Qatar Islamic Bank

Flash Note 31 January 2010

Strong Recoveries, Upgrade to Buy

- **Earnings driven by stable core operating performance and benign asset quality**
- **We believe the bank would benefit from government infrastructure/transport projects this year**
- **Upgrade the stock to "Buy" and adjust target price to QAR89.7**

Results highlight: Earnings were in line with our/street estimates helped by stable core operating performance: net interest income and fee income. Loan growth remained strong primarily driven by government/semi-government and trading books. Margins improved during the quarter to 3.86%, further supporting net interest income. Credit expansion also boosted fee income, which rose 90%, quarterly. Operating expenses increased during the quarter/year due to expansion initiatives.

Due to customer repayments, the bank saw more recoveries than loan loss charges, leading to negative loan loss provisioning during the quarter. NPL ratio also declined to 1.2% from 1.6% in the previous quarter, helped by the bank's focus on risk management. Management expects NPL ratio to improve this year on the back of strong recoveries and tight risk management.

What we think: Strong bad loan recoveries and relatively high growth, amid a challenging environment, are a positive. Being the biggest Islamic bank in Qatar with a strong track record, we believe the bank is well placed to benefit from infrastructure projects and trading activities in Qatar. Nonetheless, investment income is likely to be at lower levels this year due to its real estate tilt stemming from Islamic orientation.

Action: We upgrade our rating to Buy from Hold and adjust our target price to QAR89.7. We raise our loan growth assumptions and lower loan loss charges in light of the benign asset quality experienced by the bank. QIB stands out in terms of strong loan recoveries, especially in the current context of heightened risk, when the sector is still struggling with bad loans. As such, the stock offers better earnings visibility, in our view.

Valuation and catalyst: Despite trading in line with the FY10f PB Qatar sector average, we find the stock attractive after the drop in share price—translating to an upside potential of 24%. It is trading at a 9% discount to its implied PB and at a 70% discount to its five-year average historical PB. The stock has fallen 21% since its peak in September 2009 and is underperforming the market. We believe the stock deserves to trade at a higher multiple than the sector given its better growth prospects and benign asset quality. Expected increase in infrastructure projects in Qatar and international expansion would act as catalysts to the stock.

KPIs (QAR mn)	New		Old		Consensus	
	FY10f	FY11f	FY10f	FY11f	FY10c	FY11c
Net interest income	2,101.7	2,402.4	1,419.1	1,586.4	-	-
Total income	2,242.3	2,559.4	2,145.6	2,495.5	2,295.0	2,717.0
Net income	1,527.9	1,779.7	1,596.1	2,069.2	1,401.0	1,653.0
Net interest margin	4.01%	3.99%	4.12%	4.13%	-	-
Gross loans (bn)	30.4	34.9	30.3	33.6	-	-
Cost/Income	24.0%	24.1%	22.8%	22.9%	-	-
Gross LD	120.0%	110.0%	120.0%	110.0%	-	-
EPS	7.45	8.69	7.37	9.55	-	-
DPS	1.49	1.74	1.47	1.91	-	-
Dividend Yield	2.06%	2.40%	1.91%	2.48%	-	-
P/E (x)	9.7	8.3	10.5	8.1	-	-
P/B (x)	1.6	1.4	1.9	1.6	-	-
ROAE	16.8%	17.7%	16.2%	17.0%	-	-
ROAA	3.6%	3.8%	3.5%	3.6%	-	-

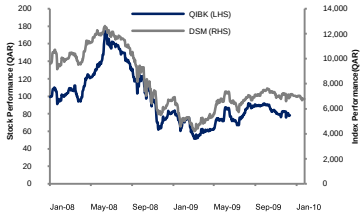
Buy

Target Price (QAR)	89.7
Market Price (QAR)	72.3
Upside	24.1%
Listed on	DSM
Bloomberg	QIBK QD
RIC	QISB.QA
Market Cap. (QAR mn)	14,804
Market Cap. (USD mn)	4,067
No of Shares (mn)	207
Foreign Ownership Limit	25.0%
Foreign Ownership Level	4.7%

Shareholders Structure

Free Float	90.8%
QIA	5.0%
Others	4.2%

Price Performance Chart



Janany Vamadeva
► +971 4 293 5384
► janany.vamadeva@af-hc.com

Germaine Benyamin
► +971 4 293 5382
► germaine.benyamin@af-hc.com

* Disclaimer: See Page 5

Table 1: Comparison (quarterly) of Actual vs. Estimates

QAR million	4Q09a	4Q08a	YoY	3Q09a	QoQ	4Q09e	Surprise
Net Interest Income	335.1	263.1	27%	307.0	9%	348.8	-4%
Non-Interest Income	127.7	117.9	8%	106.7	20%	129.3	-1%
Total Income	462.8	381.0	21%	413.6	12%	478.0	-3%
Operating Expense	149.5	115.4	30%	121.4	23%	126.1	19%
Operating Profit	313.3	265.6	18%	292.2	7%	351.9	-11%
Provision	7.0	106.0	-93%	106.7	-93%	97.8	-93%
- Loan loss	(55.0)	41.0	-234%	86.1	-164%	87.2	-163%
- Other	62.0	65.0	-5%	20.7	200%	10.6	483%
Net Income	320.9	392.0	-18%	188.5	70%	317.8	1%
Cost-to-Income Ratio	32%	30%		29%		26%	
in billion							
Net Loans	25.5	18.9	35%	22.4	14%	25.0	2%
Deposit	20.4	16.6	23%	20.2	1%	20.9	-3%
Shareholders' Equity	9.0	7.1	26%	7.8	16%	8.5	6%

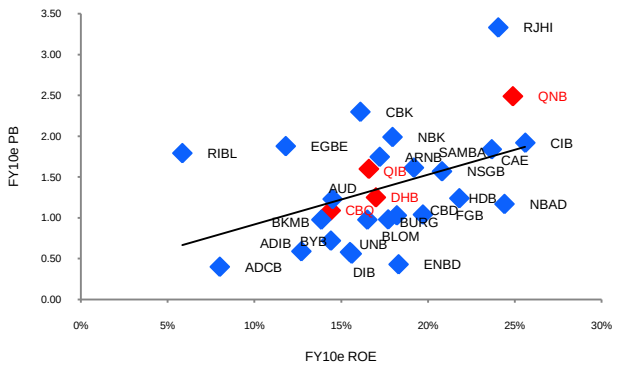
Table 2: Comparison (annual) of Actual vs. Estimates

QAR million	FY09a	FY08a	YoY	FY09e	Surprise
Net Interest Income	1,288.7	897.8	44%	1,302.3	-1%
Non-Interest Income	613.4	1,268.2	-52%	614.9	0%
Total Income	1,902.0	2,165.9	-12%	1,917.2	-1%
Operating Expense	487.4	443.9	10%	464.1	5%
Operating Profit	1,414.6	1,722.0	-18%	1,453.1	-3%
Provision	130.8	17.3	658%	221.6	-41%
- Loan loss	31.1	(47.8)	-165%	173.3	-82%
- Other	99.7	65.0	53%	48.3	106%
Net Income	1,322.1	1,642.5	-20%	1,318.9	0%
Cost-to-Income Ratio	26%	20%		24%	
in billion					
Net Loans	25.5	18.9	35%	25.0	2%
Deposit	20.4	16.6	23%	20.9	-3%
Shareholders' Equity	9.0	7.1	26%	8.5	6%

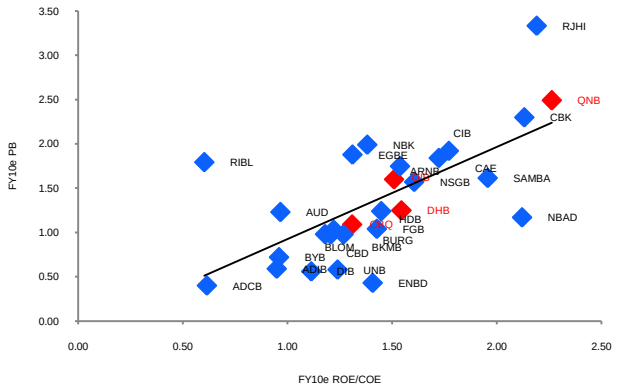
Source: Company reports, HC Brokerage

Chart 1: Valuation

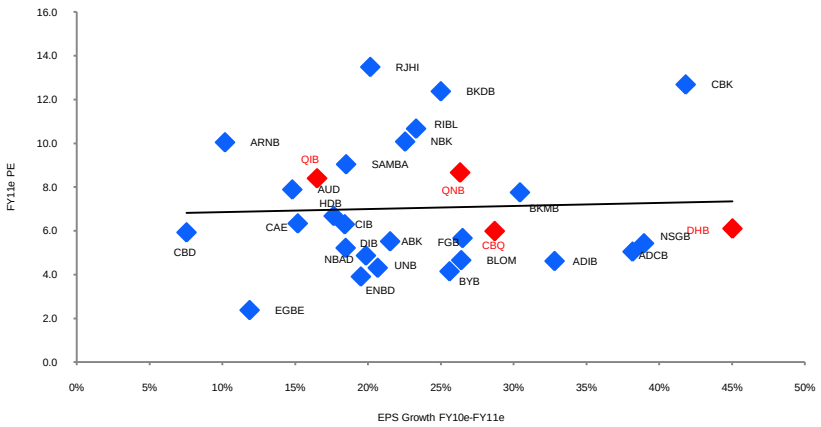
FY10e PB vs. ROE



FY10e PB vs. ROE/COE



FY11e PE vs. EPS growth



Source: Bloomberg, HC Brokerage

Financial Statements

QAR million	2008a	2009a	2010f	2011f	2012f	2013f
Income Statement						
Interest Income	1,286.4	1,799.0	2,101.7	2,402.4	2,702.2	3,033.4
Interest Expense	388.7	510.4	608.7	709.1	738.6	819.0
Net Interest Income	**897.8**	**1,288.7**	**1,492.9**	**1,693.3**	**1,963.6**	**2,214.3**
Fees and Commissions	223.2	258.7	297.5	342.1	376.4	414.0
FX Income	(80.7)	45.1	45.6	47.9	50.3	52.8
Investment Income	548.5	253.9	245.6	274.8	307.8	344.7
Other Income	577.2	55.6	160.7	201.2	225.2	252.1
Non-interest Income	**1,268.2**	**613.4**	**749.4**	**866.1**	**959.7**	**1,063.6**
Total Income	**2,165.9**	**1,902.0**	**2,242.3**	**2,559.4**	**2,923.2**	**3,277.9**
Total Operating Expenses	443.9	487.4	540.3	621.5	702.8	789.3
Pre-provision Income	1,722.0	1,414.6	1,702.0	1,937.9	2,220.4	2,488.6
Provisions	17.3	130.8	126.8	103.2	70.2	78.2
Associate and Other Income	-	-	-	-	-	-
Pre-tax Income	**1,704.7**	**1,283.8**	**1,575.2**	**1,834.7**	**2,150.2**	**2,410.4**
Income Taxes	-	(10.9)	-	-	-	-
Net Income After Tax	**1,704.7**	**1,294.7**	**1,575.2**	**1,834.7**	**2,150.2**	**2,410.4**
Minority Interest	62.2	(27.4)	47.3	55.0	64.5	72.3
Net Income	**1,642.5**	**1,322.1**	**1,527.9**	**1,779.7**	**2,085.7**	**2,338.1**
Balance Sheet						
Assets						
Cash Due from Central Bank	1,023.2	1,338.2	1,921.4	3,292.9	4,983.5	5,657.4
Due from Banks	6,367.7	8,902.6	9,032.7	8,093.3	8,498.0	9,517.7
Investments	2,947.2	1,818.6	2,032.4	2,276.2	2,549.4	2,855.3
Gross Loans	**21,234.7**	**25,734.3**	**30,366.5**	**34,921.5**	**38,413.6**	**42,255.0**
NPL Provisions	234.0	264.2	169.9	64.8	(55.9)	(174.7)
Unearned Profit	2,134.9	2,806.6	2,846.9	3,055.6	3,457.2	3,169.1
Net Loans	**18,865.9**	**22,663.5**	**27,349.8**	**31,801.0**	**35,012.3**	**39,260.5**
Other Assets	4,078.9	4,250.7	4,526.0	4,811.0	5,293.0	5,828.7
Net Fixed Assets	260.3	299.1	301.4	308.8	317.0	331.9
Total Assets	**33,543.2**	**39,272.7**	**45,163.6**	**50,583.2**	**56,653.2**	**63,451.6**
Liabilities						
Total Deposits	**16,591.8**	**20,361.0**	**25,305.4**	**31,746.8**	**36,584.4**	**42,255.0**
Due to Banks	8,696.7	8,691.0	8,981.5	6,768.0	6,085.5	5,090.8
Borrowings	-	-	-	-	-	-
Other Liabilities	885.8	1,021.9	1,259.5	838.2	931.4	1,017.9
Total Liabilities	**26,174.4**	**30,073.9**	**35,546.4**	**39,353.0**	**43,601.2**	**48,363.7**
Shareholders' Equity	**7,368.8**	**9,198.8**	**9,617.2**	**11,230.3**	**13,052.0**	**15,087.9**

Rating Scale

Recommendation	Upside
Buy	Greater than 20%
Hold	-5% to 20%
Sell	Less than -5%

Disclaimer

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Qatar

HC Research		research@hc-si.com	
Karim Khadr	Regional Head of Research	karim.khadr@af-hc.com	+971 4 2935381
Tudor Allin-Khan, CFA	Chief Economist/Strategist	tudor.allin-khan@af-hc.com	+971 4 2935386
Amr Abdel Khalek	Junior Economist	aabdelkhalek@hc-si.com	+202 3332 638
NematAllah Choucri	Telecoms	nchoucri@hc-si.com	+202 3332 8610
Sarah Shabayek	Telecoms	sshabayek@hc-si.com	+202 3332 8640
Germaine Benyamin	Banks & Financials	germaine.benyamin@af-hc.com	+971 4 2935382
Janany Vamadeva	Banks & Financials	janany.vamadeva@af-hc.com	+971 4 2935384
Hatem Alaa	Industrials	halaa@hc-si.com	+202 3332 8614
Mennatallah El Hefnawy	Industrials	melhefnawy@hc-si.com	+202 3332 8632
Mai Nehad	Industrials	mnehad@hc-si.com	+202 3332 8626
Nadine Weheba	Industrials	nweheba@hc-si.com	+202 3332 8644
Majed Azzam	Real Estate	majed.azzam@af-hc.com	+971 4 2935385
Ankur Khetawat	Real Estate	ankur.khetawat@af-hc.com	+971 4 2935387
Nermeen Abdel Gawad	Real Estate	ngawad@hc-si.com	+202 3332 8628
Rehaam Romero	Editor	rromero@hc-si.com	+202 3332 8634
Mohamed El Saiid, MFTA	Head of TA Research	msaeed@hc-si.com	+202 37496008 (Ext. 175)
Wael Atta, CFTe	Senior Technical Analyst	wael.atta@af-hc.com	+971 4 2935388
Sameh Khalil, CFTe	Technical Analyst	skhalil@hc-si.com	+202 37496008 (Ext. 361)

HC Brokerage – Cairo, Egypt		salesandtrading@hc-si.com	
Shawkat El-Maraghy	Managing Director	selmaraghy@hc-si.com	Ext. 200
Mostafa Saad	Local & Gulf Sales	msaad@hc-si.com	Ext. 213
Yasser Mansour	Local & Gulf Sales	ymansour@hc-si.com	Ext. 217
Hossam Wahid	Local & Gulf Sales	hwahid@hc-si.com	Ext. 206
Hassan Kenawi	Local & Gulf Sales	hkenawi@hc-si.com	Ext. 300
Abou Bakr Shaaban	Local & Gulf Sales	ashaaban@hc-si.com	Ext. 238
Nihal Hany	Local & Gulf Sales	nhany@hc-si.com	Ext. 219
Mohamed Helmy	Foreign Sales	mhelmy@hc-si.com	Ext. 207
Ahmed Nabil	Fixed Income Trader	anabil@hc-si.com	Ext. 218

HC Brokerage – Dubai, UAE			
Hassan Aly Choucri	General Manager	hassan.choucri@af-hc.com	+971 4 293 5305
Mohamed Hegazy	Head of Sales	mohamed.hegazy@af-hc.com	+971 4 293 5365
Mohamed Galal	Head of Sales Trading	mohammed.galal@af-hc.com	+971 4 293 5309
Anne Marie Browne	Foreign Institutional Sales	annemarie.browne@af-hc.com	+971 4 293 5301
Richard Frost	Foreign Institutional Sales	richard.frost@af-hc.com	+971 4 293 5302