Presentation

Operator: Ladies and gentlemen, welcome to Al Rajhi Bank's Second Quarter 2019 earnings call. I'll now hand over to your host Mr. Amr Sager, Investor Relations Director. Sir, please go ahead.

Amr Sager, Head IR

Hello everyone. It gives us great pleasure to welcome you to Al Rajhi Bank's earnings call and webcast with management to present second quarter 2019 results. You can download a copy of the presentation from the webcast link. Financial statements and material will be available on our website early next week.

With us today are

- **CEO, Stefano Bertamini**
- **CFO, Abdullah Alkhalifa**

We will start with Stefano who will give an update on the business performance and the progress we have made on our 2020 strategy and then Abdullah will provide details on the financial results. We then will open the call for Q&A. Let's start. Steve, over to you.

Stefano Bertamini, CEO

If you turn to the management summary page, we want to share with you highlights from 2019. In terms of the strategy, things remain on track and we continue to deliver a strong financial performance. We're continuing to see very good growth in mortgages. And also as you saw, we continue to expand our net profit margins. We also continue to further improve our customer service, digitalization offers, and new products. We also expect to see continued growth for the balance of this year. In terms of the operating results, which Abdullah will go into more details, during H1, we saw growth of 16.2% net income before zakat, which again, you'll hear a bit more as to zakat change that took place this year. Also which I'm sure will be a question down the track, we did have some one-offs during the second quarter. If you normalize for the one-offs, we would have been up around close to 20% in net income before zakat.

We continue to see very good improvement in yields, continue to do a good job from an operational efficiency perspective, cost of risk remains flat and we're seeing good profit growth across all three engines, retail, corporate, and treasury. We also had a good second quarter. In terms of balance sheet, we are at an all-time high in terms of non-profit bearing deposits. We remain very well capitalized and maintain very high coverage ratios. We did have very good loan growth compared to last year. Year on year retail was up 5.1%. And corporate was up 5.8%. In terms of the market data that we saw from SAMA, year to date, the market's grown 2.3% in terms of our loan growth and we're up by 3.1%, we're trending above the market.

If I could now turn your attention to the strategic overview. Most of you have been through this but just for some newcomers, we've been running a five-point strategy that we call "ABCDE" since second half of 2015. The strategy was put in place to address five issues that we faced at the time. First is we had been underperforming in the market in terms of financials and we have seen a decline in market shares. We had low employee engagement, our customer service was poor, we under invested in digital, and our execution also could have been improved. Therefore, we got together as a management team and put in what we call our "ABCDE" strategy.

A stands for accelerate growth, with the goal of exceeding the industry, which I believe we've shown consistently we've done over the last four years. And one of those key pillars has been to grow our mortgage book, to enhance our SME and corporate capabilities and off course, treasury. Also, to improve our yields we've continued to do consistently.

B which stands for become employer of choice, our goal here was to have higher engagement. As you can see here, we've continued to engage our workforce. I've just received some preliminary results from our employee survey and it looks like we've improved again over the last year. We've also materially enhanced our training and development programs.

C for Customer Focus, We've done a lot of work around customer focus, which I'll highlight a bit more in the next page.

D is for Digital Leadership; we're now leading in digital on many fronts. And we may do a more full update of this during our 3Q call. These efforts are being led by our deputy CEO, Waleed Al Mogbel, and we'll ask him to join the call next time around.

E stand for Execution Excellence, also we continue to do a very good job as seen by our performance.

If I then take the more general themes into some specific areas that show our progress, I'm now turning to the strategy updates on page 4 of the deck.

A ccelerated Growth, You can see the strong growth we've had in operating income year on year. We've also grown our mortgage book by 39%. If you go to the visual below, you that we've effectively doubled the size of our mortgage book from 2015. Also during that period, our market share has increased from 20.6% at the end of December 2015, to 29.1% as of 1Q 2019. We've also continued to grow our current accounts which are up 9% year on year, and very good continued expansion in our profit margins.

B ecome Employer of Choice, in terms of employer of choice, the additional comment I can provide is we continue to expand our leadership programs. I think I mentioned during the last call, we launched a female graduate program. We've also now launched an IT program and more recently, a security program as well. We also continue to make very good progress in terms of increasing the mix of females in the business. And we continue to increase the number of volunteering hours that we do year on year.

C ustomer Focus, On the customer focus area, what I'm proudest of, literally found out about this about four days ago is that we've now achieved the number one position on Net Promoter Score. You recall when we first started we were number seven in the country, it's taken us three and a half years but as of the second quarter, we're now in the top position.

D igital Leadership, We've made tremendous progress, we continue to invest in our point of sale infrastructure. We now have 25% share of units in the market and a volume of 22%, which is up 200 basis points since the end of last year. We've also added 1 million active digital users during this year alone. This month, we actually added over 130,000 active customers, which is the highest single month increase we've had, so it shows you momentum continues. When we talk about the mix of manual to digital, we actually achieved our December 2020 target as of the first half of this year, and we'll continue to see progress in the mix of business.

E xecution Excellence, as we've talked about before, continued investment in enhancing our efficiency. Many of investment continues in the IT area to improve resilience and also enhance our systems, whether it be treasury, lending systems, etc. You can see that the number of transactions that we service per month continues to increase. Just since December of last year, we're up over 25 million transactions per month. And with that, I'll turn it over to Abdullah to take you through the financials in a bit more detail.

Abdullah Alkhalifa,CFO

Good afternoon everyone. Thank you again for taking the time to dial in for our earnings call for the second quarter 2019. before I start talking about the performance of the bank in the first half this year, I want to first spend some time on the material change that happened this quarter as far as the treatment of zakat. zakat in banks and also insurance companies, these two sectors which are supervised by SAMA, has always been treated as an item of the shareholders' equity including Q1 this year. However, in July we received a letter from our regulator saying that we should start this quarter to treat zakat as a P&L item just as all other sectors in the Saudi Stock Exchange. Therefore, we included this in H1 results. That's why you see that for the first time banks are announcing results after zakat.

I want to give you heads up because once we publish our Q4 results 2019, as you recall, there had been a settlement for zakat in Q4 2018. That settlement as part of the treatment to P&L, will have to be recycled to our income statement in Q4 2018. Therefore, just to let you know so you won't be taken by surprise the settlement of 5.4 billion will come as a P&L item in 2018.

The income for H1 before zakat has continued on a strong growth 16.2%. we had some one-offs and if we neutralize the effect would have been closer to 20%. We've also announced first half dividends of 1.5 riyals, that represent a 15% increase over last year. It is in line with what we keep telling investors in different meetings that you should expect 60 to 70 pay-out ratio. If you calculate that before zakat, it's 65%, and after zakat it's 72% pay-out ratio.

the change in net income after Zakat from the first half last year of 4.8b to 5.2b this year, you'll find there's a big item which is zakat, 404 million. In quarter four last year, part of the terms of the settlement decides what is the zakat charge for 2018 in Q4. We've been accruing up to the first nine months of the year in 2018 zakat as per our Shariah calculation. That's why you see the big difference between the first half this year and last year when it comes to zakat. Nothing changes effectively, both are close to 10%, last year effectively about 9%, this year is 10%. But that change only happened in Q4. So in Q4 2018, not only the settlement but the catch up for the zakat. We have over 760 million that came in Q4 for 2018 zakat.

performance of operating income of 12.7% growth is driven mainly by the growth of yield income. Compared to the same period last year, we picked up 65 basis points in our net profit margins. Our average earning asset is up by 4%, this improvement in net profit margins is driven by different factors. One of them is the very strong growth on mortgage business, year on year is 39%. And as you know, we mentioned in previous earnings calls that currently mortgage business is yielding higher than other retail products, except obviously revolving credit card. Also we have a very strong growth on current accounts 9% year on year. Even if you look at year to date, the growth in current accounts is 6.1%. That's double the growth that we've seen in the market overall, which is 3%. So we've doubled the growth of the market.

cost-to-income is 31.3%, and our guidance is below 31%. We had one-offs, otherwise would be similar to the first quarter of this year. Compared to last year, our net profit margins picked up 45 basis points in the first half compared to the full year last year.

The next slide shows you the trends of total operating income quarter by quarter as well as income before zakat. Slide 8 shows the Zakat effect for Q4 2018 because both the settlement amount of 5.4 billion as well as the catch up on the zakat. That's why I'm giving you the comparison here. If you look at ROE, as previously reported is 19.8% for 2018. However, if you do actually recycle the settlement amount to 5.4 and the catch up of the zakat, that ROE will drop to 7.6% roughly. Similar for the ROA on the next chart, you'll find that it drops from 2.9% to 1.1% in 2018 after adjusting for the settlement and the change in zakat methodology or calculations are releasing.

If I then direct your attention to page 9, we actually have now 97% of our customer deposits that are non-interest bearing deposits. As I mentioned 9% solid current accounts growth year on year. Financing this year is very promising, as we already witnessed year on year 5.3%. This is driven by both corporate and retail, both have witnessed good growth this year. On the capital adequacy, you'll find that obviously because of the settlement, we dropped from 22% down to 20.5%.

On page 10, we mentioned twice so far the one-offs, I believe this came with the news about VAT. There has been a change in regulation or a clarification on the VAT that came out late Q1. And a series of workshops were held with the tax authority. It was clear that banks have to pay VAT on home loans, even the ones below SAR 850K which was supposed to be excluded. As a result, banks have to adjust because we have adjusted our numbers, and of course that attracted a penalty on the late payments as well as we had also some penalties from SAMA. If we exclude those one offs as well as more other one-offs also, our growth in operating expenses would have been only 3.7%. These are shown under the bottom right chart; you find that they are all coming from other G&A expenses.

On asset quality we see improvements. Last year Q1 NPL ratio was 0.94%. It's gone down as improvement in corporate, down to 0.85%. Our coverage ratio picked up slightly from 342% at end of last year to 353%. Capitalization is obviously strong despite the zakat settlement. Risk-weighted assets have seen some growth because of the growth on the corporate and retail loans.

Going through the guidance now, we have 3 changes there. We're maintaining the guidance on the financing as year to date we had 2.9% growth on loans. We we will keep and our guidance to be mid-single digits. As far as the net profit margin, we upgraded that. Initially, we gave 25 to 30 basis point, now we've increased this to 30 to 40 basis points. We already have six months past and I mentioned we already picked up 45 basis points of it, it came in the news Wednesday July 31st as expected, the Federal Reserve has cut the rates by 25 basis points. But as you recall, most of our assets in retail are fixed rate, so it will not be majorly impacted as the long term for repricing. In terms of cost-to-income, we're still maintaining our guidance to be below 31%.

Cost of risk is changed from 55-65 basis points to 60-70 basis points, we slightly increase that because we've been close to the top end of previous guidance but we are not expecting any deterioration. The other change is ROE, as we mentioned before, zakat now is a P&L item, so we adjusted zakat and amended the guidance from above 22% to above 21%.

Question and Answer Session

Our first question is from Naresh Bilandani from JP Morgan. Please go ahead.

Naresh Bilandani

It's Naresh from JPMorgan. Congrats on the Q2 results. Just a few quick questions please. The first one is around mortgages and NIMS. Now, while you kindly explained the dynamics of the net profit margins in the previous calls, can you kindly shed some light on how much further upside do you see from here doing that, you've already delivered a widening, which is above your guidance year to date? I'm just keen to understand if we do get another rate cut from the U.S. and I know it's a bit confusing after the Fed's comments overnight, but how should we expect to see the net profit margins trend given your unique pricing dynamics into the second half of the year. Also, alongside the NIM, it would be very helpful if you kindly throw some light on the mortgage pricing in the recent months as the market reference rates have declined. And I know the mortgages are not directly linked to the SAIBOR in most cases. But this is a product where every bank is trying to get ahead. So, will much appreciate it if you can throw some light on the state of the industry here. So that's the first set of questions on the NIM and as well as on the mortgages.

My second question is generally on asset quality. Now, we have in the news again, one of the top contractors in the country looking to restructure their liabilities. So could you please comment on whether in your view this offers risk of a fresh bout of provisioning across the industry? Or do you think banks are likely to have provisions for this exposure in some form already? Now, I appreciate Al Rajhi' s building and construction book is quite small. So you may not have much to worry about with your peers. But I'm just keen to hear thoughts on the extent to which this could become a broader industry wide issue. So any thoughts will be appreciated. Thanks.

Abdullah Alkhalifa
Naresh, thanks for the questions. Obviously, as we mentioned before, growth in the mortgage is very supportive to net profit margins expansion. Because as I mentioned before, it's higher yielding assets compared to personal finance for example. Yes, I know the competition is heating up, but so for our growth is very strong, as we mentioned, 39% growth year on year. We're not witnessing slow down on the growth that would lead us to amend our prices. But eventually, we will see some reduction in prices, unlikely this year. I'm not saying that it's sustainable, but I don't think there's going to be major change this year for that business. So it's very supportive of net profit margins expansion. Don't forget also, Naresh, we had 9% growth year on year on current accounts. That's also very supportive of net profit margins expansion.

Stefano Bertamini
So just to add to that, before talking about asset quality, as I think we've mentioned in prior calls, as long as we don't see any sustained deterioration in our market share or market share growth, there's also no reason for us to get concerned about pricing, on margins. As I shared at the beginning, we continue to increase our market share and expect we'll be above 30% by the end of this year, and we think if we can stabilize around the third, that's probably the right place to be. In terms of asset quality, the book remains very solid. You're going to have problems in companies from time to time, happens to be this is the latest one. I think most of this has been processed by the industry pretty substantially. As you are aware, most banks are extremely well capitalized .

So I don't think this is a major trend, especially as you're aware, IMF recently upgraded the GDP growth rate for Saudi. So for this year, they increased it to 1.9 from 1.7. And for next year, it's been upgraded from 2.1% to 3%. So I think that implies even in construction, demand will begin to pick up. I also read somewhere actually, for the first time in a while, the number of expats increased during the first quarter. So I think as the momentum begins to build on some of these long awaited government projects, that should be a positive for the industry and ultimately for asset quality over time if anyone has an issue.

Abdullah Alkhalifa

Another supportive indication that we're seeing recently is the amount of Letter of Credits (LC) open this year and that's up year on year by 13.7%, which tells you there's more and more activities on construction also.

Naresh Bilandani

Great. So just quick follow ups on those. So thanks for the statements. First on the margins. So given the fact that okay, we've seen a 45 bps widening already in the first half and your guidance assumes that we could see some level of flotations coming in the second half of the year. Will this to a large extend be driven by the non-retail or the corporate portion of your book, which I guess is a 30 odd percent at this stage. Is that a fair assumption to make? That's first. And on the asset quality, just as a quick follow up, could you share your thoughts on how standardized and comparable these ECL models are across a different banks. Have these been audited by SIMAH for all banks. So, in effect the stage two or stage three loans of say Al Rajhi, would these be comparable to other banks in any form?

Abdullah Alkhalifa

Well, on the first part, obviously, the flatness of net profit margins or slowdown of growth of net profit margins or maybe a reduction of net profit margins, that obviously comes from the wholesale, because wholesale is usually linked to the benchmark. So when SAIBOR goes down, obviously, most of the corporate assets or treasury assets, of course we'll get the price lower. For retail is predominantly fixed rate lending. As far as the stage two or stage one. I think we tend to be more proactive in moving exposure from one stage to another than maybe other competitors are.

But we tend to be conservative. Even in our internal rating, which obviously drives the provision because internal rating is linked to probability of defaults. and clearly you can see our coverage ratio, our provisions percentage of gross loans, we've always seem to be very conservative.

Naresh Bilandani

Certainly. Thank you very much for your replies. Much appreciated.

Operator

Our next question is from Neri Tollardo from Morgan Stanley

Neri Tollardo

Yes, thank you very much for the call. I got two questions, please. One, I just want to make sure that I understand the zakat treatment correctly. So did I understand correctly that when you report full year 19 results, the full year 18 results in the income statement will be restated by the 5.4 billion hit that you've already taken to equity, but also a top up in zakat for the first three months of 2019 and the first nine months of 2018. And if that is correct, what is the extra amount on top of the 5.4 billion, and whether including that would have any impact on your capital ratios? And then the second question is on pay-out ratios because as far as I'm aware, the central bank puts a limitation on the pay-out ratios for Saudi banks at 75% of reported net income. Did that change now that your reported net income is post zakat and anything on your pay-out ratio going forward? Thank you.

Abdullah Ali Alkhalifa

Thanks, Neri. On zakat, yes, you're correct. We will recycle the settlement as well as the catch up on the zakat as I mentioned. If you look at the full year 2018, the zakat charge was 992 million. We've been accruing zakat for the first nine months on our own methodology. That methodology changed in Q4 2018 and we had to basically accrue for 764 million. This is all going to be a P&L as well as the settlement. It'll be treated as an income statements. Pay-out ratio, I have been in the bank for so long. I'm not aware of any ceiling from our regulator, as far as the pay-out ratio. Of course, all the dividend announcement that we do is obviously after the approval of SAMA.

Neri Tollardo

Sorry, just to follow up on that, so 764 million extra that you need to provide for, for the first nine months of 2018. Is that already reflected in your capital? And on the pay-out ratio, I was just under the impression that 25% of net profit needs to go into statutory reserves and that's why I said the 75% ceiling. But is that still the case?

Abdullah Ali Alkhalifa

Yes, you're right. You're referring to setting 25% to statutory reserves, but you have to realize that is after zakat. Therefore, if zakat is 10% and then you take the 25%, that effectively becomes 22%. So 22% plus 10%, which means 32% is not available for distribution, the rest is. The zakat as we said, if you look at last year financial was 992 million. What we accrued for the first nine months was only 288 million and the difference came in Q4 2018. So it's not additional zakat. It's zakat that's already been accrued last year. It will just be treated as a P&L item as well as the settlement has to be recycled for income statements.

Operator

Next question is from Hootan Yazhari from Bank of America Merrill Lynch. Please go ahead.

Hootan Yazhari

Thank you, gentlemen. I have a couple of questions, please. Firstly, on the corporate loan market, have you started to see activity levels there picking up yet, given that there was a well flagged and widely expected rate cut coming. Have you seen corporate sitting on the side-lines waiting for greater clarity before they get engaged? And is there a bigger pipeline developing in the second half? Or do you expect similar sort of levels as the first half as your guidance for asset growth would suggest? The second question is really regarding your digital strategy. How much you've been investing there, whether you feel the current rate of investment is sufficient to achieve your goals, or whether you think this needs to intensify that. Your thoughts on those two matters would be greatly appreciated.

Stefano Bertamini

Okay. Thanks for your questions. In terms of the corporate loan market, I'd say it's better than last year, but it hasn't really picked up as much as we'd like to see. What's happening is the high quality corporates are seeing a lot of competition from banks. And we continue to see very tight margins. We continue to be quite selective in terms of where we choose to deploy our capital, particularly in thinly priced corporate deals. I think that may begin to improve a bit during the second half, we are seeing a lot more requests, particularly from our structured finance team. We've actually added resources there for the first time, certainly since I've been in the bank. So I think things are beginning to pick up. Whether that necessarily comes through second half of the year, now it's a bit early to call, but so far, it's a good improvement on last year, the fact that we're up over 5% year on year is also positive.

In terms of digital strategy, we have been investing steadily on this from day one, we have intensified our efforts. But that doesn't necessarily translate to materially higher levels of spend. Because we can only put so much through our IT infrastructure in any one year. And obviously, we have a lot of other things that we need to do to ensure that it remains robust and fit for purpose given the kind of volumes that we're seeing. So we believe that we're in good shape on digital, we've accelerated the amount of innovation that we've done in terms of features, products. and we continue to see extremely strong growth.

So, we believe we're on track but as you know, digital is a fast changing environment and we'll continue to monitor.; and if we think that needs to change at some stage, we'll communicate that which I think may be a result of our next strategic review, which we'll have with the board in October where we start talking about 2025 and we'll give you a heads up at that time if something changes as a result.

Operator
Our next question is from Rahul Bajaj from Citibank. Please go ahead.

Rahul Bajaj

Hi, thanks for taking my question. I have two quick questions, actually. The first one relates to the one-offs that you mentioned, which impacted the cost line, so the VAT arrangement and the other one-off. I just wanted to understand, is this additional cost in any way, you're seeing impacting growth for those products? So for example, the mortgage VAT, who bears that cost and is that a cost from consumer and how does that impact growth? The second question is, coming back to zakat because it's slightly getting technical here. So to my understanding, and please correct me if I'm wrong. To my understanding, in the fourth quarter of last year, you already moved your reserves, as in made provisions in your liabilities out of your equity. So, you already kind of provisioned for it and you paid some 20% in 2018, the rest would be paid over next five instalments over five years. So, what happens in fourth quarter of 19 for the 2019 number? Will we see kind of a part of settlement going to the income statement in fourth quarter of 19 as well? Thank you.

Abdullah Ali Alkhalifa

As far as the one offs, as I mentioned before, the bulk of that amount came from the VAT and I explained the background. Banks were under the impression that mortgages given for amount less than 850 million are not subject to VAT. That was clarified and if you recall, the VAT regulation came in effect at the beginning of 2018. Only this year, they came out with the clarification. Following the workshops, it was clear to banks that banks are supposed to pay VAT on all the amounts, all the loans given from the beginning of 2018. And that's why we had to amend it, so that's why it's one-off because it's not something we expect going forward to bear that cost on an ongoing basis. And we don't expect that this will lead to any damping of the demand of housing because of VAT.

For the zakat, you're right, there's no impact on equity. I believe I forgot to answer the questions about the zakat impacting equity. The amount of 5.4 billion was allocated in equity and was transferred to other liability at the end of 2018. Now, when we recycle the 5.4 as a P&L item, we'll have to put back the 5.4 in equity. Therefore, the net net has no impact on equity and no impact on capital adequacy.

Operator

Our next question is from Edmond Christo from Bloomberg Intelligence. Please go ahead.

Edmond Christo
I think most of my question has been asked, but I will go back to the first question which is on mortgage yield. I think we talked about 6 to 8%. We see the real estate refinance companies lowering the rate now on long term fixed mortgages. Also they are providing cheaper source of funding to mortgage finance company. I think your comment that we will not see it this year, we'll see it next year. So I think the point to make here is how you're managing the cost on mortgage origination. The other question is; can you give me some update on retail Sukuks markets? And do you see any impact coming on your deposit in the medium-term? Thank you.

Stefano Bertamini
In terms of mortgage yields, we really haven't seen any impact so far from new products in the market or competition. The benchmark that we use is market share. So until we see any impact of slow down or deterioration in market share, we're really not making any adjustments. Obviously, as Abdullah also mentioned, the fact that we continue to see strong growth in current accounts effectively also gives us ability to protect our net profit margins, even if at some point in the future, we have to make some adjustments. The mortgage pricing varies by tenure, by income level, by ministry, etc. So it isn't as simple as, pick a rate and assume that's the right one. it's quite a complex pricing grid.

Abdullah Alkhalifa
Retail Sukuks is obviously the change in the Sukuks which to bring the minimum amount of 1000 riyals. We haven't seen any impact on it. I don't think there's a runoff from our retail to invest in Sukuk. As I mentioned to you, we had a very strong growth on current accounts. Year to date, 6.1%, double that of the market growth.

Operator

Our next question is from Chiro Ghosh from SICO. Please go ahead.

Chiro Ghosh

Yeah, most of my question has been answered, just one quick one is about the mortgage loan. What percent of your mortgage loan is backed by REDF and if you can throw some color just to get us to get a sense of the asset quality of those loans.

Stefano Bertamini

We don't give specific information on that. But I can tell you that a lot of the growth that we've seen this year has been primarily through government backed programs, which is obviously different from what we saw in the past. We also happen to have record mortgage volume this last month. We continue to see strong growth, a lot of it is coming from the government, but over time as that changes, we'll be happy to update.

Chiro Ghosh

And so these loans are backed by the government or it's like a salary account and hence you feel safe, and the mortgage rate for the first five years is fix rated on if you take a 20-year loan for 20 years it's fix rated?

Stefano Bertamini

There's approximately 14 different programs at least, so it says not a binary a simple yes, . And by the way, we obviously underwrite every loan. So it isn't just because a name comes, that you write the loan. On some of them, the government is providing assistance with a down payment. On others, it's on the principal. On others, it's a different type of subsidy. So it's relatively wide based, these are all salary assigned, as well. We also have the real estate as collateral. The average mortgage tends to be around 620 thousand SAR. These are entry level homes and a very wide exposure across all the major cities. We don't see any material concern. Our retail portfolio loan losses remains exceedingly low and mortgages even well below the retailrun rate. The fixed rate mortgages are fixed for the entire term of the loan.

Operator

Our next question is from Vikram Vishwanathan, from NBK Capital. Please go ahead.

Vikram Vishwanathan

Yes, thank you for the call. In terms of margins, given that the SAIBOR has been declining through the year, would it be possible to give some sense of how the margins will look like in 2020?

Abdullah Alkhalifa

No, the guidance we give is for this year. following Q4 results this year we'll give guidance for 2020.

Operator

Our next question is from Sayed Avi from Avinma Invest. Please go ahead.

Sayed Avi

Hi, gentlemen, this is Sayed Avi from Avinma Invest. My question is regarding the mortgage portfolio. Obviously, you've been in the past before this boom came in, the focus was in consumer finance, specifically or primarily the government employees. Given the current balance sheet leverage, loan deposit ratio, given the current conditions, how would you be able to grow the mortgage portfolio without actually displacing your current, you know, customer base, which is essentially government employees or consumer finance, portfolio. How much of that growth would come at the expense of this and how much of the growth will just come in as a result of increasing leverage on the balance sheet?

Stefano Bertamini

There are some recent changes made on debt burden ratio by the regulator, which were designed to encourage customers to borrow for a home as opposed to other types of borrowing. And we've seen in our portfolio, lower growth rate, for example, in personal loans and much higher growth rate in line with what the government is trying to achieve in mortgage. From a balance sheet leverage perspective, we can easily double the size of our book and that's not going to have any impact on our ability to grow our corporate book, ability to support SME, ability to grow other products within retail portfolio. So, at this stage, we don't see any impact on our ability to continue to support the kind of growth rates we've seen so far.

Operator

Our next question is from Adnan Farooq from Jadwa Investments. Please go ahead.

Adnan Farooq

Thank you for the call. I have a couple of questions. What percentage of your investment book is fixed rated as opposed to floating rate? And the second question is, would it be fair to say that given mortgages grew 39% year on year, the rest of your retail portfolio is fairly flat or even declining? And can you mention what percentage of your retail book is mortgages now?

Abdullah Alkhalifa

Let me answer the last question first. Mortgage represent now 24% of our retail portfolio. Now, as far as the breakdown of fixed versus floating in our investment portfolio we do have both however the majority is floating investments such as 22 billion of sukuk. We also have some Sukuks from corporates and banks, that are floating. The rest is fixed rates.

Operator

Our next question is from Noman Khan from NCB Capital. People go head.

Noman Khan

Hello. First of all, congratulations for your excellent results again, I think you have been outperforming the market for quite some time now. Just wanted to have a quick question. I think it is a follow up question from what you have already answered as you said. The total book of mortgage is about 24% of retail. Is it a target ceiling that you're looking at for the mortgage loan as a percentage of the overall book size to be very honest? Because if I'm correct, it could possibly lead to a majority mismatch between your assets and liabilities. So is there any target ceiling that you're looking for, for mortgage as part of the total per loan portfolio?

Stefano Bertamini

The short answer is we don't have a target ceiling at this stage. If you look at most banks globally, particularly retail banks, normally mortgage is at least half of the retail book. So I think over time, you can certainly see that happen here in Saudi but again, we have no internal cap at this stage and, we'll obviously look at that when it becomes an issue that we need to consider.

Abdullah Alkhalifa

As far as the mismatch of asset liability that's obviously always been a feature of the Saudi banking system. I know we're expanding now as banks in general, expanding in the longer duration assets, such as the mortgage. But if you recall, we've always had short term funding financing long term assets. For us, as always, it's very important to realize how sticky our current accounts. Current accounts are very sticky and actually growing year on year. So this is providing us zero funding cost as far as financing these assets. We haven't tapped into the capital market; and if we see a need for it, we can definitely issue fixed rates for longer duration liabilities.

Noman Khan
My last question again, would be if you can guide about overall loan growth that you are looking for industry and what are you looking at? What your loan growth target is? And apart from mortgage, do you think any other product is showing any signs of recovery apart from mortgage in the retail side.

Stefano Bertamini
We've already given guidance on loan growth, which is mid-single digits. We're seeing, for example, very strong growth in cards. Card business continues to do well. We're seeing good growth also in the mix of business coming from our E channels. Corporate book, as we mentioned is growing, treasury is doing a good job. So the only thing that we've seen really flat to down is auto. That's been the one sector that's been somewhat impacted. Everything else I think remains fairly steady and obviously mortgage being the stand out growth driver right now.

Operator
Our next question comes from Karim Kehiah from Arqaam Capital. Please go ahead.

Karim Kekiah
The Responsible Lending criteria, which was implemented last year, do you think that basically, the strong growth in mortgages could come at the expense of lower loan growth and auto loans and personal loans going into basically once DBR start to increase or not necessarily, or is this not being enforced at all?

Stefano Bertamini
No, it's being enforced and has definitely had an impact. This is something we've seen happening since the changes were made. Also, auto sales overall, are down quite a bit. I believe the last number I saw was around 26%,; so auto sales are down to begin with. The DBR makes the financing more challenging, so less people are eligible. So they tend to, for

example, move to a lower value car. And we're seeing, low single digit growth in consumer lending, which is pretty much in line with usually a bit higher than GDP.

Operator
Our next question comes from Waleed Mohsin from Goldman Sachs. Please go ahead.

Waleed Mohsin
Yes. Hi, good afternoon, good evening. Thank you so much for the presentation. Waleed here from Goldman Sachs. Three questions from my side. The first question is regarding to asset quality. I was wondering if you could provide some details around stage two exposures that you have which are sitting at 8%. I just wanted to get a little bit of color on stage two exposures. And have you recently seen the migration from stage two to stage three? And then again, migration from stage one to stage two. Just want to get a sense of how much of this is corporate, I presume it's mostly stage two. So a lot of this would be corporate, just interested in the sectors. That's question one.

Secondly, in terms of the substantial growth in mortgages, obviously, Al Rajhi continues its market leadership. And we've also seen the rest of the sector pick up. So, initially, when the total mortgages in the system were less than 10% of total lending, SAMA may have had a different view. I just wanted to get a sense that is it a push from the regulator, despite the fact that the cost of deposits is sticky. They are contractually short term but from a behavior perspective, they're longer term. Is it a push from the regulator for banks to explore other avenues of funding mortgages? Whether it's through bonds or actually, in terms of when SAMA thinks about capital, are they requiring banks to maintain a higher level of equity so that as a backstop, you have ample long term sticky funding to take care of the substantial growth which has come to mortgages. And last question in terms of the savings product, where are you with your savings product? What stage are you and what are your expectations regarding the savings deposit product? Thank you.

Stefano Bertamini

I'll take the last two and Abdullah will answer the first one. In terms of savings product, as of today, we don't have a savings product. We are expecting to launch one either late Q4, early Q1. We don't expect to see a material impact from that. Because culturally savings is still not something that has obtained the momentum , obviously the government and the regulator would like to see. But, y we will do our part. Interestingly, we did recently launch an employee savings scheme, which had a good take up. So I think you'll see savings being encouraged more by companies as opposed to necessarily depositors, particularly in a low rate environment. In terms of mortgage, no, there is no push from SAMA, certainly, that I'm aware of in terms of funding or mismatch or anything like that. There's no additional requirements on equity. I mean, we just went through ICAAP, ILAAP, we have no issues or concerns on that front.

Abdullah Alkhalifa

Waleed also on the staging, we actually do disclose this on the annual basis. I haven't seen in the first quarter or second quarter any change in trends as far as the migration between one stage to the other, that is something that we will disclose I believe on the annual financials. Basically no, there hasn't been a change on the migration from one stage to the other.

Operator

our last question comes from Mohamed Toumali from NCB Capital. Please go ahead.

Mohamed Toumali

Hi, good afternoon, gentlemen. And thanks for the call. My question is related to the securitization deal you signed with eXtra, which is one of its first kind in Saudi. My question is regarding the level of profitability of such deals for Al Rajhi, the priority, how big such markets would be for Al Rajhi, going forward in Saudi.

Stefano Bertamini

We launched our securitization product, I towards the beginning of last year, we started with some other portfolios. This is an interesting transaction. I think there's a market for it, but it's still early days. So I'm not expecting a huge growth in this in the short term. But it is something that obviously makes sense for us. It's very well structured, well priced. So we think this is a good product, but, I don't expect it to contribute materially, certainly, in the short term.

Conclusion

thank you very much all for your interest and continued support. We're very proud of the results that the bank delivered in both financial and non-financial terms and we remain confident in our ability to continue to deliver in 2019 and beyond. Thanks again, everyone. Have a nice weekend.
