



Saudi Arabia Banking Pulse

Quarter 1, 2020

FOREWORD

Alvarez & Marsal Middle East Limited (A&M) is delighted to publish the 1st edition of the Kingdom of Saudi Arabia (KSA) Banking Pulse (“The Pulse”). In this planned quarterly series, we share results from our research examining the top ten largest listed KSA banks by assets, and highlight key performance indicators of the KSA banking industry. The Pulse aims to help banking executives and board members stay current on industry trends.

All the data used in this report has been obtained from publicly available sources and the methodology for the calculations is discussed in the glossary. Calculation of several metrics will be subject to change based on available information.

Due to the COVID-19 pandemic, the industry will be significantly impacted with respect to challenging macroeconomic conditions and lower interest rates. And this is already evident in QoQ performance for Q1’20. While the KSA government and the central bank have introduced a series of support measures for the economy and the banking industry, the government has also announced plans that could rationalize public finances.

The performance in Q1’20 may not be entirely comparable with that of the previous quarters, but the COVID-19 related impact on the industry is expected to continue for FY 2020.

We hope that you will find our first edition of the KSA Banking Pulse useful and informative.



Disclaimer:

The information contained in this document is of a general nature and has been obtained from publicly available information plus market insights. The information is not intended to address the specific circumstances of an individual or institution. There is no guarantee that the information is accurate at the date received by the recipient or that it will be accurate in the future. All parties should seek appropriate professional advice to analyze their particular situation before acting on any of the information contained herein

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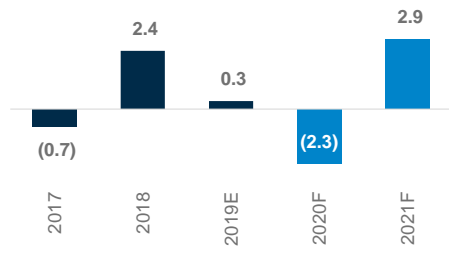
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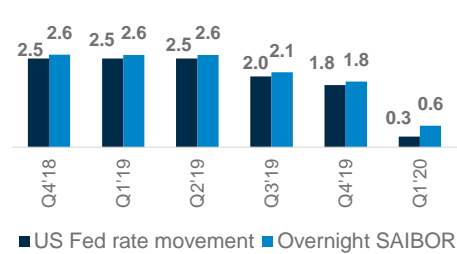
Saudi Arabia Macro & Sector Overview

Macro overview

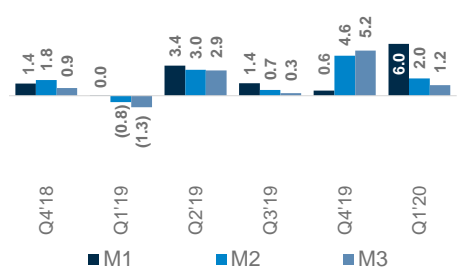
KSA GDP Growth Rate¹, %



US Fed Funds Rate², SAIBOR %



KSA Money Supply³, (% Quarterly)



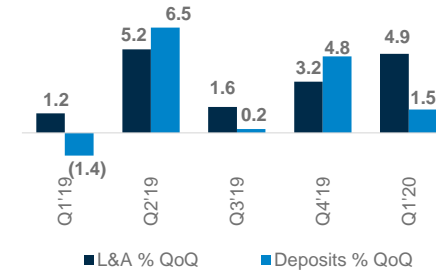
- In April'20, KSA reported that its Q4'19 GDP growth declined 0.3%, due to weakness in oil sector
- In Q1'20, the average PMI indicated economic contraction, with value of 49.9 when compared to 57.7 in Q4'19
- COVID-19 led slowdown along with low oil price environment will negatively impact going forward. To offset, the **VAT rate was increased to 15% from 5%, in addition to suspending the cost of living allowance**
- As per IMF, KSA's economy is expected to decline by 2.3% in FY'20, with rebound expected next year**

- In light of COVID-19, **in Mar'20, the US Fed reduced its lending rates close to 0% mark** for the first time since the 2008 financial crisis. The central bank also introduced a quantitative easing program worth USD 700bn
- The Saudi central bank also trimmed interest rates, with the overnight SAIBOR declining to 0.6% at the end of Q1'20
- Interest rates are likely to remain low in the foreseeable future**, as Saudi central bank would look to stabilize the economy from the ongoing economic headwinds

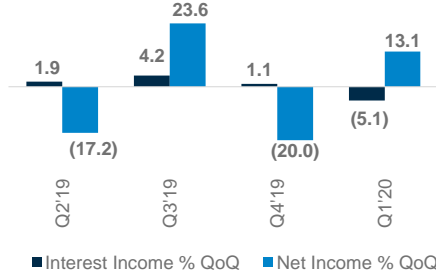
- Domestic liquidity, demonstrated by M2 money supply increased 2.0% QoQ and 10.6% YoY in Q1'20
- M2 money supply increased mainly due to a sequential **increase in demand deposits, which increased 6.1% QoQ to SAR 1.2tn**
- M1 increased by 6.0% QoQ in Q1'20 to SAR 1.4tn, while M3 money supply advanced 1.2% QoQ to SAR 2.0tn

Banking overview Q1'20

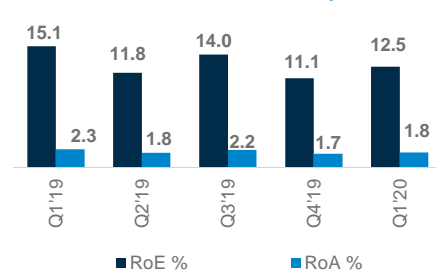
KSA Banks L&A and Deposits⁴, %



KSA Banks' Profitability⁴, %



KSA Banks' Profitability⁴, %



- Loans & Advances (L&A) growth of top ten banks in KSA grew at +4.9% QoQ in Q1'20
- While, deposit growth (+1.5% QoQ) slowed, after rising by 4.8% in the previous quarter
- The performance of KSA banks in terms of L&A growth has been encouraging**, in light of the outbreak of COVID-19, as most sections of the economy were under the lockdown in the latter half of Q1'20

- Interest income of top ten banks declined by 5.1% QoQ, on account of lower interest rates
- However, **net income rebounded strongly (+13.1% QoQ) after declining by about 20% in Q4'19**, driven by higher non-interest income and lower operating expenses
- Profitability is likely to remain under pressure for FY'20

- Increase in net income supported return ratios during the quarter
- Return on Equity (RoE – Q1'20 annualized) rebounded, after declining by 2.9% points in the preceding quarter
- Despite an increase, Q1'20 RoE (12.5%) remained below average RoE (13.0%) achieved in FY'19**
- Similarly, return on asset (RoA – Q1'20 annualized) marginally increased from 1.7% in Q4'19 to 1.8% in Q1'20

¹ IMF forecast, ² US Board of Federal Reserve, ³ KSA Central Bank, ⁴ Company Financials, * Data for top ten KSA banks by asset size as of March 31st 2020, QoQ stands for quarter over quarter

COVID-19 Impact on Saudi Arabia

Government and Central Bank Measures

- The Saudi economy and the banking sector were expecting FY'20 to be better compared to past years, however, the ongoing COVID-19 crisis has made guidance difficult to achieve
- Government in March'20 announced emergency funds worth SAR 70bn**, in the form of delays of tax payments and exemptions of various government fees and levies
- In addition to hike in VAT, **the government also slashed budget spending by ~10%**, while also indicating the further need to take strict measures to deal with the situation
- In March '20, central bank announced a stimulus package worth SAR 50bn** largely for SMEs. The package includes deferred payments, concessional financing and loan guarantees. The central bank has also reduced rates by 125 bps so far this year
- In June'20, the central bank injected SAR 50bn** worth of liquidity to enable banks to lend money to the private sector

L&A Growth

Based on Bank Calculations	FY'19	FY'20 Original Guidance	FY'20 Revised Guidance
National Commercial Bank	+6.5%	+10% - 12%	+8% - 10%
Al Rajhi Bank	+7.7%	Mid Single Digit	High Single Digit
Banque Saudi Fransi	+4.2%	High Single Digit	High Single Digit

Cost to Income

Based on Bank Calculations	FY'19	FY'20 Original Guidance	FY'20 Revised Guidance
National Commercial Bank	30.7%	Below 32%	Below 33%
Al Rajhi Bank	32.8%	Below 31%	Below 33%
Banque Saudi Fransi	33.3%	NA	Below 33%

Banking Sector Reactions

- Banks will be impacted by the state of liquidity in the economy in the near term, **as lower oil prices could possibly induce government to withdraw their bank deposits**
- Following the Q1'20 results **major banks have reduced their FY'20 guidance** acknowledging the tough market conditions
 - KSA's largest bank, NCB, has reduced its L&A growth guidance. On the contrary, RJHI has increased its L&A growth guidance
 - Major banks are now expecting NIM compression and increased provisioning (cost of risk) for FY'20
- SAMBA's Chairman projected that the economic consequences of the COVID-19 might stretch to one to two years

Net Interest Margin

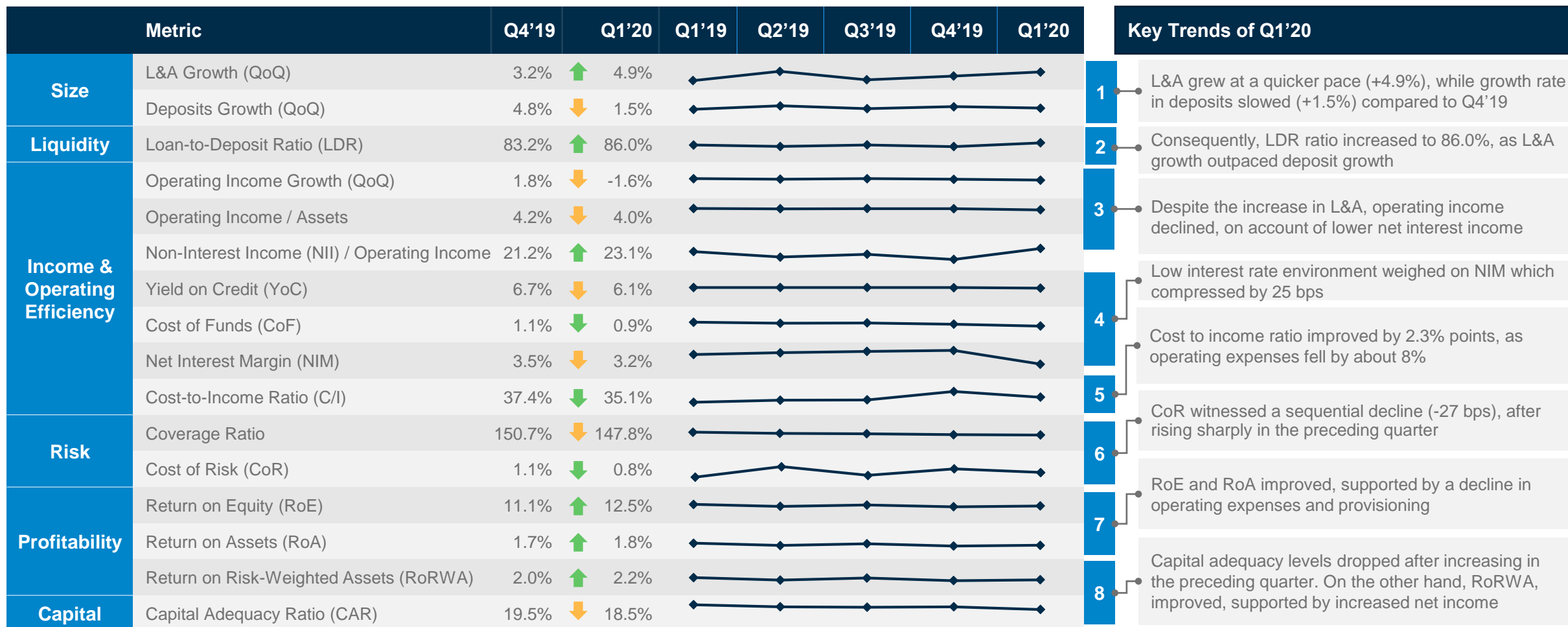
Based on Bank Calculations	FY'19	FY'20 Original Guidance	FY'20 Revised Guidance
National Commercial Bank	3.77%	3.60% - 3.80%	3.40% - 3.60%
Al Rajhi Bank	5.22%	5.22% - 5.32%	4.77% - 4.97%
Banque Saudi Fransi	3.04%	3.09% - 3.19%	2.94% - 3.04%

Cost of Risk

Based on Bank Calculations	FY'19	FY'20 Original Guidance	FY'20 Revised Guidance
National Commercial Bank	0.51%	0.60% - 0.80%	0.80% - 1.00%
Al Rajhi Bank	0.71%	0.60% - 0.70%	0.80% - 1.00%
Banque Saudi Fransi	0.79%	0.75% - 0.90%	1.00% - 1.20%

Pulse: Top Ten KSA Banks Showed Mixed Performance in Q1'20, as Improved Operating Efficiency and Lower Provisioning was Offset by the Effect of Reduced Interest Rates

→ Improved ← Stable → Worsened



Note 1: Growth in loans & advances and deposits were presented QoQ instead of YoY

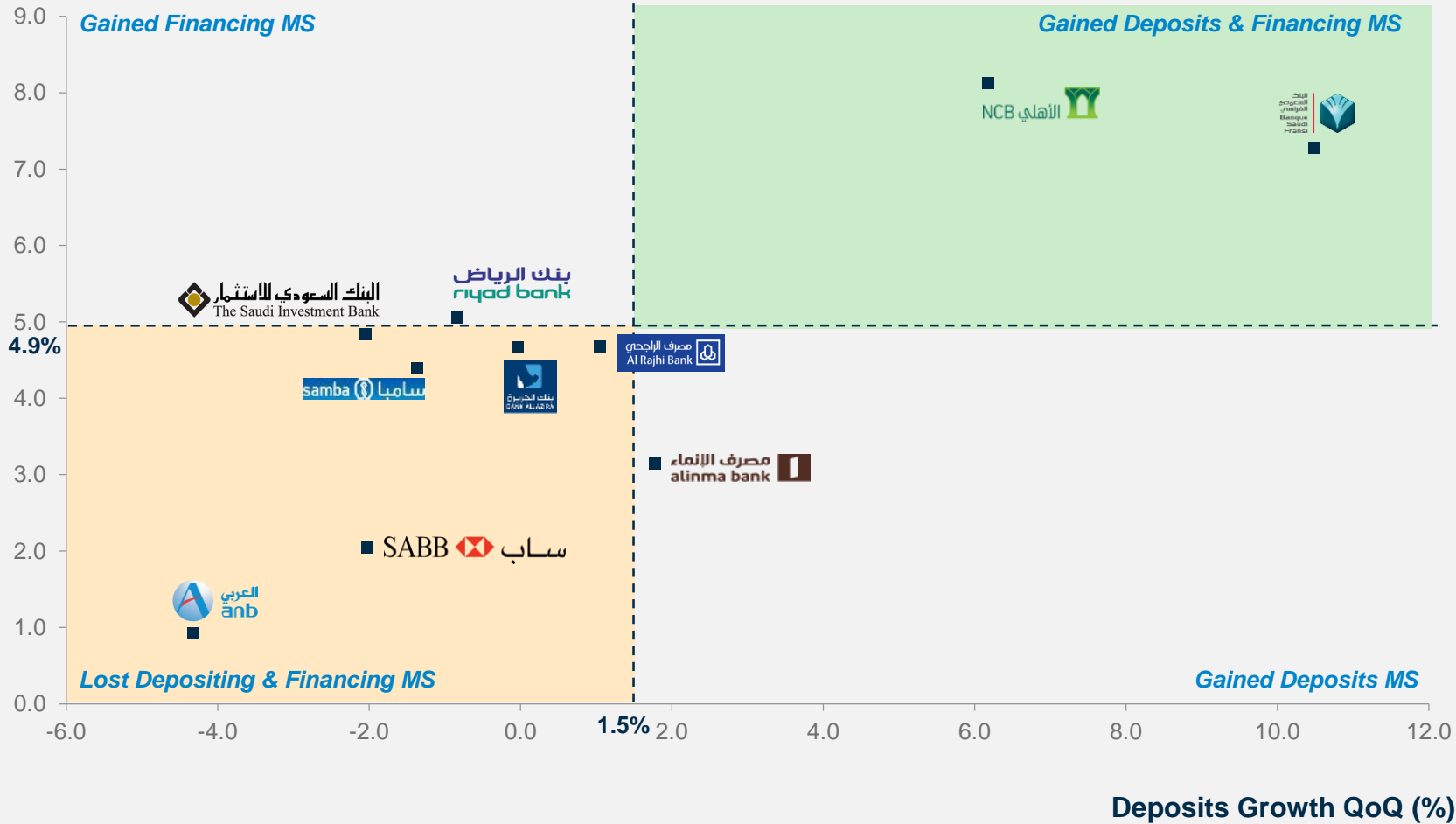
Note 2: Quarterly income was used in the calculation of operating income growth

Source: Financial statements, Investor presentations, A&M analysis

NCB and BSFR Reported Strong L&A and Deposit Growth

L&A Growth QoQ (%)

----- Q1'20 Av



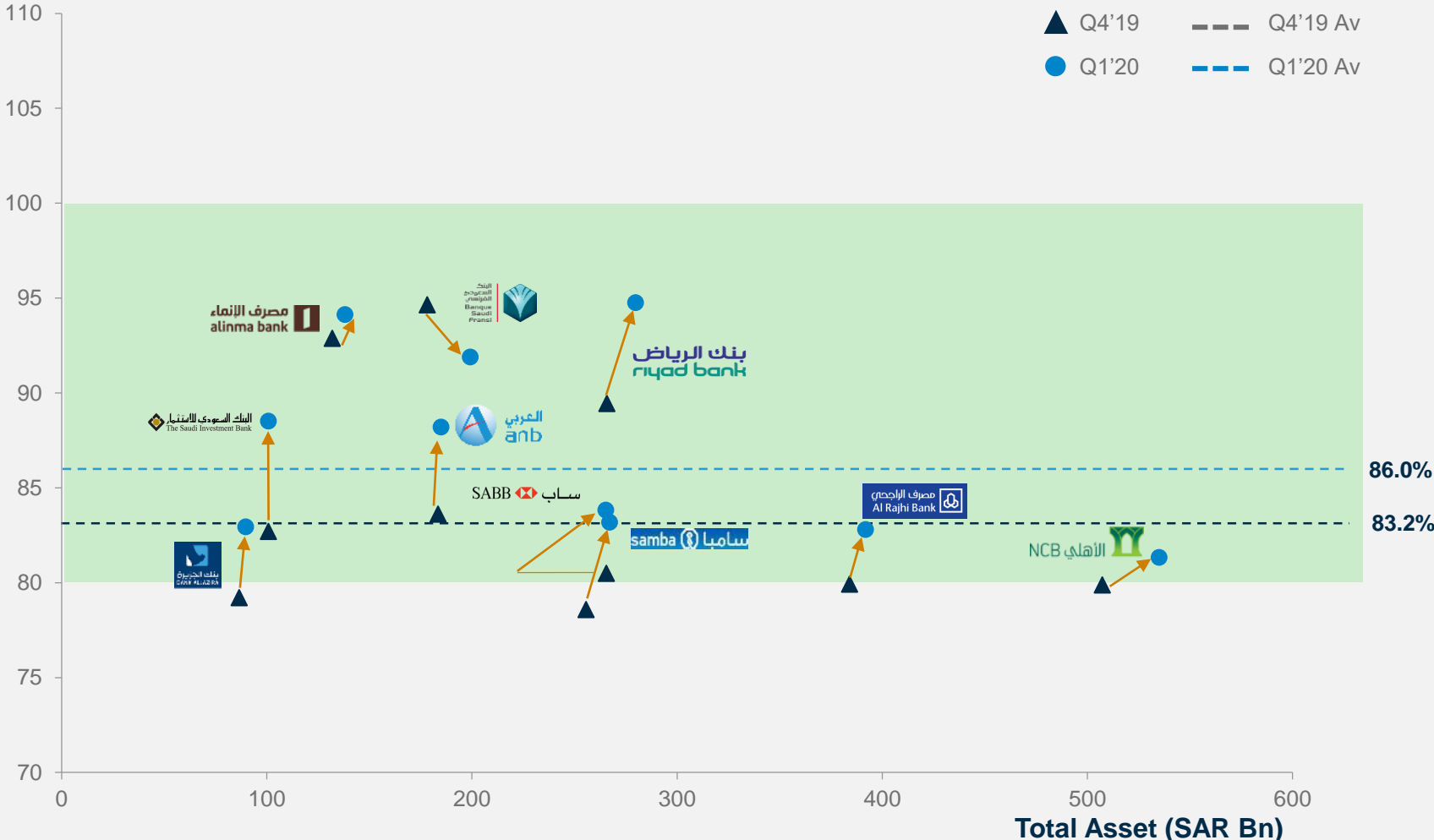
KEY TAKEAWAYS

- L&A and deposits of top ten banks increased 4.9% and 1.5%, respectively
- NCB’s L&A growth (+8.1%), outperformed its peers
 - Strong lending in retail mortgage, corporate and financial institutions supported NCB’s L&A growth
- BSFR reported the strongest deposit growth (+10.5%)
- ARNB underperformed its peers by reporting the lowest L&A (+0.9%) and deposits (-4.3%) growth
 - The bank reported time and demand deposit outflow to the tune of SAR 4.9bn

Note: MS stands for market share
Source: Financial statements, Investor presentations, A&M analysis

Loan to Deposits Ratio Increased for All, except for BSFR

Loans to Deposits Ratio (%)



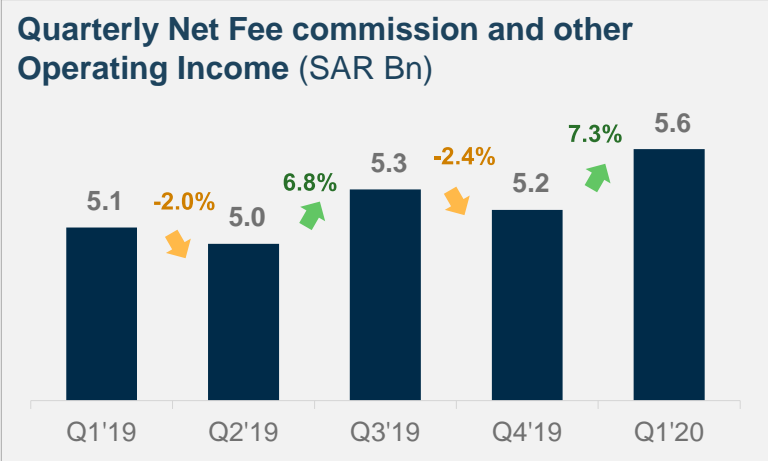
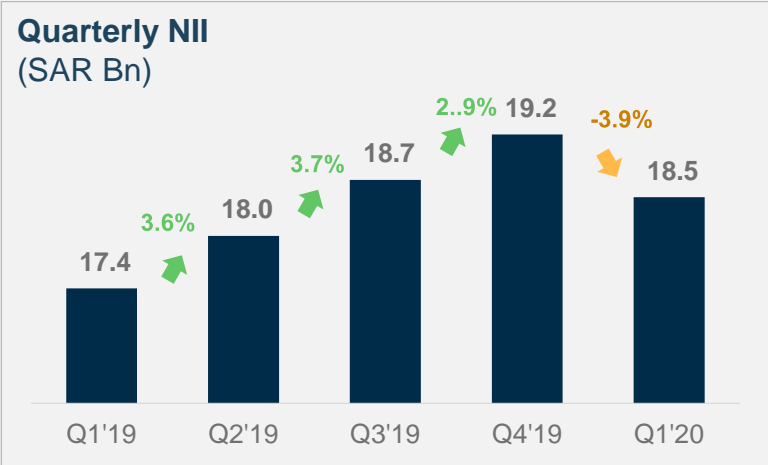
KEY TAKEAWAYS

- Aggregate LDR increased from 83.2% in Q4'19 to 86.0% in Q1'20
- SIBC (+5.8% points), RIBL (+5.3% points), and SAMBA (+4.6% points) reported the highest increase in LDR
- On the other hand, BSFR's LDR fell 2.7% points to reach 91.9% in Q1'20

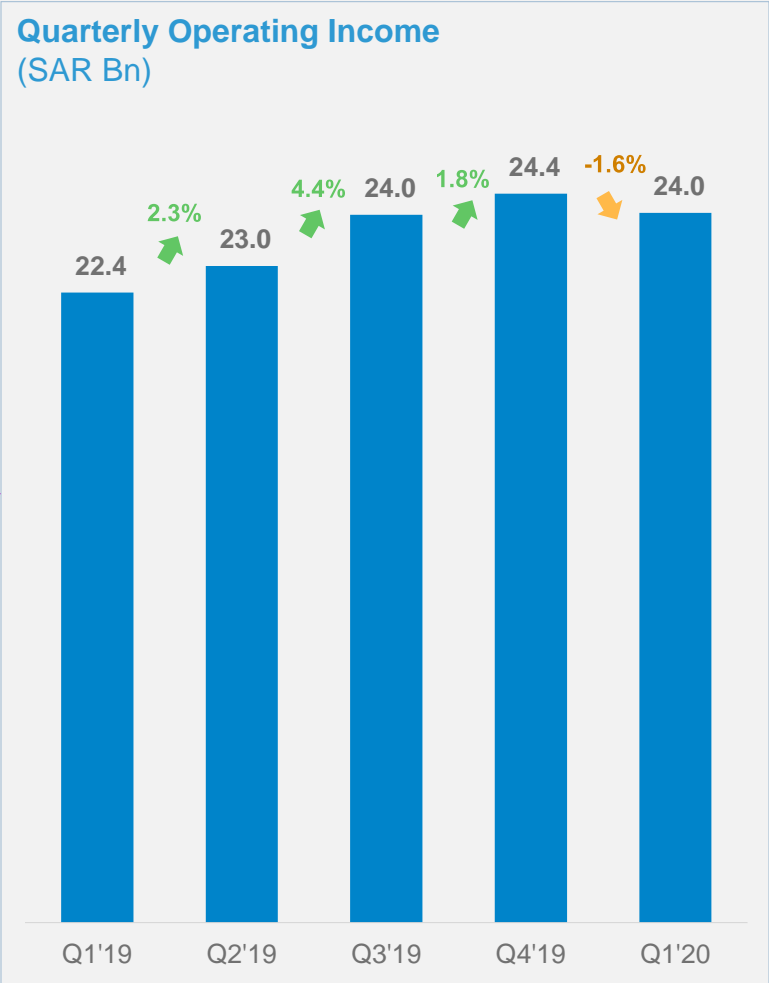
Note: The green zone is an area of healthy liquidity
 Source: Financial statements, A&M analysis

Operating Income Impacted by Decline in NII, Partially Offset by Sizeable Increase in Non-Interest Income

➔ Improved ↔ Stable ➔ Worsened



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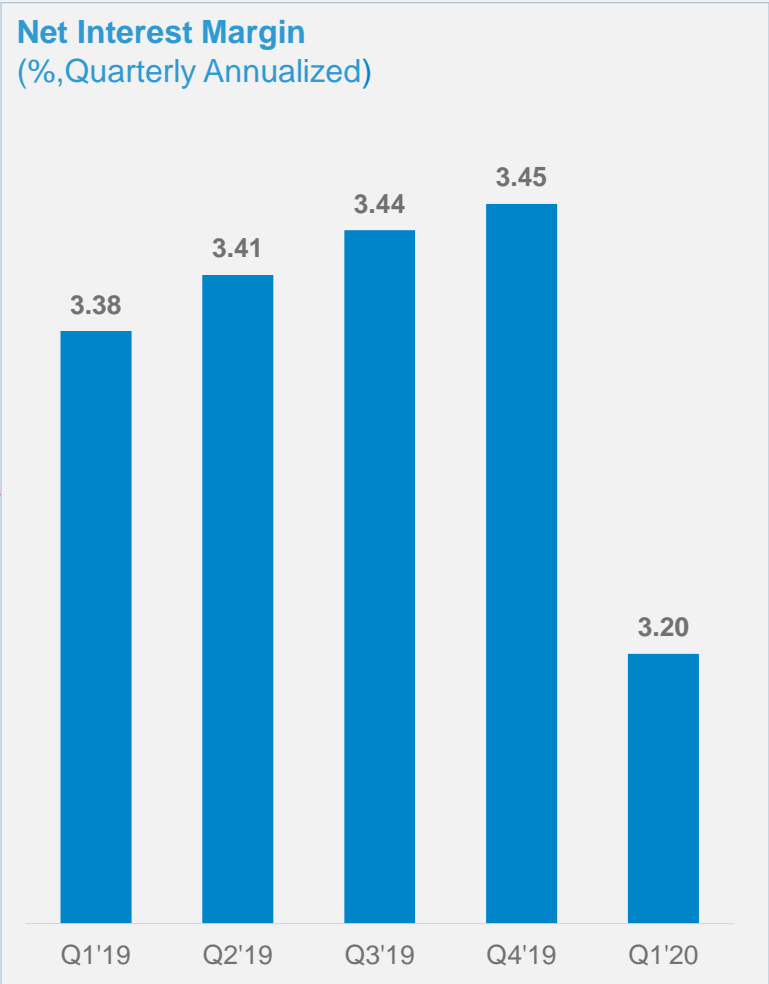
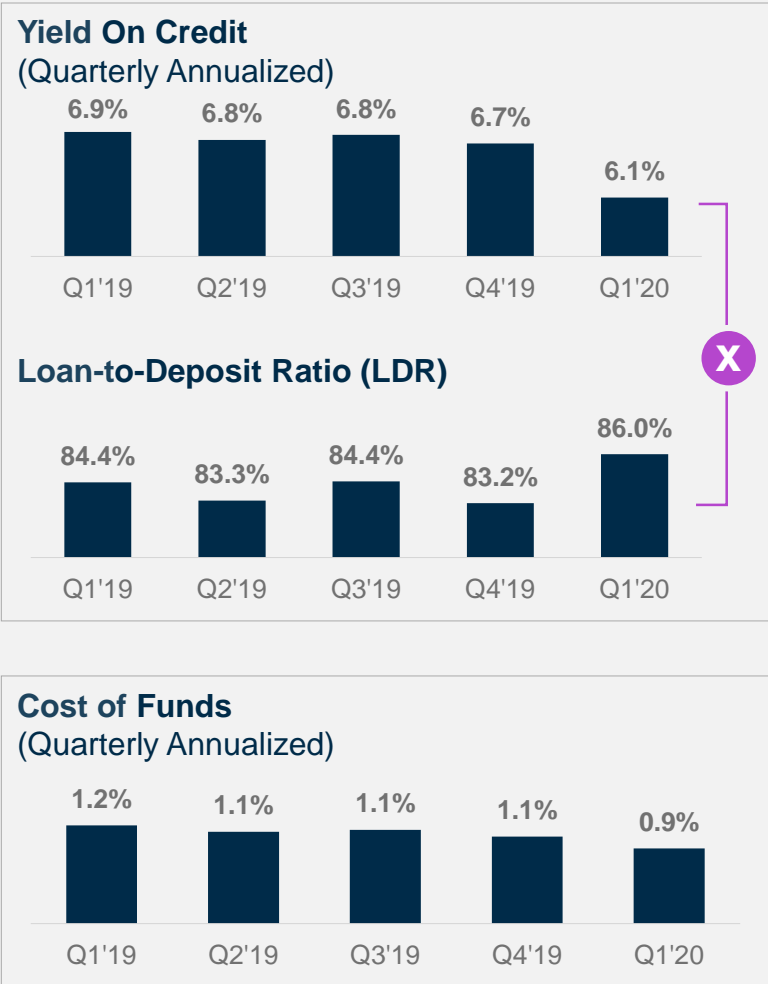


KEY TAKEAWAYS

- Total operating income fell 1.6%, largely on account of decline in NII
- NII declined 3.9% QoQ, as lower interest rates more than offset the increase in lending activity
- Non-interest income, on the other hand, increased strongly, driven by strong increase in fee & commission and trading income of select banks
- SAMBA (+3.3x QoQ) and RIBL (+76.9% QoQ) led the increase in non-interest income, as both banks' trading income increased sharply

Note: Some numbers might not add up due to rounding
Source: Financial statements, investor presentations, A&M analysis

Central Bank Cuts Impacted NIM



KEY TAKEAWAYS

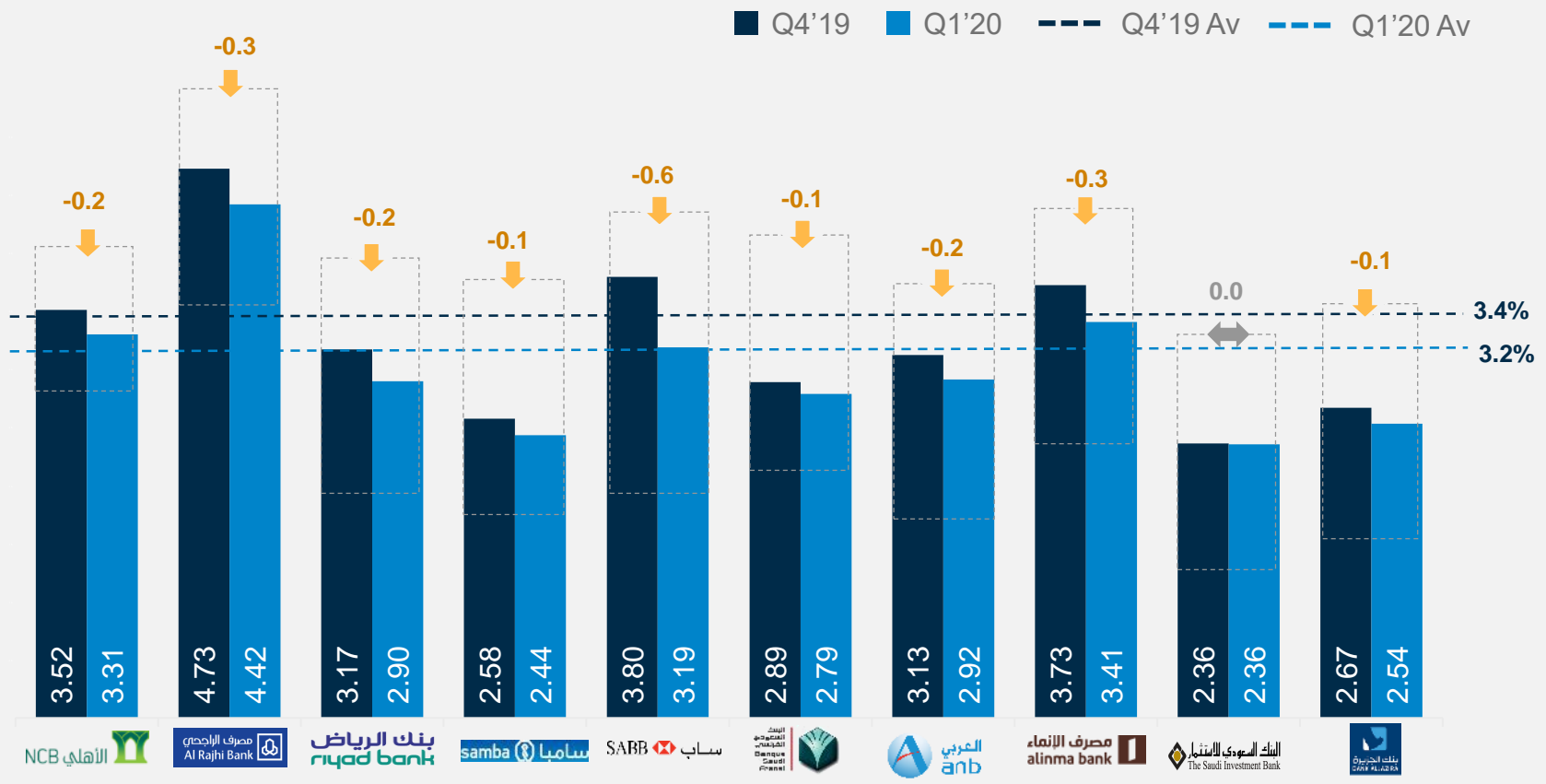
- NIM fell by 25 bps to reach 3.2%, the lowest level in past several quarters
- The decrease in NIM was primarily attributable to 59 bps decline in yield on credit
- The decline in yield on credit fully offset the decline in cost of funds (from 1.1% in Q4'19 to 0.9% in Q1'20) and an increased LDR ratio (86.0% in Q1'20 from 83.2% in Q4'19)

Note: Relation between elements above represents a functionality and not necessarily an exact mathematical formula
 Source: Financial statements, Investor presentations, A&M analysis

Low Interest Rates Impacted NIM of Most of the Banks

→ Improved ← Stable → Worsened

Net Interest Margin (% Quarterly)



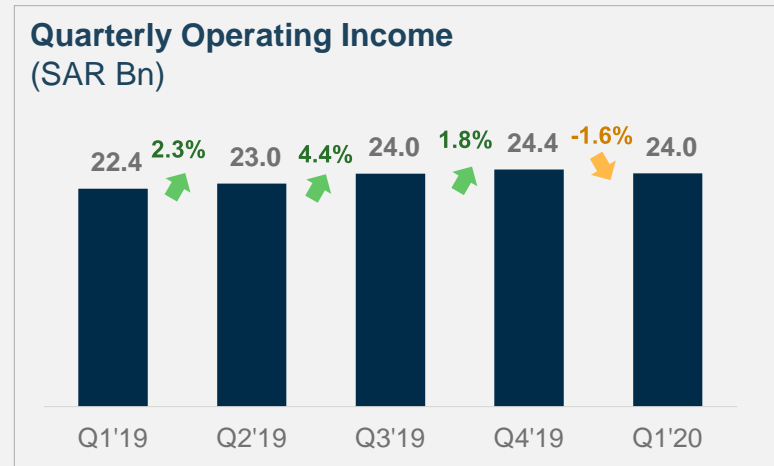
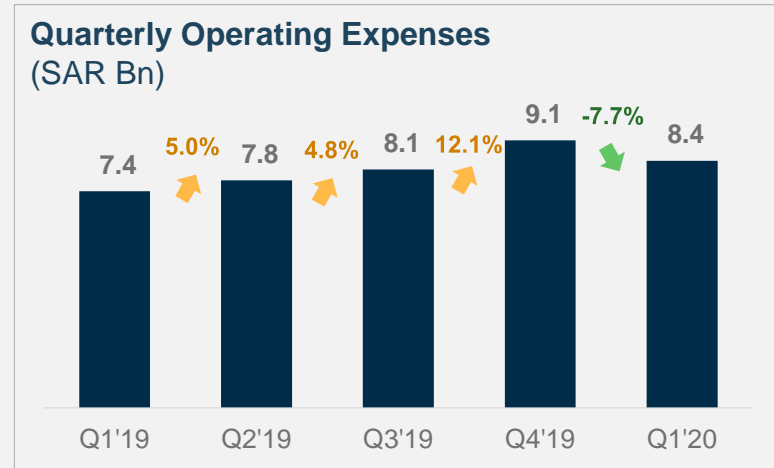
KEY TAKEAWAYS

- Low industry-wide interest rates impacted NIM of individual banks, as nine of the top ten banks reported a decline in their NIM during Q1'20
- SABB and ALINMA reported highest decline in NIM of 59.8 and 31.5, respectively
 - Yield on credit of both banks decreased by 108 and 56 bps, respectively
 - In case of SABB, cost of funds fell by only 10 bps, which resulted in a sizeable contraction in NIM
- SIBC's NIM remained broadly unchanged during the period

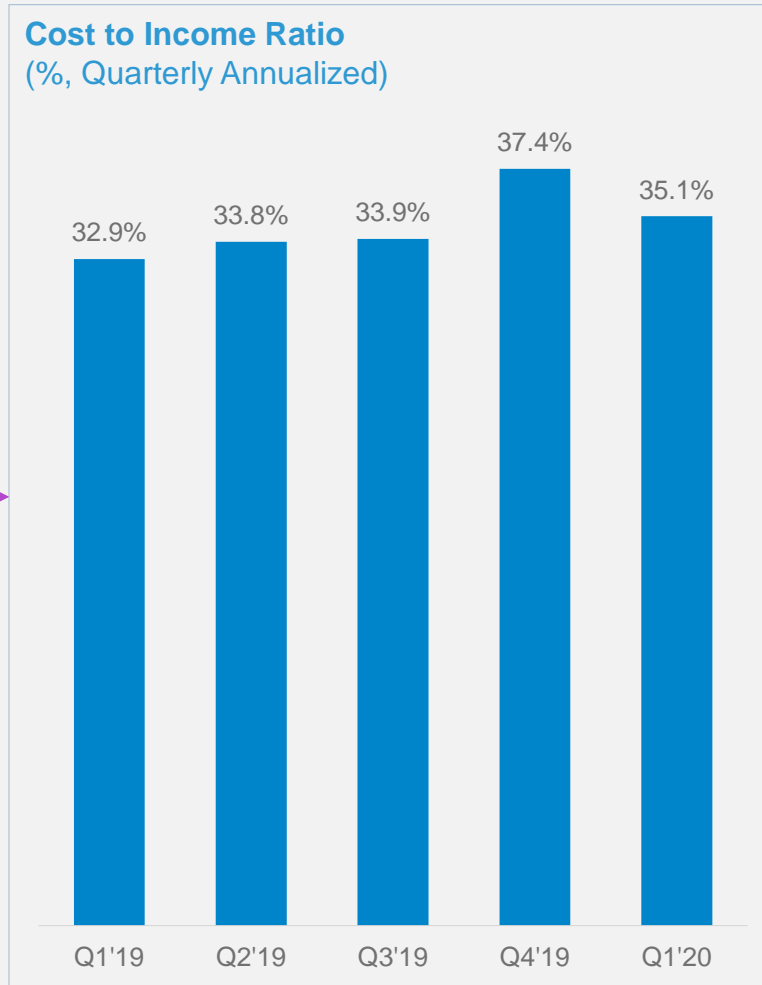
Note: Some numbers might not add up due to rounding
 Source: Financial statements, investor presentations, A&M analysis

C/I Ratio Dropped After Rising for Three Consecutive Quarters

➔ Improved ↔ Stable ➔ Worsened



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KEY TAKEAWAYS

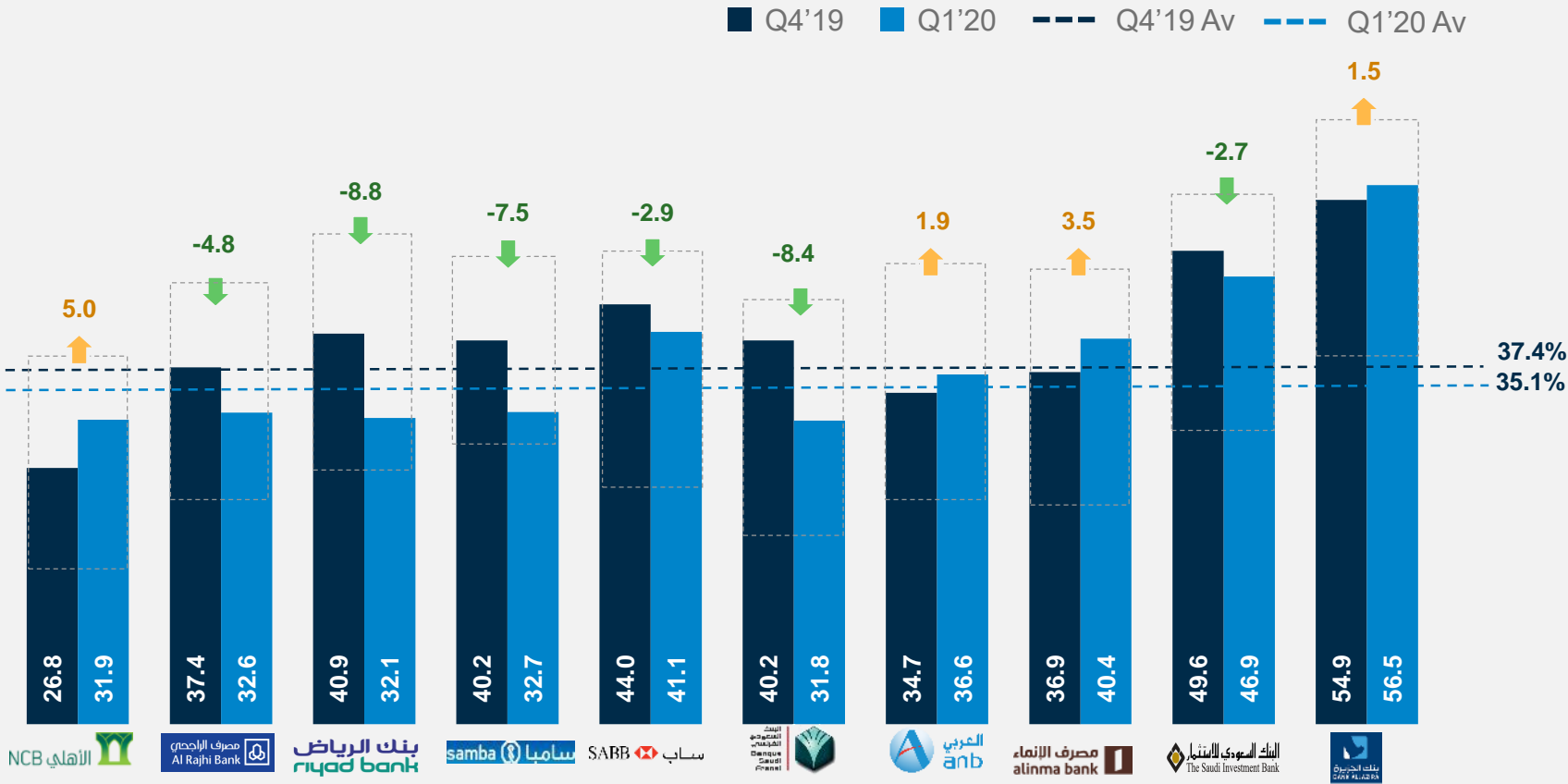
- C/I ratio witnessed a sequential decline of about 2.3% points, as banks implemented various cost optimization measures
- Total operating expenses decreased 7.7% QoQ, which helped in offsetting a decline in operating income
- Despite the decline, Q1'20 C/I ratio remains above the average of the same in FY'19 (34.5%)
- KSA banks are likely to additional introduce cost controlling initiatives, over the medium to long term, including digitization of operations

Note: Some numbers might not add up due to rounding
 Source: Financial statements, investor presentations, A&M analysis

Operating Efficiency Improved Across Most of the Banks

➔ Improved ➔ Stable ➔ Worsened

Cost to Income Ratio (% , Quarterly)



KEY TAKEAWAYS

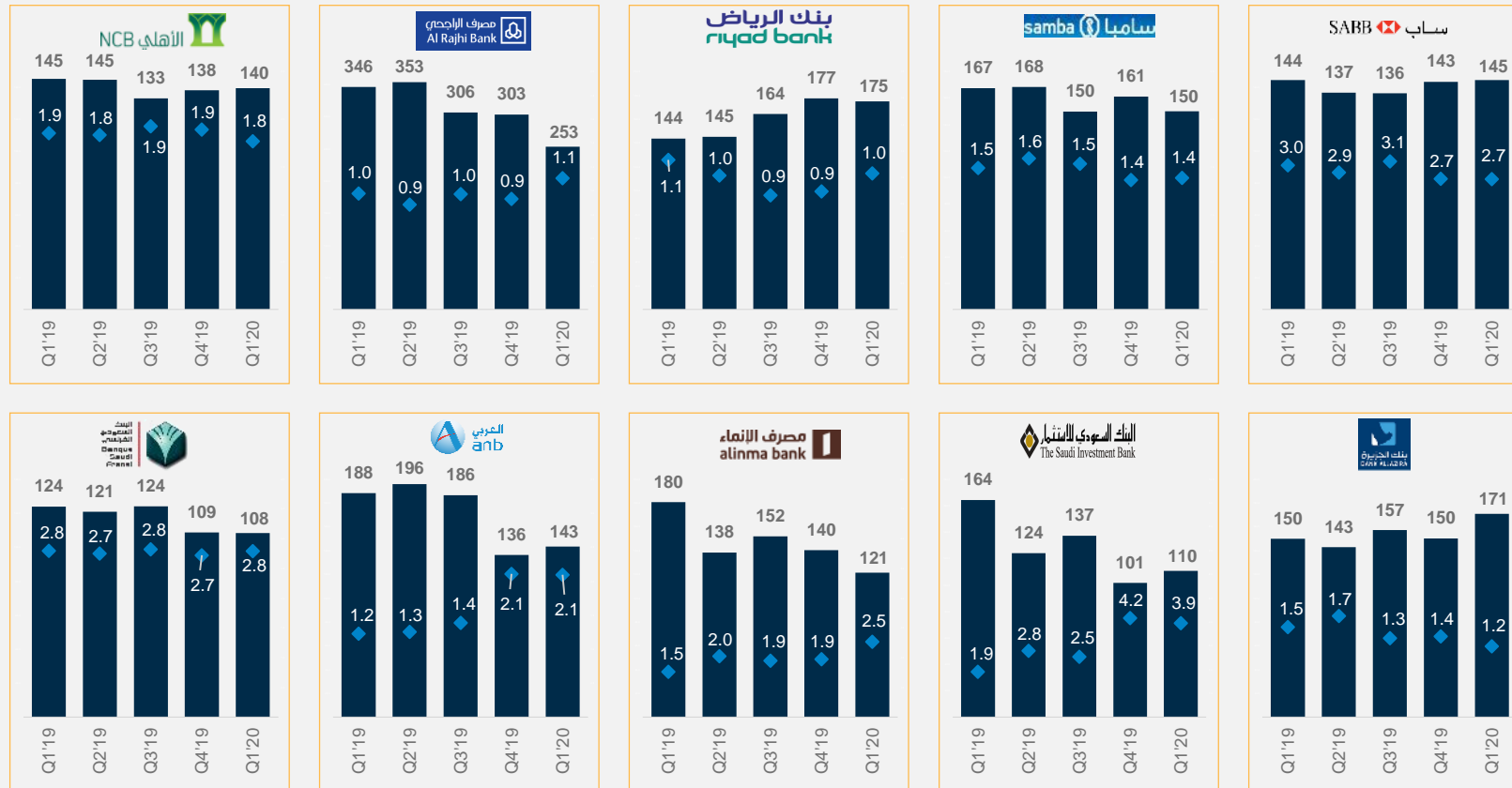
- C/I ratio improved for majority of the banks except NCB, ARNB, ALINMA and BJAZ
- RIBL, BSFR and SAMBA saw improvement in C/I ratio of 8.8% points, 8.4% points and 7.5% points, respectively
- SABB stated that there were certain one-off expenses incurred during the quarter. Excluding those one-off costs the bank's CI ratio stands at 36.0%
- BJAZ continued to report highest C/I ratio at 56.5%, while BSFR reported the lowest C/I ratio at 31.8%

Note: Scaling and some numbers might not add up due to rounding
 Source: Financial statements, investor presentations, A&M analysis
 *Comparison on QoQ basis

Coverage and NPL/Net Loan Ratio Deteriorated for the Fourth Consecutive Quarter

■ Coverage Ratio, % ◆ NPL / Net loans, %

Coverage Ratio¹ and NPL / Net Loans Ratio (% , Quarterly)



KEY TAKEAWAYS

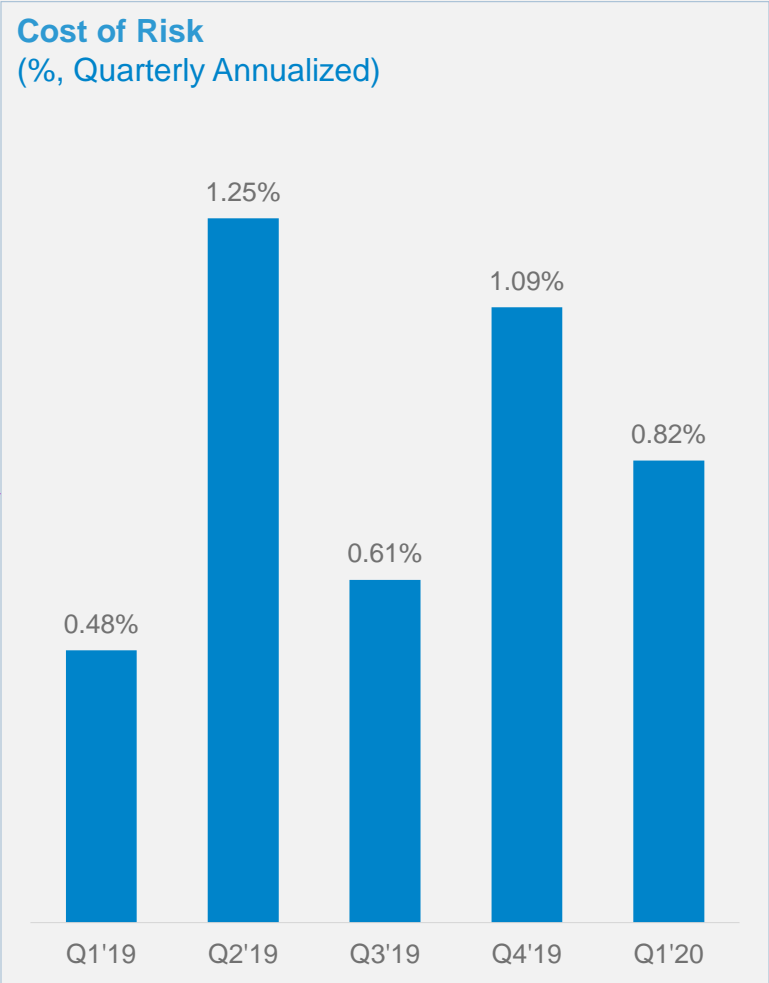
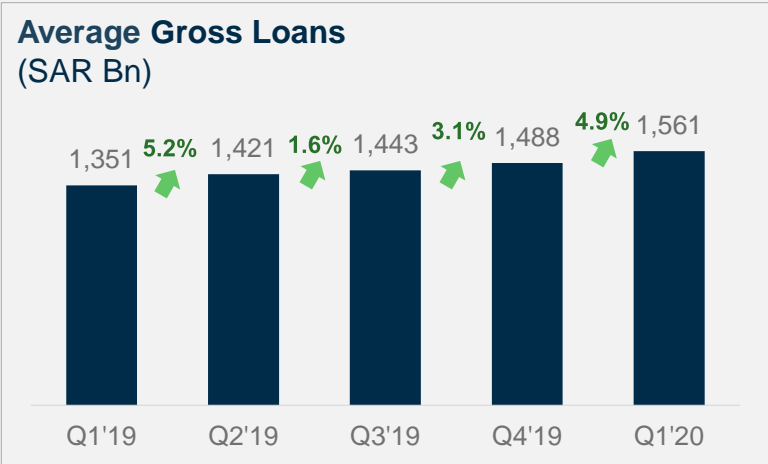
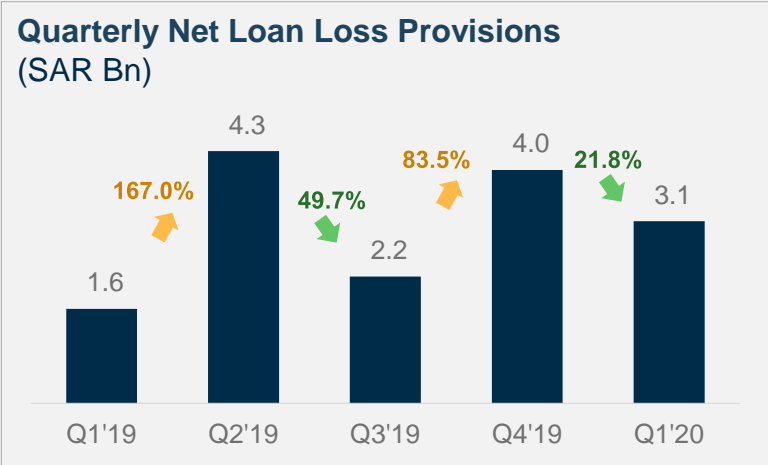
- Aggregate coverage ratio declined to 147.8% (-2.9% points), while NPL / net loan ratio increased to 1.9% in Q1'20 (+0.1% points)
- RJHI's coverage ratio fell at the highest pace (-49.8% points), as NPLs advanced by 24.5%
- Similarly, ALINMA's NPL / net loan ratio increased the most (+0.6% points), as the bank's NPL increased 34%
- On the other hand, BJAZ reported the largest increase in coverage ratio (+20.7% points). SIBC showed the highest decrease in NPL / net loan ratio (-0.2% points)

Note: Scaling and some numbers might not add up due to rounding

Source: Financial statements, investor presentations, A&M analysis, ¹ accumulated allowance for impairment / NPL

Volatile Trend in Cost of Risk Continues

➔ Improved ↔ Stable ➔ Worsened



KEY TAKEAWAYS

- Cost of Risk has seen a fall from 1.09% in Q4'19 to 0.82% in Q1'20, however, it is almost double compared to Q1'19
- While the gross L&A has consistently reported reasonable increase, provisioning has seen a volatile trend since Q1'19
 - Total provisioning fell by 21.8% QoQ to SAR 3.1bn, after increasing by 83.5% in the preceding quarter
 - SABB (-61.2% QoQ) reported the highest decline in total provisioning, followed by ARNB (-53.3% QoQ)

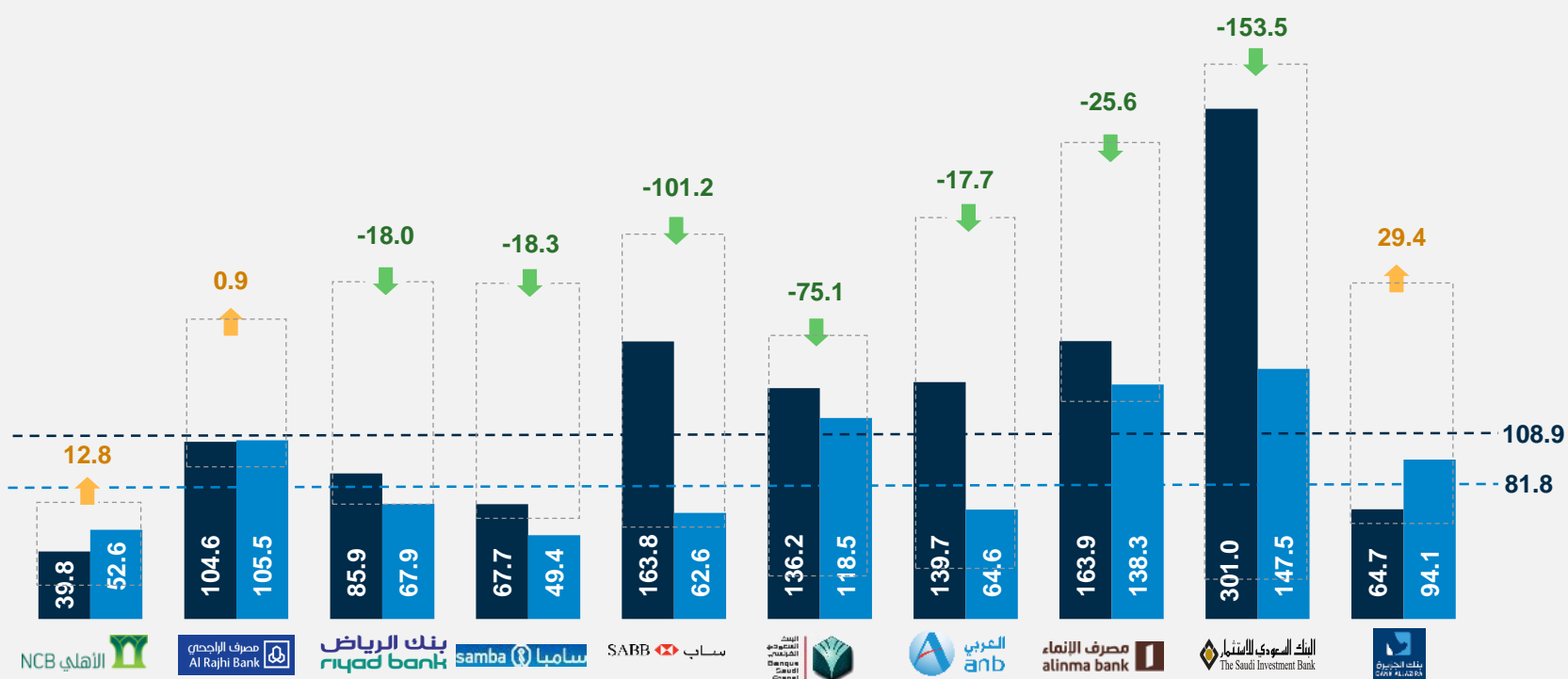
Note: Scaling and some numbers might not add up due to rounding
 Source: Financial statements, investor presentations, A&M analysis

Cost of Risk Decreased for Most of the Banks

➔ Improved ➔ Stable ➔ Worsened

Cost of Risk (bps) – Net of Reversals

■ Q4'19 ■ Q1'20 - - - Q4'19 Av - - - Q1'20 Av



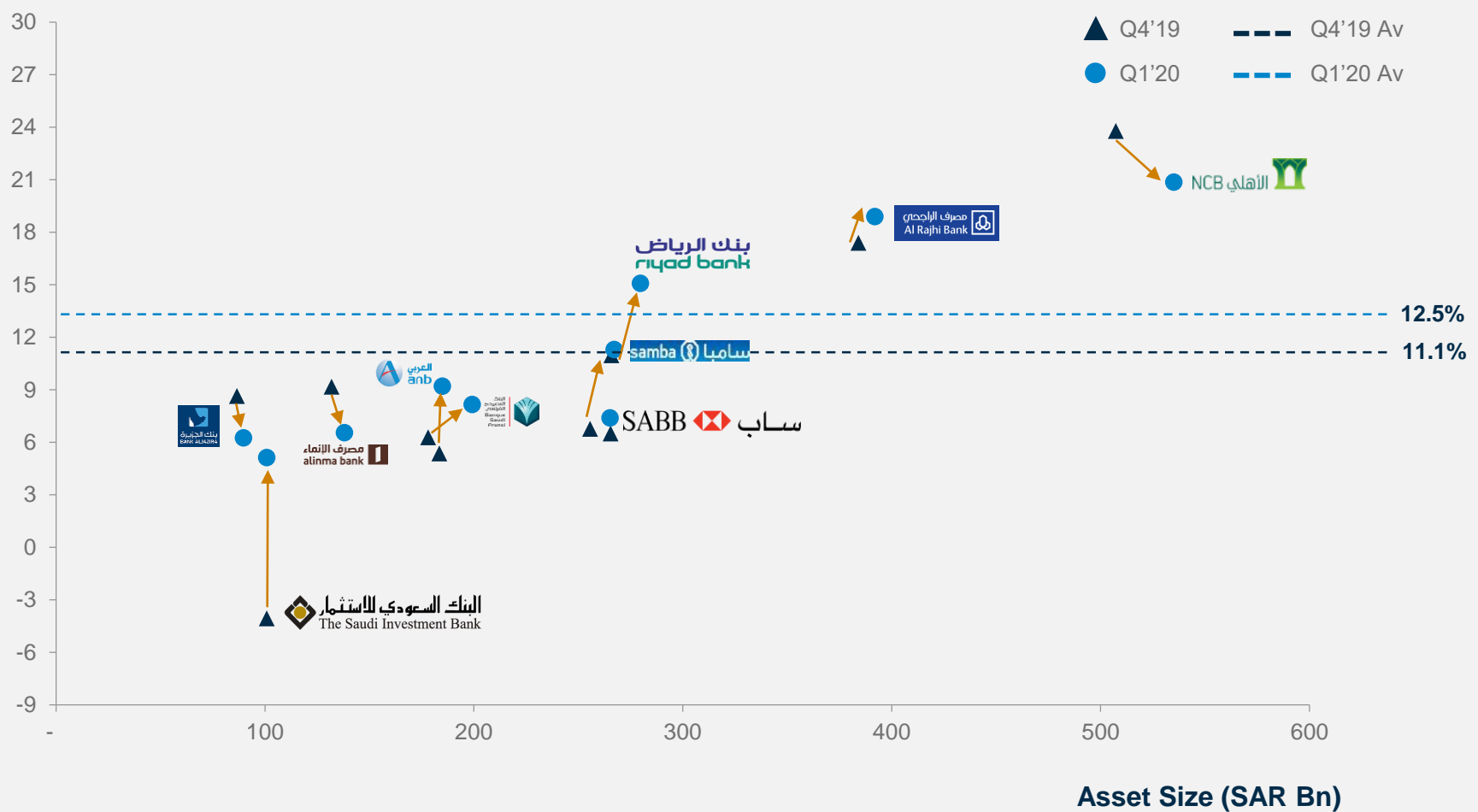
KEY TAKEAWAYS

- SIBC and SABB reported the highest decrease in cost of risk at 153.5 bps and 101.2 bps, respectively
- BJAZ, NCB and RJHI, on the other hand, reported an increase in cost of risk during the quarter

Note: Scaling and some numbers might not add up due to rounding
 Source: Financial statements, investor presentations, A&M analysis

Increased Operating Efficiency and Reduced Provisioning Supported Profitability of the Banks

Return on Equity (%)



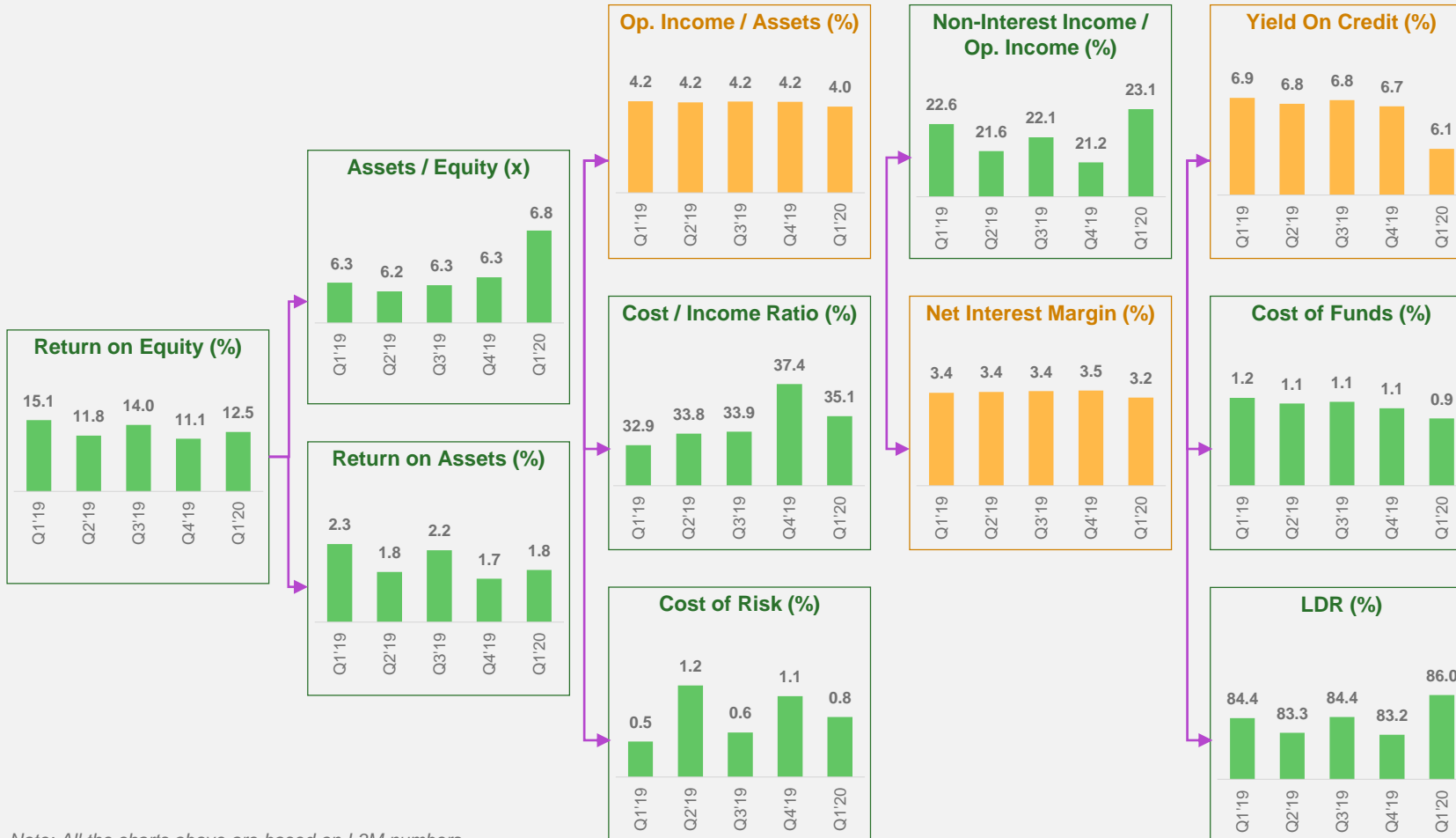
KEY TAKEAWAYS

- RoE of majority of the banks increased except for NCB, BJAZ and ALINMA
- SIBC reported the largest jump in RoE from -4.1% in Q4'19 to 5.1% in Q1'20
- NCB reported the highest RoE (20.9%), while SIBC reported the lowest RoE (5.1%) for the period

Source: Financial statements, Investor presentations, A&M analysis

KSA Banks Likely to Witness COVID-19 Headwinds in the Near Term

■ Improved
 ■ Stable
 ■ Worsened



Note: All the charts above are based on L3M numbers
 Op Income stands for Operating Income
 Scaling and some numbers might not add up due to rounding
 Source: Financial statements, Investor presentations, A&M analysis

KEY TAKEAWAYS

- RoE increased to 12.5% in Q1'20, as increased operating efficiency and lower provisioning helped in negating the effect of lower operating income
- While there was an improvement in the profitability, the sector is likely to face challenging environment due to COVID-19 headwinds
 - Lower oil prices and austerity measures from the government would likely delay major projects and impact demand in the economy
 - Thus, loan growth would remain limited, while low interest rate regime coupled with a possible increase in provisioning would impact profitability
 - In the medium to long term, banks are likely to focus more on rationalizing their costs to hedge against the uncertain conditions

GCC Banking Consolidation

GCC list of M&A transactions in banking sector during 2019

Announcement Date	Target Company	Target Country	Acquirer Company	% Sought	Consideration (SAR Mn)	Deal Status*
29-Jan-19	Union National Bank PJSC	UAE	Abu Dhabi Commercial Bank PJSC	100%	11,774	Completed
29-Jan-19	Al-Hilal Bank PJSC	UAE	Abu Dhabi Commercial Bank PJSC	100%	NA	Completed
15-Mar-19	Banque Saudi Fransi	Saudi Arabia	Olayan Investments, Ripplewood Advisors LLC	5%	1,643	Completed
03-Apr-19	Oman United Exchange Co	Oman	Private Investor	25%	NA	Completed
10-Apr-19	Invest bank PSC	UAE	Emirate of Sharjah United Arab Emirates	50%	1,010	Completed
21-Apr-19	HSBC Saudi Arabia Ltd	Saudi Arabia	HSBC Holdings PLC	2%	32	Completed
07-Apr-19	Noor Bank PJSC	UAE	Dubai Islamic Bank PJSC	100%	NA	Completed
12-May-19	Gulf Bank KSCP	Kuwait	Alghanim Industries Ltd	16%	NA	Completed
20-Jun-19	Warba Bank KSCP	Kuwait	Kuwait & Middle East Financial Investment Co KSCP	75.7%	NA	Proposed
08-Aug-19	DenizBank AS	Turkey	Emirates NBD PJSC	0.2%	NA	Completed
15-Aug-19	Cqur Bank LLC	Qatar	VTB Bank PJSC	19%	NA	Completed
12-Sept-19	Ahli United Bank BSC	Bahrain	Kuwait Finance House KSCP	100%	21,883	Pending
31-Dec-19	Alizz Islamic Bank SAOG	Oman	Oman Arab Bank SAOC	81%	NA	Pending

Source: Bloomberg

*Proposed Status: Board suggests shareholders to consider the acquisition

*Pending Status: Acquisition has announced

*Completed Status: Acquisition has completed











GLOSSARY



Glossary

	Metric	Abbreviation	Definition
Size	Loans and Advances Growth		QoQ growth in EOP net loans and advances for the top 10
	Deposits Growth		QoQ growth in EOP customer deposits for the top 10
Liquidity	Loan-to-Deposit Ratio	LDR	(Net EOP loans and advances / EOP customer deposits) for the top 10
Income & Operating Efficiency	Operating Income Growth		QoQ growth in aggregate quarterly operating income generated by the top 10
	Operating Income / Assets		(Annualized quarterly operating income / quarterly average assets) for the top 10
	Non-Interest Income / Operating Income		(Quarterly non-interest income / quarterly operating income) for the top 10
	Net Interest Margin	NIM	(Aggregate annualized quarterly net interest income) / (quarterly average earning assets) for the top 10 Earnings assets are defined as total assets excluding goodwill, intangible assets, and property and equipment
	Yield on Credit	YoC	(Annualized quarterly gross interest income / quarterly average loans & advances) for the top 10
	Cost of Funds	CoF	(Annualized quarterly interest expense + annualized quarterly capital notes & tier I sukuk interest) / (quarterly average interest bearing liabilities + quarterly average capital notes & tier I sukuk interest) for the top 10
	Cost-to-Income Ratio	C/I	(Quarterly operating expenses / quarterly operating income) for the top 10
Risk	Coverage Ratio		(Loan loss reserves / non-performing loans) for the top 10
	Cost of Risk	CoR	(Annualized quarterly provision expenses net of recoveries / quarterly average gross loans) for the top 10
Profitability	Return on Equity	RoE	(Annualized quarterly net profit attributable to the equity holders of the banks – annualized quarterly capital notes & tier I sukuk interest) / (quarterly average equity excluding capital notes) for the top 10
	Return on Assets	RoA	(Annualized quarterly net profit / quarterly average assets) for the top 10
	Return on Risk-Weighted Assets	RoRWA	(Annualized quarterly net profit generated / quarterly average risk-weighted assets) for the top 10
Capital	Capital Adequacy Ratio	CAR	(EOP tier I capital + tier II capital) / (EOP risk-weighted assets) for the top 10

Glossary (cont'd.)

Bank	Assets (SAR Bn)*	Abbreviation	Logo
National Commercial Bank	535.0	NCB	 NCB الأهلي
Al Rajhi Bank	391.9	RJHI	 مصرف الراجحي Al Rajhi Bank
Riyad Bank	279.6	RIBL	 بنك الرياض riyad bank
Samba Financial Group	267.0	SAMBA	 sambam سامبا
Saudi British Bank	265.2	SABB	 SABB ساب
Banque Saudi Fransi	199.2	BSFR	 البنك السعودي الفرنسي Banque Saudi Fransi
Arab National Bank	184.9	ARNB	 البنك العربي anb
Alinma Bank	138.0	ALINMA	 مصرف الإنماء alinma bank
Saudi Investment Bank	100.8	SIBC	 البنك السعودي للاستثمار The Saudi Investment Bank
Bank Al-Jazira	89.7	BJAZ	 بنك الجزيرة BANK ALJAZIRA

Note: Banks are sorted by assets size
* As on 31st March 2020