

## **Absa FY19 speaker notes**

### **Daniel Mminele – Chief Executive**

Having been part of Absa for just under two months, today presents a good opportunity for me to share my initial impressions of the group with you, and to comment on our 2019 results before Jason unpacks our financials.

I spent a significant part of the last two months on a “listening tour” to familiarise myself with our business. This entailed introductory sessions with my group executive committee and their teams, connecting with board members, meeting some key clients, and engaging with some large shareholders and some of our regulators. As part of launching the Absa brand, I also had an opportunity to get a sense of operations in two of our largest markets outside South Africa – Ghana and Kenya, and I visited a number of our branches in South Africa and Ghana.

### **Initial impressions of Absa**

My impressions of the organisation are starting to take shape, giving me an appreciation of the key drivers of the business, and where our opportunities and challenges lie.

My sense is that Absa has great potential based on its product range, from universal banking to bancassurance, with solid businesses, a substantial customer base, and backed by both a strong, refreshed brand and talented, committed people.

I also believe that the execution and change management capability we have gained through the Separation can be leveraged to accelerate the execution of our other strategic priorities.

I believe that this will help us to continue to regain our rightful place in the South African market in terms of market share and earnings. Our pan-African ambition will allow us to take full advantage of the opportunities that exist on the continent and to further diversify our earnings, while making a meaningful contribution to Africa’s growth and development.

To achieve this, we will have to transform our culture, be consistent and agile in our execution, and harness digital technologies such that we can leverage our strengths to better serve our customers, and add value to our other stakeholders, including shareholders.

Allow me to comment on Absa's strategy, as I am aware that there have been questions around whether I buy into the current strategy, or whether I want to change it, or even whether I have the space to make any changes.

An important part of the conversations I had with the Board prior to joining Absa, involved the future direction of the Group, including its strategy. I was taken through the process of how it was developed, and how data and evidenced-based it was. It is my understanding that it involved a thorough analysis of the operating environment and megatrends, and was co-created involving all levels of the organisation.

I am comfortable with the strategic choices that Absa has made and believe they match our growth ambition.

Having said that, in a fast-changing environment we need to ensure that we remain relevant, and we must be prepared to refine our strategy accordingly. It has been almost two years since we began implementing our strategy, and we are now in a position to evaluate whether we are seeing the desired outcomes.

In this regard, I have a full mandate to review our strategy and its execution and to make changes where necessary.

### **We aspire to be a globally respected African organisation**

The key elements of our strategy entail:

- Restructuring the group to truly focus on customers,
- Driving growth and regaining lost market share,
- Leveraging digital and innovation,
- Transforming our culture,
- Being an active force for good in society, and
- Reinforcing our pan-African ambition.

These strategic choices translated into the selection of three Strategic Focus Areas, which are supported by three Enablers to ensure that our strategy supports a holistic transformation of the business.

### **Reflecting on our FY19 performance**

Turning to the business of the day, let me give you my high-level assessment of our business performance in 2019, before I hand over to Jason to delve into the financials.

Overall, we have made progress, and the steady strategic momentum yielded a resilient performance, achieved against a challenging macroeconomic backdrop.

South Africa's GDP growth has consistently disappointed for the past 5 years, averaging just 0.8%, well below the 3.5% global GDP growth over the same period. GDP per capita has also regressed as population growth outstripped GDP and income growth rates. Last year, the weakness was evident across most sectors, but particularly pronounced in energy, construction, transport, retail and communication.

The worse than expected decline in fourth quarter GDP growth, renewed load shedding, a deteriorating fiscal position and heightened uncertainty around global economic developments on account of the coronavirus outbreak, all point to significant downside risks to growth forecasts.

Economic developments in our other markets have been mixed, with some countries doing better than others. Our planning assumptions had higher GDP growth in eight of our ten markets, particularly in Mozambique and Zambia. Ghana, our largest market outside SA by earnings, was an exception, with strong growth of 7%. A key issue that will require careful monitoring will be rising debt levels and increasing external vulnerability, which could undermine prospects and heighten country risk.

Our balance sheet, revenue and earnings growth were all in line with peers after lagging for a number of years. However, the second half was tough for the industry. Positively, we maintained our balance sheet momentum, with gross loans and deposits growing by 9% and 12% respectively. The growth was broad-based across most businesses and Jason will elaborate further on this.

While our net interest margin declined by 14 basis points, it stabilised in the second half. Non-interest income grew by 4%, and there is still significant scope to grow our transactional revenue.

Managing costs while continuing to invest is crucial in a low-growth environment, and underlying costs grew by just 2% in constant currency. This supported a 5% growth in pre-provision profits, which improved from 1% in 2018. Although our credit loss ratio increased to 80 basis points from 73, it remains at the bottom end of our through-the-cycle target range.

With the tough operating environment and muted outlook in mind, we have maintained solid capital levels, with an 11.8% CET1 ratio, strong liquidity and prudent credit provisions. Our return on equity declined to 15.8% from 16.8%, which is indicative of the challenging operating environment.

### **Restore leadership in our core businesses**

In Retail and Business Banking South Africa, the underlying momentum continues to show signs of a turnaround. We have gained market share in retail deposits and retail loans and advances, including personal loans, new home loans and vehicle finance.

Our customer numbers grew by 1% to 9.7m, and the number of products per customer is growing, supported by improved customer service metrics.

In the third quarter of last year, we combined the wealth and insurance business with our RBB business in SA, creating an integrated bancassurance delivery model that is already yielding positive results. For example, Absa Life was voted #1 in the industry for service according to the South Africa Customer Service Index.

In Corporate and Investment Banking, client franchise revenues showed positive signs of growth in a challenging environment, and the client experience metrics are tracking positively. Our expertise has been acknowledged by numerous awards, including being named the best Investment Bank in Africa in the African Banker Awards, and the leading provider of Cash Management products and services by Euromoney.

We made progress towards building a global coverage model that is responsive to the needs of our clients. In 2019, we received approval from the US authorities to open our representative office in New York, and we signed a major collaboration agreement with Société General, which enables us to deliver a joint value proposition across 27 African markets.

Despite the challenges of managing a demanding separation programme, our Africa Regional Operations delivered double-digit earnings growth, after a strong second half. The primary customer base and number of products held per customer in our retail and business banking portfolio improved, and our corporate and investment banking earnings grew by 15%.

### **Digital innovation**

Digital adoption across our estate has improved meaningfully. In RBB SA, our active app users increased by 24%, and our banking app was rated #1 by customers on both iOS and Android in South Africa.

We introduced a digital fraud warranty – the first of its kind in the South African market - that protects our customers in the event of digital fraud.

We are leveraging robotics and artificial intelligence to automate our processes end to end. This has significantly reduced the processing and turnaround times in our business, notably in Vehicle and Asset Finance and in our call centres.

And we continue to leverage strategic partnerships across our digital estate to deepen market reach and to create new revenue streams. In partnership with Jumo and MTN, we launched a mobile lending and savings proposition in Ghana and Zambia.

Timiza, the virtual banking proposition in Kenya launched only two years ago, has seen a 35% growth in loan disbursements, and an 8-fold increase in repeat borrowing customers, driving a revenue growth of 70%.

From my various engagements across the organisation thus far, it is encouraging to find that our people are supportive of our strategy, and want to see further transformation of our business to meet our customer needs.

I will now hand you over to Jason for more detail on our financials, after which I will make some concluding remarks, before we take your questions.

## **Jason Quinn – Financial Director**

Thank you Daniel and good morning everybody.

As usual, I will cover our performance for the year and then update you on the finalisation of our separation from Barclays, before providing our guidance for 2020 and the medium-term.

### **Key FY19 takeaways**

Before getting into the details, I want to pull out the key aspects of our 2019 performance.

Firstly, as Daniel highlighted, the macro economic backdrop has been tougher than expected. That has been very evident in the current reporting season for SA corporates and particularly in the events of the last few days. The macro outlook is still weighted towards downside risk.

Second, looking at our P&L, I am pleased that our net interest margin stabilized in the second half. Most of the margin compression over the past two years came from adopting IFRS 9 and pressure on the funding side as our loan growth improved. Our structural hedge has provided us with some protection against falling rates, which will remain a feature near-term.

Third, as you would expect given the tough macros and the subdued environment for revenue, we continue to control costs well. Excluding one-off items and incremental runs costs from separating from Barclays, our underlying cost growth was sub-inflationary, although we continued to invest for growth.

Looking at our businesses, RBB SA showed improving operational momentum, as we delivered on our commitment to catch up with market growth. Meanwhile, our Regional Operations again underpinned group growth and returns, highlighting the diversity it provides.

It is pleasing that our separation is now largely complete with less than three months to go and we remain on track and within budget. As Daniel mentioned, we have used separation as a catalyst to “reset” our group, and we aim to deploy the core change skills we have developed during the process elsewhere.

Lastly, given the market volatility and uncertainty, we have focused on increasing coverage, and maintaining solid capital and liquidity levels, which I will cover a bit later. We built provisions with IFRS 9 last year and its day one provisions are earlier, so there is new business strain. These are good things in this environment. We also proactively reduced approval levels in some areas at the end of the year. We are more actively managing our capital, while improved deposit growth strengthened our funding.

### **Resilient normalised salient features**

Moving to our salient features, we continue to normalize our results while we separate from Barclays, as it better reflects our underlying performance. I talk to our normalised financials throughout the presentation and we reconcile our normalised and reported IFRS results in our booklet.

Our diluted HEPS grew 1% and we increased our dividend per share in line with this, putting us on a dividend yield of 9.3%.

Our NAV per share grew 5% to R126, putting us on a historical price to book of below 1.

Given 8% growth in our average equity and only 1% earnings growth, our return on equity declined to 15.8%, from 16.8%.

This reduced our PARCC, or profit after regulatory capital charge, for the period by 30% to R2.1bn.

As expected, our net interest margin declined year on year, mostly on the funding and endowment side, although I was pleased to see our margin stabilizing in the second half.

Our operating JAWS were slightly negative, increasing our cost to income ratio marginally to 58%, although our pre-provision profit grew 5% to almost R34bn.

New business strain and improved coverage increased our credit loss ratio to 80 basis points, dampening our pre-provision growth.

## **Income statement broadly in line with guided**

Looking at our income statement, its shape was again broadly as we guided.

Currency translation effects only had a very small positive impact on our 2019 group performance.

Revenue growth improved to 6%, or 5% in constant currency, due to 7% higher net interest income and 4% growth in non-interest income. This was despite prior year WIMI disposals reducing revenue by R300m and a R350m revenue drag from implementing IFRS 16.

Operating expenses were again very well controlled, increasing by 6% or 5% in constant currency, with low single digit underlying growth, which I will unpack further in a later slide.

Credit impairments grew 24% off a low base and remain at the low end of our through-the-cycle credit loss ratio guidance range.

The effective tax rate decreased to 26% from 28%, which we believe is a more sustainable level.

The 31% rise in non-controlling interest was largely due to raising over R3bn of additional tier 1 capital.

Normalised headline earnings grew 1% to R16.3bn.

The normalisation items are shown on the right. Separation-related operating expenses of R2.4bn was the largest item, although this was 24% lower than in 2018, as services from Barclays were terminated on or ahead of schedule and expenses related to the planning phase reduced on completion of those initiatives.

At a headline earnings level, we added back R1.7bn, slightly less than last year's R2.0bn, with our IFRS reported headline earnings rising 3%.

## **Loan growth momentum maintained ...**

Balance sheet momentum continued, with gross loans up 9% to R947bn, or 7% excluding reverse repos.

Growth was evident across most of our businesses.



RBB SA, our largest book, grew 7%, or 9% adjusting for the disposal of the Edcon storecard portfolio, an improvement from last year's 6% growth.

CIB SA's gross loans increased 9% to R300bn, with strong 34% growth in commercial property finance off a relatively low base. Gross loans rose 4% excluding reverse repos, with term loans up 2%.

ARO's gross loans increased 15%, with CIB up 21% and RBB 9%.

Looking at RBB's loan growth in SA on the right hand side, our key products all achieved good growth.

Importantly, Home Loans' overall market share has now stabilized for the first time in several years.

Vehicle and Asset Finance grew 9%, despite 3% lower new car sales last year.

Personal Loans grew 14%, due to strong production via branches and digital channels and targeted marketing campaigns, but remains very small in our overall portfolio.

Credit cards increased 18%, adjusting for the Edcon storecard portfolio, largely due to limit increases to existing high quality customers.

Lastly, Relationship Banking grew 12%, with double digit growth in commercial property finance, Agri, term loans and overdrafts. Commercial growth was strong, while growth in the SME segment slowed, given the tough macro backdrop.

We are pleased with the momentum within RBB SA lending, as well as the quality of new production, which is translating well into improved annuity revenues.

### **... as deposit growth also improved**

As you know, growing core deposits is one of our priorities and it's an important sign of improving franchise health.

Total deposits grew 12% year-on-year, or 11% excluding reverse repos, roughly double our 2018 growth. Adding R83bn in deposits, produced positive balance sheet JAWS.

Customer deposits increased to 75% of our total funding mix from 72%.

RBB SA grew 10% to R373bn or 46% of our total deposits, given 15% growth in low margin deposits, with fixed deposits up 15% and savings 11%, while current account deposits increased 4%.

Within RBB, our retail deposits rose 10% to R227bn, increasing our market share slightly to 22%.

Relationship Banking, rose 10% with growth in transactional and savings due to new products and growth in the public sector.

Deposits are also a key focus area for CIB SA and grew 19% or 9% on average, off a low base, with very strong growth in fixed deposits, reverse repos and notice deposits. Some of its growth is relatively volatile in nature, particularly reverse repos.

ARO's deposits increased 13%, or 19% in constant currency. RBB's deposits rose 11% in constant currency and CIB's 29%, due to improved products and platforms and greater focus on key clients.

Our proportion of long-term funding improved to a high of 28%, from 26% in 2018.

Our net stable funding ratio improved to 113%, from 110%, well above the regulatory requirement of 100% and our target range of 104% to 107%.

### **Funding and endowment reduce net interest margin**

As we guided, our net interest margin decreased, mostly due to lower funding margins. Our average interest bearing assets grew 10% to over R1tn and our net interest income grew 7%.

Our loan margins declined, with lower pricing primarily in Investment Bank SA and Relationship Banking, although front book margins continued to improve in Home Loans and Personal Loans. Mix-wise, slower growth in Home Loans than our overall book was positive, as was strong growth in Card and Personal Loans, partially offset by high CIB SA growth.

Our deposit margin narrowed by 13 basis points. Pricing was impacted by competition in Everyday and Relationship Banking. Increased reliance on wholesale funding and stronger growth in lower margin Everyday Banking deposits had an adverse mix impact.

We continue to hedge structural balances of about 13% of our South African capital and liabilities. Our structural hedge released R595m, or 6 basis points, to the income statement, which was in line with the previous period. The programme's cash flow hedging reserve was R1.1bn after tax at yearend.

Endowment on equity and liabilities after hedging had a 4 bps negative contribution reflecting the mix impact of slower growth in endowment balances relative to the Group's overall interest-bearing assets

Our hedge programme should provide us some protection, with the forward market currently pricing in two more 25 basis point rate cuts this year.

In ARO, lower interest rates in many of our markets and competitive pricing of foreign currency loans and deposits had a minimal impact on group margins.

In 'other', the negative impact of implementing IFRS16 reduced our margin by 3 basis points, although there was an equal reduction in costs. High quality liquid assets growing less than interest-bearing assets had a positive mix impact.

Margins were stable in the second half.

### **Core non-interest income growth emerging**

Balance sheet growth and a focus on growing our customer base and improving primacy is starting to translate into better non-interest income growth.

Our non-interest income increased 4% to almost R34bn or 42% of total revenue. It grew 6% excluding the fall in CIB net trading income.

Annuity income is a large component, as net fee and commission income accounted for 70% of the total after growing 5%, and I'm pleased RBB's customer numbers have stabilized.

Net trading excluding hedge accounting declined 4% and is a relatively small part of our overall non-interest income.

Net insurance premium income grew 9%, with solid growth in our Life business.

At a divisional level, RBB South Africa grew its non-interest income 6%, with 11% growth in merchant income, 9% higher Transactional and Deposit non-interest income and its Insurance Cluster up 7%.

CIB SA's non-interest income fell 18%, with the Investment Bank down 29% due to a poor trading performance in Markets, which I will cover in more detail later. This was partially offset by Corporate's 8% growth.

Our Regional Operations grew 17%, or 14% in constant currency. RBB ARO rose 13%, due to foreign exchange sales and trade income. CIB ARO increased 22%, with strong growth in global Markets off a low base.

### **Underlying cost growth well contained**

Our operating expenses grew 6%, or 5% in constant currency, to R46bn.

Our underlying cost growth was far better. 2019 included an additional R600m of incremental run costs due to separating from Barclays, plus R400m more of staff restructuring costs. Management actions reduced the potential incremental run costs by almost R600m. 'Other' includes a number of one-off items, including increased fraud losses in RBB, but also excludes the IFRS 16 implementation impact of R350m.

Excluding these items, our underlying cost growth was 3% or 2% in constant currency. This reflects successful targeted cost reductions of R3bn, including over R1.3bn in RBB SA, R750m in operations, R300m in CIB SA and over R200m in both ARO and our real estate portfolio. These are structural and sustainable reductions and we are planning to reduce a further R3bn from our cost base over the next 2 years.

Looking at the table, staff costs grew 7%, or 6% in constant currency, and remain the biggest component at 55% of the total.

Salaries grew 9%, or 8% in constant currency, with restructuring costs counting for half of this growth. Provision for bonuses decreased 6%. Our headcount in South Africa declined by 2500 colleagues YoY, or 8%.

Non-staff costs increased 5%, including 4% lower marketing, 5% higher professional fees and 3% growth in cash transportation costs.

IT costs grew 16%, due largely to higher post separation run costs and annual contract increases. Our total IT spend, including staff and depreciation, grew 18% to R9.3bn, which is 20% of group expenses.

The 54% higher depreciation and 42% lower property-related costs were due to adopting IFRS 16, which added R1.1bn in depreciation for right-of-use assets, with a corresponding decrease in property operating lease expenses. Our total property costs continued to benefit from optimizing our corporate and retail branch portfolios and grew by only 2% YoY.

Amortisation of intangible assets grew 35% due to an increase in software assets to R5bn.

Communication costs grew 7% reflecting higher market data costs in CIB after separating from Barclays.

Within 'other costs', travel and entertainment fell 17%, which was offset by higher fraud costs, due to implementing a new fraud model and increases in RBB.

Given the tough operating environment, you would expect us to continue to manage costs tightly. We see further structural cost saving opportunities in operations and technology, within ARO and RBB, while still reducing discretionary costs. The benefits from our restructuring over the past 18 months should become more evident this year, as our overall cost run rate continues to improve.

### **Unpacking the increase in our credit impairments**

Our credit impairments grew 24% to R7.8bn, off a low base. Given our charge was probably higher than the market expected, I'll spend more time than usual on our credit impairments today, starting by unpacking the increase.

To calculate the underlying growth we make three changes.

Firstly, we adjust 2018's base for the large CIB SA single name charge net of a recovery in ARO that occurred in 2018.

Second, given day one IFRS 9 provisions, new business strain increased our credit impairments, largely in Card and Personal Loans in SA, where loan growth was strong.

Next, our coverage increased, again primarily in SA Card and Personal Loans and also vehicle finance following IFRS 9 charges for increased macro-economic and industry risk factors.

After factoring in these items, the underlying increase in our credit impairments was closer to 8%, which is similar to our loan growth.

### **Credit loss ratio increased ...**

Our credit loss ratio increased to 80 basis points from 2018's low 73 basis points.

RBB SA's credit impairments grew 38%, resulting in a 118 basis point credit loss ratio. Although Home Loans' charge rose 61%, its remains low at just 8 basis points, a testament to the quality of the business we are writing. Over time, we think that the Home Loans credit loss ratio should range between 25 and 35 basis points.

Everyday Banking, the largest component, increased to 5.5%, which I have a separate slide on later. Vehicle and Asset Finance's charge declined slightly as improving early arrears and improved collections outweighed a weaker economic outlook.

Relationship Banking's credit loss ratio was stable, reflecting normalizing losses in commercial asset finance and pressure on SMEs, offset by recoveries in Wealth and commercial property finance.

CIB SA's credit impairments fell 63%, improving its credit loss ratio to 11 basis points. This was largely due to the non-recurrence of a single name charge in the comparative base, partially offset by book growth.

ARO's credit impairments rose 53% off a low base, particularly in CIB, increasing its loss ratio to 98 basis from 78.

### **... but remains relatively low**

Our group credit loss ratio of 80 basis point remains at the bottom end of the through-the-cycle annual charge we expect under IFRS 9 of 75 to 100 basis points.

RBB SA has now moved into the bottom end of its 110 to 155 basis points range.

CIB's overall charge of 14 basis points is below its through-the-cycle range of 20 to 30 basis points, which it exceeded slightly in 2018, when we had a significant single name charge.

Despite increasing noticeably, ARO's charge remains slightly below the 100 to 140 basis point range we expect for it, which suggests the potential for a further increase this year.

Lastly, our group stage 3 assets improved to 4.7% of total loans from 5.1% and we consider our 44% cover on this appropriate.

### **Capital levels remain strong**

Moving onto our capital base, our common equity tier 1 ratio remains strong within the context of our healthy loan growth.

Group risk-weighted assets grew 6% to R870bn, slightly less than our customer loan growth, consuming 90bps.

We remain very capital generative, as profits added almost 2% to our CET1 ratio year on year, while dividends reduced it by 1.1%.

Our resulting normalised CET1 ratio of 11.8% is at the top end of our Board target range.

Of course, our CET1 is stronger on a statutory basis, which includes another 30 basis points for what remains of the separation contribution from Barclays.

Our total normalised Group capital ratio of 15.5% is also at the top end of our target range, which we believe is appropriate, given the tough macro backdrop and heightened uncertainty.

We are also taking a more active approach to managing our balance sheet and capital. Disposing of the Edcon storecard portfolio was the first step, which releases R1bn in capital in the first quarter of 2020.

During the year we also issued over R3bn of new-style Basel III AT1 capital and R1.6bn of tier 2 capital and followed that through into this year where we raised R2.7bn of tier 2 capital last month.

We were the first African bank to conclude a deal with MIGA, guaranteeing \$497m of capital in seven ARO subsidiaries enabling us to grow lending, including to SMEs and projects with environmental benefits.

### **Lower SA returns outweighed improved ARO RoE**

Moving onto our divisional returns, our South African operations RoE declined.

RBB South Africa's return on regulatory capital decreased to 21%, which remains attractive.

Meanwhile, given its poor Markets trading performance, CIB South Africa's return on regulatory capital declined to 13.3%. Our total CIB return on regulatory capital is stronger at 18%, from 21% in 2018.

ARO's RoE improved slightly to 19% and remains well above the 13% when we acquired it six years ago.

### **Continue to benefit from a diversified portfolio**

Our earnings remain reasonably diversified by product, activity and geography.

RBB South Africa, which includes the Insurance Cluster, declined 2%, but still contributed 58% of our earnings. Excluding the non-core Edcon storecard portfolio, which has been sold, its earnings were flat.

CIB South Africa's earnings decreased 6% due to its negative JAWS on the back of lower Markets trading revenues.

On a total view, however, CIB's earnings grew 3%, or 1% in constant currency, and accounted for over a third of group earnings.



After a strong second half, ARO's earnings increased 16%, or 12% in constant currency, to account for almost a quarter of group earnings, from 13% in 2013.

### **Solid pre-provision profit growth despite CIB SA**

It was pleasing to grow the group's pre-provision profits by 5%, well ahead of last year's 1% increase.

RBB SA's positive JAWS produced 7% higher pre-provision profits, given its improved topline growth and strong cost containment.

CIB SA's pre-provision profits fell 15%, again due to its lower Markets trading revenue.

ARO's pre-provision profits grew strongly, driven by its 14% revenue growth.

### **RBB SA earnings grew excluding Everyday Banking ...**

Now let's have a look at RBB, our largest business. We are broadly in line with the commitments made at the RBB investor day in December 2018 and while RBB's restructuring is complete, it is still in a "fixing" stage until the end of this year. We are seeing the benefits of continuity of management and in the successful execution of plans, integrating bancassurance, fixing its loans and deposits value propositions and improving its sales and collections capabilities.

Home Loans accounts for 27% of our gross loans excluding reverse repos and 15% of RBB SA's earnings. Its earnings grew 1%, as credit impairments increased materially off a low base to offset positive operating JAWS.

Vehicle and Asset Finance grew earnings 41%, due to positive JAWS on 7% net interest income growth and 1% cost growth. There is further scope to improve VAF's cost to income ratio and returns.

Within the Insurance Cluster, Life Insurance earnings grew 11% to almost R1bn, as it benefited from integration with RBB, which increased branch sales by 17% and saw new business volumes exceed 114,000 a month in the second half. Net premium income growth of 11% offset increased retrenchment

and disability claims. Short-term insurance earnings rose 6%, given 7% net premium growth and a 6% underwriting margin, in part due to the absence of significant catastrophe events.

Relationship Banking includes Business Banking, card acquiring, commercial asset finance, Private Banking, Wealth and Financial Advisory. Its earnings grew 7% to R3.7bn, as pre-provision profits increased 6%, largely due to cost containment. It also achieved double digit loan and deposit growth. Its customer base grew for the first time in many years. Relationship Banking is our largest divisional business unit, accounting for 22% of group earnings.

Everyday Banking incorporates Transactional and Deposits, Personal Loans and Card issuing. Its earnings fell 13% to R3.5bn, as 50% higher credit impairments outweighed 9% pre-provision profit growth.

### **... as unsecured lending offset improving transactional**

Given its size, it's important to understand the components of Everyday Banking's earnings. For starters, Transactional and Deposits earnings increased 9%, given positive operating leverage and slightly lower credit impairments. I am pleased to report that we have stemmed customer attrition for the first time in years, with growth in target segments. Including our bancassurance customers, RBB SA's customers grew 1% to 9.7m, while primary customers are now stable at 3.1m. Also, we are starting to leverage our full product suite to improve our 2.3 products per customer.

Card and Personal Loans were the reason Everyday Banking earnings fell, although they produced 5% and 19% higher pre-provision profit growth respectively. Personal Loans, in particular, had strong 16% revenue growth. However, both had significantly higher credit impairments, which are also worth delving into.

### **Unpacking Card and Personal Loans credit charge ...**

Combining Card and Personal Loans credit impairments, the usual trend of seasonal improvement did not materialize in the second half. This was caused by management actions to build balance sheet coverage due to the weak macro backdrop and the new business strain under IFRS 9, as we grew our

production and increased card limits. You would have seen similar trends among our peers who reported recently.

New Business strain was responsible for most of the increase in credit impairments. We started growing our card receivables in late 2018, largely through limit increases to existing low risk clients. Under IFRS 9, moving into a growth environment the newer vintages increase provisions in the first two years before they 'season'.

In Personal Loans, where we started growing earlier, the seasoning of those vintages is now mostly behind us with credit losses at their expected peak levels. Together these contributed R800m to the charge in 2019.

Balance sheet coverage was further increased by R300m, given the softer macro environment in second half of the year.

On an underlying basis, our impairments for these products grew 17% which is aligned with the book growth.

Overall, we have provided appropriately for these books, which are both performing in line with our risk and return expectations.

### **... where we wrote high quality new business**

Credit bureau data shows that we are writing high quality new business in both Card and Personal Loans, as we have the highest proportion of low risk new business among the banks.

So we are not sacrificing quality to grow these books. As I explained, their increased credit impairments reflect new business strain under IFRS 9 and building increased coverage given the macro backdrop.

### **Retail loan production and pricing momentum continues**

Maintaining momentum in our loan production is an important part of our strategy to regain leadership in RBB SA.

Our loan production strategies generated above-market growth in retail lending, in a tough economy and compared to a higher base, because we started improving our loan production in some segments such as mortgages in the second half of 2017.

Home Loan registrations grew 24%, well above the market's 5% growth in registrations, improving our flow market share to 22% from 19%, as we focused on granting higher LTV loans to low risk customers. New business through mortgage originators increased 39%.

In vehicle finance, production improved in the second half, rising 11% for the year, well above the 3% lower new vehicle sales for the year. We strengthened our dealer relationships and improved our share in the used segment by 2%, in line with our strategy to be the 'bank to the dealer'.

Personal loan production grew 23%, largely through improved operational processes and lending to existing customers, without changing our risk appetite. In fact, in response to the macro environment, we constrained our approval rates towards the end of the year. There is further scope to increase our low market share here of just 11% on a product basis.

Credit card turnover grew 8%, largely due to increasing limits for existing customers. Our total card limits grew 17%.

Contrary to many opinions, our pricing has improved in key areas despite gaining share of new business in a subdued market. As you can see on the right, our new business pricing improved by 8 basis points in Home Loans and 74 in Personal Loans, while credit cards was flat. Pricing remains tight in Vehicle and Asset Finance, with increased competition in a weak market.

### **Prudent mortgage growth at the right price**

Although our strategy in recent years is to grant higher LTV mortgages to low risk customers, our LTVs remain relatively conservative versus peers. Our average LTV on new mortgages increased to 86% last year from 84%. As you can see, our market share of 100%+ mortgages is the lowest of the big 4 banks. In fact, peer 1 has two-thirds of industry LTVs over 100% if you include their home loans subsidiary.

The graph on the right shows how our mortgage pricing has improved noticeably in recent years, having lagged peers during the period when our new business LTVs were well below the market, which reduced

our pricing power. Last year our pricing was above most of our peers, although our share of low risk new business was the highest in the market.

### **Strong CIB ARO growth offsets lower SA earnings**

Moving onto CIB, we show all of its components, in line with how we run it on a Pan-African basis.

CIB's earnings grew 3%, or 1% in constant currency, to R5.9bn.

Including ARO improves CIB's return on regulatory capital to 18%, although this is down from 21% last year.

CIB's earnings in SA declined 6% to R3.2bn, as 4% lower revenue produced negative JAWS that outweighed 63% lower credit impairments off a high base.

Within this, SA Corporate earnings rose 2% to R1.2bn, largely due to 6% higher pre-provision profits given its 8% growth in non-interest revenue.

Investment Banking earnings fell 10% in SA to R2bn, as revenue fell 12%, outweighing a material decline in credit impairments off a high base.

We still see growth potential in target areas and aim to win primary relationships to increase our transactional revenue and deposits. Doing so should improve CIB's low returns in SA

CIB earnings in our Absa Regional Operations grew 15%, or 10% in constant currency, to R2.7bn or 46% of CIB's total. Pre-provision profits grew 12%, outweighing significantly higher credit impairments off a low base. Strong 22% non-interest revenue growth exceeded relatively high cost growth, as incremental run costs increased materially. CIB ARO's second half earnings were strong, growing 26% YoY.

ARO's Corporate earnings rose 8%, as pre-provision profit growth offset normalizing credit impairments. It is a large business now and is considerably larger than our SA business, having grown materially over the past 5 years.

ARO's IB earnings rebounded from a tough 2018, rising 37%, given strong 25% revenue growth, as we continue to build our client franchise and roll out more advanced infrastructure and remains a significant opportunity for us going forward.

### **CIB earnings mix well balanced**

CIB's earnings were evenly split last year.

In total, Corporate increased 5% to R3.2bn or 53% of CIB's earnings, while the Investment Bank was flat at R2.8bn.

ARO's 15% growth increased it to almost half of CIB's earnings, although we expect South Africa's contribution to rise this year, given the undemanding base.

### **CIB Markets performance diverged**

Given our underperformance here, I would like to explain the 10% drop in our overall Markets revenue.

The graph on the left provides the view of our SA trading operations that I showed in August. You can see that our client franchise remained resilient, as we maintained our share of a declining institutional market and largely retained our corporate revenue flow. Markets client facilitation risk was the swing factor, given a decline of R900m YoY.

Our SA Markets revenue declined 28%, with Fixed Income and Credit down 23% due to the non-recurrence of notable renewables trades in the base and adverse risk management and market illiquidity in 2019, while FX and commodities fell 7%. Equities and Prime Services dropped 65% due to lower client and market volumes globally and challenges in exiting client facilitation risk positions. We have now removed most of the risk from the portfolio and are more confident in our outlook for 2020, where we expect to do a better job of reducing the negative client facilitation risk. So far, Markets has had a strong start to the year in SA.

On the far right we show ARO's Markets revenue, which grew 25% off a relatively low base, as we gained market share in FX, due to improved cross selling, new client acquisition and products, and rolling out electronic platforms across our branch network.

The key takeaway is that CIB's core client franchise in South Africa remains healthy and that ARO's diversification benefit remains intact.

### **Africa Regions enhances our earnings growth and returns**

It is very evident from the graph on the left that Africa Regions has enhanced our earnings growth, particularly given South Africa's low growth for the past three years.

After a strong second half, Africa Regions' earnings grew 17% to almost R3.6bn, up 13% in constant currency. It accounted for 22% of our earnings and 24% of group revenue.

Its pre-provision profits grew 18%, which was partly offset by normalising credit impairments off a low base.

I covered CIB earlier, which accounts for 77% of its earnings. RBB's earnings grew 22%, as positive operating leverage offset higher credit impairments.

ARO's RoE has improved materially since we bought it in 2013, to around 19%.

We are cautious about ARO's earnings growth this year, as its credit impairments remain below through-the-cycle levels and its incremental run costs post separating from Barclays increase further.

Medium-term though, we see scope to grow our CIB franchise, where returns are attractive, and reduce RBB's high 70% cost to income ratio once we have concluded the separation.

## **Separation largely complete**

I am very pleased that our separation from Barclays is almost complete, with less than three months to go and only 3 key projects left, and remains on track. We have delivered another 49 projects and terminated 24 services contracted with Barclays since my August update.

At December, we had spent R11bn on separation execution and R2bn on Transitional Services Agreement costs. Our remaining budget of R4bn includes sufficient contingency to mitigate potential risks on the outstanding projects.

We have rebranded our ARO subsidiaries this year, which has progressed really well, reinvigorating those businesses. The largest remaining projects are CIB's cash management and FX trading platforms, which are on track.

## **2020 outlook and beyond**

I will finish with updating our 2020 guidance.

In South Africa, we expect 0.9% real GDP growth this year. However, the macro outlook is very uncertain, given local issues including our sovereign credit rating and power supply, plus global developments such as the impact of corona virus and most recently the contagion effects of price wars in the oil markets.

In our ARO markets, we see real GDP growth improving to 5.6% during 2020, given continued infrastructure investment, and improved mining output and agriculture, although there are downside risks to this.

Based on our current assumptions, and excluding any major unforeseen political, macroeconomic or regulatory developments, our guidance is as follows:

For 2020, we continue to forecast reasonably similar balance sheet growth. Loan growth could exceed deposit growth, particularly in CIB. We expect better loan growth from ARO in constant currency than from South Africa.



Although ARO had a very strong second half, I should caution though that incremental run costs and normalizing credit impairments are likely to dampen ARO's 2020 growth, but it still provides us with medium-term growth potential.

Our net interest margin is expected to be similar to 2019's 4.5%, given positive mix impacts from higher growth in retail unsecured lending and ARO, partially offset by growth in low margin deposits and slightly lower policy rates.

Costs will remain well controlled and we are targeting positive operating JAWS, in part due to non-recurring costs in the base.

Our credit loss ratio is expected to increase slightly, but remain in the bottom half of our through-the-cycle target range. There is increased risk of further strain in our South African portfolios.

Our RoE is likely to be similar to 2019 and our CET1 ratio should remain at the top end of our Board target range and we are comfortable with our dividend cover at current levels.

Looking further forward, over the medium-term, and within the context of a much tougher environment than we expected when we published medium-term guidance this time last year, we continue to expect to execute well against the strategic priorities that Daniel set out earlier.

We are on track to deliver the separation from Barclays in the next few months in a safe and capital and cash flow neutral manner.

Our revenue momentum should continue, with an appropriate and prudent approach to lending and a strong focus on customer primacy and transactional revenues across our business.

Our cost management and efficiency opportunities are being well executed, with further structural savings planned. We thus expect to steadily improve our cost to income ratio over the next few years.

We still believe that an RoE target of 18% to 20% is appropriate for our group, although we do not envisage achieving it until 2022 at the earliest, which is heavily dependent on the state of SA's economy.

Once again, given the tough global backdrop at the moment and ongoing macro uncertainty, we are very focused strong capital and liquidity management and appropriate balance sheet coverage.

Thanks very much for your attention, and I'll hand you back to Daniel.

### **Daniel Mminele – Chief Executive**

A few closing remarks from me before we take your questions on Slido.

These are challenging times indeed. Covid-19 is clearly having a huge impact on the global macro outlook, and we know that the global environment is key to our region's economic prospects. The risks we collectively face are substantial.

We will continue to drive the execution of our strategic objectives with speed and agility, and seek to lead our peers by managing risk more effectively, and take advantage of emerging opportunities as quickly as possible.

But we are very aware that leading with balance sheet in a tough environment has to be done at the right price and returns, with adequate risk and collections capabilities.

As a major banking group, we will be constructive in our engagements with clients and shareholders, diligent in our risk appetite, and supportive of business initiatives that can help improve the general outlook.

I am determined that we embed a culture and operating model that supports our ambition. We will continue to be a force for good, playing a shaping role in the communities and countries we serve. We are a founding signatory of the United Nations Principles for Responsible Banking, and will soon be publishing our group sustainability policy and a standard for financing coal projects.

It is a privilege to lead this organisation at this pivotal point in its evolution, and to harness the energy, determination and potential of our 38 000 colleagues to accelerate our business performance.

Thank you. We will now take your questions.