

Al Khalij Commercial Bank (KCBK)

Recommendation	MARKET PERFORM	Risk Rating	R-3
Share Price	QR13.65	Target Price	QR15.00
Implied Upside	+9.9%		

Changing Estimates (2018 & 2019); Maintain PT QR15/sh

Al Khalij Commercial Bank is one of the smallest banks domestically. In terms of loans (~4% market share as of 2016), KCBK is one of the smallest of the five-listed conventional banks (6th among the eight-listed banks). KCBK has one of the lowest RoEs (6.4% 2016) among listed banks and it is below its cost of equity of 11.52%. Based on average RoE of 11.10% within our forecast horizon vs. cost of equity of 11.52%, the bank is generating economic losses

Highlights

- Net profit in-line with our estimates; weak set of results as expected.** Al Khalij Commercial Bank (KCBK) reported a net profit of QR158.9mn in 2Q2017 vs. QR160.9mn in 1Q2017 (QR164.1mn in 2Q2016), in-line with our estimates of QR164.4mn (-3.4% variation). KCBK reported total revenue of QR297.7mn, in-line with our estimate (QR289.1mn, +3.0% variation). Moreover, net operating income also came in-line at QR209.9mn vs. our estimate of QR204.4mn (+2.7% differential).
- KCBK's net profit receded by 1.3% QoQ due to lackluster non-funded income and higher opex.** The bank posted non-funded income of QR32.4mn (QR81.2mn in 1Q2017), dropping by 60.2% due to f/x losses and investment losses. On the other hand, opex gained by 4.9% to QR87.8mn. As such the C/I ratio moved up to 29.5% vs. 26.8% in 1Q2017. Profitability on a YoY basis retreated by 3.2% on the back of a 50.2% drop in non-funded income and higher credit provisions. Provisions for credit losses came in at QR50.7mn vs. QR26.4mn.
- Margins significantly improved.** Net interest income jumped by 14.9% and 16.9% QoQ and YoY to QR265.3mn, respectively. Net interest margin expanded by 28bps and 30bps QoQ and YoY to 1.93%, respectively.
- Net Loans and deposits declined.** Net loans decreased by 1.7% QoQ (flat YTD) to QR35.2bn. Further, deposits declined by 5.5% QoQ (-1.8% YTD) to QR32.4bn. As such KCBK's LDR remained elevated at 108% vs. 104% in 1Q2017 (106% in FY2016). *Indicating, liquidity is still an issue for KCBK.*
- Asset quality further worsened but remains manageable.** The bank's NPLs increased by 10.8% and 18.3% QoQ and YTD to QR644.4mn. As such, the NPL ratio jumped to 1.79% vs. 1.59% in 1Q2017 (1.52% at the end of 2016). However, coverage ratio reached 113%, which is positive. *The increase in NPLs and jump in provisions signals further asset quality deterioration.*

Catalysts

- Beyond a stabilization/recovery in oil prices, the following developments could be perceived positively by the market: Visible progress in management's strategy:** 1) a consistent rise in market share and 2) an expansion of attributable RoAE beyond 12% (2017e and 2018e RoAE: 6.6% and 8.5%, respectively) & 3) a possible buyout target.

Recommendation, Valuation and Risks

- Recommendation and valuation: We maintain our Price Target at QR15.00.** KCBK trades at P/TB and P/E of 0.8x and 12.6x on our 2017 estimates, respectively.
- Risks:** 1) Geopolitical Factors/issues, 2) Depressed oil prices remains the biggest risk for KCBK and the banking sector; 3) KCBK's market share gains do not materialize; 4) Untested loan book and asset quality and 5) concentration risk.

Key Financial Data and Estimates

	FY2016	FY2017e	FY2018e	FY2019e
Attributable EPS (QR)	1.04	1.08	1.42	1.82
EPS Growth (%)	-38.6	4.4	30.5	28.6
P/E (x)	16.1	12.6	9.6	7.5
Tangible BVPS (QR)	16.3	16.7	17.4	18.2
P/TB (x)	0.9	0.8	0.8	0.8
DPS (QR)	0.75	0.75	1.00	1.15
Dividend Yield (%)	5.2	5.5	7.3	8.4

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

Key Data

Current Market Price (QR)	13.65
Dividend Yield (%)	5.5
Bloomberg Ticker	KCBK QD
ADR/GDR Ticker	N/A
Reuters Ticker	KCBK.QA
ISIN	QA000A0M6MD5
Sector*	Banks & Fin. Svcs.
52wk High/52wk Low (QR)	18.49/11.79
3-m Average Volume ('000)	38.6
Mkt. Cap. (\$ bn/QR bn)	1.3/4.9
Shares Outstanding (mn)	360.0
FO Limit* (%)	49.0
Current FO* (%)	10.5
1-Year Total Return (%)	-15.9
Fiscal Year End	December 31

Source: Bloomberg (as of July 25, 2017), *Qatar Exchange (as of July 24, 2017); Note: FO is foreign ownership

Shahan Keushgerian

+974 4476 6509

shahan.keushgerian@qnbfs.com.qa

Saugata Sarkar

+974 4476 6534

saugata.sarkar@qnbfs.com.qa

Change in Estimates

	2017			2018			2019		
	Old	New	Change (%)	Old	New	Change (%)	Old	New	Change (%)
Net Interest Income	938	1,003	6.9%	991	1,074	8.4%	1,093	1,190	8.9%
Non Interest Income	255	183	-28.2%	274	244	-10.7%	321	271	-15.5%
Total Revenue	1,193	1,186	-0.6%	1,264	1,318	4.2%	1,414	1,461	3.3%
Net Operating Income	850	880	3.4%	914	1,004	9.9%	1,055	1,124	6.6%
Net Income (Reported/Headline)	456	456	-0.1%	547	578	5.5%	691	727	5.2%
Net Income (Attributable)	391	391	-0.2%	480	510	6.2%	620	656	5.7%

Source: QNBFS Research

Detailed Financial Statements

Income Statement (In QR mn)	FY2016	FY2017e	FY2018e	FY2019e
Net Interest Income	913	1,003	1,074	1,190
Fees & Commissions	198	192	206	222
FX Income	31	(4)	19	21
Other Income	19	(5)	19	28
Non-Interest Income	248	183	244	271
Total Revenue	1,160	1,186	1,318	1,461
Operating Expenses	(341)	(306)	(314)	(337)
Net Operating Income	819	880	1,004	1,124
Net Provisions & Impairments	(403)	(405)	(402)	(366)
Net Profit Before Taxes & Non-Recurring Items	416	475	602	758
Non-Recurring Income	-	-	-	-
Net Profit Before Tax	416	475	602	758
Tax	11	(19)	(24)	(30)
Net Profit (Headline/Reported)	427	456	578	727
Interest Payment on AT1 Note	(42)	(55)	(55)	(55)
Social & Sports Contribution Fund	(11)	(10)	(13)	(17)
Net Profit (Attributable)	374	391	510	656

Source: Company data, QNBFS Research

Balance Sheet (In QR mn)	FY2016	FY2017e	FY2018e	FY2019e
Assets				
Cash & Balances with Central Bank	2,359	2,366	2,461	2,567
Interbank Loans	6,489	6,761	5,679	5,134
Net Investments	15,608	14,071	15,764	17,347
Net Loans	35,180	36,480	39,248	43,196
Other Assets	620	620	589	648
Net PP&E	191	190	189	189
Goodwill & Other Intangibles	150	144	138	138
Total Assets	60,597	60,633	64,069	69,219
Liabilities				
Interbank Deposits	12,899	11,509	10,784	11,737
Customer Deposits	32,195	33,805	37,862	42,784
Term Loans & Borrowings	6,137	6,137	6,137	5,299
Other Liabilities	2,333	2,028	1,893	1,711
AT1 Perpetual Bonds	1,000	1,000	1,000	1,000
Total Liabilities	54,564	54,480	57,676	62,530
Total Shareholders' Equity	6,033	6,153	6,393	6,689
Total Liabilities & Shareholders' Equity	60,597	60,633	64,069	69,219

Source: Company data, QNBFS Research

Ratios/Financial Indicators	FY2016	FY2017e	FY2018e	FY2019e
Profitability (%)				
RoAE (Attributable)	6.2	6.4	8.1	10.0
RoAA (Attributable)	0.6	0.6	0.8	1.0
RoRWA (Attributable)	0.7	0.8	0.9	1.1
NIM (% of IEAs)	1.7	1.8	1.8	1.9
NIM (% of RWAs)	2.3	2.4	2.5	2.5
NIM (% of AAs)	1.6	1.7	1.7	1.8
Spread	1.6	1.6	1.5	1.6
Efficiency (%)				
Cost-to-Income (Headline)	29.4	25.8	23.8	23.0
Cost-to-Income (Core)	29.9	25.7	24.2	23.5
Liquidity (%)				
LDR	109	108	104	101
Loans/Assets	58.1	60.2	61.3	62.4
Cash & Interbank Loans-to-Total Assets	14.6	15.1	12.7	11.1
Deposits to Assets	53.1	55.8	59.1	61.8
Wholesale Funding to Loans	51.7	46.1	41.0	39.4
IEAs to IBLs	123.1	119.9	119.8	117.3
Asset Quality (%)				
NPL Ratio	1.52	1.87	2.00	1.75
NPL to Shareholder's Equity	9.03	11.34	12.61	11.60
NPLs to Tier-1 Capital	8.37	10.36	11.69	10.87
Coverage Ratio	110	120	131	147
ALL/Average Loans	1.7	2.3	2.7	2.7
Cost of Risk	103	105	96	80
Capitalization (%)				
Tier-1 Ratio	15.8	16.0	15.8	14.2
CAR	15.8	16.0	15.8	14.2
Tier-1 Capital to Assets	10.7	11.1	10.8	10.3
Tier-1 Capital to Loans	18.5	18.5	17.6	16.5
Tier-1 Capital to Deposits	20.2	19.9	18.2	16.7
Leverage (x)	10.0	9.9	10.0	10.3
Growth (%)				
Net Interest Income	-1.2	9.9	7.1	10.8
Non-Interest Income	12.7	-26.0	33.3	11.1
OPEX	-12.8	-10.2	2.5	7.1
Net Operating Income	8.8	7.4	14.1	12.0
Net Income (Reported/Headline)	-31.8	6.8	26.8	25.9
Loans	5.2	3.7	7.6	10.1
Deposits	4.1	5.0	12.0	13.0
Assets	7.0	0.1	5.7	8.0
RWAs	8.8	2.4	3.7	14.9

Source: Company data, QNBFS Research

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

Contacts

Saugata Sarkar

Head of Research

Tel: (+974) 4476 6534

saugata.sarkar@qnbfs.com.qa

Mohamed Abo Daff

Senior Research Analyst

Tel: (+974) 4476 6589

mohd.abodaff@qnbfs.com.qa

Shahan Keushgerian

Senior Research Analyst

Tel: (+974) 4476 6509

shahan.keushgerian@qnbfs.com.qa

QNB Financial Services Co. WLL

Contact Center: (+974) 4476 6666

PO Box 24025

Doha, Qatar

Zaid Al Nafsoosi, CMT, CFTe

Senior Research Analyst

Tel: (+974) 4476 6535

zaid.alnafsoosi@qnbfs.com.qa

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