4Q 2021 Earnings Call Transcript

Presentation

Mazen Alsudairi:

Good day all. This is Mazen Alsudairi from Rajhi Capital. Rajhi Capital is proud to host Rajhi Bank Q4 2021 Earning Call. Welcome all to the call. And now I will hand over to Rayan, head of investor relations.

Rayan Alshuaibi:

Thank you Mazen. Good day, everyone, and thank you for joining the call. With us today on the call, our CEO, Waleed Almogbel, CFO, Abdulrahman Alfadda, and COO, Abdullah Alomari. Our CEO will start with results highlight and strategy update, then followed by our CFO to give further detail on the financial performance. Again, we thank you for joining the call and Waleed over to you.

Waleed Almogbel:

Thank you Rayan. Good morning and good afternoon to everyone. We welcome you and thank you for attending our Earning Call for the fourth quarter of 2021. Before we start, we greatly value your trust in us and proud that Rajhi Bank is currently ranked number 15 globally and number one in MENA region among banks by market cap.

First of all, as you may know, the bank yesterday announced the board of director recommendation to the extraordinary general assembly to increase the bank capital from SAR 25 billion to SAR 40 billion through bonus shares. As a result, three bonus shares will be granted for every five shares owned. The reason of this increase is to support the bank in capturing growth opportunity, which should be as we believe, a positive sign reflecting the management confidence in future growth over the medium- and long-term

For our presentation, we will go as always through our full year highlight. Then I will give you an overview of our strategic performance for the fourth quarter last year regarding Bank of the Future strategy. Now, let's go ahead and take a closer look on the first slide.

If we move to slide number one, we will start with the balance sheet. As you can see, we deliver the strong growth of 7% quarter-on-quarter and 33% year-on-year. The full year growth came from all lines of business, 46% from retail, 34% from corporate and 40% from investment book.

If we look forward to the net financing, we deliver the growth of 43% year-on-year, and that resulting in financing portfolio reaching to SAR 453 billion. That's mainly driven by mortgage with a growth of 63%. Now the mortgage represents 37% of our total book and 46% of our retail book.

If we look to the liability side, total liability stand now at 556 billion with a solid increase of 35% year-on-year. A good growth also recorded in the demand deposits of around 13% compared to a market growth of 6%. That gives us a stable LDR of around 82%, which give us additional room to grow in financing portfolio.

On the net income side, we delivered a solid net income with a growth of 39% for last year to reach SAR 14.7 billion. That is driven mainly from both net yield income, which increased by 21% year-on-year, and also from non-yield income with a growth of 40% year-on-year mainly driven by fees from brokerage and the digital payment. Our total operating income has increased by 24% year-on-year standing at 25.7 billion.

If we go to the third element, we continue to maintain best-in-class assets equality. Cost of risk is healthy. It is standing at 60 bps supported by a good recovery compared to 75 bps for the year end 2020. Although the gross provision has increased of almost 18% compared to 2020. Additionally also, we continue to maintain a low NPL, which stands at now 65 bps compared to 2020, 76 bps, with a healthy and stable coverage ratio of above 300%.

Lastly, the management continue also to deliver on cost efficiency, which led to improve our cost-to-income ratio by more than 5.5%, resulted in cost-to-income ratio that currently stands at 26.9% compared to last year of 32.5%.

If you allow me to move now to the next slide, we are on track executing our Bank of the Future strategy. If you recall, we have four pillars. First is building on the core. We continue to focus on retail as a core banking business, and we have seen a financing growth of 46% year-on-year as I mentioned. Additionally, we continue to expand our corporate portfolio and reposition ourself. We have seen a finance growth year-on-year in corporate portfolio by almost 33% compared to full year in 2020 of 3%.

Also SME is an integrated part of our strategy, positioning ourself as bank of choice for SME. We have seen a good growth for 2021 of 61% year-on-year. Now SME represent 18% of our corporate book compared to 15% in 2020. Although we have seen a massive growth in large corporate book.

Demand deposits also continue to be one of our priorities. And as per the initial data from the Central Bank, our market share has increased to 27.3%. One of the items that we focus on in the first pillar is our non-yield income as a percentage of our total operating income. It continues to increase reaching now 21% compared to 2020 of 18%.

Moving to the second pillar, outperforming our competition. We continue to focus on delivering the best customer experience in the market, maintaining NPS leadership at 72% compared to 66% in 2020. For the banking asset market share, as per the initial data from the Central Bank, the growth we delivered in 2021, our market share reached 19% compared to 16% in 2020.

With regard to loyalty program, we have done a good progress last year for the loyalty program. Our loyalty program now the top of mind loyalty brand in the banking industry with total registered customers reaching almost four million customers. Additionally, we are proud also to share with you that as of 2022, the bank received an MSCI ESG rating of BBB. The rating was upgraded from BB last year.

Moving to the third pillar, transform technology. One of the strengths of Al Rajhi Bank is our modern technology and digital infrastructure as we are continuously improving our channels. Digital to manual ratio currently stands at 90:10 compared to last year of 83:17. It is worth to mention that online account opening reaching 89% of the total retail account opening in 2021. Also, additionally, we have seen an improvement in our end-to-end digital financing, which has reached 36% of our retail personal finance.

In terms of the operation excellence, we have currently more than 360 bots. They are doing more than 37,000 average daily transaction in our back office operation. Our 4Q21 average transaction per month has increased to reach now more than half billion transactions conducted in our IT infrastructure. This is an increase of 50% year-on-year.

Last pillar of our strategy is to focus on client needs and requirements. Number of active customers have reached to more than 12 million customer. We provide our sales team with a 360-degree system to ensure we have a proper cross selling assisting them in all the products and services we have. Having said that, we continue to improve our payment solution. Our point of sale terminal market share has increased to reach now 32%.

If you allow me to move to the next slide. As we mentioned in the previous slide, we are on track to deliver our strategic objective of building the bank of the future. We have highlighted in earlier calls the launch of Emkan, our microfinance fintech company, and also Neoleap, our payment fintech company, which provide a payment solution for merchants and individuals as well.

We are proud today to present to you our latest addition to the group, which is Ejada. As you may know, the bank has fully acquired Ejada in January, a move that we believe it will help us to accelerate our strategic initiatives in digital and IT infrastructure.

As you know, technology and banks have evolved from being a function within the organization to a fundamental part of what a bank is. Banks are becoming more like of technology companies, around which a financial ecosystem is established. That requires banks to continuously and dynamically deploy and upgrade technology capabilities to support their ecosystem. That is mainly to enable open banking/open APIs, upgrade Cybersecurity and accelerate cloud adoption as well as accelerating digital transformation.

Many financial institutions also have centralized their technology capabilities in various forms. This proven concept is in line with our approach to “unbank the bank”, to address new markets and segments with high capabilities focused on improving customer experience and efficiency and time to market, which is an important pillar in fintech world.

We would like to highlight that Ejada will continue to serve its more than 300 clients from various industries, including government, banking, telecom, healthcare, and others. We are very optimistic about the future of Ejada and we will continue to focus on delivering value to our customers and shareholders.

Now, if you allow me, I will hand over to Abdulrahman, our CFO, to give you a detailed update of our financial performance. And thank you so much.

Abdulrahman Alfadda:

A salam Alyukom wa rahmt Allah w barkatah. Good day, ladies and gentlemen. It is my pleasure to welcome you again in our 4Q Earning Call. I'm very proud to present to all of you our outstanding performance for 2021 result, where there has been a good progress in our strategy execution. Having said that, I'll go over the financial performance slides very quickly, given that most of the information has already been shared in our earning release as well as we uploaded our financial statement yesterday, so that you can have a further time during the Q&A session later on.

Our total assets has reached SAR 624 billion, almost 33% increase year-on-year, around 7% on a sequential basis. To analyze further the movement in our total assets, as you can see on the bottom left-hand side of the chart, cash and interbank have been reduced, which is in line of our strategy to optimize both non-yielding assets, as well as improving the average earning assets. Investments have increased by almost 40% year-on-year, financing 43% year-on-year, and we'll cover further details on the financing in the following slides.

As far as of the movement into the funding, as you can see on the bottom right-hand side of the chart, the majority of the funding came from the customer deposits, whereby almost 34% increase in our customer deposit and also our total equity have increased by almost 16%. It's worth to highlight in 2021, we have paid the total cumulative dividends of around SAR 6 billion.

Zooming further into the main driver of our balance sheet. On the financing side, our total net financing have reached almost SAR 453 billion, 43.4% increase year-on-year, 8% on a sequential basis. Retail financing reached almost SAR 366 billion, which represent 81% of the total financing versus 79% in 2020. Non-retail, at an SAR 87.1 billion, which represents almost 19% of the net financing compared to 21% in 2020.

The movement in financing. As you can see in the top right-hand side of the chart, we have grown our mortgage book by 63%, ex-mortgage of retail around 30%, which will drive the total retail growth of around 46%. Corporate, 33% increase. SME, almost 61% and we have reduced our financial FI lending due to some maturities. Totally, non-retail growth were almost 34%. So we have seen a broad based growth among all business line.

Total customer deposits have reached SAR 512 billion, whereby demand deposit have reached almost SAR 375 billion, which translates to almost 75% of our total customer deposits. To analyze further the movement in our customer deposits, as you can see in the bottom right-hand side of the chart, demand deposits have increased by 12.5%. Worth to highlight that the market overall growth was 6%. Subsequently, we managed to grow our market share to 27.3% versus 25.5% in 2020. Time deposits have increased by almost three folds, to support our growth in the total assets.

If we move to the profitability section, our 4Q net income before zakat have reached almost SAR 4.5 billion, 28.5% year-on-year, and almost 6% on a sequential basis. If you can see on the bottom left-hand side of the chart, to analyze the full year net income, our net income before Zakat, almost SAR 16.5 billion, 39.2% increase year-on-year. The main driver where as follows: yield 21%, fees 40%, which will bring the total operating income to be 24% increase year-on-year offsetted by 3% increase in our OpEx, which will drive the total pre-provision profit to be 34% year-on-year increase. Impairments were 8% higher on a year-on-year basis.

From a sequential basis, as I mentioned earlier, the growth was 6% and the growth were attributed to the following. Almost 3% growth on the yield, 10% non-yield, which will drive the operating income to be 4%, offsetted by 2% increase in our OpEx, which will drive the pre-provision profit growth on a sequential basis to be 5%. Impairment were almost flat.

To further zoom in into the net income driver. I'll start with an operating income. Operating income for 4Q were almost 6.8 billion, which is almost 18.3% higher year-on-year, 4% on a sequential basis. For the full period, our total operating income were SAR 25.7 billion, almost 24% growth on a year to year basis, 4% on a sequential basis.

The drivers were as follow. Although that our average earning asset have increased by 24%, however, our net yield have increased by only 21% due to the NIM contraction. Our fees have increased by 48% year-on-year and the reason attributed to the following. A, brokerage revenue; we have seen the average daily volume increased by 7% in 2021 versus 2020. Also, the host of this call, our sister company, Al Rajhi Capital, have managed to increase their market share to almost 19.5%. B, second driver were in the payment revenue, which is a strategical objective and a focus for the bank. Consumer spending have increased by 10%, that's number one. Second, we've seen a further acceleration of the positive migration to the cashless payment method, whereby ATM transaction have went lower by 7%, point-of-sale by 32% higher, eCommerce by 91%. Third reason is also increase in the point-of-sale market share, where our market share and the point-of-sale terminal were at 32.2% versus 28.4% in 2020.

The other third reason was also increase in the business activities, giving that we have seen a further improvement into the trade, cash management, FI rebate, current account related activities, and wealth management activities that we have seen in last year. Exchange income were almost flat. Other operating income were 65% year-on-year growth. I would like to highlight, in 4Q, we've taken advantage of the low interest environment and we've realized some capital gains through selling some portion of our treasury investments.

Our NIM. As you can see on the bottom left-hand side of the chart, we have almost 50 bps contraction on a year to year basis, 9 bps on a sequential basis. The 9 bps sequential translates to almost 36 bps on annual basis. The driver of the 50 bps contraction on the NIM were attributed to the following. A, 45 bps contraction due to the retail portfolio. And what we have seen last year, an aggressive competition into the retail. That's number one. B, if you recall, mortgage pricing is around160 bps lower compared to 2020. C, corporate and treasury; we've seen a combined almost 7 bps due to the fact that the average SAIBOR in 2021 were 38 bps lower than average SAIBOR of 2020. D, cost of fund has attributed to 9 bps impact on the NIM. Our cost of fund for last year was 23 bps versus 13 bps in 2020. Having said that, the management have delivered almost 12 bps to compensate the drop in the NIM. The management action points were driven by change in mix, improvement in our average earning assets, as well as optimizing the non-yielding assets.

To move and analyze the second driver of our net income, our OpEx. Our 4Q OpEx were close to 1.8 billion, almost 1.6% year-on-year growth, 2% on a sequential basis. And for the full year period, as you can see in the top right-hand side of the chart, our total OpEx was 6.9 billion, 2.7% growth compared to 2020. And the driver, as you can see, mainly are coming from the staff salaries and benefits, whereby, supporting the balance sheet growth of almost 33%.

Depreciation have increased by 2.1% due to capitalizing some of the investment that we have done in our digital and transform our IT infrastructure. G&A was almost flat. Having delivering operating income growth of 24.1% versus operating expense of 2.7% growth, we managed to deliver positive jaws that have attributed to 590 bps improvement in our cost-to-income ratio.

It's worth also to highlight, in addition to the cost-to-income ratio, we also monitored from an efficiency perspective, the following factors. Non-yield as a percentage of OpEx, have improved from 56.5% to almost 77%. OpEx as a percentage of total assets have improved from 144 bps to almost 111 bps.

On the asset quality, our cost of risk stands at 60 bps compared to 75 bps in the same period in 2020. It's worth to highlight that our gross cost of risk was 94 bps negated by 34 bps on our recovery.

Our NPL have increased by 23%, mainly on the retail side where our total NPL as of 2021 was almost 3 billion, which translates to almost 65 bps, as you can see on the bottom left-hand side of the chart compared to 76 bps where we've seen further improvement in our non-retail and a small uptake on our retail portfolio. NPL coverage is still healthy at almost 306% and well ahead in terms of the overall competition NPL coverage.

4Q net impairment charges was SAR 590 million, 7% year-on-year, and almost flat on a sequential basis. That full year net impairment charges were almost SAR 2.3 billion, 8% growth compared to the same period last year. It's worth to highlight that our gross charge has increased by 253 million, while we have improved further our recovery by SAR 74 million.

Stage one, still healthy at 97% of the overall loans, haven't materially changed over the period. Our ECL coverage, although that we have seen a small reduction in our stage one and stage two coverage. However, we've managed to top up our stage three coverage to reach almost 75.6%. And those stage coverage were well ahead in terms of the competition, which reflect Al Rajhi Bank prudent risk management.

Liquidity position remains very healthy and within the regulatory requirement. As you can see that, although that the headline LDR stands at 88%, but our actual LDR at 82.3%, LCR and NSFR at a comfortable levels and within the regulatory requirements.

On the capital side, our total RWA have increased by 32% year-on-year, driven by 37.4% increase on the credit risk RWA, mainly on the increase on the financing as well as on the investment. Our total RWA density still at 68.2% as of 4Q. Our Tier I capital stand at 70.2 billion, versus 67.3 billion of a total shareholder equity. The Delta, as you recall, is the 2.9 billion, FTA that we've highlighted to you guys in our 2Q Earning Call.

Having said that, the growth that we have seen have resulted in a further reduction in our CET1 ratio. It came down from 18% to almost 16.5%, a 150 bps reduction. The drivers of those reduction were on the bottom right-hand side of the chart, where you can see that the portfolio growth and the total assets have contributed to almost 524 bps drop in the capital ratio due to the total RWA. Nevertheless, that has been offsetted by 285 bps of an internal capital generation that has been delivered last year.

Finally, the bank delivery of a record full year result have resulted in a further improved return matrices. Our RORWA still stable at 3.94%, earnings per share for 4Q at SAR 1.6, for the period is 5.9 versus 4.24 last year. Our ROE have further improved to almost 23.9% and finally, a stable ROA at 2.7%.

So before we start providing the guidance for 2022, we will give our assumptions and what are the drivers. We forecasted the GDP growth to be almost 7.7% in 2022, which is close to MoF forecast, mainly driven by 15.5% growth in the oil GDP and 3.4% in non-oil GDP. We also forecast that for the first time since 2013, the government will deliver a fiscal surplus by almost 120 billion Saudi Riyal, which equates to almost 3.2% of GDP.

Consumer spending have further improved last year and will continue to further improve this year, given the vaccine rollout and the containing of the pandemic situation in the Kingdom. The credit growth is expected to further improve this year. The improved economy outlook will further provide a positive impact on the financing portfolio growth, as well as cost of risk optimization.

However, on the interest rate, our best case forecast is five rate hike by the Fed, which translate to almost four rate hike by SAMA. We still continue to believe that the competition on the retail as well as the corporate side will impact the margin going forward. Also worth to highlight that the retail ex-mortgage of the book, usually re-price within one to three years. Hence, that will have negative impact on our NIM.

Finally, on the strategy execution, given that, as Waleed mentioned earlier, the focus to build an ecosystem to further improve the customer experience through launching of some of the fintech company and our focus will further help us improve our cost-to-income ratio, fees as a percentage of operating income, earning per share, and also finally, our ROE. Having said that, the guidance for 2022 is as follows.

High teens growth in the financing portfolio. NIM, to contract between 55 to 45 basis point, cost-to-income ratio to be below 27%, ROE in the range between 23% to 24%, cost of risk in the range between 50 to 60 basis point. And finally, our Tier I ratio in the range between 17% to 18%. Waleed, back to you.

Waleed Almogbel:

Thank you, Abdulrahman, for the financial performance of review. The good progress made on our bank of the future strategy helped us to deliver a record year. I would like to just highlight on four points.

Number one, Al Rajhi Bank maintained a track record of earning per share, ROE growth combined with a healthy delivery on few line items such as, fee as % of operating Income , cost efficiency and cost of risk.

Number two, Best in class Balance sheet Matrices such as liquidity, capital and stage coverage.

Number three, agile & performance driven culture that supported us to execute the key pillar of our strategy and outperform the competition.

And last one, we have been a key player to support the Kingdom 2030 Vision initiatives, such as home ownership, private sector contribution to GDP, digital economy and payment.

We will continue driving excellence to go beyond the unthinkable to unbank the bank through creating a financial ecosystem that provide our valuable customers with innovative and smart financial solutions addressing their changing needs.

Now, we will open the floor for Q&A session. Operator back to you.

Operator:

Thank you. If you would like to ask a question and you've joined us through WebEx, please use the raise hand icon in the reactions tab. Alternatively, you may submit a written question in the Q&A box. If you've joined us via the telephone lines, please press star followed by one on your telephone key pad. When preparing to ask your question, please ensure that your line is unmuted locally. Our first question comes from Waleed Mohsin of Goldman Sachs. Waleed, your line is open. Please go ahead.

Waleed Mohsin:

First on loan growth, your high teens loan growth guidance, If you could please talk about the expectations that you have for various segments, especially mortgages and corporate. Because if we look at your mortgage book, it's almost 40% of your total book. And if we continue at the pace that the monthly mortgages are growing, which is around 12 billion per month, that in itself is probably going to drive low teens growth. So, wanted to get a sense of what your mortgage expectations are and the expectation for the remainder of the book. So that's the first question.

Secondly, if you could please talk about the recent changes introduced by the REDF. My understanding is that now customers can transfer mortgages amongst banks and the REDF guarantee would continue. So if you could talk about, what is the change and any implications on your business from that?

And my third and final question. So it seems there's no cash dividends for the second half. And given that most of your loan growth last year came from mortgages, which are 50% risk weight. So I want to understand the reason to hold back or preserve capital. Is it management thinking about some of the regulatory changes which are coming? For example Basel IV, which will have some implication for mortgages? Or is it to do with the capital buffers that banks are required to hold due to the ALM gap? These are my three questions. Thank you very much.

Abdulrahman Alfadda:

Waleed, thank you very much. So, first of all, on the loan growth. From our perspective in 2021, we managed to grow our mortgage book by almost 63%. And if you recall, we've been saying that our expectation on the mortgage growth is almost 30% on a CAGR basis between 2021 - 2023, front loaded in 2021. We've seen a bit of slowdown in the mortgage origination in 4Q. For example, the total mortgage origination in 4Q were close to almost 47.7 billion, which is lower compared to the peak that we have seen in 1Q were 65.6.

So this is in line of our initial forecast of a slowdown. Again, let me clarify, we've mentioned slowdown in terms of a percentage, but in terms of the absolute growth, still, we believe that there is a further room for the growth into the mortgage.

The loan guidance that we've provided is taken into consideration the following factors. The mortgage as well as retail, corporate and SME. And I think that we have seen in 2021, a broad-base growth, and we are expecting that to continue inshallah in 2022. Unfortunately, I cannot give you the exact numbers, but hopefully, the trends that I've highlighted can help you to make your judgment.

The second question, regarding the recent development on the REDF. Yes, there has been a change whereby a customer can opt to go to another bank and that's considered to be a mortgage buyout. Whereby he can go to another bank and take a mortgage at a lower rate than existing rates. Nevertheless, we don't see any value for that to happen apart from increasing the DBR for the customer. So far since that rule has been changed, the number of cases that we have seen is very minimal. Now, how things will evolve, we are not forecasting that much, but this is more of a watch and see kind of a strategy. But from our perspective, we are ready, whatever it take to make sure that we are protecting our mortgage market share. Waleed?

Waleed Almogbel:

Thanks Abdulrahman. Waleed, as I mentioned in the beginning that the bank announced yesterday bonus share to increase the capital to SAR 40 billion from SAR 25 billion, and that will help our equity. The main purpose of this increase is to support the bank capital position to capture the potential growth opportunity in the market that we are anticipating inshallah this year.

If you recall, when it comes to dividend, we have been always communicating to the market that the management always weigh in between distribution dividend and preserving capital to support future growth. So, our view always is capturing the growth as long as it is in the market. And that's the reason why we recommended to the board and the board approved the increase in the capital by giving three bounce shares for every five shares.

Abdulrahman Alfadda:

Also, I'd like to add, Waleed, as a follow-up in terms of what you see on the Tier I ratio, this is covering both the Pillar 1 and a Pillar 2 ratio, which is in line of the Basel recommendation.

Nevertheless, there is a Pillar 2 risk weight that we monitor, which is in line of the SAMA guidelines, which is in the best practice as Basel. Unfortunately, those Pillar 2 parameters are not disclosed. And from our perspective, rest assured that we are in line of all the regulatory requirements to be able to support the growth over the medium and a longer term.

Waleed Mohsin:

Perfect. Thank you so much. That's very helpful. Very helpful as always. Thank you.

Operator:

Thank you, Waleed. Our next question today comes from Rahul Bajaj from Citi. Rahul, your line is open. Please go ahead.

Rahul Bajaj:

Hi, this is Rahul from Citi. Two quick questions from my side.

First is on your non-interest revenue line. You mentioned, Abdulrahman, about some gains in the fourth quarter coming in that line. And if I recall correctly, there were similar gains in some of the previous quarters in 2021 as well. So my question is, as we move into a, probably a higher interest rate trajectory, how should we expect these gains and the trading revenue line, basically, to kind of shape up? Should we expect some normalization there lower than 2021 levels? Or you think there is room for this particular line item and this particular business segment, the treasury business segment, to grow further? So that's my first question.

My second question is on the 45 to 55 bps compression in margin that you have guided to. And you kindly mentioned, I think you based in four rate hikes within that kind of margin guidance. Just wanted to understand how... I mean, this kind of breakdown for this 45 to 55, if you could provide us? I mean, how much upside you think will come from actual interest rate increase versus kind of declines coming from several items?

And linked to this is your deposit guarding strategy because this particular deposit guarding strategy has changed quite meaningfully in 2021 when Rajhi has been particularly active on the time deposit side in 2021. So is this the strategy that will continue in 2022 as well? That's my question. Thank you.

Abdulrahman Alfadda:

Thank you, Rahul. So the first question related to the capital gain that we've taken in 4Q. I think over the quarter in 2020, there has been a small disposable of non-core assets. So it's not material. The only material amount that I would like to highlight was the capital gain that our treasury team have booked in 4Q taking into consideration the interest rate environment.

Nevertheless, in the current rising rate environment, and I think is something that we believe that the capital gain that we've taken 4Q, is none recurring and subject to the market levels. Historically, Al Rajhi Bank is not very active in taking a capital gain to be able to manage the P&L. So, that's number one.

Second, and I'm very glad that you've asked the question about the NIM. Let me give you how we are looking at it. So, first of all, our disclosure in our financial statement, note 27-3, which will give you the profit risk or the interest rate risk sensitivity, you can see that there are almost 96.5 billion of assets will be repriced over in a one year time. That will have an impact for every 25 basis point movement in SAIBOR, around three to five basis point pickup in the NIM.

Nevertheless, the reason why the NIM compression, can attribute it to four main factors.

Number one on the competition side. We've seen a very aggressive competition on the retail last year. And also, we've seen a further spillover in the competition to the corporate side where we've seen the margin are being, I would say, lower than whatever it used to be. We've taken that into consideration.

Factor number two, Rahul. If you recall, when I presented our NIM chart, the drop in 4Q was nine basis point. If you annualize that, that's almost 36 basis points. Our exit rate for 2021 is 3.85. So what we are expecting is, I would say, a steep drop in 1Q, probably to some extent in 2Q. But then I think flattish over the second half, then we'll be providing a further pickup as we go and enter in 2023 subject to several market conditions.

Third line is on the cost of fund. You've seen that our time deposits went higher by three folds. Our cost of fund have increased from 13 basis point to 23 basis point, which have an impact of a 9 basis points last year and it'll be also one of the components in 2022. And to address your question, we provided a guidance on high teens on the financing. We don't anticipate that the overall market will grow in the demand deposit by that amount. So, deposit gathering to be able to fund the growth is going to be a continuation of what we have delivered in 2021.

The fourth item, which I've talked about very briefly is delay on the pricing. If you look at our composition of our financing portfolio, corporate is floating and that will be re-priced accordingly. On retail mortgage is an average duration 17 to 18 years. That will not be re-priced over the next few years. However, the ex-mortgage of the portfolio, which is almost 50% of the 365 billion of the book is, usually the pricing is happening anywhere between one to three years. Because usually, the customer will come and top up and when they top up, they will top up at the prevailing market rate, which is usually five year rate. As and when, curve will steepen further, that will have a further improvement into the NIM.

So these are the highlights. And the bottom line is, the rising rate environment, the impact on us, on Al Rajhi Bank, is not muted. Nevertheless, it's delayed.

Rahul Bajaj:

Understood, very clear. Thank you.

Operator:

Thank you, Rahul. Our next question comes from Shabbir Malik of EFG-Hermes. Please go ahead, Shabbir.

Shabbir Malik:

Thank you very much. Thanks for this presentation. Just a quick question. You have a good track record of delivering on your loan growth guidance. Your high teens, the guidance for 2022, do you see any risk to this growth guidance or do you foresee any challenges or this potential for any upside risk?

My second question is on your fee income, a very strong 2021. What do you think will be the key drivers for you going into 2022? And was it safe to assume that it's going to be more or less in line with your balance sheet growth, fee income would be in line with balance sheet growth for 2022?

And finally, you've given a cost of risk guidance of 50 to 60 basis points, which is, I guess, in line or slightly better than last year. Given the interest rate outlook with rising interest rates and also the potential ending of the deferred program, do you see any risk to this cost of risk guidance? That's all from me. Thank you.

Abdulrahman Alfadda:

Thank you, Shabbir. First question, related to the loan growth. Again, this is what we believe in at the current macro level. If things have changed, we will adjust accordingly, but from our perspective, we are forecasting our best estimate for the time being is on the high teens growth. There are multiple factors to consider, if there is any slowdown or further pick up in the mortgage or in the corporate demand or the infrastructure project, etc.. So there are a lot of variables, but as we speak in February, I think the best estimate for us is high teen loan growth.

The second question related to the fee income, this is in line of our strategy to be able to improve the revenue mix, whereby fees as a percentage of total operating income, as Waleed mentioned earlier, have improved. The management focus will continue to be able to further improve that and to able to compensate whatever the NIM drop that we have seen last year and also forecasting for this year as well.

I think it's driven by all business lines, whether it be on brokerage, whether it be on payments, whether it be on trade, cash management, multiple business lines. And I think we'll continue to focus, to further improve the fee income as a percentage of our operating income.

Finally the cost of risk, it's worth to highlights that, A, just to clarify your statement, it is better than last year which was 60 basis point, our guidance is 50 to 60 basis points. So, that's from the improved macro outlook, And also with the improved recovery activity, and I think we will be able to deliver that cost of risk guidance.

Having said that, it's worth also to highlight that we have taken close 426 million of management overlay in 2021 on the corporate side. Out which 228 million was related to the SME deferral. And we're quite comfortable that with the current overlay that we're having and with our risk and the business team effort to speak to the client. So we are quite comfortable that whatever the provision that we have is adequate. Subsequently the cost of risk guidance is intact.

Shabbir Malik:

Oh, thank you very much. That's very clear.

Operator:

Thank you, Shabbir. We have a question from Chiro Ghosh of SICO. Chiro, your line is open. Please go ahead.

Chiro Ghosh:

Quick question. The first one is related to the mortgage book, which you're planning to move towards the private sector. So how different would it be from your primary mortgage book, which it was, which I believe is primary to the public sector? So obviously, would you expect more risk to that sector? Would you see more competition? That's my first question.

The second one is more related to this Emkan and your digital banking. So how much growth are you perceiving from that side of the business? And the third one is related again to the NIM question in continuation. So a quick back of the envelope of calculation suggests that a corporate book is roughly around 13% odd. And over the 50% mortgage book, if I assume, say 15 to 20% would get repriced in one year, still a big chunk of the book will not get repriced over the one year. So do you expect this 50 basis point NIM pressure to continue even in 2023 onwards if the interest rate goes up? Some clarity will be highly helpful. Thank you very much.

Abdulrahman Alfadda:

Sure. So I'm not sure whether I've mentioned that we have continued to go to the private sector, but overall, still underwriting standard hasn't changed. We still focus on the government related employees. Salaries assigned, the risk is quite acceptable so I'm not sure about that. So that's the first clarification.

On the third question, and I think I've mentioned earlier, our drivers for the NIM. And I've mentioned that the exit rate is 3.85%. And I've mentioned earlier that we're expecting a steep drop in 1Q and 2Q as well. Not to that extent, but we are expecting that mainly the unsecured loan, which is usually repriced on anywhere between one to three years to kick off the benefit from 2023 and beyond.

As far as Emkan, we launched it back in 2020, and I think we've delivered a good growth. Nevertheless, it is still unmatured business and we still continue to focus. This is something new to the group and we'll continue to evaluate, continue to improve our understanding and the underwriting standard, etc., to be able to further focus on that. But nevertheless, we are quite comfortable so far.

Chiro Ghosh:

Thank very much. Just a very quick question on one small part. Last year, most of the banks are looking to get into the mortgage business. So I want to get an understanding how is the corporate borrowing demand in the Kingdom? So will the corporate focus bank move towards the corporate sector? Will that reduce your competition in the mortgage and the retail loan business? So just to get a ground reality.

Abdulrahman Alfadda:

We still believe is that there is a good demand on the corporate side in 2022 and beyond. There has been a positive sign that we have seen. A lot of giga project has been awarded some of the infrastructure project. There has been also, and I think historically, there is a lag factor between improvement in the oil prices versus the corporate demand. So I think we're quite positive on the corporate side over the medium and longer term.

Chiro Ghosh:

Okay. That's it from my side. Thank you very much.

Operator:

Thank you, Chiro. In the interest of time, this concludes today's Q&A session. Any additional questions should be addressed to the investor relations team whose contact details are available at the end of the presentation. With that, I would like to hand back over to Mr. Waleed Almogbel, CEO, for any closing remarks.

Waleed Almogbel:

Thank you, everyone dialing and for your trust in us. And we are very proud of our result and really value your trust in us by ranking the Al Rajhi Bank, number 15 globally and number one in MENA. We will continue to focus on execution and achieving our strategy goal for this year and beyond. Finally, we look forward to meeting you in the first quarter Earning Call. Thank you.