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# UAE Banking Pulse

## Quarter 1, 2020

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الإمارات  
THE EMIRATES

# FOREWORD

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Alvarez & Marsal Middle East Limited (A&M) is delighted to publish the Q1'20 edition of the UAE Banking Pulse ("The Pulse"). In this quarterly series, we share results from our research examining the top ten largest listed UAE banks by assets, and highlight key performance indicators of the UAE 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 has been changed from the previous version to accommodate available information.

In light of the COVID-19 pandemic, the macroeconomic events are impacting the industry in a significant manner. The decline in US Fed rates and various stimulus measures announced have made some of the macroeconomic analysis less impactful. However, the information on the UAE banking space remains relevant.

The UAE Central Bank has announced several measures to reduce the impact of COVID-19 on the domestic economy. It has decreased the lending rates to 0.75% and is offering interest free loans worth upto AED 50bn to banks, as a relief measure for providing liquidity to individuals and SMEs.

The central bank has also extended the capital buffer reliefs for the banks, which would inject additional liquidity into the system. Profitability of the top UAE banks in Q1'20 has showed signs of weakness, with declining interest income and increased provisioning weighing on the net profit. Consequently, RoE has touched multi-period low levels.

All these recent performance hence may not be entirely comparable with that of the previous quarters, but it is expected to impact the results in the coming quarters as well.

We hope that you will find the 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

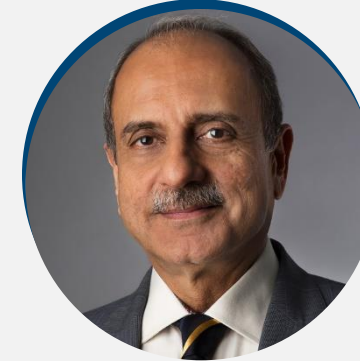
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**Dr. Saeeda Jaffar**

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**

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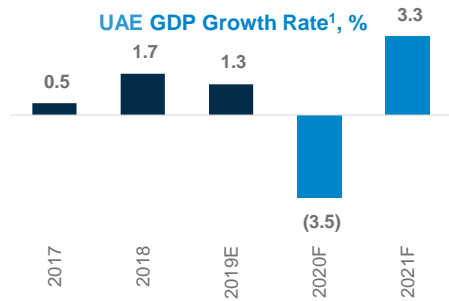
- 30+ years of experience in banking
- Focuses on performance improvement, turn-around, credit management, and formulating and managing strategic and operational changes in financial institutions
- Former CEO of banks in the UAE & Kenya

**CONTACT  
DETAILS**

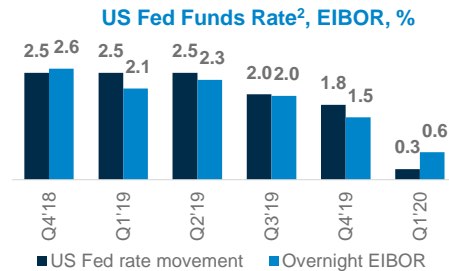
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# UAE Macro & Sector Overview

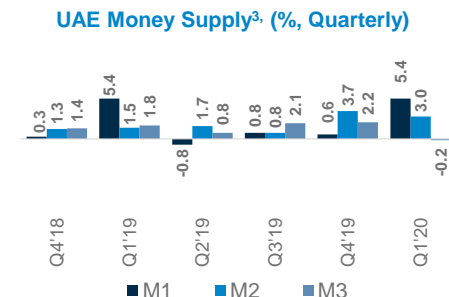
## Macro overview



- *The IMF expects the UAE's economic growth to decline by about 3.5% in FY'20*, before rebounding (+3.3%) in FY'21
- Economic headwinds on account of COVID-19, low oil prices and the delay in Expo 2020 are the key factors for the lower growth in FY'20
- The average Q1'20 Emirates NBD Purchasing Managers' Index (PMI) has declined to a multi-period low of 47.9, largely on account of a drop in new business volumes



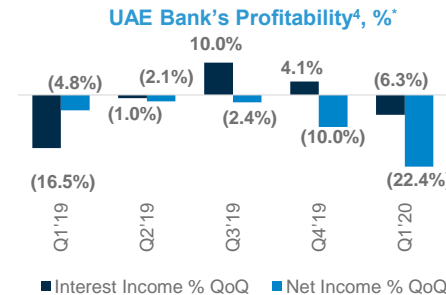
- *In Mar'20, the US Fed cut its interest rates to near 0% and started an USD 700bn quantitative easing program*, to stabilize the economy from the COVID-19 headwinds
- In line with the trends in US Fed fund rates, overnight EIBOR witnessed a sharp decline, after the UAE's central bank reduced its interest rates in Q1'20
- Interest rates are **expected to remain at current levels as most central banks would ensure to stabilize the economy from the effects of the ongoing pandemic**



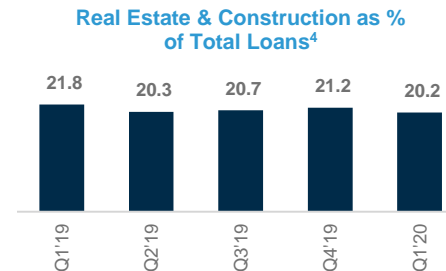
- M2 money supply grew 3.0% QoQ and 9.5% YoY in Q1'20
- The growth was mainly due to the **increase in non-government resident deposits by 2.5% QoQ to AED 1,368.7bn**
- M1 increased by 5.4% QoQ in Q1'20. On an annual basis, M1 increased by 6.0% to AED 542.7bn
- M3 fell 0.2% QoQ, but increased 5.0% YoY to reach AED 1,714.1bn

<sup>1</sup> IMF, <sup>2</sup> US Board of Federal Reserve, <sup>3</sup> UAE Central Bank, <sup>4</sup> Company filings, ENBD net income adjusted for one time gain of AED 4.4bn from disposal of stake in jointly controlled entity during 2019, <sup>5</sup> Bloomberg & A&M Analysis, <sup>6</sup> based on data of 8 banks; \* Data for top ten UAE banks by asset size as of March 31<sup>st</sup> 2020

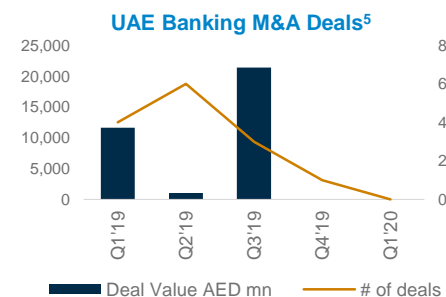
## Banking overview Q1'20



- The top ten UAE banks **reported a combined 6.3% QoQ drop in the interest income largely due to the low interest rate environment**
- Net profit declined by about 22%, on account of 3.6% drop in **operating income and 35.0% increase in provisioning**
- Subdued economic activities would likely keep profitability under pressure. However, central bank's stimulus measures can provide some support in the near to medium term



- **The UAE banks exposure to the real estate sector reduced by ~100 bps<sup>6</sup>**, after rising in the earlier quarter
- Real estate market in the UAE is likely to remain under pressure in the near term, on account of slowdown in the economy and persistent oversupply conditions
- The Central Bank has provided some relaxations for lending activity in the sector, subject to conditions that banks should hold additional capital



- No deals materialized during Q1'20. In contrast, in FY'19 about 14 M&A deals took place in the UAE. Total value of the reported deals stood at AED 34.1bn
- Rising competition along with a increased focus towards digitization would likely drive consolidation wave in domestic banking sector

# Pulse: Low Interest Rate Environment and Sluggish Economic Conditions Weighed on Profitability and Return Metrics

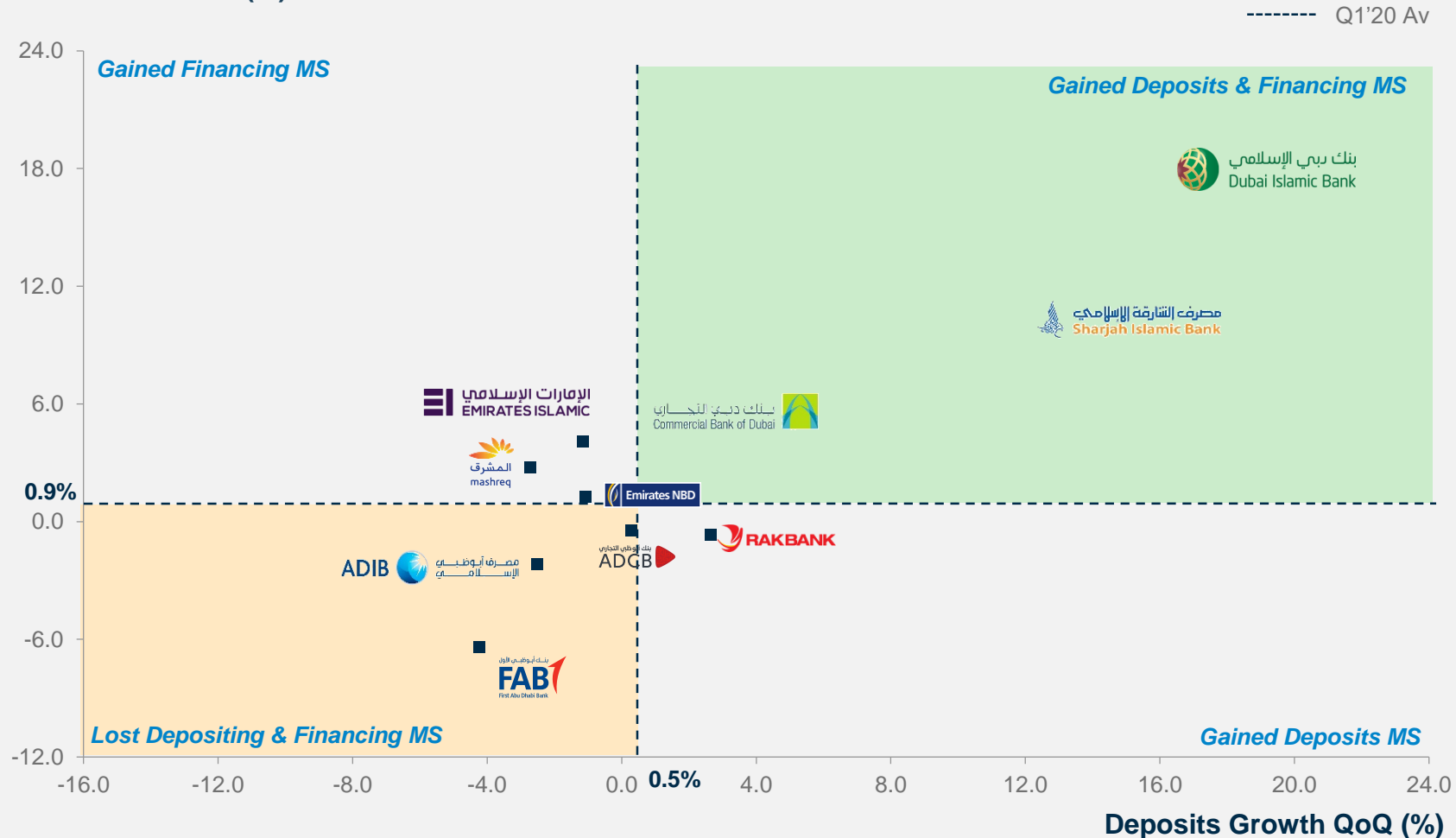
➔ Improved  
 ↔ Stable  
 ➔ Worsened

	Metric	Q4'19	Q1'20	Q1'19	Q2'19	Q3'19	Q4'19	Q1'20	Key Trends of Q1'20
<b>Size</b>	Loans and Advances (L&A) Growth (QoQ)	3.0%	0.9%						1 The growth in L&A and Deposits slowed to 0.9% and 0.5% respectively, amid tight market conditions
	Deposits Growth (QoQ)	3.5%	0.5%						
<b>Liquidity</b>	Loan-to-Deposit Ratio (LDR)	87.4%	87.8%						2 LDR ratio increased to 87.8% as banks witnessed faster increase in L&A compared to deposits
<b>Income &amp; Operating Efficiency</b>	Operating Income Growth (QoQ)	6.5%	-3.6%						3 Operating income declined in Q1'20 after rising for two consecutive quarters, on account of decline in major income streams
	Operating Income / Assets	3.6%	3.4%						
	Non-Interest Income(NII) / Operating Income	29.9%	29.5%						
	Yield on Credit (YoC)	7.3%	6.7%						4 NIM declined by 0.2% on the back of a series of rate cuts by the central bank
	Cost of Funds (CoF)	2.2%	1.9%						
	Net Interest Margin (NIM)	2.7%	2.5%						5 Decline in operating expenses (-7%) helped in improvement of C/I ratio by 1.1% points
	Cost-to-Income Ratio (C/I)	35.1%	34.0%						6 CoR increased as banks took increased provisioning, on account of challenging operating environment
<b>Risk</b>	Coverage Ratio	100.5%	97.0%						7 The RoE and RoA continued to decline in Q1'20, on the back of decline in income (-4%) and higher provisioning (+35%)
	Cost of Risk (CoR)	1.4%	1.8%						
<b>Profitability</b>	Return on Equity (RoE)	11.6%	9.0%						8 RoRWA also declined further in Q1'20, as RWA increased in line with total assets. The capital adequacy ratio declined after increasing in the preceding quarter
	Return on Assets (RoA)	1.5%	1.1%						
	Return on Risk-Weighted Assets (RoRWA)	2.1%	1.6%						
<b>Capital</b>	Capital Adequacy Ratio (CAR)	17.3%	16.1%						

Note 1: QoQ stand for quarter over quarter  
 Note 2: Growth in loans & advances and deposits were presented QoQ instead of YoY  
 Note 3: Quarterly income was used in the calculation of operating income growth  
 Source: Financial statements, Investor presentations, A&M analysis

# DIB and SIB Reported Double-Digit L&A and Deposit Growth, While FAB's L&A and Deposits Decreased

L&A Growth QoQ (%)



## KEY TAKEAWAYS

- Banks' L&A (+0.9%) and deposit (+0.5%) growth was the slowest in the past four quarters
- DIB reported highest growth in L&A and deposits by 19.4% and 21.6%, respectively, as a result of its merger with Noor Bank
- SIB reported the second highest growth in L&A and deposits of 12.2% and 15.3%, respectively
- FAB underperformed in terms of L&A (-6.4%) and deposit (-4.2%) growth. The bank's L&A fell, due to a repayment of a large short-term credit line. Deposits had decreased on account of outflows of government deposits (-31.0%<sup>1</sup> QoQ)

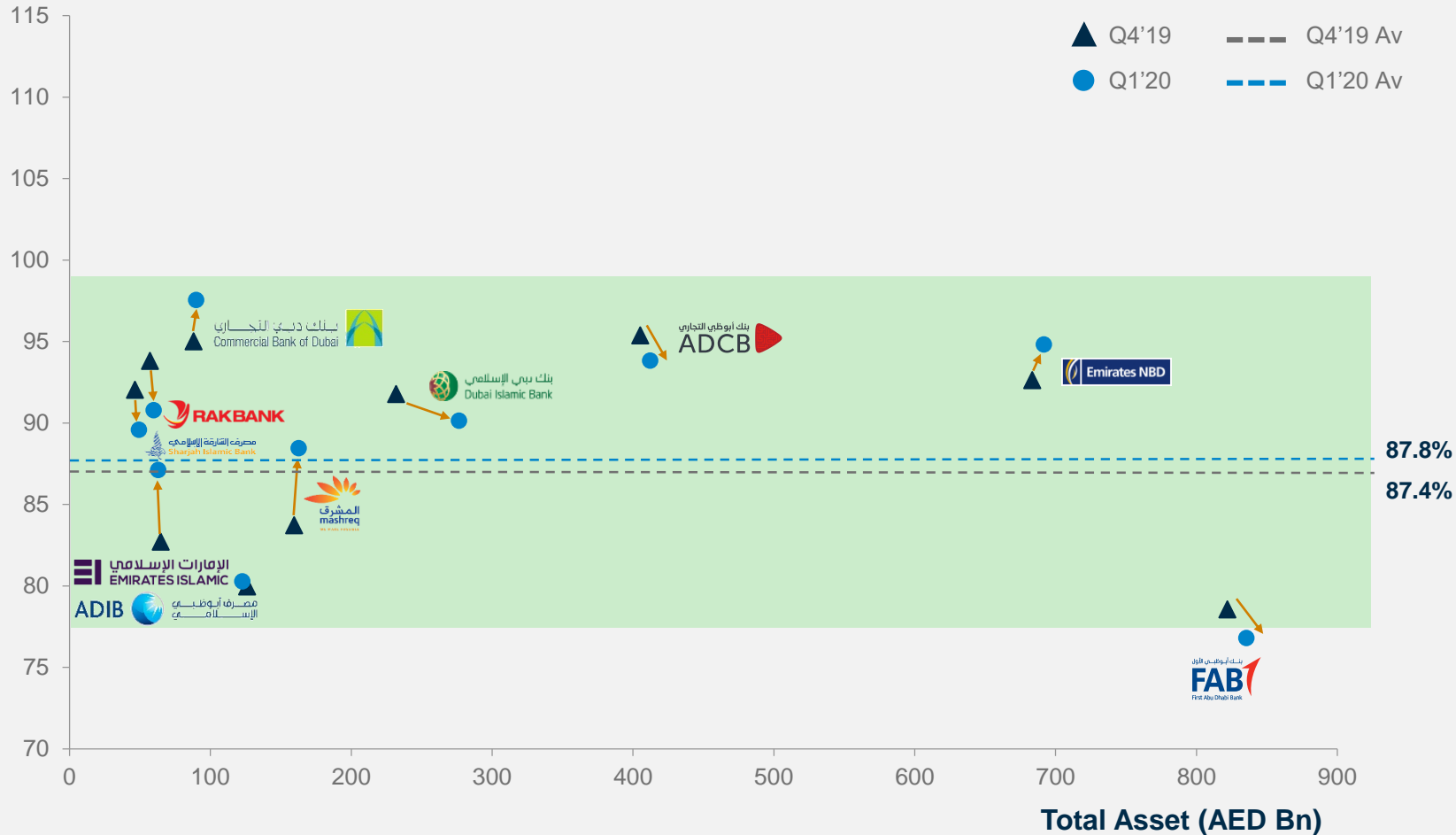
Note: MS stands for market share

Source: Financial statements, Investor presentations, A&M analysis, <sup>1</sup> net outflow based on Q1'20 and Q4'19 data



# MSQ and EIB Reported the Largest Increase in LDR in Q1'20

Loans to Deposits Ratio (%)



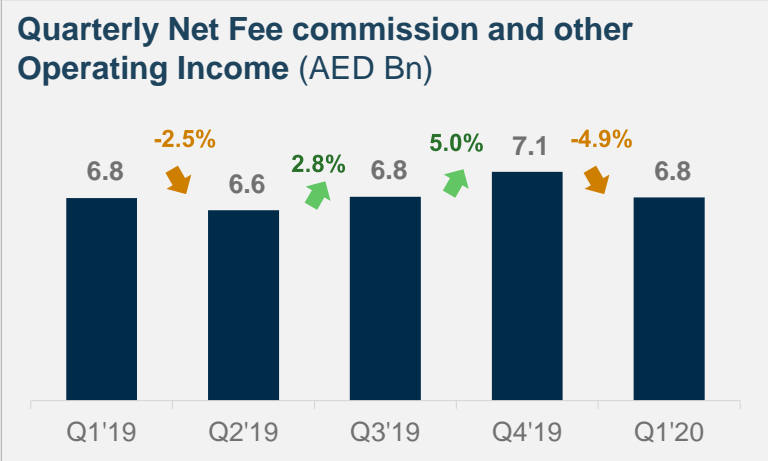
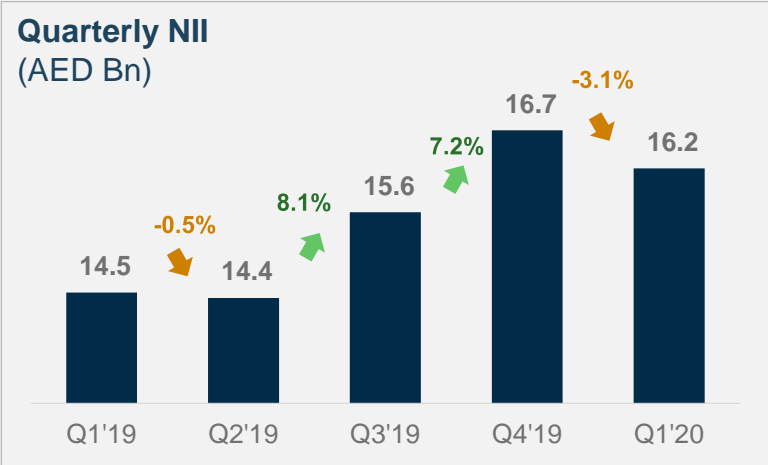
## KEY TAKEAWAYS

- LDR marginally increased to 87.8% during Q1'20 from 87.4% in Q4'19
- ENBD, MSQ, CBD and EIB reported sequential increase in LDR (more than 1.5% points), while the same for FAB, DIB, SIB and RAK fell at a similar pace
- MSQ (+4.7% points) and EIB (+4.4% points) reported the highest increase, as their L&A (MSQ: +2.8%, EIB: +4.1%) increased, while deposits declined (MSQ: -2.7%, EIB: -1.2%)
- RAK, on other hand, reported the highest decline of 3.0% points in LDR, as the bank's deposits increased (+2.6%), while L&A fell (-0.7%)

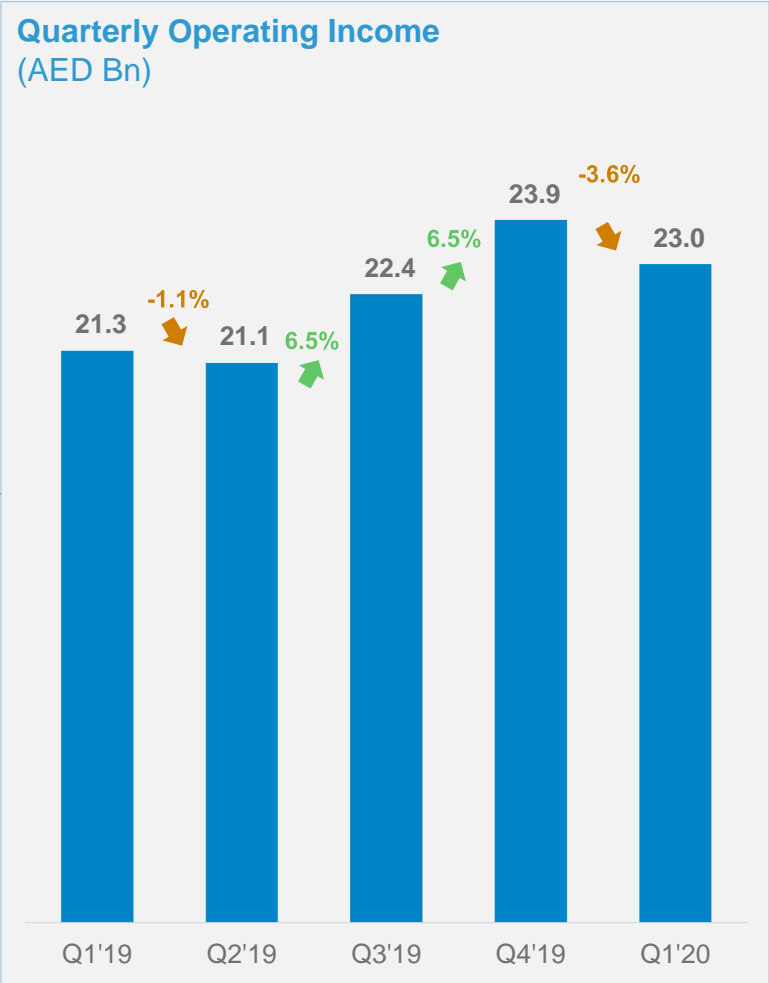
Note: The green zone is an area of healthy liquidity  
Source: Financial statements, A&M analysis

# Operating Income Declined After Increasing for Two Consecutive Quarters

➔ Improved    ↔ Stable    ➔ Worsened



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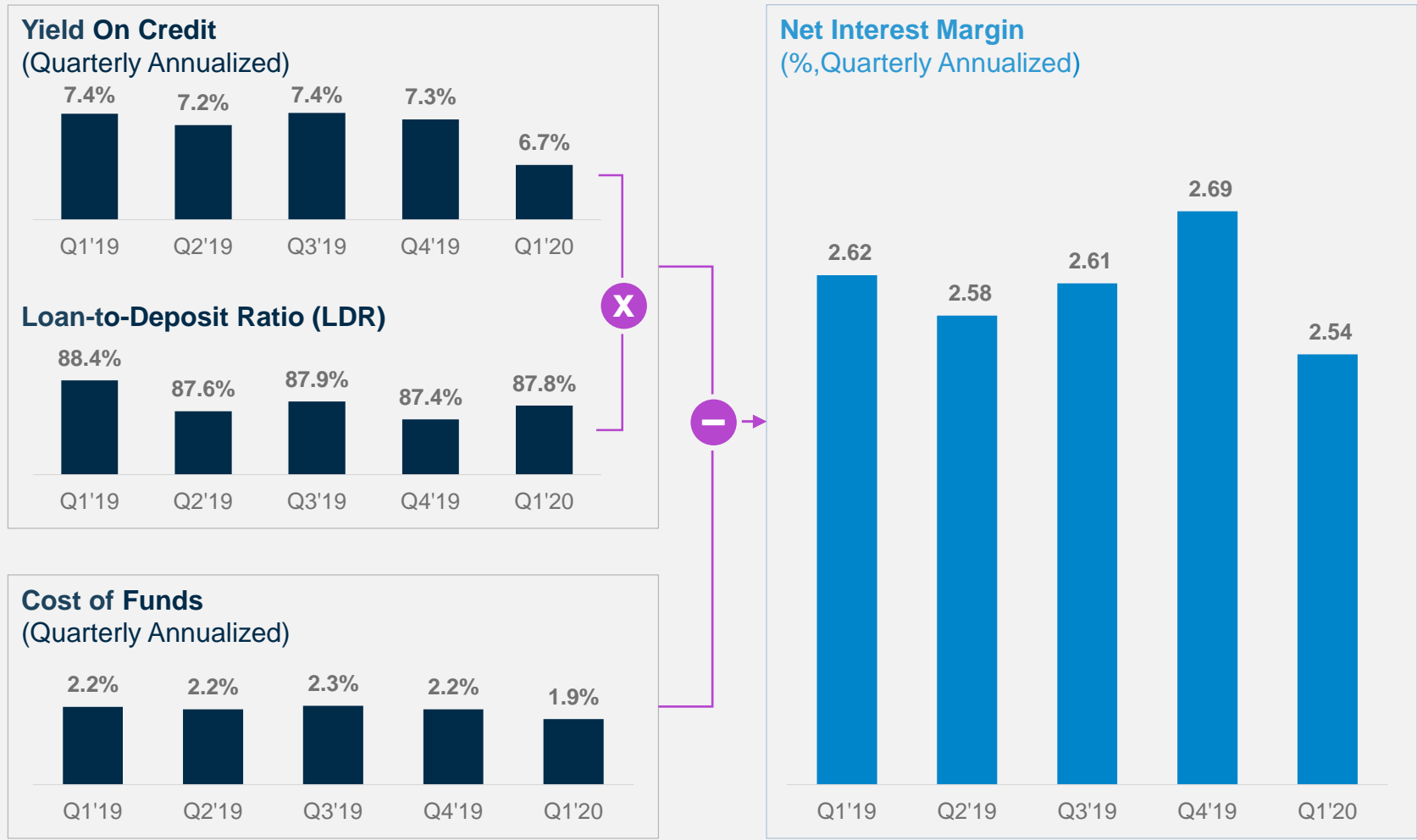
## KEY TAKEAWAYS

- Operating income declined by 3.6% QoQ, amid a 3.1% and 4.9% decline in net interest income and non-interest income, respectively
- Non-interest income fell, as net fees and commission income in ADCB declined by ~16%, while FAB's other operating income declined by 47.4%
- ADIB reported the sharpest decline (-15%) in operating income, on the back of a sharp drop (-37%) in net fees and commission income
- MSQ, EIB and RAK reported an increase in their operating income, as strong increase in fees and other operating income helped in offsetting a decline in net interest income

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



# NIM Witnessed Sizeable Contraction, as Cost of Funds Fell at a Slower Pace Compared to Yield on Credit



## KEY TAKEAWAYS

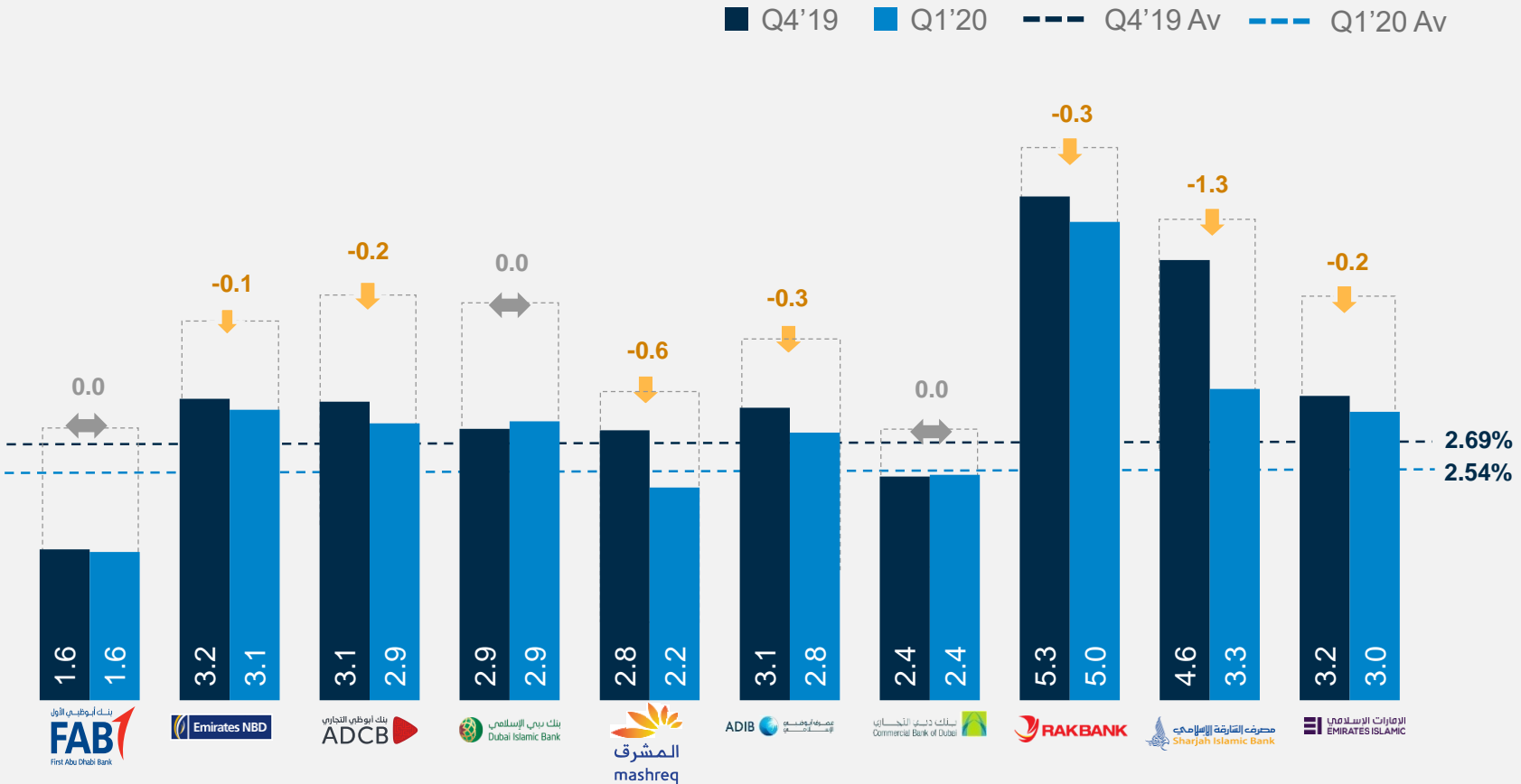
- NIM declined by ~15.0 bps during Q1'20 to 2.5% compared to 2.7% in Q4'19
- The decrease in NIM was largely on account of a 59.0 bps decline in yield on credit, partially offset by a 28.0 bps decline in cost of funds

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

# NIM Fell for Most of the Banks

➔ Improved   ➔ Stable   ➔ Worsened

## Net Interest Margin (% Quarterly)



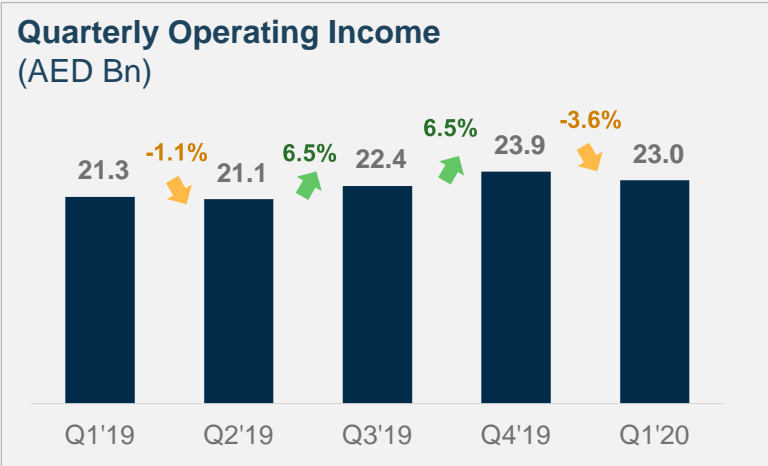
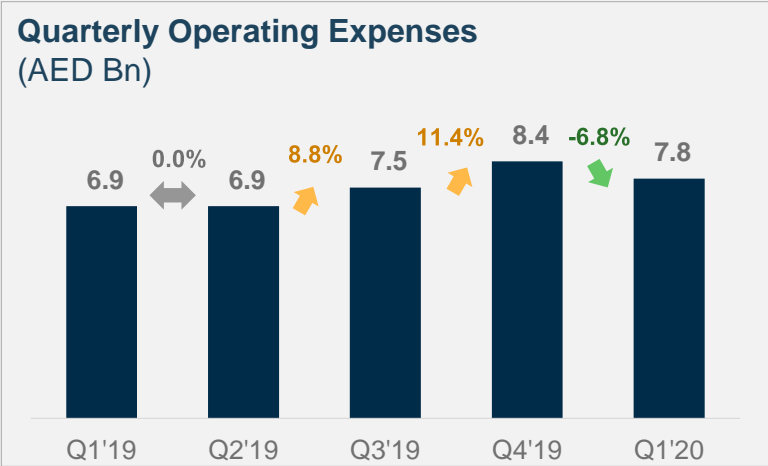
### KEY TAKEAWAYS

- Seven of the top ten banks reported a decline in NIM during Q1'20
- SIB (~130 bps), MSQ (~60 bps) and RAK (~30 bps), reported the fastest decline in NIM
- FAB, DIB and CBD had their NIM almost flat compared to the preceding quarter

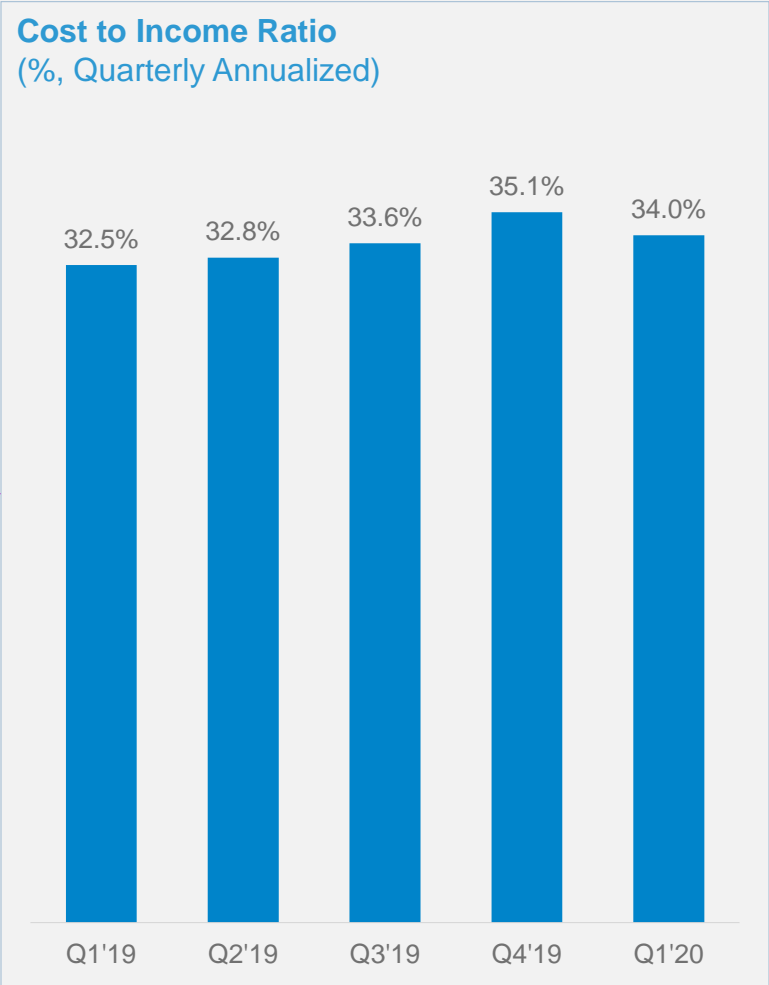
Note: Some numbers might not add up due to rounding  
Source: Financial statements, investor presentations, A&M analysis

# Cost Optimization Measures Supported C/I Ratio

➔ Improved    ↔ Stable    ➔ Worsened



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## KEY TAKEAWAYS

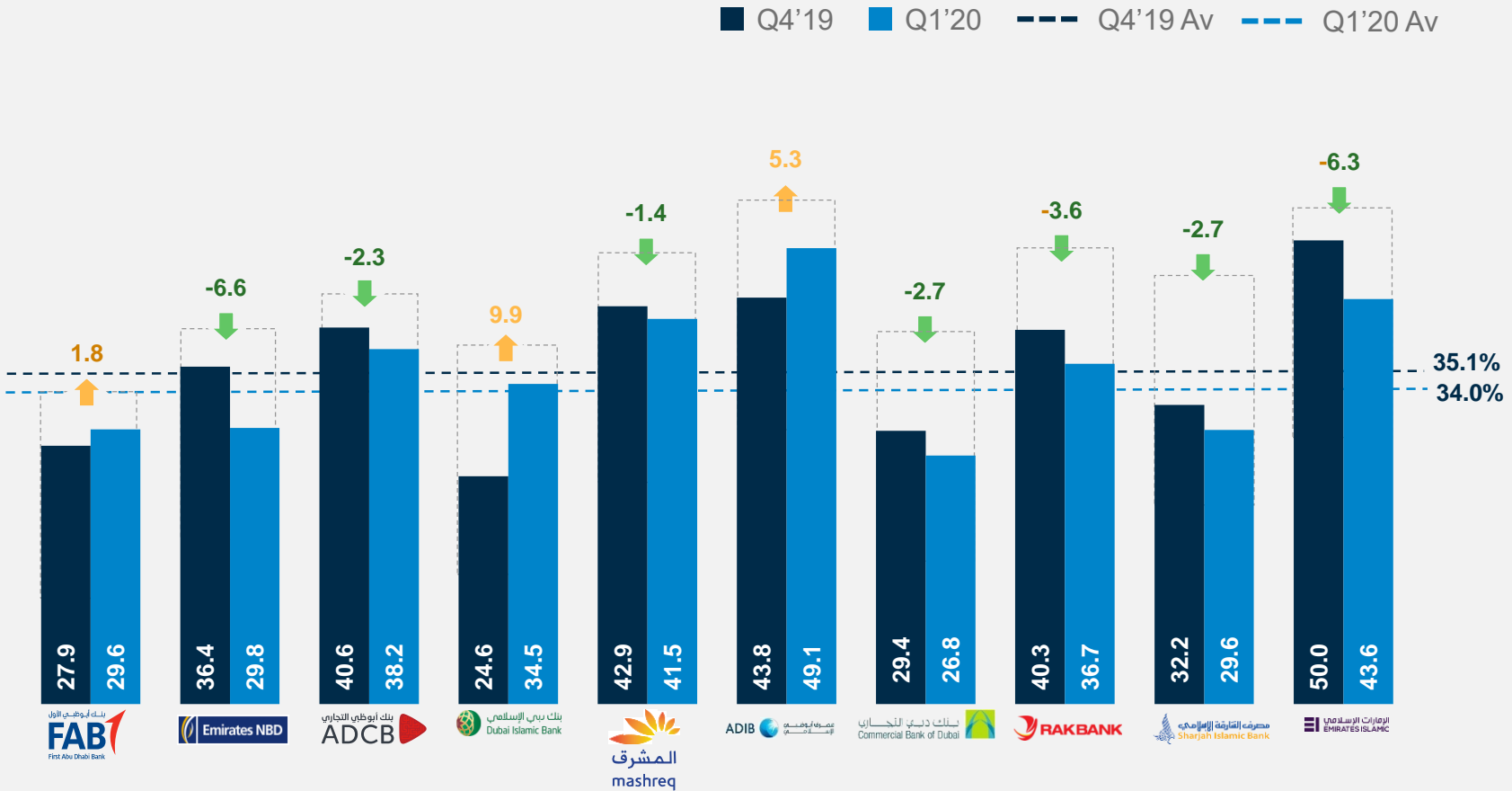
- During Q1'20, C/I ratio improved by ~110 bps, after rising for the previous quarters
- The lower C/I ratio was reported due to decline in SG&A expenses by 6.8%
- The decline in SG&A expenses was largely on the back of cost-cutting measures adopted by the banks, as eight of the ten banks reduced their expenses

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

# ENBD and EIB Reported the Largest Decrease in C/I Ratio

➔ Improved   ➔ Stable   ➔ Worsened

## Cost to Income Ratio (% , Quarterly)



### KEY TAKEAWAYS

- C/I ratio improved for most of the banks except FAB, DIB and ADIB
- The sharpest improvement was seen for ENBD and EIB, of 6.6% points and 6.3% points respectively
- FAB, DIB and ADIB reported an increase in the ratio by 1.8% points, 9.9% points and 5.3% points, respectively
- DIB's C/I ratio increased substantially, as the bank is yet to realize the cost synergies from the acquisition of Noor Bank

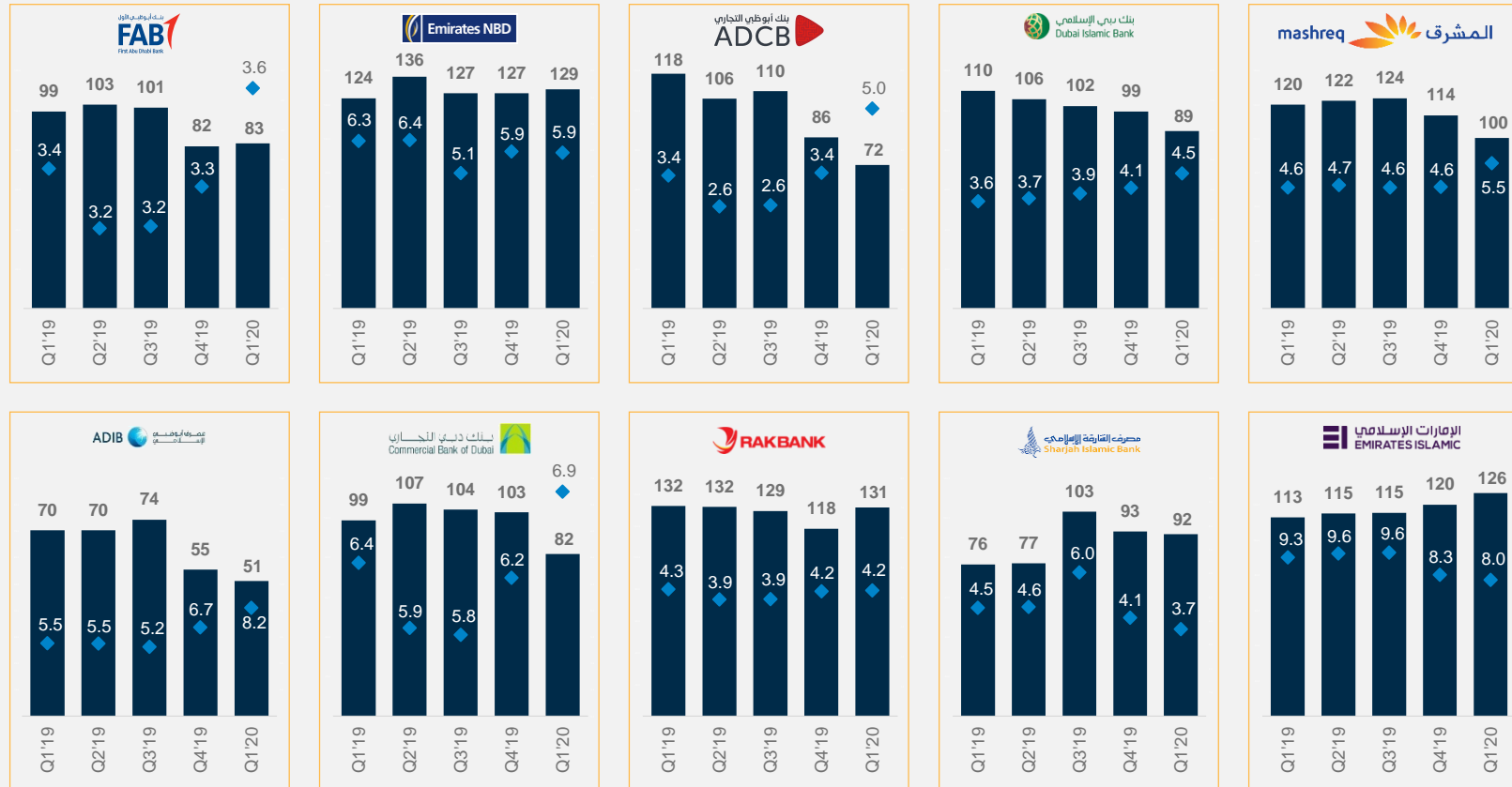
Note: Scaling and some numbers might not add up due to rounding  
 Source: Financial statements, investor presentations, A&M analysis  
 \*Comparison on QoQ basis



# Coverage and NPL/Net Loan Ratio Deteriorated Substantially in Q1'20

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

## Coverage Ratio<sup>1</sup> and NPL / Net Loans Ratio (% , Quarterly)



## KEY TAKEAWAYS

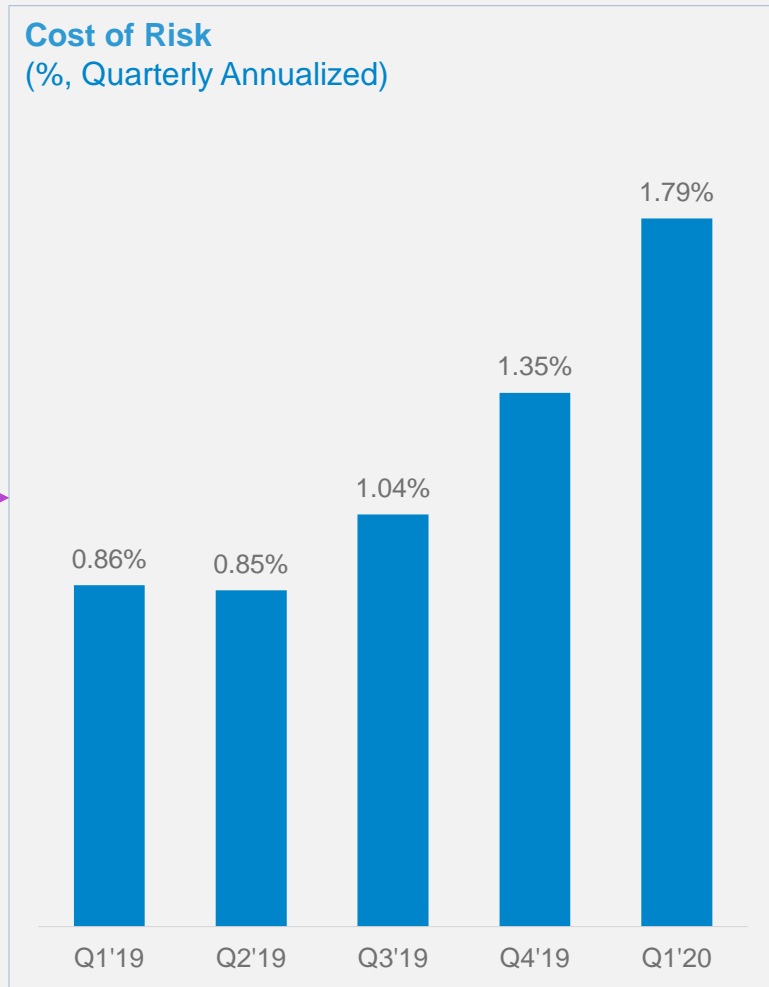
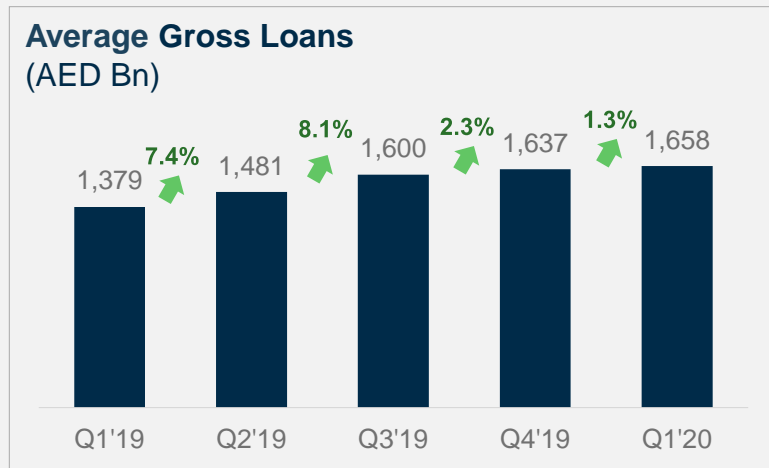
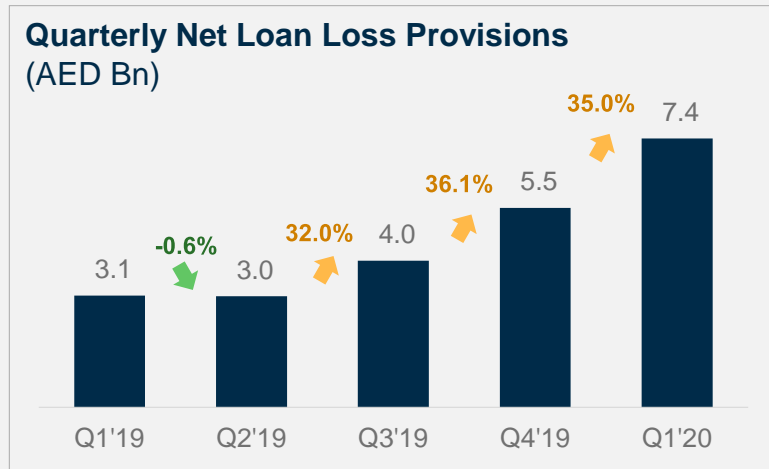
- Coverage and NPL / net loan ratios for six of the ten banks witnessed deterioration in Q1'20
- Overall, the coverage ratio fell to 95.8% (from 99.1%) while NPL / net loan ratio increased to 5.2% (from 4.6%)
- CBD reported the highest decline in coverage ratio (-20.9% points), while ADCB witnessed the highest increase in NPL / Net loans ratio (+1.6% points)
- On the other hand, RAK reported the largest increase in coverage ratio (+13.4% points), while SIB showed the highest decrease in NPL / net loan ratio (-0.5% points)

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

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

# 5 Cost of Risk Increased due to Increase in Net Loan Loss Provisions

➔ Improved  
 ↔ Stable  
 ➔ Worsened



## KEY TAKEAWAYS

- CoR continued to rise for the third consecutive quarter, amid strong increase in loan loss provisions
- ADCB's and ADIB's loan loss provisions more than doubled during the period
- Exposure of the banks towards NMC Health could be the possible reason behind increased provisioning. The UAE banks have an exposure of about USD 2.2bn towards NMC

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

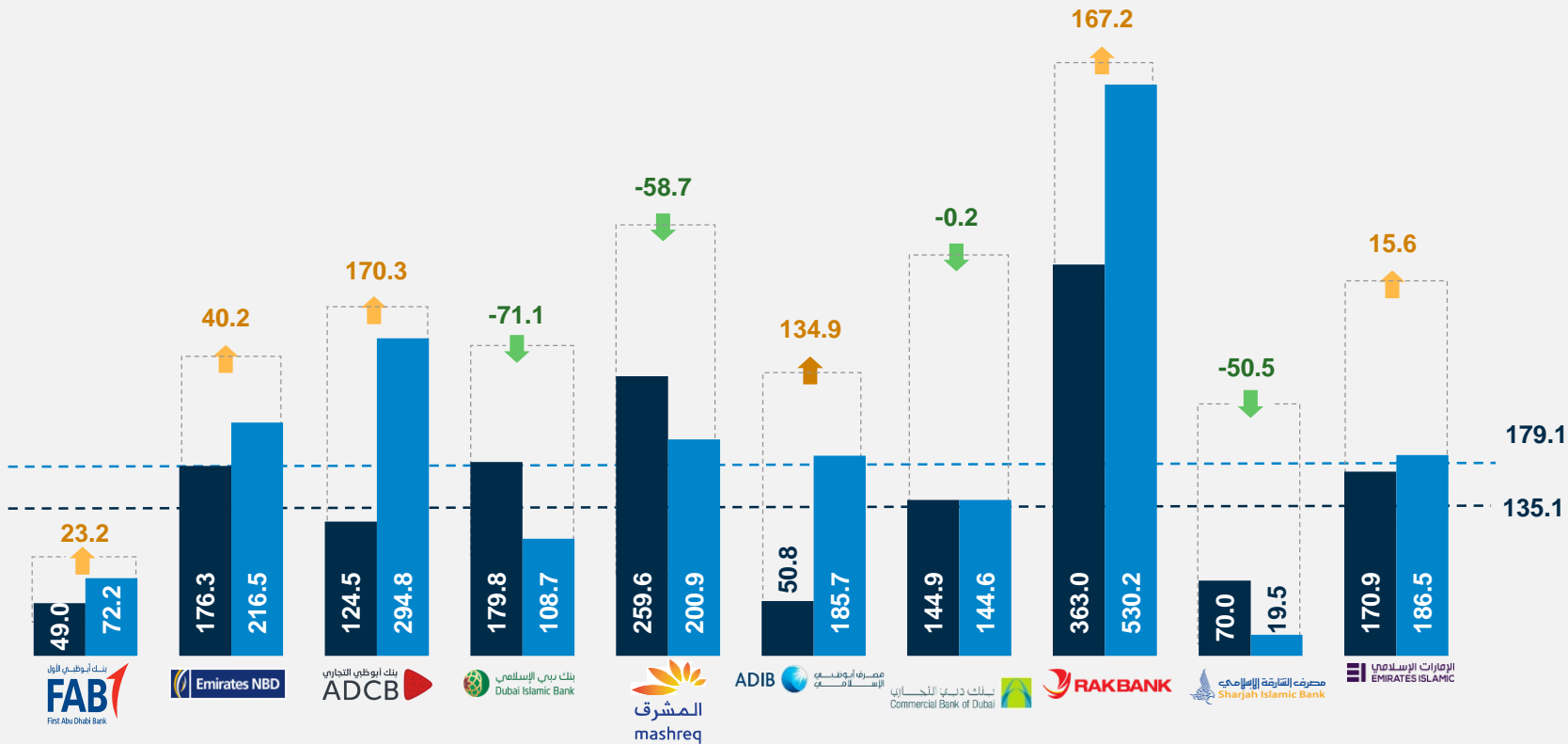


# Cost of Risk Increased Sharply on Account of Challenging Economic Conditions

→ Improved   ← Stable   → Worsened

## Cost of Risk (bps) – Net of Reversals

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



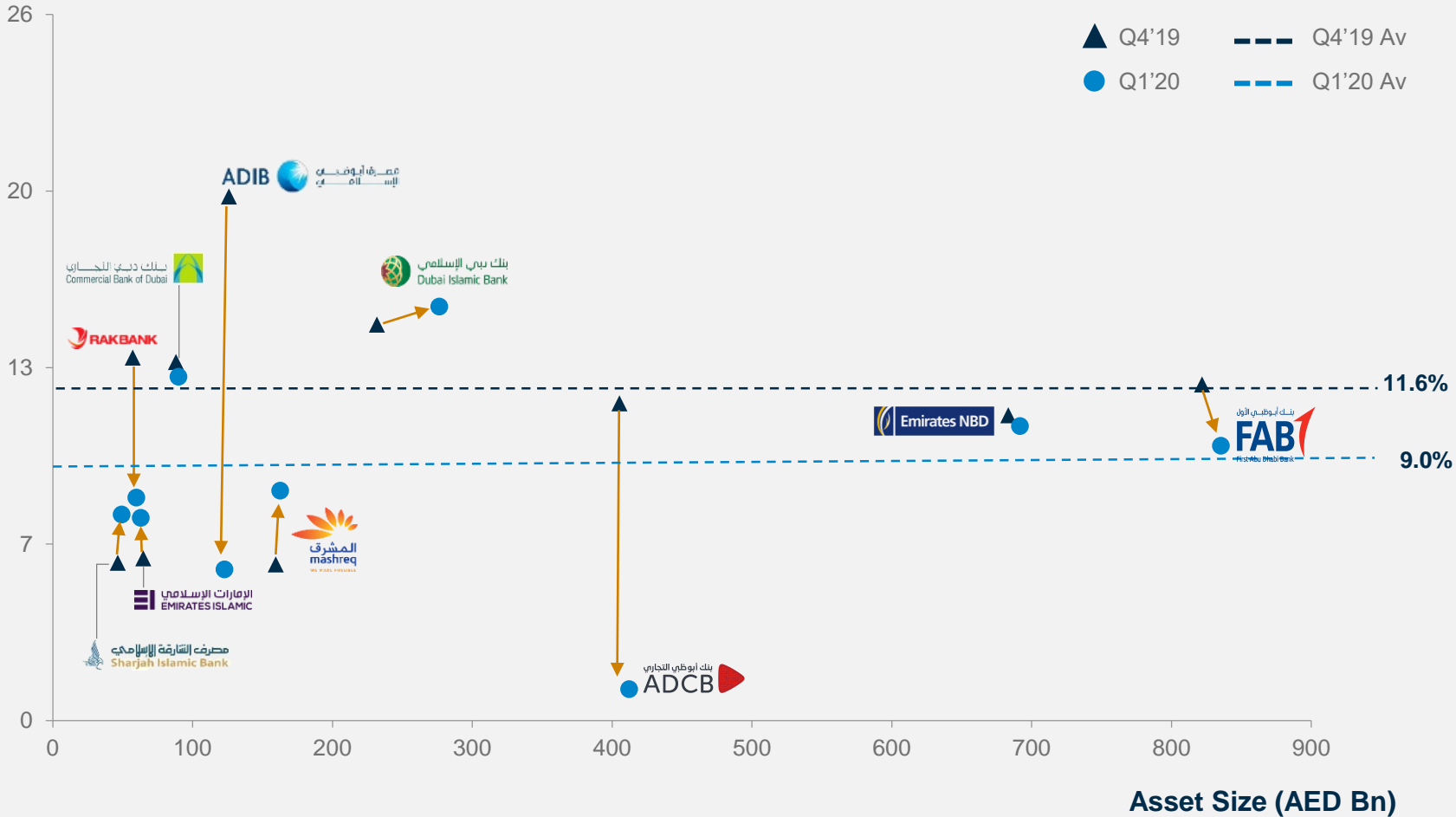
## KEY TAKEAWAYS

- ADCB and RAK reported the highest increase in cost of risk at 170.3 bps and 167.2 bps, respectively
- DIB's, MASQ's and SIB's cost of risk, on the other hand, declined by about 71 bps, 59 bps and 51 bps, respectively

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

# RoE Continued to Decline in Q1'20

## Return on Equity (%)



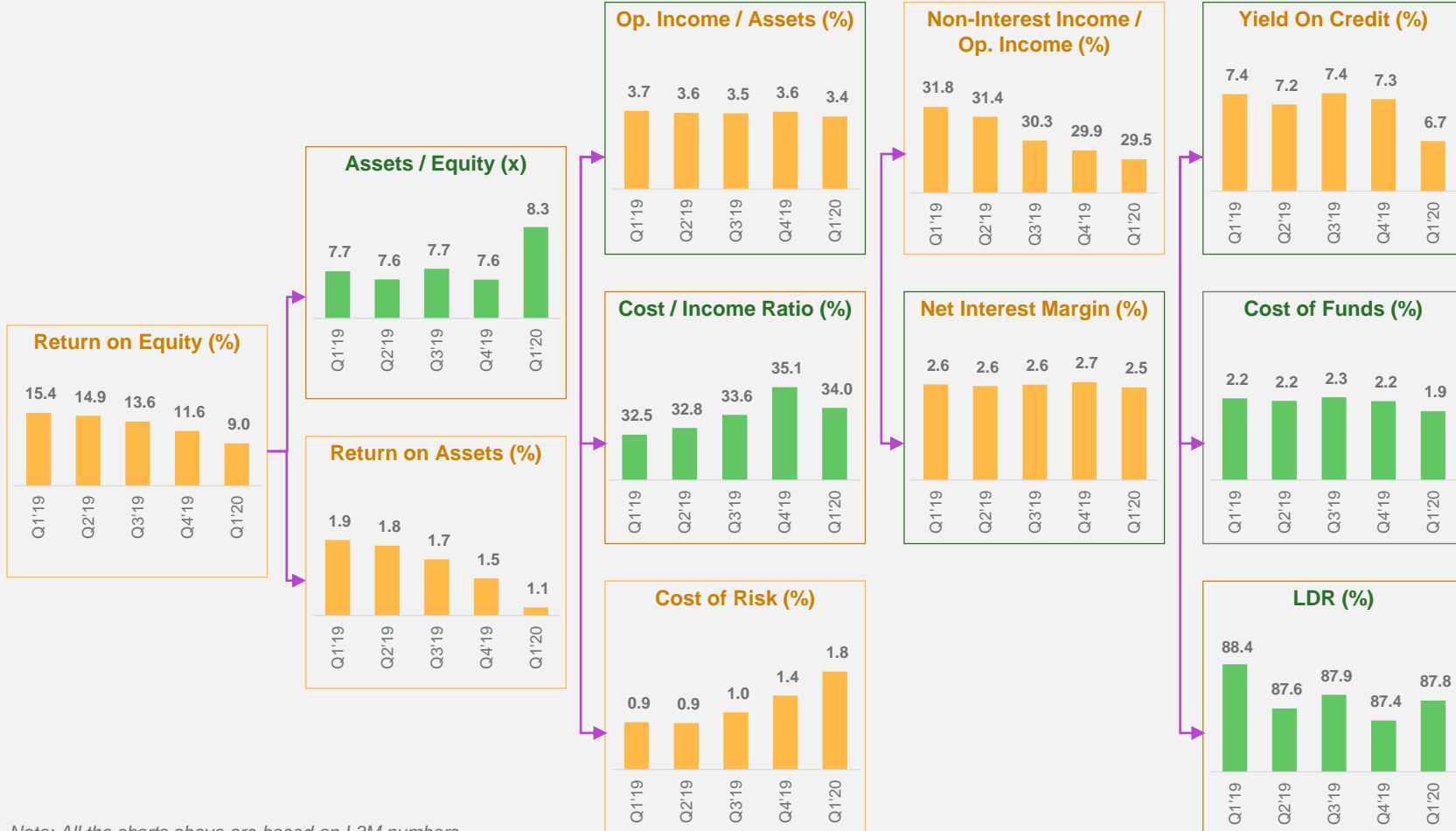
## KEY TAKEAWAYS

- Average RoE for the universe declined to 9.0% during Q1'20, compared to 11.6% during Q4'19
- RoE was impacted by the reduced operating income due to a series of rate cuts and increased provisioning
- ADCB and ADIB reported the largest decline in RoE, while EIB, SIB, MSQ and DIB showed improvement

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

# UAE Banks' Profitability Decreased; Anticipating Additional Decline in Coming Period

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 declined to 9.0%, on account of increased provisioning and lower operating income due to reduced interest rates
- The UAE's banking sector would likely face headwinds in FY'20, due to the consequences of COVID-19 pandemic
  - Additional oil production cuts and the delay in Expo 2020 could lead to subdued economic activity
  - Low interest environment along with economic slowdown would likely weigh on profitability over the near to medium term
  - However, banks' robust capitalization levels would act as a strong buffer in withstanding the headwinds

# 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 (AED Mn)	Deal Status*
29-Jan-19	Union National Bank PJSC	UAE	Abu Dhabi Commercial Bank PJSC	100%	11,531	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%	1,609	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%	989	Completed
21-Apr-19	HSBC Saudi Arabia Ltd	Saudi Arabia	HSBC Holdings PLC	2%	31	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%	21,431	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

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## Glossary

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# 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 (AED Bn)*	Abbreviation	Logo
First Abu Dhabi Bank	835.4	FAB	
Emirates NBD	691.7	ENBD	
Abu Dhabi Commercial Bank	412.2	ADCB	
Dubai Islamic Bank	276.4	DIB	
Mashreq Bank	162.6	Mashreq	
Abu Dhabi Islamic Bank	122.7	ADIB	
Commercial Bank of Dubai	89.9	CBD	
Emirates Islamic Bank	62.9	EIB	
National Bank of Ras Al-Khaimah	59.8	RAK	
Sharjah Islamic Bank	49.3	SIB	

Note: Banks are sorted by assets size  
\* As on 31<sup>st</sup> March 2020