

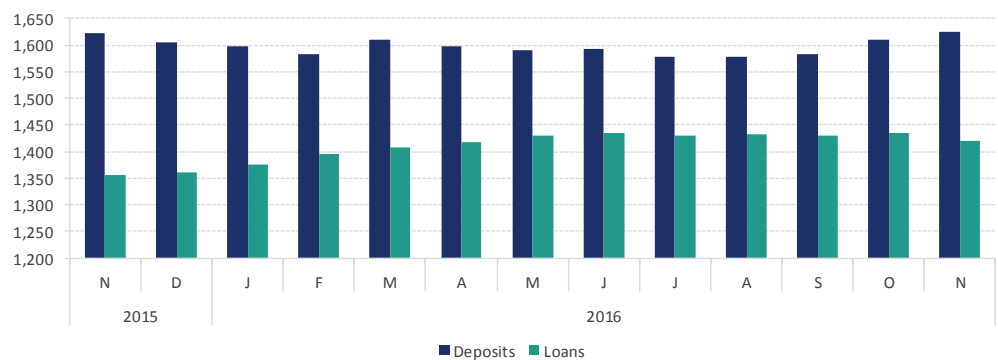
January 03, 2017

SAUDI ARABIAN BANKS 4Q2016 Preview

Positivity Returns

Saudi Arabian Monetary Agency (SAMA) announced its monthly financial data for the month of November recently. Deposits have grown by +1% M/M while loans have contracted at the same pace. In addition, 3-month SAIBOR has witnessed a significant decline during the fourth quarter. With deposits picking up again and SAIBOR declining, the liquidity crunch has eased considerably. On the other hand, the outlook for asset quality has improved significantly, especially for the short term, with the announcement of delayed contractors' payments by the government. However, future growth of contractors' loan portfolio is in question as capital spending, the growth driver, is being rationalized.

Exhibit 1: Banking Sector's Deposits (SAR bln)

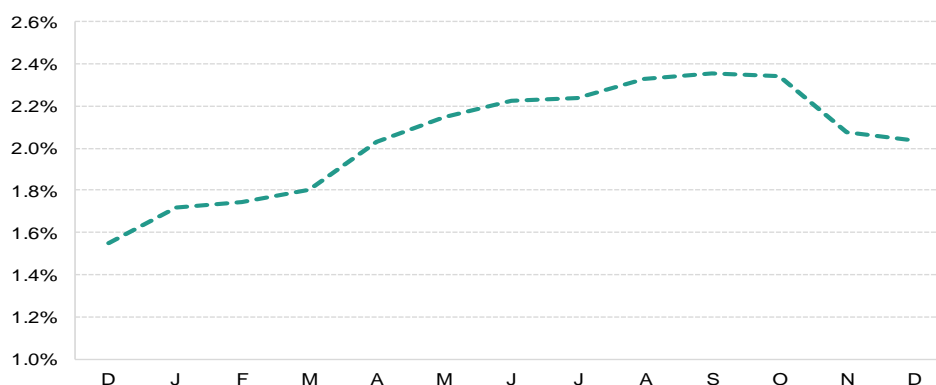


Source: SAMA

During 2016 (until November), deposits have increased by SAR 19 billion, (+1.2% YTD) while the loan portfolio jumped by SAR 58 billion (+4.3% YTD). After pressure during the early part of the year, deposits bottomed out in July, increasing thereafter by SAR 46 billion until November. Majority of that increase came in during 4Q, as the government started settling delayed payments. The settlement not only provided liquidity but also relieved some of the concerns regarding banks' asset quality.

3-Month SAIBOR soared in 2016. It started the year at 1.55% and peaked at 2.36% by 3Q-end indicating liquidity pressure. The increase supported banks' profitability in the first half and would have done so in 3Q as well if it was not for higher provisioning levels. However, with liquidity pressure easing substantially, SAIBOR witnessed a rapid decline reaching 2.04% by year-end. Payment to contractors started flowing coupled with the successful international debt issuance in 4Q. SAIBOR remain largely unaffected by the reverse repo rate hike of SAMA.

Exhibit 2: 3-Month SAIBOR



Source: Bloomberg

4Q2016 Expectations

Table 1 below details our 4Q2016 forecasts for banking stocks under coverage. We expect an average +22% Y/Y rise in net special commission income (NSCI). NIMs have widened considerably this year as the market experienced a hike in interest rates. Tight liquidity in the market ensured that SAIBOR shot up from 1.55% in January to its peak of 2.36% in September but has now mellowed down to 2.04%. Besides higher interest rates, net advances are expected to grow substantially with an average rise of +7% Y/Y for banking stocks under our coverage. Thus, a combination of both these factors has resulted in higher net commission income for the banks. However, growth in net income on average for our stocks is likely to be +7% Y/Y, muted as compared to NSCI. This is due to weaker other income numbers in general as the market was less conducive to fee based income coupled with higher provisioning charges.

While some banks posted a jump in provisions in 3Q, such as Alawwal Bank and Alinma Bank, we expect others to also be conservative in 4Q (in view of a weaker economic climate) and hike provisions. We would like to point out that there is some ambiguity with regards to provisioning by the banks, which could swing net income substantially either way. For BSF, we forecast provisions of SAR 228 million in 4Q versus SAR 95 million in the preceding quarter and SAR 181 million last year while ANB may book SAR 231 million as compared to SAR 212 million in 3Q. Similarly, expect a rise to SAR 231 million at SABB in 4Q versus SAR 190 million in the preceding quarter.

We expect overall deposits of our coverage universe to increase by +4% Y/Y. It is likely that ANB would post a -2% drop while Alawwal and SABB are expected to be flat in terms of deposit growth. Alinma is likely to be the best with a +24% Y/Y growth as they have continued to offer higher rates to attract fresh money. Alrajhi is likely to do well with a +8% Y/Y rise despite intensified competition in the sector.

Loan demand has been robust in 2016 especially until 3Q as some delays in payments caused companies to borrow in order to finance working capital requirements. We forecast an overall +7% Y/Y growth in advances. Alinma is likely to be a leader here as well with a +29% rise, followed by +10% Y/Y at BSF and +8% at Alrajhi. SABB is expected to lag with a meager +2% growth.

Table 1: 4Q2016 Estimates (SAR mln)

Company	Net Comm Income			Net Income			Net Advances			Deposits		
	4Q2015	4Q2016E	Y/Y Chg	4Q2015	4Q2016E	Y/Y Chg	4Q2015	4Q2016E	Y/Y Chg	4Q2015	4Q2016E	Y/Y Chg
ALAWWAL	593	627	6%	451	348	-23%	76,144	79,272	4%	88,832	89,276	0%
BSF	1,032	1,160	12%	950	994	5%	123,443	135,525	10%	141,751	144,586	2%
SABB	1,076	1,235	15%	939	985	5%	125,424	127,898	2%	148,639	149,382	0%
ANB	901	1,092	21%	586	747	27%	115,144	118,136	3%	135,687	132,973	-2%
SAMBA	1,180	1,470	25%	1,334	1,346	1%	129,819	133,141	3%	171,396	175,681	3%
ALRAJHI	2,263	2,971	31%	1,726	2,030	18%	210,218	226,285	8%	256,228	278,007	8%
ALINMA	571	756	33%	386	343	-11%	56,570	73,172	29%	65,542	81,272	24%
Group Total	7,616	9,312	22%	6,371	6,794	7%	836,762	893,429	7%	1,008,074	1,051,176	4%

Source: Riyad Capital, Company Reports

We maintain our target prices for the banking names under coverage. However, we have revised all Buy recommendations to Neutral given that stock prices have run up substantially in this rally and all stocks trade in the vicinity of our fair values. It is heartening to see all names trading above their book value with an average 2016E P/B of 1.2x versus 0.9x at the same time last quarter.

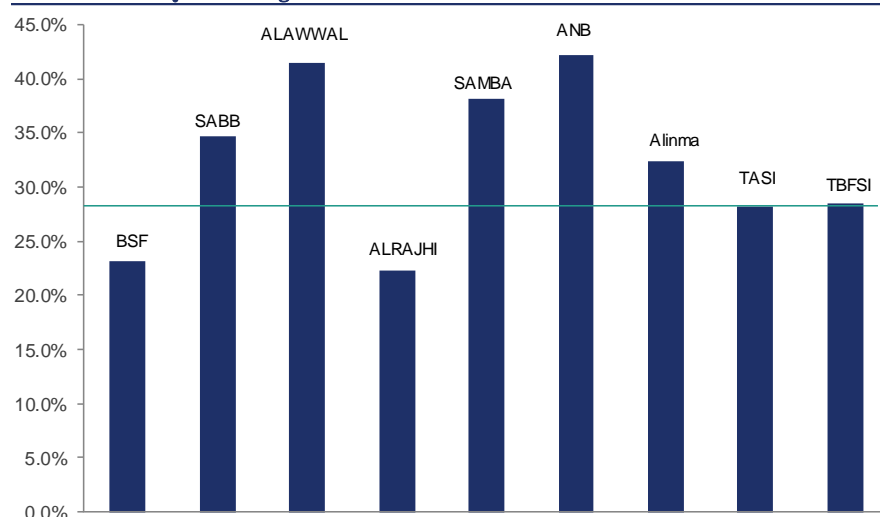
Table 2: Ratings and Valuations (SAR mln)

Company	TASI Code	Current Price	Market Cap	Target Price	Rating	Dividend Yield	P / E		P/B	
							2015	2016E	2015	2016E
ALAWWAL	1040	13.60	15,546	12.00	Neutral	3.7%	7.7x	9.4x	1.3x	1.1x
BSF	1050	25.60	30,858	27.00	Neutral	3.9%	7.6x	7.5x	1.1x	1.0x
SABB	1060	25.00	37,500	24.00	Neutral	3.0%	8.7x	8.8x	1.3x	1.2x
ANB	1080	22.00	22,000	22.00	Neutral	4.5%	8.4x	8.2x	1.1x	1.0x
SAMBA	1090	23.95	47,900	25.00	Neutral	3.8%	9.2x	9.1x	1.2x	1.1x
ALRAJHI	1120	63.25	102,781	51.00	Neutral	2.4%	14.4x	12.7x	2.2x	2.1x
ALINMA	1150	15.10	22,650	14.00	Neutral	3.3%	15.4x	15.6x	1.2x	1.2x
Group Average							10.2x	10.2x	1.4x	1.2x

Source: Riyad Capital

Barring BSF and Alrajhi, all other covered banks have outperformed the TASI in 4Q reflecting a change in the outlook for the banks to positive with the new developments discussed in detail above. In line with our view, Alawwal and ANB have proved to be the best performers in the quarter. In view of recent performance and valuations (2016E P/B of 1.0x and P/E of 7.5x), BSF appears to be a good bet at this stage.

Exhibit 3: 4Q Banking Sector vs. TASI Performance



Source: Tadawul

Stock Rating

Buy	Neutral	Sell	Not Rated
Expected Total Return Greater than 15%	Expected Total Return between -15% and +15%	Expected Total Return less than -15%	Under Review/ Restricted

** The expected percentage returns are indicative, stock recommendations also incorporate relevant qualitative factors*

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