Addiko Bank

Addiko Group YE19 Results: Webcast Transcription

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Speakers:
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Operator	Dear ladies and gentlemen, welcome to the conference call of the management of Addiko Bank AG. At our customer's request, this conference will be recorded. As a reminder, all participants will be in a listen-only mode. After the presentation, there will be an opportunity to ask questions. If any conference call participant has difficulties during the conference, please press * followed by 0 on your telephone for operator assistance. May I now hand you over to the Addiko team, who will lead you through this conference. Please go ahead.
Razvan Munteanu	Hello. This is Razvan Munteanu I am the CEO of Addiko Bank and I welcome all the participants joining the Addiko Bank earnings call for the 2019 results. I'm joined on this call by Johannes Proksch, CFO, Edgar Flaggl, Head of Investor Relations, and as we are at the presentation for the YE19 results, I have Markus Krause and Csongor Nemeth from the Group Management Board sitting here with us for the Q&A session. During this call, we will inform you of our results in 2019, and the developments since our previous call. Johannes will provide details on financial results and key risk metrics for 2019. At the end, as usual, we'll open the floor to questions from the audience. Please go now to page number 4. In line with the results presented in quarter 3 and the publication of our preliminary results for 2019, we are very proud to complete 2019 delivering a 32% improvement of our adjusted result after tax of EUR 40.7 million. The adjustment includes positive and negative one-off effects, which we carefully assessed as being linked to the transformation and non-recurrent. They were carefully reviewed with auditors by Johannes and the team, Johannes can provide more details a little bit later in this call. The reported results after tax for 2019 is at EUR 35.1 million. We see this as a solid achievement, it's the third profitable year. This includes the negative effects from the Swiss Franc conversion law in Serbia and legal provisions in Croatia related to historic Swiss Franc loans. It also includes the costs of preparing and executing the IPO in July last year. The transitional CET1 is at 17.7%, this is including 2019 profit and the proposed dividend distribution. The risk profile continues to improve with NPE ratio down to 3.9% now, illustrating an excellent portfolio quality with limited risk concentration. 93% of our loan exposure is current, so it doesn't have any days past due. This reflects our prudent approach to our business strategy. We continued our efforts in the direction of digital transformation, digital users increased 18% compared to 2018. More important, the business origination through digital channels accelerated, 9% of unsecured lending volume came through digital channels and 13% of SME volumes in Slovenia and Serbia came from the automated lending tool. This has also helped us reduce the average ticket size in SME from 217

thousand Euros in 2018 to 190 thousand Euros in 2019, while growing the book at stable yields. Let's continue on Page 5.

As indicated in previous calls, previous announcements and calls, we continued our dialogue with the regulators in Austria in order to identify the optimal measures demonstrating that our risk profile is factually better than the current capital requirements would suggest. There is already a 20 basis points reduction from the Pillar 2 Requirement from the draft to the latest SREP letter, maintaining it at the 2019 level of 4.1%. A well-prepared action plan is ongoing to address feedback from regulators with the objective to see progress reflected in the next SREP rounds, which is expected during the autumn. We will propose to the AGM the distribution of a EUR 40 million dividend, which is 2.05 Euros per share. This is in line with the guidance we gave at the time of the IPO. We have also revisited the mid-term targets in the context of continued low interest rate environment and newly introduced consumer lending restrictions. They remain to a large extent in line with prior communication, more material adjustments relate to the effect of the persistent low interest rate environment and approximately one year longer time horizon to reach the guidance level. Johannes will provide further details during the call today. Please move on to page number 6.

Our straightforward business model to become a specialist focused on consumer lending and SME banking is reflected by the transformation of our book, the key to our value creation model is growth in the focus segment, gradual contraction of non-focus area to free up capital and liquidity and support earnings generation while we execute this transformation. The build-up of the consumer and SME book continued. They represent now 62% of our total performing loan book, at the end of the year in 2019, setting us well on track to achieve the targeted 80% plus in the mid-term. Gross yields have contracted mildly in consumer, driven by the increased focus on payroll customers and conversion of long tenures in Serbia to shorter ones. Given the interest rate environment and regulatory pressure on consumer lending, we see the defense of the consumer margins as very effective so far, particularly keeping in mind that in the last six months the new volumes which are booked at the gross yields above that of the back book. So, the new book in the last six months shows yields above those of the back book. On the SME, we also indicated this in the previous call, the flat gross yields in the context of ample liquidity in all markets must be read in correlation with the improved risk profile and a solid increase in commission income from this segment.

On Page 7 a closer look at the focus lending segments shows strong continuous growth on the consumer book to over EUR 1.3 billion, which is a 13% year on year growth. This was supported by an increase of 10% of new loan originations in 2019. Focus on lending limited the capacity allocated to some of the NCI programs, which increased in consumer by only 3% on the back of very successful

previous initiatives. Those initiatives were specifically in the areas of bancassurance and dynamic currency conversion. Several initiatives have already started in the quarter four of last year to accelerate NCI in consumer, focusing explicitly on repricing, accounts packages redesigned and improved capabilities on the cards product.
On the SME front, the growth of the book to over EUR 1 billion represents a year on year progression of 14%, driven by 12% acceleration in new volumes. New customer acquisition and connecting lending to turn over supported a very healthy growth in NCI and SME segment by 18.4% year on year. Let's have a quick look at the consumer lending market, this is something we regularly covered in our calls. In such calls, I mentioned that the consumer lending market share progression with an indication of 8 to 10% target in all our markets. This target, 8 to 10% market share in consumer lending is very important for us in three ways. First, it confirms that we have ample space to grow and we can do it with our model. If you look at Slovenia and Montenegro, we achieved the kind of levels that we're targeting. Second, we can achieve growth without becoming aggressive either in risk parameters or pricing. Thirdly, it shows the importance to progress in selected largest markets, Serbia and Croatia. In Serbia, we focused in 2019 on aligning the portfolio to the new regulation on maximum loan duration. Even in this context, we grew more than the market, and this will become visible in the market share over the coming quarters.

There is very good growth in Croatia with prudent risk parameters, even in the continued limitations related to the unavailability of the credit bureau. We gained here close to half a percent in market share.

A few words on digital, which is central to our strategy. I mentioned in the introduction the effects of our super pragmatic approach to the digital transformation. We identified digital solutions which work in more advanced markets and bring them to our customers. We focus strictly on three KPIs, number of digital users, consumer loans origination, digital SME loans. We added just over 30 thousand digital users in 2019, mostly through mobile banking, and we are now at 206 thousand customers, digital users. Consumer loans originated digitally are at 9% from 3.8% last year. Very solid growth and still a lot of way to progress. Add to that the 27% origination happened through Bank@Work, so our total out of branch origination accounts for 36% of our production. This encouraged us to close 17 branches in 2019 compared to the initially targeted 8.

Digital SME loans in Slovenia and Serbia contribute 13% of our acquisition. This is very solid. Croatia has been implemented in quarter 4 and the initial results are very convincing there as well. The Digital SME lending platform also helped us to reduce our average ticket size, as I was mentioning from 217 thousand Euro in 2018 to 190 thousand Euro in 2019. This is central to our strategy to defend the margin. Further pragmatic developments in the area of digitizing, automating, data utilization for the focus areas continues. We will inform you of such initiatives, both related to bringing new solutions to our market or rolling out everywhere services which we currently have only in selected markets. Visual Identification, M-loans, digital SME loans. With this, I would like to hand over to Johannes, who will take us through the financial and risk metrics for the year 2019.

Johannes Proksch

Thank you, Razvan. Before we come to that, please let me once more highlight that we adjust our numbers in order to provide you with a clear view of the underlying historic development. This was particularly relevant for the development from 2018 to 2019 and will become less important going forward. We have therefore provided you with extra two pages on these adjustments in the appendix, as well as a detailed breakdown in our audited year end financials, published this morning on our website. But here in brief. The most significant impact in 2018 was the Tier 2 waiver in the first quarter by, our at that time sole shareholder, we adjusted our 2018 figures accordingly. More importantly, the major one-offs during 2019 were in other results of EUR 3.9 million restructuring costs for the successfully implemented cost optimization program, built in the second and fourth quarter, and used so far in the amount of EUR 2.1 million. The IPO related costs were ultimately EUR 2 million, the release of a gain of EUR 4.3 million related to the resolution of our largest non-performing exposure, the write-offs related to the Swiss Franc conversion law in Serbia of EUR 8.1 million and the provision in relation to the Croatian Supreme Court ruling regarding Swiss Franc loans of EUR 8.7 million, fully reflected already in our Q3 results. And now let me explain on page 11 how our strategy is reflected in our 2019 numbers by highlighting the progress we made in the full year or fourth quarter of 2019 compared to the previous year's period.

Like in the last year during 2019 the higher rates on the focused business translated into a further increase of our interest income from this portfolio and, as a consequence of further reduced deposit yields, increased our net interest margin by 20 basis points to 3%. Our net commission income, of which 90% are related to our focus business further increased during 2019 by 7.7%, predominantly driven in the consumer area by payments, meaning account packages, transaction cards, as well as bancassurance and with accelerated contribution from SME related products as mentioned by Razvan earlier with cards income lower than expected. This positive development in net interest income and net commission income is also visible in the quarter comparison.

Operating expenses have remained flat. Our announced cost optimization, meaning the reduction of FTE numbers by 180 and 8 branches in the second half of 2019 was overachieved, as we will highlight later, and has kept our expenses in line with 2018, therefore helping us to contribute to cost improvements in 2020. All this has helped us to reach an adjusted post-tax profit of EUR 40.7 million or reported EUR 35.1 million, the main difference being the adjustments mentioned earlier, particularly the Swiss Franc conversion law with EUR 8.1 million in Serbia and the Supreme Court ruling on Swiss Franc closes in Croatia with the provisioning of EUR 8.7 million. All of the above led us to an adjusted return on tangible equity, at 14.1% CET1, of 5.6%.

Now on page 12 and 13, we provide our usual breakdown to show a granular picture of the development of our interest income and expenses composition and respective field related developments. On the interest income, this is on page 12, I would like to highlight, the continued increase over the quarters predominantly related to our focus business reflecting now 73% of the total market related interest income and clearly overcompensating the managed contraction in our non-focus areas. The relatively stable development of our focus yield, despite a negative market interest environment, is proving again that we were able to defend our margins in a challenging environment via our proposition on convenience and speed. As mentioned by Razvan earlier, new business yields in consumer have actually increased by 30 basis points during 2019, which is a promising sign that we will achieve stabilization of the overall consumer book yield. SME remained relatively flat, supported by the continuous increase of disbursements from our automated digital lending process for small tickets also driven by lower maturities and better rated clients. For the ones of you interested in the development of our other interest income, we have a page in our appendix highlighting the continuous decrease on our revenues from our plain vanilla bond portfolio of roughly EUR 1.1 billion, yielding 145 basis points, in 2019. The decrease in unwinding income as we continue to resolve successfully our non-performing exposures and the interest-like income related to fees accrued over the lifetime of the loan.

And now on page 13 we illustrate that our discipline repricing of deposits over the last years has also in 2019 contributed to decreased interest expenses on the back of reduced funding yields by roughly 12 basis points, meaning we paid today on average 49 basis points on our funding.

On page 14, the net commission income, I would like to highlight that earlier 2019 versus 2018 shows an increase of close to 7.7%, of which 90% are related to our focus business with an increasing share of SME related net commission income, since our clients increasingly use us for transactions and digitally sold guarantees and for trade finance business, while the consumer area had another strong fourth quarter predominantly driven by account packages and transactions.

Let's move now to operating expenses on page 15. As mentioned earlier, 2019 has shown so far a contribution of our operating expenses from 2018 of roughly EUR 47 to 48 million per quarter, or just below EUR 190 million for the full year 2019, while shifts in 2019 are reflected in the various cost categories. A part of the neutral shift between depreciation and administration expenses related to the adoption of IFRS 16 approximately EUR 7.1 million into depreciation, higher depreciation in IT are increasingly compensating by the other cost items such as premises expenses and intellectual expenses, except marketing which we keep relatively flat over time. The announced cost optimization initiative for the second half was better implemented than anticipated as we were able to reduce our FTEs by 229 and 17 branches versus an initial plan of 180 FTEs and 8 branches. In addition to that, we are proactively managing IT related costs, particularly related to our core systems, and apply a high scrutiny towards IT related intangible assets to manage future depreciation.

Let's now move to risk on page 16. We have already presented this page a number of times and you can see again the significant progress in 2019, where we are now, where we have now a non-performing exposure of EUR 277 million or 3.9%. You can also see the continuous reduction during the four quarters in 2019.

Broken down best segments on page 17 you see that NPEs in focus areas are well under control where the portfolios are growing with very healthy and stable coverage ratios. And in the non-focus areas we were able to release provisions related particularly to mortgages and large corporates, which helped us to even compensate the impact related to Serbian Swiss Franc conversion law on mortgages with write-downs of EUR 8.1 million in the second quarter of 2019 reflected in the credit loss expense line. The consumer related risk provisions of EUR 20.3 million during 2019 were better than expected, reflecting the portfolio ramp-up, which is based on a prudent underwriting and portfolio quality assessment process. The comparison to the full year 2018 provisions in consumer is limited, given that they were positively influenced by releases as a consequence of the sale of legacy portfolios with a gain.

On page 18, you see the current breakdown of our top ten non-performing exposures, of which 35% are related to large corporates. In 2019, we were quite successful in halving the exposure to EUR 42.4 million, mainly by restructuring, among others our largest non-performing exposure, a large Croatian retailer via debt equity swap and a subsequent sell of the resulting equity piece in the market at a gain of EUR 4.3 million, booked under other income and excluded from the adjusted results, as mentioned earlier. The top 10 continue to be healthy provisioned with coverage levels above 61% excluding collaterals and above 137% including conservatively valued collaterals.

And now a brief update on our capital position on page 19. Not much changed during 2019 with regards to our regulatory capital ratios, and we continue to have a very healthy total capital ratio, which in our case is equal to the CET1 of 17.7% on a transitional basis or 17.1% IFRS 9 fully loaded, after considering the profit for the year 2019 and the proposed dividend payment. RWAs were reduced during the last quarter, mainly via a shift of bonds from higher into lower risk weights.

Now let's move to the outlook, mid-term targets and dividend guidance chapter, on page 21 and page 22. Let's start with the outlook for the year 2020. We expect a benign macroeconomic environment in the coming years with expected macro-economic growth to remain comparably steady at approximately 2.8% for 2020. We will continuously progress in shifting from the non-focus to the focus segments and will increase the share of focus by another 5 percentage points. We'll continue to defend our margins and grow our net banking income. Net fee and commission income growth is expected to be comparable to 2019, accelerating towards the end of the year 2020, following the full implementation of the new cards platform. Operating expenses for 2020 are expected to continue the developments in 2019 by cost reductions resulting from the optimization carried out in 2019, are widely eliminated by increases in IT related depreciation. Cost of risk is expected to increase along a growing focus loan book and significant less releases from the non-focus areas. And on the question on a potential impact related to the coronavirus we can only respond that such impact remains unclear and will largely depend on future developments.

Now to the guidance on dividends. We remain committed to fulfill our original guidance as presented to you investors and research analysts during the IPO process to distribute another EUR 40 million for the year 2020 and an annual dividend payout of 60% of net profit in the following years. In relation to the annual SREP process where the next draft is expected in autumn this year, we expect that the annual SREP decision on both, Pillar 2 Requirement and Pillar 2 Guidance, will reflect the continuous progress in financial and risk parameters as reached in 2019, and the specifics of countries where Addiko is present. The distribution of any excess capital will follow this annual SREP decision and will be included in the dividend proposal to the AGM for the respective financial year. We will continue to pursue capital optimization by issuing eligible capital instruments, an AT1 or Tier 2, reflecting the development of future capital requirements, and will time these activities in line with the respective SREP decisions.

And now our reviewed mid-term targets on page 22. Our focus on consumer and SME lending and payment services and the rigorous commitment to the digital transformation has allowed us to further progress during 2019 towards our mid-term targets, originally presented to investors in the context of our IPO last summer. We reviewed our mid-term targets in the context of our budget and planning process during the last months and reflected on one hand the interest rate outlook which has significantly changed since we

	set our regional mid-term targets beginning of 2019, meaning that we do not expect interest levels to improve from current levels, and that further administrative restrictions curbing consumer lending will result in lower revenues, which will be compensated over time. And on the other hand, further cost optimizations to be introduced to compensate for the loss in revenues. This has resulted in our reviewed mid-term targets to be achieved one year later than originally planned, which compared to the original targets as follows: The continuous shift of the loan book from the non-focus to the focus areas will reach more than 85% in the focus area, previously this was 80%. The net interest margin, reflecting now the constant low Euribor interest rate environment, will be at 3.8%, previously c. 4%. Net fee and commission income growth will be roughly 10%, previously low-teens CAGR. The cost income ratio will reach below 50%, previously it was below 45%, but there was a 5% reflected due to the Euribor increase in the previous target, cost of risk based on net loans will be at minus 1.5%. Previously this was minus 1.6%. The return on tangible equity at 14.1% CET1 ratio is around 9.5%, previously it was above 12%, but the above 12% also included 2% related to the Euribor increase. Total capital ratio, including the management buffer at the mid-term is expected to be 16.1% or above 16.1%. So, this is unchanged and the loan to deposit ratio at around 100% has also not been changed. And now back to you Razvan.
Razvan Munteanu	Before turning to Q and A, four messages I want to reiterate on this call. First, we delivered a strong 2019, absorbing many of the one-offs related to the adverse events confronting us, enabling us to propose a dividend distribution of 2.05 Euro per share in line with the IPO promise. Second: our transformation is firmly on track with moderate adjustments to the mid-term targets, mostly in terms of timeline. Three: Digital transformation, which is key to our strategy, is progressing well on the back of our pragmatic approach, supporting expansion of sales and cost efficiency. And four, our dialogue with the regulators, is providing us with a clear basis to an action plan which should lead to improved capital requirements and by consequence, improved dividend distribution capability. With this, I ask the operator to please open the floor for questions and answers.
Operator	Ladies and gentlemen, we will now begin our Q&A session. If you have a question for our speakers, please dial 01 on your telephone keypad now to enter the queue. Once your name has been announced, you can ask a question. If you find your question is answered before it is your turn to speak, you can dial 02 to cancel your question. If you are using speaker equipment today, please lift the handset before making your selection. If you participate via the audio webcast, you can write questions via the Q&A function of the webcast by pressing the question mark button. One moment,

	please, for the first question. The first question is from Anna Marshall of Goldman Sachs, your line is now open.
Anna Marshall	Good afternoon. Thank you for the presentation. Two questions, please. Firstly, regarding capital requirements. Could you please provide more color on the action plan that you've developed following the discussions with the regulator, and also kind of looking into the horizon further down the road, what are your thoughts regarding potential impact of CRD V implementation, specifically in terms of their ability to cover a Pillar 2 R with other forms of capital rather than CET1, and as well as the treatment of intangible deductions related to software. So that was the first question. And the second question just to confirm regarding your 2020 outlook, especially for cost of risk, are there any assumptions at all in terms of macro impact or anything related to the coronavirus situation? Thank you.
Razvan Munteanu	So, I ask Markus Krause who is with us, our CRO, to address the capital response. And then I'll respond on the coronavirus.
Markus Krause	Related to the action plan, you were asking for, the SREP process started, the new one relevant then for the requirements changed to be effective then from 2021 on, will start in April roughly this year. And we will get the first draft as Johannes shared in autumn this year. What is the reference base for these action plans, what the bank has done during 2019. So, the snapshot what they use at the end of the year 2019. So, we are very confident about our progress what we made during the year. That is exactly also the action plan where we are in the process of the new SREP. We will share with them all of these achievements we did and the progress we did and certain items which have been identified as improvement needs. And that keeps us quite confident that we can deliver here the progress they need to have to reflect that in the Pillar 2 Requirement. In the Pillar 2 Guidance, it is very similar. Also here the discussion has been started in exchanging more details about how the regulators approach that topic. We are sharing also the way in terms of more granular data which we have available and they might not have to reflect also the financial progress we made in the last years properly in the calculation of the Pillar 2 Guidance. And all these results will then be communicated and reflected latest in autumn 2020 by the regulators in the draft. Is that answering your question, Anna?
Anna Marshall	Yes. Partially. The second part of the question regarding CRD V?
Markus Krause	The CRD V question was related to the capital structure?

Anna Marshall	Yes, the question basically with the introduction of CRD V, would you expect the possibility to fill part of Pillar 2 R with other capital level rather than CET1, basically Tier 2 or AT1?
Johannes Proksch	This will actually be defined in the draft letter. So, normally the regulator defines what kind of quality you need to hold against the various buckets. So, we don't see at the moment that this could change.
Anna Marshall	Okay. And regarding the treatment of deduction of software intangibles, would you expect any changes there?
Johannes Proksch	No, but I believe this was clear from the beginning, that our regulator does not allow basically these intangibles, goodwill and so on, which we actually don't have to be accounted for. So, this is not something which is in …. please, I am not aware that this is actually possible with our regulator. Therefore, we have never considered that one. So, we have a more conservative approach on this one.
Anna Marshall	Okay. Thank you.
Razvan Munteanu	On the potential impact of the coronavirus. In our modeling and mid-term targets that we provided to you, we do not include a physique impact associated with that. We however, I would make three mentions here. First of all, we are still in a privileged situation where the effect of the coronavirus in our markets is very, very limited and while we hope it to stay that way, we are preparing for potential effects either directly in our markets or affecting the supply chains. First of all, like I guess most of the organizations, we have an internal crisis team set-up, providing communication and business continuity preparations. Secondly, we also addressed the potential business impact. We are assessing various industries and we are preparing to address potential effects of disrupted supply chains that would affect the economies in our region through temporary suspension of activities. We are addressing this both by preparing solutions for existing borrowers, providing them relief and preparing to engage with the regulators in a dialog on this topic, as well as in terms of preparing recovery products for those customers, which in such a scenario will be confronted at some point with a temporary cashflow shortage.
Anna Marshall	Thank you.

Simon Nellis	Oh, hi. Thanks for the call. Just on the capital front, again, maybe I didn't quite understand the answer on the capital action plan but is your hope that the regulator will lower the P2R, or P2G as part of this plan? And, I guess the 60% payout ratio that you are guiding for future years, I guess that's predicated on you getting the regulator lowering the P2G to a point where you won't be in breach of that metric. Right?
Johannes Proksch	This is Johannes here. We obviously tried to basically convey the message in a way as we also had a dialog with the regulator around these topics, without pre-concluding what the outcome will be. But what we basically say is that the progress in our financial and risk numbers will be reflected in the SREP decisions in the future. And therefore, when we give a mid-term guidance of 16.1%, and this is unchanged from the one during the IPO, we basically believe that the progress in our financial numbers, which has now been shown over three years since we break through and three years of profits will be reflected, including the year 2019, as the regulator always looks on the past year when he does his assessment. So, the assessment, which will be completed in autumn this year will include the 2019 figures. And this progress should lead to a reduction, but we can obviously not pre-conclude how much and when this will happen, precisely. This is ultimately what the regulator will come up with.
Simon Nellis	Right. Okay. I see that you have a new shareholder, the DDM Group. Have you had any interaction with them? And do you know what their plans are for being a shareholder longer term.
Razvan Munteanu	We did meet DDM in one of our roadshows and we had an interaction which was based on exactly the same narrative and information that we provided to all our other investors and to the market. This happened back in November, on the third quarter of nineteen. Since then, we didn't have any individual interaction with them.
Simon Nellis	I mean, do you see any synergy from having such a shareholder? I guess they are knowledgeable in working out problematic debts and?
Razvan Munteanu	I cannot speculate on that, Simon. We didn't meet them yet. Our expectation is that they will reach out to us at some point in the near future subject to their transaction with AI Lake being concluded.
Simon Nellis	Understood. Could I also ask just about your, I mean, your medium-term outlook for risk cost is pretty clear, but can you help us kind

	of on the outlook for this year and for next year? I mean, you expect less recoveries, but it sounds like the credit environment still pretty benign. What kind of risk cost in the near term would you expect, if you can give us any guide? Thank you.
Markus Krause	This is Markus speaking. We have, as you have seen, the non-performing loan book has been reduced significantly down EUR 277 million. One of the key reductions was in the large corporate portfolio where we were leveraging on also what you see in the presentation itself, significant in terms of P&L. So, we cannot endlessly repeat that, so this comes to an end now while on the mortgage we still will leverage on releases because we are running down that portfolio gradually. So, there is something coming out of that. On the consumer you see what we have booked here, and Johannes has mentioned that this was better actually than the plan. So, take it as a direction and guidance. We, of course, use the latest developments also called forecasting the development in 2020. So, something in that direction ratio-wise, you cannot assume. And for the SME, where we had very low costs, we also have a certain risk appetite, especially with our lending in smaller business, where we go with small tickets, where we go more with automatic lending. We have to have that risk appetite and that is also reflected in the cost of risk. So, we expect an uptick here which is, so no releases anymore. There is some let's say amount which is in the ramp up of the portfolio over the years reflecting the appetite related on a risk return basis.
Simon Nellis	Okay. If you don't mind, I will just ask a few more questions. On the employee expense, I saw that the salaries of, you know, employee expense divided by average FTEs, it actually went down year on year. It is kind of surprising, because I thought there was quite a lot of labor cost pressure.
Razvan Munteanu	Yes, I can explain that, Simon. Our, this is Razvan, the restructuring program that Johannes referred to was that executed not in the typical way where you see FTE cuts predominantly from the bottom of the employment chain, if I may say so, but we had a very balanced approach with a number of senior positions being taken out. In the context of our migration from a universal bank into a focused specialist. There are certain functions and activities that we can either combine or give up, and this allowed us to reduce the average cost per employee as well.
Simon Nellis	Okay, I mean, would you expect that trend to continue going forward or is that kind of a one-off?

Razvan Munteanu	I think we didn't make a calculation from the angle you are describing, but the effort will go in the same direction. So, we will continue to consolidate or eliminate functions that are related to activities we are no longer focusing on. So probably, to a certain extent, it will continue.
Simon Nellis	Okay. And then just a question on intangibles. I saw that they came down in the balance sheets in the fourth quarter. What was driving that?
Johannes Proksch	Yes, I referred to this one. We basically take a quite scrutinized view on intangible, particularly if they are related to system (00:46:26 break in recording). So basically, we just reviewed them and there was one element in the other income line where we basically reduced the capitalization of these intangibles.
Simon Nellis	Okay. I think that is all for me for now. Thanks very much.
Jovan Sikimic	Good afternoon, I have a question on dividend. Was this proposal somehow coordinated with the regulator, in the course of this ongoing discussions on capital requirements?
Johannes Proksch	Obviously, the decision on a dividend is being taken by the management board and our year end financials, which are audited, have been also approved by the supervisory board. We had an open and constructive communication with the regulator, and they are acknowledging basically our decision. But there is no requirement for a sign-off by the regulator on such a dividend. That is a decision being made by the management.
Jovan Sikimic	And also, given the fact that payout is higher than 100%. Also, no need for any special approval from them?
Johannes Proksch	That's, you compare obviously the group profit post-tax profit of EUR 35.1 million with a dividend of 40. The dividend is actually paid out of the parent company, which has a profit of EUR 40 million. So, it is not eating into the capital. It is basically paying out the profit of the holding company. The financials have also been published this morning. It is on page 205.
Jovan Sikimic	Okay, and on the capital in general, is there any requirement from the regulator to close the gap, if you include also Pillar 2 Guidance throughout the year until the new SREP draft is out for 2021.

	I mean, you had pointed to Tier 2, but is there a kind of requirement from the regulator to close the gap?
Johannes Proksch	Usually, there is a transition period. We have so far not received the administrative decision. So, what we have received is a draft and a decision, but not the in Austria it's called the "Bescheid". We would expect at some point in time to see the transition period. But as you can see, also in the communication around the topic, the next SREP draft decision is expected in autumn. So, this is, I think, to be considered in that context. And that's why we also had the dialogue with the regulator and have a continuous dialogue with the regulator, to fulfill all the requirements and show them the progress, including the 2019 figures, so that they can come up with a decision in autumn on the new SREP. And we believe that that will be the relevant one for further action, meaning generating excess capital or closing gaps via a Tier 2 transaction or risk weighted assets optimization.
Jovan Sikimic	Okay. If you speak about risk weighted assets, I mean, there was this favorable treatment from Serbian Sovereign Bonds. I mean, can you quantify what could be the impact on Core Tier 1 ratio, roughly?
Johannes Proksch	First of all, although this happened end of 2019, it was only effective in 2020, so you don't see this in the financials. This will be in the first quarter financials you will see this impact, but obviously there are also off-setting impacts as the loan portfolio is growing, so we will basically update on the first quarter with regards to this effect. And then there were other implications in 2019 and I referred to this in the last quarter. Also, the weights on some bonds have changed and therefore we had a positive impact in the last quarter in terms of risk weighted assets in 2020.
Jovan Sikimic	Okay. Thanks for this. So just in terms of guidance, I mean, did I understand it correctly? So, the initial guidance will be achieved one year later?
Johannes Proksch	Correct. Well, the initial review, so basically, we say one year later and the numbers I have mentioned during the call. So, there is adjustments in one or the other direction, but mainly, you can see this on page 22, you basically can see the original mid-term target level versus the review. But please consider one thing, that during the IPO, when we have shown the original mid-term target level, we also referred to the implication, at that time, of the Euribor which was already at minus 10 basis points. So, we already mentioned during that period that the return on tangible equity will be not above 12%, but at around 10%. And so therefore, the review which we conducted over the last couple of weeks and months is

	basically a further reduction of half percent to that one. But it is now at 9.5%. Otherwise, you can read all these numbers they are in the presentation and also in our financial statements.
Jovan Sikimic	And the last one if I may, I mean, which interest rate level do you now embed? Because there is apparently another move, negative move on the market.
Johannes Proksch	There was one, I'm not aware of one over the few last days, but there was one I think in autumn and I currently see it at 41 basis points negative. Throughout the whole period.
Jovan Sikimic	Okay. That is fine for me. Thank you very much.
Operator	There are no further questions over the telephone lines.
Edgar Flaggl	All right, thank you operator. We have a question on the webcast from Alo at SEB. Number one, do you expect any response from the regulator on dividend proposals before the AGM? Do you expect the proposal to be approved in the current form or will it be adjusted lower? Question number two, can you comment on the recent changes in the shareholder structure?
Johannes Proksch	Okay, so I think, one, we already partially at least answered the first part. We don't expect any response from the regulator. This dividend is not new to them, this proposal. We decided on this one and the supervisory board decided on that one as well to be proposed to the AGM. So now it is only up to the AGM to decide for the dividend and they normally would accept it. That would be the normal course. And the second part is shareholder structure. So basically, I mean, we obviously welcome the changes in the shareholder structure, as we believe that it was clear that Advent is reducing their stake and the shareholder structure to stabilize, it is always a good thing to happen. You have seen the various announcements, including the one this morning that EBRD has now a direct stake in Addiko and that Advent has therefore further reduced or Al Lake their participation. So, we are obviously welcoming the stabilization in our shareholder base and the reduction of the overhang of shares.
Edgar Flaggl	We have another question on the webcast from Thibault Nardin at Wellington. What sort of consumer growth, consumer loan growth do you expect for 2020, given the new lending restrictions? And do you think there is a chance these could be rolled back?

Razvan Munteanu	This is Razvan, let me take this question. We see ourselves as specialists in the consumer lending capable to overcome the circumstances in the market. Maybe taking us one to two quarters to adjust to the new set-up. Based on our assessment currently, we see a continued growth similar to that of last year, going forward. We are confronted with specific restrictive regulations on consumer lending or recent ones in Slovenia, Montenegro and Croatia and Serbia, in particular. In Serbia, we aligned our portfolio to the new regulations, and we expect now the good sales performance to be reflecting market share gains and growth in the coming quarters. We do not have visibility in Serbia with regards to potential rollback of the regulation. In Slovenia, where the effect of the regulation is probably the most significant, we are in a positive situation of already operating within our target market share of 8 to 10%. So, we think that the effect on the overall growth from Slovenia was anyway weighted to this particular situation. So, it does not significantly affect our plans going forward. We also hear, we have informal signals that the regulation could be revisited by the regulators in the third or fourth quarter of this year. In Montenegro the regulation was introduced with the explicit time plan of two years. So, it expires after two years. It is also one of our smaller markets and a place where we achieved the level of market share that we target. Still, we see the portfolio growing there as well. And Croatia, where the regulations have not been adjusted, but there are recommendations from the regulators with regards to certain prudential measures, we see our growth continuing in the same pattern.
Edgar Flaggl	Good, we have another one from Thibault on the webcast. Any chances you could try tapping the Tier 2 market? You are also mentioning AT1 in your presentation, so should we understand you could try to further optimize your capital structure?
Johannes Proksch	Yes. Thank you for the question. Yes, we intend obviously to look at all these instruments. We are fully aware that the markets are very favorable. For us it is still important to see what the, and to have the transparency of the next round of a SREP decision in autumn. And we will then adjust volumes around that topic. And the instruments, obviously, both available to us, so we will then try to optimize our capital structure even further.
Edgar Flaggl	All right, we have one more question on the webcast from Mladen Dodig at Erste. First, dividend guidance, 40 plus 40, is it possible for this year to pay out the 40, since the DPR is seen as 60%? Two, considering the timeline for administrative decision from the regulator, do you plan or need Tier 2 issuance already in 2020?

Johannes Proksch	So, thanks for these questions. I think the first is just a clarification. EUR 40 million is for the year 2019 and we continue to confirm the initial guidance of another EUR 40 million for the year 2020, basically then obviously being paid out in the subsequent year, and 60% thereafter. The second part of the question is with regard to the timing. I think I mentioned before, we will adjust the size and obviously then also the time, once we know what the outcome is, the most likely outcome or maybe already on the basis of the draft SREP letter, we will then basically decide on the size. So, we aim for the end of the year to basically react to this one. Now, we don't want to predict or pre-conclude what the outcome could be. We expect a reduction and from that we will then decide the size of which we would like to issue. We also, as I mentioned before, don't know the timing to achieve this. For the moment, we understand that normally, timing is 12 to 18 months but could also be shorter at that point in time.
Edgar Flaggl	All right. Operator, back to you, we have no more questions on the webcast.
Operator	Okay, then we have a follow up on the telephone lines. It is from Simon Nellis again. So, your line is open again.
Simon Nellis	Oh, hi. Just a few more questions. Just to be crystal clear, on page 21, your guidance for fees and OpEx for this year, you are basically saying that the growth rate will be similar to last year. I guess you mean on the adjusted basis, right? So largely flat, flat costs on an adjusted basis and around 8% fee growth again?
Johannes Proksch	Yes, that's the right conclusion.
Razvan Munteanu	I would also add that as we move forward, we expect that our reported and adjusted numbers will become very similar.
Simon Nellis	Okay. And then just on funding costs, I mean, it's been coming down quite nicely for a while. How much further do you think it can come down?
Johannes Proksch	Not much more. It was always a positive surprise but obviously the past year will not be reflected in 2020, the reduction. So, it is difficult to estimate because there are still longer-term maturities coming to the end and we will continue to optimize, but don't expect much more coming out of the reduced interest or funding costs.

Razvan Munteanu	But also, I think it is important to make it clear that we are not counting in our results, on further material reductions of our funding costs.
Johannes Proksch	Yes.
Simon Nellis	Right. And then just last on the Croatian, I think it was a Supreme Court ruling, due at some point on Swiss Franc mortgages. What is your potential liability if they rule that the clients that have already converted to Euro can also ask for some kind of compensation or annulments?
Johannes Proksch	We didn't do these kinds of calculations. We understand that the already converted ones are excluded from the Supreme Court decision. We hear that there are noises around this topic. We haven't done the calculation and we don't know how this is exactly and the timing and how this is, what the result that would be. But it's an uncertainty, unfortunately, which hopefully can be clarified rather soon.
Simon Nellis	Do you have any provisions created against some kind of ruling or what would that be?
Johannes Proksch	No, to be clear on this already converted ones by law would be, again, basically touched by a Supreme Court decision. This is not part of our expectation. And this is also a wild speculation because you don't even know in what should that be then converted, into what kind of interest rate that should be converted. So, we believe that we have very prudently assessed the Supreme Court decision from September last year and provisioned the EUR 8.7 million against that one, but that did not include a conversion of already converted cases from the 2015 law. And it's almost impossible to provide or to make a provision on something which is highly speculative or where there is no ruling on that basis.
Simon Nellis	Got it. Very clear. Thank you very much, that is all for me.
Jovan Sikimic	Yes. Once more than we are then also Croatia. I mean, you mentioned in the report that the number of court cases against the bank increased 2019. Could you be more specific maybe on that front just to have a feeling about legal risks in this country?

Johannes Proksch	Yeah. So basically, I think there are two areas where customers are basically suing us. One is the so-called unilateral interest rate. These were the cases where Euribor reductions were not passed over to the customers. On that one, in 2019, the statute of limitation expired and therefore, all the cases which came through are basically closed. So, it is not any longer possible that new ones would come through. And we have provisioned for that in the first half, an appropriate amount, and we do not see there any further risk. And then there are obviously new cases based the Swiss Franc, Supreme Court decision. So far, far less than we would have expected. But also, not enough to conclude now what that would really mean. We are, at the moment, absolutely within all the expectations which we have used for establishing the provision, with one exception, that we expected far more cases to come through quicker.
Jovan Sikimic	Okay. That's helpful. Thank you.
Operator	As there are no further questions I hand back to the speakers for the conclusion.
Razvan Munteanu	Ladies and gentlemen, with this, we conclude our call concerning the earnings for 2019, and we thank you for your attendance. Once again, our key messages were a strong 2019, very good results. We are proposing a distribution of 2.05 Euro per share to the AGM. Digital transformation going on the right track, and our dialogue with the regulators gives us the basis for an action plan that we expect will lead to a better reflection of our risk profiling into our capital ratios. With that, I thank you very much for the participation and wish you an excellent day going forward. Goodbye.
Operator	Ladies and gentlemen, thank you for your attendance. This call has been concluded. You may disconnect now.