SAUDI HOLLANDI BANK

Doubling Earnings

28 OCTOBER 2008

SAUDI | BANKING

ST Rec. : Accumulate	Current Price*: SAR 41.10
LT Rec. : Buy	LT Fair Value : SAR 73.70

• **3Q2008 Earnings Up by 88% Y-o-Y:** Saudi Hollandi Bank (SHB) released detailed financials for 3Q2008 results. The bank reported net profit of SAR306 million (EPS: SAR1.16), 88% higher Y-o-Y. Earnings for 3Q2008 were 5.3% below our expectation of SAR323 million, a discrepancy attributable to marginally lower revenues. Total banking income grew 19.8% Y-o-Y to SAR526 million, which was 6.5% lower than our expectation of SAR563 million.

• **Spreads Hit by Higher Funding Costs:** Though special commission income grew by 10.7% Q-o-Q, growth in net special commission income was dented by a 24.7% Q-o-Q increase in funding costs. Net interest spreads declined by 16 bps to 2.85% due to a 45 bps increase in costs of funds as banks continued to chase deposits to meet loan book growth requirements. We expect deposit cost pressures to continue in the short term as loan growth continues to out pace deposit growth.

• **Fee & Commission Income Drops 9% Q-o-Q:** Non-special commission income grew 20.4% Y-o-Y but dropped 9.3% Q-o-Q. The Q-o-Q decline is attributable primarily to an 8.7% Q-o-Q drop in fee and commissions income to SAR117 million, less than our expectation of SAR133 million. We believe the decline in fee income is on the back of lower broking revenues, as overall trading volumes at the Saudi stock market slumped in 3Q2008. Trading income also declined to SAR22 million from SAR34 million in 2Q2008 but was significantly higher than the SAR5 million of 3Q2007.

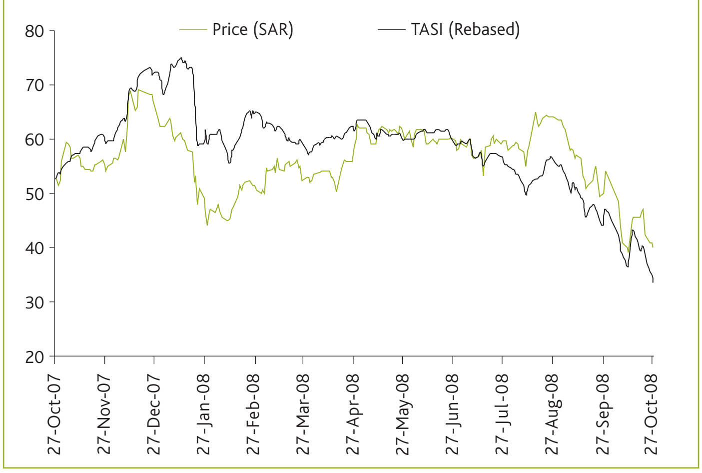
• **Costs Remain Contained:** Administrative costs remained almost flat Y-o-Y and declined marginally Q-o-Q to SAR215 million for 3Q2008. However, with the Q-o-Q drop in revenues, the cost-to-income ratio increased to 40.7% from 39.8% in 2Q2008, but was still significantly lower than the 49.1% of 3Q2007. We expect cost ratios to remain around 40% for 2008 following the completion by management of a restructuring exercise in 2007. Credit provisions also remained flat Q-o-Q at SAR6 million but were significantly lower than the SAR61 million of 3Q2007. There was no surprise on investment provisions, as SHB has one of the lowest exposures among Saudi banks to international and domestic equities.

• **Robust Balance Sheet Growth:** SHB reported 27.4% Y-o-Y and 5.0% Q-o-Q growth in total assets to SAR61.4 billion, driven primarily by 41.7% Y-o-Y and 14.7% Q-o-Q growth in net loans. Total investments, which remain pre-dominantly government securities, grew by 33.1% Y-o-Y and 12.8% Q-o-Q to SAR15.2 billion. Customer deposits grew strongly, rising 45.1% Y-o-Y and 6.2% Q-o-Q to SAR44.5 billion.

• **Revision in Earning Estimates:** SHB's 9M2008 earnings have exceeded our expectations and are already close to our full year earning estimates. We will be revising our 2008 earnings upwards in light of these results. However, given the strong growth already recorded in 2008, we expect earnings growth to be lower in 2009 and onwards compared to our existing estimates. We will be fine-tuning our earning estimates after meeting the management.

• **Recommendation:** We maintain our liking for SHB, which has continued to deliver strong growth in earnings over the last three quarters. With over 95% of its assets invested domestically, SHB remains the least exposed to the immediate impact of the ongoing financial turmoil. We recommend a ST Accumulate / LT Buy on SHB.

FLASH NOTE



	2008e	2009e	2010e
EPS	3.87	4.81	5.88
P/E* (x)	10.36	8.33	6.82
DPS	0.00	0.96	1.18
Div. Yield*	0.0%	2.4%	2.9%
BVPS	21.05	26.57	31.27
P/BV* (x)	1.90	1.51	1.28

Figures in SAR unless otherwise stated

Stock Data	
Last Ex-Div Date	*SAR0.71 on 28 July 2007*
Mkt. Val. (mn)	*SAR10,610*
Shares (mn)	*264.6*
Av. Mthly Liqd. (mn)	*SAR89.7*
52-Week High / Low	*SAR69.00 / 39.00*
Bloomberg / Reuters	*AAAL AB / 1040.SE*
Est. Free Float	*31.88%*

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**prices as of 27 July 2008*

Table 1: Income Statement

(SAR mn)	3Q2007a	2Q2008a	3Q2008a	Y-o-Y	Q-o-Q
Special Commission Income	750	674	747	-0.3%	10.9%
Special Commission Expense	452	314	392	-13.4%	24.7%
Net Special Commission Income	**298**	**360**	**356**	**19.5%**	**-1.1%**
Non Special Commission Incom					
Fees from Banking Services	88	129	117	33.6%	-8.7%
Exchange Income	15	21	24	64.6%	15.2%
Investment Income	39	39	29	-26.0%	-24.6%
Other Operating Income	(0)	-	-	N/A	N/A
Total Non-Special Commission Income	**142**	**188**	**171**	**20.4%**	**-9.3%**
Total Income	**440**	**548**	**526**	**19.8%**	**-4.0%**
Administrative Expenses					
Salaries & Related Expenses	115	127	127	10.9%	0.3%
Rent & Premises	14	18	19	31.6%	1.2%
Other General & Admin Expenses	87	73	69	-20.9%	-5.7%
Total Operating Expenses	**216**	**218**	**215**	**-0.6%**	**-1.6%**
Pre-Provision Profit	**224**	**330**	**312**	**39.3%**	**-5.5%**
Provision for Credit Losses	61	4	6	-90.5%	51.3%
Net Income	**163**	**326**	**306**	**87.9%**	**-6.2%**
EPS (SAR)	0.62	1.23	1.16		
Key Ratios					
Net Interest Spreads	2.58%	3.01%	2.85%		
Non-Special Comm. Inc./Total income	32.2%	34.3%	32.4%		
Cost-to-Income Ratio	49.1%	39.8%	40.7%		

Source: SHB, EFG-Hermes

Table 2: Balance Sheet

(SAR mn)	3Q2007a	2Q2008a	3Q2008a	Y-o-Y	Q-o-Q
Assets					
Cash and Balances with SAMA	2,011	6,186	4,659	131.6%	-24.7%
Due from Banks & Fis	6,173	3,690	1,300	-78.9%	-64.8%
Investments	11,421	13,475	15,204	33.1%	12.8%
Loans & Advances	27,457	33,914	38,910	41.7%	14.7%
Fixed Assets	314	439	443	41.1%	0.8%
Other Assets	818	794	885	8.1%	11.5%
Total Assets	**48,195**	**58,498**	**61,400**	**27.4%**	**5.0%**
Liabilities					
Customer Deposits	30,671	41,897	44,505	45.1%	6.2%
Due to Banks & Fis	10,934	9,361	9,320	-14.8%	-0.4%
Term Loan	700	700	700	0.0%	0.0%
Other Liabilities	1,270	1,458	1,530	20.5%	5.0%
Total Liabilities	**43,576**	**53,416**	**56,055**	**28.6%**	**4.9%**
Share Capital	2,646	2,646	2,646	0.0%	0.0%
Reserves	1,973	2,436	2,699	36.8%	10.8%
Total Equity	**4,619**	**5,082**	**5,345**	**15.7%**	**5.2%**
Total Equity & Liabilities	**48,195**	**58,498**	**61,400**	**27.4%**	**5.0%**

Source: SHB, EFG-Hermes

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