# Conference call

Interim report – first nine months 2019

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Investor Relations

## CORPORATE PARTICIPANTS

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## SPEECH

**Chris Vogelzang – Danske Bank – CEO**

Hello, and welcome to the presentation of Danske Bank's financial results for the first nine months of 2019. Thank you all for taking the time to listen in on this call today. My name is Chris Vogelzang, CEO. And with me, I have our CFO, Jacob Aarup-Andersen; and Head of Investor Relations, Claus Ingar Jensen.

Slide 1, please. Today's call will start with a short presentation of Danske Bank's financial results for the first nine months of 2019. Afterwards, we will present our ambitions to be realised by 2023, including guidance on the financial performance for 2020. After the presentation, we will open up for a Q&A session as usual. And afterwards, also feel free to contact our IR department if you have any more questions.

Slide 2. Since joining Danske Bank in June this year, it became clear to me that it is a fundamentally strong bank with great potential. We have a strong market position, a solid customer base, good products and services and a highly skilled and dedicated organisation with a real desire to serve our customers and do the right thing. But in recent years, we have failed to live up to the expectations of key stakeholders. And financially, we are currently not performing at a satisfactory level. AML is such an example, and although we have made significant progress through our AML and ODD programmes, we still have a way to go to fully integrate the highest standards into our day-to-day business.

The first nine months of this year have been particularly challenging. Net profit for the period, including the sale of Danica Pension Sweden, came in at DKK 10 billion, 14% lower than in the same period last year. The result represents a return on shareholders' equity of 8.5%, against 10.1% in the same period the year before. The underlying growth in our business was good, with lending up 3% at Banking Nordic and good business momentum at Banking DK in the third quarter, in particular, driven by strong remortgaging activity.

However, based on the financial results for the first nine months, the outlook for the full year has been adjusted. We now expect net profit for 2019 to be at the lower end of the DKK 13-15 billion range we provided as a guidance in our report for the first half of the year.

Given the development in our financial results that we have seen during the year to date and the conditions we are operating under, we announced in our financial report for the first half year that we clearly see the need for initiatives to improve our financial performance and regain business momentum.

Therefore, we have worked hard over the past three months to analyse our business, identify obstacles and set new ambitions. Today, we are able to announce a set of new ambitions, including an ambition to achieve a return on shareholders' equity of 9-10% in 2023.

My new management team and I are 100% committed to disciplined and dedicated execution. In order to do so, we must first stop the downward trend by stabilising underlying costs and invest heavily in the core capabilities and digitisation that will drive our future performance. We see that as particularly necessary, and it will have a significant impact on our results in 2020, for which we expect a return on shareholders' equity of 5-6%.

I will comment on our plan in more detail later in this presentation. I will now hand over to Jacob for a brief run-through of our income statement. Slide 3, Jacob.

**Jacob Aarup-Andersen – Danske Bank – CFO**

Thank you, Chris. As Chris just mentioned in the executive summary, net profit for the first nine months came in at DKK 10 billion, that's 14% lower than in the same period last year. The result for Q3 amounted to DKK 3 billion, against DKK 4 billion in Q2. The result of the first nine months benefited from the gain from the sale of Danica Pension Sweden, where we made DKK 1.3 billion of gain. The decline in net profit was caused by a lower total income and an increase in both costs and loan impairment charges.

Net interest income was adversely affected by significantly higher funding costs, changes in the product mix and intense competition, all putting pressure on margins, whereas fee income benefited from the inclusion of SEB Pension Denmark and high remortgaging activity in Denmark, despite the provision for the compensation related to the Flexinvest Fri case.

However, in Q3, we saw a slight increase in NII and good fee income from continued remortgaging activity. Net trading income was adversely affected by lower income at C&I, where FI&C remains challenged by difficult conditions in the rates market. Unfortunately, the negative trend continued in Q3 with illiquidity and volatility in the Danish fixed income market hampering our ability to profit from facilitating customer flows. As the challenges for the rates business now seems to be of a more persistent nature, we have initiated initial work to determine the degree of structural and cyclical impact on the business and our initial mitigating response. We will come back on this shortly in this presentation.

Then on expenses, expenses came in 2% higher than in the same period last year, which was affected by the donation of DKK 1.5 billion of income from the Estonian branch. Expenses in Q3 came in somewhat lower than in the preceding quarter when we expensed the compensation related to the Flexinvest Fri case. Loan impairment charges amounted to DKK 0.8 billion, against a net reversal of DKK 0.6 billion in the same period last year. The charges we have seen so far this year relate mostly to C&I, where impairments against exposure to the Shipping, Oil & Gas and Retailing industries have increased. Overall, credit quality remains strong.

Finally, the result of our Non-core activities, which was a negative DKK 0.2 billion for the period due to a one-off value adjustment caused by the repositioning of the Baltic activities to Non-core.

Slide 4, please. Trading income has fallen significantly since 2017, primarily because of a negative development in fixed income and currencies, or FI&C, at Corporates & Institutions. The decline in FI&C income is caused by both structural and cyclical factors, with structural factors estimated to have lowered income by up to DKK 1 billion.

Key structural drivers include a changed business model with lower risk utilisation and the transfer of activities to Group Treasury, but also regulatory changes with MiFID II and LCR by currency contributing to margin pressure and lower income in both rates and liquidity and securities finance.

Cyclical factors also contributed to the income decline as the result of negative value adjustments on the derivatives portfolio, driven by DVA losses and challenging macroeconomic conditions characterised, among other things, by relatively flat yield curves and negative interest rates. The current macroeconomic outlook for low-for-longer implies a heightened risk that the cyclical headwinds experienced since 2017 will prove more persistent.

Slide 5, please. As a result, a number of actions will be taken to improve profitability. IT and business resources will be allocated to optimising and digitalising core value chains in order to lower our end-to-end cost. Capital-intensive activities will be reviewed in order to optimise the deployment of capital. Direct staff cost will be reduced by up to 15% in the short term, and non-staff cost efficiencies will also be implemented. Cost and capital efficiencies will be supplemented and enabled by an updated service model that will allow for more self-servicing customers by expanding Danske Bank's presence on e-platforms and by realising synergies from interlinked value chains. As an example, via cross asset sales coverage and increased customer segmentation.

We will also expand the low-touch service model to more customers and further digitise the markets engine by increasing straight-through processing and investing in rebuilding legacy infrastructure. The result will be an FI&C business with a lower cost-to-serve and more efficient capital deployment, which are the prerequisites for delivering improved returns in this current macroeconomic environment.

Slide 7, please. And over to you, Chris.

**Chris Vogelzang – Danske Bank – CEO**

Thank you, Jacob. We recognize that we face a number of challenges today. Some of these are structural issues that apply to the financial sector as a whole, and others are specific to Danske Bank. As examples of structural issues, customers expect greater levels of convenience in personalisation, and recent and new regulation continues to shape how we do business, et cetera. We must also continue to find ways to deliver high-quality service to customers in an environment with low or negative interest rates.

Examples of specific Danske Bank priorities: We've made significant progress within compliance, but more work is required. Cost levels are higher than what we consider to be sufficiently competitive, and we need to become more agile and invest further in digitisation, core processes and IT. We have already taken a number of steps in the right direction, including the setup of a new leadership team that is committed to this journey, welcoming Berit Behring as a new Head of Wealth Management, Stephan Engels as CFO in April next year. And Jacob Aarup-Andersen will be acting CFO before taking up his position as Head of Banking DK. I will act as COO as we continue to look for the right person to head this unit.

Revised accountabilities, including the transfer of private wealth management to the banking units to facilitate better collaboration and serve our customers as one bank and the resolving of Group Development to bring responsibility closer to the business.

Slide 8, please. We believe that our strategic direction to be a Nordic bank that services both personal and business customers to meet all their financial needs in our core markets is fundamentally right, and it provides a solid foundation for rebooting the transformation to deliver the required results. Over the past few years, we have pursued an ambition to be an integrator and move closer and become more relevant to our customers, break down internal silos and also move closer to the societies we are part of. These will remain priorities and are represented by our renewed stakeholder promises. In addition, we have formulated four principles for how we can work better together to deliver on both our strategy and our promises.

Slide 9, please. To deliver on our promises and measure our progress, we have set ambitious 2023 targets for all of our key stakeholders. We consider these as interdependent prerequisites for success. And therefore, it is important to have tangible and measurable targets for each. Customers are the reason we exist, and we want to be, on average, one of the top 2 performers on customer satisfaction in everything we do. We aspire to have engaged employees who are proud to work at Danske Bank and aim for at least 90% of employees to be engaged as measured by our Employee Engagement Index.

We will operate sustainably, ethically and transparently and measure our societal impact across seven identified focus categories, including sustainable investment, diversity & inclusion and environmental footprint. And for our investors, we will continuously improve our profitability level by leveraging our full potential. We have broken this into three key targets: A 9-10% return on equity by 2023; a cost/income ratio in the low 50s; and a dividend pay-out ratio of 40-60%. These targets are ambitious, given the headwinds we will see, but we can achieve them if we consistently leverage the potential of our franchise.

In the following, I will elaborate on what it will take to deliver on these ambitions and what the journey towards 2023 looks like. Slide 10, please. 2020 is a crucial year for delivery on our ambition. We aim to end the downward trend, that is, we will stabilise underlying cost levels via the realisation of quick-win cost measures. At the same time, we will invest heavily in the initiatives that are core to driving our future performance, most importantly, the digitisation of our core customer journeys. From 2021, 2022, we expect to see an upward trend in our performance, and we'll report on the progress of implementation on an ongoing basis. By 2023, we expect full realisation of the benefits of our strategy to reach our ambitions.

Slide 11, please. Executing on the six core pillars is essential for our journey towards 2023. These relate to delivering in the short term and investing in future success. For the short term, we will bring compliance and the cost base under control while gaining commercial momentum. In parallel, we will invest in our future success by simplifying and digitising our business and scaling up agile ways of working. We will promote clear accountabilities and deliver a positive societal impact. We have already started executing this agenda, and I will elaborate on each of these six pillars.

Slide 12, please. Pillar 1, compliance under control. In 2020, we will arrive at the peak of our compliance investments, in alignment with requirements. The focus of our efforts so far has been the settlement of our legacy burdens and ensuring a fully compliant setup. Now we will focus our efforts on the optimisation of our AML efforts by more efficient integration into our core processes and digitisation to combine efficient delivery with fully compliant processing.

Pillar 2, cost base under control. In recent years, we have focused primarily on AML and compliance and less on cost discipline. In the short term, we will reinforce cost discipline via strong focus in the leadership team on this topic. Meanwhile, we will focus on keeping underlying costs stable in the short term. In order to achieve that, we have started a cost programme with a short-term aim of achieving quick wins in relation to the non-personnel cost base as well as our support functions.

Pillar 3, commercial momentum gained. We also strive to reverse the trend of our income development. While we are still facing headwinds due to increased funding costs and margin deterioration, we are confident that we have a set of initiatives at hand that will help strengthen our income base. On top of strength and discipline, in terms of pricing and capital allocation, we will also harvest the benefits of recent changes, including the integration of private wealth management into our banking units to better capture the investment potential of our customer base and the investment in our capabilities to more dynamically manage our banking book. The more structural levers, including digital journeys and differentiating our service models to capture the full potential of our client wallets, are expected to generate a relative impact from 2021 onwards.

Slide 13, please. Pillar 4, complexity reduced, agility improved and the business further digitised. Product simplification is a starting point for optimising and digitising our core processes. We will define a core and consistent offering across countries to meet the demands of our target customers. The target offering will be a starting point for defining efficient and homogeneous target processes and rolling out large-scale end-to-end digitisations. We will start with our core processes, such as housing and financing. And essentially, we have already started those. We have tried to launch similar exercises in the past, this time, to achieve the best results and avoid silo thinking, we will adopt a truly agile way of working as a first large effort to bring this to life.

Pillar 5, accountabilities and leadership promoted and developed. We will look to integrate our new ambitions into the Danske Bank purpose, updating and refreshing the solid foundation we already have to date to create something that resonates with our employees, customers and society. We will drive broader cultural change, investing in short- and long-term efforts to further empower employees and create a more open culture. The introduction of Enterprise Agile will be a significant component of this. We will further improve our performance management cycle by realigning our incentives with focus on execution and value while driving transparency, simplicity and consistency across the business.

Pillar 6. I'm pleased that Berit has taken over the responsibility for delivering on our societal and sustainability ambitions. As such, we will come back with a more detailed and nuanced plan as Berit continues to drive the agenda. The primary focus will be on making sure that the ambitions are integrated in our day-to-day work. For example, realigning incentives for our employees, training portfolio managers in ESG investing to make sustainable investing an integral part of the business and reengineering processes to be more sustainable. Until then, we will continue to invest in a number of specific societal and sustainability priorities, such as our volunteer work, aiding entrepreneurs and delivering programmes to improve financial literacy.

Finally, we will look for ways to continue driving an inclusive culture, such as the use of strategic workforce planning and succession planning to promote greater levels of diversity across the organisation.

Slide 14, please. And over to Jacob.

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**Jacob Aarup-Andersen – Danske Bank – CFO**

Thanks, Chris. Our AML-related costs will peak in 2020. AML costs are driven by FTE increases to strengthen our lines of defence and also to increase the capacity for handling KYC or ODD and monitoring processes as well as costs for handling the Estonia case. The AML digitalisation work that we announced in Q1 will, of course, continue as planned with investments over the next two years. After 2020, we expect AML costs to gradually reduce and reach a steady-state level of DKK 1.1-1.3 billion in 2023.

Slide 15, please. So let's have a look at our new ROE ambition of 9-10% in 2023. Our starting point is the ROE for the first nine months of 2019 adjusted for one-off items. In 2020, we see a continued impact from funding issuance, margin pressure and difficult financial market conditions. Further, we assume normalising loan impairments as well as higher AML spend as just described on the previous slide. In addition, we are making significant investments in 2020 to support our 2023 ambition.

In the period from 2020 to 2023, we are going to reduce gross costs significantly and increase operating efficiency. This is crucial to deliver on our ambitions and covers five different levers, including digitising housing and financing processes, refocusing our support functions as well as reinforcing non-personnel cost discipline. We also expect material savings, as the AML cost level normalises at the DKK 1.1-1.3 billion level in 2023.

Income growth is expected to contribute positively to all major income lines. We expect broadly unchanged dynamics for loan growth, and we have set key strategic priorities to deliver income growth. We will continue to improve the digital customer experience, revise service models, integrate Wealth Management products into banking and leverage the full potential of our partnerships. Macroeconomic and regulatory headwinds come from inflation, normalisation of loan losses, regulatory effects and a higher nominal equity. We maintain our dividend policy of a pay-out ratio of 40-60%, and our core tier 1 target is above 16% in the short term.

We will continue to adapt our capital targets to the developments in capital requirements and will maintain a strong capital position throughout the period. To summarise, the ambition of a 9-10% ROE in 2023 is driven by significant investments in 2020, followed by significant cost initiatives and income growth. We are assuming unchanged macroeconomic conditions, including unchanged interest rates and normalising impairments. We think this is a realistic yet ambitious level of profitability given the environment we're operating in.

Slide 16, please. As the preceding slide shows, a critical part of achieving our 2023 ROE ambition is to become a leaner, more efficient organisation. While we aim for a significant gross reduction of our current cost base, our most important ambition is to simplify our business processes and ensure a superior delivery for our customers. We strongly believe that we will achieve a better service model at lower cost.

In the past two to three years, the focus was on managing the AML case, now we will again turn our focus to operating efficiency. We will be employing five main levers over the course of 2020 as we drive towards the longer-term goals, and we expect to see the initial impact of these measures to be reflected already next year. As a first step and underpinning each of the others, we intend to reduce the complexity in the business, firstly, by becoming more focused in our product range and increasing scalability and synergies across the Group. For example, harmonising the retail operating model across the Nordics. And secondly, by simplifying our service model, we will be able to deliver higher value to our customers with a leaner organisation. One example is the measures for FI&C mentioned earlier.

As a second step, building on this less-complex foundation, we intend to digitise our core customer journeys to make it easier, both for our customers to engage with us and for our staff to serve them. This is a process that is already underway, for example for housing, but will be the focus of our accelerated investments in 2020 to create a market-leading platform in coming years. Beyond structural changes, we will also be focusing on reducing day-to-day costs associated with running the business. There is opportunity to be more disciplined within non-personnel costs in particular. Tighter control within consulting, marketing, travel and business costs should drive the short-term impact in 2020, but in the longer term, we will revisit our governance model and push for structural cost reductions.

There is also an opportunity to run our support functions more efficiently. Key areas that we'll be looking into include the following: realising synergies from reorganising activities to avoid duplication of activities and establishing one owner; reviewing our service model, also internally, to reflect the needs of a less-complex organisation; we will terminate activities, focus deliverables and reduce the service level in areas where it's not critical for our business success or regulatory compliance.

Thirdly, we will leverage the potential of technology and automation within our support functions.

And then lastly, and as we already touched upon, AML costs will peak next year before returning to a steady-state level by 2023. During this time, we intend to develop and integrate AML processes into our day-to-day business workflows to enable us to operate to the highest standards in an efficient manner, building on digitalisation. Beyond costs, especially the first and the second levers will contribute to income growth.

Slide 17, please. In general, we expect a challenging environment for all of our businesses in the years to come. The persistently low interest rate levels and continuous margin deterioration for assets under management, just to name two examples, implicitly require that we first have to compensate for these effects before being able to realise net growth. Yet, we believe that Danske Bank has a strong brand and team. We have a strong position in our core markets and have a clear potential to capture not only the expected market growth but also a larger share of the pie. While each business unit follows its individual strategy targets to its customers, we have defined four core initiatives that we will address at Group level to push income growth and harvest synergies.

First of all, the digital customer experience. As mentioned on the slide before, the digitalisation of our core customer journeys is a key enabler of income growth. We strive to offer a state-of-the-art customer experience that brings together the expertise of our staff and digital offerings. Improved service quality, ease of doing business as well as the speed of delivery are our key aspiration.

Secondly, revising our service model. Our service model in various areas still relies on product or pure quantitative criteria. Looking ahead, we will strive for more sophisticated differentiation based on customer behaviour and customer needs. We will invest in our data and analytics capabilities to enable the early identification of the right service model. This will also support our advisers in acting more proactively to offer the right products at the right point in time to our customers.

Thirdly, about fostering integration. As a key part of our reorganisation in September, we integrated private wealth management into Banking DK and Banking Nordic. We are convinced that the increased proximity after the integration is going to place us in a much better position to capture the full potential of our customers to serve them with their investment needs. In parallel, we will also establish integrated sales channels between Wealth Management and the banking units to further push this.

Fourthly, strengthen our product offering and leverage partnerships. While our general ambition is the simplification of our offering in several areas, we will strengthen our offering to better serve our customers, either by developing in-house products or by enabling third-party partnerships. For example, establishing a digital customer platform for our C&I customers that allows the efficient on-boarding of new products.

Besides the strategic levers outlined, we will also work on the efficiency of our balance sheet. We expect that a more dynamic management of our banking book, applying more sophisticated steering of our liquidity and interest rate risk without increasing the absolute risk levels, can contribute a relevant upside to our NII. Furthermore, we are still impacted by higher funding costs as a result of the Estonia case, especially due to the need to issue non-preferred senior debt. We have not factored in any structural upside in our plan, yet we would expect that we will benefit from improved funding conditions in the mid-term.

Slide 18, please. And over to Chris.

**Chris Vogelzang – Danske Bank – CEO**

Thank you, Jacob. Today, we have discussed the root causes that prevent us from unlocking our full potential, our 2023 ambitions and key initiatives to deliver on these ambitions. We now push to deliver in the short term, including the initiation of a Group-wide cost programme.

Following today's announcement, we will start executing on new initiatives to bring our cost base under control, invest strategically in our ambition and launch a Group-wide digitisation and enterprise agile agenda. And we'll measure and update continuously on the progress of our efforts. As said, we expect 2020 to be a crucial year to deliver on our ambitions. And therefore, we will go into execution mode as soon as possible.

Slide 19. Those were our initial comments and messages. We are now ready for your questions. (Operator Instructions).

Operator, we are ready for the Q&A session.

**Operator**

(Operator Instructions) Our first question is from Jakob Brink from Nordea.

**Jakob Brink – Nordea**

Just the first question, I'll have them one at a time. The first one, if I try to estimate your assumed income growth, given your Slide 15 and the roughly two percentage points add-on to ROE from income growth, it translates into on consensus 2019 around 2.9% -- sorry, on consensus 2020 revenues that translate into around 2.9% compounded growth from 2020 until 2023. I know you just went through the page, Jacob, on page 17, and you mentioned something about a material positive impact to NII from balance sheet optimisation, but could you please repeat that part and maybe give a bit more quantitative on how you should expect to grow revenues 3% per year, given that's not exactly what you have been doing in recent years?

**Jacob Aarup-Andersen – Danske Bank – CFO**

Okay. Thank you, Jakob. Thanks for the questions. So in terms of the assumed income growth, you're saying 2.9% on your calculations. I think that sounds around the numbers that we would also get if we do the same math. So I think you're pretty spot on, on that. In terms of the components there, and you asked about whether we could give some more details. First of all, I would also remind you that when you look at this bridge, obviously, all of these are ranges. And when you look at the income growth, it is also -- as some of you have pointed out during the day here, it's also clear that we can hit the 9-10% with some variability on the income growth side.

What is in this plan is roughly 3% CAGR when you do the math as you say. There are a number of reasons why we believe this is the right ambition to have as a team. When you look at the assumptions behind, we think they are ambitious but not heroic. The growth assumptions that we have across our core markets are a continuation of the growth trends we have seen in terms of the volumes we've seen and in terms of our position in those markets. So, a continued good growth in our challenger markets combined with the stabilisation of our Danish franchise is part of the plan.

We also assume that we will enhance our income growth by seeing a better driver of our ancillary business. So we expect to be better over time at driving ancillary business and fee business, especially in our challenger markets, where you can say we still have upside potential in terms of our cross-sell potential. And that is obviously, especially within our Wealth Management products.

You asked specifically around the balance sheet optimisation, and this is, as you say, as we also pointed out here, it's a Group-wide project driven by Treasury across the bank. This pertains to a number of things, it pertains to things such as the liquid asset buffers, our long-term funding programmes, but it's a -- also in terms of our capital utilisation and the use of our balance sheet across the different business units. So working more efficiently with our balance sheet, working more intelligently with our balance sheet and also utilising it better in terms of driving customer business. There is nothing in this plan that drives a different risk profile than the one you've seen today. It's a question of, you can say, having a more holistic perspective on our balance sheet also from a central perspective. We do believe that those efforts driven out of Treasury, both within Treasury but also throughout the business units, will be one of the drivers on the top-line. Hopefully, that gives you a little bit more colour.

**Jakob Brink – Nordea**

And then just a final question on the macro and regulatory bucket. I have discussed this with IR, but I would like to hear your view as well because if you take 2.5% cost inflation on sort of an underlying cost base in 2020, that basically utilises or uses the full 1-1.5%. It gets actually to the upper end of 1.5% of the range, which means that what you also put in this one, i.e., an increase in the nominal equity, there's not really room for that in the 1-1.5%. So how should I read this?

**Claus I. Jensen – Danske Bank – Head of IR**

Yes. Jacob, as you already said, we have had a discussion around this earlier today. And I think it's quite clear from that discussion that we cannot discuss very specific numbers as the bridge entails spreads on different buckets. And that's why it's up to the reader's own underlying assumptions on where we will get. We believe that the macro and regulatory bucket is able to contain both inflation, other macro and also the impact from higher equity.

**Jakob Brink – Nordea**

Just to make sure, there's not like you have included any fine, which could then reduce the equity?

**Claus I. Jensen – Danske Bank – Head of IR**

No, we have not made any fine assumptions, and we simply cannot make any comments on fines. But as we said, we assume a higher nominal equity by the end of the period compared to the beginning.

**Operator**

And our next question is from Mads Thinggaard from ABG.

**Mads Thinggaard – ABG Sundal Collier**

I think the first one is relating to the cost reductions. In the bridge, you were just discussing here, the DKK 5 billion, I mean, gross cost takeout. I mean most of that is not from compliance costs down, but rather trimming ordinary costs? And could you put a bit of flavour and perhaps not breaking it into years, but just stating whether that will be front-end loaded or back-end loaded in your plan here?

**Chris Vogelzang – Danske Bank – CEO**

Thank you very much. This is Chris. We'll be investing in our digitisation processes during 2020, and the effects of those will be seen in the years afterwards, and they will come in gradually. So not front-loaded nor back-loaded but gradually in 2021 and 2022.

**Mads Thinggaard – ABG Sundal Collier**

Okay, perfect, understood. And then the second question is on, now you have kind of a nominal cost-cutting ambition. And you have a cost/income target that is -- perhaps had a bit of flexibility, but still it is kind of a target that, I mean, would be impacted if income drops, what would kind of be the levers there -- I mean yes, what would you do if income is lower than the 2% added to growth that you show in the bridge?

**Chris Vogelzang – Danske Bank – CEO**

Okay. This is Chris again. I can make this extremely clear. If income does not grow as we are expecting, then we will still hit the 9%. So you can make up your own mind what we then do, but we will most likely have to increase our cost cutting, and we will. So 9% is the absolute minimum for us.

**Operator**

And our next question is from Sofie Peterzéns from J.P. Morgan.

**Sofie Peterzéns – J.P. Morgan**

It's Sofie from J.P. Morgan. So I was wondering if you could just give a little bit more details around where the cost savings are coming from, the DKK 5 billion that you mentioned in the report? And also -- yes, if you can give details on how we should think about the net cost saves over the next 3 years?

**Jacob Aarup-Andersen – Danske Bank – CFO**

Thank you, Sofie, Jacob here. So thanks for the questions. I guess if you talk about net versus gross, I guess we give you the gross number here, and we also give you our inflation assumption of 2.5%. So hopefully, that should give you the numbers to work with. But I guess more importantly to the core of your question in terms of where they're coming from and giving you some more colour, I guess as Chris also alluded to in his intro, we've already initiated recently a larger cost transformation programme where we will be focusing on all of our non-personnel costs. So that is something we can start focusing on immediately. And we do believe that there is a strong cost potential in our non-personnel costs across all categories.

At the same time, all of the investments that we are doing over the next 12 to 18 months in terms of digitalisation of our end-to-end journeys, especially core journeys, like the housing and the financing journeys, et cetera, that will bring a lot of efficiency gains out of it. So we think these major journeys, as we see it, and as we work through it, there are significant structural cost takeout potential by digitising these journeys. And they will be one of the core components of driving the cost efficiencies, beyond the more, you could say, ordinary cost transformation programme around non-personnel costs. So hopefully, that gives you a little bit more colour.

**Sofie Peterzéns – J.P. Morgan**

And maybe a little bit more around the divisions, how should we think about the cost cuts across the divisions? Will it be equally split between the various divisions? Or is it more tilted towards certain divisions? I mean if you could give a little bit more details around that.

**Jacob Aarup-Andersen – Danske Bank – CFO**

Listen, I think that's completely fair. I think first of all, I think one of the core tenants of journeys is the fact that it goes across the bank. And therefore, you will see cost takeout across different parts of the bank. But what I'm referring to here is, obviously, a lot of it is back and middle-office focused. And therefore, when you look at this, we will obviously do our utmost to ensure as little impact on the frontline as possible as we do this, it's very much around taking out the core back and middle office around these processes. But the structural takeout you will see across the units. I won't point to a specific unit that will be driving more than the others, but we do have major journeys across all of them.

**Sofie Peterzéns – J.P. Morgan**

Okay. And you have spent by 2023, DKK 15 billion in money laundering and compliance costs, how do we know that this is kind of the end. Do you think that -- it seems that it's a spend that continues to never stop? What makes you certain that DKK 15 billion by 2023 is enough that it doesn't increase again by DKK 1 billion or DKK 2 billion per year?

**Jacob Aarup-Andersen – Danske Bank – CFO**

So the DKK 15 billion you're referring to, where do you see that?

**Sofie Peterzéns – J.P. Morgan**

So basically, if I go to your slide with AML costs, and I add up all the costs between 2017. So Slide 14, if I add up DKK 1 billion for...

**Jacob Aarup-Andersen – Danske Bank – CFO**

Fine. This is the cumulative cost over the years. Okay. Yes, fine. Well, I guess just taking a step back here, a lot of what we are looking into and when we talk about a normalised AML cost of DKK 1.1-1.3 billion. That is the cost of running a modern bank in today's society. So a lot of these costs are part of running a bank. What we have seen in the recent period and that's what we see in 2020 and somewhat in the following years as well is that we have a higher level than normalised in terms of our investments within this area, and that is to bring our operations up to a level of automation and digitalisation that we think is appropriate to hit normalisation. So a good part of this, for us, is not an extraordinary investment in the AML and compliance areas. That is the ongoing part of running a bank. The normalised cost around compliance is no different from us than the cost of running a credit organisation or any other part or any other risk organisation in the bank.

**Sofie Peterzéns – J.P. Morgan**

Okay. And then just a final question. Do you have any plans of introducing negative interest rates in Denmark?

**Chris Vogelzang – Danske Bank – CEO**

This is Chris. What we have said consistently, so our message is not different. We do not intend to introduce negative interest rates to the ordinary account holders, i.e., the vast majority of current account holders. We are monitoring the situation with regards to the other segments. But we do not have plans at this particular time to extend it.

**Operator**

And our next question is from Per Grønborg from SEB.

**Per Grønborg – SEB**

On the business plan, DKK 5 billion in cost reduction or approximately 20% of your group cost. The only segment where you come out with a specific comment today is for the FI&C business, where you intend to cut direct staff by 15%. Somehow, the only area you address specifically is going to cut less than the Group cost. There's probably a reason why the equity margin is somewhat sceptical to your long-term ambitions. What's your plan effectively giving the market more clarity on how you will deliver on this programme, because it's pretty evident when I look at your share price today, the market doesn't believe in your story?

**Chris Vogelzang – Danske Bank – CEO**

As we've said before, we will invest heavily into digitisation processes, which will have a significant effect on the way we run our back and middle offices. Apart from the cost savings we've just mentioned, we believe that investing in these particular processes will give us the opportunity to reduce those costs significantly.

**Per Grønborg – SEB**

But no plans of giving us the visibility? We saw another Nordic Bank just last week, actually, with a month's notice having called for CMD where they want to explain how they want to achieve their plans. Right now, we have 30 minutes to run a Q&A. Is that what we should expect to get?

**Chris Vogelzang – Danske Bank – CEO**

That's your question.

**Claus I. Jensen – Danske Bank – Head of IR**

I think there that we have tried to manage expectations as good as possible. We have stated that the plans we have published today are an overall Group plan in order to restore the profitability and the performance of the bank. And we have also said that we will give updates during that process. I think that's what we can comment on for now. We do not have a CMD on the agenda, and that's not what we have agreed to deliver today.

**Per Grønborg – SEB**

Is this also a reflection of this more being a top-down plan, more than it's actually, let's say, a bottom-up plan you are presenting to us today?

**Chris Vogelzang – Danske Bank – CEO**

No, I -- this is Chris. I'd like to say something different. We went, in order to define the possible cost reductions in this business, in great detail. So we are, as a management team, not committing here to the whole market saying that we believe that we can reduce the cost base by gross DKK 5 billion if we don't believe that it is very feasible. If you just look one step deeper into our economics, and if you see where our costs are, you will see that taking out DKK 5 billion of costs by automating some of our processes, and if you see, it's very, very feasible. It's not easy, but it's very, very feasible. So it's not a goal reasoning, like target reasoning, like this is what we need to have. No, we looked at every process, and we looked at every process and the associated current costs with that. So I don't agree with what you are saying. This has been grounded very well.

**Operator**

And our next question is from Antonio Reale from Morgan Stanley.

**Antonio Reale – Morgan Stanley**

I've got two questions, please, one on the NII outlook and the second one on fees. So the first one, we've seen your capital requirements go up and so has your MREL number. You've issued the bulk of your senior non-preferred bucket already this year, but you now have another DKK 41 billion to go, which is a big headwind on your NII, and this could be up to DKK 350-400 million my numbers depending on price assumptions. Is it fair to assume that a good portion of your 0.5% ROE drop in operational effects next year comes from lower NII? That's the first question.

**Jacob Aarup-Andersen – Danske Bank – CFO**

Hi Antonio, it's Jacob here. So I think that's a fair assumption, yes. We made it clear that when we look at the bridge towards 2020, the operational bucket, that there is a clear impact from the funding issued in 2019, but also from new funding issued in 2020 at unchanged spreads. Obviously, you can make up your assumption in terms of what we can issue at but with no other knowledge than what the market tells us, we've been assuming where we are currently. So yes, I think it's a fair assumption.

**Antonio Reale – Morgan Stanley**

And on the fees then, we've seen a nice rebound this quarter across divisions, except for Corporates & Institutions, which have remained relatively weak. Can you share a bit more colour there, more broadly for the fees into next year? For the Group, how sustainable you see those numbers? And maybe share what you're seeing in Corporate & Institutions, where I think P&L has been particularly weak?

**Jacob Aarup-Andersen – Danske Bank – CFO**

Yes. Let me do that. So first of all, as you know, we don't guide on individual lines into next year, we may do that when we come out with the full year results. But at this stage, we've given you a more general guidance. But when we look at fees, if you look at the dynamics we've seen so far, if you look at fees year-on-year, they're up 3% year-on-year in the first nine months. And we are seeing a big positive effect from the remortgaging in Denmark. And we're also seeing a positive effect from the inclusion of SEB Pension now fully in the year. We also, obviously, sold Danica Sweden in May. So do remember that Danica Sweden falls out when you look at the numbers next year, but that should probably be mitigated by the fact that we had a negative from Flexinvest in the second quarter.

So all in all, if you take that out, we've had some positives and some negatives this year impacting. But no doubt that the biggest, you can say, short-term driver of fees has been the remortgaging activity in Denmark in the last couple of quarters.

When we look at C&I specifically, you were asking about that, there's no doubt that when you look at Q3, it has been a very volatile quarter also in terms of financial markets. That does impact the fee business in C&I more than it impacts the fee business in any other area of the bank, given that a good part of the fee business in C&I comes out of the capital markets business. And as you know, capital markets businesses very quickly become volatile with markets in terms of the fee-generating capabilities. So we don't see this as anything structural, but more a sign that we've been having volatility in markets. So we are generally quite constructive on the fee outlook, but I would refrain from giving you specific guidance on where we're going next year.

**Operator**

And our next question is from Robin Rane from Kepler Cheuvreux.

**Robin Rane – Kepler Cheuvreux**

So on the capital, you say in the assumptions that you see some regulatory effects from Basel IV. Can you give some colour on what kind of RWA inflation you assume as one?

**Claus I. Jensen – Danske Bank – Head of IR**

We can give you a little bit of colour. We cannot provide a specific number, but we can confirm that we have included some RWA inflation. And that is, of course, primarily coming from Basel IV. There is no doubt that the regulators are overall trying to accelerate internal model updates in order to avoid a cliff effect when we approach 2023. So we expect that there will be an update of internal models, including the EBA guidelines. And we also expect that we will look into revised standard methods and constraints on internal models, and that also includes FRTB, CVA risk charge and IRB restrictions. That is what we are including in our assumptions around RWA. However, output floors are not part of the plan in this bridge as we do not expect that to have an effect until after 2023.

**Robin Rane – Kepler Cheuvreux**

Okay. And then the Pillar II add-on from the FSA from -- was it IT complexity or so, is that now included in the requirement or...

**Claus I. Jensen – Danske Bank – Head of IR**

That is now included. Also the add-on we got from the product risk, that's also included in the Q3 numbers.

**Robin Rane – Kepler Cheuvreux**

Okay. And then lastly, how should we think about the short-term 16% target? Is that contingent on the development of potential consequences of the AML affair? How should we think about the 16%?

**Jacob Aarup-Andersen – Danske Bank – CFO**

It's Jacob. Thanks, Robin. So it's correct that we increased the capital target to be above 16% now. And we do that in light of the increased capital requirement. And I wouldn't read anything into it in terms of you said specifically around the AML situation, et cetera. We have said a while ago when we raised capital targets for the first time in a while, we said at that point that it also reflected the general uncertainty there was around capital requirements. We don't think that has changed specifically. Yes, there is at least a dialogue with regulators around the AML case, but there is also an uncertainty around the phasing-in of Basel IV and how that will be implemented in an EU and in a Danish context. So there are those uncertainties, and therefore, that is also reflected in the way we set the target.

**Operator**

And our next question is from Johan Ekblom from UBS.

**Johan Ekblom – UBS**

Just two questions. First of all, we've kind of did the math before that the midpoint implies something like a 3% revenue growth, but have you assumed any underlying revenue attrition from the cost cuts? So is there sort of real underlying even beyond 3%? So that would be the first question.

And then secondly, just in terms of thinking about the -- what's investment versus what's restructuring cost, et cetera? So when we think about the DKK 2.5 billion cost increase that you're flagging for next year, is all of that investments? Or is there some proportion of restructuring cost included in the DKK 28.5 billion that will be upfront, and therefore, kind of be a quick win in '21? Or how should we think about the one-off components in this plan?

**Jacob Aarup-Andersen – Danske Bank – CFO**

Thanks, Johan. Jacob here. So thanks for the two questions. On the first one, in terms of the revenue assumptions, yes, when we look at our assumptions in terms of income growth, we are naturally factoring in the different headwinds we have. One of those headwinds will be the potential loss of business. If we look into our cost-cutting plans, and there are areas which we will focus less on or where we will focus on fewer products or other client groups, et cetera, those types of plans obviously will lead to less revenue in those parts. So this is a net number when we talk about income growth. There is not a net reduction somewhere that we haven't included in the bridge.

In terms of the up to DKK 2.5 billion of investments that you referenced, yes, there is an assumption in there that we will be spending some amount on severance. So that is what you would refer to as restructuring. But the vast majority of the money we are talking about here is for what you just referenced to as real investments. But obviously, as part of those investments and in terms of also delivering on the longer-term efficiency ambitions, there needs to be some level of severance and restructuring.

**Johan Ekblom – UBS**

And does that mean that as these investments pay off over time, we should expect a higher recurring restructuring cost, I guess out until 2022 to then be kind of fully reflected or fully implemented by 2023?

**Jacob Aarup-Andersen – Danske Bank – CFO**

No, we wouldn't give you that straight guidance. We cannot rule out that there could be potential amounts set aside in '21 or '22, but it's not a material factor that we would otherwise be guiding you on. But as we go along, and as we implement the plan, I can guarantee you if I gave you a very clear guidance on what we think those effects would be in '21 and '22, I would be precisely wrong. And I'd rather be fairly right here by telling you that the vast majority of these investments happen in '20 as we have laid them out.

**Johan Ekblom – UBS**

And so it's fair to assume that the majority of the DKK 2.5 billion will be gone already in 2021 rather than sort of a gradual stepdown?

**Jacob Aarup-Andersen – Danske Bank – CFO**

It's fair to assume that the majority of these investments will be gone in '21, yes.

**Johan Ekblom – UBS**

Yes. Well, I guess that's a confirmation.

**Operator**

And our next question is from Jacob Kruse from Autonomous.

**Jacob Kruse – Autonomous**

I have two questions. Firstly, on the trading line, you gave some guidance on the sort of structural headwinds and where you were and why you are where you are at this nine-month stage. So if I look at this on a sort of asset basis, should I think about your normal trading in the current cyclical environment and with the current structural headwind that's sort of a DKK 3.0-3.5 billion annual level? And regardless of what that level is, would you see a headwind on that number from the restructuring you're planning, or the changes you're planning to that business area?

And then my second question was just on AML. You talked about the completion time for your internal reviews as being Q4 2020. Do you think that Danish regulators can come up with their final verdict before your internal investigations are concluded? Or does this also mean that regulatory decisions will be more than a year out?

**Jacob Aarup-Andersen – Danske Bank – CFO**

Thanks, Jacob. Just to actually take your last question first, and then I'll let Claus speak about the trading line. Just on the AML side, yes, we talk about our internal investigation, current estimate being Q4 2020. That is our internal investigation, and we really have no view on what that means in terms of regulators and their deadlines. We will refrain from speculating in terms of what timelines regulators are working with and what actions they will take. So this is purely an update on where we are on our internal work. And let me hand over to Claus.

**Claus I. Jensen – Danske Bank – Head of IR**

Yes. Thank you, Jacob. I don't think you can see this as us having started to guide on trading income because that is definitely not the case. The bucket that is called cyclical is what we see now as being a potential in a best-case scenario. The structural part, which we are commenting on, which is up to DKK 1 billion, that is structural and that is of course less likely that, that could come back to the market. So what we are trying to illustrate is that a return to the levels we saw in 2016 and 2017 is not very likely. But no guidance on trading income, I think that's the message.

**Operator**

And our next question is from Richard Smith from KBW.

**Richard Smith – KBW**

Most of mine have been asked. Just one really in terms of the Basel IV impact that you're assuming there. I noted your comment earlier that it doesn't include an output floor, I think was what you said. Just wondering -- I just wanted to confirm really, but in terms of the op risk aspect, presumably, again, given that you're not including any view on fines, they would also not include any headwind on operational risk from fines that might come through?

**Claus I. Jensen – Danske Bank – Head of IR**

Well, that's a part of what we are looking also into -- up to 2023, that is that there could be a revision of the operational risk, yes.

**Operator**

And our next question is from Martin Gregers Birk from Carnegie.

**Martin Gregers Birk – Carnegie**

I guess last time we met, Chris, in August, you said that the focus right now was on execution. And if a larger overhaul of the strategy was needed, it would be within 12 to 18 months. Is that still how you see it? Or is this what we are going to get? That was my first question.

**Chris Vogelzang – Danske Bank – CEO**

No, we as a team are convinced that we have to implement the things we have presented today, period. Obviously, we all keep on thinking, so if circumstances change significantly, et cetera, we might have to have a look at things again. But I think it is extremely important that this bank focuses on the programme we are now announcing, which is a cost reduction, which is digitisation, which is, et cetera, et cetera, et cetera, because we believe that that is the right way forward and that we do not have an essential strategic problem but more of an operational execution challenge.

**Martin Gregers Birk – Carnegie**

Okay. Just back to an operational question. I've been tracking your loan growth, especially in Sweden, and it has been looking fairly poor and also in terms of pricing, you guys have been looking slightly off. What should we think about? Is that a purposely change of strategy? Or has something changed?

**Jacob Aarup-Andersen – Danske Bank – CFO**

Thanks, Martin. It's Jacob here. So it is correct, if you look at Sweden over the last couple of quarters, we've slowed down our growth a bit. And if you look at it, it's driven by a couple of things. But the overarching reason is that we have decided to take a little bit more of a cautious view in terms of the competitive environment and the market environment we've been seeing. We need to constantly, as we promised you, grow with a good and profitable growth. And we think there are some segments where we've been holding back a little bit in the last couple of quarters, it has nothing to do with any longer-term view on the Swedish market or anything, but there's just been pockets where we decided to pull a little bit back from a risk perspective. I think we've been very clear about that, that it's a conscious choice, and it doesn't change our strategic focus on Sweden in any way.

**Martin Gregers Birk – Carnegie**

Okay. And just a quick question here. Once you are done with your AML investigation in Q4 2020, are you guys going to update the market on whatever findings you guys may have?

**Jacob Aarup-Andersen – Danske Bank – CFO**

There are no plans for any big external report or anything like that, like we had September last year. What we have made clear to you is if we find something that is material for financial markets then we will obviously update financial markets. But there's no plan for an external report or anything like that this time around. But we will update you if there are any material findings that are relevant for you.

**Operator**

And our next question is from Riccardo Rovere from Mediobanca.

**Riccardo Rovere – Mediobanca**

Just one question if I may. Can you help us in trying to better understand how your financials profitability could progress from 5-6% ROE to 9-10% ROE in 2023 because 2023 is a bit far away? Shall we assume that it's going to be a linear progression? Or should we assume that the cost savings, the cost benefits should be more back-loaded, so more visible in 2023 rather than 2021? How should we think about the phase-in of the moving between 5-6% to 9-10% because from here to 2023, anything could happen?

**Chris Vogelzang – Danske Bank – CEO**

Okay. Thank you. As I said earlier, you can assume a linear progression from 2020 to 2023, where 2023 full year results should represent a 9-10% ROE. So a linear progression.

**Riccardo Rovere – Mediobanca**

Okay. And just to get to beyond the sense if I understood it correctly in a previous question. With regard to the, let's say, to the set of information on the bridge on how you're going to get to 9-10%. This is the only set of information we will be given, right? There's not going to be any Capital Markets Day, there is not going to be anything more on top of today, unless the usual discussions with IR and so on, correct? There is nothing?

**Chris Vogelzang – Danske Bank – CEO**

You are correct.

**Operator**

And our next question is from Adrian Cighi from RBC.

**Adrian Cighi – RBC**

This is Adrian Cighi. Two questions from my side, please. They're both follow-ups. One on the Estonia case and one on the targets. On the Estonia case, can you confirm that the enhanced methodology has been initiated at the request of the authorities? And the second question on the target, just following from Riccardo's question. You've changed the outlook on 2019 several times over the last 12 months, what would you say that your degree of confidence in the 2023 targets will be? Is this something that you have the degree that you can flex the self-help component if the revenue doesn't come out right? Or where you expect it to go?

**Jacob Aarup-Andersen – Danske Bank – CFO**

So thanks for your questions. Your first question was in terms of the sanctions work, whether that had been initiated at the request of regulators? I'm not fully aware where you have that information from. I stated at the time of the publication last year, we said that we had looked at customers, but further work remained on the sanctions side. We are now reviewing associated persons and customer transactions. So the tools that we've used to perform the sanction screenings have gradually been enhanced and also reapplied to customers, and that's a methodology that we constantly share with authorities, so we have a good dialogue with authorities on that. So we're screening against sanction lists, and we're also looking for connections to sanctioned countries. That's the steps that are all part of our ongoing efforts to continually assess and test that we are identifying the key facts that are relevant in this case and obviously for authorities. As I said earlier also, if we find something material, we will of course update the financial markets via the usual channels.

Then on the other question in terms of the degree of the targets and the fact that we have seen a change of guidance over the last couple of quarters, I think it's fair to say that if you look across the Nordic region, I think most of our competitors as well have seen the same. We are in an environment that has changed quite dramatically over the last couple of quarters. And one of the things we've seen is a significant change also in the rate environment that we're dealing with and the underlying macroeconomic environment. So whether that affects our ability to create a 2023 plan and deliver on that, I wouldn't infer anything from that. As you point out yourself, when you look at the plan, a lot of this is things that we drive ourselves. And therefore, the vast majority of this plan is in our own making and is within our own ability and within our own reach and scope. As Chris said earlier, if we end up struggling on some of these levers, we will have to double down on some of the other levers. So there's a strong focus on executing and on delivering here. And as you will see, the plan has -- most of its components are things that are within our control.

**Operator**

And our last question is from the line of Geoff Dawes from Société Générale.

**Geoff Dawes – Société Générale**

It's Geoff Dawes here from SocGen. Hopefully, a couple of quick questions as I'm last to fire. First of all, on net interest income, you seem to be guiding that it'll be down year-on-year in 2020 versus 2019. Can you just confirm that that is what you're telling us? And second of all, if that is the case, when do you see some sort of inflection point or turning point in the net interest income run-rate coming through as the funding costs come through and everything else?

And then the second question is a very quick clarification on the 40-60% dividend policy, just to be clear on the assumption – that will be on reported net income, I assume, rather than net income less exceptional items and restructuring costs and everything else. Those are the two questions.

**Jacob Aarup-Andersen – Danske Bank – CFO**

Thanks, Geoff. Jacob here. So I thank you for asking the clarifying question on NII. What I have been responding to is whether or not we will have a negative funding impact next year. And I can confirm that we will have a negative funding impact next year, both from the annualisation of the 2019 issuance but also on the issuance in 2020. Whether that means that NII, the reporting line itself will go down, we haven't been as specific towards that. But this is one of the components in the NII line, no doubt about it. We are also making it clear that we think that the competitive environment that we are looking into next year, we think that remains at the same high competition level that we're seeing right now. But we haven't guided you specifically on whether that line goes up or down.

In terms of the 40-60% pay-out ratio, yes, well, we have always historically been calculating our pay-out ratio on the reported net income. If the Board decides to do anything differently in the future, that will be up to the Board. But the policy of Danske is that the pay-out ratio is calculated on the reported net income. So that's correct.

**Chris Vogelzang – Danske Bank – CEO**

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

So thank you very much all and hope you have a great weekend.