

MARK Alert – QCB Approves Merger Between MARK & KCBK; Reiterate Outperform on MARK

The Qatar Central Bank (QCB) gives final approval of the merger between Masraf Al Rayan (MARK) and Al Khalij Commercial Bank (KCBK). We await the approval of the Ministry of Commerce & Industry and other relevant official bodies, which should happen shortly. The merger is in the process of being finalized to ensure all other legal formalities are completed in the shortest time possible

KCBK will cease to exist and MARK will become one of the largest Shar'ah-compliant banks in Qatar with a market share of 10%, in-line with QIBK. MARK has a 7% market share in loans, while KCBK has a market share of 3%. The combined bank will have assets north of QR164bn. *Increased weighting in MSCI and FTSE indices should drive further momentum in MARK shares.*

FOL increase to 100% has been approved by the BoD and shareholders. This should further boost MARK's weight in major indices such as MSCI EM and FTSE EM and contribute to increased foreign institutional ownership in the company.

Merger pricing mechanism. MARK will issue 0.50 shares for every KCBK share, corresponding to a total of 1,800 million new shares issued to KCBK's shareholders. This results in a pricing of QR2.277/share.

Key Takeaways:

- **Both banks are more than adequately capitalized.** For 9M2021, MARK's Tier-1 ratio stands at 19%, while KCBK's rests at 17%.
- **MARK and KCBK are both cost-efficient:** As of 2020, MARK enjoys a cost-to-income ratio (C/I) of 21.5%, while KCBK's is at 23.0%. There could be cost synergies resulting from the merger as both banks are costs focused and have very little retail exposure (retail banking is generally a cost intensive business).
- **Merger could dampen RoE.** MARK has one of the highest RoEs (15.2% as of 2020) in Qatar. However, KCBK's RoE is weak at 10.2% and below the bank's cost of equity. Hence, KCBK generates economic losses.
- **Both banks enjoy healthy asset quality.** MARK has the lowest NPL ratio (1.46% as of 9M2021) in Qatar as it is heavily exposed to the public sector (47% of loans). On the other hand, KCBK has been de-risking its loan book over the past several years and as such its NPL ratio improved to 1.62% as of 9M2021 (very healthy ratio). Moreover, KCBK has limited exposure to the public sector.
- **KCBK has a very liquid balance sheet position.** MARK could benefit from KCBK's liquid position.

Valuation:

- **MARK trades at a P/B and P/E of 2.3x and 15.7x on our 2021 estimates, respectively.** We rate MARK an Outperform with a PT of QR5.113/ share.
- We will adjust our estimates and model pending further clarity from management in terms of synergies, integration costs, etc.

Key Ratios and KPIs

	MARK				KCBK			
	2017	2018	2019	2020	2017	2018	2019	2020
NIM (IEAs)	2.48%	2.39%	2.37%	2.60%	1.78%	1.79%	1.98%	2.04%
NIM (RWAs)	3.71%	3.61%	3.65%	4.27%	2.43%	2.36%	2.63%	2.77%
RoE	15.6%	15.7%	16.0%	15.2%	8.2%	8.8%	10.6%	10.3%
RoA	2.0%	2.1%	2.1%	1.9%	0.8%	1.0%	1.1%	1.1%
RoRWAs	3.2%	3.3%	3.4%	3.3%	1.2%	1.4%	1.5%	1.6%
JAWs	-12.8%	-13.9%	5.2%	6.2%	6.6%	-4.3%	3.1%	2.0%
<i>Growth (Net Profit)</i>	-2.3%	5.0%	2.3%	-0.1%	28.8%	11.7%	6.9%	5.3%
Cost-to-Income Ratio	21.1%	24.0%	22.8%	21.5%	27.6%	28.8%	27.9%	27.4%
Net Loans (Growth)	6.6%	0.6%	3.2%	14.9%	-0.2%	-9.9%	-2.6%	3.9%
Deposits (Growth)	7.8%	-1.5%	6.6%	5.0%	1.5%	-11.7%	1.2%	2.1%
LDR (Loans to Stable Sources of Funds)	115.3%	111.0%	105.5%	112.8%	91.3%	91.8%	88.5%	90.3%
Liquid Assets to Total Assets	24.2%	20.5%	24.7%	24.7%	35.2%	35.7%	39.0%	36.9%
NPL Ratio	0.47%	0.83%	1.01%	1.13%	1.94%	1.85%	1.86%	2.00%
Coverage Ratio	49%	93%	84%	94%	118%	228%	251%	248%
CoR (bps)	15	N/M	7	35	84	60	59	61
Tier 1 Ratio	19.3%	18.7%	19.7%	19.6%	16.7%	15.6%	17.9%	18.2%

	Combined			
	2017	2018	2019	2020
NIM (IEAs)	2.22%	2.18%	2.24%	2.57%
NIM (RWAs)	3.20%	3.13%	3.27%	3.92%
RoE	13.1%	13.4%	14.3%	13.9%
RoA	1.57%	1.69%	1.74%	1.65%
RoRWAs	2.42%	2.57%	2.69%	2.69%
JAWs	-3.8%	-9.9%	4.5%	10.8%
<i>Growth (Net Profit)</i>	2.7%	6.4%	3.2%	2.6%
Cost-to-Income Ratio	23.1%	25.4%	24.3%	22.0%
Net Loans (Growth)	4.3%	-2.8%	1.4%	11.6%
Deposits (Growth)	3.8%	-0.2%	7.2%	4.8%
LDR (Loans to Stable Sources of Funds)	152%	141%	133%	139%
Liquid Assets to Total Assets	27%	25%	29%	28%
NPL Ratio	0.96%	1.15%	1.26%	1.32%
Coverage Ratio	96%	161%	158%	143%
CoR (bps)	37	17	22	55
Tier 1 Ratio	18.2%	17.6%	19.0%	19.1%

Combined Income Statement

Combined Income Statement (In QR mn)	2017	2018	2019	2020	9M2021
Net Interest Income	3,248	3,183	3,279	4,045	3,334
Fees & Commissions	456	505	565	392	315
FX Income	182	191	180	177	131
Other Income	66	53	46	48	18
Non-Interest Income	703	749	791	617	464
Total Revenue	3,951	3,932	4,070	4,662	3,798
Operating Expenses	(912)	(998)	(988)	(1,025)	(800)
Net Operating Income	3,039	2,934	3,082	3,637	2,998
Net Provisions & Impairments	(432)	(168)	(221)	(716)	(704)
Net Profit Before Taxes & Minority Interest	2,607	2,766	2,861	2,921	2,293
Tax	(16)	(18)	(27)	(17)	(11)
Net Profit Before Minority Interest	2,591	2,748	2,834	2,904	2,282
Minority Interest	(13)	(9)	(10)	(5)	(11)
Net Profit (Reported/Headline)	2,579	2,739	2,825	2,898	2,272
Social & Sports Contribution Fund	(66)	(69)	(70)	(72)	N/A
Interest on AT1 Perpetual Note	(55)	(55)	(55)	(55)	N/A
Net Profit (Attributable)	2,457	2,615	2,700	2,771	2,272

Recommendations

Based on the range for the upside / downside offered by the 12-month target price of a stock versus the current market price

OUTPERFORM Greater than +20%

ACCUMULATE Between +10% to +20%

MARKET PERFORM Between -10% to +10%

REDUCE Between -10% to -20%

UNDERPERFORM Lower than -20%

Risk Ratings

Reflecting historic and expected price volatility versus the local market average and qualitative risk analysis of fundamentals

R-1 Significantly lower than average

R-2 Lower than average

R-3 Medium / In-line with the average

R-4 Above average

R-5 Significantly above average

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