

Al Khalij Commercial Bank (KCBK)

Recommendation	MARKET PERFORM	Risk Rating	R-3
Share Price	QR11.67	Target Price	QR15.00
Implied Upside	+28.5%		

2018 Driven by Lower CoR; Tweaking Estimates

KCBK posted 2018 net income of QR608.4m, in-line with our estimate of QR609.0mn. The result was +11.7% Y-o-Y, mostly due to a material decline in provisions. Total revenue declined as a result of the current operating environment. However, NIM improvement was visible. Loans & deposits contracted YoY, but liquidity remained strong with LDR at 92%. Cost of Risk improved to 60bps and we predict further improvement in 2019 and beyond. DPS came in-line with our forecast at QR0.75, offering an above market average yield of 6.4% at current levels. The upcoming market-wide 10-for-1 stock split could inject some liquidity into the name, which has historically faced thin trading volumes. We retain our Market Perform rating and QR15.00 Price Target on KCBK.

Highlights

- KCBK's 2018 attributable net income increased by 11.7% on the back of a 40.3% drop in provisions & impairments, while total revenue exhibited weak performance.** KCBK reported net income of QR608.4mn, in-line with our estimate of QR609.0mn. The bank's revenue declined by 5.9% as a result of net interest income. Given the current operating environment, we are of the view that growth in 2019's bottom-line could also be driven by an improvement in CoR.
- Opex containment persisted but drop in revenue led to an uptick in C/I ratio.** Revenue declined by 5.9%, while opex receded by 1.6%. As a result, KCBK generated negative JAWS. Moreover, C/I ratio moved up to 28.8% in FY2018 vs. 27.6% in FY2017. We do note the current efficiency ratio is acceptable and still in-line with management's target of less than 30%.
- Margins inched up as the bank shed expensive deposits.** NIMs marginally moved up by 2bps YoY to 1.81%. Yields expanded by 58bps YoY to 4.22%, outpacing CoFs. CoFs increased by 50bps YoY to 2.71%, leading to the gains in margins. It is worth mentioning that interest bearing deposits declined by 13.8% YoY.
- Gross loans and deposits declined.** Gross loans contracted by 8.9% YoY to QR32.7bn while deposits dropped by 12.5% to QR28.6bn. Nevertheless, the liquidity position remained strong with LDR (based on stable sources of funds) amounting to 92%. The bank divested non-core loans in order to sharpen focus on preferred segments.
- Asset quality improved, CoR dropped.** The bank's NPLs dropped by 11.9%. As such, the NPL ratio declined to 1.88% vs. 1.94% at the end of 2017. Moreover, the coverage ratio (coverage of stage 3 loans/NPLs) moved up to 83% vs. 79% in 3Q2018. We expect the coverage ratio to continuously increase as management exercises prudent risk control. CoR also improved, receding to 60bps vs. 84bps in 2017. We foresee further improvement in CoR, penciling in 46bps in 2019.
- Tier-1 remained strong, although slightly lower.** The bank's CET-1 and Tier-1 ratios declined to 13.0% (14.2% in 2017) and 15.6% (16.7% in 2017), respectively. Moreover, KCBK ended 2018 with a CAR of 16.7% (15.8% in 2017). We expect capitalization to remain robust in 2019 and the coming years.

Catalysts

- Visible progress in management's strategy:** 1) an expansion of attributable RoE beyond 12% (2019e and 2020e RoE: 10.7% and 11.1%, respectively), 2) improvement in the liquidity of the stock and 3) M&A activity.

Recommendation, Valuation and Risks

- Recommendation and valuation: We maintain our Price Target at QR15.00.** KCBK trades at P/TB and P/E of 0.7x and 6.8x on our 2019 estimates, respectively.
- Risks:** 1) Geopolitical factors/issues, 2) KCBK's market share gains do not materialize, 3) possible asset quality concerns and 4) concentration risk.

Key Financial Data and Estimates

	FY2018	FY2019e	FY2020e	FY2021e
EPS (QR)	1.54	1.71	1.86	2.09
EPS Growth (%)	11.7	11.0	8.8	12.7
P/E (x)	7.6	6.8	6.3	5.6
Tangible BVPS (QR)	15.1	15.9	17.0	18.3
P/TB (x)	0.8	0.7	0.7	0.6
DPS (QR)	0.75	0.75	0.75	1.00
Dividend Yield (%)	6.4	6.4	6.4	8.6

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

Key Data

Current Market Price (QR)	11.67
Dividend Yield (%)	6.4
Bloomberg Ticker	KCBK QD
ADR/GDR Ticker	N/A
Reuters Ticker	KCBK.QA
ISIN	QA000A0M6MD5
Sector*	Banks & Fin. Svcs.
52wk High/52wk Low (QR)	13.58/10.70
3-m Average Volume ('000)	117.7
Mkt. Cap. (\$ bn/QR bn)	1.1/4.2
Shares Outstanding (mn)	360.0
FO Limit* (%)	49.0
Current FO* (%)	10.9
1-Year Total Return (%)	-7.4
Fiscal Year End	December 31

Source: Bloomberg (as of January 23, 2019), *Qatar Exchange (as of January 23, 2019); Note: FO is foreign ownership

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Change in Estimates

	2019e			2020e		
	Old	New	Change (%)	Old	New	Change (%)
Net Interest Income	977	943	-3.5%	1,063	1,026	-3.5%
Non Interest Income	266	234	-12.0%	256	231	-9.7%
Total Revenue	1,244	1,177	-5.4%	1,264	1,257	-0.5%
Net Operating Income	904	842	-6.9%	967	915	-5.4%
Net Income (Reported/Headline)	671	669	-0.2%	721	724	0.4%
Net Income (Attributable)	600	598	-0.4%	648	650	0.4%

Source: QNBFS Research

Detailed Financial Statements

Income Statement (In QR mn)	FY2018	FY2019e	FY2020e	FY2021e
Net Interest Income	915	943	1,026	1,129
Fees & Commissions	190	182	166	186
FX Income	38	40	42	40
Other Income	0	12	23	25
Non-Interest Income	228	234	231	250
Total Revenue	1,143	1,177	1,257	1,379
Operating Expenses	(329)	(335)	(343)	(363)
Net Operating Income	814	842	915	1,017
Net Provisions & Impairments	(190)	(155)	(173)	(188)
Net Profit Before Taxes & Non-Recurring Items	624	687	742	829
Non-Recurring Income	-	-	-	-
Net Profit Before Tax	624	687	742	829
Tax	(16)	(17)	(19)	(21)
Net Profit (Headline/Reported)	608	669	724	808
Interest Payment on AT1 Note	(55)	(55)	(55)	(55)
Social & Sports Contribution Fund	(15)	(17)	(18)	(20)
Net Profit (Attributable)	538	598	650	733

Source: Company financials, QNBFS Research

Balance Sheet (In QR mn)	FY2018	FY2019e	FY2020e	FY2021e
Assets				
Cash & Balances with Central Bank	2,881	3,782	3,404	3,932
Interbank Loans	6,085	6,619	4,425	5,617
Net Investments	10,663	11,537	10,349	9,867
Net Loans	31,309	33,112	35,935	39,743
Other Assets	687	662	683	795
Net PP&E	335	355	375	397
Goodwill & Other Intangibles	143	133	119	119
Total Assets	52,102	56,200	55,290	60,469
Liabilities				
Interbank Deposits	9,495	10,097	6,725	7,867
Customer Deposits	28,601	31,519	34,040	37,444
Term Loans & Borrowings	5,568	5,568	5,568	5,568
Other Liabilities	1,861	2,143	1,702	1,872
AT1 Perpetual Bonds	1,000	1,000	1,000	1,000
Total Liabilities	46,526	50,326	49,036	53,752
Total Shareholders' Equity	5,577	5,874	6,254	6,717
Total Liabilities & Shareholders' Equity	52,102	56,200	55,290	60,469

Source: Company financials, QNBFS Research

Ratios/Financial Indicators	FY2018	FY2019e	FY2020e	FY2021e
Profitability (%)				
RoE Attributable (Based on Beginning Book Value)	8.6	10.7	11.1	11.7
RoAA (Attributable)	1.0	1.1	1.2	1.3
RoRWA (Attributable)	1.1	1.2	1.3	1.4
NIM (% of IEAs)	1.8	1.9	2.0	2.2
NIM (% of RWAs)	2.4	2.4	2.5	2.6
NIM (% of AAs)	1.7	1.7	1.8	2.0
Spread	1.5	1.6	1.6	1.7
Efficiency (%)				
Cost-to-Income (Headline)	28.8	28.5	27.2	26.3
Cost-to-Income (Core)	28.8	28.8	27.8	26.8
Liquidity (%)				
LDR	109	105	106	106
Loans/Assets	60.1	58.9	65.0	65.7
Cash & Interbank Loans-to-Total Assets	17.2	18.5	14.2	15.8
Deposits to Assets	54.9	56.1	61.6	61.9
Wholesale Funding to Loans	46.2	45.5	32.6	32.3
IEAs to IBLs	121.0	114.2	116.9	115.7
Asset Quality (%)				
NPL Ratio	1.88	1.77	1.55	1.50
NPL to Shareholders' Equity	11.03	10.43	9.30	9.26
NPLs to Tier-1 Capital	10.43	9.47	8.48	8.60
Coverage Ratio	228	243	276	280
ALL/Average Loans	4.1	4.4	4.5	4.4
Cost of Risk	60	46	48	45
Capitalization (%)				
Tier-1 Ratio	15.6	16.2	16.4	15.5
CAR	16.9	16.2	16.4	15.5
Tier-1 Capital to Assets	11.3	11.5	12.4	12.0
Tier-1 Capital to Loans	18.8	19.5	19.1	18.2
Tier-1 Capital to Deposits	20.6	20.5	20.2	19.3
Leverage (x)	9.3	9.6	8.8	9.0
Growth (%)				
Net Interest Income	-7.0	3.0	8.9	10.0
Non-Interest Income	-1.0	2.6	-1.3	8.2
OPEX	-1.6	1.7	2.2	5.8
Net Operating Income	-7.5	3.4	8.7	11.1
Net Income (Reported/Headline)	10.5	10.0	8.1	11.7
Loans	-10.8	5.8	8.5	10.6
Deposits	-12.5	10.2	8.0	10.0
Assets	-10.0	7.9	-1.6	9.4
RWAs	-5.5	5.9	4.6	11.9

Source: Company financials, 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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