



Saudi Arabia Banking Pulse

Quarter 3, 2020

FOREWORD

Alvarez & Marsal Middle East Limited (A&M) is delighted to publish the 3rd edition of the Kingdom of Saudi Arabia (KSA) Banking Pulse (“The Pulse”). In this 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.

Kindly note that total asset base of Bank Albilad (BALB: SAR 92.3bn) has exceeded that of Bank AlJazira (BAJ: SAR 91.9bn) in Q3’20. Hence, we have changed our universe of top ten banks to include BALB and exclude BAJ, as the Pulse tracks the performance of the top ten banks by asset size. Hence, for consistency of comparison, all historical data has been adjusted to include BALB instead of BAJ.

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.

The IMF has predicted that the Saudi Arabian GDP is expected to contract at slower rate (-5.4%), compared to its previous estimate (-6.8%) during FY’20. However, persistently low oil price environment is expected weigh on the economy in the near term. The government in September’20 announced that the budget spending for 2021 would be 7.5% lower in light of current economic environment. Thus, economic environment is likely to remain challenging in the near term.

We hope that you will find our third 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

Co-Authors



Dr. Saeeda Jaffar

Co-Author, Managing Director
Head of Middle East

- 18+ years of international experience in management consulting and industry
- Focuses on strategic and performance-related matters in financial institutions, sovereign wealth funds, family businesses, real estate, private equity and private investments
- Emirati National, frequent speaker and moderator in Banking & Finance events



Asad Ahmed

Co-Author, Managing Director
Head of ME Financial Services

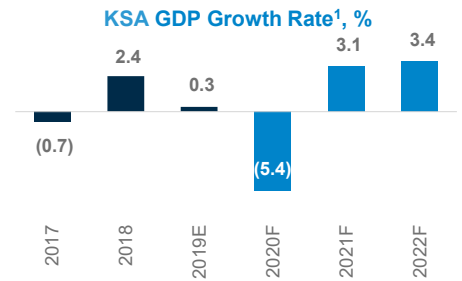
- 30+ years of experience in banking
- Focuses on performance improvement, turn-around, credit management, and formulating and managing strategic and operational changes in financial institutions
- Former CEO of banks in the UAE & Kenya

**CONTACT
DETAILS**

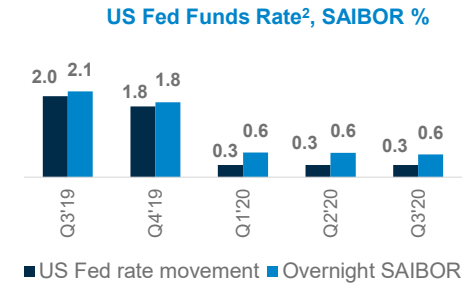
financialservices-me@alvarezandmarsal.com
Phone: +97145671065

Saudi Arabia Macro & Sector Overview

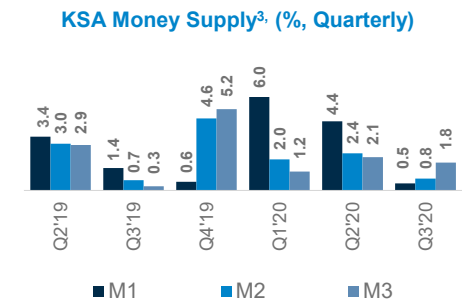
Macro overview



- In Q2'20 KSA's GDP contracted 7.0%, on the back of contraction in oil (5.3%) and non-oil (-8.2%) sectors
- In Q3'20, the average PMI reading increased to 49.8 from 46.7 in Q2'20, showing that the private non-oil economy continued to contract during the last quarter
- In Oct'20, the IMF forecasted the nation's GDP to contract by 5.4% for FY'20, compared to its previous estimate to contract by 6.8%**



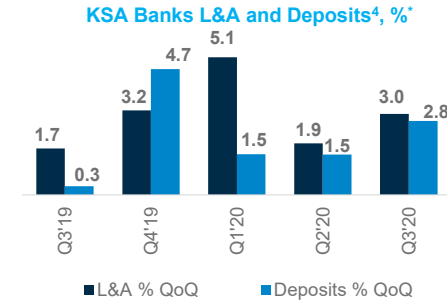
- The US Fed has committed to keep its lending rates at current levels until the US economy is fully recovered
- Overnight SAIBOR has also remained at its record low levels and has settled at 0.56% at the end of Q3'20**
- Consequently, the Saudi Arabian central bank is also expected to hold its interest rates at current levels in the foreseeable future, to offset the headwinds from COVID-19



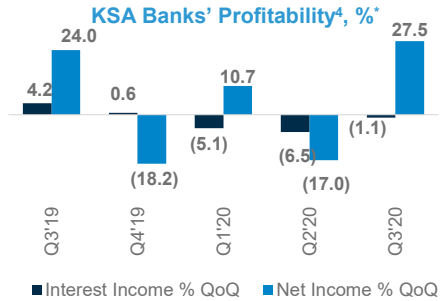
- In Q3'20, M2 money supply growth stood at 0.8% QoQ, and 10.0% YoY to reach SAR 1.9tn
- M2 money supply increased primarily driven by **1.7% QoQ increase in time & savings deposits to SAR 0.5tn**
- M1 increased by 0.5% QoQ in Q3'20 to SAR 1.4tn, while M3 money supply grew 1.8% QoQ to SAR 2.1tn

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 September 30th 2020, QoQ stands for quarter over quarter, net income excludes the one-off impairment charge reported by Saudi British Bank in Q2'20

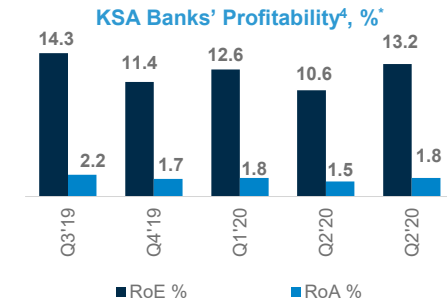
Banking overview Q3'20



- Total loans & Advances (L&A) of top ten KSA banks grew at a faster pace in Q3'20 (3.0% QoQ), compared to Q2'20 (1.9% QoQ)
- Similarly, deposit growth improved to 2.8% QoQ, compared to 1.5% QoQ in the preceding quarter
- The improvement in the L&A and deposits growth could be partially attributable to the unlocking of certain sections of the economy post Q2'20



- Interest income of top ten banks declined by 1.1% QoQ, amid persistently low interest rates
- Net income rose by 27.5% QoQ, facilitated by an increase in operating income (+6.5% QoQ) and decrease in provisions (-36.7% QoQ)
- While there has been an improvement in profitability, the near term outlook remains bearish in light of sluggish economic environment



- The return ratios improved during the quarter primarily driven by increased net income
- Return on Equity (RoE – Q3'20 annualized) reached 13.2%, highest level in last three quarters
- Similarly, return on asset (RoA – Q3'20 annualized) increased from 1.5% in Q2'20 to 1.8% in Q3'20

Pulse: KSA Banks Reported a Surprising Recovery in Profitability, Driven by Unlocking of Certain Sections of Economy

➔ Improved
 ↔ Stable
 ➔ Worsened

Metric		Q2'20	Q3'20	Q3'19	Q4'19	Q1'20	Q2'20	Q3'20	Key Trends of Q3'20	
Size	L&A Growth (QoQ)	1.9%	3.0%						1	Growth in L&A stood at 3.0% QoQ, while deposits increased by 2.8% QoQ
	Deposits Growth (QoQ)	1.5%	2.8%						2	LDR increased for the third consecutive quarter to 86.9%, as L&A growth outpaced deposits growth
Liquidity	Loan-to-Deposit Ratio (LDR)	86.7%	86.9%						3	Operating income growth (+6.5% QoQ) saw a sizeable recovery, as net interest income and net fee income increased 2.0% and 20.0%, respectively
Income & Operating Efficiency	Operating Income Growth (QoQ)	-3.9%	6.5%						4	NIM compressed further by 3 bps to reach near the 3% threshold
	Operating Income / Assets	3.7%	3.9%							Banks continued to improve their efficiency, as C/I ratio improved for the third consecutive quarter to reach 34.3%
	Non-Interest Income (NII) / Operating Income	21.6%	24.9%							CoR decreased substantially (-50 bps QoQ), as impairment charges reduced by 36.7% QoQ
	Yield on Credit (YoC)	5.5%	5.3%							RoE and RoA saw improvements after a fall last quarter
	Cost of Funds (CoF)	0.6%	0.5%						5	RoRWA and CAR improved to 2.2%, and 19.4% respectively in line with increased net income
	Net Interest Margin (NIM)	3.1%	3.0%						6	
Risk	Cost-to-Income Ratio (C/I)	34.9%	34.3%						7	
	Coverage Ratio	148.3%	144.1%						8	
Profitability	Cost of Risk (CoR)	1.3%	0.8%							
	Return on Equity (RoE)	10.6%	13.2%							
	Return on Assets (RoA)	1.5%	1.8%							
Capital	Return on Risk-Weighted Assets (RoRWA)	1.8%	2.2%							
	Capital Adequacy Ratio (CAR)	18.8%	19.4%							

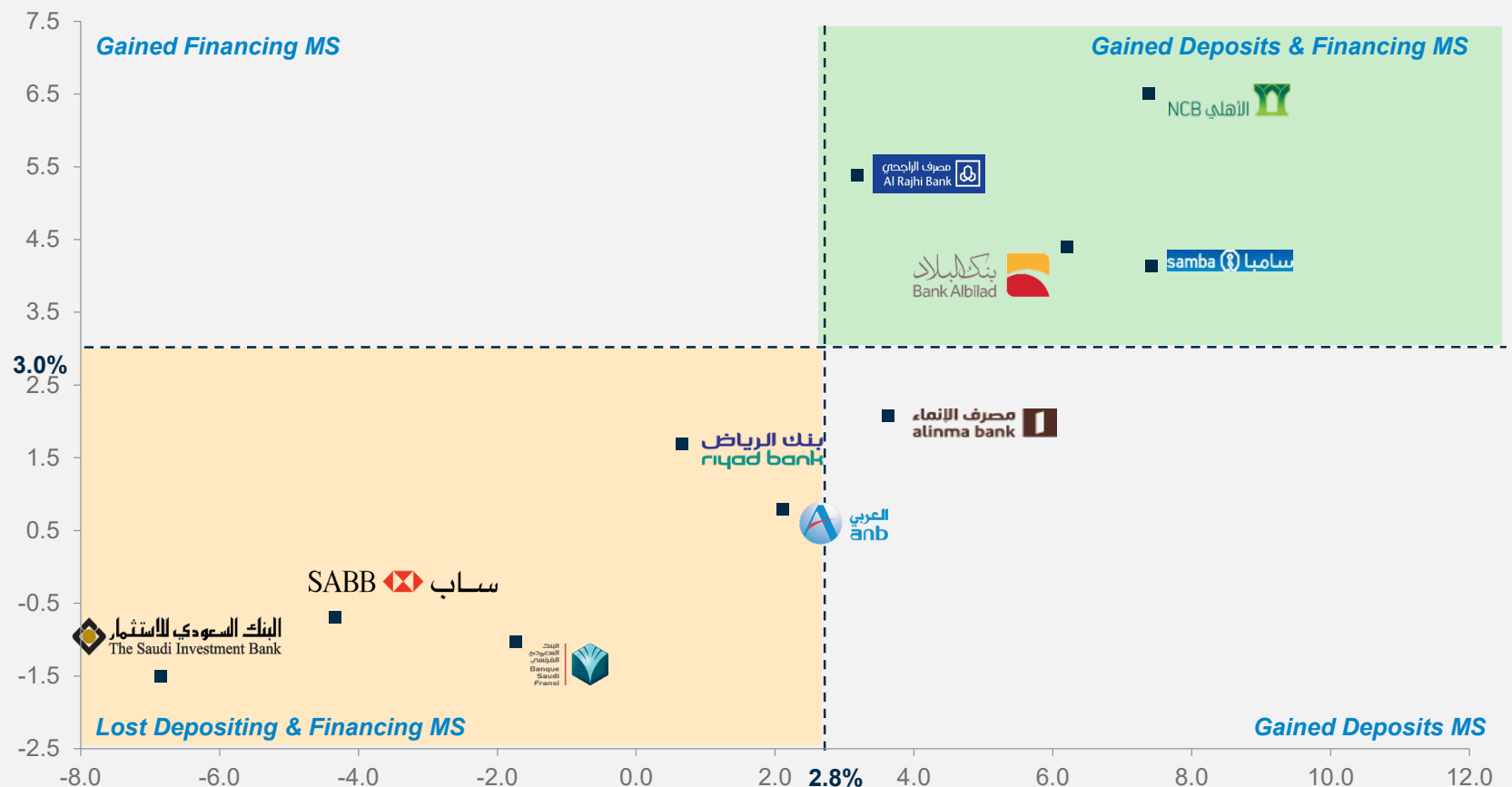
Note 1: Growth in loans & advances and deposits were presented QoQ instead of YoY

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

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

NCB Witnessed a Growth in Both L&A, while SAMBA's Deposits Growth Outperformed its Top Peers

L&A Growth QoQ (%)



KEY TAKEAWAYS

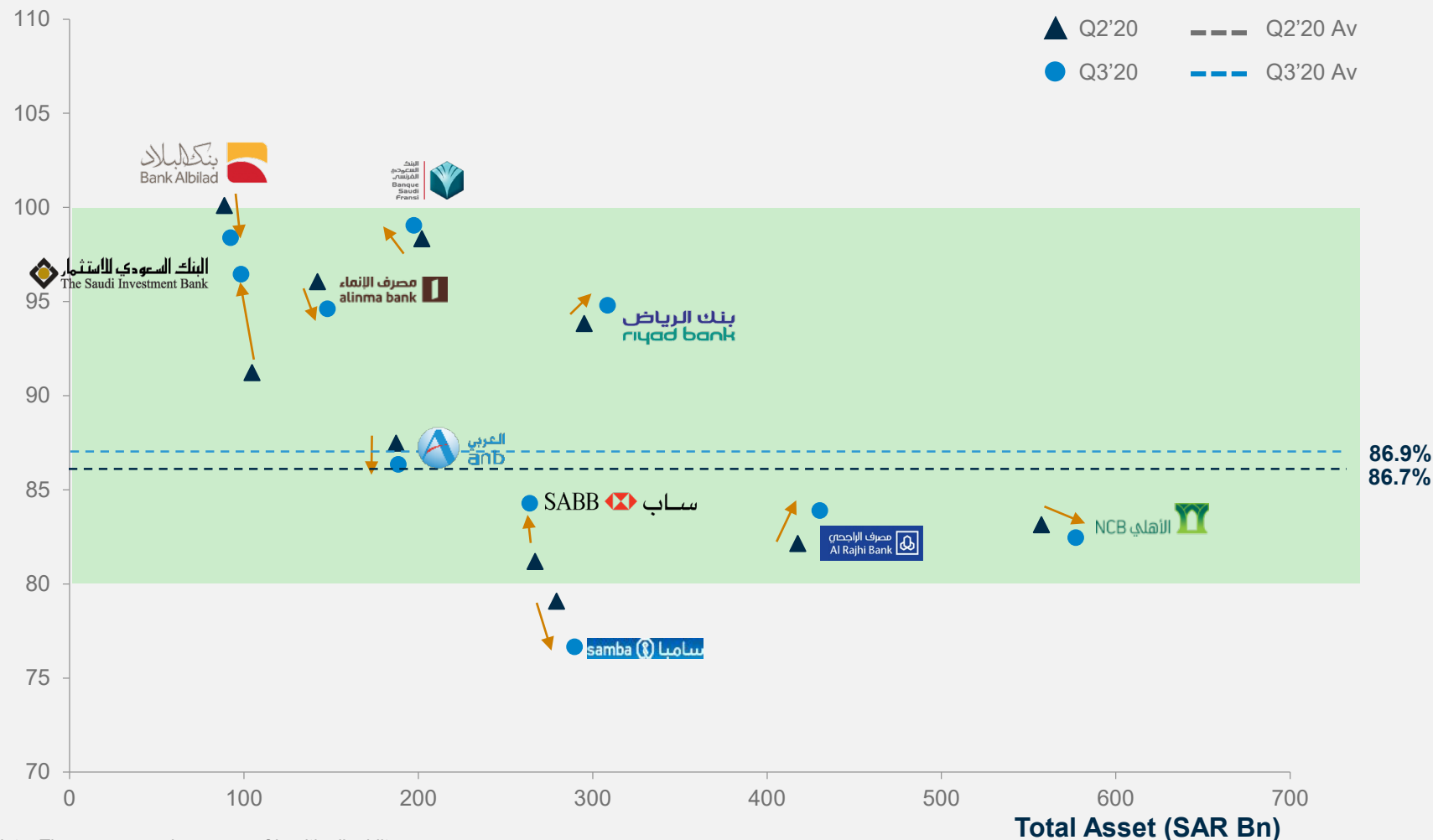
- L&A and deposits of top ten banks increased by 3.0% and 2.8%, respectively
- L&A growth of NCB (+6.5%) was the highest among all peers
 - The growth was largely driven by increased credit uptake in consumer & credit card segment
- SAMBA reported the highest increase in deposits (+7.4% QoQ), as time deposits increased 20.2% QoQ
- On the other hand, SIBC's L&A decreased the most (-1.5%)
- SIBC reported the largest decline in deposits (-6.9% QoQ), as the bank's demand deposits declined 13.5% QoQ

Note: MS stands for market share

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

Five of the Top Ten Banks Reported an Increase in LDR

Loans to Deposits Ratio (%)

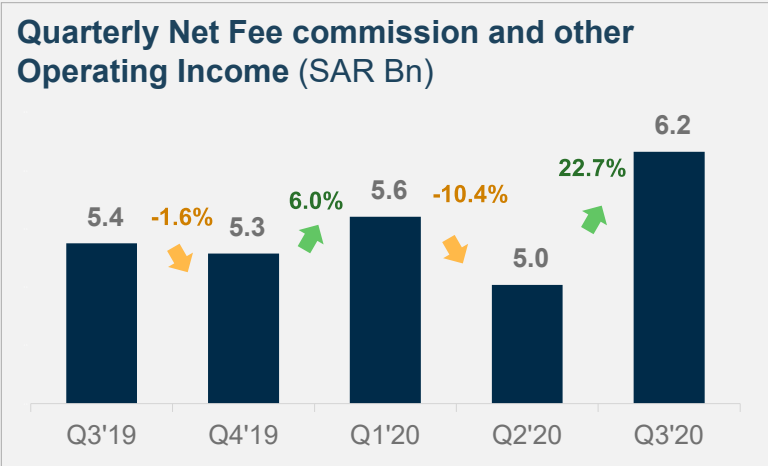
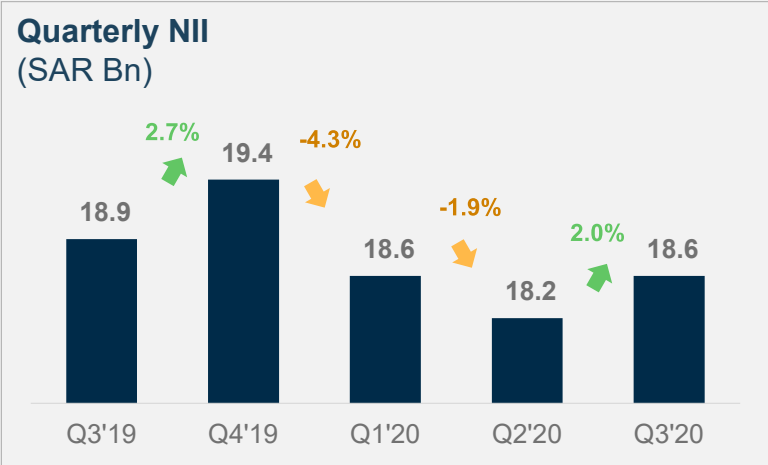


KEY TAKEAWAYS

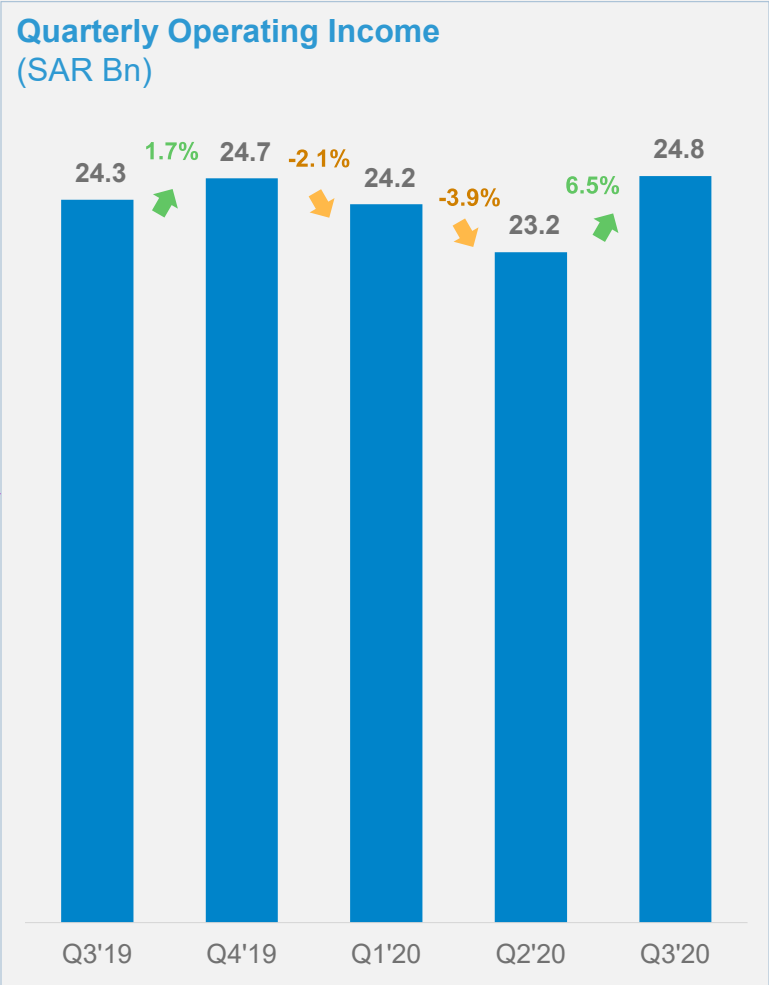
- Aggregate LDR increased from 86.7% in Q2'20 to 86.9% in Q3'20
- SIBC (+5.2% points) reported the highest increase in LDR, while SAMBA (-2.4% points) reported the highest decline in LDR during the quarter

Easing of Lockdown Measures Facilitated Operating Income Growth

➔ Improved
 ↔ Stable
 ➔ Worsened



+

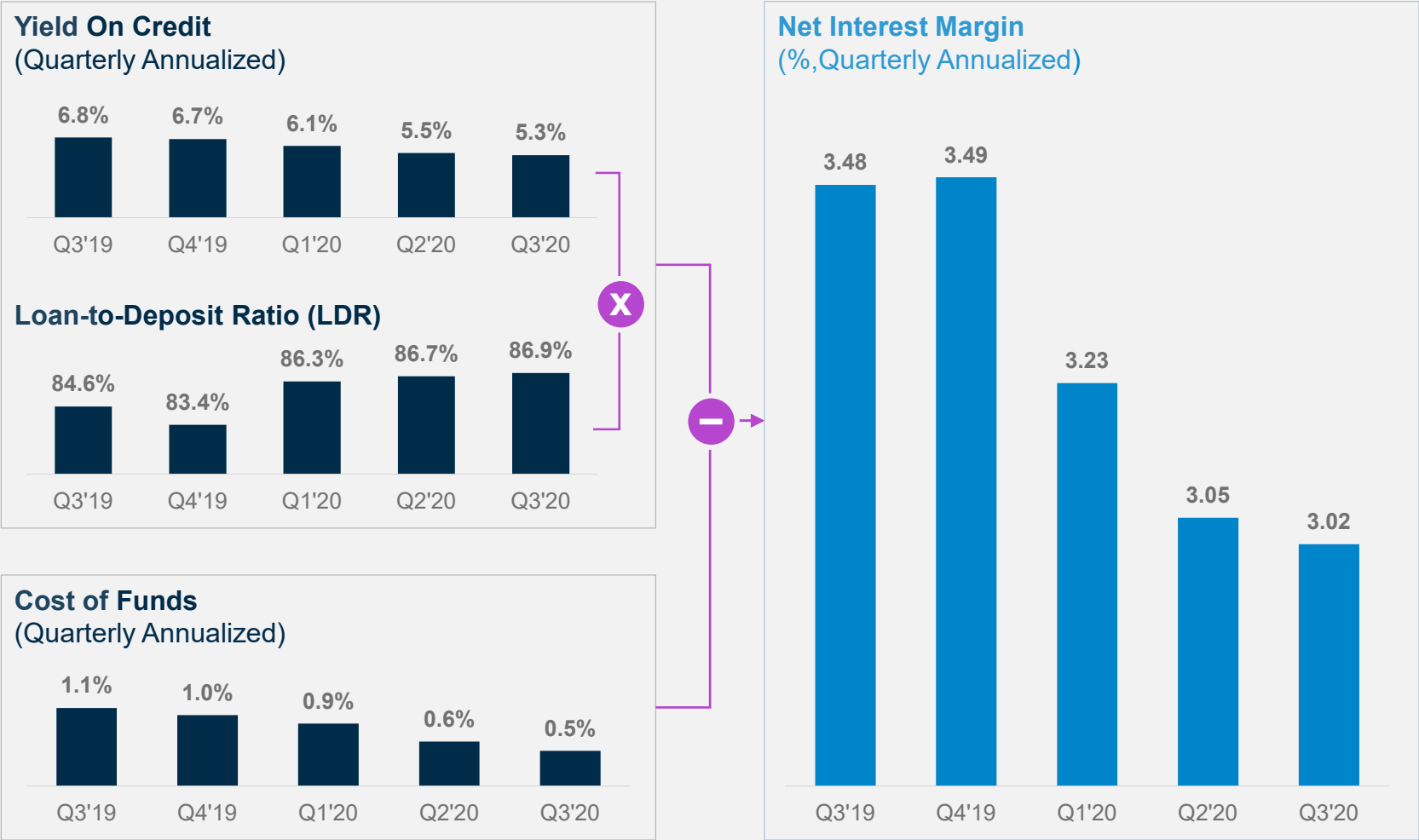


KEY TAKEAWAYS

- Total operating income increased by 6.5% QoQ. Increase in NII (+2.0%) and non-interest income (+22.7%) facilitated operating income growth
- Non-interest income rose, as net fee income increased (~20% QoQ), driven by unlocking of certain sections of economy
- Among the individual banks, NCB (+18.3%) reported the biggest jump in operating income, as the bank was able to increase its NII
- On the other hand, SABB's operating income decreased -7.6%, as the bank's NII reduced, largely on the back of decline in L&A (-0.7% QoQ)

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

NIM Compressed for the Third Consecutive quarter

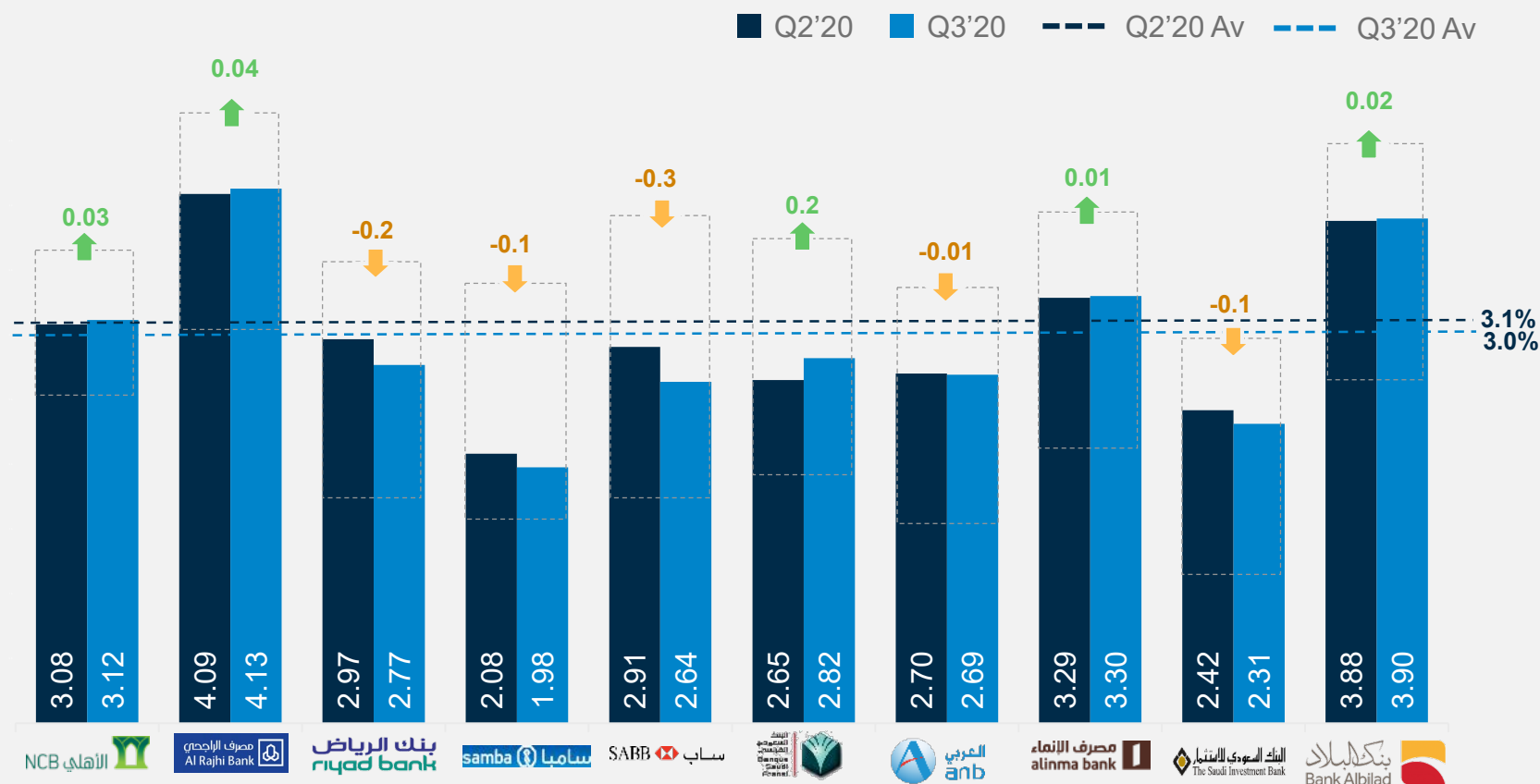


- KEY TAKEAWAYS
- NIM fell by 3 bps to reach 3.02%, the lowest level in past several quarters
 - Persistent decline in yield on credit (-19 bps QoQ in Q3'20) has been the major factor impacting NIM during this year

NIM of Most of the Banks Remained Broadly Unchanged

→ Improved ↔ Stable → Worsened

Net Interest Margin (% Quarterly)

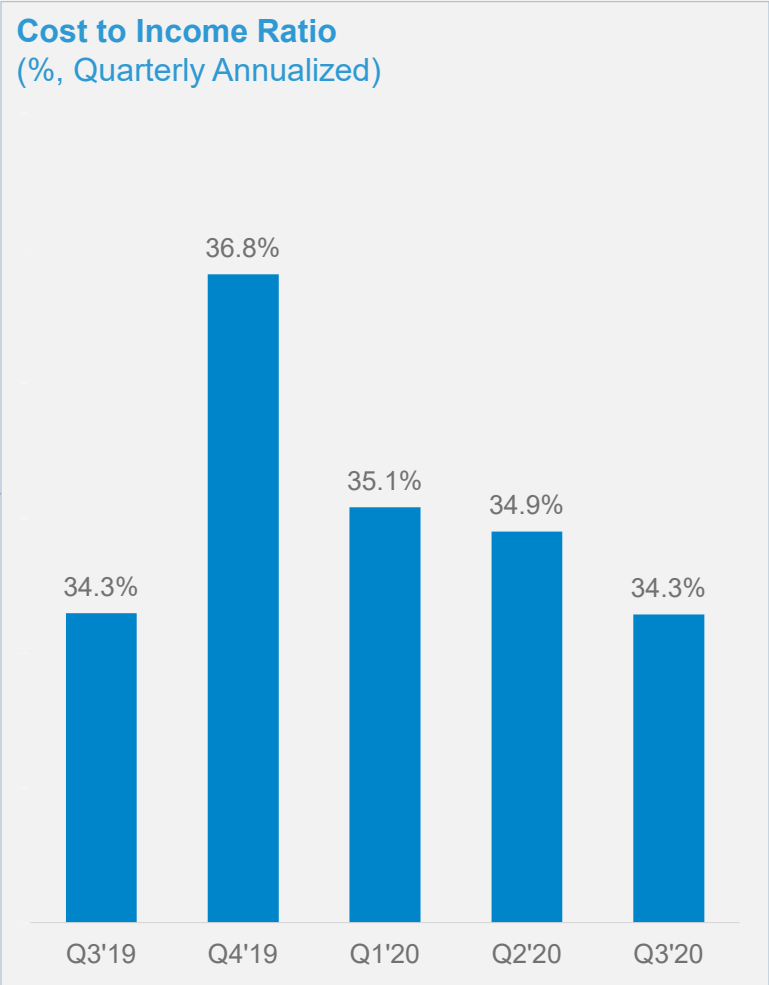
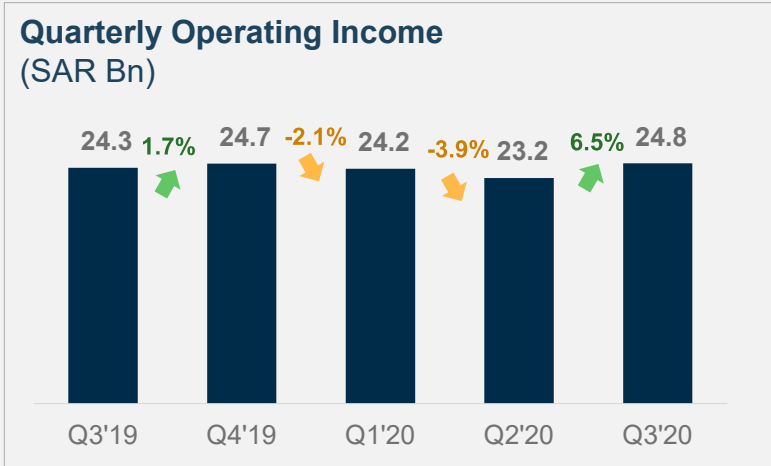
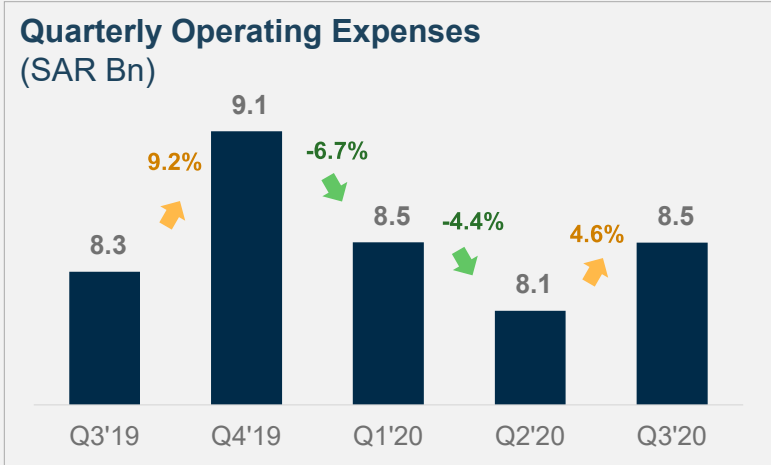


KEY TAKEAWAYS

- SABB and RIBL reported highest decline in NIM of 27 bps and 20 bps, respectively
- On the other hand, BSF (+17 bps QoQ) reported the highest increase
- NIM for NCB, ALRAJHI, ANB, ALINMA and BALB remained broadly unchanged during Q3'20

Aggregate Operating Efficiency Improved for the Third Consecutive Quarter

➡ Improved ↔ Stable ➡ Worsened



KEY TAKEAWAYS

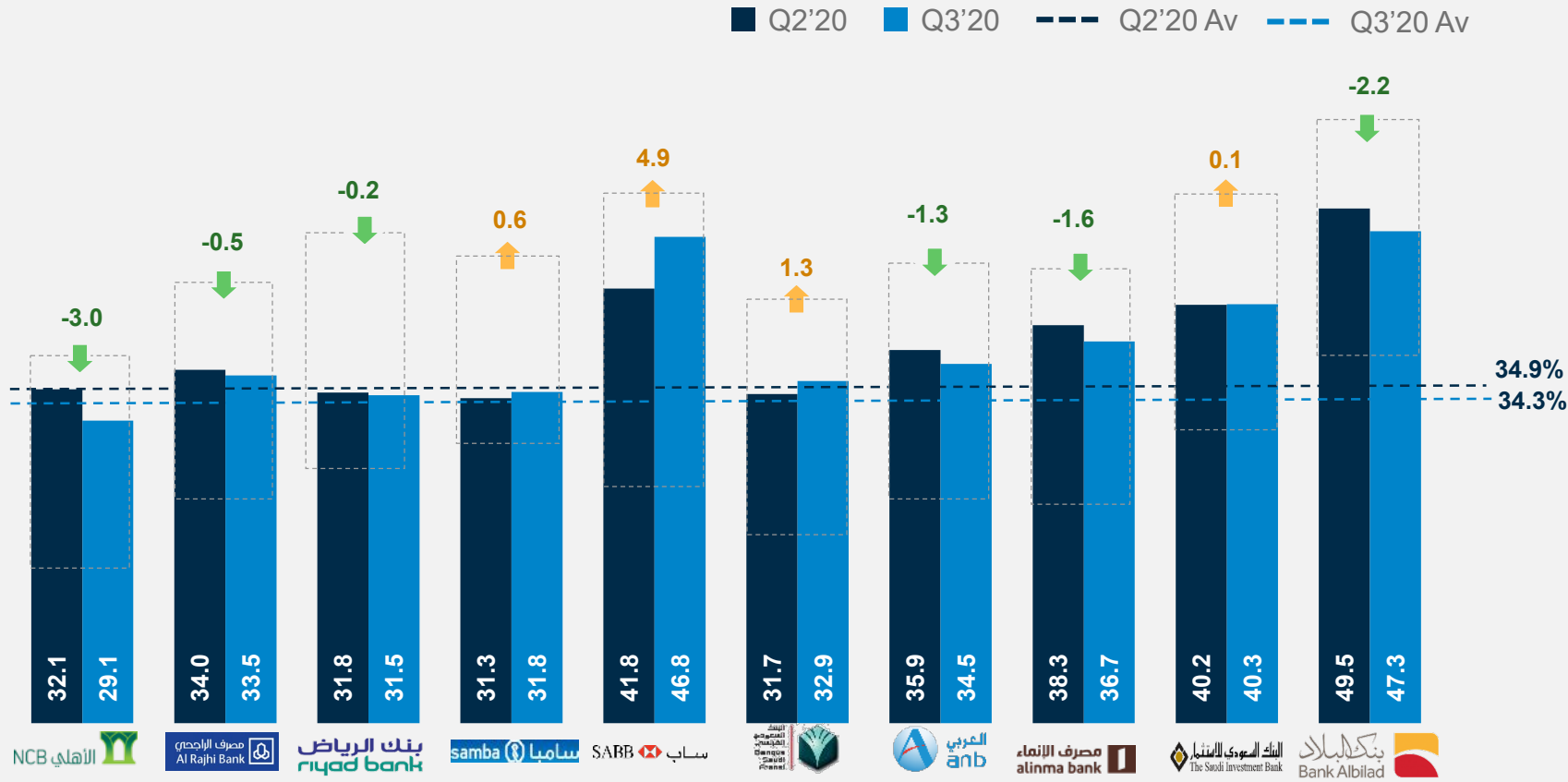
- C/I ratio continued to decline for third consecutive quarter, by 0.6% points QoQ to 34.3%
- Though there is an increase in operating expenses (+4.6% QoQ), C/I ratio fell as operating income increased at a quicker pace (+6.5% QoQ)
- The C/I ratio now stands below the average achieved in FY'19 (34.5%)

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

Operating Efficiency Improved the Most for NCB, while it Deteriorated the Most for SABB

➔ Improved ➔ Stable ➔ Worsened

Cost to Income Ratio (% Quarterly)



KEY TAKEAWAYS

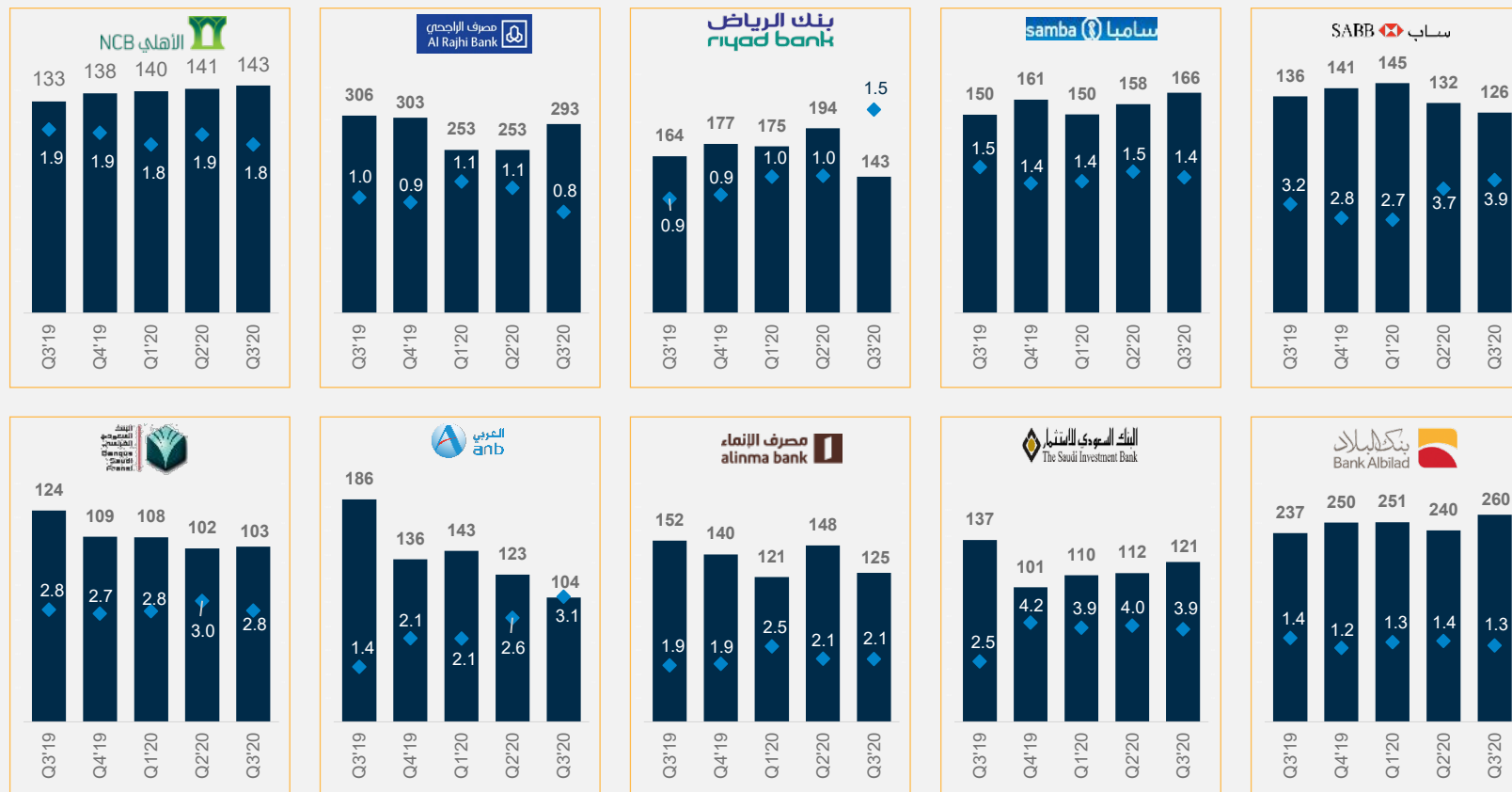
- Six of the top ten banks reported a decline in the C/I ratio
- NCB saw the highest improvement in C/I ratio of 3.0% points despite an increase of 7% QoQ in operating expenses
- SABB's C/I ratio increased by 4.9% points, as the bank's operating income fell ~8%, while costs increased ~3%

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 Ratio Deteriorated for the Fifth Consecutive Quarter

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

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



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

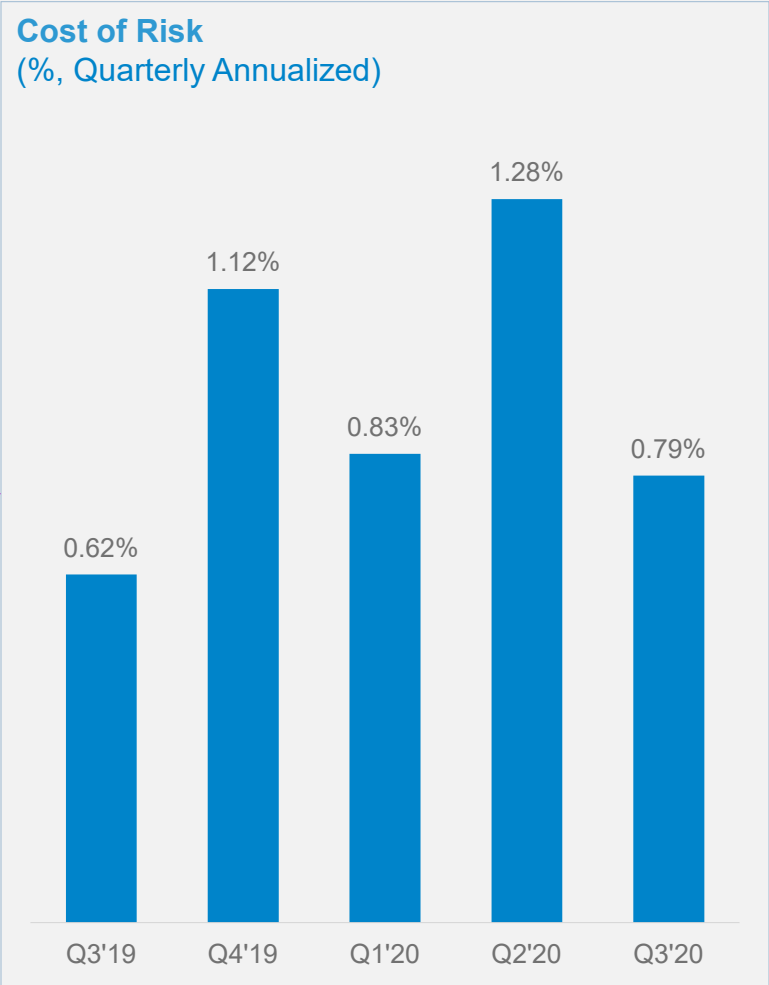
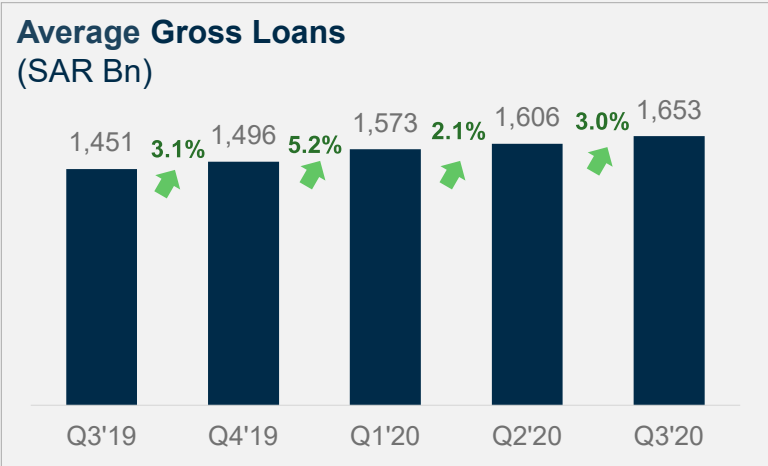
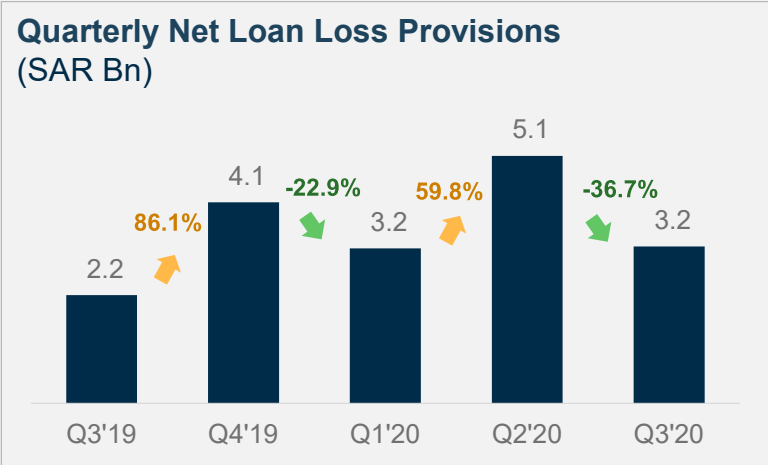
Source: Financial statements, investor presentations, A&M analysis, ¹ accumulated allowance for impairment / NPL

KEY TAKEAWAYS

- Aggregate coverage ratio decreased to 144% (-4.2% points), while NPL / net loan ratio increased slightly to 2.0%
- RIBL's coverage ratio declined at the highest rate (-50.6% points), as NPLs rose by ~51%
- On the other hand, ALRAJHI reported the highest increase in coverage ratio of 40.1% points
- ANB's NPL / net loan ratio increased the most (+0.5% points), as the bank's NPL increased sharply by ~21%

Cost of Risk Reached Below Q4'19 Levels

➡ Improved ↔ Stable ➡ Worsened



KEY TAKEAWAYS

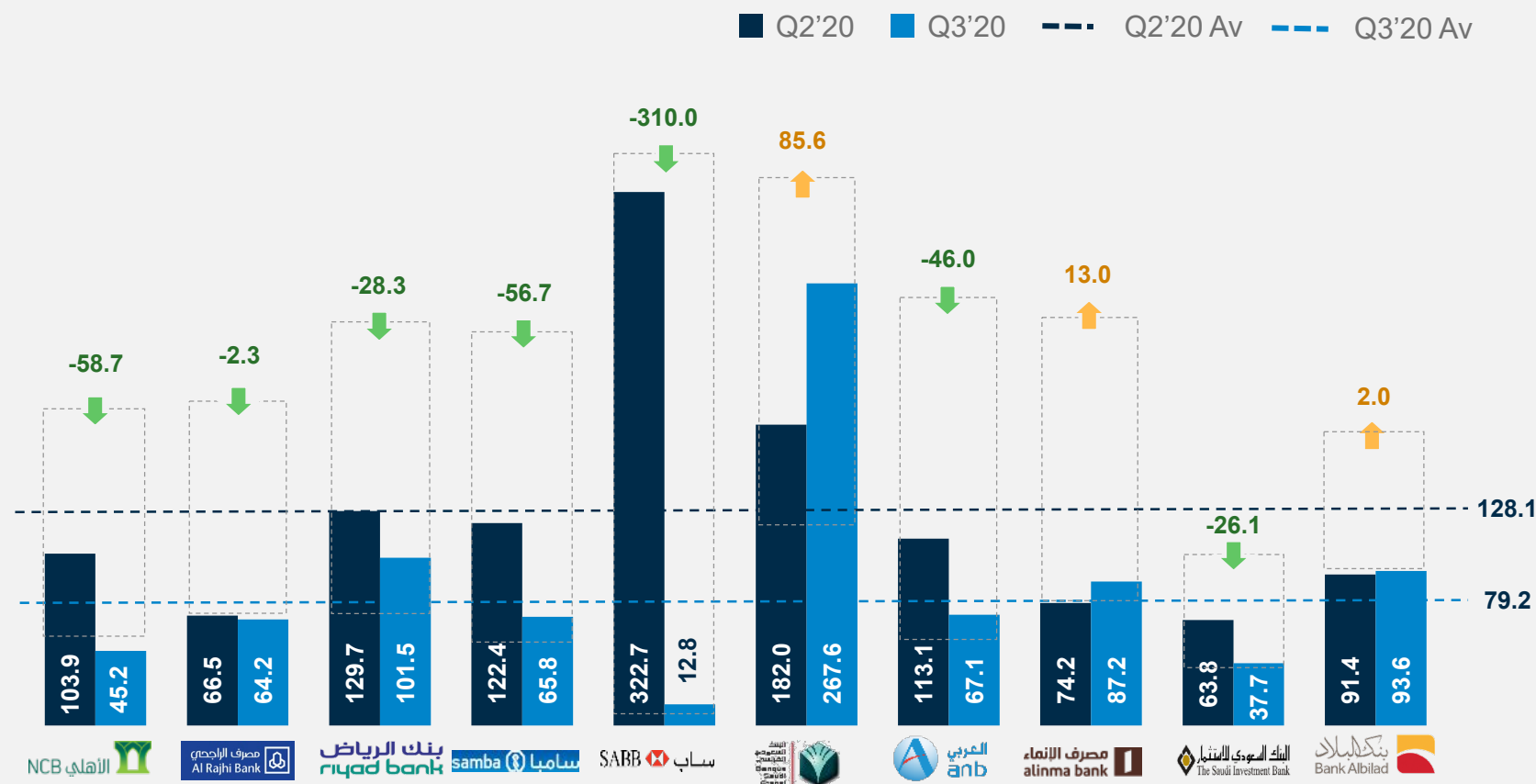
- Cost of Risk decreased 49 bps QoQ to 0.79% in Q3'20, due to decrease in provisioning (primarily on account of SABB's provisions)
- Total provisioning decreased by 36.7% QoQ to SAR 3.2bn in Q3'20, continuing its volatile trend
- Gross L&A increased at a higher pace (+3.0% QoQ), compared to Q2'20

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

SABB Reported Highest Decrease in Cost of Risk

→ Improved ← Stable → Worsened

Cost of Risk (bps) – Net of Reversals



KEY TAKEAWAYS

- SABB reported the highest decline in cost of risk (-310.0 bps QoQ), as the bank had reported a strong increase in provisioning in Q2'20
- Similarly, NCB (-58.7 bps QoQ) and SAMBA (-56.7 bps QoQ) also reported an improvement in their cost of risks
- BSF reported the highest increase in cost of risk (+85.6 bps QoQ), largely on the back of increased provisioning in the commercial portfolio

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

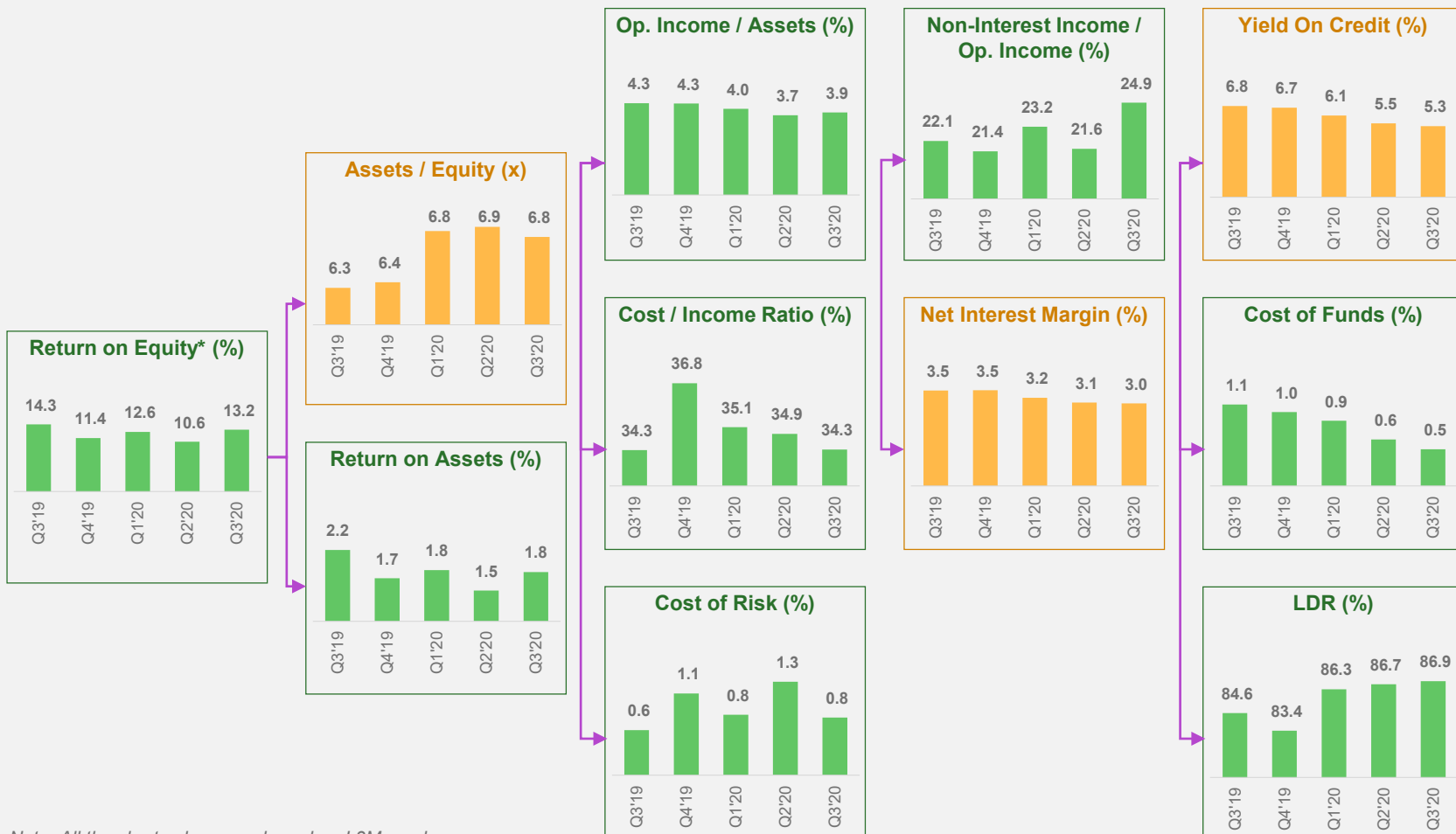
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- Combined RoE increased from 10.6% in Q2'20 to 13.2% in Q3'20
- RoE for all banks increased except for BSF
- BSF's RoE decreased 4.0% in Q3'20, compared to 5.2% in Q2'20, as the bank's net income fell ~24% QoQ
- NCB reported the highest RoE at 22.5%

KSA Banking Sector: Bearish Macroeconomic Outlook Could Impact Profitability

■ 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

- Aggregate RoE rose to 13.2% to reach its highest level since Q3'19
 - Profitability was supported by increased operating income (+6.5% QoQ) and reduced provisioning (-36.7% QoQ)
- While there has been an improvement in profitability, the near term outlook for domestic banks remains bearish
- The Saudi government is set to cut budget spending by 7.5% in 2021, which could have a spill-over effect in other sections of economy
- Interest rates are likely to remain at current record low levels, which could limit NII growth
- However, strong capitalization levels would provide some cushion against any material deterioration of the fundamental profile of banks

GCC Banking Consolidation

GCC list of M&A transactions in banking sector since January 2019

Announcement Date	Target Company	Target Country	Acquirer Company	% Sought	Consideration (SAR Mn)	Deal Status*
16-Sep-20	Ahli United Bank Egypt SAE	Egypt	Ahli United Bank BSC	14.4%	304	Pending
30-Jun-20	Al Khaliq Commercial Bank PQSC	Qatar	Masraf Al Rayan QSC	100%	4,492	Pending
25-Jun-20	Samba Financial Group SJSC	Saudi Arabia	National Commercial Bank SJSC	100%	58,397	Pending
31-Dec-19	Alizz Islamic Bank SAOG	Oman	Oman Arab Bank SAOC	81%	NA	Pending
12-Sep-19	Ahli United Bank BSC	Bahrain	Kuwait Finance House KSCP	100%	21,860	Pending
15-Aug-19	Cqur Bank LLC	Qatar	VTB Bank PJSC	19%	NA	Completed
08-Aug-19	DenizBank AS	Turkey	Emirates NBD PJSC	0.20%	NA	Completed
20-Jun-19	Warba Bank KSCP	Kuwait	Kuwait & Middle East Financial Investment Co KSCP	75.70%	NA	Proposed
12-May-19	Gulf Bank KSCP	Kuwait	Alghanim Industries Ltd	16%	NA	Completed
21-Apr-19	HSBC Saudi Arabia Ltd	Saudi Arabia	HSBC Holdings PLC	2%	31	Completed
10-Apr-19	Invest bank PSC	UAE	Emirate of Sharjah United Arab Emirates	50%	1,009	Completed
07-Apr-19	Noor Bank PJSC	UAE	Dubai Islamic Bank PJSC	100%	NA	Completed
03-Apr-19	Oman United Exchange Co	Oman	Private Investor	25%	NA	Completed
15-Mar-19	Banque Saudi Fransi	Saudi Arabia	Olayan Investments, Ripplewood Advisors LLC	5%	1,641	Completed
29-Jan-19	Union National Bank PJSC	UAE	Abu Dhabi Commercial Bank PJSC	100%	11,762	Completed
29-Jan-19	Al-Hilal Bank PJSC	UAE	Abu Dhabi Commercial Bank PJSC	100%	NA	Completed

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	577.1	NCB	NCB الأهلي 
Al Rajhi Bank	430.3	ALRAJHI	مصرف الراجحي Al Rajhi Bank 
Riyad Bank	308.6	RIBL	بنك الرياض riyad bank 
Samba Financial Group	289.6	SAMBA	samba سامبا 
Saudi British Bank	264.0	SABB	SABB ساب 
Banque Saudi Fransi	197.4	BSF	البنك السعودي الفرنسي Banque Saudi Fransi 
Arab National Bank	188.5	ANB	العربي anb 
Alinma Bank	147.8	ALINMA	مصرف الإنماء alinma bank 
Saudi Investment Bank	98.3	SIB	البنك السعودي للاستثمار The Saudi Investment Bank 
Bank Albilad	92.3	BALB	بنك البلاد Bank Albilad 

Note: Banks are sorted by assets size
* As on 30th September 2020