

Al Rajhi Bank

Continued rise in cost-of-funds restricted profitability

Rating : ACCUMULATE

First Look Note – 1Q23

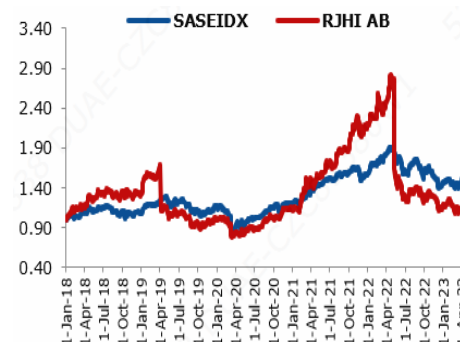
Sector: Banking

Recommendation

Current Price (28-Apr-23)	76.80
Target Price (SAR)	85.00
Upside/Downside (%)	+11%

Stock Information

Market Cap (mm)	307,600.00
Paid Up Capital (mm)	40,000.00
52 Week High	117.40
52 Week Low	69.00
3M Avg. daily value (SAR)	327,211,600



Financial Ratios

Dividend Yield (12m)	1.63
Dividend Pay-out (%)	29.15
Price-Earnings Ratio (x)	18.26
Price-to-Book Ratio (x)	3.67
Book Value (SAR)	20.93
Return-on Equity (%)	22.72
Earning Per Share (SAR)	4.21
Beta	1.15

Stock Performance

5 Days	0.52%
1 Months	4.63%
3 Months	-5.18%
6 Months	-9.53%
1 Year	-30.33%
Month to Date (MTD)	0.00%
Quarter to Date (QTD)	4.63%
Year to Date (YTD)	2.26%

1Q23 Net Profit lower than our estimate

Al Rajhi Bank's ("ALRAJHI", "The Bank") net profit rose marginally 0.3% YOY to SAR 4,145 Mn in 1Q23, lower than our estimate of SAR 4,444 Mn. The increase is mainly due to a decrease in total operating expenses, impairment charges, and marginal increase in non-funded income partially offset by a decline in net funded income.

P&L highlights

ALRAJHI's financing and investing income rose 48.8% YOY to SAR 8,768 Mn in 1Q23 from SAR 5,891 Mn in 1Q22 primarily due to robust growth in net advances. Moreover, the Bank's financing and investment expense rose substantially to SAR 3,643 Mn in 1Q23 from SAR 551 Mn in 1Q22 owing to an increase in interest rates. Thus, net financing and investment income declined 4.0% YOY to SAR 5,125 Mn in 1Q23. ALRAJHI's total non-funded income inclined 2.5% YOY to SAR 1,656 Mn in 1Q23. Resultantly, total operating income decreased 2.5% YOY to SAR 6,781 Mn in 1Q23 owing to a decline in net financing and investment income, and other operating income, and an increase in fees from banking services, and exchange income. Total operating expenses before credit provisions rose 1.8% YOY to SAR 1,800 Mn in 1Q23 with a cost-to-income ratio of 26.5% in 1Q23. The bank's profit before provisions declined 4.0% YOY to SAR 4,981 Mn in 1Q23. In addition, impairment charges fell 37.9% YOY to SAR 359 Mn in 1Q23. Zakat expense rose marginally 0.3% YOY to SAR 477 Mn in 1Q23 in line with rise in profit.

Balance Sheet highlights

ALRAJHI's net Advances rose significantly 19.1% YOY to SAR 577.0 Bn in 1Q23 with a loan-to-deposit ratio of 103.7% in 1Q23 as compared to 100.6% in 4Q22. Total assets inclined 18.0% YOY to SAR 776.2 Bn in 1Q23. Customer deposits rose 9.5% YOY to SAR 556.2 Bn in 1Q23. Whereas, total equity increased 26.7% YOY to SAR 99.2 Bn in 1Q23.

Target price and rating

We maintain our ACCUMULATE rating on Al Rajhi Bank with a target price of SAR 85.00. The bank's financing portfolio continued to report a robust growth of 19.1% YOY and 1.3% QOQ in 1Q23. ALRAJHI further anticipates its financing portfolio to increase by a mid-single-digit in 2023. Asset quality of the Bank continued to remain impeccable with NPL ratio of 0.5% and coverage ratio of 260.2% in 4Q22 providing cushion against rise in adverse scenarios. It also managed to control operating expense through efficiency measures as a result operating expense rose 1.8% YOY SAR 1,800 Mn in 1Q23. Despite all these positives, cost of funds continued to rise due to liquidity pressure in the system. Based on our calculation, NIMs declined during 1Q23 as a result of higher cost of funds. Loan-to-deposit ratio rose from 100.6% in 4Q22 to 103.7% in 1Q23 further pressurizing cost of funds. The issuance of the US denominated Sustainable Sukuk will ease some liquidity pressure for the Bank. Considering all these factors, we maintain our ACCUMULATE rating on the stock.

Al Rajhi Bank - Relative valuation

(at CMP)	2018	2019	2020	2021	2022	2023F
P/E (x)	33.5	30.8	29.5	21.2	18.4	17.6
P/B (x)	7.0	6.6	5.4	4.6	4.0	3.4
Dividend Yield (%)	2.2%	2.4%	0.8%	1.1%	1.6%	2.6%

FABS Estimates & Co Data

Al Rajhi Bank - P&L

SAR mm	1Q22	4Q22	1Q23	1Q23F	Var.	YOY Ch	QOQ Ch	2022	2023F	Change
Financing & investment inc.	5,891	8,534	8,768	8,793	-0.3%	48.8%	2.7%	28,202	37,308	32.3%
Financing & investment exp.	-551	-2,955	-3,643	-3,081	18.2%	561.6%	23.3%	-6,029	-13,800	128.9%
Net fin. & Investment inc.	5,340	5,579	5,125	5,712	-10.3%	-4.0%	-8.1%	22,173	23,508	6.0%
Total non-funded inc.	1,616	1,685	1,656	1,564	5.9%	2.5%	-1.7%	6,402	6,578	2.7%
Net operating income	6,957	7,264	6,781	7,276	-6.8%	-2.5%	-6.7%	28,575	30,085	5.3%
Total operating expenses before credit impairment	-1,769	-2,001	-1,800	-1,800	0.0%	1.8%	-10.0%	-7,451	-7,633	2.4%
Profit before provisions	5,188	5,263	4,981	5,476	-9.0%	-4.0%	-5.4%	21,124	22,452	6.3%
Impairment charge	-578	-353	-359	-522	31.3%	-37.9%	1.8%	-2,001	-2,398	19.8%
Total operating exp.	-2,347	-2,353	-2,159	-2,322	-7.0%	-8.0%	-8.3%	-9,452	-10,031	6.1%
Net income before zakat	4,609	4,911	4,622	4,954	-6.7%	0.3%	-5.9%	19,123	20,055	4.9%
Zakat	-476	-506	-477	-510	-6.5%	0.3%	-5.8%	-1,972	-2,066	4.8%
Net profit for the year	4,134	4,404	4,145	4,444	-6.7%	0.3%	-5.9%	17,151	17,989	4.9%

Al Rajhi Bank - P&L KPI

	1Q22	4Q22	1Q23	1Q23F	YOY Ch	QOQ Ch	2023F	Change
Net FI/OI	78.9%	76.8%	75.6%	78.5%	-119	-122	78.1%	54
Cost to income	25.8%	27.5%	26.5%	24.7%	112	-100	25.4%	-70
Impairment/PPP	-9.2%	-6.7%	-7.2%	-9.5%	394	-51	-10.7%	-121
NP/OI	60.4%	60.6%	61.1%	61.1%	171	50	59.8%	-23
ROAA	2.3%	2.3%	2.2%	2.3%	-20	-5	2.3%	-20
ROAE	21.6%	21.7%	17.2%	21.6%	-514	-446	21.1%	-238

FABS estimate & Co Data

Al Rajhi Bank - B/S Key Items

SAR mm	1Q22	2Q22	3Q22	4Q22	1Q23	YOY
Net advances	484,526	519,701	557,498	568,338	577,011	19.1%
QOQ change	7.0%	7.3%	7.3%	1.9%	1.5%	
Total assets	657,628	709,779	740,627	762,366	776,196	18.0%
QOQ change	5.5%	7.9%	4.3%	2.9%	1.8%	
Customer deposits	507,892	552,957	555,767	564,925	556,197	9.5%
QOQ change	-0.8%	8.9%	0.5%	1.6%	-1.5%	
Total equity	78,341	81,913	86,101	100,225	99,227	26.7%
QOQ change	16.4%	4.6%	5.1%	16.4%	-1.0%	

FABS estimate & Co Data

Valuation:

We use Residual Income and Relative Valuation (RV) method to value ALRAJHI. We have assigned 70% weight to Residual Income, and 30% to RV method.

Valuation Method	Target	Weight	Weighted Value
Residual Income	87.1	70.0%	60.99
Relative	79.9	30.0%	23.97
Weighted Average Valuation (SAR)			84.96
Current market price (SAR)			76.80
Upside/Downside (%)			11.63%

1) Residual Income Method:

We have discounted the economic profit/excess equity using the cost of equity of 8.15%. Cost of equity is calculated by using 10-year government bond yield of 4.5%, beta of 1.0 and equity risk premium of 3.7%. Government bond yield is calculated after adding KSA 10-year CDS spread over 10-year US risk free rate. Also, assumed a terminal growth rate of 2.0%.

Sum of PV (SAR, Mn)	52,952
Terminal value (SAR, Mn)	216,858
Book Value of equity (as of March 2023)	78,725
FV to Common shareholders (SAR, Mn)	348,534
No. of share (Mn)	4,000
Current Market Price (SAR)	76.80
Fair Value per share (SAR)	87.13

Residual Income Method

(All Figures in SAR Mn)	FY 2023E	FY 2024E	FY 2025E	FY 2026E	FY 2027E
Net Profit	17,798	19,547	23,700	26,949	30,874
(-) Equity charge	-7,475	-8,431	-9,563	-10,797	-12,025
Excess Equity	6,882	11,115	14,136	16,152	18,847
Discounting Factor	0.95	0.88	0.81	0.75	0.69
Present Value of Excess Equity	6,532	9,755	11,471	12,119	13,075

2) Relative Valuation:

We have used Saudi peers to value ALRAJHI and it is valued using the PB multiple. We applied premium to peer valuation since it generates superior return on assets as compared to its peers also, expect this premium to be maintained. During the historical period too, the Bank traded at a significant premium to its peers. It is valued at PB multiple of 3.5x as compared to peer valuation of 1.5x.

Company	Market (USD Mn)	P/B (x)		PE (x)		Dividend Yield (%)	
		2023	2024	2023	2024	2023	2024
Alinma Bank	16,735	2.2	2.1	14.1	12.9	3.9%	4.4%
Bank Albilad	10,887	2.7	2.4	15.4	13.3	1.4%	1.7%
Riyad Bank	24,203	1.7	1.6	11.7	11.0	4.2%	4.5%
Banque Saudi Fransi	12,399	1.2	1.1	10.5	10.3	4.9%	5.3%
Arab National Bank	10,613	1.2	1.1	11.0	10.9	4.8%	4.9%
Saudi National Bank	58,925	1.3	1.3	12.0	10.9	4.1%	4.7%
Average		1.7x	1.6x	12.4x	11.6x	3.9%	4.2%
Median		1.5x	1.4x	11.8x	11.0x	4.2%	4.6%
Max		2.1x	1.9x	13.5x	12.5x	4.7%	4.8%
Min		1.2x	1.2x	11.1x	10.9x	3.9%	4.4%

Research Rating Methodology:

Rating	Upside/Downside potential
BUY	Higher than +15%
ACCUMULATE	Between +10% to +15%
HOLD	Lower than +10% to -5%
REDUCE	Between -5% to -15%
SELL	Lower than -15%

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