Pre-close call Q2 2022

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Danske Bank – Investor Relations

SPEECH

Claus I. Jensen – Danske Bank – Head of IR

Good afternoon and welcome to the Danske Bank Q2 2022 pre-close call. My name is Claus Ingar Jensen, and I am Head of Investor Relations. With me, I have Olav Jørgensen and Patrick Skydsgaard 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. Given that we conduct this call via Teams, please be aware that if you want to ask questions, you must log on via the Teams app or your browser. If you are online via a telephone line, the IR team will be available for questions 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 1st July ahead of the publication of our Q2 report on 22nd July. 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 only answer questions related to already disclosed information and one-offs as well as publicly available data as of 21th June 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.

Firstly, I would like to recap on the current macro-economic outlook before we go through the line items. First of all we have very low predictability and high uncertainty. But we can see that inflation has continued to rise in Q2 from already high levels, which has led central banks to hike interest rates, especially in the US, where rate increases are now likely to trigger a recession and lead to weaker global demand. In the Nordic economies we currently have heated economies in varying degrees, which is expected to soften the negative impact from weaker global demand, but higher interest rates, global weakness, and consumer spending eroded by lower real incomes and lower asset values all point to a weaker outlook and lower house price in the Nordics in 2023.

Also I have no updates to our announcement on 28th April 2022 regarding the Estonia matter. We have no estimate regarding the timing, form of resolution or amount of a potential settlement or fine, which is likely to be material.

That said; let us start by having a look at net interest income.
Please remember that Q2 haves one interest day more than Q1 with an NII impact of around DKK 30-40 million per day.
During the quarter until now, the Swedish krona has depreciated around 3% against the Danish krone, while the exchange rate of the pound sterling was around 2% lower and the Norwegian krone depreciated around 8% against the Danish krone on the basis of publicly available data. Looking at the interest rate environment, we note that interest rates have generally risen further since the start of April and yield curves have seen almost the same rise in longer term yields and short-term yields.

Regarding volume developments, we refer to publicly available sector statistics as the only externally available source of insight and note that we continue to see a positive trend for corporate lending in Denmark and Sweden based on April figures. In general, please be mindful of potential fair-value effects in the reported Q2 volume figures relating to Realkredit Danmark.

With respect to margin developments, we also refer to publicly available sector statistics as the only externally available source of insight. We note that the trend we have observed over the past couple of quarters with a change in retail customers' preferences for products with higher margins such as interest-only and variable-rate loans is likely to continue.

Since Q1, 3-month NIBOR and CIBOR has increased 11 and 13 basis points, respectively, while STIBOR has increased around 40 basis points, all on the basis of quarterly averages.

Today it was announced that the Norwegian Central Bank raised its key policy rate from 0.75% to 1.25%. As of today, we have not yet communicated any adjustments to customer pricing.
Following Riksbanken raising interest rates to +0.25% at the end of April, we also adjusted prices for home loans in Sweden. This was done by up to 35 bps with effect from 6th May for variable-rate loans and fixed-rate loans. Noting that around 25% of our Swedish mortgage stock is variable rate. With effect from 24th of May fixed rate pricing was increased again by an additional up to 60 bps across maturities. Also, from 1st of June, interest rates on consumer loans in Sweden were increased with 45 bps.

Finally, as a result of the latest Bank of England rate hike, with effect from 17th June, we increased the Danske Bank Reference Rate in Northern Ireland by 25 bps to 1.25%.

Turning to funding, we remind that we issued a dual tranche non-preferred senior benchmark which settled 1st April. The 3NC2 tranche was of USD 750 million priced equivalent to 3M EURIBOR +98bps and the 6NC5 tranche was USD 1,250 million done at equivalent to 3M EURIBOR +138bps. Both well received by investors leading to healthy oversubscription.
Please note; that we called EUR 750 million AT1 at the effective call date 6th April, which means we have no remaining equity accounted AT1s. For clarity, note that the interest expense on the equity accounted AT1s has been deducted below the line. Also, as announced on 20th April we redeemed EUR 378,334,000 NPS at par on 24 May 2022.

As always, our fee income is dependent on market conditions for the capital markets, development of the equity markets and the general activity level in our banking operations. As the activity and level of issuance in primary markets has slowed, it is also likely that our Capital Markets business will be negatively affected.
With regard to investment fees, the negative development in the equity markets since April has continued. As a result, as of 20th June, the OMX C25 index was down 12% and the S&P 500 index was down 19%.
Consumer confidence measured by Danmark Statistik is at very low level compared to historic levels. However consumer spending seems relatively unaffected as yet. We refer to our publicly available Spending Monitor paper (dated 10 June 2022), in which card data shows that spending is up from the level in 2019, which continues to confirm that Danish consumers are fairly resilient in the face of higher uncertainty and rising prices. This is supportive for activity driven fees. In addition, for lending fees, we reiterate that the development in the interest rates in Denmark has enabled some of our customers to benefit from remortgaging.

Turning to trading income, increasing expectations for a recession in the US (and Europe) and markedly higher central bank rates, have led to a significant drop in equity markets and an increase in longer term rates to a level not seen since 2014. Also short term swap rates for instance 2Y Swap rates in Denmark and Sweden have widened to levels not seen in at least a decade. Turning to Danish mortgages, we have seen a continued widening of credit spreads on especially variable rate mortgages of some 20bp from the level in Q1. Callable bonds spreads have been very volatile during Q2 and OAS spreads are in general 10 bps wider depending on coupon and duration. In addition, spreads between Danish and German government bonds widened by 5-8 bps. The accompanying increase in volatility and illiquidity may have a negative effect on income generated by financial market activity in the second quarter primarily for rates and equities. Q1 trading income was affected by several value adjustments and as mentioned in Q1 the effect could come back in the future. However, the timing of this is subject to market development and unlikely in Q2 given the current market volatility.

Looking at net income from insurance business, we can again point to the negative developments in the markets during Q2 and the issues just mentioned for trading income. The decrease in the investment result driven by valuation adjustments we saw in Q1 was expected to normalise in 2022, however, we do not expect it to normalise in Q2 and the future outlook is uncertain.
In addition, we can confirm that Danica Pension has received all the necessary regulatory approvals of the sale of Danica Pension in Norway as communicated in the press release earlier today. We still expect a gain for Danske Bank of approximately DKK 0.4 bn., however it is currently uncertain if the gain will be booked in Q2 or Q3.

We do not have any specific comments on Other Income, except that we reiterate that we still expect the MobilePay transaction to close in the second half of 2022 which will result in a one-off gain of DKK 400-500 million, exempted from tax. Also we want to remind you; that the gain of the sale of our Luxembourg activities of DKK 421 million pre-tax was included in our Q1 numbers.

This concludes our comments on the income lines.

If we look at the cost line, we would like to reiterate our guidance for elevated remediation costs for the full year. Other than that, we do not have any specific comments regarding our cost development and we have no changes to our cost guidance for the full year.

In respect of credit quality we have nothing to add from when we published our Q1 report. Recent macro forecast by Danske Bank Research doesn't cause immediate concern for credit quality in Q2.

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

This concludes our comments on the P&L.

Finally I would like to talk a bit about capital. As always, our capital will be impacted by earnings less the dividend accrual.
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. However, as we are now in initial discussions with U.S. and Danish authorities on a resolution of the Estonia matter, Danske Bank decided not pay out dividends in connection with the interim report for the first quarter of 2022. The decision for paying dividends for 2021 is described in the Interim Report Q1-22 and Company Announcement #7 from 28th April 2022.
On 31st May, the Swedish FSA announced their plan to raise the countercyclical buffer value to a normal level of 2% per June 2023. This is fully in line with our capital planning. 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 1st July. Shortly after today's call, we will also start collecting consensus estimates with a contribution deadline on 4th July EOB. Please note that we will publish our Q2 2022 report on 22th July at 7:30am CET and that the conference call for investors and analysts will take place at 8:30am.
As of 1st May our new organisation took effect, splitting Personal & Business Customers into two units, Personal Customers and Business Customers. We expect to be able to publish restated comparison figures in the week commencing Monday 4th July. Analysts covering Danske Bank will also receive the figures via e-mail.

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