GROUPE SOCIETE GENERALE

"BRD Group 9M and Q3 2024 Financial Results Conference Call and Webcast"

Q&A session

Thursday, October 31st 2024, 12:00 RO Time

Participants:

Mrs. Maria ROUSSEVA – CEO

Mrs. Madalina TEODORESCU – Deputy CEO – Retail

Mr. Philippe THIBAUD – Deputy CEO – Risks

Mrs. Simona PRODAN – Finance Executive Director

Operator — Thank you. As a reminder to ask a question, you need to press star one and one on your telephone and wait for your name to be announced. To withdraw your question, please press star one and one again. Once again, please press star one and one on your telephone and wait for your name to be announced. Thank you. We are now going to proceed with our first question.

Participant #1 — Okay, I just wanted to ask you, considering that you said the credit policy and the risk appetite have not changed, is it fair to assume cost of risk in 2025 at roughly the same level as 2024 in relative terms, despite the more dynamic lending activity? Thank you.

Philippe THIBAUD — So we'll come back on 2025 with more precise guidance, but when we look at the macroeconomic, first, 2024 has been challenging, I mean, we started the year, like all the banks, with new challenges, in particular in the retail and consumer finance segment where we had more frauds, so it's kind of operational risk for us, so we had to deal with it. We started also with expectation of growth, which were more optimistic than the ones we have today. So since the growth, so now let's be clear, frauds and these problems that we experienced at the beginning of the year are completely under control, and when we look at the perspective, we have a new look at the macroeconomic evolution in 2025, and still, despite what the disclaimer I'm putting on what I'm going to say, I would expect the cost of risk to increase slightly next year, or I would expect the guidance to increase a bit. Note that, again, we are changing anything to our risk appetite and to our credit policies, but just I expect the macroeconomic context to become a bit bumpy. If it doesn't get more bumpy, then obviously we would remain in the same range.

Participant #2 — Hi, hello, thank you for the presentation. I have several questions. The first one regards the Q3, P&L, other operating expenses. You there booked an income from tangible assets disposed in the quarter. Please let us know what was the value of this amount. The other question regards the Basel IV impact that you previously guided that would stand at 150-200 bps. Please let us know if you revise in some way this guidance, and also let us know if this impact will also impact at its turn the payout ratio, the dividend payout ratio. So, pushing it towards the lower range level, so around 50, so that would be a normal expectation for the payout this year of around 50%. And also your capital adequacy ratio without the regularly temporary treatment stands at 23%. What would be going forward this level, a level that would allow you to be very comfortable or the level that NBR is advising? So we all know that this level is far above the regulatory, the threshold level, but what is the level advised or the level that you target to keep going forward for the next five years? Thank you.

Maria ROUSSEVA Okay, I would say we'll start with your first question, and Simona will explain about the extraordinary income from the sale.

Simona PRODAN Yes, yes indeed, we mentioned this element in the slide on the OPEX because it was a specific one-off, though we intend to continue in the future. We had the sale of some agencies, some branches, particularly in Iasi and Constanta, and also some as we decrease the branches network, we also renegotiate and we do some resiliation of contracts. As such, we have booked from the sale around 25 million RON result.

Going on the Basel IV, though we don't have yet all the implementation done, as you know, the deadline is Q1 2025. We have an estimate now and we know that we'll have a deterioration, let's say, from the operational risk components, as you know, BRD currently is under advanced method and we shall be switching under the Basel IV rules on the standardized method. But on the opposite side, we estimate to benefit from the more favorable treatment of the real estate portfolio. So, all in all, at this moment, we expect a decrease of the ratio, the capital adequacy ratio in between 100 and 150 basis points. And of course, we shall refine further this estimate, but this is on a downward trend. And looking at the capital adequacy and afterwards, Maria will discuss on the payout.

Maria ROUSSEVA But let's talk about the payout. First, now it's well understood that we did not pay dividends as we wished because it was strongly advised by our regulator, as we mentioned in June, and we are mentioning again now and we have to respect it. We would have had the opportunity to do it, having a very comfortable equity situation, especially after the SRT we performed in the first quarter. Regarding the next year expectation, what the regulator will think, we can't know. We can't anticipate. We don't know what exactly will happen geopolitically. And to know that, as Simona said before, since the macro and geopolitical situation is considered still a bit stressed, it's possible that regulators, not only in Romania, but generally, are more prudent. But we don't know. We don't know. We would be targeting the usual distribution, which we have practiced for years, having in mind the impact of the Basel IV starting at the beginning of the year. So, if we have the opportunity, we would be rather going to our standard distribution policy. Again, here we have the impact of what the regulator would think, and we have the precise impact of the Basel IV introduction in the beginning of the year.

Simona PRODAN And maybe returning to your last question because you indeed mentioned the 23% capital adequacy ratio, here maybe to give more, let's say, more information on the minimum regulatory requirements. Because as you have seen in our transparency report, in fact, the overall capital requirement for us is close to 18%. While we consider that such a level, so around, let's say, 22%, is a fair level for a business-as-usual mode when we need to support growing business. And you've seen that we are delivering quite important growth year on year. And in the same time, to have this 300, 400 basis points buffer to cover any potential stresses that we have seen happening frequently over the past three, four years. So I'll say that the level in a very basic case of 22% is not particularly high or exceptionally high in order to allow this two elements.

Participant #2 Thank you for answering my questions. So going forward, this total capital ratio should stay above 22%. This is right?

Simona PRODAN Let's say on the base case, this is the level that we are comfortable with.

Participant #2 Just regarding a little bit the outlook, next year, for example, in terms of lending, you said that next year probably the cost of risk will increase a little bit compared to this year due to the macroeconomic risk and so ever. But in terms of lending, what do you believe? What do you feel? Because my feeling is that, for example, is that the lending activity in terms of growth would be higher than this year. That is accurate, not accurate, but we are resonating on this feeling?

Madalina TEODORESCU

I will take this question. Indeed, there is a lot of unpredictability. And even this year, the market actually exceeded our expectations in terms of forecasting, if I actually look back exactly one year ago. So we were not expecting at that moment this growth. However, for next year, we assume that the market will continue growing much slower than this year growth versus the previous year. So we expect, if I would say, we were budgeting around between 5% to 10% depending on the segment and on different products we actually want to focus on. Again, these are current expectations used for the next year budgeting. However, once we actually are very close to the dynamic of the market and we see that the actuals are different than initial expectation, we adjust properly, focusing on our strategy to continue growing the market share.

So the expectation is still to continue growing above the market. Of course, it was mentioned with a prudent growth in the same risk appetite using omni-channel, using also digital channels or alternative channels, and continue supporting the sustainable financing in all the segments.

Participant #2 Okay, thank you. Now, if I may ask another question. So in the last two or three quarters, I think you surprised me with the evolution of the lending activity. Not much, but you surprised me positively. Usually, before that, you used to surprise me negatively, but this time it's a positive surprise. So let me know, I don't understand what changed. So how come BRD started to outpace the market in terms of lending? What is the main trigger? This I don't understand.

Maria ROUSSEVA I love your question. I think you asked this last time as well, but I'm enjoying answering that question. If you can ask me also next time, it would be great, especially if there are reasons why. No, I will explain you, and this is really serious. Actually, we are very happy that you noticed that we are more active than we were. It is because our bank, in terms of capital, in terms of liquidity, in terms of capacity of our people, in terms of the brand we are having, in terms of the position in general, and because also the market is quite good, there is a place to grow.

We just took advantage of all our strengths. I'm not just answering approximately, this is exactly what happened. We have combined all our strengths into very clear commercial actions, and our teams have been constantly mobilized to deliver good commercial performance. That's what is happening because there is no other reason. You know, we have not changed the risk appetite. It is not because of risk.

We have not performed in a kind of dumping price or being in a price war, so it was not because of the price. We have been just navigating, fortunately, successfully commercially in all segments, in all products, so that our bank is using its capacity to deliver the results. So, that's it.

Participant #2 Okay, thank you. This is the same answer as the last time. Now, regarding the cost-to-income ratio, yes, my estimates are at the individual level, so I see it at 51%. Should I expect this year for the bank to end at this level in terms of cost-to-income ratio, 51% or above 50%?

Maria ROUSSEVA You know that we do not like giving precise figures one quarter before that. Maybe Simona, you would like to say something not that precise, so that we answer?

Simona PRODAN No, but let's say we keep the trend that we have seen so far.

Participant #2 Okay, thank you a lot for answering my question, and congratulations for the results.

Participant #3 Thanks for taking my questions, and congratulations on the strong results. I don't have many questions, but the first one would be on dividends. Do you think that you'll be able to complement this year's distribution to reach the level that you first wanted to distribute in the beginning of the year, but you're not allowed or you were recommended not to distribute that much? So, do you think that you'll be able to?

Maria ROUSSEVA Just wanted to correct you that not allowed is not correct, right? But it's the recommendation, right? Yes. And therefore, we will stick to the recommendation of the regulator.

Participant #3 Okay, understood. The other question that I have, it's about the new budget plan that was recently published by the government. And it's just sort of like your take on what sort of like impacts do you anticipate for the banking sector, mainly in terms of taxation and perhaps also loan book growth, because probably we have a new VAT tax coming, so it's affecting consumption. So, yeah, your view here would be appreciated.

Maria ROUSSEVA Okay, we don't know exactly. Honestly, like let's wait a bit, because we know that there will be intensive work on the fiscal context after the elections. So, I would not like to speculate here. What we have seen is also that apparently the government has negotiated with the European Commission a step-by-step convergence for several years into the desired deficit. So, there is space, I would say. But let us not speculate on that. For the time being, we do not anticipate a particular impact, which we can quantify right now. But of course, since we do not know all elements, we can't precisely answer. But we are comfortable so far.

Participant #3 Okay, understood. That was all from me. Thanks a lot.

Participant #4 Hello. Thank you very much for the presentation and thank you also for taking my question. I understand that you're not ready to talk about next year and specific numbers and budget outlook and so on and so forth. But going into the next quarters, what is your feeling on the net interest margin? Would the NII still be driven by volume growth, or do you see funding costs stabilizing sufficiently that you could see a more positive effect on the top line in the coming quarters and maybe also or in 2025 as a whole? And then also, you talked about the underlying, excluding the turnover tax, underlying positive jaws thus far in 2024. Is that something that you expect also for the coming quarters in 2025? And then lastly, on risk costs, I would just like to have a bit more of a breakdown of the risk costs in Q3 and maybe also the prior quarters.

Where were these risk costs now originating from? Is that Stage 3 inflows? And what was the reason for the NPL ratio increasing specifically in Q3 now? Thank you.

Maria ROUSSEVA Okay, so I will start with the expectations of the next quarter commercial-wise, let's say. So far, we observe a good solid pipeline, meaning that if it is realized, we will have strong commercial next quarters. What we will not do is to enter into a very aggressive price competition, so we will still try to keep our rates at the level which we consider reasonable. But we are optimistic based on this rather good pipeline that we will be maintaining the dynamism also for the next quarter. Related to the margin, because we are adjusting also our deposit rates accordingly, we do not expect further suppression of the margin yet. That's something which we see even now. Then the positive jaws is something which we are planning to keep, right? By the way, we have communicated the cost-income ratio, improving and excluding the revenue tax, but we can tell you that it is impacting us with about three points on the cost-income ratio. So obviously, if there is kind of change in this tax, which we do not anticipated as at now, of course it will going to impact us. We know that as of next year, this tax should not be changed. The year after, the tax should actually be decreased according to what was decided at the moment of its introduction. Now I think we need to talk about the cost of risk, Philippe, and the NPL. Maybe just a second before I pass the floor to Philippe on the impact, since he talked about the fraud. Let me just explain what type of fraud, in order not to have any misunderstanding.

In Romania, and related to all banks in Romania, we have observed a very significant activity of fraudsters organizing social engineering type of activities, impacting clients across the board. This started in the last quarter of previous year and continues, let's say, we see the impact on us until late summer, I would say. All banks, and including us, we have taken important measures to fight it, including now we will continue having campaigns on awareness of the people, because these activities, in fact, people are deciding to do certain things in advance just for themselves, listening or being influenced by fraudsters. So when we are talking about fraud, it's very important that you understand which type of fraud, which in some cases leads to bad loans. And even if these bad loans are not bad, namely the clients continually paying them, we approve them, and we provision them, and we book them as problematic loans. So now I give the floor back to you, Philippe.

Philippe THIBAUD Thank you, Maria, for the opportunity to clarify. When I'm talking about frauds, I'm talking about external frauds. And this is something that we've seen in Europe, and especially in Romania, developing strongly, as Maria indicated. Now, they are not technological frauds. They are really social engineered frauds. Yet, because we work with the digital channels, because we have technology everywhere in our life nowadays, we had to develop tools, we had to develop models to try to control these frauds and reduce their chances in succeeding.

So this is what has been done. Just to be very transparent and very open, because it's not purely for BRD, for all the markets, you should know also as consumers, you should know that people are now hijacking kind of telephone numbers. So you can receive on your mobile phone number, on your mobile, you can receive a call from someone who will have the ID of someone from the police, from National Bank, from anyone. They can fake the ID on the smartphone. And so people, when they pick up the line, they believe they are talking truthfully to the authorities.

And so this is not a technological fraud. It's really social engineering and psychological manipulation. So this has been impacting, indeed, the cost of risk this year more than what we expected originally. But it was well contained and still within the margins that we have in terms of cost of risk.

And it didn't require us to change our credit policy. So the credit policy was unchanged. It's only the tools that we put in place in order to flush these frauds out. And the cost of risk in Q3 was a kind of copy-paste of Q2. When you look at the proportion, so actually it's really in terms of Stage 1, so the Stage 1 increased. I can't give you the number, but it's increased slightly because obviously the portfolio increased.

And we had more Stage 2, obviously, on all markets, on the SME market, on the retail market. When we look at for the corporate, the deterioration of some ratings, it increased the Stage 2. But globally, when we look at the portfolio, we see that on the corporate market, ratings are not deteriorated. Globally, we still have quite a nice improvement of the portfolio. So these clients are staying in Stage 1. They are even improving in Stage 1, but you just need a few clients deteriorating for them to show up in Stage 2. And this is explaining why we have more of these Stage 2, especially on the retail market, where indeed we did have more weakening of the clients. I mean, very small business, especially, which impacted the Stage 2. And on the Stage 3, and I would say on the corporate, the Stage 3 was like in the previous quarter, balanced by the recoveries. So few new defaults and offset by the recoveries. For the retail market, we don't have so many recoveries. So indeed, we had more new defaults, but honestly, they're as much as in Q2. So the structure of the cost of risk is not changing. It's still the same structure of the cost of risk. And, as I said, we do expect to see cost of risk increasing slightly next year, but we'll come back on this.

Participant #4 Super, thank you very much for these answers. Let me just come back on the net interest margin. Would you say that on funding costs, you are past the peak?

Simona PRODAN Yes, so it's true that when you look and I commented on the different evolutions, we've looked on interest income increase, which is correlated with the volumes increase, while indeed on the interest expense, we have a higher pace of, we have still a higher pace of increase, but we observed quarter after quarter that this year on year increase of the interest expense on deposit is reducing. As on one side, the increase of the term deposit, the pace of increase of term deposit is cooling down. And also following the decrease of the market rate, also all the banks and so did BRD started to reprice on a downward, the retail deposit and also the corporate deposit. So indeed we see this pressure reducing. On the NII, we target to maintain let's say, similar growth pace we've seen so far and with positive jaws.

Participant #4 Very good, thank you very much.

Operator There are no further questions, so I'll hand back to you for closing remarks.

Maria ROUSSEVA Okay, thank you everyone for joining us this time again. And thank you for the interesting and very detailed questions. See you in the next quarter. Have a good day.

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