

Doha Bank (DHBK)

Recommendation	ACCUMULATE	Risk Rating	R-3
Share Price	QR39.25	Current Target Price	QR47.00
Implied Upside	19.7%	Old Target Price	QR53.00

Revising Estimates and Price Target On Tepid Outlook

Doha Bank is Qatar's 3rd largest conventional bank with a market share of ~8% in loans and deposits, respectively (5th largest among all listed banks). DHBK was known for solely being a retail bank with retail loans representing ~42% of its loan book in 2008. However, the bank has shifted its strategy by tapping other sectors of the economy such as contracting and real estate. As of FY2015, loans to contractors made up ~17% of its loan portfolio vs. ~10% in 2008. During the same period, retail loans dropped from ~42% to ~19%. The bank has recently become more cautious about lending to contractors; it plans to target prime contractors as opposed to subcontractors. Going forward, DHBK intends on approaching contractors with a consortium of banks rather than engage in bilateral lending. Given a soft macro outlook and liquidity conditions, we forecast net loans to grow by 5.6% in 2016, 7.8% in 2017 and 9.9% in 2018 with a CAGR of 9.6% during 2015-2020e vs. a CAGR of 15.9% (2010-2015). We also expect this growth to be accompanied by further capital hikes (~QR3bn) in 2016e-2018e and aggressive deposit raising.

Highlights

- Soft macro-economic outlook, high LDR (105%), Liquidity, higher funding cost and CoR may prove to be a challenge for DHBK in our view; we revise some of our assumptions for 2016 and 2017.** We lower our 2016 bottom-line estimate by 6.0% (we now expect attributable net profit to drop by 6.1% to QR1.15bn). The change in the bottom-line is due to 1) lower net interest income (which we expect to marginally grow by 3.7%) on the back of larger interest bearing deposits complemented by higher funding costs; expect NIMs to drop by 15bps to 2.66%, 2) we pencil in a CoR of 60bps which results in net provisions growing by 21.7% to QR356.8mn, 3) investment impairments growing by 9.4% and 4) larger payment on Tier-1 bond in order to account for the second issuance (coupon pmt. of QR240mn vs. QR120mn in 2015). On the other hand, we estimate flat opex as DHBK braces for a weak year. 2017 could be a better year for Doha Bank mainly due to a drop in investment impairments. Thus, we expect net profit to grow by 8.6% to QR1.244bn. We continue to expect higher funding costs and pressure on NIMs. We estimate NIMs to drop by another 10bps to 2.56% as the bank continues to raise interest bearing deposits. The main reason we are estimating low loan growth and margin pressure is due the bank's high LDR, which remains elevated at 105%. We note in light of the current situation, QCB may not require banks to adhere to the new ceiling (LDR of 100%) by end-2017, in our view.
- Based on our revised estimates, we decrease our price target to QR47.00 from QR53.00 and maintain our Accumulate rating.** Our revision reflects a subdued fundamental outlook in 2016. We have also made some changes to our valuation assumptions. We revised our cost of equity to 11.8% vs. 11.4% previously and kept our terminal growth rate unchanged at 4.0%. On the other hand, we changed our forecasted average RoAE to 13.7% vs. 14.4% previously. *Based on our revised estimates, the WEV and RI methods yield a price target of QR46.00 and QR47.00 respectively, yielding a blended fair value of QR47.*

Catalysts

- Beyond a stabilization/recovery in oil prices, the following developments could be perceived positively by the market:** 1) improvement in asset quality, 2) Clarity on capital raising could act as a further catalyst, 3) better execution of the bank's strategy and 4) a reduced DPS of QR2.50 in 2016 (vs. QR3.00 in 2015), still implying an attractive dividend yield of 6.4%.

Recommendation, Valuation and Risks

- Recommendation and valuation: We revise our Price Target to QR47.00 and maintain rating at Accumulate.** DHBK is trading at a 2016e P/B and P/E of 1.1x and 8.9x, respectively. The stock offers a yield of 6.4% in 2015 and 2016.
- Risks:** 1) Declining oil prices remains the biggest risk for DHBK and the banking sector and 2) Exposure to the retail & contracting segments create concentration risk.

Key Financial Data and Estimates

	FY2015	FY2016e	FY2017e	FY2018e
Attributable EPS (QR)	4.72	4.43	4.82	5.33
EPS Growth (%)	1.2	-6.1	8.6	10.8
P/E (x)	8.3	8.9	8.2	7.4
BVPS (QR)	35.8	37.3	39.6	42.4
P/B (x)	1.1	1.1	1.0	0.9
DPS (QR)	3.00	2.50	2.50	2.75
Dividend Yield (%)	7.6	6.4	6.4	7.0

Source: Company data, QNBFS estimates; Note: All data based on current number of shares

Key Data

Current Market Price (QR)	39.25
Dividend Yield (%)	6.4
Bloomberg Ticker	DHBK QD
ADR/GDR Ticker	N/A
Reuters Ticker	DOBK.QA
ISIN	QA0006929770
Sector*	Banks & Financial Svcs.
52wk High/52wk Low (QR)	56.20/33.45
3-m Average Volume ('000)	241.3
Mkt. Cap. (\$ bn/QR bn)	2.8/10.1
Shares Outstanding (mn)	258.4
FO Limit* (%)	49.0
Current FO* (%)	11.9
1-Year Total Return (%)	(20.7)

Fiscal Year End December 31

Source: Bloomberg (as of March 08, 2016), *Qatar Exchange (as of March 08, 2016); Note: FO is foreign ownership

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Revising Estimates

Soft macro-economic outlook, high LDR (105%), Liquidity, higher funding cost and CoR may prove to be a challenge for DHBK in our view; we revise some of our assumptions for 2016 and 2017. We lower our 2016 bottom-line estimate by 6.0% (we now expect attributable net profit to drop by 6.1% to QR1.15bn). The change in the bottom-line is due to 1) lower net interest income (which we expect to marginally grow by 3.7%) on the back of larger interest bearing deposits complemented by higher funding costs; expect NIMs to drop by 15bps to 2.66%, 2) we pencil in a CoR of 60bps which results in net provisions growing by 21.7% to QR356.8mn, 3) investment impairments growing by 9.4% and 4) larger payment on Tier-1 bond in order to account for the second issuance (coupon pmt. Of QR240mn vs. QR120mn in 2015). On the other hand, we estimate flat opex as DHBK braces for a weak year. 2017 could be a better year for Doha Bank mainly due to a drop in investment impairments. Thus, we expect net profit to grow by 8.6% to QR1.244bn. We continue to expect higher funding costs and pressure on NIMs. We estimate NIMs to drop by another 10bps to 2.56% as the bank continues to raise interest bearing deposits. The main reason we are estimating low loan growth and margin pressure is due the bank's high LDR, which remains elevated at 105%. We note in light of the current situation, QCB may not require banks to adhere to the new ceiling (LDR of 100%) by end-2017, in our view.

Major Estimate Changes

	2016e			2017e		
	Old	New	Change (%)	Old	New	Change (%)
Net Interest Income	2,216	2,124	(4.2)	2,424	2,232	(7.9)
Non Interest Income	782	801	2.4	835	852	2.1
Net Operating Income	1,938	1,896	(2.2)	2,141	2,019	(5.7)
Net Income (Attributable)	1,218	1,145	(6.0)	1,400	1,244	(11.1)

Source: QNBFS estimates

Valuation

Based on our revised estimates, we decrease our price target to QR47.00 from QR53.00 and maintain our Accumulate rating. Our revision reflects a subdued fundamental outlook in 2016. We have also made some changes to our valuation assumptions. We revised our cost of equity to 11.8% vs. 11.4% previously and kept our terminal growth rate unchanged at 4.0%. On the other hand, we changed our forecasted average RoAE to 13.7% vs. 14.4% previously. *Based on our revised estimates, the WEV and RI methods yield a price target of QR46.00 and QR47.00 respectively, yielding a blended fair value of QR47.00.*

We value DHBK using a blended valuation methodology, which assigns a 50%:50% weighting to a) Warranted Equity Valuation (WEV) and b) Residual Income Model (RI).

a) We utilize a WEV technique derived from the Gordon Growth Model: $P/B = (RoAE-g)/(Ke-g)$.

This model uses sustainable return on average equity (RoAE) based on the mean forecast over the next seven years, cost of equity (Ke) and expected long-term growth in earnings (g) to arrive at a fair value for this stock. We consider this method best suited to arriving at an intrinsic valuation through the economic cycle.

b) We also derive DHBK's fair value by employing the RI valuation technique, which is calculated based on the sum of its beginning book value, present value of interim residuals (net income minus equity charge) and the present value of the terminal value (we apply a fundamental P/B multiple based on the Gordon Growth Model to the ending book value at the end of our forecast horizon).

The RI model is suitable for the following reasons: 1) when the company does not pay dividends or the pattern of dividend payments is unpredictable; 2) the company is expected to generate negative free cash flows for the foreseeable future and 3) as the traditional free cash flow to equity (FCFE) formula does not apply to banks. A major advantage of RI in equity valuation is a greater portion of the company's intrinsic value is recognized from the beginning BVPS as opposed to the terminal value (common in traditional FCFE methodology).

In Doha Bank's case, 77% of the fair value is derived from the bank's beginning BVPS vs. 14% from the terminal value. Both valuation methodologies are based on a common Cost of Equity (CoE) assumption of 11.8%.

We calculate a risk free rate of 4.5% and factor in an adjusted beta of 1.05 vs. 0.87 (adjusted from Bloomberg) as we believe banks are a direct proxy for the economy. Finally, we add a local equity risk premium of 7.02% to arrive at a CoE of 11.8%.

Valuation Matrix

WEV	
Sustainable RoAE (%)	13.7%
Book Value of 2016e (QR)	37.26
Estimated Cost of Equity (%)	11.8%
Terminal Growth Rate (%)	4.0%
Intrinsic Value (QR)	46.00
Current Market Price (QR)	39.25
Upside/(Downside) Potential (%)	17.2%
Equity Value (QR mn)	11,885

RI	
Beginning BVPS (2016) (QR)	35.85
Present Value of Interim Residuals (QR)	4.45
Present Value of Terminal Value (QR)	6.33
Terminal Growth Rate (%)	4.0%
Intrinsic Value (QR)	47.00
Current Market Price (QR)	39.25
Upside/(Downside) Potential (%)	19.7%
Equity Value (QR mn)	12,143

Source: Bloomberg, QNBFS estimates

Price Target Calculation

Methodology	Equity Value (QR mn)	Weight (%)	Fair Value (QR mn)
WEV	11,885	50	5,943
Residual Income	12,143	50	6,072
Blended Equity Value			12,014
Shares Outstanding (mn)			258.372
Target Price (QR)			47.00
Upside/(Downside)			19.7%

Source: Bloomberg, QNBFS estimates

We present below a scenario analysis of possible price targets based on a Base, Bull and Bear scenario

Scenario Analysis	Bear	Base	Bull
Sustainable RoAE	12.5%	13.7%	14.5%
G	3.0%	3.0%	4.5%
Ke	12.8%	11.8%	10.8%
P/B	0.97	1.23	1.58
Blended Fair Value Based on WEV & RI	37.00	47.00	60.00

Source: QNBFS estimates

Detailed Financial Statements

Ratios	FY2015	FY2016e	FY2017e	FY2018e
Profitability (%)				
RoAE (Attributable)	13.2	12.1	12.5	13.0
RoAA (Attributable)	1.7	1.6	1.6	1.6
RoRWA (Attributable)	1.6	1.4	1.4	1.4
NIM (% of IEAs)	2.81	2.66	2.56	2.52
NIM (% of RWAs)	2.76	2.55	2.51	2.47
NIM (% of AAs)	2.58	2.44	2.35	2.32
Spread	2.3	2.2	2.2	2.2
Efficiency (%)				
Cost-to-Income (Headline)	36.7	35.2	34.5	34.3
Cost-to-Income (Core)	37.6	36.2	35.6	35.3
Liquidity (%)				
LDR	105.4	103.0	101.9	97.4
Loans/Assets	66.8	64.8	63.8	66.7
Cash & Interbank Loans-to-Total Assets	16.7	18.6	19.1	14.1
Deposits to Assets	63.3	62.9	62.6	68.4
Wholesale Funding to Loans	26.6	29.6	31.5	20.9
IEAs to IBLs	142.6	132.6	125.8	127.9
Asset Quality (%)				
NPL Ratio	3.26	3.65	3.72	3.55
NPLs to Shareholder's Equity	20.3	23.2	24.0	23.5
NPLs to Tier 1 Capital	24.7	24.9	25.7	25.2
Coverage Ratio	109.1	108.2	110.4	117.1
ALL/Average Loans	3.8	4.1	4.3	4.4
Cost of Risk	0.54	0.60	0.63	0.59
Capitalization (%)				
Tier 1 Ratio	14.5	15.0	14.7	14.2
CAR	14.8	15.4	15.1	14.5
Tier 1 Capital to Assets	13.9	14.3	13.7	13.6
Tier 1 Capital to Loans	20.9	22.1	21.4	20.5
Tier 1 Capital to Deposits	22.0	22.8	21.8	19.9
Leverage (x)	9.0	9.4	9.7	9.5
Growth (%)				
Net Interest Income	5.5	3.7	5.1	6.0
Net Operating Income	-1.7	4.0	5.5	5.9
Net Income (Attributable)	1.2	-6.1	8.6	10.8
Loans	14.5	5.6	7.8	9.9
Deposits	14.8	8.0	9.0	15.0

Source: Company data, QNBFS estimates

Income Statement (In QR mn)	FY2015	FY2016e	FY2017e	FY2018e
Net Interest Income	2,048	2,124	2,232	2,366
Fees & Commissions	497	506	537	591
FX Income	98	102	109	101
Other Income	170	192	207	210
Non-Interest Income	764	801	852	902
Total Income	2,812	2,925	3,085	3,268
Operating Expenses	(1,031)	(1,029)	(1,065)	(1,119)
Net Operating Income	1,781	1,896	2,019	2,148
Net Provisions	(403)	(477)	(498)	(489)
Net Profit Before Tax	1,378	1,420	1,521	1,659
Tax	(5)	(5)	(5)	(5)
Net Profit (Headline/Reported)	1,374	1,415	1,516	1,653
Interest on Tier-1 Note	(120)	(240)	(240)	(240)
Social & Sports Contribution Fund	(34)	(29)	(32)	(35)
Attributable Net Profit	1,219	1,145	1,244	1,378

Source: Company data, QNBFS estimates

Balance Sheet (In QR mn)	FY2015	FY2016e	FY2017e	FY2018e
Assets				
Cash & Balances with Central Bank	3,563	3,989	4,348	4,286
Interbank Loans	10,385	12,918	14,562	10,441
Net Investments	12,198	13,418	15,311	18,224
Net Loans	55,615	58,717	63,311	69,606
Other Assets	757	831	864	1,019
Net PP&E	786	789	809	799
Total Assets	83,304	90,662	99,204	104,375
Liabilities				
Interbank Deposits	8,776	11,316	12,996	6,913
Customer Deposits	52,767	56,988	62,117	71,434
Term Loans	6,040	6,040	6,946	7,641
Other Liabilities	2,464	2,690	2,919	3,429
Tier-1 Perpetual Note	4,000	4,000	4,000	4,000
Total Liabilities	74,047	81,034	88,979	93,417
Total Shareholders' Equity	9,257	9,628	10,226	10,958
Total Liabilities & Shareholders' Equity	83,304	90,662	99,204	104,375

Source: Company data, QNBFS estimates

Recommendations

Based on the range for the upside / downside offered by the 12 - month target price of a stock versus the current market price

OUTPERFORM	Greater than +20%
ACCUMULATE	Between +10% to +20%
MARKET PERFORM	Between -10% to +10%
REDUCE	Between -10% to -20%
UNDERPERFORM	Lower than -20%

Risk Ratings

Reflecting historic and expected price volatility versus the local market average and qualitative risk analysis of fundamentals

R-1	Significantly lower than average
R-2	Lower than average
R-3	Medium / In-line with the average
R-4	Above average
R-5	Significantly above average

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