Equity Research report
SNB AB Equity
7 August 2023

Target Price: SAR50/share
Current Price: SAR37.15/share
Upside: 34.5% (+Div. Yield: 5.4%)
Rating: Overweight

Saudi National Bank

Due for a reversal. Initiate with a TP of SAR50/sh.

- SNB has underperformed the KSA Banking sector in the last two years for reasons we believe are done and is likely set up for a reversal.
- In terms of valuation multiples, from a premium of 27% till mid-2021, the stock trades at a discount of 18% to the benchmark KSA banks index, which is unjustified in our view.
- We value the bank at SAR50/share using an equal weightage of residual income method and relative valuation (1.5x P/B) and initiate SNB with an Overweight rating.

Due for a catch-up: Even before acquiring a 9.88% stake in Credit Suisse (CS; post which SNB declined 16%), the merger with Samba resulted in SNB underperforming the KSA banks index. The underperformance was partly justified given weak results in 2021 and later drop in CS share price. However, we believe negatives are behind us because: 1) SNB's growth has recovered, with loans up 6% YTD (~10% for 2023e). 2) With a blended mix of different loan types, MINs are fully yet to pick up as seen in corporate banks. 3) With 1/3 of IEA in investments, rate softening could reverse or at least stabilize OCI weakness. 4) Macro-wise, oil prices are better positioned with the OPEC+ supply cuts, and historical data suggest its strong correlation with SNB share prices. 5) SNB has a liquidity comfort of an L/D of 96% in 2Q23. 6) Given its size, SNB would be naturally at the forefront of Vision 2030 initiatives/giga projects, which are picking pace.

Reversal of multiples too: SNB traded at a 27% premium to the KSA Banks index till the first half of 2021. However, currently, this has reversed to a discount of 18% to the broader banking index. At this valuation, we believe the worst is already priced in, and any growth return as such will help the bank in outperformance. SNB has a healthy blend of retail (53% as of 2Q23) and corporate (39%) loan mix. Opex is also under control, with a reported cost-to-income ratio of 27% in 1H23 vs 38% at the end of 2021. We forecast a RoE of 12.2% (ROTE: ~16%) in 2023.

Risks: Downside risks include slower loan growth due to adverse economic conditions, further increase in interest rates/cost of funds impacting NIMs, exposure to international investments

Figure 1: Key financial metrics

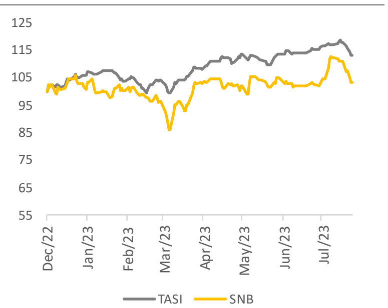
SARmn	2022a	2023e	2024e	2025e
Net Special Commission Income	26,286	28,351	33,806	35,635
y/y growth	*18.8%*	*7.9%*	*19.2%*	*5.4%*
NIM Margin	*3.1%*	*3.1%*	*3.4%*	*3.3%*
Fee & other income	6,717	7,765	8,552	8,650
Total operating Income	33,003	36,117	42,358	44,285
Net income	18,581	20,731	24,244	25,447
EPS (SAR)	4.1	3.3	3.9	4.1
DPS (SAR)	1.6	1.9	2.0	2.1
Net loans and advances	545,311	599,577	656,755	710,321
Customers deposits	568,283	631,002	693,884	751,172
BVPS (SAR)	27.7	29.0	31.3	33.5
NPL Coverage Ratio	127%	135%	135%	135%
Capital Adequacy Ratio	19.0%	21.8%	21.9%	22.0%
COR (bps)	32	31	41	40

Source: Company Data, GIB Capital

Stock data	
TASI ticker	1180
Mcap (SARmn)	222,903
Trd. Val (3m) (SARmn)	183.5
Free float	62.7%
QFI holding	14.1%
TASI FF weight	7.00%

Source: Bloomberg

Prices indexed to 100



Source: Bloomberg

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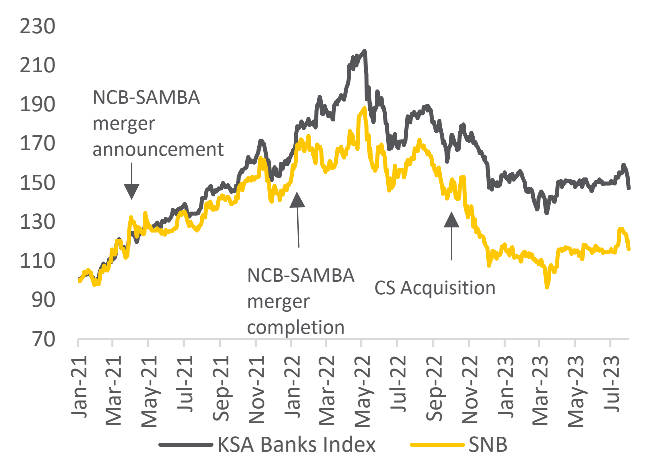
Investment case

1. **Impact of 10% stake in CS:**

SNB acquired a 9.88% stake in CS for SAR5.5bn in November 2022. By the end of FY22, the value of SNB's investment in CS had declined by nearly 20%, and by the end of 1Q23, it was down further by approximately 70%. As a result, the carrying value of the CS investment on SNB's balance sheet at the end of 1Q23 reduced to SAR1.3bn and constituted 0.5% of SNB's 1Q23 investment portfolio of SAR264bn. The CS meltdown resulted in a decline in SNB's equity by nearly SAR3.1bn in 1Q23; however, no financial impact was recognized in the income statement as the bank made an irrevocable election. Post completion of the merger between CS and UBS on 12 June 2023, SNB derecognized its investment in CS by charging the fair value loss within the retained earnings and has started accounting for its investment in UBS (SAR1.3bn as of 2Q23; 0.5% in UBS) as held at fair value through other comprehensive income (FVOCI).

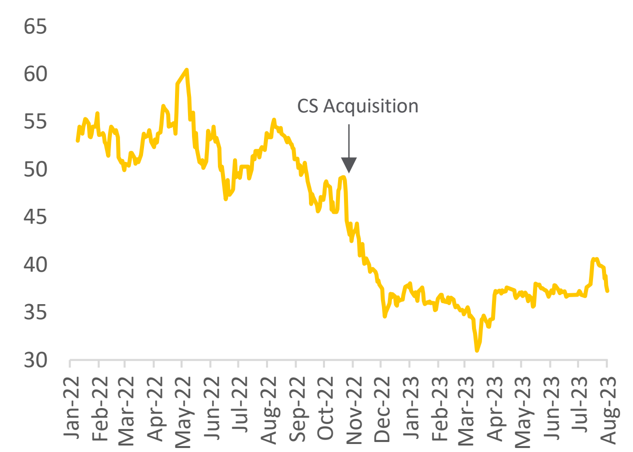
Since the CS deal was announced, SNB share prices have underperformed compared to the KSA banks index. SNB's market capitalization on 25 October 2022 (deal announcement date) was SAR286bn, which has fallen by 22% to SAR224bn as of 06 August 2023. However, as the CS concerns have abated in recent months after the completion of the UBS-CS merger, a rerating in SNB's share price is expected.

Figure 2: Price performance comparison (indexed to 100)



Source: Bloomberg

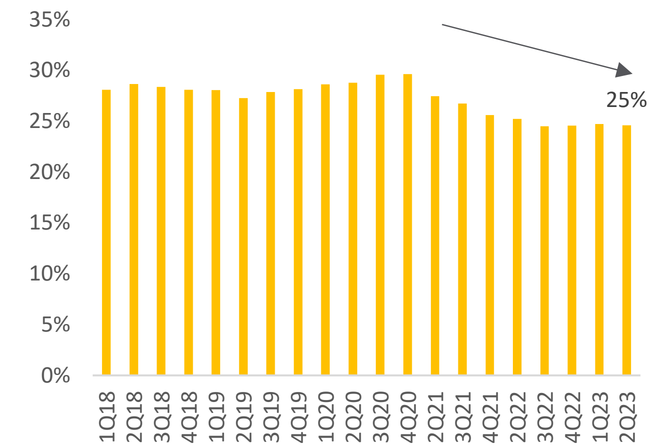
Figure 3: SNB share price (SAR)



Source: Bloomberg

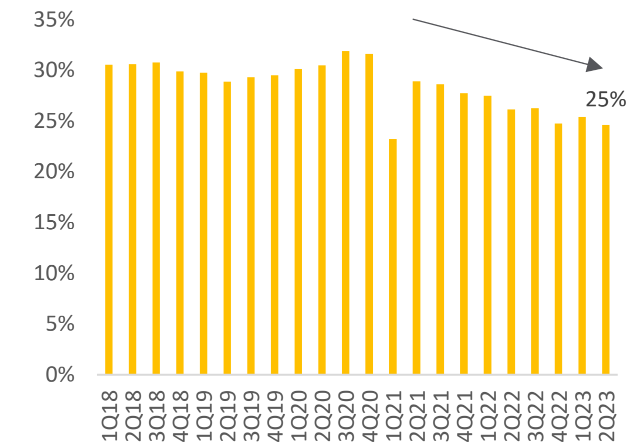
The market share of SNB (post-merger of NCB with Samba, 1Q23) in terms of deposits fell to 25% from the pre-merger (proforma as of 4Q20) market share of 32%. Similarly, the loan market share (post-merger) has also fallen to 25% from the pre-merger (proforma as of 4Q20) market share of 30%. However, the integration between the banks is now nearly complete, with merger synergies expected to be realized. We expect a turnaround in both loan and deposit market share, given SNB's industry leadership position. We expect SNB's loan to grow at a CAGR of 6% between 2022 and 2030, while deposits to grow at a CAGR of 7% during the same period.

*Figure 4: SNB's loan market share**



*Source: Company Data; *Includes NCB+SAMBA data except for 1Q21*

*Figure 5: SNB's deposit market share**

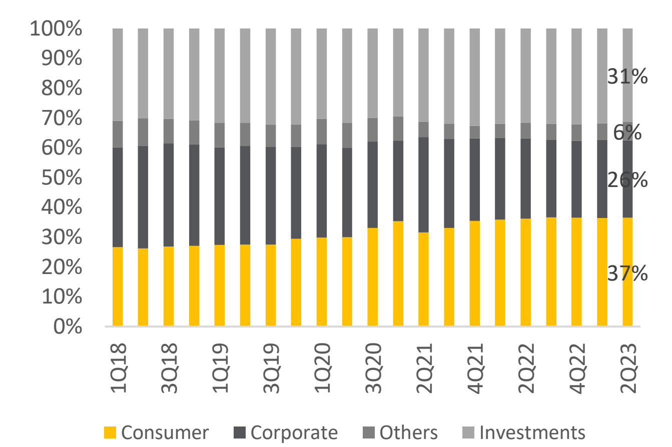


*Source: Company Data; *Includes NCB+SAMBA data except for 1Q21*

2. Reversal/Stabilization of OCI

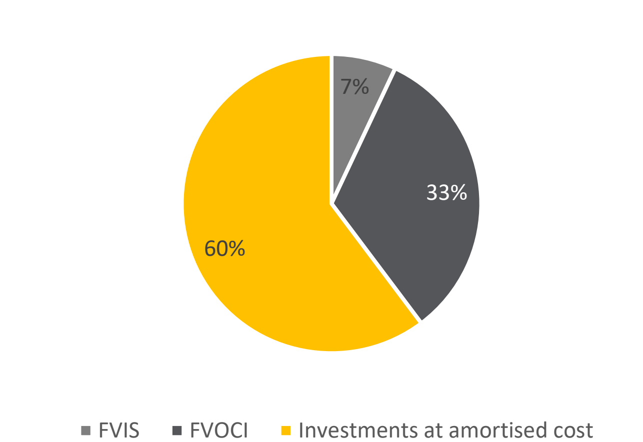
The group's investments form almost a third of its interest-earnings assets (IEA). The composition of IEA is nearly a balanced split between consumer loans, corporate loans, and investments.

Figure 6: Interest Earnings Assets of SNB



Source: Company Data

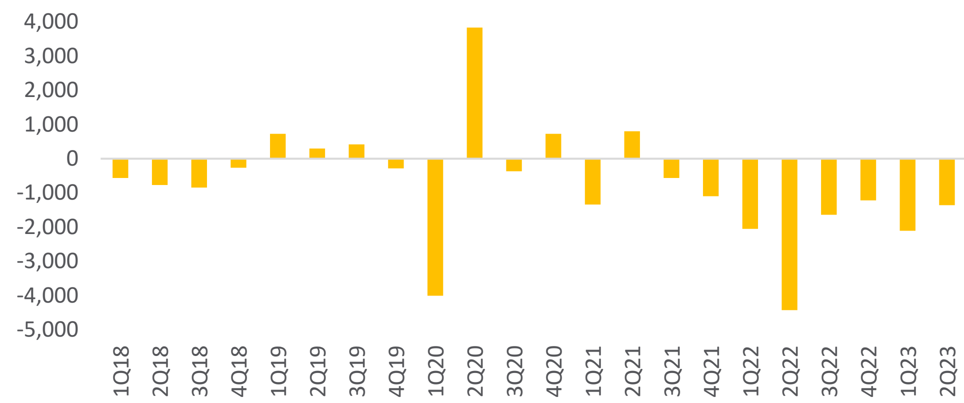
Figure 7: Investments assets split in 2Q23



Source: Company Data

SNB has witnessed rising losses (OCI) from its FVOCI investments, which comprise 31% of its investment portfolio. As and when the market conditions turn favorable (decline in rates), the losses could reverse and hence boost equity value, in our view.

Figure 8: SNB's other comprehensive income/ loss (SARmn)

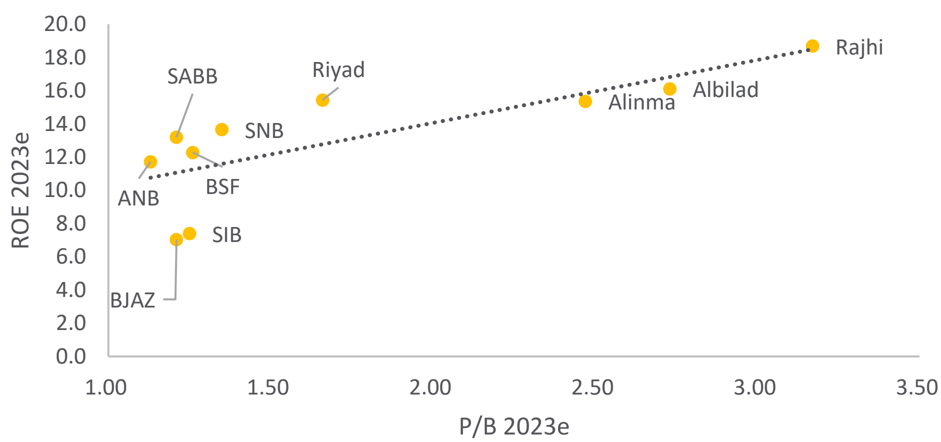


Source: Company Data

3. Attractive valuation

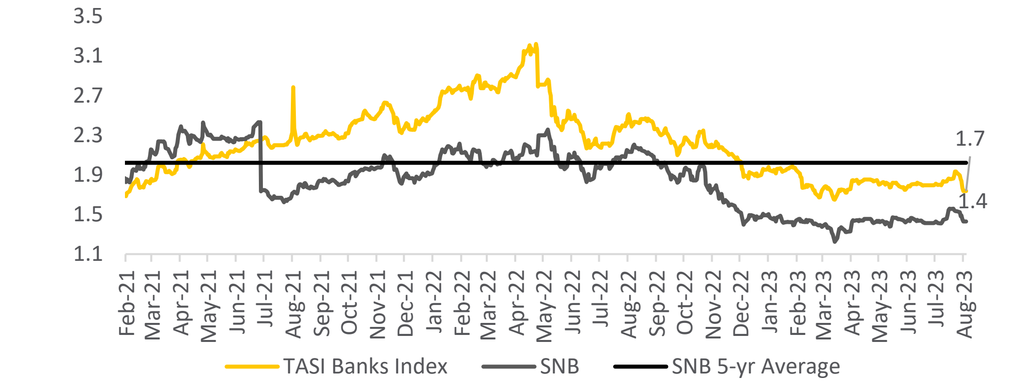
According to Bloomberg, SNB was trading at a premium of 27% to the KSA banks benchmark index till the first half of 2021. Post that, SNB's stock was repriced since it managed only single-digit loan growth compared to mostly double-digit growth for its peers and CS deal. Now, with a healthy ROE, it is priced reasonably at a price/ book value of 1.4x (Figure 10) compared to a 5-year average of 2x. We believe the repricing, which was caused due to multiple factors, could reverse with better guidance and a favorable rate environment.

Figure 9: Price to Book value versus Return on Equity



Source: Bloomberg. As of 03 August 2023

Figure 10: SNB Price to Book multiple comparisons with KSA Banks Index



Source: Bloomberg

4. Improved guidance

SNB upgraded its loan growth guidance for 2023 to low double-digits, up from high single-digits at the end of 2022. The bank expects corporate loans to outpace retail loans, which can be a positive given the faster repricing of such loans. SNB expects only 1-3bps pressure on NIMs for every 25bps rate increase. The group also expects a positive impact of higher interest rates, which are expected to peak in 2023.

Figure 11: SNB guidance change

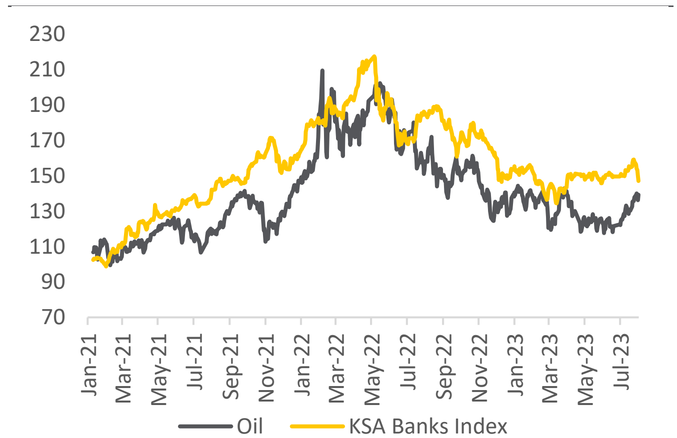
Guidance	FY22a	1H23a	2023e	
			Earlier Guidance	Revised Guidance
Loan growth	10%	+6%	High single-digit	Low double-digit
NIM	3.15%	3.11%	3.2% - 3.3%	3.0%-3.2%
Cost-to-income*	27.7%	27%	Below 27%	Below 27%
Cost of Risk	33	20bps	30-50bps	30-50bps

*Source: Company Data, * excl. goodwill amortization*

5. Oil prices vs SNB

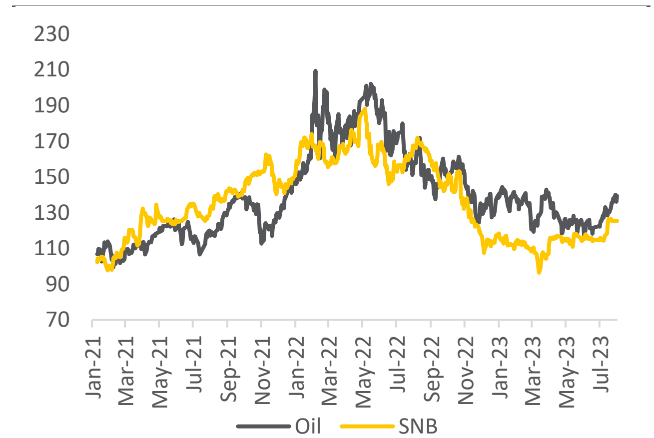
Over the past decade, the performance of KSA's banking sector has closely tracked crude oil prices. During high oil prices, lending and deposit volumes have expanded, leading to strong performance for the banking sector. In recent quarters, the KSA banks index has largely outperformed the oil prices (Figure 12), but SNB prices have underperformed (Figure 13), indicating room for repricing in the share price.

Figure 12: Oil vs. Banks Index



Source: Bloomberg

Figure 13: Oil vs. SNB

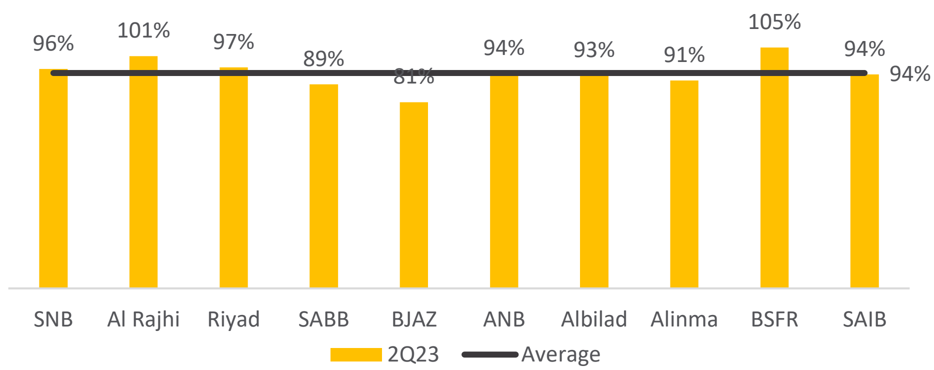


Source: Bloomberg

6. **LDR**

SNB has a strong liquidity profile, with a loan-to-deposit ratio (LDR) standing at 96% at the end of 2Q23, above the industry average of 94%. This indicates that the bank can expand its loan portfolio. Due to the high-interest rate environment, the recent growth in time deposits at the sector level is expected to weigh negatively on the funding cost. The group has been guided to acquire market share in both loans and deposits.

Figure 14: LDR

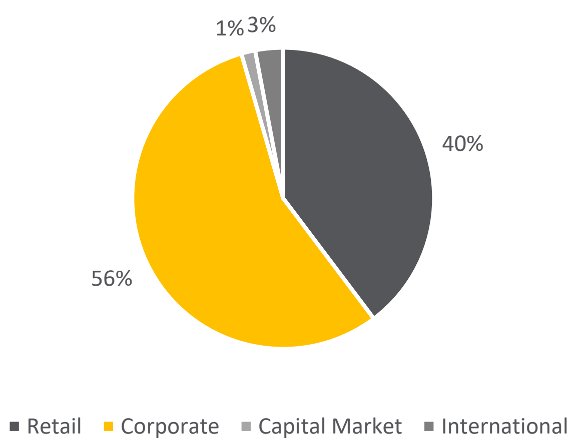


Source: Company

7. **A blend of retail and corporate bank**

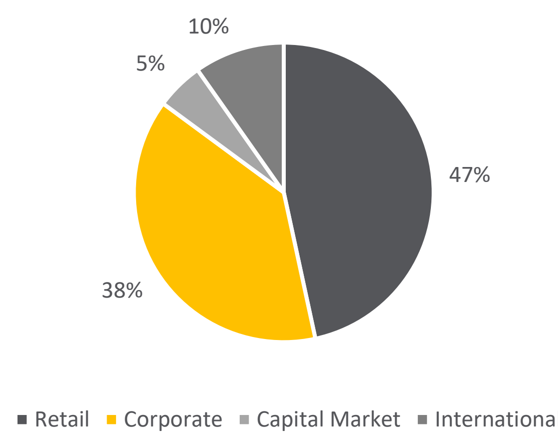
At the end of 2Q23, corporate exposure accounted for 56% of the total assets, while retail exposure stood at 40%. Meanwhile, the share of retail and corporate segments in total operating income remained at 47% and 38%, respectively. The rate hike environment is expected to underpin SNB's earnings because of healthy corporate exposure and investment book.

Figure 15: Asset Mix in 2Q23



Source: Company Data

Figure 16: Operating income by segment in 2Q23



Source: Company Data

Valuation and risks

We have used two valuation approaches to arrive at our final target price.

Residual income method: In this approach, we derive the fair value for the bank using a combination of the present value of the residual income (cost of equity: 9.5%; terminal growth: 4%) over 2024-30e and current book value to arrive at a fair value of SAR50/share.

Key Assumptions

Figure 17: Key Assumptions for GIB capital forecasts

	2023e	2024e	2025e	2026e
Loan Growth	10%	9.5%	8.2%	6.5%
Cost of Risk (bps)	31	41	41	40
NIM	3.14%	3.42%	3.33%	3.22%
SAIBOR (%)	5.90	5.72	4.65	3.96

Source: GIB Capital

Figure 18: Residual Income calculations

SAR mn	**2023e**	**2024e**	**2025e**	**2026e**	**2027e**	**2028e**	**2029e**	**2030e**
Net Income	20,731	24,244	25,447	26,079	27,494	29,310	30,205	31,832
Equity charge	16,548	17,850	19,101	20,262	21,357	22,386	23,305	24,271
Residual income	4,183	6,393	6,346	5,817	6,137	6,924	6,900	7,561
Discounted Value	4,032	5,627	5,101	4,270	4,114	4,239	3,857	3,860
Total Discounted Value	38,237							
Current Book Value	174,192							
Terminal Value	142,966							
Discounted Terminal Value	72,987							
Equity value	285,415							
Fair value per share (SAR)	**48**							
Adjusted Fair value per share (SAR)	**50**							
Cost of Equity (Ke)	9.5%							
Terminal or perpetual growth rate (g)	4.0%							

Source: GIB Capital

Figure 19: Sensitivity analysis of Residual Income valuation

		Cost of Equity				
		8.5%	**9.0%**	**9.5%**	**10.0%**	**10.5%**
Terminal Growth	**3.0%**	57	52	48	45	41
	3.5%	59	54	49	45	42
	4.0%	62	55	**50**	46	42
	4.5%	65	57	52	47	43
	5.0%	68	60	53	48	44

Source: GIB Capital

Relative valuation: Using P/B for its peers of 1.5x with a 2024 BVPS of SAR31.3/share, we arrive at a fair value of SAR50/share.

Figure 20: Relative valuation

Relative Valuation	
BVPS 2024E (SAR)	31.3
Target P/BV Multiple for 2024E (x)	1.50x
Fair value per share (SAR) - P/BV Multiple	47
Adjusted Fair value per share (SAR) - P/BV Multiple	**50**

Source: GIB Capital

Figure 21: Sensitivity analysis of relative valuation

		BVPS				
		28.3	**29.8**	**31.3**	**32.9**	**34.5**
P/B(x)	**1.3x**	39	41	43	45	47
	1.4x	42	44	46	49	51
	1.5x	45	47	**50**	52	55
	1.6x	48	50	53	56	58
	1.7x	51	53	56	59	62

Source: GIB Capital

Figure 22: Peer valuations

	Mkt Cap (USDmn)	Free Float (%)	P/E		P/B		Dividend Yield		ROE	
			2023e	2024e	2023e	2024e	2023e	2024e	2023e	2024e
SNB	59,613	62.4	11.3	9.6	1.3	1.2	5.0	5.4	12.2	13.4
Rajhi	76,176	100.0	17.3	15.2	3.2	2.8	2.8	3.5	18.7	19.6
Riyad	24,325	51.1	11.4	10.8	1.7	1.5	4.4	4.7	15.4	15.2
BJAZ	3,985	90.0	17.7	14.6	1.2	1.2	2.5	2.7	7.0	8.1
BSFR	12,438	73.8	10.7	10.2	1.3	1.2	5.1	5.5	12.3	11.9
Alinma	19,204	90.0	16.3	15.0	2.5	2.3	3.3	3.7	15.4	15.7
ANB	10,342	44.4	10.1	9.9	1.1	1.1	5.3	5.6	11.7	10.6
SABB	19,073	48.7	10.2	9.6	1.2	1.1	5.4	5.7	13.2	13.0
Albilad	11,149	53.9	18.1	16.0	2.7	2.4	1.4	1.7	16.1	16.0
SIB	4,673	74.4	10.3	9.4	1.3	1.2	4.1	4.6	7.4	7.5
Mean	**24,098**	**68.9**	**13.4**	**12.1**	**1.7**	**1.6**	**3.9**	**4.2**	**13.1**	**13.2**
Median	**15,755**	**68.1**	**11.4**	**10.7**	**1.3**	**1.2**	**4.2**	**4.6**	**13.4**	**13.5**

Source: Bloomberg

Blended valuation: We arrive at a blended target price of SAR50/share by assigning an equal weightage to both valuation methods.

Figure 23: Weighted Average Fair Value

Valuation Method	Adj. FV/share (SAR)	Weightage	Weighted value per share (SAR)
Residual income	50	50.0%	25.1
Relative Valuation - P/B	50	50.0%	24.8
Target Price (SAR)			**50.0**
CMP (SAR), 06 Aug 2023			37.15
Upside/(Downside)			**34.5%**

Source: GIB Capital

Key Risks

1. **Slower loan growth due to adverse economic conditions**
   The broader global macroeconomic environment remains uncertain. The Central Banks have signaled toward further rate hikes if inflation remains persistently above the target rates. Considering such an effect is seen with a lag, it is likely that in 2023 or beyond, loan growth could slow down and impact SNB's attempts to acquire market share.

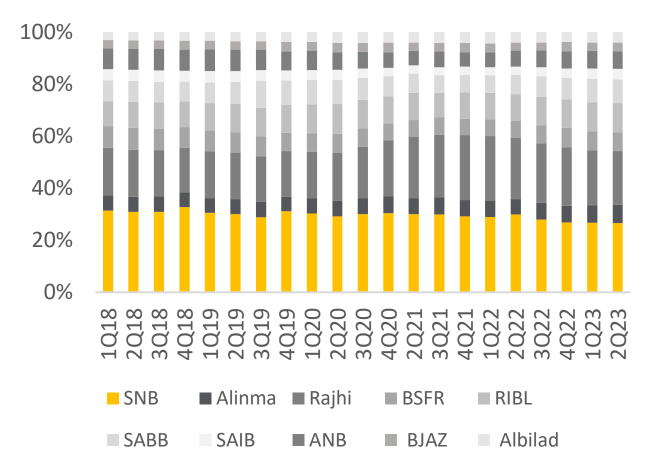
2. **Rising interest rates may increase the cost of funds, impacting NIMs**
   The continued higher interest rate environment has resulted in the cost of funds outpacing the asset yields of all the banks. If banks cannot pass these higher costs to borrowers, their NIMs will be squeezed. NIM compression was also one reason SNB lost its valuation premium over peers in 2022. If NIMs continue to be lower, it will be a key risk to turnaround expectations.

3. **Credit Suisse's failure highlights the risks of international investments**
   SNB’s investment failure in Credit Suisse has highlighted the risks of international investments. SNB also has exposure to Pakistan and Turkey, where macroeconomic and regulatory trends remain key to monitor. The economic value of these investments may not be significant given the size of the SNB's investment portfolio; however, any downturn in these portfolios could further dampen investor sentiment.

SNB in charts

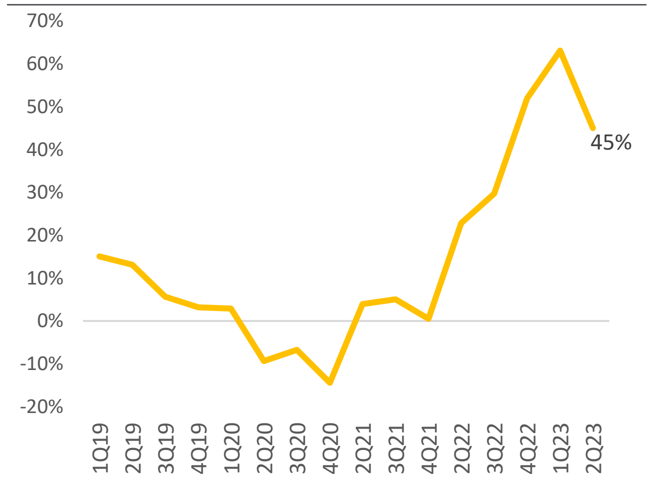
SNB is the largest bank in KSA in terms of share of interest income, both gross and net. Nearly half of the group's net income before zakat comes from corporate business, even though most of its loans are retail. SNB also has exposure to international markets, which accounted for 8% of the group's net income before zakat. In terms of non-performing loans (NPLs), consumer loans have performed better than corporate or international businesses.

Figure 24: Gross interest income market



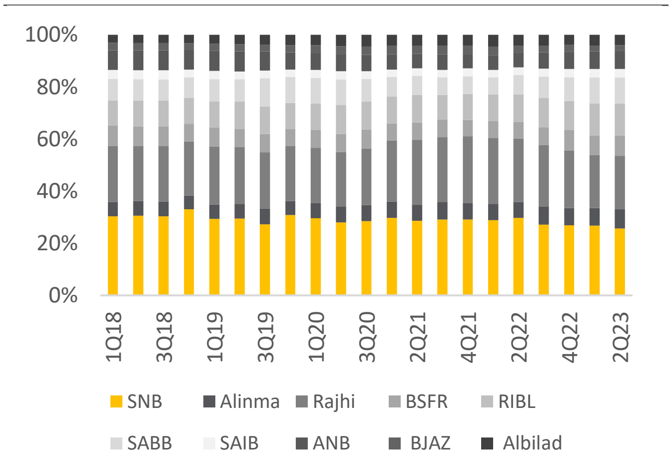
Source: Company Data

Figure 25: SNB interest income growth (y/y)



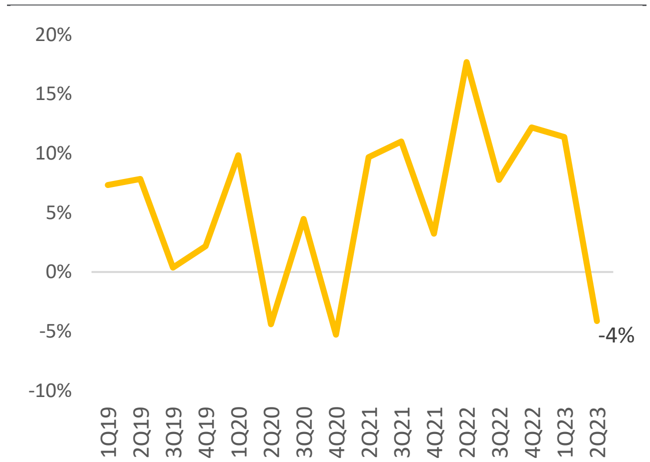
Source: Company Data

Figure 26: Net interest income market share



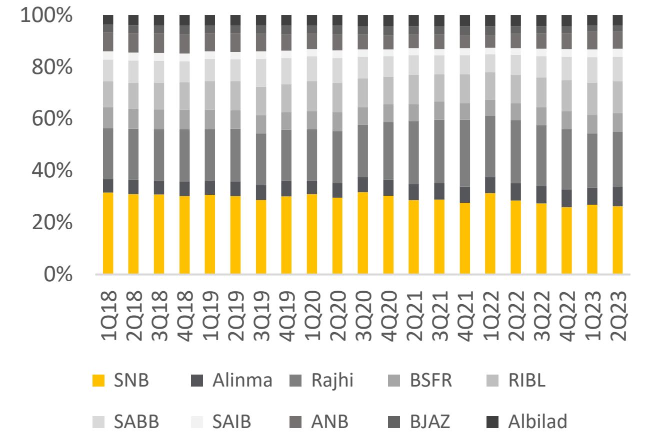
Source: Company Data

Figure 27: SNB net interest income growth (y/y)



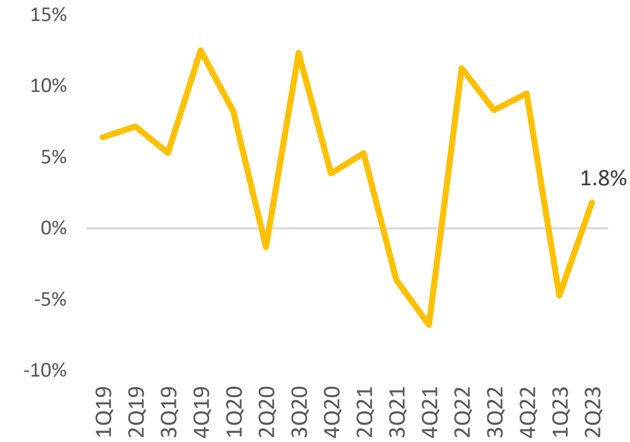
Source: Company Data

Figure 28: Operating income market share



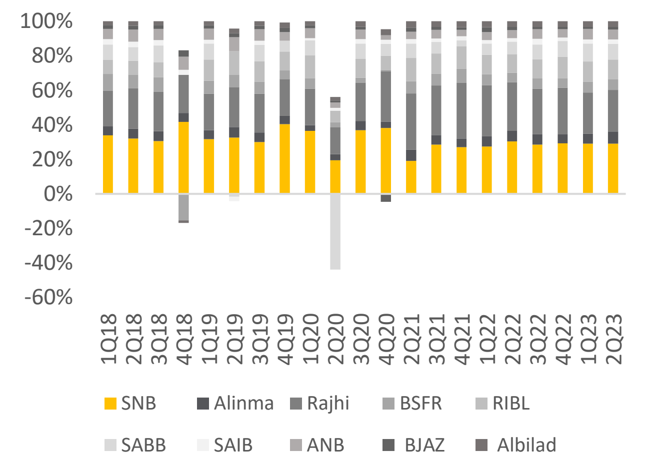
Source: Company Data

Figure 29: Operating income growth (y/y)



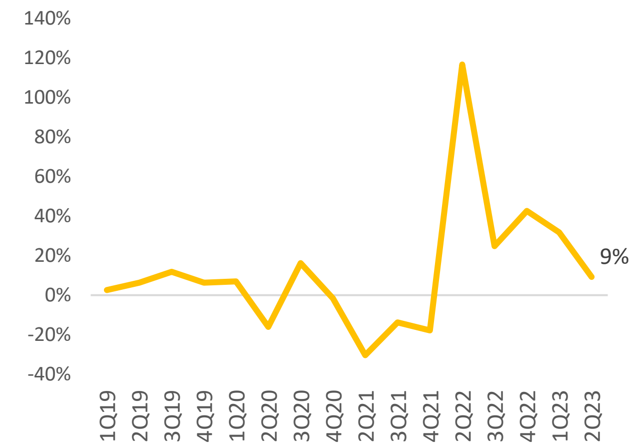
Source: Company Data

Figure 30: Net income market share



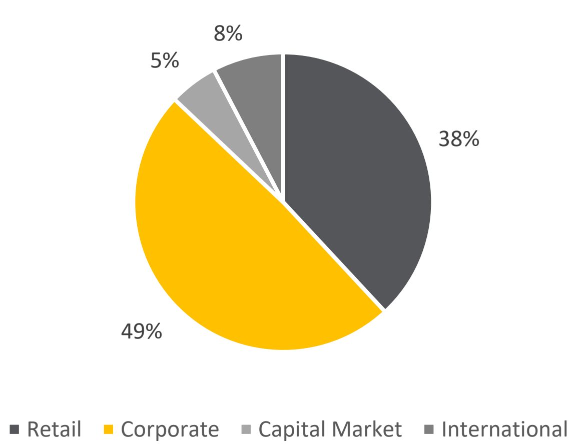
Source: Company Data

Figure 31: Net income growth rate (y/y)



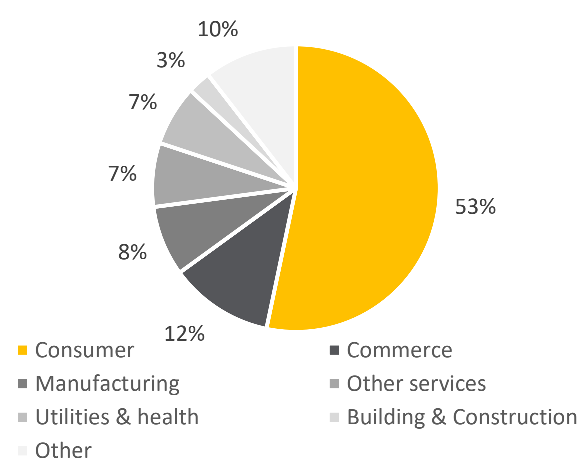
Source: Company Data

Figure 32: Net income before zakat by segment in 2Q23



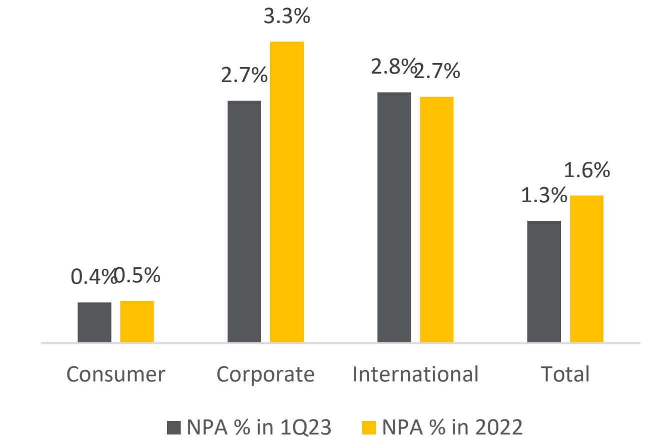
Source: Company Data

Figure 33: Loan exposures by sector in 2Q23



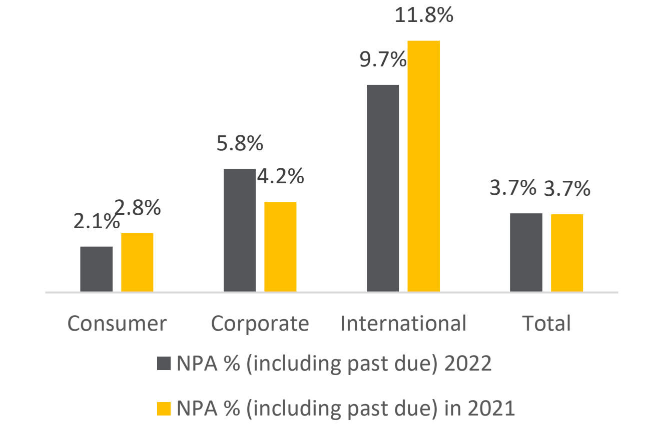
Source: Company Data

Figure 34: NPA by loan type – 2Q23



Source: Company Data

Figure 35: NPA by loan type excluding impaired - 2022

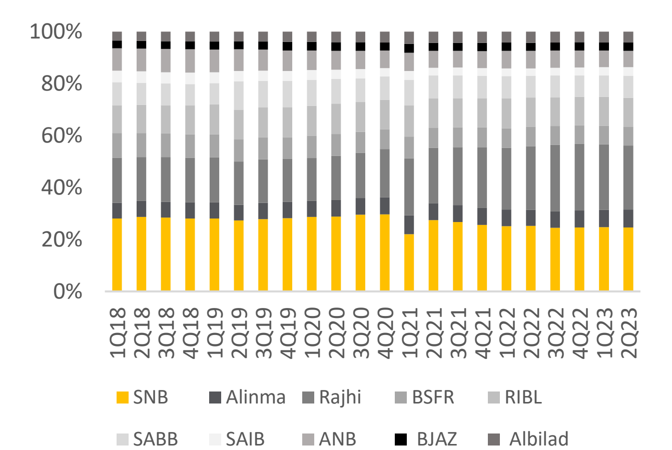


Source: Company Data

Second largest loan book in the market

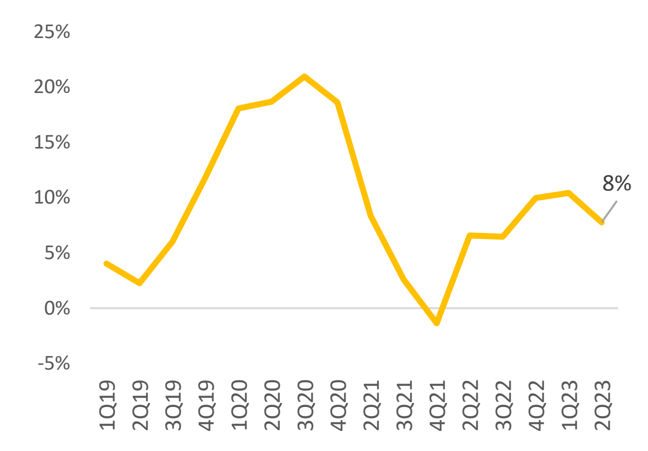
SNB is the second-largest bank in KSA by loan book size after Al Rajhi. SNB's exposure to retail loans is higher than corporate loans. In recent quarters, consumer loan book growth has outpaced corporate loan growth, driven by the growth of mortgages. This is due to the strong housing demand in KSA. However, going forward, corporate loan growth is expected to exceed retail loan growth. This is primarily due to slowing mortgage loans amid a higher interest rate environment and subsidy-related changes. In the current interest rate environment, we believe banks with considerable corporate exposure benefit more than dominant retail ones, as corporate loans get repriced sooner than retail loans or mortgages. SNB is expected to be a beneficiary of such repricing.

Figure 36: SNB loan market share*



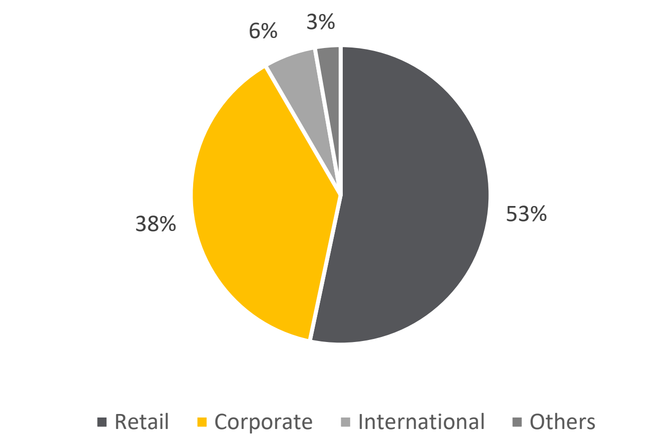
*Source: Company data; *Historical data includes NCB+SAMBA loan books except 1Q21*

Figure 37: SNB loan growth (y/y)



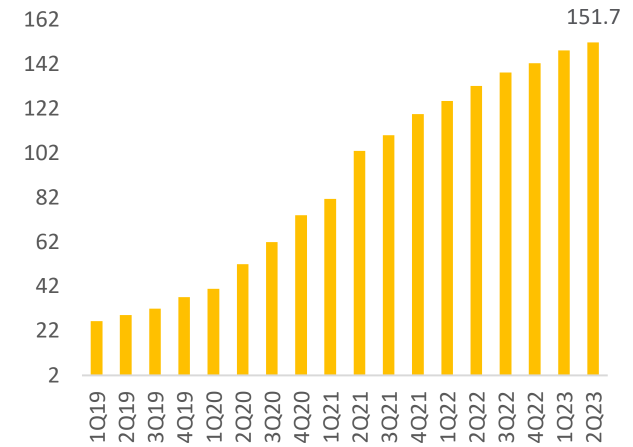
Source: Company data

Figure 38: SNB loan book by type – 2Q23



Source: Company Data

*Figure 39: SNB mortgage loans development (SARbn)**

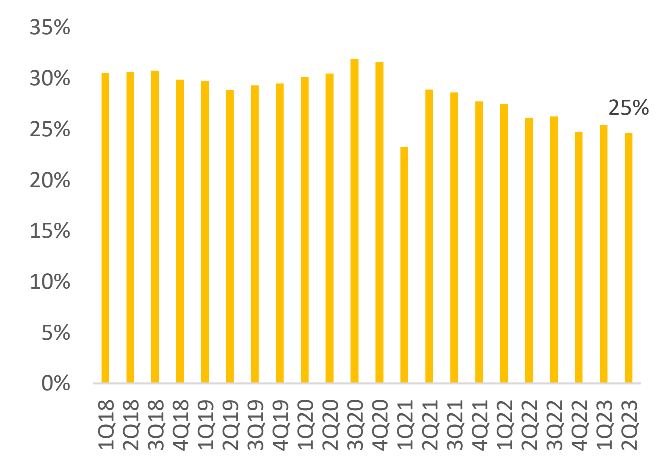


*Source: Company Data; *Historical data includes NCB+SAMBA loan books except 1Q21*

Strong deposit base, but deposit growth slowing in the near term as part of industry trend

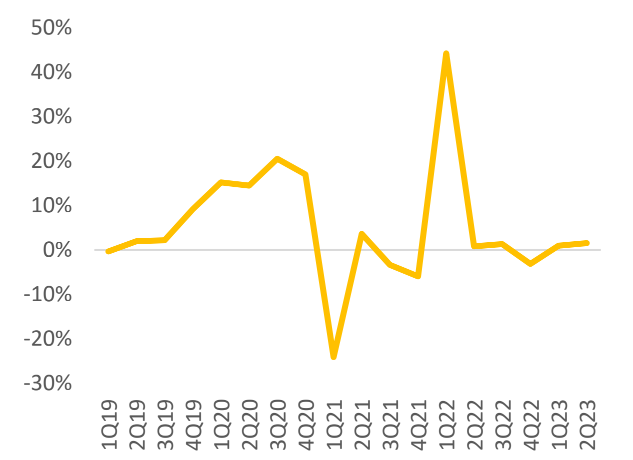
Since the start of 2021, SNB has seen an increase in deposit flow. This has helped the bank to improve its market share from 23% to 25% in 2Q23. SNB has also seen a spike in its cost of funds as deposit growth has outpaced loan growth in 1H23. Additionally, the gradual change in the deposit mix towards time deposits is also leading to an increase in the cost of funds. Despite the rise in the cost of funds, SNB's healthy balance of corporate loans is expected to bolster the bank's net interest income in the coming quarters.

*Figure 40: Deposit market share**



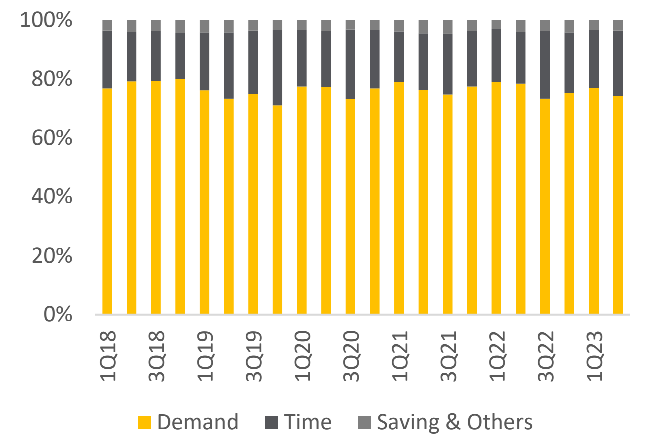
*Source: Company Data; *Historical data includes NCB+SAMBA deposits except 1Q21 which are causing a dip*

Figure 41: SNB deposit growth (y/y)



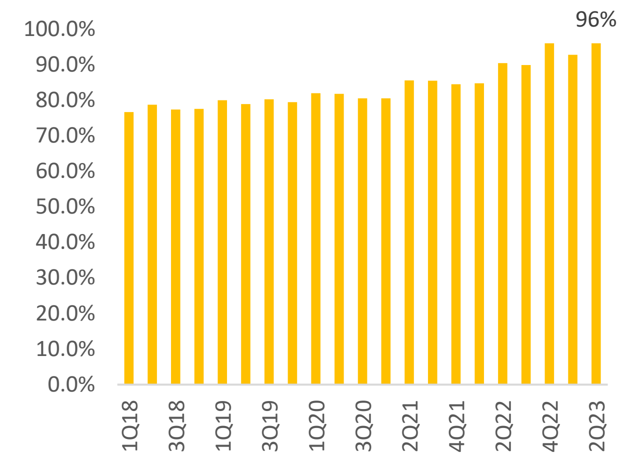
Source: Company data

Figure 42: SNB deposit by type



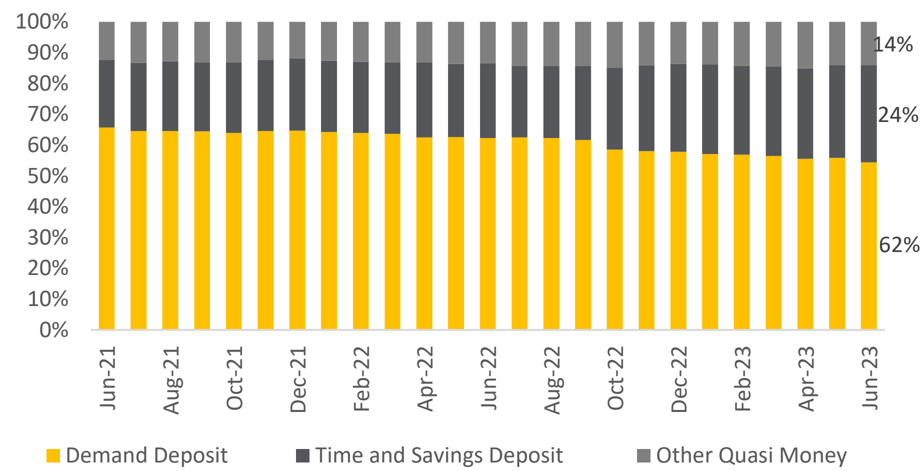
Source: Company Data

Figure 43: SNB simple LDR (non-SAMA) ratio development*



*Source: Company Data; * 1Q21 does not constitute NCB+SAMBA data*

Figure 44: Sector deposits break up by type

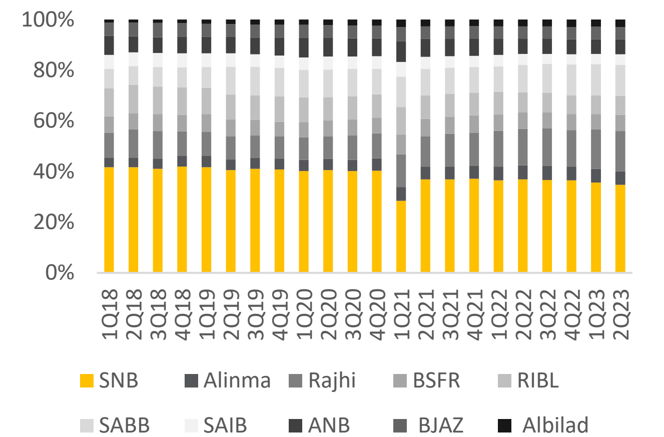


Source: SAMA

Investment book market share is the largest, with a significant lead over the closest peer.

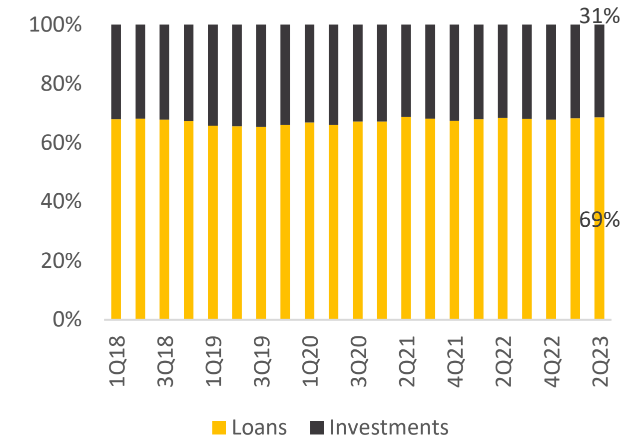
The market share of investment books for SNB was highest in 2Q23 at 35%, much higher than 16% for Al Rajhi. While Rajhi has replaced SNB as the bank with the largest loan book, SNB remains the largest in interest-earning assets due to its higher Investments. Investments accounted for 31% of the total interest-earning assets of SNB at the end of 2Q23.

*Figure 45: Market share of investments**



*Source: Company Data; *1Q21 investments do not constitute NCB+SAMBA*

*Figure 46: Loan and investments mix**

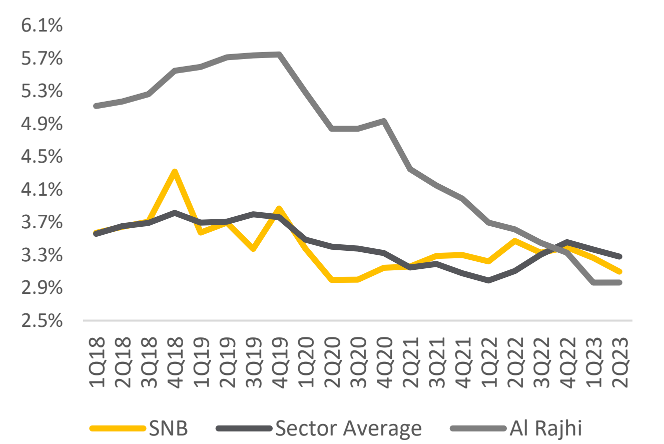


*Source: Company Data; * 1Q21 does not constitute NCB+SAMBA data*

NIMs compress over the quarters and recover slower than their peers.

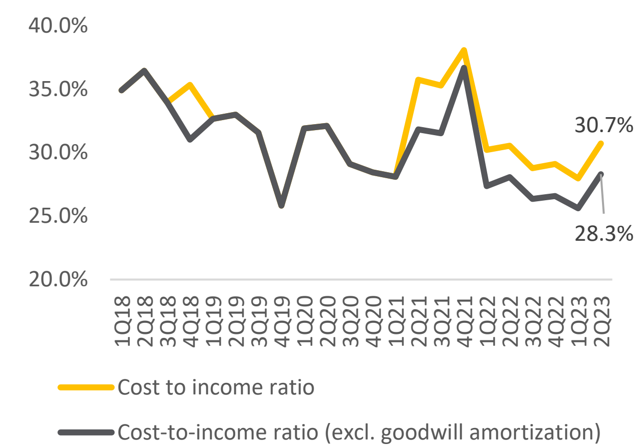
The Net Interest Margin (NIM) for SNB compressed at the beginning of FY21 due to the lower interest rate environment. SNB's NIM has been averaging around 3.4% in the last five years, witnessing a decline since the onset of the pandemic, reaching the lowest NIM margin of 3.0% in 2Q20. The NIM gradually recovered in the rest of FY21 due to improved yield and financing mix. SNB's peers have followed a similar trend with the NIM compressing due to lower interest rates, with the margin reversing the trend post the interest rate hike cycle. SNB's NIM is expected to remain flat in the near term and is expected to rise gradually as interest rates peak by the end of 2023.

Figure 47: NIMs: SNB vs peers



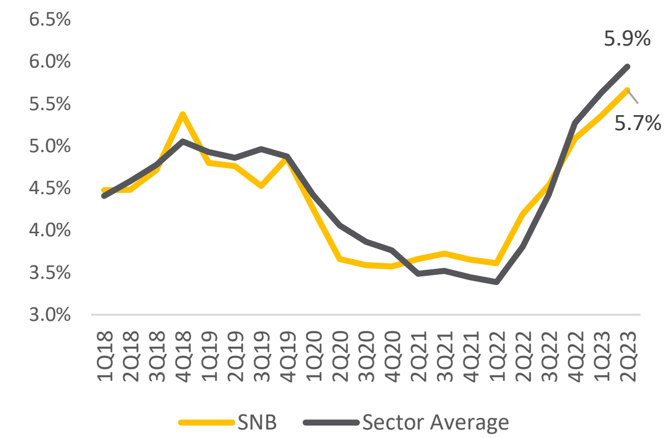
Source: Company Data

Figure 48: SNB's cost to income ratio



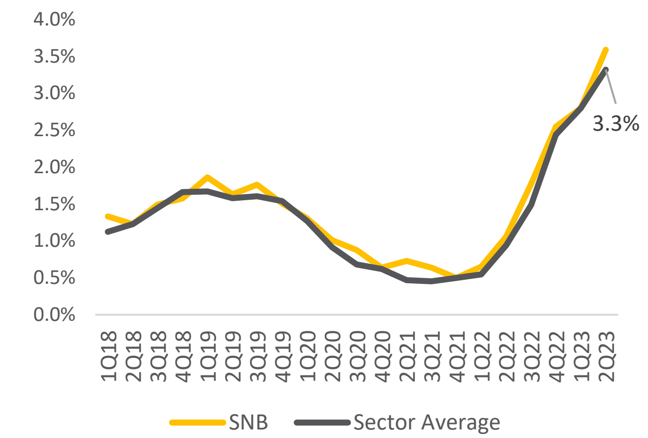
Source: Company Data

Figure 49: Asset yields SNB vs peers



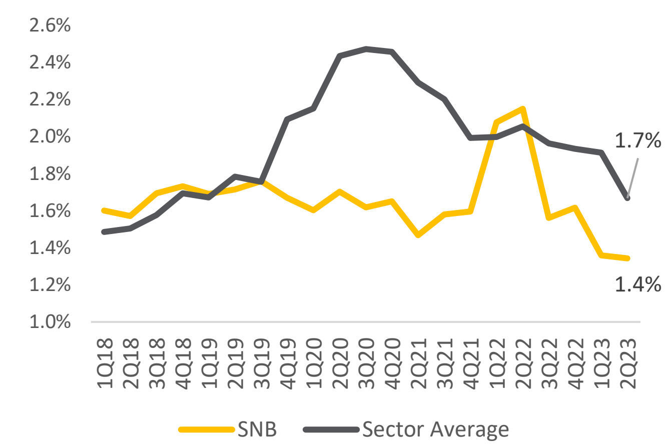
Source: Company Data

Figure 50: Cost of funds SNB vs peers



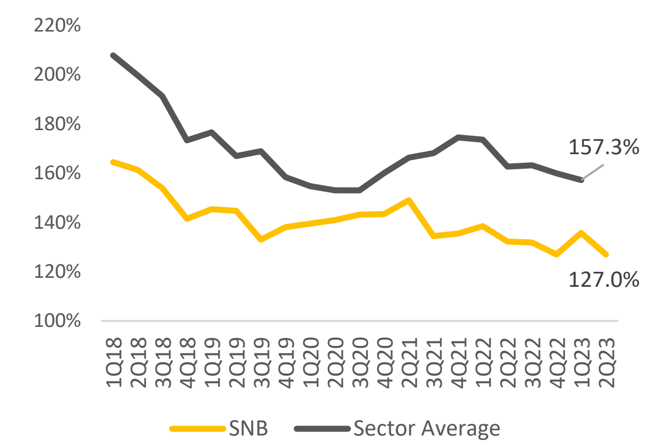
Source: Company Data

Figure 51: NPL/gross loans



Source: Company Data

Figure 52: Provision coverage SNB vs peers

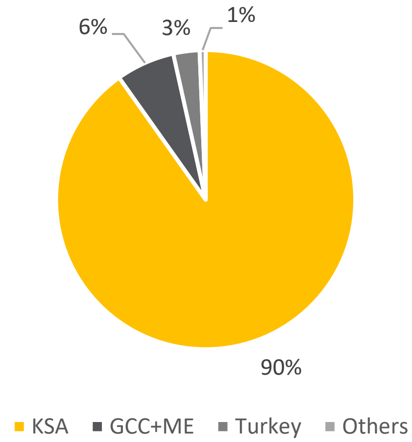


Source: Company Data

SNB's Turkey exposure remain limited; however, any downturn might impact sentiments

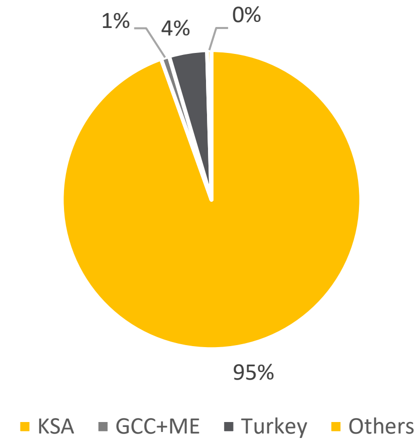
SNB owns ~67% of Türkiye Finans Katılım Bankası (TFKB), a leading Turkish bank with 286 branches. In 2008, SNB made its first overseas investment by acquiring the majority stake in Turkiye Finans. Fitch has maintained a credit rating of "B- "and a Negative outlook on THKB amid weak fundamentals and operating environment risks. Moreover, Fitch has maintained Turkiye's sovereign rating at "B" with a negative outlook, indicating sovereign risks for TFKB's operations. SNB's loan book exposure to Turkey stood at 3%, and deposits at 4% at the end of 2022. Meanwhile, the contribution of Turkish operations to total revenues remained at 7%, and to net income was 2%. Despite the limited exposure in Turkey, any downturn may impact SNB's performance.

Figure 53: SNB loan book by region at the end of 2022



Source: Company Data

Figure 54: SNB deposits by region at the end of 2022



Source: Company Data

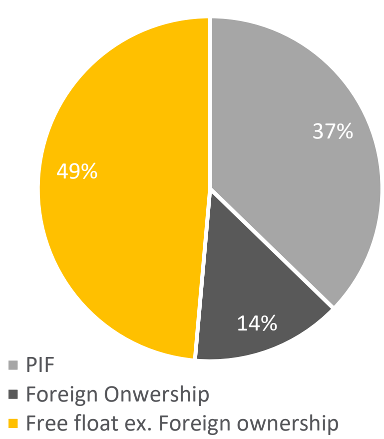
Synergy benefits from the SAMBA merger were realized ahead of the planned target.

The merger between National Commercial Bank (NCB) and Samba was completed in 2Q21. The union combined two complementary banks in KSA to attain a strong market share position. The strategic rationale was to become a leading bank in the Middle East with multi-channel distribution and reach. Out of the total revised targeted cost synergies of SAR1,400mn, SNB has achieved 99% (SAR1,379mn) of the real cost synergies ahead of the revised target. The integration costs are on track, with the bank committing 63% (SAR880mn) of the total integration cost of SAR 940mn. The bank has also made significant progress in digital innovation, complementing Vision 2030 agenda. A stand-alone digital bank catering to financial services to drive innovation and development of a digital product suite is under development and expected to be commercially launched in 2H23, subject to regulatory approvals and licenses.

Ownership Summary

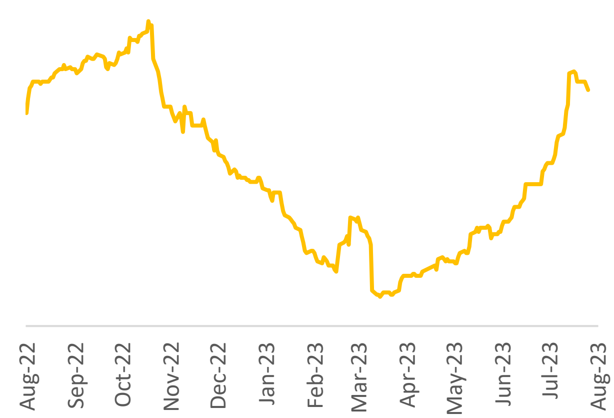
PIF is the largest shareholder in SNB; the group has a free float of c.63%, of which foreign shareholders hold nearly 14%.

Figure 55: Ownership summary



Source: Bloomberg

Figure 56: SNB's foreign ownership trend

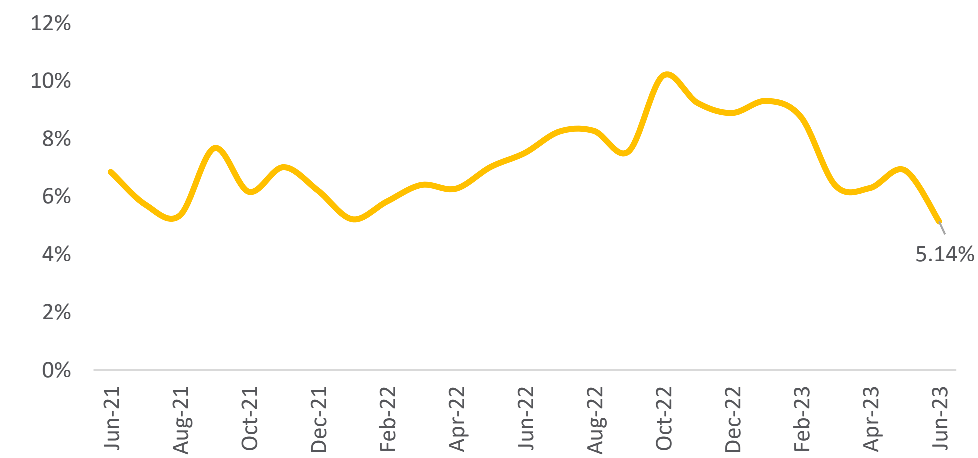


Source: Argaam

KSA Banking Sector Overview

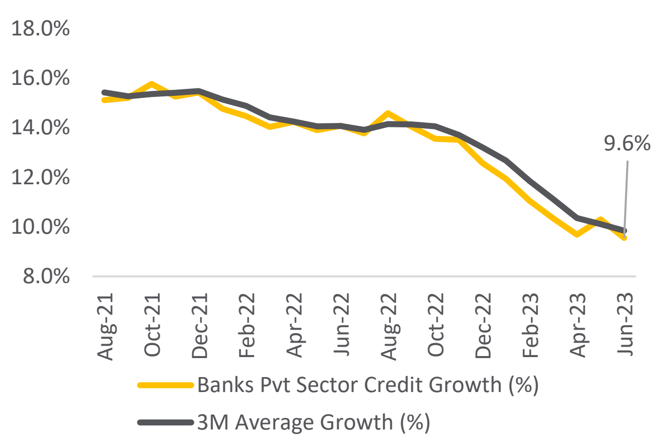
The Kingdom’s total outstanding loans stood at SAR3.1tn (incl. claims on private and Govt. and Quasi Govt. sector) at the end of June 2023, depicting a 9.9% y/y growth from June 2022. SAMA's repo rate and reverse repo rate are closely correlated with the US Fed rate regime since SAMA needs to maintain SAR's currency peg with US$. The US increased its Fed rate eleven times since the first hike in March 2022, resulting in the current US Fed rate of 5.50%. Consequently, SAMA's repo rate rose to 6.0% in August 2023 from 1.25% in March 2022.

Figure 57: Banking Sector Total Assets Growth (y/y)



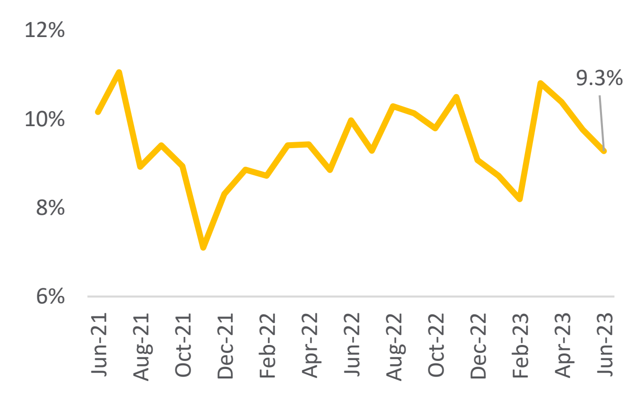
Source: SAMA

Figure 58: Banks' Private Sector Credit Growth (y/y)



Source: SAMA

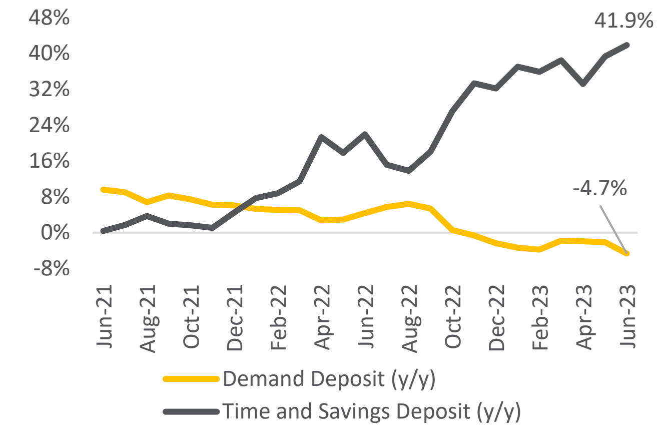
Figure 59: Banks Deposit Growth (y/y)



Source: SAMA

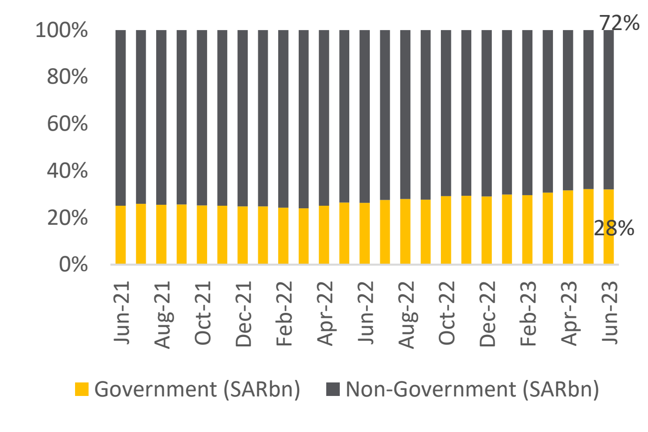
The US Fed has signaled more rate hikes in 2023, as inflation remains higher than the target. If the current interest rate environment continues for a longer period, the operations of banks in KSA might be impacted further. Conventional corporate banks have benefited in recent quarters, as corporate loans are repriced in line with the increased rates. However, generally mortgage dominated retail banks have seen a decline in yields as loans are repriced with a lag due to their longer duration. The trend might continue in the near future if the US Fed continues to maintain high-interest rates.

Figure 60: Demand vs. Time and Savings growth (y/y)



Source: SAMA

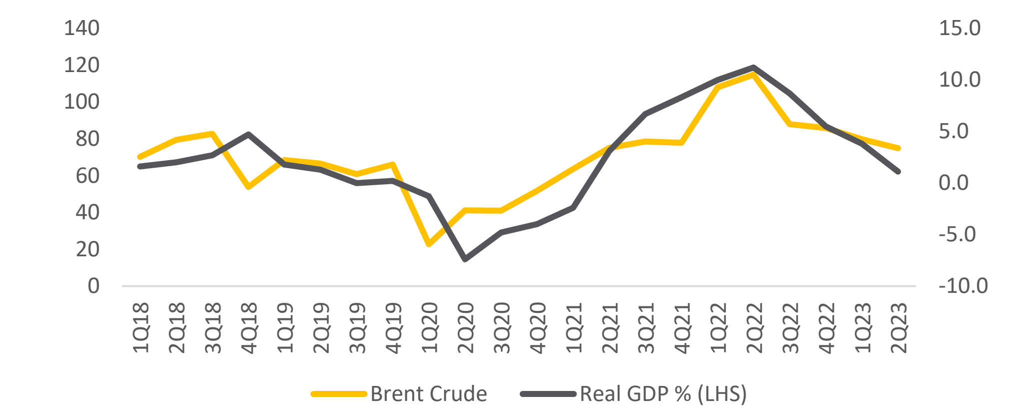
Figure 61: Mix of Deposit – Government and Non-Government



Source: SAMA

The loan growth moves in line with government spending which is a function of oil prices. The oil prices have remained mostly healthy despite disruptions in demand. As the demand from China is expected to rise helped by the recent stimulus package and OPEC+ pursues supply cuts, oil prices are expected to remain firm, which could benefit loan growth in KSA.

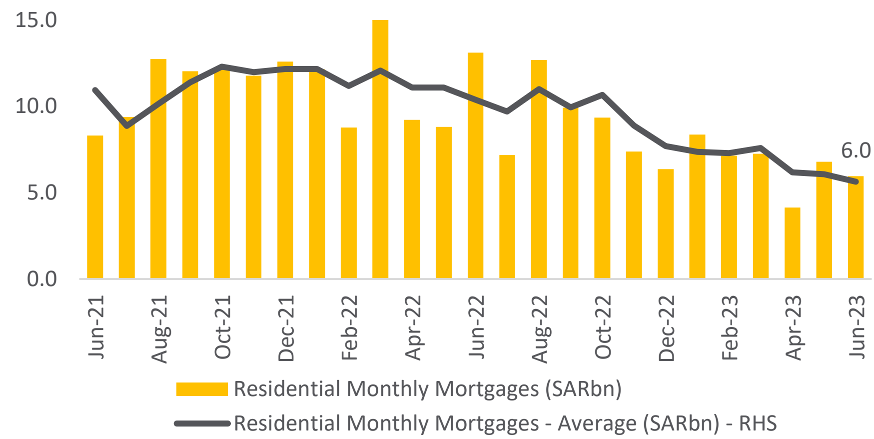
Figure 62: Brent Crude and KSA GDP correlation



Source: SAMA, Bloomberg

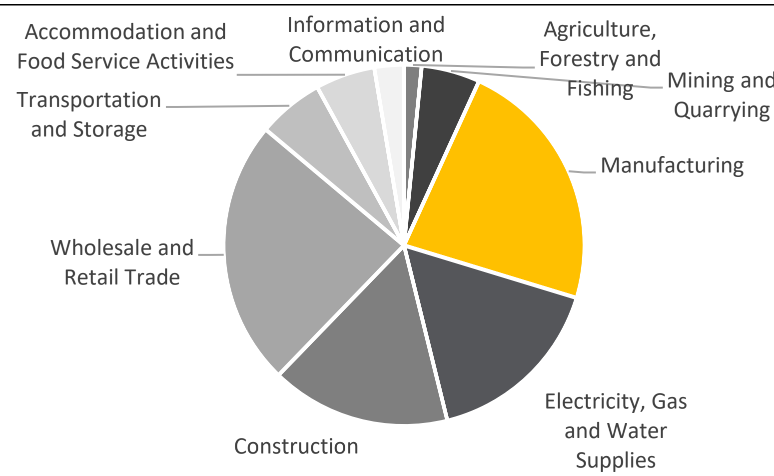
Lastly, the economic growth outlook for KSA stood at 1.9% for 2023 and 2.8% for 2024, as per IMF's World Economic Outlook update in July 2023. Meanwhile, the implementation of Vision 2030 should drive infrastructure projects and housing. This should largely benefit corporate loans and housing mortgages. Mortgage growth should help banks with a retail tilt like Rajhi, while SNB, with a balanced consumer and corporate profile with mortgage accounting for nearly half of Retail, is expected to benefit the most. Moreover, increasing mortgages and corporate loans could raise the debt maturity of the loans. This can be positive for the sector. Among other drivers, the resumption of Hajj pilgrims to pre-COIVD levels and strengthening SMEs under Vision 2030 should further provide tailwinds to the banking sector.

Figure 63: Residential monthly mortgages



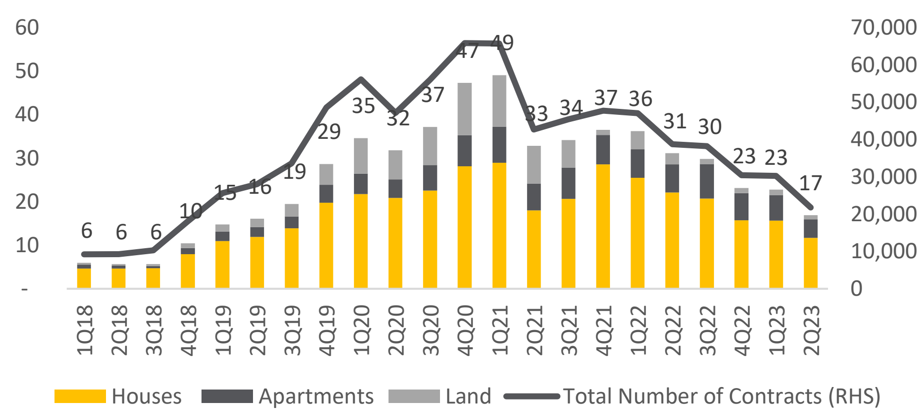
Source: SAMA

Figure 64: Loan profile by sector – June 2023



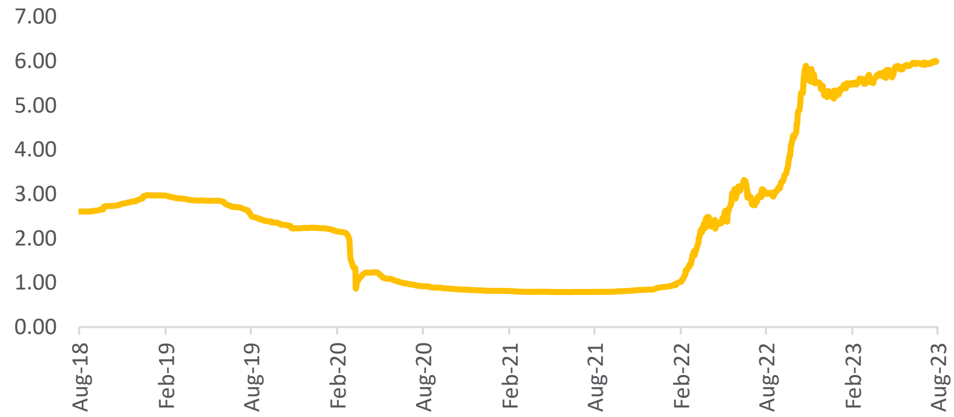
Source: SAMA

Figure 65: Mortgage Origination (SARbn)



Source: SAMA

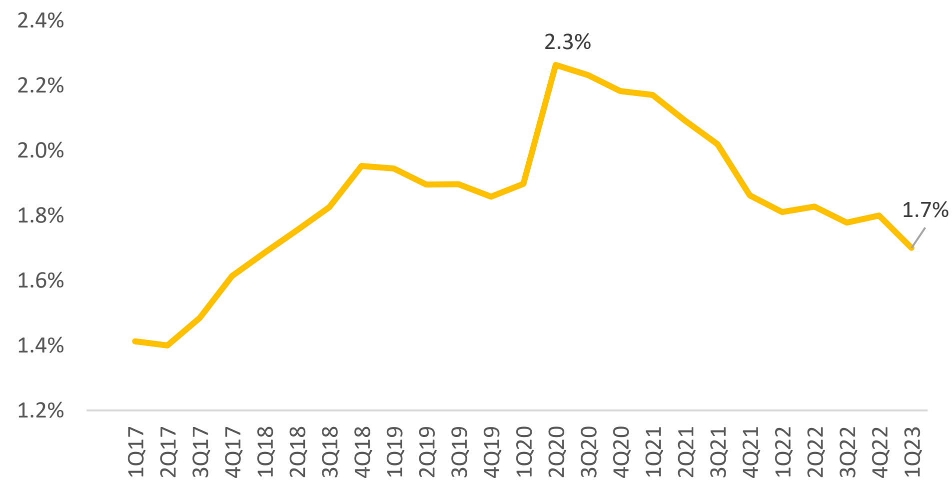
Figure 66: SAIBOR 3month yield



Source: Bloomberg

On the risk part, the NPL cycle is currently moving towards a low. The sector NPLs have decreased to SAR38bn in 2Q23 from SAR41bn in 2Q21, with the NPL ratio is at 1.7% from 2.3% during the same period. Meanwhile, the banking sector average reported coverage ratio stood at 155% in 2Q23. The cost of risk for the sector, which is currently at around 45bps, is also among the key positives.

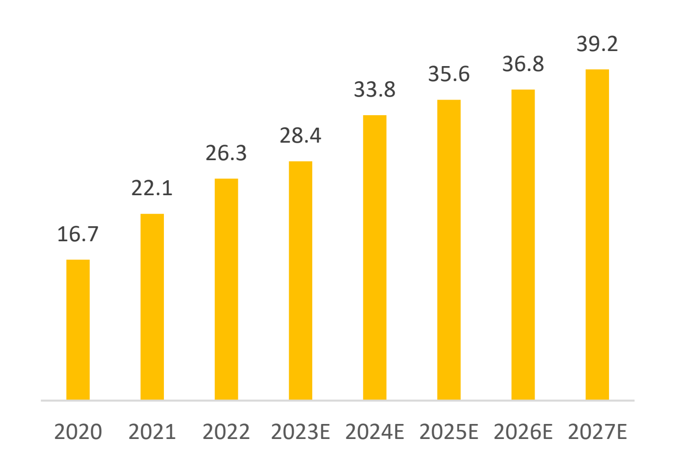
Figure 67: SAMA reported non-performing loans as a % of total loans



Source: SAMA

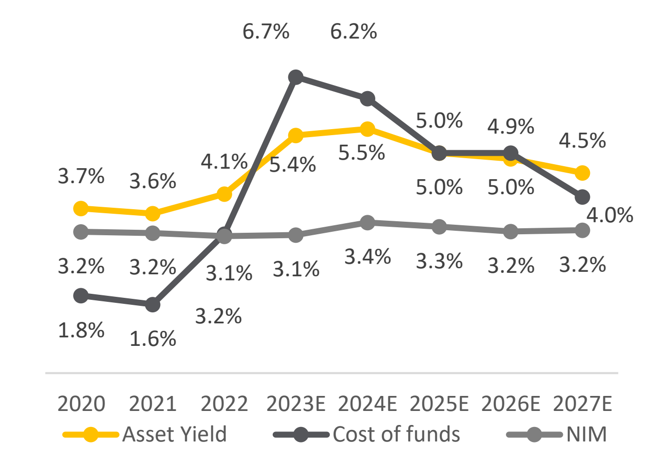
Financials analysis in charts

Figure 68: Net special commission income (SARbn)



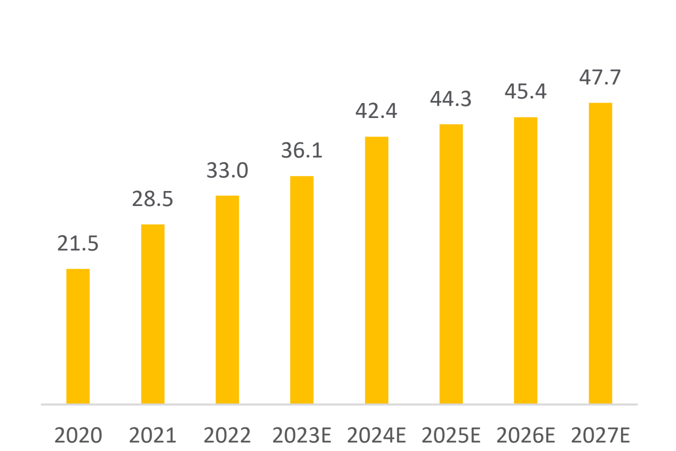
Source: Company Data, GIB Capital

Figure 69: SNB's yield analysis



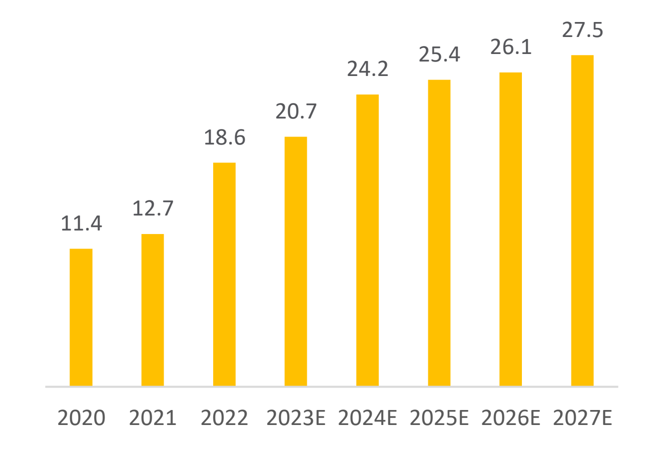
Source: Company Data, GIB Capital

Figure 70: Total operating income (SARbn)



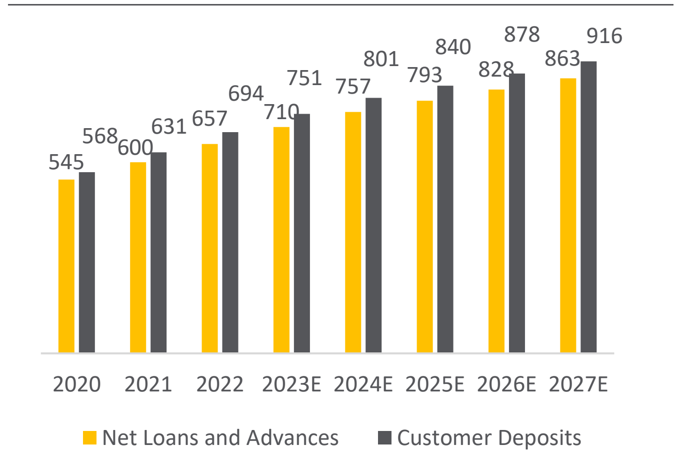
Source: Company Data, GIB Capital

Figure 71: Net income att. to equity holders (SARbn)



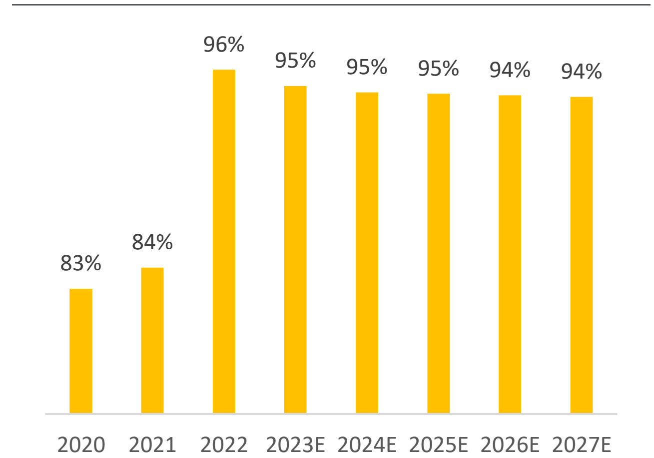
Source: Company Data, GIB Capital

Figure 72: Loans and deposits (SARbn)



Source: Company Data, GIB Capital

Figure 73: Loan to deposit ratio



Source: Company Data, GIB Capital

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Financials

Figure 74: Summarized basic financial statements (SARmn)

Income statement	2022a	2023e	2024e	2025e	2026e
Net Special Commission Income	**26,286**	**28,351**	**33,806**	**35,635**	**36,845**
NIM Margin	*3.1%*	*3.1%*	*3.4%*	*3.3%*	*3.2%*
Fee & other income	6,717	7,765	8,552	8,650	8,594
Total Operating Income	**33,003**	**36,117**	**42,358**	**44,285**	**45,439**
Operating Expenses	11,469	12,008	14,202	14,733	15,154
*Cost-to-income ratio**	*29.6%*	*28.4%*	*27.5%*	*27.0%*	*26.8%*
Net operating income before impairments	**23,220**	**25,875**	**30,710**	**32,328**	**33,261**
Impairments	1,685	1,766	2,554	2,776	2,976
Net operating income after impairments	**21,534**	**24,109**	**28,156**	**29,552**	**30,285**
Other non-operating (expenses)/income	(258)	(121)	(48)	(49)	(49)
Net income for the year before zakat	**21,277**	**23,987**	**28,108**	**29,503**	**30,236**
Zakat/tax	(2,548)	(2,859)	(3,373)	(3,540)	(3,628)
Net Income att. to Equity holders	**18,581**	**20,731**	**24,244**	**25,447**	**26,079**
Net margin	*56%*	*57%*	*57%*	*57%*	*57%*
y/y	*47%*	*12%*	*17%*	*5%*	*2%*
EPS	**4.1**	**3.3**	**3.9**	**4.1**	**4.2**
DPS	1.6	1.9	2.0	2.1	2.3
Payout	38%	56%	51%	50%	55%

Balance Sheet	2022a	2023e	2024e	2025e	2026e
Cash and balances with SAMA	41,611	44,771	44,771	44,771	44,771
Due from banks and other financial institutions	16,497	18,146	18,509	18,880	19,257
Investments	258,292	283,809	311,538	335,921	359,471
Net loans and advances	545,311	599,577	656,755	710,321	756,814
Property & equipment	9,993	10,943	11,116	11,227	11,235
Other assets	73,793	73,593	75,019	76,070	77,161
Total Assets	**945,496**	**1,030,839**	**1,117,710**	**1,197,190**	**1,268,709**
Interest-Earning Assets	861,710	946,303	1,031,575	1,109,894	1,135,541
Due to banks & other financial institutions	150,995	165,990	172,730	179,639	186,825
Customers deposits	568,283	631,002	693,884	751,172	801,089
Debt securities issued	12,987	13,719	13,719	13,719	13,719
Other Liabilities	123,465	117,691	113,870	108,443	99,194
Total Liabilities	**855,730**	**928,402**	**994,203**	**1,052,974**	**1,100,828**
Interest Bearing Liabilities	732,265	810,711	880,333	944,531	1,001,633
Equity	165,973	174,192	187,899	201,063	213,283
Total Equity and Liabilities	**945,496**	**1,030,839**	**1,117,710**	**1,197,190**	**1,268,709**
BVPS	27.7	29.0	31.3	33.5	35.5

*Source: Company, GIB Capital *incl. goodwill amortization*

Figure 75: Key ratios

Key ratios	2022a	2023e	2024e	2025e	2026e
Profitability ratios					
Asset Yield	4.1%	5.4%	5.5%	5.0%	4.9%
Cost of funds	3.2%	6.7%	6.2%	5.0%	5.0%
NIM	3.1%	3.1%	3.4%	3.3%	3.2%
ROE	11.3%	12.2%	13.4%	13.1%	12.6%
ROA	2.0%	2.1%	2.3%	2.2%	2.1%
Liquidity ratios					
Loans/ Customer Deposits	96%	95%	95%	95%	94%
Loan/Total deposits	76%	75%	76%	76%	77%
Loans / Assets	58%	58%	59%	59%	60%
Capitalization ratios					
Tier I Ratio	18.3%	20.9%	20.9%	21.0%	21.2%
Total capital adequacy (CAR)	19.0%	21.8%	21.9%	22.0%	22.1%
Equity/Total assets	17.55%	16.90%	16.81%	16.79%	16.81%
Asset Quality					
Gross NPL Ratio	1.6%	1.3%	1.2%	1.3%	1.3%
Net NPL Ratio	-0.4%	-0.5%	-0.4%	-0.4%	-0.4%
Coverage ratio	127.0%	135.0%	135.0%	135.0%	135.0%
COR (bps)	32	31	41	41	40
Valuation ratios					
P/E	9.2	11.3	9.6	9.1	8.9
P/B	1.3	1.3	1.2	1.1	1.0
Dividend Yield	4.2%	5.0%	5.4%	5.5%	6.2%

Source: Company, GIB Capital

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