

Flash Note

October 21, 2011

Bank Audi Q3/2011 Results
Sector: Banking

Country: Lebanon

Bank Audi's net profits at USD 92.1 million in Q3/11 flat year on year, although up 7% in 9M/11 year on year

Bank Audi's net profits totaled USD 92.1 million in Q3/11 relatively unchanged from USD 91.7 million in Q3/10 although growing 7% yoy in 9M/11 to USD 271.3 million. Diluted EPS was USD 0.25 in Q3/11 flat from Q3/10, while 9M/11 EPS was up 8.5% yoy to USD 0.73 as compared to USD 0.67 in 9M/10. A decline by 11% in net interest income between Q3/10 and Q3/11 on the back of tepid balance sheet growth and weak lending activity was more than counterbalanced by a 41% increase in non-interest income in Q3/11 over Q3/10 mainly driven by a surge in trading and investment income (+81%). Higher provisioning levels as well as a higher income tax rate at 19.9% in Q3/11 up from 18.3% in Q3/10 capped the bottom line, as bank efficiencies were unchanged represented by a cost-to-income of 47.4% in Q3/11 relatively stable yoy.

Summary Income Statement

<i>in USD millions</i>	Q3 11	Q3 10	YoY %	9M 11	9M 10	YoY %
Net interest income	132.0	147.7	-11%	397.8	361.3	10%
<i>As a % of total operating income</i>	53.4%	64.4%		54.9%	55.5%	
Fees and commission income	45.1	42.9	5%	135.6	128.4	6%
Trading and investment income	70.2	38.8	81%	191.5	161.5	19%
Non-interest income	115.3	81.7	41%	327.1	289.9	13%
<i>As a % of total operating income</i>	46.6%	35.6%		45.1%	44.5%	
Total operating income	247.3	229.4	8%	725.0	651.2	11%
Personnel expenses	-66.8	-57.4	16%	-192.7	-167.6	15%
Non personnel expenses	-50.4	-51.9	-3%	-143.1	-138.0	4%
Total operating expenses	-117.2	-109.3	7%	-335.8	-305.6	10%
<i>Cost-to-income</i>	47.4%	47.6%		46.3%	46.9%	
Pre-provision profit before tax	130.1	120.1	8%	389.2	345.6	13%
Provisions	-15.1	-7.9	92%	-51.9	-30.3	71%
<i>Provisions as a % of pre-provision profit</i>	11.6%	6.5%		13.3%	8.8%	
Profit before tax	115.0	112.3	2%	337.3	315.3	7%
Income tax	-22.9	-20.6	11%	-66.1	-61.9	7%
<i>Income tax rate</i>	19.9%	18.3%		19.6%	19.6%	
Net profits	92.1	91.7	0%	271.3	253.4	7%
Minority interest	0.8	3.8	-78%	6.3	10.5	-40%
Net profits (group share)	91.3	87.9	4%	265.0	242.8	9%
EPS to common (basic)	0.25	0.25		0.73	0.69	
EPS to common (diluted)	0.25	0.25		0.73	0.67	
EPS TTM to common (diluted)	1.00					

Source: Bank Audi

Net interest income down 11% yoy in Q3/11 reflects tepid balance sheet growth and weak lending activity

Net interest income totaled USD 132.0 million in Q3/11, down 11% from USD 147.7 million in Q3/10 which could be partly attributed to stagnation in balance sheet growth, weak lending activity, and pressures on margins on the back of lower yields on T-bills and Eurobonds. Despite the weaker balance sheet of the Lebanese government, Lebanese government securities have relatively outperformed MENA and emerging markets, thereby tightening spreads this year. In 9M/11, net interest income amounted to USD 397.8 million representing a 10% growth rate compared to 9M/10.

Non-interest income up 41% in Q3/11 mainly driven by a surge in trading and investment income

Bank Audi witnessed a 41% increase in non-interest income yoy at USD 115.3 million in Q3/11 compared to USD 81.7 million in Q3/10, as an increase in fees and commissions income of 5% to USD 45.1 million was registered in parallel to a jump in trading and investment income to USD 70.2 million representing an increase of 81%. Consequently, the contribution of non-interest income to total operating

income increased to 47% in Q3/11 from 36% in Q3/10 hovering around the Bank's target of 40%. Simultaneously, the contribution of fees and commissions to total operating income remained almost stable at 18.2% in Q3/11 relatively unchanged from 18.7% in Q3/10. In 9M/11, non-interest income was up 13% yoy to USD 327.1 million driven by a 19% increase in trading and investment income and a 6% increase in fees and commissions income.

Higher provisions and income taxes put a strain on profits as bank efficiencies stagnate

Cost-efficiencies were flat in Q3/11 as the cost-to-income stood at 47.4% as compared to 47.6% in Q3/10, the reflection of similar growth rates in operating income and operating expenses (+8% and 7% respectively). Operating expenses were mainly driven by an increase in personnel expenses (+16% yoy in Q3/11) as non-personnel expenses decreased by 3% over the same period. While bank efficiencies remained stable, the increased provisions as well as the higher tax rate have capped earnings growth. Income tax rate stood at 19.9% in Q3/11 up from 18.3% in Q3/10. While provisions increased by 92% yoy in Q3/11 to USD 15.1 million, they are down sequentially from Q2/11 as we expect some improved visibility in regional operations, particularly in Egypt.

Summary Balance Sheet

USD millions	Q3 11	Q2 11	Q4 10	QoQ %	YTD %
Cash and balances	5,245.7	4,930.7	4,434.2	6%	18%
Due from banks and other financial institutions	3,438.2	4,482.1	4,204.3	-23%	-18%
Financial assets	10,506.8	10,117.8	10,583.1	4%	-1%
Loans and advances	8,562.3	8,566.3	8,547.5	0%	0%
Intangible assets and goodwill	200.6	203.2	200.8	-1%	0%
Other assets	760.6	781.7	718.1	-3%	6%
Total assets	28,714.3	29,081.8	28,688.0	-1%	0%
Due to Central Banks	89.5	88.5	88.5	1%	1%
Due to banks and other financial institutions	618.0	597.4	603.4	3%	2%
Deposits	24,877.0	25,267.7	24,847.8	-2%	0%
<i>Immediate liquidity to deposits</i>	<i>34.9%</i>	<i>37.3%</i>	<i>34.8%</i>		
<i>Loans- to- deposits</i>	<i>34.4%</i>	<i>33.9%</i>	<i>34.4%</i>		
Other liabilities	813.6	819.6	727.9	-1%	12%
Total liabilities	26,398.2	26,773.2	26,267.6	-1%	0%
Shareholders' equity	1,948.1	1,942.5	2,052.7	0%	-5%
Preferred shares	250.0	250.0	250.0	0%	0%
Minority interest	118.0	116.1	117.7	2%	0%
Total shareholders' equity	2,316.1	2,308.6	2,420.4	0%	-4%
Total liabilities and shareholders' equity	28,714.3	29,081.8	28,688.0	-1%	0%
Book value per share	6.31	6.29	6.61	0%	-5%
Book value per share to common	5.59	5.57	5.89	0%	-5%
Tangible book value per share to common	5.01	4.99	5.31	0%	-6%

Source: Bank Audi

Flat balance sheet aggregates since the beginning of 2011 as liquidity holds steady

Deposit growth, the main balance sheet driver, has been tepid since the beginning of 2011 as macroeconomic conditions on the domestic scene were softer and capital inflows into Lebanon slowed down. Consequently, Bank Audi's assets, deposits and loans stagnated since the beginning of 2011 and amounted to USD 28,714 million, USD 24,877 million and USD 8,562 million by the end of Q3/11. At these growth levels, the loans-to-deposits ratio remained stable at roughly 34%, an indicator of the Bank's ample liquidity levels, providing financial flexibility to resume its expansion strategy once the visibility on the regional scene improves. It should be noted that Q3/11 witnessed slight deposit outflows as the deposit base narrowed by 2% over the quarter which could be possibly attributed to the Bank's interest margin preservation strategy by maintaining its cost of funds and outflows from its Syrian entity.

Low levels of NPLs and increased levels of provisioning given the developments in Syria and Egypt

Bank Audi's net doubtful loans represented 0.51% of gross loans at end Q3/11, unchanged from the previous quarter; while the coverage of those loans by specific provisions reached 81.2% at end-September 2011 (vs. 80% at end-June 2011 and 73% at end-December 2010). The increasing level of provisions is mainly attributed to management's cautious approach and increasing preventive measures facing the recent events in Syria and Egypt, despite no evidence of credit quality deterioration.

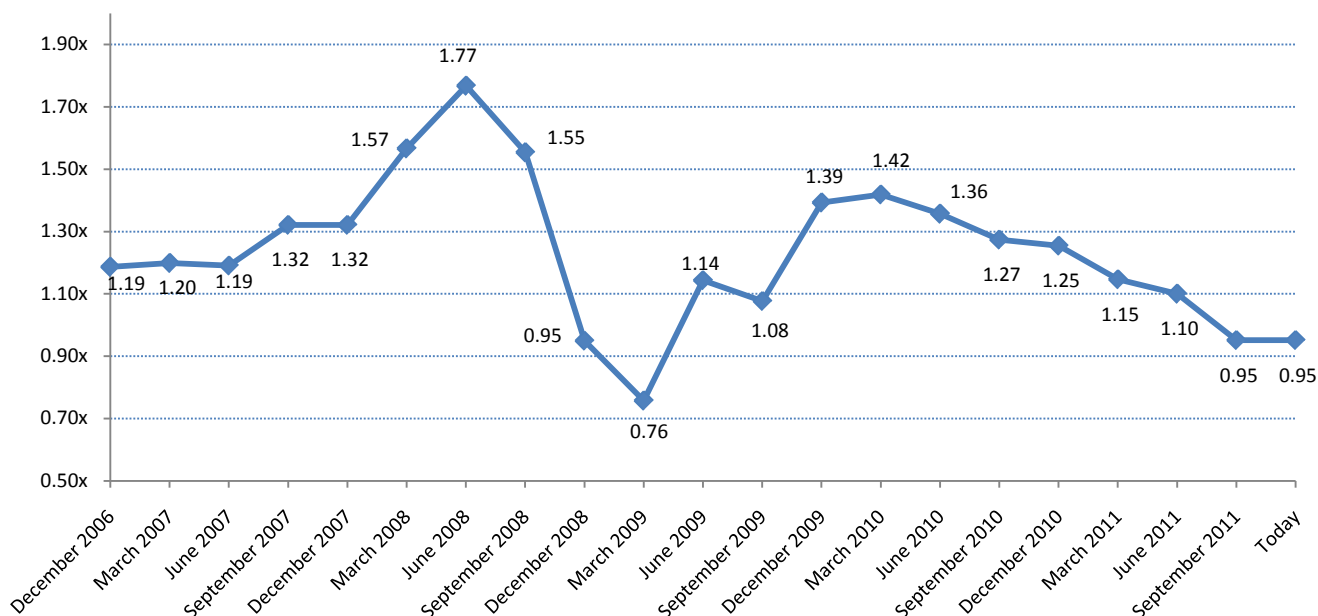
Capitalization levels and profitability ratios unchanged quarter on quarter

Bank Audi's capital adequacy ratio was 11%, highlighting a comfortable capitalization level, and roughly unchanged from Q2/11. The firm's equity to assets ratio was 8.0%, down from 8.1% in Q2/11 and 8.4% in Q4/10. The TTM ROA was unchanged at 1.3% from Q2 11. The TTM EPS was USD 1.00 in Q3/11, while book value per share is estimated at USD 6.31 (USD 5.59 to common).

Continue to expect moderate bottom line growth into year-end although highlight shares are trading at potentially oversold levels

As a function of the softer Lebanese economy impacting lending activity and weaker capital inflows from regional turmoil moderating funding, we expect Bank Audi will see softer earnings growth in 2011 as moderating income is met with higher provisions and flat bank efficiencies. We believe management has prudently deferred growth plans and focused on safeguarding assets while growing earnings within a difficult operating framework in Lebanon and the region. Bank Audi shares are down 28% from their 52-week highs and we see them oversold at these levels, trading at 1.07x P/B, 6.0x P/E TTM, and offering a dividend yield of 6.7%. In fact with shares trading at USD 6.00, applying a historical P/E average of 7x on 12-month recurring earnings of 1 USD per share would equate to a discount to Lebanese earnings and assigning no value to international operations.

Bank Audi Historical P/B



Source: Bank Audi, Zawya, Beirut Stock Exchange

Contacts:

Head of Research: Nadim Kabbara, CFA

n.kabbara@ffapivatebank.com

+961 1 985 195

Analyst: Raya Freyha

r.freyha@ffapivatebank.com

+961 1 985 195

Sales and Trading, FFA Private Bank (Beirut)

+961 1 985 225

Sales and Trading, FFA Dubai Ltd (DIFC)

+ 971 4 3230300

Disclaimer:

This document has been issued by FFA Private Bank for informational purposes only. This document is not an offer or a solicitation to buy or sell the securities mentioned. This document was prepared by FFA Private Bank from sources it believes to be reliable. Past performance is not necessarily indicative of future results. Therefore, FFA Private Bank makes no guarantee or warranty to the accuracy and thoroughness of the information mentioned, and accepts no responsibility or liability for damages incurred as a result of opinions formed and decisions made based on information presented in this document. All opinions expressed herein are subject to change without prior notice.