

Mashreq Bank

Improvement in asset quality and NIMs boost profitability

1Q23 Net profit exceeded our estimate

Mashreq Bank ("MASQ"/The Bank) net profit more than doubled from AED 667 Mn in 1Q22 to AED 1,662 Mn in 1Q23, higher than our estimate of AED 949 Mn. The increase in net profit is mainly driven by robust growth in net funded and non-funded income coupled with a decline in impairment charges partially offset by a rise in operating expenses.

P&L highlights

MASQ's interest income rose significantly from AED 1,120 Mn in 1Q22 to AED 2,584 Mn in 1Q23 driven by a healthy growth in net advances and increase in asset yield. Similarly, interest expenses witnessed a sharp rise from AED 374 Mn in 1Q22 to AED 985 Mn in 1Q23 due rise in cost of funds driven by higher benchmark rates. Consequently, income from Islamic financing grew 116.9% YOY to AED 267 Mn in 1Q23 whereas Islamic financing expenses rose to AED 119 Mn in 1Q23, up from AED 41 Mn in 1Q22. Thus, MASQ's net funded income rose 111.0% YOY to AED 1,746 Mn in 1Q23. MASQ's NIMs rose 196 bps YOY and 54 bps QOQ to 4.4% in 1Q23. The Bank's net fee and commission income rose 63.7% YOY to AED 583 Mn in 1Q23 whereas income from investment securities rose marginally 3.4% YOY to AED 18 Mn. In addition, other operating income declined 43.0% YOY to AED 172 Mn in 1Q22. Resultantly, non-funded income grew 14.5% YOY to AED 774 Mn in 1Q23. Total operating income rose 67.6% YOY to AED 2,520 Mn in 1Q23. General and administrative expenses increased 25.6% YOY to AED 761 Mn in 1Q23 due to a rise in business volumes. However, the cost-to-income ratio improved from 1,010 bps YOY to 30.2% in 1Q23 owing to strong growth in operating profit. Impairments declined 57.9% YOY to AED 96 Mn in 1Q23 attributable to a solid improvement in asset quality. Income tax expense declined from AED 30 Mn in 1Q22 to AED 28 Mn in 1Q23.

Balance sheet highlights

MASQ's net advances rose 5.6% YOY and 0.9% QOQ to AED 91.1 Bn in 1Q23 driven by an increase in lending to the construction and trade segment. Manufacturing accounted for 18.2% of gross Loans in 1Q23, followed by trade at 16.0% and personal at 15.0% in 1Q23. Furthermore, total assets rose 10.2% YOY and 2.0% QOQ to AED 201.2 Bn in 1Q23. Customer deposits increase significantly 15.3% YOY and 5.6% QOQ to AED 120.2 Bn in 1Q23 due to an increase in current account deposits on QOQ basis. CASA accounts for 65% of total deposits in 1Q23. Total equity rose 14.5% YOY and declined 1.2% QOQ to AED 23.3 Bn in 1Q23.

Target price and rating

We maintain our BUY rating on Mashreq Bank with an unchanged target price of AED 145.0. The Bank reported robust growth in net profit on the back of strong growth in NIMs and non-funded income. MASQ benefited from the rise in interest rate and is further expected to benefit as 62.5% of the total loan book comprises of corporate loans in 1Q23. The Bank's NIMs grew 196 bps YOY and 54 bps QOQ to 4.4% in 1Q23. MASQ growth in loan book is driven by the increase in lending across the construction and trade segment in 1Q23. MASQ's asset quality improved with an NPL ratio of

Rating: BUY

First Look Note – 1Q23

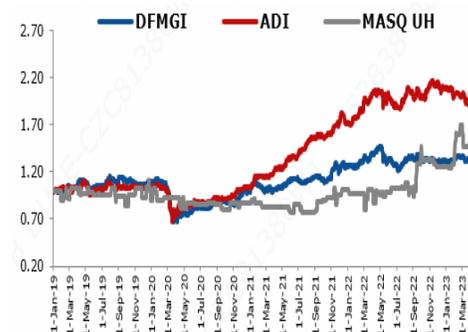
Sector: Banking

Recommendation

Current Price (1-May-23)	120.0
Target Price (AED)	145.0
Upside/Downside (%)	+20.8%

Stock Information

Market Cap (mm)	24,073.18
Paid Up Capital (mm)	2,006.10
52 Week High	135.00
52 Week Low	72.90
3M Avg. daily value (AED)	1,285,086



Financial Ratios

Dividend Yield (12m)	7.44
Dividend Pay-out (%)	0.00
Price-Earnings Ratio (x)	5.11
Price-to-Book Ratio (x)	1.08
Book Value (AED)	110.72
Return-on Equity (%)	22.12
Earning Per Share (AED)	23.48
Beta	0.27

Stock Performance

5 Days	0.00%
1 Months	0.00%
3 Months	16.50%
6 Months	16.50%
1 Year	60.00%
Month to Date (MTD)	0.00%
Quarter to Date (QTD)	0.00%
Year to Date (YTD)	23.08%

2.7% in 1Q23 as compared to 3.6% in 4Q22. The Bank's coverage ratio strengthened to 192.3% in 1Q23, up from 140.6% in 4Q22 providing cushion against unforeseen circumstances. However, the stage 2 loans rose marginally from 5.6% in 4Q22 to 5.7% in 1Q23. The bank's capitalization stood strong with a Tier 1 capital ratio of 15.1% and a total capital ratio of 17.4% in 1Q23. Wholesale banking, the Bank's largest asset segment accounted for 47% of total assets and 51% of total liabilities in 1Q23. Moreover, MASQ's deposit rose 15.3% YOY to AED 120.2 Bn in 1Q23 while CASA balance stood strong at 65%. Loan-to deposit ratio stood strong at 75.8% which indicates additional room for loan growth. In addition, the Bank declared a dividend of 90% of the paid of capital in 2022 with a dividend yield of 7.5%. Thus considering all these factors we maintain our BUY rating on the stock.

MASQ - Relative valuation

(At CMP)	2018	2019	2020	2021	2022	2023E
P/B (x)	1.19	1.12	1.24	1.19	1.07	0.91
P/E (x)	11.68	11.66	NA	24.02	6.50	4.84
Dividend yield	2.9%	2.9%	0.0%	0.8%	7.5%	4.2%

FABS Estimates & Co Data

MASQ - P&L

AED mm	1Q22	4Q22	1Q23	1Q23F	Var.	YOY Ch	QOQ Ch	2022	2023F	Change
Interest income	1,120	2,190	2,584	2,159	19.7%	130.7%	18.0%	6,415	10,111	57.6%
Inc. from Islamic financing	123	219	267	214	24.7%	116.9%	21.7%	672	1,010	50.4%
Funded income	1,243	2,409	2,851	2,373	20.1%	129.4%	18.3%	7,087	11,121	56.9%
Interest expense	-374	-816	-985	-865	13.9%	163.3%	20.8%	-2,255	-3,962	75.7%
Dist. to Islamic depositors	-41	-109	-119	-74	60.2%	191.3%	9.1%	-260	-500	92.3%
Net funded income	828	1,484	1,746	1,433	21.8%	111.0%	17.7%	4,572	6,659	45.7%
Net Fee & Commission inc.	356	505	583	412	41.7%	63.7%	15.6%	1,741	2,124	22.0%
Inc. from Invst. securities	18	65	18	25	-27.0%	3.4%	-71.7%	92	101	10.0%
Other Operating inc., net	302	160	172	189	-9.0%	-43.0%	7.4%	1,091	818	-25.0%
Total other OI	676	730	774	626	23.6%	14.5%	6.0%	2,924	3,044	4.1%
Total Operating income	1,504	2,213	2,520	2,059	22.4%	67.6%	13.8%	7,496	9,703	29.4%
G&A expenses	-606	-966	-761	-828	-8.1%	25.6%	-21.3%	-3,066	-3,542	15.5%
Pre provision profit	898	1,247	1,759	1,231	42.9%	95.9%	41.0%	4,430	6,161	39.1%
Impairment allowance, net	-228	-27	-96	-204	-52.8%	-57.9%	NM	-497	-691	38.8%
Overseas income tax exp.	-30	-87	-28	-62	-53.9%	NM	-67.4%	-146	-383	162.1%
Non-controlling interests	27	-68	27	-17	-259.0%	0.0%	-140.4%	-80	-82	3.0%
Net Profit	667	1,066	1,662	949	75.1%	149.2%	56.0%	3,706	5,005	35.1%

FABS estimate & Co Data

MASQ - P&L KPI

	1Q22	4Q22	1Q23	YOY Ch	QOQ Ch	2022	2023F	Change
Net FI/OI	55.1%	67.0%	69.3%	1,425	227	61.0%	68.6%	764
NIM	2.4%	3.9%	4.4%	196	54	3.3%	4.3%	101
NIS	2.4%	3.8%	4.3%	187	54	3.3%	4.6%	125
Fees & comms/OI	23.7%	22.8%	23.1%	-55	35	23.2%	21.9%	-134
Trading/OI	1.2%	2.9%	0.7%	-45	-221	1.2%	1.0%	-18
Cost to income	40.3%	43.6%	30.2%	-1,010	-1,345	40.9%	36.5%	-441
Impairment/PPP	25.4%	2.2%	5.5%	-1,997	329	11.2%	11.2%	-2
NP/OI	44.3%	48.1%	65.9%	2,160	1,781	49.4%	51.6%	214
ROAE	8.0%	17.0%	21.0%	1,302	399	17.3%	20.4%	308
ROAA	0.9%	1.9%	2.4%	146	43	2.0%	2.5%	49

FABS estimate & Co Data

MASQ - Key BS Items

AED mm	1Q22	2Q22	3Q22	4Q22	1Q23	YOY Ch
Net advances	86,295	89,676	91,326	90,303	91,109	5.6%
<i>QOQ changes</i>	5.9%	3.9%	1.8%	-1.1%	0.9%	
Total assets	182,581	188,644	187,588	197,246	201,233	10.2%
<i>QOQ changes</i>	3.1%	3.3%	-0.6%	5.1%	2.0%	
Customer deposits	104,228	109,335	109,430	113,806	120,162	15.3%
<i>QOQ changes</i>	2.7%	4.9%	0.1%	4.0%	5.6%	
Total equity	20,369	20,220	22,111	23,599	23,314	14.5%
<i>QOQ changes</i>	0.7%	-0.7%	9.4%	6.7%	-1.2%	

FABS estimate & Co Data

Valuation:

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

Valuation Method	Target	Weight	Weighted Value
Residual Income	155	70.0%	109
Relative	123	30.0%	37
Weighted Average Valuation (AED)			145
Current market price (AED)			120
Upside/Downside (%)			+20.83%

1) Residual Income Method:

We have discounted the economic profit/excess equity using the cost of equity of 8.2%. Cost of equity is calculated by using 10-year government bond yield of 4.7%, beta of 1.00 and equity risk premium of 3.4%. Government bond yield is calculated after adding Dubai 10-year CDS spread over 10-year US risk free rate. Also, assumed a terminal growth rate of 2.0%.

Sum of PV (AED, Mn)	6,515
Terminal value (AED, Mn)	2,091
Book Value of equity (as of March 2023)	22,498
FV to Common shareholders (AED, Mn)	31,103
No. of share (Mn)	201
Current Market Price (AED)	120.00
Fair Value per share (AED)	155.05

Residual Income Method

(All Figures in AED Mn)	FY 2023E	FY 2024E	FY 2025E	FY 2026E	FY 2027E
Net Profit	4,972	4,411	4,007	3,598	3,132
(-) Equity charge	-2,170	-2,436	-2,652	-2,834	-2,962
Excess Equity	2,802	1,975	1,355	764	170
Discounting Factor	0.97	0.94	0.87	0.81	0.74
Present Value of Excess Equity	2,729	1,863	1,181	616	127

2) Relative Valuation:

We have used local peers to value MASQ and it is valued using the PB multiple. It is valued at PB multiple of 0.9x in line with peers.

Company	Market (USD Mn)	P/B (x)		PE (x)		Dividend Yield (%)	
		2023	2024	2023	2024	2023	2024
Sharjah Islamic Bank	1,628	0.9	0.9	10.8	10.2	4.6	4.9
Commercial Bank of Dubai	3,685	1.1	1.0	0.0	0.0	7.0	6.4
Emirates NBD	22,700	0.9	0.8	6.4	6.1	5.5	6.0
RakBank	2,145	0.8	0.8	6.8	7.5	7.3	7.2
UAB	646	1.0	1.0	10.4	11.1	2.9	3.6
Average		1.0	0.9	6.9	7.0	5.5	5.6%
Median		0.9	0.9	6.8	7.5	5.5	6.0%
Max		1.0	1.0	10.4	10.2	7.0%	6.4%
Min		0.9	0.8	6.4	6.1	4.6%	4.9%

FAB Securities Awards



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