

December 25, 2018

SAUDI ARABIAN BANKS

Sector Update

Zakat Issue Resolved

After months of negotiations, the General Authority of Zakat and Tax (GAZT) and the Saudi Banks have reached an agreement pertaining to Zakat assessment for prior financial years until 2017. The total Zakat payable for the sector is SAR 16.8 billion while the reduction in Shareholders' Equity would be SAR 11.2 billion as some banks have already partially accounted for the settlement (and in some cases, overcompensated). Al Rajhi's BVPS takes the biggest hit at -10.4%, while the total impact for the sector is -3.3%. The impact on Tier-1 ratio varies, most at Al Rajhi -2.1% while ANB would actually show a +0.7% increase due to the reversal. The following table summarizes the details of the settlement:

Table 1: Zakat Settlement Impact on Banks (SAR mln)

Bank	Shareholders' Equity as at Sep-30, 2018 (1)	Zakat Amount Due (2)	Impact on Shareholders' Equity (3)	Difference Between (2)&(3)	Number of Shares (mln)	Impact on BVPS (SAR)	Impact on BVPS (%)
Alrajhi	51,975	5,405	(5,405)	-	1,625	(3.33)	(10.40%)
SAIB	12,500	775	(775)	-	750	(1.03)	(6.20%)
Albilad	7,941	393	(393)	-	600	(0.65)	(4.95%)
BSFR	31,836	1,511	(1,511)	-	1,205	(1.25)	(4.75%)
Aljazira	11,646	551	(551)	-	820	(0.67)	(4.74%)
SAMBA	42,813	2,316	(1,816)	500	2,000	(0.91)	(4.24%)
SABB	32,727	1,628	(1,128)	500	1,500	(0.75)	(3.45%)
RB	36,751	2,970	(787)	2,182	3,000	(0.26)	(2.14%)
Alawwal	13,714	374	(100)	274	1,143	(0.09)	(0.73%)
Alinma	20,212	-	-	-	1,500	-	-
NCB	55,504	183	105	288	3,000	0.04	0.19%
ANB	24,725	649	1,113	1,762	1,000	1.11	4.50%
Total	342,344	16,756	(11,249)	5,506			(3.29%)

Source: Riyad Capital, Tadawul and Company Reports

According to the banks' announcements on Tadawul, the settlement is until financial year 2017 but the impact on 2018 financial statements would include the 2018 charge as well, which has not been disclosed yet. Thus, the effect on Shareholders' Equity would be higher than what has been disclosed to date.

There are two key pieces of information which are awaited:

1. Details of the new Zakat rules that would apply from 2019. What we can safely assume is that the revised annual Zakat charge would be higher than what has historically been the case.
2. Payment of this settlement amount. It is likely that the banks will get some relief to pay the settlement amount. According to the Chairman of Alawwal Bank, the payment would span a period of five years. This would cause minimal disruption to dividend payments. We believe the charge on Shareholders' equity would be immediate.

Tier-1 Capital

Table 2 below illustrates the impact on Banks' Tier-1 capital ratio after the charge on Shareholders Equity has been accounted for. Again, the effect would be higher once 2018 charge is also taken. Al Rajhi takes the biggest hit at -2.1% followed by Al Jazira at -1.1% while the Tier-1 ratio for ANB actually improves by +0.7%.

Table 2: Change in Tier-1 Ratio (%)

Bank	Current Tier-1 Capital (SAR mln)	Post Zakat Tier-1 Capital (SAR mln)	RWA (SAR mln)	Tier-1 Ratio (Current)	Tier-1 Ratio (Post Zakat)	Impact on Tier-1 Ratio
Alrajhi	51,975	46,570	252,630	20.57%	18.43%	(2.14%)
Aljazira	12,198	11,646	51,713	23.59%	22.52%	(1.07%)
SAIB	14,925	14,150	84,623	17.64%	16.72%	(0.92%)
SAMBA	45,097	43,281	203,921	22.11%	21.22%	(0.89%)
BSFR	33,224	31,713	183,666	18.09%	17.27%	(0.82%)
Albilad	7,998	7,605	58,868	13.59%	12.92%	(0.67%)
SABB	34,123	32,995	171,398	19.91%	19.25%	(0.66%)
RB	36,751	35,964	223,188	16.47%	16.11%	(0.35%)
Alawwal	14,083	13,983	76,426	18.43%	18.30%	(0.13%)
Alinma	20,791	20,791	107,372	19.36%	19.36%	-
NCB	64,316	64,421	361,091	17.81%	17.84%	0.03%
ANB	25,166	26,280	164,723	15.28%	15.95%	0.68%

Source: Riyad Capital, Tadawul and Company Reports

It is important to point out that we need to look at the absolute level of the Tier-1 ratio post Zakat as this points to the bank's capital strength. Thus, while ANB's Tier-1 ratio rises, it is still only at 15.9% versus Al Rajhi, which stands at 18.4% even after the decline. Post-Zakat, Al Jazira and Samba lead with 22.5% and 21.2% respectively. Albilad is the weakest at 12.9% followed by ANB at 15.9%.

Largely neutral for valuations

The most important question on investors mind is how this settlement will affect valuations? The P/B ratio at the post zakat book value per share would increase (for majority of the banks). However, we believe this should not be a big concern for investors given that the Return on Equity would be higher going forward. In addition, these announcements finally eliminated the uncertainty concerning Zakat charge, which will be taken positively by investors.

Al Rajhi, which has the biggest impact, had already created reserves for majority of the amount under Shareholders Equity implying that the P/B was understated. In our view, the most negatively affected is Albilad due to impact on book value and Tier-1 ratio. Table 3 below details the change in P/B ratio using the average share price-year to date.

Table 3: Banks Valuations In-Terms of P/B (x)

Bank	Average Share Price YTD (SAR)	Average P/B at current BVPS	Average P/B at Post Zakat BVPS
Alrajhi	80.37	2.51	2.80
NCB	43.00	2.32	2.32
Albilad	23.59	1.78	1.88
Alinma	20.79	1.54	1.54
SABB	30.72	1.41	1.46
SAMBA	28.39	1.33	1.38
RB	15.29	1.25	1.28
BSFR	31.45	1.19	1.25
ANB	30.49	1.23	1.18
Alawwal	13.68	1.14	1.15
SAIB	16.89	1.01	1.08
Aljazira	13.52	0.95	1.00

Source: Riyad Capital, Tadawul and Company Reports

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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