

9 May 2011

Buy

Target price
Dh3.83 (from Dh3.65)

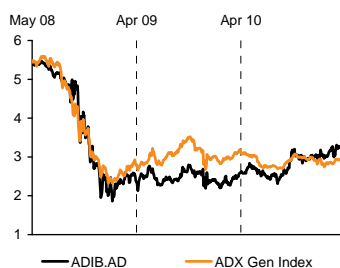
Price
Dh3.24

Short term (0-60 days)
n/a

Market view
No Weighting

Price performance

	(1M)	(3M)	(12M)
Price (Dh)	3.24	3.05	2.74
Absolute (%)	0.0	6.2	18.2
Rel market (%)	-4.0	4.2	21.8
Rel sector (%)	-7.8	-0.3	9.7



Market capitalisation
Dh7.66bn (€1.44bn)

Average (12M) daily turnover
Dh2.10m (US\$0.58m)

Sector: ADX Bank & Fin Index
RIC: ADIB.AD, ADIB.UH
Priced Dh3.24 at close 5 May 2011.
Source: Bloomberg

Analyst

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Abu Dhabi Islamic Bank

Progress, despite obstacles

We think ADIB has the fastest improving franchise of the UAE banks in terms of growth through the crisis, customer satisfaction and revenue diversification. Recent retail lending regulations, a troubled HNW portfolio and property market exposure raise queries, but not enough to eliminate the upside potential we see.

Key forecasts

	FY09A	FY10A	FY11F	FY12F	FY13F
Reported PTP (Dhm)	75.00	1,071	1,200 ▼	1,747 ▼	2,218
Reported net profit (Dhm)	77.80	1,023	1,200 ▼	1,747 ▼	2,218
Reported EPS (Dh)	0.01	0.40	0.45 ▼	0.68 ▼	0.88
Normalised EPS (Dh)	0.01	0.40	0.45 ▼	0.68 ▼	0.88
Dividend per share (Dh)	0.00	0.22	0.09 ▼	0.27 ▼	0.41
Normalised PE (x)	557.2	8.11	7.17	4.76	3.69
Price/book value (x)	1.49	1.37	1.19	1.04	0.90
Dividend yield (%)	0.00	6.68	2.78	8.43	12.60
Return on avg equity (%)	1.50	19.10	20.00 ▼	25.30 ▼	27.90

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

Strong 2010 yet to follow through into 2011

After customer service and product improvements, the results in 2010 were characterised by customer acquisition, market share improvements and increased revenue diversity particularly through fee and commission growth. However, after an average net customer acquisition of 20,908 per quarter through 2010, this slowed to 2,211 in 1Q11, with loan growth declining to 0.7% qoq in the same period.

HNW portfolio and retail banking regulations also providing headwinds

We believe that much of the legacy high net worth portfolio (13% of the loan book) is linked to property transactions. With the sales and rental markets still in the doldrums, this represents a risk. However, we believe any such NPLs will not, in general, go bad. Another issue is the impact of retail banking regulations, which is a concern given 60% of ADIB's book is retail. We believe there will be an impact on growth and fee income, although the latter will be smaller and offset by continued revenue diversification.

Relatively sanguine, but still downgrading 2011 numbers

In light of 4Q10 and 1Q11 loan growth weakness and weaker 2011 guidance we are reducing our 2011 loans forecast by 11%, and make compensating adjustments elsewhere on the balance sheet. We lower our forecast for deposits in particular by 15% as ADIB makes more use of capital market financing. This is also reflected in reductions in net Islamic returns of 9% and fee income of 18%, as well as possible further impairments of property valuations at Burooj Properties.

Still an underappreciated quality stock

In spite of downgrades, we believe that ADIB is moving in the right direction. There is still low-hanging fruit, such as moving Burooj Properties back to profitability, addressing the high (43% 1Q11) cost-income ratio, bringing the new branches up to speed and putting the new private banking operation on the right track. More speculatively, ADIB Egypt may benefit from the increased prominence of Islamic Banking in Egypt.

Important disclosures can be found in the Disclosures Appendix.

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Income statement

Dhm	FY09A	FY10A	FY11F	FY12F	FY13F
Net interest income	2109	2596	2720	2917	3245
Non-interest income	357.3	371.5	351.0	568.4	763.9
Total income	2466	2967	3071	3486	4009
Operating costs	-996.4	-1304	-1393	-1394	-1563
Goodwill (amort/impaired)	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>	1469	1663	1678	2091	2445
Provisions charges	-1391	-606.6	-499.5	-378.6	-301.6
<u>Post-prov op prof</u>	78.2	1056	1179	1713	2144
Associates (pre-tax)	-3.22	14.8	21.0	33.8	74.3
Other pre-tax items	0.00	0.00	0.00	0.00	0.00
Reported PTP	75.0	1071	1200	1747	2218
Taxation	-1.03	-6.82	-11.6	-16.9	-21.4
Minority interests	-0.25	-0.22	-0.06	-0.06	-0.06
Preference dividends	-60.0	-120.0	-120.0	-120.0	-120.0
Other post-tax items	64.0	79.2	131.6	136.9	141.4
Reported net profit	77.8	1023	1200	1747	2218
Tot normalised items	0.00	0.00	0.00	0.00	0.00
Normalised PTP	75.0	1071	1200	1747	2218
Normalised net profit	77.8	1023	1200	1747	2218

Source: Company data, Rasmala forecasts

year to Dec

Balance sheet

Dhm	FY09A	FY10A	FY11F	FY12F	FY13F
Net loans to customers	40474	47953	51346	57257	64986
Other int earn assets	14658	15730	11810	14028	15922
Goodwill	0.00	0.00	0.00	0.00	0.00
Oth non-int earn assets	3194	3685	4969	5592	6315
Total assets	64084	75258	75186	84069	94565
Total customer deposits	48220	56517	54941	61265	68885
Oth int-bearing liabs	6424	8538	9562	10489	11651
Non int-bearing liab	2297	2610	2253	2920	3525
Total liabilities	56940	67665	66756	74674	84062
Share capital	5141	5589	6427	7391	8500
Reserves	0.00	0.00	0.00	0.00	0.00
Total equity (excl min)	7141	7589	8427	9391	10500
Minority interests	2.86	3.08	3.08	3.08	3.08
Total liab & sh equity	64084	75258	75186	84069	94565
Risk weighted assets	53011	61894	66275	73904	83880
Est non-perf loans	n/a	n/a	n/a	n/a	n/a
Specific provisions	-1751	-2277	-2733	-3057	-3298
General provisions	n/a	n/a	n/a	n/a	n/a

Source: Company data, Rasmala forecasts

year ended Dec

Capital

Dhm	FY09A	FY10A	FY11F	FY12F	FY13F
Risk weighted assets	53011	61894	66275	73904	83880
Reported net profit	77.8	1023	1200	1747	2218
Opening risk assets	41472	53011	61894	66275	73904
Closing risk assets	53011	61894	66275	73904	83880
Change in risk assets	11538	8884	4380	7630	9976
Capital required	1154	888.4	438.0	763.0	997.6
Free capital flow	-1016	255.0	881.8	1104	1341
Ordinary dividend paid	0.00	-511.8	-212.8	-645.5	-967.9
Share buy back/spec div	0.00	0.00	0.00	0.00	0.00
Equity / preference issue	0.00	0.00	0.00	0.00	0.00
Cash flow from financing	0.00	-511.8	-212.8	-645.5	-967.9
Net capital flow	-1016	-256.8	669.0	458.0	372.6
Tier 1 capital	7169	8069	8978	10025	11228
Tier 1 capital ratio (%)	13.5	13.0	13.5	13.6	13.4

Source: Company data, Rasmala forecasts

year to Dec

Standard ratios	ADIB					Dubai Islamic Bank			Qatar Islamic Bank		
Performance	FY09A	FY10A	FY11F	FY12F	FY13F	FY11F	FY12F	FY13F	FY11F	FY12F	FY13F
Non-int inc/gr op inc (%)	14.5	12.5	11.4	16.3	19.1	31.3	33.4	n/a	39.4	41.2	38.7
Cost/income (%)	40.4	44.0	45.3	40.0	39.0	41.2	41.2	n/a	27.3	26.4	26.9
Costs/average assets (%)	1.73	1.87	1.85	1.75	1.75	1.58	1.58	n/a	1.08	1.04	1.22
Net income growth (%)	-91.3	1338	11.6	45.6	27.0	32.2	27.0	n/a	11.7	30.2	14.4
Net cust loan growth (%)	18.4	18.5	7.08	11.5	13.5	4.47	8.64	n/a	17.7	19.0	18.4
Cust deposit growth (%)	28.6	17.2	-2.79	11.5	12.4	3.65	7.78	n/a	15.4	19.0	18.4
Net interest margin (%)	4.19	4.23	4.13	4.16	4.09	3.37	3.25	n/a	3.23	3.26	3.94
Return on avg assets (%)	0.24	1.64	1.75	2.34	2.62	1.45	1.75	n/a	2.58	2.76	3.19
Return on avg equity (%)	1.50	19.1	20.0	25.3	27.9	14.6	17.8	n/a	14.9	16.6	19.0
RORWA (%)	0.16	1.78	1.87	2.49	2.81	1.74	2.07	n/a	3.38	3.54	4.07
				year to Dec			year to Dec			year to Dec	
Valuation											
Normalised EPS growth (%)	-98.4	6767	13.1	50.7	29.0	36.0	27.0	n/a	1.80	23.5	14.4
Reported PE (x)	557.2	8.11	7.17	4.76	3.69	7.54	5.94	n/a	13.3	10.7	9.39
Normalised PE (x)	557.2	8.11	7.17	4.76	3.69	7.54	5.94	n/a	13.3	10.7	9.39
Price/book value (x)	1.49	1.37	1.19	1.04	0.90	0.95	0.90	n/a	1.80	1.68	1.57
Price/adjusted BVPS (x)	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Dividend yield (%)	0.00	6.68	2.78	8.43	12.6	8.07	8.41	n/a	5.07	5.28	6.47
				year to Dec			year to Dec			year to Dec	
Per share data	FY09A	FY10A	FY11F	FY12F	FY13F	Solvency	FY09A	FY10A	FY11F	FY12F	FY13F
Tot adj dil sh, ave (m)	2365	2365	2365	2365	2365	Tier 1 capital ratio (%)	13.5	13.0	13.5	13.6	13.4
Pre-prov prof/share (AED)	0.62	0.70	0.71	0.88	1.03	Total CAR (%)	17.0	16.0	16.7	16.7	16.4
Reported EPS (AED)	0.01	0.40	0.45	0.68	0.88	Equity/assets (%)	11.1	10.1	11.2	11.2	11.1
Normalised EPS (AED)	0.01	0.40	0.45	0.68	0.88	Net cust loans/dep (%)	83.9	84.8	93.5	93.5	94.3
Book value per sh (AED)	2.17	2.36	2.72	3.13	3.59	Rep NPL/gr cus adv (%)	0.00	0.00	0.00	0.00	0.00
Dividend per share (AED)	0.00	0.22	0.09	0.27	0.41	Tot prov/rep NPLs (%)	0.00	0.00	0.00	0.00	0.00
Dividend cover (x)	0.00	2.00	5.64	2.71	2.29	Bad debts/advances (%)	2.75	1.11	0.93	0.63	0.44
				year to Dec						year to Dec	

Priced as follows: ADIB.AD - Dh3.24; DISB.DU - Dh2.18; QISB.QA - QR79.10
Source: Company data, Rasmala forecasts

Valuation methodology

Stage 1 (2010-2013)			2010	2011	2012	2013
Explicit Dividends	Forecast CF to shareholders		512	213	646	968
NPV Stage 1		1,518	1,840	1,518	1,492	968
Stage 2 (2014-23)			Model Numbers			
Modelled Dividends	Excess Capital	951	ROE1	Growth	Capital Req'd	RWA
	Modelled Dividends	4,072	21%	15%	7,549	83,880
NPV Stage 2		3,844				
Stage 3 (2024+)			Model Numbers			
Terminal Value	2023	18,376	ROE1	Growth	Capital Req'd	
			11%	6%	30,541	
NPV Stage 3		3,692				
Total NPV	Stage 1 (2010-2013)	1,518	COE			
	Stage 2 (2014-23)	3,844	US RFR	3.31%		
	Stage 3 (2024+)	3,692	Country Risk Spread	5.00%		
NPV		9,054	Sector Risk Spread	3.00%		
			Stock Spread	3.00%		
Shares		2,365	Discount Rate	14.31%		
Price Target		3.83				
Price		3.24				
Upside/(Downside)		18%				

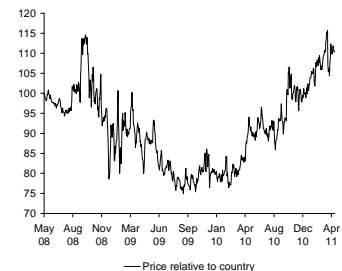
Source: Company data, Rasmala forecasts

Company description

Buy

Price relative to country

ADIB is a universal bank, based in Abu Dhabi, within the UAE, with a domestic branch network of 55 branches. Of these, ADIB's main presence is in Abu Dhabi Emirate, where it has 35 branches, with the remainder being split over Dubai and the Northern Emirates. Although ADIB is a universal bank, its main business is retail and private banking, which can be seen both in the divisional segmentation and in the loan book.



Strategic analysis

Average SWOT company score:

2

Loan book split, 2010

Strengths

3

Strong Emirati retail penetration (forming 80% of ADIB's customer base).

Weaknesses

1

A concentrated loan book (62.2% retail loans) combined with a high NPL ratio (8.5%) and low coverage ratio (43%) are primary weaknesses. The other concern is the property exposure through subsidiary Burooj Real Estate, amounting to a further Dh2.4bn (equal to 47% of common shareholders' equity).

Opportunities

2

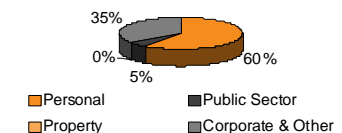
Expanding into new geographies (both domestic and foreign) - thereby increasing cross-selling activities and increasing the share of non-interest income. Further, the capability to increase leverage is also expected to drive future growth.

Threats

2

A significant decline in oil prices (thus limiting country growth rates) or geopolitical instability remain top threats for the UAE banks.

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



Source: Company data

Market data

Headquarters

Al Bateen Building, Bainuna Street, Al Bateen Area, P.O. Box 313, Abu Dhabi, United Arab Emirates

Website

www.adib.ae

Shares in issue

2364.7m

Freefloat

38%

Majority shareholders

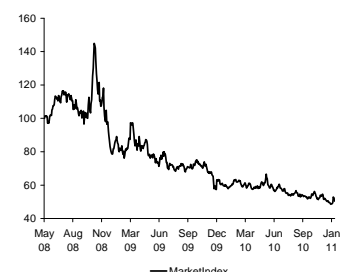
Emirates International Investment Co (41%), Abu Dhabi Investment Council (8%)

Country view: United Arab Emirates

Country rel to M East & Africa

MENA markets are showing characteristics of a textbook 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:

4+

Broker recommendations

Supplier power

3+

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 the UAE.

Barriers to entry

4+

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

Customer power

5+

Customer power is extremely low in the UAE, as any change in bank policies has to be accepted by clients. Points of contact at institutions remain limited, thus raising customer redressal issues.

Substitute products

4+

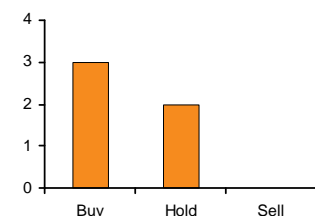
We believe the availability of substitute products (capital markets and syndicate loans) has diminished in recent times, thus improving margin capabilities for banks in the core interest business.

Rivalry

4+

Competition (and price war) among local banks is low. However, recent low growth has forced a few newer institutions to lower product prices, indicating a trend towards more competition long term.

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

Abu Dhabi Islamic Bank (RIC: ADIB.AD, Rec: Buy, CP: Dh3.24, TP: Dh3.83): 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 to our GGM-based valuation and target price include a severe decline in Abu Dhabi real estate prices and management not being able to achieve its core business targets of 25% ROE, a cost-to-income ratio of 33% and annual growth of 20%.

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