

Equity Research - Flash Note - Bank Audi Q4/16 Results

Sector: Banking
Country: Lebanon

MARKETWEIGHT

Target Price	USD 7.00
Closing Price	USD 6.66
52 Week Range	USD 5.85-7.00
Year to Date %	-2.06%
Market Cap.	USD 2,662.3 million
Dividend Yield	6.0%
P/E (TTM)	6.2x
P/B to Common	0.90x

Note: the share data represents Bank Audi listed shares (AUDI LB)
Bank Audi GDR shares at USD 6.80 (BQAD LI) and USD 6.90 (AUSR LB)
Source: Bloomberg, FFA Private Bank
Market close on February 1, 2017

Bank Audi Q4/16 Results Summary vs. FFA Private Bank est.

USD million except per share data	Q4/16a	FFA Q4/16e	QoQ	YoY
Net interest income	257.5	270.1	-1%	3%
Fees & commissions	73.0	77.7	-89%	3%
Trading & investment	109.7	59.0	10928%	144%
Operating income	440.2	406.8	-54%	20%
Provisions	-84.7	-35.7	-35%	141%
Operating expenses	-197.9	-226.1	-50%	-5%
Income tax	-52.8	-30.5	-52%	84%
Net profits	119.8	114.6	-4%	21%
Diluted EPS to common	0.25	0.26	-20%	10%
Assets	44,396	44,147	-2%	5%
Deposits	35,955	36,871	-3%	1%
Loans	17,344	18,768	-8%	-3%
BVPS to common	7.38	7.88	-3%	3%

	Q4/16a	FFA Q4/16e	Q3/16a	Q4/15a
FFA Net interest margins	2.34%	2.49%	2.33%	2.41%
Core income to total operating income ratio	75.1%	85.5%	99.9%	85.9%
FFA Cost-to-income ratio	45.0%	55.6%	41.8%	56.6%
Immediate liquidity-to-deposit ratio	43.8%	39.0%	41.7%	35.5%
Loan-to-deposit ratio	48.2%	50.9%	50.9%	50.2%
Equity-to-asset ratio	8.5%	8.5%	8.1%	7.8%

Source: Company reports and FFA Private Bank estimates

Material currency losses in key markets weighed on consolidated balance sheet growth with assets, deposits and loans down -2%, -3% and -8% in Q4/16

Bank Audi's assets, deposits and loans at respective USD 44.4 billion (-2% QoQ, +5% YoY), USD 36.0 billion (-3% QoQ, +1% YoY) and USD 17.3 billion (-8% QoQ, -3% YoY) as growth in consolidated balance sheet was pressured by large currency devaluations in Turkey and Egypt which account for respective 24% and 7% of Bank Audi's assets and 43% and 10% of loans. As a result, loan-to-deposit ratio declined to 48.2% in Q4/16 vs. 50.9% in Q3/16 and 50.2% in Q4/15 despite stronger lending in Turkey with LDR at ~100% up from ~92% in Q3/16. We highlight stronger balance sheet growth in local currencies in Turkey and Egypt while Lebanon component likely grew above sector averages at ~+3% QoQ (sector grew ~+1.5% from September to November 2016). At constant exchange rates, growth rates for consolidated assets and deposits are estimated at respective +15% and +10% YoY.

Stronger capitalization following BDL debt swap operations and ahead of new regulatory requirements with improvement in profitability metrics

Bank Audi's capital adequacy ratio (as per Basel III) at 15.3% in Q4/16 unchanged from Q3/16 and above BDL's 14.0% regulatory requirement (14.5% by end of 2017 and 15.0% by end of 2018), with CET1 ratio at 9.5% and Tier 1 capital at 12.1%. Bank Audi's CAR improved YoY from 13.4% in Q4/15, recently helped by BDL circular 446 related to gains released from banks participation in debt swap. TTM ROA came in slightly higher in Q4/16 at an estimated ~1.1% from ~1.0% in Q3/16 and Q4/15 while TTM ROE was at an estimated ~13.3% in Q4/16 up from ~13.1% in Q3/16 and ~12.2% in Q4/15. We highlight improved profitability across pillars with higher ROA in Lebanon, Turkey and Egypt. TTM EPS increased to USD 1.08 from USD 1.05 in Q3/16 and USD 0.92 in Q4/15. Equity-to-asset ratio at 8.5% in Q4/16 higher than 8.1% in Q3/16 and 7.8% in Q4/15 while estimated book value per share was at USD 8.95 (USD 7.38 to common, -3% QoQ, +3% YoY).

Expect Bank Audi's earnings stream to benefit from diversified business model while shares should trade favorably going into dividend season

We believe Bank Audi benefits from a more diversified income stream given more developed business model across segments and markets, which also helps to moderate sovereign risk in its home market. We highlight increasing market share, interest margins and profitability across main pillars which also include Turkey, Egypt and private banking with contained asset quality despite challenging conditions including unfavorable currency fluctuations in regional operations. We see this translating into a more favorable risk return profile for investors particularly as shares have languished since recent developments which included BDL debt swap and government formation. While bank shares typically trade favorably going into dividend season, we do not expect a hike in dividend given Bank Audi's room for improvement in regulatory capital ahead of tougher BDL requirements. Bank Audi shares trade at multiples in line with domestic peers under our coverage although at discount to regional peers at ~1.2x and ~12x on a P/E and P/B basis respectively.

Net profits at USD 119.8 million in Q4/16 (-4% QoQ, +21% YoY) above FFA est. of USD 114.6 million as weaker-than-expected net interest income was largely offset by stronger financial gains and lower opex

Bank Audi's net profits at USD 119.8 million (-4% QoQ, +21% YoY) in Q4/16 above FFA est. of USD 114.6 million while diluted EPS at USD 0.25 (-20% QoQ, +10% YoY) below our USD 0.26 est. on account of recent issuance of preferred shares completed late 2016 as preferred share dividends get paid after net profits. Total operating income at USD 440.2 million (vs. FFA est. USD 406.8 million) as higher-than-expected trading and investment income at USD 109.7 million (vs. FFA est. USD 59.0 million) offset lower-than-expected net interest income at USD 257.5 million (vs. FFA est. USD 270.1 million) and fees and commissions income at USD 73.0 million (vs. FFA est. USD 77.7 million). Lower-than-expected opex at USD 197.9 million (vs. FFA est. USD 226.1 million) partly offset by heavier-than-expected credit loss provisions at USD 84.7 million (vs. FFA est. USD 35.7 million) from reallocations following BDL Circular 446 and income tax at USD 52.8 million (vs. FFA est. 30.5 million) mostly from BDL debt swap transactions and higher tax expense in Egypt operations. We highlight lesser impact from Circular 446 on Bank Audi's Q4/16 results compared to peers under coverage as a large part of the debt swap's gains allocation to collective provisions, IFRS 9 requirements, goodwill impairment and deconsolidation of foreign entities was completed in Q3/16 despite some readjustments in Q4/16. Assets grew in line with our forecasts at USD 44.4 billion while deposits and loans below our est. at respective USD 36.0 billion and USD 17.3 billion. Net profits for the full year 2016 at USD 470.1 million above FFA est. at USD 465.0 million and up +17% YoY from USD 403.1 million in 2015 while EPS in line with FFA est. at USD 1.08, up +17% from USD 0.92 in 2015.

Weaker net interest income growth at USD 257.5 million (-1% QoQ, +3% YoY) in Q4/16 weighed QoQ by decline in balance sheet while NIMs improved at slower pace

Bank Audi's net interest income at USD 257.5 million (-1% QoQ, +3% YoY) with net interest margins estimated at 2.34% in Q4/16, slightly above 2.33% in Q3/16 and below Q4/15 level of 2.41%. On a QoQ basis, consolidated net interest income was unfavorably impacted by currency devaluations in foreign markets and increase in interbank placements while we highlight that lending in EGP and TRY f/x stood at a solid ~25% of total loans. We note QoQ improvement in spreads in Turkey although at a slower pace, while flat in Lebanon despite improvement in LBP and USD asset yields in the domestic sector, and slightly lower in Egypt. On a YoY basis, net interest income was higher likely helped by growth in balance sheet despite weaker NIMs on a consolidated basis although we note improvement in NIMs on local currency basis.

Non-interest income at USD 182.7 million weaker QoQ on lower fees and commissions income at pre-debt swap levels despite stronger trading and investment income

Non-interest income at USD 182.7 million in Q4/16 (-74% QoQ, +58% YoY) on account of stronger trading and investment income at USD 109.7 million resulting from Bank Audi's larger involvement in capital market activities in Lebanese securities in addition to f/x gains from Egypt operations. Fees and commissions income came in at USD 73.0 million (-89% QoQ, +3% YoY) in line with pre-debt swap levels although slightly higher YoY from USD 70.7 million in Q4/15. We highlight a YoY deterioration in Bank Audi's income quality mix with contribution of core income (net interest income + net fees and commissions) to total operating income at 75% in Q4/16 from 86% in Q4/15.

Cost-to-income ratio lower YoY while higher QoQ as operating income adjusts to pre-debt swap levels following strong gains in Q3/16

Bank Audi's reported improved YoY efficiencies with cost-to-income estimated at 45% vs. 57% in Q4/15 with improvement driven by higher non-interest income and lower non-personnel opex. On a QoQ basis, cost-to-income is estimated higher following particularly lower level in Q3/16 which was helped by non-recurring income from participation in BDL debt swap.



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