Pre-close call Q1 2022

31 March 2022

Danske Bank – Investor Relations

Claus I. Jensen – Danske Bank – Head of IR

Good afternoon and welcome to the Danske Bank Q1 2022 pre-close call. My name is Claus Ingar Jensen, and I am Head of Investor Relations. With me, I have Olav Jørgensen, Patrick Skydsgaard and Nicolai Tvernø from our IR team. Please note that this call is being recorded for compliance reasons, and the script used for this call will be published on the Investor Relations website after the call. As this is the first time we conduct this call via Teams, please be aware that if you plan on asking questions, you should log on via the Teams app or your browser. If you are only online via a telephone line, the IR team is available after the call.

In today's call, I will highlight relevant public data and macro trends in our markets as well as one-offs that you should be aware of before the start of the silent period on 8th April ahead of the publication of our Q1 report on 29th April. I will go through the P&L statement line by line and remark on capital at the end. Afterwards, we will open up for a Q&A session.

But before we start, for sake of good order, I would like to highlight the following. I will answer only questions related to already disclosed information and one-offs as well as publicly available data as of 28th March unless otherwise noted. In this connection, I wish to stress that developments in specific indices may not always have the same effect on our performance.

First, I would like to comment on the current geopolitical situation. We are monitoring the war in Ukraine closely and I would like to refer you to our publication of 8th March regarding our very limited exposure to customers residing or established in Russia, Ukraine and the Baltics. We also note a continually clouded visibility regarding secondary and third round effects of the disruption in supply-chain mechanism, including the energy supply chain. The Nordic economies in general; are fundamentally strong economies, as we have seen during the pandemic, and they thus have a comforting starting point for weathering the implications of the war. Overall, we remain confident that our strong capital position, diversified business model and credit exposure are important factors in order to adapt to the changes.

That said; let us start by having a look at net interest income.
Please remember that Q1 has two fewer interest days than Q4 with an NII impact of around DKK 30-40 million per day.
During the quarter, the Swedish krona depreciated around 2% against the Danish krone, while the exchange rate of the pound sterling was flat and the Norwegian krone appreciated around 5 % against the Danish krone on the basis of publicly available data.

Regarding volume developments, we refer to publicly available sector statistics as the only externally available source of insight and note the positive trend for corporate lending in Denmark In addition, we would like to remind you that the repayment of government corona loans is expected to begin in April. As with the pandemic, we are well positioned to support our customers in this transition, and we have launched initiatives to help our small business customers.

With regard to margin developments, we also refer to publicly available sector statistics as the only externally available source of insight. Despite the increased interest rates for mortgages in Denmark, we continue to observe some margin pressure, but to a lesser degree than previously. Among other factors, we point to the trend we have observed over the past couple of quarters of a change in retail customers' preferences for products with higher margins such as interest-only and variable rate loans.

Since Q4, 3-month CIBOR has remained flat, while STIBOR has increased around 7 basis point and NIBOR has increased around 39 basis points, all on the basis of quarterly averages.

With regard to interest rate changes, we remind that the Norwegian central bank raised benchmark interest rate to 0.50% on 16th December. In relation to this we increased our lending and deposit rates by up to 25 bps for almost all customers with effect from1st February and 23rd February, respectively. Additionally, at 3rd February we implemented minor pricing adjustments for mortgages for Personal Customers Norway, including Akademikerne, taking effect for existing customers on 16th March and 3rd February for new customers. Most recently, the Norwegian central bank announced its plans to hike the policy rate to 0.75% from 0.50%. As per this week, we have announced a 25 bps price change for loans, taking effect from 13 May for existing loans and immediately for new loans, including Akademikerne, however from 20 April.

To mitigate the development of market and funding rates, we also adjusted prices for home loans in Sweden with effect from 1st January and 17th February with up to 25bps and 81bps, respectively.

Finally, as a result of the two Bank of England rate hikes, we adjusted the Danske Bank Reference Rate in Norhtern Ireland as well, which from 18th March has been 0.75%.

With this in mind, we would like to remind you that our overall NII sensitivity guidance in a +/- 25 bps parallel shift in the interest yield curve across all currencies is DKK +850/-600 million respectively. The effects come primarily from Danish kroner and euros.

Then, in Q1 on the funding side, we issued our third green NPS, which was well-received by the market, judging by an oversubscription of almost 100%. The issue was an EUR 750 million 5NC4 at a price equal to EURIBOR +92bps. Additionally, earlier this week, we issued a dual-tranche USD non-preferred senior of USD 2 billion, which was oversubscribed more than three times. The 3NC2 of USD 750 million came in at a spread equivalent to 3-month Euribor +100 bps and the 6NC5 of USD 1.25 billion equivalent to 3-month Euribor +134 bps.

Although not directly linked to the funding on the NII line, we also gave notice on 2nd March to our last equity-accounted AT1 of EUR 750 million with a 5.875% coupon and effective call date on 6th April.

In conclusion, with regard to funding, we have good access to the market, despite the uncertainty and somewhat elevated spreads we have seen during Q1.

Our fee income is, as always, dependent on market conditions for the capital markets, development of the equity markets and the general activity level in our banking operations.

Starting off with Capital Markets, there is no doubt that 2021 was a very strong year in terms of activity, both for the market in general and for Danske Bank which translated into record-high fee levels, which included a landmark deal booked in Q1 2021. During the first quarter of 2022, it is clear, that the uncertainty in the markets following the Russian invasion has an impact on capital markets activity in the short term, as customers have now adopted more of a wait-and-see position. With reference to publicly available Bloomberg League tables at end of February for DCM and sustainable finance issuances, we remain in a strong position relative to peers especially, and demand related to the green transition remains high. On ECM, we have a good pipeline going into 2022, however the Russian-Ukrainian war has led to low market activity in general, with very few new deals being launched.

On the investment side, first of all, we remind about the seasonality of our performance-fee bookings in Q4 which amounted to DKK 0.3 billion in Q4-2021. Next, we observe the correction in the equity markets in January followed by high volatility and then the Russia/Ukraine war. As a result, at closing of 28th March, the OMX C25 index was down 11% and the S&P 500 was down 4%. Please note; that the negative development in the financial markets will have an impact on our AuM which combined with the current volatility could be notable headwinds for our investment fee performance.

For activity driven fees, we refer to our publicly available spending monitor paper, in which Dankort and MobilePay data show spending slightly up from the level in to 2019, even when adjusted for the currently high inflation rate. The most recent consumer confidence numbers in Denmark reflect the uncertainty related to the war, but the Danish economy comes from a strong position with low unemployment and healthy public finances as well as strong household finances, yet increasing prices in general must be assumed to have some effect on the activity level overall.

For lending fees, we should divide activity into three categories, namely 1) property market activity, 2) remortgaging activity and 3) refinancing of variable rate loans, all in Denmark.
In terms of the first category, we note that the activity level in general is slowing slightly from a very strong level last year, however, we are working diligently to improve trend of our market share.
For the second category, the development in the interest rates in Denmark has enabled some of our customers to benefit from remortgaging, and we generally see good activity.
Finally, with regards to refinancing, of the around DKK 80 billion up for refinancing in the market for 1st April, we have around DKK 46 billion, which will have a seasonal small positive effect on fee income in Q1 historically of around DKK 80 million.

Turning to net trading income, we saw good customer activity at our FX desk during the quarter. However, please bear in mind that our FIC trading has historically been negatively biased towards higher spreads. Volatility in the DKK mortgage market has been significant given both the uncertainty of the central bank responds to high inflation and the Russia-Ukraine war. Spreads on callable bonds have seen quite different developments, with lower coupons at nearly unchanged and higher coupons at 20-30 basis points wider with significant daily volatility during the quarter. 5Y non-callable bonds have seen more issuance and spreads are 5-9 points wider than the start of the year. Danish government bonds have also seen spread volatility vs. German government bonds. However, 10 year Danish-German spreads towards end of the quarter are 3 basis points wider.

Finally, please remember, that we do not have any commodities trading desk.

Looking at net income from insurance business, we would like to remind you about the very strong contribution from the financial markets last year, and point to the negative developments in the markets at the start of the year, which may have a negative effect on earnings in Q1. In addition, the sale of Danica Norway is still expected to be approved in H1-2022, and is expected to have a one-off effect of DKK 400 million, exempted from tax.

With regard to Other Income, we want to remind you; that the gain of the sale of our Luxembourg activities will be included in our Q1 numbers. The gain is in line with our guidance of around DKK 340 million pre-tax and DKK 250 million post tax. Please also note that the closing of the transaction relating to the MobilePay merger is still expected in 2022 and will result in a one-off gain of DKK 400-500 million, exempted from tax.

This concludes our comments on the income lines.

If we look at the cost line, please remember that Q4 included higher performance-based compensation, partly related to the higher activity level. Furthermore, with the current high level of inflation, we expect the potential impact for Danske Bank to be on our salary

costs. In Denmark a significant part of our employees are covered by a collective agreement with pre-agreed salary increases. The current agreement is up for renegotiation during 2023.
Moreover, as we have guided for, we expect remediation costs to remain at an elevated level throughout 2022, including the first quarter.

Turning to the impairment line and credit quality, we have a few things, we want you to have top of mind. Firstly, our limited direct exposure to the war. Secondly, in Q4 2021, despite recognising net reversals for the quarter in total, we made notable changes to our macro models reflecting, the higher risk of a potential severe macroeconomic scenario at the time in the midst of the pandemic uncertainty, which led to charges of around DKK 0.4 billion charges. Subsequently, societies more or less re-opened in the early part of 2022. Thirdly, there are fundamental differences between the abrupt lockdown of societies across the world in Q1-2020 and the current situation. Moreover, we have largely kept our PMAs in place following the pandemic, and in general we have a strong credit quality as well as a well-impaired and diverse credit portfolio. That said; there is no doubt, that the macroeconomic indicators will and have changed, and visibility regarding the medium to longer term effects is more uncertain.

We do not have any comments on Non-core or the tax line.

This concludes our comments on the P&L.

As a final point, I would like to touch on capital. As always, our capital will be impacted by earnings less the dividend payout.
As approved at the AGM, we have distributed 2 kroner per share of 2021 net profit, with an intended 5.5 kroner to be paid out in tranches after each interim report in 2022. The latter part is currently reflected in the shareholders' equity but will not be included in the CET1 ratio.

Last week, it was decided to increase the Norwegian Counter-cyclical buffer to 2.5% effective from 31st March 2023. This will impact our fully phased-in capital requirements in our Q1 report, where the basis so far has been 2%, hence a limited Group impact of around 0.06%. However, the 2.5% was already accounted for in our capital planning.
Moreover, we have noted the Danish Systemic Risk Board's recommendation to increase the counter-cyclical buffer to 2.5% from 2.0% in Q1 2023. We would like to remind you that this has not been approved by the ministry and will not be reflected in our fully phased-in requirements until it is approved[1]. However, for reference, 2.5% is already included in our capital planning.

Contrary to the past several quarters, we do not have any specific comments to REA, besides noting that market risk is as always subject to volatility in the market.

This concludes our initial comments in this pre-close call. Before we move on to the Q&A session, I would like to highlight that we enter our silent period on 8th April. Shortly after today's call, we will also start collecting consensus estimates with a contribution deadline on 11th April EOB. Please note that we will publish our Q1 2022 report on 29th April at 07:30 CET and that the conference call for investors and analysts will take place at 08:30am.

We are now ready for the Q&A session. If you wish to ask a question, please use the "raise your hand function".

[1] Please note this has been approved as per 30 March