Conference call

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Investor Relations

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Claus I. Jensen – Danske Bank – Head of Investor Relations

Thank you, operator, and hello, everyone. Welcome to the conference call for Danske Bank's financial results for 2020. Thank you all for taking the time to listen in on this call today. My name is Claus Ingar Jensen, and I'm Head of the Investor Relations team. With me today, I have our CEO, Chris Vogelzang; and our CFO, Stephan Engels.

Slide 1, please. In today's call, we will present Danske Bank's financial results for 2020. We aim to keep this presentation to around 30 minutes. After the presentation, we will open up for a Q&A session, as usual. Afterwards, feel free to contact our Investor Relations department if you have any more questions. I will now hand over to Chris.

Chris Vogelzang – Danske Bank – CEO

Thanks, Claus. In many ways, the year 2020 was a challenging year. The global society, and of course also the banking sector faced major disruption caused by the pandemic. Disruption that had a huge impact on the way we live our lives in general terms and more specifically on the way we conduct our business and interact with our customers. One of our key priorities in 2020 was a strong and dedicated focus on our 2023 plan to become a better bank for all our stakeholders. In many areas of the bank, we have made tangible progress with our transformation and we clearly see 2020 as a year where we turned a corner and laid the foundation for continued execution of our journey for the coming years. One of the key building blocks for our transformation was the redesign of our organisation we have now launched a new commercial and agile organisation.

We have reduced the number of business units from 4 to 2 with a clear purpose of decreasing complexity and simplifying the organisation. This is key for us in order to ensure high-quality live processes and make us a more competitive bank. The outbreak of the pandemic has had a direct impact on our ways of working. We have successfully transitioned to a working from home setup while also supporting our customers with a wide range of initiatives, ranging from advisory services to providing liquidity facilities and extending credit lines. All with the aim of providing the best possible assistance to our customers during this very difficult period.

Overall, our underlying business was stable at the level of the preceding year, driven by Banking Nordic and our business with large corporate customers.

At Banking Denmark, we launched several supporting initiatives to help our customers through the corona crisis, at the same time as we continue to focus on our Better Bank journey. We announced a new setup for servicing retail customers, planned for launch in 2021. We introduced a fixed-rate version of our FlexLife mortgage loan and a number of services to support the green transition.

Late in 2020, given the continually negative interest rates, we adjusted our deposit pricing accordingly, also for retail deposits with effect from the 1st of January '21.

Banking Nordic was able to continue the onboarding of many new retail customers despite the corona turmoil, while we also supported existing customers through the effects of the corona crisis. We continued to make good progress on our Better Nordic Retail Bank transformation, combined with an acceleration of digital offerings.

At Corporates & Institutions, we have been busy securing liquidity facilities for our large corporate customers, while at the same time providing advisory services and access to the primary debt and equity markets. Our investments in Capital Markets-related products paid off in primary debt as well as in equity capital markets. There was thus an increasing number of transactions with a strong sustainability focus and financed by green loans.

At Wealth Management, we continue to expand the product offering with more sustainable solutions at both Danica Pension and Danske Invest. Despite corona-crisis related market turmoil, we delivered positive returns to our customers. In many of our investment products, we saw the highest above-benchmark return in the past 3 years.

Financially, we are today presenting results for 2020 of DKK 4.6 billion, slightly higher than our outlook with good evidence of a stable development in most of our income lines when adjusted for one-offs. Expenses amounted to DKK 28.1 billion and showed good progress as a result of our cost management initiatives. Nevertheless, costs were also impacted by planned costs for our transformation and elevated costs related to compliance remediation and, of course, the Estonia case. On top of this, we also booked provisions related to the continued transformation in '21.

Impairment charges amounted to DKK 7 billion and were significantly affected by the pandemic, including charges against legacy oil-related exposure. A good part derives from changes to model assumptions. Most of that was reversed during the year and replaced by post-model adjustments due to continually limited visibility for the economy. Only a limited part was due to specific credit deterioration in other sectors.

On the basis of the results for 2020 and our continuously strong CET1 capital ratio of 18.3%, the Board of Directors is proposing a dividend of DKK 2 per share to be paid.

Finally, for 2021, we expect net profit in the range of DKK 9-11 billion, which Stephen will comment on in more detail later on in this call.

Slide 3, please. Now I'd like to update you on our multi-year transformation and the deliveries we made in 2020 in order for us to become a Better Bank for our stakeholders. As mentioned before, 2020 was a busy year impacted by the global coronavirus pandemic, but we have continued executing and transforming Danske Bank. These efforts are also supported by the recent organisational changes made to reduce the number of business units from 4 to 2, which will enable us to become simpler and more competitive to the benefit of all stakeholders.

Let's look at customers. Looking back at some of the deliveries of the past year, we have continuously supported our customers during corona crisis. This led to improved CSAT, customer satisfaction levels, in a number of surveys conducted by Prospera on commercial and C&I customers. We've also improved our digital solutions, for example, District and Danske Mobile Banking, adding new and improved functionality. Furthermore, in 2020, we have developed and launched various new products such as the FlexLife mortgage loan with a fixed interest rate for 30 years and the Danica Balance Sustainable Choice investment option.

With regards to employees, the following: Our employees are, of course, our main asset, and we aspire to have engaged employees who are proud to be working at Danske Bank. During 2020, the majority of our employees were able to work from home, thus continuously supporting and helping customers despite being challenged by the coronavirus pandemic. In order to support our employees while they work from home, we launched Working@Danske, allowing for increased flexibility of working routines going forward. We've also shaped a new purpose and culture commitment, which will be integrated in the organisation shortly. Employee flexibility and autonomy will be further increased by the recently launched agile transformation, which allows us to create an even more engaging workplace. We have also launched initiatives to improve diversity.

With regard to society, we are making good progress with the societal agenda, and with helping our customers with their transformation to become more sustainable. We saw significant progress on our sustainable finance agenda in 2020. A total amount of more than DKK 100 billion was issued in green loans. Furthermore, we were able already to reach 2/3 of our 2023 ambitions for green investments.

A second proof point for our contribution to society is entrepreneurship. In this area, we use our platforms to support a significant number of start-ups and scale-ups. Furthermore, a robust compliance culture is the foundation for fighting financial crime and meeting our regulatory compliance obligations, thus ensuring that we always have the best interest of our customers in mind. In 2020, we completed ongoing due diligence on more than 2.5 million customers, with a substantial portion of this completed on the basis of increasingly automated processes.

With regard to investors. In addition, we launched BWoW and set the agile organisation As mentioned, we are committed to reducing complexity and making Danske Bank a much simpler bank, which is also impacting our product portfolio. While introducing new and relevant products for our customers, we also want to keep on simplifying. In Banking DK and Banking Nordic, we reduced the number of products by 25% and by more than 50% at Corporates & Institutions.

Our transformation journey is not over as it is a multi-year journey. 2020 was a year of investing, and we're now starting 2021 with an even stronger organisational setup, and together with our highly skilled and committed employees, we will continue to push for our ambition to become a Better Bank for customers, employees, society and, of course, shareholders.

Next slide, please. As mentioned earlier, we recently introduced our Better Ways of Working, which involve almost 5,000 employees. We appointed 4,000 employees to new positions, this continues with around 500 positions, and we reduced the number of managers. The new agile ways of working for our development organisation will enable us to develop products and solutions to our customers with faster go-to-market times and to be more efficient. Because we have empowered employees with end-to-end responsibility, broken down hierarchies and simplified our governance structure.

In 2020, we laid the foundation, and in 2021, we will focus on the further digitalisation of our core customer journeys and on utilizing our agile organisation. This will enable us to harvest the benefits for our customers with better products and solutions and achieve a more efficient cost base to support our 2023 ambitions of becoming a Better Bank.

Next slide, please. As you may recall, last February, we announced 7 quantified targets for our sustainability efforts to be reached by the end of 2023. Today, we have published our 2020 results for all 7 of those targets, and I will be providing some comments on these. However, before I comment on the specific targets, please allow me to say 3 things. Firstly, as we also mentioned last February, our ambitions are broader than our targets, and we are pleased to be able to say that execution on our full sustainability agenda is well underway, with particular focus on sustainable finance, in which area we aim to take a leading position in the Nordic countries. Secondly, we are pleased to note that our progress on sustainability agenda has recently been recognised by several ESG rating agencies, including CDP and MSCI. Thirdly, right from the outset, we recognised that the sustainability field is moving fast, and these targets would likely need to be recalibrated towards 2023. And indeed, we'll be adjusting some of our sustainability targets during the first half of 2021 once there are more clarity on EU regulations relating to sustainable finance, particularly the EU taxonomy.

Now let's have a look at some of the highlights. For sustainable financing, we ended the year with a cumulative volume of DKK 102 billion, up from DKK 46 billion at the end of 2019. Our original target was well above DKK 100 billion by 2023, and as we're now already over DKK 100 billion, we are looking to revise the target upwards during the first half of this year.

Moving closer into the increase in 2020, arranged bonds contributed DKK 41 billion. RD loans, mortgage credit loans, DKK 9.8 billion, and bank loans, DKK 12.5 billion. We saw a steady growth of arranged green bonds as well as strong uptick in social bonds arranged for our customers. On the lending side, renewable energy as well as real estate continue to be major areas of refinancing. In terms of our relative position, we ranked #1 among Nordic banks in the Bloomberg league tables for green, social and sustainability bond arrangements. And as for our efforts to set a climate target for our corporate lending portfolio, we joined the Partnership for Carbon Accounting Financials (PCaF) as the first large Nordic bank, and we've met the climate impact of 23% of the portfolio. We published our financed emissions for the shipping portfolio in '20 and we look to start disclosing finance emissions for selected sectors in the first half of this year.

On the sustainable investing side, Danica Pension's investments in green transition ended the year at DKK 27.2 billion, up from DKK 10.3 billion the year before. That means that Danica Pension is well ahead of schedule to meet its green investment milestone targets of DKK 30 billion by 2023, DKK 50 million by 2025 and DKK100 billion by 2030. It is also relevant to point out that Danica Pension joined the UN- convened Net-Zero Asset Owner Alliance in 2020, thus committing to transitioning its investment portfolio to net-zero greenhouse gas emissions by 2050, in line with the Paris Agreement climate target. To meet that goal and ensure progress, Danica Pension will be setting milestone targets for its emission reduction for specific sectors.

Continuing now to entrepreneurship. We ended the year with a bit more than 5,000 start-ups and scale-ups supported through our platform, slightly below what was expected prior to the pandemic. Nevertheless, our quick turnaround towards digital execution proved successful, and we were able to help start-ups navigate the crisis. Looking ahead, we expect a rebound and remain optimistic about reaching our 2023 target of supporting 10,000 start-ups and scale-ups.

Finally, for our environmental footprint, we saw a significant positive side effect of the pandemic with a 48% year-on-year reduction of our emissions, largely driven by significant reduction in travel. It's important to note that this is an annual emissions target. So each year, the meter is basically reset. This means that there is no automatic impact in our 2023 target. That being said, we certainly aim to leverage positive learnings from pandemic, such as our increased use of digital meetings in order to achieve more permanent CO_2 reductions.

So allow me to conclude this slide by saying it while the sustainability field continues to develop rapidly with regulation and methodologies maturing as we speak, we will continue to push ahead execution as our aim is to play a leading role in the Nordic countries in terms of sustainable finance. Along the way, we will calibrate these targets as necessary. Several of them will be done already in the next few months once we have greater clarity on the criteria in EU regulations, and as always, for those of you who are interested in further details, more information can be found in our Sustainability Report and Sustainability Factbook.

Slide 6, and that's for Stephan.

Stephan Engels – Danske Bank – CFO

Yes. Thank you, Chris. Let us now look at the financial results for the full year, which overall reflect steady progress. Across our markets, we have seen generally lower economic activity with some fluctuations between quarters. However, key economic indicators such as housing market activity and customer spending held up well. While government support packages ensure low unemployment and few bankruptcies are currently reviewed because of the current second corona wave. The better-than-expected macroeconomic development, evidenced by our Nordic lending activities, which increased 4% in local currency compared to 2019. In addition, the positive development in the financial markets was beneficial for both fee and trading income. Despite different degrees of lockdowns throughout the year, customer activity, including housing market activity, held up well. The latest positive outlook for development and distribution of vaccines from multiple suppliers looks promising for the economies going forward, however, most likely drifting towards the second half of 2021.

Total income came in at DKK 42.4 billion, in line with the level last year when adjusting for the one-off effects in 2019 and 2020. Total income for Q4 in isolation came in at DKK 11 billion, up 4%, primarily due to higher fee income and despite negative one-offs of DKK 0.7 billion. Net interest income was stable year-over-year as a result of good business activity, however, impacted by headwinds from continued margin pressure and FX development. Increased lending and a strong development for deposits, which increased 24% in the period, primarily because of corporate deposits at market rates drove the development. The increase in retail deposits, primarily on ordinary transaction accounts, was due to the change we have seen in consumer spending behaviour during the pandemic. Net interest income in Q4 was unchanged when adjusting for a negative one-off of DKK 0.1 billion.

As announced in our previous financial report, we have responded to the continuous increase in deposits in what seems to be a permanent negative rate environment by adjusting the threshold for charging for negative interest rates for both retail deposits and corporate deposits with effect from January 1 this year. Fee income was overall stable, as better results generated by investment and capital market activities, were able to offset the decline in activity-related income, including lower remortgaging activity. Fee income in Q4 reflects record high-performance fees from asset management and from strong activity in our Capital Market-related activities in C&I. Adjusted for one-off effects in both 2019 and 2020, trading income was up 7% despite an overall lower headline number. The outbreak of the pandemic had a short-lived negative impact in the financial markets, where conditions have been constructive during most of the year, followed by strong customer activity. Trading income for 2020 was supported by positive valuation adjustments following negative adjustments the year before. The result for Q4 in isolation reflects continued good customer activity, albeit to a lower extent than in the previous quarter. In addition, the Q4 number included negative one-off effects related to Danica Pension of DKK 0.3 billion.

Expenses came in at DKK 28.1 billion, in line with our guidance for the full year. Transformation initiatives under our 2023 agenda, elevated but non-sticky costs for the Estonia case and compliance remediation had a significant impact on our total costs for 2020. The cost management initiatives we launched during the year had a positive impact on underlying costs, which I will comment on later in this call. In addition, the Q4 numbers include a provision for part of the transformation costs for 2021, in the form of additional severance pay and other restructuring costs. We will continue to reduce our costs further in '21 in order to ensure good traction for our 2023 plan. In relation to the redesign of our organisation, as we announced in Q3, we have booked an extraordinary write-down of intangible assets in Q4. The write-down relates to software and amounts to DKK 0.4 billion.

Loan impairment charges, which to a high degree explained the difference in the financial results for 2019, amounted to EUR 7 billion for the period, up DKK 0.7 billion, in line with our guidance. Overall credit quality remains strong with very limited losses directly linked to the pandemic. Two items explain the development; firstly, model-driven charges recognised in early 2020 have been reversed and replaced by post-model adjustments; secondly, an adverse development for our oil-related exposure. I will come back to credit quality later in this presentation.

Slide 7, please. Now let us take a closer look at the underlying development in the net interest income for the Group. I will make more specific comments for our business units on the next slide. Compared to last year, NII saw positive effects from good customer activity in the form of volume growth, and deposit margins benefited from a steeper yield curve in the short-term money market in Denmark. The positive effect was, to some extent, offset by headwinds from currency effects, but also from the pressure on lending margins, resulting from the low interest rate environment. Adjusted for currency effects, NII was up 1%. In Q4, NII was stable, adjusted for a one-off of 0.1 billion related to a correction of income in the liquidity portfolio held in Group Treasury. The decline in deposit margins from the preceding quarter was due to an adjustment of the funds transfer pricing model, which to a large extent, is offset in NII other. As part of the pricing initiatives I mentioned earlier, we have now adapted to current market conditions in Denmark by lowering the threshold for charging of negative interest rates on retail deposits from DKK 1.5 million to DKK 250,000, and altogether removing the threshold on corporate deposits, which was previously DKK 200,000. In isolation, both initiatives will contribute positively to NII with an annual effect of approximately DKK 0.5 billion all else equal and subject to changes in customer behaviour and deposit balance developments at Banking DK.

At the end of 2020, redeemed long-term funding of 64 billion has been replaced by new long-term funding of DKK 75 billion in various instruments at average higher spreads, confirming the negative impact on NII.

For 2021, we expect NII to be slightly higher as volume growth and pricing initiatives are expected to offset margin pressures, whereas the effect from funding costs is expected to be neutral, however, subject to market conditions.

Lending at Banking DK on slide 8, please, was down 1% year-on-year due to a decline in demand because of various effects resulting from the corona crisis support measures. However, lending volume was slightly higher in Q4 from the level in Q3, driven by the commercial segment. The pressure on lending margins was most evident at Banking DK, where we see the effect of our customers' shift towards longer-term fixed-rate mortgages with lower margins. Deposit margins benefited, as mentioned from the hike in interest rate from the Danish central bank.

At Banking Nordic, we saw growth in business activity, with lending up 3% or 4% in local currency, as a result of strong growth in retail Sweden, and Norway, where the inflow from the partnership agreements continued during the year. We also saw higher lending in the commercial segment in all 3 countries. NII at Banking Nordic improved from the same period last year, benefiting from lending volume growth as well as an improvement in lending margins. C&I saw higher customer activity, reflecting higher corporate credit demand, primarily in the first 3 quarters of the year. The demand was for short-term credit facilities in order to strengthen customer liquidity positions during the corona crisis. Overall, average lending at C&I was up, however, we saw a decrease in lending volume towards the end of the year. NII and C&I benefited year-over-year from higher lending and significantly higher deposit volumes at market rates. The elevated level of deposits as well as some of the short-term lending facilities provided to corporate customers, should be seen in the context of the current uncertainty, and are therefore not necessarily of a permanent nature.

Slide 9, please. Let's have a look at fee income. Overall fee income maintained the good momentum and was in line with 2019. Adjusted for extraordinary items at Banking Nordic, fee income in 2020 was slightly up compared with the year before. In 2020, investment fee income, in particular, benefited from a strong increase in performance fees from wealth management. In addition, we saw a positive development for investment in Capital Market-related activities, whereas remortgaging was significantly lower. Activity-based fee income in general was lower due to the impact from the corona crisis.

Fee income at Banking DK benefited from an uptick in activity in Q4, which contributed to stable fee income from lending and guarantees. In 2019, remortgaging activity was historically high, which explains the decline year-on-year. In Banking Nordic, fee income in Q4 amounted to almost the same level as last year, excluding the effect from negative value adjustments of DKK 0.2 billion related to a distribution agreement in Finland.

The higher fee income generated by our capital markets activities at C&I benefited from strong franchise value and came in higher than last year due to stronger customer activity and our investments in capital markets-related products. Fee income in Q4 was strong and increased from a low level in the preceding quarter, due to good activity in both debt and equity capital markets. And Wealth Management fee income benefited from strong performance fees at Asset Management and higher risk allowance fees at Danica Pension. As the majority of these fees are booked close to year-end, this explains the strong increase in investment fees in Q4.

Slide 10, please. Now let's turn to trading income. In the fourth quarter, despite being a period with usually low trading activity, we continue to see relatively strong customer activity. Income in Q4 was almost at the same level as in the preceding quarter when adjusted for one-offs and lower value adjustments. Trading income year-on-year came in 7% higher when adjusted for extraordinary items in 2019 and 2020, significantly higher income at C&I compensated for lower income in the other business units due to the impact on activity from the coronavirus. The higher income at Corporates & Institutions was based on strong franchise value and solid activity among our FI&C customers, from improved market conditions as well as positive value adjustments. At both Banking DK and Banking Nordic, trading income came in lower due to lower investment activity among customers, and in Banking DK, remortgaging activity was much lower compared to the very high activity from last year.

At Wealth Management, the underlying result in Q4 benefited from a stronger investment result in the health and accident business in Danica. However, trading income year-on-year as well as quarter-on-quarter was lower due to the effects from one-offs in Danica Pension.

Slide 11, please. Our operating expenses for 2020 came in at DKK 28.1 billion. This is at the lower end of our most recent guidance, excluding the provisions we have booked for further transformative initiatives in 2021. This should be seen as part of additional measures we take in order to ensure good tractions into 2021. The cost-saving initiatives we have launched during the year have shown tangible results, in particular, in the second half of the year, where we saw lower underlying staff costs and lower cost as a result of the overall strong cost discipline. Effects from the pandemic had an impact in the form of lower traveling activity, among other things. A higher contribution to the Danish Resolution fund, however, had an adverse effect.

Reported costs came in higher than in 2019 as a result of the planned costs for the Better Bank transformation, compliance and the Estonia case. The costs for the transformation amounts to more than DKK 1.7 billion, as they includes the before mentioned for further provision for further transformative initiatives in 2021.

Costs for compliance remediation and the Estonia case came in DKK 0.9 billion higher than in 2019, totalling DKK 4.1 billion for the full year, which is in line with our expectations.

All business units were impacted by costs related to the Better Bank transformation and continued work with compliance remediation.

In Wealth Management, however, costs were lower, as 2019 included integration costs and compensation related to the Flexinvest Fri case.

Expenses in Q4 reflect a significant amount booked for transformation, including DKK 600 million for severance and seasonality due to year-end booking for certain cost items. In order to continue execution on our 2023 plan and to maintain strong progress towards a lower cost base, which is essential for our ability to remain competitive, we will during 2021 announce further cost-saving initiatives. Including initiatives announced by the end of January, tangible progress has been made as we now have discontinued approximately 700 positions out of the up to 1,600 mainly Nordic positions we announced in October 2020. As we still have a lot of execution in front of us, this work will proceed at the same time as we continue to focus on further cost-saving initiatives, including efficiency measures and non-personnel expenses.

Slide 12, please. Total impairment charges for 2020, which amounted to DKK 7 billion, are in line with our guidance. The charges for Q4 reflect a further reversal of DKK 0.5 billion, as our update of model-driven assumptions in Q4 reflects a more benign economic recovery in 2021. However, given the limited visibility regarding economic developments, we have increased post-model adjustments by DKK 0.7 billion in Q4 to DKK 2.7 billion for the full year. As changes in the macroeconomic assumptions have led to a reversal of DKK 0.3 billion, impairments recognised for anticipated credit deterioration amount to DKK 2.4 billion.

The oil-related exposure, the offshore service and drilling segment in particular, continues to be challenged and led to additional, but declining, impairments of DKK 0.5 billion in Q4. This exposure continues to be challenged by difficult market conditions and low activity that makes restructuring increasingly difficult, and we see pressure on collateral values affecting impairments. During 2020, our impairments against the oil-related exposure have been affected by extraordinary charges in order to de-risk the portfolio. But we expect lower impairment charges in '21 against this exposure. However, uncertainty remains. Overall credit quality continues to be strong and only very limited deterioration has been recognised in Q4 against other types of exposures.

The impairment charges recognised in Q4 are equivalent to a reported loan loss ratio of 13 basis points, however, with significant fluctuations between business units. As a result, the allowance account stands at DKK 22.6 billion in total. The decline in the allowance account was mostly due to write-offs of already impaired oil-related exposure.

Slide 13, please. Our capital position remained strong with a reported Core Tier 1 capital ratio of 18.3% at the end of the fourth quarter. The CET1 capital ratio was up 0.2 percentage points, driven mainly by earnings, a lower deduction at Danica Pension and intangibles. The fully loaded CET1 capital ratio was 18%. The total REA came in DKK 18 billion higher than at the end of last quarter, due to an increase in credit risk. This is as expected due to the implementation of EBA guidelines. The first half of this year, we expect an impact on credit risk REA from model updates related to further implementation of EBA guidelines of DKK 25 billion to DKK 35 billion, all else being equal.

The leverage ratio was unchanged at 4.4% according to transitional rules and 4.5% fully phased in. On the basis of the result for 2020 and our continued strong Core Tier 1 capital ratio of 18.4%, the Board of Directors is proposing a dividend of DKK 2 per share, representing a pay-out ratio of 38%.

Slide 14, please. And then the financial outlook for 2021. Please note that the outlook has been aligned with the new presentation of Danica Pension, which going forward, will be presented as net income from insurance business. An overview of the changes is presented in our annual report and is also available on page 38 in the conference call presentation. The new presentation of Danica Pension is a result of the redesign of our organisation, whereby our asset management activities are now part of Large Corporates & Institutions. In order to present our financial performance as transparently as possible, we will now disclose our insurance business performance on a separate basis.

The outlook we expect total income to be slightly higher than the level in 2020, subject, obviously, to commercial momentum and broader economic developments. Our expectation for slightly higher total income will be driven by slightly higher NII and fee income, whereas less benign market conditions will affect trading income.

Expenses are expected to be more than DKK 24.5 billion, driven by ongoing cost initiatives and lower costs for transformation and remediation. Please be aware that the outlook for expenses is net of the DKK 1.5 billion cost related to Danica Pension due to the reorganisation.

Loan impairments are expected to be no more than DKK 3.5 billion, subject to a modest economic recovery based on a positive impact from COVID-19 vaccines.

We expect net profit to be in the range of DKK 9 billion to 11 billion.

Slide 15, please and over to Claus.

Claus I. Jensen – Danske Bank – Head of Investor Relations

Thank you, Stephan. Those were our initial comments and messages. We are now ready for your questions. Please limit yourself to 2 questions. If you are listening to the conference call from our website, you are welcome to ask questions by email. A transcript of this conference call will be added to our website and the IR app within the next few days.

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

Operator

(Operator Instructions). Our first question comes from the line of Adrian Cighi from Credit Suisse.

Adrian Cighi - Credit Suisse

It's Adrian from Credit Suisse. I have one on capital and one on market share. On capital, I'm trying to understand your outlook for this. You flagged the EBA guidelines as a headwind in H1. Are there any other developments that you might flag in terms of either positive or negative impacts going forward? And then on market share. I noticed that you continue to lose market share in your home market in Denmark and in your growth market I have seen. Do you believe that the current restructuring efforts are impacting your customer satisfaction and could be, therefore, a driver behind these developments? Or is that due to other factors?

Chris Vogelzang – Danske Bank – CEO

This is Chris. Let me first take the market share. I mean let's distinguish the different segments. We are actually doing well in business customers, and we're doing well in corporate customers. And indeed, our retail franchise in Denmark, is and has been under pressure for a while. If you look at the customer satisfaction figures, you see that the customers of the bank actually value the advisers, they value our products, but they still have an issue with our general image, which is very much derived from Estonia and a few cases, which were extremely large in the Danish press this year. I feel pretty confident that given the underlying quality of the satisfaction with regards to specifics in the total offering, we should be able to turn it around. But this just takes a long time. I mean, we now see that the outflow, and I mean, still outflow is bad, but the outflow has been reduced by 30%. So there are maybe some initial signs. But I think the most important thing is to get the Estonia case out of the way and more specifically, get some of the legacy cases, some of them coming back from the early 2000s, get them out of the way. With regard to the restructuring, we have actually, as part of the restructuring, we believe that we did some things, which should accelerate our commercial momentum in Denmark. We changed management quite significantly and have a new generation of managers there. We have also introduced a Commercial Leadership Team, which is also going to be focusing much more on the Danish franchise and the retail franchise. So in that sense, it has our attention. We are not happy enough with it, but the retail franchise is still an issue in that market. Stephan, on the other topic?

Stephan Engels – Danske Bank – CFO

Yes. Basically as in 2020, we will keep on implementing EBA guidelines on our, call it, trajectory to increased real density in general. You know that there are also certain additions to our capital requirements, reflecting these things. I don't think they will go completely in sync between these two requirements, but again, the DKK 25-35 billion range is our best indication for the first half of 2021. And obviously also in that sense, caters for the expected REA growth from business growth.

Operator

And the next question comes from the line of Sofie Peterzéns from J.P. Morgan.

Sofie Peterzéns – J.P. Morgan

Here is Sofie from J.P. Morgan. My first question would be on your performance fees. They were very strong, around DKK 550 million in the fourth quarter. Some of your peers are saying that we should expect the performance fees over time to fully disappear. What's your view on charging asset management performance fees? Do you think there is the risk that we could see performance fees disappearing over time? And then my second question would be on kind of how should we think about dividends and buybacks going forward? Do you have, or if you could share with us your thoughts on buybacks and kind of how you think about this?

Chris Vogelzang – Danske Bank – CEO

Sorry, can I clarify the question? Are you talking about performance fees changing from a legal perspective? Or are you talking about performance fees disappearing because of a performance perspective?

Sofie Peterzéns – J.P. Morgan

Well, I was more thinking that other banks are charging less and less performance fees so more from a competitive standpoint that given competition on the asset management side, you have more new entrants. It's more from that side.

Chris Vogelzang – Danske Bank – CEO

I am at the moment, in the Danish environment, not very worried about that. There's still a very, very standard way of doing things. I mean, I agree with you that if you look at asset management in general, the business model or the profit pools change from fees to portfolio management fees, et cetera, et cetera. So you actually do see quite a lot of changes happening in the world. In Denmark, that is very, very limited, if anything. So for the moment, that is not high on our concerns.

Stephan Engels – Danske Bank – CFO

Yes. And I think it also needs to be seen in really outstanding performance, which we have seen by our asset management teams, partly beating the indices by up to 74%, so in the sense, I think that is also reflecting this. On dividends and share buybacks, the dividends, we have a standing capital distribution policy, which calls for dividends within a payout ratio between 40-60%. And I see no reason so far to change it. The discussion of share buybacks, I guess, is a bit premature. I think we all would want to see the Estonia case finally closed before we start discussing that again. So in that sense, we'll probably need to wait a while.

Sofie Peterzéns – J.P. Morgan

And in terms of the Estonia case, is there any update on when we would have a little bit more clarity?

Chris Vogelzang – Danske Bank – CEO

No. I mean, there's nothing to report. I mean we truly don't know. I mean, we have done our work. There's always some outstandings, but that's back and forth in discussions, of course. But essentially, we have done our work. And now we're waiting for the authorities to come back to us.

Operator

Than the next question comes from the line of Mads Thinggaard from ABG.

Mads Thinggaard – ABG Sundal Collier

I guess, the first one I have is for you Stephan, and it's a bit about the NII outlook, you were so kind to give us before, slightly higher NII in 2021. And I was thinking here a bit, I mean with quite strong Nordic growth here in Q4, deposit initiatives and also zero effect or neutral effect from funding costs, what kind of competitive margin pressure do you factor into that outlook? And what are the key sources for that margin pressure? That would be the first question. And then the second question is a bit on the cost side. I think we kind of got the impression on Q3 when you lowered the cost guidance that you were a bit ahead on cutting underlying costs. And I also noted, I think, not more than DKK 24.5 billion in 2021. Are you still a bit ahead on the cost-cutting according to your plan? And do you still see compliance costs down to DKK 1.5-1.7 billion in 2023, as you have guided for before?

Stephan Engels – Danske Bank – CFO

Yes. On the NII, I think there's many moving parts. First of all, the market with the low interest rate environment so far at least, has been under pressure. So margins have been shrinking in general. Then keep in mind that the mortgage customers still clearly prefer long-term fixed-rate mortgages over the variable mortgages that they had before. That, as such, has lower margins. And this time goes on there is a front book, back book effect out of that, obviously, as well as more customers move on to the, as I said, to the lower margin fixed-rate models. On cost, first, maybe on compliance, that's clearly still the goal and the indication that the business as usual number for compliance costs should be somewhere between 1.5-1.7, at least from today's perspective. So that's unchanged. Costs, in general, I think what you see in Q4 is -- and I do agree that there is a little bit of movement, including severance pay, we have also catered for a number of restructuring initiatives that we will take in '21. I think the 28.1 also reflects a very prudent view of what the year-end view on certain things should be. So I don't want to say, I'm ahead, but I think we are going into quarter one of this year with a strong momentum and a good understanding that DKK 24.5 billion should be achievable.

Mads Thinggaard – ABG Sundal Collier

Okay. And just a small follow-up. I think you have guided for a DKK 1 billion drop from external compliance costs in 2021 before. Is that still the case?

Stephan Engels – Danske Bank – CFO

Yes. I wouldn't necessarily call it directly compliance cost because that gives the impression as if we are scaling back on the compliance, which we are effectively not. We still invest into third line, so that's compliance and risk. But what we will see go away is a lot of the remediation efforts, the forensic efforts also in relation to the before-mentioned reporting to the authorities, which drives, obviously, also a lot of our external supplier costs. And if you look closely at Q4, you'll find out that external suppliers are starting to go down at least slightly.

Operator

And the next question comes from the line of Per Grønborg from SEB.

Per Grønborg – SEB

Two questions from my side as well. Deposits, we have discussed a number of times, you state yourselves that you have adapted to the current market standard. What would the upside be if you took the remaining step lowering the deposit threshold to 100,000 and starting to charge market rates on pension accounts instead of awarding cash part by 1 basis point positive return. That was the first question.

Stephan Engels – Danske Bank – CFO

Yes, Per, thanks. I think that's a little bit of speculation land. And secondly, looking at only the isolation of doing one of these things without considering what it does, for example, on customer satisfaction, customer migration or some other movements, I think that's not the prudent way to look at this, to be honest. It's also pretty clear that we have chosen a very, call it, considered approach in lowering the thresholds. I think now the market in Denmark has stabilised, and we feel well positioned with where we are, which again is obviously subject to whatever happens throughout the rest of the year. But for the time being, I think, that's a good thing. And now let's get started with that.

Per Grønborg – SEB

What has the client reaction been on what you're doing now 1st of January?

Stephan Engels – Danske Bank – CFO

Yes. So far, what you can see a little bit, and then you can debate whether you want to attribute that to the measures taken, you can see that deposit growth has a bit slowed in Banking DK in Q4, whether that is due to this or something else is hard to tell, as always. Secondly, I think we need to wait at least until the end of Q1 to really see what the customer base will start doing, because we only start really charging as of Q1. And for many people, it makes a difference whether they read about it or whether they find a real charge on their account statement. So I think it's a bit early to tell. But in general, I think the market on the deposit side is still more driven by people saving money rather than spending it. And in that sense, let's see what Q1 has to say.

Per Grønborg – SEB

Okay. My second question is related to your cost. Of course, looking for the cost bridge you presented 1.5 years ago and an update on that one. What you call transformation cost, DKK 1.7 billion, last quarter, you talked about DKK 500 million being postponed into next year. Is that number now down to only approximately 300?

Stephan Engels – Danske Bank – CFO

We still expect that to be DKK 500 million, to be honest. And in that sense, again, I think the overshoot on transformation cost in 2020 is also reflecting to a good bit, the DKK 600 million of severance pay provision that we took at the end of the year.

Per Grønborg – SEB

Yes, of course. When we look at the compliance cost, they were DKK 3.1 billion last year. You're adding DKK 900 million. So compliance is underlying running at approximately DKK 4 billion in 2020. Is that reasonable?

Stephan Engels – Danske Bank – CFO

Yes, DKK 4.1 billion.

Operator

And the next question comes next question comes from the from the line of Nick Davey from Exane BNB Paribas.

Nick Davey – Exane BNP Paribas

A couple of questions. On the internal investigation that you've now finalised, I just wanted to hear whether you had any intention to publish that report? And/or if we would have heard an update if it had found anything new relative to the last external publication of the facts, please. And then the second question relates to Basel III. I was just looking at an EBA impact study from December, which estimated 15-20% RWA inflation for the Danish banking system as a whole. I know it's early, I know things are changing, but they did look at various changes being considered, and that was still the RWA inflation range. I wondered if you had any comments on that.

Chris Vogelzang – Danske Bank – CEO

This is Chris. I will take the first one. The answer on the first part of your question is no. We will not publish the details of the investigation ourselves. Two, the answer is yes. If we would have found anything material where we, according to disclosure rules, had to disclose it to the market, we would, of course, have done it, and that's not the case. So in that sense, there is nothing new versus the last quarters, and it's for us now, we are in waiting mode.

Claus I. Jensen – Danske Bank – Head of Investor Relations

Yes. I can take the second question, Nick. I'm not especially aware of the report that you are mentioning here. But it seems to be well in line with what we have communicated recently that we will gradually implement EBA guidelines and other regulatory stuff in order to avoid a cliff effect on our capital. We added DKK 19 billion of EBA effect in Q4 2020, and we expect that there will be a further DKK 25-35 billion impact in 2021. And then let us come back on what we see once we are beyond that point. And the effect we expect here in 2021 will be in the first half of the year.

Operator

The next question comes from the line of Maria Semikhatova from Citi.

Maria Semikhatova – Citi

A couple of follow-up questions. Just on your cost outlook, if we adjust for Danica Pension presentation, you're effectively looking for a reduction in costs of around DKK 2.1 billion for 2021. And you mentioned that around DKK 1 billion would be coming from lower compliance and remediation expenses, and then we will have DKK 1.2 billion reduction in transformation costs. So that effectively implies that underlying costs are staying flat year-over-year. Just wanted to confirm that this understanding is correct. And you think that cost savings for the underlying portion will be coming later on. And then on AML and compliance charges, can you provide the updated number of FTEs currently employed in compliance? I think the last time you disclosed this number was in the second quarter. And just how the automation of compliance functions is proceeding?

Stephan Engels – Danske Bank – CFO

Yes. Let me start with the first one. On the surface of it, your triangulation reflects pretty much the numbers. I would nevertheless make 2-3 remarks. One is the underlying cost will also in 2021 include additional functions that were taken over by the first-line out of the compliance pot. So they will need to compensate for that, which then, if you want so, is the first challenge that they have. The second is we are foreseeing for '21, at least from now, that marketing and travel activity, which has been exceptionally low in 2020 will pick up again. So that's the second effect. And the third is obviously the usual cost drift from inflation, wage increases and other stuff, which we also will fully compensate in the underlying. So that is I think the broad bridge I would give from today's point of view. I have to look at Claus for the FTE number at compliance, and he's shaking his head as well. So we will come back to you on that one. And the third one was…

Maria Semikhatova – Citi

Just in terms of optimisation or automation of these compliance functions.

Stephan Engels – Danske Bank – CFO

Yes. We are we are consecutively introducing new programmes and new IT and we are seeing an increasing number of not only automation, but also of quality and results being better manageable in the sense of false negatives, false positives and all the other stuff.

Chris Vogelzang – Danske Bank – CEO

But, I mean, to add on that, I think for about 2.5 million clients, we have done ODDs automatically. So given the circumstances in this market, we can't go fully automatic yet, given that we need to check and double check, first time, we have done it, et cetera. We have confidence that once we actually have this thing going on well, that the compliance cost will actually go down as we discussed earlier. And we benchmark that all the time.

Maria Semikhatova – Citi

I understand. Just maybe a minor follow-up on that. Since you mentioned the underlying cost and wage inflation, can you disclose what your assumption for this year?

Stephan Engels – Danske Bank – CFO

Yes. Traditionally, the wage inflation is around 2% in Denmark.

Claus I. Jensen – Danske Bank – Head of Investor Relations

And maybe somewhat higher in some of the other countries that we operate in.

Chris Vogelzang – Danske Bank – CEO

Yes, in Lithuania and India, it's over 5 and sometimes over 10.

Operator

Next question comes from the line of Riccardo Rovere from Mediobanca.

Riccardo Rovere – Mediobanca

Just a couple of follow-ups, if I may. The first one, when you mentioned the DKK 25-35 billion RWA inflation related to the EBA guidelines. So this inflation only relates to EBA guidelines? It does not include anything with regard to positive or negative risk migration or anything like that. Do I get it right?

Claus I. Jensen – Danske Bank – Head of Investor Relations

That is correct, yes. Yes, that's right.

Riccardo Rovere – Mediobanca

Okay. And the 25-35 does not include the 19 that were already visible in 2020?

Stephan Engels – Danske Bank – CFO

No, it's on top. Just to give you a little bit of a hint. The range also reflects, obviously, our overall REA density movement. So in a sense, the movements on some of the other parts also do have a certain effect on where we end in the range.

Riccardo Rovere – Mediobanca

Okay. All right. Okay. And the second question I have, if I may. On the guidance on impairments you are providing and thanks for that, is it possible for you to give us an idea what are the macro assumptions, at least the most important numbers behind the impairments that you are providing us.

Stephan Engels – Danske Bank – CFO

I would think the simple version, and Claus will you give you a more detailed breakdown, but the simple assumption is that we see positive economic growth across the Nordics, again probably a bit more elevated in the second half of the year than in the first half. Secondly, I think we need to understand, and that is, I think, the more relevant part for the impairments, is what exactly will happen if some of the government support programmes start to run out? And how long will the second wave really go? And in a sense, I think we all soberly need to expect that some of the industries that we find most affected by corona will probably see a pickup in insolvencies and related in 2021. Claus, do you want to add something?

Claus I. Jensen – Danske Bank – Head of Investor Relations

No, I just have -- if you are interested, we have the specific changes to the GDP and the property prices, which are those that we have been most focused on. And besides that, we have changed the composition of the base case, the up case and the down case, then we have a more positive outlook now for 2021 when it comes to GDP in all scenarios and the same goes for property prices, which also have been adjusted upwards to reflect a more benign environment in 2021.

Riccardo Rovere – Mediobanca

Okay. So Claus, just to be sure I understand it correctly. When I look at your Nordic outlook and macro assumptions, of the various countries, that is more or less the numbers underpinning the impairment.

Claus I. Jensen – Danske Bank – Head of Investor Relations

Yes. That is correct. And that is very much in line with the scenario we have received from the Danish central bank, maybe a little bit more on the conservative side on our part.

Riccardo Rovere – Mediobanca

Okay. Okay. That's very clear.

Operator

And the next question comes from the line of Namita Samtani from Barclays.

Namita Samtani – Barclays

Thanks for the questions. Just a question on more of a clarification on the revenue guidance where 2021 is going to be slightly higher than 2020, what's the right 2020 comparison base? Is it excluding the one-off items?

Stephan Engels – Danske Bank – CFO

So that's a tricky one. It depends a little bit. I think what you need to do is two things. One is, you also need to take the Danica part out. And then I think we are roughly at DKK 41 billion. Exactly. And then some of the one-offs do also relate to Danica so it's probably a little bit more than the 41 billion, call it, 41.2 or 41.3 would be my guess, but we can follow-up later on. And I would think that is a good starting point.

Operator

We have one more question from the line of Jacob Kruse from Autonomous.

Jacob Kruse – Autonomous

So just two quick questions. The first one is the one-offs that you book in Q4, the various accounting adjustments and corrections. Are they one-offs on a 2020 full-year basis as well or does some of this relate to overbooking of revenues earlier in the year? And then my second question was just on the – I think you talk about this gradual EBA implementation or gradual risk weight density increase. How should I think about your kind of end-point here? How much more gradual – or to put it more simply, the DKK 25-35 billion, is that most of that gradual increase? Or are we sort of halfway through to where you think you want to get to? Or could you give some kind of idea what you're thinking?

Claus I. Jensen – Danske Bank – Head of Investor Relations

Well, I think that we will take it step by step. We have previously guided for that there will be a gradual implementation of different regulatory issues, including the EBA guidelines. And that will take place also in 2022. But I think it's a little bit premature for us to make a specific guidance on the impact for next year. What we have said is that we expect that to be reflected in some of our Pillar II requirements. So that should also be taken into consideration. And we have also stated that adjustment of risk weight floors is not a part of this exercise.

Stephan Engels – Danske Bank – CFO

And on the Q4 one-offs, I would phrase it the following way: given that this was my first full year annual accounts as the new CFO, I think we took, in general, obviously within management judgment boundaries as set by IFRS, we took a sober view on all the things that you look at at the end of the year, and probably we're a bit more cautious, also reflecting COVID-19 and uncertainties. None of that was a correction in the sense of overstated income or revenues during 2020. There are quite some items also reflecting older stuff like distribution agreements or residuals from acquisitions in the past. So I think that is as much colour I would give. Again, I wouldn't expect that to happen on a regular basis.

Jacob Kruse – Autonomous

Okay, but a clean full year 2020 run rate should add back the entirety of the one-offs taken in Q4?

Stephan Engels – Danske Bank – CFO

I would be -- now again, I would be probably a bit careful in giving credit to all of it. And again, I need to speak mentally with my external auditor sitting on my left shoulder. So I wouldn't give credit for all of it, definitely not. But as I said, within management judgment, we have tried to be cautious.

Claus I. Jensen – Danske Bank – Head of Investor Relations

Operator, can we have the last question, please?

Operator

And the last question comes from the line of Martin Birk from Carnegie.

Martin Birk – Carnegie

I have two questions. The first one goes on dividends. Let's say the regulator gives you the green light by September, would you be willing to consider any sort of mid-Q4 dividends? Or how should we think about the bridge from the 38% to mid-range in your dividend guidance? That will be my first question.

Stephan Engels – Danske Bank – CFO

Maybe also to put the 38% a bit into perspective. That is basically the lower end of our guidance and 40% would have been DKK 2 and 1 or 2 øre, which is why we ended up at the 38. So this is a very practical issue rather than trying to be too difficult on that one. Second one. I think that is a very good question, which we will probably really answer somewhere in September.

Martin Birk – Carnegie

Okay. All right. My second and last question is on your 9-10% 2023 ROE guidance. I guess you provided a bridge a year and a half ago, a lot has happened since. Sort of the path to 9-10% becomes more and more blurred. Do you have any plans of updating your bridge on how to bridge the 9-10% ROE?

Stephan Engels – Danske Bank – CFO

I would tend at least to disagree a little bit. I think the two last consecutive quarters at least show a clear direction. And in that sense, I think the trajectory is less blurred than it might have been at the beginning of the corona crisis. Secondly, there is still a corona crisis, which specifically clouds a little bit the visibility on income outlook. And in that sense, I would still clearly state that 9-10% is the goal for 2023. And again, I think we have now two consecutive quarters where we can show that we are turning the corner and on the right trajectory.

Chris Vogelzang – Danske Bank – CEO

Okay. Thank you, Stephan, and 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 had time to look at the financial results in detail. I wish you a very a nice remainder of the afternoon, and I hope to see you face-to-face in a future quarter.