Conference call

Interim report – first nine months 2017

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Investor Relations

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SPEECH

Operator

Good day, ladies and gentlemen, and welcome to Danske Bank's third quarter 2017 conference call. For your information, today's conference is being recorded.

At this time, I would like to turn the conference over to Mr. Thomas Borgen. Please go ahead, sir.

Thomas Borgen - Danske Bank - CEO

Thank you, operator, and thank you all for taking time to listen into this call today. I have with me in the room today our CFO, Jacob Aarup-Andersen, and Head of IR, Claus Jensen.

Slide 1 please. In today's call, we have the pleasure of presenting Danske Bank's financial results for the first nine months of 2017. We aim to keep this presentation to around 15 minutes. After presentation, we will open up for a Q&A as usual. Afterwards, feel free to contact our IR department if you have any more questions.

Slide 2 please. With a net profit of DKK 15.3 billion, the first nine months of 2017 was a satisfying period for Danske Bank. Net profit grows 7% over the level in the same period the year before, and the return on shareholders' equity was at 13.3%, an increase of 0.7 percentage points from the first nine months of 2016. The financial results clearly demonstrate, not only for the first nine months, but also for the third quarter in isolation, that we continue to meet our financial targets by maintaining a strong focus on becoming an even more customer-centric, simple and efficient bank.

The development in the first nine months of the year was backed by positive macroeconomic trends in the Nordic region, most notably in Denmark and Finland where GDP growth is now above 2%. The strong underlying business momentum continued in the first nine months of the year based on a solid and well-balanced inflow of business from personal and business customers across the Nordics. Loan growth for the Group was up 3% from the same period last year. The execution of our Nordics strategy continues. In Norway and Sweden in particular, the good momentum was generated by the partnership agreements as well as a strong development in Business Banking.

In both countries, lending rose above Group average, while at the same time we maintained a strong focus on credit quality. The full potential of our new customer relations are further to be explored. The development in the financial markets was more positive in the first nine months than in the same period of last year. Customer activity increased in the period, particular in the first half of the year. And our capital market activities have been able to take advantage of the business opportunities, and thereby continue to strengthen our competitive position in the Nordic markets.

In Wealth Management, we also benefited from stronger customer activity evidenced by a net inflow of customers and a strong increase in premiums. We are confident that our newly formed Wealth Management organisation will be able to utilise the long-term potential in this area.

Expenses rose from the level in the first nine months of last year because of initiatives taken to meet increased regulatory requirements and our decision to further enhance digital capabilities in order to secure Danske Bank's long-term competitive position. Higher costs related to increased customer activity, however, were mitigated by efficiency measures.

Credit quality remained strong and had a positive impact on the financial results. We continue to see a net reversal of loan impairment charges now for the fourth consecutive quarter. Our capital position remained very strong. The core tier 1 capital ratio was 16.7% by the end of the third quarter, which is well above our target. The number is net of the total share buy-back programme of DKK 10 billion we're currently executing on.

Overall, our result for the first nine months clearly demonstrates that we continue to develop Danske Bank as a solid, balanced and predictable financial institution. Finally, we have revised our outlook for the full year. We now expect net profit for 2017 to be in the range of DKK 19 billion to DKK 21 billion.

I will now turn the presentation over to Jacob, who will take you through the financial results in more detail. Slide 3 please.

Jacob Aarup-Andersen - Danske Bank – CFO

Thank you, Thomas. Let's take a look at the main items of our financial results. Net interest income came in at DKK 17.4 billion. This was a 7% increase over the level in the same period the year before, and it was driven mainly by lending growth of 3%. Excluding currency effects, NII was up 8%. In Q3, there was one more interest day than in the preceding quarter.

Looking at net fee income, this came in at DKK 11.1 billion, up 9% from the level last year when fee income was low because of subdued investment activity. All Nordic business units contributed to the increase, Wealth Management and C&I in particular.

Net trading income came in at DKK 6.3 billion, unchanged from the same period the year before, and was driven by strong customer activity at C&I, primarily in the beginning of the year. Other income fell significantly from the level last year where we benefited from the sale of our domicile properties in Copenhagen.

Operating expenses were up 2% to DKK 17 billion. The figure for the same period last year was based on lower IT-related costs and included positive one-offs. In the first nine months of this year, expenses reflect increased expenses for regulatory compliance projects and a continued focused on digitalisation, whereas higher activity-related costs were mitigated by efficiency measures.

The cost/income ratio came in at 47.2%, slightly below the level of the year before. Finally, we saw net loan impairment reversals of DKK 0.6 billion as a result of improved credit quality in particular at Business Banking.

Slide 4 please. In the first nine months of the year, our two Nordic banking units, Personal Banking and Business Banking, benefited from good business momentum in almost all markets. The improvement in the results was based on a higher customer activity than last year and a good inflow of new business in Norway and Sweden in particular. In Northern Ireland, the lower UK rates and the development in the pound sterling had an adverse effect on the financial results.

Now let's look more closely at the three different units. Personal Banking delivered good results with profit before loan impairment charges up 14% to DKK 3.9 billion. Total income was 5% higher than last year and that's owing to improvement in all income lines. Expenses were down 1% despite higher activity and regulation-driven investments.

Looking at impairment charges, here we saw a small reversal, which reflects a continuation of strong credit quality. The return on allocated capital was 21.5%. Total lending volume was up 2%, owing to growth in Norway and Sweden, while lending volumes measured in local currency rose 8% and 18%, respectively. These strong gains came primarily from our partnership agreements, under which we continue to see a good inflow of new customers particularly in Sweden. In Denmark, where volume was stable, the trend towards higher mortgage lending and lower lending within conventional loan products continued, however at a slower pace. In Finland, lending volume was up 1%.

Moving to Business Banking. Here we continued the solid progress in all markets. Overall profit before loan impairment charges was up 11%. Measured in local currency, lending volume was up in all markets, most notably in Norway and Sweden where volumes rose 11% and 10%, respectively. But also in Finland, growth in lending gained further momentum and was up 8% from the year before. In Denmark, excluding Realkredit Danmark, our mortgage unit, lending rose 5%.

Total income was 5% higher than last year due to higher customer activity. The improvement was driven by NII and fee income. Expenses were down 4%, owing to efficiency measures offsetting higher regulatory and activity-related costs. Impairment charges showed a significant reversal of DKK 0.8 billion as a result of strong credit quality. The return on the allocated capital was 18.1%.

Finally in Northern Ireland, the result was adversely affected by the depreciation of the pound sterling, lower interest rates and reduced loan impairment reversals. The underlying performance was positive with good growth in new business. Total income fell 11%. Adjusted for the depreciation of the currency, it was down 4% as a result of lower UK interest rates and one-off income last year. Expenses were unchanged. Again adjusted for the exchange rate effect, they were up 9%, partly due to increased pension-related costs and investments. The return on the allocated capital was 14.5%.

Slide 5 please. Now let's take a closer look at Personal Banking Sweden as a good example of how we are realising our Nordic potential. A significant part of the growth we're seeing in Sweden is based on the strategic partnership agreements with SACO and TCO, which started to have a visible effect on our numbers in the second half of last year. On-boarding takes place digitally for more than 90% of new customers. Since the second quarter of 2016, lending has increased 22% accompanied by an increase in NII of 41%. The new business is clearly profitable for us, as the effect on cost has only been marginal.

There are three important points to note from our growth in Sweden. Firstly, we maintain a very strong focus on credit quality. The partnership agreements represent a selected growth strategy with sound credit quality, as is clearly demonstrated by the PD numbers for the SACO customers. Secondly, the inflow of new customers gives us a very good platform for cross-selling in the medium to longer term. Opportunities that are key for us in order to obtain a stable and balanced presence in Sweden. And thirdly, we comply with the 25% risk rate floor in Sweden. Finally, we have established Danske Hypotek, our new mortgage subsidiary in Sweden dedicated to obtaining local funding on a level playing field with the Swedish banks.

Slide 6 please. Let's have a look at the units that are more dependent on the capital markets. At C&I, profit before impairments rose 23% over the level last year when customer activity was low due to challenging market conditions. Increased activity in FICC was fuelled by a number of geopolitical events, primarily in the first quarter of the year, whereas activity within capital markets in general banking remained high during the first nine months.

Total income rose 13%, owing to improvement in all major income lines. Fee income benefited from increased customer activity within all areas in Capital Markets and a number of large transactions in General Banking. Expenses were broadly unchanged despite high activity in the period. Impairments, which by nature fluctuate at C&I, amounted to DKK 0.4 billion. That's down 51% from the level last year. The charges were primarily against exposure to the oil sector. Despite high activity at C&I, capital consumption was stable and was down 3% from the level in Q2 due to lower counterparty and market risk.

At Wealth Management, profit before tax was up 2%, as the unit, like the other business units, benefited from improved market conditions and higher customer activity. Fee income was up 12% from the level last year, driven mainly by an increase in assets under management and higher customer activity. Expenses were up 7% due to higher activity and increasing costs for the implementation of new regulation. Assets under management were up 10% from the level in the same period last year. In the first nine months of this year, premiums in Danica Pension and net sales from Asset Management amounted to DKK 29 billion and DKK 11 billion, respectively.

Slide 7 please. Moving on to expenses. Total expenses for the first nine months of the year amounted to DKK 17 billion, up 2% from the level last year. In the first nine months of last year, expenses benefited from positive one-offs and lower IT-related costs than we have seen this year. The increase in expenses related to IT-related regulatory compliance work, enabling us to implement and comply with regulatory requirements, such as MiFID II, GDPR, PSD2 and other regulation.

Furthermore, we continue to prioritise our digital capabilities. That's a key driver for enhancing the customer experience and more efficient end-to-end processes. The increased costs related to high activity were mitigated by efficiency measures. The underlying cost development remains satisfying, and we confirm our outlook for expenses for the full year to be around the level in 2016.

Slide 8 please. The positive trend in credit quality continued in the third quarter. In the preceding quarters, we had a net reversal for the group. The reversals for the first nine months of the year were DKK 0.6 billion, against a charge of DKK 0.2 billion in the same period in 2016. The loan loss ratio for the first nine months of 2017, excluding Non-core, was minus 4 basis points. With a net reversal of DKK 0.2 billion in the third quarter, Business Banking had the largest decline among our core business units driven by reversals within agriculture and a continuation of positive outcomes of workout cases mainly in Denmark.

At C&I, we booked impairment charges of DKK 0.1 billion in the third quarter, mainly against oil-related exposure, as difficult market conditions for subcontractors in the oil and gas industry continued. Individual impairment charges accounted for the increase in the quarter. Collective charges stood at DKK 1.2 billion, up slightly from the preceding quarter. At Non-core, reversals in the third quarter amounted to DKK 0.2 billion and related to exposures in Non-core banking.

Slide 9 please. Our capital position remained very strong with a reported common equity tier 1 capital ratio of 16.7%. That's up 0.5 percentage points from the preceding quarter and well above our target range of 14% to 15%. The full deduction of the DKK 10 billion share buy-back programme was booked in the first quarter. Total capital ratio was 21.6%, up from 21.1% at the end of the second quarter. The REA level fell DKK 10 billion in the third quarter. That's owing to a reduction in market and counterparty risk as a result of the currently low volatility in the financial markets.

The leverage ratio was 4.2% according to transitional rules and 4.1% on the basis of fully phased-in rules. The share buy-back programme of DKK 10 billion in 2017 is progressing according to plan. As of the end of week 43, we had bought back 30.6 million shares, representing a gross value of DKK 7.5 billion. We aim to communicate capital distribution for 2017 in connection with the publication of the full year financial report in February 2018.

Slide 10 please. And finally our outlook. We now expect net profit for 2017 to be in the range of DKK 19 billion to DKK 21 billion. This is due to higher than expected income in all major income lines as a result of higher customer activity and also lower loan impairment charges in the first nine months of 2017. The outlook is subject to uncertainty and macroeconomic developments.

And now over to Thomas and Slide 11 please.

Thomas Borgen - Danske Bank - CEO

Thank you. Those were our initial comments and messages. We are now ready for your questions. Please limit yourself to two questions. If you are listening to the conference call from our website, you are welcome to ask questions by e-mail. Operator, we are ready for the Q&A session.

Operator

(Operator Instructions) We will now take the first question from Jakob Brink from Nordea.

Jakob Brink – Nordea

The first one regarding net interest income. Could you maybe give us a bit more detail? There're some -- I don't know if they are funny, but some pretty large moves in the different business segments. I see that for Norway and Sweden, NIM goes up quite a bit quarter-on-quarter. I've seen in Norwegian press that you have talked about lowering the rates for mortgages in Norway. So should we expect it to come back in the fourth quarter to around the Q1 level or Q2 level? Also Northern Ireland, a pretty big drop in NII quarter-on-quarter, so could you just elaborate a bit on that? My second question on fee income, it looks like your asset management and pension fees are somewhat soft in this quarter at least compared to Q2. So it doesn't quite follow the normal seasonality. So could you also give us a bit more detail on that please?

Jacob Aarup-Andersen - Danske Bank – CFO

Let me try to answer your questions here. So let's start on the NII side. So you're pointing to the movements in the quarter on NII. So if we just take a quick overview of the different lines here, so you're right that you're seeing an improvement in Sweden and Norway on the NII side. We – when we communicated here, you're seeing overall flattish margins across the Group, but what you're pointing to is Sweden and Norway, we've seen a slight increase in the reported lending margins. The reason has been better funding conditions, so you can say the spread has improved, and conditions have been amenable to that. You point directly to our announcement around Norway. It is correct that we have in certain segments been out communicating slightly lower prices. We do not guide to exactly to where the margin in Norway would be in Q4. So we'll let you do some work on your own there. I'm sure you will be able to do that. But obviously that can have a small effect on the margin. But obviously then if you do believe that, there is also a potential volume effect going the other way. Otherwise, when you look at NII, where you referred to Northern Ireland also, one thing you need to be cognizant of is the movement in NII other, which you have to net out when you look at the different business units. And NII other goes up a bit in this quarter. And it's only natural that we see this increase in the Internal Bank when we have a growing lending book and lower liquidity cost. There was, as you know, a lag effect in terms of reversing this into the business units, so that number goes up and down, and it does have some technical effect into some of the NII on a quarterly basis. But we are not seeing a change in margins in Northern Ireland as you asked for. So it's pure technicalities what you're seeing. And do remember as we've already spoken about, there is also some one-off effects in Q2 and Q3 on NII that you need to net out here. You know we flagged a DKK 90 million one-off in Q2, and we are flagging a DKK 40 million one-off in Q3 in NII other. So those effects you also have to take into account. So some moving parts. But overall, no change in Northern Ireland, and it's correct that there's a slight margin increase in Sweden and Norway. On the fee side, you asked on Wealth Management. It is correct that we are seeing a small drop in Wealth Management in Q3. That is seasonality. When we look at seasonality here, I think there's two things to point to; one is that private banking activity in the private banking space will impact the investment fees, and the other point is that you haven't seen any fund launches in Q3 due to the summer period, and that those two effects will be seen on the fee line. So it's activity-driven. There's no major mix change or anything else to point to in Wealth Management.

Operator

We will now take our next question from Jan Wolter from Credit Suisse.

Jan Wolter – Credit Suisse

So if I just start looking at the capital and the counterparty risk and market risk seems to be going down here, at least in the last couple of quarters. I think in the beginning of the year, you had counterparty risk just shy of DKK 50 billion, market risk around that level as well. And now I think we've seen those two come down by 20%, 25% year-to-date. If you just could talk to why that is and it is only because or absolute majority, reason being low volatility and low client activity? Or is there a meaningful part which is driven by de-risking? And if so, then should we expect market and counterparty risk to jump up again? So that's my first question. And then on the Treasury NII there, is there any impact in the quarter or in the past couple of quarters in real economic terms, i.e. lower funding costs which will be sustainable going forward? Or is this just a transfer from the business units to Treasury?

Jacob Aarup-Andersen - Danske Bank – CFO

Okay. Let's start with the question on capital. So yes, you are definitely right that market risk and counterparty risk have come down. You know that we have been very focused on the de-risking of our C&I business. You know that's been a multi-year story, and we've also said it continued into this year. So a good part of this is de-risking. What we have also said in recent quarters is that we are also seeing the effect of the very low market volatility. So we would not be surprised if market volatility comes up that you will see some increase in market risk, but not to the extent of the entire drop you have seen here. So expect to see some comeback if there's volatility, but generally this is a good de-risking from the team. On Treasury NII, as I said, this is a business units versus Treasury Internal Bank component. We do not run any proprietary risk in our Treasury department. So this is not treasury gains we're talking about. This is a question of funding the business units.

Jan Wolter – Credit Suisse

And if I may just follow up on the capital there? I think in the report you state that you expect a smooth adaption to changing regulatory requirement. What does that mean really? Do you need to think in terms now of scaling back the buy-back programme in order to adapt to a certain outcome from Basel IV for example or other regulatory requirements? If you could share some colour on that please?

Jacob Aarup-Andersen - Danske Bank – CFO

Sure, Jan. And thanks for that question. I think when we talk about smooth, it's actually I think I guess we mean calm is the word as well. You were referring to future regulation. When we look at our capital position, it's very strong. Let's just have that starting point. We generated another 50 basis points in this quarter at 16.6% fully phased. We are 4.6% above our fully phased capital requirement. And that, with that starting point and the continued capital generation of the group, we feel we're in a very, very strong position on the capital side. That is what this statement reflects. We can obviously not talk about what our distributions will be in the coming years because that's up to the Board, et cetera. But we are highlighting again today that we have a very strong capital position. And from that perspective, obviously our guidance on capital and distributions has not changed.

Operator

We will now take our next question from Willis Palermo from Goldman Sachs.

Willis Palermo – Goldman Sachs

The first one is on the revenue line, still on the fee income follow up to the previous one. Could you maybe elaborate what happened on the flow side? I understand there were no new launches of funds, but why was there outflow this quarter despite the very strong performance, and also the management fee margin went down quite a lot. Is it purely seasonality-related or was there anything else to flag on the pricing side? And the second question is on the volume side, where it was quite strong across the board except in the corporate division, if you could say a word on that. And also on the partnership agreements, when you say it started to be visible, how would it translate when it would be fully visible, especially on the TCO deal that started recently?

Jacob Aarup-Andersen - Danske Bank – CFO

Okay, so let us start on the fee side. On the fee side, you're referring to the comment around an outflow in Q3 in Asset Management. We have seen some specific clients deciding to insource some of their mandates for internal reasons. So it's not performance-related or anything else, and that will happen once in a while. So it's -- and when we look at the underlying trend in terms of the sales flow, it is a continuation of what we've seen so far. So there's no drama around that. In terms of management fee and your question on whether we are seeing the tier rating pricing, no we are not. There are obviously always some mix effects when you look at the margins on a quarterly basis, but part of the management fee here will also be activity-driven. So generally, no, we are not seeing a change in momentum on the sales side, and we're not seeing a change in the momentum on the pricing side as well. So it is a low seasonal quarter, but the underlying trends are continuing. On the volumes on C&I, do remember that the C&I business is very lumpy. This is obviously large commitment to large corporates, et cetera, and often it's transaction driven, large M&A driven. It can be bridged to bond and these types of situations, which also means that larger facilities will then flow out of the accounts again, et cetera. We've seen very good activity in this segment, but large corporates are washed with cash and therefore a lot of our activity then actually occurs in our Capital Markets business instead of on the lending book. So there is no major drama in the fact that the C&I lending book is down a bit in the quarter. You asked finally about partnership agreements, and when we would see the full effect of TCO. You can see we feel we are seeing quite a good effect of TCO in the numbers. It's a very high growth rate. What we have also said is that we will not approach all TCO members at one time, so this will be a continued work from our side in terms of gradually broadening out the offering to make sure that we are approaching an amount of people that we can also handle in terms of treating them well, et cetera, et cetera. So therefore, we think you will be seeing a good effect of TCO for quite a long time, but we do not have a certain measure as when you see full effect, et cetera. It's going to be an ongoing effect from TCO.

Operator

Our next question comes from Amal Shah from Redburn.

Amal Shah – Redburn

I've got two questions. First one is, in the second quarter you mentioned setting up a proper structure to generate the fee growth from the partnership agreements. So could you give us the progress on this and what sort of fee to NII split that we should expect? And then the second question, has the slowdown in the Norwegian and Swedish housing markets affected your outlook for how much growth you can expect from these partnership agreements?

Jacob Aarup-Andersen - Danske Bank – CFO

Okay. Thanks, Amal. So I think in terms of your first question, I don't know if we have said that we would set up a specific structure. I think you're referring to our ambition to make sure that we cross sell well enough under partnership agreements, which is clearly a strong ambition from our side and hopefully also something you have heard us referring to when we went through the slides. At some point, we can give more data as data comes along. As we've had more quarters with the partnership agreements, we can start being a bit more precise in terms of cross-selling, et cetera. There's a clear ambition and clear targets internally in terms of how to drive cross-sales in these partnership agreements. So it's a very fair question. At this stage, we're not giving numbers on it, but I can guarantee you it's a big focus for the management team to make sure we get the full value out of these customer relationships. And then on your other question on the outlook for the partnership agreements given the backdrop you described on property markets. Do remember one thing here. So let's just take a quick step back. The Danske Bank size in both the Swedish and the Norwegian market is one that entails that we can grow significantly more than the market if we want to and if we find good risk-adjusted profitable growth. So for us whether housing markets are up or down 5% does not make a material difference in terms of the attractiveness of the partnership agreements or the potential for us.

There is a very large group of potential clients in these partnership agreements. And for us, it's more a question of making sure that we can offer them the right customer proposition or value proposition that makes it attractive for them. So we do not think property markets being up or down will have a massive impact on the potential. So I mean, that's the short version from here.

Operator

We will now take our next question from Mads Thinggaard from ABG.

Mads Thinggaard – ABG Sundal Collier

This is Mads from ABG here with two questions. And the first one relates to the high growth you have in Business Banking in both Norway and Sweden this quarter. Could you put a bit more flavour on that; what is exactly happening here, and why are you taking such large shares here? And also could you confirm that there's no link to the drop in C&I? I mean meaning that you have moved customers to Business Banking. That was the first question. And then on the second question regarding your unchanged communication on distributions, I mean that may seem a bit different from what you hear from some of the local peers and perhaps also what the Danish FSA is communicating about getting distributions down this year. And there, I mean I know you can't say anything about what it's going to be. I'm just curious if you have felt some change with the Danish authorities in the discussions on distributions, or you feel that they have an unchanged stance towards distributions?

Jacob Aarup-Andersen - Danske Bank – CFO

Thanks, Mads. I'll take the first one in terms of Business Banking. Yes, very pleased to see that you have seen the good growth rates in Business Banking in Norway and Sweden. As you say, they are a bit higher than the market. But do remember they have been a bit higher than the market for quite a long time. So for us, this is not a dramatic change in this specific quarter. We are still writing good diversified business in both markets. So it's not one specific segment that is driving it. For Business Banking, we do acknowledge that the growth rates were a little bit higher this quarter compared to last quarter, but there is also some lumpiness here in terms of larger deals, et cetera. So this is a continuation of the diversified growth you've seen. I'm not to speculate why we continue to see such good growth in terms of a competitive perspective, but what I can say is that we're very pleased with the quality of the business we're putting on the books. You asked an additional question in terms of C&I. There's no technicalities there. We're not moving business across the line. So it's two different things.

Thomas Borgen - Danske Bank - CEO

Okay. Mads, to your other question about distribution. I think the starting point is that our capital strategy and capital distribution are unchanged. First of all, we aim to meet our capital targets. And, as you may recall, that is to have a CET 1 between 14% and 15%. Subsequently, we intend to keep the dividend between 40% and 50% after profits. Thirdly, then we would like to take the profitable growth we see in our core markets, in other words the Nordic markets, which we've also been able to do during many quarters. And then we have said if there is any excess capital, we would like to distribute that back to the shareholders in one way or another. That has not changed. But the final pay-out strategy or payment conclusions will be a part of the Board's discussions after Q4. Then you allude to a question about the regulator. I think it's fair to say that one of the regulator's mandates is to remind all institutions to remain diligent on pay-outs. That is not new. So I see no change in the way we have a dialogue with the Danish FSA, but of course all FSAs, including the Danish FSA, will always remind institutions to remain diligent.

Operator

We will now take our next question from Andreas Håkansson from Exane BNP Paribas.

Andreas Håkansson – Exane BNP Paribas

We covered a few things. So I really just have a follow-up question on a different topic, and that's the Estonian money laundering. Could you just tell us what -- I know that the Estonian FSA has an ongoing investigation, and we have read about the French courts. Could you tell us if the Danish FSA is investigating at the moment, and have you had any contacts with any US authorities of any kind related to the money laundering?

Thomas Borgen - Danske Bank - CEO

Okay. Thanks for your question. Let's take the French first. We are currently early in the stage of the investigation. The bank has not been indicted at this point. And, of course, there is no certainty that it will be. And in that sense, it's too early to speculate on any outcome. Then you have a wider question. We have a continuous dialogue with supervisory authorities in the markets where the bank is active, including the US authorities. And as a part of our ongoing dialogue with authorities in those markets, we have also discussed these matters, and several financial supervisory authorities, including the Danish FSA, have asked questions pertaining to this case. We do not, of course, comment on individual interactions with supervisory authorities, but in Denmark, orders and reprimands are publicly available.

Andreas Håkansson – Exane BNP Paribas

And have you made any provisions or thought about making provisions for any potential fines coming out of it?

Thomas Borgen - Danske Bank - CEO

No, no financial provisions have been taken at this point. And we currently do not foresee fines and legal costs in this matter that will have any material impact on Danske Bank.

Operator

We will now take our next question from Per Grønborg from SEB.

Per Grønborg – SEB

This is a set of numbers where it's actually quite easy, so a few nitty-gritty questions. Norway Business Banking, quite large loan losses now for the second quarter in a row. Could you comment a bit on that? I guess it's oil-related that it is climbing from C&I down to the bit smaller clients. Then on your divestment in Ireland, you now tell that you have closed the deal. Can you give some indication of the REA impact, there doesn't seem to be anything already at this time? I assume that the cost related to the transaction and the big loan loss reversals in Non-core relate to the transactions, so there will be no impact in the fourth quarter. Is that the right way of looking at it? Can I squeeze in a third one also to the anti-money laundering issue? The cost related to the investigations you are doing currently, will that be any visible amount, or is that something we shouldn't be concerned about?

Jacob Aarup-Andersen - Danske Bank - CFO

Let me do the Irish one to start with. So yes, you asked in terms of release of capital, and so we expect the release of capital from the sale of Non-core Ireland to be between DKK 5 billion and DKK 6 billion of REA. And we expect that to happen in Q4, if the transaction obviously closes in Q4 as expected. It is expected to close there. Then you are right that there are some movements in the Non-core line, and they are reflecting what has been going on in Ireland, so you are spot on in terms of that. You asked about Q4 impacts. At this stage, we expect Non-core to report a gain of probably around DKK 100 million in Q4. So the Non-core line, it's not going to be dramatic but probably around DKK 100 million in Q4. The big impact here, as you also pointed out yourself, is the REA impact, which is a release in Q3.

Thomas Borgen - Danske Bank - CEO

Okay. To your two other questions, no, our own investigation will not have any material impact on the cost line. Then to Norway Business Banking, you're right that the impairments are slightly higher in Norway than we see in other markets. And these are primarily related to, as you also alluded to, the oil service sector, which has stabilised but to some extent could be challenged, but it seems to be stabilised with the present oil prices. Secondly, there has been one particular case, which has been challenged in Business Banking during the quarter, which has been public in the Norwegian press.

Operator

We will now take our next question from Johan Ekblom from UBS.

Johan Ekblom – UBS

I think most things have been answered. Maybe just two questions for more details. In terms of your capital allocation, why do we see such a big increase in the capital allocation in Personal Banking in this quarter? So that's the first thing. And then secondly, I think two or three times during your presentation, you referred to the weak top line in Northern Ireland due to low rate, and now we have slightly higher rates in the UK. Do you have any impact as to what kind of sensitivity we should expect from that?

Jacob Aarup-Andersen - Danske Bank - CFO

Thanks for the questions. Let's just take them one at a time here. So in terms of Personal Banking, you're right, the capital allocation goes up. It goes up not due to a massive change in models or anything like that, but there is quite strong lending growth, as you've noticed, in Personal Banking and that obviously drives some capital allocation. We show this in our little deep dive on Sweden, Personal Banking Sweden. We also write there that we adhere to the Swedish regulator's 25% risk weight flow on the Swedish mortgages. You can see a lot of growth in Sweden this quarter as well. So that also impacts the REA as well. So our capital allocation follows the regulatory capital usage as you know, and therefore it's a reflection of the strong lending growth. Regarding your other question in terms of weak top line in Northern Ireland, yes, we have also noticed the decision of the Bank of England today. It will naturally have a positive impact on Northern Ireland. We haven't given the sensitivity, but it is a small help to the Northern Irish top line, which we appreciate. I also understand that they said in the statement today that we should not expect many further hikes in the near future, so it's a small little improvement, yes.

Johan Ekblom – UBS

Thank you. But can I just come back to the capital allocation? I mean it's up 9% in the quarter, which no matter how I FX adjust my volumes, and if all the growth is in Swedish mortgages, I still struggle to get there. Is there any time lag in how you implement this, or did you sort of allocate the 25% this quarter for the first time, or is it just sort of a bit of a random walk in that sense?

Jacob Aarup-Andersen - Danske Bank - CFO

I can guarantee you we don't do random walks. But there can be a quarter-to-quarter in terms of the averaging, et cetera. So I'm very happy that IR can walk you through it afterwards, but on quarter-to-quarter there can be an averaging effect as well. So the number you are looking at right now is the one you should use. The walk-up to Q3, IR can walk you through.

Operator

We will now take the next question from Kim Bergøe from Deutsche Bank.

Kim Bergøe – Deutsche Bank

It's Kim from Deutsche Bank. I'm just -- I think most of my questions have been answered. So just one from me, and that's in terms of the margin outlook, sort of assuming interest rates stay about where they are and just sort of concentrating on the customer side, you touched a bit upon what you have done in Norway. How should we think about the margin outlook? Where do you see pressures? We've seen some of your Danish peers talking about quite significant pressure in Denmark. What's your own view going forward on customer margins?

Thomas Borgen - Danske Bank - CEO

Thanks. I would say we are in basically 17 business cells or 16, meaning 4 countries with 4 business units, and number 17 is, of course, Northern Ireland. I think we are planning and looking into flattish margins basically in all of them. So no major changes.

Operator

Our next question comes from Geoff Dawes from Société Générale.

Geoff Dawes – Société Générale

Geoff here from SocGen. I just want to spend a little bit of time on Denmark and lending volumes in particular. Looking at the country-by-country guidance and trends, so from what we have seen so far it does seem to be going a lot slower than everything else. Can you just give us a little bit of feedback as to why that is, first of all? Is it a supply issue from yourselves, you're deliberately losing market share? Is it a demand issue, is there anything in the economy that's moving lending volumes forward a little bit? And second of all is a related question. If things pick-up materially in Denmark, better than your expectations, would that directly impact your buy-back guidance and plans? I know that for you, growth is a priory over buyback. Just your thoughts on that would be great.

Thomas Borgen - Danske Bank - CEO

Thank you. There is no question that the Danish economy has picked up substantially during the last 12 months. And we see that the GDP for 2017 is expected to be well above 2%, a closer estimate maybe 2.4%. And our chief economists also believe that we will have 2% or slightly above also in 2018. There is through times very often a link between the growth and the request for capital. So said, there is less request for capital for the time being as many of the Business Banking clients in Denmark are well cash rich. So in that sense, the underlying credit demand is subdued to around 1% to 2%. In the private customer market, we see the same. There is some deleveraging taking place, which from a societal point of view is only good. And that's around the same level. No, we are not losing any market share, actually we are slightly gaining market shares. But over time, with such a big market share we have, you should expect us to more or less follow the market but that can, of course, fluctuate quarter-to-quarter. So we will, of course, benefit if the credit demand increases going forward. No, we cannot make a link between the credit demand in Denmark and the payout. That's two different issues and that goes back to our capital strategy.

Operator

Our next question comes from Vardhman Jain from Macquarie.

Vardhman Jain – Macquarie

Couple of quick ones. Firstly on Denmark. One of your peers, Jyske Bank, recently mentioned the new Danish FSA proposals around limiting certain mortgage products. Especially the interest-only and the ARM mortgages. Could you just give us more colour on that, and how that might impact on the credit outlook for Danish economy? And secondly, just coming back on the buy-back question. Clearly, you have a very strong capital position now, but your leverage position is at 4.1%. I guess my question is would you be comfortable in dipping below the 4% target when you decide on the buyback for the next year?

Jacob Aarup-Andersen - Danske Bank - CFO

Thank you very much for your questions. So I think what Jyske Bank was referring to is that the Danish regulators are looking at implementing a debt-to-income rule for certain types of products that is correct in terms of interest only et cetera. It's been a debate for a while, and you see similar things in the other Nordic countries. So there is no major drama around that. There's been a public debate about it but that was a first proposal, which is now being amended, and it has also been delayed. It looks like the amended proposal will have a shape that has less impact than the first one, based on what we see and hear. And we do not think this changes the outlook for the Danish publishing market materially. It may take some peak momentum out of certain smaller segments, but this is not something that will change anything for us in terms of what we expect for our business going forward here. Then your other question was on the leverage ratio. We have a target of maintaining around a 100 basis points above the 3% recommended level. So that is around 4%. If we dip just below 4%, that is not a major drama for us, but we want to over time stay at 4 or above. So it is not a hard, hard limit for us but it is our target, and we obviously run the business to maintain that target.

Operator

(Operator Instructions) We will now take the next from Riccardo Rovere from Mediobanca.

Riccardo Rovere – Mediobanca

Just one question from my side. If I have a look at what has been happening over the past 12 months, I see that the loan book has been growing by around DKK 35 billion more or less, if my numbers are correct. This is true for Danske Bank, but this is true for the overall country in general. So the level of debt in the country has not gone down. Because of available credit and because of negative rates, real estate prices are going up across the board. Real estate prices going up are driving your credit losses, your reversals, on one hand, and are also driving your maybe PDEs, LTDs, and your risk-weighted assets are down by DKK 45 billion in 12 months. When I look at your payout, and I take that and also account for the buyback, you're basically paying out everything 100% payout. Including the reversals, for how long can this situation be considered sustainable? Because it looks like it is a virtuous circle now but it could become actually a vicious circle if something goes wrong. For how long do you think this situation can go on?

Jacob Aarup-Andersen - Danske Bank - CFO

Thank you for that question. We do actually believe the situation is a little less dramatic than you painted here. I think there are a number of things you need to do to take into account when you do your math here. First of all, you're referring to our growth and the REA movements et cetera. Let's just remember a couple of facts here. We have over the last couple of years reduced our Non-core book, which obviously has very, very high risk weights. We've reduced that materially, and as you will know after Q4, it will be close to zero. We will have some exposures left but very, very small. So, Non-core has been reduced materially. In the same way, we have grown significantly in low risk areas, which is obviously lower risk-weight areas, which means the composition of our REA, our risk weights will have a natural positive mix effect. So do remember those facts before we then move in to the majority of the REA decrease here, which is market risk and counterparty risk. That is driven by the fact that we have changed our business model in our Markets business, where we have moved from having proprietary risk in a number of areas to having a completely client-driven business. So there are many factors that I think you're missing in your equation here. I can see why from a headline perspective it could make sense but I think you need to have all these facts as part of the equation. On top of that just a last comment. You mentioned the house prices, obviously house prices going up will have a positive effect on any bank, simply due to higher collateral values. And therefore it's also a better ability for most of your clients to adhere to their commitments, et cetera. But our business, and when you talk about capital, you referred to PDs, LTDs et cetera as if we were running a pure point in time model. Danske is more of a through-the-cycle build-up, which means that we do not have the same sensitivity around the collateral values as you referred to. So, I think there are many nuances. I think the biggest nuances here are around the entire change of our market risk and counterparty risk, the de-risking of Non-core and that our growth has happened in these low risk areas.

Operator

We will now take our next question from Jacob Kruse from Autonomous.

Jacob Kruse – Autonomous

Jacob from Autonomous. I guess just one question. On the cost side, you target DKK 23.6 billion. Last year and the prior year there was significant seasonality in Q4. How comfortable are you that you can hit that? I guess it's about DKK 5.6 billion, of course, in Q4 to do the DKK 23.6 billion target?

Jacob Aarup-Andersen - Danske Bank - CFO

Thanks, Jacob. Well if I have to be a bit cheeky, we just delivered better–than-expected costs in the quarter, so we should be more comfortable. We are comfortable. I think we said very clearly to you guys over the last couple of quarters that in 2017, we would see less seasonality in Q4, and that we are sticking to. And we are iterating our guidance today and are fully behind that. So there's no change to the messaging around that.

Thomas Borgen - Danske Bank - CEO

Operator, can I ask you to deliver the last question, please?

Operator

Certainly, sir. We will now take our final question from Bruce Hamilton from Morgan Stanley.

Bruce Hamilton – Morgan Stanley

Just a couple of follow-up questions. Firstly on the competitive dynamics in Denmark both in terms of volumes and margins. I guess one of your peers has a quite attractive incentive structure on mortgages. So how do you see that impacting your ability to compete on pricing in the business? I guess as you said already you think margins should be fairly stable across the different parts of the business or in the round. I mean just wanted to check how much that is – do you expect some funding benefits but some compression in lending margins or is there any other sort of way to think about that? And then my second question, obviously as you say you're doing a very good job on costs, so the targets this year are on. I mean the expectation in the market is you stick to fairly stable costs looking forward over the next couple of years. Given the efficiencies, you're running through the organisation, does that strike you as sensible or is that even low ball given what you can achieve?

Jacob Aarup-Andersen - Danske Bank - CFO

Okay. Let me start on the cost side. I think the answer here would be pretty quick. We don't guide for '18 and beyond. We've guided for '17. What I can make very clear is that we are very focused on taking out structural costs. We constantly invest in digitalisation across the bank and therefore, it's a massive focus for us to constantly make sure we lower our cost to serve. At the same time, and that's what you have seen this year, we are also seeing cost pressures from continued investments in our regulatory projects. And we have a very strong IT and digital agenda. So, we're seeing some pressures and also a continued focus on efficiencies. So, you know our focus on this line, but we're not going to give you guidance for '18 and beyond.

Thomas Borgen - Danske Bank - CEO

Okay. To your first question, in all markets there are good competitive dynamics, including, what you asked specifically about, on the Danish market. We remain very competitive today, and I expect us to remain very competitive tomorrow. You asked specifically if one institution's particular incentive systems makes lives more difficult for us, the answer is no. We are today gaining clients. We are today keeping a very good market share, actually increasing slightly. So, I think we remain and will remain very competitive also going forward.

Okay. Thank you all for your keen interest in Danske Bank and for your good questions. As always, you are welcome to contact our IR department if you have more questions after you have had the time to look at the financial results in more detail. A transcript of this conference call will be added to our website and the IR app within the next few days. Thank you very much and have a good afternoon.

Operator

Ladies and gentlemen, this concludes the Danske Bank's third quarter 2017 conference call. Thank you all for your participation today. You may now disconnect.