

## Flash Note

April 19, 2013

## Bank Audi Q1/13 Results

Sector: Banking

Country: Lebanon

### MARKETWEIGHT

Target Price	USD 7.00
Closing Price	USD 6.60
Year to Date %	8.4%
52 Week Range	5.15 -6.90
Market Cap.	USD 2,308.3 million
Dividend Yield	6.1%
P/E (TTM)	6.7x
P/B to Common (TTM)	1.04x

Note: the share data represents Bank Audi listed shares (Bloomberg ticker: AUDI LB)

Source: Bloomberg, FFA Private Bank

### Net profits at USD 85.5 million in Q1/13, 9.5% down yoy and below our estimates

Bank Audi's net profits amounted to USD 85.5 million in Q1/13, down from USD 94.5 million in Q1/12, while diluted EPS was USD 0.23 down from USD 0.26. This year on year decrease in the bottom line in Q1/13 can be attributed to a 4% decline in operating income to USD 255 million coupled with an 18% surge in operating expenses from the launch and expansion of Turkish operations following an organic growth strategy. We note that operating income was weak as roughly stable interest income was matched by softer fees and commissions (-7%) and lower booked gains on financial investments. Lower provisions and taxes helped soften pressure on net profits. On the balance sheet side, the Bank saw solid growth in key aggregates at high single digits to low double digits in three months' time which is mostly attributed to Turkish operations.

As highlighted in table 1 net earnings were below our USD 104 estimate on account of lower than expected operating income (USD 255 million vs. est. 298 million) coupled with higher than expected cost-to-income ratio (51.8% vs. est. 48%) and despite lower than expected provisions (USD 14 million vs. est. USD 24 million).

Table 1: Bank Audi Q1/13 results vs. FFA Private Bank estimates

USD million	Q1/13a	FFA Q1/13e	Q4 12a	Q1/12a	QoQ %	YoY %
Net interest income	142	164	141	143	0%	-1%
Operating income	255	298	285	266	-11%	-4%
Net profits	86	103	68	94	26%	-9%
Diluted EPS	0.23	0.27	0.18	0.26	28%	-12%
Assets	33,284	31,950	31,302	28,661	6%	16%
Deposits	28,735	27,479	26,805	24,388	7%	18%
Loans	11,587	10,584	10,428	8,866	11%	31%
BVPS to common	6.36	6.48	6.33	6.13	0%	4%
FFA Cost-to-income ratio	51.8%	48.0%	57.0%	41.9%		
Loans-to-deposits ratio	40.3%	38.5%	38.9%	36.4%		

Source: Bank Audi and FFA Private Bank estimates

Table 2: Summary Income Statement

USD million	Q1 13	Q4 12	Q1 12	QoQ%	YoY %
Net interest income	141.6	141.3	142.8	0.2%	-0.9%
As a % of total operating income	55.6%	49.6%	53.7%		
Fees and commissions income	43.9	50.6	47.3	-13.3%	-7.3%
Trading and investment income	69.1	93.2	76.0	-25.8%	-9.1%
Non-interest income	113.0	143.8	123.4	-21.4%	-8.4%
As a % of total operating income	44.4%	50.4%	46.3%		
Total operating income	254.5	285.0	266.2	-10.7%	-4.4%
Personnel expenses	(72.8)	(79.5)	(59.7)	-8.5%	22.0%
Non-personnel expenses	(59.0)	(82.9)	(52.0)	-28.8%	13.5%
Total operating expenses	(131.8)	(162.5)	(111.6)	-18.9%	18.0%
Cost-to-income ratio	51.8%	57.0%	41.9%		
Pre-provision profit before tax	122.8	122.6	154.6	0.2%	-20.6%
Provisions	(14.2)	(27.2)	(31.1)	-47.7%	-54.3%
Provisions as a % of pre-provision profit	11.6%	22.2%	20.1%		
Profit before tax	108.5	95.4	123.4	13.8%	-12.1%
Income tax	(23.0)	(17.3)	(29.5)	33.5%	-22.0%
Income tax rate	21.2%	18.1%	23.9%		
Profit after tax from continuing operations	85.5	84.6	93.9	1.0%	-8.9%
Result of discontinued operations	0.0	(10.4)	0.6		
Net profits	85.5	67.7	94.5	26.3%	-9.5%
Minority interest	(0.3)	(6.1)	(1.1)	-95.3%	-72.7%
Net profits (group share)	85.2	61.6	93.4	38.4%	-8.7%
EPS to common (basic)	0.23	0.18	0.26	27.9%	-12.1%
EPS to common (diluted)	0.23	0.18	0.26	28.1%	-12.0%
EPS TTM to common (diluted)	0.98				

Source: Bank Audi

### Net interest income flat in Q1/12 given pressures on interest margins

Bank Audi's net interest income totaled USD 141.6 million in Q1/13, roughly flat from Q4/12 and Q1/12 stemming from narrowing interest spreads and despite solid balance sheet expansion (+6% Ytd and +16% YoY). In fact interest spreads have declined to 1.85% in Q1/13 well below their 2% level in the context of relatively low yields on the uses of funds. The latest statistics from the Association of Banks in Lebanon reveal that Lebanese banks are still operating in a low interest environment, limiting potential to improve earning asset yields. Figures highlight that spreads in USD have decreased to 1.57% in February 2013 down from 1.66% one year earlier driven by i) lower rates on LIBOR (average 3 months on USD deposits down to 0.29% down from 0.50%), ii) lower yields on Eurobonds (weighted average down to 7.06% from 7.48%), iii) lower rates on deposits at the BDL (average down to 2.79% from 3.06%) and slightly lower lending rates (weighted average down to 6.97% from 7.05%). On the LBP side, it should be noted that yields on T-bills and CDs issued were also lower YoY (at 6.59% and 8.99% respectively in February 2013 down from a respective 6.79% and 9.23% a year earlier). Looking ahead, Bank Audi's margins could benefit from redeployment of liquidity and investments into more attractive yielding avenues including lending in Turkish operations.

### Non-interest income down 8% YoY in Q1/13 on lower fees and commissions and booked gains on financial investments

In Q1/13 Bank Audi saw an 8% decrease in non-interest income YoY at USD 113 million compared to USD 123 million in Q1/12, as fees and commissions income declined 7% to USD 44 million and trading and investment income decreased by 9% on the back of lower booked gains on financial investments. Looking at the earnings mix for Q1/13, we note: i) the contribution of non-interest income to total operating income at 44% in Q1/13 slightly down from 46% in Q1/12 and ii) the contribution of fees and commissions to total operating income at 17% in Q1/13 compared to 18% in Q1/12 and in the previous quarter. In the medium term, Bank Audi is seeking a breakdown of revenues between interest income and non-interest income at 60%/40%.

### Higher operating expenses mostly linked to Turkey expansion weighed on earnings in Q1/13, while lower provisions helped

Cost-efficiencies deteriorated in Q1/13 as the cost-to-income increased to 52% up from 41.9% in Q1/12 (yet lower than 57% in previous quarter). This can be attributed to an 18% increase in operating expenses and a 4% decline in operating income. Operating expenses were driven by an increase in both personnel expenses and non-personnel expenses (at a respective +22% and +14% YoY in Q1/13). The significant growth in operating expenses to reach USD 132 million is attributed to launch of operations in Turkey encompassing a network of 9 branches and 523 employees. In parallel, lower provisions as well as a lower tax rate alleviated some pressures on bottom line. Allocated provisions amounted to USD 14 million in Q1/13 compared to USD 27 million in Q4/12 and USD 31 million in Q1/12 in light of a potential cap in NPL levels given that the Bank have been downsizing its loan portfolio in Syria thus limiting the impact on consolidated asset quality. Income tax rate stood at 21% in Q1/13, down from 24% in Q1/12 (yet higher than 18% in Q4/12).

**Table 3: Summary Balance Sheet**

USD million	Q1 13a	Q4 12a	Q1 12a	QoQ%	YoY%
Cash and balances	6,663.6	6,276.9	5,883.8	6.2%	13.3%
Due from banks and other financial institutions	3,473.3	3,543.1	2,906.9	-2.0%	19.5%
Financial assets	10,656.9	10,209.5	10,049.1	4.4%	6.0%
<b>Loans and advances</b>	<b>11,586.7</b>	<b>10,428.5</b>	<b>8,865.8</b>	<b>11.1%</b>	<b>30.7%</b>
Intangible assets and goodwill	175.9	180.7	184.7	-2.7%	-4.8%
Other assets	728.0	663.1	771.3	9.8%	-5.6%
<b>Total assets</b>	<b>33,284.4</b>	<b>31,301.8</b>	<b>28,661.5</b>	<b>6.3%</b>	<b>16.1%</b>
Due to Central Banks	88.9	88.3	267.4	0.7%	-66.7%
Due to banks and other financial institutions	1,184.5	1,229.0	798.3	-3.6%	48.4%
<b>Deposits</b>	<b>28,735.4</b>	<b>26,804.6</b>	<b>24,388.4</b>	<b>7.2%</b>	<b>17.8%</b>
<i>Immediate liquidity to deposits</i>	<i>35.3%</i>	<i>36.6%</i>	<i>36.0%</i>		
<i>Loans- to- deposits</i>	<i>40.3%</i>	<i>38.9%</i>	<i>36.4%</i>		
Other liabilities	592.7	502.5	488.6	18.0%	21.3%
<b>Total liabilities</b>	<b>30,601.5</b>	<b>28,624.4</b>	<b>26,186.3</b>	<b>6.9%</b>	<b>16.9%</b>
Shareholders' equity	2,222.8	2,213.2	2,141.6	0.4%	3.8%
Preferred shares	400.0	400.0	250.0	0.0%	60.0%
Minority interest	60.1	64.2	83.6	-6.5%	-28.1%
<b>Total shareholders' equity</b>	<b>2,682.9</b>	<b>2,677.4</b>	<b>2,475.2</b>	<b>0.2%</b>	<b>8.4%</b>
<b>Total liabilities and shareholders' equity</b>	<b>33,284.4</b>	<b>31,301.8</b>	<b>28,661.5</b>	<b>6.3%</b>	<b>16.1%</b>
Book value per share	7.50	7.47	6.84	0.4%	9.6%
<b>Book value per share to common</b>	<b>6.36</b>	<b>6.33</b>	<b>6.13</b>	<b>0.4%</b>	<b>3.7%</b>
Tangible book value per share to common	5.85	5.81	5.60	0.7%	4.5%

Source: Bank Audi

### **Solid growth in key balance sheet indicators mostly driven by recently launched Turkish operations**

Bank Audi's consolidated assets and deposits grew by a solid 6% and 7% respectively in the first three months of 2013 to a respective USD 33,284 million and USD 28,735 million. The bulk of this increase stems from Turkey where Bank Audi launched its banking activities in late 2012 raising USD 4.3 billion in assets and USD 3.6 billion in deposits in 5 months. Turkey now represents 13% of the Group consolidated assets and raised the contribution of entities abroad to consolidated assets from 32.4% at end-December 2012 to 36.3% at end-March 2013 in line with Management's objective to reach a more balanced breakdown of assets between Lebanon and abroad. Also, we mention that the expansion of Turkish operations fully offset further deposit outflows in Syrian operations and weaker volumes into the Egyptian entity. During Q1/13 the assets of Bank Audi Syria had contracted to USD 558 million while assets in Egypt declined by 5% according to Management to USD 3,245 million.

The consolidated loan portfolio grew by a strong 11% in the first three months of 2013 to USD 11,587 million mainly attributed to banking activities in Turkey. The loans-to-deposits ratio breached the 40% level standing at 40.3% at the end of Q1/13 from 38.9% at the end of Q4/12 and 36.4% a year earlier, while the immediate liquidity to deposits ratio remained roughly stable at 35%.

### **Contained NPLs and satisfactory provisioning levels result in lower provisions in Q1/13**

Bank Audi's consolidated gross NPLs stood at 2.7% by the end of Q1/13 unchanged from previous quarter. The coverage of gross doubtful loans by specific loan loss provisions was 71% in Q1/13 down from 76% in Q4/12 and highlighting satisfactory provisioning levels particularly when including collective at 0.9% of net loans. Additionally, we favorably view a significant decrease in bad debts written off to around USD 10 million in Q1/13 compared to a total of USD 105 million for the full year 2012.

### **CAR III at 11% and ROE estimated at around 14.5% strained by Turkish expansion**

Bank Audi's capitalization and profitability were strained by the organic expansion in Turkey. On one hand, Bank Audi's capital adequacy ratio (Basel III) went down from 11.6% in 2012 to 11% and the firm's equity to assets ratio was down to 8.1% from 8.6% in previous quarter. On another hand, the TTM ROA stood at 1.2% compared to 1.3% in the previous quarter while the TTM ROE is estimated around 14.5% compared to an estimated 15.2% in Q4/12, which is still interesting in our view. The TTM EPS was USD 0.98 in Q1/13 while book value per share is estimated at USD 7.50 (USD 6.36 to common). Based on today's listed share price, Bank Audi is trading at 6.7x P/E, 0.88x P/B (P/B to common of 1.04x) and dividend yield of 6.1%. We highlight the relative attractiveness of Lebanese banks dividends and we note that Lebanon has the 2<sup>nd</sup> highest dividend yield in the MENA region after UAE. Bank Audi paid its dividends earlier this month with common shareholders receiving LBP 603 per share (USD 0.40 gross or USD 0.38 net of 5% withholding tax).

### **Recent AGM resolved to issue new classes of preferred shares including Series G and H to increase capitalization levels**

AGM's resolutions included: i) the cancellation of the series D and increase the Bank's capital to round up the individual nominal value of the Bank's Shares to LBP 1,299 ii) the increase of the Bank's capital through the issuance of 1,500,000 series G preferred shares and 750,000 series H preferred shares.

Bank Audi's total preferred shares would then amount to USD 500 million up from the current USD 400 million and would strengthen the capital base and support the growth strategy.

---

#### 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.