

Transcription

Title: Swedbank Third Quarter Report 2018

Date: 23.10.2018

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Conference Ref. No: EV00079760

Duration: 48:28

Presentation

Gregori Karamouzis

Thank you and good morning everyone. And thank you for joining us on this call presenting Swedbank's third-quarter results. With me, I have our CEO, Birgitte Bonnesen; our CFO, Anders Karlsson; and our Chief Risk Officer, Helo Meigas. Before we run through the financials, I will hand over to Birgitte who will say a few words of our operations in the Baltics. Birgitte, please.

Birgitte Bonnesen

Good morning everyone and welcome to the call on the quarterly results. Before we dig into the results and I hand over to Anders, we have had a number of questions from many of you in the last couple of weeks on the Danske case and AML in the Baltics, so primarily in Estonia. For which reason, I thought that I would just give you a few facts to lead you through the topic, and then we'll go over to talk about essentials of the quarter.

Okay, first of all, I think the most thing is remember who we are. We are a big retail bank, we have four home markets, we cater for private individuals and corporates. We also have very large market shares in all the daily banking products, being it loans, saving products or payments. This is who we are; it's the same thing in all four countries.

And then when we move on to the next slide, this is where you see our number of non-resident customers. Before I start to go into more details around this and the deposits, I would like to remind you: what is a non-resident? A corporate non-resident is a corporate that is not incorporated in the country. It's all the entities that the Swedish corporates have in Estonia – they're all non-residents – entities where they have a setup in Latvia. We have some Swedish corporates that decided to set up a subsidiary in Latvia, and then they have an entity in Estonia; that entity is a non-resident. So there are many, many non-residents that come from our home countries, also from the other Baltic countries. And this is a really important thing to remember. All the embassies are corporate non-residents too, and ironically enough, Danske's branch in Estonia is a non-resident.

When you look at the private side, it's everybody who doesn't have a – or who has a foreign passport. Just in this room now, we have two persons with foreign passports in Sweden and we are theoretically non-residents in Sweden. This is the way it looks. In Estonia for one country, there are many, many students that come in every year and there are also a considerable number of migrant workers that we've seen coming in, in the past couple of years. And this is what you see when you look at the slide, you see the total non-resident, you see the corporate non-resident from outside of the EU, which is really, really low. Corporate non-residents has been low and stable over time in Swedbank, and then you see the private non-residents that have increased; it's actually primarily Lithuania. The same goes – it's more or less the same you see for Estonia. You see how it has developed over time and you see it picked up a bit in the last couple of years.

The other thing that we've got many questions on, and that – yeah, that I think that I need to go into, even though I don't think that it's an important element to understand AML – and that's about the deposits, the non-resident deposits. In Swedbank, the Baltic banking share of non-resident deposits is around 2.4% today. It's – when you look at the corporate non-resident deposits, today or currently it's below 1%. And when you go back in time, because this is a question that we've gotten a lot from 2007 until '15, I can say that it's been very stable around 5% Baltics. But in the contents of AML, a non-resident deposit is not the sort of – the important thing to look for; the important thing to look for is the actual transactions.

And on the next slide, you see what was published by the Estonian central bank yesterday. They published a document where they talked about how the FSA had worked with Danske, and how the FSA – you get a good impression from that document on how the FSA works. The quality of the FSA is high, in my opinion, and they are also very proactive. In this case now that they have sent together with the central bank, they have come out with the numbers, which I hope you will find helpful.

Here you see for Swedbank, you see that it's a very, very stable market share over time and it reflects the business, it reflects our market share of corporate banking business. And I can tell you that today, more than 80% – closer to 85% of the transaction flow is within our home markets, so that tells you something. Okay? Let's move on to the next.

This is sort of an add-on, and this is just to show you how we've developed over time. And what you see in – on the volumes, you see that the growth more or less reflects the development of the Estonian economy, which it should. And you know well that our ambition is to grow with the economy, and we have seen an increase in GDP over time over these past years – and in all of the Baltic countries, but also in Estonia in particular.

What I would like leave with you – the important message in this – is that apart from the fact that we have a systematic approach to assure detection of suspicious transactions and business activities, the important thing is we run a retail bank. We run a retail bank, we're focused on domestic business, domestic customers, serving the many – the many private individuals, the many corporates exactly as we do in Sweden, in Latvia and Lithuania.

The second thing is that on top of the fact that you need to develop your KYC constantly, you need to develop your systems and your processes. You know well that we are a low-risk bank, and this goes for this too. And I think that one of our strengths is that we are humble enough to realise that money laundering is something that is extremely complex. However much we do, we will never be able to detect everything ourselves. And this is why we work actively and reach out proactively to other banks – foreign banks as well as domestic – to the regulator, the police, etc. This is extremely important, and I sometimes get the question: do you think that you have everything in place to detect this? I think with the help from our friends and the proactive attitude that we have, I think we are in a really good shape.

But the third thing, and the most important thing, is the fact that every time we detect a laundering attempt, we act, and we act forcefully. We investigate, and if there are things we don't like, we act immediately.

So I will just close this part with these words, and then I will leave over to Anders to talk about a quarter where we deliver according to plan and that reflects the core business, which is really important to Swedbank. There you go, Anders.

Anders Karlsson

Thank you, Birgitte. As Birgitte mentioned, we are delivering another strong quarterly result. Income is supported by continued loan growth and strong net commission income, and underlying expenses are in line with our plan. All key financial metrics are solid with a return on equity of 16.9%. I will now walk you through the key P&L lines and sum it all up before I comment on our capital position, and then Helo will comment on our asset quality before we open up for questions.

Net interest income is higher quarter over quarter, loan growth in all our home markets of total SEK 11 billion contribute the most. Swedish mortgages continued to grow broadly in line with our back-book market shares, while we keep prices towards customers stable. Lending in the Baltics grew in euro terms and corporate lending increases moderately, both in Swedish Banking and LC&I. Margins are overall stable in the quarter. There is, again, a technical impact in Swedish mortgage and deposit margins of 1 to 2 basis points as market rates on average increased and prices towards customers remained stable; the effects cancel each other out.

Corporate margins were slightly higher this quarter, due to a few specific deals. The resolution fund fee is, this quarter, at its correct level amounting to SEK 440 million, but leads to a positive delta quarter over quarter, as we adjusted the booked fee up last quarter after having received the final level from the authorities. The resolution fund fee will next year be reduced to 9 basis points and reverse this year's increase of around SEK 450 million. An extra day in the quarter had a positive impact. Group Treasury's NNI is weaker this quarter as the short-term US dollar funding market conditions were less favourable compared to earlier in the year. And the covered bond buybacks contributed less as the bonds bought back have longer remaining maturity. This means that the NII benefit will come through over a longer period than usually, up until mid of 2020.

Over to net commission income, and yet another strong performance this quarter. Following on from very strong cards income development last quarter, mainly due to exceptional good weather condition, we see the usual seasonal effect in Q3, albeit somewhat smaller. In our asset management business, mutual fund inflows continued to be solid in all our home markets with around SEK 5.8 billion of net inflows in the quarter. Equity funds saw the largest inflows. Assets under management grew in total by SEK 34 billion, mainly due to positive asset value development, and were the main driver for increased income in the quarter.

Turning to net gains and losses and other income: despite the summer period we saw stable trading activity from clients, especially towards the end of August and in September. Credit and fixed income trading performed well, while equity trading was a bit weaker. In addition, a valuation effect in derivatives had a positive effect this quarter. In Group Treasury, however, larger covered bond buyback volumes this quarter compared to last quarter led to negative valuation effects. Also, as mentioned earlier when I commented – the movements in NII – the remaining maturity of the bonds was longer causing an even bigger negative impact, reminding you, however, that the buyback activity is income-neutral over time as the negative NGL is compensated by positive NII. In addition, somewhat widening credit spreads had negative valuation effects in our liquidity portfolio.

Looking at Group Treasury income in more detail for the full year of '18, we expect the combined NII and NGL to be a few SEK 100 million lower compared to '17, assuming that market rates, credit spreads, etc., are stable. The lower covered bond buyback activity and the continued unfavourable US dollar short-term funding conditions will lead to significantly lower NII, but somewhat higher NGL compared to last year.

When looking at other income and excluding last quarter's one-off capital gain from the sale of UC and this quarter's positive impact of SEK 180 million from changed valuation of the VISA Inc. shares, underlying business had a good development, especially the insurance business with higher premiums and lower claims. I would like to remind you that the income booked in this line is part of our core operations and has, throughout the years, demonstrated steady growth. It relates primarily to our insurance business, the credit card joint venture, Entercard, and other associates such as our part ownership in savings banks.

Now turning to expenses, which, underlying, are developing in line with our full-year guidance. This quarter, we have released SEK 200 million of the restructuring reserve we set aside in Q4 2017 to deal with the reorganisation of our IT and business development units. The benign external job markets and the fact that we have been able to match many of the involved competencies with other units' needs have led us being able to carry out the reorganisation at a significantly lower cost than anticipated. When we set our cost guidance for 2018 and '19 to be below SEK 17 billion, we had taken into account some unexpected volatility, for example, from FX and pension cost movements. Since then, however, the Swedish krona has depreciated by roughly 10% against most major currencies, relevant for us being euro, Norwegian krone and US dollars. If you assume stable FX rates from hereon, this will lead to approximately SEK 300 million of cost headwind in '18. It is, however, important not only to look at FX-related impacts from a cost perspective. As you know, Swedbank's income is sensitive to FX movement with a roughly 2x larger effect than the expenses. Hence, our shareholders have benefited from this development.

In addition to FX, inflation expectations and long-dated interest rates have both moved unfavourably with regards to our pension cost and has led to a headwind of around SEK 150 million in 2018. Looking at the expenses line isolated, these two headwinds combined will lead to roughly SEK 450 million of increased cost this year. Underlying cost development has, however, been according to plan. And as we intend to cope with the headwinds, we reiterate that our total expenses for '18 will be below SEK 17 billion, excluding the effects from the released restructuring reserve.

Looking ahead, if FX rates were to stay at current levels, the full-year effect would be an additional SEK 150 million, i.e., a total of SEK 450 million for 2019. And assuming that also interest rates as well as inflation expectations are stable, we would enter next year with a headwind of roughly SEK 600 million.

Underlying expenses are developing in line with our plan, and we intend to keep a steady state with regards to our investment agenda and the key priorities for next year, as we are convinced that the initiatives are crucial to our long-term competitiveness. But, as we have had exceptional FX rate movements during the past 12 months and we might see further volatility ahead, I wanted already now to highlight this for you, and will, in conjunction with our Q4 result, revert to you on this matter.

Last but not least, I want, however, to reiterate that the Swedish krona depreciation is net positive for our bottom line, and that cost discipline and our return on equity target of at least 15% both remain key priorities ahead.

Now, summing it all up at Group level, our core products performed strongly yet another quarter. We saw loan growth in all our home markets, both in the corporate and private segments. Net commission income was stronger on the back of solid economic conditions. The stabilisation of housing prices countrywide in Sweden has led to that the market has found its new level of transaction prices in most geographical locations. Compared to last year, volume growth is down somewhat, but not materially. And with the stabilisation in prices, we foresee continued solid mortgage growth on the back of the strong economic fundamentals, demand and natural turnover in the market. Corporate loan activity returned this quarter to moderate. Property management continued to show solid growth, while other sectors were more subdued with smaller loan amounts. Lending in the Baltic countries continues to be solid in euro terms, equally in the private as in the corporate sectors across all three countries.

Turning to capital, our capital position remains strong with a CET1 capital ratio of 24.3% implying a buffer to the Swedish FSA's minimum requirements of around 280 basis points. The net profit, excluding dividend, impacted the CET1 capital base positively, while slightly lower inflation expectations impacted the pension valuation positively. The risk exposure amount decreased by SEK 7 billion in the quarter. More collateral and FX movements mitigated the increased lending.

Helo will now walk you through the developments in asset quality.

Helo Meigas

Thank you, Anders. I shall now give a short overview of credit in Q3. Again, it was a strong quarter with stable asset quality, and we recorded moderate volume growth of SEK 11 billion in all our home markets. Anders has already walked you through the lending development for business areas, so I will go straight into the credit impairments.

Credit impairments in Q3 were [inaudible], which consists of an increase in Swedish banking by SEK 71 million and by SEK 37 million in Large Corporates and Institutions. This means asset quality in all our home markets stays strong. Our exposure to the housing development in Sweden, which I have talking about last quarters, is at the same level as last quarter. And the quality of the portfolio is stable.

Also a few words regarding the agriculture portfolio, which has been in the focus of media after the difficult summer in all our home markets. We have having been close contact with our clients throughout the autumn and we do see strained cash flow situations with some of them, which may lead to moderate rating migrations in the coming quarters. However, overall the customers are strong, and we have good collateral positions, so we do not expect this to result in any significant credit impairments.

With that, I hand over to Gregori.

Q&A

Gregori Karamouzis

Thank you, Helo. Operator, we are ready to take any questions that people might have on the line.

Operator

Thank you. Ladies and gentlemen, if you have a question please press 01 on your telephone keypad, and you'll enter a queue. After you are announced, please ask your question. The first question is from the line of Andreas Håkansson from Exane. Please go ahead, your line is open.

Andreas Håkansson

Thank you and good morning everyone. Two questions: first one, if we look at the Treasury NII, you're saying that it will come down significantly, and it has of course; we're now at SEK 231 million and we used to see somewhere between SEK 400 million and SEK 500 million. Going forward, what would you expect this level to be, if you can help us with that?

And then second question on mortgage pricing, you say that your customer mortgage pricing has been stable in the quarter, which is quite remarkable given that we see quite a few of your competitors in Sweden having cut prices. And you, on top of keeping it flat, continue to have a stable market share. Could you tell us what makes it easier for you to have your prices stable compared to your competitors? Thank you.

Anders Karlsson

Thank you, Andreas. On your first question, the best guidance I can give you for the remaining part of this year is that Q3 is a good indication for where Q4 will end up. When it comes to mortgages, I think we have said for quite some time that the way we handle mortgages is that we are not pricing it on a daily basis. As you know, we are geographically diversified all over the country, and I think that competition is different in different parts of the country. And we will try to maintain this going forward.

Andreas Håkansson

Anders, can I just try on an outlook of the Treasury NII for 2019? What's your feeling for the different lines and moving parts there?

Anders Karlsson

I think there are two main things, Andreas, to watch out for. And that is that we'll continue to buy back less next year compared to what we have done in the past, which means that the traffic between NGL and NII will be less; NGL will be more stable, so to say. And the second thing: if you assume that the US dollar short-term rates continue to be unfavourable, some of that activity will be much smaller next year.

Andreas Håkansson

So the Q3 level is somewhere what we should expect; we shouldn't expect it to recover to the high levels in the past?

Anders Karlsson

It will not be as volatile going forward.

Andreas Håkansson

Thank you.

Operator

Our next question is from the line of Magnus Andersson from ABG. Please go ahead, your line is open.

Magnus Andersson

Yes, good morning. Just on corporate lending, as you pointed out, Anders, we see that property management is still doing well. And my question is just you have talked about temporary volume effects here now for two quarters in a row. To me, this level looks quite sticky now for the last three quarters at least, and is up 8% year on year. What – is there anything – I mean, is this underlying loan growth, should we start with these levels going forward, please?

Anders Karlsson

That's a really interesting question, Magnus. I think that what you have seen over the year is that there has been – I mean what you see is net. The underlying gross movements are quite substantial in terms of where – quarter over quarter. What we have said, though, is that the activity is high, but I would like to reiterate that the asset-intensive part is real estate. When you come to other sectors, there might be a lot of activity, but the tickets are much, much smaller. So it's not picking up to the extent that we expect broad based, but it seems to be on a fairly healthy level.

Magnus Andersson

So the property balance, there shouldn't be any volume growth or so looking forward; this is the starting point we should use, really?

Anders Karlsson

Yeah. I think that is a good starting point, Magnus.

Magnus Andersson

Okay. And then secondly – you mentioned it yourself – but this insurance income is now up almost 40% year on year. What is really happening? Are there any reserve releases or anything we should know about, or is it just underlying growth? And if such, where is it coming from, to increase our understanding?

Anders Karlsson

It's two things primarily. It's sales being very good, and at the same time the claims have been lower than expected. So that's – are the main drivers behind it.

Magnus Andersson

Is it fair to say that claims are unsustainably low, or again, is this a proper run rate to expect going forward?

Anders Karlsson

It's a good question, Magnus. It's in – I have lots of skills, but having – forecasting insurance and claims business is not one of those.

Magnus Andersson

Okay, thank you very much.

Operator

Next question is from the line of Peter Kessiakoff from SEB. Please go ahead, your line is open.

Peter Kessiakoff

Yes, good morning. So I thought that I'd give it a try, to get the – to squeeze some comments out of you, Anders, on the cost side. And first of all, I mean, I hear what you're saying in terms of the restructuring of some SEK 300 million that you announced in Q4 last year. Now, you reversed SEK 200 million of that. Does that mean that a large part of the individuals that you were perhaps looking to, or the FTEs, the reductions that you were aiming for, have not been carried through? Is that one part of it?

Anders Karlsson

Thank you, Peter. No, that's not the part. Actually, if you look at it, as I tried to say, there is a benign job market out there, people working within those areas are scarce resources. A lot of people have left the bank voluntarily, so to say, to search for other job experiences. And some of them have moved internally, which is typically how we handle changes like this. So no, it's not about that.

Peter Kessiakoff

Okay. And in terms of the increase in investments, or the increase in hiring that you will do, could you say something around how that is developing, whether it's quite back-end loaded for this year? I mean, I notice that if you look at the local kind of newspapers, there has been full-page ads out both before summer but also after summer, where you look for individuals. Should we see that it's very back-end loaded, the recruitment that you're making?

Anders Karlsson

It's no drama, really. We have hired around 200 and 250 persons up until now, and that will continue going forward. So there is no drama in that specifically.

Peter Kessiakoff

Yeah, but just thinking about kind of the cost levels entering into 2019, and how we should look at that. But then also, I guess, on the cost side, is it possible to give any kind of comments in terms of what kind of headroom that you gave yourself when you announced the 2019 cost targets? Where – I'm hearing what you're saying on the headwind side on FX and pension, but how much room did you give yourself initially? Is it possible to have any comments on that?

Anders Karlsson

Not really, Peter, you have to trust me on that. We had a buffer for unexpected expenses and we will continue to have a buffer for unexpected expenses going into '19.

Peter Kessiakoff

Okay. Then just moving to margins and especially kind of Baltics where margins look to continue increasing. What's your expectations there going into Q4 and perhaps 2019? Do you see room for further margin expansion in that region?

Anders Karlsson

I think yes, you're right. We have been managing actually to take market share and increase margins in this quarter on the private side; on the corporate side, it has been more or less flat. I think the conditions will remain for Q4.

Peter Kessiakoff

Okay. And on the corporate side, is there anything to comment on the margin side? I think you stated it's fairly flat, I think I've seen some comments that margins are up slightly on the corporate side, but – and this goes kind of for the Swedish operations. Do you have anything to say there? Do you see any signs of better pricing environments?

Anders Karlsson

I think in the quarter, the reason behind the couple of bps that I talked about was a mix change in the composition, so I think stable is the thing to look for.

Peter Kessiakoff

Okay, I think I'll stop there. Thank you.

Operator

The next question is from the line of Sofie Peterzéns from JP Morgan. Please go ahead, your line is open.

Sofie Peterzéns

Yeah hi, here is Sofie Peterzéns from JP Morgan. I actually wanted to ask a little bit more about your non-resident clients in the Baltics. Could you just give us details on the 55,000 non-resident customers that you have in the Baltics? How many are from Russia or former Soviet states? Based on kind of general statistics, it looks, in general, that 80% of these non-residents come from Russia or former Soviet states. And could you also give the split between the different countries and retail and corporates? That would be my first question.

And my second question would be, are you aware of any investigations or reviews into your Baltic operations at the moment? And what makes you so confident that you're not going to be drawn into this money laundering scandal, given that less than two years ago you were fined in Latvia, you also stopped transacting with around 500 clients. And you, as recently as February this year, got a warning from the Lithuanian authorities for weak AML. So if you could just comment on why you feel so confident that you're not going to be drawn into the Baltic money laundering issues.

And lastly, could you just remind us what your core equity Tier 1 and the minimum requirement will be post the Pillar 2 to 1 adjustment later this year? Thank you.

Birgitte Bonnesen

Sofie, Birgitte here. We can be very confident for the reasons that I mentioned, the three that are important to remember. First of all, what kind of business we run. We run a domestic business. Look at the slides that came out of the Estonian central bank. I think that tells everything. We focus on the many private individuals and corporates, primarily domestic, so I think that is one thing. The second thing is that we've – we didn't get that Lithuanian on weak AML, we got it from a weakness in one of our processes that had already been mitigated. I think, actually, that the fact that the regulator is efficient and come in and help us go through things, that is a strength of these countries. The third thing – and also the fact that what I mentioned before, the help that we take from regulators and from other banks. And the third thing is the fact that we act so forcefully every time we see an attempt, or anything that is suspicious. That is a strength, and that is also why I can be confident in talking to you.

You asked about the non-residents, and I hope that you've got the point that non-resident is – there's nothing wrong with being a non-resident. This is a very important message, and such a big part of the non-resident clients of Swedbank originate from our home market. The CIS origin is less than 0.5%, less than 0.5%.

Sofie Peterzéns

Sorry, less than 0.5% of all your deposits in the Baltics are customers, or...

Birgitte Bonnesen

Of the number of non-resident clients.

Sofie Peterzéns

So the remaining 99.5% of your clients are Nordic people, or European people who open a bank account in the Baltics. Because my understanding is that a non-resident, if you look at the definition, is that you don't have an address in the country, so basically –

Birgitte Bonnesen

No, no, no, that is not true, that is not true. It's – a non-resident is if you are not – you know, we – our branch or our subsidiary in Estonia is not – it's a resident. So it's not a – the fact that you don't have a – we have many – you know, all the embassies, they're all non-residents. The entities of Swedish companies that I mentioned before, they're also non-residents. I just went through this list of our non-resident customers yesterday, so this is exactly what it looks like.

Sofie Peterzéns

Sorry, the 0.5% of your customers who are kind of non-residents from Russia and former CIS states, it's of your total customer base or of your non-resident customer base?

Birgitte Bonnesen

It's of – yes, it's from the customer base.

Sofie Peterzéns

Okay, but that's still – if you have 3 million customers roughly in the region, that's still 15,000 non-resident customers that you have that are from Russia or former CIS states, which is at the same level Danske had over an eight-year period. How do you feel comfortable that it –

Birgitte Bonnesen

But Sofie, remember many of these are private individuals –

Sofie Peterzéns

Yeah, but I mean –

Birgitte Bonnesen

They are migrant workers that have come in from Belarus or Ukraine and work there for some time and go home, they are students, they are – yeah, others that come in and work for a time.

Sofie Peterzéns

Yeah, but I mean, 15,000 non-resident former Russian or CIS states, it's still a reasonably large number at least compared to Danske Bank. These are twice as many customers as they had that's very suspicious over an eight-year time period.

Gregori Karamouzis

Okay. Sofie, hi, it's Gregori here. I think Birgitte has answered your questions. If you have any more detailed questions on this topic, we can take them after the call, but let's –

Sofie Peterzéns

Okay. Could you just give, while on the call, equity Tier 1?

Gregori Karamouzis

You had a question about the capital as well, Anders will take that question.

Sofie Peterzéns

Yeah.

Anders Karlsson

It will move from currently 24.3% down to roughly 16.4%, and the minimum requirements will come down from 21.5% to 14.6%. The buffer is the same size in absolute terms.

Sofie Peterzéns

Okay, great, thank you.

Operator

The next question is from the line of Bruce Hamilton from Morgan Stanley. Please go ahead, your line is open.

Bruce Hamilton

Thanks, morning, guys. Two quick ones, just on the REA decline, can you just help us understand how much of the move down is FX and how much collateral value update? And in terms of the collateral values, which parts of the book has that mainly impacted, is it corporate or elsewhere?

And then secondly, just going back to the comments you made on costs, did you say that for '18, even excluding the SEK 200 million benefit, you think you'd be below the SEK 17 billion target number? And then for next year, just to check, I think you said SEK 650 million would be the FX-related pressure, but obviously you'd get a benefit on the top line as well, which would more than outweigh that – just to clarify. Thank you.

Anders Karlsson

Thank you. Yeah, if you look at the risk exposure amount dynamics to start off with, it's related to corporates; it's more collateral coming in, so it's decreasing LGD. Primarily, that is the main explanation for the change, then you have FX which is around SEK 1.5 billion. But what you also have, which you did not see explicitly, is that the exposure at default is increasing with around SEK 1.7 in REA. That is actually a mix shift in terms of corporates going out of the book with higher-risk weights than more – corporates coming in. So there are three dynamics explaining the change in REA – that was, I think, your first question.

The second question is, yes, you're correct. Another way of putting it is to be below SEK 16.8 billion. When it came – comes to '19, what I said is that if FX interest rates and inflation expectations stays at the same level as they are today, we will start off with a headwind of SEK 600 million, of which FX is SEK 450 million. Roughly speaking, that will lead to an increase in income versus the forecasting period of more than SEK 1 billion. So you're right, it's benefiting the shareholder.

Bruce Hamilton

Thank you.

Operator

Next question is from the line of Adrian Cighi from RBC. Please go ahead, your line is open.

Adrian Cighi

Hi there, this is Adrian Cighi from RBC, two questions on net interest income, please. We've seen Norway increase its rates earlier this summer by some 25 basis points with the key banks there almost all increasing their mortgage rates by an average of 18 to 22 basis points. However, one of the banks with operations in both Sweden and Norway commented that the Swedish market is somewhat different in terms of dynamics and could see a lower level of increase. You still provide a SEK 6 billion sensitivity to a 100 basis points rate increase. What's your view on the potential sort of freedom to increase or pass on some of the expected rate increases to your customers?

And then maybe just a second one following up on the headwind from US dollar funding. Is there anything you're doing in terms of looking at changing or offsetting some of the headwinds there with potentially pricing or repricing deposits elsewhere? Thank you.

Anders Karlsson

If we start off with your first question, you're right that we state a number where you have to do the assumptions yourself about how we will act in an upcoming or up-going interest rate environment. What we have said and we continue to say is that it is definitely our ambition to reprice when funding cost is coming up. But as you know, we are not the only player in the market, so we need to relate to the competitors. What we also have said, which I think is important to remember, is that a very large part of the deposit base is today subsidised by us by paying zero with negative rates. So you will have an automatic benefit on that side of the balance sheet, as well.

Coming to your second question, which was about US dollar funding, it has been a benign market for short-term US dollar funding that has been primarily placed with the Federal Reserve or with any – the European Central Bank. So it's not a part of core operation, we are not funding any structural assets or anything; it's more that this opportunity has vanished during the year.

Adrian Cighi

Okay, thank you.

Operator

The next question is from the line of Matti Ahokas from Danske Bank. Please go ahead, your line is open.

Matti Ahokas

Yes, thank you, good morning. A question also on the NII and the mortgage margins. And just to clarify, when you talk about that the margins have gone down, then you're referring to just purely the spread between your mortgage rate and the STIBOR rate and not your actual funding cost. Is this correct?

Anders Karlsson

I'm referring to STIBOR movements during the quarter, yes.

Matti Ahokas

And is it also fair to assume – I guess it is – that actually the STIBOR is not your real funding cost. So could you give us some indication of that – the margins regarding – compared to your actual funding costs on the Swedish mortgage market?

Anders Karlsson

I think three months' STIBOR is a very good indication of our funding cost.

Matti Ahokas

Okay. Yeah, thanks for your question.

Operator

The next question is from Riccardo Rovere from Mediobanca. Please go ahead, your line is open.

Riccardo Rovere

Thanks, and good morning to everybody. Just a couple of questions from my side, the first one is on – sorry to get back on Baltics. Now just to understand, the problem here is, if you process a payment that you think could be suspicious, the problem is processing the payment, or not reporting that that payment might be suspicious. What is the problem here? Where is, let's say, the theoretical, you know, criminal activity here, processing it or not having reported it? This is my first question.

The second question I have – sorry to get back on cost and NII guidance but, you know, the feeling I have is the numbers are, you know, flying all over the place in this call. Can you summarise, as we were children of five years, what you expect on cost and NII? You know, because I understand there are some headwinds, but then you have the restructuring that will not be present anymore. Can you really summarise in a few words what is your guidance here for this year and next year?

Birgitte Bonnesen

Riccardo, good morning. Your first question: both, I would say, and we work on both sides.

Anders Karlsson

And on cost, Riccardo, I'm sorry if you felt that the numbers were flying around. What I tried to say is for this year, we stick to the guidance of SEK 17 billion excluding the reserve that we released in the quarter. That is, in more exact words, we will end up below SEK 16.8 billion this year. Next year, the guidance for the underlying cost remains stable at SEK 17 billion. But I also wanted you to understand that given the FX rate movements, the inflation expectation movements and the interest rate movements, we will start off with a headwind of SEK 600 million if it continues. And we will not change our investment agenda and the key activities that we have put forward for next year.

When it comes to NII, what I specifically said is that you should expect Group Treasury's NII to decrease going forward, but you will also see less volatility in NGL and NII combined – that is what I said to you.

Riccardo Rovere

Okay, I understand. Thank you very much, now it's very clear. Thanks again.

Operator

The next question is from the line of Jacob Kruse from Autonomous. Please go ahead, your line is open.

Jacob Kruse

Hi, thank you. Just two quick questions: firstly on the NII in your presentation, you have this bridge, and this quarter, Treasury and others are negative SEK 107 million. Just to clarify, Treasury, I think is about SEK 50 million. What is the other here in the Q2 to Q3 bridge?

And then the second question was just on the suspicious transactions – sorry, on the AML discussions. We talked about the 15,000 non-residents CIS clients and we had the flow numbers coming out of the Estonian central bank yesterday. Have you looked at your client base back in 2008–15 to determine that you did not have what Danske was kind of classifying as suspicious clients? And I think they looked at the residency and the source of funds. So have you done any kind of spot check to see that you are not in a similar situation, or that most of these – or the client base is as you would like it to be in terms of documentation? Thank you.

Birgitte Bonnesen

Jacob, yes, just to answer your last question first, because that's very short: yes, we have.

Jacob Kruse

And could you just quantify what the outcome was, if this is, you know, 90%, or in terms of what –

Birgitte Bonnesen

No, I can – yes, I can say to you that we didn't have any of the names that were in the Danske report; they had not been – they are not current clients of ours. And we've gone through the time from 2007 until now, and they haven't been. So we've checked for everything.

Jacob Kruse

Okay great, thank you.

Anders Karlsson

And on the – your question on ‘other,’ I mean, primarily it is – the lion part is Treasury, but then you have some NII movements from what we phrase as ‘Group Functions,’ or ‘Other Group Functions.’ You can find that in the fact book on page 28.

Jacob Kruse

Okay, thank you.

Operator

The next question is from Paulina Sokolova from Barclays. Please go ahead, your line is open.

Paulina Sokolova

Hi, thank you for taking my question. Most of them have been answered actually, but just one more clarifying question on cost. So your earlier comments, I was just wondering, do they imply that if FX and interest rates stay where they are, does that mean the as-reported cost base might be higher than the SEK 17 billion underlying ceiling?

Anders Karlsson

Yeah, my point was that the underlying cost development is under full control. However, what I tried to say is that if FX continues to develop the way it has, that is beneficial for the shareholders. And there is a limit where you – I will not, or we will not stop doing things that we find important for long-term competitiveness due to FX movements. That was my signal.

Paulina Sokolova

Okay, thank you.

Operator

And we currently have no further questions registered, so I'll hand the call back to the speakers. Please go ahead.

Gregori Karamouzis

Thank you and thanks, everyone, for participating on this call. We'll meet many of you on the road over the next few days, but please reach out to me if you have any further questions. Thank you and see you on the road.