Conference Call Transcript

20 September 2024

Investec Pre-close Briefing

Operator

Good day, ladies and gentlemen, and welcome to the Investec pre-close briefing. All participants will be in listen-only mode. There will be an opportunity to ask questions later during the conference. If you should need assistance during the call, please signal an operator by pressing star and then zero. Please note that this call is being recorded. I would now like to turn the conference over to Fani Titi, Chief Executive of the Investec Group. Please go ahead.

Fani Titi

Thank you, Judith, and good morning, all. Thank you for joining us for our pre-close trading update. This update reflects the financial performance for the five months ended 31st August 2024, and also covers the expected results for the half year to 30 September 2024.

I'm joined this morning by Nishlan Samujh, our Group Finance Director. Ruth Leas, the CEO of our UK business. And Cumesh Moodliar, the CEO of our South African business.

We are pleased with the group's year-to-date performance, which demonstrates continued momentum from our diversified client franchises. This was achieved against the background and a backdrop of low activity levels in the initial months of the period. As we look forward, we are encouraged by a more positive economic outlook, reflecting increasing certainty on global interest rate cuts.

Turning to underlying performance for the five months ended 31st August 2024, higher revenue was supported by balance sheet growth and increasing contribution from our various growth initiatives, supported by higher average rates. Continued client acquisition and improving activity levels underpinned non-interest revenue growth. Cost to income ratio improved as revenue grew ahead of costs. Fixed operating expenditure reflected continued investment in people and technology for growth, as well as inflationary pressures.

Looking at the underlying drivers of our core franchises, net core loans from our banking businesses increased by 6.1%, annualised £31.7 billion, driven by private client lending in both geographies and corporate lending in the UK. Customer deposits remained flat at £39.5 billion. Funds under management in our Southern African wealth and investment business increased by 10.7% to £23.2 billion. We saw strong inflows in the discretionary funds and positive inflows in non-discretionary funds.

For the half year ending 30 September 2024, we expect to report the following. Pre-provision adjusted operating profit to be ahead by 7 to 13% relative to the prior period. Adjusted earnings per share to be between 4% behind to 4% ahead of the prior period. Cost to income ratio to be below the 53.3% reported in the prior period. Credit loss ratio to be around the upper end of the through the cycle range. The overall credit quality to remain strong in line with the position at financial year 2024, with no evidence of trend deterioration.

Group ROE to be between 13 and 14% within the group’s upgraded medium-term target range of 13 to

17%. The group return on tangible equity ROTE is expected to be between 15.5% and 16.5%, within the 14 to 18% medium-term range. We maintained strong capital and liquidity levels, positioning us well to support our clients and scale identified growth opportunities in an improving economic environment. The group continues to trade in line with its previously given FY 2025 guidance. I will now turn the call over to questions.

Operator

Thank you. Ladies and gentlemen, if you would like to ask a question, you may press star and then one on your touch-tone phone or on the keypad on your screen. You will hear a confirmation tone that you have joined the queue. If you wish to withdraw your question, you may press star and then two, to remove yourself from the question queue. Once again, to ask a question, you may press star and then one.

The first question we have is from Nicola Mawson of Business Report. Please go ahead.

Nicola Mawson

Good morning. Thank you very much for the call. Just in terms of the pre-provision, could you provide a bit more detail on the amount of the provision, as well as exactly what it is for, please?

Fani Titi

Nicola, I'm not sure that we understand your question. The pre-provision operating profit relates to the operating profit before provision for impairment. We've given you that we expect the momentum in the business to continue, and we would expect growth in this metric to be 7 to 13% ahead of last year.

With respect to impairments, we have indicated that we expect impairments to be towards the upper end of our through the cycle range, and that is at 25 to 45 basis points. And in the South African environment, we've indicated that impairments are expected to be below the midpoint of the indicated through the cycle range. In the UK, that we will be above the previously indicated range of 50 to 60 basis points. That's how we see both the strength of our revenue on the one hand, and the profile of our impairments on the other. I hope that clarifies the issue.

Nicola Mawson

No, not especially, sorry. I was obliquely referring to the Daily Maverick article by amaBhungane, in terms of the German federal tax.

Fani Titi

Let me deal with that question. That’s a very different question.

Nicola Mawson

You mentioned [overtalking].

Fani Titi

That refers to the German probe into what is called CumEx tax issues in Europe. The issues arose in the late 2000s, say 2009, 10, 11 or so, and there has been varied investigation by the authorities into both banks, legal firms and related advisers. And we, four years ago, took a provision, which we indicated to the market we thought was sufficient to cover a potential liability.

We did not indicate the exact amount of the provision, for the simple reason that this matter is under litigation. And it is pretty standard practice that when a matter of this nature is under investigation, that we would not give the specifics of the provision we have made, because that would undermine our legal position. That is the issue, if you're referring to the CumEx German investigation.

Nicola Mawson

How does that fit back into your numbers, into that pre-provision number that you're talking about? Am I thinking on the same line?

Fani Titi

This doesn't have anything to do with, this is an operating profit number before provisions that have been taken in the current period. The provision we're talking about, we took about four years ago, so this is a historical matter. I was actually quite surprised that the biggest paper dug this one out, and it was covered quite extensively in the past.

Nicola Mawson

That provision is done and dusted, and there's no need to provide for anything in these numbers.

Fani Titi

Yes, that's right. That's an old story, provided for a number of years ago, so that's the correct understanding.

Nicola Mawson

And then just in terms of your position on the issue, if you don't mind.

Fani Titi

We indicated that this is a historical matter, a legacy matter. Our attitude is to cooperate with the German authorities, and we continue to work with them towards a resolution of the issue. And that investigation continues and when there is resolution, we will duly inform the market. But we continue to be comfortable that we are appropriately provided.

Nicola Mawson

There's absolutely no change from four years, or however long ago it was.

Fani Titi

No change. No new information, no change.

Nicola Mawson

Great. Thank you so very much. Appreciate your patience on that.

Fani Titi

Thanks, Nicola.

Operator

The next question we have is from Alex Bowers of Berenberg. Please go ahead.

Alex Bowers

Morning, everyone. Three questions from me, if I may. Just firstly, on loan growth, given we're likely in a rate cutting cycle now, could you give us any view on growth expectations for H2?

The second question is on NII sensitivity to base rates. Again, given we've entered the rate cutting cycle potentially, is there any change in your guidance of NII sensitivity to base rates in both the UK and South Africa?

And then lastly, you mentioned there were some specific impairments in the UK business, which would have drove the credit loss ratio to the upper end of your guidance range. Could you please unpack this a bit more around what areas of the business this was mostly driven from? Thanks.

Fani Titi

I'm going to start on loan growth. We've indicated that we have seen an annualised 6.1% growth in our loan book. And we've also said that in the early part of this period, we faced elections in both the UK and in South Africa, and as a consequence of the uncertainty that normally precedes the elections, we saw activity levels being much lower.

As we look ahead, we do expect that with more certainty, certainly in South Africa, where we have a government of national unity, a posture from that government that appears to be more business friendly, and the levels of confidence in this economy have increased, as measured by a number of metrics. We would expect that activity would pick up. And over the year, we would hope and expect a better growth. I don't think we will give you a forecast now of the growth outlook for the rest of the year.

Similarly, in the UK, while there is still a level of uncertainty, given that we expect the Autumn Statement to be issued next month. And in that statement, we will have a better sense of some of the economic policy parameters, including the positions of the Labour Government, on certain taxes. And that obviously will feed into the overall level of confidence within that economy and consequently activity.

But with the overall expectation of interest rate cuts globally, we expect better confidence, better activity, less pressure on consumers and clients, and generally a better outlook. We will be able to give you a better sense of our outlook when we report in November.

On impairments, I'm going to ask Ruth to address impairments in the UK. The statement says very clearly that we do not see trend deterioration, and also deals with the fact that the elevated level was driven by specific impairments. We also reiterate that for the year as a whole, we continue to be comfortable with the guidance we gave when we announced our FY 24 results. And in that guidance, we said in the UK, we would expect impairments to be in the range 50 to 60 basis points.

While a little more elevated in this period that we are in, we would still expect for the whole year that impairments would come into that range. Ruth, do you want to talk a little more about the impairment outlook or experience in the UK?

Ruth Leas

Hi, Alex. I think Fani covered it really, mostly around his answer. As the statement says, we've seen certain specific impairments. We do not see trend deterioration in the overall book. I think one would expect at this stage of the interest rate cycle, where we've seen rates higher for longer, that there would be certain idiosyncratic events related to certain borrowers, and we've needed to take impairments for those.

Outlook, as Fani says, remains as it was when we gave FY 25 guidance. We're still very comfortable with the overall asset quality of the book and the performance of our borrowers. I think nothing really more to say on that.

Just in terms of loan growth, as Fani said, we have seen good loan growth relative to market here in the UK and Europe, and in the other areas and geographies where we operate. And as the rate cycle moderates and rates come down, we'd expect a better experience and stronger growth for both loans and from an impairment perspective.

And then just picking up on your NII sensitivity question, that has reduced a little around £5 to £6 million, I would say, for the UK at this point in time. We are working very well to manage impacts related to reductions in interest rates.

Fani Titi

Cumesh, do you want to cover the South African?

Nishlan Samujh

In South Africa I think our guidance is very similar to that of the year end, of about 100 million rand for every 25 basis points.

Fani Titi

Alex, hope that covers your questions?

Alex Bowers

Brilliant, thank you. The 5 to 6 million is for 25 bips as well, is that right? Just to double check, in the UK?

Ruth Leas

Yes.

Alex Bowers

Brilliant, thank you very much.

Operator

The next question we have is from Asanda Notshe of Mazi Asset Management. Please go ahead.

Asanda Notshe

Good morning. I hope you can hear me.

Fani Titi

Yes, we can hear you, Asanda, go ahead.

Asanda Notshe

Great, thanks. Two questions, quickly. Firstly, just with the conclusion of the Assupol transaction, any insight you can give us in terms of the timing and implications of the Bud Group exit?

And then secondly, just back on the NII question, what's your policy, sorry if you've spoken about this before, just policy around hedging, interest rate hedging? Thanks.

Nishlan Samujh

Asanda, hi. I think on the Assupol transaction, the announcement put out by them is that actual payments and transfers happens on 7th October. It's now completely unconditional, so we basically will see that as a receivable for the half year, and it will be settled on 7th October. We close the year end with a carrying value of our position in IEP at around about 4.3 billion. The expected flows from this or the flows that we now know is about 1.7 billion. That reduces the portfolio to about 2.6 billion. There's three remaining key assets and we'll continue to realise that as opportunities continue to unfold over the next little while.

And then with regard to NII, I think we detailed our hedging strategy in the UK. The strategy itself has remained consistent with that of the year end, really focussed on, Ruth, if I remember, the equity element. And from a South African perspective, I don't think there is an active, there's no active hedging policy, but we obviously position ourselves as we anticipate rates, but no active management or hedges in place.

Asanda Notshe

Great. Thank you.

Operator

Ladies and gentlemen, just a final reminder, if you would like to ask a question, you may press star and then one. The next question we have is from Chris Steward of Ninety One. Please go ahead.

Chris Steward

Good morning, and thanks very much for the opportunity to chat. Just a couple of quick questions from my side. One is, your UK business adjusted operating profit guidance including Rathbones seems to imply, given the context of your guidance around the specialist bank, that the earnings contribution from Rathbones is going backwards, which is something of a surprise. Maybe you could just unpack that, to the extent that you can. I understand it's a listed entity, just maybe the guidance around the specialist bank versus the UK business in its entirety.

And then you've given some indications of positive net flows within the South African wealth business and the AUM, all of which sounds encouraging. Is there any comment? The release appears to be absent commentary with regard to earnings from that particular entity. Is there anything that you could add in that regard, please?

Nishlan Samujh

Sure. Hi, Chris. Just a couple of points on the Rathbones transaction. I think at the time when we combined the businesses, Rathbones itself had an operating margin of about 22 to 23%, the wealth business an operating margin of around 26 to 27%. The initial combination, having taken a combined share of 41.25%, will result in an initial dilution in terms of our share of operating profit, really not material in terms of the overall numbers.

And I think some of the very key points reported by Rathbones is, firstly, in the 30th June full-year results, the achieved operating margin was 25.3% with around about £20 million of run rate achieved synergies. We will anticipate, and also commitment to the fact that they see the overall path to achieving the level of synergies committed to in the transaction itself continues to unfold in a positive manner.

In terms of the short term, yes, it's slightly behind, similar to what we saw at the end of March, but that gap will close. And as we move forward, all things equal.

Fani Titi

Cumesh, there was a question on SA wealth.

Nishlan Samujh

The wealth business in South Africa, I think really, just giving you some of the detail on the underlying AUM, their contribution will be significantly positive in this period, but we'll unpack that detail when we go through the actual numbers with the results in early November.

Chris Steward

While I've got the floor, I'll push my luck. Some of what you've said seems to imply in the last year, your H1/H2 split was pretty close to 50/50. Would you hazard that the operating environment is more conducive for a stronger second half than the first half, based on what you're seeing right now?

Nishlan Samujh

I think, Chris, just drawing your attention to the concluding remark, which is that we still are operating in line with our guidance that we provided for the full year. And I think that in it contains some indication that we anticipate a better momentum into the second half.

Chris Steward

Great. Thanks, Nishlan, thanks very much.

Operator

The next question we have is from Khaya Mthembu of Longmark Securities. Please go ahead.

Khaya Mthembu

Morning, guys. Thank you very much for the update and the opportunity. Could you please provide some more colour on the customer deposit performance in South Africa? Thank you.

Fani Titi

Sorry, Khaya, do you want to repeat? We missed what you said. Colour on?

Khaya Mthembu

Customer deposit performance in South Africa.

Fani Titi

Customer deposit performance in SA. I'll give Cumesh that question. Just before we answer that, obviously quite pleased with the performance of both businesses, as we have indicated. And in this particular statement, we've indicated that we expect the performance of the South African business to be at the upper end of the ROE range of 16 to 20, so really a good performance. And in the UK, equally, we're quite happy with that performance. Cumesh, do you want to cover your business?

Cumesh Moodliar

Thanks, Khaya. I think just a couple of points in terms of our deposits in SA. The retail deposits in our business emanating from both our private bank and corporate cash management channel, continue to grow quite strongly year-on-year. And we’re up about 10-odd percent just in that segment. On the wholesale deposits, we've taken a strategy to shed some of the wholesale deposits in line with growing our spread between retail and wholesale deposits, and also within the context of our deposit book, ensuring that we're shifting our profile of some of the deposits over a longer period, from cool to more notice-based deposits.

We've got a longer-term retail deposit strategy, as well as looking at how we manage our wholesale deposits.

Fani Titi

Thanks, Cumesh. Khaya, I hope that covers your question.

Khaya Mthembu

That's good, thank you.

Operator

Thank you. It seems at this point, we have no further questions and I would like to hand back to Fani for any closing comments.

Fani Titi

Thank you all for your time this morning and for your questions and interest in our business. As usual, if you have any further questions, please don't hesitate to get in touch with our team. Again, we look forward to a more fuller report in November when we report our half-year results. Thank you again.

Operator

Ladies and gentlemen, that concludes today's conference. Thank you for joining us, you may now disconnect your lines.