

**BUY**

Target Price  
KWD0.814

# National Bank of Kuwait (NBK)

## Market Data

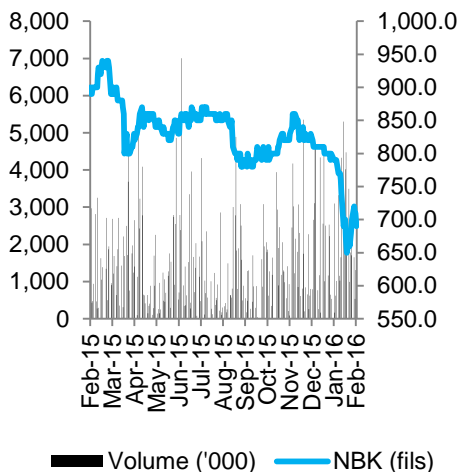
Bloomberg Code:	NBK KK
Reuters Code:	NBKK.KW
CMP (07 Feb, 2016):	0.730
O/S (mn)	5,039.7
Market Cap (KWD mn):	3,679.0
Market Cap (USD mn):	12,229.0
P/E 2016e (x):	11.2
P/BV 2016e (x):	1.3

## Price Performance 1-Yr

High (KWD):	0.905
Low (KWD):	0.650
Average Volume ('000):	1,562

	1m	3m	12m
Absolute (%)	-15.0	-17.1	-21.5
Relative (%)	-3.3	-3.1	3.8

## Price Volume Performance



Source: Bloomberg

Naveed Ahmed, CFA

Senior Manager  
nahmed@global.com.kw  
Tel.: (965) 22951280

Global Investment House  
www.globalinv.net

- Investors need to see beyond the 4Q15 results
- Best positioned to benefit from acceleration in government projects
- Trading close to historic lows in terms on multiples
- Maintain BUY on the stock despite downward revision in FV

NBK, given its sheer size and lending capacity will continue to benefit most from big ticket government projects, which seem to have gained some momentum recently. With a well maintained and constructively high asset quality, quantified by a NPL ratio of 1.3% and coverage ratio of 322%, the bank should be well-considered by investors avoiding riskier banking stocks. It is true that the bank has been a victim of unrelenting provisions and that excessive provision buildup has taken its toll on the bank's ROE (~600bps), some solace can be found in the fact that asset deterioration has a smaller part to play in it. Moving ahead of an extraordinary 2015, loans growth projections for the bank are slightly lower but still in the vicinity of 10% each year. Combine that with NIMs that are seen inching up (average of 6bps yearly) and we are confident of a 4-yr CAGR of 10% in the top-line. Despite high provisions, on the back of our general conservativeness, prodded further by the prevalent economic conditions and slide in the equity markets (requiring collateral top-up calls or higher provisions), we see the bank's bottom-line surging by 17%YoY in 2016e; we also forecast a 4-yr CAGR of 15% in net earnings. We believe that investors need to move beyond the 4Q15 results or at least gauge them in the proper context.

Albeit, the bank is trading at a 2016e PE of 11.2x and P/BV of 1.3x as compared to the Kuwaiti industry average of 11.0x and 1.2x respectively, making it seem fairly valued or slightly expensive in the local context. However, NBK's higher than sector ROE (12.2% vs. 11.8%) should allow it to trade at a premium. The recent market hammering has resulted in NBK trading close to one of its lowest multiples in the last few years and despite our FV cut, it offers a decent upside from current levels. We maintain our BUY rating with the FV at KWD0.814/share, offering an upside of 11.5%.

### NBK's bottom-line declines in 4Q15 driven by one-offs

NBK reported a 6.3%YoY decline in net profit in 4Q15, primarily due to huge jump in provisions (+45.1%YoY) and higher operating expenses (+17.1%YoY). The bank's net and non-interest income rose during the quarter, which partially offset the fall of the bottom-line. Notably, the bank's net interest income including Islamic financing in 4Q15 rose 14.3%YoY, while non-interest income grew 13.4%YoY. Fee income was up by 5.5%YoY. Strong growth in net-interest income was driven by a stable loan growth; furthermore, the bank's NIM improved by 8bps YoY during the quarter. The bank's yield grew 22bps YoY while cost of fund grew 14bps YoY, which resulted in a single-digit rise in NIM.

In 2015, the bank's bottom-line witnessed a 7.8%YoY growth due to growth in the bank's top-line and non-interest income. Net interest income rose 13.0%YoY; non-interest income grew 3.6%YoY. The bank's provisions grew 12.1%YoY in 2015 due to addition of impairment losses on associates (KWD18.5mn) and intangible assets (Kuwait brokerage license, KWD5.4mn). Balance sheet growth of the bank was pretty good during the year with net loans rising 13.8%YoY, while customer deposits increased 7.1%YoY. NBK continued to improve its asset quality ratios with NPL ratio dropping to 1.34% in 2015, down from 1.50% a year earlier, and NPL coverage ratio increasing to 322%, up from 276% in 2014.

Considering the one-offs during the year namely sell-off gain from IBQ (KWD21.9mn, ~KWD16.4mn post-tax), exit costs related to IBQ (KWD4.7mn), impairments in associates and intangibles (KWD23.9mn), loss of income from IBQ (~KWD10mn), the bank did do remarkably well during the year. NBK Board has proposed cash dividends of 30 fils per share and 5% bonus shares in 2015.

### Valuation update – maintain BUY

NBK remains amongst our top picks in Kuwait. We draw comfort from continuation of decent loan growth and strong top-line growth figures as well as double-digit bottom-line growth. Despite an increase in the benchmark interest rates, we remain conservative in our estimates regarding increase in the banking spreads. Presently, the bank is trading at a 2016 P/E of 11.2x and P/BV of 1.3x, as compared to sector average of 11.0x and 1.2x. If we were to adjust NBK's book value to cater for the excessive provisioning, by adding back provisions above coverage of 200% to the book value, the 2016e P/BV would drop to 1.2x. Notably, NBK offers one of the highest 2016e ROEs (12.2%) within our Kuwait banking coverage and ROE is expected to reach at 14.7% by 2019e.

We have slashed down our fair value estimate for NBK from KWD0.985/share to KWD0.814/share following lower net income and hence ROE expectations over the forecast horizon. We maintain **BUY** rating on the stock with an upside potential of 11.5% from the bank's current market price of KWD.730/share as on 07 February, 2016. This is due to significant fall in the bank's stock price recently. We assumed the risk-free rate (US 10- year Treasury yield) at 2.0% and risk premium at 8.6% including country- and stock-specific risk.

#### Income Statement

(KWD mn)	4Q15	4Q14	YoY%	3Q15	QoQ%	2015	2014	YoY%
Interest Income	185.0	157.4	17.5%	174.7	5.9%	691.5	600.6	15.1%
Interest Expense	45.4	35.3	28.5%	40.2	12.9%	161.3	131.2	22.9%
<b>Net Interest Income</b>	<b>139.6</b>	<b>122.0</b>	<b>14.4%</b>	<b>134.5</b>	<b>3.8%</b>	<b>530.2</b>	<b>469.3</b>	<b>13.0%</b>
Fee & Commission Income	32.3	30.7	5.1%	32.2	0.3%	129.8	121.8	6.5%
Investment Income	3.3	6.0	-44.7%	-4.9	-168.1%	31.9	33.1	-3.6%
Other Income	9.6	3.1	205.7%	9.2	4.0%	36.9	36.7	0.4%
<b>Non-Interest Income</b>	<b>45.2</b>	<b>39.9</b>	<b>13.3%</b>	<b>36.4</b>	<b>24.2%</b>	<b>198.6</b>	<b>191.7</b>	<b>3.6%</b>
<b>Total Operating Income</b>	<b>184.8</b>	<b>161.9</b>	<b>14.1%</b>	<b>170.9</b>	<b>8.1%</b>	<b>728.8</b>	<b>661.0</b>	<b>10.2%</b>
Provisions Expense	57.9	40.0	44.8%	36.4	59.1%	164.4	146.7	12.1%
Operating Expenses	61.9	52.9	17.0%	59.4	4.2%	234.7	215.1	9.1%
<b>Profit Before Taxation</b>	<b>65.0</b>	<b>69.1</b>	<b>-5.9%</b>	<b>75.2</b>	<b>-13.6%</b>	<b>329.7</b>	<b>299.3</b>	<b>10.2%</b>
Taxation & Minority Interest	10.6	11.2	-4.8%	10.7	-0.8%	47.5	37.5	26.9%
<b>Net Profit for Parent</b>	<b>54.4</b>	<b>57.9</b>	<b>-6.1%</b>	<b>64.5</b>	<b>-15.7%</b>	<b>282.2</b>	<b>261.8</b>	<b>7.8%</b>

Source: Company Accounts

### 2016e bottom-line estimates revised down

We have revised our estimates for most of the line items from the balance sheet and income statement after the release of the bank's 2015 results and post seeking fresh guidance from the management. We have reduced our 2016e gross loans estimate by 0.5% and deposits estimate by 2.0%, as we believe, due to the falling oil and tighter growth in the economy, lending and deposits growth would be lower than what we estimated previously. Our net interest income forecast stands largely unchanged (reduced by 0.9%) as our loan projections were trimmed slightly. Operating income projection was revised down by 1.8%. We have raised our provision expectations by 47.4% as we assume higher build-up of provisions due to slowdown in the economy. Overall, these revisions result into a 16.8% reduction in the bank's bottom-line for 2016e.

#### Estimates Revision - 2016e

KWD mn	Earlier Estimates	Revised Estimates	% Change
Loans	15,662.3	15,583.8	-0.5%
Deposits	14,166.8	13,882.6	-2.0%
Net Interest Income	597.1	591.9	-0.9%
Operating Income	797.5	782.8	-1.8%
Provisions	101.6	149.8	47.4%
Net Profit	395.4	328.8	-16.8%

Source: Global Research

## Financial Statements

	(KWD mn)	2013	2014	2015	2016e	2017e	2018e	2019e
Income Statement	Interest/Financing Income	563	601	691	796	905	1,027	1,180
	Interest Expense/Payment to Depositors	(112)	(131)	(161)	(204)	(258)	(322)	(397)
	<b>Net Interest/Financing Income</b>	<b>451</b>	<b>469</b>	<b>530</b>	<b>592</b>	<b>647</b>	<b>705</b>	<b>783</b>
	Fee & Commission Income	111	122	130	139	147	159	172
	Investment Income	19	33	32	12	22	28	30
	Other Income	45	37	37	40	43	45	48
	<b>Total Non-Interest/Financing Income</b>	<b>175</b>	<b>192</b>	<b>199</b>	<b>191</b>	<b>212</b>	<b>232</b>	<b>250</b>
	<b>Total Operating Income</b>	<b>626</b>	<b>661</b>	<b>729</b>	<b>783</b>	<b>859</b>	<b>937</b>	<b>1,033</b>
	Provisions expense	(149)	(147)	(164)	(150)	(149)	(139)	(138)
	Operating Expenses	(207)	(215)	(235)	(253)	(274)	(301)	(331)
	<b>Profit Before Taxation</b>	<b>270</b>	<b>299</b>	<b>330</b>	<b>380</b>	<b>436</b>	<b>497</b>	<b>564</b>
	Sale of associate (net)	-	-	-	-	-	-	-
Taxation & Minority Interest	(32)	(37)	(48)	(51)	(59)	(67)	(76)	
<b>Net Profit Attributable to Parent</b>	<b>238</b>	<b>262</b>	<b>282</b>	<b>329</b>	<b>378</b>	<b>430</b>	<b>488</b>	
Balance Sheet	Cash Balances	2,412	3,132	3,481	3,722	3,996	4,730	5,056
	Deposits with Banks & FIs	900	2,051	1,427	1,284	1,310	1,113	946
	Investment Securities	3,205	3,373	3,968	4,289	4,536	4,707	5,019
	Gross Loans & Financings	11,131	12,423	14,164	15,584	17,095	18,954	21,246
	Loan Loss Reserve	(435)	(515)	(613)	(742)	(881)	(1,008)	(1,136)
	Net Loans & Financings	10,695	11,909	13,551	14,841	16,214	17,946	20,110
	Investment in Associates	260	119	93	94	95	96	96
	Investment Properties	-	-	-	-	-	-	-
	Net Fixed Assets	192	203	227	245	264	285	308
	Other Assets	936	997	851	868	888	909	932
	<b>Total Assets</b>	<b>18,600</b>	<b>21,784</b>	<b>23,598</b>	<b>25,343</b>	<b>27,302</b>	<b>29,786</b>	<b>32,468</b>
	Deposits from Banks & FIs	4,945	6,706	7,306	7,672	8,055	8,458	8,881
	Deposits from Customers	10,719	11,935	12,714	13,883	15,203	16,983	18,891
	Other Borrowings	-	-	335	335	335	335	335
	Other Liabilities	359	414	409	445	488	532	594
	Paid-up Capital	457	480	504	529	529	529	529
	Retained Earnings	934	1,018	1,107	1,253	1,447	1,680	1,944
	Other Reserves	983	1,014	996	984	984	984	984
	Shareholders' Equity	2,374	2,512	2,607	2,766	2,959	3,193	3,457
	Minority Interest	203	217	224	242	262	284	310
<b>Total Equity &amp; Liability</b>	<b>18,600</b>	<b>21,784</b>	<b>23,598</b>	<b>25,343</b>	<b>27,302</b>	<b>29,786</b>	<b>32,468</b>	
Ratio Analysis	Return on Average Assets	1.4%	1.3%	1.2%	1.3%	1.4%	1.5%	1.6%
	Return on Average Equity	10.2%	10.7%	11.0%	12.2%	13.2%	14.0%	14.7%
	Recurring Income/Operating Income	89.8%	89.4%	90.6%	93.4%	92.5%	92.2%	92.4%
	Interest Earning/Financing Assets Yield	4.0%	3.7%	3.8%	4.0%	4.2%	4.4%	4.7%
	Cost of Funds	0.8%	0.8%	0.8%	1.0%	1.1%	1.3%	1.5%
	Net Spread	3.2%	3.0%	2.96%	3.03%	3.07%	3.12%	3.20%
	Cost to Income Ratio	33.1%	32.5%	32.2%	32.4%	31.9%	32.1%	32.1%
	Net Loans to Customer Deposits	99.8%	99.8%	106.6%	106.9%	106.7%	105.7%	106.5%
	Non Performing Loans	218	186	190	203	239	265	297
	Loan Loss Reserve	435	515	613	742	881	1,008	1,136
	NPLs to Gross Loans	2.0%	1.50%	1.3%	1.3%	1.4%	1.4%	1.4%
	NPL Coverage	199.8%	276.1%	322.4%	366.5%	367.9%	379.8%	381.8%
	Provisions/Total Income	23.8%	22.2%	22.6%	19.1%	17.3%	14.8%	13.4%
	Cost of Risk (bps)	134	115	98	87	84	71	64
	Equity to Gross Loans	21.3%	20.2%	18.4%	17.7%	17.3%	16.8%	16.3%
	Equity to Total Assets	12.8%	11.5%	11.0%	10.9%	10.8%	10.7%	10.6%
	DPS (fils)	30.0	30.0	30.0	30.0	32.5	35.0	40.0
	Dividend Yield	3.9%	3.8%	5.3%	4.1%	4.4%	4.8%	5.5%
	Dividend Payout Ratio	56.5%	54.0%	52.6%	48.2%	45.5%	43.0%	43.4%
	Adjusted EPS (fils)	49.6	54.5	58.8	68.5	78.7	89.7	101.6
Adjusted BVPS (fils)	471.1	498.4	517.4	548.8	587.2	633.5	685.9	
Market Price (fils) *	890.0	910.0	650.0	730.0	730.0	730.0	730.0	
P/E Ratio (x)	18.8	17.5	11.6	11.2	9.7	8.5	7.5	
P/BV Ratio (x)	1.7	1.7	1.3	1.3	1.2	1.2	1.1	

Source: Company Reports & Global Research

\* Market price for 2016 and subsequent years as per closing prices on KSE on 07 February, 2016

## Disclosure

The following is a comprehensive list of disclosures which may or may not apply to all our researches. Only the relevant disclosures which apply to this particular research has been mentioned in the table below under the heading of disclosure.

### Disclosure Checklist

Company	Recommendation	Bloomberg Ticker	Reuters Ticker	Price	Disclosure
National Bank of Kuwait	BUY	NBK KK	NBKK.KW	KWD0.730	1,10

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BUY	Fair value of the stock is between +10% and +20% from the current market price
HOLD	Fair value of the stock is between +10% and -10% from the current market price
SELL	Fair value of the stock is < -10% from the current market price

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**Global Investment House**Website: [www.globalinv.net](http://www.globalinv.net)

Global Tower

Sharq, Al-Shuhada Str.

Tel. + (965) 2 295 1000

Fax. + (965) 2 295 1005

P.O. Box: 28807 Safat, 13149 Kuwait

**Research**

Naveed Ahmed, CFA  
(965) 2295-1280  
[nahmed@global.com.kw](mailto:nahmed@global.com.kw)

**Wealth Management**

Rasha Al-Qenaei  
(965) 2295-1380  
[alqenaei@global.com.kw](mailto:alqenaei@global.com.kw)

**Global Kuwait**

Tel: (965) 2 295 1000  
Fax: (965) 2 295 1005  
P.O.Box 28807 Safat, 13149  
Kuwait

**Global Bahrain**

Tel: (973) 17 210011  
Fax: (973) 17 210222  
P.O.Box 855 Manama, Bahrain

**Global UAE**

Tel: (971) 4 4477066  
Fax: (971) 4 4477067  
P.O.Box 121227 Dubai,  
UAE

**Global Egypt**

Tel: (202) 24189705/06  
Fax: (202) 22905972  
24 Cleopatra St., Heliopolis, Cairo

**Global Saudi Arabia**

Tel: (966) 1 2994100  
Fax: (966) 1 2994199  
P.O. Box 66930 Riyadh 11586,  
Kingdom of Saudi Arabia

**Global Jordan**

Tel: (962) 6 5005060  
Fax: (962) 6 5005066  
P.O.Box 3268 Amman 11180,  
Jordan

**Global Wealth Manager**E-mail: [contactus@global.com.kw](mailto:contactus@global.com.kw)

Tel: (965) 1-804-242