvement. So part of it is coming from the back end. But again, I would assume that you'd only assume the 30 to 40 bips if there's actually savings in the liability side. In other words, increasing your cost of percentage.

Abdullah AlKhalifa: No, look, I think when I talked about the NIMs or Adel talked about NIMs, we're saying that our cost of funding, we're expected to go higher next year, but not significantly because of the rate change because most of the liability already replaced close to the current market rates. Assets otherwise, on the other hand, would reprice, especially the six months LIBOR loans, one-year LIBOR loans that will come for a significant shift in terms of pricing. My ability of deposits will have a volume impact because the growth in loans will require us to grow or take more time deposits. There'll be a volume impact but not significant rate impact. That's what I'm saying. While it's going to be very significant for the corporates, the rate impact on the asset side.

Speaker: Fair enough. Just one last part. And don't you probably think or did you actually guys charge the clients a discount from the cyber plus the fixed portion, or are you going to pass it all through to the clients? Because I've known some banks they do some cuts on the rates, which is very high. And that's how they get to keep their clients or even increase the market share. So do you expect to have all of these rates pass through to the clients or not? Thank you.

Abdullah AlKhalifa: Of course, we're not in the business of lending below our costs. If you talk about retail mortgage, for example, there's a maximum pricing by administrative housing if you're qualified for subsidies. So these are applicable all the time. We don't go significantly below those pricing. If the customer is not beneficiary for any subsidies and there's no limit on pricing, then you have to compete to the market. But I honestly don't want to continue on explaining because I'm not very clear about your question.

Speaker: It's fine. I can send you guys an email and then probably you can take it offline. Thank you very much.

Abdullah AlKhalifa: Thank you.

Operator: We'll go next to Adnan Farooq with Jadwa investment.

Adnan Farooq: As-Salaam-Alaikum. Thank you for the presentation and congratulations on the numbers. I have a couple of questions. One is on the deposit mix. You mentioned that you expect cost of funding to go up because of the volume impact. I just wanted to take your opinion on where do you think the CASA mix will settle for you and for the sector because we are seeing acceleration in the shift when the rates started going up. Do you think most of the impact has happened? How much more do you think will move? That's the first question.

And the second is on asset quality. You explained the asset quality very well on the corporate side, but we see a pickup in retail NPLs as well. Is there anything alarming or is it just that because your book has grown fast, these are stage one or basic provisions that you have taken? Just wanted to confirm.

Abdullah AlKhalifa: Thanks for the questions. Now CASA to be honest, I know we've been transparent and want to measure the expectation in the market. As we said at the end of the first half last year, we said, guys, we expect loan growth to continue, which means with interest rates, you also see a shift from current to time that the market phenomena that we see here. Don't expect CASA as a percentage to increase or even to maintain the levels that we had before and we've seen it. For next year, we're expecting further dilution on shares of CASA.

We continue to obviously try our best to grow CASA through all the initiatives we're doing whether it's cash, whether it's SME, whether it's new customers for mid-corporates, whether it's the customer acquisition within retail and so on. So all of this will continue to push for higher growth in CASA. But reality is the growth in loans, which we gave guidance in our mid-teens certainly will be funded. A lot of that will be funded by expensive deposits. So as a percentage, CASA is expected to dilute further.

Your other questions about the migration you've seen in retail, not just corporate or foreign bills because [inaudible] explain the cases. I think in retail we started last year and we launched non-salary assigned loans. As you know, these non-salary assigned loans tend to be obviously higher risk but the same price, same time, your pricing reflective of those risk and more. We had some migration into stage three. We're very focused now on the process in place to ensure collection remind the customers because not automated deduction from the salaries, non-salary assigned.

So the customer has to take action to pay the monthly installment. And I think we're getting this under control. We're obviously learning from this experience to improve our credit scorecard, and that will help because that's really going to be – I don't know how many years it will take, but that will be the future of retail i.e., non-salary assignment I would expect in the long term. At the moment this is the reason. Otherwise, the salary assigned in terms of risk is very, very low default rate, extremely low default rates. And this is not just Alinma, that's all industry.

Adnan Farooq: Thank you. That's very helpful. Just one follow-up on this. What's the credit spread between salary-assigned and non-salary assigned loans? If you can give a ballpark number, that would be helpful.

Abdullah AlKhalifa: You're asking for pricing basis. Look, we price different segments for non-salary assigned differently, right?

Adel Abalkhail: Yeah, it is different. We have different substrates. This depends on the employer and your salary income. But there is significant differences between salary and unassigned in terms of the pricing.

Adnan Farooq: Thank you.

Waleed Mohsin: Perfect. With that, given that we're running out of time, I would like to thank Alinma Bank management for their time and to everyone for participating in this call. Thank you much. That ends today's call. Have a good evening, everyone.

Abdullah AlKhalifa: Thank you, all.

Operator: This does conclude today's conference. We thank you for your participation.