NLB Group

Third Quarter 2023 Financial Results Conference Call

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Conductors:

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Conference Call Conducted by Chorus Call Hellas

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OPERATOR: Ladies and Gentlemen, thank you for standing by. I am Konstantinos, your Chorus Call operator. Welcome and thank you for joining the NLB Group conference call and live Webcast to present and discuss the Third Quarter 2023 Financial Results.

At this time, I would like to turn the conference over to Mr Blaž Brodnjak, CEO, Mr Andreas Burkhardt, CRO, and Mr Archibald Kremser, CFO.

Mr Brodnjak, you may now proceed.

BRODNJAK B.: A warm welcome. Good afternoon, everyone, to the regular quarterly webcast. Let me draw your attention to the regular disclaimer. And as usual, I will start with a short introduction of general developments. We are looking back to another very, very strong quarter. Very solid recurring performance, both in terms of revenues, continued cost discipline, and especially in terms of asset quality, we have not seen any deterioration, any meaningful deterioration, despite pretty high uncertainty in the international environment, of course, and the outbreaks of last security crises, as well. So, so far, so good, I would say, for our region.

We are specifically happy and this time around, I'm actually reporting in from Belgrade about the results in Serbia. This evening, there is going to be a special occasion, and that's why I'm also here, because we are opening officially, with the partners, one of the largest congress centres in Europe, and one of the biggest ones, actually, around a 1,000 km circle, that is going to position Belgrade again among the top congress locations in the world even, ahead of the 2027 Expo that is coming. So, in this respect, a very solid development of the town, of the city, of the country, and of our business, as well. So, Serbia, this year, is already contributing in the first three months,

NLB Komercijalna banka, close to €150 million, which was, on an annual basis, was not expected before 2025, which is, of course, something that we like a lot. And it's just reaffirming how good a decision this has been throughout these last years. We have seen, as we have been guiding for, let's say a mid-single digit growth in terms of loans. A very good evolution, especially given the fact that this is happening, of course, now at rates that are a bit more attractive. We have seen no deterioration in deposit portfolios, in terms of outflows. We have, indeed, actually reacted, finally in September, with a bit of an uptick in Slovenia, and that was, of course, as a euro country, is still lagging behind, in terms of term deposit pricing.

So, we have started paying up to 2.5%, and there has been a gradual shift towards term deposits, but all within what has been expected. And this all is guiding towards a direction that where we are raising questions to ourselves, and of course, legitimately and logically, also, coming from your end, have we seen the peak of the interest margins? The ECB seems to have paused, at least, if not stopped, when it comes to the hikes.

And now the real question is what the further margin evolution will be, and what the further base rates of the ECB are going to be. And by that, determine the total margin, in terms of interest and operational for the NLB group. So far, it has still been opening, so this is very positively contributing to the results, strengthening further our capital position.

We are sitting on a very strong base, and we are further strengthening it. And the region has been growing ahead of what has been the European Union average, and these expectations remain the same for the upcoming periods. I'm specifically happy and proud of the completion of the integration that we announced of two banks in Slovenia, so NLB d.d. and N Banka, a successful former Sberbank in Slovenia. It was a smooth and flawless process, regular challenges at the end with clients, but in principle, nothing that is causing too high of an inconvenience or would cause any instability. So, we're really happy about the outcome. We are now two months almost, already a full two and a half months after the go live, and everything works fine.

And we are resuming now to development mode, accelerated development mode, focusing on processes, and focusing, obviously, also on the main priorities, when it comes to client experience and so on. There has also been very good news also in terms of the dividend payout. As we have been announcing, the second tranche of this year's dividend is coming in

December. We are suggesting it to the General Assembly to be held in December. And by that, continuing on further promise, and second, on the trajectory of holding two AGMs a year, which we believe is worthwhile and valuable, in terms of being able to discuss strategic matters with our shareholder base.

We will, and I will be talking about that in the outlook, be thinking of what the dimensions will be of these dividend flows in the future, but so far, it is solid, it is within what we have been announcing, and indeed, within a very strong performance, something that, in relative terms, has been less ambitious, in terms of relative payouts, but still high in absolute payouts. There have been some challenges that are besides the unexpected or difficult to assess further decisions of the ECB impacting potential profitability. There have been some regulatory potential changes. We have no clarity yet what will be happening with the obligatory results.

With the ECB, there have been some changes in various geographies. Here, in our region, there have been some announcements of taxation, specifically in Slovenia, a balance sheet tax, which you will have been able to see for sure. There has been a public discussion, and it might come into place in 2024. There have been some pricing constraints and regulations with caps and so on, but some others have expired. So, there are some uncertainties, some questions around what would be actually the bottom-line capacity for the upcoming years. But we stay very firm and confident with our guidance. And I will touch on that later on.

Cost of risk is totally under control, and Andreas will be talking about the evolution. So, despite volatility in the international environment, our performance of our books is extremely solid. With that, I will pass over to Archibald to guide you in a more detail in financial terms, and Andreas will add the asset quality main points, and I will come back with the outlook. Thank you.

KREMSER A.: Thanks, Blaž. I'll step you fairly quickly through the quarter, which, as Blaž indicated, was fairly regular, actually, with still rising rate revenues from the latest ECB activities, and fairly normal cost of risk, still muted development on the back of the stable cost base. So, overall, a very solid, regular quarter. The macro backdrop is what appears, for our region, to come down to, more or less, lending. Of course, the jury is still out, and we all follow the news in various macro environments that are relevant for us. Specifically, of course, the neighbouring countries, including Germany, Italy, etc. But so far, this region has shown, and continues to show, resilience and optimism, translating into above Eurozone average growth rates.

Inflation is still a little bit higher, contributing to a bit of cost pressure on our side, obviously, especially on the labour cost side. We have to simply adjust to realities. But we'll come to that on the cost equation. Other than that, the macro environment is still supportive to growth, which is what matters most. So, we see real growth, obviously, supporting then loan growth. And we have heard about healthy loan growth dynamics year-to-date. Actually, totally in line to what we have been indicating. So, we see a single digit figure for this year. And of course, the P&L is also extremely robust in Q3, on the back of factors I mentioned. And you've noticed that net interest income is still moving in line with the rate environment.

Of course, there will be a kind of a softening of that trend, absolutely, because of our repricing of deposits. In the meantime, in Slovenia, half of our deposits are sitting in value added products, such as savings accounts and term deposits, so this will show through. And then we are also actively considering to hedge our variable position, to some extent, in the coming months. So, in terms of NIM margin, I haven't yet factored it into the wholesale funding equation that will also kick in next year. We have probably seen, or will see in Q4, something like a peak. Nevertheless, Q3 was strong, and the 144 bottom line is just exceptional, and continues to be exceptional. And we are pretty much, I would say, sailing in s sweet spot environment, from a bank's profitability point of view.

We can see the NIM still expanding, also still on a quarterly basis, and of course, as I said, contributed to this quarter, in particular to simply ECB and Euribor movements. Our variable position is unchanged in the ballpark of combined loans and cash, something in the range of €10 billion. So, this is a pretty straightforward translation to the NIM result and the margin. And in that sense, on the non-interest income side, we are mute. To some extent, we really try to urge and support our customers by not unnecessarily adding to fee and charge pressures. So, in that sense, we have been shown, also responsibly towards our customers. But of course, given the environment overall, that is no dilemma whatsoever.

On the cost side, you see the dynamic I mentioned before. So, year-on-year, this is a fairly visible cost dynamic. We are working on the cost equation, as you see, in two markets, as we speak. Slovenia and Serbia, in particular. Other markets are increasingly, let’s say, feeling comparable pressures. But in those markets, which are materially most important for us, we work fairly actively, and have, in the past, been very, very actively consolidating, let's say, cost base and position or so. We will, and continue to invest. We have just had a very good and productive discussion with the Board, and we will continue to invest in the advancing of the technology agenda, which is, of course, key for our long-term sustainable business.

On the loan dynamics, actually, it's really a sweet spot. It's pretty much in line with what we have indicated. A very strong performance in Slovenia, and in our subsidiary market. Nevertheless, the pressures from the rate environment, there is still a healthy demand for both consumer and housing products. And also, a healthy and a bit muted demand for corporate. And this is all fully in line with our risk appetite, considering the situation we are in, and also, making sure asset quality remains at highest levels.

In that sense, capital, of course, as a function of all of that, very, very robust dynamics. We have a bit of up and down on the OCI side from positive valuations coming back, obviously, as our fair value position is running off. And a little bit of reverse on the special treatment of the very same position. But overall, a very robust 350 bps, as you see passes on to our OCR P2G requirement, and in that sense, plenty of room for growth, both organic and non-organic. The funding equation, you can see here the list of instruments outstanding. In the meantime, quite an impressive amount for our bank, at least, 1.4 billion across the range of all instruments.

And indeed, you will see us in the market next year again in both the senior, and presumably, also the tier two space. So, that is becoming now a more frequent exercise. And accordingly, we put a lot of effort and emphasis in the IR dimension on continuously working on the investor base, expanding it, tapping into new potential. And I have to say the experience, from the senior preferred benchmark issuance, was very encouraging already, with, as you remember, four times oversubscribed issuance.

The funding costs, I mentioned. We have now considerable parts of this Slovenian deposit base. You can see it in the middle pie chart, it says 46% in value added products, which is good. Good for customers. And having done a fair share of the rate returns, you can see that almost 50% sits in savings in term deposits. On terms, as mentioned, we paid 2.5%. Not to forget, we also offer very attractive investment opportunities, where we combine cash and funds, making it up to 4%, or even more, on the cash side, if you combine it with a saving in a mutual fund product. So, in that sense, we really, I think, have now a complete range of retail offerings. And of course, we'll continue to think about possible further extensions.

That moderately, but still visibly, raises funding costs on the deposit side. And in that sense, as indicated, margins, at some point, will peak, but the outlook, as Blaž will tell you, remains very, very robust. With that, I will pass on to Andreas on asset quality.

BURKHARDT A.: Archibald, thank you very much. The distribution between the pockets you're already used to, we are actually growing in all segments now in the last period, with one exception in corporate, but that's not due to less new business, that's due to a lot of repayments in different sectors. And from the distribution by geographies, obviously, very stable. Overall, you see the subsidiary banks are growing a little bit faster than we do, and that's why you see, for the first time, 51%

of the majority of our portfolio actually outside Slovenia, and 49% here, in Slovenia.

As I have mentioned already, in the last period, we saw quite some repayments on corporates. That is still energy, for example, also in the real estate, it's finished projects and so on. So, in a sense, let's say more one-time effects, so the strength of the portfolio growth is also intact in corporate, overall. And what you see in corporate, and what you saw in the last quarters, there's not too much of a change. Instead, it's a well-diversified portfolio, and honestly speaking, what is amazing is that in times, which are not necessarily the easiest ones, is that this portfolio really, also on the corporate side here, is very, very robust, and actually, no bad surprises whatsoever.

Staging, also a very, very stable situation. What you see is, again, a little bit of an uptick in stage two. Basically, none in stage three, but a little bit, again, in stage two in retail. Retail, of course, in this environment in which we are, not everybody necessarily gets a salary increase in line with inflation, and then of course, there's pressure on the retail loans. On the other side, by the way, who gets these salary increases in line with inflation, this is reducing the effective value of the loans. So, that then, rather helps, so we see two effects. But you have, here, in retail, the lower end, which you now see in staging.

NPLs, almost a little bit amazing at one point of time. So, the NPL percentage is still reducing. And as you are used to from us, coverage is very, very solid. A good part of the NPL portfolio is even without delays. Also, this is a story that you know from the past. So, cases, which are still not fully through the restructuring cycle, and still flagged NPL, but which are basically paying fully on time. And distribution between the geographies, in the meanwhile, is also very, very much in line with expectation, or in line with the shares these geographies have also in our total portfolio.

Impairments and provisions, so far in the three quarters, we actually see quite a solid release. What you actually see is a zero from the regular portfolio development, and honestly speaking here, retail, we see inflows of provisions, and corporates, we still see outflows. As I told you, the corporate portfolio is behaving still brilliantly, and retail, we see a very expected trend, and actually, to a more moderate extent than we were actually assuming a while ago. So, overall, you see a release, but also, that is still strongly driven, again, strongly driven also by repayments from off balance sheet items. So, our off-balance book, which is still approximately a billion, still has, here or there, some juice, which we are extracting as well as we can.

The trend in variable versus fixed, you'll see that in retail, we are still moving a little bit towards fixed interest rates. And on the other side, corporate is slowly turning. So, that's the trend slowly going in the other direction. And what you see on the development of Euribor, actually, the Euribor in the house, of course, logically, because it's a one-, three-, or six-month frequency, it's running a little bit after. But what you can see here is that we still have a little bit of a buffer to current Euribors, so there's a little bit more juice to come. Of course, if you compare with earlier this year, a good part of the juice is now already in. And, of course, you see this in the profitability of the bank, but there's still a little more to come.

Overall, given the very solid development in the NPLs and in provisioning, we, again, also uplifted a little bit our view on provisioning overall for the entire year, as you're used to. Quarter Four is usually a little bit more provisioning heavy, but again, very, very moderate, but more details from Blaž. And with this, I'm also now handing back to Blaž. Thank you.

BRODNJAK B.: Thank you Andreas. The outlook, of you can flip the slide, please, this year, obviously, is going to be an enormous performance historically looked at, as well. So, this is really ROEs normalised exceeding 20% on one side, on the other side, also showing very, very strong performance from the cost of risk and growth of revenues, obviously, above what was expected, even a month ago still. And finally, also efficiency measures, in terms of process improvements, on one side, further continuous focus on costs. But at the end, also now a much-improved interest environment.

We have delivered now the cost income ratios of well below 50%, which was one of the most challenged questions in previous years. And despite all of the uncertainties regarding the rate environment, regarding eventual regulatory or sovereign charges coming, regarding the eventual shift of portfolios to term deposits, and so on, we still anticipate that we will maintain this level of performance also throughout the upcoming midterm period. We are still talking about normal stories of 20%. We are talking about cost income ratios below 50%. We are talking about profits, here we say, exceeding 400 million.

We are pretty confident about these numbers. And in this respect, obviously, this is something that we can be very positive about. There has been a cost tension, so this is evident. We are now slightly revising the outlook for this year, and slightly revising the outlook for cost for the midterm. Since we have been consciously assessing the situation as the right moment to invest into a further push for digitisation on one side. And on the other side, we have still been living in an environment with significant wage inflation, and still significant higher levels of inflation, frankly, than in the core of the European Union as of today.

So, this is still causing significant pressure, but as said, we have always been reacting by optimising the processes, or adjusting the channels, also the physical footprint and so on. The real question, of course, with such results is, what's happening with the dividend? So, we still here show the old cumulative 500 million payout promise, which means that of course, in the upcoming two years, there will be a meaningfully increasing dividend every year. On the other hand, clearly, if you're delivering half a billion almost of profits, it’s paying out 110, and then slightly growing the dividends enough in the eyes of the investors. And it is a legitimate and valid question.

We have announced, and now we can formally also confirm that as of December, we will officially kick off the strategizing process, within which, we will really try to understand the revenue pools for organic and, or M&A evolution in the upcoming midterm period. The result of which will have to be communicated at the investor day, and will be communicated, obviously, at the upcoming investor in Ljubljana on 9th May next year. And depending on the outcome of this process, we will then also be potentially addressing the shareholder base with a set of the planned activities to actually accrete value through growth, and, or potential revised dividend assumptions in this respect.

So, for this General Assembly in December, obviously, we're following the flow of what's been discussed so far and disclosed so far. The upcoming regular General Assembly in June next year will already be a result of a completed strategizing process, and defined ambition levels, also in terms of capital consumption. So, which opportunities we'll look at actively, and with a certain level of predictability when it comes to actionability, and you know what portions of capital could be allocated for these accretive opportunities, and what could actually be distributed in which form to the shareholder base.

So, the news is good. We will not be paying less, we will eventually be paying more, but it depends on whether we will be able to find really meaningful value accretive alternative deployments of capital. We hope that we have, and we believe that this has been the case, that in the last three to five years, we have gained your trust, that we have been able to transact, in terms of M&A. That we have been able to meaningfully not only acquire, but also integrate. And we might be, as we speak, already amidst some of the potential and additional news that might come. I can't disclose more than what has been publicly disclosed by now, which means that we have been working on productive engagement of capital, serving and delivering your shareholder value.

We also have been suggesting to the AGM collectively with our supervisory board at the governing body, an upgrade and enhancement of the remuneration policy, which is also going in this direction, actually benchmarking our performance with the relevant peers, in terms of total shareholder return, and also, ESG related targets and so on. So, we believe this is all serving, actually, the interest of our key stakeholders, and by that, showing these numbers, and with more information to come, immediately after we complete the strategizing process, towards 9th May, we will keep delivering the good news.

That is all from our side, and we are open for any questions or comments you might have, and then I will wrap up at the end. Thank you.

Q&A

OPERATOR: The first question comes from the line of Goodacre, Sam, with JP Morgan. Please go ahead.

GOODACRE S: Good afternoon, Blaž, Andreas, and Archibald, thanks very much for the call. My first question is about your midterm cost guidance. You're obviously increasing that to 530 million from flattish on this year level. Could you give us a bit of colour, is that largely inflationary? Or are there any projects that you have line of sight on that you know are going to be costing money in the midterm? Thank you.

BRODNJAK B.: It is, actually, partly coming from the wage inflation environment. We have seen announcements in a couple of countries of, for example, increased minimum wage as a simple legal framework. On the other hand, we've been really trying to accelerate the digitisation agenda, which means that we want to accelerate some of the developments, for example, delivering new workflow tools and CRM tools across the board, improving client experience of our M&A, in order to be able to migrate more decisively from traditional format.

And this is, indeed, perceived now as a significant hike in cost, but if you look combined, it's actually not that high, that we have so far. So, we're actually investing in people and systems. We are bringing on additional stuff, especially for data stream, especially, obviously, for development of platforms, as well. And we are also beefing up a bit M&A a capacity, frankly, and this all costs a bit of money. We can't be concrete on what M&A we are talking about, but we have been actually engaged, and it is difficult to, in parallel, deliver integration, and work on M&A. So, we are, on one side, a holding company, but at the same time, we are the largest operating bank in the country.

And in this respect, across the board, we are investing in cybersecurity, we are investing, obviously, as I said, in the upgrade of platforms, and we are investing, above all, in people. And part of it is simply unavoidable, because of legal changes, significant increases in minimum wages, for example, upcoming in Serbia and some other countries, which automatically bring such expectations across the board. We still stay, of course, fully committed to the efficiency agenda. And there are there are plans, of course, for further reductions of traditional format. But this couple of years coming is somehow really transitionary, in the sense that now we really need to invest a bit more. And if we benchmark our investment in IT, generally with peers, we are not overspending at all. But Archibald will add some tones to it, some flesh to it.

KREMSER A.: Not really much to add, other than we are very, very cost conscious. On the other side, we have to accommodate, to some extent to reality. I should also admit that in Serbia, we are not as fast as we wanted to be, in terms of reaping synergies. So, that is a year, if you want, time lag on that agenda. But the agenda remains unchanged, and broadly speaking, the whole digitisation agenda is, ultimately, the trade-off of, I call it intangible assets, in other words, IP, technology spend, and of course, mostly human capital and talents versus physical footprint, efficiencies in not necessarily reducing branches, but the way we operate them, the way we use them more for sales and advisory, rather than operating very high fixed cost cash handling operations.

So, this transition is simply a midterm effort, and it requires, predominantly, this pre-investment, upfront investment, in tech and talents. So, we believe the future is in tech powered finance. This is premium element of the advisory capacity in locations that are reachable to our customers, and we invest in this transition. But we do this very, very cost consciously. I am CFO, and also oversee the IT business, so believe me, that this is done in a very diligent and thorough way.

GOODACRE S: Thank you very much. And perhaps the next question is more one for Andreas on the risk outlook. Andreas, when you think about the migration of certain retail portfolios or files to stage two, what is your view that they do deteriorate further? And so, in the next 12 months, we could, indeed, see an increase in your NPL ratio? And what extent of cost of risk burden might that mean?

BURKHARDT A.: The situation in retail, if you see the overall figures, what is migrating to stage two, if you see it on the bank level, it is still minimal. And we might see some of these cases to migrate to NPL, and they will. On the other side, we are still very, very successfully working on the NPLs, so you have the effect on two sides. I would expect next year, for sure, a little bit of a further trend in this direction, which actually, we have already seen since a year. On the other side, on the corporate side, we don't really see any clouds in the sky, which is impressive enough in these circumstances.

But if you ask me, this is also depending a little bit, especially here, in Slovenia, on how the companies are positioning themselves. Some of them are actually rather underleveraged than overleveraged, which in a different economic environment, might be a disadvantage, but now it's an advantage. So, overall, because you have cost of risk, at the end of the day, I would expect that slowly, we are migrating to what we're expecting midterm, so 30 to 50 bps is midterm.

I would see us, next year, still below that, but probably not anymore at zero.

GOODACRE S: Thanks, Andreas. And where you are seeing small bits of pressure within retail, is that in any particular market? So, are there jurisdictions where the pressure on the consumer is slightly more intense than elsewhere?

BURKHARDT A: No. Actually, if you look at the three months buckets, you'll see, here and there, a little more or a little less. One of our banks, which is filling the space very well is our bank in Skopje. Of course, then you, now and then, also see a little bit more migration here. Filling the space good means they really do the business they should. We are sometimes, as a Group, still a little bit too conservative, which triggers a very low cost of risk, but which leaves a little bit of money on the street. So, that's one geography, which I saw. But if you ask me, that's not a trend, that's just a short-term item.

And then the big geographies are always, of course, more the attention, Slovenia and Serbia, but also here, very, very controlled, very moderate. So, overall, if you ask me, I don't see strategically here now any big outliers. Luckily, I have to say, the very strong tendency here, in these markets, is people, private individuals, want to repay their loans. We're supporting that a lot, of course, also on the restructuring side, in case of need. But that is also a little bit a question of the culture on retail, and here, we are in the very lucky situation that actually, this is maybe a little bit counter intuitive, if you look at salaries in some geographies, but that's actually rather a strength in this region, that people here are really committed to repaying their loans.

And I don't see any strong trends. What we see a little bit is, of course, the lower end salaries, where we are, anyhow, under average exposed for many reasons. Of course, we see a few more cases incoming, but that's from the portfolio, then then the smallest part, both in volumes per case and in overall volume.

GOODACRE S: Okay, that's very clear, thank you. And perhaps my last one, back to you, Blaž. I appreciate you said that you can't be too specific on M&A, but obviously, over the course of this year, you have increased your targeted RWA absorption from €2.5 billion to €4 billion. You've done a couple of larger acquisitions, but you have also spoken in the past about smaller bolt-on type deals. So, how should we think about the use of €4 billion total between a larger transaction and several smaller?

BRODNJAK B: There might be, of course, various things happening. There might be a leasing deal, potentially in the market in Slovenia, potentially, there might be something smaller of these deals in Croatia. There might be, of course, other deals, potentially happening. Nothing is necessarily happening as of today but might become actionable. We will really know in a structured way, together with our supervisory board, so the entire governing body, go through our strategic aspirations, and define, really, the target revenue pools, and then really try to figure out what would be the most meaningful allocation of capital, and to apply it as per these potential opportunities.

So, in case that until the end of April, middle of May, when we communicate our new strategy on 9th May, we didn't have anything meaningful on the horizon, in terms of really concrete, sizable acquisitions, this might, I'd say might, well lead to a conclusion that we significantly size up the dividend. We might think of share buybacks, but that's all hypothetical, because this all has to enter now the pipeline of discussions with our board. The capital absorption is very high. The total capital adequacy is very high.

The organic growth does not show such a potential to be able to consume this €4 billion plus of risk weighted assets, so in this respect, if there is no really meaningful further acquisition, the potential, in terms of really actionable assets in the upcoming, let's say, 12 months or 18 months, then this might well rather mean we really revise the dividend payouts. But it's a bit too early, so we kindly ask you for a bit of patience, patience and trust. We will now lock into the room, really look at the alternatives, consider is this region the only region? Is this the only possibility? Banking only, and leasing only, is there something else potentially?

So, we don't yet have an upfront immediate response to what you're asking, but there might be some smaller tactical things in the asset management space, but immaterial for the banking group, as of today, there might be some digital online platforms, immaterial for the business side as of today, nothing really big has been pending, as of right now. But as said until April, May, April at the latest, we should have, pretty much, a clear picture of what, potentially, we can really count on, in terms of capital consumption. And then really, at the convocation of the AGM in June 24, actually discuss this in a very meaningful way with the shareholders.

GOODACRE S: Okay, thank you very much, all, and congratulations on the great result. Cheers.

BRODNJAK B: Thank you, Sam, for everything.

OPERATOR: The next question comes from the line of Nellis, Simon with Citibank. Please go ahead.

NELLIS S: Hi. Thanks for the opportunity. Could you say a few words about the regulatory environment? You've already mentioned this Serbian mortgage rate cap, you've got the Slovenian windfall profit tax, has that actually been formally enacted? And is there anything else that's pending? That will be my main question for you.

BRODNJAK B: Thanks. These two have been the most material. Serbia is actually enacted, so this is in place. There is a ceiling on the housing loans rates. On the other side, there was also a freeze of certain fee evolutions for 12 months, which has expired. So, this is, to a significant extent, somehow also offsetting the effect of the first one. So, Serbia is not that material. It will cause one-off adjustments in our results, but it's not a killer. Slovenia is publicly communicated as a draft version so far, so it is in a debate, in a public discussion. Of course, the Bank Association has a view, ECB has just published a written opinion, a warrant Republic of Slovenia, when it comes to the stability and bank capacity to lend, willingness to lend, and so on. So, let's see how this potentially impacts the discussion.

It is 0.2% of the balance sheet, as per the end of the year, which means if you look at our Q3, you can assume just short of €32 million for 2024. And then depending on the growth rate supply, of course, it would gradually increase. But this is, at the end of the day, not that high, if you look at the total profit, as well, so it is in the range of €30 million plus, which is compared to the effective tax rate that this Group has been paying, also somehow still combined, but also not a killer. There is a cap on it, when it comes to the annual profits. But of course, this charge is well below 30% of now existing NLB’s profits.

We see, as we have discussed so far, here and there, a bit of a minimum reserve somehow, which we see as a hidden attempt to somehow also extract some value from the banking system adjustments. We still see, for example, in some of the markets, very low rates paid by the central banks. Now in the Federation of Bosnia, it was practically almost still zero and so on. But this is all close single digit millions, which is not that material. We haven't seen other really heavy attempts. There are some pre-elections atmosphere here and there. There is, in Slovenia, a bit of a populistic element of the floods. But generally, the banks are willing, and of course, happy to contribute, when it comes to the good of society and benefit for the people from the region.

We just count on that this is, of course, not then being somehow constrained on a specific one-off weather phenomenon, when it comes to taxation of banks, and when it comes to regulatory control over the conditions, terms and conditions of the banking system, as well. It seems that we have seen the peak in terms of interest environment, at least this is perceived by the environment as such, as well, because we already see players, international competitors, moving down by some prices, or at least not increasing anymore for quite some time already.

So, on longer ends, it seems that everyone is expecting a significant reduction of rates. Where this is going to be, of course, no one has a crystal ball. So, I would expect that also by normalisation, gradual normalisation of profit, there will be less pressure. But indeed, we are still talking about 20% ROE normalised, and we operate with the assumption that this would be the case, despite all of these happenings.

NELLIS S: Thanks. And just on the margin front, if your rates stay where they are for the next two to three quarters, where do you think your margin will go? Is there still further upside going forward? Or are we at peak margin now? Where do you think it would peek under that scenario?

BRODNJAK B: Well, if you apply the assumption that they will not move for two to three quarters, then it's a bit of an easier calculation and you can do your math. It is then depending on to what extent we might move some of our deposits to the term deposit bucket, which is paying up to 2.5% in Slovenia. In other markets, actually, we have already been, more or less, adjusting these levels before. There has been some competition for deposits in specific currencies already before, so we won’t see there such a movement. And then it all depends on where would you see the yields of the instruments in the market, as well.

So, at the end, of course, we will also be issuing, as Archibald mentioned, further senior bonds and subordinated bonds in significant amounts, which will also slightly impact that, as well. So, overall, I believe we can be talking about that we have been around peaking, very likely. Where this moment is exactly happening, it is very difficult to say. And then maybe a gradual reduction, if the rates keep stable, then, for two to three periods. But I can't be specific more than that. Archibald, you might add something here.

KREMSER A: Nothing to add really. You might see that jump a bit in Q4, given behavioural dynamics, etc. But then the latest is funding steps, and as I said, we will, at some point, also consider hedging, to some extent. So, in other words, swapping short term result against stabilised midterm results. So, all of that will eat into margin a little bit. But everything north of 3% is very, very good and supportive to the case we are presenting here.

NELLIS S: Understood. Thanks so much.

OPERATOR: The next question comes from line of Ghadia, Ronak, with EFSG Hermes. Please go ahead.

GHADIA R: Good afternoon. Just a couple of questions on the guidance that you've provided. I was wondering if it's being a bit too conservative, because for example, if I look at the regular income guidance above €1 billion, it seems pretty conservative, given that you are already, I think, at around 820, or so, by the 3Q, or 840 by 3Q. So, I'm just wondering if Management are being conservative there. And likewise, I'm trying to understand the guidance around Serbia contribution of more than €100 million by 2025.

Again, if you can just clarify what that is referring to. Because if I look at the financials provided by the bank, it seems like Serbia was already contributing more than €100 million of profits by Nine Months 23. So, again, is that just being conservative, or am I looking at the wrong figure here? Thank you.

BRODNJAK B: Ronak, maybe starting with Serbia. That's why we are removing from the midterm guidance, because originally, it was in, as you know, it would be a success story, if we delivered €100 million in 2025. But since we have been delivering more than €100 million already in Q3 of 2023, we can just establish this was a marvellous transaction. And by that, we stopped actually specifically highlighting it. We will obviously deliver more than €100 million this year already, so this is, for us, no topic anymore. When it comes to the general guidance on revenue, indeed, it can be perceived as conservative. We have continuously been a bit conservative, when guiding.

We have mentioned, on various occasions, that we were rather positively surprised on this point. And this is simply an attribute of ours. Could we be a bit less? This is something that we can also discuss, of course, with our Board within the strategizing process. We believe that we are showing here a very ambitious picture. But I would add an attribute of confidence, so we are confident that we will deliver this.

GHADIA R: Understood. And then just a final, or maybe a follow-up on Simon's question. On the windfall tax, as you mentioned, the draft has been submitted, the timing remains uncertain. But if it is approved this year, then should we see some of that being booked in the current financial year, or the €30 million or so will start coming through from next year?

KREMSER A: The way we understand it, as it's not enacted, it will be affecting the financial 24 onwards.

GHADIA R: Thank you.

OPERATOR: Ladies and gentlemen, we will now move on to our webcast questions. The first webcast question comes from Jovan with Raiffeisen, and I quote, do you plan, and if yes, when, to skip guiding nominal dividends, and instead, to align your dividend outlook with earnings development?

BRODNJAK B: This is what I said before, we are really now taking a bit of time off to sit with the Board, and understand what is actually in front of us, potentially, in terms of meaningful acquisition targets. If we didn't find anything, we might well return to something that was originally used by us, and was basically a dividend payout ratio. So, in this respect, it is unclear yet. What we can say from today's perspective is there will be significantly growing dividend flow, and there is only an upside potential, in principle, if we didn't find appropriate targets to consume capital productively.

And you know what is left, when it comes to what was not paid from the €500 million pot, so you know there are going to be two significant increases of the dividend in the upcoming two years, in any case. And then, of course, given such a capital buffer that we will be holding for eventual acquisitions, this might only improve. We have not yet consciously returned to the dividend payout ratio positioning of our guidance, but it might be the case after we conduct the strategizing process.

OPERATOR: The next webcast question is a follow-up question from Jovan with Raiffeisen, and I quote, excess CET1 to TCR above the minimum is greater than €500 million, even without 2023 earnings. Do you have any concrete plans as regards capital deployment? Some of the peers keep surprising on that front in the third quarter. Thank you.

KREMSER A: No surprise planned, and actually, nothing to add from what Blaž has mentioned. This is the same equation. Ultimately, we are looking at for this year, the dividend equation is concluded. And for subsequent years, we will communicate in May.

OPERATOR: The third webcast question is, again, a follow-up from Jovan, and I quote, as the results of Serbian banks continue soaring, do you see risks of any additional state interventions, apart from interest rate caps, given the relatively tight budget situation and upcoming elections? Congratulations on the good results, and thank you.

BRODNJAK B: Thank you, and I guess you would be a better judge to assess that, frankly. You would know the market even better than us. We don't know, frankly. What has been introduced, has been introduced. The minimum reserve intervention was there, and the interest cap intervention was there. Is there more to come? We, frankly, don't expect it, but I wouldn't call it impossible.

OPERATOR: The next webcast question comes from Anton from Allianz, and I quote, 4% of your total NPLs come from Croatia. This is rather high, considering you do not have a physical presence in Croatia. Kosovo, with its €1.2 billion assets, has 6% share in total NPL. So, how come Croatia has that high of percentage? Thank you.

BRODNJAK B: Well, this is all legacy book. This is a 15 plus year old book, and this is, more or less, a wind down. It is now down to a fraction of what it was, and this just means that we have practically no NPLs in other geographies, because it is such a symbolic Croatian exposure, still has such an important share. It just reaches and speaks about the quality of our books, but Andreas might add something here.

BURKHARDT A: Not much to add to that, but to the Croatian part, that's fully legacy. As you are aware, we are not even able to do new business in Croatia, and we don't. So, there is still new business, so that's fully legacy. And we'll take, from 310 million, which is minimal on our Group level, 4%, well, minimal within that pocket. But that is legacy. And just because you mentioned Kosovo, also that was a good point, Kosovo, honestly, speaking, when I came to this Group, I couldn't believe the figures, because they were already very good at that time, so quite some years ago. And honestly speaking, they are, on the NPL side, just getting better.

So, it's amazing that the market, which from outside, doesn't look exactly easy, has such good NPL figures. But after all of these years being in this Group, I'm very, very confident, and we were checking that that is for real. And it's just really, they are doing wisely here on choosing clients at the right time, a brilliant job. Risk management here also seems to be very much on top of things, which is great. So, yes, Kosovo, from the NPL side, actually, a little bit counterintuitively, but that's our style.

OPERATOR: The next webcast question is a follow-up question from Anton, and I quote, net non-interest income has basically stagnated for some time now. Which opportunities do you see in the future for its growth? Thank you.

BRODNJAK B: Well, it's been stagnating partly also because this year, there are no high balance fees anymore, which were booked here, as well. And there is no Croatian kuna anymore, there was quite some FX coming from Croatia, and so on. So, in principle, there have been some major shifts in this respect. So, if you sterilise for that, you will actually see a pretty solid 4% or 5% growth, which would not be that bad at all. It's also coming mainly from regular traditional revenue streams, when it comes to fee income. We will further focus absolutely on payments. We believe payments, in general, the value proposition to clients, still has a lot of potential to enhance the experience, and potentially, also, the revenue pool.

When it comes to the asset management and insurance business, we are definitely adding the capacity now in Serbia significantly. We have bought, together with Komercijalna banka, also an asset management company, which we will now shift from Komercijalna banka to our NLB funds business, and really put strong focus on developing and replicating, actually, the business model from Slovenia to Serbia, as well. We are a market leader in Slovenia, as you know, with almost 40% market share. And we simply have a very successfully vertically integrated business model in distributing these services, investment funds, and mutual funds, and also, unit linked insurance products.

So, also, insurance as another stream leasing is showing very good trends, especially in Slovenia, of course, but also, especially in Serbia, and we are just starting in Macedonia. So, there are quite some ancillary services that have just begun in specific markets become a real opportunity. And the more the wages grow, the more they will become meaningful value propositions, both for clients and us. And on the other hand, simply with focusing on housing lending, as soon as you will see a more moderate rate environment, it will resume.

With every housing loan, basically, you cross sell five to 5.5 other products, and this is simply boosting your fee income, as well. And you always lock in, of course, the accounts, so the entire family you lock in, also, long term savings schemes, insurance, and so on. So, this is our primary focus, and this is naturally evolving this way. So, in midterm, this 1% here is actually a bit more, if you sterilise for Croatian euro adoption, and as said, the abolishment of the high balance fees, once we exited the negative territory last July. And, of course, this is evident here.

And that was also a cap on fees that was introduced, or the Republic of Serbia a required return to the original position for 12 months, and this also took quite some millions away. So, if you combine all of that, if you sterilise for that, the fee evolution was actually very good.

OPERATOR: The next question comes from a line of Dodig, Mladen with Erste Group Bank. Please go ahead.

DODIG M: Good afternoon, gentlemen. Thank you for the call, and congratulations, of course, on the great results. Just a short one. Could you please remind us of this modification impact in Serbia for the rate cap on mortgage loans? I think you communicated that already earlier, but if you could please remind me.

KREMSER A: You can basically anticipate for Q4 something in the ballpark of €15 million, give or take, in accounting. One, five, for this modification. This, of course, is coming back over time, as we keep accruing these loans.

DODIG M: Of course. Just for the sake of conversation, because Serbia was mentioned in the sense of potential windfall taxes, and right now, the most recent move by the government was decreasing, actually, the GDP, the public debt, sorry, budget deficit from 3.3% to 2.8% for this year. Also, the Serbian government is looking to get an investment grade for credit rating, and then in the whole electoral narrative right now, banks are fortunately not mentioned any more than this rate cap. So, I would say that the budget still is in good shape.

Thank you, once again, and congratulations, once again.

BRODNJAK B: Thank you, Mladen, for giving us confidence. There is no more to come.

OPERATOR: The next question is a webcast question from Anton with Allianz, and I quote, what are your thoughts on the net interest margin in 2024?

KREMSER A: I believe we mostly answered the question. We are very happy with the margin, as it stands, but obviously we expect these margins to compress with all the things we've mentioned already from wholesale funding, depository repricing, hedging, eventually. So, if we stay in the 3% territory, we are more than happy.

OPERATOR: The next webcast question comes from Jovan with Raiffeisen, and I quote, zero risk cost guidance for 23 would imply a very high provisioning level in the fourth quarter. Again, too conservative. Also, 30 to 50 pbs guidance for 2025 looks very conservative. What is the realistic picture for 2024? And the last one is, if you can comment on that, what is the share of legacy corporate loans to exposure, which might be a subject for potential recoveries in the future? Thank you.

BURKHARDT A : So, on 2023 zero cost of risk, yes, that might be a little bit conservative. What you just simply see, in the last quarter, there is usually a little bit more going on that side. And we have indications on some concrete cases, which are, however, not big cases. Overall, it might still be a little bit conservative, I can agree with that. But to say more, or more optimistic than zero cost of risk, for me, given a very vivid environment, is still a little bit too much. Where I agree less is on the 25 outlook, the 30 to 50 bps seems too conservative or conservative. I think we will simply not ever live in dreamland. 30 to 50 bps cost of risk in this region, if you ask me, it's a pretty realistic assumption.

You also have to see that we are still profiting from quite some recoveries, actually, from off balance items, which are also, of course, contributing here. And here, one special effect we saw, because we have approximately a billion off balance, and this portfolio is getting older and older, and more and more squeezed out, so I would expect here, rather, looking forward less and less. On the other side, with the acquisition of Komercijalna Banka, I think the one thing we underestimated a little bit in the due diligence is that the off balance portfolio was actually not intensively worked on for whatever reason. So, here, we have collected already in the past period quite some money back, and by the way, this year, from the 17 million you saw on the slide, a solid portion from that is from Serbia.

So, that this maybe still a little bit more active, but also decreasing. And in the transition, I have said it before, from this year around zero. Maybe if you want to be optimistic, even a little better to this 30 to 50 bps, I would expect us, more or less, here, on a linear transition path. So, I would not expect zero cost of risk next year, but I would not necessarily see us yet on 50 bps. That's my best estimation for now. And I think what I have implicitly answered already a little bit is last question. We still have quite a sizable off-balance book, but this is getting older and older, and off balance, by definition, means that actually, you are not expecting much anymore.

We, honestly speaking, in the last three or four years here, saw one or the other little miracles coming up to cases, where for 25 years, we did not collect a penny. And now suddenly, we collected a few million. But I would not expect too much from that to come anymore. And from the NPL portfolio, on balance, by definition, you cannot expect too much, because simply that portfolio, as you can see here actually in front of you, it's simply not big. I still see something coming back from off balance, and hopefully, also a little bit from this NPL book, but magnitude over a while decrease.

OPERATOR: The next webcast question comes from Hans-Henrik from Coeli, and I quote, given the share price valuation, are buybacks something you consider on top of dividends, most be better investment than any M&A?

BRODNJAK B: That must be a valid alternative. We have, so far, not actually been actively working on it, but within the comprehensive assessment of the deployment of capital, i.e., as a derivative returning value to shareholders, this is not excluded. It is just, of course, a bit more of a complex process, requiring more tedious regulatory approvals, and so on. But I would not eliminate it as an option, and it will be communicated in the package for the upcoming AGM. Archie, will you add anything?

KREMSER A: Nothing, other than we hear, from shareholders, two different versions. One would like it, the other one would like it less, because obviously, the drawback is that you take out liquidity from the stock, and in that sense, it's a two-edged sword. But we understand the question, and I think more materially, we are focused on dividends and capital return. But yes, it's something we also try to understand better in whether there's a merit to it.

OPERATOR: The next webcast question is a follow-up from Hans-Henrik with Coeli, and I quote, you guys are above €400 million in profit. Given that the Nine Months profit is already at €386 million, is it fair to assume profit around, or even above, €500 million euros? Or is there anything in the fourth quarter that would hinder similar profit, as the first quarter to third quarter, so it will be materially lower than the previous quarters? Thank you.

BRODNJAK B: There are two things. One is that we just said that that there would be modification adjustments in Serbia, for example, in the amount of €15 million that you have trendily, a bit more of a cost evolution in the last quarter, which we also showed here with the revised cost guidance. On the other hand, I can just say that exceeding €400 million was meant for 2025, and here, we don't talk about this. In this respect, we can just state that we are confident about the result of 2025. We can't be more specific than that. But it is going to be significantly above Q3.

KREMSER A: There is one thing just to add, in Q4, something we are looking at, customarily, is revaluation of DTA, our deferred tax assets. There is talk, and in the draft, actually, anticipated and envisaged higher corporate income tax, so that might result in a revaluation of the DTA. So, there are a few ups and downs for 23. I think Blaž even mentioned that we will be very close, if not exceeding, to 500, and as said, for 25, nothing to add to what Blaž has said.

OPERATOR: And our last webcast question comes from Cihan from S&P, and I quote, do you have an estimate regarding additional credit losses from the August floods related to damaged properties and more collateral revaluations for full year 2023, or is it an immaterial amount? Thank you.

BURKHARDT A : Thank you for that question. Luckily, the impact on the bank is minimal. We see, in retail currently, 37 moratoriums, so that is, a pretty small amount. We see, overall, on the mortgage side, some €7 million to €8 million of potentially impacted loans in total. But that doesn't mean that the client doesn't pay, or that doesn't mean that we would have to do a write-off for this amount. It's just that these are, of course, all high attention points. But if you see that in total, that's very, very limited. Of course, we had some damage from clients on the corporate side, but luckily, I have to say, primarily, clients, which are very solidly ranked, very good businesses, so they very swiftly overcome it, and we didn't see, basically, any fallout from that. So, overall, impact is very, very limited.

If you ask me, what helps? Here are two things. On the one side, hopefully, what is an impact, or hopefully, for sure, is an impact, as we see it now is that, of course, when establishing mortgages, we also look at whether that would be in a flood area, so we are careful, if it is, and often not giving the loan then. And so, also avoiding the exposure. And the other element, honestly speaking, is a little bit of good luck. So, some of our competitors are considerably more in these areas, which have been flooded, present than we are, so we have an under average presence, and that also contributed to the very, very small impact.

OPERATOR: Ladies and gentlemen, there are no further questions at this time. I will now turn the conference over to Mr Brodnjak for any closing comments. Thank you.

BRODNJAK B: Thank you very much, Jan. As said, despite all the volatilities and uncertainties, we are on very, very good track. We are ahead of an exciting six-month period, within which, we will try to understand the eventual opportunities in front of us, in a way to really productively deploy capital and share success with you. I'm really happy that I can report today from Serbia, because this means we are doing business, we are actually having an event, a really prominent event, the opening of what was once the most prominent congress facility in the broader region, and it's been revived in partnership with the Group and NLB is the financing party.

And it's going to really position Belgrade on the map globally, and Serbia, and also, the region in the map differently. So, next time around, do check out. We are on the path of success, on a journey of success, and we are gladly sharing it with you, and we are really thanking you for your trust on the journey.