



Bank Audi Q2/15 Results

Sector: Banking
Country: Lebanon

MARKETWEIGHT

Target Price	USD 7.50
Closing Price	USD 6.00
Year to Date %	0.0%
52 Week Range	5.80 - 6.99
Market Cap.	USD 2,398 million
Dividend Yield	6.7%
P/E (TTM)	7.2x
P/B to Common	0.88x

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

Source: Bloomberg, FFA Private Bank

Net profits were at USD 102 million in Q2/15 (+2% QoQ, -2% YoY) below our USD 107 million estimate on lower than expected operating income partially offset by lighter opex and income tax

Bank Audi's net profits were at USD 102 million in Q2/15 (+2% QoQ, -2% YoY) below our USD 107 million estimate. Diluted EPS was at USD 0.23 unchanged from Q1/15 and vs. USD 0.27 in Q2/14 and FFA est. USD 0.24. While operating income came in lower than our estimates from mainly lighter than expected financial gains, the negative variance to our expectations was partially offset by lower opex, provisions and income tax. Cost-to-income ratio stood at ~54% in Q2/15, below our estimate. Provisions were lighter than our forecast at USD 28 million in Q2/15 equivalent to an estimated 67 bps annualized cost of risk, lower than Q1/15 cost of risk of 80 bps and considerably lower from exceptionally high 160 bps in Q4/14. NPL ratio was at 3.1% in Q2/15 slightly lower than 3.2% in previous quarter. Tax rate moderated at 18.6%, lower than our estimate of 23.0% and Q1/15 rate of 22.2%, after a spike to 32.0% observed in Q4/14. On the balance sheet side, assets, deposits and loans grew 2%, 3% and 4% respectively QoQ, in line with our estimates, despite challenging economic and political conditions across the region, with assets mainly driven by operations in Egypt (+18%) and Turkey (+13%) in addition to domestic operations. LDR reached 47.2% at the end of Q2/15 vs. FFA est. 46.8%. Looking at H1/15, net profits rose +7% YoY to USD 202 million with an EPS at USD 0.46 vs. USD 0.49 in H1/14 (due to capital increase).

Table 1: Bank Audi Q2/15 results vs. FFA Private Bank estimates

USD million except per share data	Q2/15a	FFA Q2/15e	Q1/15a	Q2/14a	QoQ %	YoY %
Net interest income	234	237	223	204	5%	15%
Operating income	336	374	339	335	-1%	0%
Net profits	102	107	100	104	2%	-2%
Diluted EPS to common	0.23	0.24	0.23	0.27	2%	-14%
Assets	42,310	42,097	41,458	39,262	2%	8%
Deposits	36,106	36,149	35,054	33,960	3%	6%
Loans	17,035	16,933	16,440	16,034	4%	6%
BVPS to common	6.78	7.24	7.10	6.28	-4%	8%
FFA Cost-to-income ratio	54.2%	54.8%	52.4%	57.1%		
Loans-to-deposits ratio	47.2%	46.8%	46.9%	47.2%		

Source: Company reports and FFA Private Bank estimates

Table 2: Summary Income Statement

USD million	Q2/15a	Q1/15a	Q2/14a	QoQ%	YoY%	H1/15a	H1/14a	YoY%
Net interest income	233.9	222.5	204.0	5.1%	14.6%	456.4	391.6	16.5%
As a % of total operating income	69.6%	65.6%	61.0%			67.6%	63.1%	
Fees and commissions income	66.7	59.2	63.1	12.6%	5.7%	125.9	115.2	9.3%
Trading and investment income	35.2	57.5	67.6	-38.8%	-47.9%	92.8	113.6	-18.3%
Non-interest income	101.9	116.8	130.7	-12.7%	-22.0%	218.7	228.7	-4.4%
As a % of total operating income	30.4%	34.4%	39.0%			32.4%	36.9%	
Total operating income	335.8	339.3	334.7	-1.0%	0.3%	675.1	620.4	8.8%
Personnel expenses	(103.3)	(101.4)	(107.6)	1.8%	-4.0%	(204.7)	(196.4)	4.2%
Non-personnel expenses	(78.7)	(76.3)	(83.4)	3.1%	-5.6%	(155.0)	(151.5)	2.3%
Total operating expenses	(182.0)	(177.7)	(191.0)	2.4%	-4.7%	(359.7)	(347.9)	3.4%
Cost-to-income ratio	54.2%	52.4%	57.1%			53.3%	56.1%	
Pre-provision profit before tax	153.8	161.5	143.7	-4.8%	7.1%	315.4	272.4	15.8%
Provisions	(28.5)	(33.0)	(14.6)	-13.8%	95.3%	(61.5)	(34.7)	77.4%
Provisions as a % of pre-provision profit	18.5%	20.4%	10.1%			19.5%	12.7%	
Profit before tax	125.4	128.5	129.1	-2.5%	-2.9%	253.9	237.8	6.8%
Income tax	(23.3)	(28.5)	(25.1)	-18.3%	-7.3%	(51.8)	(48.1)	7.8%
Income tax rate	18.6%	22.2%	19.5%			20.4%	20.2%	
Net profits	102.1	100.0	104.0	2.0%	-1.9%	202.1	189.8	6.5%
Minority interest	(4.8)	(4.4)	(3.1)			(9.2)	(5.1)	
Net profits (group share)	97.2	95.6	100.9	1.7%	-3.6%	192.9	184.6	4.5%
EPS to common (basic)	0.23	0.23	0.27	1.8%	-14.3%	0.46	0.49	-7.0%
EPS to common (diluted)	0.23	0.23	0.27	1.8%	-14.3%	0.46	0.49	-7.0%
EPS TTM to common	0.83							

Source: Company reports

Net interest income rose QoQ in Q2/15 (+5%) on higher balance sheet volumes, improved margins and increased benefit from Odea Bank

Bank Audi's net interest income came in at a strong USD 234 million in Q2/15 (+5% QoQ, +15% YoY) mainly on higher balance sheet volumes and improved margins (from both higher asset yields and lower cost of funds to a lesser extent). Net interest income was up from USD 391 million in H1/14 to 456 million in H1/15. Based on our estimates, we noticed better interest margins at 2.23% in Q2/15 vs. 2.17% in Q1/15 and 2.10% in Q2/14 principally driven by Odea Bank. Net interest income generated from Odea Bank increased to ~USD 120 million in H1/15 from ~USD 78 million in H1/14, translating into higher total income for Odea Bank at ~USD 147 million in H1/15. Going forward we expect Bank Audi consolidated margins to remain favorably impacted by higher margins from Odea Bank as they continue converging towards Turkish banking sector average and as branch network gains maturity.

Latest banking sector's statistics from the ABL for the month of May 2015 reveal, in a continued low interest environment, an improvement in USD spreads compared to LBP, with challenges due to limited capacity to decrease the cost of funds

Spreads in USD were higher in May 2015 while spreads in LBP were lower compared to one year earlier. Latest statistics from the ABL for the month of May 2015 reveal that Lebanese banks are still operating in a low interest environment, with persistent challenges due to the limited capacity to decrease cost of funds given market share concerns amidst slower deposit accumulation.

Spreads in USD increased to 1.30% in May 2015 from 1.21% in May 2014 which has a substantial positive impact on bank's profitability given that the bulk of their liquidity is in USD. This difference was driven by an increase in weighted average on uses of funds (+24 bps to 4.44%), partially offset by higher cost of funds at (+15 bps to 3.14%).

Spreads in LBP narrowed to 0.83% in May 2015 from 1.04% in May 2014 from higher cost of funds (+10 bps to 5.58%) and lower return on uses of funds (-11 bps to 6.41%) which was dragged down by lower rate on CDs issued by the BDL (-6 bps to 8.15%), lower lending rate (-26 bps to 7.05%) despite higher weighted yields on T-bills (+5 bps to 6.95%).

Fees and commissions displayed solid growth QoQ in Q2/15 (+13% QoQ, +6% YoY) with a higher contribution in total revenues at 20% in Q2/15 vs. ~17% in previous quarters

Bank Audi's net fees and commissions income came in higher sequentially (+13% QoQ) at USD 67 million in Q2/15, representing a +6% increase from Q2/14, but were offset by significantly lower financial gains that came at USD 35 million in Q2/15 (-39% QoQ, -48% YoY), driving non-interest income lower at USD 102 million in Q2/15 (-13% QoQ, -22% YoY). We view a stronger core income mix in Q2/15 positively from higher net interest income contribution as well as fees and commissions income at 70% and 20% respectively, from 66% and 17% in Q1/15, whereas financial gains' contribution to total operating income was at 10% in Q2/15 from 17% in Q1/15. Total revenues in H1/15 grew to USD 675 million (+9% YoY) mainly as a result of rapid growth of Odea Bank's revenues. Going forward, we believe Bank Audi should continue to benefit from increased fees and commissions, helped by the expansion of the Group including the rapidly growing franchise in Turkey as well as increased focus on private banking operations, which represented over USD 10 billion when including fiduciary deposits, AUMs and security accounts.

Table 3: Summary Balance Sheet

USD million	Q2/15a	Q1/15a	Q4/14a	QoQ%	YTD%
Cash and balances with Central Banks	8,841.0	8,928.3	8,787.7	-1.0%	0.6%
Due from banks and other financial institutions	4,056.1	4,485.4	4,336.7	-9.6%	-6.5%
Financial assets	11,040.6	10,275.3	10,249.5	7.4%	7.7%
Loans and advances	17,034.6	16,440.3	17,171.0	3.6%	-0.8%
Intangible assets and goodwill	188.1	183.4	192.5	2.6%	-2.3%
Other assets	1,149.8	1,144.7	1,223.3	0.4%	-6.0%
Total assets	42,310.2	41,457.5	41,960.7	2.1%	0.8%
Due to Central Banks	315.4	359.2	290.8	-12.2%	8.5%
Due to banks and other financial institutions	1,261.0	1,151.6	1,184.6	9.5%	6.4%
Deposits	36,106.1	35,054.3	35,820.8	3.0%	0.8%
<i>Immediate liquidity to deposits</i>	35.7%	38.3%	36.6%		
<i>Loans- to- deposits</i>	47.2%	46.9%	47.9%		
Subordinated notes	645.1	647.8	507.4	-0.4%	27.1%
Other liabilities	854.4	866.6	809.5	-1.4%	5.6%
Total liabilities	39,182.0	38,079.5	38,613.1	2.9%	1.5%
Shareholders' equity	2,711.0	2,836.3	2,805.7	-4.4%	-3.4%
Preferred shares	375.0	500.0	500.0	-25.0%	-25.0%
Minority interest	42.3	41.7	42.0	1.3%	0.8%
Total shareholders' equity	3,128.3	3,378.0	3,347.6	-7.4%	-6.6%
Total liabilities and shareholders' equity	42,310.2	41,457.5	41,960.7	2.1%	0.8%
Book value per share	7.72	8.35	9.45	-7.5%	-18.3%
Book value per share to common	6.78	7.10	8.02	-4.4%	-15.5%
Tangible book value per share to common	6.31	6.64	7.47	-4.9%	-15.5%

Source: Company reports

Improved efficiencies YoY in Q2/15 although still below pre-Turkey expansion levels. Odea Bank's net profits reached USD 6 million in Q2/15 after turning positive in Q2/14

Despite an increased cost-to-income ratio sequentially at 54% in Q2/15 from 52% in Q1/15, Bank Audi cost-to-income ratio still lower than 57% in Q2/14, pointing to improvement YoY in overall cost efficiencies, with cost control on general operating expenses at USD 182 million in Q2/15 (+2% QoQ, -5% YoY). Bank Audi's cost-to-income ratio remains higher than pre-Turkey expansion levels where Bank Audi built a USD 10.5 billion asset base coupled with a network of 53 branches (including kiosks) since the launch of operations. Odea Bank reported net profits of ~USD 6 million in Q2/15, lower QoQ on Turkish currency pressures, but still confirming a trend initiated in Q2/14 when Odea Bank started showing its first set of net profits. We expect profitability in the Turkish entity to continue to improve as margins, efficiencies (and LDR to a lesser extent) move higher towards Turkish peers.

Gross NPL ratio improved to 3.1% in Q2/15 from 3.2% in Q1/15 and cost of risk decreased to an annualized 67 bps following a provisioning spike in previous quarters

Bank Audi's consolidated gross NPLs were lower at 3.1% in Q2/15 from 3.2% in previous quarter, still contained and lower than peers under coverage. We noted a lower cost of risk in Q2/15 to an estimated ~67 bps following a normalization in Q1/15 at 80 bps after a provisioning spike to ~160 bps in Q4/14. On a YoY basis, cost of risk was still higher mainly from greater NPL formation. For Q2/15, net provisions were lower QoQ but still higher YoY at USD 28 million compared to USD 33 million in Q1/15 and USD 15 million in Q2/14.

Net profits at USD 102 million (+2% QoQ, -2% YoY) and tax rate moderated at 18.6% in Q2/15

Bank Audi's net profits in Q2/15 came in at USD 102 million (+2% QoQ, -2% YoY). Despite a solid increase in net interest income YoY (+15%), non-interest income was affected by significantly lower financial gains income (-48%), keeping total operating income unchanged YoY. Provisions were higher YoY from USD 15 million in Q2/14 to USD 28 million in Q2/15 while income tax was slightly lower at USD 23 million in Q2/15 from USD 25 million in Q2/14. Tax rate was lower at 18.6% in Q2/15 compared to 22.2% in Q1/15 and 19.5% in Q1/14.

Despite softer domestic conditions and currency pressures in key growth markets, balance sheet indicators grew QoQ and YoY

Following seasonal weakness in Q1/15 and despite challenging political and economic conditions across the region, persistent softness in domestic banking sector, and depreciating foreign exchange rates of both Turkish lira and Egyptian pound, Bank Audi's consolidated assets, deposits and loans increased QoQ/YoY in Q2/15 by +2%/+8%, +3%/+6%, +4%/+6% to reach USD 42 billion, USD 36 billion and USD 17 billion respectively. Bank Audi's deposits to assets ratio was unchanged sequentially at 85%, and LDR at 47% well above the Lebanese banking sector average (~35%), attributed to continued fast lending growth driven by Turkey.

CAR III lower at 12.8% in Q2/15 from 13.7% in Q1/15 as balance sheet assets grew and Bank Audi redeemed series "E" preferred shares

Bank Audi's equity to assets ratio was lower at 7.4% in Q2/15 from 8.1% in Q1/15 due to higher total assets in Q2/15 and redemption of USD 125 million series "E" preferred shares at maturity. Bank Audi's capital adequacy ratio (Basel III) decreased 12.8% in Q2/15 from 13.7% in Q1/15. Profitability ratios came in mixed sequentially with TTM ROA lower at an estimated ~0.9% roughly unchanged from previous quarter while the TTM ROE was higher at an estimated 12.4% vs. 11.8%. The TTM EPS was USD 0.83 in Q2/15 from USD 0.86 in Q1/15, while book value per share (to common) came at an estimated at USD 6.78 in Q2/15 vs. USD 7.10 in Q1/15.

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