Conference Title: BSF Q3 Earnings Call

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Nida Iqbal Siddiqi: Good afternoon, everyone. Welcome to BSF's nine months 2024 results Earnings Call. Thank you for joining us today. I'm Nida Iqbal from Morgan Stanley Research and joined today by Mr. Bader Hamad AlSalloom, CEO of BSF. Mr. Ramzy Darwish, Chief Strategy and Finance Officer. Mr. Zuhair Mardam, Chief Treasury and Investment Officer. And Ms. Yasminah Abbas, Head of Investor Relations.

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With that, I would like to pass the call to Ms. Yasminah Abbas, Head of Investor Relations, for some introductory remarks.

Yasminah Abbas: Good afternoon, ladies and gentlemen, and welcome to BSF's Q3 2024 Earnings Call. I would like to thank you, Nida and the Morgan Stanley team, for hosting us today. Speaking first is BSF's CEO, Bader AlSalloom, who will go over the earnings summary for the quarter as well as give an update on the strategy execution. He is then followed by CSFO, Ramzy Darwish for a more detailed walkthrough of the financial performance, and then the platform will be open for Q&A through the raise hand or the type in question option.

Before I hand over the mic, I would like to note to the investor community that the 2023 ESG report has been published today, showcasing the strides BSF is taking into the ESG journey. And with that, I'll hand it over to Bader AlSalloom, our CEO.

Bader Hamad AlSalloom: Good afternoon, everyone. Thank you for joining our call today. I'm pleased to present our results for the third quarter of 2024. We delivered a resilient performance over the last nine months. The results were characterized by strong balance sheet momentum and improved credit quality, leading to profitability improvement despite headwinds on funding mix and costs. We also focused on executing our strategy with a technology upgrade as a key priority. Our rebranding, launched earlier this year, delivered strong results, boosting customer engagement across social media and our website. Brand awareness and equity have risen, and we've seen a clear increase in account opening and card issuances since the launch.

Let me take you through the key financial highlights for the first nine months of 2024. We achieved strong and balanced loan growth of 15% year-on-year, driven by a 15% increase in the commercial segment and 16% increase in consumer lending. Investments rose by 24% year-on-year, which helped us manage interest rate risk by increasing our fixed rate exposure in a high-yield environment. Deposits grew by 16% year-on-year, primarily due to interest-bearing deposits, reflecting the current rate environment. Operating income declined by 1%, mainly due to a 2% decrease in net interest income resulting from NIM contraction and higher funding costs. However, our non-interest income increased by 7% year-on-year, supporting our top line. Our bottom line grew by 1% as lower impairments more than offset rising expenses.

Next to asset quality, capital, and liquidity. We've seen further improvements in asset quality, with our NPL ratio decreasing to 0.83% and our coverage ratio improving to 193%. The cost of risk is at 57 basis points, with notable improvements in the commercial portfolio year-on-year. Our capital funding and liquidity positions remain strong, comfortably within regulatory limits, with a tier one ratio of 18.6% and an LCR of 162%. There has been an expected year-on-year decline in the non-interest bearing deposits ratio, although we've seen some improvement over the last quarter, bringing it to 46.7%.

Next, let's briefly review our strategic updates. Execution of our strategic plan continued well this quarter with an overall completion rate now at 75%, up from 72% last quarter. In wholesale banking, we achieved an 87% completion rate. Key advancements include an increase in our new-to-bank government customers, helped by refined account segmentation criteria. We've expanded our global reach in financial institutions, capturing business opportunities in, for example, Africa, Kuwait, Iraq, and Korea. Global Transactional Solutions also successfully launched three new trade finance products and enhanced its liquidity and cash management, operating model and talent pool.

In personal banking, our progress has risen to 63%. We've strengthened our collaboration with BSF capital to offer investment products and improved cross-sell framework with JB. The new digital app was launched and we initiated our branch network transformation project to improve efficiency in sales. And finally, we've successfully launched several new products, including Lombard lending for our upper affluent clients, new affluent credit card offerings, and an auto lease program with JB.

For private banking, I'm pleased to report that private banking has now fully completed its strategic refocus goals. This includes launching key offerings in partnership with BSF Capital and introducing tailored family products. We are now working on a new private banking strategy to further enhance our private banking offering and coverage by revamping our operating model.

JB continues to work on strategic initiatives with an 88% completion rate. As we mentioned before, JB is focused on its 2024 transformation plan, and good progress was made in modernizing its core systems, improving digital customer journeys, and optimizing mobile app services. At BSF Capital, our completion rate is now at 54%. We are advancing key partnerships and collaboration initiatives. Real estate advisory and solutions are also being strengthened in partnership with BSF private banking and our pipeline for real estate funds is developing well.

Now let's discuss our key advancements in technology infrastructure upgrade. For the Integrated Corporate Portal, ICP, we've rebase lined the implementation plan with a target go-live date for the first half of 2025. We conducted staff training on ICP during the third quarter, and expect to conclude testing for both back-end and front-end by the first quarter of 2025. Our omnichannel platform has successfully released features from release two and some enhancements are being tested for production release in the coming weeks. We anticipate the official public release and subsequent feature enhancements to start this quarter.

Significant strides were made in our core banking system. We've successfully kicked off the end-to-end process for both corporate lending and term deposits, with the design for retail term deposits completed and development currently at 70%. We anticipate launching corporate lending and limits, as well as corporate and retail term deposits by the end of next year or the beginning of 2026.

In summary, we made solid progress in our strategic initiatives this quarter, with an overall completion rate of 75%. Our focus on enhancing customer engagement and product offering has led to notable advancements across all segments. The successful launch of key products and ongoing upgrades to our technology infrastructure positions us well for future growth.

Now, I'll turn it over to our CSFO, Ramzy Darwish, who will share further insights into our financial performance. Ramzy, over to you.

Ramzy Darwish: Hey, everyone. Thank you, Bader. And thank you to all of you for joining us today. I'm pleased to be here to walk you through our financial results for the third quarter of 2024. We've achieved a solid and resilient financial performance, supported primarily by our efforts in driving asset growth and robust risk management practices. This quarter, despite certain challenges, particularly from margin compression and higher expenses related to our strategic initiatives, we've managed to achieve positive outcomes. These challenges have been partially mitigated through

strong fee income generation and lower impairment charges. This outcome is a testament to our careful planning and strategic focus.

Now, let's dive into the details, starting with the balance sheet overview on slide nine. First, on total assets, I'm pleased to report that our total assets have grown by an impressive 14% year-to-date. This growth is largely underpinned by a strong 12% increase in loans and advances, coupled with an 18% expansion in our investment portfolio. The strategy to balance both loan growth and strategic investments has paid off, helping us strengthen our financial position. This diversified approach means we're not solely relying on one area for growth, but are building a well-rounded portfolio that enhances our resilience.

On a sequential basis, assets remained relatively stable this quarter. This is primarily due to the deliberate redeployment of excess liquidity from interbank placements to loan growth, a shift that allows us to more proactively and effectively support customer demand while maintaining a prudent risk posture.

On the liability side, customer deposits grew by 12% year-on-year. This includes growth in both interest bearing as well as non-interest bearing deposits. It's particularly encouraging to see this growth as it demonstrates the trust and confidence our customers have in the bank. Additionally, we've been proactive in diversifying our funding sources through interbank placements and debt issuance markets, raising over $1 billion in the first nine months alone. This variety in funding ensures we're well-positioned to manage any potential liquidity needs.

Our equity base has also strengthened, increasing by 12% year-to-date. This has been mainly driven by retained earnings and favorable other comprehensive income movements from the investment portfolio. Furthermore, our capital base has been fortified with an additional tier one sukuk issuance of 3 billion riyals. This issuance supports our ongoing growth and prepares us for

a potential call of the existing tier one issuance next year. This aligns with our commitment to maintaining a strong capital structure that can support our future ambitions.

On the following slides for loans and advances, we've seen a robust 12% year-to-date increase in this area, covering both our corporate and retail portfolios. In commercial lending, we recorded a 12% growth. This reflects strong demand across key sectors like commerce, tracking, and utilities over the last nine months. This demand signals that the economy continues to be dynamic and that businesses are willing to invest, a positive indicator for future economic activity. Our team has been diligent in managing this growth, ensuring we focus on quality assets that align with our risk framework and contribute positively to our overall portfolio.

On a sequential basis, we took a more measured approach in commercial loan growth, coming in at 1.3% for the quarter. This reflects a more selective lending slant, which we communicated last quarter. By prioritizing strategic clients, we're positioning ourselves to ensure sustainable growth in the long run, balancing opportunity with prudence. On the retail side, consumer lending has grown by 14% year to date. This increase is fueled by strong demand across mortgages, personal loans, and auto loans. The continued expansion of our consumer offerings, particularly through our JB subsidiary, has played a significant role. With our focus on customer-centric products and digital accessibility, we're meeting the evolving needs of our clients and deepening our relationship with them.

On the next slide, our deposit base has expanded by 12% year to date. This growth has been primarily driven by interest bearing deposits, especially during the first half of the year. In the latter part of the quarter, however, we observed a strong uptick in non-interest bearing deposits. This shift illustrates not only our adaptability in response to changing market dynamics but also the confidence customers place in the bank as a trusted financial partner.

Overall, interest bearing deposits have grown by 13% year to date, while non-interest bearing deposits increased by 11%. This balance between different types of deposits is essential to our funding strategy, enabling us to manage our cost of funds effectively while supporting our lending activities and investment strategies. With this growth, we've enhanced our liquidity position, giving us the flexibility to navigate an evolving market landscape and capitalize on emerging opportunities.

It is worth noting that the inflow of non-interest bearing deposits in the third quarter was partly transitory and occurred toward the end of September, therefore did not have a significant impact on funding costs for the quarter. As a result, non-interest bearing deposits accounted for 46.7% of total deposits by the end of Q3. We expect this to moderate slightly in the fourth quarter as the balance normalizes.

On slide 12, now focusing on net income. For the first nine months of 2024, our net income increased by 1% year-on-year, driven by a 30% reduction in impairment charges. This was a notable achievement that reflects our commitment to prudent risk management. This improvement was partially offset by a rise in operating expenses as we continue to invest in growth and strategic initiatives. Although total operating income declined by 1% year-on-year, our non-interest income grew by 7%, which helped mitigate the 2% decline in net interest income. This performance in non-interest income underscores the diversity of our revenue streams, providing resilience even as we face margin pressures during the first half of the year.

On the next slide, for net interest income, we saw a 2% decline year-on-year due to tighter margins. Average interest earning assets rose by 16% over the period, helping to partially offset the margin pressure. The combination of higher cost funding and the rising rate environment impacted net interest income but our disciplined approach to balance sheet management helped alleviate some of that.

On slide 14, as expected, our net interest margin contracted by 57 basis points year-on-year, landing at 3.06% as of the first nine months of 2024. This shift was largely driven by higher cost funding pressures, which have affected margins. However, the recent increase in non-interest bearing deposits has not materially impacted the net interest margin. With the 50 basis points rate cut in September and an anticipated one or two further 25 basis point cuts by the end of the year, we expect an initial improvement in net interest margin. This is because funding costs typically adjust more quickly than asset yields, allowing us to capitalize on the rate environment in the short term.

On slide 15. On the topic of rate sensitivity, as we consider the long-term effect of these expected cuts, we continue to foresee minimal impact on our interest rate risk profile. Our strategy keeps us nearly neutral to changes in interest rates, thanks to the robust interest rate risk policy. While we are seeing a gradual reduction in cash flow hedge swaps, our investment portfolio remains strategically diversified with increased fixed rate assets, which will help us manage our interest rate risk more effectively.

Now on slide 16 for non-interest income. This category has contributed significantly to our top line growth this year, increasing by 7% year-on-year. This increase reflects strong performance in net fee and commission income along with investment related income. Drilling down a bit further, net fee and commissions grew by 8% year-on-year, driven largely by asset management income and an uptick in trade finance fees. Lower card fees partially offset this growth, but overall, the diversified sources of non-interest income continue to strengthen our revenue base.

Moving on to operating expenses on slide 17, which have increased by 12% year-on-year. This rise was driven primarily by three factors. First, employee costs rose by 10% year-on-year. This increase was due to a combination of factors annual salary increments, upskilling initiatives, and our commitment to future-proofing the workforce. These investments are essential for supporting

our long-term growth strategy and ensuring we have the right talent to navigate an evolving market landscape.

It's also important to note that growth in employee costs has started to moderate sequentially from a 12% year-on-year increase in the first half of the year to a 10% increase in the first nine months. This shift reflects our ongoing efforts to balance investment in talent alongside cost discipline.

Moving on to our G&A expenses. These were impacted by several non-recurring factors this quarter. These include an operational risk expense, a write-off of a previously capitalized expense, and a previous year tax adjustment. Collectively, these items comprise most of the quarter-over-quarter increase in G&A expenses. Additionally, depreciation expenses have risen largely due to our investments in technological infrastructure. This includes major projects the CEO has mentioned like the core banking system, ICP, and omnichannel platforms. These investments are essential for our long-term strategy to enhance operational efficiency as well as the customer experience.

As a result of the above factors, our cost-to-income ratio rose to 34.4%. While we do see some upward pressure on this ratio in the short term, we're committed to bringing it down to the 32%, 33% level over time. Achieving this target is a priority as we balance cost control with strategic investments. Due to this target, we are actively optimizing costs while continuing to invest in technology and operations. We expect volume growth to positively impact our net interest income and we're focusing on enhancing our fee income. Our strategy is about rationalizing expenses rather than cutting them. As we move into next year, we are confident in our ability to reverse this trend and improve the cost-to-income ratio.

Turning now to slide 18 on impairment charges. These have decreased by 30% year-on-year. This reduction reflects improved credit quality and effective risk management, particularly within the commercial lending portfolio. The cost of risk declined by 57 basis points for the first nine months

of 2024, driven by a reduction in commercial impairments and partially supported by lower consumer impairments. This is a direct result of our proactive approach to managing credit risk and our focus on maintaining a high-quality portfolio.

On non-performing loans on slide 19. Our NPL ratio improved to 83 basis points, down from 94 basis points in the last quarter. This improvement highlights the strength of our credit underwriting standards and our focus on asset quality. Additionally, NPL coverage increased to 193.1%. This was primarily driven by the upgrade of a corporate customer from non-performing to performing status. In combination with continued steady provisioning informed by our macroeconomic models, we are well prepared for potential future risks in the portfolio.

Moving to liquidity on slide 21. Our liquidity remains well above regulatory requirements. Specifically, we ended the quarter with a liquidity coverage ratio of 162% and a net stable funding ratio of 118%. These strong liquidity metrics reflect our prudent approach and provide a solid foundation for future growth. The loan-to-deposit ratio stood at a comfortable 81%, with the headline ratio at 104%. This balance supports our strategy in maintaining ample liquidity while also meeting customer needs.

On the next slide for capital ratios, we continue to remain strong on those ratios, with the tier one ratio increasing to 18.6% and the capital adequacy ratio rising to 19.4%. This increase was supported by the additional tier one sukuk issuance and favorable movements, as mentioned on the other comprehensive income for investments. Additionally, our cash flow hedge reserves have provided additional stability, enabling us to sustain capital strength and support ongoing growth initiatives. Furthermore, last week, the CMA approved BSF Capital increase of 12.9 billion by granting bonus shares to shareholders of around 1.07 shares for every existing share held. This increase will be through capitalization of 5 billion riyals from the statutory reserve and 7.9 billion from retained earnings.

Lastly, regarding the guidance. Based on current trends, we're maintaining our loan growth guidance in the mid-teens for the full year of 2024. We're mindful of our selective approach to corporate lending and are anticipating cyclical repayments towards the end of the year. This outlook reflects our confidence in balancing disciplined growth with prudent risk management as we move forward.

On net interest margin, we're maintaining guidance in a range of 3% to 3.15%. As of the end of the third quarter, our exit net interest margin stood at 298 basis points and we anticipate some initial relief on funding costs as rates continue to decline in the fourth quarter. This adjustment should help ease margin pressures and provide stability moving forward. In terms of the cost of risk, we expect it to remain stable within the range of 55 to 65 basis points by year-end. Our proactive approach to risk management has been instrumental in maintaining the stability, allowing us to navigate economic uncertainties with confidence.

Now, on our cost-to-income ratio guidance. As highlighted, we are revisiting this to around 34% from our previous target of less than 33%. This adjustment reflects the fact that cost optimization initiatives need time to materialize. Additionally, the non-recurring costs I mentioned earlier also impacted this metric. However, we remain optimistic that the cost-to-income ratio will start improving from the fourth quarter onwards as top line momentum and cost management efforts gain traction.

Moving to return on equity, we are also refining our guidance to around 11%, which is at the lower end of our previous range of 11% to 13%. This adjustment aligns with our aspirational target for next year and we remain committed to strengthening returns as we work through the current economic landscape. Lastly, we're aiming to bring our common equity tier one ratio closer to 16%, supported by retained earnings generation and favorable market dynamics. This target reflects our commitment to maintaining a strong capital base that can support future growth and shareholder value.

In closing, this quarter's results reflect our commitment to resilient, balanced growth achieved through disciplined risk management, strategic investments, and a relentless focus on efficiency. We've demonstrated our ability to navigate pressures from both margin and cost perspective, while ensuring a strong capital and liquidity position that supports future growth.

Looking ahead. While we remain vigilant about challenges in the economic environment, we are confident that our initiatives whether in managing costs, optimizing the balance sheet or driving non-interest income growth, position us well for sustainable success. Our selective approach to corporate lending and our targeted deposit strategies provide a foundation that supports both stability as well as expansion even as we adapt to changing market conditions. We are committed to delivering value to our shareholders by strengthening our core business, embracing operational efficiencies, and strategically positioning ourselves for the opportunities that lie ahead.

With that, that brings us to a close for the report and we can move on to Q&A.

Nida Iqbal Siddiqi: Thank you very much. Thank you to the BSF management for the detailed presentation and overview of the results. For our listeners, if you would like to ask a question, please raise your hand. Perhaps as we wait for questions, I can start with the first question from my side on margins. I see you're expecting 4Q margins to get positively impacted with rate cuts as deposits reprice faster than the asset side. How long do you think that benefit from rate cuts and the faster liability repricing continues for? Is it one quarter? Or do you think it could be longer than that?

And just linked to that for BSF in particular, of course, cost of funding has been a key headwind. So with rate cuts coming through, do you expect some of those pressures to ease? And do you see any indications or willingness on the deposit side from, let's say, retail deposits to shift into non-interest bearing as rates are lowered? Thank you.

Ramzy Darwish: Thank you for the question. Maybe I'll tackle that first and allow the treasurer to also add his feedback. So we mentioned at least initially, given the repricing that we have on assets typically for loans is let's say three to nine months. On average, you would say somewhere around six. Whereas for the liability side, it's much shorter. We're talking there between one to three months. So you'd see an immediate impact more on the liability side first and then on assets.

I would say primarily it would be gone within one quarter. But again, it depends on whether it's – if we have continued cuts going forward, then you would always have more and more adjustments to make. But I would say over a quarter to two with no more additional rate cuts, you would see that effect taken already.

On the cost of funding, I really don't see a significant change going forward, even with the rates being lower. I think it does depend on how low it goes in terms of the appetite, especially on the retail side. But I think given the advent of Islamic products for profit bearing deposits, I think the customer base has really gotten accustomed to that level of profit.

The question I'd really ask maybe is going forward, the growth in deposits is this going to continue at the same level of Casa as we are currently at, or will all new deposits continue as we've seen over the last two to three years, really come more in the form of time deposits and cost bearing liabilities? But I wouldn't see that cost pressure coming off, at least as of right now.

Nida Iqbal Siddiqi: Thank you. That's very clear. Our first question comes from the line of Shabbir Malik. Shabbir, I've just unmuted you. If you would like to go ahead and ask your question, please.

Shabbir Malik: Hi. Can you hear me?

Nida Iqbal Siddiqi: Yes.

Shabbir Malik: Great. Thank you for the presentation. I wanted to check with you regarding corporate tax for Saudi banks. What's the latest discussion there? Some of the regional banks with international operations have been talking about corporate tax from next year at about 15%. In Saudi Bank's case, the Saudi banks already pay zakat at least 10% in corporate tax on the proportion of earnings for foreigners at around 20%. So what's the discussion there on corporate tax? I think that's going to be – just curious about that.

My second question is about your subsidiary, JB. I just want to kind of understand what the strategy is with that business. In terms of the consumer segment, which segment is it targeting? What are the key products that it's offering? So some color on that would be pretty useful. And what are your longer-term aspirations with that? Any color on that would be very useful. Those are the two main questions, please. Thank you.

Ramzy Darwish: Thank you. Shabbir, I'll take the first question on the corporate tax. Unfortunately, I'm going to make it a very simple answer, but as of now, we don't have really an update as to any impending changes. So, so far as we know, it's no change until otherwise. So I honestly can't add too much more to that.

Bader Hamad AlSalloom: On the JB question, JB of course, originally, Saudi Fransi leasing was originally established as an auto leasing business. Recently, we have expanded into other products. Last year we rolled out personal finance loans and we are looking into rolling out further products in the future, potentially buy now, pay later, low limit credit cards, and others. And we have positioned JB as our mass segment consumer lending arm, which from time to time offloads some of its balance sheet onto BSF.

And especially now with our strategy focus with retail banking focusing mostly on the affluent segment, we positioned JB as our mass consumer lending segment, which then offloads to the

bank. Since the recent rebranding, we've had, of course, the pick up in business. We've also shifted into digital offering with the JB app, which we continue to, of course, enhance and expand and add features to.

Shabbir Malik: Great. So basically, it's targeting a different product, a customer base relative to what BSF would target, which would be more affluent and probably high net worth.

Bader Hamad AlSalloom: Correct. Yeah. BSF will continue, of course, to be dominantly a corporate bank also focusing on private and affluent banking with JB being our mass segment consumer lending arm. Now, of course, that does not mean that we will not be having any consumer lending within the bank itself. However, from a target audience focus, JB will be for more of the mass younger segments.

Shabbir Malik: Got it. And maybe in terms of the cost of risk you've got your guidance for this year is about 55 to 65 basis points. Considering your high NPL coverage levels, NPL formation is also quite subdued. Can this be lower potentially next year, cost of risk? Could this come down further?

Ramzy Darwish: I think it's a percentage. We're at the stage now analyzing that. I think when we look at the absolute minimum when we discuss stage one coverage or cost of risk, we're really looking at 40 basis points as the absolute minimum, notwithstanding any staging changes or recoveries. But it could presumably be lower. I'd say the caveat there is dependent on the model review that occurs on a regular basis taking into account macroeconomic factors. It could be on the positive side as well but also recoveries could change how this reacts as well.

Shabbir Malik: Thank you.

Nida Iqbal Siddiqi: If I may ask, just a follow-up question on the cost of risk. We've seen some recent developments in the sector regarding certain contracting companies. Are you able to comment on your exposure there and how you expect BSF to be impacted?

Bader Hamad AlSalloom: Sorry. Is this specifically regarding the recently announced contractor or in general?

Nida Iqbal Siddiqi: Yes.

Bader Hamad AlSalloom: On the recently contractor, of course, when it comes to BSF, we can't really comment given that we were not participants in the recently announced agreement given our insignificant small unfunded exposure to that specific contractor. So we really can't comment on that one. However, we do see this development as a very positive development for both the contractor and the banks with the uncertainty definitely reduced and with good ripple effects as, of course, this contractor is in a much better position to reactivate its activities at a time where there are many opportunities that they can participate in. And especially given that it's a time where lots of contractors are in need, of course, to execute the ongoing vision 2030, the Giga and Mega projects.

Nida Iqbal Siddiqi: Understood. Thank you very much. Our next question comes from the line of Olga Veselova. Olga, I've just unmuted you. If you would like to go ahead and ask your question.

Olga Veselova: Thank you, Nida. And thank you very much for hosting this presentation. I have several questions. One is big picture question. What is the strategy for the bank going forward? So what do you think will be your balance between volumes expansion versus margins protection? Which segments do you find appealing, especially in the corporate book? And do I understand correctly that you are gradually reducing the usage of interest rate hedges versus history? So this is my first question.

My second question is on provisioning. In your ECL models, the provisioning models, what are the top three, four macro parameters, which drive provision charges or releases? Is it budget expenditures? Is it oil price? So it would be great to understand that. And my third question is what part of your new lending now could be classified as Giga project related lending? Thank you.

Ramzy Darwish: Thank you, Olga, for the questions. Maybe I'll start with the first one and allow the CEO to add on to that. But in terms of strategy between the balance of, let's say, balance sheet growth and margin protection, I think we have highlighted that we do want to focus on return on equity. And so long as the business is profitable and it is accretive to ROE, we would continue wanting to grow. I think there's still plenty of opportunities across really all the business lines that we have. I'd say more notably now we see quite significant growth for a growth opportunity for JB, for BSF capital.

But alongside that within retail with lower interest rates, also much bigger potential and corporate, I think continuing the progress we've seen over the last few years in terms of growth giving plenty of opportunities. I think also, again, plenty of opportunities gives us the option to be more selective, focusing again on those strategic clients where it's not only the funded business and we can really focus on the full customer value relationship there. So both interest income, non-interest income focus across the board.

For the second question, in terms of hedges declining, the way we're looking at this is really from an interest rate risk perspective. So the IRB Basel regulations and really our positioning that we want to be in going into a lower rate environment. I think there are multiple options in terms of being able to hedge the interest rate risk. The cash flow hedge was one of the most important at the time. But more recently, you've seen the investment book, which is also fixed rate growing quite significantly over the last year, including year to date.

And then the third item would be retail assets, which are predominantly fixed rate as well, giving us additional exposure to hedge the balance sheet from an interest rate risk perspective. These three combined alongside the balance sheet position on the liability side have brought us to a more neutral position on interest rate risk.

For the other question on the ECL model. The two main factors that we look at are oil price and GDP. And lastly, I think on the fourth question, in terms of new lending opportunities, I'll let the CEO answer.

Bader Hamad AlSalloom: If I understood your question correctly, it was regarding our exposure to the Giga and Mega projects. Is that correct?

Olga Veselova: Yes, correct. Thank you.

Bader Hamad AlSalloom: Okay. Yes. So of course, being a corporate bank, by nature, we are exposed both directly and indirectly to the Giga and Mega projects. I would say when it comes to direct exposure to these Giga and Mega projects, they're relatively on the lower side. They're actually in the single-digit percentage wise. However, when it comes to indirect, obviously, given that these Giga and Mega projects continue to be the main driver when it comes to corporate credit growth. We do have indirect exposure to these projects.

However, that being said, we continue to maintain a well-diversified corporate loan portfolio when it comes to sectors. Maybe the one sector that did witness some growth compared to others is the contracting sector, unsurprisingly. And that being said, also given that we are more focused and specialized in project finance, I can say that within the project finance space, it is roughly around 20% of our corporate lending, which of course includes some Giga and Mega projects and some other projects within the vision 2030.

Olga Veselova: Perfect. Thank you.

Nida Iqbal Siddiqi: Our next question comes from the line of Naresh Bilandani. Naresh, please go ahead and ask your question.

Naresh Bilandani: Thank you. Hi. Can you hear me? Hi. Can you hear me?

Nida Iqbal Siddiqi: Yes, we can hear you.

Naresh Bilandani: Excellent. Hi, Bader and Ramzy. Thank you very much for the call. It's Naresh Bilandani from JP Morgan. Three questions, please. So first, the way the NII has trended, it seems like we're likely to end up having a flat NII growth this year for the franchise. Now, do you reckon that even with a few cuts, you could end up having a positive NII growth in 2025? Or the funding cost pressures as they persist across the system, you could expect the worst trend to continue? That's the first question. So thoughts on the NII growth next year if that can improve compared to the flat this year?

My second question is just could you please elaborate further on the OPEX that seems to be trending still worse than your expectations? Could you just highlight what areas the negative pressures are coming through compared to your previous expectations? And what strategy do you have at this place to reduce these pressures going forward? That's the second question on OPEX.

And my third and final question is, so overnight, this news on NDMC arranging a syndicated loan of 23 billion Saar for the Ministry of Finance of Saudi Arabia, along with Saudi and international banks. I mean, with this being related to Saudi Binladin transaction, I'm just keen to understand the structure of this transaction better and the implication that it can have for the industry as a whole.

Now, I know this is positive for the health of the contractor, so I'm just keen to understand the implications this could have from a bank's perspective with regards to liquidity or the capital relief. And just to understand the structure of this transaction better. So any color that you can provide there would be super helpful. Thank you.

Ramzy Darwish: Thank you, Naresh, for the questions. I'll start with the first one on net interest income. I think we do continue to see more or less the same for the rest of this year in terms of being flat positive potential. I think, again, the rate cuts and when and how they occur are one key driver. But at the same time, I think the biggest caveat BSF and other banks face is the ability to generate non-interest bearing deposits as well to support some of this growth. So I would say, given where we see things stand currently, probably more or less the same as previous quarters with a flat net interest income for the year.

With regards to OPEX, again, there has been some actions really across the board. I think with staff we've seen this sequential decline in the growth that was witnessed in the earlier half of the year. For other items, including G&A, there were some one-offs mentioned that occurred in the third quarter. Some of these, like operational risk, I think can occur obviously throughout the year, but in one individual quarter, it can be sizable in percentage terms.

But the other two items we highlighted was the capitalization of an existing asset where we had written down some of that value. In addition, I think on the positive side for this expenditure is really to support some of the transformation across the board in particularly more in the technology and operations areas. And add on to that would be in the subsidiaries where to support the significant growth we've seen on the revenue side, there have been additional costs allocated. So those are the three elements that have really driven up OPEX. But again, I think we want to try to balance as much as possible rationalize and not necessarily cut.

Naresh Bilandani: Okay. Ramzy, I'm sorry. Before we go to the Binladin question, could you please like, just once again, my question for the NII growth? And thanks for providing the color for the rest of the year. But my question was more on going into 2025. I think it's kind of given that it's more or less now going to be flattish this year. 2025, do you expect growth in any material manner from the current trend or the funding cost pressures persist and the asset growth that you have booked does not like yield sufficiently to mitigate those pressures? And I could still be sluggish. Is that a fair reality, or am I being too conservative here in the thought process?

Ramzy Darwish: Yeah. Apologies, Naresh. I misunderstood. I think we're going to be providing guidance on this the upcoming quarter. But if I look at the impact first from rate cuts and the fact that at least from BSF's perspective, we are, for a great part, neutral all else equal in terms of keeping the balance sheet stable. With additional loan growth, we would expect to see NII grow. So I would say it's more positive in terms of expectations.

Naresh Bilandani: Understood. All right. Thank you, Ramzy. That's good color. Thank you.

Bader Hamad AlSalloom: Yes. And on the question regarding the recent development or announcement regarding the large contractor. Again, given that BSF was not a participant in this agreement given our insignificant exposure to this client, we really can't comment on the mechanics of the agreement and its impact on banks. However, as a general comment on the situation, we continue to see this development as a very positive development for this specific contractor, the contracting sector in general, and of course, the banks going forward.

Naresh Bilandani: Okay, Bader. Thank you. Thanks, Ramzy, for your request. Thank you.

Ramzy Darwish: Thank you.

Nida Iqbal Siddiqi: Thank you for that. If I just may, if I could ask a follow-up on the NII and the nearly neutral sensitivity to rate cuts? I guess, of course, this is based on a static point in time. What do you think is the key risk factor to this neutral rate sensitivity? Under what scenario, what are the moving parts that could result in a negative sensitivity to rate cuts?

Zuhair Mardam: Yeah, thanks for the question. So as we speak, we're closer to neutrality and we do realize that the outlook is based on a one-year outlook when it comes to, let's say NIM sensitivity. However, the risk is typically in terms of where does the cycle end? As of today, the market is pricing in a terminal rate of 3.5%. Should this go further, we would, let's say, be more neutral on interest rate let's say volatility. However, should the interest rate of fed fund turn and the outlook remains, let's say pricing in what's going on in the longer end of the curve and inflation goes up? This could be potentially limited risk to the upside in terms of how we could view this.

I would also highlight that we're studying it for next year. And at one point of time, we would like to re-shorten our interest rate risk duration as interest rates, let's say stabilize and you have a normalized interest rate risk environment. But this is, as we speak, it's within the study period for next year.

Nida Iqbal Siddiqi: Understood. Thank you very much. Our next question comes from the line of Murad Ansari. Murad, please go ahead and ask your question.

Murad Ansari: Thank you. Good afternoon, everyone, and thanks for the presentation. I had a question around the loan growth outlook. So if I heard this correctly, you were mentioning that there are some cyclical repayments that you expect in the fourth quarter? But given your mid-teen guidance that would still suggest about roughly 3 to 4 billion riyal expansion in the loan book. So I just wanted to get your thoughts on that. Is the way I'm looking at it, is this correct? And this 3, 4 billion kind of expansion is broadly in line with what you've seen sequentially in the third quarter, so doesn't really have a big impact in terms of sequential growth if there are cyclical repayments.

And secondly, on the loan growth, I mean, consumer growth book has been quite impressive. It's actually year-to-date stronger than what your corporate loan book has grown by. And part of it is obviously mortgages that have been a good story for BSF. How do you see the consumer growth story evolving as rate cuts come through? And are you seeing some pick-up on personal loans or non-mortgage consumer loans come through? Is that appetite building up?

Then secondly on the rate environment. So just wanted your thoughts on how the competitive environment is on loan pricing. Is there opportunity to kind of stabilize the loan pricing or there are still pressures on margins over there? And if you could probably comment on the interbank rates. What we've seen is that ahead of the rate cut we saw cyber coming off, we've seen at one point cyber falling down to about 5.6, but we've seen a slight pickup over the last few weeks. So just your thoughts, if you could maybe shed some light on what you're seeing on the interbank rate evolving.

And last question I had was on the investment book. So I'm looking at your split of the loan book and almost 90% of your loan book is either for OCI or amortized costs or fair to assume that whatever. If there are rate fluctuations and we see further reductions, none of that should be coming through the P&L in terms of mark to market gains, if there are any. So it's only flowing through either your top line in terms of interest income or if you choose to realize any gains. And maybe on that also, how do you see further build-up in the investment book? We've seen quite a strong growth over the last, let's say, 12, 18 months. Is the size now comfortable or we'll continue to see steady growth into next year as well? Thank you.

Bader Hamad AlSalloom: Sure. I'll start with maybe answering the first question regarding the loan growth before I hand it over to my colleagues for the other questions. We do expect that loan growth in Q4 to be more in line with Q3, especially when compared to the first half of the year, and hence why we're sticking to our guidance to unchanged when it comes to that loan growth. And

we do expect to land at the end of the year, again, with the fourth quarter more in line with the third quarter when it comes to growth. Again, more selective when it comes to asset growth and more focus on returning profitability and spreads when it comes to that loan growth, especially after the rapid growth in the first half of the year.

On the consumer lending, it has been a positive momentum on both mortgages, personal loans, and auto loans actually, which witnessed the biggest jump. For us, auto loans actually witnessed a jump of 23% compared to last year with, of course, personal loans and mortgages in the range of 12%. We do expect that growth to continue with the current interest rate environment and expected rate cuts coming through. And of course, through the implementation of our strategy when it comes to focusing on affluent, more specifically for consumer lending within the bank itself and again, relying on JB for more of the mass segment and more specifically the authorities.

Zuhair Mardam: On the cyber question. So we have seen an uptick. That's true. The credit remains stronger than the deposit base across the sector. Moreover, that three months today would go into next year's maturity. So banks are positioning themselves to cover their liabilities through the return. Hence, we have seen that little uptick. We expect that obviously to continue going down as the Fed cuts their fed funds rates going forward.

With regards to OCI, we have seen an improvement growth in our OCI driven by the drop in interest rates, so the longer end of the curve. That will be recycled into P&L on accrual basis. The decision on whether to take gains or not, these will happen strategically as per the decision on where we are in the cycle.

Murad Ansari: Just a quick one. I mean, you've seen your other reserves swing from negative to positive in the last quarter, obviously largely helped, I'm assuming by the rate cuts. How much capital support can you see on the tier two ratios coming in from that? I mean this could be significant given the size of your book if rate cuts continue.

Zuhair Mardam: Yeah. Typically, the longer end of the curve has already pricing in those cuts. So as we decay, that will translate into P&L on interest income. So I would say that I wouldn't see too much movement in OCI since the market is pricing in several cuts with a terminal rate of 3.5 in two years' time. So should the market price in further cuts, we would expect a further increase or improvement in OCI. But until then, I think is well-priced in.

Murad Ansari: All right. Thank you so much.

Zuhair Mardam: Thank you.

Nida Iqbal Siddiqi: Thank you very much. That brings us to the end of our Q&A for today. I will now pass on to management for closing remarks.

Bader Hamad AlSalloom: Thank you very much, everyone. Thank you for joining us today and your continued support. We're pleased with the growth momentum and the progress made on our strategic initiatives and the opportunities ahead. Thank you for your time today and we appreciate your continued support and engagement. Thank you.