

22 April 2011

Comm Bank of Qatar

Growth and value

Buy

Target price
QR98.44 (from QR109.40)

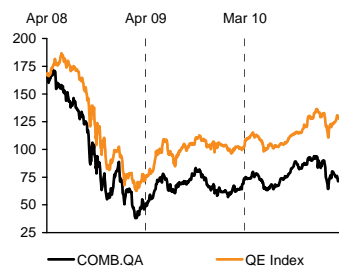
Price
QR72.50

Short term (0-60 days)
n/a

Market view
No Weighting

Price performance

	(1M)	(3M)	(12M)
Price (QR)	74.80	88.50	76.20
Absolute (%)	-3.1	-18.1	-4.9
Rel market (%)	-8.0	-13.9	-16.8
Rel sector (%)	-7.3	-13.3	-20.2



Market capitalisation
QR17.94bn (€3.36bn)

Average (12M) daily turnover
QR20.78m (€5.49m)

Sector: QE Bank Index
RIC: COMB.QA, CBQK QD
Priced at close of business 20 Apr 2011.
Source: Bloomberg

Analyst

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CBQ has de-rated significantly this year in both relative and absolute terms. New Islamic and retail banking regulations are partly to blame, as well as possible rising competition in large corporate banking. Nevertheless, we believe the 1Q results show CBQ's numbers are on track and it is a key Buying opportunity.

Key forecasts

	FY09A	FY10A	FY11F	FY12F	FY13F
Reported PTP (QRm)	1,359	1,635	1,886	2,125 ▼	2,393 ▼
Reported net profit (QRm)	1,524	1,635	1,886	2,125 ▼	2,393 ▼
Reported EPS (QR)	6.57	7.05	7.72	8.34 ▼	9.39 ▼
Normalised EPS (QR)	5.84	7.05	7.72	8.34 ▼	9.39 ▼
Dividend per share (QR)	5.73	7.00	5.68 ▼	5.86 ▼	6.66 ▼
Normalised PE (x)	12.40	10.30	9.39	8.69	7.72
Price/book value (x)	1.54	1.51	1.38	1.31	1.25
Dividend yield (%)	7.90	9.66	7.83	8.09	9.19
Return on avg equity (%)	14.10	15.20	15.80	15.50 ▼	17.50 ▼

Use of ▲ ▼ indicates that the line item has changed by at least 5%.
Accounting standard: IFRS
Source: Company data, Rasmala forecasts

year to Dec, fully diluted

Recent weak performance unjustified, in our view

CBQ's share price has fallen 22% ytd, vs a flat market. This is partly due to new regulations on Islamic banking and retail banking, but in both cases CBQ's exposure is less than that of others in the sector. Nor can the decline be attributed to associates, with the share prices of NBO and UAB falling 12% and 8% over the same time period. CBQ did make some slightly cautious comments on spreads and NPLs, but we do not believe this justifies the de-rating.

1Q10 results – second best in our Qatari banks coverage universe

There were two assumptions we were relying on for 1Q11 results: that CBQ could gain market share in public sector lending, and that the dip in fee income seen in 4Q10 would be temporary. Both these assumptions were justified. CBQ's headline numbers were up 45% qoq and just 2% below our forecast. We did see some pressure in asset yields, which was only in part off-set by lower liability yields. We believe this is due to a mix of competitive pressures, mix effects and liquidity. Provisioning exceeded our forecasts, in common with the rest of the sector, but the message was that it remained under control, falling 52% qoq.

Structurally lower ROE driven by low gearing, not low profitability

One reason CBQ has remained unloved has been its structurally lower ROE. Nevertheless, we argue that this is primarily driven by its low gearing, which is in turn the result of its substantial investments in associates. Indeed, our calculated ROAA is above our coverage universe average for 2010A (2.75% v 2.68%) and 2011F (2.89% v 2.69%).

TP reduction, driven by going ex-dividend, discount rate and asset yield

We trim our earnings forecast by 4% in 2011, as a result of lower asset yields and higher provisioning, placing our 2011F headline net income number 3% below the Bloomberg consensus. We modestly raise our discount rate from 10.66% to 10.81% on the basis of regulatory uncertainty and competitive pressures. Our new DCF-based target price is QR98.44. With CBQ trading at 9.4x our 2011F PE, and with potentially mid-teens levels of growth as it expands in the public sector, we believe it offers the best opportunity in Qatar.

Important disclosures can be found in the Disclosures Appendix.

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Table 1 : Results, 1Q11

QR m	1Q10A	4Q10A	1Q11A	1Q11F	Yoy	Qoq	v est
Balance Sheet							
Loans & Islamic Financing	31,623	33,567	34,808	34,864	10%	4%	0%
Financial instruments	9,811	10,024	12,355	13,248	26%	23%	-7%
Total Assets	55,451	62,520	60,780	62,347	10%	-3%	-3%
Customer deposits & Islamic Funding	28,808	34,188	31,339	35,148	9%	-8%	-11%
Total Liabilities	44,257	51,608	47,837	50,978	8%	-7%	-6%
Net Liquid Assets	4,237	9,387	4,176	4,678			
Shareholders' Equity	11,195	10,912	12,944	11,370	16%	19%	14%
NPL ratio	1.85%	2.40%	2.40%	2.31%			
Income Statement							
Net Interest & Islamic Returns	409	470	445	480	9%	-5%	-7%
Fees & Commissions	163	98	145	127	-11%	48%	15%
FX & Derivative	28	29	29	34	4%	1%	-15%
Other Operating Income	14	21	11	22	-20%	-49%	-49%
Core non-interest	205	148	185	182	-10%	25%	2%
Trading & Investments	(17)	(35)	36	13	-305%	-202%	n.a.
Non-core non-interest	(17)	(35)	36	13	-305%	-202%	185%
Total Non-Interest Income	188	113	221	195	18%	95%	13%
Total Banking Income	597	583	665	674	12%	14%	-1%
Total Operating Expenses	(196)	(209)	(206)	(231)	5%	-2%	-11%
Provisioning	(12)	(110)	(53)	(34)	341%	-52%	54%
Other Adjustments	21	44	40	49			
Profit before tax	410	309	446	458	9%	45%	-2%
Tax, Minorities & Appropriations	-	(33)	-	-			
Attributable Income	410	276	446	458	9%	62%	-2%
Headline Net Income	410	309	446	458	9%	45%	-2%
Comprehensive Income	456	358	417	458	-9%	16%	-9%

Source: Company data, Rasmala forecasts

Income statement

QRm	FY09A	FY10A	FY11F	FY12F	FY13F
Net interest income	1661	1778	1885	2041	2271
Non-interest income	770.1	656.4	860.2	990.7	1137
Total income	2431	2434	2745	3032	3408
Operating costs	-759.5	-787.3	-877.3	-1001	-1125
Goodwill (amort/impaird)	n/a	n/a	n/a	n/a	n/a
Other costs	0.00	0.00	0.00	0.00	0.00
<u>Pre-prov operating profit</u>	1671	1647	1868	2032	2283
Provisions charges	-465.6	-166.5	-171.4	-139.1	-160.0
<u>Post-prov op prof</u>	1206	1480	1696	1892	2123
Associates (pre-tax)	152.9	155.2	189.2	232.3	269.5
Other pre-tax items	0.00	0.00	0.00	0.00	0.00
Reported PTP	1359	1635	1886	2125	2393
Taxation	-34.2	-36.7	-54.0	-60.9	-68.6
Minority interests	0.00	0.00	0.00	0.00	0.00
Preference dividends	0.00	0.00	0.00	0.00	0.00
Other post-tax items	198.9	36.6	54.0	60.9	68.6
Reported net profit	1524	1635	1886	2125	2393
Tot normalised items	164.8	-0.20	0.00	0.00	0.00
Normalised PTP	1359	1635	1886	2125	2393
Normalised net profit	1359	1635	1886	2125	2393

Source: Company data, Rasmala forecasts

year to Dec

Balance sheet

QRm	FY09A	FY10A	FY11F	FY12F	FY13F
Net loans to customers	31929	33567	38972	44883	52023
Other int earn assets	15391	14261	17927	18627	19248
Goodwill	0.00	0.00	0.00	0.00	0.00
Oth non-int earn assets	5623	5989	6148	6958	7640
Total assets	57317	62520	66944	74507	83593
Total customer deposits	26639	34188	36230	41815	48571
Oth int-bearing liabs	17316	14547	14961	15908	17033
Non int-bearing liab	2685	2873	2767	3123	3591
Total liabilities	46640	51608	53959	60846	69195
Share capital	10677	10912	12985	13661	14398
Reserves	0.00	0.00	0.00	0.00	0.00
Total equity (excl min)	10677	10912	12985	13661	14398
Minority interests	0.00	0.00	0.00	0.00	0.00
Total liab & sh equity	57317	62520	66944	74507	83593
Risk weighted assets	48240	49821	57843	66617	77213
Est non-perf loans	n/a	n/a	n/a	n/a	n/a
Specific provisions	-549.4	-709.8	-773.2	-835.0	-911.5
General provisions	n/a	n/a	n/a	n/a	n/a

Source: Company data, Rasmala forecasts

year ended Dec

Capital

QRm	FY09A	FY10A	FY11F	FY12F	FY13F
Risk weighted assets	48240	49821	57843	66617	77213
Reported net profit	1524	1635	1886	2125	2393
Opening risk assets	63582	48240	49821	57843	66617
Closing risk assets	48240	49821	57843	66617	77213
Change in risk assets	-15342	1581	8023	8774	10596
Capital required	-1534	158.1	802.3	877.4	1060
Free capital flow	3058	1477	1083	1247	1333
Ordinary dividend paid	-1299	-1588	-1405	-1451	-1648
Share buy back/spec div	0.00	0.00	0.00	0.00	0.00
Equity / preference issue	1615	0.00	1615	0.00	0.00
Cash flow from financing	315.5	-1588	209.2	-1451	-1648
Net capital flow	3373	-110.6	1293	-203.2	-315.3
Tier 1 capital	8299	8294	9869	10383	10943
Tier 1 capital ratio (%)	17.2	16.6	17.1	15.6	14.2

Source: Company data, Rasmala forecasts

year to Dec

Company description

Buy

Price relative to country

Commercial Bank of Qatar (CBQ), established in 1975, is the country's second largest bank with a loan market share of 11% by value and a distribution network of 32 branches (24 conventional and eight Islamic). Although the bank provides retail, Islamic, and investment banking services, the bulk of its revenues continue to come from corporate banking. The bank actively seeks inorganic growth within the MENA region and currently owns 40% of UAE based United Arab Bank (UAB) and 34.9% of National Bank of Oman (NBO), as well as operating exclusive Diners Club franchises in Qatar, Oman and Egypt.



Strategic analysis

Average SWOT company score:

3

Revenue split, 2010

Strengths

4

An established brand, physical franchise and strong corporate relationships are key strengths of CBQ. We believe that CBQ has the best corporate banking product team in Qatar. It has also long experience (with NBO) of exporting expertise to associates.

Weaknesses

3

CBQ is poorly positioned for growth, with weak exposure to the public sector. In addition, with consumer, real estate and construction accounting for 50% of the loan book, CBQ is one of the more cyclical stocks in Qatar.

Opportunities

3

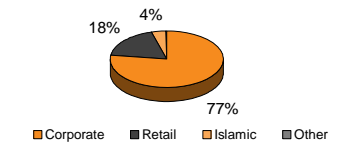
The primary issue is whether CBQ can capture public sector growth, using its strengths in loan structuring to offset its weakness in relationship banking. In addition, utilisation of excess capital to fund future loan growth, increasing associate revenue synergies are main opportunities.

Threats

3

The main challenge for CBQ is to make sure it gets its share of growth. To this end, it is currently aiming to take a slice of public sector lending. Meanwhile, QNB is expanding its operations into CBQ's home patch.

Scoring range is 1-5 (high score is good)



Source: Company report

Market data

Headquarters

Commercial Bank Plaza, 380 Al Markhiya street, 60 Al Dafna Area, P.O. Box 3232, Al Doha, Qatar

Website

www.cbq.com.qa

Shares in issue

247.4m

Freefloat

70%

Majority shareholders

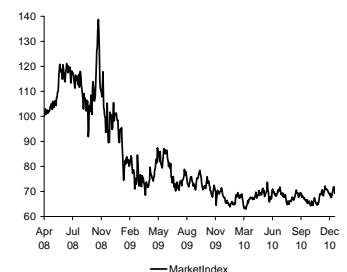
Qatar Investment Authority (17%), Qatar National Bank (3%), Deutsche Bank (3%)

Country view: Qatar

Country rel to M East & Africa

MENA markets are showing characteristics of a text book case of loss aversion. This is expected given the magnitude of losses investors experienced since 2008, with 2009 lagging emerging markets by a fairly wide margin. Rising oil prices and budget surpluses drove asset prices across the region higher resulting in a real-estate bubble that has negatively impacted speculators and the banking system. Bubbles do pop and recover over time if there is a legal system in place that enables the transfer of assets. The bad news is such a mechanism did not exist. The good news is that with the creation of RERA and the possibility of Strata Law, this could change and facilitate the transfer of properties from speculators to real investors.

The country view is set in consultation with the relevant company analyst but is the ultimate responsibility of the Strategy Team.



Competitive position

Average competitive score:

3+

Broker recommendations

Supplier power

5+

The lack of significant regulator control allows the banks to change contract arrangements (such as the base rate). This substantially increases the supplier power for all banks in Qatar.

Barriers to entry

3+

Strong local Government ownership in most banks coupled with branch limits for foreign banks keeps barriers to entry high.

Customer power

3+

Retail customer power is weak, but corporate and the public sector can be more demanding, if they were more price sensitive.

Substitute products

2+

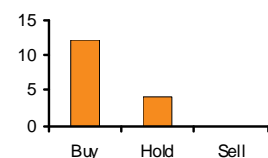
We believe the availability of substitute products (capital markets and wholesale lending) is on the rise, but it is currently unclear to what extent Qatar will favour its own banking system.

Rivalry

4+

Competition amongst local banks is low in Qatar. However, low growth rates have forced banks to look for growth wherever they can find it, and that may spark greater competition.

Scoring range 1-5 (high score is good) Plus = getting better Minus = getting worse



Source: Bloomberg

Recommendation structure

Absolute performance, long term (fundamental) recommendation: The recommendation is based on implied upside/downside for the stock from the target price and only reflects capital appreciation. A Buy/Sell implies upside/downside of 10% or more and a Hold less than 10%.

Performance parameters and horizon: Given the volatility of share prices and our pre-disposition not to change recommendations frequently, these performance parameters should be interpreted flexibly. Performance in this context only reflects capital appreciation and the horizon is 12 months.

Market or sector view: This view is the responsibility of the strategy team and a relative call on the performance of the market/sector relative to the region. Overweight/Underweight implies upside/downside of 10% or more and Neutral implies less than 10% upside/downside.

Target price: The target price is the level the stock should currently trade at if the market were to accept the analyst's view of the stock and if the necessary catalysts were in place to effect this change in perception within the performance horizon. In this way, therefore, the target price abstracts from the need to take a view on the market or sector. If it is felt that the catalysts are not fully in place to effect a re-rating of the stock to its warranted value, the target price will differ from 'fair' value.

Valuation and risks to target price

Comm Bank of Qatar (RIC: COMB.QA, Rec: Buy, CP: QR72.50, TP: QR98.44): We base our valuation on a 3-stage DDM: a 3-yr stage of explicit forecasts, a ten year stage of trend forecasts and a terminal stage based on a GGM. Downside risks include a significant rise in NPLs as only 15% of lending is to the public sector, with consumer, real estate and construction accounting for 48%, collectively. A rise in competition could spur compression in interest margins. Lastly, deteriorating market conditions could hamper UAE-based UAB's growth, thus lowering CBQ's overall ROE prospects.

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