



UAE Banking Pulse

Quarter 4, 2020



الإمارات
THE EMIRATES

FOREWORD

Alvarez & Marsal Middle East Limited (A&M) is delighted to publish the Q4'20 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 sector. 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 metrics has been updated, where required, to reflect appropriate comparative information.

Top ten UAE banks ended FY'20 with a marginal loan growth rate of 1% and a 38% drop in net income. Net income declined due to unprecedented market conditions which resulted in an 80% increase in provisioning. While FY'21 is expected to remain less volatile compared to past year, banks might witness deterioration of their asset quality, post the completion of central bank's deferral program in June'21.

Profitability metrics have taken a hit with RoE slipping to single-digit levels (7.7% in FY'20, compared to 13.3% in FY'19). Despite a challenging business environment, aggregate capital adequacy ratio of the UAE banks remained robust at 17.6% at the end of December'20, compared to 17.3% at the end of December'19.

We hope 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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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



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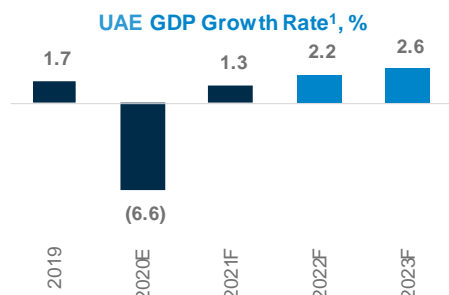
- 30+ years of experience in banking
- Focuses on performance improvement, turn-around, credit management, and formulating and managing strategic and operational changes in financial institutions
- Former CEO of banks in the UAE & Kenya

**CONTACT
DETAILS**

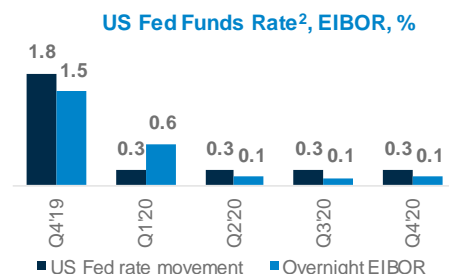
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UAE Macro & Sector Overview

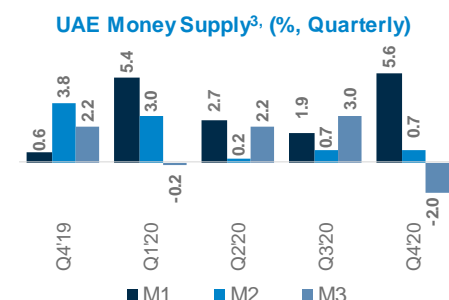
Macro overview



- UAE's economic growth is expected to rebound in FY'21 to +1.3% after contracting by 6.6% in FY'20. Economic growth is expected to strengthen in the subsequent years, driven by government initiatives
- For 2021, the UAE's government has reduced its budget spending by 5.5% to AED 58bn, a large part of which would be spent on social welfare, health and education sectors
- Average Q4'20 UAE's Purchasing Managers' Index (PMI) declined marginally to 50.1 compared to 50.4 in Q3'20, on account of reduced demand and output



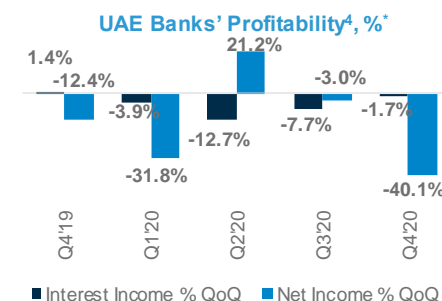
- In February'21, the US Fed reaffirmed to keep interest rate at record low levels until there are concrete signs of economic and labor market recovery
- The overnight EIBOR saw a marginal increase in Q4'20 by ~1 bps to 0.14% compared to Q3'20
- UAE's central bank is likely to hold the interest rates at the current levels until the domestic economy moves out of the pandemic effect



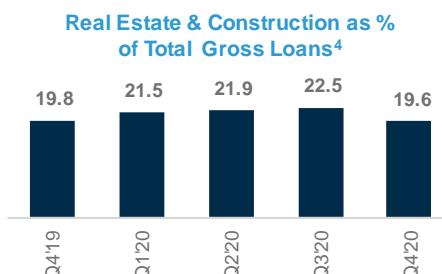
- M2 money supply rose by 0.7% QoQ in Q4'20 to AED 1,478.6bn, it increased by 4.6% YoY
- M2 money supply increased as monetary deposits grew by 7.2% QoQ in Q4'20
- M1 increased by 5.6% QoQ in Q4'20 to AED 600.1bn. On an annual basis, M1 increased by 16.5%
- M3 money supply decreased by 2.0% QoQ, due to 13.7% QoQ fall in government deposits. On an annual basis, M3 increased by 3.0%

¹ IMF, ² US Board of Federal Reserve, ³ UAE Central Bank, ⁴ Company filings, ENBD net income adjusted for one time gain of AED 4.4bn from disposal of stake in jointly controlled entity during 2019, DIB's net income adjusted for one-time gains of AED 1.0bn on bargain purchase in 2020, ⁵ Bloomberg & A&M Analysis, ⁶ based on data of 8 banks for Q3'20, weighted average exposure of all banks; * Data for top ten UAE banks by asset size as of September 30th 2020

Banking overview Q4'20



- Total interest income of top ten UAE banks continued to decline for the fourth consecutive quarter (-1.7% QoQ), on the back of persistently low interest rate environment
- Aggregate net income decreased substantially by ~40% QoQ, as increased operating expenses and impairment charges weighed on profitability
- Recovery of UAE's banking sector is expected to remain gradual and that pandemic effects will likely continue in the initial quarters of FY'21



- The UAE banks' exposure to the real estate and construction sector reduced by ~300 bps⁶ QoQ
- Currently, the real estate sector is facing headwinds in the form of persistent oversupplied conditions and pandemic driven slow down
- The sector is expected to recover over the medium to long term, on the back of regulatory amendments such as offering citizenship and golden visas to qualified expats



- While there were no deals disclosed in Q4'20, FAB announced to acquire Bank Audi SAE, the Egyptian arm of Lebanon-based Bank Audi SAL in January'21
- The financial terms of the deal are still not disclosed. However, FAB will become the largest international bank with an asset base of USD 8.1bn operating in Egypt post the acquisition

Pulse: Profitability Metrics of the UAE Banking Sector Continue to Decline, as Pandemic Effect Persists

→ Improved ← Stable → Worsened

	Metric	Q3'20	Q4'20	Q4'19	Q1'20	Q2'20	Q3'20	Q4'20	Key Trends of Q4'20
Size	Loans and Advances (L&A) Growth (QoQ)	-0.01%	↓ -0.4%						1 L&A fell 0.4% QoQ, due to challenging environment. Deposits growth (-2.8% QoQ) reached to its lowest levels in last seven quarters
	Deposits Growth (QoQ)	4.2%	↓ -2.8%						
Liquidity	Loan-to-Deposit Ratio (LDR)	84.1%	↑ 86.2%						2 LDR increased to 86.2% from 84.1% as deposits declined at a higher rate compared to L&A
Income & Operating Efficiency	Operating Income Growth (QoQ)	-3.4%	↑ 2.7%						3 Operating income increased after declining for three consecutive quarters, on the back of higher net interest and other operating income
	Operating Income / Assets	2.8%	↔ 2.8%						
	Non-Interest Income(NII) / Operating Income	30.9%	↓ 30.5%						
	Yield on Credit (YoC)	5.3%	↔ 5.3%						4 NIM expanded by 5 bps QoQ, as funding costs improved for banks C/I ratio increased further to 36.7% to move above the pre-pandemic levels
	Cost of Funds (CoF)	1.3%	↓ 1.2%						
	Net Interest Margin (NIM)	2.0%	↑ 2.1%						
	Cost-to-Income Ratio (C/I)	34.3%	↑ 36.7%						
Risk	Coverage Ratio	90.3%	↓ 89.5%						5 CoR increased to 2.0% as compared to 1.3% due to 53% QoQ increase in impairment allowances. Coverage ratio decreased slightly
	Cost of Risk (CoR)	1.3%	↑ 2.0%						
Profitability	Return on Equity (RoE)	8.8%	↓ 5.0%						6 RoE and RoA declined significantly in line with 40.1% QoQ decrease in net income
	Return on Assets (RoA)	1.0%	↓ 0.6%						
	Return on Risk-Weighted Assets (RoRWA)	1.5%	↓ 0.9%						
Capital	Capital Adequacy Ratio (CAR)	17.6%	↔ 17.6%						8 RoRWA decreased tracking lower net income, while the capital adequacy ratio remained flat

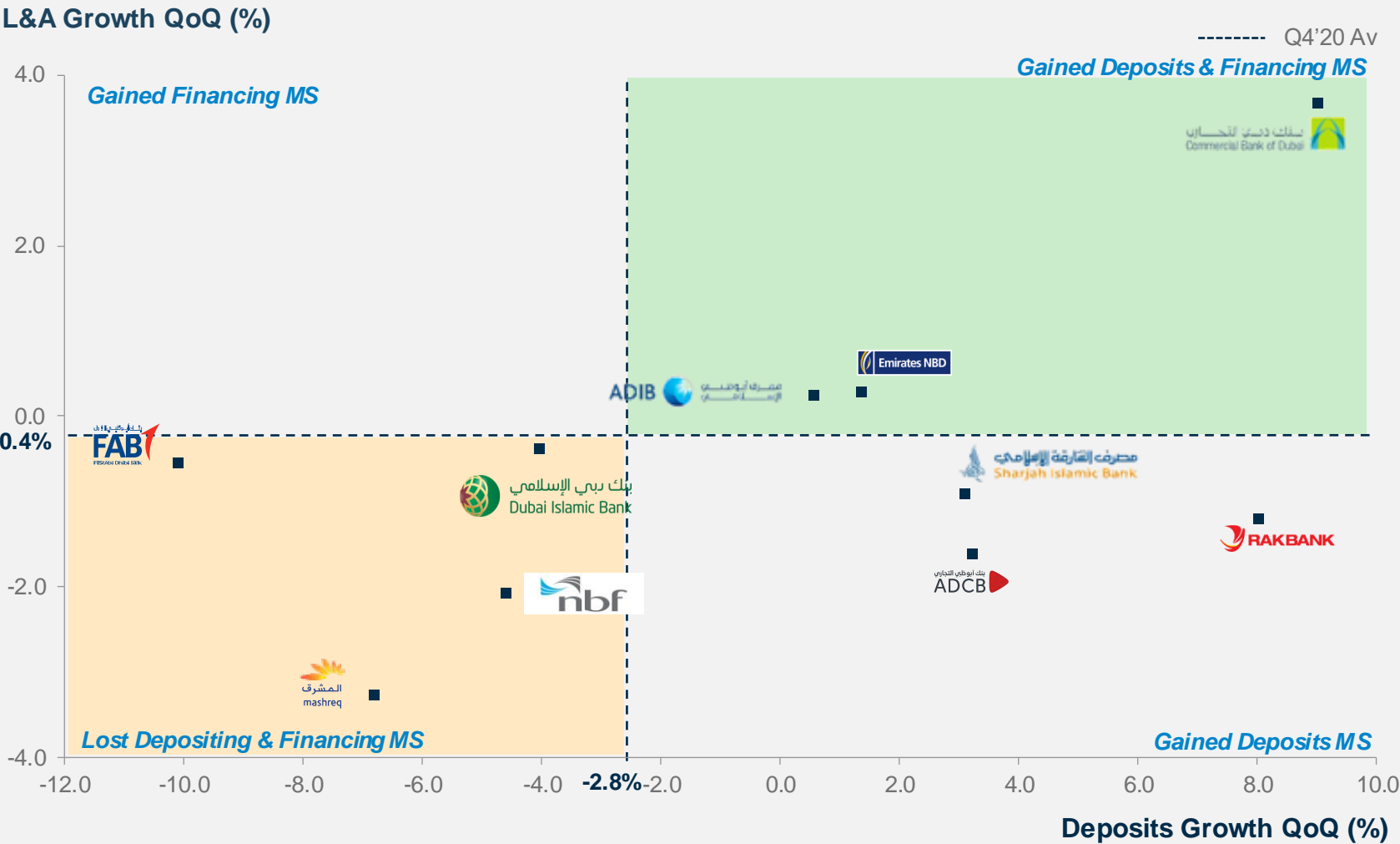
Note 1: QoQ stand for quarter over quarter

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

MSQ Underperformed its Peers on L&A Growth, while FAB's Deposits Declined Substantially



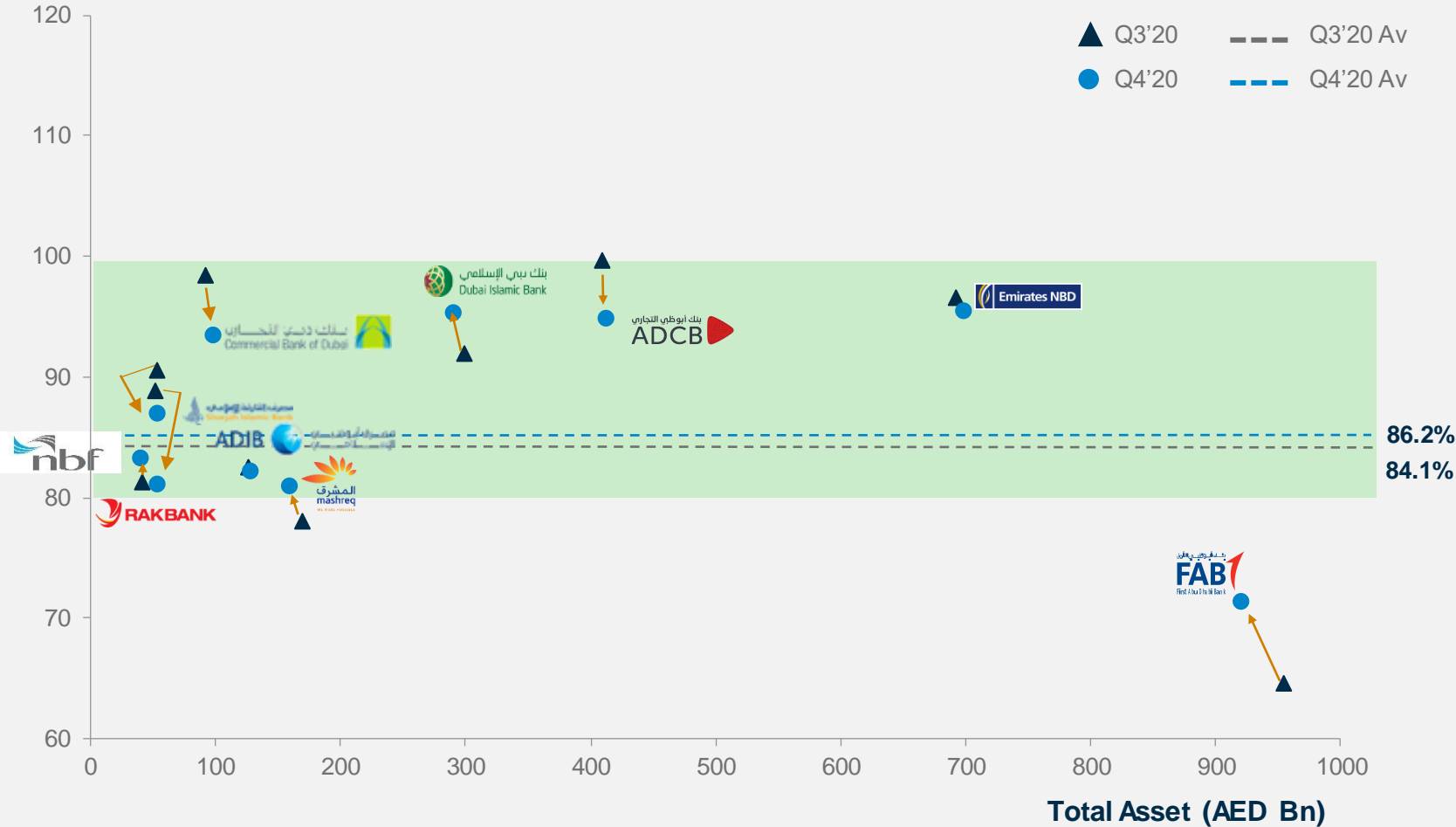
KEY TAKEAWAYS

- Top ten UAE banks' L&A and deposits decreased by 0.4% QoQ and 2.8% QoQ, respectively
- MSQ's L&A fell 3.3%, as the bank took a cautious lending approach in an uncertain economic environment
- FAB reported the highest decline in deposits (-10.1%), on the back of increased outflow from government and corporate deposits
- On the other hand, CBD reported the highest growth in deposits (+9.0% QoQ) and L&A (+3.7% QoQ)

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

Aggregate LDR Increased After Decreasing in the Preceding Quarter

Loans to Deposits Ratio (%)



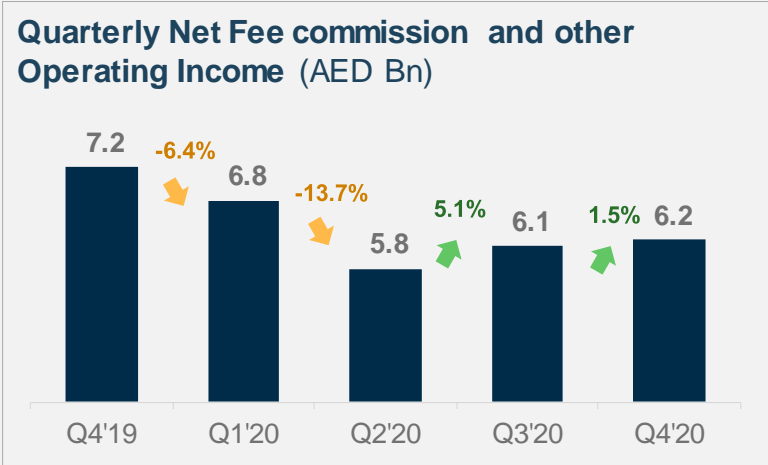
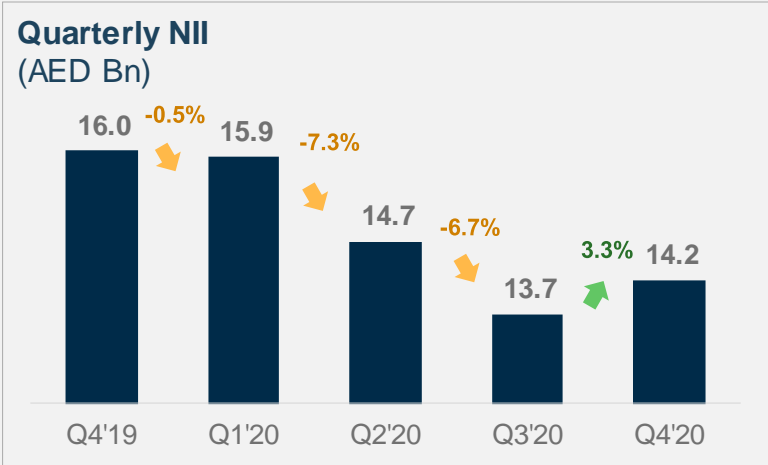
KEY TAKEAWAYS

- Aggregate LDR increased to 86.2% in Q4'20 compared to 84.1% in Q3'20
- FAB (+10.6% points QoQ) reported the highest increase in LDR to 71.5%
- RAK (-8.6% points) and CBD (-4.9% points) reported the largest decline in their LDR during the quarter

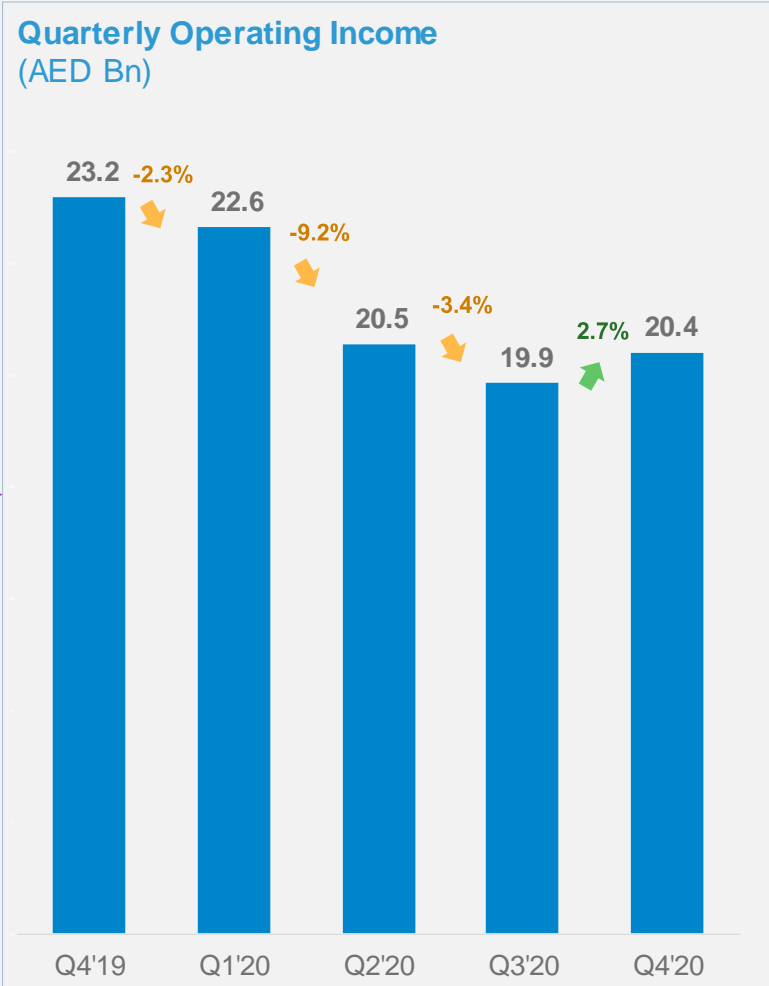
Note: The green zone is an area of healthy liquidity
Source: Financial statements, A&M analysis

Operating Income Increased as NII and Other Operating Income Inched Higher

➔ Improved
 ↔ Stable
 ➔ Worsened



+

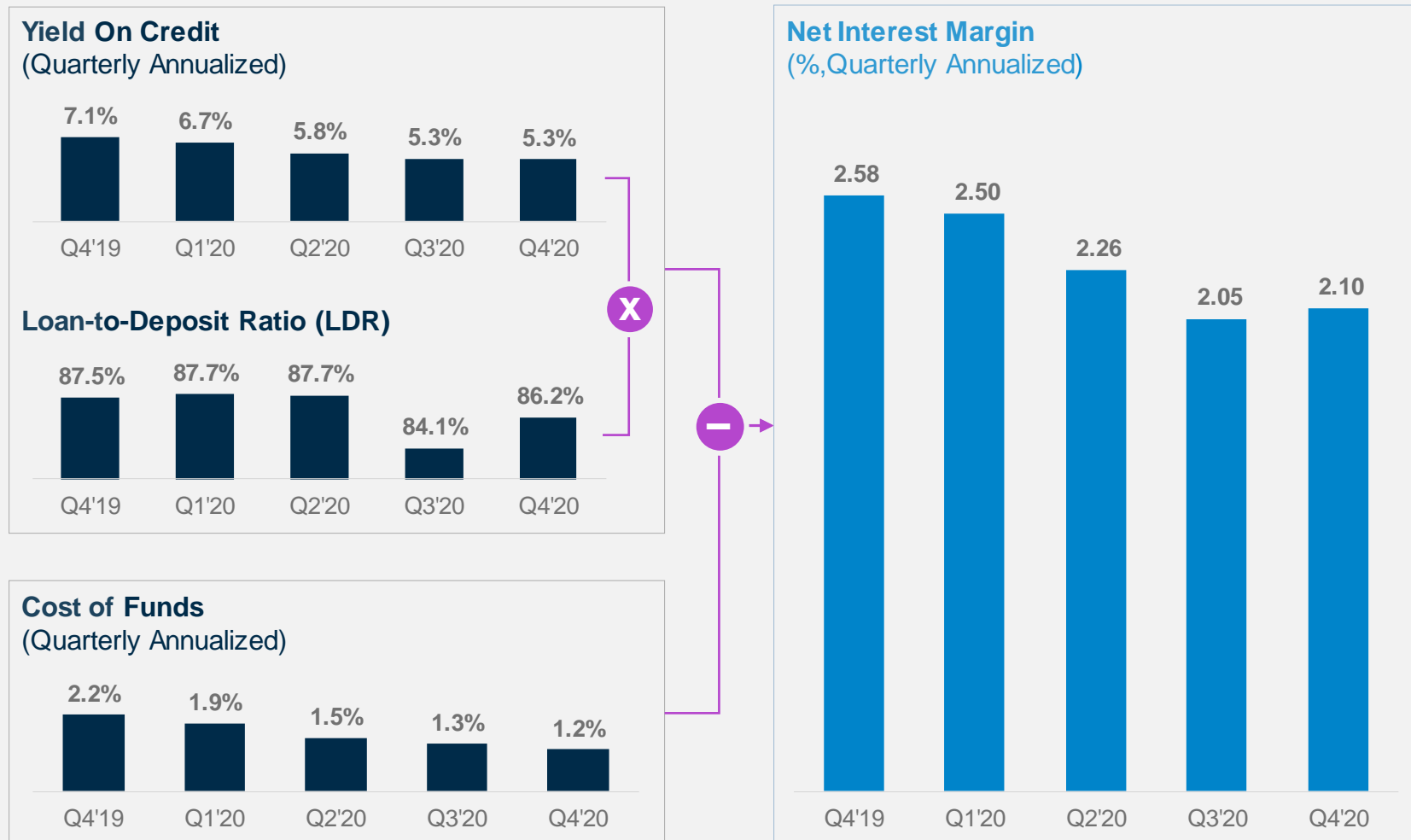


KEY TAKEAWAYS

- Operating income climbed by 2.7% QoQ, primarily driven by 3.3% QoQ increase in NII and 17.3% QoQ growth in other operating income
- This was partially offset by ~10% QoQ decline in fee income, as pandemic driven slowdown continued to impact card and commission income for banks
- CBD (+24.7% QoQ) reported the highest increase in its total operating income, followed by DIB (+14.6%) and SIB (14.5% QoQ)
- ENBD (-12.7% QoQ) and RAK (-5.3% QoQ) were the only banks which reported reduced operating income

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

4 NIM Improved After Declining for Five Consecutive Quarters



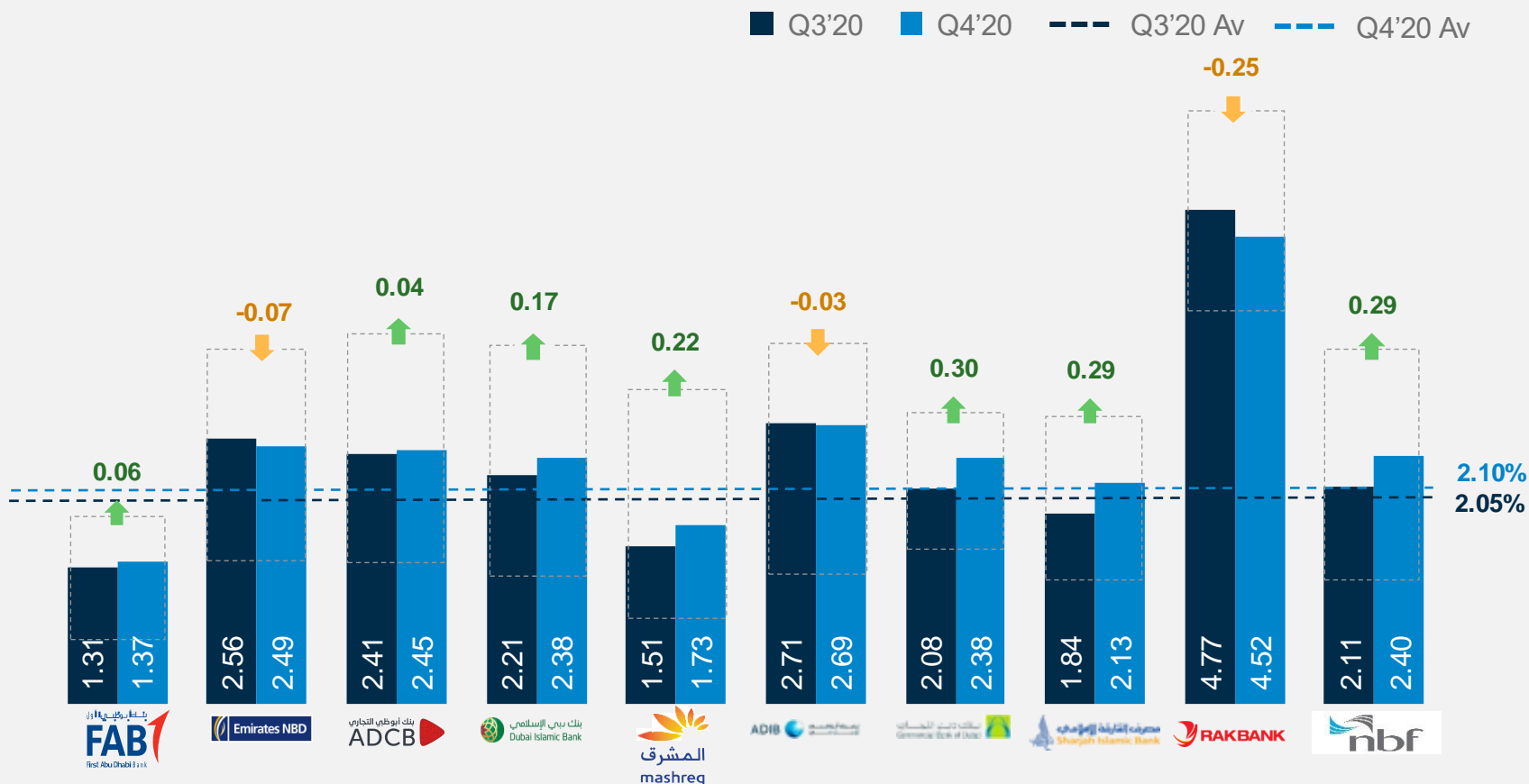
KEY TAKEAWAYS

- NIM increased by ~4.7 bps QoQ to 2.1%, remaining close to its multi-period low levels
- Yield on credit remained largely unchanged at 5.3%, while cost of funds declined ~15.2 bps to reach 1.2%

NIM Improved for Most of the Banks

→ Improved ← Stable → Worsened

Net Interest Margin (% Quarterly)



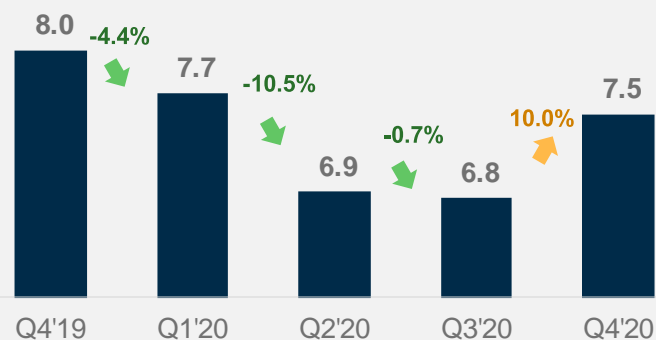
KEY TAKEAWAYS

- NIM improved by ~4.7 bps QoQ, as banks were able to reduce their funding costs further
- CBD reported the highest increase in NIM (~30 bps QoQ), followed by SIB (~29 bps QoQ)
- RAK reported highest decline (~25 bps QoQ) due to the impact of lower interest rates
- ADCB's NIM improved marginally, on account of lower cost of funds and increased NII due to fair value adjustments

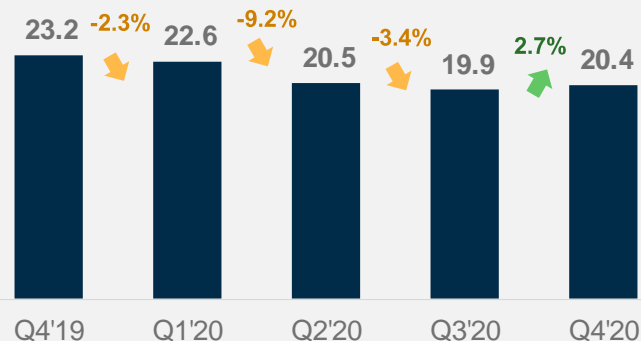
Cost to Income Ratio Increased to Pre-Pandemic Levels

→ Improved ↔ Stable → Worsened

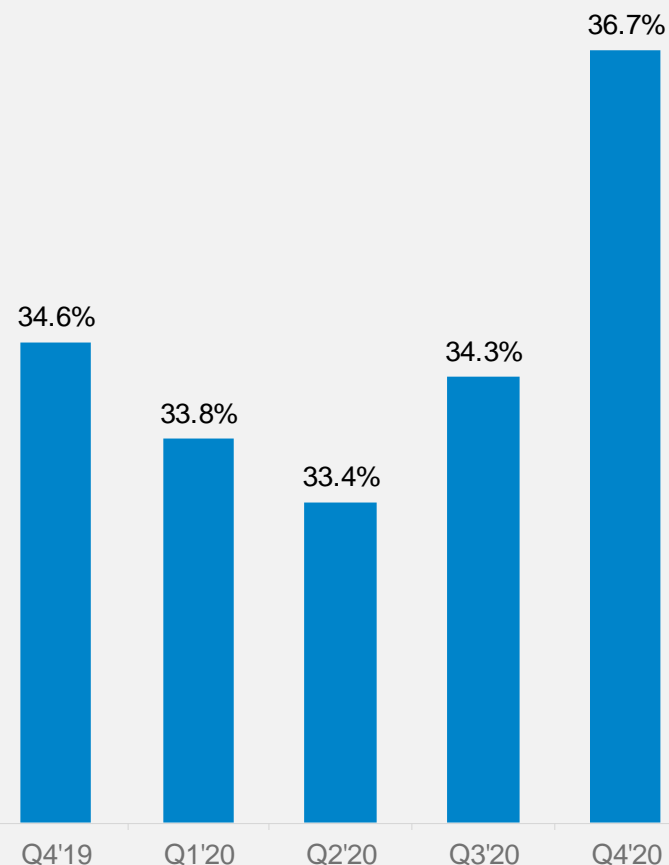
Quarterly Operating Expenses
(AED Bn)



Quarterly Operating Income
(AED Bn)



Cost to Income Ratio
(%, Quarterly Annualized)



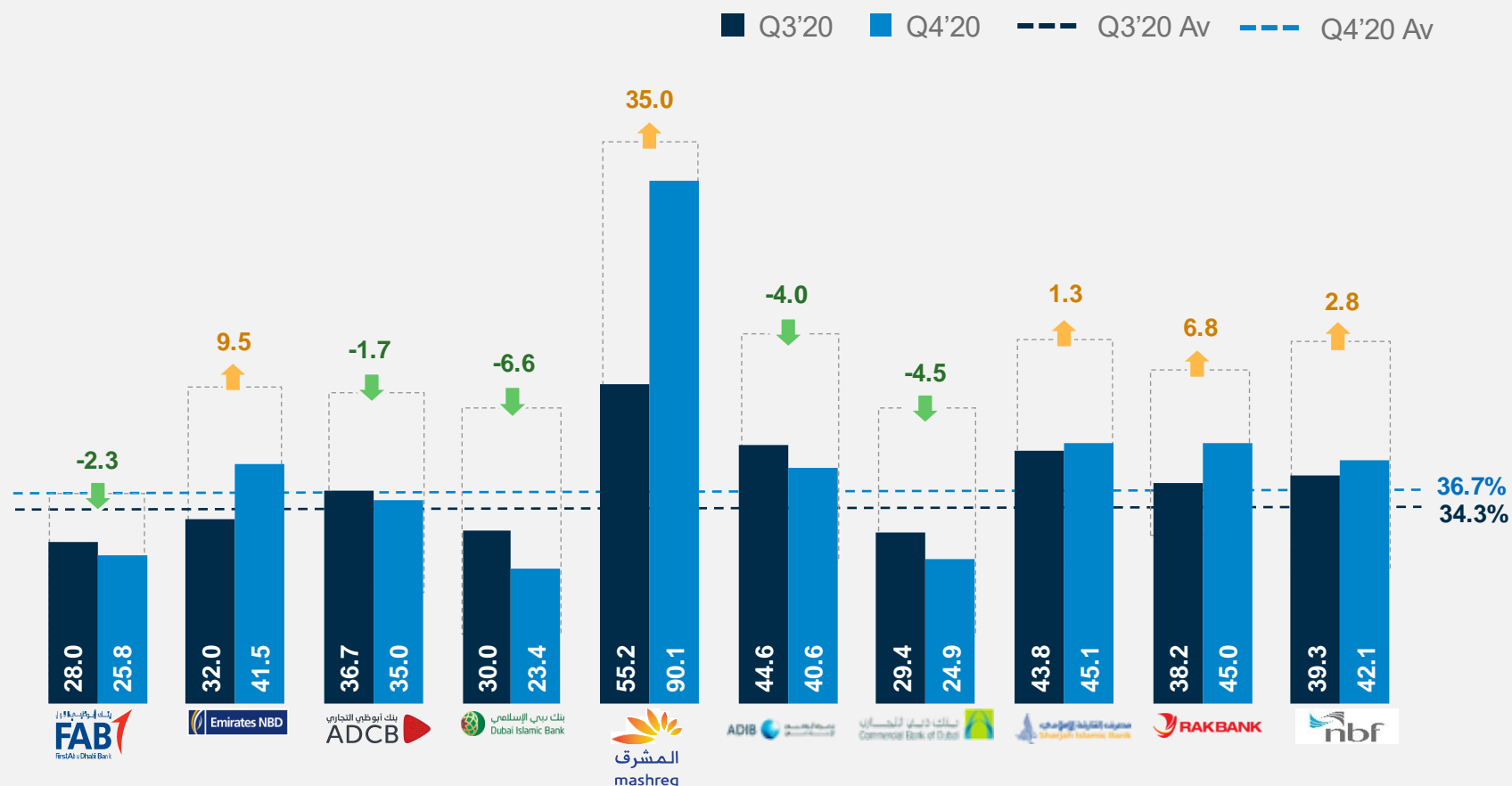
KEY TAKEAWAYS

- C/I ratio increased for the second consecutive quarter to reach 36.7%
- Operating expenses grew by ~10% QoQ, the highest increase in past several quarters
 - The increase is largely on account of seasonality effect and one-off expenses incurred by banks
 - ENBD's (+13.1% QoQ) and MSQ's (+68.7% QoQ) operating expenses increased at the highest pace

Efficiency Ratios of MSQ and ENBD Saw the Highest Deterioration

→ Improved ← Stable → Worsened

Cost to Income Ratio (% , Quarterly)



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

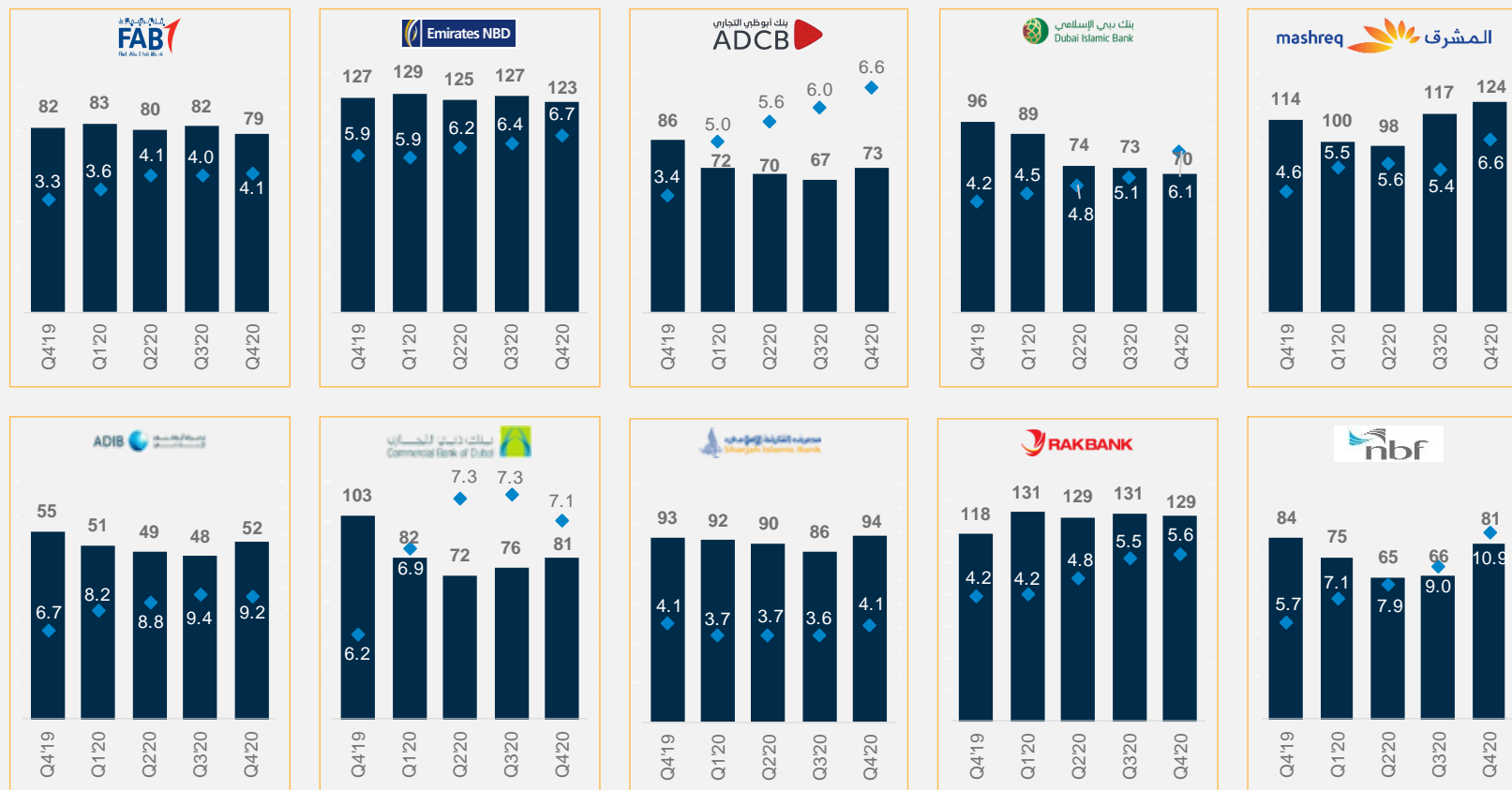
KEY TAKEAWAYS

- Five of the top ten banks reported increased C/I ratio
- MSQ's C/I ratio increased at the highest rate (+35.0% points QoQ) impacted by one-off branch rationalization costs, Covid-19 related expenses and investments in digital
- Similarly, ENBD's C/I ratio increased 9.5% points QoQ, on account of completion of certain cost management initiatives and seasonality effect
- On the other hand, DIB's C/I ratio improved the most (-6.6% points QoQ), as the bank's administrative expenses decreased by ~30% QoQ

Overall Coverage Ratio Decreased Slightly

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

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



KEY TAKEAWAYS

- Aggregate coverage ratio for the banks fell marginally to 89.5% in Q4'20 compared to 90.3% in Q3'20
- Coverage ratio of NBF (+15% QoQ) and SIB (+9% points QoQ) improved the most
- Aggregate NPL / net loan ratio continued to increase for the fifth consecutive quarter to reach 6.1%, as NPLs increased ~6.5%

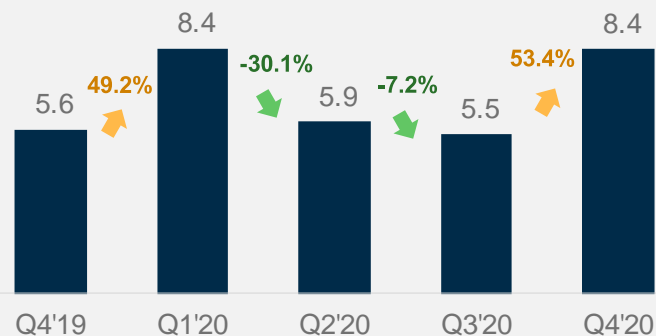
Note: Scaling and some numbers might not add up due to rounding

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

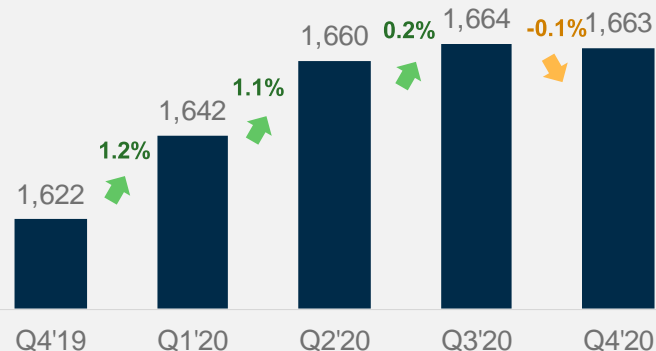
Cost of Risk Increased Significantly as Provisioning Rises

→ Improved ← Stable → Worsened

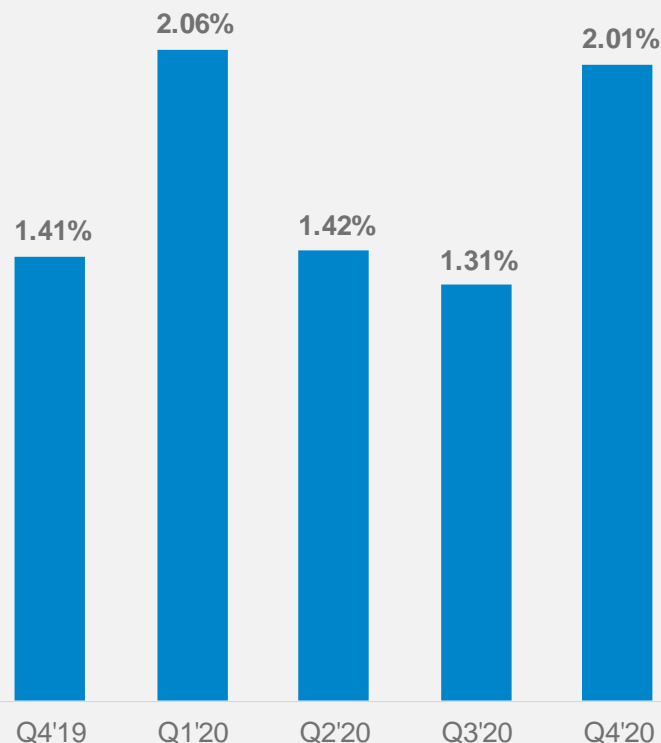
Quarterly Net Loan Loss Provisions
(AED Bn)



Average Gross Loans
(AED Bn)



Cost of Risk
(%, Quarterly Annualized)



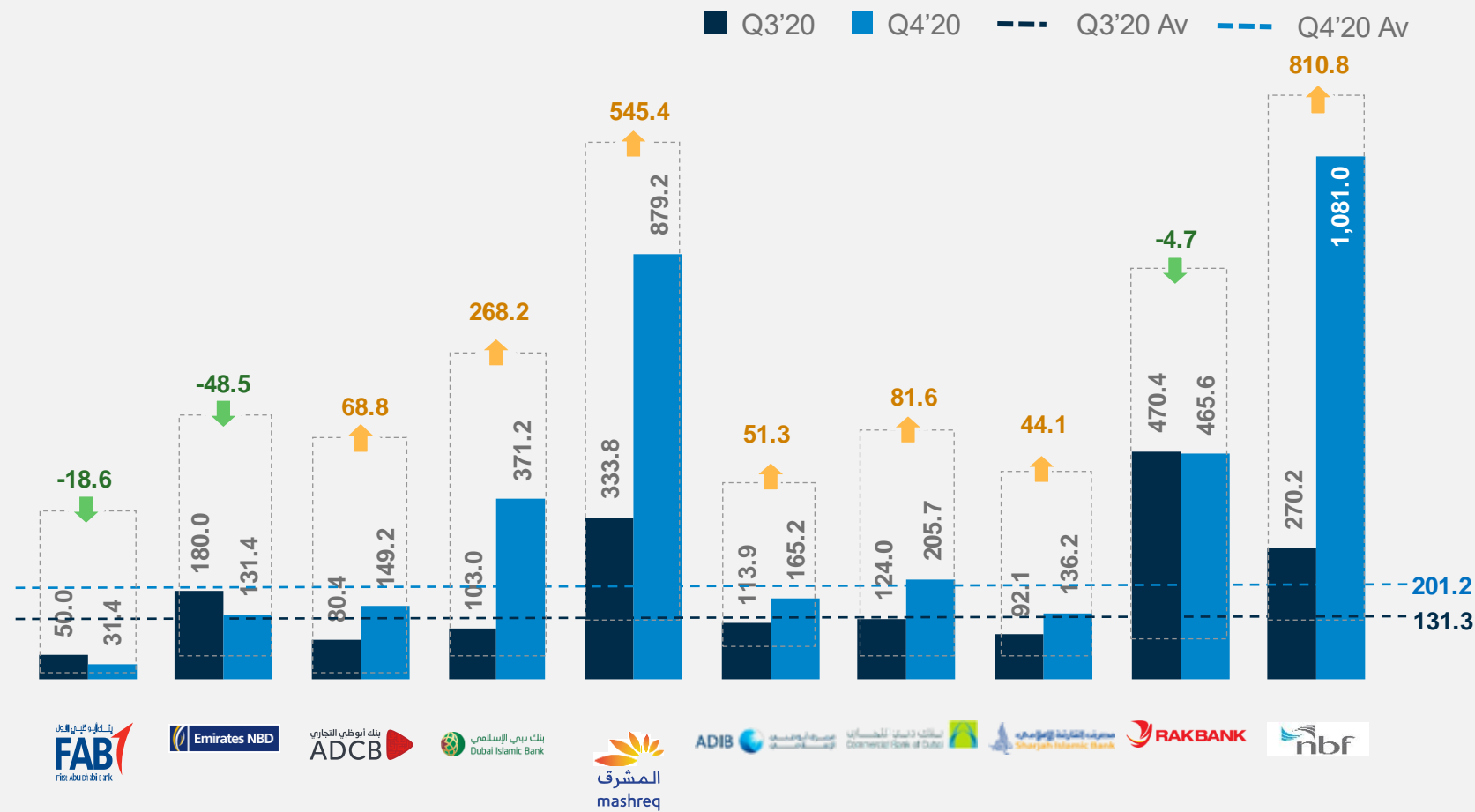
KEY TAKEAWAYS

- Aggregate cost of risk increased by ~70 bps QoQ, as total provisioning increased ~53.4% to AED 8.4bn
 - Overall increase in provisioning is primarily driven by higher impairments from DIB (+3.6x QoQ) and MSQ (+2.6x QoQ)
 - MSQ's provisions increased due to challenging conditions in corporate banking (contracting and NBFI) segment
- On the other hand, FAB (-37.0% QoQ) reported a sizeable decrease in provisioning

NBF Reported the Highest Increase in Cost of Risk

➔ Improved
 ↔ Stable
 ➔ Worsened

Cost of Risk (bps) – Net of Reversals



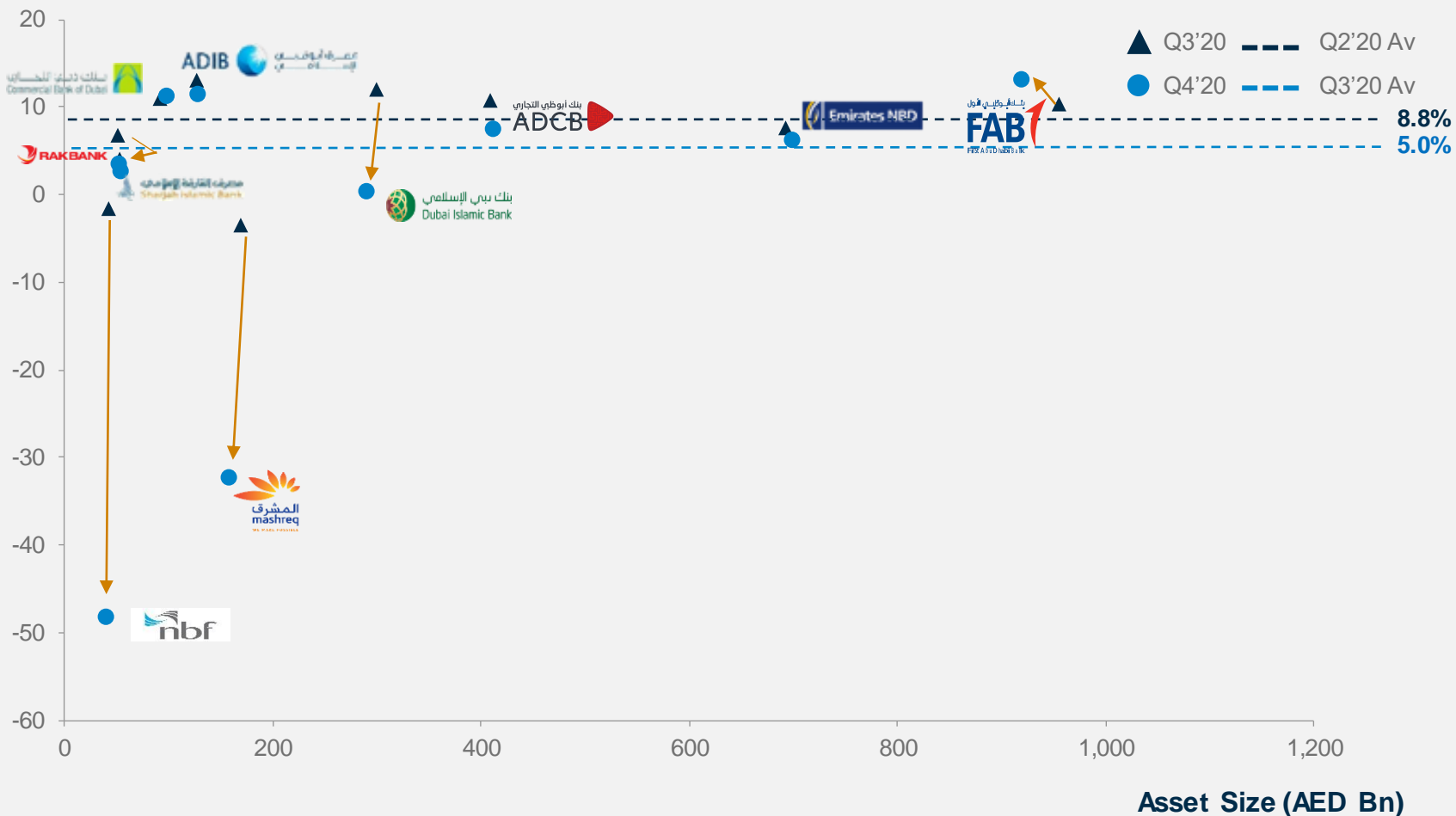
KEY TAKEAWAYS

- Seven of the top ten banks reported an increase in cost of risk
- NBF’s cost of risk increased at the highest rate (810.8 bps QoQ)
 - The increase resulted from 3.9x rise in provisions
- Similarly, DIB’s cost of risk increased by 268 bps, as the bank’s provisioning increased 3.6x, on account of one-off charges

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

7 RoE Continued to Decline for the Second Consecutive Quarter

Return on Equity (%)

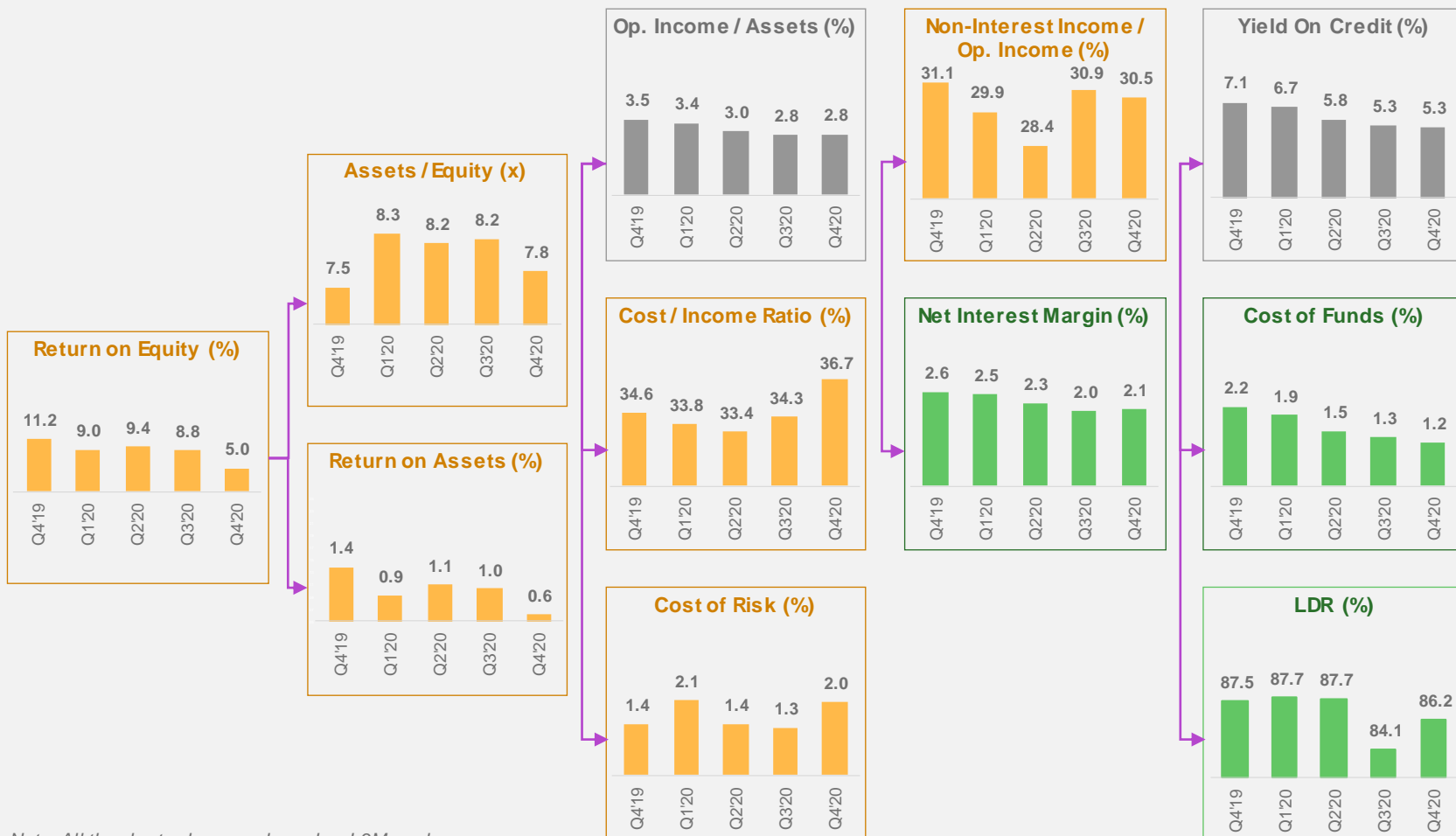


KEY TAKEAWAYS

- Aggregate RoE declined further to 5.0% in Q4'20, amid increased impairments and operating expenses
- MSQ and NBF reported steep decline in RoEs as losses for banks widened during the period
- FAB (13.2%) reported the highest RoE, followed by ADIB (11.6%) and CBD (11.4%)

Operating Environment for the UAE's Banking Sector is Expected to Remain Less Volatile in FY'21

■ 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

- The UAE's banking sector is expected to witness prolonged effect of the pandemic at least during H1'21
- Events such as Expo and a gradual economic improvement are expected to be the key catalysts for the sector in the near term
- However, interest rates are likely to remain low in the foreseeable future that would impact income streams for banks
- Following the completion of TESS program in June'21, banks might witness further deterioration in their asset quality
- FAB's acquisition of Bank Audi Egypt reinstated the M&A wave in the region and other banks could follow the trend to consolidate their position

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*
20-Jan-21	Bank Audi SAE (Egypt)	Egypt	First Abu Dhabi Bank PJSC	100%	NA	Pending
16-Sep-20	Ahli United Bank Egypt SAE	Egypt	Ahli United Bank BSC	14.4%	298	Pending
30-Jun-20	Al Khaliq Commercial Bank PQSC	Qatar	Masraf Al Rayan QSC	100%	4,404	Pending
25-Jun-20	Samba Financial Group SJSC	Saudi Arabia	National Commercial Bank SJSC	100%	57,252	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%	21,431	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%	989	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%	1,609	Completed
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

Source: Bloomberg

*Proposed Status: Board suggests shareholders to consider the acquisition

*Pending Status: Acquisition has announced

*Completed Status: Acquisition has completed

Glossary













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	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	919.1	FAB	
Emirates NBD	698.1	ENBD	
Abu Dhabi Commercial Bank	411.2	ADCB	
Dubai Islamic Bank	289.6	DIB	
Mashreq Bank	158.5	MSQ	
Abu Dhabi Islamic Bank	127.8	ADIB	
Commercial Bank of Dubai	97.4	CBD	
Sharjah Islamic Bank	53.6	SIB	
National Bank of Ras Al-Khaimah	52.8	RAK	
National Bank of Fujairah	39.9	NBF	

Note: Banks are sorted by assets size
 • As on 31st December 2020