Deutsche Bank AG

Deutsche Bank Q3 2020 Analyst Conference Call

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Transcript

Speakers:
Christian Sewing, Chief Executive Officer
James von Moltke, Chief Financial Officer
James Rivett, Head of Investor Relations

JAMES RIVETT

- Thank you all for joining us
- As usual on our call our CEO, Christian Sewing, will speak first, followed by our chief financial officer, James von Moltke
- The presentation, as always, is available for download in the investor relations section of our website, db.com
- Before we get started let me just remind you that the presentation contains forward-looking statements which may not develop as we currently expect
- We therefore ask you to take notice of the precautionary warning at the end of our materials
- With that let me hand over to Christian

CHRISTIAN SEWING

Slide 1 -- Continued progress on strategic transformation

- Thank you James and welcome from me
- It is now five quarters since we launched our strategic transformation
- And for the fifth quarter in a row we have delivered on or ahead of our financial targets and transformation agenda
- This positions us well to deliver against our long-term targets
- We were profitable in the third quarter and in the first nine months of the year with results ahead of our internal plan
- The results are clearly a reflection of our refocused strategy
- And yes, the results are in part driven by higher revenues in the Investment Bank where market conditions remained supportive
- But we see our revenue growth in the Investment Bank as much more than just market driven
- The performance also reflects the refocus of this division around businesses where we have market leading positions
- In Q3 we have outperformed peers in several of our key areas within fixed income and increased market share

- Despite the revenue headwinds we are facing in the Corporate Bank and Private Bank, the results are in-line with our original plans
- Asset Management is performing in-line with our expectations as well
- We also continue to reduce costs with the 11th quarter in a row of year-on-year declines
- The combination of higher revenues and lower cost is driving higher Core Bank profitability which more than offset the combined impacts of:
    - transformation costs to implement our strategy
    - the burden of winding-down the Capital Release Unit which continues in-line with our plan
    - and elevated provisions for credit losses given the COVID-19 pandemic
- And, finally, we continue to manage our balance sheet conservatively
- Capital was broadly stable in the quarter while liquidity further increased
- This provides a solid position in the current environment to maintain our financial strength and to support our clients
- Let us go through these themes in more detail starting with our progress against our strategic transformation on slide 2

Slide 2 - Disciplined delivery of our transformation agenda

- In July 2019 we identified the transformation related effects that we would take over the next 14 quarters
- After just five quarters we have put over 80% of these costs behind us
- In the third quarter we continued to implement our strategic transformation
- Some examples include:
- In the Private Bank Germany, we announced the reduction of a further 100 Deutsche-Bank branded branches
- Since 2016 we will have removed approximately 30% of our entire German branch network including Postbank
- This announcement reflects the changes in customer behaviour that we are seeing - including a near doubling of online securities transactions of which 30% are now coming through our mobile app
- To support our revenue objectives, we extended partnerships with Zurich and Mastercard

- We further rationalized our real estate footprint with the early closure of a significant part of our New York campus
- We continued to simplify our legal entity structure with the completion of the sale of our Trust business in Mexico
- And we completed the formation of the International Private Bank and introduced a simplified reporting and leadership structure
- This should unlock further revenue and cost synergies between Wealth Management and the former Private & Commercial Bank International consistent with our agenda
- These examples demonstrate our relentless focus on execution
- Let me now discuss our revenue performance on slide 3

Slide 3 -- Stabilizing revenues under re-focused strategy

- A core objective of our transformation has been to stabilize and then grow revenues
- We have grown group revenues by approximately half a billion euros over the last 12 months, driven mainly by the Investment Bank
- The revenue growth in our refocused business model has offset the exit from equities trading
- Clients have re-engaged with a model which focuses on our core strengths
- In each of the last four quarters we have grown FIC revenues year-on-year by a high double digit percentage
- This includes a near doubling of Rates revenues, mainly driven by strong underlying client flow
- In Origination and Advisory, we have consistently outperformed the global fee pool in 2020, resulting in our highest market share in 6 quarters
- This includes ranking third in green bond issuance, up from 14th in 2019
- As a result, we see a substantial part of the Investment Bank revenue performance to be sustainable
- You see this in Core Bank revenues which have increased to around 24 billion euros over the last 12 months
- This puts us close to the plan of 24.5 billion euros that we described at the last Investor Deep Dive as part of our path to the 8% return on tangible equity target in 2022
- But we are not complacent

- We will continue to work on measures to offset the interest rate headwinds and the further anticipated normalization of market conditions in investment banking
- Turning now to our progress on cost reductions on slide 4

Slide 4 – Cost discipline continues for the 11th consecutive quarter

- We promised that we would not let COVID-19 slow down our pace of execution – and we kept that promise
- We have delivered 11 quarters of year-on-year reductions in adjusted costs excluding transformation charges and bank levies
- Excluding transformation charges and prime finance costs, adjusted costs were 4.7 billion euros in the third quarter
- This puts us well on track to meet our 2020 target of 19.5 billion euros – this would be a reduction of 3.3 billion euros – almost 15% over the past two years.
- Our relentless focus on costs is now in the mind-set of the bank and will continue
- The disciplined execution is becoming increasingly visible in our financial results as you can see on slide 5

Slide 5 -- Strategic transformation drives growth and higher profitability

- A core objective of our transformation is to improve sustainable profitability
- That means generating positive operating leverage by growing revenues and, at the same time, reducing costs
- We have generated positive operating leverage for 4 quarters in a row at both a Group and a Core Bank level
- This operating leverage has driven significant improvements in Core Bank profitability
- The improved Core Bank performance has increasingly offset the negative impact of the wind-down of the Capital Release Unit
- Over time, more of the Core's Bank profitability should flow to the Group's bottom line as we continue to make progress on our transformation agenda and provisions for credit losses normalize
- I am also encouraged that all four of our core businesses generated positive operating leverage as you can see on slide 6

Slide 6 – Driving operating leverage with disciplined resource allocation

- The improvements were driven by disciplined implementation of our strategy as each business works to improve its return on equity
- Both the Corporate Bank and the Private Bank have implement measures to offset the interest rate headwinds
- The Corporate Bank now has charging agreements in place on approximately 68 billion euros of deposits
- These agreements added 55 million euros to revenues in the current quarter alone
- This is materially above the targets we laid out at the investor deep dive in December
- To further accelerate growth, we have recently combined all our operations for business clients in Germany, into a single unit
- The Investment Bank benefited from the before mentioned recovery in revenues combined with ongoing cost reductions
- The Private Bank generated 5 billion euros of net new client loans and 3 billion of net inflows into investment products in the quarter
- On the cost side, in the Private Bank we have now generated 260 million euros of cost synergies from the German merger year-to-date
- Here, we remain on track to reach our full year objectives
- In Asset Management, DWS has shown its resilience with a rebound in revenues driven in part by ongoing cost reductions as well as net asset inflows
- DWS has generated 17 billion euros of net inflows year-to-date with more than one third in ESG products
- Across our businesses, the operating leverage has not been generated at the expense of resource discipline
- Over the last 12 months risk weighted assets were broadly flat or slightly down in each of our businesses
- This discipline around risk weighted assets is a key element of our commitment to conservative balance sheet management which we discuss on slide 7

Slide 7 -- Maintained strong balance sheet

- We held our CET1 ratio broadly stable at 13.3%
- Liquidity reserves increased to around 250 billion euros
- Both of these metrics are comfortably above regulatory requirements

- Provision for credit losses was 25 basis points of loans on an annualized basis in the third quarter
- Performance in our loan portfolios since the first quarter supports our guidance for the full year that provisions will remain in the 35 to 45 basis point range
- We reiterate this guidance even with the recent renewed uncertainties in the macro-economic outlook
- This compares favourably to our international peers, reflecting the high quality nature of our loan portfolios and tight management of credit risk
- It also reflects the fact that around 50% of our loan portfolio is in Germany
- In summary:
- Our performance is in-line with or even ahead of all our major strategic and financial objectives
- We are confident we can continue on this path including our expectation to be profitable at the pre-tax level for the full year
- We look forward to discussing this with you in more detail in our Investor Deep Dive on the 9th of December
- With that let me hand over to James

<u>JAMES VON MOLTKE</u>

<u>Slide 8 – Q3 2020 Group Financial Highlights</u>

- Thank you Christian
- Let me start with a summary of our third quarter financial performance compared to the prior year on slide 8
- As Christian said, operating leverage was strong in the quarter
- On a reported basis we generated 23% operating leverage as revenues increased by 13% while non-interest expenses declined by 10%
- Excluding specific revenue and cost items which are detailed on slide 34 of the appendix, operating leverage was 17%
- On this basis, revenues increased by 9% while adjusted costs excluding transformation charges declined by 8%
- We generated a profit before tax of 482 million euros or 826 million euros on an adjusted basis

- In the nine months, profit before tax was 846 million reported or 1.5 billion euros adjusted
- Excluding specific revenue items, restructuring and severance and transformation charges, the Core Bank generated a post-tax return on tangible equity of 6.8% in the third quarter
- Tangible book value per share of 23 euros and 21 cents was slightly below the second quarter driven by FX translation

Slide 9 – Provision for Credit Losses

- Turning to provision for credit losses on slide 9
- Consistent with our full year guidance, provision for credit losses returned to more moderate levels this period
- The provision was 273 million euros in the quarter, or 25 basis points of loans on an annualized basis
- Incremental provision for credit losses related to COVID-19 was 76 million euros including 215 million of stage 3 builds
- The stage 3 build was partly offset by releases in stages 1 and 2 reflecting the better consensus macro-economic outlook in the quarter
- We implemented a larger management overlay compared to the second quarter given uncertainties in the macro-economic outlook which partly offset the release generated by the model
- Including the provisions taken in the third quarter, we ended the period with 4.8 billion euros of allowance for loan losses, equivalent to 111 basis points of loans

Slide 10 – Capital ratios

- Turning to capital on slide 10
- Our CET 1 ratio was 13.3% at quarter end, 285 basis points above our regulatory requirement of 10.4%
- The CET1 ratio increased by 2 basis points in the quarter
- Progress in the Capital Release Unit, lower operational risk RWA and repayment of client credit facilities were broadly offset by movements in OCI and growth in Core Bank RWA
- The leverage ratio was 4.4% at quarter end, an increase of 28 basis points

- The increase reflected the exclusion of certain central bank balances from the leverage ratio denominator following the implementation of the CRR quick fix

Slide 11 – Adjusted Costs

- Slide 11 shows the progress we are making on reducing adjusted costs
- Adjusted costs declined by 424 million euros or 8% excluding transformation charges
- Costs declined across all major categories while we continued to invest in our IT and control programs
- Adjusted costs included 89 million euros of expenses eligible for reimbursement related to Prime Finance and 104 million euros of transformation charges
- These costs are excluded from our 2020 adjusted cost target
- On this basis, adjusted costs were 4.7 billion euros in the quarter and 14.9 billion for the first nine months
- As Christian said, this puts us on a good path to the 19.5 billion euro target this year
- With that, let's turn to the progress our businesses have made compared to the prior year period, starting with the Corporate Bank on Slide 13

Slide 12 - Segment Results

Slide 13 - Corporate Bank

- Pre-tax profit in the Corporate Bank was 189 million euros in the quarter, or 243 million euros excluding transformation charges and restructuring and severance which we detail in the appendix
- This equates to a 6.9% adjusted post-tax return on tangible equity
- Revenues of 1.3 billion euros decreased by 5% on a reported basis or 2% excluding the impact of FX translation
- The Corporate Bank partly offset the interest rate headwinds and lower client activity with deposit repricing, higher episodic items, balance sheet management and ECB tiering
- Despite the challenging interest rate environment and other macro-economic headwinds, Corporate Bank revenues for the first nine months were essentially flat year on year

- The Corporate Bank also made progress on reducing costs to offset the revenue headwinds
- Non-interest expenses declined by 1% and included 39 million euros of restructuring and severance charges, mainly related to the finalisation of the German corporate and commercial banking integration
- Adjusted costs excluding transformation expenses declined by 7%, reflecting reductions in non-compensation expenses and FX translation benefits
- Provisions for credit losses of 42 million euros were mainly driven by releases due to the improved macro outlook with modest new impairments

Slide 14 - Corporate Bank revenue performance

- Global Transaction Banking revenues declined by 8% or 4% on an FX-adjusted basis as shown on slide 14
- Cash Management revenues declined as deposit repricing, balance sheet management and ECB Tiering were more than offset by the interest rate headwinds and lower client activity in parts of the quarter
- Trade Finance and Lending revenues were essentially flat excluding the impact of FX translation and episodic items
- Securities Services and Trust and Agency Services revenues declined as a result of interest rate reductions in key markets
- Commercial Banking revenues increased by 1% as growth in deposits and fee revenues was partly offset by lower lending-related revenues
- Turning to the Investment Bank on slide 15

Slide 15 - Investment Bank

- The Investment Bank generated a profit before tax of 957 million euros in the third quarter with a 12% post-tax return on tangible equity
- We made further progress on our strategic objectives including standardization of processes to reduce costs, growing revenues in focus areas and reducing funding costs
- Revenues of 2.4 billion euros increased by 35% excluding specific items, driven by the benefits of strategic repositioning, strong market conditions and good client flows
- Noninterest expenses of 1.4 billion euros declined by 14% in part reflecting lower restructuring expenses

- Adjusted costs excluding transformation charges declined by 5% on continued disciplined expense management, despite higher compensation costs on significantly higher revenues
- Provision for credit losses of 52 million euros, or 29 basis points of loans reflected the improved macroeconomic outlook, partly offset by further COVID-19 related impairments
- Loan balances declined during the quarter returning to more normalized levels, with further repayment of client credit facilities and prudent balance sheet deployment

Slide 16 – Investment Bank revenue performance

- Revenues in Fixed Income, Currency Sales & Trading increased by 43% excluding specific items as you can see on slide 16
- This included a near doubling of revenues in the trading businesses
- Rates revenues more than doubled with further improvements in client engagement given the renewed strength of the franchise
- Foreign Exchange revenues were significantly higher reflecting higher volatility and strength in derivatives
- Revenues from Credit trading were significantly higher driven by the continued recovery in credit markets and strong client flows
- Emerging market revenues were higher compared to a weak prior year quarter principally due to strength in CEEMEA and Latin America, specifically in the flow businesses
- Financing revenues were essentially flat excluding the impact of FX translation headwinds
- Third quarter Financing revenues benefited from a rebound of ABS activity and a further strengthening of the US CMBS market
- Revenues in Origination and Advisory increased by 15%
- Equity Origination revenues were significantly higher driven by market share gains in a record fee pool environment
- Growth in Debt origination also reflected market share gains across both Investment Grade Debt and Leveraged Finance
- Advisory revenues were significantly lower against a strong prior year but in-line with industry performance
- Turning to the Private Bank on slide 17

Slide 17 - Private Bank

- The Private Bank reported a pre-tax loss of 4 million euros in the quarter
- Excluding specific revenue items, restructuring and severance expenses as well as transformation charges, profit before tax was 180 million euros, more than 50% higher than last year
- Revenues were flat as growth in volumes offset ongoing deposit margin compression and the negative impacts from COVID-19
- Both client activity and assets under management have further improved but remain below the pre-crisis levels
- The Private Bank made continued progress on its broader strategic initiatives, including the ongoing redesign of the distribution network and establishing strategic sales partnerships
- In the quarter we generated 115 million euros of German merger related cost synergies
- Noninterest expenses were broadly flat as reductions in adjusted costs were offset by higher restructuring charges
- The charges reflected further progress towards the head office and branch network optimization in Germany
- Adjusted costs excluding transformation charges declined by 10%
- Non-compensation costs declined in part driven by lower internal service cost allocations
- Compensation costs were also lower reflecting reductions in the workforce
- Provision for credit losses was 174 million euros or 30 basis points of loans reflecting the macro-economic environment
- Turning to revenues by business area on slide 18

Slide 18 - Q3 Private Bank revenue performance

- Revenues in Private Bank Germany increased by 1%
- Growth in lending revenues, higher fee income from investment products and higher episodic insurance revenues offset the ongoing deposit margin compression and COVID-19 impacts
- Business growth continued with 3 billion euros of net new client loans and 1 billion of net inflows in investment products in the quarter
- This quarter we implemented the new management and reporting structure for the International Private Bank

- This division combines Wealth Management and the former Private & Commercial Business International
- Revenues in the International Private Bank declined by 1% excluding workout activities related to the Sal. Oppenheim franchise
- The International Private Bank continued to grow volumes with 2 billion euros of net new client loans and 2 billion euros of net inflows in investment products
- The revenues for the two sub-business within the International Private Bank are reported in the Financial Data Supplement
- International Private Banking and Wealth Management combines the former Wealth Management segment with our wealthy international clients
- Revenues in this client segment were essentially flat excluding specific items and headwinds from foreign exchange translation
- Volume growth, reflecting targeted hiring, broadly offset deposit margin compression and COVID-19 effects on average assets under management
- International Personal Banking principally serves retail and affluent customers in our target markets
- Revenues in International Personal Banking declined by 1%, as continued deposit margin compression and the negative impacts of COVID-19 were broadly offset by a valuation adjustment on an investment

Slide 19 - Asset Management

- Asset Management continued to perform well as you can see on slide 19
- To remind you, the Asset Management segment includes certain items that are not part of the DWS stand-alone financials
- Asset Management pre-tax profit of 163 million euros, increased by 56% driven by both cost reductions and higher revenues
- The Asset Management divisional cost income ratio improved by 12 percentage points to 63% compared to 62% at the DWS level
- DWS is on track to achieve all targets set at the IPO
- Revenues grew by 4% principally reflecting a positive impact from the change in fair value of guarantees and lower funding cost allocations
- Compared to the prior quarter, revenues grew by 3% on higher management fees given the increase in average assets under management
- Noninterest expenses declined by 12% with adjusted costs excluding transformation charges down by 11%

- The reduction in costs was driven by ongoing efficiency initiatives, lower transaction costs as well as the absence of write-downs on buildings and leases recorded in Q3 2019
- Net inflows were 11 billion euros in the quarter while assets under management increased by 14 billion euros to 759 billion, within 1% of year-end 2019 levels

Slide 20 – Corporate & Other

- Corporate & Other reported a pre-tax loss of 396 million euros in the quarter, as shown on slide 20
- The loss included 179 million euros of valuation and timing differences
- These differences principally relate to mark to market movements on swaps the group uses to mitigate the interest rate and cross currency risks from funding activities
- The negative impact of Other items also increased, due in part to certain real estate transformation charges as we accelerate our New York real estate footprint rationalization
- It was also impacted by higher than planned infrastructure costs, that have not been charged to business divisions
- Turning to the Capital Release Unit on slide 21

Slide 21 – Capital Release Unit

- The Capital Release Unit recorded negative revenues of 36 million euros
- Revenues were driven by de-risking, hedging and funding costs partly offset by the Prime Finance cost recovery and positive effects from valuation adjustments
- Non-interest expenses in the third quarter were 50% lower, in part reflecting lower restructuring & severance, lower transformation charges and reduced litigation costs
- Adjusted costs excluding transformation charges declined by 40%
- The decline was driven by lower internal service cost allocations as well as a reduction in compensation and non-compensation costs including professional service fees, market data, and other employee driven spend
- Risk weighted assets declined by 3 billion euros in the quarter to 39 billion euros compared to the 38 billion euro target for year-end
- Leverage exposure declined by 12 billion euros or 12% in the quarter

- Consistent with our prior guidance, we expect leverage exposure to continue to decline by 10 to 15 billion euros in the coming periods, subject to market movements
- For both RWA and leverage exposure our 2022 targets remain unchanged

Slide 22 – On track to reach near-term objectives

- As Christian highlighted, we have continued to navigate successfully through the challenging environment
- The progress that we have made in the first nine months of the year puts us on a good path to reach our 2020 financial milestones which are shown on slide 22
- We have updated the outlook statements in the earnings report to reflect our current expectations
- Our group revenue expectations are now marginally higher than our prior outlook primarily reflecting the stronger than expected performance in the first nine months
- Our current planning assumes a normalization of investment banking revenue performance in the fourth quarter compared to earlier in the year
- We expect relatively stable performance in our other core businesses sequentially
- Revenue in the Capital Release Unit is also forecast to return to the range that we outlined at the Investor Deep Dive of between negative 100 to 250 million euros
- We remain on track to reach our 19.5 billion euro adjusted cost target excluding transformation charges and the impact of the Prime Finance transfer
- We have previously guided to deferred tax asset valuation adjustments of 400 million euros for the full year
- Based on our improved profitability and outlook, we now expect this tax item to be 100 million euros for the full year, of which we have taken 25 million in the first nine months
- The improved outlook on DTA should be partly offset by higher restructuring and severance as we work to accelerate as much as possible of our transformation
- Provisions for credit losses in the fourth quarter are likely to be similar to the third quarter level, consistent with our guidance for the full year
- We will continue to manage our CET1 ratio conservatively and we expect to remain well above our 12.5% long-term target

- Our strong CET1 ratio in the third quarter provides sufficient headroom to absorb the likely regulatory inflation and to support clients as they navigate the pandemic
- These are themes that we will address in detail at our next Investor Deep Dive on Wednesday December 9th
- With that, let us take your questions

Question and answer session

To follow