Transcription

Title: Wema Bank FY 2016 Investor and Analyst Conference Call

Date: 07.04.2017

Speakers: Ademola Adebise and Tunde Mabawonku

Presentation

Operator

Hello and thank you very much for joining today's Wema Bank Full-Year 2016 Investor and Analyst Conference Call. Throughout this, all participants will be in listen-only mode, and afterwards there'll be a question-and-answer session. And just to remind you, this is being recorded. Today I'm pleased to present Ademola Adebise. Please begin.

Ademola Adebise

Good afternoon, ladies and gentlemen. Welcome to Wema Bank's conference call to review the financial performance for 2016. My name is Ademola Adebise; I'm the Deputy Managing Director. With me today I have Mr Tunde Mabawonku, who is the Chief Finance Officer; Mr Sylvanus Eneche, who is the Chief Risk Officer. Our presentation is going to be in three segments. We're going to look at the business and operating highlights. I will take that. We're then going to go into a deep dive into the financial performance, the facts behind the figures, and that will be taken by Tunde. And then I'll come back to review the outlook for 2017 and the strategy of the Bank.

Please turn to slide 4. We continue to record improvements in our retail – implementation of our retail strategy. That can be seen very clearly here. The Bank recorded an 18% growth in gross earnings in 2016, despite the headwinds and the – all the headwinds in the economy in 2016 and the various downgrades of ratings. Wema Bank was able to maintain its credit rating from GCR and Fitch ratings with a stable investment grade. Also in alternate channels, we've continued to push on those frontiers: ATMs, POS, branch network, and also the channels – the – what we call the unstructured supplementary service data, USSD channel. And we've continued to push on these frontiers, and we are recording appreciable progress. We'll go into more details as we go into the presentation.

On branch network, we have since the – since we got the national license, we have moved into other areas in the north – other regions that we were not present. We've opened Minna and Lokoja branches in the north. We opened three branches in Lagos. Abuja, we opened one branch, and then Port Harcourt, we opened one branch. Just a few days ago, we opened our Kaduna branch, and as we speak we have Aba, Enugu, Kano and Bauchi branches going under development. In terms of service delivery, we have improved our service ratings, based on the KPMG ratings for 2016. We moved from number 19 to number 13 in terms of service rating, and our target for this year is to move to number 10 or below. And the big one for us, really – it's around the ALAT digital bank that we are working on. This will be launched very, very shortly, in May. Basically we embarked on a review of our retail strategy last year, working with one of the big four. And we have moved – since moved into the implementation stage. And as I speak today we are in beta testing for the ALAT digital bank. This will be launched in May. It promises to be a very exciting bank; the first fully digital bank in Nigeria.

Please turn to slide 5. On the global scene, the presidency of Mr Donald Trump in the US and the Brexit have created a new world order for anti-establishment movements, and we believe that this will have great impact on the way things are ordered in the economy going forward. A number of trade agreements will also be reworked, and a number of realignments will have to happen. And this will definitely have impact on the way business is done, and on Wema Bank as a bank. On the – in terms of oil prices, we recorded – we've seen some oil recovery after the cutback by OPEC and non-OPEC members by 1.8 million barrels per day. And this hopefully will be – continue to see some stability and – in the oil price. Illiquidity continues to characterise the market locally, due to lack of FX. Also, the delay in implementation of the budget, the low oil prices, the incidents and disruption in the Niger delta has also continued to affect Government revenue. And, of course, during the year, the Government slid into recession. Also, we observed that the monetary and fiscal policies of the central bank – there were divergence in the monetary and fiscal policy, and this continued to affect the economy. Disposable income was impacted, based on the rise in inflation and of course the Governments' – the state Governments' inability to pay salaries on time.

Let's now move into the commitments we made, slide 6. We made some commitments in 2016, and – along five key, broad objectives. Basically, to grow the franchise; to enhance asset quality and capital; to improve efficiency; also improve organisational capacity; and to continue to push hard on the alternate channels. On growing the franchise, as I said earlier, we opened a number of branches. And we're quite pleased, and we're quite on course in terms of our branch opening. As I said, we would not – we will not – it is not going to be a continuous exercise, but what we'll do is open in locations where there are really opportunities for business. On deposits, despite the slight dip in our deposits by 0.58%, you can see a massive improvement in the retail deposits, moving by 18.9% from 89 billion in 2015 to 106 billion. This is a testament to all the activities we have put in place. Basically, partnerships with telcos, and agency and mobile banking. This is – you can see the outcome. In Nigeria, we are reckoned with as one of the foremost and forward-looking banks in terms of the use of technology. We have a very robust technology platform, as you see. And of course I'll talk a little bit more about that as we move on.

In terms of asset enhancement, asset quality and capital, we fully repaid the 50 billion loan – tier 2 loan, and we've also successfully tried to raise, to replace this – we raised about 6.2 billion in Q3 of 2016. We hope to continue with this exercise. As we speak, we have engaged advisers, and we're looking to raise another tranche of a 50 billion programme that we got approval for last year.

In terms of improving efficiency, despite the inflation rate that closed at about 18.6%, OPEX – operating expense – rose by 5.6% in 2016. We could not achieve the target of 75 to 80% in terms of cost to income ratio. We closed at about 88%. Despite this, we believe that this was still below the inflation rates. Net interest margins shrunk to 5.93% because of the huge cost of funds. As you know, rates went quite high during the year. As we speak, a Treasury bill is the – over in the range of 18, 19%.

In terms of organizational capacity, well, we were able to improve our service rating, as I said earlier, from 19 to 13 based on the KPMG survey. We expect that this year we will – we should – to be one of the top 10 in terms of service. In terms of alternate channels, we – deployment of ATMs continues to increase, by 17%, POS by another 17%. Number of active cards increased by 26%. We had an alliance with Etisalat, and this is for the introduction of our Wema Easy Savers Account, and this is making a lot of progress in the market. As I said, we also have another channel called the USSD channel. And we are – the traction on the channel is quite impressive because of the ease of use. We also have another product that we pushed out to our merchants. Today we have about 300 merchants, and this is called the mCash.

Based on all these achievements, we can see the impact on it. Go to slide 7. The impact on our income statement – growth in gross earnings of 18% –18.48%, growth of 7.5% in PBT, profits after tax of 11.16%. We believe that this is some progress that we're making, and we believe that there's still a lot of work to do, and we are not relenting on this oars. And we'll continue to push very hard to ensure that we deliver shareholder value.

At this point, I will now hand over to Tunde, the CFO, to do a deep dive into the financials; to give us the facts behind these figures. Tunde.

Tunde Mabawonku

Okay. Thank you very much, Mr Adebise. Good afternoon. My name is Tunde Mabawonku, the Bank's Chief Finance Officer. What I'm going to do in the next couple of minutes is to walk you through some more insights into the financial statements of the Bank. Please can we all go to slide number 9, the financial highlights? Largely, in this slide is to first of all share with you the context in which we operated, and then go – do a deep dive into the numbers.

I think firstly is to acknowledge, indeed, the poor macroeconomic performance in 2016, and that had implications for the banking industry in general and for Wema Bank in particular. A number of key points on this slide. Firstly, we had additional provisioning on our loan assets during the year, which, like I said, is a reflection of what happened within the economy. NPL moved up from 2.67 to the regulatory threshold of 5.07%. And what happened was, largely because the Bank was well protected, impairment charges was almost largely minimal. But, as you see, the impact on capital adequacy – capital adequacy dropped from 15% to 11% on the back of two things. Firstly, the Bank fully repaid an outstanding 50 billion tier 2 capital that the Bank took a couple of years ago. And then secondly was the impact of the changes in the regulatory risk result, driven by the additional provisioning. But despite these headwinds in terms of NPL, in terms of slightly lower CAR, in terms of slightly tighter margins, the Bank was still able to deliver PBT numbers stronger than the year before. PBT moved up from 2.99 billion to 3.28 billion. PAT also moved up to 2.59 billion from 2.27 billion the previous year. So largely in summary for this slide 9, two things will come out. Firstly, the macroeconomic environment had some slight impact on our performance. But despite this, the Bank ensured some consistency of performance, and we came up with slightly robust PBT numbers.

As we go through the slides, I will shed more light on the details of the financials. If we move to slide 10 – and I think this starts first by telling the story of the consistency of earnings, despite the negative performance in the economy. Slide 10 speaks to the earnings trend of the Bank. You can see the growth in earnings, comparing annual growth rates, of 11%. Largely, the bulk of the Bank's earnings comes from interest income – interest income on loans and advances, and interest income on money-market instruments. That continues to grow strongly, obviously on the back of loan growth and on the back of improved yield on some assets. But the other interesting story really is improvement in non-interest income. And that has been driven by a number of initiatives, like the DMD mentioned earlier. We've seen phenomenal growth on the USSD platform, and that has helped non-interest income. The partnerships at the retail end of the market, in terms of account opening, in terms of mobile banking, has also impacted and improved on non-interest income. So as we go forward you see – we shed some more colour on this. But for Wema Bank, largely that a lot more emphasis is also being place on fee-based income going forward.

Slide 11 talks on efficiency. Largely, throughout the year, inflation averaged 17, 18%. But on the back of this, the Bank was able to manage its operating expense growth to 6.73%. Still not where we wanted it to be – we didn't expect OPEX to grow more than 5% – but largely a number of inflationary elements. Cost of transportation, cost of power, cost of energy. And also the exchange rate impacted on cost of doing business. Our cost to income ratio is at 88.32%, still quite high, but if you look at the trend, you see coming down from a high of 142 a couple of years ago. What we've done is, first and foremost, keep a lid on costs, manager our controllable costs and then continue to grow top-line earnings. And as we grow top-line earnings in the following years, we'll start seeing cost to income ratio continue to push down.

Slide 12 really talks about the margins. Like we mentioned earlier, margins moved – net interest margins moved from 6.92 to 6.56%, slightly below our guidance of 7%, but on the back of two things. What happened was there were pressures on cost of funds during the year, as we noted that deposit customers reprice faster than our ability to transfer the rise in rates to lending customers. So we saw a higher cost of funds in the year, compared to the previous year. Yes, some of the gains were moved on in terms of higher yield on assets, but there's also a threshold in which you have to manage your interest rate so that it also doesn't become a disincentive to loan payback. Margins at 6.56% still continues to give the Bank some decent level of profitability.

Talking of profitability, if we move to slide 13 it shows the PBT trend in the last couple of years. And again, what strikes out is the consistency in earnings, despite the economic outlook. 3.09 billion, 3.05 billion and 3.28 billion in PBT year on year. Like I mentioned earlier, there are pressures on cost of funds, and this impacted on the margins that we thought we could achieve, but we were able to largely offset that by improvement in fee income and improvement in income from alternative channels. The cost management initiatives that we deployed helped the Bank to manage the rate of growth in cost, and we expect to see a lot more of that in subsequent years. So slide 13 largely does show the PBT trend in the last couple of years.

Moving on to some further breakdown of the Bank's deposit liabilities, we go to slide 14. What this slide show is in three sections. Firstly it shows the trend in deposits. From 175 billion in 2012, we've moved to a high of 284, and now at 283 billion in deposits. So largely those liabilities remained flat during the year. The deposit mix improved slightly. We gave an assurance that we'd do at least 50/50; 50 low-cost funding and 50 in priced deposits. Unfortunately, we were not able to achieve that. What happened was really the impact of the high interest rates, the crowding out – what we call crowding out nature of Government instruments on the pricing of our deposits. So we saw a lot more customers increasingly – getting increasingly sophisticated and demanding pricing that was related to pricing of Government securities. But despite that, we still improved on savings volume, and we improved on deposit volumes from the retail end of the market. What we did was, while we worked with the corporate customers, we also did a lot of market storms, campus storms, to opening up more serious accounts and a lot more retail and SME accounts. So you can see the mix. Commercial and SME accounted for 68% of the deposits of the Bank, and a lot of this is largely SME; the small traders, that keep balances within – keep balances in the Bank. Our expectation for rates eventually is in 2017, the second half of the year, that rates will begin to moderate. And as we see that moderate, we expect to see a reduction in cost of funds of the Bank.

What we've done in slide 15 is to give you a lot more colour on the loan book of the Bank, to show the growth year on year, to show the mix in terms of business segment. And it also gives you some insight in the NPL numbers. Slide 15, the left-hand side shows the loan breakdown in terms of naira. On the right, it shows the loan breakdown in terms of percentages. And what you can see is a fairly diversified loan book, no sector accounting for up to 20% of the loan portfolio. The ones that will come out striking is oil and gas; oil and gas at 18%, and this is largely – 90% of this is largely downstream trading. The Bank's exposure to upstream is less than 4% of its loan book. The Bank's exposure to foreign currency loans is also around 6% of its loan book, so 94% of the Bank's loan book is naira-denominated. So a number of the headwinds that happened in terms of devaluation did not impact on the Bank's loan book.

The next slide, slide 16, just gives you more colour on the NPLs of the bank. NPLs went up to 5.07%, largely, as you can see here, some increase in NPLs in certain sectors – general and general commerce, and some other sectors. But what we've done is really largely to, working with regulators, take a more conservative approach. But good enough, like I mentioned earlier, if the increase in NPL did not result in a significant increase in impairment, but a significant chunk of these loans had good collateral and good coverage. So what happened was there was a shift in regulatory risk result, but impairments remained relatively low. NPLs closed at 5.07%, which, from what we see, is still lower than the industry average of 14. We have the regulatory threshold of 5, but still lower than the – what we expect of the industry average of 14%.

Slide 17 just talks on funding of the Bank; both the short-term funding and the long-term funding. The first – the left-hand side shows the liquidity ratio. The right-hand side shows the mix in terms of funding, largely from customer deposits at 67%. Our capital adequacy ratio closed at 11.07%, still above the 10% mark for a commercial bank with national authorisation. Liquidity also remained above the threshold at 30.03%. What has happened, like I mentioned earlier, was that CAR dipped on the back of two things. Firstly was the full repayment of the 50 billion tier 2 capital. We raised additional funds of 6.25 billion, but largely we tried to moderate the amount we raised, given the high interest rate regime at the second half of the year. But we will be going back to the market later this year, when we think rates will have moderated to raise an – to raise additional tier 2 capital. But what we see was 11.07% CAR. By the time additional funds come in, we see capital adequacy ratio going back up to 14.5, 15% mark.

Slide 18 just shows a summary of the balance sheet. Growth from 396 billion the previous year to 421 billion naira in 2016. The balance sheet, as is typical of a commercial deposit money bank, remains funded from deposits from customers. The added assets also a mix of loans and advances and money-market instruments.

On slide 19 talks largely about managing risk. And if you recall, on the last conference call we spent a lot of time on risk and risk management initiatives. At the last conference call, we made mention of the fact that technology risk was – had become a major risk within the industry, and the Bank went ahead to appoint a Chief Information Security Officer, largely to work with the Bank; introduce best practices as regards managing technology risks. But despite that, there still are the risk and other headwinds. Risk on credit risk, risk on foreign exchange. In fact, a new terminology – regulatory risk – has also come on board. And really, for a commercial bank, our ability to manage risk, you can see that reflected in NPL numbers and in the growth numbers of the Bank. But one of the other things we've done is improved automation and improved forecasting capabilities, because all of this are necessary on the back of the implementation of IFRS9. Going forward, we continue to manage risk and put forecasting at the heart of what we do.

Lastly, on slide 20, this just shows the summary of the performance indices of the Bank. NIMs at 6.56%. Loan to deposits are 70%. The coverage ratio on non-performing loans dipped slightly, but still at the 100% mark. Our ROE numbers, what I'll say is that they are still work in progress, but in the last five years, as you can see here, there has been some consistency in the numbers in terms of return, in terms of margins and in terms of growth of the Bank. So to summarise the financial performance, four critical things. First and foremost, consistency in performance, despite the headwinds. Yes, secondly, we were slightly impacted by the macroeconomic performance in the last couple of years, but you can see that the Bank largely mitigated this on the back of relatively good profit-before-tax numbers. Capital adequacy ratio, we're already dealing with that by putting in place additional plans to raise capital. Right now, we are 11%. By the time the tier 2 kicks in, we will be back again to between 14 and 15%. And then, as we give – we will give you more guidance on plans to raise tier 1 capital subsequently. And largely – lastly for us, we've seen a lot of traction on fee-based income from alternate channels – from digital channels. And that we intend to focus on a lot in 2017 financial year.

On the back of this, I will hand over to Mr Adebise, the Deputy Managing Director, to continue with the outlook and guidance. Thank you very much.

Ademola Adebise

Thank you, Tunde. Please switch to slide 22. On the – we talk about the outlook for 2017. On the global economy, we expect that the impact of the Brexit and the new – and the leadership in the US will continue to shift the way economies have a base on the rising need for – rising threat of the nationalism – you know, communal. We also believe that this will – the negotiations of the Brexit and – will bring about so many things. We already hear the Scottish asking for a referendum. So a number of things will happen. This will lead to new trade agreements and partnerships. We also believe that oil prices will mainly be volatile to low, resulting from the increase – the outlook from the US. The Fed funds; they've increased rates once. We believe that they're going to increase rates again. Of course, this will continue to impact the value of the dollar and the weakening Chinese demand.

On the domestic front, the budget is yet to be passed. Of course, we all know that. We were a bit optimistic that, hopefully by Q3, Nigeria should begin to turn the corner in terms of the recession that we're in. We also believe that, with the introduction of the economic recovery and growth plan, things will begin to take shape. However, the 2019 elections – those are round the corner – will be some challenge to this. We believe that inflation should moderate as we move on in the year and as we begin to see some stability in the FX market. Analysts are of the view that the sustainability of this from the Central Bank is still of some concern. We believe that the money and fixed income markets will continue to remain stable for investors, considering the downward trends in the current equity markets.

For us as a bank, we'll continue to push very hard on the implementation of our strategy – our retail strategy. However, this is going to be on the three pillars that we call three Es: expertise, excellence, efficiency. Expertise from the point of view of ensuring that we manage the quality of our assets. We ensure that the Bank is adequately capitalised. We stay very close to our customer. We leverage technology to ensure that we push, and we also push our alternate channels. We hope that with this, and also on the excellence side, I think we want to continue to stay very close to our customers. And as I said, value propositions with partnerships. As I speak, a lot more partnerships are being signed after the Etisalat engagement, and all this will be on the build as we move on in the year. In terms of efficiency, as I said, we will continue to do more with less, you know, trying to ensure that we eliminate wastages and ensure that we are – our processes are more efficient, and then our cost performance. We will push very hard, and on the back of all this is the fact that we're going to be very well – pushing very hard on the digital – in the digital space. As I said earlier on, we are going to be launching a truly digital bank in May, and this is going to be the first fully digital bank in Nigeria and in Africa. We started this joint last – January last year, and we are very, very excited with what we have. We believe it's going to be a game-changer in the industry, and some disruption is going to happen. Just watch out. We believe that, with this, we will be able to continue to push hard on the retail space – our retail numbers.

And if we go to slide 24, where we give some guidance. Yes, we believe that, with all these efforts, we will be able to push our deposits – grow deposits by at least 10%, with retail penetration recording an increase of 10%. We expect that we will have probably flat loan growth, trying to be a bit more efficient and nimble. Probably call back and recall some of our loans. And at the end of the day, we believe that the bottom line should be looking much better. We expect that, at the end of the day, our net interest margin should improve from about 5.9% to between 6.5 to 7%. This – these are the things that we're doing, and we're committed to this.

On the corporate governance side, the board is stable, and a number of things are happening and showing that we – gender diversity and all the other issues around sustainability, we're ensuring that we have diversity. For us, 2017 is going to be – we're going to approach it a bit more cautiously, as I said based on the guidance, and we'll ensure that by the end of the year we should have delivered on a number of our objectives. On this note, I want to thank you for joining us on this conference call, and we'll now invite questions from you. Thank you very much.

Q&A

Operator
Hello. So we have a question here from Michael Akinyemi. Please go ahead with your question. Your line is now open.

Okay, their line may be on mute. Once again, if you have a question, could you please press 0 and 1 on your phone keypad now.

Okay, we go back to that gentleman. Please go ahead. Your line is now open. Could you take yourself off mute?

Michael Akinyemi
Hello?

Operator
Yes, I can hear you. Please go ahead with your question.

Michael Akinyemi
Okay, thank you. Thank you very much for your presentation. This is Michael Akinyemi from Standard Chartered Bank. I just have three questions. I just wanted to get clarity on the difference between general commerce and general under your – the loan book – under the industry classification.

The second question is on restructured loans. Do you have any restructured loans on your book, and what are the – what is the percentage of total restructured loans to gross loans?

Finally, looking at your liquidity ratio, just want to get a sense on what the plans are around increasing the Bank's liquidity ratio and what the target is for this year on liquidity ratio. Thank you.

Tunde Mabawonku
Okay. Thank you very much, Mike. My name is Tunde Mabawonku. I'll take a couple of the points, and then I'll yield the floor to my colleagues. Starting with the liquidity ratio, we closed with 30.3%. Our guidance for 2017 is 35 to 37%. What happened – for the better part of 2016, up until the second half, was rates were a little bit low in the market. And if you recall, the typical commercial bank – you have a liquidity ratio of 30%, cash reserve ratio of 27.5 before and now 22.5%. So we have 57% of the deposits locked up in low-yielding assets. It was imperative for us as a smaller bank to sweat our portfolio and do a lot more in terms of the loan book. But towards the end of the year, as money market rates started going up, we wanted to give you that. As loans unwind, it made some more profit sense to do the money market. So we expect to see liquidity ratio to go up. We think it will be between 35 and, at best, 40% in 2017.

On your question on difference between general and general commerce, the general sector largely refers to personal loans, loans to small individuals, loans to religious organisations. But general commerce talks largely on commercial loans to bigger businesses that do trading and buying and selling. So one has to do a lot more with the personal loans and loans to medium and small SMEs, while the general commerce is really on commercial and trading loans.

In terms of the restructure of the loan book, yes, the Bank restructured its loan book, or part of some loans, during the year. I think at the last check was 7% of the loan book. Some of the customers were in the oil and gas space. I guess the DMD will speak on that. But percentage of the loan book that was restructured was less than 10%, and last count I think was at 7% mark. Ademola, do have any colour?

Ademola Adebise

Yes, basically some of these loans in the oil and gas space has to do with the dollar-denominated loans that are for vessels – vessels that are acquired, and they are operational in the – to the oil – the oil majors. And due to the lull in the economy, a number of the contracts were re-priced, and – which led to the fact that we had to extend the tenure of these facilities. Those were the key restructurings that happened, you know, during the year.

Michael Akinyemi

Thank you.

Tunde Mabawonku

Thank you.

Ademola Adebise

Thank you.

Operator

Once again, if you have any further questions, could you please press 0 and then 1 on your phone keypad now.

Once again, any further questions, please press 0 and then 1 on your phone keypad now.

As there are no further questions, may I please pass the call back to you?

Ademola Adebise

So, thank you very much for listening to us, and we look forward to having you at the next conference call. Thank you very much.

Operator

This now concludes today's call. Thank you all very much for attending. You may now disconnect.