


Update for Q3 2015

Sector: Banking
Country: Jordan
Date: December 8, 2015

Share Price (JOD): 6.04
Target Price (JOD): 5.86
Downside: -3.03%
Recommendation: Reduce
Risk: Medium (Market)

Issuing a REDUCE rating with a Target Price of JOD 5.86 per share on slow Q3 results

Arab Bank results for the first 9 months of 2015 revealed a mere 0.15% increase in profits over the same period of 2014 to reach \$ 615 million. Q3 standalone results came in lower than 2014Q3, recording \$ 192 million versus \$199 million last year. Although the bank's results up to September reflect the decreasing interest environment it is now exposed to, the bank success at growing its deposits base by 1% y-t-d to \$ 32.39 billion, and increasing its loans to deposits ratio from 66.55% in December 2014 to 67.86% by September 2015 led to enhanced net revenues by 1.35% to \$ 1.16 billion.

The main pressure on the bank's profits came from the surge of non-interest expense (salaries and wages) by 7.46% to \$617 million. Meanwhile, writing off loan impairments boosted the third quarter's results by \$21 million. The group's provisions for defaulting loans have lessened since pre-2014 years, and are now at around 0.9% of net revenues, compared to previous level of 15% of net revenues in 2014, and exceeding 30% earlier.

Group's core operations concentrated in highly volatile countries

Rated BBB- by Fitch, Arab Bank's score is above that of Jordan's, as the bank's operations are well diversified regionally. By Q3 2015, Arab Bank's loans distribution showed a lower share in Jordan and the Arab world, (24.89% and 65.36% by 2015Q3 vs 25.97% and 70.48% by 2014Q3), in favor of Europe and the rest of the world (4.61% and 3.72% vs 0.95% and 1.19% in Q3 2014). Granted, the group's core operations and credit risk exposure remain heavily concentrated in the Arab World, with the ratio of such deposits to total global deposits slightly decreasing from 82.96% at end-2014 to 82.37% by Q3 2015.

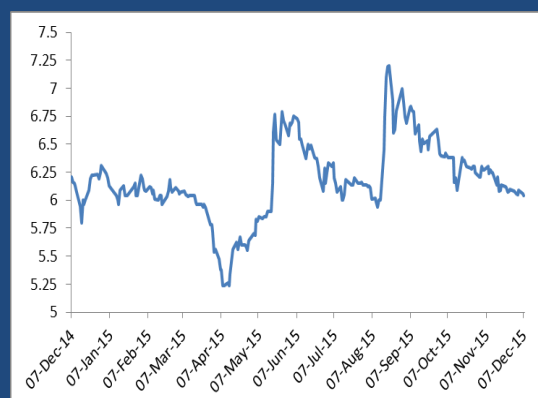
Arab Bank performance holds steady and slow in 2015

Arab bank's interest environment was mainly affected by the recent decision of the central bank of Jordan, which lowered interest rates driving down the weighted average interest rate on loans and advances to 8.28%, from 8.84% at the end of FY 2014. We expect the bank's performance in 2015 to finish closely to that of 2014, unless arising provisions in Q4 wipe off more gains. Coupled with the expected yearly decrease in profits, Arab bank's Return on Assets and Return on Equity ratios are expected to end 2015 lower at 1.16% and 6.92%, compared to respective figures of 1.20% and 7.32% by end-2014.

Share Data

Bloomberg Symbol	ARBKJR
Reuters Symbol	ARBK.AM
Market Cap (JODm)	3,998
Number of Shares (m)	640.8
Free Float	46.0%
Price-to-Earnings	9.95
Price-to-Book	0.7

Source: Bloomberg.

Share Performance


1 Month Return	-4.13%
3 Month Return	-11.18%
6 Month Return	-7.79%
12 Month Return	-1.95%
52 Week Range	5.11-7.25

Source: Reuters, Zawya

Contact Information:

Equity Analyst: David Achdjian
 david.achdjian@blominvestbank.com

Head of Equities: Maya Mantach, CFA
 maya.mantach@blominvestbank.com

Head of Research: Marwan Mikhael
 marwan.mikhael@blominvestbank.com

Performance and Forecasts

	2012	2013	2014	2015e
Net Interest Income (USDm)	1,011	1,064	1,075	1,075
Net Income (USDm)	344	497	574	565
EPS (USD)	0.64	0.93	1.01	0.86
BVPS (USD)	14.12	14.27	13.63	12.58
ROA (%)	0.8%	1.1%	1.20%	1.16%
ROE (%)	4.7%	6.6%	7.32%	6.90%

Source: Arab Bank, Blominvest

Recommendation

We recommend a Reduce rating on Arab Bank' s share, as we expect this year to close on a 2.17% decline in profits to \$564.6 million, incorporating our estimates that Q4 will end with a minor loss due to: the continuing decline in average interest rates on deposits and loans which is offsetting the mild growths achieved in deposits and loans, the increasing non-interest expenses, and the anticipated provisions typically accounted for at year end. We therefore expect 2015' s profits to end at \$564.6 million despite a steady stream of net revenues reaching \$1,075 million.

We expect 2016 onward to fare slightly better but view tighter interest rates and spreads in 2016 as the bank expands outside the high-yield-environment countries in the MENA region. While the latter countries continue to represent growth opportunities, their economic and political volatility (such in Palestine, Egypt, Tunisia and Lebanon) threaten a lower asset quality and higher non-performing loans (NPL), knowing that the current NPL ratio of Arab Bank as at September 2015 remains high at 6.4% compared to 6.7% at end of 2014. Meanwhile, diversifying away towards the GCC countries and Europe, will pressure interest revenues given their low interest environment.

Assuming a payout ratio of 25% in 2015, similar to 2014' s 24.5%, and given a 4 year period with a terminal payout ratio of 45%, the Dividend discount model yielded a fair value USD 8.30 (JOD 5.86). We believe the bank' s share has little room for appreciation, as the bank has reached a mature and steady period of growth in its current locations of presence. Arab Bank group' s current dividend yield is also low compared to its regional peers, standing at 1.76%.

Regarding the lawsuits raised in the United States against the bank for financing of terrorists and terrorist organizations in Palestine, the court decision was adjourned until May 2016 after both parties agreed to arrangements, deemed in favor of the bank. We have no reason to believe that further provisions than the ones already allocated by the bank, will be necessary for this case or for the other cases held against Arab bank, but we continue to see medium risks in light of the uncertain outcomes.

Valuation Summary

Dividend discount model

In 000'USD	2013	2014	2015e	2016f	2017f	2018f	2019f
Net Income (to shareholders)	497,021	573,687	552,840	617,800	647,617	682,615	715,069
Payout Ratio	45%	17%	25%	25%	25%	25%	45%
Dividends	225,900	96,400	138,210	154,450	161,904	170,653	321,781
Terminal Value					-	-	6,393,642
NPV of Dividends & Terminal Value				142,766	138,335	134,781	4,902,575
Estimated Fair Value				5,318,458			
Outstanding Shares				640,800			
Fair Value, USD				8.30			

Relative Valuation

Using a relative approach based on the P/B multiple, Arab Bank' s share appears undervalued with a current implied PB of 0.7x compared to 1x in Jordan and 1.14x in the MENA region. Meanwhile, the PE multiple shows a fair valuation, and the current dividend yields for the bank' s comparable companies place Arab bank at the lower range.

Banking Industry in Jordan

Ticker	Name	Market Cap (USD M)	YTD Total Return %	P/B	P/E	Div Yield
<i>Median</i>				1.0	9.80	4.23%
ARBK JR	Arab Bank PLC	5,530	-2.85%	0.7	9.95	1.76%
THBK JR	Housing Bank for Trade and Finance	3,305	6.09%	2.4	18.47	3.76%
JOIB JR	Jordan Islamic Bank	686.6	-4.12%	1.7	11.30	3.83%
CABK JR	Cairo Amman Bank	482.3	2.23%	0.9	8.07	4.62%
BOJX JR	Bank of Jordan	546.1	0.92%	1.1	8.79	8.03%
JOKB JR	Jordan Kuwait Bank	509.9	-15.62%	0.8	9.65	-

Source: Bloomberg, December 8, 2015

Regional Banking Companies

Ticker	Name		Mkt Cap (USD B)	YTD Total Return %	P/B	P/E	Div Yield
<i>Median</i>					1.14	9.35	3.40%
DIB UH	UAE	Dubai Islamic Bank	6.23	-10.83%	1.15	6.39	6.90%
ALINMA AB	KSA	Alinma Bank	5.50	-31.11%	1.13	14.63	3.65%
ARBK JR	JOR	Arab Bank PLC	5.53	-2.85%	0.70	9.95	1.76%
COMI EY	EGY	Commercial International Bank	5.18	-8.33%	2.57	8.74	2.71%
MASQ UH	UAE	Mashreq Bank	5.03	-7.65%	1.07	7.41	3.66%
CBD UH	UAE	Commercial Bank of Dubai	4.85	-	2.19	14.37	3.15%

Source: Bloomberg, December 8, 2015

Arab Bank Highlights

Arab Bank PLC is a Jordan-based public shareholding company engaged in banking services with branches all over the world. The Bank is active, along with its sister company and subsidiaries, all types of banking business, including Consumer banking, Corporate and Institutional Banking, Treasury, leasing and Insurance. The group employs around 9,676 employees.

Management team

Nehmeh Elias Sabbagh	CEO
Randa Mohammed Toufic Sadiq	Deputy CEO
Eric Modave	COO

Historical and Projected Income statements - *selected items*

<i>USDm</i>	2012a	2013a	2014a	2015e
Interest Income	1,765	1,838	1,845	1,792
Interest Expense	(754)	773	770	717
Net Interest Income	1,011	1,065	1,075	1,075
Commission Income	323	342	349	354
Commission Expense	(21)	(24)	(27)	(28)
Net Commission Income	302	318	322	326
Other Revenue (includes financial assets)	57	118	133	148
Net Revenue	1,370	1,501	1,529	1,548
Loan Impairment Loss/Provision	(348)	(286)	(236)	(204)
Net Revenue After Provisions	1,023	1,215	1,293	1,344
Non-Interest Expense	(755)	(784)	(800)	(848)
Operating Income	268	431	493	496
Profits from Associates	294	310	348	373
Pretax Income	563	741	841	869
Income Tax Expense	(211)	(240)	(264)	(304)
Net Income	352	502	577	565
Minority Interest	(8)	5	3	12
Net Income Att. to Shareholders	344	497	574	553

Source: Arab Bank, Blominvest

Historical Balance Sheets – selected items

<i>USDm</i>	2012a	2013a	2014a	Q3 2015a
Assets				
Cash and Due from Central Bank	7,749	8,180	7,392	8,718
Due from Banks	4,943	3,492	4,664	3,674
Direct Credit Facilities	20,480	20,971	21,341	21,977
Total Investments	8,799	9,918	10,721	10,173
Investments in Subsidiaries/Associates	2,426	2,618	2,829	2,847
Other Assets	1,248	1,221	1,203	1,326
Total Assets	45,647	46,400	48,151	48,715
Due to Banks	3,836	3,029	4,081	3,751
Due to Customers	29,352	30,723	32,065	32,387
Cash margin	3,534	3,667	2,904	2,452
Borrowed funds	157	105	87	73
Other liabilities	1,068	1,108	1,126	1,848
Total Liabilities	37,947	38,632	40,263	40,511
Total Equity (att. to shareholders)	7,538	7,621	7,762	8,076
Minority Interest	161	146	127	128
Total Equity	7,699	7,768	7,888	8,204
Total Liabilities & Equity	45,647	46,400	48,151	48,715

Source: Arab Bank, Blominvest

Quarterly Income Statements 2014-2015

<i>USD '000s</i>	2014 Q1a	2014 Q2a	2014 Q3a	2014 Q4a	2015 Q1a	2015 Q2a	2015 Q3a	2015 Q4e
Interest Income	463,395	465,027	455,503	461,171	448,024	453,705	449,946	441,166
Interest Expense	(197,370)	(196,250)	(188,127)	188,401	180,571	181,047	177,364	178,558
Net Interest Income	266,025	268,777	267,376	272,770	267,453	272,658	272,582	262,608
Commission Income	87,741	91,956	85,283	83,948	86,677	90,571	85,218	91,067
Commission Expense	(6,378)	(6,960)	(6,751)	(7,246)	(6,231)	(7,993)	(6,572)	(7,202)
Net Commission Income	81,363	84,996	78,532	76,702	80,446	82,578	78,646	83,865
Other Revenue (includes financial assets)	35,067	31,587	33,745	32,168	34,098	47,690	26,784	39,002
Net Revenue	382,455	385,360	379,653	381,640	381,977	402,926	378,012	385,475
Loan Impairment Loss/Provision	(4,613)	(16,854)	(15,582)	(199,112)	(6,755)	(24,340)	20,929	(193,812)
Net Revenue After Provisions	377,842	368,506	364,071	182,528	375,242	378,586	398,941	191,663
Non-Interest Expense	(187,290)	(196,243)	(190,721)	(225,575)	(186,066)	(204,615)	(226,404)	(231,285)
Operating Income	190,552	172,263	173,350	(43,047)	189,176	173,971	172,537	(39,622)
Profits from Associates	86,822	95,240	91,020	75,119	92,559	103,977	86,458	89,562
Pretax Income	277,374	267,503	264,370	32,072	281,735	277,948	258,995	49,940
Income Tax Expense	(61,075)	(68,914)	(65,041)	(69,136)	(64,519)	(72,295)	(66,716)	(100,486)
Net Income	216,299	198,589	199,329	(37,064)	217,216	205,653	192,279	(50,546)
Minority Interest	(336)	(351)	120	(2,899)	(1,764)	(2,348)	(3,087)	(4,562)
Net Income Att. to Shareholders	215,963	198,238	199,449	(39,963)	215,452	203,305	189,192	(55,108)

Source: Arab Bank, Blominvest

BLOMINVEST BANK s.a.l.

Research Department
Verdun, Rashid Karamah Str.
POBOX 11-1540 Riad El Soloh
Beirut 1107 2080 Lebanon

Tel: +961 1 991784
research@blominvestbank.com

For your Queries:

Marwan Mikhael, Head of Research
marwan.mikhael@blominvestbank.com
+961 1 991 784 Ext: 319

Maya Mantach, Head of Equities
maya.mantach@blominvestbank.com
+961 1 991 784 Ext: 320

David Achdjian, Equity Analyst
david.achdjian@blominvestbank.com
+961 1 991 784 Ext: 327

Equity Rating Key

Recommendations are based on the upside (downside) between our 12-month Fair Value estimate and the current Market Price.

Buy: Fair Value higher than Market Price by at least 20%

Accumulate: Fair Value higher than Market Price by 10% to 20%

Hold: Fair Value ranges between -5% to +10% in relation to Market Price

Reduce: Fair Value lower than Market Price by 5% to 15%

Sell: Fair Value lower than Market Price by at least 15%

Risks are based on share price volatility along with qualitative factors such as the nature of the business,

IMPORTANT DISCLAIMER

This research is based on current public information that we consider reliable, but we do not represent it is accurate or complete, and it should not be relied on as such.

Blom Bank SAL or Blom Invest SAL can have investment banking and other business relationships with the companies covered by our research. We may seek investment banking or other business from the covered companies referred to in this research. Our salespeople, traders, and other professionals may provide oral or written market commentary or trading strategies to our clients and our proprietary trading desks that reflect opinions that are contrary to the opinions expressed in this research. Our asset management area, our trading desks and investing businesses may make investment decisions that are inconsistent with the recommendations or views expressed in this research.

We and our affiliates, officers, directors, and employees, excluding equity analysts, will from time to time have long or short positions in, act as principal in, and buy or sell, the securities or derivatives (including options and warrants) thereof of covered companies referred to in this research.

This research is not an offer to sell or the solicitation of an offer to buy any security in any jurisdiction where such an offer or solicitation would be illegal. It does not constitute a personal recommendation or take into account the particular investment objectives, financial situations, or needs of individual clients.

Clients should consider whether any advice or recommendation in this research is suitable for their particular circumstances and, if appropriate, seek professional advice. The price and value of the investments referred to in this research and the income from them may fluctuate.

Past performance is not a guide to future performance, future returns are not guaranteed, and a loss of original capital may occur. Certain transactions, including those involving futures, options, and other derivatives, give rise to substantial risk and are not suitable for all investors. Fluctuations in exchange rates could have adverse effects on the value or price of, or income derived from, certain investments.

Copyright 2014 BlomInvest SAL.

No part of this material may be copied, photocopied or duplicated in any form by any means or redistributed without the prior written consent of Blom Invest SAL.