BAWAG Group

BAWAG Group Q1 2020

Earnings Call

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Transcription

<u>Speakers</u>:

Anas Abuzaakouk

Enver Sirucic

Anas Abuzaakouk: Good morning everyone. I hope everyone is keeping well and staying healthy. It goes without saying, we're living in unprecedented times and having to address an environment that we have not seen before. However, I can assure you we will do our best to navigate these uncertain and volatile times ensuring that we protect our employees, support our customers and local communities, and protect our franchise. Before we jump into the financials, we wanted to provide an update as to the actions we've taken in response to COVID-19.

On slide 2, in Austria, which is the core and foundation of our business, a lockdown was implemented affecting all businesses with the exception of critical infrastructure (this includes hospitals, clinics, pharmacies, grocers, and bank branches).Austria was one of the early movers in imposing a quarantine on March 15 and has been one of the early movers in slowly easing restrictions and beginning to open the economy a month later on April 14.Prior to the quarantine, our team instituted a COVID-19 task force to mobilize teams across the Group to address health and safety guidelines for our employees and customers, operating protocols, home-office measures, and systems stability.

We migrated to a home-office model successfully with approximately 75% of employees working from home to-date. We've also provided flexible work hours, home care programs and special leave measures for our employees as they juggle balancing the competing needs of their families and work. We're proud to say we've also not tapped into any government furlough, employee subsidy or special assistance programs as these are earmarked for those most in need.

Recognizing the challenging times ahead, taking into account public sentiment, ensuring we do our best for our various stakeholders and most importantly doing what we think is "right", the entire Management Board waived their 2019 bonuses and any potential bonuses for 2020. We also instituted a special bonus program for our front-line branch employees, who represent the best of the banking community and who have gone above and beyond in supporting our customers and our local communities. A special thanks goes out to employees in our call centers, operations, technology, sales force and collections team in going above and beyond to support our customers and communities during their greatest time of need.

Over the past 6 weeks, we've maintained 100% access to our branches and self-service devices, maintained normal operating hours with enhanced security protocols and social distancing guidelines, and ensured that 99% of ATMs were functioning across our network. We've also proactively reached out to customers through "take-care" outreach calls to check in on customers, answer their questions, and support them the best we can. We've established new online processes and have encouraged customers to adopt digital channels, or access our call center, to reduce branch visits. We're doing our best to ensure customers understand the various stimulus programs and provide support where possible.

Given the fluid nature of events and the uncertainties in both scope and length, this may result in an overall challenged and volatile market environment over the coming months and we are prepared to navigate these unchartered waters as we continue supporting our employees, customers and local communities to the best of our ability while also protecting the franchise.

On Slide 4, a summary of the first quarter results. We delivered net income of € 61 million, earnings per share of € 0.69 per share, and a return on tangible common equity of 9.1%.On a normalized basis, taking into account the first quarter front-loaded regulatory charges, this translates to a net profit of € 81 million and a return on tangible common equity of 11.9%.

Since early March, when the World Health Organization (WHO) characterized the outbreak of COVID-19 as a global pandemic, we've witnessed unprecedented market volatility and uncertainty not seen since the financial crisis. Despite this, the underlying operating performance of the business remained strong in the first quarter with pre-provision profits of € 171 million and a cost-income ratio of 42%.To address the deteriorating macroeconomic environment as well prudently provision against the observed build-up of customer payment deferrals due to the COVID-19 crisis, we posted an incremental general reserve of € 25 million for the quarter, leading to total risk costs of € 55 million. We're fortunate that we enter this crisis on very strong footing, having transformed the franchise over the past decade. This will allow us to navigate the challenges ahead and weather any potential further macroeconomic deterioration. We hope for the best, however, we will be prudent in how we manage and assess the risks ahead.

The bank's capital position remained strong, with a fully loaded CET1 ratio of 12.7%, down 60 from the year-end 2019 figure when including the first quarter dividend accrual. The Bank continues to deduct the full year 2019 and first quarter 2020 dividends from capital and will wait for further guidance from our regulators regarding capital distributions later in the year.

Given the COVID-19 crisis, the unprecedented demand shocks we're seeing, the overall market volatility, and difficultly in projecting the scope and length of this pandemic and the deterioration in the macroeconomic environment, we've withdrawn our targets for the year as this would be unreliable. We are all flying in the dark to a certain degree as the inability to forecast accurately the initial demand shock to the economy as well as the Day 2 impact on economic output, longer term unemployment, and potential structural changes to the economy. We will do our best to provide clear and transparent updates to the best of our ability, bearing in mind the fluid situation.

However, given our strategic focus, strength of the franchise, and the transformation that has taken place over the years, we're committing to a medium-term target, generating a return on tangible common equity >15% and a cost-income ratio <40% in a normalized environment.

Moving on to Slide 5.For the first quarter, core revenues were € 292 million, up 2% versus the prior year.Operating expenses decreased by 1% as a result of past investments and efficiency measures, resulting in a stable cost-income ratio of 42%. Our pre-provision profit was € 171 million, stable versus prior year despite the volatility during the month of March and a reflection of the strong underlying operating performance of the business.

The first quarter 2020 also included regulatory charges of € 36 million, which represent approximately 85% of full-year-charges that are required to be booked in the first quarter. Risk costs were € 55 million in the quarter, an increase of € 43 million from the first quarter of 2019, or more than 3.5x risks costs for the prior year. To address the deteriorating macroeconomic environment as well as prudently provision against the observed build-up of customer payment deferrals due to COVID-19, a general reserve of € 25 million was posted in the Retail & SME business. Additionally, we took a specific provision of € 10 million for an existing exposure with the provision in the Oil & Gas sector in our Corporates business.

Earnings per share came in at € 0.69, down 29% versus the prior year. Tangible book value per share was € 30.41, down 2% versus the prior quarter and flat versus the prior year. This assumes the deduction of the full year 2019 dividend as well as the dividend accrual for the first quarter 2020.

We were also able to grow both total assets and customer loans 2% over the quarter. We will look to use our capital and liquidity to support our customers and communities in the months ahead while also being prudent and protecting our franchise.

On slide 6, we highlight the capital development during the quarter. With a CET1 ratio starting point of 14.4%,which does not deduct the 2019 full year dividend, we ended the quarter at 13.9% CET1 ratio, down 40 .We generated 40of gross capital through earnings. This was offset by 40 basis points from increasing RWAs, a direct result of 2% net asset growth, and a 50 basis point decline primarily due to negative OCI movements as a result of widening credits spreads during the month of March in our securities portfolio. As of last Friday, the negative OCI impact was all but offset, with credit spreads tightening during the first 3 weeks of April having resulted in a 40 basis point increase in our CET1 ratio already in the second quarter. Assuming we are able to make dividend payments for both the full year 2019 dividend as well as the first quarter dividend accrual, our proforma CET1 ratio would be 12.7%.We will continue to deduct the full year 2019 and quarterly 2020 dividends from capital as we wait for further guidance from our regulators regarding capital distributions later in the year.

On slide 7, we wanted to highlight the main pillars of our business and the strategic transformation we undertook since 2012, as these actions allowed us to enter the crisis in a strong position and underpins the bank’s resiliency. We entered into the crisis from a position of strength, having transformed the business over the years to be able to withstand economic downturns. We have strong capital levels with a year-end 2019 CET1 ratio of 14.4% (or 13.3% after deducting the full year 2019 dividend).We have a solid funding profile with two-thirds of our funding coming from customer deposits. Our liquidity coverage ratio is 135%, with liquidity buffers north of € 7 billion that we can draw upon.

And we have a highly efficient business with a cost-income ratio in the low 40’s generating mid-teen returns pre-COVID-19 crisis and high levels of pre-provision profits. This will give us the flexibility to proactively and prudently address risks that may arise from a severe economic downturn. Our asset quality is defined by a conservative risk appetite and disciplined underwriting since 2012, which is best reflected in a low NPL ratio under 2% and low risk costs through the years, albeit having benefited from a benign credit environment.

While it’s too early to tell how the crisis will unfold, I’m confident our team will be able to navigate these unchartered waters given the transformation we executed since 2012, the resiliency of our business, and the capabilities of our team.

On slide 8, we wanted to provide a snapshot our overall customer business, in terms of products, countries and secured versus unsecured lending. At the end of the first quarter, customer loans amounted to € 31.8 billion, of which 75% were secured or Austrian public sector lending. Our business focus has always been focused on the DACH region and the developed markets of Western Europe and the United States, with approximately 70% of customer exposure in the DACH region and the residual in Western Europe and the United States.

In our Retail & SME business, 83% of our lending is secured, approximately 84% comprised of mortgages, and approximately 88% tied to the DACH region.

In our Corporates & Public business, almost two-thirds of the business is asset backed real estate or public sector lending. The geographic split of the business is 50% DACH region and 50% Western Europe and the United States.

On Slide 9, the Retail & SME segment delivered a pre-tax profit of € 75 million, down 10% versus the first quarter 2019, impacted by rising risk costs. The business generated an 18% RoTCE and a cost-income ratio of 39%. Pre-provision profits were € 142 million, up 17% versus the prior year. The solid underlying business performance was driven by core revenue growth of 10% versus cost growth of only 3%.The risk costs were € 42 million for the quarter, up € 27 million, or almost 3x the prior year levels. This was a result of deciding to book a general reserve of approximately € 25 million to address the COVID-19-related impacts.

Slide 10, we provide a portfolio overview of the € 18.3 billion of customer loans and leases across the Retail & SME business. The page captures the credit and arrears profile for our key product groups, highlighting the split of secured versus unsecured lending, NPL ratios, total reserve ratios, and arrears profile. We also captured the loans and leases with payment deferrals as of April 22.The key points to highlight are the following:

Our Retail & SME business is highly collateralized, with ~83% of the lending done on a secured basis, of which 84% are mortgages. Our unsecured lending is made up primarily of consumer personal loans and overdrafts. Approximately 80% of personal loan customers are primary banking customers with a direct debit salary current account.

Overall, our 90 days past due (dpd) delinquency is around 1% for secured lending products and 3.1% for our unsecured lending products pre-COVID-19 crisis.

To-date, we’ve observed payment deferrals of approximately4% across the segment. Payment deferrals are defined as the sum of the total customer loan or lease balance with a payment holiday request, divided by total loans and leases).The behavior is quite consistent between secured and unsecured customers at approximately 4%.

Given the unprecedented demand shock, the deteriorating macroeconomic condition, and the many unknowns ahead of us, we booked a general reserve of approximately € 25 million during the first quarter. This was comprised of a € 14 million reserve tied to the recently published macroeconomic forecasts published by the IMF, which translates to full year GDP decline of minus 6.5% in 2020 and an uplift of 3.9% in 2021 across the markets we operate in. We will continue to monitor the deteriorating macroeconomic condition and make further adjustments as needed.

Additionally, we booked an € 11 million reserve primarily related to the build-up of customer payment deferrals across our unsecured loans. We will closely monitor this metric and take a prudent approach to provisioning these balances as we monitor payment deferral balances and overall customer behavior in the months ahead. We will also attempt to provide a longer-term perspective on underlying trends we see in the portfolio. Our approach will always be to err on the side of caution and be both prudent and conservative in provisioning.

On Slide 11, the teams continue to support our customer base while executing on a variety of operational and strategic initiatives that we had planned in the beginning of the year. First and foremost, we are focused on responding real-time to our customer needs during this crisis – be it through maintaining 100% branch openings, maintaining normal service hours and access to our ATMs and self-service machines, or through proactive “take care” calls touching base with our customers and seeing how we can help.

While responding real-time to the changed customer needs during the crisis, we continued executing on a variety of business initiatives. During the first quarter, easybank was merged into BAWAG P.S.K. While the brand easybank will remain and there is no change for customers, this will bring efficiencies in processes and product offerings. We also redesigned the Austrian Retail organizational set-up and are working on a number of initiatives to enhance customer analytics and overall digital engagement. In Germany, we continued the centralization of middle-and-back-office activities that have been accelerated as we take advantage of the subdued business activity and assess the opportunities ahead. The integration of the businesses acquired in 2019 is complete and the focus will now be on growth and profitability initiatives for these channels. This will come in the form of new partnerships and expanding our existing product offering to new markets and industries when the time is right.

On slide 12, the Corporates & Public contributed a pre-tax profit of € 31 million during the first quarter, down 34% versus the previous year, with a return on tangible common equity of 11% and a cost-income ratio of 30%.Pre-provision profit was € 49 million and flat versus prior year. Core revenues were down 9%, but this was offset by a 21% reduction in operating costs. Risk costs were € 12 million for the quarter, primarily related to the booking of a specific reserve of € 10 million for an exposure in the Oil & Gas sector, which we had provisioned in prior quarters. We are beginning to see solid lending opportunities with good risk-adjusted returns. Nevertheless, we will continue to maintain our disciplined underwriting and focus always on risk-adjusted returns.

On Slide 13, we provide a portfolio overview of the € 13.5 billion of customer loans across the Corporates and Public business. We break down key risks we see across portfolio and exposures to cyclical sectors that are higher risk at the moment. The key points to highlight are the following:

In Corporate lending, we've been conservative over the years with a focus on senior secured lending, free cash flow generating companies with defensive business profiles and solid capital structures. We have not been as active over the years in corporate lending as we've found the space challenging from a risk-adjusted returns standpoint. Of the € 4.9 billion, our net exposure to higher risk cyclical sectors, which is defined from our standpoint as Oil & Gas, Shipping, Hotels, Non-grocery retailers, and airlines, is € 91 million, or 1.9% of total corporate assets, which is equal to 29 basis points of total customer loans. One-third of the exposures are Non-Performing Loans and we have been proactively monitoring the positions, having taken a provision already in the first quarter. We will continue to be prudent and conservative, addressing any reserve requirements as needed.

In asset backed lending, we've taken an equally conservative approach to lending. Our focus has been on senior secured lending with no mezzanine financing and has been real estate focused. On average, we underwrite to a Loan-to-cost or Loan-to-value of under 65% and an interest coverage ratio of > 2.0x.We work with a handful of established sponsors and have been active in NPL financing over the years. We feel good about the overall portfolio. Given the acute stress on retailers and hotels, we are actively monitoring real estate loans with stand-alone exposure to these types of businesses, which amounts to approximately 8% of the asset-backed lending portfolio. The majority of the loans have either an interest reserve, or free cash flow, for approximately 6 months without any payment deferrals in the current environment. Of these exposures, over 25% of the principal has been repaid as the vintages date back to 2017 and 2018.

The Public sector lending is focused 100% on Austrian government entities comprised of municipalities, Federal States and the Republic of Austria. As the payments provider to the Republic of Austria, we've been active in public sector lending for quite some time and feel good about our exposure.

I will now pass to Enver to go through the Investment book and detailed financials. Thanks.

Enver Sirucic: Thank you, Anas. I will continue on slide 14. We wanted to give you an overview of what happened in Q1 in terms of our excess cash position and our investment book and also wanted to reiterate the key metrics of our liquidity book. So, after we divested approximately € 1.6 billion of our liquidity book during 2019 given low or negative spread environment of the last year, we now re-deployed € 1.5 billion of our cash position into high quality securities again. The overall cash and cash equivalents position went from € 7.1 billion at year-end to € 5.6 billion at the end of Q1, while the investment book went from € 4.7 billion to € 6.2 billion in the same period of time. The composition of the book remains unchanged in terms of quality, 98% of the book is investment grade, 80% is rated single A or higher. Also, in terms of maturity profiles and concentration we followed our existing strategy of shorter duration and high diversification.

This leads me to slide 16, development of our P&L and key ratios. Let me start with revenues first: core revenues were largely stable versus Q4 with a solid net interest margin of 2.34%. This quarter core revenues made up 99% of our operating income, while Other revenues came in significantly lower versus prior quarter and only represented 1% of the operating income. Operating expenses further came down versus Q4, but also were lower compared to Q1 of last year. The cost-income ratio improved slightly and stood at 42.3% as of Q1. All these developments led to a very solid pre-provision profit of € 170 million. This probably underlines best the strong quality of our earnings of our bank. As every year, we booked 85% of the expected fully-year regulatory charges in the first quarter. We already have talked about the general risk provisions related to Covid-19 in the Retail & SME segment and the provisions for oil & gas exposures in our Corporates & Public segment, which all together explains the significant increase in risk costs compared to our normal run-rate of € 15 to € 20 million per quarter.

Moving on to slide 17. Totals assets were up 2% as we grew our customer loans by approximately € 500 million in Q1 and as previously mentioned re-deployed € 1.5 billion of our excess cash into high quality securities, this also led to parallel increase in risk weighted assets of 2% in Q1. On the funding side, we issued a € 500 million covered bond in January and participated with € 1.25 billion in the LTRO in March. Customer deposits were largely stable after considering usual seasonal movements.

On slide 18, core revenues. A very solid quarter taking into account actual circumstances. Net interest income was down versus the prior quarter, driven in large part by lower number of days in Q1 vs Q4. The good underlying performance is reflected in a solid net interest margin of 2.34% for the quarter. Despite the current challenges we expect a stable NII development for the year on the back of nice growth of interest-bearing assets in Q1 and also the positive momentum in interest rates, especially the improving 3-months Euribor that we've been seeing for the last couple of weeks. Net commission income was actually up 3% versus the prior quarter, but we expect a challenging year assuming negative impacts on our advisory and branch business from the COVID-19 crisis. So, the outlook for 2020 is stable NII and a negative impact of up to 15% on net commission income.

With that, moving on to slide 19. Operating expenses were down 7% versus the prior quarter and down 1% versus Q1 of last year. The cost–income ratio was at 42.3% and absolute costs were at € 125 million. This is really a reflection of all the initiatives we started working in 2019, like the centralization of the middle-and-back office activities in Vienna.

In general, nothing has changed in our discipline around cost. We are now assessing the implications from COVID-19 on our operating model – including a higher shift from physical to digital, both in terms of our customer approach, but also in terms how we operate, i.e. home office versus office. We think this could actually be a catalyst for future cost initiatives and good starting point to rethink and redefine our operating infrastructure. We are positive about the cost development in 2020 and we think costs could come down approximately 5% versus 2019.

Slide 20, a lot has already been said on risk costs, but let me briefly summarize all effects. So the two special effects this quarter are coming from the COVID-19 related € 25 million general provision in our Retail & SME segment and the € 10 million specific oil & gas provision in our Corporates & Public segment. In total, both effects account for € 35 million of the € 55 million risk costs in Q1. The remaining € 20 million of risk costs represent our normal run-rate of approximately € 17 million and another € 3 million for ECLs booked for new business in Q1.

NPL ratio improved slightly from 1.7% to 1.6%. Just given the market uncertainty and the ongoing deterioration in macroeconomic environment, we cannot give a reliable outlook on risk costs for 2020.

On slide 21, a summary of what happened on the capital front. Most of the highlights have been mentioned earlier in the presentation, but in a nutshell: CET1 ratio came in at 12.7% and our total capital ratio was at 16.3%. Both ratios are after deducting the full year dividend for 2019 of € 230 million and a dividend accrual of € 30m for the first quarter, so in total € 260 million of dividends are deducted from the capital ratios shown here.

Risk-weighted assets increased from € 20.4 billion to € 20.9 billion driven by growing customer loans and securities, while the RWA density remained completely unchanged at 45%. For the rest of the year we expect to further accrete capital from earnings and a potential increase in risk weighted assets, primarily coming from our organic business.

Moving on to slide 22, we tried to summarize current regulatory measures and recommendations and how we as BAWAG are impacted and what we decided to do. Let me address all points on the left side: ECB allowed banks to fully use capital buffers and liquidity buffers, but given our strong capitalization and liquidity levels we do not intend to make use of these allowances. On the second point, the new composition of P2R was moved forward and came already into effect, allowing us to meet 88 basis points of our 200 basis points P2R with non-CET-1-instruments, effectively reducing our SREP CET1 requirement from 10.2% to 9.3%. We also followed the regulator's recommendation not to pay dividends until October and will assess the situation once there are firm guidelines or a new recommendation in place, in the meantime we continued to deduct the 2019 and Q1 '20 dividends from our capital and capital ratios. Updated macro-economic scenarios are expected to be provided by the ECB later in Q2, we decided to apply the most recent IMF scenario in the meantime for our Retail & SME segment. A lot has been done in providing market liquidity by the ECB, the new TLTRO program is something that we will most likely participate in.

On slide 23. Really short, the key messages are three-fold. First, our funding profile remains solid with a high share of customer deposits and secured funding. Second, we have a very manageable amount of redemptions in the next few years, so no need to raise funding if conditions are not favorable and third, our liquidity ratios are comfortably above required levels and we have very high liquidity buffers in place.

Coming to slide 24. So we tried to provide here more transparency on the outlook for 2020. Let me reiterate the key points; we think that the net interest income will remain fairly stable compared to 2019, net commission income will be negatively impacted and based on various assumptions it could be down up to 15%. Other income we expect to be lower year-over-year, while we see a positive development in operating expenses, which we expect to be 5% lower than in 2019. We are obviously running different scenarios on risk costs and also comparing with data from previous crises, such as 2008 and 2012, but it is truly not comparable, our asset quality is much stronger as of today, but also the crisis and the situation is very different and given the ongoing market uncertainty and deteriorating macro environment, we cannot give a reliable outlook on risk costs at this point in time, but rest assured we will do our best to protect our balance sheet. Having said that, we are committed to deliver an RoTCE of greater than 15% and a cost-income ratio of below 40% in the medium term based on a normalized environment. Lastly, we decided to move our AGM to the fourth quarter as well as to move the Capital Markets Day to the first half of next year.

With that I would hand over to Anas for final remarks. Thanks.

Anas Abuzaakouk: Thanks Enver. I just wanted to wrap-up the presentation with a few remarks. We entered this crisis, which is like none we've seen or lived through before, having spent the better part of the last decade transforming our business and are fortunate to be going into this from a position of strength. We did a great deal of heavy lifting over the years, having invested significant amounts to make our business more efficient, more digital, and more dynamic. We are confident that we will be able to navigate the unchartered waters ahead.

We've also tried to provide more detailed information about the overall business, our asset quality, how we manage risk, and highlight areas where we potentially see challenges. We believe being clear and transparent is most critical during a crisis.

Just one last note. We have a highly efficient business with a cost-income ratio in the low 40's, generating mid-teen returns pre COVID-19 and high levels of pre-provision profits. This will give us the flexibility to proactively and prudently address risks that may arise from a severe economic downturn. We hope for the best, but we'll manage our business prudently.

With that, operator, we can open up the call for questions.

Operator: Thank you ladies and gentlemen. For those who wish to ask a question you will need to press star and one and wait for the operator to get your first and last name. Once again star and one if you wish to ask a question. Your first question comes from the line of Pawel Dziedzic from Goldman Sachs. Please ask your question.

Pawel Dziedzic: Hi, good morning everyone and thank you for the presentation. I have a couple of questions and I will start with asset quality. So you mentioned that part of your general charge that you took this quarter is driven by assumptions on basically on payment holidays that you granted an assumption of migration to non-performing exposures. Now at the end of March, if I read correctly on slide 10, you granted payment deferrals to around 4% of your clients. Would you be able to give us a sense if the number changed since and by how much and how high it can get? And obviously, if you would be still planning to impair or book impairments in line with assumption that 50% will default. And maybe if you can give us a little bit background on how you came up with this assumption. So that's the first question.

The second question is on your non-Retail lending. And obviously, in particular, on Corporate and asset backed lending. So what measures are you taking there, if any, at this point in time, to ensure that you are in a good position to minimize the losses? Are you giving any payment holidays? Are you working with the clients actively? And would you see it as a potential source of risk going forward? Because as far as I could tell from your earlier remarks, it sounds that you are pretty confident that you are in a good place.

And maybe just the last question on costs, and I appreciate that you're taking extra measures, and you plan to take the cost down by 5% this year. Are those any new initiatives? Are those previously planned measures? And if you look back at the steps that you can take in the current environment, to what extent do they rely on reduction in your FTE's, which might be possibly more difficult in the current circumstances than in normal times? Thank you.

Anas Abuzaakouk: Yes. Thanks, Pawel. All really good questions. Let me go ahead and address the questions and then Enver, if you have any inputs obviously jump in. So Pawel, in terms of the customer payment deferrals on slide 10, just to highlight because you said as of the end of March, the payment deferral balances are as of April 22, so we tried to give as much of a real-time update as possible, and the general provision reflects that 4.1% payment deferral balance for consumer unsecured. The reality is those customers that are granted payment holidays today, we're sober about the fact that not everyone will return to being a paying customer or performing customer. And what we've tried to do is be proactive in anticipating, based on historical roll-rates in terms of delinquency buckets from 1 to 90, the 90 days past due, using kind of a loss rate and the percentage on that customer payment deferral balance. So what we've done is as of April 22, taking that balance, assumed 50% effectively on that in terms of migration to delinquency buckets and then put a severity factor against that.

Just to be acting out of an abundance of caution and prudence, knowing that not everybody will migrate back to being performing post the payment holidays. But that figure is as of April 22, just to be clear, in terms of the payment balances. And what we plan to do is share the payment deferral balance going forward on each quarterly update. We think it's important to be transparent and give you guys a sense of how the portfolio is developing. That's on, I think, the first question, asset quality.

The second one, you asked about Corporates and Public sector. What we've tried to do here, Pawel, is be incredibly transparent as to where we see exposures that are more challenging. We listed the different sectors that we think are more high-risk from oil and gas to shipping to retailers to hotels and airlines. The total balance of € 91 million, 1/3 of that is actually under non-performing loans. The oil and gas risk that we provisioned in the first quarter, actually is an incremental provision on existing exposure that we had provisions on from before. We feel pretty good. I mean, as good as we can feel, given just the de minimis exposure that we have to these high-risk sectors. But this is one where you asked about how do we manage. We try to proactively contact the customers. And this isn't something that just started during the COVID-19 crisis. We've been managing these positions for some time. And I think we will benefit in large part because of the discipline in prior years. We've always said, I think you remember this, it's been a pretty challenging corporate lending environment, given that we thought there was an imbalance in terms of risk reward.

Hopefully, at least from this, we'll see a little more discipline enter the marketplace. But I think, the best thing that we can do from a portfolio monitoring standpoint is just be proactive and how we're managing customer exposures as well as reaching out to customers.

You had a question about payment holidays. It's been pretty de minimis on the corporate side, but that's something that we could probably provide in future calls. And then on the asset backed lending, we feel good about the overall portfolio. We try to highlight the one area we say that's more high risk, which is direct exposure to retailers and hotels. But even that, from a portfolio standpoint, we feel we're actively managing that well, and we'll obviously give updates in the coming quarters.

And then lastly, on the cost. When Enver went through the outlook for total 5% reduction versus 2019, that's in large part driven by measures that we put in place during the course of 2019 in the first 2 months of this year. As far as active reduction in FTE, we're sensitive to the environment, and we've put a pause in terms of restructurings. Although just to remind everyone, our restructurings have always been on a voluntary basis, as we work closely with the workers' council, and we have a social plan in place. But we're sensitive to what's going on in the market. I think more importantly, Enver mentioned that we're thinking about what is Day 2 post COVID environment look like, given the success of the home office infrastructure and really thinking about our footprint and how we operate just as far as an organization, the home office as a model potentially to use going forward, across different divisions. And I think that will be some good lessons learned, but it's still early. But without a doubt, we're going to take some measures in that respect. I hope that answers your questions Pawel.

Pawel Dziedzic: Yes thank you very much, it was very clear. Thank you.

Operator: Thank you, your next question comes from the line of Mate Nemes from UBS. Please ask your question.

Mate Nemes: Good morning and thanks for the presentation. I have a few questions, please. First is still on provisions and risk costs. I was wondering if you could confirm that the IFRS 9 macro adjustment, whether this is a complete one-off for now? And also that you are in a position to provide perhaps some sensitivities here. I think this € 14 million provision charge is based on the current IMF forecast at 6%, 7% GDP contraction in 2020 and 3%, 4% recovery in 2021. Can you comment on how this charge would look like should we go into perhaps a high single-digit or low teens type of recession scenario? That's the first question. Secondly, on net commission income. You have mentioned up to 15% decline is expected there. Can you discuss what are the underlying assumptions for this worst-case 15% scenario? And thirdly, more of a conceptual question, I guess, a general question. Can you discuss your initial experience with the state-guaranteed loans to SMEs and corporates? Can you talk about how much have you disbursed so far? And what is your expectation going forward? And how easy this is in terms of processing and application and so on, that would be very helpful.

Anas Abuzaakouk: Yes. Thanks, Mate. I hope you're doing well. Enver, if you can answer the question on IFRS 9 as well as the NCI assumptions, and I'll pick up with, just our initial experience.

Enver Sirucic: Sure. So Mate, on the IFRS 9 macro, you're right. This is already considering the macro piece. But just to be clear, for the Retail & SME part we apply the IMF forecast, not on the Corporates where we do individual assessments. The sensitivity is quite low, so if you would go to high single-digit numbers, the impact would not change. Obviously, we don't know what the forecast will be at the end that will be applied from the ECB. This is what then will feed into the numbers later in Q2.

On the NCI, the minus 15% was basically from the assumption, that there are two things that are impacted. One is the advisory business, where we have physical customer contact. The other is just foot traffic in the branches that also creates NCI. These are obviously impacted by the lockdown, even though all our branches are open. Our expectation is that we will suffer a stress in Q2 and Q3 and kind of going slightly back to normal in Q4. This is the assumption behind the 15%.

Anas Abuzaakouk: And then, Mate, the last piece with regards to just our initial experience. The most important thing over the past, I think 6 weeks what we've tried to do across the organization is to mobilize, be it the sales force, our collections team, our inbound or outbound call centers, our technology group, doing everything we can to make sure that we serve as a conduit or transmission mechanism to the customers, given the vast amount of stimulus programs that have been communicated, be it in Austria or Germany or other countries. I think the biggest role that we can play today is that conduit. So what we've tried to do is educate customers as to what the nature of the stimulus programs are, what the eligibility requirements are in terms of the application. And then service that conduit.

I should mention, though, from an SME standpoint, we have a pretty small -- I think we have the smallest percentage of SME exposure across the large Austrian banks. It's under 10% for our Retail & SME. So we're not, we just historically haven't been a big SME exposure, so we obviously haven't had the volumes in terms of disbursements. But we've tried to play a role as being a conduit and educating customers as to what's available. And I think the most important thing that we can do at this moment is to serve as that transmission function. I hope that answers your question.

Mate Nemes: It does. Thank you.

Anas Abuzaakouk: Thanks Mate.

Operator: Thank you. Your next question comes from the line of Giulia Miotto from Morgan Stanley. Please ask your question.

Giulia Aurora Miotto: Good morning. Can you hear me?

Anas Abuzaakouk: Yes, hi Giulia.

Giulia Aurora Miotto: OK fantastic. Hi, good morning.

Anas Abuzaakouk: Welcome back.

Giulia Aurora Miotto: Oh thank you, thank you. I have 2 questions, one on capital and one on revenues. So on capital, at every quarter, we discussed the M&A pipeline, and I think you mentioned for the full year results that you were exclusive on a number of transactions. Does the current environment change your thinking there? So can we assume that everything is on hold? Or perhaps do you see some opportunities opening up because of the current environment? So that's the first question. Then the second question, so NII, you guided for it to be stable, I assume, versus 2019 or is that the quarterly level? This is just a small technical question. And then more generically, why are you confident that NII will be stable? Because for example I would assume there would be a material slowdown in loan-growth. I don't see why people would be asking for mortgages or, you know, in this current environment. So if you can provide an update on how you are thinking NII is stable. Thank you.

Anas Abuzaakouk: Thanks Giulia. I'll take the capital question and Enver, if you can take the NII question that would be great. As far as capital, with regards to M&A, we actually had a few deals in the pipeline that we communicated at our year-end results. Given the current environment, we made a decision to put things on hold. The reality is, to be able to assess credit risk in this environment is incredibly difficult and we didn't want to try to re-trade on any commitments that we had made as far as valuation. So what we said is we will put it on pause and re-look at things in a more normalized environment, for the deals that we're looking at. And more broadly speaking, your question around M&A. Absolutely, this in no way restricts us from M&A but the reality is the hurdle or the thresholds to be able to get comfortable with a business, in particular obviously, the credit book, is much, much higher. So we will have to look at the world through a different lens and make sure that we're comfortable with the overall credit book if there is any potential M&A. But this in no way detracts us from looking at potential deals. I don't think you'll see anything anytime soon, just given the nature of events and kind of, the crisis mode that a lot of banks are working under. But it in no way detracts us from looking at deals, so we're still interested but I think we also have to act out of an abundance of caution to make sure that we understand what we're buying. And Enver, if you can take the NII?

Enver Sirucic: Yes. So Giulia, I think on the NII. The first question, refers probably to both. So to full year 2019 and the Q1 2020 where Q1 was still very normal in terms of NII. And both shows an average € 220 million per quarter, so it doesn't really make a difference what the starting point would be. Why we feel comfortable, I think it's really two-fold, but the biggest reason is that we have grown our balance sheet by 2% and mainly in loans and in securities, which gives us a nice uplift in interest-bearing assets for the rest of the year. Yes, we assume there will be less activity in new business lending that's already factored in the guidance with stable NII. And the other element that we assume will be, could be a positive actually, is the improving 3-month Euribor. We show the sensitivity so it's 10 basis points improvement leads to roughly € 1 million per month better NII. If you look at the 3 months EURIBOR, we have seen the 3 months EURIBOR going below 20 basis points negative right now.

Giulia Aurora Miotto: Got it, thank you.

Anas Abuzaakouk: Thanks Giulia.

Operator: Thank you. Your next question comes from the line of Gabor Kemeny from Autonomous Research. Please ask your question.

Gabor Kemeny: Hi, this is Gabor. Thanks for being upfront about the business risks. Firstly, on the net interest income. Can you break out how much additional revenues do you assume from the new securities investments from deploying some of your excess liquidity into higher-yielding securities? And then coming back to the corporate and CRE book. You didn't seem to take any portfolio-based provisions in the first quarter. Now going into the second quarter, is there a scenario, a macro scenario, where you think you might need to do some portfolio-based provisioning on the Corporate & Asset-backed loan book? And then finally on the Austrian debt moratorium. Can you remind us whether you now assume 3-month tenure, 3-month duration for this moratorium, or 6-month and what would be the provision impact of extending the loan guarantees by 3 months. Thank you.

Anas Abuzaakouk: Thanks Gabor. So Enver, if you can take the NII and the moratorium and then I'll answer the Corporates & Public sector portfolio.

Enver Sirucic: Sure. So NII, Gabor we don't disclose the specifics on the NII. This is all baked into the guidance that we are giving. Overall, the NII will be stable, offsetting, as I said, the lower new business with the higher securities balance and higher loan balances versus Q1. And on the Austrian debt moratorium, the extension, so the moratorium is defined as 3+3 months, so it can be extended to 6 months. It has no impact on the provision level. What will drive the provision level is if the number, the absolute volume of payment deferrals continues to go up, but the extension itself is technically not an impact.

Anas Abuzaakouk: Thanks, Enver. Gabor, in terms of the Corporates & Public sector, Enver mentioned earlier, so we took a macroeconomic assumption for the Retail & SME, on a portfolio basis. We didn't do that for the Corporates & Public sector because we are managing it on more of an idiosyncratic basis. So we know the individual corporate names, we know the individual real estate names and we'll take provisions accordingly. I think I highlighted some of the cyclical exposures, the cyclical sectors that we have exposures to. We're going to be acting out of an abundance of caution and prudence. Both on that side and anything, any development on the asset-backed lending portfolio, we will do it more on a loan-specific basis.

Gabor Kemeny: Thank you.

Operator: Thank you, your next question comes from the line of Johannes Thormann from HSBC. Please ask your question.

Johannes Thormann: Good morning everybody, Johannes Thormann from HSBC. Two follow-ups, please. First of all, on the sustainability of your cost savings now in this year, should we expect like everybody is hoping for a V-shaped recovery of the economy, that the travel and other admin expenses, which are going down and probably lead to this 5% cut will jump up in the next year again? Or can you see a more sustainable level there? And secondly, for me, help me understanding your 15% drop in net commission income. You secure this business, which might be impacted, yes. That's just a tiny part. And why should the payments business, which is the largest chunk of your fee income be so heavily impacted? Thank you

Anas Abuzaakouk: Thanks, Johannes. Enver, do you want to go ahead and take the questions?

Enver Sirucic: Yes, of course. So I think you're right, absolutely right. So we will have a benefit of lower expense for travel and other G&A. It's not a huge part. And it's too early probably to already give guidance for '21. But yes, I think if you followed us for the last couple of years, I don't think there was a single year where we had higher OpEx the year following the prior year. So I think we are very positive that the OpEx in the long-term will be sustainably down. And on the second one on the NCI. Yes, it sounds like a high number, but I think the opposite. 85% of our NCI does not have an impact, which actually reflects the high portion of the payments in credit account business. When I said payments, it's not the payments that you know just from current accounts, it's just the foot traffic where people still do OTC transactions, which is still roughly, what, 9%, I think, of our overall transaction, that drives NCI, and that is basically now down. I mean you basically have to assume no one really is going to the branches. You have a very low number of customers. And the combination of these two led us to the assumption that the overall impact will be up to 15% for the full year.

Johannes Thormann: Ok understood, thank you.

Operator: Thank you and your next question comes from the line of Stefan Maxian from RCB. Please ask your question.

Stefan Maxian: Yes hello, two or three questions. First, with regard, it's a number-question on your loan book in Retail and SME. Compared to the fourth quarter, I think you have changed a little bit the outline of household loans and the switching from portfolio loans into household loans, if you could just say what that is? And then on capital, I mean, you don't give a capital guidance anymore in the presentation. I mean, in Q4, we still had the 13% correct for CET1? So what's your thoughts right now on this number? And based on that, would you expect -- because so far, you said you didn't have any risk-weighted assets updrift from model recalibrations or anything like this. What do you expect in this respect? And secondly, in the call in the morning, you said the OCI effect has partly reversed already now in the second quarter. If you could comment on that again. Thank you.

Anas Abuzaakouk: Thanks, Stefan. Enver, do you want to go ahead and take the questions?

Enver Sirucic: Yes, sure. So on the portfolio, what we did, we just carved out the Swiss franc mortgages, which was organic business that we discontinued, we moved that into housing loans. And then small changes from some leasing portfolios and credit cards that we moved in the unsecured piece. But we changed it consistently as well. On the second one, 13% CET1, we have not made any changes to yet, but obviously, it will have an impact to change P2R composition. That is now basically moving 88 basis points out of CET1 and AT1/Tier 2. That will be reflected going forward in our considerations, talking about the 13% target. On the RWA, I think it's too early. It will take time. It really flows through the machines and the models and also consider that less than 50% of our portfolio is under IRB, so we have just less impact of any model-driven RWA increases. That's why I would say it's too early to actually say something about it. And you're absolutely right. We have seen widening of credit spreads in the first quarter. It's firstly March, that was minus 50on our CET1, but almost everything reversed. In the first couple of weeks of April. And we are giving, I think, that is as of April 24. So actually, end of day, as a Friday, 40of the 50came back, which means net impact is only 10in the capital.

Stefan Maxian: Alright, thank you.

Operator: Thank you. And your last question comes from the line of Simon Nellis from Citi Bank. Please ask your question.

Simon Nellis: Thanks very much. My question would be just about the expectation for NPL and NPE progression. I know you said that you can't really give much guidance, but just wondering what you're thinking in terms -- because it seems that your provisioning seems very precautionary. Your NPL ratio actually went down quarter-on-quarter. So when do you actually think you'll see NPL’s rise and if you have any view on the magnitude and what the impacts of all the fiscal stimulus and moratoriums and all that? Is that just going to kind of, I guess, lead to maybe peak NPL’s coming maybe even next year rather than this year? Thanks.

Anas Abuzaakouk: Thanks, Simon. Good question. I would tell you on the Retail & SME, that's where we're acting out of -- we're proactively being cautious and prudent because of the forbearance that's in place in the migration. And the reality is it's going to take -- I mentioned it earlier in the presentation, the severity of the economic downturn. But there's a ton of stimulus that's out there. Understanding the short-term demand shock, whether that's 1, 2, 3 quarters and then really understanding the Day 2 impact, which is, what does that mean in terms of unemployment? What are the structural changes to the economy? What do growth rates look like? I don't think anybody can accurately or reliably provide a forecast. What we're trying to do is acknowledge the fact that when somebody asks for a payment holiday or the deferral balance that we highlighted, the 4%, the reality is not all of those customers will be back to performing customers, given the changing economic situation. And we're trying to proactively address those provisions, irrespective of the migration of non-performing loans because, obviously, they'll be non-performing when they're 90 days past due. But we don't have that visibility in terms of 90 days or 180 days. What we do know though today is that we want to be cautious and prudent, and we'll provision for that. So that's on the retail and SME. The Corporates and Public sector is more idiosyncratic. So if we do have a payment default, that'll be one where we'll see the migration in terms of non-performing loans. And we mentioned that on the corporate side, there's € 90 million, I'd call it, high-risk sectors or exposures across the portfolio. Of that, 1/3 is already a non-performing loan, and you could potentially see some of those names go into NPL as well. So I think that will be more specific, more real-time as opposed to on the Retail & SME, it's more of a portfolio approach. But we're trying to address that both through the general reserve in terms of the macroeconomic assumption, and we can adjust that even further, as well as trying to put a provision against the payment deferrals proactively, knowing that this is going to be something that, in due course, will eventually evolve into a non-paying customer. I hope that helps.

Simon Nellis: That's helpful. I mean, I guess, on a related question, what's actually happened to your Stage 2 loans? Have you increased those significantly over the quarter? Just to kind of get an idea of what you're thinking in terms of riskier exposures progression?

Anas Abuzaakouk: Enver, do you want to take just the IFRS 9, just how we're going on that?

Enver Sirucic: Yes, we have just normal migration into stage 2, but not yet really a significant impact from COVID. I think this is too early. This will then happen over the next quarters. Part of it is already kind of reflected in the assumptions that we did in Retail where the migrations have not happened as we expect them to happen. And then on Corporate, I think it's too early. It will take time. It's going to be probably more a Q2, 3, 4 event.

Simon Nellis: Okay. And then just one last somewhat related question as well. I mean you mentioned that you're trying to be a conduit of credit, I guess, using state guarantee programs to companies. Can you give us an idea of how much credit you've actually extended under those programs? And maybe you could also just give us a brief summary of how they work, the technicalities?

Anas Abuzaakouk: Enver, do you want to take that?

Enver Sirucic: Yes. So in total, right now, the overall balance that we extended is slightly above € 30 million that we provided. Which, just also to put it in context, our SME, which is the biggest part of the guaranteed programs, is a very small number. So we are not a real relevant player in the SME market in Austria. How it works? There are different programs. So it goes from 80% now with the new guarantee program to up to 100%. Different cut-outs, different thresholds in terms of volumes. And there are different guarantee institutions established in Austria where you could apply. So there is a specific guarantee program, for example, for hotels and tourism. We are almost not using that because we don't have an exposure. There's a general one that is called the AWS program where you can handle most of these. So different institutions handling based on different sets of rules. And it is a collaboration between the bank, the customer and this institution, and we follow the guidelines given by the government, and that's how it gets processed. Now, everyone is trying to accelerate that process, and now I think the idea is to actually hit most of the new 100% guaranteed loans are processed within 24 to 48 hours.

Simon Nellis: And just the terms -- in terms of the credit, you rather fixed rates on them? What's the economics, I guess?

Enver Sirucic: So it's interest free, the 100% guarantee is interest free, basically. And then it moves to floating, and I think it goes up to 75 basis points because you basically have Republic of Austria risk. On the other one, it's a mix to apply your margin on the guaranteed part, it is based on interest free. So it's a mixed product.

Simon Nellis: Ok, thank you.

Operator: Thank you, there are no further questions at this time. Back to you, Anas.

Anas Abuzaakouk: Thank you, everyone, for joining the call. Sorry for this one going a little over but I know there was a lot of questions and we wanted to make sure that we address all the questions from across the analyst group. We look forward to talking to you guys in the second quarter and providing you with further updates. Thanks, everyone. Take care and stay safe. All the best.