

Masraf Al Rayan (MARK)

Recommendation	MARKET PERFORM	Risk Rating	R-3
Share Price	QR37.70	Price Target	QR34.00
Implied Upside	(9.8%)		

Net Reversals Drive 3Q2018 Bottom-Line; Lowering Estimates for 2019 and 2020 On Account of Margin Pressure

Masraf Al Rayan (MARK) is the second largest Shari'ah compliant bank among listed banks. Incorporated in 2006, MARK is focused on the public sector, which dominates its loan portfolio. Public sector loans grew by a CAGR (2010-2017) of 22% and represents 56% (December 2017) of MARK's loan portfolio. Notably, MARK has the best asset quality among Qatari banks with a NPL ratio of 0.6%, one of the highest RoEs of ~17% and robust capitalization at 18%.

Highlights

- **MARK's 3Q2018 bottom-line increased YoY and QoQ on the back of net reversals.** MARK reported net income of QR566.0mn (ahead of our estimate QR536.1mn; +5.6% variation), increasing by 4.4% YoY (+5.8% QoQ). The beat was due to the bank booking net reversals of QR15.1mn vs. net reversals of QR2.8mn in 3Q2017 (net provisions of QR4.9mn in 2Q2018). Net operating income (before provisions) grew by only 1.6% both YoY and QoQ to QR552.2mn (in-line with our estimate of QR551.1mn). Net operating income was mainly attributed to strong fee income as Net interest & investment income was weak YoY and QoQ.
- **Margins remained under pressure on a YoY basis, while stable sequentially.** Net interest margin decreased by 11bps YoY (flat QoQ) to 2.42%. Tightening of the NIM was led by a rise in cost of funds exceeding the increase in yield on assets. Cost of funds increased by 38bps YoY to 2.63% (+22bps QoQ), whereas yield on assets increased by 21bps to 4.59% (+17bps QoQ). *The drop in margins is in-line with our expectations.*
- **Operating efficiency remains good; Generating JAWS would be a positive.** MARK ended 3Q2018 with C/I ratio of 23% vs. 22% in 3Q2017 (24% in 2Q2018)
- **Asset quality risks still remain negligible.** NPL ratio remained at 0.64% vs. 0.63% in 2Q2018 while absolute NPLs decreased to QR481.7mn. Coverage ratio of stage 3 loans (impaired or non-performing) remained at 44% at the end of 3Q2018 vs. 2Q2018. MARK's stage one loans (credit risk has not increased significantly since initial recognition) represent 88.2% of total loans while stage two loans (past due but not impaired; credit risk has increased significantly since initial recognition) represent 11.1%.
- **Net Loans and deposits displayed encouraging performance.** Net loans moved up by 1.9% QoQ (+2.9% YTD) to QR74.2bn, while deposits flowed suit and increased by 2.8% QoQ (+3.1% YTD) to QR64.5bn. Thus, MARK's LDR remained elevated and at 115% vs. 116% in 2Q2018 & FY2017. *We are still of the opinion that the bank may increase its borrowings in order to enhance its liquidity profile/lower LDR.*

Catalysts

- News flow and or strategy in growing the business

Recommendation, Valuation and Risks

- **Recommendation and valuation: We maintain our Price Target of QR34/share and Market Perform recommendation.** MARK is trading at P/B and P/E of 2.1x and 13.2x on our 2018 estimates, respectively. *The market is pricing a fundamental P/B (2.1x) and a sustainable RoE (18.9%) vs. our estimates (P/B: 1.7x & RoE: 16.3%).* The name trades at a PEG of 2.3x based on 6% CAGR (2017-23e)
- **Risks:** 1) Geopolitical factors, 2) More than expected increase in credit costs and 3) losing market share in the government segment.

Key Financial Data and Estimates

	FY2017	FY2018e	FY2019e	FY2020e
EPS (QR)	2.70	2.85	3.01	3.29
EPS Growth (%)	-2.3	5.4	5.6	9.2
P/E (x)	13.4	13.2	12.5	11.5
Tangible BVPS (QR)	17.6	18.3	19.2	0.0
P/TB (x)	2.1	2.1	2.0	1.9
DPS (QR)	2.00	2.00	2.25	2.50
Dividend Yield (%)	5.5	5.3	6.0	6.6

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

Key Data

Current Market Price (QR)	37.70
Dividend Yield (%)	5.3
Bloomberg Ticker	MARK QD
ADR/GDR Ticker	N/A
Reuters Ticker	MARK.QA
ISIN	QA000A0M8VM3
Sector*	Banks & Financial Svcs.
52wk High/52wk Low (QR)	42.78/33.01
3-m Average Volume ('000)	267.6
Mkt. Cap. (\$ bn/QR bn)	7.8/28.3
Shares Outstanding (mn)	750.0
FO Limit* (%)	49.0
Current FO* (%)	12.6
1-Year Total Return (%)	+10.7
Fiscal Year End	December 31

Source: Bloomberg (as of October 16, 2018), *Qatar Exchange (as of October 15, 2018); Note: FO is foreign ownership

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Change In Estimates

	2018e			2019e			2020e		
	Old	New	Change (%)	Old	New	Change (%)	Old	New	Change (%)
Net Interest Income	2,405	2,336	-2.9	2,666	2,473	-7.2	2,912	2,683	-7.9
Non Interest Income	504	550	9.2	569	597	4.9	637	668	4.9
Net Operating Income	2,274	2,244	-1.3	2,541	2,365	-6.9	2,795	2,587	-7.5
Net Income (Attributable)	2,059	2,085	1.3	2,377	2,201	-7.4	2,541	2,404	-5.4

Source: QNBFS Research

Detailed Financial Statements

Income Statement (In QR mn)	FY2017	FY2018e	FY2019e	FY2020e
Net Interest Income	2,264	2,336	2,473	2,683
Fees & Commissions	274	304	340	364
FX Income	143	180	191	214
Other Income	56	66	66	90
Non-Interest Income	473	550	597	668
Total Revenue	2,736	2,887	3,070	3,352
Operating Expenses	(577)	(642)	(705)	(765)
Net Operating Income	2,159	2,244	2,365	2,587
Net Provisions	(113)	(87)	(91)	(103)
Net Profit Before Taxes & Non-Recurring Items	2,045	2,157	2,274	2,484
Non-Recurring Income	0	0	0	0
Net Profit After Non-Recurring Income	2,045	2,157	2,274	2,484
Tax	(5)	(5)	(3)	(3)
Net Profit Before Minority Interest	2,041	2,152	2,272	2,481
Minority Interest	(13)	(13)	(14)	(15)
Net Profit (Headline/Reported)	2,028	2,138	2,258	2,466
Social & Sports Contribution Fund	(51)	(53)	(56)	(62)
Net Profit (Attributable)	1,977	2,085	2,201	2,404

Source: Company data, QNBFS Research

Balance Sheet (In QR mn)	FY2017	FY2018e	FY2019e	FY2020e
Assets				
Cash & Balances with Central Bank	2,800	3,188	3,619	3,996
Interbank Loans	3,312	3,438	3,303	4,614
Net Investments	23,423	19,637	21,616	22,810
Net Loans	72,097	76,406	82,570	92,271
Investment In Associates	520	536	553	573
Other Assets	636	840	537	554
Net PP&E	160	170	170	169
Total Assets	102,949	104,215	112,367	124,986
Liabilities				
Interbank Deposits	25,123	19,656	20,681	20,879
Customer Deposits	62,531	66,408	72,385	83,243
Other Liabilities	1,905	4,232	4,667	5,499
Total Liabilities	89,559	90,296	97,733	109,620
Total Shareholders' Equity	13,191	13,709	14,410	15,127
Total Liabilities & Shareholders' Equity	102,949	104,215	112,367	124,986

Source: Company data, QNBFS Research

Ratios	FY2017	FY2018e	FY2019e	FY2020e
Profitability (%)				
RoAE (Attributable)	15.9	15.5	15.7	16.3
RoAA (Attributable)	2.1	2.0	2.0	2.0
RoRWA (Attributable)	3.4	3.3	3.2	3.0
NIM (% of IEAs)	2.43	2.38	2.40	2.37
NIM (% of RWAs)	3.58	3.66	3.56	3.37
NIM (% of AAs)	2.27	2.26	2.28	2.26
Spread	2.0	1.9	1.9	1.8
Efficiency (%)				
Cost-to-Income (Headline)	21.1	22.3	23.0	22.8
Cost-to-Income (Core)	21.9	22.7	23.4	23.4
Liquidity (%)				
LDR	113.7	115.1	114.1	110.8
Loans/Assets	68.3	73.3	73.5	73.8
Cash & Interbank Loans-to-Total Assets	6.7	6.4	6.2	6.9
Deposits to Assets	60.1	63.7	64.4	66.6
Wholesale Funding to Loans	36.4	28.6	28.2	26.1
IEAs to IBLs	124.3	120.3	117.1	116.5
Asset Quality (%)				
NPL Ratio	0.14	0.60	0.68	0.75
NPLs to Shareholder's Equity	0.77	3.54	4.14	4.87
NPLs to Tier 1 Capital	0.91	4.14	4.88	5.78
Coverage Ratio	50.5	49.4	55.2	58.5
ALL/Average Loans	0.1	0.8	0.9	0.9
Cost of Risk	0.00	0.09	0.11	0.11
Capitalization (%)				
Tier 1 Ratio	18.2	17.8	16.7	14.8
CAR	18.2	17.8	16.7	14.8
Tier 1 Capital to Assets	11.1	11.2	10.9	10.2
Tier 1 Capital to Loans	16.2	15.3	14.8	13.8
Tier 1 Capital to Deposits	18.5	17.6	16.9	15.3
Leverage (x)	7.6	7.6	7.8	8.3
Growth (%)				
Net Interest Income	14.0	3.2	5.9	8.5
Non-Interest Income	-0.2	16.4	8.5	12.0
OPEX	23.5	11.3	9.8	8.5
Net Operating Income	8.0	4.0	5.4	9.4
Net Income (Attributable)	2.2	5.4	5.6	9.2
Loans	2.4	6.0	8.1	11.7
Deposits	5.0	6.2	9.0	15.0
Assets	10.8	1.2	7.8	11.2
RWAs	2.4	6.7	11.0	17.6

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

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