



Pre-close call Q3 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 Q3 2022 pre-close call. My name is Claus Ingar Jensen, and I am Head of Investor Relations. With me, I have Olav Jørgensen and Nicolai Tverne 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 macroeconomic trends in our markets as well as one-offs that you should be aware of before the start of the silent period on 7th October ahead of the publication of our Q3 report on 28th October. 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 the 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 26th September, 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 macroeconomic outlook before we go through the line items. The environment overall is characterised by uncertainty, and our outlook therefore remains clouded. Central banks appear committed to bringing down the rapid rise in inflation, even if this requires an extended period of below-trend growth and some weakening of labour market conditions. Our most recent economic outlook indicates a further uplift in central bank rates, and though unemployment is expected to rise, we still see it being at a low level of around 3%. So far, economic activity has remained high and household finances were robust in the third quarter – a good starting point for entering a potential recession.

With regard to the Estonia matter, we still have no estimate regarding the timing, form of resolution or amount of a potential settlement or fine, which as previously stated is likely to be material. We can only refer to company announcement number 7 released on 28th of April.

On 31st of August, we presented a solution for our legacy debt collection issues. This included setting the outstanding debt for 90,000 debt collection customers to zero, and our operating expenses for 2022 are therefore expected to increase by approximately DKK 0.6 billion due to an increase in provisions for compensation to customers. The write-down of debt will also lead to an increase in loan impairment charges of DKK 0.65 billion, which includes part of the compensation to customers. These items will be booked as one-off items in the third quarter of 2022.

Finally, as announced on the 16th of September, the changes in the ownership shares of the MobilePay merger will not materially affect Danske Bank's previously communicated expectations. The tax-exempted one-off gain on the transaction is expected to be approximately DKK 400 million on the basis of the merger and the distribution of shares in the new parent company, in which Danske Bank will now have an ownership share of 27.8% rather than the previously announced 25%. The merger continues to be subject to approval by the relevant authorities, including the EU Commission. In respect of the timing of the financial gain, we have noted that some estimates include this one-off gain in the third quarter. However, as we expect final approval to be given in Q4 2022, this should be reflected accordingly in your estimates.

That said; let us have a look at net interest income.

As always, please note the impact of currency fluctuations in the regions in which we operate, and further note that Q3 has one interest day more than Q2, with an NII impact of around DKK 40 million per day.

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, particularly in Denmark, based on August figures.

As we saw in Q2, please be mindful of the potential fair-value effects on the reported lending volume at Realkredit Danmark when rates are moving up.

Since Q2, 3-month STIBOR and NIBOR have increased 93 and 102 basis points, respectively, all on the basis of quarterly averages. Please be aware that such increases will lead to higher funding costs in Norway and Sweden, all else being equal.

We have seen several central bank hikes during the quarter across the markets in which we operate.

Further to the increases in policy rates, we have also adjusted our deposit and lending rates for customers. However, as always, these adjustments will be implemented with a slight delay due to notice periods for certain products.

I will now highlight the policy rate changes we have seen in the regions in which we operate that will have an impact on NII in Q3:

Following the ECB's and the Danish central bank's rate hikes of 50bps on 21st of July, we expect a 2022 effect of DKK 330-340 million, with a 2-month effect in Q3.

In Norway, at its meeting on 22nd of June, the Committee decided to raise the policy rate by 0.5 percentage point to 1.25%, and we followed on almost all lending products and, to a lesser degree, on deposits – due to the notice period, prices in Norway were adjusted with effect from 12th of August.

In Sweden, on the 30th of June, Riksbanken announced that they would raise its policy rate by 50bps to 0.75%. We have taken numerous price initiatives related to lending products to reflect the higher central bank and funding rates, while we passed through some of the effect on the deposit side.

On 4th of August, the Bank of England raised its Bank Rate by 50 basis points to 1.75%. In high-level terms, the higher BoE rates were largely passed through on the lending side, while on the deposit side, pass-through has been more mixed depending on product and pricing.

Additionally, please note that we have seen several rate hikes from central banks towards the end of the quarter, but the price actions we have taken following these rate hikes will be implemented with effect only beyond Q3.

Generally, we maintain our Group NII sensitivity guidance across all currencies of around DKK 800 million per 25 basis points, with slightly positive convexity for the next 100bps increase.

Turning to funding, we remain comfortable with our funding position. On 6th of September, we successfully issued a new EUR 1.25 billion 3-year covered bond. The benchmark issue was priced at mid-swap flat, had a 2.125% coupon and was more than 2.5 times oversubscribed.

In respect of our fee income in the third quarter, we have noted that retail activity generally remained relatively high. Our recent spending monitor highlighted that, based on card data for Denmark, spending was up 2.6% in August from August 2021 – with a similar increase in July from the year before. Real spending, adjusted for inflation, has slowed however, with an implied drop of 3-4% from a high level.

The relatively high activity is in contrast to the consumer confidence level measured by Statistics Denmark, which is at a historically-speaking very low level. Considering the current erosion of purchasing power and uncertainty for households, the resilience of consumer spending is so far supporting activity-driven fees, but we could see an impact beyond Q3.

Additionally, we reiterate that the development in interest rates in Denmark has enabled some of our customers to benefit from remortgaging, although this is countered by a general slowdown on the housing market.

Finally, in respect of activity-driven fees, corporate activity generally remained at a high level, as indicated by public volume statistics.

Activity remained subdued in the capital markets during Q3, with low issuance activity in primary ECM markets in particular. We therefore expect income from capital markets fees to be affected, and the same for investment fees due to lower expected assets under management, in line with our guidance for total income in 2022.

Looking at trading income and net income from insurance business, we can point to the volatile developments in the markets during Q3. In this context, we have seen a very large widening of spreads on callable bonds of some 25-50bp, mostly for lower-coupon bonds. Credit spreads on non-callable bonds have also been widening but only 10bp for 5Y bonds from the level in the preceding quarter. The yield spread between Danish and German government bonds has widened 4bps.

Performance related to customer activity in FI&C will always be subject to market conditions, whereas the valuation adjustments from our Treasury operations and Northern Ireland, which contributed negatively in Q2 is likely to add materially to the uncertainty for trading income in Q3 driven by significantly higher interest rates in the UK market in particular.

For both trading income and income from insurance we continue to expect a below normalized level based on significant lower income in the first six month of the year.

Please note that when comparing income from insurance to the level in the preceding quarter, we had a gain of approximately DKK 400 million in Q2. In addition, we expect a one-off product-related cost of approximately DKK 125 million in Danica.

We do not have any specific comments on Other Income, except that the merger of MobilePay will not be reflected in Q3, as mentioned in the beginning of this call.

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 underlying cost guidance for the full year, when you disregard the impact of the solution we have presented for our debt collection customers, which will result in a one-off cost of DKK 600 million in Q3.

Specifically for impairments, we are mindful of the potential impact of the deteriorating macroeconomic environment, but we remain comfortable with the quality of our lending book and the adequate provisions we have previously made in terms of buffers. In addition, the starting point for households in the Nordic countries remains solid, with healthy home equity levels and since the employment level remain high. We therefore do not have any immediate concerns with regard to credit quality in Q3, and in respect of credit quality, we have nothing to add from when we published our Q2 report when you keep in mind the impairments related to the debt collection case of DKK 650 million that I mentioned earlier. Finally, please note the DKK 250 million one-off we booked in the second quarter related to a potentially lower recovery rate for debt collection customers in Denmark.

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

This concludes our comments on the P&L.

Finally, our capital position will, as always, be impacted by earnings less the dividend accrual. We do not have any specific comments on the REA, besides noting that market risk remains 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 the 7th of October. Shortly after today's call, we will also start collecting

consensus estimates with a contribution deadline on the 7th of October EOB. Please note that we will publish our Q3 2022 report on 28th October at 7.30am CET and that the conference call for investors and analysts will take place at 8.30am.

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