Dukhan Bank – Q3-23 Earnings Call Transcripts

Date: 30 October 2023
Time: 13:30 Doha Time

Executives from Dukhan Bank:

1. Ahmed Hashem - Acting Group Chief Executive Officer
2. Osama Abu Baker - Group Chief Financial Officer
3. Riaz Khan – Head of Reporting & Budgeting and Investor Relations

QNBFS Chairperson:

1- Shahan Keushgerian, Sr. Research Analyst

Operator:	Hello and welcome to the Dukhan Bank Conference Call. I would like to advise all participants that this call is being recorded. Thank you. I'd now like to welcome Shahan Keushgerian to begin the conference. Shahan, over to you.
Shahan Keushgerian [QNBFS]:	Thank you, Gavin. Hi, hello everyone, I want to welcome you to Dukhan Bank's Third Quarter 2023 Financial Results Conference Call. So, on this call from management, we have the Bank's Acting CEO, Ahmed Hashem, Group CFO, Osama Abu Baker, and Riaz Khan, Head of Reporting & Budgeting and Investor Relations. So as usual, we will conduct this call with first, management reviewing the Bank's results, followed by a Q&A session. I will turn the call over now to Ahmed. Please go ahead.
Ahmed Hashem [Dukhan Bank]:	Thank you, Shahan. Good afternoon, everyone, and I appreciate you all joining us today. As usual, I'll begin by briefly discussing the broader economic context before moving into our key accomplishments for the first nine months of 2023. Later on, my team will provide you with updates on the financial performance of the Group, followed by the usual Q&A session. Let's start by addressing the global macroeconomic landscape, which continues to be influenced by geopolitical conflicts, persistent inflation and the resulting monetary policy tightening. These factors have collectively led to a notable slowdown in global economic growth, contributing to financial uncertainty and market volatility. Now, shifting our focus to the domestic markets, after experiencing a somewhat sluggish first two quarters of the year, we are now observing a resurgence in the momentum as we enter the third quarter. All sectors of the economy have exhibited promising growth. Notably, we have witnessed a remarkable 157% surge in visitors, as Qatar welcomed over 2.56 million visitors during first nine months of 2023, surpassing the total arrivals recorded in 2022. This has certainly positively reflected on the local consumption sector.

	Furthermore, tailwinds from planned CAPEX investments under the flagship Northfield Expansion Project coupled with related downstream projects, is also providing a boost to the overall economic growth. Additionally, during the recent government procurement forum, Qatar plans to launch $19bn worth of projects by 2024 to be carried out by Public Works Authority (Ashghal) and Qatar General Electricity and Water Corporation (Kahramaa). All of these investments will combine with ongoing diversification efforts and structural reforms by the State, are expected to further stimulate economic activity and spending across various services and manufacturing sectors, while ensuring alignment with Qatar's 2030 vision, with particular emphasis on healthcare, education, travel and tourism. Now, let's turn our attention to the Group's financial performance for the first nine months of 2023. I'm pleased to report that we have achieved notable success. Our total income has grown by QAR 1.2 billion, reaching QAR 4.4 billion. Consequently, our bottom-line profitability for the first nine months increased by 2.5% from last year and reached QAR 1.1 billion. Our liquidity remained robust and capital adequacy ratio was comfortably higher than the minimal requirement and currently standing at 17.7%. In terms of our operational performance, we have continued our journey to launch modern digital services and products to enable our customers in completing their banking transactions seamlessly, even when they are on the move. Our customer-centric approach, coupled with the strategic incorporation of technological advancements, remains a cornerstone of our growth strategy. Additionally, our commitment to creating value through the integration of ESG initiatives into our strategy positions us for long-term success. Also, I am delighted to announce our remarkable achievement in the capital markets space. Dukhan Bank is now included in all major indices, including the MSCI Emerging Market Index, FTSE mid-cap index, and all the QSE indices. This is a historic achievement for us, especially considering our listing on the Qatar Stock Exchange earlier this February. By ending here, I will let Osama and Riaz to share details on our nine-months performance followed by Q&As.
Osama Abu Baker [Dukhan Bank]:	Thank you, Ahmed, and welcome everyone. As mentioned in our previous calls it has been a challenging year for the banking sector, in particular, but despite that our total income grew by 39% compared to the first nine months of last year, and reached QAR 4.4 billion. This coupled with strong credit recoveries resulted in a growth in net profits of the Group, which increased by 2.5% i.e. from QAR 1.08 billion to QAR 1.12 billion for the first nine months of 2023. Total assets which currently stands at QAR 113 billion, mainly comprises of financing assets – 67% at QAR 76 billion, followed by investments portfolio – 17% at QAR 19 billion.

The balance sheet is mainly funded by customer deposits, about 79% of total liabilities, and amounts to QAR 77 billion, followed by market funding contributing 19% and amounts to QAR 19 billion each.

Regulatory LDR is maintained at 96.5%, being one of the lowest among Qatari banks despite the fact that we reduced our reliance on non-resident deposits which currently stands at less than 3.5%, while growing our strategic and generational relationships.

As we continue to protect our margins and control our cost of funds, net profit margin was maintained around 2% level, which is bit similar to last year-end closing position, despite high cost of funds.

We now expect an end to the rising cost of funds cycle, which has been mainly linked to FED rate hikes and corresponding rate increases to QCB benchmark rates, as the inflation appears to be cooling-off recently. This is expected to reduce pressure on our cost of funds.

Detailed break-down of Group's total income includes:

- Financing and investments income which was up by QAR 1.2 billion or 41% versus last year's first nine months, and reached to QAR 4.0 billion. This income stream contributes 91% to the Group's total income;

- Second highest contribution to total income is from 'net fee and commission income', which was higher by 42% versus the first nine months of last year, and amounts to QAR 225 million; and

- Lastly, forex and other income which slightly declined 4% on a year-on-year basis, and stood at QAR 186 million for the current nine months period.

Moving onto the impairments - Net impairment charge after taking the impact of recoveries for the current nine-month period amounted to QAR 77 million, versus QAR 379 million during 2022.

Where, gross impairment charge was about QAR 222.5 million, which has been comparatively lesser than last year's first nine months which amounted to QAR 443 million.

Strong 'cash recoveries' of QAR 146 million were noted up to the first nine months of 2023 in comparison to QAR 63.5 million reported during the first nine months of last year.

Staging of financing activities is broadly in line with the industry, with Stage-I comprises 81%, Stage-II 14% and Stage-III NPLs at 5.0% with a decent coverage of 5.6% against Stage-II accounts and 68.9% coverage against Stage-III accounts. However, if we consider eligible collateral benefit, then the Stage-III coverage ratio becomes around 90% against NPLs.

	Financing book remained well diversified, which covers all the sectors including Government 23%, Real Estate 25%, Commercial 10%, Consumer 6%, Contracting 5%, Industrial manufacturing 2% and Services & others about 29%. CAR at end of September 2023 was 17.7%, well above the regulatory requirement of about 14.4%. This gives us an ample room to grow in the future while maintaining adequate dividend for our investors. On the segmental breakup, in terms of total assets: Wholesale banking (which caters Corporates, Government and Institutional customers) comprises 34%, Retail and Private Banking segment with weightage of nearly 35%, followed by Treasury & Investments Group, which accounts for 30% of total assets. In terms of net financing and investments income: Wholesale banking contributes 45% followed by Retail and Private Banking 39%, and remaining 16% by Treasury and Investments Group. We expect 2023 continue to be a challenging year, however, the management is striving to deliver another good year by focusing on the NIM protection, robust liquidity management, while sustaining our existing market share and growing the balance sheet by mid-single digits during the year versus last year. Further, we don't anticipate any material deterioration in the credit quality and we believe the cost of risk would remain less compared to 2022, due to a strong cash recovery noted during the current year. Hence, we anticipate the net provisioning to be on a slightly lower side than the last year. Now we open the floor for the Q&A session, Thank you.
Operator:	If you wish to ask a question, please press star followed by one on your telephone and wait for your name to be announced. That is star one, if you wish to ask a question. Your first question comes from the line of Nikhil Phutane from CBFS. Your line is open
Nikhil Phutane [CBFS]:	Yes. Good afternoon, gentlemen, thanks for the presentation. My questions are related to your performance on the top line. Well, actually, I was just looking on a quarter-to-quarter basis, at how the scenarios stand out. What I see is in the current high interest rate environment when the banks normally are finding it very difficult to pass on the increase in cost of funds to your customers. So, we can see that yields have actually come down as against an upward move which we have seen over the last several quarters. So, the first question given the fact that another likely hike could be there in December, do you foresee your yield flatting off with the current levels are decreasing. Secondly, in terms of your cost of funds, interestingly, you are one of the banks in the local banking system who have been able to increase their current account. I mean, you can say 100% on a quarter-on-quarter basis, I mean that is not getting reflected in your cost of funds, which has further increased. On the other way of looking at it is, unlike other Islamic banks who have reverted to their unrestricted investment accounts, we have to keep their cost of funds in check, your account actually has seen a decrease. So, I wanted to understand from the management's views on this. Thank you.

Osama Abu Baker [Dukhan Bank]:	Okay. I'll start with the question on the current accounts because it's an easy one. As you know, we have a good number of customers both in the corporate, government, and private banking sectors, and the movement of funds can happen in the last few days of the month. So, it was a coincidence at the end of this quarter that we have received a good amount from both the private and government sector towards the end of the month. So, it was a one-off at the end of the month and these funds should be deployed in the coming few weeks and months towards the directions or directives that we receive from those customers. So, that was not something that we expected to come more frequently. If I move to the first question you have asked if I understand correctly, do we expect any change on the yields due to the expected interest rate hike? That's what I understood. If any, hopefully, we'll be able to pass part of that to the customers on the asset side, i.e., on the loan side. As an Islamic Bank, we try to manage the timing of the rollovers of the facilities to be as short as possible in order to manage any gaps, the gap risking here. Definitely, some customers will be able to pass directly, some of them on the rollover dates, some of them are on a fixed basis, which is very minimal in the book that will not be charged with any extra cost of funds. So, I don't expect any decline in our net margins for the remaining of the year.
Nikhil Phutane [CBFS]:	Okay. I mean, coming back to your cost of funds and you've mentioned you don't see much decline in this, sorry, I mean flatting off, I mean this is actually in the light of when we see your real estate exposure is one of the highest in the region and in terms of what we see it going forward very likely… I mean, in case, suppose you're saying you will be able to pass on the cost, it does look like your cost of risk will increase. So, am I correct in analyzing that?
Osama Abu Baker [Dukhan Bank]:	Our exposure, the real estate exposure, I don't think it's one of the highest in the region, but it is around 25% of the book. And if we consider the composition of this, I believe it's more than 50% relating to GREs who are supported by the government, either through direct ownership, through direct offtake, etc. So, I don't see there is a reason to believe that the cost of risk would increase due to this. Plus the Dukhan Bank, more than four years actually, stopped lending to undergoing Real Estate projects, i.e., we lend only to completed projects, and where we have an offtake agreement with GREs. Plus, our exposure to real estate is managed by limiting the dealings to only government, GREs and well-established companies. i.e., we don't take small speculative initiatives. As such, we don't finance white lands, or speculative trading in real estate, that's why we believe that our portfolio is well managed, and we don't see any increase in the cost of risk relating to the real estate portfolio.
Nikhil Phutane [CBFS]:	Okay. So, If I could only, again, add-on to this. So, what you're saying in terms of your provisions on your Stage 3 loans, I mean you can say the coverage which we are seeing around 75%, do you feel that you will be able to increase it further going forward, that it is again relatively low compared to other local peers? I mean, generally say around 95 to 100% or not, do you see that going forward, maybe not necessary in 2023-2024 next year going ahead and increasing it?
Osama Abu Baker [Dukhan Bank]:	Yes, currently the coverage is low compared to other peers, but we should note that this coverage that we are referring to here in the financials does not account for any collaterals or securities. We have either cash or real estate mortgage or shares etc. So, if we include the eligible security with the haircut specified by the regulator, our coverage jumps to 90%. So, definitely we would like to increase this unadjusted

	coverage to 100%. It's not going to be next quarter or next year, it will come over time and I don't see that that's going to affect the profitability or overall profitability of the bank.
Nikhil Phutane [CBFS]:	Okay, fine. And one last question on your cost-to-income ratio. I mean, we are seeing actual during the third quarter is quite short up. I mean from around 30% down to 22% with around under 30%, we are talking about 36% in the third quarter. So, do you see the same trend continuing going forward in the fourth quarter?
Osama Abu Baker [Dukhan Bank]:	Well, it has increased. The cost of income increased because of the increase in the cost of funds which affected the net banking income. But if you look at the absolute amounts, the G&A or the admin cost, and the people cost did not increase compared to last year. So, the ratio has increased due to the decline in the net banking income, but the absolute amounts are stable, and I expect the absolute amounts to continue to be stable compared to last year.
Nikhil Phutane [CBFS]:	Okay, thank you. In case I do have further questions, I'll let other participants ask and I will be there. Thank you.
Osama Abu Baker [Dukhan Bank]:	Thank you.
Operator:	As a reminder, please press star followed by one on your telephone and wait for your name to be announced. That is star one if you wish to ask a question. And currently, there are no questions I'd like to hand back to Shahan.
Shahan Keushgerian [QNBFS]:	I have a question. It could have been addressed. The cost of risk so far nine months annualized is immaterial. It's something it's like 8 basis points versus last year. Are you expecting more recoveries in the fourth quarter and what kind of credit provisioning can we expect for the end of the year? I mean, would it be in line with fiscal year 2022 or lower than fiscal year 2022?
Osama Abu Baker [Dukhan Bank]:	All right, so the recovery, this is the first question you asked, we aim for recoveries. But as you know, it is subject to the legal system and the execution within the legal section. Yes, we have a lot of cases but how certain I am that those will be booked this year? I cannot give you any assurance, but we are working in some cases. The absolute provisioning number before recoveries compared to the previous years will be lower because we have covered most of the bad debts and our coverage with effect of collaterals as we mentioned is on the 90% level. So, by default, it will be lower than the previous year and this is an exercise, it takes place in the last quarter. So hopefully, the results of this exercise will be positive, and it will show that no further deterioration in the portfolio that needs additional provisioning.
Shahan Keushgerian [QNBFS]:	Thank you very much.
Operator:	So again, if you do wish to ask a question, please press star followed by one on your telephone and wait for your name to be announced. Your next question comes from the line of Mustafa Aamer from Al Rayan. Your line is open.
Mustafa Aamer [Al Rayan]:	Thank you, gentlemen, for the presentation. Carrying on to the same provisioning, is this the provision that you have reversed in the third quarter of this year? Is it related to change in assumptions on your ECL models, or is it actually that some of your clients

	which were earlier provided for the unit settlements? Is it specific to one client where the settlement happened, or is it across a number of them? Thank you.
Osama Abu Baker [Dukhan Bank]:	Also, these reversals are cash recoveries, i.e., we have liquidated the securities, or we have collected the bad debts. That's why we have reversed the provisions. Minimum amounts relating to the classification of the customers or reversal of ECL. The majority is cash collection.
Mustafa Aamer [Al Rayan]:	Thank you. My other question is on the fee income. We saw quite an improvement compared to last year same quarter. Could you give us some idea on what is leading to this increase?
Osama Abu Baker [Dukhan Bank]:	Yes, it was a good improvement compared to previous quarters and previous years. As you know, in Dukhan Bank, we have a good base of private customers, corporate, and government entities. So, we have been working on these deals since the beginning of the year, so it's diversified. I mean among all sectors, it relates to swaps, to hedging, to arrangements, and to advisory. So, it came from many divisions within the bank. It's not relating to one division. And as I mentioned, it took us more than nine months of hard work to have those deals materialized. So, if your question is, shall we assume the same for the fourth quarter? No, fourth quarter will become back to normal amounts which are the fees relating to LC, LGs, and the other business. I wouldn't call it a one-off. It is a materialization of many efforts that came to materialize in Q3. It was a coincidence that all these initiatives materialized in the third quarter.
Mustafa Aamer [Al Rayan]:	Sounds good. My last question is on…you had mentioned that your current account improved at the end of the quarter, that's why you were not able to deploy those funds. Would those funds be deployed more towards these loans, or will it be investments? Or would you think of letting go of some of your higher expensive deposits because now like you've got such a good current account, current deposits? Thank you.
Osama Abu Baker [Dukhan Bank]:	As you know, managing liquidity is an art and if we have received some funds from our customers towards the end of the month or the quarter, that doesn't mean that we will let go of our whole deposits. Core deposits are the bread and butter to fund the balance sheet and we cannot let go. Currently, we are deploying those into the money market short-term medium-term, and our Treasury Department is responsible to manage the liquidity to minimize the risk, the liquidity risks. So, some of those funds might be drawn by the customers might be utilized by the customers. So, there is no single answer that I can give you now. We keep a proactive approach to manage the liquidity but definitely, our core deposits are something that we will not let go because we have received some funds.
Mustafa Aamer [Al Rayan]:	Sounds good. Thank you.
Operator:	The next question comes from the line of Nikhil Phutane of CBFS. Your line is open.
Nikhil Phutane [CBFS]:	Yes. Well, thanks again for the questions you've answered. This is regarding… you have mentioned that in 2024 likely you could be seeing projects coming up from other aspects apart from LNG. So, I just wanted to have your view in terms of where you see for the Dukhan Bank for 2024 in terms of credit growth rate?
Osama Abu Baker [Dukhan Bank]:	Actually, we continue to aim, to grow with the local economy. As you know, we are a local bank, a Qatari bank, we don't have operations outside Qatar. So, our growth is linked to the economy, plus we have a special advantage here where we have good relations, in fact generational relations with good corporates in Qatar, and private banking customers. So, we aim to grow with the expected growth of the national economy.
Nikhil Phutane [CBFS]:	Okay. And your peers have mentioned around 3% to 4% growth likely in 2024. So, do you hold to that view?

Osama Abu Baker [Dukhan Bank]:	Close to the expectations for the Qatar economy, yes.
Nikhil Phutane [CBFS]:	Okay. Thank you. Thank you, sir.
Osama Abu Baker [Dukhan Bank]:	Thank you.
Operator:	Again, if you would like to ask a question, please press star followed by one on your telephone and wait for your name to be announced. And there are no further questions at this time to let the hand back to Shahan.
Shahan Keushgerian [QNBFS]:	Okay, great. If there are no more questions, we can wrap this call up. I'd like to thank management for giving us an update on the bank's figures for the nine months. And I'd like to thank the participants for dialing in and we can pick this up again next quarter. Thank you.
Ahmed Hashem [Dukhan Bank]:	Thank you, Shahan. Thank you all for joining us today.
Operator:	That does concludes our conference for today. Thank you for participating. You may now all disconnect.